BEFORE THE MINNESOTA OFFICE OF ADMINISTRATIVE HEARINGS
600 NORTH ROBERT STREET
ST. PAUL, MINNESOTA 55101

FOR THE MINNESOTA PUBLIC UTILITIES COMMISSION
SUITE 350
121 SEVENTH PLACE EAST
ST. PAUL, MINNESOTA 55101-2147

Beverly Jones Heydinger	Chair
David C. Boyd	Commissioner
Nancy Lange	Commissioner
Dan Lipschultz	Commissioner
Betsy Wergin	Commissioner

IN THE MATTER OF THE APPLICATION OF NORTHERN STATES POWER COMPANY, D/B/A XCEL ENERGY, FOR AUTHORITY TO INCREASE RATES FOR ELECTRIC SERVICE IN MINNESOTA

MPUC Docket No. E-002/GR-13-868
OAH Docket No. 68-2500-31182

PROPOSED FINDINGS OF FACT OF THE MINNESOTA DEPARTMENT OF COMMERCE

Dated: October 14, 2014

Respectfully submitted,

LINDA S. JENSEN
Attorney Reg. No. 0189030
Telephone: 651-757-1472

PETER E. MADSEN
Attorney Reg. No. 0392339
Telephone: 651-757-1383

JULIA E. ANDERSON
Attorney Reg. No. 1038721
Telephone: 651-757-1202

445 Minnesota Street, Suite 1800
St. Paul, MN 55101-2134
Attorneys for Minnesota Department of Commerce

TABLE OF CONTENTS

INTRODUCTION 1

PROCEDURAL HISTORY 1

ARGUMENT 6

I. XCEL BEARS THE BURDEN OF PROOF TO SHOW THAT THE PROPOSED RATE CHANGES ARE JUST AND REASONABLE 6

II. COST OF CAPITAL: RETURN ON EQUITY AND OVERALL RATE OF RETURN (ISSUES 1 AND 12) 7

- A. Summary of DOC ROE Position 8
- B. Overview of Cost of Common Equity and Fair Rate of Return 10
- C. Determining a Fair Rate of Return on Equity 12
  - 1. The cost of common equity capital: discounted cash flow (DCF) method 12
- D. The DOC's Recommended ROE of 9.64 Percent Is Reasonable 13
  - 1. Selecting Comparable Groups 13
  - 2. The Expected Growth Rate of Dividends 15
  - 3. The Expected Dividend Yield 15
  - 4. Flotation Costs 15
  - 5. Summary of Results of DOC's DCF Analysis in Direct Testimony 16
  - 6. Surrebuttal Update 16
  - 7. DOC's Checks on the Reasonableness of its DCF Recommendations 17
  - 8. DOC's Updated (Surrebuttal) CAPM Analysis 18
- E. DOC Criticism of NSP's Cost of Common Equity Analyses 19
  - 1. Xcel's DCF Is Flawed 19
  - 2. Xcel's Application of the CAPM is Flawed 21

3. Mr. Hevert's Risk Premium Analysis 22

4. Summary of DOC-Modified Xcel DCF and CAPM Results 23

F. DOC Response to the ICI Group's Mr. Glahn 23

1. The Glahn Comparison Group was flawed 23

2. Mr. Glahn's DCF Analyses were flawed 24

3. Flotation costs 24

G. DOC Response to the Commercial Group 24

H. Decoupling Does Not Require an Adjustment to Xcel's ROE 25

III. THE CAPITAL STRUCTURE, THE COST OF SHORT- AND LONG-TERM DEBT, AND THE COST OF CAPITAL FOR NSP, FOR 2014 (ISSUE 12-IN PART–FOR 2014) 26

A. NSP's Proposed Capital Structure for 2014 (Issue 47, in part-for 2014) 26

1. Long-Term Debt 26

2. Short-Term Debt 27

3. Common Equity Capital 27

4. NSP's Proposed Capital Structure is Reasonable 27

B. The Costs of Short- and Long-Term Debt 28

C. The Initial 2014 Cost of Capital for NSP 29

D. NSP's Updated 2014 Proposed Capital Structure, Updated Cost of Common Equity, and the Updated Overall Cost of Capital for NSP 29

IV. THE CAPITAL STRUCTURE, THE COST OF SHORT- AND LONG-TERM DEBT AND THE COST OF CAPITAL FOR NSP, FOR 2015 (ISSUE 12-IN PART-FOR 2015) 30

A. NSP's Initial Proposed Capital Structure for 2015 (Issue 47, in part-for 2015) 30

B. Overall 2015 Updated Cost of Capital for NSP 32

V. 2014 TEST YEAR ADJUSTMENTS TO XCEL'S PROPOSED RATE BASE AND INCOME STATEMENT 33

A. Prairie Island Extended Power Uprate (EPU) (Issue 3) 33

B. Xcel's PI LCM/EPU Split Correction (Issue 39) 39

C. Hollydale Transmission Project (Issue 38) 39

D. Post-Retirement Medical Expenses (FAS 106) (Issues 6 and 19) 40

1. Expected Rates of Return (EROAs) 41

2. Plan Measurement Date (Issue 19) 42

3. The 2008 Market Loss (Issue 6, in part) 42

4. Discount rate (Issue 6, in part) 43

E. Post-Employment Benefits (FAS 112) (Issue 21) 44

F. Active Health Care (Issue22) 46

G. Affiliated Interest Service Company Allocations (Issue 37) 52

H. Monticello Extended Power Uprate (EPU) 2014 In-Service Date and 2015 Prudency Adjustment (Issue 2) 53

1. Introduction 55

2. Xcel bears the burden of demonstrating that the Monticello EPU is used and useful to ratepayers in 2014 56

3. The record does not support a conclusion that it is likely the EPU will be operating at 671 MWe, with NRC approval, by the end of 2014 61

4. For accounting purposes, not ratemaking purposes, the Department does not oppose Xcel booking the EPU as "in service" in 2014 67

5. Neither Xcel nor MCC has demonstrated the reasonableness of allowing 2014 and 2015 EPU costs, but deferring recovery of the 2014 EPU costs to 2015 67

6. XLI's position for partial 2014 recovery of EPU cost should be denied. 69

7. Department Recommendation 69

I. Prairie Island Site Administrative Building for 2014 and 2015 (Issue 29) 70

J. Non-Qualified Pension (Issue 20) 71

K. Qualified Pension: 2014 Test Year (Issue 4 and Issue 5) 71

1. Disputed Issue: level of discount rate for ratemaking purposes 72

2. Disputed Issue: Xcel's 2008 Market Loss request....................................80

3. Resolved: Xcel's proposed expected return on the pension asset (EROA) rate assumption for the XES and NSPM Plans is reasonable 88

4. Resolved: The measurement date assumption proposed by Xcel of December 31, 2013 is reasonable (Issue 18) 88

5. Resolved: The wage rate assumption proposed by Xcel of 3.75 percent is reasonable 88

L. Changes to In-Service Dates of Capital Projects for 2014 and 2015 (Issue 11) 89

M. Big Stone-Brookings Transmission Project Correction (Issue 41)........................93

N. Theoretical Reserve Correction Adjustment (Issue 43).......................................93

O. Net Operating Loss (NOL) Correction Adjustment (Issue 44 and Issue 47).........93

P. Cash Working Capital Methodology and Calculation (Issue 49, in part-2014) 94

Q. Test-Year Rate Base Summary 95

R. Cost Amortizations (Issue 8) 95

S. Nuclear Retention Program (Issue 23)..97

T. Property Tax (Issue 14)..100

U. Foundation Administration Expense (Issue 40)...104

V. Customer Care O&M Credits (Issue 24) 104

W. Investor Relations (Issue 26) 108

X. Insurance – Surplus Distribution (Issue 16)...109

Y. Emissions Control Chemicals for 2014 and 2015 (Issue 15 and Issue 33)..........113

Z. Nuclear Fees for 2014 (Issue 25) 114

AA. Bargaining Unit Wage Increase (Issue 42) 116

BB. Total Labor for 2014 (Paid Leave) (Issue 7) 116

CC. Depreciation Reserve for Nuclear Plant – XLI Proposal (Issue 75) 119
DD. Sales Forecast (Issue 13) 120
1. Overall 121
2. Disagreement as to Forecasted December Sales. 122
EE. Conservation and Decoupling (Issues 58 and 50) 132
1. Recovery of Conservation Improvement Program Expenses (Issue 58) 133
2. Xcel's Revenue Decoupling Mechanism (RDM) Proposal Should Not Be Approved Unless Harm to Ratepayers is Mitigated. (Issue 50) 136
3. ALJ Recommendations concerning a potential full decoupling mechanism 160
FF. Interest Synchronization Methodology and Calculation (Issue 49A) 161
GG. Test-Year Operating Income Summary and Summary of 2014 Test Year Financial Issues 162
1. Test-Year Operating Income Summary 162
2. Summary of 2014 Test Year Financial Issues 162
VI. 2015 STEP YEAR RATE BASE AND INCOME STATEMENT ADJUSTMENTS 163
HH. 2015 STEP – Xcel's STEP Methodology and Calculation 163
II. 2015 STEP – General Ledger IT (Issue 28) 163
JJ. 2015 STEP – Pleasant Valley & Border Winds (Issue 30) 164
KK. 2015 STEP – 2015 In-Service Date Changes (Issue 11) 166
LL. 2015 STEP – 2015 Passage of Time for 2015 Depreciation and 2015 Retirements (Issue 10) 166
1. Xcel's opposition to the principle of lowering the 2015 rate base to reflect depreciation and accumulated depreciation, for capital projects not included in the 2015 Step, is unreasonable 168
2. Xcel did not demonstrate that the Department's calculation of the passage time adjustments is incorrect 173

3. Conclusion regarding Passage of Time in 2015 Step 174

4. Summary of Adjustments 174

MM. 2015 STEP – Rate Moderation Plans – Depreciation Reserve and Department of Energy (DOE) Payments for 2014 and 2015 Step (Issues 9 and 34) 175

1. Theoretical depreciation reserve surplus 176

2. Excess DOE settlement payments to reduce 2015 Step....177

3. Results of the Department's analysis....178

4. DOC recommendation on rate mitigation....180

NN. 2015 STEP Placeholder -Monticello EPU Prudency (Issue 2, in part)....181

OO. 2015 STEP Calculation Monticello EPU 2015 STEP (Issue 2, in part) 181

PP. 2015 STEP – Cash Working Capital (Issue 49, in part-2015)....181

QQ. 2015 STEP – DOC Total 2015 STEP Rate Base Adjustment Summary....182

RR. 2015 STEP – Nuclear Outage Amortization for 2015 (Issue 27) 182

SS. 2015 STEP – Emission Chemicals (Issue 33)....183

TT. 2015 STEP – PI Admin Building (Issue 29)....184

UU. 2015 STEP – Sales Forecast (Issue 13, in part -for 2015)....184

VV. 2015 STEP – Property Taxes (Issue 32)....184

WW. 2015 STEP – Interest Synchronization Methodology and Calculation (Issue 49A)....185

XX. 2015 STEP–DOC Total STEP Adjustment and Operating Income Adjustment Summary 185

VII. OTHER COMPLIANCE CONCERNS REGARDING ANNUAL INCENTIVE COMPENSATION PROGRAM, SHERCO 3 INSURANCE CLAIMS AND LITIGATION, AND STEP COMPLIANCE 186

A. Reasonableness of Xcel's Annual Incentive Compensation Program (Issue 82) 186

B. Sherco 3 Insurance Claims and Litigation....187

1. Insurance Settlements 189

2. Insurance Coverage 191

C. STEP Compliance (Issue 35 and Issue 36) 191

VIII. CLASS COST OF SERVICE STUDY. (ISSUE 51, ISSUE 56, ISSUE 57, ISSUE 59, ISSUE 67) 193

A. The Objective and Steps in a Class Cost of Service Study 195

B. Xcel's Embedded Class Cost of Service Study 196

IX. RATE DESIGN 205

A. Rate Design Background 206

B. Rate Design Goals 206

C. Legal Standards Reflected in Rate Design Principles 207

D. Apportionment of Revenue Responsibility (Issue 53) 208

1. Apportionment of Revenue Responsibility By Class 208

2. The Role of Inter-Class Subsidies and Rate Shock 211

3. Surrebuttal Update of Revenue Apportionment 211

A. Customer Charges 213

1. Residential and Small General Service Classes (Issue 54) 213

2. Base Energy Charges for the C&I Demand Class (Issue 62A) 217

3. Time-of-Day Energy Charges (Issue 60, in part) 218

4. Energy Charge Credit (Issue 60, in part) 218

5. Interruptible Service Customers (Issue 52) 219

B. Response to Energy CENTS Coalition Witness Roger Colton and the OAG 220

1. The Department Considered Ability to Pay 220

2. Low Income Customers 220

3. Residential Customer Charges (Issue 55) 221

C. Inclining Block Rate (Issue 80) 224

1. Initial Rebuttal Inclining Block Rate Recommendation....224

2. The Parties' IBR Agreement....224

D. A New CIP Program for Low Income Renters (Issue 81)....225

INTRODUCTION

The Minnesota Department of Commerce, Division of Energy Resources, Energy Regulation and Planning Unit (the Department or DOC) respectfully submits these Proposed Findings of Fact to assist the Administrative Law Judge (ALJ) Jeanne M. Cochran and the Minnesota Public Utilities Commission (Commission or MPUC) regarding the application for a general rate increase filed by Northern States Power Company, d/b/a Xcel Energy (NSP, Xcel or the Company) in Docket No. E-002/GR-13-868 (13-868 or Multi-Year Rate Case). The Department's Initial Brief was the principal document used to create these Proposed Findings such that the headings are left intact to assist the reader.

PROCEDURAL HISTORY

1. On October 3. 2013, Xcel filed sales forecast data as required by the Commission in its Finding of Fact, Conclusions of Law and Order in the Company's most recent 2012 general rate case, Docket No. E-002/GR-12-961, to be provided 30 days in advance of the filing of NSP's subsequent rate case.

2. On November 4, 2013, Xcel filed its Multi-Year Rate Case with the Commission. Xcel sought authority to increase electric rates, through a multi-year rate plan pursuant to Section 216B.16, subd. 1 and 19, (the MYRP Statute) with 2014 and 2015 test years effective January 3, 2014 and January 1, 2015, respectively. Xcel requested a two-year increase made up of $192.7 million, or 6.9 percent, in 2014, and $98.5 million, or 3.5 percent, in 2015, for a total increase of $291.2 million, or 10.4 percent over the two years. The 2014 and 2015 revenue deficiencies are each based on a 10.25 percent return on equity. The Company also sought an interim rate increase of $127.4 million on an annualized basis to be charged to ratepayers until the Commission decides this rate petition.

3. On November 5, 2013, the Commission issued a notice requesting comments on whether the Company's Multi-Year Rate Case should be accepted as complete and referred to the Office of Administrative Hearings (OAH) for a contested case proceeding.

4. On November 13, 2013, the Commission received comments from the Department recommending that the Commission find Xcel's filing to be substantially complete and that the matter be referred to the OAH for a contested case proceeding.

5. Also on November 14, 2013, a group of customers called the Xcel Large Industrials (XLI)[1] filed comments recommending that the matter be referred to the OAH for a contested case proceeding. Between November 5 and December 26, 2013, the Commission also received comments from at least six Xcel ratepayers and shareholders regarding the Company's requested rate increase and/or executive compensation.

6. On December 12, 2013, the matters came before the Commission.

7. On December 31, 2013, Xcel submitted a filing required by Order Point 9 of the Commission's September 3, 2013 Order in Docket No. E-002/GR-12-961, which required Xcel to provide an analysis and report on the Sherco Unit 3 total costs, insurance recoveries, and costs not covered by insurance in its November 2013 rate-case filing, and to provide the completed accounting and report by December 31, 2013.

8. On January 2, 2014, the Commission issued three orders: First, in its Order Accepting Filing and Suspending Rates the Commission found the filing to be substantially complete, and suspended the operation of the proposed rate schedule.

9. Second, the Commission's Order Setting Interim Rates approved Xcel's proposed interim rate increase to cover a revenue deficiency of approximately $127,406,000 per year, to be implemented by January 3, 2014 – that is, 60 days after its November 4, 2013 filing.

10. Third, the Commission's Notice and Order for Hearing referred the matter to the OAH for contested case proceedings.

11. In its January 2, 2014, Notice and Order for Hearing, the Commission identified the following issues for parties to address in the course of the contested case proceedings:[2]

a) Is the test year revenue increase sought by the Company reasonable or will it result in unreasonable and excessive earnings by the Company?

b) Is the rate design proposed by the Company reasonable?

c) Are the Company's proposed capital structure, cost of capital, and return on equity reasonable?

d) Has the Company fully complied with past Commission orders?

e) How should the Commission incorporate into this case the results of the ongoing investigation into the prudence of Xcel's expenditures for life cycle management and the extended power uprate at the Monticello Nuclear Generating Plant?

---

[1] XLI is made up of Flint Hills Resources, LP, Gerdau Ameristeel Corporation, Unimin Corporation; and USG Interiors, Inc.

[2] Notice and Order for Hearing at 2.

f) How should the proceeds of any insurance claims and litigation proceeds related to the Company's Sherburne County Generating Station Unit 3 be incorporated into Xcel's rates?

g) What will be the short- and long-term consequences of the rate mitigation strategy proposed by the Company?

12. In addition, the Commission stated that parties may also raise and address other issues relevant to the Company's proposed rate increase.

13. On January 31, 2014, Xcel filed its "Bad Debt Study – Supplemental Information," in compliance with Order Point 31 of the Commission's September 3, 2013, Findings of Fact, Conclusions, and Order in Docket No. E002/GR-12-961.

14. On January 28, 2014, ALJ Cochran held a prehearing conference.

15. On February 7, 2014, following discussion at the prehearing conference, including discussion of item 5 from the Commission's Notice and Order for Hearing, incorporation of information from MPUC Docket No. E-002/CI-13-754 (*ITMO a Commission Investigation into Xcel Energy's Monticello Life Cycle Management/Extended Power Uprate Project and Request for Recovery of Cost Overruns*, (13-754 or Monticello Cost Overrun Investigation)), the Xcel filed its limited waiver of its rights under Minn. Stat. § 216B.16, subds. 2(a) and (e) and 19, and agreed to a date on or about March 24, 2015 for a final determination by the Commission, as well as other commitments.

16. On February 14, 2014, ALJ Cochran issued the First Prehearing Order and a Protective Order. In her Prehearing Order, ALJ Cochran noted that the Commission's Notice and Order for Hearing named Xcel, the Department, and the Office of the Attorney General – Antitrust and Utilities Division (OAG) as parties. The ALJ granted the Petitions for Intervention filed by the Commercial Group,[3] Energy CENTS Coalition (ECC), the Suburban Rate Authority (SRA), the ICI Group, and the Xcel Large Industrials (XLI).

17. ALJ Cochran's First Prehearing Order set procedures for parties in the case and established the following schedule:

February 28, 2014	Intervention
June 5, 2014	Direct Testimony (Intervenors)
July 7, 2014	Rebuttal Testimony

[3] The Commercial Group is an ad hoc group of commercial customers of Xcel that is composed of JC Penney Corporation, Inc., Macy's, Inc., Sam's West, Inc., and Wal-Mart Stores, Inc.

August 4, 2014	Surrebuttal Testimony
August 8, 2014	Status Conference
August 11-18, 2014	Evidentiary Hearing
September 10, 2014	Applicants' Draft Issue Matrix
September 23, 2013	Initial Briefs
September 30, 2014	Comments to Issues Matrix
October 7, 2014	Final Issues Matrix (Xcel)
October 14, 2014	Reply Briefs and Proposed Findings of Fact
December 22, 2014	ALJ Report

Public hearings to be held the week of June 23, 2014.

18. On March 5, 2014, the ALJ granted the following petitions to intervene: 1) the Minnesota Chamber of Commerce (the Chamber or MCC); and 2) Fresh Energy, the Izaak Walton League, the Sierra Club, the Natural Resources Defense Council and the Minnesota Center for Environmental Advocacy (Clean Energy Intervenors or CEI).

19. On March 14, 2014, the ALJ granted, with limitations, AARP's petition to intervene as a party. The ALJ limited AARP's participation to the issues of rate design and decoupling, as well as any service quality issues that affect the unique interests of its members.

20. On March 14, 2014, the ALJ denied the petition of Minnesota Power (MP) to intervene as a party. The ALJ ordered that MP may file an *amicus curiae* brief of up to 40 pages no later than September 30, 2014, to which parties may respond.

21. On June 5, 2014, the following parties filed direct testimony in accordance with the schedule set forth in the ALJ's First Prehearing Order: OAG, ECC, the Commercial Group, the Chamber, the ICI Group, AARP and XLI.

22. On June 6, 2014, the Department filed its Direct Testimony, which was late-filed the previous evening. On June 25, 2014, the ALJ granted the Department's Motion for a one-day extension to June 6, 2014, for good cause shown.

23. ALJ Cochran held public hearings as follows:

- Earle Brown Heritage Center, Minneapolis, Minnesota at 1:00 p.m. on June 23, 2014.

- Sabathani Center, Minneapolis, Minnesota at 7:00 p.m. on June 23, 2014.
- West Minnehaha Recreation Center, St. Paul, Minnesota at 1:00 p.m. on June 24, 2014.
- Woodbury Central Park, Woodbury, Minnesota at 7:00 p.m. on June 24, 2014.
- Civic Center, Mankato, Minnesota at 7 p.m. on June 25, 2014.
- Eden Prairie City Center, Eden Prairie, Minnesota at 7:00 p.m. on June 26, 2014.
- Lake George Municipal Complex, St. Cloud, Minnesota at 1:00 p.m. on June 27, 2014.

24. On July 7, 2014, the following parties filed Rebuttal Testimony: the Department, OAG, ECC, CEI, AARP, XLI, and Xcel.

25. On July16, 2014, ALJ Cochran and ALJ Mihalchick convened a joint prehearing conference for the present docket and the Monticello Cost Overrun Investigation. The July 17, 2014, Joint Prehearing Order determined that the protective order in the present docket will be used in the Monticello Cost Overrun Investigation, and that the issues to be considered in the above dockets are as follows:

a) The issue of the reasonableness and prudence of the costs for the Life Cycle Management and Extended Power Uprate at the Monticello Nuclear Generating Plant will be addressed in the Monticello Cost Overrun Investigation.

b) The issue of whether the Extended Power Uprate should be considered "used and useful" during 2014 will be addressed in the Monticello Cost Overrun Investigation.

c) The issue of cost allocation between the Extended Power Uprate and Life Cycle Management will be addressed in the Monticello Cost Overrun Investigation.

d) The issue of the recovery and amortization of expenses from the Monticello Cost Overrun Investigation will be addressed in Xcel's Multi-Year Rate Case.

26. On August 4, 2014, the following parties filed Surrebuttal Testimony: Department, OAG, ECC, MCC, ICI (filed on August 5th), CEI, AARP, XLI and Xcel.

27. On August 8, 2014, the ALJ convened a status conference to facilitate an orderly and efficient evidentiary proceeding.

28. The evidentiary hearings were held on August 11-15, 2014, in the Commission's large hearing room.

29. On September 10, 2014, Xcel filed its Preliminary Issues List, in compliance with the ALJ's directive, that identified the Company's view of the issues that are resolved between one or more parties, and the issues that remain contested.

30. On September 23, 2014, parties filed Initial Briefs.

ARGUMENT

I. XCEL BEARS THE BURDEN OF PROOF TO SHOW THAT THE PROPOSED RATE CHANGES ARE JUST AND REASONABLE

31. Xcel bears the burden of showing that its proposed rates are reasonable. Minn. Stat. § 216B.16, subd. 4 (2013). Minnesota law requires that every rate established by the Commission must be just and reasonable, and that any doubt is to be resolved in favor of the consumer:

> Every rate made, demanded or received by a public utility . . . shall be just and reasonable. . . . Any doubt as to reasonableness should be resolved in favor of the consumer.

Minn. Stat. § 216B.03 (2013).

32. The Minnesota Supreme Court found that the burden is on the utility to prove the facts required to sustain its burden by a fair preponderance of the evidence. In *In re Northern States Power Co*., 416 N.W.2d 719, 722 (Minn. 1987), the Supreme Court described the Commission's role in determining just and reasonable rates in a rate proceeding, including its role in evaluating whether the utility has met its burden to show the reasonableness of recovery particular costs from ratepayers:

> [I]n the exercise of the statutorily imposed duty to determine whether the inclusion of the item generating the claimed cost is appropriate, or whether the ratepayers or the shareholders should sustain the burden generated by the claimed cost, the MPUC acts in both a quasi-judicial and a partially legislative capacity. To state it differently, in evaluating the case, the accent is more on the inferences and conclusions to be drawn from the basic facts (i.e., the amount of the claimed costs) rather than on the reliability of the facts themselves. Thus, *by merely showing that it has incurred, or may hypothetically incur, expenses, the utility does not necessarily meet its burden of demonstrating it is just and reasonable that the ratepayers bear the costs of those expenses.*

Id. at 722–23 (emphasis added).

33. The DOC's recommendations below reflect the positions taken in prefiled testimony and during the evidentiary hearing after a thorough and comprehensive analysis of Xcel's application and extensive discovery. Through the normal course of developing and narrowing issues in prefiled testimony, some issues were resolved. The remaining issues are contested as described herein. In those instances where the Company failed to meet its burden as indicated, the ALJ and the Commission should reject Xcel's proposals. Based on the record in this proceeding, the DOC concludes that Xcel has not supported a rate increase in the amount it requested in the application.

34. The Department notes with appreciation that Xcel's performance in providing responses to information requests and efforts to narrow the number of disputed issues in this proceeding improved considerably from the performance in the last rate case. While the length of the Department's initial brief is considerable, much of the length is due to efforts to explain issues rather than the degree of disputes that occurred in the prior rate case. Of course, there continue to be issues for the ALJ and Commission to decide.

35. The Department calculated the Company's revenue deficiency; the calculation includes specific adjustments recommended by Department Witnesses Dale V. Lusti, Angela C. Byrne and Nancy Campbell, discussed in below sections V (adjustments to rate base) and VI (adjustments to operating income and expenses) and VII (compliance issues). It also includes Department Witness Dr. Amit's recommended return on equity and overall rate of return adjustments, discussed in below section II, and his discussion of Xcel's capital structure in sections III (2014) and IV (2015) as well as Mr. Davis's conservation adjustment and Mr. Shah's sales forecast adjustment, also discussed in section V below.

36. As discussed herein, the Department recommends a final revenue requirement for the 2014 test year $45,887,000 as compared to Xcel's initial request of $192,709,000. The Department also recommends a 2015 STEP increase of $66,499,000, compared to Xcel's requested $98,535,000 for a total increase over the two years of $112,386,000, compared to Xcel's total request over two years of $291,234,000, a decrease of $178,848,000. DOC Ex. 451 DVL-EH-2 and DVL-EH-21 (Lusti Opening Statement).

II. COST OF CAPITAL: RETURN ON EQUITY AND OVERALL RATE OF RETURN (ISSUES 1 AND 12)

ROE and ROR

Disputed between DOC, Xcel and ICI Group: DOC recommends an ROE of 9.64 percent rather than Xcel's proposed 10.25 percent, with both percentages including an allowance for the same flotation cost adjustment. ICI recommends an ROE of 9 percent with no flotation costs. *Compare* DOC Ex. 403 at 7 (Amit Surrebuttal) *with* Xcel Ex. 27 at 55 (Hevert Direct) *and* Glahn at 4 (Glahn Surrebuttal). DOC recommends an ROR of 7.31 percent for 2014 and an ROR of 7.34 percent for 2015. DOC Ex. 403 at 29 (Amit Direct); DOC Ex. 403 at 11 (Amit Surrebuttal). By contrast, Xcel proposes an ROR of 7.64 percent for 2014 and 7.67 percent for 2015. Xcel Ex. 30 at GET-1, schedule 2, pages 1-2 (Tyson Direct).

Resolved between DOC and Xcel: DOC recommends approving Xcel's proposed capital structure as modified by the Company in its Rebuttal Testimony Xcel Ex. 31 at GET-2, schedule 3 and schedule 7 (Tyson Rebuttal). DOC Ex. 403 at 11, 29 (Amit Surrebuttal); DOC Ex. 400 at 51 (Amit Direct).

Flotation Costs

Resolved between DOC and Xcel; Disputed by ICI Group: DOC recommends accepting Xcel's proposed flotation costs adjustment of 2.926 percent. DOC Ex. 400 at 32 (Amit Direct). ICI recommends no recovery of flotation costs.

Decoupling Adjustments to ROE

Resolved between DOC, Xcel, and CEI; Disputed by AARP: DOC, Xcel, and CEI all agree that if the Commission accepts Xcel's decoupling proposal, that a downward adjustment to ROE is not reasonable. Xcel Ex. 28 at 49 (Hevert Rebuttal); CEI Ex. 290 at 5–6 (Cavanagh Direct); DOC Ex. 403 at 27–28 (Amit Surrebuttal); *But see,* AARP Ex. 311 at 14–18 (Brockway Rebuttal).

37. Department witness Dr. Eilon Amit provided DOC's recommendation regarding a fair rate of return on common equity capital (ROE) and a fair overall rate of return (ROR) for NSP.[4]

A. Summary of DOC ROE Position

38. Department Witness Dr. Eilon Amit summarized the Department's position regarding Xcel's proposed ROE and overall ROR in his Opening Statement at the Evidentiary Hearing of this matter, as follows:

> I recommend a return on common equity capital of 9.64 percent for NSP. My recommendation for return on common equity capital is based on my discounted cash flow (DCF) analysis in combination with, when appropriate, two growth rates DCF (TGDCF) analysis. I performed these analyses on two groups with investment risks similar to each other and similar to NSP's. These groups are the Final Electric Comparison Group, FECG, and the Final Combination Comparison Group, FCCG. Additionally, the results of my DCF-TGDCF analyses are supported by my Capital Asset Pricing Model or CAPM analyses.
>
> My recommended overall rate of return for NSP is based on the updated capital structure, the updated costs of short- and long-term

[4] NSP is a subsidiary company of Xcel Energy. As such, it is not publicly traded on any stock exchange. DOC Ex. 400 at 7 (Amit Direct).

> debt as provided by the Company in its Rebuttal Testimony, and my updated cost of common equity.

DOC Ex. 443 at 1-2 (Amit Opening Statement).

39. Dr. Amit also summarized the similarities and main differences between the Department's and Xcel's analyses, and why the Department's more recent information regarding dividend yields and projected growth rates, and an appropriate weighting result in the Department's reasonable recommended ROE and ROR for Xcel. Dr. Amit explained the reasonableness of his recommendations in comparison to the Company's witness, Mr. Hevert, as follows:

> I will . . . briefly compare and contrast the testimony of the Company's expert witness, Mr. Hevert, with my testimony. We both base our recommendations primarily on DCF/TGDCF analyses applied to an electric comparison group and a combination comparison group. The main reason for the difference in our recommendations is due to the different periods to which we applied our DCF and TGDCF analyses, and to Mr. Hevert's reliance to some degree on his risk premium and CAPM results. First, Mr. Hevert's analysis is based on average [daily] prices over 30, 90 and 180 day-periods. In contrast, my analysis is based on [average daily prices over] a 30-day period only. As I explained in my direct testimony, using the average prices over a 90-day or 180-day period is inappropriate because it represents outdated market information that may not be relevant to the forward looking DCF analysis.
>
> Second, for his updated 30-day period analysis, Mr. Hevert calculated the dividend yields using the average prices over the period May 1, 2014 to May 30, 2014. In contrast, my updated dividend yields are based on the average prices over the period June 7, 2014 to July 7, 2014. Thus, my updated DCF and TGDCF analyses better reflect the current market expectations regarding the expected rate of return on equity for NSP. Finally, I note that updating Mr. Hevert's DCF and TGDCF analyses, using the period June 7, 2014 to July 7, 2014, and using Mr. Hevert's assigned weights of 80 percent and 20 percent to his electric and combination group, respectively, results in a rate of return on equity of 9.59 percent, including an allowance for flotation costs. That is, his updated rate of return on equity is 5 basis points lower than my recommendation.

40. In his opening statement Dr. Amit also explained the main shortcomings of Mr. Glahn's analyses on behalf of ICI Group. Dr.Amit stated:

Mr. Glahn's Recommendation on behalf of the ICI Group

Mr. Glahn performed four DCF analyses each using different growth rates. My disagreements with Mr. Glahn's analyses are detailed in my Rebuttal Testimony. To summarize:

1. Mr. Glahn's selection of companies to be included in his comparison group was somewhat arbitrary and inconsistent.
2. His DCF analyses were technically incorrect and except for his earnings growth rate DCF, his DCF analyses were based on inappropriate expected growth rates.
3. His earnings growth rates DCF analysis produced unreasonable results for certain companies such as 5.89% return for Consolidated Edison and 6.55% for Northwestern Corporation.

DOC Ex. at 2-3(Amit Opening Statement).

B. Overview of Cost of Common Equity and Fair Rate of Return

41. A fair rate of return is, by definition, that rate which, when multiplied by the rate base, will give the utility a reasonable return on its total investment. Minn. Stat. § 216B.16, subd. 6 (2014). DOC Ex. 400 at 2 (Amit Direct). The sum of a utility's fair return, operating expenses, depreciation expenses and taxes equals the utility's total revenue requirement. *Id.*

42. In the regulated utility industry, the role normally assumed by competition is assumed by regulatory agencies, which must ensure that public utilities provide an appropriate supply of satisfactory services at reasonable rates. To provide these services, the utility must be able to compete for necessary funds in the capital markets. To attract these funds the utility must earn enough to offer competitive returns to investors. Thus, a fair return is one that enables the utility to attract sufficient capital, at reasonable terms. *Id.*

43. The Commission must set rates that are just and reasonable. Minn. Stat. § 216B.03 (2014). The determination of reasonableness involves a balancing of consumer and utility interests. A reasonable rate enables a public utility not only to recover operating expenses, depreciation and taxes, but also to compete for funds in capital markets. Minnesota law recognizes this principle when it defines a fair rate of return as the rate that, when multiplied by the rate base, will give a utility a reasonable return on its total investment. Minn. Stat. § 216B.16, subd. 6 (2014).

44. The United States Supreme Court defined the proper regulatory balance between the investments made by investors and ratepayers, in the *Bluefield* and *Hope* cases. The Court held in *Bluefield Waterworks & Improvement Co. v. Pub. Serv. Comm'n of W. Va* (*Bluefield*), 262 U.S. 679 (1923), that a utility's return must be reasonably sufficient to assure financial soundness and provide the utility adequate means to raise capital. The Court concluded that a utility had no right to large profits similar to those realized in speculative ventures, but that the utility's return:

> [S]hould be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under

> efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.

Bluefield, 262 U.S. at 693.

45. In *Fed. Power Comm'n vs. Hope Natural Gas Co.* (*Hope*), 320 U.S. 591 (1944), the Court reaffirmed and refined the *Bluefield* principles. The *Hope* Court reiterated the investor requirement for a return sufficient to cover operating expenses, including services on debt and dividends on stock and to assure confidence in the utility's ability to maintain credit and attract capital. The Court added that a just and reasonable return should be similar to returns on investments in other businesses having a corresponding risk. *Hope*, 320 U.S. at 603.

46. In addition, the Court acknowledged that regulation must attempt to strike an equitable balance between investors and ratepayers. In *Covington and Lexington Turnpike Road Co. v. Sanford* (*Covington*), 164 U.S. 578 (1896), the Supreme Court recognized:

> [S]tockholders are not the only persons whose rights or interests are to be considered. The rights of the public are not to be ignored. . . . The public cannot properly be subjected to unreasonable rates in order simply that stockholders may earn dividends.

Covington, 164 U.S. at 596.

47. In *Fed. Power Comm'n v. Natural Gas Pipeline Co. of Am.*, 315 U.S. 575 (1942), the Court reemphasized this point:

> The consumer interest cannot be disregarded in determining what is a "just and reasonable" rate. Conceivably, a return to the company of the cost of service might not be "just and reasonable" to the public.

Id. at 607 (Black, J., concurring).

48. To determine a fair rate-of-return on common equity capital for Xcel, the DOC used the following economic guidelines, as set forth in the *Bluefield* and *Hope* cases.

- The rate of return should be sufficient to enable the regulated company to maintain its credit rating and financial integrity.
- The rate of return should be sufficient to enable the utility to attract capital at reasonable terms.
- The rate of return should be commensurate with returns being earned on other investments having equivalent risks.

DOC Ex. 400 at 3 (Amit Direct).

C. Determining a Fair Rate of Return on Equity

49. One of the main goals of rate setting, as noted above, is to ensure that the utility has a reasonable opportunity to recover capital costs of providing adequate electric service. DOC Ex. 400 at 2 (Amit Direct). The cost of equity capital to Xcel is the rate of return that it may pay to investors to induce them to invest in its regulated operations. DOC Ex. 400 at 3-4 (Amit Direct). To estimate this cost, DOC Witness Amit used a market-oriented approach and relied on the concept of "opportunity costs." *Id.* Investors are faced with many investment opportunities in the financial markets. To attract investors, Xcel must pay an equity return similar to the equity return that investors expect to earn on investments of comparable risk. *Id.* This rate of return is the cost of equity capital to NSP.

1. The cost of common equity capital: discounted cash flow (DCF) method

50. When investors buy the common stock of a utility, they acquire the right to share any dividends that the company may declare in the future. The prospect of these dividends serves as an inducement to investors. DOC Ex. 400 at 3-4 (Amit Direct). Investors' expected dividend divided by the purchase price of the stock (the expected dividend yield) is a critical component of the cost of equity capital. *Id.* at 4.

51. Financial theory postulates that the price of the stock in the present period equals the present value of all the expected future dividends discounted by the appropriate rate of return. *Id.* If annual dividends grow at a constant rate over an infinite period, the required rate of return on common equity capital can be estimated using the following formula:

> The expected (required) rate of return on equity = the expected dividend yield + the expected growth rate in dividends.

DOC Ex. 400 at 4-5 (Amit Direct).

52. The Discounted Cash Flow (DCF) method reflected in the formula above (also called the Constant Growth Rate DCF Method) is a reasonable market-oriented method for determining a fair ROE for Xcel. *Id.* at 4-5; DOC Ex. 401 at EA-32 (Amit Direct Att.). The ALJ agrees.

53. A variation of the DCF model, the Two Growth Rate DCF (TGDCF), accounts for situations where, for a relatively short time period, the dividends may be expected to grow annually at a different rate than they may be expected to grow over the long-term. DOC Ex. 400 at 5-6 (Amit Direct); DOC Ex. 401 at EA-32 (Amit Direct Att.). Specifically, the short-term earnings growth rates may be either unusually low or unusually high, relative to a Company's historical earnings and the industry averages. Accordingly, short-term earnings growth may result in unreasonably low or high DCF estimated ROEs. In either case, to the degree that such growth rates may not be sustainable in the long-run, the TGDCF method accommodates two different growth rates: short-term and long-term (sustainable) growth rates. DOC Ex. 400 at 38 (Amit Direct). DOC Witness Dr. Amit applied the TGDCF to five companies in his Final Electric Comparison Group (FECG), because of their relatively high or low growth rates in

comparison to the mean expected growth rate for the FECG. DOC Ex. 400 at 35-36 (Amit Direct).

D. The DOC's Recommended ROE of 9.64 Percent Is Reasonable

54. The DOC recommends that the Commission adopt an ROE of 9.64 percent for Xcel based on the DOC's DCF and TGDCF analyses. DOC Ex. 403 at 2 (Amit Surrebuttal). The following discussion explains the DOC's DCF/TGDCF analyses and demonstrates the bases for its recommended ROE for Xcel. The discussion focuses first on selection of a comparable group of companies with risks similar to NSP and Xcel, and then addresses the application of DCF and TGDCF analyses including adjustments for flotation costs. The Department's recommended ROE of 9.64 percent is reasonable.

1. Selecting Comparable Groups

55. NSP is a division company of Xcel Energy and, as such, is not publicly traded on any of the stock exchanges. Therefore, no DCF analysis can be directly performed on NSP. DOC Ex. 400 at 6-7 (Amit Direct). When a company's (or division's) stock is not publicly traded, alternative applications of the DCF model are available. First, a DCF analysis could be performed on the parent company. *Id.* In 2012, Xcel received a very significant percent of its revenues and net income from its regulated electric operations; therefore a DCF analysis directly applied to Xcel Energy could provide useful information regarding the cost of equity for NSP. *Id.* at 6-7. However, a DCF analysis on a single company may be more sensitive to the random nature of stock prices and an analyst's specific growth-rate predictions. Therefore, Dr. Amit performed a DCF analysis for Xcel as part of his DCF analysis for his combination group. *Id.* at 7.

56. A second alternative is to perform a DCF analysis on a group of companies with investment risks similar to that of division within a company. *Id.* As noted above, to attract investors, Xcel must pay investors an equity return similar to the equity return they expect to earn on investments of comparable risk. DOC Ex. 400 at 4 (Amit Direct). Thus the cost of common equity capital for companies with comparable risk provides an appropriate proxy for the cost of common equity capital for Xcel. Therefore, to estimate the cost of equity for NSP, DOC's Dr. Amit used DCF and TGDCF analyses for groups of companies with investment risks similar to that of NSP. Additionally, he used the Capital Asset Pricing Model (CAPM) to check the reasonableness of the results of his DCF and TGDCF analyses. *Id.*

57. It is a well-accepted financial principal that companies with similar investment risks are expected to have similar required rates of return. Thus, the goal of selecting a comparable group for a DCF analysis is to find companies that have similar investment risks, from the perspective of investors, to Xcel. DOC Ex. 400 at 8 (Amit Direct). The DOC selected companies for its two comparable groups (the all-electric group called the Final Electric Comparison Group (FECG), and the combination electric and gas group called the Final Combination Comparison Group (FCCG) that passed the following screens:

- Has an SIC code of 4911 (Electric Services) for the Electric Comparison Group, and 4931 (Electric and other Services) for the Combination Comparison Group,
- Publicly trades shares on a stock exchange,
- Is domestic, not a foreign company,
- Currently pays dividends,
- Mainly provides regulated retail electric services,
- Has bond ratings within the BBB- to A+ range (Xcel's rating is A-),
- Had 2012 regulated revenues and regulated operating incomes that were at least 60 percent of total revenues or operating incomes,
- Has both a beta and standard deviation that deviated by no more than one standard deviation from the group's mean (both are measures of investment risk),
- Is not expected to merge into or be acquired by another company in the near future, and
- Has positive growth-rate projections from expert analysts.

DOC Ex. 400 at 10-14 (Amit Direct). Additionally, DOC Witness Amit eliminated companies whose DCF analyses resulted in ROEs that were too low to be reasonable based on well-established financial principles (*i.e*., an ROE less than 8 percent). DOC Ex. 400 at 14-17 (Amit Direct).

58. Finally, the DOC checked the investment risk- comparability of its FECG and FCCG groups to that of Xcel and NSP by evaluating readily available measures of investment risk (*i.e*., the volatility of rates of return, common equity ratios and long-term debt ratios). Specifically, the volatility of the rate of return as measured by either the beta or by the Standard Deviation of Price Changes (STDPC) is an important measure of the risk of investing in common stock. DOC Ex. 400 at 9-10 (Amit Direct). The standard deviation of returns measures the total variability in a security's returns. As this standard deviation rises, the uncertainty of the future returns also rises. The beta measures only a portion of the variability in a stock's return – the portion that maintains a systematic relationship with a broad market index. The beta indicates the direction and degree of change in a stock's return relative to changes in the market's return as a whole. *Id.*

59. Beta is the most direct measure of investment risk and is directly used to estimate the required rate of return on equity. Moreover, beta is the most readily available risk measure to investors. In addition bond ratings is another widely used investment risk measure which reflects both business and financial risks. Based on Dr. Amit's examination of these two measures (beta and bond ratings), Xcel's investment risk is somewhat smaller than the investment risks of the two comparison groups. DOC Ex. 400 at 21 (Amit Direct). Also based on the equity ratios, the long-term debt ratios and the bond rating for NSP (the only three risk measures available for NSP), Dr. Amit concluded that NSP is somewhat less risky than the two comparison groups. DOC Ex. 400 at 21-22 (Amit Direct). The ALJ agrees.

2. The Expected Growth Rate of Dividends

60. Any DCF analysis requires a determination of expected growth rates of dividends and expected dividend yields. DOC Ex. 400 at 22 (Amit Direct). For the expected growth rates of dividends, historical growth rates may be poor indicators of future growth rates for the comparison group. For most utilities, returns on equity and payout ratios have not remained constant, and growth in book value has occurred not only due to retained earnings, but also due to the issuance of new shares of common stock. *Id.* at 23. Moreover, in recent years, the electric utility industry has experienced significant changes including, among other things, the creation of Independent Transmission Companies, Independent System Operators, and the introduction of retail competition in certain areas of the country. *Id.* As a result, historical growth rates may be poor indicators of future growth rates. *Id.*

61. Therefore, Dr. Amit used only the projected growth rates in earnings per share (EPS). DOC Ex. 400 at 24, 25-29 (Amit Direct). He used the projected growth rates in earnings per share (EPS) provided by the following three widely-used and respected investor services: Zacks Investment Research (Zacks), The Value Line Investment Survey (Value Line or VL), and the First Call Consensus long-term earnings growth rate estimate provided by Thomson Financial Network (Thomson). *Id.* It is reasonable to rely only on the projected EPS growth rate for several reasons including that the long-run sustainable growth in dividends is solely driven from the growth in earnings. *Id.* at 27-29.

3. The Expected Dividend Yield

62. The second component of the DCF analysis is the expected dividend yield, D_1/P_0, where P_0 is the current price and D_1 is the dividend in the next period. DOC Ex. 400 at 24 (Amit Direct). The use of this dividend yield assumes that dividends are distributed at the end of each period (year). *Id.* at 24, 30. Regarding the price component, recent prices must be used since the current price per share incorporates all relevant publicly available information. *Id.* at 24. Using non-recent (historical) prices in calculating the expected dividend yield would be inappropriate. *Id.* Additionally, share prices are very volatile in the short run. *Id.* Therefore, one must use a period of time long enough to avoid short-term aberrations in the capital market, yet short enough to avoid including irrelevant historical information. *Id.* To ensure that the DOC's expected dividend yield is current, and yet represents a long enough period of time to avoid very short-term aberrations in the capital market, Dr. Amit selected the most recently available four-week period of daily closing prices to calculate the expected dividend yield (October 1, 2013 to October 31, 2013). DOC Ex. 400 at 30 (Amit Direct).

4. Flotation Costs

63. The DCF analysis above must be adjusted to allow for the cost of issuing new shares of common stock without causing dilution, which is a decrease in the value of stock due solely to the cost of issuing new shares of common equity. DOC Ex. 400 at 32 (Amit Direct). This adjustment is appropriate even if no new issuances are planned in the near future because failure to allow such an adjustment may deny Xcel the opportunity to earn its required rate of return in the future. *Id.* Such a denial would be contradictory to the purpose of rate-of-return regulation. Dr. Amit demonstrated the need for an issuance-cost adjustment. DOC Ex. 400 at 32

(Amit Direct); DOC Ex. 401 at EA-34, Appendix C (Amit Direct Att.). The ALJ agrees that the DCF analysis results must be adjusted by including flotation costs.

64. Dr. Amit also agreed that Xcel's calculated flotation cost of 2.926 percent is reasonable. DOC Ex. 400 at 32-33 (Amit Direct); Xcel Ex. 27 at Schedule 3, page 1 (Hevert Direct). Xcel's flotation cost calculations appropriately account for the zero flotation costs of non-public common equity issuances and, thus, the Department adjusted its DCF results by using flotation costs of 2.926 percent. DOC Ex. 400 at 32-33 (Amit Direct). The ALJ agrees.

5. Summary of Results of DOC's DCF Analysis in Direct Testimony

65. In his Direct Testimony, Dr. Amit's DCF (including the TGDCF analyses) results for the FECG (all electric) and FCCG (combination), including flotation costs of 2.926 percent are summarized as follows:

Table 1: DCF results for FECG and FCCG

Group	Low	Mean	High
FECG	8.89%	10.02%	11.10%
FCCG	9.09%	9.47%	9.89%

DOC Ex. 400 at 37 (Amit Direct).

6. Surrebuttal Update

66. In his Surrebuttal Testimony, Dr. Amit updated his analysis, as is his normal practice, to reflect the most recently available current data. DOC Ex. 403 at 2 (Amit Surrebuttal). *See* DOC Ex. 400 at 44 (Amit Direct) (practice to update in surrebuttal). Consistent with his Direct Testimony, Dr. Amit explained that it is reasonable to use the most recently available data to calculate the expected dividend yields and the projected growth rates. DOC Ex. 403 at 1 (Amit Surrebuttal). For his FECG, Dr. Amit included one additional company, Hawaiian Electric (HE), because its updated mean expected rate of return satisfied his screen (exceeded 8.00 percent), and excluded Empire District Company (EDE) Electric because its updated expected rate of return was below 8 percent. DOC Ex. 403 at 2 (Amit Surrebuttal). Dr. Amit also excluded Pepco Holding and UIL holding because they were involved in merger and restructuring. *Id.* For his FCCG, Dr. Amit included Amern Corp. because its mean rate of return "now exceeds 8 percent." *Id.*

67. The Department updated its DCF analysis using the same methodology and sources of information used in calculating the ROE in its Direct Testimony. DOC Ex. 403 at 2-7 (Amit Surrebuttal). Dr. Amit calculated updated dividend yields using closing prices from the most recently available thirty-one day period, June 7, 2014 to July 7, 2014. *Id.* at 3. While the expected growth rates are much less likely to change significantly in such a short period, consistency requires the use of the most recently available projected growth rates as well. *Id.* In his Surrebuttal analysis, Dr. Amit used the same adjustment for flotation cost as in his Direct

Testimony. *Id.* at 5. Based on his analysis in his Surrebuttal Testimony, Dr. Amit recommends a return on equity capital of 9.64 percent for NSP. DOC Ex. 403 at 7 (Amit Surrebuttal). Table 2 below summarizes Dr. Amit's updated DCF analysis. DOC Ex.403 at 6 (Amit Surrebuttal). The ALJ agrees that the Department's recommended ROE of 9.64 percent is reasonable.

Table 2: Updated DCF results for FECG and FCCG

Group	Low	Mean	High
FECG	8.90%	9.72%	10.59%
FCCG	8.90%	9.52%	10.09%

7. DOC's Checks on the Reasonableness of its DCF Recommendations

68. As a check on the reasonableness of its DCF analysis, the Dr. Amit estimated the ROE using the Capital Asset Pricing Model (CAPM). DOC Ex. 400 at 37-42 (Amit Direct).

a. DOC's CAPM (Direct Testimony)

69. The CAPM's basic premise is that any risk that is company-specific can be diversified away by investors. Therefore, the only risk that matters is the systematic risk of the stock. *Id.* at 37. This systematic risk is measured by beta. *Id.*; *see id.* at 16 (discussing beta as measure of system market risk). In its simplest form, the CAPM assumes the following:

$k = r + beta\ (k_m - r)$, where:

k is the required rate of return for the stock in question;

r is the rate of return on a riskless asset; and

k_m is the required rate of return on the market portfolio.

DOC Ex. 400 at 37 (Amit Direct). While the CAPM is theoretically sound, its use raises some difficult issues including difficulties in determining the appropriate beta, the appropriate riskless asset, and the effect of taxes. For these reasons, Dr. Amit used the CAPM results only as a check on the reasonableness of his DCF analyses. *Id.* The ALJ agrees that the CAPM is a reasonable method for checking the reasonableness of DCF results.

70. Dr. Amit used the 20-year treasury bonds for the risk free asset, the Value-Line betas for beta and the S&P 500 Index for the market portfolio. DOC Ex. 400 at 37-41 (Amit Direct). Using the CAPM formula k = r + beta (km-t), Dr. Amit's CAPM results were:

FECG: 3.50% + 0.745 x (11.70% - 3.50%) = 9.61%, or 9.73% including flotation costs

FCCG: 3.50% + 0.736 x (11.70 - 3.5%) = 9.54%, or 9.66% including flotation costs

DOC Ex. 400 at 41 (Amit Direct). Dr. Amit referred to the CAPM results based on the expected return on the market as the "ex-ante" CAPM results. *Id.*

b. Comparison of CAPM to DOC's DCF (Direct Testimony)

71. Dr. Amit's CAPM's ROE was reasonably close to the lower end of Dr. Amit's DCF's ROE for both the FECG and FCCG groups. DOC Ex. 400 at 42 (Amit Direct). A summary of Dr. Amit's DCF analyses and his Ex-Ante CAPM analyses is shown with flotation cost adjustments in the following table:

Table 3: Summary of DOC DCF Analyses (Amit Direct)

DCF

Group	Low	Mean	High
FECG	8.89%	10.02%	11.10%
FCCG	9.09%	9.47%	9.89%

Ex-Ante CAPM

FECG	9.73%
FCCG	9.66%

DOC Ex. 400 at 42 (Amit Direct)

72. Because the Ex-Ante CAPM's results are inside the range of Dr. Amit's DCF results for the FCCG group and for the FECG group, respectively, Dr. Amit concluded that Ex-Ante CAPM's results confirmed the reasonableness of the DOC DCF's results for the required rate of return for NSP. *Id.*

8. DOC's Updated (Surrebuttal) CAPM Analysis

a. Updated CAPM estimates

73. In his Surrebuttal Testimony, Dr. Amit updated both his CAPM analyses to check the reasonableness of his updated DCF/TGDCF analyses. Using the CAPM formula, $k = r + \text{beta}(k_m - r)$, the DOC's updated ex-ante CAPM estimates were:

FECG: 10.05% including flotation costs

FCCG: 9.55% including flotation costs.

DOC Ex. 403 at 8 (Amit Surrebuttal).

b. DOC conclusion of updated checks on reasonableness of updated DCF

74. As shown above, the DOC's updated checks on the reasonableness of the updated DCF analyses resulted in ROE calculations that were inside the DCF's ranges for the FECG and FCCG, respectively (Table 2 above). Therefore, Dr. Amit concluded that when using expected risk premiums, the ex-ante CAPM is useful in confirming the reasonableness of his updated DCF estimates for the required rate of return on equity for NSP. DOC Ex. 403 at 7-8 (Amit Surrebuttal). The ALJ agrees.

E. DOC Criticism of NSP's Cost of Common Equity Analyses

1. Xcel's DCF Is Flawed

75. Dr. Amit examined Xcel's DCF analysis in detail and concluded that it is flawed for two main reasons. The ALJ agrees. First, Xcel used longer-term historical prices to calculate the dividend yield. DOC Ex. 400 at 57-58 (Amit Direct). The Company performed DCF analyses using prices for a 30-day, 90-day and 180-day period to calculate the dividend yields. *Id.* at 57. Using a 30-day period to calculate the dividend yield is appropriate because it is consistent with the basic financial principle that financial markets are efficient such that the current stock prices fully reflect all publicly available information. *Id.* at 57. For the same reason, Xcel's use of longer-term historical prices may result in biased dividend yields that reflect irrelevant outdated information. *Id.* at 57-58.

76. Dr. Amit showed that Xcel's 90-day and 180-day average dividend yields are 16 basis points and 30 basis points lower, respectively, than the 30-day average dividend yield. DOC Ex. 400 at 58 (Amit Direct). Moreover, using 90-day and 180-day average dividend yields may create a mismatch between such dividend yields and more recent projected growth rates. *Id.*

77. Using only Xcel's 30-day dividend yield analysis, Dr. Amit calculated the required ROE for NSP, using Xcel's comparison groups. DOC Ex. 400 at 59 (Amit Direct). The DCF ROE for Xcel's comparison groups, HECG and HCCG, including flotation costs, were as follows:

Table 4: DOC Calculation of Xcel's DCF results for HECG and HCCG, using only the 30-day average dividend yield

Group	Low	Mean	High
HECG	9.44%	10.18%	10.90%
HCCG	9.06%	9.63%	10.21%

DOC Ex. 400 at 59 (Amit Direct).

78. Second, Xcel's DCF analysis is flawed because the Company did not show that it is reasonable to assign at least 80 percent weight to its electric comparison group (HECG) and no

more than 20 percent weight to its combination comparison group (HCCG). DOC Ex. 400 at 60 (Amit Direct).

79. Dr. Amit discussed how Mr. Hevert assigned weights to his HECG and HCCG. DOC Ex. 400 at 60 (Amit Direct). *See also* DOC Ex. 403 at 16 (Amit Surrebuttal). Specifically, Mr. Hevert argued that no more than 20 percent weight should be assigned to his estimated ROEs for his HCCG because this proceeding is about determining the rate of return for NSP's electric operations and, as such, at least 80 percent weight should be assigned to his estimated ROEs for his HECG. Xcel Ex. 27 at 21 (Hevert Direct). Dr. Amit explained that according to Mr. Hevert, over the period 2011–2013, NSPM derived an average of 91.67 percent of its net income from electric operations, *id.,* while Dr. Amit noted that his FECG derived an average of 90 percent of its net income from electric operations. DOC Ex. 403 at 16 (Amit Surrebuttal). For the same time period, Dr. Amit's FCCG derived an average of only 78.39 percent of its net income from electric operations. *Id.* Therefore, according to Mr. Hevert, the weights assigned to FECG and FCCG should reflect the differences between the net income received from their electric operations and the amount Xcel receives from its electric operations. *Id.* (citing Xcel Ex. 28 at 18 (Hevert Rebuttal)).

80. Dr. Amit did not agree that Mr. Hevert's argument on this issue was reasonable. DOC Ex. 400 at 60 (Amit Direct); *see also* DOC Ex. 403 at 16-17 (Amit Surrebuttal). As Dr. Amit testified, under well-accepted financial principles, the required rate of return for a company is closely related to the financial and business risk of the company. DOC 400 at 19–20, 60 (Amit Direct). Thus, as long as the investment risks for Mr. Hevert's HECG and HCCG groups are similar and as long as the companies in both his comparison groups operate under similar economic and regulatory environments, there should not be a significant difference between the weights assigned to the estimated ROE's for the two groups. *Id.* at 60. Moreover, while Mr. Hevert screens the companies for his HECG and HCCG groups based on different measures of their percentage of electric operation, Value Line, a widely used investment service, lists all of the companies in Mr. Hevert's HECG and HCCG groups as electric utilities. *Id.* The difference in the percentage of net income derived from electric operations may not be a significant indicator of risk and therefore, may have an insignificant impact on the required rate of return on equity. DOC Ex. 403 at 17 (Amit Surrebuttal). In principle, it is the overall investment risk, not the percentage of income received from electric operations, that should determine the appropriate required rate of return on equity. *Id.*

81. According to SIC definitions, the definition of SIC 4911, Electric Services, is as follows:

> This industry classification includes establishments engaged in generating, transmitting and distributing electricity.

SIC 4931, Electric and Other Services Combined, is defined as:

> Establishments primarily engaged in providing electric services in combination with other services, with electric services as the major part though less than 95 percent of the total.

DOC Ex. 400 at 61 (Amit Direct). So, based on the SIC Codes and the VL classification, investors may not view companies in the HECG and the HCCG groups as being significantly different from each other. *Id.* For example, three of the companies in Hevert's HCCG, Black Hills Corp., Dominion Resources, and UIL Holdings, are classified as electric utilities with an SIC 4911. *Id.* Therefore, as Dr. Amit explained, assigning *four times* more weight to the HECG than to the HCCG, as done by Mr. Hevert, may inappropriately bias Mr. Hevert's estimated ROEs toward his estimates for his HECG. DOC Ex. 400 at 61 (Amit Direct).

2. Xcel's Application of the CAPM is Flawed

82. The Department provides only a short summary of the issue of Xcel's flawed application of the CAPM. Dr. Amit largely agreed with Mr. Hevert's CAPM parameters with three key exceptions. DOC Ex. 400 at 63 (Amit Direct). The main three flaws of the Company's CAPM analysis are:

1. It used the 30-year treasury bonds as the risk-free asset. The yield on such an asset includes interest risk premium.
2. It used the wrong yield to calculate the risk premium. It used the projected yield on 30-year bond rather than the current yield.
3. Mr. Hevert incorrectly estimated the ROEs for his market portfolio, because he applied DCF analyses to individual companies that issue no dividends.

Id. at 63-64.

83. Dr. Amit corrected these flaws. Table 5 below summarizes Mr. Hevert's corrected CAPM ROE estimates.

Table 5: Adjusted Mr. Hevert CAPM ROEs

Group	Low ROE	Mean ROE	High ROE
HECG	9.07%	9.65%	10.22%
HCCG	9.22%	9.72%	10.21%
60/40 Percent Weights	9.13%	9.68%	10.22%

DOC Ex. 400 at 64-65 (Amit Direct).

84. Using the current yield on twenty-year Treasury bonds, and adjusting Mr. Hevert's market portfolio DCF analyses to account for companies with no dividends, Dr. Amit showed that Mr. Hevert's corrected CAPM's ROE estimates are very close to Dr. Amit's CAPM's ROE estimates:

	Electric Group	Combination Group
Dr. Amit	9.73%	9.66%
Mr. Hevert	9.65%	9.72%

DOC Ex. 400 at 66 (Amit Direct).

3. Mr. Hevert's Risk Premium Analysis

85. As noted above, Mr. Hevert estimated the risk premium between the allowed returns on equity for regulated electric utilities and the yields on thirty-year Treasury bonds. DOC Ex. 400 at 66 (Amit Direct) (citing Xcel Ex. 27 at 44 and RBH-1, Schedule 7 (Hevert Direct)). Using an econometric model, he estimated the risk premium as a function of the yields on long-term Treasury bonds. *Id.* He used the following equation:

> Risk Premium = Constant (c) + a * NL (Treasury yield)
>
> where the risk premium = allowed rate of return for electric utilities minus the yield on thirty-year Treasury bonds, and NL = natural logarithm.

DOC Ex. 400 at 66 (Amit Direct).

86. Using regression analysis and data from January, 1980 through September, 2013, Mr. Hevert estimated the constant, c, to be -0.0308 and the coefficient, a, to be -0.0294. *Id.* at 44 (citing Xcel Ex. 27 at RBH-1, Schedule 7 (Hevert Direct)). Using the Blue Chip forecasted yields on thirty-year Treasury bonds of 3.95 percent and the current yield of 3.79 percent, his estimated ROE's would be 10.37 percent and 10.33 percent, respectively. *Id.*

87. Dr. Amit concluded that Mr. Hevert's Bond Yield Plus Risk Premium analysis was not reasonable. DOC Ex. 400 at 66 (Amit Direct). Dr. Amit explained that Mr. Hevert's regression analysis assumes that both coefficients, c = -0.0308 and a = -0.0294, are stable over time and do not depend on investors adjusting their expectations depending on different Federal monetary and fiscal policies. *Id.* at 67. To the degree, however, that investors adjust their behavior to adapt to changing Federal policies, both of the coefficients (c and a) are *not* stable and *cannot* be used to estimate the expected risk premium. *Id.*

88. As discussed in Mr. Hevert's Direct Testimony, the recent economic environment has two significant impacts on the risk premium. DOC Ex. 400 at 67 (Amit Direct) (citing Xcel Ex. 27 at 8–14 (Hevert Direct)). First, while the risk premium as measured by historical data declined, the expected risk premium may have actually increased due to the increased risks of investing in common equity relative to investment in treasury bonds. *Id.* Second, due to the increased risk of investing in common equity, investors substituted investment in fixed income securities, such as Treasury bonds, for investment in common equity. *Id.* As a result, the current yields on risk-free assets are lower than they would have been, absent the economic crisis. *Id.* Moreover, recent yields on Treasury bonds have started to rise due to the increased uncertainty regarding continuation of the Federal Reserve's "Quantitative Easing" policies. *Id.* In fact, on December 18, 2013, the Federal Open Market Committee (FOMC) announced that starting in January, 2014, the Federal Reserve will reduce its open market purchases of long-term treasuries and mortgage-backed securities by $10 million. *Id.* The factors mentioned above may have caused the estimated values of c and a to change, counter to Mr. Hevert's regression analysis that

assumes the coefficients c and a are stable over time. DOC Ex. 400 at 68 (Amit Direct). For this reason, Mr. Hevert's regression-based risk premium analysis may be inappropriate. *Id.*

4. Summary of DOC-Modified Xcel DCF and CAPM Results

89. Mr. Hevert's recommendation relies mainly on his DCF analysis. DOC Ex. 400 at 66 (Amit Direct). He also uses CAPM and Risk Premium analyses to support his DCF estimates. *Id.* Table 6 below summarizes Mr. Hevert's estimated ROEs, which include Dr. Amit's recommended modifications:

Table 6: Mr. Hevert's Estimated ROEs Including DOC Modifications

	DCF			CAPM		
Group	Low	Mean	High	Low	Mean	High
HECG	8.79%	9.63%	10.67%	9.07%	9.65%	10.22%
HCCG	8.82%	9.43%	10.00%	9.22%	9.72%	10.21%
Weighted Average	8.80%	9.55%	10.40%	9.13%	9.68%	10.22%

For the DCF results *see* DOC Ex. 403 at 22 (Amit Surrebuttal); for the CAPM results *see* DOC Ex. 400 at 68 (Amit Direct). Dr. Amit did not update Mr. Hevert CAPM analysis in his Surrebuttal Testimony. *Id.* As shown by Dr. Amit, Mr. Hevert's ROE for Xcel, as corrected, would be 9.55 percent rather than the 10.25 percent recommended by Mr. Hevert. *Id.*

F. DOC Response to the ICI Group's Mr. Glahn

90. In his Direct Testimony, ICI Group witness William L. Glahn recommended that the Commission grant NSP an ROE of 9.00 percent. DOC Ex. 402 at 1 (Amit Rebuttal) (citing ICI Ex. 250 at 15 (Glahn Direct)). Mr. Glahn performed four DCF analyses on what, in his opinion, is a risk comparable group of utilities, which Dr. Amit referred to as the Glahn Comparison Group. DOC Ex. 402 at 2 (Amit Rebuttal); *see* ICI Ex. 250 at 19–24 (Glahn Direct). Dr. Amit disagreed that Mr. Glahn's recommended ROE was reasonable, for two overall reasons: 1) Mr. Glahn's selection of companies for the Glahn Comparison Group was not reasonable; and 2) Mr. Glahn's DCF analyses were incorrectly performed. DOC Ex. 402 at 6-13 (Amit Rebuttal).

1. The Glahn Comparison Group was flawed

91. Dr. Amit demonstrated that the Glahn Comparison Group was flawed and the ALJ agrees. Mr. Glahn stated that he eliminated the companies listed in Value Line that were listed under the Electric Utility Industry and had negative projected earnings per share and/or dividend per share growth rates. DOC Ex. 402 at 2-3 (Amit Rebuttal). However counter to this screen, Mr. Glahn eliminated from his comparison group several companies with positive projected earnings per share and dividend per share growth rates. DOC Ex.402 at 2-6 (Amit Rebuttal). At the evidentiary hearing, Mr. Glahn could not reconcile the fact that he eliminated companies from his comparison group with positive projected EPS and DPS growth rates with

his screen that "companies that are not expected by *Value Line* to enjoy earnings and/or dividend growth during the period studied were not considered." Tr.V. 3 at 117–134 (Glahn); ICI Ex. 250 at 17 (Glahn Direct) (emphasis in original). The Glahn Comparison group is arbitrary and is not accepted.

2. Mr. Glahn's DCF Analyses were flawed

92. Mr. Glahn's DCF analyses were incorrectly performed. Mr. Glahn performed four different DCF analyses: dividend growth rates, earning growth rates, sustainable 2014 growth rates and sustainable growth rates. DOC Ex.402 at 6 (Amit Rebuttal). For all of his DCF analyses, Mr. Glahn used incorrect expected growth rates and incorrect expected dividend yields. DOC Ex.402 at 6-13 (Amit Rebuttal). Therefore, the ALJ finds that Mr. Glahn's DCF analyses are without merit and should be rejected.

3. Flotation costs

93. Mr. Glahn argued that because Xcel does not plan to issue common stock in 2014, the DCF should not include flotation cost adjustment. This claim is not reasonable. DOC Ex. 402 at 11-12 (Amit Rebuttal). Dr. Amit demonstrated that flotation costs adjustments are required even if no new common equity issuances are planned for the test-year. *Id.*; DOC Ex. 400 at 32 (Amit Direct); DOC Ex. 401 at EA-34 (Amit Direct Att.).

94. Mr. Glahn's proposed ROE is unreasonable.

G. DOC Response to the Commercial Group

95. Commercial Group witness Mr. Chriss testified that the Commission should consider the authorized ROEs in other states to help it determine the appropriate ROE for NSP. DOC Ex. 402 at 15 (Amit Direct) *citing* CG Ex. 225 at 8–9 (Chriss Direct). Moreover, Mr. Chriss testified that inclusion of construction work in progress (CWIP) in the rate base reduces NSP's risk, and therefore, such an inclusion should result in a lower ROE for NSP. DOC Ex. 402, *supra* at 14; CG Ex. 225 *supra* at 11.

96. Dr. Amit showed that the use of recently authorized ROEs in other states to determine Xcel's ROE in this rate case is flawed for the following reasons. First, to avoid circularity, it is necessary to include non-regulated companies in any analysis comparing ROEs, since the allowed rates of return for regulated companies are highly influenced by the regulatory process. DOC Ex. 402 at 15 (Amit Rebuttal). Second, the state decisions cited by Mr. Chriss are based on outdated data. *Id.* That is, Mr. Chriss cited decisions issued over the period 2012, 2013 and in the first part of 2014. *Id.* Such decisions, however, are based on analyses completed at least six months, if not nine months, prior to the decision's issuance. *Id.* Therefore, the ROEs cited by Mr. Chriss are outdated and cannot be used to determine the appropriate ROE for NSP at this time. *Id.*

97. Regarding the issue of CWIP, investors are well aware of its regulatory treatment. DOC Ex. 402 at 16 (Amit Rebuttal). Moreover, NSP's treatment of CWIP in this rate case is consistent with its treatment of CWIP in its prior Minnesota rate cases. DOC Ex. 402 at 16 (Amit

Rebuttal). To the degree that the treatment of CWIP impacts NSP's investment risk, such an impact is fully reflected in investors' required return on equity for NSP, and no additional adjustment is required. *Id.*

98. Mr. Chriss's recommended ROE for Xcel is not reasonable.

H. Decoupling Does Not Require an Adjustment to Xcel's ROE

99. Dr. Amit showed that it would be unreasonable to adjust NSP's ROE downward in the event that the Commission approves decoupling. Xcel witness Mr. Hevert and CEI witness Mr. Cavanagh both concluded that it would not be reasonable to adjust NSP's ROE downward to recognize the impact of decoupling. DOC Ex. 403 at 26 (Amit Surrebuttal) (citing Xcel Ex. 28 at 49 (Hevert Rebuttal)); CEI Ex. 290 at 5–6 (Cavanagh Direct). Mr. Hevert performed a rate-of-return analysis on electric and combination comparison groups. DOC Ex. 403 *supra* at 27; *see generally* Xcel Ex. 27 (Hevert Direct). Based on those analyses, Mr. Hevert recommended what, in his opinion, is the appropriate ROE for NSP. *Id.* Since the majority of the companies in his comparison groups have either decoupling provisions or other various revenue stabilizing policies, Mr. Hevert concluded that his comparison groups appropriately capture any lower risk associated with decoupling provisions requested by NSP. DOC Ex. 403 at 27 (Amit Surrebuttal) (citing Xcel Ex. 28 at 49 (Hevert Rebuttal)). Therefore, Mr. Hevert concluded that no additional ROE adjustment is reasonable. *Id.* Mr. Cavanagh relied on a study by the Brattle Group that concluded that decoupling may not lower utilities' cost of capital. DOC Ex. 403 at 26 (Amit Surrebuttal) (citing CEI Ex. 290 at 5 (Cavanagh Direct) and Xcel Ex. 28 at 49, 54 (Hevert Rebuttal)). AARP witness Ms. Brockway, however, argued that if the Commission approves NSP's proposal for decoupling, then NSP's allowed ROE should be adjusted downward. AARP Ex. 311 at 14–18 (Brockway Rebuttal).

100. Based on the March 20, 2014 study by the Brattle Group, Xcel Ex. 27 at RBH-1, Schedule 10 (Hevert Direct), which Dr. Amit found to be reasonable, DOC Ex. 403 at 27 (Amit Surrebuttal) and Mr. Hevert's estimated beta for Pepco Holdings shown on pages 50-51 of Mr. Hevert's Rebuttal Testimony, Dr. Amit concluded that Ms. Brockway's proposal to adjust NSP's ROE downward if the Commission approves a decoupling mechanism for NSP is not reasonable. DOC Ex. 403 at 27–28 (Amit Surrebuttal). Dr. Amit explained that the Brattle Group study showed that there is no significant difference in the cost of capital between electric utilities with and without decoupling, and that it is reasonable to conclude that Mr. Hevert's comparison groups capture any decoupling impact on risk. *Id.* at 28.

101. The Department concluded that no additional adjustment is needed to account for decoupling, in the event it is allowed by the Commission. *Id.* The ALJ agrees that no additional adjustment is necessary.

III. THE CAPITAL STRUCTURE, THE COST OF SHORT- AND LONG-TERM DEBT, AND THE COST OF CAPITAL FOR NSP, FOR 2014 (ISSUE 12-IN PART–FOR 2014)

A. NSP's Proposed Capital Structure for 2014 (Issue 47, in part-for 2014)

102. To arrive at the cost of capital (overall rate of return, ROR) for NSP, it is necessary to determine the amount of long-term debt, short-term debt, preferred stock, and common equity held by NSP. DOC Ex. 400 at 44 (Amit Direct). These amounts are represented as dollar amounts and as percentages of the total capital and are called the capital structure. *Id.* It is a well-accepted premise in financial literature that an optimal capital structure—*i.e.*, one that minimizes the overall cost of capital—exists for each company. *Id.* It is not easy, however, to test whether NSP's capital structure is reasonable. *Id.* A possible test for the reasonableness of NSP's capital structure is to compare its long-term debt ratio and equity ratio to those ratios for the comparison group. *Id.* at 44-45. If NSP's equity ratio and long-term debt ratio are similar to the averages of the two groups, we may conclude that NSP's capital structure is reasonable. *Id.* at 45.

103. NSP does, in fact, have its own capital structure apart from Xcel Energy. DOC Ex. 400 at 45 (Amit Direct). NSP issues its own debt securities which are credit rated by the various rating agencies such as S&P and Moody's. *Id.*

104. The Company proposed a projected capital structure using the test year (calendar year 2014).[5] *Id.* Its proposed capital structure is:

Table 7: NSP's Proposed Capital Structure (Direct Testimony)

Capitalization	Amount ($000's)	Percent of Total Capitalization
Long-Term Debt	$4,003,447	45.61%
Short-Term Debt	$165,474	1.89%
Common Equity	$4,608,420	52.50%
Total	$8,777,341	100.00%

Id.

1. Long-Term Debt

105. NSP calculated its proposed long-term debt component as the average balances for the twelve month period ending December, 2014, including scheduled retirements and forecasted security issuances. DOC Ex. 400 at 46 (Amit Direct). Based on Dr. Amit's review of NSP's calculation, he concluded that the calculation of the cost of long-term debt component is

[5] The calculation for each component of the capital structure is provided by the Company's witness, George E. Tyson II. DOC Ex. 400 at 45 (Amit Direct). Xcel Ex. 30 at GET-1, Schedule 6 (Tyson Direct) shows the long-term debt calculation, Xcel Ex. 30 at GET-1, Schedule 7 shows the short-term debt calculations, and Xcel Ex. 30 at GET-1, Schedule 10 shows the common equity calculations. DOC Ex. 400 at 45 (Amit Direct).

appropriate. *Id.* This calculation method is consistent with the method used in NSP's last rate case (Docket No. E002/GR-12-961). DOC Ex. 400 at 46 (Amit Direct).

2. Short-Term Debt

106. NSP's proposed short-term debt component is calculated as the twelve-month average of the month-end short-term balances ending December, 2014. DOC Ex. 400 at 46 (Amit Direct). This approach is reasonable. *Id.* at 47. Calculating a twelve-month average is an appropriate methodology to arrive at the amount of short-term debt to be included in the capital structure. *Id.* Moreover, when forecasting the monthly balances, rather than using historical actual balances, using month-end forecasted balances is appropriate. *Id.* Finally, this method of calculating short-term debt is consistent with the method used by Xcel Energy in its last rate case (Docket No. E002/GR-12-961). *Id.*

3. Common Equity Capital

107. NSP calculates its common equity as the thirteen-month average over the period ending December 31, 2014, using the month-end equity balance for each month. DOC Ex. 400 at 47 (Amit Direct). NSP's proposed common equity component in its capital structure is reasonable. *Id.* NSP's method of calculating its proposed level of common equity in its capital structure is the same as that approved by the Commission in Xcel's last rate case (Docket No. E002/GR-12-961). *Id.*

4. NSP's Proposed Capital Structure is Reasonable

108. NSP's proposed capital structure is reasonable. The average long-term debt ratio for the FECG for 2012 is 49.86 percent with a range from 44.60 percent to 59.10 percent. *Id.* at 48; DOC Ex. 401 at EA-13 (Amit Direct). NSP's proposed long-term debt ratio of 46.49 percent (excluding short-term debt) is lower than the group's average and is fairly close to the group's low end of the long-term debt ratio range. *Id.* at 48. Finally, S&P expects an A- rated company to maintain a debt ratio in the range of thirty-five to fifty percent, which indicates that NSP's long-term debt ratio is fairly close to the upper end of the range provided by S&P. *Id.*

109. Moreover, NSP's proposed equity ratio may be appropriate if it is similar to the FECG 2012 average common equity ratio. DOC Ex. 400 at 48 (Amit Direct). The FECG 2012 average common equity ratio was 50.14 percent and ranged from a low of 40.90 percent to a high of 55.40 percent (excluding short-term debt from the capital structure). *Id.* While NSP's proposed equity ratio of 53.51 percent (excluding short-term debt from the capital structure) is significantly higher than FECG's 2012 average equity ratio, it is well inside the range of equity ratios for the FECG group. *Id.* In addition, NSP's proposed equity ratio is well inside the range of the FECG's 2012 average equity ratio plus (minus) one standard deviation (this range is 44.89 percent to 55.39 percent). *Id.* Finally, NSP's proposed equity ratio is well inside the equity ratio range recommended by S&P for an A-rated utility (50 to 65 percent). *Id.*

110. Both economists and financial analysts agree that there exists an optimal (cost minimizing) capital structure for each company. DOC Ex. 400 at 49 (Amit Direct). It is also a well-accepted financial principle that, all other things the same, the higher the business risk of

the company, the higher the company's optimal equity ratio. *Id.* Given the above two principles, the exact optimal capital structure for a company cannot be analytically determined. *Id.* For any company in general, and for NSP in particular, their goal, however, is to maximize profit, which requires them to minimize costs. *Id.* Therefore, NSP has no incentive to have too much equity relative to its cost minimizing equity. *Id.* In particular, between rate cases if NSP has "too much" equity, it could increase its profit by lowering its equity ratio and thus, reduce its costs. *Id.* The main conclusion from the above discussion is that any electric utility in general, and NSP in particular, has no incentive to raise its equity ratio above the cost of capital's minimizing equity ratio. *Id.*

111. After his own analysis, Dr. Amit concluded that NSP has a reasonable equity ratio even though it is somewhat higher than the average equity ratio for the FECG. DOC Ex. 400 at 50 (Amit Direct). Further, based on his analysis of the Company's proposed capital structure, Dr. Amit concluded that it is also appropriate. *Id.* at 51. Therefore, Dr. Amit proposed to use the same capital structure as proposed by the Company, as shown above in Table 7. *Id.*

B. The Costs of Short- and Long-Term Debt

112. The Company used short-term future interest rate contracts for 2014 for estimating short-term debt costs. DOC Ex. 400 at 51 (Amit Direct). The London Interbank Offered Rate (LIBOR) provides future short-term interest rate contracts on a daily basis, which are traded on the Chicago Mercantile Exchange. *Id.* Specifically, NSP used the LIBOR's three-month rates for 2014 as forecasted by Global Insight on July, 2013. *Id.* Applying these rates to the monthly short-term debt over the period January, 2014 through December, 2014, NSP's average cost of short-term debt for 2014 is estimated at 0.67 percent, which also includes the estimated monthly fixed fees for NSP's credit facility (0.37 percent).[6] DOC Ex. 400 at 51 (Amit Direct).

113. Dr. Amit agreed that NSP's methodology and calculations are reasonable for estimating short-term debt costs. DOC Ex. 400 at 52 (Amit Direct). Using short-term interest rate future contracts is the appropriate methodology for estimating future short-term interest rates. *Id.* Therefore, Dr. Amit used a 0.67 percent rate in his analysis. *Id.*

114. Regarding NSP's proposed long-term debt cost, NSP used the average twelve-month balances for the period January, 2014 through December, 2014 to calculate its 2014 long-term debt costs.[7] DOC Ex. 400 at 52 (Amit Direct). These calculations result in a long-term debt cost of 4.93 percent, which includes a $300 million thirty-year loan to be issued on May 14, 2014 at an interest rate of 4.70 percent (the calculations are based on $200 million to reflect eight months of 2014). *Id.* The rate of 4.70 percent is based on the LIBOR's forecasted yields for thirty-year loans in the second quarter of 2014. *Id.*

---

[6] The calculations of this average rate are shown at Xcel Ex. 30 at GET-1, Schedule 7 (Tyson Direct). DOC Ex. 400 at 51 (Amit Direct).

[7] The Company's calculations are shown in at Xcel Ex. 30 at GET-1, Schedule 6 (Tyson Direct). DOC Ex. 400 at 52 (Amit Direct).

115. After reviewing the Company's calculations, Dr. Amit concluded that the Company's proposed cost of long-term debt of 4.93 percent is reasonable. DOC Ex. 400 at 52 (Amit Direct). Therefore, Dr. Amit used this cost in calculating the overall cost of capital for NSP. *Id.*

C. The Initial 2014 Cost of Capital for NSP

116. Based on Dr. Amit's initial recommended ROE of 9.80 percent, short-term debt cost of 0.67 percent, and long-term debt cost of 4.93 percent, Dr. Amit's initial recommended 2014 cost of capital for NSP was 7.41 percent, as follows:

Table 8: Overall Initial 2014 Cost of Capital for NSP

Component	Capitalization Ratio (%)	Cost (%)	Weighted Cost (%)
Long-Term Debt	45.61	4.93	2.25
Short-Term Debt	1.89	0.67	0.013
Common Equity	52.50	9.80	5.15
Total	100.00		7.41

DOC Ex. 400 at 53 (Amit Direct).

D. NSP's Updated 2014 Proposed Capital Structure, Updated Cost of Common Equity, and the Updated Overall Cost of Capital for NSP

117. While NSP witness George Tyson used the same methodologies in his Rebuttal Testimony as he did in his Direct Testimony, he updated NSP's capital structure in his Rebuttal Testimony based on more recent available information. DOC Ex. 403 at 10 (Amit Surrebuttal) (citing Xcel Ex. 31 at 25–28 (Tyson Rebuttal)). Mr. Tyson explained that the changes included in the Company's updated capital structure included:

1. The actual 4.125 percent interest rate on the $300 million, 30-year first mortgage bonds that were issued on May 13, 2014; and
2. The actual short-term balances and the actual short-term debt cost for the period January 1, 2014 through April 30, 2014.

Id. As a result of these updates, the cost of short-term debt went down from 0.67 percent to 0.62 percent, and the cost of long-term debt went down from 4.93 percent to 4.90 percent. DOC Ex. 403 at 11 (Amit Surrebuttal) (citing Xcel Ex. 31 at GET-2, Schedule 3 (Tyson Rebuttal)).

118. Dr. Amit agreed that NSP's updated capital structure and updated costs of short- and long-term debt are reasonable.[8] DOC Ex. 403 at 10 (Amit Surrebuttal). NSP's updated capital structure and updated cost of short- and long-term debt are based on the same methods used by NSP to arrive at its original capital structure and cost of short- and long-term debt. *Id.* Moreover, NSP's updated common equity ratio did not change. *Id.* The following table summarizes Dr. Amit's recommendation for NSP's overall cost of capital, which is based on NSP's updated capital structure, updated costs of short- and long-term debts, and Dr. Amit's recommended rate of return on equity:

Table 9: NSP's Updated Overall 2014 Cost of Capital

Component	Capitalization Ratio (%)	Cost (%)	Weighted Cost (%)
Long-Term Debt	45.60%	4.90%	2.234%
Short-Term Debt	1.90%	0.62%	0.012%
Common Equity	52.50%	9.64%	5.061%
Total			7.31%

119. Based on his updated analyses, Dr. Amit recommended an ROE of 9.64 percent on NSP's common equity capital and an overall ROR of 7.31 percent on NSP's total capital, for 2014. *Id.* at 11. The ALJ agrees that Dr. Amit's recommended ROE of 9.64 percent on NSP's common equity capital and an overall ROR of 7.31 percent on NSP's total capital, for 2014, is reasonable.

IV. THE CAPITAL STRUCTURE, THE COST OF SHORT- AND LONG-TERM DEBT AND THE COST OF CAPITAL FOR NSP, FOR 2015 (ISSUE 12-IN PART-FOR 2015)

A. NSP's Initial Proposed Capital Structure for 2015 (Issue 47, in part-for 2015)

120. As part of its multi-year rate case filing for 2014–2015, NSP proposed to base its 2015 rate increase request on a different capital structure, using different costs of short- and long-term debt than was used for its 2014 rate increase request. DOC Ex. 400 at 53 (Amit Direct).

[8] Mr. Glahn's recommendations regarding NSP's capital structure are not reasonable. He proposed that NSP use Value Line's 2014 projected equity ratio for Xcel (47.50%) and 2015 projected equity ratio for Xcel (49.00%) for its 2014 and 2015 test years, respectively. ICI Ex. 250 at 26 (Glahn Direct). This recommendation must be rejected because it violates basic financial and economic principles. DOC Ex. 402 at 14 (Amit Rebuttal). For example, Mr. Glahn did not recognize that NSP has its own capital structure; it issues its own long-term debt and its common equity represents its accumulated retained earnings plus any net infusion of common equity capital from Xcel to NSP. *Id.* Xcel, NSP's parent company, has its own capital structure, which reflects Xcel's investment risk. *Id.* The parent company's investment risk may be somewhat different than NSP's investment risk. *Id.* NSP's ratepayers must pay all prudent costs of serving them. *Id.* These costs include NSP's cost of capital, which is appropriately calculated using NSP's own equity and long-term debt, not the parent company's equity and long-term debt. DOC Ex. 402 at 14 (Amit Rebuttal).

121. On June 17, 2013, the Commission issued an Order that set specific requirements regarding capital structure and cost of capital in the second year of any multiyear rate plan. *In the Matter of the Minnesota Office of the Attorney General – Antitrust and Utilities Division's Petition for a Commission Investigation Regarding Criteria and Standards for Multiyear Rate Plans under Minn. Stat. § 216B.16, subd. 19*, Order Establishing Terms, Conditions, and Procedures for Multiyear Rate Plans, Docket No. E,G-999/M-12-587, 7, 12–16 (Jun. 17, 2013) [hereinafter Multiyear Rate Plans Order]. The Multiyear Rate Plans Order requires a utility to use the same cost of equity capital as approved by the Commission for the first year of the multiyear rate plan (Point 4 of the above Commission Order). *Id.* at 7, 12. While the Multiyear Rate Plans Order does not set any specific requirements regarding the capital structures and the costs of long- and short-term debt in the second year of the multiyear plan, it does provide some guidance on this matter, though only indirectly. DOC Ex. 400 at 54 (Amit Direct). Order Point 1 of the Multiyear Rate Plans Order provides that:

> A utility may propose a multiyear rate plan to improve the regulatory process for the recovery of –
>
> A. Costs related to specific, clearly identifiable capital projects; and
>
> B. Appropriate non-capital costs.

Multiyear Rate Plans Order, *supra* at 12. Thus, the Company's filing of new capital structure and new costs of short- and long-term debts is allowed under Point 1, Part B of the Commission Order as "non-capital costs." DOC Ex. 400 at 54 (Amit Direct).

122. NSP's proposed 2015 capital structure can be summarized by the following table:

Table 10: Overall Initial 2015 Cost of Capital for NSP[9]

Component	Amount ($000s)	Capitalization Ratio (%)	Cost (%)	Weighted Cost (%)
Long-Term Debt	$4,211,010	45.63	4.97	2.27
Short-Term Debt	$172,784	1.87	1.129	0.02
Common Equity	$4,383,794	52.50	9.80	5.15
Total	$9,229,910	100.00		7.44

123. Compared to NSP's 2014 proposed capital structure, 2015's common equity ratio is the same: 52.50 percent. DOC Ex. 400 at 55 (Amit Direct). The long-term debt ratio, however, is four basis points higher and the short-term debt ratio is two basis points lower. *Id.* The change in the long-term debt ratio reflects an estimated issuance of $250 million of ten-year

[9] The Cost of Common Equity shown in this table is the initial ROE recommended by the Department.

long-term debt and $250 million of 30-year long-term debt, both expected on August 15, 2015. *Id.* The higher 2015 cost of long-term debt reflects the projected cost of the above-mentioned new long-term debt to be issued in 2015. *Id.* These higher costs reflect the higher projected LIBOR's rates in 2015 as compared to 2014. *Id.;* Xcel Ex. 30 at GET-1, Schedule 8 (Tyson Direct).

124. NSP's initial proposed 2015 capital structure and its proposed costs of short- and long-term debts are reasonable. DOC Ex. 400 at 55 (Amit Direct). The 2015 debt and equity ratios are essentially the same as their respective ratios for 2014, which Dr. Amit deemed reasonable. *Id.* Moreover, the Company used the same methodology to calculate its proposed 2015 short-term debt, long-term debt and common equity as it did for 2014. *Id.* at 55–56. Finally, the Company appropriately estimated the costs of its short- and long-term debt. *Id.* at 56. Thus, updated to reflect the Department's recommended ROE for 2014 in 2015, the results are reasonable.

B. Overall 2015 Updated Cost of Capital for NSP

125. The Company updated its 2015 capital structure and costs of long- and short-term debt, based on more recent information available to it. DOC Ex. 403 at 29 (Amit Surrebuttal); Xcel Ex. 31 at 28–30, GET-2, Schedule 7 (Tyson Rebuttal). Mr. Tyson used the same methodologies as in his Direct Testimony to calculate the capital structure and the costs of long- and short-term debt. DOC Ex. 403 *supra;* Xcel Ex. 31 *supra.* The following table summarizes NSP's 2015 updated capital structure and updated costs of long- and short-term debt and the cost of common equity:

Table 11: Overall 2015 Updated Cost of Capital for NSP

Component	Amount ($000)	Capitalization Ratio (%)	Cost (%)	Weighted Cost (%)
Long-Term Debt	$4,209,484	45.61%	4.94%	2.2531%
Short-Term Debt	$174,310	1.89%	1.12%	0.0211%
Common Equity	$4,846,116	52.50%	9.64%	5.0610%
Total	$9,229,910	100.00%		7.34%

DOC Ex. 403 at 29 (Amit Direct); Xcel Ex. 31 at GET-2, Schedule 7 (Tyson Rebuttal).

126. The ALJ finds that Dr. Amit recommended a reasonable cost of common equity of 9.64 percent and an overall cost of capital of 7.34 percent for NSP for 2015, whereas neither Xcel nor Mr. Glahn did so.[10]

[10] Dr. Amit's updated recommendations regarding NSP's 2015 capital structure and costs of short- and long-term debts are summarized in table 10 above.

V. 2014 TEST YEAR ADJUSTMENTS TO XCEL'S PROPOSED RATE BASE AND INCOME STATEMENT

127. Xcel used forecasted data for the 12-month period ending December 31, 2014, which the DOC as the basis for its investigation and recommended financial adjustments. DOC Ex. 437 at 4 (Lusti Direct). The DOC's financial investigation included a review of Xcel's test year data, the Commission's Order in Xcel's last rate case, and the relevant Commission Orders since Xcel Energy's last rate case, DOC Ex. 437 at 5 (Lusti Direct), along with the effects on this proceeding of cost allocation issues being developed in a concurrent proceeding, Docket No. E,G002/AI-14-234) as indicated in Ms. Byrne's Direct and Surrebuttal Testimonies, DOC Ex. 423 at 3-5 (Byrne Public Direct) and DOC Ex. 427 at 2-3 (Byrne Public Surrebuttal).

128. During the course of this proceeding, numerous issues were resolved between Xcel and the Department as reflected in Xcel's proposed Issues Matrix dated September 10, 2014. Many of the Department's concerns with the Company's rate case proposal remain unaddressed, however. The list below reflects the order of the financial issues as they were presented in the DOC testimony, rearranged to discuss first the 2014 Test Year, then the 2015 STEP Year, and indicates the extent to which issues were resolved between the Department and the Company.

A. Prairie Island Extended Power Uprate (EPU) (Issue 3)

Resolved between DOC and Xcel: The recovery of costs of the cancelled PI EPU. DOC agreed with Xcel that $78.9 million in costs for the cancelled PI EPU project (including PI EPU costs of $66,086,393 and costs for allowance for funds used during construction, AFUDC, of $12,798,523) are recoverable from ratepayers. DOC Ex. 437 at 16-18 (Lusti Direct); Xcel Ex. 45 at 11, Table 1 (Weatherby Direct).

Resolved between DOC and Xcel: The amortization methodology. Xcel accepted a DOC alternative to Xcel's proposed recovery; the alternative would allow Xcel to earn 2.24 percent, the debt component of its cost of capital, on the $78.9 million over the remaining 20.3 year life of the facility. This adjustment results in a total 2014 Test Year revenue reduction of $4.867 million. Xcel Ex. 140 at 1 (Heuer Opening Statement); DOC Ex. 451DVL-EH-7, Page 1 of 4, Column (a) (Lusti Opening Statement).

129. The Commission's Order in Docket No. E002/CN-08-509, regarding a Certificate of Need (CN) for Xcel to build an Extended Power Uprate at the Prairie Island,[11] observed that Xcel had proposed to expand the generating capacity of the Prairie Island Plant by 1) acquiring fuel assemblies with thicker rods of uranium, thereby permitting the generation of greater heat and therefore more steam to turn the turbines, and 2) improving its plant to convert steam into

[11] *In the Matter of the Application of Northern States Power Company d/b/a Xcel Energy for Certificate of Need for an Extended Power Uprate at the Prairie Island Nuclear Generating Plant,* Docket No. E002/CN-08-509, ORDER ACCEPTING ENVIRONMENTAL IMPACT STATEMENT, AND GRANTING CERTIFICATES OF NEED AND SITE PERMIT WITH CONDITIONS ISSUE DATE, dated December 18, 2009, at 8.

electric energy more efficiently. The Commission's Order noted that Xcel had estimated a cost of $322 million to implement its uprate proposal. DOC Ex. 437 at 12-13 (Lusti Direct). Thereafter Xcel cancelled its plans; the Commission's Order in Xcel's last rate case, Docket No. E002/GR-12-961, required, regarding the PI EPU cancelled plant that:

> In the initial filing in its next rate case, Xcel shall provide a complete justification for any rate recovery or deferral of its Prairie Island extended power uprate costs, including at least the following information:
>
> - All work order charges,
> - Summary of costs by categories, including narrative description of each cost category and support for why costs should be allowed recovery,
> - Dollar amount of each cost category by year incurred, including total cost amount, and
> - Any additional information necessary to support the Company's request for recovery of the PI EPU cancelled plant.

DOC Ex. 437 at 13 (Lusti Direct) (citing Docket No. 12-961, Findings of Fact, Conclusions, and Order, dated September 3, 2013, Ordering Paragraph 51).

130. The Company requested recovery of the PI EPU cancelled plant costs. Mr. Clark explained that the Company sought to recover $66.1 million from ratepayers, which is the total amount Xcel expended to carry out the Project, plus accrued AFUDC of $12.8 million. DOC Ex. 437 at 14 (Lusti Direct) (citing Xcel Ex. 99 at 31 (Clark Direct)). Mr. Weatherby further documented these totals. His Table 1 (below) summarized by year of incurrence all costs that the Company seeks to recover from ratepayers. DOC Ex. 437 at 14 (Lusti Direct) (citing Xcel Ex. 45 at 11, Table 1 (Weatherby Direct)).

Mr. Weatherby's Table 1: Summary of Prairie Island LCM/EPU Costs by Year

		Split of Column A			*Final EPU Only*
	Column A	Column B	Column C	Column D	Total C + D
Costs through:	Total EPU/LCM Costs in Work orders 10532527 and 10562058 (without AFUDC)	LCM/Other Costs Charged to EPU Work order for Year	EPU Costs Charged to EPU Work order for Year	AFUDC recorded by Year	Costs in EPU Work orders 10532527 and 10562058 (with AFUDC)
12/31/2006	$854,392	$ 0	$ 854,392	$32,491	$886,883
12/31/2007	$1,065,379	$ 0	$ 1,065,379	$110,323	$1,175,702
12/31/2008	$2,143,914	$ 146,911	$ 1,997,003	$256,665	$2,253,668
12/31/2009	$15,004,650	$ 1,867,569	$13,137,081	$688,075	$13,825,156
12/31/2010	$28,984,960	$ 1,578,912	$27,406,048	$2,856,147	$30,262,195
12/31/2011	$17,114,563	$ 1,572,482	$15,542,081	$5,287,676	$20,829,757
12/31/2012	$6,785,963	$ 701,554	$ 6,084,409	$4,119,947	$10,204,356
12/31/2013				($552,802)	($552,802)
Total	**$71,953,821**	**$5,867,428**	**$66,086,393**	**$12,798,523**	**$78,884,916**
		Transferred to various LCM Work orders			Transferred to Regulatory Asset

131. The Commission has allowed recovery of reasonable and prudent costs for cancelled project in other recent proceedings, such as the Interstate Power & Light Company's (IPL) cancelled Sutherland Generating Station Unit 4 project and Otter Tail Power Company's (OTP) cancelled Big Stone II project. DOC Ex. 437 at 15 (Lusti Direct) (*citing* Xcel Ex. 99 at 32-35 (Clark Direct); IPL Docket No. E001/GR-10-276, Order of August 12, 2011; *and* OTP Docket E017/GR-10-239, April 25, 2011 Order). The Commission allows recovery only of cancelled project costs that are found to be prudent. In the IPL case, for example, the Commission stated:

> The Commission does not view the question of cost recovery for the Sutherland plant as controlled by an accounting issue. The Commission has consistently treated the issue of abandoned plant costs as turning on the unique facts and circumstances surrounding each rate case and each plant.
>
> The Commission concludes that there is no public interest or regulatory benefit to be gained by disallowing costs prudently incurred in good faith to meet future need. And there is much to be lost by potentially chilling a utility's diligence in developing resources and in promptly withdrawing from projects when

> experience shows that they will no longer serve ratepayers' best interest.

DOC Ex. 437 at 15 (Lusti Direct) (citing IPL Docket No. E001/GR-10-276, Order of August 12, 2011 at 33). In OTP's case, the Commission similarly stated:

> This Commission conducted a lengthy proceeding on the need for the project's transmission component and determined – subject to upper limits on construction and carbon regulation costs – that the project was as reasonable and prudent a means of meeting future need as any alternative in that voluminous record. Further, no one challenged the prudence and reasonableness of the Company's withdrawal from the project in the face of unforeseeable and substantial changes in projected energy prices, available supplies, forecasted need, and general economic conditions, among others.
>
> There is no public interest or regulatory benefit to be gained by disallowing costs prudently incurred in good-faith to meet future need. Further, there is much to be lost by potentially chilling Otter Tail's diligence in developing resources and in promptly withdrawing from projects when experience shows that they will no longer serve ratepayers' best interests.

DOC Ex. 437 at 15-16 (Lusti Direct) (*citing* OTP Docket E017/GR-10-239, Order of April 25, 2011 at 11).

132. In both the IPL and OTP dockets, the Commission allowed the utility to recover its costs over a reasonable period of years, with no return. In Docket No. E001/GR-10-276, the Commission allowed IPL to recover its costs for the cancelled Sutherland plant over a 25-year period, with no return, and in Docket No. E017/GR-10-239, the Commission allowed OTP to recover its Big Stone II costs, including accrued AFUDC, over a 5-year period, with no return. DOC Ex. 438 at DVL-29 (Lusti Direct Attachments); DOC Ex. 437 at 16 (Lusti Direct).

133. Mr. Lusti agreed with Xcel that the costs identified in Table 1 above should be recoverable for the following reasons. First, the amount Xcel proposes to recover is far less than the amount the Company originally proposed for the project in the (08-509) CN docket noted above. Second, when Xcel saw the costs of this EPU project increasing, the Company filed a Notice of Changed Circumstances, stating:

> We make this filing pursuant to Minn. R. 7849.0400, subp. 2(H), which provided that a utility shall inform the Commission of changed circumstances that may affect a change in the size, type, timing or ownership of a large generation or transmission facility previously certified by the commission. As we described in our Resource Plan update filed last December there have been changes

> in the timing and size of the project since it was certified. Our analysis demonstrates those changes alone would not have warranted a different decision by the Commission. However, other changes – such as our load forecasts, the costs of alternative resource options, and uncertainties now possible in the federal licensing process have reduced the potential benefits associated with the project and could combine to lead the Commission to determine the uprate program should not be further pursued. Therefore, we request the Commission review and reaffirm the project remains in the public interest before we proceed further.

DOC Ex. 437 at 16-17 (Lusti Direct) (citing Docket No. E002/CN-08-509, Xcel's Notice of Changed Circumstances, March 30, 2012, at cover page). After consideration of the facts, the Commission concluded that Xcel had demonstrated that it was in the public interest to discontinue its uprate project, and no party had shown cause for continuing construction of that project. Accordingly, the Commission terminated Xcel's CN. DOC Ex. 437 at 16-17 (Lusti Direct) (citing Docket No. E002/CN-08-509, Order, dated February 27, 2013 at 3). The Department concluded that, unless specifically challenged by another party to this rate case proceeding, the Xcel PI EPU costs totaling $66,086,393 and AFUDC costs totaling $12,798,523 as shown in Table 1 are eligible for recovery. DOC Ex. 437 at 17 (Lusti Direct).

134. The ALJ finds that the Department's recommendation is reasonable.

135. The Department did not find reasonable, however, the Company's initial proposal regarding the amortization period. The Company had initially proposed to recover $78.9 million (on a Total Company basis) in costs of the cancelled project over 12 years while earning a return on the asset, or six years if no return was permitted. DOC Ex. 437 at 18 (Lusti Direct) (citing Xcel Ex. 99 at 31 (Clark Direct)). Department Witness Mr. Lusti recommended that the Commission allow Xcel to recover the $78.9 million over the remaining life (RL) of the facility, which is 20.3 years; without earning a return on the asset. This adjustment provided for a reasonable sharing of the cost between shareholders and ratepayers. DOC Ex. 437 at 18 (Lusti Direct). The DOC adjustment to test-year rate base for $78.9 million over the 20.3 year remaining life of the facility, with no return is detailed in DOC Ex. 438 DVL-9, Column (c) (Lusti Direct Attachments). The DOC adjustment decreased Xcel's test-year rate base by $32,722,000, and test-year amortization expense by $1,929,000, as shown in DOC Ex. 438 DVL-4, column (a) and DVL-7, column (a), respectively (Lusti Direct Attachments). DOC Ex. 437 at 18 (Lusti Direct).

136. In their responsive testimonies, other parties made various recommendations regarding the PI EPU revenue requirements. The table below (DOC Ex. 442 at 5, Table 1 (Lusti Surrebuttal)) provides a summary of the initial recommendations of other parties in the proceeding. Table 1 includes Xcel's Direct and Rebuttal recommendation and alternative recommendation.

Lusti Surrebuttal Table 1: Recommendations Regarding PI EPU Revenue Requirements

Party	Recovery Amount	Amortization Period	Return	2014 Revenue Requirement
Xcel Direct	$78,900,000	12	Yes	$8,595,000
DOC	$78,900,000	20.3	No	$2,884,000
MCC	$78,900,000	20.3 (but only ½ yr in 2014)	Debt	$3,120,000
ICI	$0			$0
OAG		10	No	$4,197,000
Xcel Rebuttal (1)	$78,900,000	12	No	$4,928,000
Xcel Rebuttal (2)	$78,900,000	20.3	Debt at 4.7605%	$4,566,000
DOC Surrebuttal	$78,900,000	20.3	Debt at 2.24%	$3,728,000

DOC Ex. 442 at 6 (Lusti Surrebuttal). Mr. Lusti reviewed the positions of other parties and reaffirmed in his Surrebuttal Testimony that the approach that was most consistent with the Commission's previous decisions was to allow Xcel to amortize the $78.9 million over the 20.3 remaining life of the Prairie Island nuclear power plant, with no return. DOC Ex. 442 at 6 (Lusti Surrebuttal).

137. Mr. Lusti proposed an alternative amortization approach to allow Xcel to earn the debt component of its cost of capital on the $78.9 million over the remaining life of the plant. He stated that such an approach should fully reflect that Xcel would forego earning any return on equity for the abandoned plant. In other words, he testified, the debt level would reflect the capitalization ratio for debt as follows:

Component	Capitalization Ratio (%)	Cost (%)	Weighted Cost (%)
Long-Term Debt	45.50%	4.90%	2.23%
Short-Term Debt	1.90%	0.62%	0.01%
Total Debt Earning			**2.24%**

DOC Ex. 442 at 6 (Lusti Surrebuttal) (citing DOC Ex. 403 at 11 (Amit Surrebuttal)). With this approach, the amount that Xcel would be allowed to charge for debt costs over the 20.3 years of remaining life would be 2.24 percent. Mr. Lusti recommended that if the Commission adopted this approach, the level of debt costs should be fixed at this amount since this level reflects the timing of Xcel's decision to seek recovery for the abandoned plant. DOC Ex. 442 at 6-7 (Lusti Surrebuttal).

138. In the Company's Opening Statements, Ms. Heuer stated that the Company agreed to the alternative proposal in Mr. Lusti's Surrebuttal Testimony, in which the cost for the PI EPU would be amortized over the remaining life of the plant with a debt-only return of 2.24 percent. Xcel Ex. 140 at1 (Heuer Opening Statement). Ms. Heuer explained that this adjustment would result in a total 2014 Test Year reduction of $4.867 million. Xcel Ex. 140 at 1 (Heuer Opening

Statement). The ALJ agrees that this adjustment is reasonable, as agreed to by Xcel and the Department.

B. Xcel's PI LCM/EPU Split Correction (Issue 39)

Resolved between DOC and Xcel: Xcel agrees to DOC's recommended correction, which reduces rate base by $1,418,000 and decreases Xcel's test-year operating income by $12,000. DOC Ex. 442 at 2 (Lusti Surrebuttal); Xcel Ex. 90 at 9 (Heuer Rebuttal)**.**

139. During discovery, Xcel recommended a correction to its original petition for recovery of PI EPU costs. Ms. Heuer explained that the Company agreed to remove $2.157 million (NSPM) from the Prairie Island EPU and LCM portions of the project. DOC Ex. 442 at 2 (Lusti Surrebuttal) (*citing* Xcel Ex. 90 at 9 (Heuer Rebuttal)). As explained in the Rebuttal Testimony of Ms. Heuer:

> The Company proposes to remove $2.157 million (NSPM) from the Prairie Island EPU and LCM portions of the project. In his Direct Testimony, pages 19 and 26, DOC witness Mr. Dale V. Lusti supports this adjustment…The result of this adjustment is reflected on Xcel Ex. 90 (AEH-2), Schedule 6A, 2014 Rate Base Rebuttal Schedule, page 1, column 1 and reduces test year rate base by $1.418 million. The adjustment is also reflected on Xcel Ex 90 (AEH-2), Schedule 6B, 2014 Income Statement Rebuttal Adjustment Schedule, page 1, column 1 and decreases test year revenue requirements by $158,000.

140. Xcel Ex. 90 at 9 (Heuer Rebuttal). The Company's adjustment reduced rate base by $1,418,000 as shown in DOC Ex. 451 DVL-EH-4, column (b) (Lusti Opening Statement), and decreases Xcel's test-year operating income by $12,000 as shown in DOC Ex. 451 DVL-EH-7, column (b) (Lusti Opening Statement). DOC Ex. 442 at 2(Lusti Surrebuttal); and Xcel Ex. 90 at 9 (Heuer Rebuttal).

141. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

C. Hollydale Transmission Project (Issue 38)

Resolved between DOC and Xcel: DOC and Xcel agree that costs of the Hollydale project should be removed from the test-year revenue requirement in this proceeding. DOC Ex. 442 at 7 (Lusti Surrebuttal); Xcel Ex. 90 at 11 (Heuer Rebuttal).

142. Xcel included in the current rate proceeding, costs related to the Hollydale Transmission Project. In Xcel's Response to DOC IR 2123, however, Xcel noted that because it no longer anticipates the planned additions for the Hollydale project, a revenue requirement adjustment should be made of $43,025 to remove the plant additions from this rate case. DOC Ex. 438 at DVL-31 (Lusti Direct Attachments); DOC Ex. 437 at 20 (Lusti Direct); DOC Ex. 442 at 7 (Lusti Surrebuttal); Xcel Ex. 90 at 11 (Heuer Rebuttal).

143. The DOC concurred, and recommended that costs of the Hollydale project be removed from the test-year revenue requirement in this proceeding. DOC Ex. 437 at 20 (Lusti Direct). The DOC adjustment for removal of Hollydale costs from the test year revenue requirement reduced rate base by $388,453 and operating income by $3,000, as detailed in DOC Ex. 438 DVL-10 (Lusti Direct Attachments) and as shown in DOC Ex. 451 DVL-EH-4, column (c), and DVL-EH-7, column (c) (Lusti Opening Statement).

144. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

D. Post-Retirement Medical Expenses (FAS 106) (Issues 6 and 19)

Resolved between DOC and Xcel: The DOC concluded that the Company's proposed expected returns on assets (EROAs) of 7.25 and 6.25 were reasonable. DOC Ex. 423 at 39 (Byrne Direct).

Resolved between DOC and Xcel: Xcel agreed to DOC's recommendation to update the measurement date to December 31, 2013 (DOC Ex. 423 at 41 (Byrne Direct)) which increased the discount rate from 4.08 percent to 4.82. DOC Ex. 424 ACB-19 (Byrne Direct Attachments) and DOC Ex. 424 ACB-21 (Byrne Direct Attachments). DOC agreed with Xcel to combine the operation and maintenance (O&M) and capital adjustments into one revenue requirement adjustment of $666,522. DOC Ex. 449 at 2-3 (Byrne Opening Statement); DOC Ex. 427 at 11-12, 26 (Byrne Surrebuttal).

Disputed between DOC and Xcel: Xcel and DOC did not agree on the Financial Accounting Statement 106 (FAS) 106 adjustments for the discount rate or the 2008 market loss, which accounts for $1,591,515 of the revenue requirement adjustment being disputed. DOC's total recommended reduction to FAS 106 expenses is $2,258,037. The DOC's recommendation decreased the test-year administrative and general expense by $2,258,000, as shown in DOC Ex. 451 DVL-EH-7, column (h) (Lusti Opening Statement).

145. Xcel requested $4,099,992 in test-year O&M expenses and $1,158,512 in test-year capital expenses for post-retirement medical costs under FAS 106. DOC Ex. 427 at 22 (Byrne Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement). The post-retirement medical benefits provided under FAS 106 are paid to retired employees for health care costs such as medical, dental, vision, and life insurance. This benefit was eliminated for all active Xcel employees over ten years ago, so this proposed expense is a legacy cost of the prior program. DOC Ex. 423 at 37 (Byrne Direct).

146. The Commission's ratemaking function of establishing reasonable levels of expenses in rates differs from the utility's accounting or bookkeeping function. The level of such expense in rates must reflect the likely and reasonable expense going forward until the Company's next rate case. DOC Ex. 429 at 100 (Campbell Direct). A critical issue for ratemaking regarding proposed future benefit expenses such as FAS 106 is whether the assumptions the Company used to estimate costs are likely and reasonable, to ensure that the amount that ratepayers pay in current rates for future employee benefits are reasonable. DOC Ex. 423 at 40 (Byrne Direct).

147. Xcel accounts for its post-retirement medical benefits under FAS 106 as follows:

> The components and calculations of FAS 106 are identical to FAS 87, with one exception. Unlike FAS 87, FAS 106 asset gains or losses are not phased in before they are amortized, but instead the total gain or loss amount is simply amortized over the average years to retirement for active employees. But otherwise, the FAS 106 benefits are calculated based on assumptions regarding the discount rate, the [expected return on assets], and the salary or wage levels.

DOC Ex. 423 at 37-38 (Byrne Direct) (*citing* Xcel Ex. 81 at 114 (Moeller Direct).

148. The assumptions Xcel used to calculate its FAS 106 2014 test-year O&M expense were:

1. two expected rates of return (EROAs): an EROA of 7.25 percent for the bargaining employee plan, and an EROA of 6.25 percent for the non-bargaining employee plan. DOC Ex. 423 at 38 (Byrne Direct) (*citing* Xcel Ex. 81 at 115 (Moeller Direct));

2. a measurement date of December 31, 2012. DOC Ex. 424 ACB-16 at 4 (Byrne Direct Attachments)(DOC IR 1196); DOC Ex. 423 at 38 (Byrne Direct);

3. inclusion of a 2008 market losses. DOC Ex. 424 ACB-19 at 2 (Xcel response to IR 1189) (Byrne Direct Attachments); DOC Ex. 423 at 41 (Byrne Direct); and

4. a discount rate of 4.08 percent, Xcel Ex. 81 at 115 (Moeller Direct).

1. Expected Rates of Return (EROAs)

149. On January 1, 2013, Xcel began using two different EROAs for these plans. In response to a request from the Department to explain this change, Xcel stated:

> There are two EROAs because the asset allocation for the non-bargaining portion of the plan differs from the asset allocation for the bargaining portion of the plan. The differing asset allocations exist because the non-bargaining portion is much smaller than the bargaining portion in terms of overall asset size. A plan with a small asset balance must hold a larger percentage of liquid assets to satisfy potential claims, and the assets generally have a shorter investment horizon. Generally speaking, assets that are more liquid and that have shorter investment horizons have lower returns. In addition, the non-bargaining portion of the plan participates in the EIS Mutual Business Program #15 captive insurance product, which has a different investment portfolio than the bargaining plan does.

DOC Ex. 424 ACB-17 (Byrne Direct Attachments) (DOC IR 1188); DOC Ex. 423 at 38-39 (Byrne Direct). Ms. Byrne concluded as reasonable Xcel's rationale for using two EROAs to

calculate its post-retiree medical expense, based on the applicable paragraph in FAS 106. DOC Ex. 424 ACB-18 (Byrne Direct Attachments). Thus, the DOC concluded that the Company's proposed EROAs of 7.25 and 6.25 were reasonable. DOC Ex. 423 at 39 (Byrne Direct).

2. Plan Measurement Date (Issue 19)

150. DOC asked Xcel to update the measurement date of this asset from December 31, 2012 to a more current date of December 31, 2013. DOC Ex. 423 at 40 (Byrne Direct). DOC requested the more recent measurement date because, when using actuarial assumptions to calculate future expense, it is reasonable to use the most recent information available. DOC Ex. 423 at 41 (Byrne Direct). Additionally, DOC requested that Xcel break out the updated measurement date calculation for all benefits fund asset balances and all benefits obligation/liability amounts. DOC Ex. 424 ACB-20 (Byrne Direct Attachments) (DOC IR 2134); DOC Ex. 423 at 40 (Byrne Direct).

151. Xcel was able to provide benefit expense calculations based on a December 31, 2013 measurement date in its response to IR 1189, and Ms. Byrne concluded that updating the measurement date to December 31, 2013 was reasonable for the purposes of calculating 2014 test-year FAS 106 O&M expense. DOC Ex. 423 at 41 (Byrne Direct).

152. The financial impact of the recommendation is that changing the measurement date from 2012 to 2013 increased the discount rate from 4.08 percent to 4.82, and therefore reduced O&M expense by $653,714. DOC Ex. 424 ACB-19 (Byrne Direct Attachments) and DOC Ex. 424 ACB-21 (Byrne Direct Attachments).

153. Thereafter, Xcel agreed with Ms. Byrne's adjustment and proposed to combine the O&M and capital adjustments for the measurement date into one revenue requirement adjustment of $666,522, to which DOC agreed. DOC Ex. 427 at 11-12, 26 (Byrne Surrebuttal); DOC Ex. 449 at 2-3 (Byrne Opening Statement).

3. The 2008 Market Loss (Issue 6, in part)

154. DOC asked Xcel to provide calculations that excluded the 2008 market losses. DOC Ex. 423 at 40 (Byrne Direct), and Xcel provided the response. DOC Ex. 424 ACB-19 (Byrne Direct Attachments)(DOC IR 1189 Revised). Xcel's response indicated that its proposed test-year 2014 FAS 106 expense included $177,000 in costs related to the 2008 market loss. DOC Ex. 424 ACB-19 at 2 (Xcel's response to IR 1189) (Byrne Direct Attachments); DOC Ex. 423 at 41 (Byrne Direct). Ms. Byrne testified that it is not reasonable to include all of the 2008 market loss in 2014 test-year FAS 106 expense. She explained that, to treat the 2008 market loss costs for FAS 106 expense consistently with the treatment of the 2008 market loss for the qualified pension, the Commission should exclude 50 percent of the 2008 market loss costs from FAS 106 expense. The Direct Testimony of DOC Witness Ms. Campbell, provides a more detailed analysis of the 2008 market loss amortization and exclusion from test-year expenses, regarding qualified pension expense. DOC Ex. 429 at Section X (Campbell Direct).

4. Discount rate (Issue 6, in part)

155. DOC asked Xcel to update this cost to reflect various discount rates. In response, Xcel provided the financial impacts for these requests. DOC Ex. 424 ACB-19 (Byrne Direct Attachments) (DOC IR 1189 Revised). As to what discount rate is reasonable to select, Ms. Byrne explained that, because FAS 106 expense is calculated in the same manner as Qualified Pension expense under FAS 87, the discount rate for FAS 106 should match the respective EROA percentage, to reflect the same assumptions for funding requirements as required for pension costs and as consistent with DOC Witness Ms. Campbell's reasoning and recommendation for test-year Qualified Pension expenses, as set out in this evidentiary record at DOC Ex. 429 at 114-118 (Campbell Direct). Ms. Campbell recommended a discount rate of 7.25 percent for the bargaining employees' plan and a rate of 6.25 percent for the non-bargaining employees' plan, for a weighted average discount rate of 7.11 percent. DOC Ex. 424 ACB-19 at 2 (Byrne Direct Attachments); DOC Ex. 423 at 42 (Byrne Direct).

156. In addition, Xcel indicated that there are corresponding capital costs for all Health & Welfare benefits, which includes $1,158,512 for the FAS 106 expenses. Xcel Ex. 81 (MPM-1), Sched. 2 at 3 (Moeller Direct). Because the rate setting concern is with overall FAS 106 expenses, capital expenses should be adjusted proportionally. Because Ms. Byrne's total recommended adjustments reduced O&M expense by approximately 54 percent, she recommended a corresponding reduction to capital expenses of 54 percent, or $625,781. DOC Ex. 424 ACB-21 (Byrne Direct Attachments); DOC Ex. 423 at 42 (Byrne Direct).

157. Xcel requested $4,099,992 in test-year O&M expenses and $1,158,512 in test-year capital expenses for post-retirement medical under FAS 106. DOC's recommendations regarding FAS 106 expense adjustments reduced Xcel's request as follows:

- **Expected Rates of Return**: No adjustment recommended.

- **Measurement Date**: Change the measurement date from 2012 to 2013 increased the discount rate from 4.08 percent to 4.82, and therefore reduced O&M expense by $653,714. DOC Ex. 424 ACB-19 (Byrne Direct Attachments) and DOC Ex. 424 ACB-21 (Byrne Direct Attachments).

- **2008 Market Loss**: Remove 50 percent of the 2008 market loss reduced O&M expense by $88,500. DOC Ex. 424 ACB-21 (Byrne Direct Attachments).

- **Discount Rate**: Increase the discount rate from 4.82 percent to a weighted average discount rate of 7.11 percent decreased O&M expense by $1,472,433. DOC Ex. 424 ACB-21 (Byrne Direct Attachments) and

- **Capital Expenses**: Reduce FAS 106 Capital expenses by a corresponding amount resulted in a reduction of $625,781. DOC Ex. 424 ACB-21 (Byrne Direct Attachments).

158. Xcel proposed and DOC accepted a recommendation to combine the O&M and capital portions of DOC's FAS 106 adjustments into a single revenue requirement adjustment of

$2,258,037, which encompassed the DOC O&M and capital adjustments for updating the measurement date, the discount rate, and the 2008 market loss. Xcel and DOC agreed on the adjustment to update the measurement date, which accounts for $666,522 of the total FAS 106 adjustment.

159. DOC did not accept as reasonable Xcel's FAS 106 adjustments for the discount rate or the 2008 market loss, which accounts for $1,591,515 of the revenue requirement adjustment disputed. DOC Ex. 427 at 28-29 (Byrne Surrebuttal). DOC's total recommended reduction to FAS 106 expenses is $2,258,037. The DOC's recommendation decreased the test-year administrative and general expense by $2,258,000, as shown in DOC Ex. 442 DVL-S-7, column (h) (Lusti Surrebuttal), and DOC Ex. 451 DVL-EH-7, column (h) (Lusti Opening Statement).

160. The ALJ finds that this adjustment, recommended by the Department, is reasonable.

E. Post-Employment Benefits (FAS 112) (Issue 21)

Resolved between DOC and Xcel: Xcel agreed to DOC's recommendation that the measurement date be changed from December 31, 2012 to December 31, 2013. DOC Ex. 423 at 46-477 (Byrne Direct). Xcel and DOC agreed to combine the O&M and capital adjustments into one revenue requirement adjustment of $421,463. DOC Ex. 428 at 27 (Byrne Surrebuttal). The DOC's recommendation decreases the test-year administrative and general expense by $421,462, as shown in DOC Ex. 451 DVL-EH-7, column (i) (Lusti Opening Statement).

161. Post-employment benefits are paid to former or inactive employees after employment but before retirement, such as long-term disability (LTD) insurance and workers' compensation. DOC Ex. 423 at 43 (Byrne Direct). These insurances are partially self-insured and partially fully-insured. Xcel Witness Mr. Moeller stated:

> The accounting treatment varies for these two items depending on whether the cost is self-insured or fully-insured. In a fully-insured plan, the Company purchases an insurance plan from an outside insurance provider that assumes the risk. In a self-insured plan, the Company provides the benefits to the covered individuals and therefore effectively acts as the insurer. For the self-insured piece, the Company is required to accrue for LTD and workers' compensation costs under FAS 112, while the fully-insured piece is simply the cost of the insurance premium incurred each year along with any other miscellaneous costs. The FAS 112 accrual represents the expected disability benefit payments for employees that are not expected to return to work.

DOC Ex. 423 at 43 (Byrne Direct) (*citing* Xcel Ex. 81 at 118 (Moeller Direct)).

162. According to Mr. Moeller, all bargaining employees, as well as non-bargaining employees disabled prior to January 1, 2008 are covered under Xcel's self-insured LTD plan, while non-bargaining employees disabled after January 1, 2008 are covered under the fully-insured plan. Employees injured prior to August 1, 2001 are covered under the self-insured

workers' compensation plan, and employees injured after that date are covered under the fully-insured plan. DOC Ex. 423 at 44 (Byrne Direct) (*citing* Xcel Ex. 81 at 118 (Moeller Direct).

163. Ms. Byrne explained that the self-insured plans under FAS 112 use some, but not all assumptions similar to Xcel's qualified pension plan. In particular, the self-insured portions of post-employment benefits are accrued using a measurement date and a discount rate, but there is no need for an EROA assumption, as with qualified pension and FAS 106 expenses. FAS 112 expenses are related to insurance and do not need to be fully-funded by investment plans, as is required for pension and FAS 106 expenses. DOC Ex. 423 at 45 (Byrne Direct).

164. The assumptions Xcel used to calculate its FAS 112 O&M expense for the 2014 test-year include a measurement date of December 31, 2012 (DOC Ex. 424 ACB-16 at 4 (Byrne Direct Attachments)) and a discount rate of 3.74 percent (Xcel Ex. 81 (MPM-1), Sched. 12 at 4 (Moeller Direct)). Ms. Byrne requested that Xcel make several changes in assumptions for its FAS 106 retiree medical expense calculation. Xcel provided the financial impact from updating the measurement date from December 31, 2012 to December 31, 2013 for all of its benefits (pension, FAS 106, FAS 112); DOC Ex. 423 at 45 (Byrne Direct) (*citing* DOC Ex. 424 ACB-19 at Attachment A (Byrne Direct Attachments).

165. Ms. Byrne explained the assumptions that are reasonable to calculate 2014 test-year FAS 112 O&M expense. She did not take issue with Xcel's proposed discount rate of 3.74 percent, for two reasons. First, Xcel stated that the duration of FAS 112 cash flows is shorter than for qualified pension; therefore the discount rate will be lower than the rate used for pension. DOC Ex. 424 ACB-22 (Byrne Direct Attachments)(DOC IR 1192). Second, FAS 112 expenses are related to insurance; unlike the obligations for pension and FAS 106, and FAS 112 expenses do not need to be fully funded by investment plans.DOC Ex. 423 at 46 (Byrne Direct).

166. Ms. Byrne did take issue, however, with the measurement date. It is reasonable to use the most recent information available. Xcel was able to provide benefit expense calculations based on a December 31, 2013 measurement date in its response to IR 1189. Ms. Byrne concluded that updating the measurement date to December 31, 2013 is reasonable for the purposes of calculating 2014 test-year FAS 112 O&M expense. DOC Ex. 423 at 46 (Byrne Direct).

167. Updating the measurement date reduced the test-year O&M expense. Xcel had requested $584,446 in test-year O&M expenses for the self-insured component of LTD insurance, and $206,472 for the self-insured component of workers' compensation insurance. In its Response to IR 1189, Xcel showed that changing the measurement date from 2012 to 2013 reduced LTD expense by $399,308 and reduced workers' compensation expense by $13,190, for a total reduction of $412,498, as shown on DOC Ex. 424 ACB-19 at Attachment A (Byrne Direct Attachments); DOC Ex. 423 at 46 (Byrne Direct).

168. Ms. Byrne recommended that the measurement date used to calculate test-year FAS 112 expense be changed from December 31, 2012 to December 31, 2013. She provided an adjustment that reduced post-employment FAS 112 O&M expenses for the 2014 test-year by $412,498, as shown in DOC Ex. 424 ACB-23 (Byrne Direct Attachments); DOC Ex. 423 at 47

(Byrne Direct). Because the O&M adjustment reduced test year expenses by 68 percent, she recommended that Xcel also reduce capital expenses by the same 68 percent. Mr. Moeller's Direct Testimony showed capital costs for FAS 112 of $190,152. DOC Ex. 423 at 47 (Byrne Direct); Xcel Ex. 81 MPM-1, Schedule 2 at 3 (Moeller Direct). Accordingly, Ms. Byrne recommended a reduction to capital costs of 68 percent, or $129,303, as shown on DOC Ex. 424 ACB-23 (Byrne Direct Attachments); DOC Ex. 423 at 43 (Byrne Direct). In Rebuttal, Xcel agreed with DOC's recommendation and proposed to combine the O&M and capital adjustments into one revenue requirement adjustment of $421,463, which DOC accepted DOC Ex. 427 at 13 (Byrne Surrebuttal); DOC Ex. 449 at 3 (Byrne Opening Statement). The DOC's recommendation decreases the test-year administrative and general expense by $421,462, as shown in DOC Ex. 451 DVL-EH-7, column (i) (Lusti Opening Statement).

169. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

F. Active Health Care (Issue22)

Resolved between DOC and Xcel: Xcel agreed to DOC's recommended reduction in active health care costs. This recommendation decreases the test-year rate base by $226,000 and administrative and general expense by $1,056,000, as shown in DOC Ex. 442 DVL-S-4, column (f) and DOC Ex. 442 DVL-S-7, column (j), respectively (Lusti Surrebuttal). DOC Ex. 442 at 9 (Lusti Surrebuttal). For ease of incorporating both of these adjustments into the revenue requirement, DOC and Xcel agreed to combine these adjustments into one income statement adjustment of $1.082 million to the 2014 Test Year as recommended in Ms. Byrne's Surrebuttal Testimony. Xcel Ex. 140 at 2 (Heuer Opening Statement) and DOC Ex. 451 at Attachment DVL-EH-7, Page 1 of 4, Column (j) (Lusti Opening Statement).

Unresolved between DOC and Xcel: DOC recommended that the Commission require that Xcel, in a compliance filing in Xcel's next rate case initial filing, provide historical Active Health Care costs since 2011, both book and claims expenses, for all available calendar years, including detail to show the annual year-end Incurred But Not Reported (IBNR) accruals and the subsequent reversals, not just a net annual amount as Xcel provided in 13-868. DOC Ex. 427 at 21 (Byrne Surrebuttal).

170. Xcel's "active health care costs" are the costs associated with providing health care coverage to the Company's employees, including medical, pharmacy, dental and vision claims, administrative fees, employee withholdings, pharmacy rebates, health savings account (HSA) contributions, transitional reinsurance fees, trustee fees, interest income and opt-out funding. Medical and pharmacy costs make up the vast majority of active health care costs. DOC Ex. 423 at 27-28 (Byrne Direct) (*citing* Xcel Ex. 81 at 130 (Moeller Direct)).

171. Xcel's request for Active Health Care Costs for the 2014 test year included $36,443,475 in Minnesota Electric Jurisdictional O&M expenses (DOC Ex. 423 at 28 (Byrne Direct) (*citing* Xcel Ex. 81 (MPM-1), Sched. 2 at 1 (Moeller Direct)) and $7,777,838 for Minnesota Electric Jurisdictional capital expenses. DOC Ex. 423 at 28 (Byrne Direct) (*citing* Xcel Ex. 81 (MPM-1), Sched. 2 at 3 (Moeller Direct)). The amount included two proposed adjustments, described at DOC Ex. 423 at 29-30 (Byrne Direct) (*citing* Xcel Ex. 81 at 131-132

(Moeller Direct). In discovery, Xcel provided the following table (the IR 1194 Table) regarding the historical costs for Active Health Care:

IR 1194 Table

Active Health and Welfare Expense NSPM Electric O&M State of Minnesota			
Year	Per Book Amount	Move IBNR adjustment to Years Actual Claims were Incurred	Amount Reflecting Actual Claims Incurred in a Calendar Year
2009	$37,197,292	$(50,603)	$37,146,689
2010	$36,454,538	$162,247	$36,616,785
2011	$32,996,942	$(473,166)	$32,523,776
2012	$33,669,857	$(469,803)	$33,200,054
2013 Forecast	$35,184,359		$35,184,359
2013 Actual	$32,742,574	$1,662,391	$34,404,965
2014 Test Year	$36,443,475		$36,443,475

172. DOC Ex. 423 at 30 (*citing* DOC Ex. 424 ACB-14 (Byrne Direct Attachments) (DOC IR 1194) (Byrne Direct)). The Company explained that this table included columns to reflect the IBNR adjustments in the period to which these costs relate. Xcel stated:

> At the end of each year, an estimate of claims incurred in that year but not yet reported is calculated and a liability is established. As the claims are paid against the liability in the following year, adjustments are recorded. This column reflects the removal of IBNR adjustments recorded for prior year claims and also the addition of the IBNR adjustments that were recorded in the following year. Once these adjustments are added to the per book amounts, as shown in the third column, the amounts properly reflect the actual claims that were incurred in that calendar year.

DOC Ex. 423 at 30-31 (*citing* DOC Ex. 424 ACB-14 (Byrne Direct Attachments) (DOC IR 1194))

173. Ms. Byrne concluded that it is not reasonable for Xcel to include IBNR as part of this response. Xcel provided no support for the calculation of the $1,662,391 IBNR adjustment for 2013. Without supporting calculations or analysis, it was difficult to determine whether the approximate $1.7 million is a reasonable estimation of unreported claims relating to 2013. Information provided in Xcel's prior rate case, however, indicates that the IBNR Xcel estimated for 2013 was unreasonably high. DOC Ex. 423 at 31 (Byrne Direct).

174. In the Company's previous rate case, DOC Witness Ms. Nancy A. Campbell requested that Xcel provide historical active health care costs. Table 2 from her Direct Testimony was provided as follows:

Campbell Table 2: O&M Active Health Care Costs for 2010 to 2013

2010 Actual	2011 Actual	2011 Test Yr	2012 Prelim.	2013 Test Yr
$36,454,538	$32,996,942	$38,042,035	$33,806,164	$39,821,542

DOC Ex. 423 at 31 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, DOC Ex. 166 at 67 (Campbell Direct)

175. Ms. Byrne testified that a comparison of Ms. Campbell's Table 2 from Xcel's previous rate case with the IR 1194 Table in this case yields two observations: First, the historical amounts from 2010 and 2011 in Ms. Campbell's table tie to the "Per Book Amount" provided for 2010 and 2011 in Xcel's IR 1194 Table in this rate case. Therefore, it appears that Ms. Campbell's analysis of active health care in the previous rate case used the "Book Amount" of expenses as historical actuals, and the IBNR adjustment was not included. DOC Ex. 423 at 31-32 (Byrne Direct). Thus, Xcel including IBNR is not consistent with recovery in current rates.

176. Second, Ms. Byrne reasoned that the 2013 actual expense provided in this rate case should be more accurate than the 2012 preliminary actual expense provided to Ms. Campbell in the previous rate case. In its previous rate case, Xcel provided the 2012 preliminary actual amount of Active Health Care costs in time for the information to be included in Ms. Campbell's Direct Testimony, which was filed in February 2013. The 2012 preliminary actual figure of $33,806,164 provided in Ms. Campbell's Table 2 differs by only $136,000 from the 2012 book amount in IR 1194 Table, and differs by only $606,000 from the 2012 amount adjusted for IBNR. In this 13-868 rate case, in contrast, Xcel provided the 2013 actual figures (in its response to DOC IR 1194) to the Department in April 2014. Yet the 2013 figures provided by Xcel in the IR 1194 Table, a full two months later in the calendar year than in the last case, increased from the book amount by $1.66 million (the amount of the IBNR). The dollar amount of claims that were incurred but unreported by the end of a given calendar year should decrease, not increase, as the subsequent calendar year progresses. For this reason, it seemed unlikely to Ms. Byrne that Xcel's 2013 "Per Book Amount," as of April 2014 in this 13-868 rate case would have a significantly higher IBNR than Xcel's 2012 preliminary actual figures provided by February 2013 in Xcel's previous rate case. DOC Ex. 423 at 32 (Byrne Direct).

177. Ms. Byrne concluded that, because Xcel did not provide support for the 2013 IBNR adjustment in its IR 1194 Table, and because Ms. Byrne's review of historical actuals, in this and in the previous rate case, indicates that the 2013 IBNR adjustment is unreasonably high, the Company had not shown its proposed recovery of Active Health Care costs to be reasonable. DOC Ex. 423 at 33 (Byrne Direct). Further, she concluded that it was reasonable to use the "Per Book Amount" historical actuals provided in the IR 1194 Table for the analysis of Active Health Care costs. DOC Ex. 423 at 33 (Byrne Direct).

178. Ms. Byrne reviewed the historical "Per Book Amount" expenses in the IR 1194 Table, and observed the increase in Xcel's 2014 test year request over 2013 actual expense. She noted that Xcel's request of $36,443,475 for the 2014 test year represented an increase of $3,700,901, or 11.3 percent, over actual 2013 expenses of $32,742,574. DOC Ex. 423 at 33 (Byrne Direct).

179. Ms. Byrne also stated that the 2013 test-year Active Health Care costs had been an issue in the previous (Docket No. E002/GR-12-961) rate case. In its initial filing of its previous rate case, Xcel requested recovery of $38.9 million in O&M Active Health Care expenses and $8.5 million in capital costs on a Minnesota Electric Jurisdictional basis. DOC Ex. 423 at 33 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, DOC Ex. 166 at 64-65 (Campbell Direct)). In her Direct Testimony in the previous case, DOC Witness Ms. Nancy A. Campbell took issue with Xcel's calculation of expense, which averaged the four prior years' actual expenses and used an inflation factor of eight percent. Ms. Campbell explained in the 12-961 Docket that "normally, determining reasonable levels of costs involves either using an average-cost method for situations in which costs fluctuate on a year-to-year basis or, if costs are trending upward, using an average increase inflation factor method." Ms. Campbell further testified that "[i]t is not appropriate to use both of these methods together as suggested by Mr. Moeller." *Id.* at 67-68. Ms. Campbell also observed that the Company had over-recovered 2011 and 2012 O&M expenses by a total of $9.3 million and also over-recovered 2011 and 2012 capital costs by a total of $4.3 million. *Id.* at 67. Ultimately, Ms. Campbell in the 12-961 Docket recommended using a 2010-2012 average of O&M Active Health Care costs of $34.4 million on a Minnesota Jurisdictional basis. *Id.* at 69-70. She also recommended using a three-year average to estimate capital costs, which resulted in test year expenses of $7.2 million. *Id.* at 70.

180. In his Rebuttal Testimony in Xcel's previous 12-961 rate case, Mr. Moeller provided a changed 2013 O&M forecast of $36 million due to the decrease in claims made by Xcel employees in October through December 2012. DOC Ex. 423 at 34 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, DOC Ex. 39 at 23 (Moeller Rebuttal). Following her review of the new information provided by the Company in Rebuttal Testimony, Ms. Campbell again concluded in her Surrebuttal Testimony in the 12-961 rate case that Xcel's proposed test year expense was unreasonable. She recommended her original adjustment of test year O&M expenses of $34.4 million and $7.2 million in capital expenses. DOC Ex. 423 at 34 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, DOC Ex. 173 at 71-72 (Campbell Surrebuttal). The Commission approved Ms. Campbell's adjustments to Active Health Care costs in Docket No. E002/GR-12-961, where the ALJ agreed with Ms. Campbell's adjustments and the Commission accepted the ALJ's findings in its Findings of Fact, Conclusions and Order, issued September 3, 2013 at Order Point 2.

181. In this 13-868 Docket, Ms. Byrne was concerned with the level of Active Health Care O&M costs that Xcel included in its proposed 2014 test year because Xcel modified several aspects of its health care plan in 2011 (Xcel Ex. 78 at 61 (Figoli Direct)), and historical trends showed actual O&M costs being significantly lower than forecasted, as was shown by Ms. Byrne's Table Three, below.

Table 3: Historic Active Health Care O&M Costs

Year	Test Year/Allowed	Actual Book	Over/(Under) Recovery
2011	$38,042,035	$32,996,942	$5,045,093
2012	$38,042,035	$33,669,857	$4,372,178
2013	$34,419,215	$32,742,574	$1,676,641

Total			$11,093,912

DOC Ex. 423 at 35 (Byrne Direct). This table showed that Xcel has significantly over-recovered its O&M costs since 2011. In addition to this recent history of over-recovery, other factors indicated that health care costs will not increase as much as Xcel forecasted in its 2014 test year. First, the PriceWaterhouseCoopers's (PWC) study attached to Mr. Moeller's Direct Testimony stated that health care costs are projected to increase by 6.5 percent in 2014 on a national average in the large employer market; that amount is a full percentage lower than the 7.5 percent increase predicted by PWC for 2013. DOC Ex. 423 at 35 (Byrne Direct) (*citing* Xcel Ex. 81 (MPM-1), Schedule 16, Page 7 of 26 (Moeller Direct)).

182. Second, Xcel's over-recovery of 2013 actual O&M costs --of approximately $1.68 million --occurred even after DOC Witness Ms. Campbell adjusted the 2013 test-year expenses in the last rate case. DOC Ex. 423 at 35 (Byrne Direct).

183. Third, in the current 13-868 rate case, 2014 national costs are forecasted to increase a full percentage *less* than was predicted for 2013, yet Xcel requested an 11 percent increase over 2013 O&M expenses. DOC Ex. 423 at 36 (Byrne Direct)

184. Fourth, even with Xcel's two proposed adjustments to reduce Active Health Care O&M costs to more accurately reflect the lower costs experienced by NSPM, Xcel's over-recovery since 2011, along with other evidence suggesting that cost increases are less than forecasted, indicate that Xcel's 2014 adjusted request of $36,443,475 in O&M expenses is still unreasonably high, and that Xcel has not shown its proposed Active Health Care O&M cost to be reasonable. DOC Ex. 423 at 36 (Byrne Direct).

185. Ms. Byrne testified to a reasonable level of Active Health Care O&M costs for the 2014 test year. She explained that, because Xcel modified several aspects of its health care plan in 2011, historical costs after 2011 should provide a fairly accurate picture of costs under the new plan structure. As shown in her Table 3, costs fluctuated over the last three years, so a three-year average would be most appropriate. Based on this average, Ms. Byrne concluded that $33,136,458 is a reasonable level of O&M expense in the 2014 test year. This level reduced Xcel's proposed O&M expense by $3,307,017, as shown in DOC Ex. 424 ACB-15 (Byrne Direct Attachments); DOC Ex. 423 at 36 (Byrne Direct).

186. In addition to this adjustment for Active Health Care, which was an O&M expense, Ms. Byrne recommended a corresponding adjustment for the capitalized Active Health Care costs. She noted that there are corresponding capital costs for all Health & Welfare benefits; $7,777,838 for Minnesota Jurisdiction Active Health Care expenses. DOC Ex. 423 at 37 (Byrne Direct) (*citing* Xcel Ex. 81 (MPM-1), Sched. 2 at 3 (Moeller Direct). Because she recommended reducing test year O&M expenses by 9.1 percent, she recommend a corresponding 9.1 percent reduction of capital expenses, or $757,561, as shown in DOC Ex. 424 ACB-15 (Byrne Direct Attachments); DOC Ex. 423 at 37 (Byrne Direct).

187. In Surrebuttal Ms. Byrne reviewed Xcel's response and continued to conclude that Xcel has not fully supported its proposed test-year increase of 5.93 percent. She recommended

an inflation factor of 2.85 percent over 2013 claims expenses. This figure was an average of the annual percentage increases in claims expense of 2.08 in 2012 and 3.63 percent in 2013, as shown in her Surrebuttal Table 1:

Table 1: Annual Increases in Active Health Care Costs

	Claims Expense	**Annual $ Increase**	**Annual % Increase**
2011	$32,523,776		
2012	$33,200,054	$676,278	2.08%
2013	$34,404,965	$1,204,911	3.63%
2014 Test Year	$36,443,475	$2,038,210	5.93%

DOC Ex. 427 at 20 (Byrne Surrebuttal).

188. DOC's recommendation resulted in test-year Active Health Care O&M expense of $35,386,982, or a reduction to Xcel's request of $1,056,493. Ms. Byrne also continued to recommend a proportional reduction of capital costs, by $225,480, as shown at DOC Ex. 427 ACB-S-1 (Byrne Surrebuttal); DOC Ex. 427 at 21 (Byrne Surrebuttal).

189. Xcel Witness Mr. Richard Schrubbe stated in his opening statement that the Company agreed to Ms. Byrne's Surrebuttal position on Active Health Care costs, which reduced Xcel's requested level of Active Health Care O&M expense by slightly more than $1 million and capital costs by approximately $225,000. For ease of incorporating both of these adjustments into the revenue requirement, Xcel Witness Ms. Heuer combined the adjustments into one income statement adjustment of $1.082 million, to which DOC agreed. DOC Ex. 427 at 21 (Byrne Surrebuttal); DOC Ex. 449 at 1 (Byrne Opening Statement).

190. As a final recommendation, Ms. Byrne recommended that the Commission direct Xcel, in a compliance filing in Xcel's next rate case initial filing, to provide historical Active Health Care costs since 2011, both book and claims expenses, for all available calendar years. This information should also include detail to show the annual year-end IBNR accruals and the subsequent reversals, not just a net annual amount as was provided in IR 1194.

191. Mr. Lusti, in his Surrebuttal Testimony, summarized the test-year rate base and income statement effects, stating that the DOC's recommendation decreases the test-year rate base by $226,000 and administrative and general expense by $1,056,000, as shown in DOC Ex. 442 DVL-S-4, column (f) and DOC Ex. 442 DVL-S-7, column (j), respectively (Lusti Surrebuttal); DOC Ex. 442 at 9 (Lusti Surrebuttal).

192. The Company agreed to the Department's reduction in active health care costs as recommended in Ms. Byrne's Surrebuttal Testimony but in a combined revenue requirement adjustment of $1.082 million to the 2014 Test Year. Xcel Ex. 140 at 1 (Heuer Opening Statement); DOC Ex. 451 at Attachment DVL-EH-7, Page 1 of 4, Column (j) (Lusti Opening Statement).

193. The ALJ finds that this adjustment, as agree by Xcel and the Department, is reasonable.

G. Affiliated Interest Service Company Allocations (Issue 37)

Resolved between DOC and Xcel: DOC and Xcel agreed that the results of the Commission's order from the Affiliated Interest Docket should be incorporated into the current rate case. Xcel will calculate and reflect any changes that result from the Affiliated Interest Docket into this rate case. DOC Ex. 427 at 2-3 (Byrne Surrebuttal) (*citing* Xcel Ex. 87 at 13-14 (Stitt Rebuttal); DOC Ex. 423 at5 (Byrne Direct); DOC Ex. 449 at 3 (Byrne Opening Statement).

194. The Service Agreement between Xcel and its affiliate, Xcel Energy Service, Inc. (XES or Affiliate), contains the terms and conditions pursuant to which XES provides products and services to Xcel, such as legal and administrative services, and management of generation, transmission, and distribution assets. Parts of these terms and conditions are the methods by which the costs of these services are allocated to various users, including Xcel and other affiliated operating companies such as Public Service Company of Colorado. DOC Ex. 423 at 3 (Byrne Direct) (*citing* Docket No. E,G002/AI-14-234, Xcel's Initial Petition at 5).

195. The Commission's Order approving the current Service Agreement between Xcel and its Affiliate in Docket No. E,G002/AI-08-760 was dated January 29, 2009. Approximately five months after the Company filed this 13-868 rate case, on March 24, 2014, Xcel filed a petition in Docket No. E,G002/AI-14-234 (Docket 14-234) (the "Affiliated Interest Docket") where Xcel proposed a second amendment to the current Service Agreement. In that petition, Xcel stated:

> In preparing for our most recent general rate case, we discovered that we were, in some cases, applying a modified version of cost allocation methods than those specifically provided for in the Service Agreement. These changes had been implemented over the past several years to maintain cost-causative assignment and allocation methods, largely due to organizational changes. The modifications mostly involve a more specific application of the currently approved allocation methods in the Service Agreement. The Second Amendment resolves this disconnect between our current Cost Assignment and Allocation Manual, which has been updated from time to time and contains our current (modified) cost allocation methodologies, and the Service Agreement, which contains several outdated cost allocation methodologies.
>
> We seek Commission approval for the Second Amendment for two distinct reasons. The first is the Service Agreement, including amendments to it, is an affiliate interest transaction, and its approval is therefore subject to Minn. Stat. § 216B.48 and the Commission's rules. We believe the timing of this Petition is consistent with the requirements set forth under Minnesota law, since this filing is being made within 30 days of the Company and XES entering into the Second Amendment.
>
> The second is the Service Agreement, specifically the First Amendment, requires us to seek Commission approval before making any changes to the Service Agreement. While our intent has always been to remain in compliance with the

> executed and approved Service Agreement, we inadvertently did not make changes to the Service Agreement, nor seek Commission approval prior to implementing these new cost allocation methodologies. We apologize for our inadvertent oversight in not requesting approval of these changes in advance of implementing them. As we discuss later, we have several ideas about how we can address this on a going-forward basis that we would like to discuss with the Commission, Department and other stakeholders.

DOC Ex. 423 at 4-5 (Byrne Direct) (*citing* Docket No. E,G002/AI-14-234, Xcel's Initial Petition at 1-2).

196. With respect to Xcel's instant 13-868 rate case, Xcel stated that the cost allocation methods used to develop the test year budget were not the cost allocation methods in the approved Service Agreement. However, Xcel stated that the unapproved methods would likely allocate $1.6 million less to the Minnesota Electric Jurisdiction for the 2014 test year than if Xcel had used allocators in the approved Service Agreement. DOC Ex. 423 at 5 (Byrne Direct).

197. The Department did not make a specific recommendation in this 13-868 rate case regarding Xcel's Service Agreement Petition; however, the Department filed comments on May 29, 2014 in the Affiliated Interest Docket No. E,G002/AI-14-234 (AI Docket) on May 29, 2014 requesting additional information from Xcel to support its proposal. The Department's Direct Testimony stated the intention to incorporate the results of the Commission's order from that docket into the current rate case. DOC Ex. 423 at 5 (Byrne Direct).

198. Xcel requested a two-month extension to its reply comments in the AI proceeding, resulting in their comments being filed after surrebuttal testimony was filed in the instant case. However, Xcel agreed to incorporate the results of the Affiliated Interest Docket into this rate case. Xcel Witness Ms. Amy L. Stitt stated that in the Company committed to calculate and reflect any changes that result from the Affiliated Interest Docket into this rate case. DOC Ex. 427 at 2-3 (Byrne Surrebuttal) (*citing* Xcel Ex. 87 at 13-14 (Stitt Rebuttal). At the hearing, Ms. Byrne recommended that the Commission's Order in the in the Affiliated Interest Docket No. E,G002/AI-14-234 be reflected in the Commission's decision in this rate case, and the Company agreed to this recommendation. DOC Ex. 449 at 3 (Byrne Opening Statement).

199. In his Surrebuttal Testimony, Mr. Lusti explained that he included, for Affiliated Interest Service Company Allocations, a $0 adjustment to the test-year rate base and operating income as a placeholder for any future adjustment. DOC Ex. 442 at 9 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-4, column (g) and DVL-EH-7, column (n) (Lusti Opening Statement).

H. Monticello Extended Power Uprate (EPU) 2014 In-Service Date and 2015 Prudency Adjustment (Issue 2)

Disputed between DOC and Xcel -- 2014 Test Year. Xcel has not shown that the Monticello EPU project (71 MW) has been used and useful (available to ratepayers for 2014 at the CN-approved 71 MW operating level and approved by Nuclear Regulatory Commission (NRC) to be operated at that level), nor does the record support Xcel's argument that the EPU will be used

and useful by the end of the 2014 test year. DOC opposes Xcel's proposed partial used and useful adjustment as inconsistent with law, Commission practice and the facts of the case. Thus, DOC recommends eliminating rate base treatment and associated depreciation costs for the 2014 Test Year, as follows: a $31.284 million revenue requirement reduction such that the 2014 depreciation expense and rate base return on the Monticello EPU are excluded from the 2014 test year. DOC Ex. 450 at 3 (Campbell Opening).

Disputed between DOC and Xcel -- 2015 Test Year: As a placeholder in the present rate case, pending the Commission's decision regarding the Monticello Cost Overrun Investigation, DOC recommends an adjustment for the 2015 Test Year of a $10.237 million revenue requirement reduction (based on the assumption that the EPU will be in service in 2015); the final prudency adjustment for the 2015 Test Year will depend on the Commission's final prudency determination in Docket No. E002/CI-13-754. Ex. 450 at 3 (Campbell Opening).

Resolved between DOC and Xcel -- 2015 Test Year:
1) DOC assumes the Monticello EPU will be in-service by January of 2015, i.e., that it will have reached the CN-approved increase level of 71 MW (671 MWe) and that NRC will have approved it to be operated at this level. Assuming that Xcel makes this showing, DOC recommends rate base treatment and recovery of associated depreciation costs for the 2015 Test Year, as shown in Attachment A, column (d) of the Company's response to Department information request no. 2148. Ex. 450 at 3 (Campbell Opening).

2) If, however, by January of 2015 the Monticello EPU does not operate successfully at the 671 MWe level, and is not approved by the NRC to be operated at this level, DOC recommended requiring Xcel to refund any amounts collected in rates through the refund mechanism for the MYRP, per the terms of the Multi-Year Rate Plan (MYRP) agreement between Xcel and DOC addressed by DOC Witness Lusti (Issue 35). Ex. 450 at 3 (Campbell Opening).

Disputed between Xcel and XLI, disputed between XLI and DOC – 2014 Test Year: XLI proposed to exclude 11/12 of the Monticello EPU costs in rate base for the 2014 Test Year, based on use of a 13 month average, and assuming that the EPU is in service in December 2014. Xcel opposed this proposal as being inconsistent with the historical practice of using a beginning and ending of year (BOY/EOY) average for forecasted rate base items. DOC also opposes XLI's proposal as being inconsistent with the historical use of BOY/EOY averages; in addition, DOC opposes recovery from ratepayers of capital costs for facilities that are not shown to be wholly used and useful by the end of the test year. DOC Ex. 435 at 56 (Campbell Public Surrebuttal).

Resolved between Xcel and the MCC, disputed by DOC – 2014 and 2015 Test Years: Xcel recommends use of the Chamber's proposal for 2014 to defer depreciation and amortize the increased replacement fuel and power costs associated with the EPU delays over the life of the plant such that Xcel's proposed 2014 Test Year revenue requirements would be reduced by $12.227 million (for depreciation) and its proposed 2015 Step revenue requirement would be increased by $11.680 million. Xcel Ex. 140 at 3 (Heuer Opening); see DOC Ex. 435 at 56-57 (Campbell Public Surrebuttal); and see Tr.V.3 at 178, 185-186 (Schedin). DOC opposes MCC's proposal because the EPU is not used and useful in 2014 and, thus, EPU costs associated with 2014 should not be charged to ratepayers in 2014, and also because deferring costs does not

eliminate the costs but simply delays recovery, together with an added 2014 rate base return. Additionally, it does not make sense to defer/capitalize replacement fuel and power costs that are being paid by ratepayers currently. DOC Ex. 435 at 56-58 (Campbell Public Surrebuttal).

1. Introduction

200. Consistent with the Joint Prehearing Order dated July 17, 2014, the in-service date of the Monticello Extended Power Uprate (EPU) is an issue in this rate case; that is, the Department concludes that Xcel did not demonstrate that the EPU is or is likely to be "used and useful" during the 2014 Test Year. Issues regarding the reasonableness and prudence of the costs of the Life Cycle Management (LCM) and EPU projects as well as issues of cost allocation between the LCM and EPU projects are not issues for this rate case, but will be addressed in the Monticello Cost Overrun Investigation.[12]

201. Regarding the EPU in-service date, the Commission's January 8, 2009 Order, MPUC Docket E-002/CN-08-185, approved a CN for the Monticello EPU to expand generating capacity by 71 MW, but the plant has not yet achieved operation at the 671 MW (600 MW for the LCM and 71 MW for the EPU) level as it was intended and designed to do, and the NRC has not yet approved Xcel's operation of the plant at the 671 MW level. As of the end of the evidentiary hearing on August 14, 2014, the plant was operating only at pre-EPU levels. Specifically, Xcel witness Timothy O'Connor testified on cross-examination that the Monticello plant currently was operating at 600 MWe, and that the NRC has not provided Xcel any timeframe as to when the NRC might approve Xcel's operation of the EPU at the 71 MW level (also referred to as the 671 MWe level). As DOC witness Nancy Campbell summarized in her Opening Statement, key reasons that Xcel has not shown the Monticello EPU to be used and

[12] *See* Joint Prehearing Order at 2, MPUC Docket Nos. E-002/GR-13-868 and E-002/CI-13-754 (July 17, 2014). Also in accordance with the Joint Prehearing Order, the ultimate rate impact of the Commission decision regarding prudency in the Monticello Cost Overrun Investigation will be reflected in the Commission's final rate decision in this rate case, id., such that the Department recommends as a "placeholder" in this rate case a downward adjustment for the 2015 Test Year of a $10.237 revenue requirement reduction (based on the assumption that the EPU will be in service in 2015). DOC Ex. 450 at 3 (Campbell Opening).

In her Direct Testimony at 44, DOC witness Campbell explained the relationship of the EPU and LCM projects:

> The Monticello LCM extends the availability of the 600 MW base plant, anticipated for 20 years (due to delays this NRC license life and resulting depreciation life was only 16.8 years as of January 1, 2014 as discussed further below). The remaining 71 MW is related to the Monticello EPU, which is intended to increase the capacity of the existing plant by 71 MW anticipated for 20 years (again, this NRC license life and resulting depreciation life was only 16.8 years as of January 1, 2014, with the life continuing to get shorter at this time).

useful and, thus, why ratepayers must not be required to pay for the EPU in rates based on the 2014 Test Year are as follows:[13]

- the Monticello EPU project (71 MW) will not be available for most if not all of the 2014 test year, therefore it is not reasonable for ratepayers to pay for the Monticello EPU in the 2014 test year;
- the Monticello EPU project has not yet reached the CN-approved increase level 71 MW (671 MWe), nor has it been approved to do so; and
- human performance errors appear to have contributed to the NRC's concerns regarding the EPU power ascension testing.

202. For the 2014 test year, because Xcel has not shown that the EPU is or will be used and useful by the end of 2014, the Department recommends eliminating rate base treatment and associated depreciation costs of the EPU, as follows: a $31.284 million revenue requirement reduction such that the 2014 depreciation expense and rate base return on the Monticello EPU are excluded from the 2014 test year.[14]

203. For the 2015 Test Year, the Department bases its recommendation on the assumption that the EPU is in-service by January of 2015, as follows:[15]

- Assuming that the Monticello EPU is in-service by January of 2015, i.e., that it will have reached the CN-approved increase level of 71 MW (total plant level of 671 MWe) and that NRC will have approved it to operate at this level, the Department recommends rate base treatment and recovery of associated depreciation costs for the 2015 Test Year, as shown in Attachment A, column (d) of the Company's response to Department information request no. 2148..

- If the Monticello EPU does not operate successfully at the 671 MWe level by January 2015, and is not approved by the NRC to be operated at this level, the Department recommends that the Commission require Xcel to refund any amounts collected in rates through the refund mechanism for the MYRP.

2. Xcel bears the burden of demonstrating that the Monticello EPU is used and useful to ratepayers in 2014

204. Minnesota law protects ratepayers from paying for a utility project before the utility proves it is used and useful to ratepayers. Specifically, the law requires utilities to charge

---

[13] *See* DOC Ex. 450 at 3 (Campbell Opening); DOC Ex. 435 at 34, 43-58 (Campbell Public Surrebuttal); Tr.V. 1 at 232-33, 239 (O'Connor). *See also* Tr.V. 1 at 245 (O'Connor) (stating that when river water was coldest, the total plant operated at about 609 MWe); DOC Ex. 450 at 3 (Campbell Opening).

[14] *Id.*

[15] *Id.* at 3-4.

"just and reasonable" rates. Determining whether rates are just and reasonable, Minnesota Statute section 216B.16 requires the following:[16]

> Subd. 4. Burden of proof.
>
> The burden of proof to show that the rate change is just and reasonable shall be upon the public utility seeking the change.
>
> * * *
>
> Subd. 6. Factors considered, generally.
>
> The commission, in the exercise of its powers under this chapter to determine just and reasonable rates for public utilities, shall give due consideration to the public need for adequate, efficient, and reasonable service and to the need of the public utility for revenue sufficient to enable it to meet the cost of furnishing the service, including adequate provision for *depreciation of its utility property used and useful in rendering service to the public*, and to earn a fair and reasonable return upon the investment in such property. In determining *the rate base upon which the utility is to be allowed to earn a fair rate of return, the commission shall give due consideration to evidence of the cost of the property when first devoted to public use,* to prudent acquisition cost to the public utility less appropriate depreciation on each, to construction work in progress, to offsets in the nature of capital provided by sources other than the investors, and to other expenses of a capital nature. For purposes of determining rate base, the commission shall consider the original cost of utility property included in the base and shall make no allowance for its estimated current replacement value.

The Minnesota Supreme Court has held that utility property is "used and useful" when it: 1) is "in service"; and 2) is "reasonably necessary to the efficient and reliable provision of utility service. Finally, Minnesota law also provides that "any doubt as to reasonableness" must be resolved in favor of the consumer.[17]

205. Xcel has not shown that the EPU is or is likely to be used and useful by the end of 2014 since the EPU is not rendering service to ratepayers (the plant is operating at pre-EPU power levels), Xcel never has operated the EPU at its intended and designed level of 71 MW, the NRC has not yet given approval for the Company to operate the EPU at the 71 MW level (or even to resume power ascension testing of the EPU at any level), and there is no reasonable basis in the record to conclude, as Xcel does, that the EPU will be fully operational and approved by the end of 2014. Tr.V. 5 at 17 (Campbell); DOC Ex. 435 at 34-53 (Campbell Public Surrebuttal). Xcel's failure to show that the EPU is likely to be used and useful by the end of 2014 is set forth in greater detail in the next section of this Initial Brief.

---

[16] Minn. Stat. § 216B.16, subd. 4, 6 (2014); Minn. Stat. § 216B.03 (2014) (emphasis added).

[17] *Senior Citizens Coalition of N. Minn. v. MPUC*, 355 N.W.2d 295, 300 (Minn. 1984); Minn. Stat. § 216B.03 (2014).

206. Moreover, Xcel's arguments that the EPU is used and useful in 2014 are novel and unsupported. Specifically, the record does not support Xcel claims, 1) that the Commission, in Xcel's most recent rate case, MPUC Docket E-002/GR-12-961, determined the EPU would be used and useful as soon as the NRC issued a 20-year license, 2) that the EPU is constructed and is using the assets "to operate at uprate conditions," or 3) that a portion of the EPU is used and useful (as measured by a percentage of the total EPU attributable to the power ascension testing level of 640 MWe that the plant reached before being required for safety reasons to resume pre-EPU level operation). *See* Xcel Ex. 100 at 23-25 (Clark Rebuttal). Department witness Campbell fully rebutted these arguments.

207. First, it cannot reasonably be argued that the Commission determined in the 2012 Xcel rate case that the Monticello EPU would be used and useful as soon as it received the 20-year license from the NRC to operate at the higher EPU levels and began operating at any level higher than its base 600 MWe. The Commission made no such decision nor did the ALJ make such a recommendation. The ALJ Report in the 2013 rate case included several reasons why Xcel had not shown the EPU to be used and useful to ratepayers during the 2013 test year in that matter. Review of ALJ proposed Findings 78 – 82 clearly show multiple reasons underpinning the ALJ's conclusion that the Monticello EPU was not used and useful to ratepayers in that case. Proposed Findings No. 78–82 stated, as follows:[18]

> 78. The record in this case demonstrates that the Monticello LCM/EPU capital project is "in service" **but only** for LCM purposes. The equipment installed as part of the LCM/EPU project is being used to generate electricity at existing levels, not at the higher EPU level. [citation omitted]
>
> 79. The EPU portion of the project is not "in service" because the Company does not yet have the NRC license amendment required to operate at uprated EPU level. As a result, the Company cannot generate the additional 71 MW that the EPU is designed to provide. The Company can only operate at its current licensed capacity. The Company will not be able operate at its uprated power level until it receives authorization from the NRC. *Id.*; Ex. 19 at 16 (Robinson Rebuttal).
>
> 80. In addition, it is not reasonable to expect that the NRC will issue the license amendment for the EPU during the 2013 test year. The record in this case shows a history of delays by the NRC and the current federal government sequester calls into serious question the likelihood that the license amendment will be issued this year. Thus, the Company has failed to demonstrate by a preponderance

[18] DOC Ex. 435 at 41 (Campbell Public Surrebuttal) (referring to MPUC Docket E002/GR-12-961); Findings of Fact, Conclusions of Law and Recommendation at 16, MPUC Docket No. 002/GR-12-961 (July 3, 2013) (2013 ALJ Report).

> of the evidence that the property will be "in service" for EPU purposes during the 2013 test year.
>
> 81. In addition, the EPU required installation of equipment that was specifically designed to allow the plant to generate at the increased level. As a result, some of the equipment installed is larger than would otherwise be necessary and some equipment would not have been required but for the EPU. Because the plant has not yet operated at its increased level, the EPU-related equipment is not being used for its intended purpose and is not benefitting ratepayers at this time.
>
> 82. Thus, contrary to the assertion of the Company, the fact that the project investments are being used to generate electricity at current levels for LCM purposes does not mean that the entire LCM/EPU project is "in service" or "used and useful" for purposes of Minn. Stat. § 216.16, subd. 6. Because the plant is only generating power at existing levels, the EPU portion of the project is not "in service" or "used and useful."[FN 81] Any other interpretation of Minn. Stat. § 216B.16 would improperly allow the Company to recover EPU costs, with a return, before ratepayers ever receive the benefit of the additional 71 MW of EPU capacity. To allow recovery of the EPU costs before the plant provides the additional power would result in unreasonable rates for ratepayers.
>
>> [FN 81]: The Company's reliance on precedent to support its "used and useful" argument is not persuasive. None of the cases cited presents a situation like that in this matter where the project costs to be recovered were, in part, for an EPU but the plant was not yet operating at the increased EPU levels.

The Commission adopted the ALJ's proposed Findings regarding the Monticello EPU. Thus, Xcel's lack of an NRC license *as well as* its failure to operate the facility at the EPU's designed capacity of 71 MW were among the reasons that the Commission determined that the Monticello EPU was not used and useful to ratepayers in the 2013 rate case. [19]

208. Second, the facts of this rate case show that the EPU is not in-service, has never been in service or been operated at its intended and designed level of 71 MW for a total LCM and EPU level of 671 MWe. Under power ascension testing, the EPU briefly reached only a total 640 MWe level in early 2014 whereupon the NRC required Xcel to power down to pre-EPU levels (600 MW or lower) until Xcel met power ascension testing protocols (DOC Ex. 435 at 43 (Campbell Public Surrebuttal)) which it has not yet completed. Further discussion in the next

[19] Findings of Fact, Conclusions and Order at 19, MPUC Docket E002/GR-12-961 (Sept. 3, 2013) (2013 Order).

section of this Initial Brief shows that there is no reasonable basis to conclude that the EPU will operate at 671 MWe, with NRC approval, by the end of 2014.

209. Third, the Monticello EPU is not "operating at uprate conditions," was not previously placed in service and is not on outage. That is, the EPU "uprate level" is 71 MW as proposed and approved by the Commission in the CN (*Id.*) for a total Monticello LCM and EPU generation capacity of 671 MWe. Since the EPU has never been placed in-service, it cannot be said that the EPU is on a temporary outage of some kind. *Id.*; see also DOC Ex. 435 at 46 (Campbell Public Surrebuttal). Even before knowing about yet more delays identified by Xcel in Mr. O'Connor's Surrebuttal Testimony, (*see* Xcel Ex. 55 at 4-5 (O'Connor)) Ms. Campbell summarized in her Surrebuttal Testimony why Xcel has not shown that the Monticello EPU is like a plant outage:

> I do not agree with Mr. Clark that this very capital-intensive project should be treated like a plant outage. Given that: 1) the NRC has not allowed the plant to operate at the 671 MWe level, 2) the plant is not operating at the 640 MWe level for the reasons discussed above, and 3) the plant *is* operating at 600 MWe, current operations and non-operations of the plant cannot be considered to be a plant outage. Instead, the fact remains that the Monticello EPU has not yet been approved to be fully up and running at the 671 MW level, and may not reach that level for most or all of 2014 based on the Company's response to Department information request 115.

DOC Ex. 435 at 46 (Campbell Public Surrebuttal). At present, the Monticello plant is operating at no more than pre-EPU levels of about 600 MWe, which means the EPU isn't operating. It is curious that Xcel highlighted the fact that the Monticello plant is achieving over 90 percent of its potential, since this fact confirms that the EPU isn't being used (600/671 = 89.4 or 89 percent). [20]

210. Examination of Xcel's claim that the Monticello plant as a whole (as opposed to the EPU alone) operated at 95 percent of its operating capacity when it briefly reached the 640 MWe power level as part of the NRC's power ascension testing shows similar support for a conclusion that the EPU has not been used and useful to ratepayers at its intended and approved 71 MW level. A 640 MWe power level during power ascension testing equates to a level of 40 MW for the EPU alone, and represents a level of 40/71—about half (56 percent)—of the EPU's 71 MW designed and approved capacity. Further, the Monticello LCM and EPU was only at the 640 MWe level for 20 days before it was necessary for Xcel to power down from even that level. Currently, the EPU is not operating at all (Monticello is operating at no more than 600 MWe). Xcel must complete NRC's power ascension testing protocol successfully, with full authorization from NRC to operate at 671 MWe before the EPU can be considered to be placed into service and used and useful to ratepayers. [21]

---

[20] Tr.V. 1 at 239 (O'Connor); Xcel Ex. 53 at 14-15 (O'Connor Public Rebuttal).

[21] Xcel Ex. 53 at 15 (O'Connor Public Rebuttal); Tr.V. 1 at 231, 239 (O'Connor).

211. Fourth, there is no Commission precedent as far as the Department is aware that would support Xcel's proposed alternative of finding that the EPU is "partially" used and useful by components, percentages of completion or by some other measure like operational power levels. Xcel's proposal is unsupported and could have wide-ranging implications for other facilities and dockets before the Commission, as Ms. Campbell summarized:[22]

> I am not aware of any proceeding where the Commission has allowed part of an uprate or plant upgrade (either by component or by percentages of completion or operation) to be included in rates in such a piecemeal fashion as suggested by the Company. Such an approach seems to be particularly unwarranted given that the Monticello EPU is not currently operating at the 640 MWe level and only did so briefly in the test year. *Xcel's suggested interpretation of the "used and useful" standard would be novel at best and likely would have far reaching effects on other facilities and dockets.*
>
> Thus, I conclude that Xcel has not shown that it is reasonable for the 40/71 MW or 56.3 [percent] of the EPU to be placed in service for determining rates in 2014. The facility continues to be engaged in testing that is subject to review and approval by the NRC.

Additionally, Ms. Campbell pointed out that the number of megawatts Xcel proposes to use for its partial used and useful adjustment apparently are those megawatts attributable to the 20 days that the EPU operated at the 40 MW (total 640 MWe) during power ascension testing; those 40 megawatts, however, "are no longer available at all until power ascension testing process is completed and approved as described by Mr. O'Connor."[23]

212. The ALJ finds that Xcel has not shown that the Monticello EPU is or was used or useful and, thus, ratepayers must not be required to pay for the EPU with respect to the 2014 test year.

3. The record does not support a conclusion that it is likely the EPU will be operating at 671 MWe, with NRC approval, by the end of 2014

213. Xcel has not shown that the EPU is likely to be used and useful by the end of 2014. Review of specific problems and delays encountered by Xcel to-date undermines the Company's continued prediction that by the end of 2014 it will have completed EPU power ascension testing to the EPU level of 671 MWe with NRC approval. Attached to her Direct Testimony as NAC-8, Ms. Campbell included Xcel's response to DOC Information Request (IR) No. 115 that details particular problems identified as part of Xcel's unsuccessful attempts to

[22] DOC Ex. 435 at 45 (Campbell Public Surrebuttal).
[23] Tr.V. 1 at 231 (O'Connor); DOC Ex. 435 at 56 (Campbell Public Surrebuttal).

meet NRC power ascension testing requirements. Those problems required Xcel to return to safe power levels of approximately 600 MW. The problems included "stresses [that] were running lower than expected," human programming errors regarding initial setup for data collection (data needed to be collected for NRC to review), and erroneous wire connections due to human errors in labeling of wires. NAC-8, which was Xcel's May 5, 2014, response to DOC IR 115 in the Monticello Cost Overrun Investigation, identified the problems, but continued to estimate completion within 2014 without support, as follows:[24]

> Monticello has specific license requirements that must be met and verified during power ascension testing. The testing will take the station from its previous licensed output of 1775 MWt (approximately 609 MWe) to our new approved output of 2004 MWt (approximately 671 MWe).
>
> The process is such that the Company increases power in small increments and collects data for verification against licensed parameters. When the station reaches predefined power levels the data is collected and sent to the NRC for review. The station will not move up in power without NRC concurrence. NRC review times vary based on the data being evaluated and how close it correlates to the values submitted during the licensing process.
>
> Testing to Date:
> After receiving the EPU license on December 9, 2013, the Company began its ascension plan. Power was increased in December and testing began. We moved through the first two power ascension set points in December and January. Then on March 11, 2014, the unit reached the first required data collection plateau, which was 1864 MWt (approximately 640 MWe). The data collection is required as part of the Power Uprate License and is intended to provide verification that the steam dryer is not reasonably likely to be damaged as a result of uprated conditions as occurred at Quad Cities. The data was collected and sent to the vendor for review and their concurrence. *During that review, the vendor discovered that the stresses were running lower than expected, consistently across the entire data collection range, by a factor of 2. As a result, to comply with our license, we returned the plant to the previously known safe power level of 1775MWt (approximately 609 MWe).*

[24] DOC Ex. 429 at 51-53 (Campbell Public Direct); *see also* DOC Ex. 435 at 44, 46, 48 (Campbell Public Surrebuttal); DOC Ex. 429 at 51-53 and NAC-8 (Campbell Public Direct) (emphasis added).

The vendor reviewed the data and determined that *a programming error was made* during the initial setup for data collection. *The program was initially changed* to accommodate reactor vessel pressure testing, which is required by technical specifications to restart the reactor, *but was not reset properly to capture steam loads; thus, creating the error.* This data anomaly was easily reconciled and the offset was dispositioned by the vendor. However, as part of the normal process of conducting additional extent of condition review of the entire data provided, *we discovered a configuration issue associated with the wiring to the strain gauges on one of the main steam lines (located in the Drywell). The upper and lower wires were mislabeled and thus lead us to connect them incorrectly* at the data Collection Panel located outside of the Drywell. The physical distances are different between the upper and lower collection points and this requires the vendor to re-run their stress model with the correct configurations. Following the completion of their data set runs, Xcel Energy will review the results and submit them to the NRC as required by the license. Once the NRC completes their review we will resume power ascension testing.

Steps Going Forward:
We expect our reanalysis and re-verification of the model and the inputs and outputs to be completed by the end of June and we expect NRC review will take approximately one month, so we expect to re-enter power ascension in August, assuming no additional licensing activities are required. The Company believes that we will be able to achieve full power of 2004 MWt (approximately 671 MWe) by the end of 2014 based on the following ascension plan, which contains the same steps as our pre-data issue plan but with different dates:

- August- Raise power to 1819 MWt (approximately 624 MWe) for Steam Dryer Data only.
- Early September- Raise power to 1864 MWt (105% or approximately 640 MWe) for Steam Dryer only (This is the power level that we need to submit Dryer Data to NRC)
    - Submit the data to the NRC for their review and concurrence.
- Late September- Raise Power to 1908 MWt (approximately 658 MWe) and commence Dynamic Testing.
- October- Transition to M+ Operating Domain, as required by the license. This transition will result in a power reduction to 1686 MWt (approximately 580 MWe), which is the starting verification point on the operators Power to Flow Map.

- October- Raise power to M+ 1775 MWt (approximately 609 MWe)
- Mid-November- Raise power to M+ 1864 MWt (105% or approximately 640 MWe)
- Mid-November- Raise power to M+ 1908 MWt (approximately 658 MWe).
- End of November- Raise Power to EPU 1953 MWt (approximately 664 MWe)
    - Submit the data to the NRC for their review and concurrence.
- December- Raise Power to EPU 2004 MWt (approximately 671 MWe) output. The 2004 MWt power level correlates to the new power level of 671MWe and will end the testing window pending NRC concurrence. The time line provided is based on timely reviews by the vendors and the NRC. Should the data render unexpected results, the review times could be impacted.

214. Delays continued. Xcel extended the date it had given itself to send NRC the data required from the Company's first "data collection" power level of 640 MWe, from the end of June to mid-July.[25] The Company sent that data to NRC on July 22, 2014. Yet, despite delays, Xcel witness Mr. O'Connor continued to predict that by the end of December, 2014, Xcel will complete the EPU power ascension testing to 671 MWe.[26]

215. In her Surrebuttal Testimony, Ms. Campbell noted Xcel's lack of support for its expectation that in 2014 the Company will complete the EPU power ascension milestones to operate the plant at the total 671 MWe level. She emphasized the significant delays that had occurred since Xcel submitted its response to DOC IR 115. For example, in addition to Xcel delaying its sending to NRC the data from the first data collection, NRC clearly had not reviewed and approved the data submission within the earlier milestone timeframe, and Xcel had not resumed the EPU the power ascension process that Xcel predicted would occur in August, 2014. Moreover, Ms. Campbell's comparison of Xcel's response to DOC IR No. 115 and page 13 of Mr. O'Connor's Rebuttal Testimony showed that Xcel's expected completion of power ascension testing and NRC approval by the end of 2014 essentially to be "hope and conjecture" rather than likely fact, as follows:[27]

> [T]he new August 2014 schedule appears to be the same at 1,819 MWt as it is for the Steam Dryer Data only. However, the two schedules change after August 2014 with the response to DOC 115 appearing to provide several steps and incremental power level

---

[25] DOC Ex. 435 at 50-51 (Campbell Public Surrebuttal).

[26] Xcel Ex. 55 at 4 (O'Connor Surrebuttal); *see* Xcel Ex. 53 at 12-13 (O'Connor Public Rebuttal); *see also* DOC Ex. 435 at 50-53 (Campbell Public Surrebuttal).

[27] DOC Ex. 435 at 50-53 (Campbell Public Surrebuttal). Further delays were disclosed by Mr. O'Connor in his Surrebuttal Testimony at 4-5.

> amounts before reaching the full 2,004 MWt or 671 MWe output in December 2014. However, *Mr. O'Connor's revised schedule in his Rebuttal Testimony does not include all of the same steps and incremental power level amounts, or new expected dates, and yet somehow reaches the 2,004 MWt or 671 MWe output level in early September 2014*.
>
> Mr. O'Connor did not provide any specific information to explain why Xcel took more time to provide data to the NRC or to support the accelerated timeline to power up the EPU in his Rebuttal Testimony, although he noted generally and without specifics on page 13 that the timeline provided is based on timely reviews by the vendors and NRC. He noted that if the data render unexpected results, the review times could also be impacted. *My concern is that the Company's speculation regarding the accelerated timeline is unsupported by facts. Irrespective of who (Xcel, Xcel's vendors, or the NRC) may cause the actual Monticello EPU timeframe to become fully operational at a time later than Xcel now hopes, the fact remains that hope and conjecture are not substitutes for facts upon which reasoned decision-making is based.* The record does not include facts from which it is reasonable to conclude that Xcel's accelerated timeframe is likely.

216. In his Surrebuttal Testimony, Mr. O'Connor confirmed further delays. He testified that NRC has completed its initial review of Xcel's first data collection, but that NRC has not issued its approval. Rather, NCR asked for a new data comparison, and the new data comparison identified two outliers in the data set. Mr. O'Connor stated that Xcel is evaluating the outliers to determine if they are errors or if they need further investigation. He acknowledged that NRC's further inquiry "will push back our schedule," without providing an estimated date of resolution or an estimated date for resumption of NRC's power ascension testing protocol.[28]

217. At the evidentiary hearing, Mr. O'Connor verified that the Monticello plant currently is operating at the pre-EPU level of approximately 600 MWe, and that the plant has not operated above pre-EPU levels since the testing in March 2014. He remained confident that Xcel will complete power ascension testing, with NRC approval, by the end of 2014, but offered no assurance by NRC for his expectation. Mr. O'Connor explained that Xcel recently contacted "a couple of" unnamed utilities "over the last couple of weeks" that Xcel believes went through a similar process with NRC. He said that the utilities told Xcel that it took them about three to four months to reach full EPU operating levels. Based on this information and "given where we are," Xcel continues to believe that it will complete its power ascension testing protocol by the end 2014. [29]

---

[28] Xcel Ex. 55 at 4-5 (O'Connor Surrebuttal).

[29] Tr.V. 1 at 231-232, 235, 239 (O'Connor).

218. Xcel has not provided facts from which a reasonable conclusion may be drawn that the Company is likely to complete power ascension testing of the EPU to a total operating level of 671 MWe, with NRC final approval, by the end of 2014. The NRC and Xcel are still reviewing information concerning the first data collection and, according to Xcel there are two additional data collection power levels (98 percent and 100 percent) whereby Xcel must collect data, send that data to the NRC and the NRC must then review the data and approve.[30] Xcel has not shown that its predicted schedule of end of 2014 for operation of the EPU at its intended and approved level of 71 MW is reasonable given the delays that already have occurred and, that create doubt in the reasonableness of Xcel's predictions going forward. While Xcel expressed optimism that EPU power ascension testing and NRC approval could be completed by the end of December, 2014, Mr. O'Connor acknowledged that there is no guarantee or timeline by which the NRC will complete its review or approval.[31]

219. The Department is hopeful that Xcel will be able to address the NRC's concerns successfully, but is concerned that the NRC may find additional problems with data Xcel has submitted (or with new data not yet submitted) that may lead to identification of other problems as Xcel resumes power ascension testing. As Ms. Campbell summarized in her Surrebuttal Testimony, although the Department does not doubt that Xcel now has obtained a 20-year license to operate the EPU:

> Clearly, however, the Company is having trouble getting final sign off from the NRC during testing and review as it relates to the uprate ascension process of the Monticello EPU 71 MW. As a result, the Monticello EPU has not satisfied NRC's testing protocol and has not yet reached the 71 MW level and the EPU is not available for customer use.

Even when the Monticello EPU is used and useful, ratepayers will not receive the full benefit of the NRC license life of 20 years. That is, if the in-service date for the Monticello EPU doesn't occur until January 2015, then the remaining useful life will be reduced to a period of 15.8 years that this plant will be able to serve ratepayers, which is clearly a significant reduction to ratepayers of 21 percent of actual benefits of the EPU uprate of 71 MW.[32]

220. For these reasons, the Department concluded that the record does not support Xcel's argument that by the end of 2014, the Monticello EPU will operate successfully at its 71 MW design capacity, for a total plant capacity of 671 MWe, and that the NRC will have approved that it do so. The EPU, therefore, is not used and useful to ratepayers and has not been shown by Xcel as likely to be used and useful by the end of the 2014 Test Year. Therefore, ratepayers must not be required to pay the costs of the EPU in rates that are set based on the 2014 test year. The ALJ agrees that the Department's recommendation is reasonable.

30

31 DOC Ex. 435 at 51-53 (Campbell Public Surrebuttal); Xcel Ex. 55 at 4 (O'Connor Surrebuttal); Tr.V. 1 at 232-33, 243-44 (O'Connor).

32 DOC Ex. 435 at 47, 51 (Campbell Public Surrebuttal).

4. For accounting purposes, not ratemaking purposes, the Department does not oppose Xcel booking the EPU as "in service" in 2014

221. The Department does not oppose Xcel's proposed accounting treatment of the Monticello EPU as "in service" in 2014, but continues to conclude that the EPU is not used and useful for ratemaking purposes. Accounting and ratemaking serve different purposes and operate under different standards. Xcel witness Ms. Perkett testified that from an accounting perspective, the Monticello plant is not required to operate at the 671 MW level in order for the NRC license to be "in service." Apparently, for accounting not ratemaking purposes, a typical requirement for generation units is that they must operate for 24 hours of continuous operation before they may be booked as being "in service." Ms. Campbell summarized her conclusion that, for accounting but not ratemaking purposes, the Department does not oppose Xcel's proposed accounting of the EPU, as follows:[33]

> [F]or accounting purposes, I generally agree that the Monticello EPU may be considered to be in-service even though one could argue that it has not operated for 24 hours of continuous operation at the CN-approved level of 671 MWe. However, again, accounting standards are not ratemaking standards, and I do not oppose Xcel's accounting. Clearly, however, the Monticello EPU has not met the used and useful standard for purposes of recovery of the facility from ratepayers, as I have discussed.

222. For these reasons, and limited to accounting purposes, the Department did not oppose Xcel's proposed accounting of the EPU as being "in service" in 2014.

223. The ALJ finds that Xcel's proposed accounting of the EPU as being "in service" in 2014 is reasonable, but only for accounting purposes.

5. Neither Xcel nor MCC has demonstrated the reasonableness of allowing 2014 and 2015 EPU costs, but deferring recovery of the 2014 EPU costs to 2015

224. It is not surprising that Xcel now agrees with MCC's proposed rate treatment of the 2014 Monticello EPU costs in that this Xcel/MCC proposal allows Xcel rate base treatment for 2014 EPU costs (no adjustment to Xcel's 2014 and 2015 rate base proposals), but defers (not disallows) 2014 EPU depreciation expense as well as higher fuel costs and replacement power costs related to the 2014 Monticello EPU not being in service by amortizing those costs over the remaining life of the plant.[34]

---

[33] Xcel Ex. 94 at 45 (Perkett Rebuttal); DOC Ex. 435 at 53-55 (Campbell Public Surrebuttal).

[34] Xcel Ex. 140 at 3 (Heuer Opening); Xcel Ex. 90 at AEH-2 (Heuer Rebuttal); Tr.V. 3 at 180-181 (Schedin).

225. The Department opposes the Xcel/MCC proposal for several reasons. First, Xcel has not shown the EPU to be used and useful in 2014, and therefore it is unreasonable to impose on ratepayers 2014-related EPU costs including rate base treatment.

226. Second, neither Xcel nor MCC has shown that deferral of costs to periods outside of the present 2014 Test Year is reasonable. The Commission articulated the legal standard for the extraordinary procedure of cost deferral which requires that the costs be unusual, unforeseeable and large enough to have a significant effect on the Company's financial condition, as follows:[35]

> Deferred accounting is a valuable regulatory tool used primarily to hold utilities harmless when they incur out-of-test year expenses that, because of their nature or size, should be eligible for possible rate recovery as a matter of public policy. Traditionally, deferred accounting has been reserved for costs that are unusual, unforeseeable and large enough to have a significant impact on the utility's financial condition. Deferred accounting has also sometimes been permitted when utilities have incurred sizeable expenses to meet important public policy mandates, such as the farm tap inspection program required by the Commission.

The Commission's deferral criteria have not been met in this case since, as a practical matter, it is not unusual or unforeseeable for a utility to incur higher fuel and replacement power costs when a generation plant like the Monticello EPU is not in service.

227. Finally, the Xcel/MCC proposal is unsupported by the facts of this case because it is backwards and, for that reason, is not reasonable.[36] The proposal would allow recovery of 2014 EPU costs from ratepayers, with a return, even though ratepayers are not receiving a benefit from the EPU, while it would defer the costs of fuel and replacement power that ratepayers are using and from which they are receiving a benefit.

228. In contrast, the Department's recommendation makes sense and is grounded in fact: it would deny recovery of EPU-related costs (including any rate base return for 2014), and it would allow the higher fuel costs and the replacement power costs to be recovered in 2014 from ratepayers, who are benefitting by making no adjustment to Xcel's proposed recovery of fuel costs or replacement power costs for 2014.

229. Xcel and MCC have not shown the reasonableness of their proposal and its acceptance is not recommended.

---

[35] December 18, 2009, Order at 3-4, MPUC Docket No. E001/M-09-336. *See also* July 16, 2012, Order Denying Petition at 4-5, MPUC Docket No. E-002/M-11-1263 (denial for lack of "extraordinary" showing).

[36] *See* Tr.V. 3 at 185-186 (Schedin) (no analysis of why the Xcel/MCC proposal is reasonable).

6. XLI's position for partial 2014 recovery of EPU cost should be denied.

230. The Department continues to oppose XLI's position that 1) a 13-month average be used, rather than the historical BOY/EOY balances, and that 2) the Commission should allow 1/12 of EPU costs in the 2014 Test Year. Xcel failed to demonstrate that the EPU is used and useful at its intended and designed capacity of 71 MW, or that it is likely to be used and useful by the end of the 2014.

231. Thus, there is no reasonable basis to allow any EPU-related costs in rates for 2014.

7. Department Recommendation

232. For the reasons discussed above, the Department makes the following recommendation:[37]

a. For 2014, the Department continues to recommend that the 2014 depreciation expense and return on the Monticello EPU be excluded from the 2014 test year, resulting in a $31.284 million revenue requirement reduction.

b. For 2015, *if the Monticello EPU is in-service* by the beginning of the year, January of 2015, DOC recommends rate base treatment and recovery of associated depreciation costs for the 2015 Test Year, as shown in Attachment A, column (d) of the Company's response to Department information request no. 2148.

c. For 2015, *if by January of 2015 the Monticello EPU is not in service*, DOC supports application of the terms of the Multi-Year Rate Plan (MYRP) agreement between Xcel and DOC addressed by DOC Witness Lusti (Issue 35), such that Department would support requiring Xcel to refund any amounts collected in rates through the refund mechanism for the MYRP.

233. As Mr. Lusti showed in his Surrebuttal Testimony, the DOC's recommendation decreased the test-year rate base by $164,824,000 as detailed in DOC Ex. 438 DVL-11 (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-EH-4, column (h) (Lusti Opening Statement; and decreased the test-year depreciation expense by $12,577,000, as detailed in DOC

[37] DOC Ex. 450 at 3 (Campbell Opening).

Ex. 438 DVL-11 (Lusti Direct Attachments) and as shown in DOC Ex. 451 DVL-EH-7, column (o) (Lusti Opening Statement).

234. The ALJ finds that the Department's recommendations are reasonable.

I. Prairie Island Site Administrative Building for 2014 and 2015 (Issue 29)

Resolved between Xcel and the Department: DOC agrees that Xcel provided adequate support in response to DOC discovery for its December, 2014 in-service date and to justify the reasonableness of those capital costs that exceeded the amount Xcel had competitively bid.

235. In Direct Testimony, Ms. Campbell concluded that Xcel had not provided sufficient information to demonstrate that it is likely that Xcel employees would begin using the Prairie Island Site Administration Building (PI Building) before the end of 2014, and also had failed to demonstrate the reasonableness of the amount of capital costs that exceeded Xcel's winning competitive bid for the project. In response to Department discovery, Xcel witness Mr. O'Connor provided a detailed breakout of the total $22.6 million in costs for the PI Building including reasonable explanation for each cost. Further, in his Rebuttal Testimony, Mr. O'Connor demonstrated the likelihood that the PI Building will be complete by December 2014, and that Xcel plans to move staff to the facility beginning in December 2014 with completion of the staff transfer by March 2015.[38]

236. The Department's agreement with Xcel that the PI Building is likely to be in-service and, thus, be used and useful, by the end of December 2014, is based on the Company's showing that it is likely to actually be used in 2014. Ms. Campbell did not agree with Ms. Perkett that bookkeeping entries determine in-service dates for ratemaking purposes.[39]

237. Ms. Campbell noted in her Surrebuttal Testimony at page 20 that she no longer recommends a test-year adjustment for the PI Building. Thus, there is no adjustment to the levels Xcel proposed to recover. DOC Ex. 442 at 10 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-4, column (i) and DVL-EH-7, column (q) (Lusti Opening Statement).

238. The ALJ agrees that Xcel provided adequate support in response to Department discovery for its December, 2014 in-service date to justify the reasonableness of those capital costs that exceeded the amount Xcel had competitively bid.

[38] DOC Ex. 429 at 18, 154-156 (Campbell Public Direct); DOC Ex. 435 at 18-19 (Campbell Public Surrebuttal).
[39] DOC Ex. 435 at 19-20 (Campbell Public Surrebuttal).

J. Non-Qualified Pension (Issue 20)

Resolved between Xcel and the Department: Xcel accepts DOC's recommended removal of non-qualified pension expense and capital for an overall decrease of $704,000 to the test year revenue requirements.[40]

239. Non-qualified pension reflects a benefit that exceeds the Internal Revenue Service (IRS) limits for pension/compensation tax treatment. As a practical matter, Xcel's "Restoration" non-qualified pension plan is available only to highly paid executive employees – those making over $255,000 per year. Xcel has two non-qualified pension plans, but sought recovery from ratepayers only for the Restoration plan. As Ms. Campbell testified, Xcel did not show that it is reasonable to require ratepayers to provide what tax law does not provide:

> Since the non-qualified pension costs are basically tax payments to the Company for highly compensated individuals who exceed IRS thresholds ($255,000 per year) I consider the cost of this benefit to be excessive to charge to ratepayers. That is, I do not consider it reasonable for ratepayers to pay for these non-qualified pension or restorations costs. If the Company wants to provide supplemental or non-qualified pension costs to highly paid employees, then shareholders should pay these costs.[41]

240. In her Rebuttal Testimony, Ms. Heuer noted Xcel's acceptance of the Department's recommendation for this issue, and the resulting adjustment for non-qualified pension of a decrease to the 2014 test year revenue requirements.[42] Mr. Lusti summarized the test-year income statement effect. The DOC's recommendation decreased the test-year administrative and general expense by $702,494, as shown in DOC Ex. 451 at DVL-EH-7, column (u) (Lusti Opening Statement); DOC Ex. 442 at 10-11 (Lusti Surrebuttal).[43]

241. The ALJ finds the Department's recommendation to decrease the test-year administrative and general expense for non-qualified pension by $702,494 to be reasonable.

K. Qualified Pension: 2014 Test Year (Issue 4 and Issue 5)

Disputed between Xcel and the Department: The discount rate assumption for the XES Pension Plan, and Xcel's requested 2008 Market Loss adjustment remain disputed as to 2014 Test Year pension expense:

---

[40] DOC Ex. 450 at 1 (Campbell Opening); Xcel Ex. 88 at 21 and Schedule 11 (Heuer Direct).
[41] DOC Ex. 429 at 136-137 (Campbell Public Direct).
[42] The correct amount is $702,494 as shown on Xcel Ex. 88 at Schedule 11 page 1 of 4 (Heuer Direct). Ms. Heuer's Rebuttal at page 21 incorrectly states the amount as $704,000.
[43] DOC Ex. 450 at 1 (Campbell Opening); Xcel Ex. 88 at 21 and Schedule 11 (Heuer Direct).

1) Discount rate: DOC recommends that the discount rate assumption for the XES Plan be increased from Xcel's proposed 4.74 percent to 7.25 percent in order that the discount rate and expected return on assets (EROA) assumptions are equal; and

2) 2008 Market Loss: DOC recommends that Xcel be allowed to recover 50 percent, not 100 percent, of the $12.1 million in 2008 Market Loss, or $6,032,000.[44]

If the Commission does not agree with DOC's pension recommendation, DOC's alternative positions are noted in this Initial Brief.

Resolved between Xcel and the Department: The Department agrees with:

1) Xcel's proposed measurement date assumption of December 31, 2013, for calculating the pension asset for purposes of the test year pension expense calculation;[45]

2) Xcel's use of 7.25 percent for the expected return on assets (EROA) assumption for the NSPM Pension Plan and the XES Pension Plan;

3) Xcel's use of the same rate for both the discount rate and the EROA assumption of 7.25 percent for the NSPM Pension Plan; and

4) Xcel's wage increase assumption rate of 3.75 percent.[46]

5) Xcel agreed to DOC's recommendation that Company file in its next rate case its investment strategies, target asset allocations and justifications for those decisions from 2007 to the date of their next rate case filing.[47]

1. Disputed Issue: level of discount rate for ratemaking purposes

242. The purpose of establishing a reasonable amount of pension expense for the test year is to ensure, for ratemaking purposes, that rates are just and reasonable. Key to creating reasonable rates is to use reasonable assumptions for calculating the estimated test year pension expense. To examine Xcel's proposed pension assumptions it is important to keep in mind that a lower assumed discount rate assumption for one of the two Xcel pension plans results in higher calculated pension expense for rates.[48]

243. While it does not object to ratepayers paying for reasonable employee benefits such as pensions, the Department objects strenuously to the use of inappropriate assumptions about estimated pension costs that result in unreasonable assumptions for purposes of setting

---

[44] *See* DOC Ex. 450 at 4-7 (Campbell Opening).
[45] *Id.* at 5; DOC Ex. 435 at 88 (Campbell Public Surrebuttal).
[46] *Id.* at 75.
[47] Xcel Ex. 116 at 2 (Tyson Opening); DOC Ex. 435 at 89 (Campbell Public Surrebuttal).
[48] DOC Ex. 450 at 4 (Campbell Opening); DOC Ex. 429 at 99, 116-117 (Campbell Public Direct).

rates. It is particularly important to ensure that pension assumptions are reasonable since it is clear that the Company, not the actuary (Towers Watson), selected the pension assumptions. Thus, Xcel must show that the assumptions it used to estimate test-year pension costs are reasonable. Doing so ensures that the amount that ratepayers pay *now* in rates for *future* employee pension benefits are reasonable. Any doubt as to the reasonableness of Xcel's assumptions for ratemaking purposes must go to the ratepayer.[49]

a. Ratemaking serves different goals under different requirements than does accounting or funding requirements, although the Commission may be guided by accounting or funding requirements among other factors

244. The Commission's ratemaking responsibilities differ from the Company's accounting responsibilities. Ratemaking may, conceivably, differ from the Company's funding requirements, just as ratemaking includes recovery of income taxes even when the utility is not paying any such taxes as discussed below. However, in fact the Department's recommended level of pension costs is consistent with its funding requirements whereas Xcel's proposal is higher than its funding requirements. Given that Xcel insists for ratemaking that a particular accounting reporting (not funding) standard, Financial Accounting Standard (FAS or SFAS) 87, be used to establish the discount rate assumption for the XES Pension Plan, Department witness Ms. Campbell highlighted basic differences between the Commission's ratemaking function and Xcel's accounting requirements, as follows:[50]

> The Commission's ratemaking function of establishing a reasonable level of pension expense in rates differs in important ways from the utility's accounting or bookkeeping function. As a result, these two functions are governed by different requirements. For example, Minnesota Statutes § 216B.03, cited above, requires that rate[s] must be reasonable. As such, the level of expense in rates must reflect the likely and reasonable expense going forward until the Company's next rate case. By contrast, a utility's bookkeeping function reflects financial circumstances at a point in time, based on requirements for financial reporting, which is then updated on a monthly, quarterly and/or annual basis.

---

[49] *Id.* at 99, 112-119. The Department's discovery and analysis attempted to verify the reasonableness of Xcel's proposed discount rate assumptions for ratemaking purposes. As Ms. Campbell's testimony provides at length, Xcel did not demonstrate its very low proposed discount rate assumption for its XES Pension Plan of 4.74 percent is reasonable, although the Department confirmed the reasonableness of Xcel's other proposed assumptions including the discount rate assumption for its NSPM Pension Plan. Tr.V. 5 at 40-43, 56-57 (Campbell); DOC Ex. 435 at 79-85 (Campbell Public Surrebuttal); *See* Minn. Stat. § 216B.03 (2014).

[50] DOC Ex. 450 at 4 (Campbell Opening); DOC Ex. 429 at 100, 103-104 (Campbell Public Direct); DOC Ex. 430 at NAC-19, page 12 (Campbell Public Direct Attachments).

Pension Fundamentals

245. To assist the Commission with this complex pension topic, Ms. Campbell attached to her Direct Testimony a short twelve-page document from 2004 called, "Fundamentals of Current Pension Funding and Accounting for Private Sector Pension Plans" (Pension Fundamentals) by the American Academy of Actuaries.[51] As Ms. Campbell explained, Pension Fundamentals points out that, *for reporting purposes*, the focus is on ensuring that pension obligations are not understated:[52]

> [Pension Fundamentals] points out that actuaries and outside auditors are more concerned with a Company *understating its pension expense* rather than the statutory requirement in this rate case of ensuring that the Company has not *overstated its pension expense* significantly for the test-year. This difference highlights a material distinction between accounting/bookkeeping and ratemaking.

246. Pension Fundamentals also points out that, *for funding purposes* under the Employee Retirement Income Security Act (ERISA), the interest rate used to discount future benefits to today's dollars is based on the "expected future rate of return on pension assets"; that is, the EROA. Thus, adoption of a test-year discount rate assumption equal to the EROA assumption as the Department recommends for the XES Plan is fully consistent with Xcel's funding obligations under ERISA. The fact that pension funding requirements use the same longer timeframe to determine both the a discount rate and EROA assumptions, as does the ACM method of accounting for the NSPM Plan, confirms as reasonable the Department's recommendation for the XES Plan discount rate analysis for ratemaking. Thus the Department supports setting the discount rate assumption equal to the EROA assumption for the XES Plan, for ratemaking purposes, similar to pension funding requirements as well as the method ACM accounting method for the NSPM Plan.[53]

247. By contrast, Xcel's proposal to use a lower discount rate, resulting in higher current pension costs charged to ratepayers for the XES plan, is not reasonable. Ms. Campbell

---

[51] DOC Ex. 429 at 100 (Campbell Public Direct) and DOC Ex. 430 at NAC-19 (Campbell Public Direct Attachments) (Pension Fundamentals).

[52] DOC Ex. 429 at 100 (Campbell Public Direct) (emphasis in italics added).

[53] DOC Ex. 430 at NAC-19, page 12 (Campbell Public Direct Attachments) (Pension Fundamentals); DOC Ex. 435 at 83-84 (Campbell Public Surrebuttal). There is no dispute in this case with Xcel's setting of the discount rate assumption for Xcel's NSPM Plan equal to the EROA assumption of 7.25 percent. Xcel applied the Aggregated Cost Method (ACM) of accounting for its rate case discount rate assumption for the NSPM Plan. The ACM method uses the same timeframe for the discount rate assumption and for the EROA assumption: for the discount rate it discounts the pension obligation from the future to the present, and for the EROA it extrapolates the expected return on the pension asset from the present to the future. Tr.V. 5 at 41 (Campbell); DOC Ex. 450 at 5-6 (Campbell Opening).

gave an example of how accounting for financial purposes under FAS 87 is a different function from setting rates for ratemaking purposes in this proceeding, in part as follows:[54]

> For accounting [reporting] purposes, FAS 87 allows the expected return on pension assets and the discount rate for future pension payments to be set differently. The goal of this requirement is to try to capture effects of extreme market changes, especially since some companies in the 2008 time period came close to being bankrupt and as a result would have had to pay out their pension plan obligation at the current level at a point in time.

Use of FAS 87 as a method of determining the discount rate for ratemaking purposes could be warranted if regulated utility showed that it was at imminent risk of bankruptcy such that it would need to immediately cash out or "settle" its pension obligation, but such a circumstance has not been demonstrated in this case. In fact, as Ms. Campbell explained, a rate regulated utility would not be expected to have to cash out their pension plan obligations:[55]

> [O]ne of the overlooked benefits of rate regulation is that the financial performance of Minnesota utilities is carefully monitored. It is rare for utilities to encounter financial difficulties; further, the Commission becomes involved swiftly to resolve such matters. For example, when Xcel experienced financial upheaval due to problems with one of its former affiliates and an inappropriate imposition of the risks with this affiliate on the utility, the Commission and Xcel acted swiftly to address those issues (Docket No. E,G002/CI-02-1346). Xcel (the utility) recovered quickly and has been performing well ever since. The oversight over Minnesota utilities sets far higher expectations regarding financial accountability than is the case for most companies in the United States.
>
> Second, utility services are a fundamental need in Minnesota and elsewhere. As such, there is an ongoing demand for the services and careful consideration of their financial needs in ratemaking.

There are no facts present in this rate case record to support a suggestion or conclusion that Xcel is in a precarious financial situation.[56]

---

[54] DOC Ex. 429 at 101 (Campbell Public Direct).

[55] Xcel witness Mr. Schrubbe testified that that Xcel's discount rate assumption for the XES Plan is "consistent" with both ways of determining pension expense under FAS 87: near-term "settling" of the future pension obligation through use of annuity contracts or use of high quality fixed income investments. Xcel Ex. 83 at 43 (Schrubbe Rebuttal); DOC Ex. 429 at 101-102 (Campbell Public Direct).

[56] *Id.* at 101-102.

248. The Commission must focus on ratemaking principles in setting pension expense for the 2014 test year. In light of Xcel's claim that the discount rate assumption for the XES Plan must be set in accordance with FAS 87 which is a short-term, point-in-time measure, the ALJ agrees that the Department's showing is significant that other accounting methods, like ACM, as well as pension *funding* requirements under ERISA, better meet the ratemaking goals of being reasonable and in the public interest while still supporting a financially viable utility "in the long-run."[57]

b. Use of the term "actual cost" in the context of pension expense can be misleading

249. The Department urged caution with respect to accepting the term "actual costs" or "actual pension expense" in the context of pension expense for ratemaking purposes. "Actual" pension expense for accounting purposes is based on assumptions used to calculate a figure that is entered on the Company's books for reporting purposes. Actual pension expense for ratemaking purposes does not represent a tangible expenditure that is incurred during a test year such as an expense item like Paid Leave.[58]

250. Pension expense determined in a rate case can be and often is different from pension expense determined for other financial reporting purposes such as financial accounting. In fact, the Company calculates its pension expense (and pension assumptions) for bookkeeping purposes on a monthly, quarterly and/or annual basis[59] in contrast to the Commission's determination only in a rate case of test-year pension expense. The Commission's test-year pension expense amount remains as a rate component for several years or until the utility files its next rate case and a new test-year pension expense is determined by the Commission).[60]

---

[57] DOC Ex. 429 at 103-104 (Campbell Public Direct).

[58] DOC Ex. 429 at 109 (Campbell Public Direct). Even when a utility does show that it "actually" incurred a particular expense in the test year, that fact may be insufficient for ratemaking purposes. The Minnesota Supreme Court held that, "[B]y merely showing that it has incurred, or may hypothetically incur, expenses, the utility does not necessarily meet its burden of demonstrating that it is just and reasonable that the ratepayers bear the costs of those expenses." *In the Matter of N. States Power Co.*, 416 N.W.2d 719 at 723 (Minn.1987).

[59] *Id.* In its 2013 Rate Case Order, the Commission adopted as ALJ's recommended discount rate assumption for the XES Pension Plan of 7.50 percent. *See* ALJ Report at 34 para. 164, Docket No. E002/GR-12-961. DOC Ex. 429 at 100 (Campbell Public Direct).

[60] Note the limited relevance of certain "actual" numbers in Table 6 on page 44 of Mr. Schrubbe's Rebuttal. Xcel identified in Table 6 its "actual" annual selection, under FAS 87 (per Tr.V. 5 at 67-68 (Campbell) of the discount rate assumption that it *recorded on its books* for the XES Plan for years 2010 – 2013. The Company, however, did not include the higher discount rate assumptions it actually recorded on its books for the NSPM Plan under the ACM accounting method. Xcel did not include the "actual" discount rate assumptions used by Xcel for pension funding during those same years. Xcel did not include the "actual" discount rate assumption determined by the Commission for ratemaking purposes for the XES Plan for 2013. The Department does not challenge Xcel's claim that the Company actually recorded on its (Footnote Continued on Next Page)

c. The Commission's estimate of test-year pension expense in this rate case will not change Xcel's funding requirements or the amount of pension payments Xcel makes to its employees

251. Whatever the Commission determines in this rate case to be a reasonable estimate of test-year pension expense until Xcel's next rate case, it is clear that the Commission's rate decision will not change Xcel's pension funding requirements or the amount of pension payments to Xcel's employees. Pension funding requirements are determined by ERISA, and pension payments to employees are governed by Xcel's contracts with its employees. Thus, even if the Commission were to use a lower discount rate for ratemaking purposes than required by ERISA for funding purposes, Xcel would not be required to contribute any more money to its pension account.[61]

d. Pension expense is not the only cost component that may be treated differently for ratemaking purposes than for other financial purposes

252. Pension expense is not the only cost component that may be treated differently for ratemaking purposes than for other financial purposes. For example, the Commission imputes recovery of income taxes for purposes of setting rates when in some cases utilities have not paid those tax amounts for many years due to factors such as differences in depreciation assumptions for financial purpose. Nonetheless, it is important for income taxes (and depreciation) used in setting rates to reflect reasonable assumptions based on Minnesota statutes, rules, policies and Commission precedent.[62]

253. The Department does not oppose Xcel's request that the Commission consider the Monticello EPU to be "in service" for financial accounting purposes even though, for ratemaking purposes, the Department urges the Commission to determine that Xcel has not demonstrated for 2014 that the EPU is likely to be in-service (used and useful) to ratepayers.

e. DOC recommendation as to the XES discount rate assumption consistent with the ALJ's recommendation and Commission's Decision in Xcel's prior rate case[63]

254. In its 2013 Xcel Rate Case Order at 7, the Commission held, "The Administrative Law Judge found that the Company's future wage projections were reasonable but that the

(Footnote Continued from Previous Page)
books for the XES Plan, for accounting purposes, the discount rate assumptions noted in Table 6 as to years 2010-2013.

[61] DOC Ex. 429 at 102-103 (Campbell Public Direct).

[62] *Id.* at 103-104.

[63] DOC Ex. 450 at 5 (Campbell Opening); DOC Ex. 429 at 117-118, 171-172 (Campbell Public Direct).

challenged discount rate and earnings projections were neither adequately supported nor adequately correlated." The ALJ's proposed Findings on this issue stated in relevant part, as follows:[64]

> 161. The Company also updated the SFAS 87 Discount Rate from 5.0 percent to 4.03 percent.[FN 171] The Discount Rate has an inverse relationship to pension cost, meaning that the lower the discount rate, the higher the pension cost.[FN 172] The Company did not provide an explanation for the lowering of the discount rate other than to simply state that the Discount Rate was updated as of December 31, 2012.[FN 173]
>
> 162. The Department objected to the Company's proposed SFAS 87 Discount Rate, both as originally proposed and the rebuttal proposal. The Department maintained that the SFAS 87 Discount Rate should match the EROA rate, which is higher. *The Department noted that the Discount Rate and the EROA rate used by the Company to calculate the NSPM pension expense are the same (7.5% in Direct Testimony). The Department asserted that the Company should also match the SFAS 87 Discount Rate to the EROA for the XES plan. The Department maintained that this approach ensures that the discount rate, which is used to measure the time value of money, is consistent with the level of expected return on assets.* According to the Department, if the two do not match, then the pension obligation will be overstated and unnecessarily increase the liability to be addressed. The Department estimated that increasing the SFAS 87 Discount Rate used for the XES Plan from 5 percent to 7.5 percent (the EROA amount) would result in an $870,450 reduction to the pension expense.[FN 174]
>
> 163. *The Company countered that if the Department's recommendation on the SFAS 87 Discount Rate were adopted for the XES Plan, it would lead to permanent under recovery of costs by the Company because there are significant differences between the accounting method used for the XES plan and the accounting method used for the NSPM plan. The Company did not explain in any detail why the differences in accounting methods would lead to an under recovery of costs.*[FN 175]
>
> 164. The Administrative Law Judge concludes that the Department's recommendation to use a 7.5 percent Discount Rate

---

[64] Findings of Fact, Conclusions of Law and Recommendations at 33-34, MPUC Docket No. E002/GR-12-961) (July 3, 2013) (2013 ALJ Report) (Citation omitted, emphasis in italics added).

for the XES plan is reasonable. This approach is consistent with the approach used by the Company for the NSPM plan and appropriately matches the discount rate to the EROA. *The Company has not adequately explained why a different Discount Rate should be used for the XES Plan for ratemaking purposes.* Accordingly, the Administrative Law Judge recommends that the Discount Rate for the XES Plan be set at 7.5 percent, the same level as is recommended for the EROA rate.

f. Use of an average discount rate determined under FAS 87 would not be reasonable for ratemaking

255. In his Rebuttal Testimony, Mr. Schrubbe noted that the Commission in the recent CenterPoint rate case, G-008/GR-13-316, chose not to adopt the ALJ recommendation of using the same discount rate assumption as the EROA, but instead adopted a discount rate assumption based on an average. The Department does not support using an average to set the discount rate assumption for the XES Plan ratemaking purposes. First, any average discount rate must not be based on discount rates determined under FAS 87, since the Department has demonstrated that FAS 87 discount rate assumptions are inherently short-term and too low for ratemaking purposes because the premise underlying FAS 87 is that the Xcel is in imminent threat of bankruptcy such that it must immediately "settle" its future pension obligation. No evidence exists in the current rate case record to support a conclusion that Xcel is about to go bankrupt. Thus, calculating an average of unreasonably low discount rates would result in an unreasonably low discount rate.[65]

256. Second, Ms. Campbell explained on cross-examination that a Commission policy of using an average of FAS 87 discount rates may invite unreasonable utility manipulation to the disadvantage of the ratepayer. Specifically, she noted that Xcel, in its most recent rate case, attempted to lower one of its self-selected pension assumptions very late in the proceeding with no explanation other than it was "updated," and then proposed a three-average of discount rates under FAS 87 which, not surprisingly, resulted in a very small adjustment to the Company's proposed discount rate. In her Surrebuttal Testimony on page 52-53 in the prior rate case, Ms. Campbell raised concerns with the Company manipulating its test-year pension expense by adjusting its own assumptions.[66]

257. Third, the Pension Fundamentals document included in this proceeding shows that for purposes of funding under ERISA the discount rate and the EROA are the same, which reaffirms the Department recommendation that the discount rate and EROA should be the same in determining pension expense charges to ratepayers.[67]

258. Finally, as noted above, the fact that Xcel selects its own discount rate assumption for the XES Plan makes it all the more important that Xcel prove the reasonableness of its use for ratemaking purposes, which Xcel has not done in this case. Using an average of similarly

[65] Xcel Ex. 83 at 42 (Schrubbe Rebuttal).
[66] DOC Ex. 450 at 5-6 (Campbell Opening); DOC Ex. 435 at 83 (Campbell Public Surrebuttal).
[67] DOC Ex. 435 at 84 (Campbell Public Surrebuttal).

unreasonably low discount rate assumptions should not be used inflate rates without Xcel's satisfaction of its burden of proof in this matter.

259. For these reasons, the record in this rate case does not support for ratemaking purposes the use of an average of Xcel's self-selected FAS 87- determined discount rate assumptions.

g. DOC recommendation as to the XES discount rate assumption

260. Xcel has failed to show, for ratemaking purposes, the reasonableness of its very low discount rate assumption for the XES Pension Plan of 4.74 percent. In contrast, the Department demonstrated the reasonableness of its proposal to use a discount rate assumption of 7.25 percent which, like the ERISA pension funding requirements and the ACM accounting method, is based on using the *same* rate as the reasonable EROA assumption. The Department also notes that this adjustment to set the discount rate and EROA are equal for the XES fund, since they both apply to the same time period, is consistent with the ALJ's proposed finding and the Commission's Order in Xcel previous rate case, Docket No. E002/GR-12-961.[68]

h. DOC recommendation as to the NSPM discount rate assumption

261. The discount rate Xcel selected for its NSPM Pension Plan of 7.25 percent is reasonable. The NSPM Plan the discount rate is reasonable because it relies on a longer-term prospective and it is equal to the 7.25 percent expected return on assets assumption for the NSPM Plan, which the Department confirmed was reasonable (using the same time period to select both assumptions results in the same rates for both assumptions). Thus, for ratemaking purposes it makes sense to use for the XES Plan the discount rate assumption that is the same rate—7.25 percent—as the expected return on the pension assets for the XES Plan.[69]

2. Disputed Issue: Xcel's 2008 Market Loss request

262. Regarding the other disputed pension issue, Xcel's proposed 100 percent recovery of its 2008 Market Loss, Xcel did not show that it is reasonable to impose on ratepayers, in 2014, 100 percent of this extreme amount of $12.1 million for a 2008 market loss of $19.9 million in pension expense. Despite the financial market returning to levels above the pre-2008 market loss levels, Xcel's pension assets have not similarly recovered such that the Company has not shown that it is reasonable to recover so much of the 2008 market loss (over 60 percent of Xcel's proposed pension test-year expense) in this 2014 rate case. The Department questioned whether the magnitude of the loss that is proposed in this rate case suggests that Xcel may not have reasonably managed its pension asset (it "may have been overly optimistic about its equities

---

[68] DOC Ex. 435 at 78-85 (Campbell Public Surrebuttal).

[69] DOC Ex. 429 at 116 (Campbell Public Direct); Tr.V. 5 at 40-42 (Campbell); *see, e.g.*, Tr.V. 5 at 40-43, 56-57 (Campbell); DOC Ex. 429 at 116-119 (Campbell Public Direct); DOC Ex. 435 at 79-85 (Campbell Public Surrebuttal).

positions in the financial market prior to 2008 and later moved to a more conservative investment too soon, before the financial market had come back to current levels, resulting in the Company missing out on the upswing of the market.”). The Department does not take a position on Xcel’s pension asset mix, but is concerned that ratepayers in 2014 not bear more than a reasonable portion—50 percent—of Xcel’s 2008 Market Loss. [70]

a. The Department’s recommendation: 50 percent of the 2008 Market Loss

263. The Department has several concerns regarding Xcel’s proposed recovery of its 2008 market loss, but a principal concern is that the Company has included so much of the amount in its proposed 2014 test-year pension expense which is now 5 years beyond the 2008 loss period. Over 60 percent of Xcel’s initially proposed 2014 test-year expense of nearly $20 million, reflects its 2008 market loss of $12.1 million. Xcel requests recovery from ratepayers of 100 percent of this 2008 market loss; $8.5 million is from the NSPM Plan and $3.5 million is from the XES Plan.[71]

264. Ms. Campbell is concerned that Xcel did not show that it managed its pension assets reasonably given that Xcel is still asking ratepayers to pay $12 million in annual rates between now and its next rate case to reflect that market loss. In her Surrebuttal, she explained:

> I have concerns that the Company may have been overly optimistic about its equities positions in the financial market prior to 2008 and later moved to a more conservative investment too soon, before the financial market had come back to current levels, resulting in the Company missing out on the upswing of the market. Both of these investment choices seem to have caused higher-than-necessary 2008 market losses to be charged to ratepayers at this time. I recommend that the Company also address this concern in their compliance filing by addressing investment strategies and target asset allocations and justifications for those decisions from 2007 to the current date of their next rate case filing.

Given these concerns and as discussed below, the Department recommends that ratepayers be limited to paying 50 percent, or $6,032,000.[72]

---

[70] DOC Ex. 435 at 89, 92-94 (Campbell Public Surrebuttal); On cross-examination, Xcel witness Mr. Tyson acknowledged that Xcel’s pension asset portfolio at the 2013 measurement date of December 31, 2013, included 31 percent equities. Tr.V. 1 at 131 (Tyson); DOC Ex. 435 at 88 (Campbell Public Surrebuttal).

[71] Tr.V. 5 at 65 (Campbell); DOC Ex. 429 at 126 Campbell Public Direct); DOC Ex. 435 (Campbell Public Surrebuttal).

[72] Tr. V. 5 at 68 (Campbell); DOC Ex. 435 at 89-90, 95 (Campbell Public Surrebuttal).

265. In response to Department discovery, Xcel provided information showing that Xcel's pension assets and liabilities *will converge in the near future* (estimated to occur in 2017), that, at least for the 2014 test-year, Xcel will incur pension expense (difference between pension assets and pension benefit obligation), and the Company made contributions to the pension fund from the 2010 measurement date to the 2013 measurement date.[73]

266. Based on the information Xcel provided in discovery, the Department was persuaded that it is reasonable for some of the 2008 market loss – no more than 50 percent – to be included in 2014 rates.[74] The Department identified the following reasons for concluding that only half, rather than all, of the 2008 market loss may be recovered from ratepayers:[75]

- First, I don't agree that it is reasonable to impose on ratepayers 100 percent of this extreme amount of $12.1 million for a 2008 market loss of $19.9 million pension expense in 2014.

- Second, I continue to be concerned that, despite the financial market returning to levels above the pre-2008 market loss levels, and despite the Commission granting Xcel rate relief in its 2012 rate case for the 2008 market loss, Xcel is still proposing to charge its ratepayers so much of the 2008 market loss (over 60 percent) in the Company's proposed 2014 increase in pension expense.

- Third, I am also concerned that the Company may not have reasonably managed its pension assets, specifically by being overly optimistic about its equities positions in the financial market prior to 2008 and later moved to a more conservative investment too soon, before the financial market had time to come back to current levels such that the Company did not avoid the downswing and then missed the upswing of the market. Both of these investment choices seem to have caused higher-than-necessary 2008 market losses to be charged to ratepayers.

- Fourth, in several rate cases, including Minnesota Power, OtterTail Power and Xcel (Docket Nos. E015/GR-09-1151, E017/GR-10-239, and E002/GR-10-971) the Department has agreed that a reasonable level of retirement benefits are a legitimate cost of service, but noted that ratepayers have been paying for 100 percent of utilities' pension plan expenses since there is no contribution toward pensions on the part of the employees. The Department has not opposed Xcel's generosity to its employees but noted the

[73] DOC Ex. 430 at NAC-26 (Campbell Public Attachments); DOC Ex. 429 at 131-132 (Campbell Public Direct).
[74] DOC Ex. 429 at 131-134 (Campbell Public Direct).
[75] DOC Ex. 450 at 6 (Campbell Opening).

detriment to ratepayers of requiring that all of the costs be charged to ratepayers.

- Fifth, in Xcel's case, this issue of requiring ratepayers to pay for all pension expenses is especially troubling in light of the additional 401K plan where employees may voluntarily contribute up to 8 percent of their salary and Xcel would provide a 4 percent match, since ratepayers are also asked to pay this 4 percent 401K match on top of the pension expense. I provided a detail list and description of all of the employee benefit provided by Xcel and paid for by ratepayers on pages 104-107 of my Direct Testimony.

- Sixth, the Company indicated that it employed a symmetrical method of including both gains and losses in pension expense. I raised concerns with this claimed symmetry in the 12-961 Xcel rate case, in my Surrebuttal Testimony on page 60, where I noted that negative pension expense is not given back to customers, but instead is assumed to be $0 in rate cases when the pension expense is actually negative, and remains in the pension plan to offset future pension costs. Such an approach is consistent with the idea I recommend of recognizing that the 2008 market loss occurred but taking a longer perspective to allow the pension funds to recover. By contrast, in both the last rate case and this rate case, the Company is attempting to get recovery of all of the 2008 market loss from ratepayers in the short term.

- Seventh, I don't agree with the statement that neither shareholders nor the Company benefit by market gains exceeding expectations, because if the Company's pension plan is overfunded then the Company does not have to make payments into the pension fund. As just noted, Xcel does not refund to ratepayers gains that exceed expectations.

DOC Ex. 435 at 89-95 (Campbell Surrebuttal). The Department also noted that 100 percent recovery from ratepayers is unreasonable where the Company estimates that by 2017 to 2018, "pension assets will again exceed pension liability, resulting in pension expense going to $0."[76]

---

[76] DOC Ex. 429 at 133 (Campbell Public Direct); *but see* Xcel Ex. 83 at 25-27 (Schrubbe Rebuttal) (Xcel expects its pension expense to pension expense to be $13.7 million by 2019). Ms. Campbell also testified that the 2008 market loss should be normalized "which is the typical approach with rate case expenses to ensure that reasonable assumptions are used for ratemaking purposes, although she disagreed with Xcel's normalization approach which would rely on a tracker mechanism. DOC Ex. 429 at 133 (Campbell Public Direct).

267. In Surrebuttal Testimony, Ms. Campbell explained why Xcel's Rebuttal Testimony did not show that ratepayers should pay 100 percent of Xcel's 2008 market loss. DOC Ex. 435 at 90-95 (Campbell Public Surrebuttal). Mr. Schrubbe identified the following reasons why the Company believes it is necessary to include all of the 2008 market loss in the calculation of qualified pension expense:

> 1. Retirement benefits are a legitimate cost of service, and it is reasonable to recover from customers either the costs of our qualified pension or a reasonable alternative to it.
>
> 2. The Company's symmetrical method of including the prior years' experience of both gains and losses is necessary to determine an accurate level of pension expense.
>
> 3. The consistent use of this prior years' experience in determining current year pension costs has provided customers with very substantial benefits over time.
>
> 4. Neither shareholders nor employers have received any benefits from market gains in the years in which the pension trust fund's earnings exceeded expectations.

Xcel Ex. 83 at 16 (Schrubbe Rebuttal). The Department disagrees. First, Xcel's request for 100 percent recovery of its 2008 market loss from ratepayers is excessive, particularly when considered in the context of the considerable amounts that ratepayers pay for Xcel's normal pension expense. DOC Ex. 435 at 90-91, 94 (Campbell Public Surrebuttal); Tr.V.5 at 38 (Campbell). The Department agrees that rates should include a reasonable level of retirement benefits, but adding to that Xcel's proposed 100 percent of the 2008 market loss from ratepayers has not been shown to be reasonable. Under Xcel's pension plans, not counting the 2008 market loss, ratepayers pay 100 percent of pension plan expenses since Xcel requires no contribution toward pensions on the part of the employees. The Department has not opposed Xcel's generous pension benefits, nor the match that Xcel offers its employees under the additional 401K plan, but noted that it is the ratepayers, not the Company, who have paid for those benefits.

268. Ms. Campbell explained that if Xcel had proposed to recognize the 2008 market loss over a longer perspective to allow the pension funds to recover, Xcel's approach likely would be reasonable. The Company, however, seeks 100 percent recovery of the 2008 market loss from ratepayers in the short-term, which is not reasonable. *See id.*

269. Second, Xcel's method of including gains and losses in pension expense is not symmetrical. DOC Ex. 435 at 91 (Campbell Public Surrebuttal). Negative pension expense is not given back to ratepayers but is assumed in rate cases to be $0; negative pension expense remains in the pension plan to offset future pension costs. *Id.* Mr. Schrubbe confirmed on cross-examination that he knows of no available rate mechanism that would allow Xcel to track and return over-collections to ratepayers (Tr.V. 2 at 35 (Scrubbe)) and he is unaware of any rate case before the Commission in which Xcel gave a refund to ratepayers regarding pension costs. *Id.*

270. Third, Ms. Campbell disagreed that neither shareholders nor the Company benefit by market gains exceeding expectations because "if the Company's pension plan is overfunded then the Company does not have to make payments into the pension fund. As just noted, Xcel does not refund to ratepayers gains that exceed expectations." DOC Ex. 435 at 91-92 (Campbell Public Surrebuttal).

271. Finally, the DOC disagreed with Mr. Schrubbe's claim that the Commission should not levelize the 2008 market loss (by allowing recovery from ratepayers of only 50 percent) based only on the expected decline of one line item of expense over the next several years. Xcel Ex. 83 at 25 (Schrubbe Rebuttal). Ms. Campbell summarized her disagreement with Xcel:

> As I noted earlier, since the Company's provides both a 401k plan (with ratepayers paying for the 4 percent match) and a pension plan with ratepayers paying for this plan entirely with no contribution from employees, including numerous benefits noted on pages 104 to 107 of my Direct Testimony, I consider the Company's proposal that ratepayers should pay for all the of the 2008 market loss to be unreasonable. I also have concerns that the Company may not have reasonably managed their pension plan, since despite the financial market being above pre-2008 levels, the Company still has a significant amount of 2008 market losses not offset by financial gains.

DOC Ex. 435 at 94 (Campbell Public Surrebuttal). The Department recommends recovery of fifty percent of the market loss proposed by the Company of $12,064,000, or $6,032,000. DOC Ex. 435 at 95 (Campbell Public Surrebuttal). Additionally, regarding management of its pension asset, Xcel agreed to the DOC's recommendation that the Company file in its next rate case its investment strategies, target asset allocations and justifications for those decisions from 2007 to the date of their next rate case filing. Xcel Ex. 116 at 2 (Tyson Opening); DOC Ex. 435 at 89 (Campbell Public Surrebuttal).

272. The DOC's recommendation decreases the test-year administrative and general expense by $6,174,000, as shown in DOC Ex. 451 DVL-EH-7, column (s) (Lusti Opening Statement); DOC Ex. 442 at 11 (Lusti Surrebuttal).[77]

273. The ALJ finds the Department's conclusion to be reasonable and recommends that Xcel be permitted to recover approximately fifty percent of the 2008 market loss—$6,032,000—in 2014 rates.

[77] Xcel Ex. 90 Schedule 11, pages 1-2 (Heuer Rebuttal). DOC agreed with this $6,174,000 figure provided by Xcel for O&M and capital adjustments. *See* DOC Ex. 450 at 5 (Campbell Opening Statement).

b. Alternative rate recovery proposals for Qualified Pension Expense

274. None of the three alternative rate recovery proposals as offered by the Company to normalize or mitigate pension expense in the test-year are reasonable. DOC Ex. 450 at 7-8 (Campbell Opening); DOC Ex. 435 at 99-102 (Campbell Public Surrebuttal). If, however, the Commission does not accept the Department's pension expense recommendations in this rate case, the "least objectionable alternative for normalization proposals" is an amended version of the second proposal. Tr.V. 5 at 26-27 (Campbell). The second proposal was summarized by Ms. Campbell, as follows:

> On pages 35-36 of his Rebuttal Testimony, Mr. Schrubbe described a second proposal for normalization of pension expense. He stated that the second proposal would use the same five-year average from 2014 to 2018, which is $18,246,925, but instead of deferring the difference between the Company's actual pension expense and the normalized expense, the Company would defer the difference between the normalized amount of $18,246,925 *and the lesser of the actual and qualified pension expense amount each year, or the currently forecasted expenses for each year during this time period (2014 to 2018).*
>
> * * *
>
> He showed on his Table 5 the normalized expense of $18,246,925 compared to the forecasted amounts for 2014 to 2018, and showed the difference that would be tracked. I noted that in addition to his Table 5 example, my understanding of the Company's proposal described above is that if the actual pension expense is lower than the forecasted pension expense, then the actual pension expense would be compared against the normalized expense of $18,246,925, to determine any difference.
>
> * * *
>
> According to Mr. Schrubbe on pages 36-37 of his Rebuttal Testimony, the Company proposes that normalized pension expense would be revisited in the Company's next base rate case, which I understand may be filed in November 2015 with a 2016 test year, and that the Company would be allowed to offer a proposal in that rate case on how to amortize whatever deferred asset or liability exists at that time.
>
> * * *
>
> Mr. Schrubbe believes that, like the first proposal, the Company would like to continue to defer the XES Plan cap amounts until the normalization period ends. At that time the amounts deferred

> under the XES Plan cap could be amortized along with any other amounts that are deferred under this proposal.

DOC Ex. 435 at 99 (Campbell Public Surrebuttal) (emphasis by Campbell). Only if the Commission does not accept the Department's pension expense recommendations, the Department identified four essential amendments to Xcel's second proposal that would be necessary for the Department to support it as an alternative, as summarized by Ms. Campbell:

> Alternatively, if the Commission does not agree with the Department's recommendations then we would support the Company's second alternative normalization proposal discussed above and modified as follows. First, I do not agree that Xcel should be allowed to place any under-funded amount in rate base and earn a return on that amount, since the Company already receives a return on its prepaid pension asset (as discussed on pages 126-127 of Mr. Moeller's Direct Testimony). Allowing Xcel to earn a return on under-funding pension assets would give the Company an inappropriate incentive to make poor investment choices for pension assets. Instead, consistent with the Commission's determination in Xcel's prior rate case, I recommend that Xcel earn no return on any deferrals.
>
> Second, I recommend that the overall normalization proposal from the last rate case should impact the new alternative normalization proposals one and two, such that the $1,054,357 deferral for 2013 XES cap that the Commission decided in Xcel's 2012 rate case should be allowed continued deferral.
>
> Third, I recommend that Xcel only be allowed to defer this amount and be required to make a case for why the Company should be allowed to amortize any unfunded balances in the future. For example, any future recovery by Xcel should be allowed only if Xcel can show that the Company made reasonable investment decisions regarding its pension assets.
>
> Fourth, I recommend that Xcel's calculations of the allowed pension expense in each year be based on setting the discount rate equal to the EROA, which for example in 2014 would reduce pension costs by $1.7 million and reduce Xcel's proposed $18.246 million to $16.5 million

The Department does not support the first or third alternatives offered by Xcel. DOC Ex. 435 at 101 (Campbell Public Surrebuttal); Tr.V. 5 at 26-27 (Campbell).

3. Resolved: Xcel's proposed expected return on the pension asset (EROA) rate assumption for the XES and NSPM Plans is reasonable

275. Although the Department initially expressed surprise that Xcel's actual pension returns for 2013 were lower than the proposed EROA assumption as of December 31, 2013, based on the fact that 2013 was a very good year for the financial market, the Department accepts Xcel's EROA as reasonable. The EROA assumption of 7.25 percent is consistent with the historic trends.[78] The ALJ agrees.

4. Resolved: The measurement date assumption proposed by Xcel of December 31, 2013 is reasonable (Issue 18)

276. Similar to its assessment of Xcel EROA assumption, the Department initially was concerned that Xcel's proposed date of December 31, 2013, to measure the value of the pension fund for purposes of calculating test-year rate case expense measurement date resulted in a valuation that seemed low compared to the good financial market at that time. However, following Department discovery and further review, the Department accepted as reasonable Xcel's measurement date for this rate case. Ms. Campbell summarized her conclusion, as follows:[79]

> Mr. Tyson's Schedule 1 page 1 of 3 showed the Company's target asset allocation for the Company's pension fund and on Schedule 1 page 2 of 3 he showed how the Company's different types of investments performed compared to applicable benchmarks. Based on this information, while I do not take a position on the reasonableness of Xcel's pension asset mix, I agree for purposes of this rate case with the Company's measurement update for 2013 of qualified pension expense.

277. The DOC's recommendation increases the test-year administrative and general expense by $1,011,000 as shown in DOC Ex. 451 DVL-EH-7, column (t) (Lusti Opening Statement); DOC Ex. 442 at 11-12 (Lusti Surrebuttal).

278. The ALJ agrees that the measurement date assumption proposed by Xcel of December 31, 2013 is reasonable.

5. Resolved: The wage rate assumption proposed by Xcel of 3.75 percent is reasonable

279. The Department considers Xcel's proposed wage increase rate assumption of 3.75 percent each year to be reasonable. Ms. Campbell reviewed Xcel's methodology, stated on

---

[78] Tr.V. 5 at 34 (Campbell); DOC Ex. 429 at 121-124 (Campbell Public Direct); DOC Ex. 435 at 87-88 (Campbell Public Surrebuttal); Tr.V. 5 at 42 (Campbell).
[79] DOC Ex. 435 at 88 (Campbell Public Surrebuttal).

pages 92-93 of Mr. Moeller's Direct Testimony, now adopted by Mr. Schrubbe, in which the Company described that it relied on expectations of future pay levels which integrate both forward-looking projections and historical experience. The Company also compared this amount against other companies for reasonableness. [80]

280. The ALJ agrees that Xcel's proposed wage increase rate assumption of 3.75 percent each year is reasonable.

L. Changes to In-Service Dates of Capital Projects for 2014 and 2015 (Issue 11)

Disputed between DOC and Xcel: Based on the most current information for in-service dates for capital projects included in the 2014 test year and 2015 Step, and to reflect the capital projects that will not be in-service as Xcel initially budgeted in its initial rate case filing, DOC recommends a $2.18 million revenue requirement reduction for the 2014 test year and a $2.05 million revenue requirement reduction for the 2015 Step. DOC opposes Xcel's proposal to substitute new like-kind replacement projects that it claims will be in-service in 2014 and 2015, that Xcel did not request in its initial filing and that no intervenor has had the opportunity to confirm will be in-service.[81]

281. Xcel acknowledged that certain capital projects included in the Company's initial rate increase request will not be in-service during the 2014 or 2015 Step and, because those projects will not be used and useful to ratepayers, the Department recommends removal of costs associated with those projects: a $2.18 million revenue reduction for the 2014 test year, and a $2.05 million reduction for the 2015 Step, with the exact revenue requirement amount as calculated by Department witness Dale Lusti.[82]

282. Xcel witness Mr. Clark objected to the reductions, claiming that it is "not changing its overall request for relief" and so it should be allowed to offset an adjustment with new capital projects. He emphasized that the 2014 test year should be considered a traditional test year, as if there were no 2015 Step year, and for this reason Xcel only needs to show that the projects identified in its initial rate request filing are representative of the projects that will be in-service during the 2014 test year. He did not explain why the utility is not required to demonstrate that the capital projects are likely to be used and useful during a traditional 2014 test-year.[83]

---

[80] DOC Ex. 429 at 120, 172 (Campbell Public Direct).
[81] DOC Ex. 450 at 9 (Campbell Opening); DOC Ex. 435 at 104-106 (Campbell Public Surrebuttal).
[82] DOC Ex. 429 at 153 (Campbell Public Direct); DOC Ex. 435 at 109 (Campbell Public Surrebuttal).
[83] Xcel Ex. 100 at 15 (Clark Rebuttal); DOC Ex. 435 at 103, 105 (Campbell Public Surrebuttal). (Xcel witness Mr. Clark also stated that the Department's adjustments are contrary to the concept of a representative test year, and the number of capital projects moving outside the test year is relatively small in comparison to the total number of capital projects budgeted to go into service during 2014. *Id.* at 103.); Xcel Ex. 100 at 16-17 (Clark Rebuttal).

283. Mr. Clark testified that Xcel's proposal to replace projects for the 2014 test year that moved outside of the 2014 test year due to delays in completion, "is not materially different than our recommendation to make corresponding updates for projects moving into the test year." Again, Mr. Clark did not explain why clear differences between the Department's proposal and the Company's request are "not materially different."[84]

284. As to the 2015 Step, Mr. Clark took issue with the Department's discovery and recommendation in that he claimed it is not appropriate or needed to update changes in 2015 in-service dates. He said that there is a refund plan applicable to 2015 projects to protect ratepayers in the event a Step project is delayed or cancelled, and that the 2015 Step projects represent a limited percentage of Xcel's total investment for 2015.[85]

285. Xcel witness Ms. Perkett testified that allowing Xcel to add new capital projects would be reasonable basically because Xcel's changes to its in-service dates reflect the normal types of changes that can impact the timing of capital project completion, and she gave examples of projects within three general categories of replacement projects proposed by the Company.[86]

286. The Department's—not Xcel's—proposed adjustments are consistent with the concept of a test year, and stem from its attempt to verify in-service dates to ensure that ratepayers will not pay for projects that are not used and useful during a test year.[87] Ms. Campbell strenuously disagreed with Xcel's unsupported position that utilities routine swap out capital projects initially identified as being in-service during the test year for new like-kind projects that no party has the opportunity to confirm will be used and useful to ratepayers during the test year.[88] Rather, what is a routine part of the Department's examination of a utility's general rate increase request is discovery to assess whether a Company's representations in its initial filing are reasonable.[89] Because regulated utilities have an incentive, due to the nature of the rate case process, to estimate an earlier in-service date (within the rate case test year) than they may be able to meet, the Department issues information requests to help ensure that the dates and test year capital project amounts used for setting rates are supported and appear to be reasonable.[90] Ratepayers deserve no less discovery and examination with respect to the present Xcel rate case.

287. The Department's verification in this matter was challenging; in its initial rate case filing, Xcel budgeted 733 capital projects for completion in 2014 and 116 projects for completion in the 2015 Step year.[91] While Xcel deemed its 2015 Step projects as "limited," Ms. Campbell testified that the projects include most of Xcel's projected 2015 capital projects in that

---

[84] *Id.* at 18.
[85] *Id.* at 18-19.
[86] Xcel Ex. 94 at 39-42 (Perkett Rebuttal).
[87] *See* DOC Ex. 435 at 105 (Campbell Public Surrebuttal).
[88] *Id.* at 104-106.
[89] DOC Ex. 435 at 104 (Campbell Public Surrebuttal).
[90] DOC Ex. 435 at 104-105 (Campbell Public Surrebuttal).
[91] *See* DOC Ex. 429 at 152 (Campbell Public Surrebuttal) (Table 1).

they represent over eighty percent of the amount Xcel's claimed it could have requested for its 2015 rate base increase.[92] In response to Department discovery, the Company identified 49 of 733 projects that it has determined will not be in-service in 2014 ("moved outside 2014 to 2015"), and identified 2 of 116 projects that will not be in-service in 2015 ("moved outside the 2015 Step"),[93] for a total of 51 changes to in-service dates for proposed projects.[94] Xcel supported the majority of its proposed in-service dates, but delays or changes in the timing of the 51 capital projects resulted in the over $2 million in Department-recommended reductions for the 2014 test year and the 2015 Step.[95] As Ms. Campbell noted, verification of this kind "is what discovery is all about."[96]

288. Xcel's position appears to be that it should not be required to demonstrate the accuracy of its claimed in-service dates for 2014 and 2015 capital projects that were in its initial rate case petition."[97] The Company has not shown the reasonableness of this position. Moreover, the Department expressed concern that Xcel did not show why it apparently was unable to reasonably manage changes in capital project in-service dates for purposes of the rate case.[98] Ms. Perkett's examples of the types of capital projects that fall within Xcel's three categories of new or replacement projects do not justify allowing the Company to add new capital projects that no party has had the opportunity to review or confirm.[99] In addition, the Department's review of the project examples suggested that capital costs appear to be more likely to go down rather than up during Xcel's test-years; thus, Ms. Campbell did not support the Company's proposal to add new, late-filed projects that were not included in the Company's initial petition.[100]

289. Xcel has not shown that it is reasonable to add new projects to "offset" the Department's proposed reductions for capital projects that will not be in-service in 2014 or during the 2015 Step. Allowing Xcel to add new projects would be contrary to the Company's burden of proof, would unfairly burden ratepayers, and would not be in the public interest, as summarized by Ms. Campbell:[101]

> I do not agree that the Company in response to the 51 in-service date changes should be allowed to add new capital projects that no party has had the opportunity to consider and at the added costs of $1.8 million (per DOC information request no. 123 second

---

[92] Tr.V. 5 at 61 (Campbell); DOC Ex. 435 at 115-116 (Campbell Public Surrebuttal) (2015 Step projects equal 81.3 percent of Xcel's claimed full 2015 rate base increase).
[93] *Id.*
[94] DOC Ex. 450 at 8 (Campbell Opening).
[95] DOC Ex. 435 at 105 (Campbell Public Surrebuttal).
[96] DOC Ex. 435 at 106 (Campbell Public Surrebuttal).
[97] DOC Ex. 435 at 107 (Campbell Public Surrebuttal).
[98] *Id.* at 107.
[99] DOC Ex. 435 at 106-107 (Campbell Public Surrebuttal).
[100] DOC Ex. 435 at 108 (Campbell Public Surrebuttal).
[101] DOC Ex. 435 at 104-106 (Campbell Public Surrebuttal).

> supplement on page 151 of my Direct Testimony). It is not appropriate to allow the Company to charge ratepayers for the costs of new projects above the level that the Company included in their initial case. As noted on page 153 of my Direct Testimony, allowing the Company to add new capital projects not included in the Company's initial petition would unfairly burden parties in this rate case, including the Department, which investigates rate cases on behalf of the broad group of Xcel's ratepayers, and would not be in the public interest.
>
> * * *
>
> Parties' opportunities to issue discovery and to consider the Company's bases for its proposed rate increase would be impeded if, as Xcel proposed in its responses to discovery, utilities were allowed to keep adding additional capital projects for the first time. In light of a 2014 test year with 733 capital projects and a 2015 Step with 116 capital projects, it would not be reasonable to expect that the Department and other parties in the case could review such new requests. Such an approach would not result in development of a reasonable basis for the Commission to set rates. The burden of proving the reasonableness of the Company's request for recovery of capital projects must remain on Xcel, as required by Minnesota Statute §216B.16 subd. 4, and should not be shifted to other parties. It is up to the Company to identify all capital projects with its initial rate case filing.

290. The Department continues to conclude that the most current information for in-service dates for the specific capital projects included in the Company's initial rate case filing should be used for purposes of determining reasonable rates. As a result, the Department recommends that the Commission approve a $2.18 million revenue requirement reduction for the 2014 test year and a $2.05 million revenue requirement reduction for the 2015 step (according to the Company's calculations).[102]

291. The DOC's recommendation decreases the test-year rate base by $11,194,000 as shown in DOC Ex. 451 DVL-EH-4, column (n) (Lusti Opening Statement); and decreases the test-year depreciation expense by $1,152,000, deferred income tax by $2,654,000 and AFUDC by $120,000, and increases income tax by $3,239,000, as detailed in DOC Ex. 438 DVL-15, Column (a) (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-EH-7, column (x) (Lusti Opening Statement); DOC Ex. 442 at 11-12 (Lusti Surrebuttal).

292. The ALJ agrees that the Department's recommendation is reasonable.

---

[102] DOC Ex. 450 at 9 (Campbell Opening); DOC Ex. 435 at 102-109 (Campbell Public Surrebuttal).

M. Big Stone-Brookings Transmission Project Correction (Issue 41)

293. In her Rebuttal Testimony Ms. Heuer described a correction:

> Subsequent to preparing the capital budget relied on for our Application, a forecasted update was made to a component of the Big Stone Brookings transmission project. That update has associated with it lower [operating] costs. The resulting adjustment was made to the interim revenue requirement, but was identified too late to be reflected in our test year revenue requirement.

DOC Ex. 442 at 12 (Lusti Surrebuttal) (correctly citing Xcel Ex. 90 at 40 (Heuer Rebuttal)).

294. The Company's recommendation increased test-year rate base by $299,000 and increased operating income by $107,000 as shown in Xcel Ex. 90 at AEH-2, Schedule 6A, Page 2 of 2, Column (14), and Schedule 6B, Page 2 of 2, Column (14), respectively (Heuer Rebuttal). The DOC agreed with the Company's proposed Big Stone Brookings correction and Mr. Lusti incorporated the correction into his revenue requirement calculations the Company's recommended increase to the test-year rate base of $299,000 and increase to operating income of $108,000, as shown in DOC Ex. 451 DVL-EH-4, column (o) and DVL-EH-7, column (z) (Lusti Opening Statement); DOC Ex. 442 at 13 (Lusti Surrebuttal).

295. The ALJ finds that this adjustment, as agree by Xcel and the Department, is reasonable.

N. Theoretical Reserve Correction Adjustment (Issue 43)

296. The DOC's recommendation decreases the test-year rate base by $77,000 as shown in DOC Ex. 451 DVL-EH-4, column (p) (Lusti Opening Statement) and decreases the test-year operating income by $21,000 as shown in DOC Ex. 451 DVL-EH-7, column (ab) (Lusti Opening Statement); DOC Ex. 442 at 13 (Lusti Surrebuttal).

297. The ALJ finds that this adjustment, as agree by Xcel and the Department, is reasonable.

O. Net Operating Loss (NOL) Correction Adjustment (Issue 44 and Issue 47)

Resolved between DOC and Xcel: DOC agrees to an Xcel proposed adjustment to net operating loss (NOL) that corrected an error in Xcel's calculation of the deferred tax. Xcel Ex. 90 at 42-43 (Heuer Rebuttal). DOC noted, however, that the Commission's final approval of adjustments in this proceeding may require the Company and the Department to review an additional net operating loss correction. Ms. Heuer's NOL adjustment at this time increases the test-year rate base by $190,000 as shown in DOC Ex. 442 DVL-S-4, column (q) and increases the test-year operating income by $229,000 as shown in DOC Ex. 442 DVL-S-7, column (ac) (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-4, column (g) and DVL-EH-7, column (ac) (Lusti Opening Statement).

298. In its Rebuttal Testimony, the Company proposed a net operating loss (NOL) correction adjustment. Ms. Heuer, at pages 42-43 of her Rebuttal Testimony discussed a correction for an error in the deferred tax calculation that was incorporated into her Direct Testimony. Her recommended adjustment would increase rate base by $190,000, increase operating income by $229,000 (DOC Ex. 442 at 36 (Lusti Surrebuttal)) and decrease the revenue requirement by $366,000 as shown in Xcel Exhibit 90 (AEH-2), Schedule 24 (Heuer Rebuttal).

299. Mr. Lusti did not disagree with this adjustment, but explained that it may be appropriate to review the net operating loss calculation for the setting of final rates, because the potential exists that the Commission's final approval of adjustments in this proceeding may require the Company and the Department to review an additional net operating loss correction. DOC Ex. 442 at 14 (Lusti Surrebuttal).

300. Ms. Heuer's NOL adjustment, at the time of Mr. Lusti's Surrebuttal, increased the test-year rate base by $190,000 as shown in DOC Ex. 442 DVL-S-4, column (q) and increased the test-year operating income by $229,000 as shown in DOC Ex. 442 DVL-S-7, column (ac) (Lusti Surrebuttal); DOC Ex. 442 at 14 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-4, column (g) and DVL-EH-7, column (ac) (Lusti Opening Statement).

301. The ALJ finds that this adjustment, as agree by Xcel and the Department, is reasonable.

P. Cash Working Capital Methodology and Calculation (Issue 49, in part-2014)

Resolved between DOC and Xcel. DOC agrees that the methodology used by Xcel to calculate cash working capital was reasonable. DOC Ex. 437 at 24-25 (Lusti Direct).

Disputed between DOC and Xcel. Although not resolved, the specific amount of cash working capital in this proceeding will be calculated later, based on the Commission's approved rate base adjustments, revenue and expense adjustments, and capital structure in total, and does not need to be decided by the ALJ. The current DOC adjustment is an increase of $8,544,000. DOC Ex. 451 DVL-EH-4, Page 3 of 3, Column (r) (Lusti Opening Statement).

302. Xcel calculates its cash working capital requirement as follows: Cash working capital refers to the amount of cash a utility needs to have on hand to conduct its business. A lead/lag study is necessary to determine the amount of cash working capital that a company must reserve. Lead time is the number of days between the utility's receipt and payment of invoices it receives. Lag time is the average number of days between the utility's billing of its customers and its receipt of payment. Thus, the Company applies lead/lag study factors to its test-year O&M expenses to determine its cash working capital requirement. DOC Ex. 437 at 24 (Lusti Direct).

303. In his Direct Testimony, Mr. Lusti reviewed the lead/lag factors that Xcel uses in this proceeding, compared them to recent data, and determined that they were reasonable. DOC Ex. 437 at 24 (Lusti Direct). He also reviewed the revenues and expenses that Xcel included in

the lead/lag study. Mr. Lusti reviewed the Company's workpapers and concluded that the lead/lag study was reasonable; however, the resulting test-year cash working capital requirement needed to be modified to reflect the DOC's recommended adjustments to the rate base, revenue and expenses. DOC Ex. 437 at 24-25 (Lusti Direct).

304. Mr. Lusti explained that, as a result of the various DOC adjustments to the test-year O&M expenses and test-year rate base, Xcel's cash working capital needed to be adjusted. Mr. Lusti calculated this adjustment by applying the DOC's lead/lag days to the DOC O&M expense adjustments. At the Evidentiary Hearing, Mr. Lusti concluded that the cash working capital should be increased by $8,544,000, as detailed in DOC Ex. 451 DVL-EH-5, Line (51) and as shown in DVL-EH-4, column (r) (Lusti Opening Statement).

305. Mr. Lusti cautioned that, if the Commission does not accept the DOC's proposed rate base adjustments, revenue and expense adjustments, and capital structure in total, it would be necessary to recalculate the cash working capital to incorporate the effect of the approved rate base, revenue and expense adjustments, and the capital structure; and, similarly, if there are any additional adjustments made in this case, it would be necessary to recalculate the cash working capital to incorporate those adjustments as well. DOC Ex. 437 at 25 (Lusti Direct); DOC Ex. 142 at 15 (Lusti Surrebuttal).

Q. Test-Year Rate Base Summary

Disputed between DOC and Xcel: While DOC and Xcel disagree regarding calculation of the total adjustment to Rate Base, the ALJ does not need to decide this issue; after all other disputed issues are decided, DOC and Xcel will calculate cash working capital, and sum the adjustments to arrive at the test year rate base. At the evidentiary hearing, DOC recommended that the Commission approve a rate base of $6,501,384,000), as shown in DOC Ex. 451 DVL-EH-3, Column (c) (Lusti Opening Statement). This amount is $168,869,000 lower than Xcel's proposed rate base level of $6,670,252,000.

306. Mr. Lusti, in his Direct Testimony, recommended that the Commission approve a rate base of $6,465,963,000. DOC Ex. 437 at 26 (Lusti Direct). In his Surrebuttal, as a result of the various further DOC adjustments, Mr. Lusti recommended that the Commission approve a rate base of $6,472,738,000. DOC Ex. 442 at 35 (Lusti Surrebuttal).

307. At the evidentiary hearing Mr. Lusti calculated the effect of further changes resulting from further resolution of issues after his Surrebuttal. Mr. Lusti recommended that the Commission approve a rate base of $6,501,384,000), as shown in DOC Ex. 451 DVL-EH-3, Column (c) (Lusti Opening Statement). This amount is $168,869,000 lower than Xcel's proposed rate base level of $6,670,252,000.

R. Cost Amortizations (Issue 8)

Agreed between DOC and Xcel: Xcel may recover its estimated rate case expenses of $2,714,433 (excluding 0.2835 percent of Xcel's proposal for costs related to unregulated business), amortized over two years. Xcel Ex. 88 at 142 (Heuer Direct); DOC Ex. 438 at DVL-32 (Lusti Direct Attachments); DOC Ex. 437 at 28 (Lusti Direct).

Agreed between DOC and Xcel: Xcel may recover expenses for the Monticello Cost Overrun Investigation, estimated to be $950,000. DOC Ex. 437 at 28 (Lusti Direct).

Disputed between DOC and Xcel: Xcel recommends that, because the Monticello Cost Overrun Investigation costs were Commission-mandated, and similar in nature to a rate case, the expense that should be recovered on a current basis, not capitalized without a return over the life of the plant. DOC Ex. 442 at 16 (Lusti Surrebuttal) (*citing* Xcel Ex. 90 at 24 (Heuer Rebuttal)). DOC recommends that the costs should be spread over the remaining life of the facility, 16.8 years, without a return. DOC Ex. 437 at 28-29 (Lusti Direct); DOC Ex. 442 at 16-18 (Lusti Surrebuttal). The DOC recommendation decreases the test-year prudency review amortization expense by $418,452, as detailed in DOC Ex. 442 DVL-13, and as shown in DOC Ex. 442 DVL-7, column (d) (Lusti Direct); DOC Ex. 442 at 16, 18 (Lusti Surrebuttal).

308. Xcel sought recovery of expenses related to this 13-868 rate case and to the Commission's prudency review of the Monticello EPU. Xcel proposed to recover the estimated expenses for this rate case and for the prudency review proceeding over a two-year amortization period, in anticipation of filing its next rate case in 2015, using a 2016 test year. DOC Ex. 437 at 27 (Lusti Direct) (*citing* Xcel Ex. 88 at 142 (Heuer Direct)).

309. Mr. Lusti reviewed NSP’s calculation of its rate-case expense level in this proceeding. The Company’s estimate of the cost of the current rate case was $2,714,433 (excluding 0.2835 percent of Xcel's proposal for costs related to unregulated business). The estimate was based five cost categories, consulting fees, outside legal fees, state agency and administrative law judge fees, administrative costs (such transcripts and administration); and removal of 0.2835 percent for unregulated business. DOC Ex. 437 at 27 (Lusti Direct). Mr. Lusti agreed with the estimates of the five categories of rate case expense as developed by the Company, after reviewing supporting documentation provided by the Company in Response to DOC IR 190. Mr. Lusti challenged neither the Company’s estimate of the rate-case costs nor the allocation of rate-case expenses to the unregulated businesses. DOC Ex. 438 at DVL-32 (Lusti Direct Attachments); DOC Ex. 437 at 28 (Lusti Direct). Further, Mr. Lusti agreed that it is appropriate in this instance to recover the rate case expenses over a two-year period. DOC Ex. 437 at 28-29 (Lusti Direct).

310. Mr. Lusti also reviewed NSP’s calculation of expenses for the Monticello Cost Overrun Investigation. The Company’s estimate of the cost of the prudency review was $950,000. The estimate was based on two cost categories, consulting fees and outside legal fees. DOC Ex. 437 at 28 (Lusti Direct). Mr. Lusti agreed with the Company’s estimates of the two categories of prudency review costs after reviewing supporting documentation provided by the Company in Response to DOC IR 191. Mr. Lusti did not agree, however, with the Company’s proposed two-year recovery period for prudency review costs because prudency review costs should be spread over the remaining life of the facility, which for the Monticello EPU is no more than 16.8 years, assuming that the EPU is in service in 2014. DOC Ex. 437 at 28-29 (Lusti Direct); DOC Ex. 442 at 16, 17 (Lusti Surrebuttal). Mr. Lusti disagreed with Xcel, which contended that the Monticello Cost Overrun Investigation costs were Commission-mandated, similar in nature to a rate case expense that should be recovered on a current basis and not

capitalized over the life of the plant. DOC Ex. 442 at 16 (Lusti Surrebuttal) (*citing* Xcel Ex. 90 at 24 (Heuer Rebuttal)).

311. Mr. Lusti explained that the Monticello Cost Overrun Investigation was unlike a rate case; in a rate case, the Commission sets rates for a specific point in time, and the costs of the rate case are recovered over the time span when the new rates are to be in effect. In the Monticello Cost Overrun Investigation, the Commission reviewed whether the Company was prudent in planning and construction of the facility. The Commission's decision will continue for the life of the facility, not only until the next rate case is filed, as with rate case expenses. DOC Ex. 442 at 17 (Lusti Surrebuttal).

312. Mr. Lusti also disagreed with Xcel's contention that, because the expenses were incurred due to a Commission-mandated review, it is inappropriate to require recovery of these costs over the life of the facility without a return; he observed that, while the Commission ordered the prudency review to take place in 2014, the Monticello Cost Overrun Investigation had previously been an issue in 2011, in Docket Nos. E002/GR-10-971, where the Commission approved a Settlement Agreement that stated:

> The Company will provide a compliance update within a reasonable period of time after the LCM/EPU project is completed, outlining the total costs for the project and the additional capacity achieved, and providing the appropriate supporting facts and information for the purpose of a full prudence review of the entire project…If the Commission subsequently determines that any of the costs were imprudent, a refund mechanism for the costs deemed imprudent can be implemented, and the Company waives any defense to such a decision based on retroactive ratemaking.

DOC Ex. 442 at 18 (Lusti Surrebuttal) (*citing* Docket No. E002/GR-10-971, Settlement Agreement, November 14, 2011 at 2, section 2). Further, by not allowing a return on the un-amortized costs, there would be a sharing of these costs between ratepayers and shareholders; ratepayers would pay the Company back for the prudency review costs over the life of the facility, and the shareholders would recover the costs of the review but not earn a return on it. DOC Ex. 442 at 18 (Lusti Surrebuttal).

313. The DOC recommended an adjustment of test-year operating income for the Monticello Cost Overrun Investigation costs. The DOC recommended a decrease of the test-year rate case amortization expense by $418,452, as detailed in DOC Ex. 438 DVL-13, and as shown in DOC Ex. 438 DVL-7, column (d) (Lusti Direct Attachments); DOC Ex. 437 at 29 (Lusti Direct); DOC Ex. 442 at 18 (Lusti Surrebuttal).

314. The ALJ finds that this adjustment, recommended by the Department, is reasonable.

S. Nuclear Retention Program (Issue 23)

Resolved between DOC and Xcel). Xcel agreed to the DOC recommendation that the test-year administrative and general expense be reduced by $516,466 to reflect elimination of the nuclear

retention program expense, as shown in DOC Ex. 438 DVL-7, Column (e) (Lusti Direct Attachments); DOC Ex. 437 at 35 (Lusti Direct); DOC Ex. 442 at 24 (Lusti Surrebuttal); Xcel Ex. 140 at 2 (Heuer Opening Statement); DOC Ex. 451 DVL-EH-7, Page 1 of 4, Column (e) (Lusti Opening Statement).

315. The nuclear retention program Xcel included in this proceeding is the third year of a three-year program that was implemented in the fall of 2012, and was included in revenue requirements of the last Xcel rate case, Docket No. E002/GR-12-961. DOC Ex. 437 at 30 (Lusti Direct) and DOC Ex. 438 DVL-34 (Xcel Response to DOC IR 1174(C) (Lusti Direct Attachments).

316. The ALJ and Commission had disapproved this nuclear retention program proposal in the last rate case, Docket No. E002/GR-12-961. DOC Ex. 437 at 30 (Lusti Direct) (*citing* Docket No. E002/GR-12-961, Commission Findings of Fact, Conclusions and Order, dated September 3, 2013, Paragraph 2 (adopting ALJ Report) and ALJ Report, July 3, 2013, Findings 459 and 460. In recommending disapproval of the retention program expense, the ALJ Report stated:

> …The Company has not, however, shown that the $1.032 million requested for its new Nuclear Employee Cash-based Retention Program is a reasonable amount. There is no information in the record explaining how the Company arrived at the $1.032 million budget for its new Nuclear Employee Retention Program. Without specific financial supporting the amount requested, there is no basis upon which to determine that the amount requested for this new program is reasonable. Accordingly, the Administrative Law Judge concludes that the Company has failed to demonstrate that the $1.032 million requested for its new Nuclear Employee Retention Program in 2013 is reasonable.

317. The Company's proposed recovery in this Docket No. 13-868 was based on a Total Company number of $694,736 of nuclear retention program expenses. The Minnesota jurisdictional amount was $516,466 after applying a 74.34 percent allocation factor. DOC Ex. 437 at 31 (Lusti Direct). The initial retention program was designed to retain 33 employees in key positions for the 27-month period ending in December 2014. DOC Ex. 437 at 31 (Lusti Direct) (*citing* Xcel Ex. 78 at 50-55 (Figoli Direct) and Xcel Ex. 51 at 99-105 (O'Connor Direct).

318. Mr. Lusti explained that he inferred from the facts that Xcel had created a 27-month nuclear retention program in the fall of 2012 because the affected business unit employees were unable to meet existing performance standards. Mr. Lusti reviewed the Company's May 31, 2013 Incentive Compensation Plan Annual Report in Docket Nos. E002/GR-92-1185 and G002/GR-92-1186, and follow-up information requests; that data indicates that the Company knew the Nuclear Business Unit would not meet its 2012 Key Performance Indicator (KPI), and would probably not meet its 2013 KPI either. DOC Ex. 438 DVL-35 (Lusti Direct Attachments); DOC Ex. 437 at 32 (Lusti Direct). Thus, the affected employees would not be able to achieve as high of a level of incentive compensation as if they met or exceeded their KPI. DOC Ex. 438 at DVL-35 (Lusti Direct Attachments); DOC Ex. 437 at 32 (Lusti Direct).

319. In total, the nuclear business unit only reached 77.48 percent of its target level KPI requirements. DOC Ex. 437 at 32 (Lusti Direct). The five performance categories where the business unit did not meet its target were safety and reliability related:

- Collective Radiation Exposure – REM;
- Equipment Reliability Index;
- Safety Systems Performance Index;
- Nuclear Regulatory Commission (NRC) Findings and Violations Self-Identification Ratio; and
- Project and Outage Performance.

DOC Ex. 437 at 32-33 (Lusti Direct). Xcel indicated that it knew the nuclear unit would not achieve target level KPI in these five categories on the following dates:

- Collective Radiation Exposure – REM – November 2012;
- Equipment Reliability Index – August 2012;
- Safety Systems Performance Index – July 2012;
- NRC Findings and Violations Self-Identification Ratio – November 2012; and
- Project and Outage Performance – July 2012.

DOC Ex. 438 at DVL-38 (Lusti Direct Attachments) (Xcel's June 6, 2013 Response to DOC IRs 101 through 105 in Docket Nos. E002/GR-92-1185 and G002/GR-92-1186); DOC Ex. 437 at 33 (Lusti Direct).

320. The significance of Xcel's knowledge that the nuclear business unit would not receive its full target level or greater incentive compensation for the year 2012 (paid in March 2013) concerns the integrity of the Company's incentive compensation program. Mr. Lusti explained that the Company's proposed new compensation program appeared to be an effort to "end-run" the whole purpose of a performance incentive – to encourage better performance. DOC Ex. 437 at 33 (Lusti Direct). Mr. Lusti further explained that Xcel knew during mid-year 2012 that the nuclear business unit would not meet its target level KPI requirements for the years 2013 and/or 2014, given the cost overruns the nuclear business unit was already experiencing. DOC Ex. 437 at 33-34 (Lusti Direct) (*citing* Docket E002/GR-10-961, Koehl Rebuttal at 14-15).

321. After Mr. Lusti wrote his Direct Testimony in this proceeding, the Company's Incentive Compensation Plan Annual Report for the year 2013 was filed and made available to the Department, on May 30, 2014. DOC Ex. 442 at trade secret DVL-S-44 (Lusti Surrebuttal). Similar to the year 2012 report (DOC Ex. 438 at DVL-35 (Lusti Direct Attachments)), the nuclear business unit in 2013 was the only unit that did not achieve 100 percent of its KPI. This, despite the fact that Xcel appears to have attempted to facilitate achievement of a 100 percent KPI rating by eliminating from the 2013 KPI two KPI achievement categories --the "Equipment Reliability Index" and "Safety System Performance Index"-- that the nuclear business unit in 2012 failed to meet, having received 0 out of 15 percent in each of the two categories, resulting in 0 out of 30 percent. DOC Ex. 437 at 33-34 (Lusti Direct) (*citing* DOC Ex. 438 DVL-35, Page 32 of 40) (Equipment Reliability Index and Safety System Performance Index) (Lusti Direct Attachments); DOC Ex. 442 DVL-S-45 is a summary of the Key Performance Indicator (KPI)

Results From Xcel's Incentive Compensation Reports for the Years 2008 – 2013. DOC Ex. 442 at 23 (Lusti Surrebuttal). The removal of the categories for "Equipment Reliability Index" and "Safety System Performance Index" as performance standards from the 2013 nuclear business unit KPI are shown in DOC Ex. 442 at trade secret DVL-S-44, page 30 of 38 (Lusti Surrebuttal).

322. Mr. Lusti explained that it is reasonable to conclude that Xcel's 27-month nuclear retention program was created to provide its nuclear employees with additional compensation, to replace amounts that they would likely not receive via the traditional incentive compensation, until such time as the nuclear business unit could achieve an KPI rating adequate to earn additional compensation. DOC Ex. 437 at 24-35 (Lusti Direct). In other words, Xcel proposed that ratepayers pay for a program that circumvents the structure of Xcel's incentive compensation program to reward the nuclear business unit unable to achieve a KPI rating that would allow its employees to receive existing incentive compensation. Mr. Lusti concluded that it is not appropriate to do so. DOC Ex. 437 at 35 (Lusti Direct); DOC Ex. 442 at 24 (Lusti Surrebuttal).

323. DOC did not suggest that the Commission forbid Xcel to pay Nuclear Incentive Program payments to its employees, only that the Commission should not require Xcel's Minnesota Jurisdictional ratepayers to pay the costs of the Nuclear Incentive Program, as included in this proceeding, because the Company did not met its burden of proof to show that the level of costs it proposed is reasonable to charge to ratepayers. DOC Ex. 442 at 24 (Lusti Surrebuttal).

324. Mr. Lusti recommended that the test-year administrative and general expense be reduced by $516,466 to reflect elimination of the nuclear retention program expense, as shown in DOC Ex. 438 DVL-7, Column (e) (Lusti Direct Attachments); DOC Ex. 437 at 35 (Lusti Direct); DOC Ex. 442 at 24 (Lusti Surrebuttal).

325. In its Opening Statements, Xcel agreed to Mr. Lusti's recommended adjustment, stating: "[t]he Company agrees to a reduction of $0.516 million in 2014 Test Year Nuclear Retention Program costs recommended by Mr. Lusti in his Direct Testimony." Xcel Ex. 140 at 2 (Heuer Opening Statement); DOC Ex. 451 DVL-EH-7, Page 1 of 4, Column (e) (Lusti Opening Statement).

326. The ALJ finds that this adjustment, as agree by Xcel and the Department, is reasonable.

T. Property Tax (Issue 14)

Resolved between DOC and Xcel: Xcel agreed to a DOC alternative recommendation of a reduction of $9 million in property tax expense for the 2014 Test Year, subject to a true-up for 2014 actual accruals and a cap at the $145 million Minnesota jurisdictional level. Xcel Ex. 140 at 2 (Heuer Opening Statement). Xcel will make a compliance filing on June 30, 2015 detailing actual 2014 property taxes reflected on final 2014 property tax statements received in the spring of 2015. To the extent that actual 2014 property taxes are less than the Company's year-end 2014 property tax expense (for the Minnesota Electric jurisdiction), the Company will make ongoing, annual refunds of the difference between the Company's year-end 2014 property tax expense and the 2014 property taxes reflected on the final 2014 property tax statements. This

refund obligation continues until Xcel files its next rate case. DOC Ex. 451 at 2 (Lusti Opening Statement); DOC Ex. 451 DVL-EH-7, Page 1 of 4, Column (f) (Lusti Opening Statement).

327. Xcel included $150,000,000 in property taxes in the 2014 test year. In addition, Xcel included $162,000,000 in its 2015 STEP year. DOC Ex. 438 at DVL-14 (Lusti Direct Attachments); DOC Ex. 437 at 36 (Lusti Direct).

328. This level of proposed property tax should not have been included in the test year revenue requirement. For most of 2001 through 2013, Xcel over-recovered its allowed and/or forecast property tax. DOC Ex. 438 at DVL-14 Schedule 2 (Lusti Direct Attachments). And, even though the Commission reduced the level of Xcel's proposed 2013 property taxes in the previous rate case, Docket No. E002/GR-12-961, the Company still over-recovered property tax in 2013. DOC Ex. 437 at 36 (Lusti Direct).

329. Mr. Lusti recommended in his Direct Testimony that the test-year property tax be reduced by $13,500,000 to reflect the 9 percent difference between Xcel's estimated and actual property tax for the period 2001 through 2013, as Detailed in DOC Ex. 438 DVL-14, Schedule 1, and as shown in DOC Ex. 438 DVL-7, Column (e) (Lusti Direct Attachments); DOC Ex. 437 at 36 (Lusti Direct).

330. In his Rebuttal, Xcel Witness James J. Duevel disagreed, stating that the Department's recommendation was not based on the information that will drive the Company's 2014 property taxes and was therefore not a reasonable means of establishing test year property tax expense. He stated that approximately 97 percent of the difference between estimated and actual property taxes identified by the Department occurred from 2001 through 2005, because the property tax expense included in rates during this period was set in the Company's 1992 rate case (Docket No. E002/GR-92-1185) based on a 1993 test year. Xcel Ex. 34at 7 (Duevel Rebuttal). To support the Xcel proposal, he stated that Xcel's forecast is within 2.95 percent of the "*expected* 2014 property tax expense..." DOC Ex. 442 at 26 (Lusti Surrebuttal) (citing Xcel Ex. 34 at 3 (Duevel Rebuttal)(emphasis added).

331. Mr. Lusti observed, in response, that Xcel's property tax forecasting abilities are not established by having two forecasts that are 2.95 percent apart. In Xcel's most recent rate case, Docket No. E002/GR-12-961, the Company similarly made a series of three property tax forecasts from November 2012 to June, 2013, shown in Mr. Lusti's Surrebuttal Table 2:

Table 2: Xcel's Estimated and Actual Property Tax in Docket No. E002/GR-12-961

Xcel's Updated Estimates of Property Tax Expense in 12-961 ($ Millions)		**Change Since 11/2/12 Direct**	**Percent Change**
11/2/12 Direct Position	$181.9	--	--
3/25/13 Rebuttal Position	$191.8	$9.9	5.44%
4/19/13 Supplemental Position	$188.0	$6.1	3.35%
Commission Approved Amount	$183.4	$1.5	0.82%

June 2013 Estimate	$171.7	$(10.2)	(5.61)%
Actual 2013 Amount	$166.3	$(15.6)	(8.58)%

DOC Ex. 442 at 27 (Lusti Surrebuttal). Mr. Lusti explained that Xcel's forecasts in the 12-961 docket were not reasonably accurate, as can be seen on table 2. Mr. Duevel's initial forecast of $181.9 million on a Total Minnesota Forecasted Property Tax basis would eventually prove to be $15.6 million or 8.58 percent too high, yet his March 25, 2013 Rebuttal Testimony incorporated an additional $9.9 million or 5.44 percent increase over his initial position. In Supplemental Testimony at the Evidentiary Hearing on April 19, 2013, he slightly reduced his Rebuttal Testimony position by $3.8 million. With that amount of information and the Department's recommendation, the Commission approved the Minnesota Jurisdictional portion of the $183.4 million Total Minnesota Property Tax expense. The June 2013 estimate reduced the Forecast 2013 Property Taxes to $171.7 million. The Company's actual 2013 property taxes on a Total Minnesota basis were $166.3 million; $15.6 million or 8.58 percent less than Mr. Duevel's position in Direct Testimony in that proceeding.

332. In large part due to Mr. Duevel's forecast, the level of property tax expense that the Commission approved to be charged to ratepayers was $17.1 million, or 10.3 percent more than the Company's actual property taxes. DOC Ex. 442 at 27-28 (Lusti Surrebuttal).

333. Mr. Duevel forecasted property taxes in this proceeding in a manner similar to how he forecasted property taxes in the Docket No. 12-961, with the same variables and with data inputs for each variable that were similar to those in the Docket No. 12-961. DOC Ex. 442 at 28 (Lusti Surrebuttal) (*citing* Xcel Ex. 32 at 6-7 (Duevel Direct). Mr. Lusti testified that he did not have confidence that Mr. Duevel's initial forecast in this proceeding is reasonable or appropriate for inclusion in the test year revenue requirement, where Mr. Duevel developed this 2014 property tax forecast on a basis similar to the erroneous forecast in the 12-961 docket. DOC Ex. 442 at 28 (Lusti Surrebuttal)

334. Mr. Lusti recommended that test-year property tax be calculated in this proceeding as follows: Using actual Minnesota Jurisdictional property tax expense data for the five-year period of 2009 through 2013, Mr. Lusti compared changes between the years, and came up with an average change per year of 10.72 percent as shown in DOC Ex. 442 DVL-S-46, Schedule 2. As a result, he calculated a test-year revenue requirement for property tax expense of $136 million, based on increasing 2013 property tax by 10.72 percent. As detailed in DOC Ex. 442 DVL-S-46, Schedule 1, and as shown in DOC Ex. 442 DVL-S-7, Column (f) (Lusti Surrebuttal), Mr. Lusti recommended that the test-year property tax be reduced by $14,000,000. DOC Ex. 442 at 29 (Lusti Surrebuttal).

335. As an alternative, Mr. Lusti recommended including data from both the Company's forecast of the 2013 property taxes identified earlier in this Surrebuttal Testimony and the Company's forecast of the 2014 property tax in this proceeding. He noted that the comparative forecast contained in Mr. Duevel's Rebuttal testimony and the June 2013 Estimate each were based on the same detail of information for their respective property tax years. DOC Exhibit 442 DVL-S-47 was the calculation of the DOC's Alternative property tax

recommendation for the test year of $141 million. The DOC's alternative recommendation began with Xcel's $150 million Minnesota Jurisdictional number, the amount recommended by Mr. Duevel in Direct Testimony. That amount was reduced by 2.95 percent (which was the reduction between Mr. Duevel's Direct Testimony calculation and the calculation included with his Rebuttal Testimony). That resulting amount was reduced by 3.15 percent (which is the difference between the June 2013 Estimate and the Actual 2013 property tax amount). This alternative property tax calculation is a test year amount of $141 million and a reduction of $9 million to Mr. Duevel's recommendation in Direct Testimony. DOC Ex. 442 at 30 (Lusti Surrebuttal).

336. Xcel agreed to this alternative recommendation of Mr. Lusti, of a reduction of $9 million in property tax expense for the 2014 Test Year, subject to a true-up for 2014 actual accruals and a cap at the $145 million Minnesota jurisdictional level, as discussed by Mr. Duevel in his Rebuttal Testimony. Xcel Ex. 140 at 2 (Heuer Opening Statement) DOC Ex. 451 at 1-2 and DVL-EH-7, Page 1 of 4, Column (f) (Lusti Opening Statement).

337. Mr. Lusti explained that Xcel accepted the Department's alternative proposal to set the 2014 test year property tax expense equal to $141 million on a Minnesota electric jurisdiction basis, subject to the true-up proposed by the Company and accepted by the Department. Under the true-up, the maximum 2014 test year property tax expense would be $145 million, as shown in Mr. Duevel's Rebuttal Testimony. There is no downward boundary on the 2014 test year property tax expense, so this expense could be lower than the $141 million. DOC Ex. 451 at 2 (Lusti Opening Statement).

338. The ALJ finds that this adjustment, as agree by Xcel and the Department, is reasonable.

339. The procedure for the property tax update is that the Company will file its year-end 2014 property tax expense with the Commission on January 16, 2014. The Company's year-end property tax expense will be based on Truth in Taxation Notices received in November and December of 2014. Under the proposal, the Commission would reflect the 2014 year-end property tax expense in its determination of the Company's 2014 revenue requirement and the 2014 year-end property tax expense would be reflected in final rates in this case, up to a cap of $145 million on a Minnesota electric jurisdiction basis. DOC Ex. 451 at 2 (Lusti Opening Statement).

340. The Company also agreed to make a compliance filing on June 30, 2015 detailing the actual 2014 property taxes reflected on final 2014 property tax statements received in the spring of 2015. To the extent that actual 2014 property taxes reflected on 2014 property tax statements (for the Minnesota Electric jurisdiction) are less than the Company's year-end 2014 property tax expense (for the Minnesota Electric jurisdiction), the Company will make ongoing, annual refunds of the difference between the Company's year-end 2014 property tax expense and the 2014 property taxes reflected on the final 2014 property tax statements. Xcel agreed that this refund obligation continues until the Company files its next rate case. DOC Ex. 451 at 2 (Lusti Opening Statement).

U. Foundation Administration Expense (Issue 40)

Resolved between DOC and Xcel: DOC agreed with Xcel's additional adjustment of $114,622 for Xcel Foundation Administration expenses. DOC Ex. 442 at 3-4 (Byrne Surrebuttal)(*citing* Xcel Ex. 90 at 10 (Heuer Rebuttal)); DOC Ex. 449 at 2 (Byrne Opening Statement); DOC Ex. 451 DVL-EH-7, column (g) (Lusti Opening Statement).

341. In its initial filing, Xcel provided a test year adjustment of $320,702 ($280,954 Minnesota Electric Jurisdiction) to eliminate Foundation Administration expenses from the 2014 test year. DOC Ex. 423 at 6 (Byrne Direct) (*citing* Xcel Initial Filing, Volume 4B, Tab A-40). Xcel thereafter proposed a second adjustment for Foundation Expense. While preparing its Response to DOC Information Request No. 1186 regarding Association Dues, Xcel discovered that it did not adjust the 2014 test year for non-labor Foundation expenses. Xcel stated:

> Fees paid to the Minnesota Council on Foundations (MCF) were included for recovery in the Association Dues adjustment (Volume 4B, Workpaper A21), because they were to be excluded through the Foundation Administration adjustment (Volume 4B, Workpaper A40). However, while responding to this information request, we also discovered only labor costs related to the Xcel Foundation were excluded through the Foundation Administration Adjustment. The 2014 Test Year should also exclude $114,622 in non-labor related Foundation costs, including the $4,729 in fees paid to the Minnesota Council on Foundations. The Company will include this adjustment in Rebuttal Testimony.

DOC Ex. 423 at 6 (Byrne Direct) (*citing* DOC Ex. 424 ACB-1 (Byrne Direct Attachments) (DOC IR 1186)).

342. Ms. Byrne accepted and included Xcel's additional adjustment of $114,622 for Xcel Foundation Administration expenses in her recommended adjustments, DOC Ex. 42 ACB-2 (Byrne Direct Attachments) assuming that Xcel's proposed adjustment was a Minnesota Electric Jurisdictional amount. DOC Ex. 423 at 6-7 (Byrne Direct). Xcel Witness Ms. Anne E. Heuer subsequently clarified that the $114,622 adjustment was indeed the Minnesota Electric Jurisdictional amount. DOC Ex. 427 at 3-4 (Byrne Surrebuttal)(*citing* Xcel Ex. 90 at 10 (Heuer Rebuttal)). As a result, this issue was resolved, and DOC agreed with Xcel's additional adjustment of $114,622 for Xcel Foundation Administration expenses. DOC Ex. 427 at 3-4 (Byrne Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement). The DOC's recommendation decreases the test-year administrative and general expense by $114,622, as shown in DOC Ex. 451 DVL-EH-7, column (g) (Lusti Opening Statement); DOC Ex. 442 at 31 (Lusti Surrebuttal).

343. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

V. Customer Care O&M Credits (Issue 24)

Resolved between DOC and Xcel: Xcel agreed to the DOC recommended amount to be included in the 2014 test year of $1,216,391. Xcel already built $713,249 of O&M Credits into

its base test-year budget, so the net adjustment was an increase in credits of $503,142. DOC Ex. 427 at 5-7 (Byrne Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement); DOC Ex. 451 DVL-EH-7, column (k) (Lusti Opening Statement).

344. Xcel's Customer Care consists of the following functions:

- *Billing Services*. Responsible for the production and delivery of billing statements, researching billing inquires and resolving customer issues, and receiving and posting all customer receipts.

- *Contact Center*. Responsible for the operation of the residential customer service and business solutions centers.

- *Credit and Collections.* Responsible for accounts receivable management, minimizing customer receivable write-offs and operation of credit contact centers.

- *Customer Operations*. Responsible for staff training, quality control, process efficiencies, operational management and reporting, resolving customer complaints, communications within the organization, customer policy and low-income programs.

- *Meter Reading and Field Collections*. Responsible for reading customer meters and performing field disconnection and collection activities.

Ex. 423 at 10 (Byrne Direct) (*citing* Xcel Ex. 71 at 4 (Gersack Direct)).

345. In response to Department discovery, Xcel provided historical Minnesota Electric Jurisdictional amounts of Customer Care Costs, including 2011 to 2013 actual expenses and approved test-year amounts, as summarized in DOC Ex. 424 ACB-4 (Byrne Direct Attachments) (DOC IR 1183); Ex. 423 at 11 (Byrne Direct). The Response showed that Customer Care O&M expenses have been relatively flat since 2010, (DOC Ex. 424 ACB-4 at Attachment B (Byrne Direct Attachments)) and that Xcel has over-recovered Customer Care O&M expenses every year, for a total over-recovery in excess of $3 million in 2011, 2012 and 2013, as shown in Ms. Byrne's Table 1 below:

Table 1: Test Year versus Actual Customer Care O&M Expenses 2011-2013, Minnesota Electric Jurisdiction

	Test Year/Allowed	**Actual**	**Over/(Under) Recovery**
2011	$32,294,770	$31,763,894	$530,876
2012	$32,294,770	$30,849,349	$1,445,421
2013	$32,414,464	$31,222,353	$1,192,111
3-Year Total	**$97,004,004**	**$93,835,596**	**$3,168,408**

Ex. 423 at 11 (Byrne Direct). Ms. Byrne testified that over-recoveries in the Meter Reading Director Business Area (Meter Reading Area) accounted for almost half of the Customer Care

O&M over-recoveries from 2011 to 2013, as summarized in DOC Ex. 424 at ACB-4 at Attachment B (Byrne Direct Attachments); Ex. 423 at 11 (Byrne Direct). When she analyzed the individual cost components within the Meter Reading Area, it became apparent that the Miscellaneous O&M Credits account was the specific driver, accounting for all but $416,287 of the over-recoveries from 2011 to 2013.[103] Ex. 423 at 12 (Byrne Direct).

346. In its Trade Secret Response to further Department discovery, Xcel explained that the Miscellaneous O&M Credits are credits to be paid by Xcel's automated meter reading vendor, Landis+Gyr (Cellnet); Ex. 425 at 12 (Byrne Direct)(*citing* DOC Ex. 426 ACB-5 (Byrne Trade Secret Direct Attachments) (DOC IR 1110). The reason the O&M credits created over-recoveries in the Meter Reading Area since 2011 is that Xcel did not provide sufficient credits to ratepayers through the Company's rates. Between 2011 to 2013, Xcel had under-estimated these credits to its test year expenses by approximately $2.75 million, shown in Ms. Byrne's Table 2.

Table 2: Test Year versus Actual O&M Credits 2011-2013
Minnesota Electric Jurisdiction[104]

	Test Year/Allowed	Actual Credits	Over/(Under) Recovery
2011	($546,070)	($1,300,355)	$754,285
2012	($546,070)	($1,702,199)	$1,156,129
2013	($635,173)	($1,476,880)	$841,707
3-Year Total	**($1,727,313)**	**($4,479,434)**	**$2,752,121**

DOC Ex. 424 ACB-4 at Attachment B (Byrne Trade Secret Direct Attachments). Ex. 423 at 13 (Byrne Direct). In further Department discovery, Ms. Byrne asked Xcel to provide:

A. an updated forecast of O&M Credits for the 2014 test year;
B. an update regarding Cellnet's performance;
C. a current schedule to completion of the Company's meter reading automation; and
D. a discussion as to whether Xcel's 2014 test year budget for O&M Credits is reasonable.

Ex. 423 at 13 (Byrne Direct); DOC Ex. 426 ACB-6 (Byrne Trade Secret Direct Attachments) (DOC IR 1184).

[103] ($97,004,004 total allowed Customer Care O&M 2011 to 2013 – ($1,727,313) total allowed credits 2011 to 2013) – ($93,835,596 Actual Cust. Care O&M 2011 to 2013 – ($4,479,434) total actual credits 2011 to 2013) = $416,287.

[104] These credits reduced the actual O&M expense. Since the allowed credits built into rates were less than actual credits, Xcel's test year expenses (and the resulting rates) were higher than actual total expenses. This fact contributed to the over-recovery of Meter Reading expenses, and therefore an over-recovery of total Customer Care O&M expenses, as shown in Table 2 above.

347. Ms. Byrne concluded that Xcel's argument that the increased credits were offset by other cost increases, is not reasonable, based on two rationales. First, the forecasted increase in other costs was less than the forecasted increase in the amount of credits ($278,740) built into the test-year. DOC Ex. 426 ACB-6 (Byrne Trade Secret Direct Attachments). Thus, Ms. Byrne concluded that Xcel still owes a credit to its ratepayers. DOC Ex. 423 at 15 (Byrne Direct). Second, total Customer Care O&M expenses from 2010 to 2013 fluctuated from an annual decrease of 4.25 percent to an annual increase of 3.45 percent. When Ms. Byrne removed the O&M Credits from historical actual Customer Care O&M expenses, total expenses from 2010 to 2013 were essentially unchanged; they fluctuated from a decrease of 1.55 percent to an increase of 0.96 percent. DOC Ex. 426 ACB-7 at 3 (Byrne Trade Secret Direct Attachments); DOC Ex. 423 at 15 (Byrne Direct). Both of these facts indicated that the O&M credits paid by Cellnet increased at a rate faster than the offsetting costs incurred by Xcel. DOC Ex. 423 at 16 (Byrne Direct).

348. For its 2014 test year, Xcel initially proposed a total Customer Care O&M budget of $32,300,501, including $713,249 in O&M Credits, on a Minnesota Electric Jurisdictional basis, as shown by DOC Ex. 424 ACB-4 at Attachment B (Byrne Direct Attachments); DOC Ex. 423 at 16 (Byrne Direct). The 2014 budget represented a 3.45 percent increase over 2013 actual Customer Care O&M expense and a 51.71 percent decrease in O&M Credits over 2013 actual credits. DOC Ex. 423 at 16 (Byrne Direct).

349. Based on the information provided by Xcel, Ms. Byrne concluded that Xcel had not shown its proposed 2014 O&M Credits to be reasonable, and that Customer Care O&M Credits would be higher than Xcel's 2014 budget of $713,249 but less than actual credits from 2011 to 2013. DOC Ex. 423 at 16 (Byrne Direct); DOC Ex. 427 at 5 (Byrne Surrebuttal).

350. Ms. Byrne recommended that the Commission require Xcel's 2014 test year O&M Credits to be set at the average O&M credits from 2010 through 2013. This adjustment captured the higher credit activity in recent years, but also included 2010, when the credits were significantly lower. This adjustment resulted in test year O&M Credits of $1,216,391, and a downward adjustment to total Customer Care O&M Expenses of $503,142 (Xcel had built $713,249 into its 2014 budget). DOC Ex. 426 ACB-7 (Byrne Trade Secret Direct Attachments). DOC Ex. 423 at 17 (Byrne Direct); DOC Ex. 427 at 5 (Byrne Surrebuttal).

351. In Rebuttal, Xcel agreed with the amount of the adjustment but not the averaging methodology Ms. Byrne provided in her Direct Testimony. Xcel Witness Mr. Michael C. Gersack stated that the Company accepted the recommended 2014 test-year O&M Credits of $1,216,391, since the Company's updated forecast for 2014 credits is close in amount, with Xcel's updated test-year forecast different from DOC's recommended test-year O&M Credits by only $1,359. DOC Ex. 427 at 5 (Byrne Surrebuttal) (*citing* Xcel Ex. 72 at 1 (Gersack Rebuttal)).

352. In her Surrebuttal Testimony, Ms. Byrne stated that, while Xcel and DOC continued to disagree on the rationale for the Customer Care O&M Credits adjustment, they agreed that the amount to be included in the 2014 test year is $1,216,391. Xcel already built $713,249 of O&M Credits into its base test-year budget, so the net adjustment was an increase in credits of $503,142. As a result, this issue was resolved. DOC Ex 427 at 5-7 (Byrne

Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement). The DOC's recommendation decreases the test-year customer service and information expense by $503,142, as shown in DOC Ex. 451 DVL-EH-7, column (k) (Lusti Opening Statement); DOC Ex. 442 at 31 (Lusti Surrebuttal).

353. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

W. Investor Relations (Issue 26)

Resolved between DOC and Xcel: Xcel accepted DOC's recommended additional downward adjustment of $78,140, as shown in DOC Ex. 424 ACB-3 (Byrne Direct Attachments); DOC Ex. 423 at 7-10 (Byrne Direct); DOC Ex. 427 at 4-5 (Byrne Surrebuttal) (*citing* Xcel Ex. 31 at 30 (Tyson Rebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement); DOC Ex. 451 DVL-EH-7, column (l) (Lusti Opening Statement).

354. Ms. Byrne addressed Xcel's test year expenses for Investor Relations not only in this 13-868 Docket, but also in Xcel's previous rate case, Docket No. E002/GR-12-961. DOC Ex. 423 at 7 (Byrne Direct). In the prior 12-961 rate case, Ms. Byrne concluded that Xcel failed to show that it was reasonable for ratepayers to bear all the costs of the Investor Relations department, and that the Company had not provided a means by which to assess the relative benefits (i.e., the extent to which such costs are incurred to support ratepayers). She concluded in Docket No. E002/GR-12-961 that the Commission should exclude 50 percent of Investor Relations expense from the 2013 test year expenses. DOC Ex. 423 at 7 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, DOC Ex. 164 at 18 (Byrne Surrebuttal)). In the 12-961 case, the ALJ stated:

> 522. The Company has demonstrated that investor relations costs generally benefit both ratepayers and shareholders. Some costs, however, such as the annual meeting are of no or partial benefit to ratepayers. Absent a more exact method of allocation, the Department's position to allow 50 percent of the investor relations costs is reasonable. This recommendation is consistent with the recommendation made by the Administrative Law Judge in the last rate case.

DOC Ex. 423 at 8 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, Findings of Fact, Conclusions of Law and Recommendations, issued July 5, 2013 at 108.) The Commission accepted the ALJ's recommendations without specifically addressing Investor Relations expense in its Order. DOC Ex. 423 at 8 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, Findings of Fact, Conclusions and Order, issued September 3, 2013 at Order Point 2).

355. In its initial filing in this current 13-868 rate case, Xcel proposed a 50 percent adjustment to Investor Relations expense, with one exception. Xcel's proposal adjusted investor relations costs to reduce the Minnesota electric jurisdictional expense by $385,000, by recovering 100 percent of the Minnesota electric jurisdictional portion on the stock registration fees ($156,000) plus 50 percent of all other investor relations costs. DOC Ex. 423 at 8 (Byrne Direct (*citing* Xcel Ex. 30 at 44 (Tyson Direct)).

356. Xcel's proposed adjustment was not consistent with the Commission's Order in the previous rate case to exclude 50 percent of investor relations expense from rates, and the record is devoid of evidence to support a greater recovery from ratepayers. DOC Ex. 423 at 9 (Byrne Direct). While Mr. Tyson provided over six pages of Direct Testimony regarding investor relations, Xcel Ex. 30 at 38-44 (Tyson Direct), his testimony was essentially verbatim from his testimony in Xcel's previous rate case DOC Ex. 423 at 9 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, Xcel Ex. 43 at 8-12 (Tyson Rebuttal)) and thus provided no new support for its adjustment, other than reasoning previously rejected by the Commission in the 12-961 Docket.

357. As a result, DOC concluded that some costs (such as the annual meeting) provide little to no benefit to ratepayers, and that Xcel has provided no reasonable basis for the Commission to reach a conclusion in this instant case differing from the Company's prior rate case. DOC Ex. 423 at 9 (Byrne Direct). Ms. Byrne recommended that the Commission require Xcel to remove 50 percent of the entire amount of Investor Relations costs of $926,007 on a Minnesota Electric Jurisdictional basis, as ordered in the Company's previous rate case. Xcel had already adjusted out $384,863 from its 2014 test year (Xcel's Initial Filing, Volume 4B, Tab A41, Workpaper A41-3) so she recommended an additional downward adjustment of $78,140, as shown in DOC Ex. 424 ACB-3 (Byrne Direct Attachments); DOC Ex. 423 at 10 (Byrne Direct).

358. In Rebuttal, Xcel Witness Mr. George E. Tyson II stated that while the Company continued to believe that all Investor Relations costs are appropriate parts of the costs of providing service, the Company accepted DOC's adjustment to limit the number of contested issues in this case. DOC Ex. 427 at 4-5 (Byrne Surrebuttal) (*citing* Xcel Ex. 31 at 30 (Tyson Rebuttal). As a result, this issue was resolved, with Xcel accepting DOC's recommended additional downward adjustment of $78,140, as shown in DOC Ex. 424 ACB-3 (Byrne Direct Attachments); DOC Ex. 423 at 10 (Byrne Direct); DOC Ex. 427 at 4-5 (Byrne Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement).

359. The DOC's recommendation decreases the test-year administrative and general expense by $78,140, as shown in DOC Ex. 451 DV-EH-7, column (l) (Lusti Opening Statement); DOC Ex. 442 at 31 (Lusti Surrebuttal).

360. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

X. Insurance – Surplus Distribution (Issue 16)

Resolved between DOC and Xcel. Xcel agreed to DOC's recommendation that the Commission require Xcel to credit 2014 test-year insurance expenses by the amount of the Nuclear Energy Insurance Limited (NEIL) and Energy Insurance Mutual (EIM) surplus distributions, for a total reduction to Xcel's test-year insurance expense on a Minnesota Electric Jurisdictional basis of $1,662,299. DOC Ex. 427 at 11, 26 (Byrne Surrebuttal); DOC Ex. 426 ACB-13 (Byrne Trade Secret Direct Attachments); DOC Ex. 425 at 27 (Byrne Trade Secret Direct); DOC Ex. 449 at 2 (Byrne Opening Statement). The DOC's recommendation decreases the test-year administrative and general expense by $1,662,299, as shown in DOC Ex. 442 DVL-

S-7, column (m) (Lusti Surrebuttal); DOC Ex. 442 at 32 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-7, column (m) (Lusti Opening Statement).

361. Ms. Byrne investigated and testified regarding the topic in Xcel's last rate case, Docket No. E002/GR-12-961. DOC Ex. 423 at 22 (Byrne Direct). In Xcel's previous rate case, in light of increasing premiums for various insurance policies, Ms. Byrne requested that Xcel provide, in Direct Testimony in its next rate case:

> … information explaining: the basis for such increases, the degree of such increases, and the particular measures by which Xcel has mitigated increasing insurance costs. At a minimum, this information should include a description of coverage for each type of policy the Company holds, the amount of coverage under each policy, what the Company has done to mitigate rising costs, and a discussion as to whether shareholders receive any benefits from each policy, and the relative benefits for ratepayers and shareholders.

DOC Ex. 423 at 22 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, DOC Ex. 162 at 43 (Byrne Direct)). In his Rebuttal Testimony, in the 12-961 Docket, Xcel Witness Mr. George E. Tyson agreed to provide this information in the Company's next initial rate case filing. DOC Ex. 423 at 22 (Byrne Direct) (*citing* Docket No. E002/GR-12-961, Xcel Ex. 43 at 16-17 (Tyson Rebuttal).

362. Xcel provided the information in this 13-868 rate case in compliance with the agreement. Mr. Tyson discussed the relative benefits of each of the primary types of insurance, including Master Property, Excess Liability, Directors' and Officers' (D&O), Fiduciary, Nuclear Insurance, and Primary Casualty. Xcel Witness Mr. Michael R. Anderson discussed insurance selection, procurement and availability, as well as premium costs, in detail.

363. Ms. Byrne requested further information, and Mr. Anderson stated the following:

> [B]y utilizing Associated Electric and Gas Insurance Services (AEGIS), EIM and NEIL, we are able to obtain insurance for difficult to place risks. These industry mutual pools are, in many ways, the only reasonably available insurers for these types of risks. As an industry mutual pool, these entities seek to set their pricing based on concepts of mutuality and fairness. Consequently, we believe that the premiums we pay to our industry mutual insurance pools are per se reasonable. Further, to the extent that the premiums collected in any given year are greater than were necessary, all of these pools utilize mechanisms to allow for the return of excess funds as may be appropriate in the form of surplus distributions or continuity credits.

DOC Ex. 423 at 23 (Byrne Direct) (*citing* Xcel Ex. 35 at 17 (Anderson Direct)).

364. Ms. Byrne requested that Xcel provide information on the excess funds that may be distributed from the insurance pools, including information on frequency of distributions, actual distributions from 2009-2013, the accounting of these distributions, and whether any

distributions were included in the 2011, 2013, or current 2014 test years. DOC Ex. 425 at 23 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-11 (Byrne Trade Secret Direct Attachments) (DOC IR 1107)). In its response, Xcel stated:

> As discussed in the Direct Testimony of Company Witness Michael Anderson, our industry insurance pools may utilize mechanisms to allow for the return of excess funds as may be appropriate in the form of surplus distributions of continuity credits. These mechanisms take different forms such as surplus distributions in the case of NEIL and EIM; continuity credits from AEGIS, and the Industry Credit Insurance Program (ICRP) from American Nuclear Insurers (ANI).

DOC Ex. 425 at 24 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-11 (Byrne Trade Secret Direct Attachments) (DOC IR 1107)). Xcel further stated that NEIL surplus distributions were relatively regular from 1987 through 2008 but, after the economic downturn in 2008, the Company received only one distribution, in 2011, for the 2010 year. In addition, a distribution was announced in September 2013 for the 2013 premium year (April 2013 to April 2014), which the Company expected to receive as a credit to the premiums due April 1, 2014. Xcel also stated that if the Company were to receive a distribution from NEIL for the 2014 premium year, it would be notified of the pending distribution in the fourth quarter of 2014. DOC Ex. 425 at 24 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-11 (Byrne Trade Secret Direct Attachments) (DOC IR 1107)).

365. Regarding the EIM surplus distributions, Xcel stated that the distributions were irregular, and in 2012 Xcel received its only distribution since 2009. In addition, a distribution for the 2013 premium year was announced in February 2014. Xcel stated that this 2014 distribution would be amortized over the remainder of the policy year (August 2013 to August 2014) as a deduction in costs to EIM coverage. DOC Ex. 425 at 24 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-11 (Byrne Trade Secret Direct Attachments) (DOC IR 1107)). Further, the credits received from AEGIS directly decreased premiums paid by the Company, and the refunds under ICRP were received by check annually in July. DOC Ex. 425 at 24 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-11 (Byrne Trade Secret Direct Attachments) (DOC IR 1107).

366. Xcel stated that NEIL and EIM surplus distributions are not included in the 2014 test year because these recent distributions have been irregular. DOC Ex. 425 at 25 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-11 (Byrne Trade Secret Direct Attachments)). The amounts of the NEIL and EIM surplus distribution for the 2013-2014 premium period were set out in Ms. Byrne's Testimony at DOC Ex. 426 ACB-11 at 2 (Byrne Trade Secret Direct Attachments)), as well as the amount allocated to the Minnesota Electric Jurisdiction, at DOC Ex. 426 ACB-13 (Byrne Trade Secret Direct Attachments); DOC Ex. 425 at 25 (Byrne Trade Secret Direct).

367. Ms. Byrne explained that it was not reasonable for Xcel to exclude the NEIL and EIM credits from the 2014 test year because, first, actual insurance premiums Xcel paid in 2013 for the Minnesota Electric Jurisdiction were $18,324,079, which was $1,708,544 lower than the

$20,032,623 of authorized insurance premiums built into the 2013 test year. DOC Ex. 425 at 25-26 (Byrne Trade Secret Direct) (*citing* DOC Ex. 426 ACB-12 at Attachment A (Byrne Trade Secret Direct Attachments)(DOC IR 1108)). The main driver of this over-recovery from ratepayers is the NEIL and EIM surplus distributions announced in September 2013 and February 2014, which Xcel, in its Response to DOC IR 1107, expected to receive as a credit to premiums in 2014. But for these surplus distributions, ratepayers would have paid almost exactly what Xcel incurred in insurance premiums, rather than overpaying by $1.7 million. DOC Ex. 423 at 26 (Byrne Direct).

368. Second, Xcel Witness Mr. Anderson argued that insurance premiums paid by Xcel were reasonable, in part, because of the potential for the insurance pools to return excess funds in the form of surplus distributions or continuity credits. Xcel Ex. 35 at 17 (Anderson Direct). Ms. Byrne disputed this position, pointing out that it is not reasonable for Xcel to state that its insurance premiums recovered by ratepayers are reasonable in part due to excess funds returned by the insurance pools, when a majority of those excess funds are not returned to ratepayers. DOC Ex. 423 at 26 (Byrne Direct).

369. Last, and most important, ratepayers pay 100 percent of the insurance premiums that Xcel incurs in the course of providing utility service. It is only reasonable that Minnesota ratepayers receive the benefits of these surplus distributions that they paid for, rather than allowing the Company's shareholders to keep the refunds. DOC Ex. 423 at 26 (Byrne Direct).

370. Ms. Byrne explained that the NEIL distribution was announced in September 2013 for the April 2013 to April 2014 premium year, and the EIM distribution was announced in February 2014 for the August 2013 to August 2014 premium year. Xcel had both 2013 and 2014 forecasted rate case test years, yet Xcel proposed not to return the NEIL and EIM distributions to ratepayers in either test year. Because these distributions will be applied to premiums paid within Xcel's 2014 test year, and for the other reasons discussed above, the DOC concluded that Xcel's proposed insurance expenses are unreasonable, since the distributions should be included in Xcel's 2014 test year. DOC Ex. 423 at 26-27 (Byrne Direct).

371. DOC recommended that the Commission require Xcel to credit 2014 test year insurance expenses by the amount of both the NEIL and EIM surplus distributions. DOC Ex. 423 at 27 (Byrne Direct). The reduction to Xcel's test-year insurance expense was $1,662,299, as shown in DOC Ex. 425 ACB-13 (Byrne Trade Secret Direct Attachments); DOC Ex. 425 at 27 (Byrne Trade Secret Direct)

372. In his Rebuttal Testimony, Xcel Witness Mr. Michael R. Anderson agreed with the DOC adjustment, stating that, since the NEIL and EIM distributions were received prior to the closing of the record in this case, the Company agreed that it was appropriate to include the distributions as an offset to Xcel's 2014 test year budget. In her Surrebuttal, Ms. Byrne agreed that this issue was resolved, with Xcel agreeing to the DOC recommendation to credit 2014 test year insurance expenses by the amount of both the NEIL and EIM surplus distributions. DOC Ex. 423 at 27 (Byrne Direct); DOC Ex. 427 at 11 (Byrne Surrebuttal). The reduction to Xcel's test-year insurance expense was $1,662,299, as shown in DOC Ex. 426 ACB-13 (Byrne Trade

Secret Direct Attachments); DOC Ex. 425 at 27 (Byrne Trade Secret Direct) DOC Ex. 449 at 2 (Byrne Opening Statement).

373. The DOC's recommendation decreases the test-year administrative and general expense by $1,662,299, as shown in DOC Ex. 451 DVL-EH-7, column (m) (Lusti Opening Statement); DOC Ex. 442 at 32 (Lusti Surrebuttal).

374. The ALJ finds that this adjustment, as agreed by Xcel and the Department, is reasonable.

Y. Emissions Control Chemicals for 2014 and 2015 (Issue 15 and Issue 33)

Resolved between Xcel and the Department: For 2014, Xcel accepts DOC's adjustment of a $2.265 million reduction on a Minnesota jurisdictional basis to emission chemicals costs. DOC understands that the Company also agrees not to recover the emission chemical costs via the FCA. For 2015, Xcel and DOC resolved this issue by agreeing to a $1.4 million reduction as an appropriate level of emissions costs in 2015, (which is a 50 percent of DOC's $2.8 million reduction stated in Ms. Campbell's Surrebuttal Testimony).[105]

375. Ms. Campbell explained in detail the Company's historical pattern of over-recovering costs of emission control chemicals from ratepayers even after the Commission accepted the Department's proposed reductions to Xcel's projected test-year amounts.[106] Specifically, even with those Department-recommended downward adjustments, Ms. Campbell testified, "the Company still managed to over-recover emission chemical costs in every single year since 2009."[107] Further, the Department opposed Xcel's suggestion that it recover emission chemical costs through the Fuel Clause Adjustment (FCA).[108] Among the reasons that FCA recovery is not reasonable is Ms. Campbell's observation is that there would be no real cost containment protection:[109]

> [A]utomatic flow through of any cost does not properly incent the Company to keep costs low and work to mitigate costs, since costs included in the FAC are simply passed on to ratepayers.

The Department recommended a reduction of $2.265 million on a Minnesota jurisdictional basis for 2014, and a reduction of $2.8 million for 2015 that is related specifically to mercury sorbent costs for Sherco 1 and 2 (that will come back on line in 2015 after an extended outage to install mercury sorbent injection equipment), and includes Xcel's agreement with Ms. Campbell that 2015 emissions costs for the A.S. King plant and Sherco 3 are not related to the 2015 Step and should be removed.[110]

---

[105] DOC Ex. 450 at 2 (Campbell Opening).
[106] DOC Ex. 435 at 21 (Campbell Public Surrebuttal).
[107] *Id.*
[108] *Id.* at 27.
[109] DOC Ex. 435 at 27 (Campbell Public Surrebuttal).
[110] DOC Ex. 435 at 28 (Campbell Public Surrebuttall).

376. Xcel witness Mr. Mills testified that the Sherco 1 and 2 will use mercury sorbent with the two plants' "wet" scrubbers rather than use the dry scrubber systems at Sherco 3 and King, and use of the emission chemical with wet scrubbers will be a new experience for the Company.

377. In his Opening Statement, Mr. Mills stated the following regarding the reasonableness of a reduction of 50 percent of the Department's 2015 proposed reduction of $2.8 million:[111]

> Further, based on discussions with the Department the Company is proposing an adjustment equal to half of Ms. Campbell's proposed adjustment for our 2015 Step request related to mercury sorbent costs for Sherco 1 and 2. . . . *The Company believes this is a reasonable resolution to this contested issue given our lack operating experiences with the set-scrubber emissions control technology being deployed at Sherco 1 and 2 and the uncertainty surrounding it.* It is my understanding that the Department supports this proposal.

378. The Department agrees with Xcel that for purposes of this rate case, based on this record, that Xcel's proposed reduction of $1.4 million (50 percent of $2.8 million) is reasonable.

379. The DOC's recommendation decreased the test-year power production expense by $2,265,000, as shown in DOC Ex. 451 DVL-EH-7, Page 2 of 4, Column (p) (Lusti Opening Statement); DOC Ex. 442 at 32 (Lusti Surrebuttal).

380. The ALJ finds that the Department's recommendation is reasonable.

Z. Nuclear Fees for 2014 (Issue 25)

Resolved between Xcel and the Department: Based on the NRC's 2014 final fee rule, DOC recalculated its adjustment for total nuclear fees from $2.55 million reduction to $1 million, on a Minnesota jurisdictional basis. Xcel accepts DOC's reduction of $1 million to nuclear fees.[112]

381. Xcel included $35.2 million in proposed 2014 nuclear fees, which is an 11.9 percent more than the Company actually incurred in 2013.[113] It stated that the largest driver of the increase related to the Federal Emergency Management Agency/State Emergency Preparedness (FEMA/State EP), as well as expected increases in the fees of at least five other entities, including the NRC.[114]

---

[111] Xcel Ex. 125 at 1 (Mills Opening).
[112] DOC Ex. 450 at 2 (Campbell Opening); Xcel Ex. 123 at 1 (O'Connor Opening).
[113] DOC Ex. 429 at 68, 72 (Campbell Public Direct).
[114] DOC Ex. 435 at 68-69 (Campbell Public Surrebuttal).

382. The Department's analysis of Xcel's testimony and discovery responses as to each nuclear fee at issue showed a pattern of over-recovery from ratepayers, as summarized by Ms. Campbell, as follows:

> [T]he Company has not provided sufficiently support its proposed 11.9 percent increase in nuclear fees and dues from 2013 actuals to the 2014 test year. Beyond the sheer magnitude of the increase, another reason why these arguments are not persuasive is that the Company made similar arguments in its last rate that were not borne out in practice. In fact, despite the Department-recommended and Commission-approved downward adjustment of $1.4 million in the prior rate case, the Company still over-recovered these costs by $1.2 million ($24.7 million less $23.5 million) in rates for 2013. [FN omitted] DOC Ex. 430 at NAC-13 (Campbell Direct).

Ms. Campbell provided a chart of each fee with test-year and actuals for each year 2011 through the estimated 2014 test-year. Based on its analysis, the Department recommended a 1.1 percent annual increase consistent with past trends between 2011 and 2013 actuals, for 2014 test-year reduction of $2.55 million, on a Minnesota jurisdictional basis (as corrected by the Company in its Rebuttal Testimony).[115]

383. Mr. O'Connor showed in his Rebuttal Testimony that the NRC issued a final rule that is effective in August 2014, regarding an increase in its NRC fee (per reactor, and hourly). Accordingly, the Department accepted Xcel's NRC fee test-year budget. As to other nuclear fees, however, Ms. Campbell did not agree that the Company demonstrated likely fee increases as high as Xcel proposed. Acceptance of the NRC fee amount reduced the Department's recommended reduction in nuclear fees to $1 million for the 2014 test-year.[116]

384. In his Opening Statement, Mr. O'Connor stated that the Company accepted Ms. Campbell's Surrebuttal Testimony recommendation.[117]

385. The DOC's recommendation decreases the test-year power production expense by $1,000,000 as shown in DOC Ex. 451 DVL-EH-7, column (v) (Lusti Opening Statement); DOC Ex. 442 at 32 (Lusti Surrebuttal).

386. The Department's recalculated adjustment for total nuclear fees from $2.55 million reduction to $1 million, on a Minnesota jurisdictional basis, is reasonable.

---

[115] DOC Ex. 429 at 72, 75 (Campbell Public Direct) (Xcel's Ms. Heuer pointed out in her Rebuttal Testimony that Ms. Campbell's $2.55 million adjustment was the Minnesota jurisdictional number rather than a lower reduction, $1.9 million, that she calculated in her Direct Testimony at 75. Xcel Ex. 90 at 27-28 (Heuer Rebuttal).
[116] DOC Ex. 435 at 62-64 (Campbell Public Surrebuttal).
[117] Xcel Ex. 123 at 1 (O'Connor Opening Statement).

AA. Bargaining Unit Wage Increase (Issue 42)

387. The Company noted that the 2014 test year included a 3.0 percent wage increase for bargaining unit employees. The union ratified a new agreement with a 2.6 percent wage increase after the filing of this rate case. In Rebuttal, the Company proposed a corresponding adjustment to the test year to reduce wages by $405,000. Xcel Ex. 90 at 41 (Heuer Rebuttal).

388. The DOC's recommendation decreases the test-year administrative and general expense by $405,000, as shown in DOC Ex. 451 DVL-EH-7, column (aa) (Lusti Opening Statement). DOC Ex. 442 at 33 (Lusti Surrebuttal).

389. The ALJ finds that the Department's recommendation is reasonable.

BB. Total Labor for 2014 (Paid Leave) (Issue 7)

Disputed between Xcel and the Department: Xcel failed to show the reasonableness of its 2014 total labor costs. Based on the fact that 2013 actual total labor costs were abnormally high due to nuclear plant outages and a high number of storms which resulted in the 12.2 percent increase over 2012, and also based on a historical annual trend of 2-3 percent increases, DOC recommends a normalized 3 percent annual increase in labor costs by increasing 2012 total labor costs by 3 percent for 2013, and then increasing 2013 normalized total labor costs by 2 percent for 2014.[118]

Resolved between Xcel and the Department: DOC agrees with Xcel that the Commission should evaluate total labor costs of which paid leave is a component.[119]

390. The Department now agrees that paid leave costs are appropriately considered as compensation within the context of total labor costs. Ms. Campbell first examined Xcel's paid leave request as a component of employee benefits, and believed that Xcel had not addressed the issue in its Direct Testimony on employee benefits nor in response to Ms. Campbell's discovery despite a test-year request of nearly $50 million.[120]

---

[118] DOC Ex. 450 at 4 (Campbell Opening).

[119] Tr.V. 5 at 33 (Campbell). DOC does not agree, however, with Xcel's argument that the Commission should evaluate Xcel's total O&M budget as a whole and should not address particular components of O&M costs such as total labor costs that do not appear to be supported by the Company. *See* Xcel Ex. 87 at 9-13 (Stitt Rebuttal).

[120] *Id.*; *see* DOC Ex. 435 at 71-74 (Campbell Public Surrebuttal); DOC Ex. 429 at 95-96 (Campbell Public Direct). Ms. Campbell identified in her Direct Testimony a significant (19.4 percent) estimated increase for 2014 over 2013 actual paid leave expense. *Id.* at 97-98. She also noted Xcel's pattern of actual over-recovery from ratepayers of paid leave: $5.1 million for 2011 and $3.6 million for 2012, and $3.98 million for 2013. *Id.* The Department's initial recommendation was an estimated 3.7 percent increase over 2013 actuals, for a downward adjustment on a Minnesota jurisdictional basis of $6.556 million based on a projection of 2014 paid leave of $43.350 million. *Id.* at 98.

391. The focus now is whether Xcel showed the reasonableness of its estimated total labor costs for the 2014 test-year. Xcel explained in Rebuttal Testimony that its "paid leave" costs were addressed under "paid time off" in the Labor section of Ms. Stitt's Direct Testimony, and that paid time off is a component of compensation rather than benefits, and stated that review of paid leave should occur within the larger context of employee compensation, to which the Department agrees.[121]

392. Xcel did not show the reasonableness of estimated 2014 test-year total leave costs of $419.4 million. The Company experienced abnormally high 2013 actual labor costs of $436.2 million—a 12.2 percent increase over 2012 actuals—due in part to longer-than-planned nuclear plant outages at Monticello and Prairie Island, and an unusually high number of storms in 2013. While Xcel estimates that its 2014 test-year total labor costs will be lower than 2013 actuals, the Company has not shown that its test-year amount is reasonable: Xcel seeks an increase from 2012 actuals of 7.8 percent, which equals an annualized (year over year) increase from 2012 actuals of 3.9 percent – nearly 4 percent. The Company did not detail the basis for its 3.9 percent annualized increase amount for the 2014 test year other than that its total labor actuals "track very closely to budget over the last three years," that Xcel experienced in 2012 an actual increase of 3 percent over 2011 actuals, and its claim that its budgeting process is reasonable and deviations of actuals from budgeted numbers do not show that a change to Xcel's estimated 2014 total labor costs is warranted.[122]

393. The Company's 2014 test-year total labor recommendation is not supported. Xcel relies in part on its aberrant 2013 year – that occasioned a 12.2 percent increase over 2012 actuals -- to support Xcel's 2014 test-year request even though the Company makes no claim that its total labor costs going forward are likely to be abnormally high. That is, Xcel doesn't claim that it is likely to experience an unusual number of storms, abnormally longer-than-planned nuclear outages, or some other factor that would render 2014 likely not to be a normal year. The Company highlights its budgeted sums for the years 2011 to 2013 while ignoring the fact that actual 2013 costs were abnormally high and, thus, should not be used for comparison purposes. For example, in its Issues List at page 11 of 69, Xcel relies in part on the anomaly of 2013 actuals in its criticism of the Department's recommended adjustment to Xcel's estimated 2014 total labor costs of $5.6 million, as follows:[123]

> The Company's actual Total Labor costs exceeded the budget *for the period from 2011 and 2013*, and the increases in Nuclear and Business Systems Total Labor costs alone account for virtually all of the Department's proposed adjustment of $5.6 million.

Xcel's criticism is misplaced. Clearly, the numbers Xcel relies on for the above comparison includes the bloated abnormal 2013 total labor costs.

---

[121] Xcel Ex. 87 at 8 (Stitt Rebuttal). While the Department notes that in its last rate case, MPUC Docket No. 12-961, Ms. Stitt referred to these costs under the term "Paid Leave," the Department appreciates the Company's clarification. *See id.* at 5-7.

[122] DOC Ex. 435 at 71-74 (Campbell Public Surrebuttal); Xcel Ex. 87 at 2-13 (Stitt Rebuttal).

[123] (Emphasis in italics added).

394. The Department's $5.6 million adjustment to Xcel's 2014 test-year request, on a Minnesota jurisdictional basis, is calculated to render a 3 percent increase in total labor costs from 2011 to 2014. The basis of the 3 percent figure is two pronged: 1) Ms. Campbell's testimony that, in her experience, a 2 to 3 percent annual increase in total labor for a normal year is reasonable, and 2) her analysis showing that Xcel really did incur a 3 percent increase in total labor costs from 2011 to 2012.[124]

395. Actual total labor costs incurred for 2013 must be disregarded since that increase from 2012 to 2013 was abnormally high and, thus, is not representative of likely 2014 or years beyond. Stated another way, Xcel made no claim that total labor costs in 2014 and years beyond are likely to be abnormally high. Thus, the Department applied a 3 percent increase to 2012 actuals in order to calculate a 2013 normalized figure of $400.6 million (on an NSPM Electric basis), and applied a 3 percent increase to the 2013 normalized amount to arrive at its recommended 2014 normalized estimate of $412.6 million (on an NSPM Electric basis).[125] Ms. Campbell included the following table in her Surrebuttal Testimony to show the 3 percent normalized basis of the Department's 2014 test-year recommendation:[126]

Total Labor Costs in $(millions) for NSPM Electric

	2011 Actual	2012 Actual	DOC 2013 Normalized	DOC Revised 2014
Labor Costs	$377.7	$388.9	$400.6	$412.6
Year-to-Year Change		3% increase	3% increase	3% increase

396. The Department acknowledges that Xcel's proposed 2014 test-year of $419.4 million (on an NSMP Electric basis) equates to a normalized increase from 2012 actuals of approximately 3.9 percent,[127] which is approximately one percent higher than Ms. Campbell's recommendation of a 3.0 percent normalized increase. One percent, however, represents real money that Xcel claims to be needed from real ratepayers. The fact that positions of the parties may be close does not justify Xcel's additional 0.9 percent increase.

397. Doubt goes to the ratepayer, and Xcel's 0.9 percent overage is not supported. Further, one percent of the Xcel's very large test-year request of $419.4 million, represents $6.4 million more on an NSPM Electric basis, or an additional $5.6 million on a Minnesota jurisdictional basis, than the record supports. Ratepayers should not be required to pay an additional $5.6 million without Xcel's first proving that it is a reasonable estimate of the 2014 test-year total labor expense for a normal year, which Xcel did not do.

---

[124] DOC Ex. 435 at 72-73 (Campbell Public Surrebuttal).
[125] DOC Ex. 435 at 73 (Campbell Public Surrebuttal).
[126] *Id.*
[127] $419.4 - $388.9 = 30.5; 30.5/388.9 = 0.0784 or 7.8 percent.

398. For the reasons discussed, the Department recommends a 3 percent annual increase in total labor costs above the Company's 2012 actual total labor costs, to determine a normalized level for 2013, and then a 3 percent increase over 2013 normalized costs to determine a reasonable 2014 test year amount for total "Revised 2014" labor costs of $412.6 million, from Xcel's test-year request, on an NSPM Electric basis. The difference is a $6.4 million reduction in total labor costs for 2014 on an NSPM Electric basis; using the Minnesota Jurisdictional allocator of 87.572 percent (as used by Ms. Stitt for 2014 on her Schedule 3(a) page 1 of 2 of her Direct Testimony) results in an adjustment of $5.6 million reduction on a Minnesota Jurisdictional basis.[128]

399. The DOC's recommendation decreases the test-year administrative and general expense by $5,600,000, as shown in DOC Ex. 451 DVL-EH-7, column (w) (Lusti Opening Statement); DOC Ex. 442 at 33 (Lusti Surrebuttal).

400. The ALJ agrees and finds the Department's recommendation to reduce total labor costs for 2014 by $5.6 million on a Minnesota Jurisdictional basis to be reasonable.

CC. Depreciation Reserve for Nuclear Plant – XLI Proposal (Issue 75)

Disputed between XLI and Xcel, the Department and OAG: DOC agrees with Xcel and the OAG that XLI's proposal to reduce 2014 and 2015 rates by using nuclear production plant depreciation reserve is not supported, and should not be granted.[129]

401. XLI witness Mr. Pollack testified that Xcel miscalculated the nuclear theoretical depreciation reserve such that the figure is not $72 million a Minnesota jurisdictional basis but that the corrected amount of $208 million in theoretical nuclear depreciation reserve should be amortized over 5 years. Essentially, XLI claims, as it did in Xcel's most recent rate case, that Xcel has over-collected depreciation costs from current ratepayers with respect to the nuclear production plants, Prairie Island and Monticello. Mr. Pollack acknowledged that the Commission in Xcel's most recent rate case declined to order amortization of theoretical nuclear depreciation reserve surplus.[130]

402. The Department does not support expansion of the use of amortization of theoretical depreciation reserve surplus (if any) beyond the Commission's action in the last Xcel rate case, which appropriately excluded nuclear plant depreciation reserve. Specifically, Ms. Campbell opposes use of a supposed surplus in theoretical nuclear depreciation reserves because "this short-term rate reduction would be short sighted and would result in higher rates for ratepayers in the long run." Key to XLI's proposal is a dispute over the remaining lives of Xcel's nuclear plant. Thus, Ms. Campbell urged the Commission not to ignore the useful lives of the nuclear facilities, as studied and determined in 1) the annual and five-year depreciation

---

[128] DOC Ex. 450 at 4 (Campbell Opening); DOC Ex. 435 at 69-74 (Campbell Public Surrebuttal).
[129] DOC Ex. 450 at 11 (Campbell Opening).
[130] XLI Ex. 264 at 1-2 (Pollack Opening); XLI Ex. 260 at 10 (Pollack Public Direct); *see* 2013 Xcel Rate Case Order at 29.

studies and 2) the integrated resource plan regarding, and thus, not to recalculate those remaining lives in this rate case based on theoretical information. XLI's proposed theoretical depreciation reserve "give back" is not reasonable.[131]

403. The record in this case does not show that ratepayers have overpaid depreciation expense in the past for nuclear facilities, as suggested by XLI. Specifically, Ms. Campbell explained that XLI's claim of past overpayment is incomplete and incorrect; the claim is focused only on past depreciation, and does not consider what is occurring during the current rate case in the 2014 test year and 2015 step year and what is expected over the remaining lives of the nuclear facilities. She testified that it is not reasonable to conclude that there is a surplus in nuclear depreciation reserve, particularly in light of Xcel's request for significant recovery regarding the abandoned Prairie Island EPU, as well as the Company's requested recovery for the Monticello EPU. Thus, Ms. Campbell reasonably concluded based on this record that "it is difficult to conclude that ratepayers have over paid nuclear depreciation in the past." For these reasons, the Department recommends that the Commission not approve XLI's theoretical nuclear depreciation reserve proposal.[132]

404. The ALJ agrees that XLI's proposal to reduce 2014 and 2015 rates by using nuclear production plant depreciation reserve is not reasonable.

DD. Sales Forecast (Issue 13)

Resolved: DOC agreed with Xcel to use actual 2014 data to establish the 2014 weather-normalized test year sales and rates along with the relevant sales for the known and measurable change to the test year for the LCI class. DOC Ex. 444 at 1 (Shah Opening Statement); Xcel Ex. 119 at 1-2 (Hyde Opening Statement).

Resolved: Xcel agreed with DOC to use the Department's coefficients for the calculation of weather-normalized actual sales. DOC Ex. 444 at 1 (Shah Opening Statement); Xcel Ex. 119 at 1-2 (Hyde Opening Statement).

Resolved: DOC agreed with Xcel's proposal to submit, in addition to the five months of data already in the record, six additional months of data, and the related revenue calculations on December 16, 2014 (DOC Ex. 444 at 1 (Shah Opening Statement)); and to submit its December 2014 actual sales data no later than January 16, 2015. Xcel Ex. 140 at 5 (Heuer Opening Statement).

Disputed: The Company proposed, in the alternative, to submit forecasted December sales data in its December 2014 filing. Xcel Ex. 140 at 5 (Heuer Opening Statement). If the Commission

[131] DOC Ex. 434 at 2-4 (Campbell Rebuttal). Ms. Campbell noted in her Opening Statement at 11 her disagreement with Mr. Lindell's characterization in his Opening Statement of the Department's position. Mr. Lindell's statement, Tr.V.3 at 190-191 (Lindell), could be interpreted incorrectly to suggest that the Department supports XLI's theoretical nuclear depreciation reserve proposal, which it does not. *Id.*

[132] DOC Ex. 434 at 3-4 (Campbell Rebuttal).

uses any forecasted data in the test-year sales forecast, the Commission should use the Department's updated forecast as the basis for determining the test-year revenue requirements. DOC Ex. 444 at 1 (Shah Opening Statement).

405. The Department generally concluded that, because the Company's initially-filed forecast is unreasonable, the Commission should set rates using entire actual 2014 test year data when it is available and weather-normalization calculations from the Department's models. DOC Ex. 404 at 29-30 (Shah Direct); DOC Ex. 406 at 19-20 (Shah Surrebuttal). The Company accepted this recommendation. DOC Ex. 444 at 1 (Shah Opening Statement); Xcel Ex. 119 at 1-2 (Hyde Opening Statement).

1. Overall

406. Department Witness Sachin Shah assessed the reasonableness of the Xcel sales forecast. Based on his analysis, Mr. Shah accepted as reasonable the Company's rebuttal proposal to use actual 2014 data to establish the 2014 weather-normalized test year sales and rates along with the relevant sales for the known and measurable change to the test year for the LCI class. Mr. Shah recommended that the Commission accept the Company's proposal to use actual 2014 data for establishing rates in this proceeding. DOC Ex. 404 at 29-30 (Shah Direct); DOC Ex. 406 at 4, 9, 11, 20 (Shah Surrebuttal). The Commission should set rates using the entire actual 2014 test year data when it is available based on weather normalized actual sales for the the following customer classes: Residential without Space Heat, Residential with Space Heat, and Small Commercial and Industrial, using the weather normalization calculations from the Department's models. DOC Ex. 406 at 14, 15, 17, and 19 (Shah Surrebuttal).

407. Further, the Department concluded that the Company's coefficients are unreasonable; instead, the Company accepted the Department's recommendation to use the Department's coefficients for the calculation of weather-normalized actual sales. DOC Ex. 444 at 1 (Shah Opening Statement) Xcel Ex. 119 at 1-2 (Hyde Opening Statement).

408. Based on Company Witness Ms. Heuer's opening statement during the evidentiary hearing, Mr. Shah also generally agreed with Xcel regarding the process for actual data to be added to this proceeding, noting that the record already included actual data for the five months of January through May, 2014 (Xcel Ex. 40 JEM-2 at Schedules 1 through 6 (Marks Rebuttal)) so the Company will only need to provide an additional six months of actual data, as Xcel proposed, on December 16, 2014. DOC Ex. 444 at 1 (Shah Opening Statement).

409. Mr. Shah explained that he had one potential concern regarding Ms. Heuer's proposal that, "In the alternative, the Company would agree to submit *forecasted* December sales data in its December 2014 filing." Xcel's initial filing proposed using forecasted data for its test-year sales forecast. Mr. Shah explained that, to the extent that there is even one month of forecasted data used in the test-year sales forecast, the issues he found regarding Xcel's initially-filed sales forecasts remain unresolved and Mr. Shah's alternative proposal for forecasted data would need to be used for December 2014 sales, including the forecasted values from the Department's forecast, rather than the Company's updated forecast. DOC Ex. 444 at 1. (Shah Opening Statement.)

410. Mr. Shah further recommended that, in the event that use of actual data for the entire 2014 test year is not approved by the Commission, as an alternative, the sales used in this rate proceeding should be based on updated actual sales (actual billing month data with embedded DSM already built in) and customer data through May 2014 and the Department's model, instead of NSP's initial or updated estimates of its sales volumes and revenues. DOC Ex. 406 at 19 (Shah Surrebuttal). This alternative recommendation results in a sales volume of 30,937,253 MWh, and monthly average customer counts of 1,250,030 for 2014. DOC Ex. 406 at 20 (Shah Surrebuttal). The overall impact of this alternative recommendation, based on these adjustments is an increase in NSP's total revenues of approximately $43,228,000, as shown on DOC Ex. SS-S-3 (Shah Surrebuttal); DOC Ex. 406 at 21 (Shah Surrebuttal).

411. Mr. Shah generally supported the Company's estimates of sales for the Public Street Highway Lighting (PSHL), Other Public Authority (OPA) and Interdepartmental classes, but he raised concerns in his Direct Testimony about the Company's forecast energy sales and customer counts for various rate classes. Further, an adjustment to Xcel's initial forecast test-year sales was needed because, in general, both forecasted and historical test years should be based on "normal" conditions, with adjustments made for known and measurable changes. Mr. Shah's Direct Testimony explained that, at a minimum, the historical sales level proposed by Xcel needed to be adjusted to reflect sales that would occur under "normal" weather since, in general, weather is typically the most significant factor affecting some rate classes. Ultimately, because of these and other concerns, Mr. Shah recommended that Xcel's forecast be updated using the most recent actual historical data available. DOC Ex. 404 at 3, 24-25, and 31 (Shah Direct).

412. In summary, the Department recommended that the Commission accept the Company's proposal to use actual data and to include the addition of the known and measurable 2015 sales for the LCI class. If the Commission uses any forecasted data in the test-year sales forecast, the Commission should use the Department's updated forecast, not Xcel's, as the basis for determining the test-year revenue requirements. DOC Ex. 444 at 1. (Shah Opening Statement.)

2. Disagreement as to Forecasted December Sales.

[This section 2 is relevant only if Xcel's sales forecast is used to estimate sales in December.]

413. Reasonable sales forecasts are an essential part of the rate-making process. Test-year sales volumes are important factors in calculating a utility's revenue requirement because sales levels affect both revenues and expenses. In general, because sales levels are an integral input in calculating a utility's rates, the method of determining the sales levels must be reasonable. DOC Ex. 404 at 1-2 (Shah Direct). In addition, test-year sales volumes are essential to the Class Cost of Service Study (CCOSS), Rate Design issues, and the Company's Conservation Improvement Program (CIP) because, when designing rates, test-year sales volumes are used to allocate costs in the CCOSS which is in turn used as a benchmark comparison to establish the revenue apportionment. Moreover, when establishing final rates, the test-year sales volumes are used to determine the overall revenue requirements as well as the individual tariff rates and in calculating the Conservation Cost Recovery Charge (CCRC). DOC Ex. 404 at 2 (Shah Direct).

414. The forecast methodology that Xcel used in this rate case, generally, was that the Company forecasted customer counts and energy sales using econometrics models. For its econometrics modeling, NSP used monthly historical energy use and customer count data from January 1998 through June 2013 for all classes, except the Large Commercial and Industrial (LCI) class, for which the customer count forecast model used historical data from February 2001 through June 2013.

415. Mr. Shah had the following concerns with Xcel's input data and forecasting techniques:

a. Xcel's price variable in the Residential without Space Heat (Res w/o H) class and the Small Commercial and Industrial (SCI) class;

b. Xcel's Demand-Side Management (DSM) in the Residential without Space Heat, Residential with Space Heat (Res w/H), SCI and Large Commercial and Industrial (LCI) Classes; and

c. Xcel's customer count calculations.

DOC Ex. 404 at 8 (Shah Direct).

a. Concerns with the price variable

416. Mr. Shah had two general concerns about Xcel's price variable: (1) Xcel used a price variable derived from revenues that are subject to the interim rate mechanism, which inflated the price variable while rate case refunds provided contradictory price information; and, (2) Xcel used a price variable that in part consists of revenues from customer charges and other charges, which inflated the per-unit price. DOC Ex. 404 at 10-11 (Shah Direct). Despite these concerns, Mr. Shah did not recommend excluding the price variable in this case, because excluding this explanatory variable from the model produced sales results that appeared to be unreasonable. For example, if the price variable were excluded, total sales in the 2015 test year[133] would have amounted to approximately 31,430,465 MWh, an increase of approximately 4.39 percent over Xcel's initial filed amount of 30,108,800 MWh. DOC Ex. 404 at 11 (Shah Direct). This increase would have been too high compared to historical growth. For example, according to Company witness Ms. Marks, Xcel's total retail weather normalized sales grew approximately 0.7 percent per year between 1998 and 2012. DOC Ex. 404 at 11 (Shah Direct) (*citing* Xcel Ex. 38 at 12 (Marks Direct)).

417. Mr. Shah concluded his Direct Testimony with a recommendation that the Commission require Xcel in the future to work with the Department and other stakeholders to determine if Xcel can improve its price variable or other aspects of their sales forecasting models. DOC Ex. 404 at 11 (Shah Direct). Xcel's Ms. Marks agreed with Mr. Shah's recommendation, and specifically agreed that "using the price variable improves the overall

[133] Excluding the known and measurable amount discussed below regarding LCI class sales.

results. We will work with the Department to determine if any improvements can be made." DOC Ex. 406 at 11 (Shah Surrebuttal) (*citing* Xcel Ex. 40 at 17 (Marks Rebuttal)).

b. Concerns with Xcel's demand side management (DSM) adjustments.

418. Mr. Shah was concerned about Xcel's DSM adjustments and concluded that a better methodology--one that would not introduce uncertainty in the DSM adjustment--would be to use the billing month data that already encompasses any embedded DSM. DOC Ex. 404 at 17-18 (Shah Direct).

419. Mr. Shah indicated that, for two reasons, he was concerned that a DSM adjustment as proposed by the Company would underestimate test-year sales and therefore improperly increase the revenue deficiency. First, Mr. Shah was concerned that Xcel's DSM adjustments are estimates, the use of which would introduce uncertainty since it would require another layer of forecasting for the level of estimates. Mr. Shah concluded that the appropriate approach, which would not introduce more uncertainty in the DSM adjustment, was to use billing month data because historical DSM efforts are already reflected in these sales data used in the forecast. DOC Ex. 404 at 11-18 (Shah Direct). More importantly, Mr. Shah concluded that a DSM adjustment was not needed because Xcel's yearly DSM savings are not increasing; to the contrary, they appear to be decreasing. DOC Ex. 404 at 18-21 (Shah Direct). He concluded that a better approach would be to use the billing month data that already encompasses any embedded DSM. DOC Ex. 404 at 17-18 (Shah Direct).

i. The methodology Xcel used to make its DSM adjustment makes it less certain that the sales forecast will be accurate.

420. First, as to the methodology Xcel used, Mr. Shah explained that, to account for future DSM impacts, Xcel used a different methodology in this rate case, which involved subtracting estimated DSM effects from sales; Mr. Shah testified that the new methodology makes it less certain that the sales forecast will be accurate. DOC Ex. 404 at 12, 13 (Shah Direct). Xcel described its new methodology as follows:

> We collected monthly historical data on actual DSM achievements. We then added the historical DSM achievements to historical actual monthly sales to derive a time series of data excluding any DSM impacts. This restated time series was used as the input data to the regression modeling process described above, and a forecast of sales excluding any DSM impacts was developed. We then *reduced the forecast of sales excluding DSM by the amount of future DSM related to both historical achievements with continuing impacts and planned future new programs.*
>
> We believe our year-to-date actual sales are closely tracking with our 2013 test year forecast in Docket No. E002/GR-12-961, supporting the appropriateness of making a DSM adjustment. However, the approach proposed in this proceeding

to account for the impacts of DSM is a more transparent methodology and provides similar results.

. . .

We determined that the Company's DSM achievements, especially in recent years, have lead to lower sales growth than otherwise would have occurred. This can be seen in Figure 2 below, which compares historical billed sales for the Residential without Space Heat class both with and without DSM adjustments. It is clear that the lack of sales growth since the recession is due to the impacts of DSM programs. By adding back DSM before constructing the regression model, we were able to define a better relationship between sales and the underlying predictor variables.

DOC Ex. 404 at 12-13 (Shah Direct) (*citing* Xcel Ex. 38 at 32-35 (Marks Direct)(emphasis added).

421. Mr. Shah explained, first, that the effects of DMS on sales are not actual, but estimated amounts, because meters measure how much energy a customer uses, but cannot measure how much the customer didn't use due to DSM. As a result, it is necessary to estimate how much DSM affects sales. Since the goal is to estimate sales, Xcel's approach of adjusting the sales data before any regression analysis is done requires a high degree of rigor to avoid biases. DOC Ex. 404 at 13 (Shah Direct). Mr. Shah testified that he was concerned about Xcel's methodology.[134] He pointed out, as an example, that in the month of January 1998 for the Res w/o H class, the Company estimated historical DSM in the amount of 1,870.65 MWh. In its response to DOC IR No. 504, for the same month and class, however, the Company re-estimated historical DSM in the amount of 411.54 MWh, stating:

Differences in the values of the historical DSM impacts for the Residential and Commercial and Industrial classes are due to a re-estimation of these impacts by the DSM Strategy and Planning Department. The re-estimation is the result of increasing the level of detail used for calculating the lifetime of DSM measures, which we incorporated into the model.

DOC Ex. 404 at 14 and (SS-6) (Shah Direct). Because of his concerns about Xcel's adjustments, Mr. Shah asked the Company to explain all of the DSM changes between Xcel's initial filing and the DSM update in IR 504 and to provide a detailed explanation with calculations showing how Xcel re-estimated the impacts. DOC Ex. 404 at 14-15 (Shah Direct). Xcel explained that:

[b]etween the time of the rate case pre-filing on October 3, 2013 and the supplemented pre-filing submitted on April 9, 2014 in response to the Department of Commerce's Information Request No. 504, three changes

[134] Xcel calculated and provided its DSM adjustments in its prefiled data. DOC Ex. 404 at 13 and SS-5 (Shah Direct) [Xcel's response to DOC Information Request Nos. 1, 2 and 9]. It also provided its DSM adjustments in its responses to DOC Information Request No. 504. DOC Ex. 404 at 13 and (SS-3) (Shah Direct).

> occurred in how the impacts of historical, existing, and future DSM were calculated. These changes are:
>
> 1) Verification of data: The initial forecast included all available data records regarding implementation of historical DSM programs. We subsequently determined that some of the data should be omitted, since it could not be verified at the program level. In addition, and as described in part 2 below, we updated the DSM calculation as it pertains to measuring the lifetimes. The Company used either the planned program lifetime (as filed in an approved CIP plan) or a proxy value of one year for verified savings for programs with an unknown lifetime....

DOC Ex. 404 at 15 and (SS-6) (Shah Direct) (*quoting* Xcel Response to IR 508). This significant change in the estimated historical DSM raised concerns for Mr. Shah about Xcel's approach in estimating the effects of DSM to the degree required in sales forecasts. The response points out some sources of uncertainty about Xcel's estimates of the effects of DSM on the sales data, such as how to estimate the effects of DSM measures over the life of the DSM improvement. Mr. Shah noted that, if Xcel's method of subtracting the effects of DSM on energy sales was used, it would be necessary for the estimated effects of DSM to be highly accurate over the lives of DSM measures. Xcel's response shows that in the future, the estimated historical DSM numbers could be subject to change, which could call into question the validity of the rates set in the rate case. DOC Ex. 404 at 13-14 (Shah Direct).

422. Mr. Shah also explained that Xcel's data tends to overestimate the effects of DSM on sales, resulting in underestimated sales, as can be seen, for example, by comparing historical actual sales (which include the effects of DSM) to Xcel's estimated DSM-adjusted sales. DOC Ex. 404 at 16 (Shah Direct). In Xcel's initial filing, for the last 6 months of 2013 (July through December) Xcel *estimated* approximately 6,788,658 MWh Calendar Month Sales adjusted for DSM on a weather normalized basis for the SCI class. DOC Ex. 404 at 16 and SS-5 (Shah Direct) (Xcel Response to DOC IR 9) and SS-7 (Xcel Response to DOC IR 19). Xcel's *actual* Calendar Month weather-normalized sales (which include the actual effects of DSM) for the same period and class, however, were approximately 6,850,293 MWh. DOC Ex. 404 at 16 and SS-3 (Shah Direct) (Xcel Response to DOC IR 504). Xcel's estimated sales of 6,788,658 MWh overestimated the effects of DSM on sales compared to actual sales of 6,850,293 MWh, which included the actual effects of DSM on sales. In other words, the Company's DSM adjustment underestimated sales for this particular period and class.

423. In response to an IR, Xcel provided information on the financial impact on Xcel of its DSM adjustments to sales.[135] Xcel stated that:

> Attachment A to this response provides MWh sales by class for 2014 and 2015 before adjusting for the impacts of planned future new demand-side management

[135] Xcel calculated the impact in Attachment A to its Response to Minnesota Chamber of Commerce Information Request No. 101. DOC Ex. 404 at (SS-8) (Shah Direct).

> (DSM) programs. Please see the Direct Testimony of Company witness Ms. Jannell Marks, page 33, beginning at line 7 for a description of the methodology used to develop the sales forecast. The information provided in Attachment A is the forecast of sales excluding any DSM impacts less the amount of future DSM related to historical achievements with continuing impacts.
>
> Attachment A also provides the MWh sales with and without making DSM impacts by class for 2014 and 2015. The resulting DSM sales numbers are then multiplied by average present rates to determine the revenue impact of 2014 and 2015 DSM. *The total actual impact of DSM in 2014 and 2015 is $48.6M and $73.0M, respectively.* The revenue impact is estimated using class average seasonal base rates excluding customer charge related revenue.

DOC Ex. 404 at 16-17 and (SS-8) (Shah Direct)(emphasis added). In addition to this impact, the testimony of DOC Witness Christopher T. Davis regarding DSM financial incentives indicates that Xcel has received incentives ranging from about $40 million to $54 million annually in recent years. DOC Ex. 404 at 17 (Shah Direct).

424. Mr. Shah reiterated that these DSM adjustments are estimates, and if the regression models were performed on sales data that Xcel adjusted by using estimates, then the model results do not reflect actual sales data. Xcel's approach created another source of uncertainty because it required another layer of forecasting for the level of estimates. DOC Ex. 404 at 17 (Shah Direct).

425. Mr. Shah concluded that the appropriate approach, which would not introduce this uncertainty in the DSM adjustment, is to use the billing month data that already encompasses any embedded DSM. DOC Ex. 404 at 17- 18 (Shah Direct). Mr. Shah stated that use of actual data for sales would lessen the uncertainty associated with determining what DSM adjustments would occur because any dispute over the calculation of historical and future DSM values may be resolved by implicitly using the DSM that is already built in the billing month data. DOC Ex. 404 at 29 (Shah Direct). Such a method would be consistent with the Commission's determinations in the last Xcel's rate case, 12-961. There, the Commission adopted the ALJ determination that a DSM adjustment would under-estimate test-year sales and should not be applied to the sales forecast:

> The Commission concurs with the Department that Xcel has not shown the reasonableness of a DSM adjustment in this case. A DSM adjustment would underestimate test-year sales for several reasons. First, historical DSM efforts are already reflected in the sales data used in the forecast. Second, data provided by the Department show that Xcel's yearly DSM savings are leveling off, rather than increasing. Finally, Xcel's sales forecast with the DSM adjustment is consistently lower than actual data for five out of the last six months of 2012. For these reasons, the Commission will adopt ALJ Finding 252, revised as follows:
>
>> 252. As shown by the Department, the Company has not proven the reasonableness of a DSM adjustment in this proceeding. The inclusion of

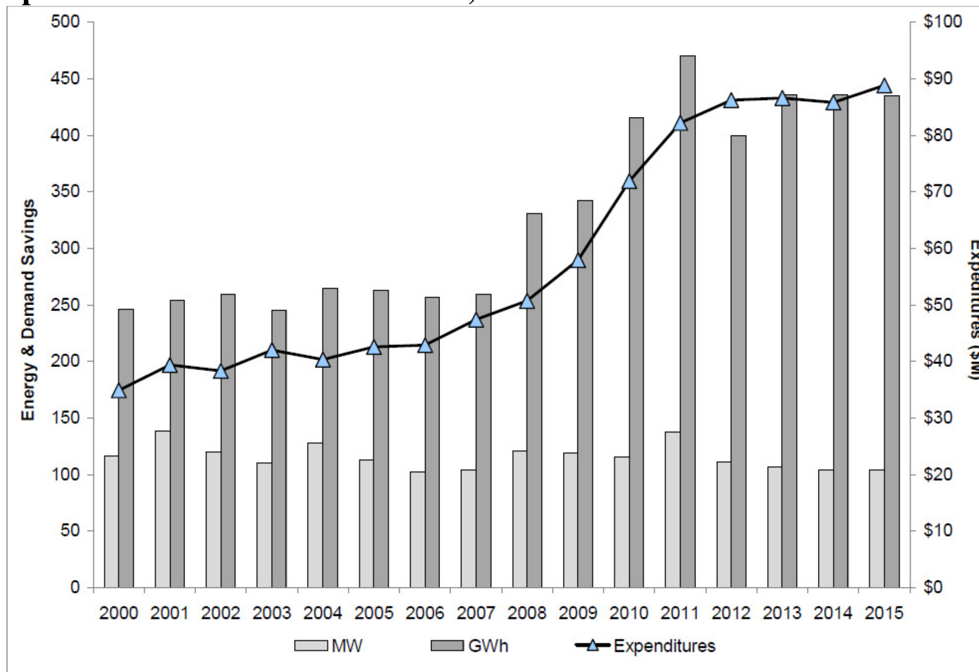
a DSM adjustment will under estimate test-year sales and should not be applied to the sales forecast in this proceeding.

ii. DSM savings are not increasing.

426. Mr. Shah was concerned that the DSM adjustment as proposed by Xcel is not needed because Xcel's yearly DSM savings are not increasing; instead, they appear to be decreasing. DOC Ex. 404 at 18-21 (Shah Direct). The Department had a similar concern in Xcel's last rate case. In the Department's initial brief in 12-961,[136] the Department demonstrated that Xcel's DSM levels were leveling off:

> As illustrated in the graph below, which is taken from the Company's most recent conservation improvement program (CIP) Triennial filing (Docket No. E,G002/CIP-12-447), Xcel pursued increased electric conservation on Xcel's Minnesota system after the enactment of the Next Generation Energy Act (NGEA) in 2007. The most relevant information in the graph is the series of bars showing actual (2000 – 2011) and forecasted (2012 – 2015) gigawatt hours (GWh) since these figures correspond to reductions in sales that the Company claims are due to or will be due to energy conservation programs.

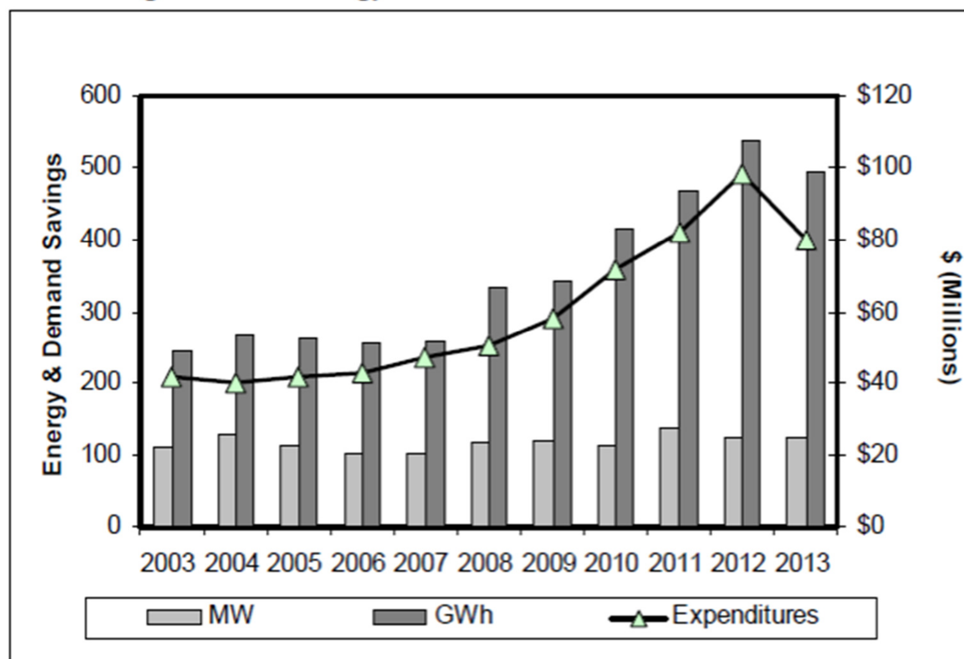
Graph 3: CIP Electric Achievements, Actual and Forecasted 2000-2015



[136] 12-961, Department Initial Brief, filed May 15, 2013 at *https://www.edockets.state.mn.us/EFiling/edockets/searchDocuments.do?method=showPoup&documentId={85FA3559-D901-45EF-84FB-0472A0109C0C}&documentTitle=20135-87028-03.*

427. As a result, the Department concluded in 12-961 that there was no need for an additional adjustment for DSM in the test year. DOC Ex. 404 at 19 (Shah Direct). That trend has continued: Xcel's recent CIP status report, filed on April 1, 2014, indicates that Xcel's expenditures on DSM had decreased. DOC Ex. 404 at 20 (Shah Direct).

Figure 1: Xcel Energy's 2003-2013 Electric CIP Achievements



The Department continues to conclude that it is inappropriate to adjust for DSM outside of the sales forecast model – whether by the after-the-fact method Xcel used in the prior 12-961 rate case or by the before-the-fact method Xcel proposes in this case. DOC Ex. 404 at 20 (Shah Direct).

428. Mr. Shah provided one further comment regarding the need for an accurate forecast, even where full decoupling is recommended and thus, Xcel would recover its allowed revenue no matter the reason for the variation in actual revenue. He explained that even with an approved revenue decoupling mechanism, the test-year sales forecast is an important part of the rate case, because a reasonable estimate of test-year sales is necessary to apportion cost and revenue properly and determine the appropriate level of revenue requirements to serve as a basis for future decoupling adjustments; and because the sales forecast is a key element to determine the appropriate amount of revenue, overall, that the Company would collect from ratepayers through the decoupling mechanism. DOC Ex. 404 at 21 (Shah Direct). For this reason, Mr. Shah explained, it is important to set the baseline forecast appropriately in the rate case.[137]

[137] Mr. Shah noted that, going forward, however, the level of uncertainty (with regards to, for example, the level of DSM that typically would be appropriate) would be rendered moot; as Xcel would recover the allowed revenue no matter the cause of variation in the actual revenues. DOC Ex. 404 at 21 (Shah Direct).

429. In its Response to Mr. Shah's concerns regarding the Company's DSM adjustment, Xcel continued to take the position that, if the Commission uses forecast data, then the Commission should adopt the Company's sales forecast, which includes adjustments for DSM. DOC Ex. 406 at 10 (Shah Surrebuttal) (citing Xcel Ex. 40 at 14 (Marks Rebuttal). The Company agreed, however, to the use of actual data, and therefore no DSM adjustment would be needed:

> Mr. Shah and I are in general agreement that the increased use of actual data to develop a sales forecast for 2014 will be beneficial to all Parties' efforts to set rates based on the most accurate forecast possible. ... in this proceeding, the schedule could allow the use of actual data, which would mean that the Commission would not need to determine the appropriate DSM adjustment.

DOC Ex. 406 at 11 (Shah Surrebuttal) (citing Xcel Ex. 44 at 6-7 (Hyde Rebuttal)).

430. Mr. Shah concluded that this issue was resolved to the extent that the Commission uses actual sales data, because the appropriate approach, which does not introduce uncertainty in the DSM adjustment, is by using the billing month data that already encompasses any embedded DSM. Mr. Shah explained that because Xcel agreed to use actual 2014 data, the Commission would not need to determine the appropriate DSM adjustment, and the issue of adjusting for DSM outside of the sales forecast model is rendered moot when using actual 2014 data for the 2014 test year. DOC Ex. 406 at 11 (Shah Surrebuttal).

c. Concerns with Xcel's customer counts.

431. In his Direct Testimony, Mr. Shah analyzed Xcel's initial filings regarding customer counts and concluded that the customer counts that Xcel used in its initial filing understated the numbers of customers on Xcel's system.[138] DOC Ex. 404 at 24 (Shah Direct). In his Direct Testimony, Mr. Shah recommended an adjustment to Xcel's forecast, based in part on an increase in customer counts between the Company's initial filing and a later discovery response. DOC Ex. 404 at 25 (Shah Direct).

432. Regarding the model used by the Company, Mr. Shah noted that for the Res w/o H, SCI, PSHL and OPA rate classes, the models are the same as those Xcel used in the 2012 rate case. DOC Ex. 404 at 23 (Shah Direct). In that 2012 case, (July 2012 to December 2013), when actual customer counts were compared to Xcel's projections, Xcel's model underestimated the number of customers in every single month. DOC Ex. 404 at 23 (Shah Direct).

433. Similarly, in this 13-868 docket, Mr. Shah reported that a comparison of Xcel's initial projections (July 2013 to December 2013) with the actual number of customers followed a

[138] Mr. Shah noted Ms. Marks' testimony that Xcel did not change the methodology the Company used in the 12-961 docket and did not adopt the Department's recommendation to use an averaging approach. DOC Ex. 404 at 21-23 (Shah Direct) (citing Xcel Ex. 38 at 35-37 (Marks Direct)).

similar pattern. DOC Ex. 404 at 23 and (SS-9) (Shah Direct). In supplemental data provided in Xcel's Response to DOC IR No. 504 in this 13-868 docket, Xcel projected adding on average 6,330 more customers in 2014 than were identified in Xcel's initial filing; in 2015, Xcel projected adding on average 10,121 customers more than it identified in Xcel's initial filing. DOC Ex. 404 at 25 and SS-9 (Shah Direct). In his Direct testimony, Mr. Shah criticized Xcel's failure to provide accurate initial customer count information and Xcel's stated plan "to make available to parties more current information as the case progresses through Rebuttal or Surrebuttal Testimony or both." DOC Ex. 404 at 23 (Shah Direct) (quoting Xcel Ex. 38 at 20 (Marks Direct)). Mr. Shah explained that Xcel's failure to provide accurate customer count data, and plan to support revising its sales forecast in its Rebuttal and Surrebuttal is not reasonable because revising a sales forecast is a comprehensive process that is difficult, if not impossible, to accomplish in a rate case.[139] DOC Ex. 404 at 24 (Shah Direct).

434. In his Direct Testimony, Mr. Shah observed that when the matter comes before the Commission, Xcel should have actual 2014 sales. He explained that he expected to examine actual sales data as that information became available[140] and, because he lacked access to accurate actual data, to provide the Department's final recommendation and conclusions in his Surrebuttal Testimony, after receiving actual sales and customer data through the most recent month available from Xcel. DOC Ex. 404 at 24 (Shah Direct).

435. In its Response, the Company agreed that it understated customer counts. Xcel Witness Ms. Marks stated:

> Mr. Shah concludes that the customer-count forecast the Company used in its initial filing understated the number of customers on Xcel Energy's system. His preliminary results used customer counts the Company provided in response to Information Request (IR) DOC-504.
>
> *I agree that the customer-count forecast in the initial filing is lower than the actual customer counts for January 15 through May 2014.* As I discussed in the Updated Forecast section, this is due to an under-estimation of households in the Minneapolis-St. Paul area. The Updated Forecast that I have presented has corrected for this under-estimation by using revised household data and an updated household forecast. *I recommend that* the Updated Forecast be used to

[139] Mr. Shah contrasted Xcel's proposal to update its forecast method with the practice in rate cases to examine updates to sales *data*, often in both rebuttal (utility) and surrebuttal (party) testimonies. He explained that in such updates, only the historical and future data involved in forecasting is updated to include the most recent values, a process that is relatively easy to conduct which improves the quality of forecasting.

[140] Mr. Shah noted that the Department received from the Company actual and weather normalized sales for January through March 2014 at approximately 6:00 PM on June 2nd, 2014 (two working days prior to the submission date of Mr. Shah's Direct Testimony). DOC Ex. 404 at 24 and (SS-3) (Shah Direct).

> set rates in this proceeding or, in the alternative, that *weather-normalized actual sales be used as Ms. Hyde describes in her Rebuttal Testimony.*

DOC Ex. 406 at 9 (Shah Surrebuttal) (*citing* Xcel Ex. 40 at 17-18 (Marks Rebuttal) (emphasis added)). Xcel's agreement to use to weather normalized actual sales data resolved Mr. Shah's concerns with the customer counts. He stated:

> The Company and Department have recommended using actual 2014 data for the 2014 test year. Because actual counts will be available, there are no more concerns regarding the level of customer counts that should be forecasted for the 2014 test year. In addition, the Company's updated forecast predicts on average 5,489 customers more than it initially filed, and actual data up to May 2014 were incorporated in the customer forecast. In Xcel's response to DOC IR No. 512, Xcel provides a detailed explanation and description of its proposal.

DOC Ex. 406 at 9-10 and SS-S-1 (Shah Surrebuttal).

EE. Conservation and Decoupling (Issues 58 and 50)

Conservation issues:

Resolved between DOC and Xcel: DOC and Xcel agree on issues of both the amount of conservation dollars and the recovery of the conservation dollars outside of the rate case through the existing annual true up mechanism. DOC Ex. 447 at 1 (Davis Opening Statement). The Commission should:

1. Accept Xcel's 2013-2015 combined electric and gas CIP, as approved by the Deputy Commissioner of the Department in Docket No. E,G002/CIP-12-447, as satisfying the filing requirement specified in Minn. Stat. § 216B.241, subd. 1 for conservation improvement plans and rate case filings.

2. Approve the zeroing out of Xcel's CCRC when Xcel's new rates go into effect and recovery of all CIP costs through the CAF.

3. If the Commission does not approve the zeroing out of Xcel's CCRC and recovery of Xcel's CIP costs through the Company's CAF, then Mr. Davis recommended that the Commission approve Xcel's proposed test-year CIP expenses of $90,715,761 and approve Xcel's proposed volumetric CIP cost allocation method. DOC Ex. 417 at 39-40 (Davis Direct).

Decoupling Issues:

Resolved between DOC and Xcel: First, any decoupling mechanism should be a three-year pilot program. Second, under a revenue decoupling mechanism, Xcel would not surcharge customers in the year after the Company fails to achieve energy savings equal to 1.2 percent of retail sales. Third, there would be no cap on refunds to customers under the decoupling mechanism. Fourth, Xcel agreed to DOC's suggested modifications to the Company's

evaluation plan, and Xcel will include in the annual RDM evaluation plan "a comparison of how revenues from traditional regulation would have differed from those collected under partial and full decoupling" among other things. DOC Ex. 417 at 23, 40 (Davis Direct). DOC Ex. 419 at 2 (Davis Surrebuttal); DOC Ex. 447 at 1 (Davis Opening Statement); Xcel Ex. 110 at 2-3 (Hansen Rebuttal).

Disputed between DOC and Xcel: DOC recommends that the Commission conclude that Xcel has not demonstrated the reasonableness of its decoupling proposal, where Xcel has not shown its proposed partial decoupling proposal to be consistent with Xcel's statutory obligation to not harm ratepayers in connection with implementation of decoupling. DOC Ex. 447 at 1-2 (Davis Surrebuttal);

Disputed between DOC and Xcel: The DOC contends that Xcel has not shown the reasonableness of its proposed five percent "soft" cap. The decoupling mechanism would be reasonable only if the cap is adjusted to have a hard cap on surcharges of no greater than 3 percent of total customer group revenue, including fuel and all applicable riders. DOC Ex. 417 at 46 (Davis Direct); Xcel Ex. 110 at 10 (Hansen Rebuttal); DOC Ex. 419 at 2-6 (Davis Surrebuttal).

1. Recovery of Conservation Improvement Program Expenses (Issue 58)

436. As required by Minn. Stat. §216B.16, subdivision 1, Xcel has an approved conservation improvement plan filed with the Department.[141] DOC Ex. 417 at 2 (Davis Direct). Thus, Mr. Davis recommended that the Commission find Xcel's conservation plan adequate under Minn. Stat. §216B.16, subd. 1, and accept Xcel's 2013-2015 combined electric and gas CIP, as approved by the Director of the Department in Docket No. E,G002/CIP-12-447 (the CIP Plan), as satisfying the filing requirement of Minn. Stat. § 216B.241, subd. 1 regarding conservation improvement plans and rate case filings. DOC Ex. 417 at 2 (Davis Direct).

437. Xcel requested recovery of almost $91 million in CIP expenses. DOC Ex. 417 at 3 (Davis Direct). Xcel Witness Ms. Heuer stated that Xcel's proposed test-year CIP expenses are at levels consistent with the CIP Plan. DOC Ex. 417 at 3 (Davis Direct) *(citing* Xcel Ex. __ at 34 (Heuer Direct). Mr. Davis confirmed that Xcel included $90,715,761 in 2014 test-year expenses for CIP funding, DOC Ex. 417 at 3 (Davis Direct) and that Xcel correctly estimated the approved CIP costs for 2014. DOC Ex. 417 at 3 (Davis Direct).

438. Xcel also proposed an alternative method to collect CIP costs. Utilities may recover costs of energy conservation improvements, by including them in rates as a Conservation Cost Recovery Charge (CCRC), as authorized by Minn. Stat. § 216B.16, subd. 6b(a), which states:

[141] Docket No. E,G002/CIP-12-447, approved by the Director of the Department on October 1, 2012.

> … investments and expenses of a public utility as defined in section 216B.241, subdivision 1, paragraph (i), incurred in connection with energy conservation improvements shall be recognized and included by the commission in the determination of just and reasonable rates as if the investments and expenses were directly made or incurred by the utility in furnishing utility service.

439. In a rate case, when CIP expenses are included in test-year expenses, a Conservation Cost Recovery Charge (CCRC) is calculated, generally, by dividing the Commission-approved test-year CIP expenses by the Commission-approved test-year sales. DOC Ex. 417 at 4 (Davis Direct).

440. Mr. Davis explained that rates are adjusted for changes in CIP costs that occur after rates are approved in a rate case. Unlike the statutory treatment of most other utility expenses, which are not changed between rate cases, utilities may recover changes in CIP expenses through an annual recovery mechanism. Minn. Stat. §216B.16, subd. 6b(c) states that the Commission "may permit a public utility to file rate schedules providing for annual recovery of the costs of energy conservation improvements." CIP expenses are accounted for by using a "tracker," which is an accounting mechanism to accumulate annual expenses for future recovery purposes. This special ratemaking treatment is intended to encourage utilities to invest in energy conservation. DOC Ex. 417 at 4 (Davis Direct).

441. Not only does the tracker keep track of changes in CIP costs, the Commission allows utilities to change rates to recover increases or decreases in CIP costs between rate cases. DOC Ex. 417 at 4 (Davis Direct), through a CIP Adjustment Factor (CAF), also known as a Conservation Cost Recovery Adjustment (CCRA). DOC Ex. 417 at 5 (Davis Direct).

442. Xcel Witness Michael A. Peppin discussed Xcel's alternative proposal to collect CIP costs:

> As an alternative, the Company proposes to zero out the CCRC and recover all CIP program costs through the CAF. Since the allocation of the two components is now the same, there is not a need to separate the recovery. In addition, removing the CCRC from base rates would simplify CIP Exempt customer accounting and the calculation of the Company's proposed revenue decoupling mechanism. The Company is interested in other stakeholder input on this alternative proposal.

Xcel Ex. 102 at 33 (Peppin Direct).

443. The DOC supported Xcel's alternative proposal. Mr. Davis testified that, given that the CCRA allows Xcel to annually true-up its total CIP expenditure recovery (the amount recovered through both the CCRC and the CCRA), and given that Xcel no longer allocates its CIP costs using two different methods, DOC Ex. 417 at 5 (Davis Direct), it is administratively efficient to zero out the CCRC and collect all conservation costs through the Company's CAF or CCRA. There is no reason to consider CIP costs both in a rate case and in Xcel's annual CCRC filing. DOC Ex. 417 at 5 (Davis Direct).

444. Mr. Davis stated that, similar to other riders, the CCRC could be zeroed out when Xcel's new (final) rates go into effect. Xcel could submit an updated CCRA filing ninety days before Xcel's new rates are estimated to go into effect so that parties have a chance to evaluate the Company's proposal and the Commission has the opportunity to approve the new CCRA in a timely manner. DOC Ex. 417 at 6 (Davis Direct).

445. Regarding allocation of CIP costs across customer classes mentioned above, Xcel proposed to allocate its CIP costs to its various customer classes as described in the Direct Testimony of Xcel Witness Michael A. Peppin:

> Consistent with the Commission's Order in the 2013 rate case, we allocated both the Conservation Cost Recovery Charge (CCRC) and the CIP Adjustment Factor (CAF) using the per kWh method. In the proposed CCOSSs, CCRC costs are allocated to class using the 2014 test year sales forecast after subtracting sales to CIP exempt customers.

DOC Ex. 417 at 6 (Davis Direct) (*citing* Xcel Ex. 102 at 17 (Peppin Direct)). Mr. Davis testified that if the Commission does not approve zeroing out the CCRC, then he recommended that the Commission approve Xcel's volumetric CIP cost allocation proposal. Mr. Davis noted that Xcel's CIP costs are allocated on a volumetric basis in Xcel's CAF. DOC Ex. 417 at 6-7 (Davis Direct). Mr. Davis also noted that if the Commission approves the alternative method of recovering its CIP expenses by zeroing out of Xcel's CCRC and moving these costs to Xcel's CAF, then allocation of CIP costs in the context of this rate case is moot.

446. Mr. Davis summarized his recommendations regarding Xcel's conservation costs. He recommended that the Commission:

1. Accept Xcel's 2013-2015 combined electric and gas CIP, as approved by the Deputy Commissioner of the Department in Docket No. E,G002/CIP-12-447, as satisfying the filing requirement specified in Minn. Stat. § 216B.241, subd. 1 for conservation improvement plans and rate case filings.

2. Approve the zeroing out of Xcel's CCRC when Xcel's new rates go into effect and recovery of all CIP costs through the CAF.

3. If the Commission does not approve the zeroing out of Xcel's CCRC and recovery of Xcel's CIP costs through the Company's CAF, then Mr. Davis recommended that the Commission approve Xcel's proposed test-year CIP expenses of $90,715,761.

4. Approve Xcel's proposed volumetric CIP cost allocation method.

DOC Ex. 417 at 7 (Davis Direct).

2. Xcel's Revenue Decoupling Mechanism (RDM) Proposal Should Not Be Approved Unless Harm to Ratepayers is Mitigated. (Issue 50)

a. Revenue Decoupling in Minnesota

447. A revenue decoupling mechanism is a revenue true-up technique allowing utilities to recover apportioned class revenue responsibility, often on a per-customer basis. The true-up decreases or increases rates charged to classes of customers if their collective usage during a given time period deviates from a set base amount. There are two general types of revenue decoupling: full decoupling and partial decoupling. Further, there are various ways to design either full or partial decoupling mechanisms. DOC Ex. 417 at 9 (Davis Direct). A revenue decoupling mechanism is considered a "full" decoupling mechanism if the true-up amount is based on deviations from forecasted revenue for any reason, including weather that differs from "normal" forecasted weather. The mechanism is considered to be a "partial" decoupling mechanism if the true-up amount excludes deviations from forecasted revenue for a specified reason, such as weather variation. DOC Ex. 417 at 9 (Davis Direct).

448. For example, if residential customers used five percent less electricity than the base amount, and half of that decrease was related to cooler-than-normal summer weather conditions, then under a full decoupling mechanism the electric utility could surcharge these ratepayers for the full five percent. Conversely, if residential customers used five percent more than the base amount and half of the increase was due to warmer-than-normal summer weather, then under a full decoupling mechanism the utility would decrease rates for these ratepayers to reflect the full five percent. DOC Ex. 417 at 9-10 (Davis Direct).

449. Under partial decoupling, if residential customers used five percent less electricity than the base amount, and half of that decrease was related to cooler-than-normal summer weather conditions, the utility would only be able to surcharge for one-half of the five percent under-recovery, or 2.5 percent of the reduction from the base. Conversely, if residential customers used five percent more than the base amount and half of the increase was due to warmer-than-normal summer weather, then under partial decoupling the utility would decrease rates to reflect only one-half of the five percent over-recovery. DOC Ex. 417 at 10 (Davis Direct).

450. The Commission has never approved a revenue decoupling program for any Minnesota electric utility. DOC Ex. 417 at 11 (Davis Direct). The Commission has approved three revenue decoupling mechanisms for natural gas utilities – two for CenterPoint Energy (CenterPoint or CPE) and one for Minnesota Energy Resources Corporation (MERC). In Docket No. G008/GR-08-1075, the Commission approved a pilot partial decoupling mechanism for CPE, known as the Conservation Enabling (CE) Rider, which started on July 1, 2010 and expired on June 30, 2013. DOC Ex. 417 at 10 (Davis Direct). Under the CE rider, CPE was allowed to true-up the difference between the level of non-gas revenues authorized in CPE's last rate case adjusted for changes in customer counts to the level of weather-normalized non-gas revenues collected by rate class. DOC Ex. 417 at 10-11 (Davis Direct). Further, CPE was allowed to true-up these revenues up to plus or minus three percent of the total volumetric charge for each of the

applicable rate classes when an adjustment was required to collect non-gas revenue. DOC Ex. 417 at 11 (Davis Direct)

451. Second, on July 13, 2012, the Commission approved a pilot full decoupling mechanism for MERC in Docket No. G-007,011/GR-10-977. Under the approved tariff, MERC was allowed to true-up revenues up to ten percent above, or below, approved non-gas margins (after removing revenues from the CCRC). The approved tariff covered MERC's Residential and General Service-Small Commercial and Industrial customer classes. DOC Ex. 417 at 11 (Davis Direct).

452. Third, in Docket No. G008/GR-13-316, the Commission approved on a pilot basis a full decoupling mechanism for CPE, called the Revenue Decoupling Rider (RD Rider). Under that tariff, CPE may true up revenues up to ten percent above or below approved non-gas margins (after removing revenues from the CCRC). Further, the RD Rider approved in Docket No. G008/GR-13-316 covered all of CPE's non-market-rate customers rather than being limited to residential and small commercial customers. DOC Ex. 417 at 11 (Davis Direct).

b. Xcel's Partial RDM proposal.

453. Xcel proposed a partial decoupling mechanism for its residential customers and the subset of its small commercial and industrial (C&I) customers that do not pay a demand charge. DOC Ex. 417 at 7-8 (Davis Direct). Xcel Ex. 109 at 2 (Hansen Direct).

454. Xcel proposes to defer 12 months of RDM revenues (January to December), determine whether customers would be surcharged or receive a lower rate, and divide the total annual RDM amount by forecasted sales for the subsequent April through March period. DOC Ex. 417 at 8 (Davis Direct).

455. Xcel would calculate fixed revenues per customer and a fixed energy charge, based on approved information from this rate case.[142] DOC Ex. 417 at 8 (Davis Direct). After the rate case, Xcel would calculate allowed total revenues using the authorized fixed revenues per customer and actual numbers of customers and compare those revenues to actual total revenues based on the authorized fixed energy charge from the rate case times weather-normalized sales, using the same weather-normalization method used in the rate case. DOC Ex. 417 at 8 (Davis Direct). If actual revenues are lower than the allowed revenues, Xcel would surcharge customers the following year. If the actual revenues are higher than the allowed

---

[142] More specifically, Xcel proposes to calculate the monthly deferral as:

Monthly RDM Rider Deferral = (FRC x C) – (FEC x WN kWh)

Where:

- FRC is Fixed Revenue per Customer = Energy charge revenues divided by customer count, calculated monthly from test year data. ($/customer)
- C is Customer Count = Actual customer count for deferral month.
- FEC is Fixed Energy Charge=Average energy charge for each month of test year. ($/kWh)
- WN is kWh Weather-normalized Sales = Weather-normalized billed sales for deferral month. (kWh)

revenues, Xcel would charge a lower rate to customers the following year. Xcel proposes to calculate a per-kWh rate for the surcharge or refund on a per-kWh amount, based on forecasted sales for the April through March period, but Xcel's tariff does not explain how the sales would be forecasted. DOC Ex. 417 at 8-9 (Davis Direct).

456. Xcel's proposed RDM rider contains ten components detailed below. Because Xcel has failed to demonstrate that components 1, 8 and 10 are reasonable, the Department concludes that modifications are needed to Xcel's revenue decoupling proposal. In particular, Minn. Stat. §216B.2412 subd. 2 states that utility decoupling proposals should not adversely impact ratepayers. Xcel's decoupling proposal would adversely impact ratepayers and thus cannot satisfy the statute unless components 1 ("partial" decoupling), 8 ("soft" cap on rate increases over 5 percent) and 10 (permanent, not pilot) are adjusted to make these components reasonable.

1. The RDM would be **a partial revenue-per-customer decoupling** mechanism that removes the effect of weather from the decoupling deferrals.

2. The RDM would apply to three customer groups: residential non-space heating, residential space heating, and small commercial and industrial customers that do not pay a demand charge.

3. The revenue requirement recovered through the non-fuel energy charge, on a per-customer basis, would be the revenue baseline for calculating the decoupling deferrals.

4. Each month, the RDM deferral for a customer group would be calculated as the difference between the monthly baseline revenue and the weather-normalized revenue collected under the volumetric rates from those customers.

5. Every 12 months, the cumulative deferral (over or under recovery) for each customer group would be incorporated into customer rates for the following year by dividing the deferral amount by the forecast of sales to that customer group. A negative cumulative deferral would result in a rate increase. A positive cumulative deferral would result in a rate decrease. The rate change would occur on April 1 of the following year.

6. Total fixed revenue amount would be calculated using the test year energy charges, minus the CIP component, multiplied by test year sales for the corresponding customer group.

7. Deferrals would be calculated starting in the month after the Commission's final Order in this proceeding and through December of that year. The RDM rate adjustment would then be calculated and put into effect on April 1 for the following 12 months.

8. **Xcel proposed a "soft" cap on rate increases and no cap on rate reductions. For the soft cap, if a rate increase is more than five percent of total customer group revenue, including fuel and applicable riders, the excess deferral amount above the five percent would be carried over to the RDM deferral account in the**

following year. More particularly, Xcel proposed a new soft cap on RDM surcharges equal to five percent of base revenue, excluding fuel and all applicable riders if the Commission approves the proposed partial RDM decoupling mechanism, and a soft cap on RDM surcharges equal to **ten percent** of base revenue, excluding fuel and all applicable riders if the Commission approves a full decoupling mechanism. DOC Ex. 419 at 7 (Davis Surrebuttal).

9. The "RDM rate adjustment" would be listed as a separate line item on the customer's bill.[143]

10. Xcel's proposed RDM would be an ongoing program, not a pilot program.

Xcel Ex. 109 at 9-16 (Hansen Direct); DOC Ex. 417 at 12-13 (Davis Direct) (emphasis added).

c. Xcel's RDM Should Be Modified to Comply with Minnesota's Energy Conservation Laws, which Require Revenue Decoupling Pilot Programs to Achieve Specific Goals, and Not to Adversely Affect Ratepayers.

457. The Next Generation Energy Act (NGEA) of 2007, and modifications to it, increased Minnesota's commitment to energy conservation in Minnesota. Minn. Stat. §216B.2401, which was originally enacted as a part of the NGEA, states:

> The legislature finds that energy savings are an energy resource, and that cost-effective energy savings are preferred over all other energy resources. The legislature further finds that cost-effective energy savings should be procured systematically and aggressively in order to reduce utility costs for businesses and residents, improve the competitiveness and profitability of businesses, create more energy-related jobs, reduce the economic burden of fuel imports, and reduce

---

[143] Xcel proposed to calculate rate adjustments in its RDM by calculating the deferral each month, for each customer group, using the following steps:

1. Multiply the "fixed revenue per customer" that is authorized in the rate case for the month times the number of customers in the customer group during the month. The product is the authorized monthly revenues for the customer group.
2. Multiply the monthly fixed-cost revenue requirement times the monthly weather-normalized billed sales to the customer group. The product of this multiplication is the authorized revenues for the customer group assuming weather-normalized sales.
3. Subtract the results of Step 2 from the results of Step 1.

Xcel Ex. 109 at 10-12 (Hansen Direct); DOC Ex. 417 at 13-14 (Davis Direct). The "fixed revenue per customer" for each customer group will be calculated as the fixed cost revenue requirement divided by the number of customers forecast for each month in the 2015 test year. The fixed cost revenue requirement is calculated using the test year energy charges, less the CIP component, multiplied by test year sales for corresponding customers. Xcel proposed to exclude customer charge revenue because that revenue is already decoupled from customer sales. Xcel Ex. 109 at 12 (Hansen Direct); DOC Ex. 417 at 14 (Davis Direct).

> pollution and emissions that cause climate change. Therefore, it is the energy policy of the state of Minnesota to achieve annual energy savings equal to at least **1.5 percent of annual retail energy sales** of electricity and natural gas through cost-effective energy **conservation improvement programs** and **rate design**, energy efficiency achieved by energy consumers without direct utility involvement, energy codes and appliance standards, programs designed to transform the market or change consumer behavior, energy savings resulting from efficiency improvements to the utility infrastructure and system, and other efforts to promote energy efficiency and energy conservation.

Minn. Stat. §216B.2401 (2013)(emphasis added). DOC Ex. 417 at 14-15 (Davis Direct). As shown in the emphasized phrases, the state's energy conservation policy: 1) includes a statewide energy savings goal of at least 1.5 percent of annual retail energy sales and 2) identifies two policy approaches for achieving this goal – energy conservation improvement programs (CIP), and rate design. DOC Ex. 417 at 14-15 (Davis Direct). The latter—rate design—is at issue with respect to Xcel's proposed decoupling mechanism.

458. The NGEA allows utilities to implement pilot projects to decouple the utility's revenue from changes in its energy sales, to encourage the utility to promote more conservation. DOC Ex. 417 at 15 (Davis Direct). Minn. Stat. §216B.2412 directs the Commission to approve at least one pilot decoupling program.:

> Subd. 2. Decoupling criteria. The commission shall, by order, establish criteria and standards for decoupling. The commission may establish these criteria and standards in a separate proceeding or in a general rate case or other proceeding in which it approves a pilot program, and shall design the criteria and standards to mitigate the impact on public utilities of the energy-savings goals under section 216B.241 **without adversely affecting utility ratepayers.** In designing the criteria, the commission shall consider energy efficiency, weather, and cost of capital, among other factors.
>
> Subd. 3. Pilot programs. The commission shall allow one or more rate-regulated utilities to participate in a pilot program to assess the merits of a rate-decoupling strategy to **promote energy efficiency and conservation**. Each pilot program must utilize the criteria and standards established in subdivision 2 and be designed to **determine whether a rate-decoupling strategy achieves energy savings.** On or before a date established by the commission, the commission shall require electric and gas utilities that intend to implement a decoupling program to file a decoupling pilot plan, which shall be approved or approved as modified by the commission.

Minn. Stat. §216B.2412 (2013)(emphasis added). DOC Ex. 417 at 16-17 (Davis Direct).

459. Minn. Stat. §216B.2412 primarily addresses pilot decoupling programs and also provides an appropriate starting point for evaluating Xcel's RDM proposal. To paraphrase the

statute, Minn. Stat.§ 216B.2412, requires a decoupling mechanism to achieve the following criteria:

1. Reduce a utility's disincentive to promote energy efficiency;

2. Be designed to determine whether a rate-decoupling strategy achieves energy savings; and

3. Not adversely impact ratepayers.

DOC Ex. 417 at 17 (Davis Direct).

460. The Department showed that Xcel's partial decoupling mechanism with its five percent "soft" cap is not reasonable and should not be approved because, while it meets the first two criteria, Xcel has failed to show that it meets the third criteria. It adversely impacts ratepayers.

i. Xcel's decoupling mechanism "reduces a utility's disincentive to promote energy efficiency."

461. Under traditional regulation the Commission sets a utility's rates based on a weather normalized revenue requirement. DOC Ex. 417 at 18 (Davis Direct). Once rates are set, the utility's financial performance depends on its levels of sales and its ability to manage its costs. Because of the high fixed costs associated with the natural gas and electric utility industries, a utility's marginal revenue (i.e., price) significantly exceeds its short-run marginal costs. Therefore, a utility has an incentive to increase sales. This phenomenon is referred to as the "throughput incentive." DOC Ex. 417 at 18 (Davis Direct). Currently, Xcel has a throughput incentive because the Company can increase its profits by selling more electricity. DOC Ex. 417 at 18 (Davis Direct).

462. Xcel's proposed RDM, which is a partial decoupling mechanism, meets the criteria of reducing Xcel's disincentive to promote energy savings, because, under Xcel's proposal the Company would not make more money through additional sales. DOC Ex. 417 at 18 (Davis Direct). On the other hand, despite Xcel's disincentive to achieve energy savings, Xcel has achieved significant increases in energy savings in recent years. Mr. Davis' Direct Table 1 (below) shows Xcel's 2007-2013 actual energy savings and Xcel's proposed energy savings goals for 2014-2015 both in terms of energy savings and percent of retail sales. DOC Ex. 417 at 18 (Davis Direct).

Table 1: Xcel Electric Energy Savings 2007-2013 and Approved Goals for 2014-2015

	kWh Savings	Average 3-year Weather-Normalized Sales	Savings as % of Retail Sales
2007	259,207,822	30,815,329,700	0.84%
2008	331,024,729	30,815,329,700	1.07%
2009	342,335,073	30,815,329,700	1.11%
2010	415,591,395	30,815,329,700	1.35%
2011	465,443,913	30,815,329,700	1.51%
2012	533,477,510	30,815,329,700	1.73%
2013	494,686,290	28,987,234,000	1.71%
2014	400,712,665	28,987,234,000	1.38%
2015	400,414,935	28,987,234,000	1.38%

Years 2014 and 2015 are forecasted. Table 1 shows that Xcel's actual energy savings increased 91 percent between 2007 and 2013. Comparing 2012, when Xcel attained its highest energy savings, to 2007 indicates an increase in energy savings of 106 percent. These are significant gains in energy savings. DOC Ex. 417 at 19 (Davis Direct). Xcel's energy savings have increased substantially because, despite the incentive to sell more electricity, there are several policies that encourage Xcel to increase its energy savings. These include, but are not limited to:

1. The State's 1.5 percent energy savings goal;

2. Minnesota's Shared Savings DSM financial incentive mechanism; and

3. Increased public interest in saving energy to help mitigate climate change.

DOC Ex. 417 at 19 (Davis Direct).

463. The Commission approved the latest version of the Shared Savings DSM financial incentive mechanism on December 20, 2012 in Docket No. E,G-999/CI-08-133. The Shared Savings DSM financial incentive mechanism rewards utilities with a percentage of the net benefits created when the utility encourages its customers to invest in energy savings. The percentage of net benefits awarded increases as electric utilities approach and surpass the State's 1.5 percent energy savings goal. DOC Ex. 417 at 20 (Davis Direct).

464. Xcel has received substantial DSM financial incentives Mr. Davis' Direct Table 2 below shows Xcel's approved DSM financial incentives between 2007 and 2012 and Xcel's estimate of its incentive for its energy savings achievements in 2013.[144]

[144] Docket No. E002/M-14-287, Xcel Electric's 2014/2015 CIP Adjustment Factor.

Table 2: Xcel Electric DSM Incentives 2007-2012 and Estimated for 2013

	Financial Incentive	CIP Expenditures	Incentive/CIP Spending
2007	$5,314,625	$47,382,619	11%
2008	$14,761,751	$50,516,190	29%
2009	$16,398,115	$57,885,077	28%
2010	$40,401,006	$71,884,336	56%
2011	$52,004,975	$76,302,262	68%
2012	$53,911,925	$87,071,903	62%
2013	$42,888,198	$79,570,696	54%

465. Table 2 indicates that Xcel's 2012 incentive was more than ten times greater than the Company's 2007 DSM financial incentive. DOC Ex. 417 at 20 (Davis Direct). Further, annual incentive costs compared to Xcel's annual CIP expenditures increased from 11 percent in 2007 to 68 percent in 2011, and 62 percent in 2012. DOC Ex. 417 at.20-21 (Davis Direct). In 2013 a less lucrative but still aggressive DSM financial incentive mechanism was applicable. Xcel's projection of its 2013 DSM incentive is $42.9 million, which is eight times the Company's 2007 incentive and 54 percent of the Company's expenditures. DOC Ex. 417 at 21 (Davis Direct).

466. In summary, while Xcel's proposed partial decoupling mechanism meets the statutory criteria for reducing Xcel's disincentive to promote energy savings, it is not the only means for the Commission to address that disincentive to achieve energy savings, as is seen by the fact that Xcel has achieved significant increases in energy savings in recent years. When balancing the achievement of this statutory criteria against the failure to meet another --the adverse impact in ratepayers, the Department recommends that the Commission conclude that Xcel has failed to demonstrate the reasonableness of its decoupling proposal.

ii. Xcel's proposal is designed to determine whether a rate-decoupling strategy achieves energy savings.

467. Xcel proposed an evaluation plan for its RDM; Xcel proposes that the following information be included in Xcel's annual evaluation plan:

a. Total over or under collection of allowed revenues by class;
b. Total collection of prior deferred revenue;
c. Calculations of the RDM deferral amount;
d. The number of customer complaints;
e. The amount of revenues stabilized and how the stabilization impacted the Company's overall risk profile; and
f. A comparison of how revenues under traditional regulation would have differed from those collected under the decoupling proposal.

DOC Ex. 417 at 21 (Davis Direct) (*citing* Xcel Ex. 109 at18-19 (Hansen Direct)). This evaluation plan meets the Commission's Revenue Decoupling Criteria and Standards in Docket

No. E,G-999/CI-08-132. DOC Ex. 417 at 21-22 (Davis Direct). The Commission's June 19, 2009 Order required the following in regards to evaluation:

> 7. Review: All utility pilot proposals shall be reviewed yearly. If the Commission determines that the pilot is harming ratepayers and/or failing to meet objectives, the Commission may suspend the pilot at any time or recommend modifications. As part of this annual review, all utilities shall provide information that shall be specified in
>
> 8. an evaluation plan established as part of the pilot plan that shall include, but not be limited to the following information:
>
> A. total adjustments by class
> B. total adjustment charges collected
> C. number of customer complaints
> D. has the pilot stabilized revenues for the class(es) under the pilot and how has such stabilization impacted the utility's overall risk profile
> E. comparison of how revenues under traditional regulation would have differed from those collected under the decoupling pilot
> F. is the utility meeting energy efficiency savings goals? has the decoupling pilot influenced the achievement or likelihood of achievement of those goals?
> G. problems encountered and improvements/suggestions for the future.

DOC Ex. 417 at 21-22 (Davis Direct) (*citing* Docket No. E,G999/CI-08-132, Order, June 19, 2009 at 8-9).

468. The information Xcel proposed to provide was helpful in many respects. However, as Mr. Davis cautioned, given the multiple policies and trends that promote conservation in Minnesota, it is impossible to parse out the specific impact of decoupling on the conservation achievements of a Minnesota utility's customers. DOC Ex. 417 at 22 (Davis Direct). It is not possible to decisively conclude or identify that decoupling in particular will lead to changes in a utility's energy savings in addition to the effects of the other policies in place.[145] Because revenue decoupling, particularly for an electric utility, is fairly new in Minnesota, Xcel's proposed reporting, if modified as the Department recommends below, would provide useful information. DOC Ex. 417 at 22-23 (Davis Direct). If the Commission approves

[145] As noted above, both MERC and CPE have or have had pilot decoupling mechanism in effect. Energy savings of both utilities increased after decoupling went into effect. However, the energy savings of natural gas utilities without decoupling also increased during the same period. Thus, Mr. Davis could not conclude that the increase in energy savings was due to decoupling. DOC Ex. 417 at 23 (Davis Direct).

decoupling for Xcel, the Company should file an annual evaluation plan with the following features.

1. Total over or under collection of allowed revenues by class;
2. Total collection of prior deferred revenue;
3. Calculations of the RDM deferral amount;
4. The number of customer complaints;
5. The amount of revenues stabilized and how the stabilization impacted the Company's overall risk profile; and
6. A comparison of how revenues under **traditional regulation** would have differed from those collected unde**r partial** and **full decoupling.**
7. **A summary of the Company's energy savings since 2007 and a qualitative and quantitative analysis of how Xcel Electric's CIP has changed since the beginning of its decoupling mechanism.**

DOC Ex. 417 at 23-24 (Davis Direct) (emphasis added). One of the modifications DOC recommended is to the sixth component of Dr. Hansen's proposed evaluation plan – it extends the comparison of revenues to all three of traditional regulation as well as partial and full decoupling. Including all three forms of potential regulation is intended to provide the Commission and others information needed for making future decisions regarding revenue decoupling. DOC Ex. 417 at 24 (Davis Direct). The second modification DOC recommends is to require the Company to update the Commission on its CIP achievements and changes in an annual decoupling report. Mr. Davis testified that it would be helpful to have the most important information relevant to the decoupling program in one spot. The seventh component of DOC's proposed evaluation plan would allow the Commission to assess whether Xcel continues to achieve and surpass the State's energy savings goal, information which will assist the Commission in making future decisions regarding policies that impact Xcel and its conservation programs. DOC Ex. 417 at 24 (Davis Direct).

iii. Xcel's Partial Decoupling Proposal Would Have A Greater Adverse Impact on Ratepayers Than Full Decoupling or Traditional Ratemaking With No Decoupling.

469. Minn. Stat. §216B.2412 subd. 2 states that utility decoupling proposals should not adversely impact ratepayers. Decoupling as a rate design can adversely impact ratepayers in a couple of ways. The first potential negative impact Mr. Davis considered is if ratepayers end up paying more under revenue decoupling, as compared to traditional rate regulation, due to customer surcharges. The second potential negative impact is if customers bear an undue risk of volatility in sales due to weather. DOC Ex. 417 at 25 (Davis Direct).

470. These negative impacts are not necessarily reasons for the Commission to deny approval of revenue decoupling, as indicated by the Commission's prior decisions on pilot decoupling projects. Instead of disapproving decoupling as unreasonable, the Commission could assess the risks of customers paying higher costs than under traditional rate design and address whether the adverse ratepayer impacts could be mitigated by changing the type of decoupling chosen, or modifying the parameters of the utility's decoupling proposal. DOC Ex. 417 at 25

(Davis Direct). The Department's analysis offered the Commission mitigation tools in the form of a cap on surcharges set at a reasonable amount of three percent, and suggested that the program be only a pilot, and employ full decoupling, which Mr. Davis's analysis showed would result in significantly lower surcharges than partial decoupling under multiple economic and weather conditions.

1. Xcel's Partial Decoupling Proposal (Xcel's RDM) Should Not Be Approved Because It Will Have An Greater Adverse Impact on Ratepayers Than Full Decoupling or Traditional Ratemaking Without Decoupling.

471. Mr. Davis evaluated whether Xcel's partial decoupling proposal would have an adverse impact on the Company's customers. He concluded that Xcel's proposed RDM would have an adverse impact on Xcel's residential ratepayers, is unreasonable, and should not be approved (DOC Ex. 417 at 32 (Davis Direct) unless modified as DOC recommended to mitigate the adverse impact on ratepayers. He began his analysis by examining the potential costs to Xcel's ratepayers under Xcel's RDM partial decoupling proposal, under full decoupling, and under traditional ratemaking (no decoupling). Mr. Davis sent Xcel DOC IR No. 312, requesting that it analyze its revenues under various alternatives for 2008 to 2013, and asking:

> Please estimate the revenues [for] each of Xcel Energy's non-market rate customer classes, under the assumption of:
>
> a. No decoupling;
> b. Xcel's proposed partial revenue per customer decoupling mechanism; and
> c. Full decoupling.
>
> When reporting the revenues for each of the five years, for each customer class, please provide:
>
> 1) An example where revenues would have been collected in the same year; and
> 2) An example where revenue deferrals, including refunds and/or surcharges, would have been collected in the manner proposed by Xcel. For 2), please separate revenues collected through base rates and revenues collected through the true-up mechanism.

DOC Ex. 417 at 27(Davis Direct).[146] Mr. Davis' analysis of Xcel's data showed that Xcel's RDM may significantly increase ratepayer costs, and that a full decoupling mechanism could

[146] Xcel's response to DOC IR No. 312 is included in the evidentiary record as DOC Ex. 417 CD-2 (Davis Direct). DOC Ex. 417 CD-3 (Davis Direct) is Mr. Davis' comparison of the impacts of partial and full decoupling to traditional rate regulation for the three customer classes that would be covered by Xcel's proposed RDM partial decoupling mechanism—residential,
(Footnote Continued on Next Page)

also increase ratepayer costs, but to a much smaller extent. DOC Ex. 417 at 27 (Davis Direct). For the years 2009 through 2013 the residential and residential space heating customers would never have received a refund under Xcel's RDM proposal. DOC Ex. 417 at 27 and CD-3 (Davis Direct). For 2009-2013, the three RDM customer classes would have been surcharged a total of $72.7 million. If Xcel's RDM had been in place during that period the residential customers would have been surcharged $70.4 million, with each residential customer paying an average of $13.20 more per year. The residential with space heating customer class would have paid an additional $2.6 million with each customer paying an average of $16.92 more per year. The small commercial, non-demand-metered class would have been refunded $332 thousand, with each customer being refunded $0.84 per year, on average. DOC Ex. 417 at 27and CD-3 (Davis Direct). Mr. Davis' Direct Table 3 summarized the potential impacts of partial and full decoupling on the three RDM customer classes. DOC Ex. 417 at 27 (Davis Direct).

Table 3: Ratepayer Changes in Costs
Comparing Partial and Full Decoupling to Traditional Regulation
2009-2013

	Increase/ (Decrease) in Revenues	Average Monthly Surcharge or (Refund)
Residential Partial	$70,398,884	$1.10
Residential Full	$15,613,233	$0.25
Space Heat Partial	$2,588,798	$1.41
Space Heat Full	$2,424,642	$1.34
Small Comm. Non-D Partial	($331,836)	($0.07)
Small Comm. Non-D Full	($2,232,093)	($0.44)
RDM Customers Partial	$72,655,847	
RDM Customers Full	$15,805,782	
Total Residential Partial	$72,987,683	
Total Residential Full	$18,037,875	

DOC Ex. 417 CD-3 (Davis Direct).

472. Table 3 shows that, if a partial decoupling mechanism had been in place from 2009-2013, the three RDM customer classes would have paid considerably higher surcharges

(Footnote Continued from Previous Page)
residential with space heating, and non-demand-metered (three RDM customer classes) small commercial. DOC Ex. 417 at 26(Davis Direct).

($70.4 million) than they would have paid under full decoupling ($15.8 million, but that both decoupling mechanisms would have resulted in surcharges for these classes than if traditional ratemaking had been in place. The small commercial, non-demand metered customers would have been refunded money under decoupling, and similarly, they would have benefitted more from full decoupling than from partial decoupling. DOC Ex. 417 at 27-28 (Davis Direct).

473. Mr. Davis explained that many factors impact customer usage—weather, the economy, and energy efficiency are some of the main ones. DOC Ex. 417 at 29 (Davis Direct). A full decoupling mechanism takes all of those factors into account and compares what the actual customer usage was (and thus what the utility's revenues were) compared to what was authorized in the rate case. DOC Ex. 417 at 29 (Davis Direct). A review of the data provided in Xcel's response to DOC IR 312 indicates that for both the residential and residential with space heating customer classes, the full decoupling mechanism would have resulted in surcharges some years and refunds some years, which is what is expected over time as the weather and economy varies. DOC Ex. 417 at 29 and CD-3 (Davis Direct).

474. Importantly, Xcel's data for the specific time period from 2009-2013 is dominated by a large surcharge of $25.2 million in 2009, such that, under full decoupling, the residential class would have received a relatively large surcharge of $24 per year based on 2009 revenues. Had 2009 been excluded from the analysis, or had a tighter cap been assumed, full decoupling would have resulted in a net refund to residential customers, for 2010 to 2013. DOC Ex. 417 at 29 (Davis Direct). The 2009 year had two significant influences causing the surcharge: 2009 had a much milder summer than normal and thus the residential class consumed much less electricity for cooling than normal and the economy in 2009 was weak.

475. The lesson is that decoupling trues-up revenues for the utility *due to any effect*, unless that effect is expressly factored out, such as factoring out abnormal weather through weather-normalization. Thus, a weak economy, such as occurred during the Great Recession, would reduce energy use and sales and lead to higher rates in the subsequent year under decoupling, unless there is a mechanism to moderate or otherwise mitigate such rate increases.[147] DOC Ex. 417 at 29-30 (Davis Direct).

---

[147] Mr. Davis confirmed that the economy and weather were independent variables; he estimated the differences in need for electric cooling, and thus higher residential electricity consumption, in the summer of 2009 as compared to other years by looking at the temperature-humidity index (THI), which is a measure of the degree of discomfort of a person in warm weather. His Direct Testimony Table 4 showed the THI for each year, 2008-2013, and compared it to the 20-year average THI, 1994-2013. The 2009 THI was almost 40 percent lower than the 20-year average, a significant departure. DOC Ex. 417 at 30 (Davis Direct). Table 4 also showed that the years 2010-2013 all had a significantly higher than the 20-year average, but 2008 had a low THI. DOC Ex. 417 at 30-31 (Davis Direct). Given that 2008 was also at the height of the Great Recession, Mr. Davis expected that residential customers would have faced a surcharge that year as well. However, Mr. Davis did not ask Xcel to evaluate 2008 in DOC IR 312. DOC Ex. 417 at 31 (Davis Direct). 2008 was evaluated in Mr. Davis' Surrebuttal. DOC Ex. 419 at 15 (Davis Surrebuttal).

476. The most important information shown in the data Xcel provided is that partial decoupling surcharges would have resulted in much higher rates for residential customers than the full decoupling surcharges. Further, full decoupling could lead to lower rates than under traditional regulation.

477. Under Xcel's RDM actual sales are weather-normalized before calculating whether Xcel has experienced an under- or over-collection for a customer class. The fact that partial decoupling would have resulted in a surcharge but full decoupling would have resulted in a refund during these years suggests that Xcel experienced non-normal weather (higher THI), which boosted its sales. Weather-related increased sales would be taken into account in a full decoupling calculation, but would not be taken into account in Xcel's proposed RDM. DOC Ex. 417 at 31 (Davis Direct). Because the increased sales were not taken into account, the partial decoupling mechanism makes it appear in the RDM as if Xcel's revenues are lower than they are and thus customers are surcharged. To evaluate the extent to which actual use per customer (UPC) was higher than the weather-normalized UPC, Mr. Davis used data provided by Xcel in response to DOC IRs Nos. 301 and 308. Mr. Davis' Direct Table 5 shows this comparison for 2005-2013.

Table 5: Comparison of Actual Use Per Customer to Weather-Normalized Use Per Customer (UPC), 2005-2013

	Actual UPC	WN UPC	Actual as Percent of WN
2005	8,321	8,116	103%
2006	8,288	8,150	102%
2007	8,387	8,170	103%
2008	7,921	7,980	99%
2009	7,690	7,918	97%
2010	8,099	7,854	103%
2011	8,069	7,851	103%
2012	8,010	7,824	102%
2013	7,938	7,684	103%

DOC Ex. 417 at 31 (Davis Direct). Table 5 indicates that a significant majority of the time, Xcel's weather-normalized use per customer (WN UPC) is lower than its actual UPC. Thus, under Xcel's proposed RDM, residential customers could be surcharged even if Xcel has recovered its fixed charges. DOC Ex. 417 at 32 (Davis Direct). Based on Mr. Davis' analysis of Xcel's data, DOC concluded that Xcel's proposed RDM would have an adverse impact on Xcel's residential ratepayers, is not reasonable and should not be approved. DOC Ex. 417 at 32 (Davis Direct).

478. In response to DOC's recommended rejection of Xcel's RDM proposal as unreasonable, Xcel's Rebuttal Testimony questioned whether DOC's analysis was of a representative period of years. Xcel Witness Dr. Hansen stated that Xcel did not agree with the

Department's recommendation because the Department based its conclusions on a period, 2009-2013, that does not necessarily reflect the conditions that will occur during the three-year RDM pilot project. DOC Ex. 419 at 10 (Davis Surrebuttal) (*citing* Xcel Ex. 110 at 5 (Hansen Rebuttal)).

479. Xcel's disagreement is not well-founded. While on the one hand, the proposed pilot period (2015-2017) may have conditions different than the study period (2009-2013), Mr. Davis explained that conditions such as an economic downturn or significantly higher energy conservation could lead to higher rates charged to customers, but would do so under either partial or full decoupling. Xcel's analysis of its RDM did not provide the Commission with adequate assurance that approving partial decoupling would adequately protect ratepayers, and Xcel has not modified its proposal to address its deficiencies. DOC Ex. 419 at 10 (Davis Surrebuttal).

480. The fact remains that Xcel's data shows that, in 2011, 2012, and 2013 residential ratepayers would have paid $45.1 million in surcharges under partial decoupling but received a refund of $7.8 million under full decoupling. Thus, partial decoupling would have cost ratepayers a total of $52.9 million more than full decoupling in that period. DOC Ex. 419 at 11 (Davis Surrebuttal). DOC concluded that it is not reasonable to allow Xcel to charge ratepayers $52.9 million more over a three year period than was needed to eliminate Xcel's throughput incentive. DOC Ex. 419 at 11 (Davis Surrebuttal).

481. In Rebuttal, Xcel also offered a calculation showing that if weather shifted one year, a deferral under full decoupling with a soft cap would increase to $45.2 million under some conditions and $58.5 million under others. DOC Ex. 419 at 11 (Davis Surrebuttal) (*citing* Xcel Ex. 110 at 7 (Hansen Rebuttal)). Xcel's analysis, however, misleadingly assumed that there would have been no hard cap on surcharges. The Department proposed a hard cap no higher than three percent of total customer group revenue, including fuel and all applicable riders, with no deferral. DOC Ex. 419 at 11 (Davis Surrebuttal) (*citing* Xcel Ex. 105 at Schedule 5, p. 1) (Huso Direct)). Xcel's analysis actually helps show why the Company's "soft cap" is not reasonable. Mr. Huso's Schedule 5 shows that Xcel proposed total residential revenues of $1,088,936,000 and $116,135,000 of non-demand small C&I test year revenues, for a total of $1,205,071 of revenues for the three RDM classes. Three percent of these revenues is $36,152,130. DOC Ex. 419 at 11 (Davis Surrebuttal). Thus Xcel's surcharge under the DOC's full decoupling proposal would never reach the size the Company discusses. The potential decoupling surcharges would be even smaller if the Commission adopted AARP's proposed hard cap of two percent. AARP Ex. 310 at 21 (Brockway Direct).

482. Finally, to further address Xcel's concern about whether the Department's analysis was of a reasonably representative time period, Mr. Davis expanded his comparison of partial, full, and no decoupling to more years and summarized the results of his analysis of January 2003 through January 2007[148] in Mr. Davis' Surrebuttal Table 4.

---

[148] The data was updated the test year 1993 data with sales data from 2003, to improve its accuracy, and subject to other reasonable assumptions. DOC Ex. 419 at 11-13 (Davis Surrebuttal).

Table 4: 2004-2013 Comparison of Partial and Full Decoupling

Customer Classes	Increase/ (Decrease) in Revenues	Average Annual Surcharge or (Refund)
Residential Partial	$60,922,437	$56.81
Residential Full	($14,212,003)	($14.19)
Space Heating Partial	$4,405,657	$149.01
Space Heating Full	$5,363,540	$184.82
Small C&I Non-Demand Partial	($21,544,039)	($264.43)
Small C&I Non-Demand Full	($24,335,169)	($297.75)
Three Customer Classes Partial	$43,784,055	
Three Customer Classes Full	($33,183,631)	
Amount by which Partial costs exceed Full Decoupling costs	**$76,967,686**	

DOC Ex. 419 at 13 (Davis Surrebuttal).

483. Table 4 shows that over the 10-year period of 2004 to 2013, the residential, residential with space heating, and demand-metered commercial classes (the three RDM classes) would have paid an additional $77 million under partial decoupling mechanism as opposed to a full decoupling mechanism. Over the 10-year period, the three RDM classes would have paid an additional $43.8 million more under partial decoupling than under no decoupling, whereas the three RDM classes would have paid $33.2 million less under full decoupling as compared to no decoupling.DOC Ex. 419 at 13-14 (Davis Surrebuttal).

484. Based on Mr. Davis' additional analysis responding to Xcel's concerns, the DOC continued to recommend that the Commission not approve Xcel's proposed partial decoupling RDM proposal and instead approve full decoupling, as discussed below. DOC Ex. 419 at 14 (Davis Surrebuttal).

2. Xcel's Proposed "Soft" Cap of Five Percent Would Adversely Affect Ratepayers, Is Not Reasonable, and Should Not Be Approved.

485. To mitigate the potential adverse impact of decoupling on ratepayers, the Commission should approve only a decoupling plan that includes a cap on surcharges of reasonable design and size; the DOC recommends a hard cap of three percent on surcharges.

486. Xcel's "soft" cap should not be approved. Witness Dr. Hansen describes the Xcel's proposed "soft" cap as follows:

> If the rate adjustment produces a rate increase that is more than five percent of total customer group revenue, including fuel and all applicable riders, the excess deferral amount above the five percent will be carried over to the RDM deferral account in the following year.

DOC Ex. 417 at 32-33 (Davis Direct) (*citing* Xcel Ex. 109 at 15 (Hansen Direct). This testimony showed that Xcel's proposed "soft cap" is not a cap at all, because it would not change the size of a surcharge, just the timing; what the utility does not collect in one year, it would collect in the next. DOC Ex. 417 at 33 (Davis Direct).

487. Moreover, even if the five percent cap was a hard cap, surcharges can be unreasonably great because five percent is too great a percentage; a smaller percentage would more reasonably mitigate the surcharges. As shown by the analysis of 2009-2013 Xcel data (provided by Xcel in response to DOC IR No. 312, as discussed above) the annual cap for residential customers would have varied from $38.8 million to $46.7 million during 2009-2013 (DOC Ex. 417 at 33 and CD-2 (Davis Direct)), meaning residential customers could have been charged for up to those amounts. Even if a hard cap were set at 2.5 percent, residential customers would have been surcharged in excess of a total of $50 million under Xcel's RDM for the five years 2009-2013, an amount far below the total surcharge that would have occurred under an annual 5 percent cap. DOC Ex. 417 at 33 (Davis Direct).

488. As Mr. Davis' historical analysis above indicates, a full decoupling mechanism may also have an adverse impact on Xcel ratepayers, particularly if its adverse impact was not mitigated. Mr. Davis' Direct Testimony Table 6 showed the average monthly surcharge or (refund) for each of the three RDM classes for each year 2009-2013.

Table 6: Average Surcharge or (Refund) Under Full Decoupling If Applied 2009-2013

	Average Monthly Residential	Average Annual Residential	Average Monthly Residential with Space Heat	Average Annual Residential with Space Heat	Average Monthly Small Commercial	Average Annual Small Commercial
2009	$2.00	$23.94	$0.66	$7.88	($1.62)	($19.44)
2010	($0.02)	($0.23)	$1.77	$21.21	$0.54	$6.53
2011	($0.04)	($0.54)	$0.85	$10.25	$2.01	$24.12
2012	($0.05)	($0.55)	$5.36	$64.28	$0.64	$7.70
2013	($0.64)	($7.65)	($1.94)	($23.24)	($3.79)	($45.42)

489. First, Table 6 indicated that the residential customer class would have experienced an average surcharge of $2 per month in 2009, or $24 per year. DOC Ex. 417 at 34 (Davis Direct). The $24 surcharge would have been approximately three percent of annual residential

bills.[149] DOC Ex. 417 at 35 (Davis Direct). For each year 2010-2013 the residential customers would have received a refund, the maximum annual refund being $7.65 in 2013. DOC Ex. 417 at 35 (Davis Direct).

490. Second, the residential with space heating customer class would have experienced a maximum annual surcharge of $64.28 in 2012 and would have been refunded $23.24 in 2013. The 2012 surcharge would have been approximately 5.4 percent of the residential space heating bills.[150] DOC Ex. 417 at 35 (Davis Direct).

491. Third, the average small commercial non demand-metered customers, according to Table 6, would have been surcharged $24.12 in 2011 and received a refund of $45.12 in 2013. DOC Ex. 417 at 35 (Davis Direct).

492. Although Mr. Davis was not concerned about the refunds, since they would have benefited customers, Mr. Davis was concerned about the sizes of the surcharges, in particular the size of the surcharge for the residential with space heating class in 2012 when the winter was mild and heating electric usage was low. DOC Ex. 417 at 35 (Davis Direct). A cap on surcharges on a full revenue decoupling mechanism could help mitigate the size of potential surcharges if it is set to at reasonable percentage.

493. As Mr. Davis described above, the cap proposed by Xcel is soft, but even if it were hard, it would have allowed in the analysis surcharges of $48 million per year for the residential class.[151] DOC Ex. 417 at 35-36 (Davis Direct). To help mitigate the impact of the full decoupling mechanism, Mr. Davis recommended a hard cap of three percent. Based on Xcel's response to DOC IR No. 319, Mr. Davis estimated that a three percent hard cap would limit annual surcharges to approximately $27 per residential customer and $35 per residential customer with space heating. DOC Ex. 417 at 36 (Davis Direct). The DOC recommends that if the Commission approves a decoupling mechanism, its adverse impact be mitigated by selecting a hard cap in a reasonable amount, such as three percent.

494. In its Rebuttal Testimony, Xcel disagreed with DOC's recommendations. Xcel Witness Dr. Hansen stated that Xcel prefers a soft cap with a deferral, positing that if the Company expects a cap to affect deferrals, the Company faces the same disincentive to promote energy efficiency that it faced in the absence of the decoupling mechanism. DOC Ex. 419 at 3 (Davis Surrebuttal) (citing Xcel Ex. 110 at 10 (Hansen Rebuttal).

---

[149] Xcel's response to DOC IR No. 319 indicates that the average monthly residential bill for October 2012 through September 2013 was $75.50, which translates into an average of $908 per year. DOC Ex. 417 at 34-35 (Davis Direct).

[150] Xcel's response to DOC IR No. 319 indicates that the average monthly residential space heating bill for October 2012 through September 2013 was $97.42, which translates into an average of $1,169 per year. DOC Ex. 417 at 35 (Davis Direct).

[151] Mr. Huso's calculations indicate that present residential revenues are set at $964,252,000. ($964,252,000 * 5 percent equals $48,212,600.) Xcel Ex. 105 SH-1 at schedule 5, Page 1 of 2 (Huso Direct).

495. Dr. Hansen's reasoning is not compelling. Analysis of the effect of Xcel's existing incentive mechanisms for conserving energy shows that any disincentive Xcel has to promoting energy efficiency has not been an obstacle to the Company promoting energy efficiency in the past, and it is not likely to be a problematic obstacle for Xcel in the future. Mr. Davis responded to Dr. Hansen's statement by explaining Xcel's existing, lucrative, and Commission-approved, DSM financial incentive mechanism that rewards the Company for energy conservation. DOC Ex. 419 at 3 (Davis Surrebuttal).

496. Xcel's DSM financial incentive mechanism is designed so that, as Xcel achieves higher levels of energy savings, measured as a percent of retail sales, the Company receives a higher percentage of the net benefits created by the conservation investments of Xcel's customers and thus, additional energy savings receive a higher award at higher levels of energy savings. Although the Company's incentive is capped so that the incentive is never greater than $0.0875 (8.75 cents) per kWh saved on average, the incremental incentive that Xcel is awarded is much greater. DOC Ex. 419 at 3 (Davis Surrebuttal).

497. Mr. Davis' Surrebuttal Table 1 showed that, at the energy savings levels that the Company has achieved in recent years, the incentive the Company receives for achieving an additional kWh of savings is as high as 18.7 cents per kWh. Thus, it would be irrational for Xcel to cut back on its energy savings achievements even if it appeared that a hard cap would impact the Company's revenue deferrals. Xcel can make far more money by saving a marginal unit of energy than by making additional sales. DOC Ex. 419 at 3 (Davis Surrebuttal).

Table 1: Xcel's Average and Marginal DSM Financial Incentives at Different Levels of Energy Savings

Savings as Percent of Retail Sales	Average Incentive per kWh Saved	Marginal Incentive per kWh Saved
0.5%	$0.012	$0.058
0.6%	$0.018	$0.047
0.7%	$0.023	$0.058
0.8%	$0.029	$0.070
0.9%	$0.035	$0.082
1.0%	$0.041	$0.093
1.1%	$0.047	$0.105
1.2%	$0.053	$0.117
1.3%	$0.058	$0.128
1.4%	$0.064	$0.140
1.5%	$0.070	$0.157
1.6%	$0.076	$0.163

1.7%	$0.082	$0.175
1.8%	$0.088	$0.187
1.9%	$0.088	$0.088
2.0%	$0.088	$0.088

498. Mr. Davis provided an example of what would happen if Xcel abandoned its present energy conservation practice, to illustrate this point. DOC Ex. 419 at 4-6 (Davis Surrebuttal). As a result, the Commission can approve a hard cap for Xcel's decoupling mechanism without concern that the hard cap might reduce the Company's interest in maximizing energy savings. DOC Ex. 419 at 6 (Davis Surrebuttal).

499. In Rebuttal Testimony, CEI's witness Mr. Ralph Cavanagh also disagreed with the hard cap that the DOC proposed because, he theorized, a hard cap would partly restore the conflict of interest that the decoupling mechanism was trying to overcome. DOC Ex. 419 at 6 (Davis Surrebuttal) (citing CEI Ex. 294 at 4-5 (Cavanagh Rebuttal)). The DOC disagreed. First, as discussed above, due to existing energy savings incentives, Xcel has an enormous incentive to continue to save energy even if the Company believes it may encounter the hard cap. Second, the Commission has to strike a balance in public policy objectives. Whether it makes sense to approve a decoupling mechanism for Xcel is a judgment call based on several requirements in Minnesota statutes. DOC Ex. 417 at 36 (Davis Direct).

500. The DOC recommends approval of full decoupling for Xcel on a pilot basis but is increasingly concerned with the cost to ratepayers of both the Shared Savings incentive mechanism and decoupling. Further, the Commission approved a hard cap for MERC in Docket G007,G011/GR-10-977 and for CenterPoint Energy in Docket No. G008/GR-13-316. The Commission should protect Xcel's ratepayers in the same way in this docket. There is no reason why electric ratepayers should have less protection than gas ratepayers. DOC Ex. 419 at 7 (Davis Surrebuttal).

501. With respect to the reasonable percentage of any cap, Mr. Davis explained that Xcel had proposed a soft cap on RDM surcharges equal to five percent of base revenue, excluding fuel and all applicable riders if the Commission approves the proposed partial RDM decoupling mechanism, or a soft cap on RDM surcharges equal to ten percent of base revenue, excluding fuel and all applicable riders if the Commission approves a full decoupling mechanism. DOC Ex. 419 at 7 (Davis Surrebuttal). Mr. Davis compared Xcel's proposals to the caps DOC and AARP proposed. Mr. Davis' Surrebuttal Table 3 showed a comparison of the different caps on maximum annual surcharges and average annual bill impacts.[152]

[152] Also, Xcel's two cap levels (5 percent and 10 percent) are not directly comparable to the caps proposed by AARP (2 percent) and the Department (3 percent) because Xcel's cap is soft-and a mere deferral-- while AARP and the Department propose hard caps.

Table 3: Comparison of Different Cap Levels[153] on Maximum Annual Customer Class Surcharges and Average Annual Bill Impacts

	2%	**3%**	**5%**	**10%**
Residential Surcharge	$20,984,320	$31,476,480	$42,530,835	$85,061,670
Residential Avg. Annual Bill Increase	$19	$29	$39	$78
Space Heating Surcharge	$794,400	$1,191,600	$1,522,552	$3,045,103
Space Heating Annual Bill Increase	$25	$37	$47	$94
Non-Dem. Small C&I Surcharge	$2,322,700	$3,484,050	$4,421,761	$8,843,522
Non-Dem. Small C&I Annual Bill Increase	$27	$40	$51	$102
Total Surcharge	**$24,101,420**	**$36,152,130**	**$48,475,148**	**$96,950,295**

DOC Ex. 419 at 7 (Davis Surrebuttal). Table 3 shows that Xcel's proposed caps of five percent for partial decoupling and ten percent for full decoupling could result in significant surcharges for the impacted customer classes. DOC Ex. 419 at 7 (Davis Surrebuttal). Further, Mr. Davis' analysis of the data provided by Xcel (DOC Ex. 419 at 8 and CD-S-1) (Xcel Response to DOC IR 334) (Davis Surrebuttal)) indicated that the residential customer class would have encountered a two percent cap under full decoupling in 2004 and 2009, but would not have encountered a three percent or higher caps. The residential with space heating customer classes would have encountered two and three percent caps in 2006 and the two, three and five percent caps in 2012 under full decoupling. The small C&I non-demand metered customers only would have encountered a cap once, under partial decoupling in 2011, and it would have been a two percent cap. DOC Ex. 419at 8-9 (Davis Surrebuttal).

502. The DOC recommends that the Commission approve the Department's proposed cap of the percent of base revenues including fuel and applicable riders. The three percent hard cap would limit ratepayers' exposure to potentially large surcharges. At the same time, Mr. Davis' extensive analysis indicates that the three percent cap would rarely be encountered. Over the ten-year period Mr. Davis' analysis showed that enforcement of the three percent cap would have limited no surcharges under full decoupling. Under partial decoupling the three percent cap would have limited surcharges only to the residential space heating customer class, and only for two years for a total of $905,000. Xcel's focus on asking for larger caps is misguided. DOC Ex. 419 at 9 (Davis Surrebuttal).

---

[153] The 2 and 3 percent caps are calculated using base revenues, fuel and all applicable riders. Calculation of the 5 and 10 percent caps are based on percentage of base revenue, *excluding* fuel and applicable riders.

503. The Commission should be guided by overall energy policies. While it could be argued that AARP's two percent cap does a better job of protecting ratepayers than the three percent cap DOC proposed, the balance for the Commission to strike concerns the protection of ratepayers and the Commission's policy goals regarding energy conservation. The DOC concluded that the three percent hard cap on full decoupling, such as Mr. Davis recommended, strikes a reasonable balance if the Commission approves decoupling. DOC Ex. 419 at 7 (Davis Surrebuttal).

3. DOC Recommends a Pilot Revenue Decoupling Program that Extends Only to Some Classes of Customers

504. Because Xcel's proposed RDM is not reasonable, if the Commission chooses to approve a decoupling plan as part of Xcel's rate design, DOC recommended that the Commission mitigate the harm to ratepayers by approving only a full decoupling mechanism with the following features:

a) The Commission approve no cap on decoupling refunds, but a hard cap on surcharges that, including fuel and all applicable riders, is an amount no greater than 3 percent of total customer group revenue.

b) Xcel not be allowed to surcharge customers in any year after the Company fails to achieve energy savings equal to 1.2 percent of retail sales.

c) The pilot program run for three years.

505. If the adverse impact of a decoupling mechanism on ratepayers is not mitigated by employing a full decoupling mechanism with these features, the DOC recommends that the Commission not approve a decoupling mechanism and instead maintain traditional rate regulation for the three affected classes. DOC Ex. 419 at 14-15 (Davis Surrebuttal).

506. DOC recommended that the Commission approve a full decoupling mechanism for Xcel as a pilot project. DOC Ex. 417 at 36 (Davis Direct), for several reasons. First, the Minnesota Commission has not approved any type of decoupling for an electric utility. Approving full decoupling for Xcel as a pilot program would provide an excellent opportunity for the Commission to observe the benefits and costs of full decoupling for an electric utility. DOC Ex. 417 at 36 (Davis Direct).

507. Second, Mr. Davis' analysis indicates that full decoupling would have increased costs (as compared to traditional rate regulation for ratepayers) under some scenarios, but under some scenarios could actually lead to cost reductions. DOC Ex. 417 at 36-37 (Davis Direct).

508. Third, a decoupling mechanism would work in conjunction with a Shared Savings DSM financial incentive mechanism. The Department may propose lower Shared Savings DSM financial incentives for Minnesota utilities in 2015 so that the costs of the incentives for ratepayers are more in line with incentive mechanisms in other states. Mr. Davis believed that approving full decoupling along with lower incentives would provide an appropriate mix of

energy savings policies so that Xcel is motivated to surpass its past achievements while minimizing costs to ratepayers. DOC Ex. 417 at 37 (Davis Direct).

509. More fundamentally, Xcel did not show that it is reasonable for the Commission to order decoupling as a permanent project, rather than on a pilot basis. The only reason offered by Xcel was in the testimony of Xcel Witness Dr. Hansen, who noted that the Commission's June 19, 2009 Order in Docket No. E,G999/CI-08-132 required all pilot proposals to be filed by December 30, 2011; for that reason, Dr. Hansen postulated that Xcel's proposed RDM mechanism would be ineligible for pilot program status. DOC Ex. 417 at 37 (Davis Direct) (*citing* Xcel Ex. 109 at 16 (Hansen Direct)). Order point 3 of the Commission's December 30, 2011 Order states, "All decoupling pilot proposals shall be filed by December 30, 2011." DOC Ex. 417 at 37 (Davis Direct).

510. Dr. Hansen drew the wrong conclusion from the facts regarding timeliness. The Commission is not precluded by prior Orders from approving a pilot project The Commission always has the ability to reopen its Orders and take other actions within its authority to protect ratepayers, and merely needs a reasonable basis for doing so. Approving a rate mechanism as a pilot project signals that the project is new or unusual, as is certainly the case with the first decoupling project for an electric utility. The pilot status also indicates that the Commission has an interest in monitoring the project to see how it performs and make any necessary adjustments over time. Because decoupling is relatively new in Minnesota, a pilot status would be a reasonable approach. DOC Ex. 417 at 38 (Davis Direct). Prior to the evidentiary hearing Xcel agreed that any decoupling mechanism should be approved as a three-year pilot program. DOC Ex. 447 at 1 (Davis Opening Statement).[154]

511. DOC also did not recommend extending the full decoupling pilot program to all of Xcel's customer classes. Although in the long run the Commission may be interested in ensuring that Xcel does not have an incentive to increase sales to its larger customers, this is a pilot project and Mr. Davis recommended starting with a small number of customer classes. DOC Ex. 417 at 38 (Davis Direct). OAG-RUD Witness Mr. Ron Nelson discussed that Xcel did not support its decision to decouple only the Residential and Commercial and Industrial Non-Demand rate classes. OAG-RUD Ex. 375 at 58 (Nelson Direct). Mr. Davis responded in his Rebuttal Testimony, and addressed whether there was a theoretical basis at this time for extending decoupling to more rate classes. Mr. Davis observed that the throughput incentive occurs when a utility can make more money by selling additional units of energy to a customer. Although Xcel states that the residential and non-demand-metered customer classes pay a higher percentage of base revenues through the energy charge than the other Xcel rate classes (Xcel Ex. 109 at 13-14 (Hansen Direct)), the Company can still earn a profit by selling more energy to

[154] Xcel also agreed that, under a revenue decoupling mechanism, Xcel would not be allowed to surcharge customers in the year after the Company fails to achieve energy savings equal to 1.2 percent of retail sales; that there would be no cap on refunds to customers under the decoupling mechanism; and that DOC's suggested modifications to the Company's evaluation plan were reasonable. DOC Ex. 447 at 1 (Davis Opening Statement).

those customer classes. Although the margin per kWh sold is lower for these customer classes, the use per customer is higher than for the Residential class. DOC Ex. 418 at 2 (Davis Rebuttal).

512. DOC cautions that there are potential costs of extending the RDM to additional customer classes. As discussed above, Mr. Davis, in DOC IR No. 312 had asked Xcel to estimate the differences in revenues that would have been collected from all of its customer classes for the years 2009 through 2013 under traditional rate regulation, full decoupling, and partial decoupling. DOC Ex. 417 at 25-26 and CD-2 (Davis Direct); DOC Ex. 418 at 2 (Davis Rebuttal).

513. In response to the concern of Mr. Nelson, Mr. Davis reiterated in his Rebuttal that implementation of partial decoupling during years 2009-2013 would have cost the residential (with and without space heating) customers and the non-demand-metered commercial customers $72.7 million more than traditional rate regulation (DOC Ex. 417 at 28 (Davis Direct)) while full decoupling would have cost the same customer classes $15.8 million more over the same period. DOC Ex. 417 at 28 (Davis Direct); DOC Ex. 418 at 2-3 (Davis Rebuttal)). If decoupling had also been extended to Xcel's small commercial demand-metered, large commercial, public authority, and lighting customer classes, however, partial decoupling would have cost customers an additional $77.4 million more than traditional rate regulation and full decoupling would have cost an additional $45.4 million. DOC Ex. 418 at 3 (Davis Rebuttal).

514. As shown in DOC Ex. 418 CD-R-1, Xcel estimated that consumption by the large commercial, public authority, and lighting customer classes is not impacted by weather and thus the impacts of partial and full decoupling would be similar. DOC Ex. 418 at 3 and CD-R-1 (Davis Rebuttal). Xcel estimated that partial decoupling would have cost the small commercial demand-metered customers $5.1 million more than traditional rate regulation during the 2009-2013 period, while full decoupling would have cost the same customer class $30 million more during the same period. DOC Ex. 418 at 2 and CD-R-1 (Davis Rebuttal).

515. From this information, Mr. Davis reached certain conclusions. He explained that a review of what the costs would have been for 2009-2013 indicates that full decoupling may be less costly than partial decoupling if all customer classes are considered. DOC Ex. 418 at 3 (Davis Rebuttal). For the same period, however, full decoupling would have cost the demand-metered, small commercial customer class considerably more than partial decoupling, the opposite result of the residential customer class. DOC Ex. 418 at 3 (Davis Rebuttal).

516. Given that Mr. Davis recommended that decoupling be approved for Xcel on a pilot basis, he also recommended that the Commission not extend decoupling to additional customer classes at this time. DOC Ex. 418 at 3-4 (Davis Rebuttal). Towards the end of the pilot period this decision could be re-evaluated. DOC Ex. 418 at 4 (Davis Rebuttal).

517. Xcel, in its Initial Brief, acknowledges that in Minnesota, the legislative "purpose of decoupling" is set forth in Minn. Stat. § 216B.2412, (Xcel Initial Br., at n. 602) and that the Department determined Xcel's proposed "partial" decoupling proposal to be unreasonable because of its "adverse impact on customers." Xcel Initial Br. at 149. Xcel nevertheless incorrectly argues that the Department's concern over that adverse impact on ratepayers is

misguided because, "the inclusion or exclusion of weather has nothing to do with fulfilling the statutory purpose of decoupling: to reduce the conservation disincentive." Xcel Initial Br. at 149.

518. Xcel's argument is incorrect because it misstates the law as set forth in Minn. Stat. § 216B.2412. The goal of "reducing the conservation disincentive" is only part of the statutory guidance. When the Commission establishes criteria and standards for decoupling, it must "design the criteria and standards to mitigate the impact on public utilities of the energy-savings goals under section 216B.241 **without adversely affecting utility ratepayers."** And, in designing the criteria, the commission must consider **weather** among other factors. Minn. Stat. § 216B.2412. Thus, the Commission is required by the statute to consider weather when designing its decoupling program and must not adversely affect ratepayers. The statutory intent of decoupling is to reduce the utility's disincentive to promote energy savings while not harming ratepayers. DOC Ex. 417 at 17 (Davis Direct).

519. It is clear from Mr. Davis' Rebuttal Testimony that, during the ten-year period of 2004 to 2013, Xcel's ratepayers would have paid $77 million more under partial decoupling, which excludes consideration of weather, as compared to full decoupling which takes weather into consideration. DOC Ex. 419 at 14 (Davis Surrebuttal). The consideration of weather—and the adverse-effect on ratepayers of not considering weather—must be taken into account by the Commission in designing any decoupling program.

520. Xcel's Initial Brief criticized the Department's analysis, based on Xcel's Rebuttal testimony, as follows:

> The Department's analysis is also dependent on the pilot period sharing economic and weather characteristics *with the recent past*. The Company showed the purported advantages of full decoupling over partial decoupling either vanish or become disadvantages with simple changes in weather assumptions.

Xcel Initial Br. (citing Ex. 110 at 5-8 (Hansen Rebuttal)). This criticism is not well founded because it was addressed in the Department's Surrebuttal testimony, where the Department extended the scope of its analysis to assess data and scenarios from an entire decade. DOC Ex. 419 at 12-14 (Davis Surrebuttal). In this more extensive analysis, the full decoupling design was shown to be clearly superior to a partial decoupling design in protecting ratepayers against unwarranted adverse impacts. DOC Ex. 419 at 14 (Davis Surrebuttal).

3. ALJ Recommendations concerning a potential full decoupling mechanism

521. The ALJ finds that the Company has not shown its proposal to be just and reasonable. The ALJ rejects Xcel's proposed RDM revenue decoupling proposal, and instead recommends approval a three-year pilot full revenue decoupling mechanism for Xcel's residential and non-demand-metered customer classes with the following provisions:

1. Accept Xcel's 2013-2015 combined electric and gas CIP, as approved by the Deputy Commissioner of the Department in Docket No. E,G002/CIP-12-447, as

satisfying the filing requirement for conservation improvement plans and rate case filings specified in Minn. Stat. §216B.241, subd. 1.

2. Approve the zeroing out of Xcel's Conservation Cost Recovery Charge (CCRC) when Xcel's new rates go into effect and instead recover all CIP costs through the Conservation Adjustment Factor (CAF).

3. In the event that the Commission does not approve the zeroing out of Xcel's CCRC and recovery of all of Xcel's CIP costs through the CAF, I recommend that the Commission approve Xcel's proposed test-year Conservation Improvement Program (CIP) expenses of $90,715,761, and approve Xcel's proposed volumetric CIP cost allocation method.

4. Reject Xcel's proposed RDM revenue decoupling proposal.

5. Approve a three-year pilot full revenue decoupling mechanism for Xcel's residential and non-demand-metered customer classes with the following provisions:

   a) The Commission approve no cap on decoupling refunds, but a hard cap on surcharges, that, including fuel and all applicable riders, is in an amount no greater than 3 percent of total customer group revenue.

   b) Xcel not be allowed to surcharge customers in any year after the Company fails to achieve energy savings equal to 1.2 percent of retail sales.

   c) The pilot program run for three years.

See DOC Ex. 417 at 38-39 (Davis Direct); DOC Ex. 419 at 15 (Davis Surrebuttal); DOC Ex. 447 at 1-2 (Davis Surrebuttal).

522. The test-year financial operating income effect of the DOC's recommendation decreases both the test-year retail revenue and customer service & information expense by $90,716,000, as detailed in DOC 442 DVL-16, and as shown in DOC Ex. 442 DVL-S-7, column (ad) (Lusti Surrebuttal); DOC Ex. 442 at 34 (Lusti Surrebuttal).

FF. Interest Synchronization Methodology and Calculation (Issue 49A)

Resolved between DOC and Xcel: DOC accepted Xcel's proposed methodology; DOC and Xcel agreed that final interest synchronization calculation will occur after the Commission determines all cost of debt, rate base and income statement adjustments in this proceeding. DOC Ex. 437 at 43-44 (Lusti Direct) and DOC Ex. 442 at 34 (Lusti Surrebuttal).

523. Xcel proposed to calculate its interest-expense deduction for test-year income-tax purposes by multiplying its rate base by the weighted cost of debt, which is 2.25 percent. DOC Ex. 437 at 43 (Lusti Direct); DOC Ex. 442 at 34 (Lusti Surrebuttal). The Department accepted Xcel's methodology.

524. Although the DOC agreed with Xcel's methodology, it noted that when an adjustment is made to the Company's weighted cost of debt, test-year rate base or operating income statement, it is also necessary to make an interest-synchronization adjustment. DOC Ex. 437 at 43-44 (Lusti Direct). Calculation of the final interest synchronization will occur after the Commission determines all cost of debt, rate base and income statement adjustments in this proceeding. DOC Ex. 437 at 43-44 (Lusti Direct) and DOC Ex. 442 at 34 (Lusti Surrebuttal); no decision is needed by the ALJ on the result of the calculation. At the evidentiary hearing, the DOC calculation of the adjustment for interest synchronization was detailed in DOC Ex. 451 DVL-EH-4, Page 3 of 3, Column (ae) (Lusti Opening Statement). The adjustment increased the test-year income taxes by $1,848,000. This adjustment resulted from the application of interest synchronization to the various DOC test-year adjustments. DOC Ex. 442 at 34 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-4, Page 3 of 3, Column (ae) (Lusti Opening Statement).

GG. Test-Year Operating Income Summary and Summary of 2014 Test Year Financial Issues

1. Test-Year Operating Income Summary

525. In his Opening Statement, as a result of the various DOC adjustments, Mr. Lusti's recommended test-year operating income was $448,348,000 as shown in DOC Ex. 451, DVL-EH-6, Column (c) (Lusti Opening Statement). This amount compares to Xcel's proposed level of $396,621,000.

2. Summary of 2014 Test Year Financial Issues

526. In his Opening Statement, Mr. Lusti testified that, at that final stage of the proceeding, all of the adjustments identified in the Opening Statement of Xcel Witness Anne E. Heuer that related to Department positions, had been incorporated into his final calculations of revenue requirement. His attachment to his Opening Statement, entitled "Summary of Revenue Requirements" (DOC Ex. 451 DVL-EH-2 (Lusti Opening Statement)) summarizes the various elements used to compute the revenue requirements (revenue deficiency) under present rates for the test year of January 1, 2014, through December 31, 2014.

- Column (a), line (7), is the Company's revenue deficiency for the test year. Xcel calculated a test-year revenue deficiency of $192,710,000 under present rates.

- Column (b) shows the DOC's June 5, 2014 Direct Testimony calculation of the test-year revenue deficiency to be $61,616,000.

- Column (c) shows the DOC's August 4, 2014 Surrebuttal Testimony calculation of the test-year revenue deficiency to be $43,221,000.

- Column (d) shows the calculation of the DOC's proposed revenue deficiency under present rates for the test year, assuming an overall rate of return of 7.31 percent per the testimony of Dr. Eilon Amit. Line (7), shows that the DOC's proposed revenue deficiency is $45,887,000.

527. In summary, the DOC recommended adjustments totaling $146,822,000 to Xcel's proposal, resulting in a final revenue requirement for the 2014 test year of $45,887,000 as compared to Xcel's initial request of $192,709,000. This change from Mr. Lusti's Surrebuttal position reflected the DOC and Xcel agreed-upon adjustment to the PI EPU cancelled plant.

528. As discussed further below, the Department also recommended a 2015 STEP increase of $66,499,000 for a total increase over the two years of $112,386,000. DOC Ex. 451 at 1-2 (Lusti Opening Statement).

VI. 2015 STEP YEAR RATE BASE AND INCOME STATEMENT ADJUSTMENTS

HH. 2015 STEP – Xcel's STEP Methodology and Calculation

529. In his Direct Testimony, Mr. Lusti explained his methodology, describing how he incorporated the 2015 STEP adjustments into his revenue requirements: He began with the DOC recommended rate base and income statements for the 2014 test year. Mr. Lusti then created a 2015 STEP Rate Base and Operating Income respectively by adding to each of those two items Xcel's 2015 STEP adjustments as well as the DOC STEP adjustments. DOC Ex. 437 at 46 (Lusti Direct). This is a reasonable methodology and is also Xcel's initial STEP adjustment.

530. DOC Ex. 438 DVL-26 identifies Xcel's STEP rate base adjustments of $411,505,000. The adjustment is simply the difference between Xcel's 2015 STEP rate base and its 2014 test year rate base. DOC Ex. 437 at 47 (Lusti Direct); DOC Ex. 451 DVL-EH-22, column (a) (Lusti Opening Statement).

531. DOC Ex. 438 DVL-27 (Lusti Direct Attachments) identifies Xcel's STEP operating income adjustment of a negative $26,331,000. The adjustment is the difference between Xcel's 2015 STEP operating income and its test year operating income. DOC Ex. 437 at 50 (Lusti Direct); DOC Ex. 442 at 38 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-24, column (a) (Lusti Opening Statement).

II. 2015 STEP – General Ledger IT (Issue 28)

Resolved between DOC and Xcel: DOC agreed that Xcel had demonstrated that the expense was reasonably included in the 2015 Step Year Expenses. DOC Ex. 427 at 7-10 (Byrne Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement).

532. The Business Systems organization is the centralized information technology organization, providing technology services across all operating companies including the Company. These services include support for the following business operations:

- Foundational Technology Infrastructure;
- Systems Controls;
- Customer Support; and
- Corporate Support.

DOC Ex. 423 at 18 (Byrne Direct) (*citing* Xcel Ex. 62 at 2-3 (Harkness Direct)).

533. Xcel budgeted total Business Systems capital additions to be placed into service in the 2014 test year to be $69.2 million, or $53.3 million on a Minnesota Electric Jurisdictional basis. DOC Ex. 423 at 18 (Byrne Direct) (*citing* Xcel Ex. 62 at 25 (Harkness Direct)). Approximately 75 percent of the total budget consists of 14 projects. DOC Ex. 423 at 18 (Byrne Direct) (*citing* Xcel Ex. 62 at 25-48 (Harkness Direct)).

534. In the 2015 Step test year, Xcel proposed to include $33 million in total Company capital additions ($24.3 million Minnesota Electric Jurisdiction), consisting of two projects: General Ledger Replacement (GL System) for $27.721 million total Company and the Regulatory Process Standardization for $5.313 million total Company. DOC Ex. 423 at 18-19 (Byrne Direct)(*citing* Xcel Ex. 62 (DCH-1) Schedule 2 at 1 (Harkness Direct)). Although Mr. Harkness initially stated that both projects were estimated to go into service in the second quarter 2015, DOC Ex. 423 at 19 (Byrne Direct) (*citing* Xcel Ex. 62 at 51 and 53 (Harkness Direct)), in discovery, Xcel provided an original and currently estimated in-service date of December 31, 2015, which was not consistent with the statement in Mr. Harkness' Direct Testimony that the original ISD for that project would be "second quarter 2015." DOC Ex. 423 at 19 (Byrne Direct) (*citing* DOC Ex. 430 NAC-25 (Campbell Direct Attachments) (DOC IR 123)).

535. Ms. Byrne requested additional information (DOC Ex. 424 ACB-8 (Byrne Direct Attachments) (DOC IR 2124); DOC Ex. 424 ACB-9 (Byrne Direct Attachments) (DOC IR 2125); DOC Ex. 423 at 19-20 (Byrne Direct)). In response, Xcel explained that the Harkness Testimony would need correction. Regarding completion of various stages of the project and whether the GL System would be fully in-service by December 31, 2015, Xcel provided further information in the Rebuttal testimony of Mr. Harkness. Ms. Byrne, in her Surrebuttal, concluded that the information provided by Mr. Harkness supported Xcel's position that the new GL System will provide benefits to the Company and to ratepayers, and therefore would be used and useful, before January 1, 2016. DOC Ex. 427 at 9-10 (Byrne Surrebuttal). Accordingly, she withdrew her initial recommended adjustment to reduce 2015 STEP rate base by $8,790,000 and considered this issue to be resolved. In her Opening Statement, Ms. Byrne reiterated that because Xcel provided reasonable support for its in-service date in its Rebuttal Testimony, and she no longer recommended an in-service date of January 1, 2016 for the Company's new GL System. She agreed that the Company had demonstrated that the expense was reasonably included in the 2015 Step Year Expenses. DOC Ex. 427 at 7-10 (Byrne Surrebuttal); DOC Ex. 449 at 2 (Byrne Opening Statement).

536. Ms. Byrne notes in her Surrebuttal Testimony at page 10 that she no longer recommends a 2015 STEP adjustment for IT General Ledger. DOC Ex. 442 at 38 (Lusti Surrebuttal).

JJ. 2015 STEP – Pleasant Valley & Border Winds (Issue 30)

Resolved between Xcel and the Department: DOC no longer recommends a downward capital cost adjustment for the 2015 Step of $5,672,482 (which was to account for both Pleasant

Valley and Border Winds excess costs).[155] Xcel agrees with DOC to include an estimated level of production tax credits (PTC) in base rates, subject to a true-up of Production Tax Credit (PTC) levels through the Minnesota renewable energy standard (RES) Rider; Xcel adjusted the 2015 Step on Robinson Schedule 1 to incorporate the revenue requirement reduction associated with the estimated PTCs revenue credits of $11.903 million.[156] For the two wind projects DOC prefers rate base treatment, but is not opposed to the RES Rider recovery recommended by MCC if that is the Commission's preference, particularly if Xcel does not otherwise increase its rates in 2016.[157]

537. The DOC no longer recommends a downward adjustment for the 2015 Step to reflect the extent that Xcel's capital costs for Pleasant Valley and Borders Wind Projects exceeded Commission-approved amounts in MPUC Docket Nos. E002/M-13-603 and E002/M-13-716, respectively. Ms. Campbell had expressed concern that, since the Pleasant Valley and Border Winds projects were selected through a competitive resource acquisition process, there should be a very high burden on the Company to justify any costs that exceed the competitive bid amount before recovery of excess costs is granted. If companies are not held to the competitive bid amounts, the bidding process is likely to become a useless tool or worse that parties may low bid their costs in order to be selected and then add additional costs later which, of course, would be inconsistent with the intent of the bidding process. Thus, as Ms. Campbell explained in her Direct Testimony, Xcel provided insufficient information to justify its capital costs over the Commission's approved amounts, and that Xcel had not included any offsetting revenue for expected Production Tax Credits (PTCs) in 2015, such that the Department recommended continued rider treatment to ensure true-up of all PTCs in the RES Rider.[158]

538. Xcel witness Mr. Robinson, on page 5 of his Rebuttal Testimony, reasonably supported the Company's request. He provided sufficient information to show that the difference in the capital costs for the two projects is primarily due to $5.96 million in allowance for funds used during construction (AFUDC). Moreover, the Department was able to confirm that about $8.4 million in AFUDC costs for both the Pleasant Valley and Border Winds was included in the strategist model, which exceeds the $5.96 million that Mr. Robinson notes was included in the 2015 step for rate case purposes on page 5 of his Rebuttal Testimony. Xcel also explained that it seeks rate base rather than rider treatment to comply with the Commission's recent request.[159]

539. The Department noted MCC's proposals for Renewable Energy Standard (RES) Rider or use of a 13-month average for reasons including that it is unclear whether the projects will be in-service in 2015. Ms. Campbell believes that Commission desires to minimize riders,

---

[155] DOC Ex. 435 at 3-5 (Campbell Public Surrebuttal).
[156] DOC Ex. 450 at 1 (Campbell Opening); Xcel Ex. 99 at 7 and Schedule 1 (Robinson Rebuttal).
[157] DOC Ex. 450 at 1 (Campbell Opening); DOC Ex. 435 at 7-11 (Campbell Public Surrebuttal).
[158] DOC Ex. 435 at 2-3, 6 (Campbell Public Surrebuttal); DOC Ex. 429 at 167 (Campbell Public Direct).
[159] DOC Ex. 435 at 3-4 (Campbell Public Surrebuttal); June 17, 2013 Order Establishing Terms, Conditions, and Procedures for Multi-Year Rate Plans (Multi-Year Rate Plan Order).

and she stated additional reasons that the Department favors rate case (rate base) treatment in 2015, and stated her opposition to use of a 13-month average and instead preferred continued use of beginning of year and end of year average for purposes of rate cases. Nonetheless, the Department would not oppose RES Rider recovery recommended by MCC if that is the Commission's preference, particularly if Xcel does not otherwise increase its rates in 2016.[160]

540. The DOC recommendation increases the 2015 STEP operating income by $6,504,000, as shown in DOC Ex. 451 DVL-EH-24, column (c) (Lusti Opening Statement); DOC Ex. 442 at 38 (Lusti Surrebuttal).

541. The ALJ finds that the Department's recommendations are reasonable.

KK. 2015 STEP – 2015 In-Service Date Changes (Issue 11)

542. The basis for this adjustment is discussed above in Section IV. L. The DOC's recommendation increases the 2015 STEP rate base by $604,000, as detailed in DOC Ex. 438 DVL-15 (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-HE-22, column (d) (Lusti Opening Statement);and increases the 2015 STEP operating income by $1,249,000, as detailed in DOC Ex. 438 DVL-15, Column (b) (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-HE-24, column (d) (Lusti Opening Statement); DOC Ex. 437 at 47 and 51 (Lusti Direct); DOC Ex. 442 at 39 (Lusti Surrebuttal).

LL. 2015 STEP – 2015 Passage of Time for 2015 Depreciation and 2015 Retirements (Issue 10)

Disputed between Xcel and the Department: To reflect Xcel's lower rate base in 2015 for facilities that are retired in 2015, and to reflect depreciation expense and accumulated depreciation step-down in rate base due to the passage of time in 2015 for projects in-service (depreciated) in 2014, DOC recommends: 1) a downward adjustment of $535,552 to the Company's revenue requirement for 2015 to reflect the 2015 retirements for transmission and distribution facilities; and 2) the $17,529,000 reduction to 2015 revenue requirements for 2015 depreciation expense and accumulated depreciation due to the passage of time for all plant in rate base, except 2015 step projects already incorporated in the 2015 step revenue requirement, or as finally calculated by Mr. Lusti. [161]

543. The Department's "passage of time" adjustment is based on Xcel's failure to show that it is reasonable *not* to reflect a downward 2015 Step adjustment that accounts for Xcel's decreasing costs in 2015 due to retirements and depreciation of facilities included in the 2015 Step. On cross-examination, Ms. Campbell gave the following example to illustrate how depreciation paid in 2014 should lower Xcel's rate base in 2015 upon which ratepayers will pay a return in 2015, and how decreasing the rate base in 2015 for rates would be similar to how costs are reflected in a rider:

---

[160] DOC Ex. 435 at 7-11 (Campbell Public Surrebuttal); DOC Ex. 450 at 1 (Campbell Opening).
[161] DOC Ex. 429 at 175-176 (Campbell Public Surrebuttal); DOC Ex. 435 at 119-120 (Campbell Public Surrebuttal).

> So, my very simple example of you have a $100 asset, you have a . . . 10-year life, so it's . . . $10 of depreciation every year. So year one you record the $10 of depreciation expense and reduce the asset to $90 because of the accumulated depreciation, that's the stepdown, and the second year you start with a $90 rate base. You need to capture that $10 stepdown.
>
> And what happened in 2014 is [for] the projects not picked up in the step, we didn't capture that stepdown, even though we gave recovery of depreciation expense. In a rider that would happen because you continually do a new balance for the next year, and that would happen. And to me it reminds me of when the Chamber made the argument on wind facilities in a prior rate case and they wanted rider recovery of something, and it's because it continues you get that stepdown. And especially when it's an expensive asset with a short life, that stepdown can be material, especially when you have a big rate base.
>
> * * *
>
> . . . [In a] rate case . . . usually we just do it on one year, but now we've introduced this second year.

The Department's passage of time adjustment does not apply to capital projects that are in-service for the first time in 2015 and are included in the 2015 Step revenue requirement (no depreciation would have occurred in 2014, and a new 2015 project in the Step would not be retired in 2015).[162]

544. Ms. Campbell stated the following reasons for the Department's passage of time adjustments:

- practically, the Company's 2015 rate base is lower for existing plant in rate base (not including 2015 capital step projects) as result of 2015 retirements and 2015 depreciation expense and accumulated depreciation recorded due to the passage of time, so ratepayers should not pay a return on a higher 2014 rate base which the Company is not actual incurring, for purposes of the 2015 step;

- equitably, it is unfair not to update for the 2015 retirements and 2015 depreciation expense and accumulated depreciation for the passage of time for existing plant in rate base for which ratepayers are currently paying, while at the same time requiring ratepayers to

[162] Tr.V. 5 at 62-63 (Campbell); DOC Ex. 435 at 109-110, 115 (Campbell Public Surrebuttal).

pay for higher depreciation amounts and higher rate base amounts caused by the 36 capital projects in the Company's 2015 step; and

- updating for 2015 plant retirements and 2015 depreciation and accumulated depreciation is consistent with the Department's comments and Commission's Order in the [Multi-Year Rate Plan] MYRP (as discussed in more detail in my Section III of my Direct Testimony) where updates for capital and capital related items such as depreciation and taxes are appropriate. [163]

545. Xcel opposes both the concept of DOC's recommendation as well as the calculation of the adjustment. [164]

1. Xcel's opposition to the principle of lowering the 2015 rate base to reflect depreciation and accumulated depreciation, for capital projects not included in the 2015 Step, is unreasonable

546. Xcel opposed the concept of the Department's passage of time adjustment for several reasons. For example, the Company stated that there is no mismatch or imbalance between projects included in the 2015 Step and the associated depreciation costs. The Department disagreed. Ms. Campbell explained the skewed, one-sided nature of Xcel's proposal:

> [T]he Company's 2015 Step method does a good job of capturing all increases in capital investment, but does not capture the reduction in 2014 capital projects (rate base) due to the normal passage of time, for projects that the Company did not include in its 2015 Step. This imbalance is why I believe the Company's proposal is one-sided and unreasonable.

547. Xcel selected 36 capital projects for its 2015 Step which either were projects that would go into service for part of 2014 or in-service in 2015, so for all of these 2014 projects depreciation was annualized. Thus, Xcel captured the full revenue requirement for those 36 projects included in the 2015 Step, but ignored the decrease in revenue requirement associated

---

[163] DOC Ex. 429 at 175-177 (Campbell Public Direct); DOC Ex. 435 at 110 (Campbell Public Surrebuttal).

[164] *See generally* Xcel's draft Issue's List, at 13-14 of 69. Xcel made the unsupported and unreasonable claim that if Commission adopts DOC's adjustments, the Company should be allowed to request its full 2015 revenue requirement (capital and non-capital related) rather than the limited number of capital projects it included in the 2015 Step in its rate case request because while some costs related to facilities in the Step are decreasing, there are costs not in the Step that are increasing. If properly calculated, Xcel believes a revenue requirement increase of $1.9 million would result. *Id.*

with non-Step facilities in 2015 due to depreciation and accumulated depreciation in 2015 due to the passage of time and due to retirements in 2015.[165]

548. Xcel witness Mr. Clark also argued that it did not annualize capital projects placed in service during 2014 to determine the 2015 Step revenue requirement, *except for the limited number of projects that were specifically included in the 2015 Step.* Again, the Department disagreed; Xcel's exception proves the existence of the rules regarding the changes in depreciation costs for capital projects year to year. Ms. Campbell demonstrated that Xcel's "limited" number of capital projects added in to the revenue requirement for the 2015 Step represent over 72 percent of the level of revenue requirements proposes for 2015, and represent over 80 percent of the amount Xcel's claimed it could have requested for its 2015 rate base increase.[166]

549. Importantly, the Department pointed out that Xcel's reflection of an entire year of depreciation in 2015 for all 2014 capital projects in the 2015 Step contradicts Xcel's proposal not to capture the step down in rate base that occurs from 2014 to 2015. Ms. Campbell described Xcel's error and the necessity of the Department's passage of time adjustments, as follows:

> Xcel's proposal to increase partial year depreciation for projects placed in service in 2014 to reflect an entire year of depreciation in 2015 completely contradicts Xcel's proposal not to decrease rate base (by increasing accumulated depreciation reserve) in 2015 for all capital projects to reflect the passage of time. Moreover, in a tradition rate case depreciation and rate base is not annualized for capital projects that are placed in service in the test year, so the Company's argument that they are entitled to annualized depreciation for all 2014 projects in the 2015 Step is incorrect.
>
> Therefore, not capturing the step down in rate base that occurs from 2014 to 2015 due to the normal passage of time and includes known 2015 retirements for several capital projects being paid for by ratepayers via rate base is not reasonable and is one-sided. [167]

550. The Department also disagreed with Xcel's claim that Ms. Campbell's recommended Emissions Control Chemicals costs adjustment (Resolved Issues 15 and 33) of 50 percent of the Company's 2015 Step adjustment is inconsistent with the Department's adjustment for the passage of time depreciation for 2015 and 2015 retirements. Ms. Campbell agreed that chemical costs (and property taxes) are *expenses directly related to the 2015 Step*

---

[165] DOC Ex. 435 at 110-111, 112 (Campbell Public Surrebuttal) (*citing* Rebuttal Testimonies of Mr. Clark, page 33 and of Mr. Robinson, Schedules 4-9); DOC Ex. 429 at 175-177 (Campbell Public Direct).
[166] DOC Ex. 435 at 111, 112 (Campbell Public Surrebuttal); Tr.V. 5 at 61 (Campbell); DOC Ex. 435 at 115-116 (Campbell Public Surrebuttal) (2015 Step projects equal 81.3 percent of Xcel's claimed full 2015 rate base increase).
[167] *Id.* at 112-113.

capital investments, but she noted that depreciation expense/accumulated depreciation reserve and plant retirements are not simply expenses *related to* 2015 capital investments, but instead depreciation expense/accumulated depreciation *are* the actual capital investment being spread over the life of the facilities:[168]

> [Depreciation expense/accumulated depreciation reserve and plant retirements] are not simply expenses directly related to the 2015 capital investment, but instead are depreciation expense and offsetting depreciation reserve that are the actual capital investment costs being spread over the life of the facilities.
>
> This distinction is important. I note that it is necessary to make the adjustment for the passage of time (from 2014 to 2015) step down in rate base by recording depreciation expense and accumulated depreciation reserve *because it is known* that customers would pay too much for these costs if they continued to pay 2014 rates in 2015 in the context of a multi-year rate case. While I agree that the Company may recover costs of new capital added in 2015, *it is known* that the rate base also steps down in 2015 due to the passage of time and retirements. As a result, the difference needs to be captured (the same as would occur if recovery of capital costs were done through a rider).

551. Xcel witness Ms. Perkett opposed the Department's passage of time adjustments on several grounds including that Xcel does not consider the scope of the second year of a multi-year plan to be similar to a full test year where all changes in the historical asset base year over year would be factored in. Additionally, Ms. Perkett argued that if Xcel has requested a full 2015 forecast of its revenue requirement, it would have requested $713.4 million rather than the $579.9 million Step. Further, she argued that, since the full overall 2015 Step is increasing more than the 2015 proposal, it is not appropriate to reduce the revenue requirement for 2015, as Ms. Campbell recommends. Xcel, however, did not prove the reasonableness of these arguments.[169]

552. Most importantly, Xcel did not seek a rate increase in 2015 of $713.4 million. It is unreasonable for any consideration to be given to this figure since Xcel did not make such a request in its initial filing. Minn. Stat. § 216B.16, subd. 5 prohibits the Commission from allowing rates that exceed the level of rates requested by the public utility.

553. Additionally, the $713.4 million has not been examined or audited for accuracy or reasonableness. It would be unreasonable to consider this figure for comparison to Xcel's Step of $579.9 million *as if* Xcel's full 2015 revenue requirement would equal $713.4 million.[170]

---

[168] *Id.* at 113-114.
[169] *Id.* at 115, 117.
[170] *Id.* at 115.

554. Also, even if the $713.4 million figure had been fully examined, the Company's assertion that the 2015 Step is limited does not bear up in light of facts. Ms. Campbell noted that Xcel's request "is hardly limited since $579.9 million is 81.3 percent of $713.4 million." This fact means that the Company has captured a significant amount of possible capital projects that are plant additions that increase rate base and that Xcel annualizes for a full year of depreciation, but it has excluded retirements that decrease rate base. At the evidentiary hearing, Ms. Campbell summarized the inequity of Xcel's proposal:[171]

> 80 percent of the capital projects were captured in those 34 [2015 Step] projects . . . so it was a pretty material amount. And then we also realized when we were looking at that process that it didn't seem fair that we were going to capture all these capital additions for 2015, but we didn't capture the stepdown that occurs from 2014 to 2015, because when you do your depreciation in the [$]10 million, that also reduces the rate base for the second year. And so we felt that we needed to capture that.

555. Ms. Campbell identified another reason that Xcel's 2015 Step proposal is unbalanced such that the Department's passage of time adjustments are needed:[172]

> [T]he Company is basically using the 2014 peak rate base amounts and adding any new incremental 2015 peak rate base amounts, for its proposed rates in this rate case for customers. That approach is like adding two peaks together and asserting that it is the new peak, even though some of the first peak declined.

556. Finally, the Department addressed two concerns of Ms. Perkett, both of which are invalid. First, regarding the Department's 2015 depreciation adjustment for the passage of time, Ms. Perkett argued that Ms. Campbell selectively increased only the accumulated depreciation reserve for non-step projects placed in service for 2014, but did not include the increases in plant from this same group of projects, which increases rate base. The Department disagreed in that it asked Xcel in discovery (IR No. 2113) (NAC-32) to update all depreciation for the passage time, which would include all changes in depreciation expense and depreciation reserve, which the Company did not do. In any event, Ms. Campbell determined that it was it was not necessary for Xcel to update depreciation for the passage of time for capital projects that were in-service by the end of 2014, because:

> [A]ll 2015 Step projects (81.3 percent) were already updated by the Company in their 2015 Step. That is, because Xcel already annualized depreciation expense for the majority of projects, it was not necessary to ask for this information. The remaining 2015 non-step projects (18.7 percent) was not in the Company's revenue requirement proposal for this rate case, so I determined that it was

---

[171] *Id.* at 115-116; Tr.V. 5 at 61 (Campbell).
[172] *Id.*

> not necessary for Xcel to update the part of the rate case that was not a part of the Company's initial proposal.[173]

557. Similarly, for 2015 retirements (for transmission and distribution), Ms. Perkett testified that the Department's passage of time adjustments were inappropriate. The Department disagreed; ratepayers should not be required to pay for retired assets that are no longer used and useful.[174]

558. Ms. Perkett's rationale regarding 2015 retirements largely mirrored Xcel's position for the depreciation-related passage of time adjustments (i.e., that the scope of second year of a multi-year rate case does not include all changes in the historical asset base, and that if the Department's recommendation is allowed, the annualized plant depreciation expense for all the 2014 additions should be included). Ms. Campbell summarized why Ms. Perkett's concerns regarding Xcel forecasted 2015 transmission and distribution retirements are not valid:

> First, if the Company is allowed to add 36 capital projects, which increases rate base by $579.9 million and increases overall revenue requirements by $68.9 million (as shown on Robinson's Table 13 of his Direct Testimony) for the 2015 Step which are on top of the 2014 test year (basically the Company is adding together the peak of 2014 rate base with the peak of 2015 rate base, and concluding that is reasonable for setting rates) then clearly there is a need also to reflect forecasted 2015 transmission and distribution retirements.
>
> Second, I don't agree with the Company's statement that no retirements were forecasted for the 2015 step, since transmission and distribution is not tracked as individual retirements (like generation) but rather tracked via the average service life method and, therefore, I would expect ongoing annual retirement for transmission and distribution. I also note that the Company did add $73.4 million in transmission plant (or $10.2 million increase in revenue requirement) in the 2015 Step and $41.354 million in distribution plant (or $5.3 million increase in revenue requirement) in the 2015 Step (as shown on Tables 5 to 8 of Mr. Robinson's Direct Testimony). In light of these Company additions in transmission plant and distribution plant, it simply is unreasonable not to incorporate my recommended forecasted 2015 retirements of transmission and distribution plant also, that results in a downward adjustment of $535,552 to the Company's revenue requirement for 2015.

[173] DOC Ex. 429 at 163 (Campbell Public Direct); DOC Ex. 430 at NAC-32 (Campbell Public Attachments); DOC Ex. 435 at 116, 117 (Campbell Public Surrebuttal).
[174] *Id.* at 119.

> Failing to reflect the 2015 retirements for transmission and distribution facilities would be inequitable to ratepayers since they should not be required to pay for retired assets. Instead, such an approach would appear to enrich the Company without a sound basis for doing so.
>
> Third, I note that the Company has requested a forecasted test year not a historical test year and, thus, reasonable and well supported forecasts including those for plant retirements should be included in the 2015 Step. I also note that the Company provided the $535,552 retirement adjustment for 2015 transmission and distribution in response to DOC information request no. 2109, which was discussed on pages 159-160 of my Direct Testimony and attached as NAC-30.[175]

559. For these reasons, Xcel did not show that it is reasonable not to reflect the passage of time, as the Department proposed. The ALJ agrees.

2. Xcel did not demonstrate that the Department's calculation of the passage time adjustments is incorrect

541. At the evidentiary hearing, counsel for Xcel attempted unsuccessfully to elicit a passage of time adjustment applicable to a revenue requirement of $713.4 million. To be clear, Xcel did not request a rate increase of this magnitude, and this figure has not been examined for its reasonableness or accuracy. The Company asked Ms. Campbell to confirm that subtracting the difference between certain numbers would equal such a passage of time adjustment. The record, however, does not allow the calculation. Ms. Campbell explained that she has not audited Xcel's claimed full 2015 revenue requirement figure, and she doesn't know if the amount Xcel represented as the associated depreciation expense is reasonable (or what it represents or whether it is already in the 2015 Step, in whole or in part). If, however, she had audited Xcel's claimed numbers and agreed with the assumptions underlying those claimed numbers, then the passage of time adjustment would be performed, as follows:[176]

> I would look at the incremental increase in depreciation expense, if there was one, and I would look at the stepdown in accumulated depreciation, if there was one, in calculating the passage time.

542. Thus, theoretically, *if* there were an incremental increase in depreciation expense, and *if* that incremental increase in depreciation expense was not already captured in the 2015 Step, and *if* Xcel had actually asked in its initial rate case petition for recovery of the full 2015 revenue deficiency, Ms. Campbell agreed that, "then, yes, we would capture that, and we would

[175] *Id.* at 118-119.
[176] Tr.V. 5 at 45-53 (Campbell); DOC Ex. 435 at 115-116 (Campbell Public Surrebuttal).

capture the stepdown in accumulated depreciation, the rate base reduction, assuming that it also wasn't in the 2015 step." The record does not support such a calculation.[177]

3. Conclusion regarding Passage of Time in 2015 Step

543. For the reasons discussed above, the Department demonstrated that its passage of time adjustments are necessary for the Commission to capture downward adjustments to rate base, which includes the step down from 2014 to 2015 due to the normal passage of time and 2015 expected retirements.[178]

4. Summary of Adjustments

544. Mr. Lusti summarized the test-year rate base and operating income effect for the "passage of time" adjustment. The DOC recommendation decreased the 2015 STEP rate base by $157,946,000, as detailed in DOC Ex. 438 DVL-17, and as shown in DOC Ex. 451 DVL-EH-22, column (e) (Lusti Opening Statement); DOC Ex. 437 at 48 (Lusti Direct); DOC Ex. 442 at 39 (Lusti Surrebuttal). The DOC recommendation decreased the 2015 STEP operating income by $1,490,000, as detailed in DOC Ex. 438 DVL-17, and as shown in DOC Ex. 451 DVL-EH-24, column (e) (Lusti Opening Statement). DOC Ex. 437 at 52 (Lusti Direct); DOC Ex. 442 at 39-40 (Lusti Surrebuttal); Mr. Lusti summarized the test-year rate base and operating income effect for the 2015 transmission retirements.

545. The DOC recommendation increases the 2015 STEP rate base by $29,000, as detailed in DOC Ex. 438 DVL-18, Column (a) (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-EH-22, column (f) (Lusti Opening Statement); DOC Ex. 437 at 48 (Lusti Direct); DOC Ex. 442 at 40 (Lusti Surrebuttal). The DOC recommendation increases the 2015 STEP operating income by $57,000, as detailed in DOC Ex. 438 DVL-18 (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-EH-24, column (f) (Lusti Opening Statement); DOC Ex. 437 at 52 (Lusti Direct); DOC Ex. 442 at 40 (Lusti Surrebuttal).

546. Finally, Mr. Lusti summarized the test-year rate base and operating income effect of the 2015 distribution retirements. The DOC recommendation increases the 2015 STEP rate base by $133,000, as detailed in DOC Ex. 451 DVL-EH-22, column (g) (Lusti Opening Statement); DOC Ex. 437 at 48-49 (Lusti Direct); DOC Ex. 442 at 40 (Lusti Surrebuttal). The DOC recommendation increases the 2015 STEP operating income by $268,000, as detailed in DOC Ex. 438 DVL-18 (Lusti Direct Attachments), and as shown in DOC Ex. 451 DVL-EH-24, column (g) (Lusti Opening Statement); DOC Ex. 437 at 52 (Lusti Direct) DOC Ex. 442 at 40 (Lusti Surrebuttal).

[177] Tr.V. 5 at 53 (Campbell).
[178] DOC Ex. 435 at 116 (Campbell Public Surrebuttal).

MM. 2015 STEP – Rate Moderation Plans – Depreciation Reserve and Department of Energy (DOE) Payments for 2014 and 2015 Step (Issues 9 and 34)

Disputed as to preferred option (between Xcel and the Department) (disputed between OAG): DOC recommends that the Commission approve acceleration over three years according to a 50-40-10 percent give back option for 2014 to 2016 depreciation reserve plus the excess Department of Energy (DOE) settlement funds (now $25.737 million, per Ms. Perkett's Opening Statement). As an alternative position DOC recommends the Company's 50-30-20 percent give back option for 2014 to 2016 depreciation reserve give back plus the $25.737 million in excess DOE funds.[179]

547. In its Direct Testimony, Xcel recommended combining two "rate moderation proposals" in order to moderate the effect of its rate increase request in this rate case: 1) accelerating over three years (50 percent, then 30 percent, then 20 percent of the $228.5 million balance for 2014, 2015 and 2016, respectively) of the Commission's previously-approved 8-year amortization of "theoretical depreciation reserve surplus," and 2) use of settlement payments from the Department of Energy (DOE). Xcel gave the following explanation of why it proposed to use different proposed to use different amortization percentages in 2014 to 2016 under the first prong of its recommendation:

> Due to the Company's projected deficiencies for 2014 through 2016, using different percentages helps achieve more moderate and predictable rate increases over this time period. The Company selected the different percentages with a goal of establishing approximately five percent year-over-year increase in rates over the next two years. Also, by preserving 20 percent of this expense for use in 2016, the Company can use this remaining amount to moderate the rate increase requested in its next rate case for the 2016 test year. [180]

548. Regarding prong one, the Department continues to disfavor a "theoretical depreciation reserve surplus" as a general principle in setting rates, but supports as an alternative Xcel's proposed acceleration (50 percent, then 30 percent, then 20 percent (50/30/20)) of the 8-year year amortization recently allowed by the Commission in Xcel's most recent rate, and prefers a 50 percent, then 40 percent, then 10 percent (50/40/10) acceleration. As to prong two, the Department agrees with Xcel that excess DOE settlement payments received by the Company for 2013 and 2014 of $35.837 million (the Department later agreed that Xcel supported the figure of $25.737 million, per Ms. Perkett's Opening Statement) also should be used at this time, and only for this rate case, to moderate the 2015 Step. Finally, the Department believes that the Commission has authority to accept a rate moderation plan, as proposed by the

---

[179] DOC Ex. 450 at 3-4 (Campbell Opening); DOC Ex. 435 at 65-69 (Campbell Public Surrebuttal).

[180] DOC Ex. 429 at 75-76 (Campbell Public Direct); Xcel Ex. 99 at 27-28 (Clark Direct).

Company, including the Department's preferred 50/40/10 percent option plus excess DOE settlements to reduce the 2015 Step.[181]

1. Theoretical depreciation reserve surplus

549. "Theoretical depreciation reserve surplus give back" simply means returning to ratepayers the difference between the Company's recorded book depreciation reserve compared to a theoretical book reserve for the Company's transmission, distribution, and general assets. Its use for ratemaking purposes is to provide a temporary benefit that results in lower rates only in the short-term. The Commission in its September 3, 2013 Order in Xcel's most recent rate case, approved an amortization give back over eight years of $261 million for the "theoretical depreciation reserve surplus" determined in that case. One year, or one eighth, of the $261 million already has been amortized, leaving a balance of $228.5 million to be amortized over the next seven years. The effect of this approach was to reduce Xcel's annual depreciation expense but increase rate base above where it otherwise would have been, on which the Company earns a return. Xcel's proposed 50/30/20 percent give back, and the Department's preferred 50/40/10 percent give back, both apply to years to 2014-2016.[182]

550. Ms. Campbell provided the Department's opposing position in Xcel's last rate case, to highlight her continued concerns over the short-term benefits but longer-term effects that she termed the "pay me now or pay me later [with a return]" effect of amortization of theoretical depreciation reserve surplus, as follows:[183]

> The Department provided the reasons below for not supporting the give back of theoretical excess depreciation reserves for both 1) generation and for 2) transmission, distribution and general plant.
>
> - Due to the significant level of nuclear generation and CapX transmission projects going in-service during the 2014 to 2016 timeframe

---

[181] DOC Ex. 429 at 94 (Campbell Public Direct). "Excess" means in excess of the currently approved nuclear decommissioning accrual which now is calculated to be $25.737 million. DOC Ex. 450 at 3-4 (Campbell Opening) (confirming $25 million, not $35 million); DOC Ex. 435 at 68-69 (Campbell Public Surrebuttal); DOC Ex. 429 at 90 (Campbell Public Direct). The Department does not agree with OAG witness Mr. Lindell who questions the Commission's authority to adopt such rate moderation proposals. *See* Tr.V. 3 at 192 (Lindell).

[182] DOC Ex. 429 at 76 (Campbell Public Direct). Moreover, according to Xcel:

> Each year's amortization of the excess theoretical reserve creates a change in accumulated depreciation reserve as well as the accumulated deferred tax balance, causing a net change in rate base which in turn impacts the return on rate base component of the revenue requirement determination.

Xcel Ex. 95 at 31 (Robinson Direct). *See* DOC Ex. 429 at 92-94 (Campbell Public Surrebuttal); Findings of Fact, Conclusions of Law, and Order, Docket No. E002/GR-12-961 (September 3, 2013 Xcel Rate Case Order); DOC Ex. 429 at 76 (Campbell Public Direct). Xcel proposed to use the DOE settlement payments only to offset the 2015 Step increase. *Id.* at 85.

[183] DOC Ex. 429 at 88-89 (Campbell Public Direct) (emphasis in italics added).

the Department did not agree that there was surplus deprecation reserve, and that *there would not continue to be a surplus depreciation reserve for much longer* due to significant capital investment;

- The Department was concerned that, while in the short-term there is a reduction in depreciation expense, there is also a decrease in accumulated depreciation, which increases rate base. So *in the long-term ratepayers would still have to pay for the depreciation expense, but they would also have to pay a return on a higher rate base amount.* This point is also known as "pay me now or pay me later" reflecting that the cost of paying later is the rate of return on the higher rate base.

- The Department was also concerned that the *theoretical depreciation assumes that the depreciation life for a plant is known to be longer, say 50 years*; however, longer lives generally require significant capital additions to reach the 50 year life. However, there are *numerous factors that cannot be known* over the assumed 50-year life (e.g. floods, unexpected damages, newer technologies) that *may suggest that such investments should not be made.*

For this reason, the more conservative method generally used in Minnesota of assuming a shorter life for depreciation and assessing whether such capital investments are reasonable based on circumstances known at that time provides better matches to the decisions in [Integrated Resource Plans] IRPs.

551. With the above concerns in mind, the Department evaluated various give-back scenarios for 2014, 2015, and 2016 with and without using excess DOE settlement payments to reduce the 2015 Step: 50/30/20, 50/40/10, 50/50/0.[184]

2. Excess DOE settlement payments to reduce 2015 Step

552. Xcel proposes to use DOE settlements funds that currently exceed the nuclear decommissioning accrual for this rate case as a rate mitigation measure. Ms. Campbell stated the Department's general view that future DOE settlement amounts should be used to offset nuclear decommissioning accruals, since that is the purposes of these DOE settlement amounts. Nonetheless, the specific DOE settlements that would offset the rate effect of the 2015 step are in excess of the currently approved decommissioning accrual. For this reason, "at this time, for purposes of this rate case," Ms. Campbell would not oppose using the DOE funding in excess of the current decommissioning accrual, as Xcel has proposed.[185]

553. The DOE payments derive from settlement payments Xcel has been receiving from DOE as a result of litigation regarding DOE's contractual obligation to take spent nuclear fuel. These payments have been used by the Commission in various ways in the past. The first

---

[184] DOC Ex. 429 at 92-94 (Campbell Public Surrebuttal).
[185] DOC Ex. 429 at 90 (Campbell Public Direct).

and second DOE settlement payments were refunded to the Company's customers, largely due to the fact that the decommissioning funding was at that time considered to be overfunded. The third DOE settlement payment was used for decommissioning purposes since the decommissioning fund was no longer considered overfunded, and resulted in an offset of the decommissioning accrual of $14,189,132 as determined in the Commission's December 4, 2012 Order in Docket No. E002/M-11-939. Finally, Ms. Campbell explained that the Company's next decommissioning study is due October 1, 2014 for the period 2015 to 2017.[186]

554. Xcel proposes to moderate the rate increase in this case by using the 2013 and 2014 DOE payments (to the extent they exceed the Company's nuclear decommissioning accrual requirements through 2015) to offset the 2015 Step. Mr. Robinson initially estimated that the amount of the excess DOE settlement payments would be approximately $35.8 million in 2014 and 2015 on a Minnesota jurisdictional basis. Ms. Campbell now agrees that Xcel witness Ms. Perkett provided sufficient additional information to confirm the likely amount of such excess DOE settlement payments is $25.737 million.[187]

3. Results of the Department's analysis

555. The Department concluded from its review of give back options that a 50/40/10 option for years 2014, 2015 and 2016, together with excess DOE settlements for 2015, is preferable, and that no other scenario provides better rate mitigation than either the 50/40/10 or the 50/30/20 option, both with use of excess DOE payments. As a starting point for its evaluation of Xcel's proposal as well as various scenarios, the Department noted that the Commission's January 2, 2014 Order Setting Interim Rates, pages 2 and 3, allowed in interim rates the Company's 50/30/20 give back of theoretical depreciation reserve surplus for 2014. Thus, since interim rates are the starting point for this rate case, and because the rates being charged to ratepayers already reflect the Company's 50/30/20% give back of theoretical depreciation reserve for 2014, giving back to customers in final rates anything less than this interim rate starting point would result in increasing customer rates for this component.[188]

556. In addition to the scenarios run by Xcel, including a straight-line depreciation method over eight years as well as a 33/33/33 option, the Department asked the Company to calculate the effects of 50/30/20, 50/40/10, 50/50/0 for years 2014, 2015 and 2016, and as to each scenario evaluation with and without using excess DOE settlement payments to reduce the 2015 Step. Ms. Campbell included the following chart, prepared by Xcel, of the two scenarios requested by the Department (50/40/10 and 50/50/0), although it includes $35 million rather than the updated $25 million as the amount of excess DOE payments for 2015, as follows:[189]

---

[186] *Id.*; Xcel Ex. 92 at 41 (Perkett Direct).
[187] DOC Ex. 429 at 85 (Campbell Public Direct) (citing Xcel Ex. 95 at 33-34 (Robinson Public Direct); DOC Ex. 450 at 3-4 (Campbell Opening).
[188] DOC Ex. 429 at 90, 94 (Campbell Public Direct); DOC Ex. 435 at 68-69 (Campbell Public Surrebuttal).
[189] DOC Ex. 429 at 79, 92-94 (Campbell Public Direct); *see* Xcel Ex. 100 at 37-42 (Clark Rebuttal); Xcel Ex. 97 at 15-17 (Robinson Public Rebuttal).

Revenue Requirement Summary				
Company Proposed 50% 30% 20%	**2013**	**2014**	**2015**	**2016**
Annual Revenue Requirements	(32,395)	(111,308)	(58,387)	(31,068)
DOE Payment Utilization			(35,837)	
Total Annual Revenue Requirement	(32,395)	(111,308)	(94,224)	(31,068)
Year over Year Rev Req Change		(78,913)	17,084	63,157
Requested 50% 50% 0% Alternative	**2013**	**2014**	**2015**	**2016**
Annual Revenue Requirements	(32,395)	(111,308)	(103,854)	17,456
DOE Payment Utilization			-	
Total Annual Revenue Requirement	(32,395)	(111,308)	(103,854)	17,456
Year over Year Rev Req Change		(78,913)	7,455	121,310
Requested 50% 40% 10% Alternative	**2013**	**2014**	**2015**	**2016**
Annual Revenue Requirements	(32,395)	(111,308)	(81,120)	(6,806)
DOE Payment Utilization			-	
Total Annual Revenue Requirement	(32,395)	(111,308)	(81,120)	(6,806)
Year over Year Rev Req Change		(78,913)	30,188	74,315

Comparison Summary				
50% 50% 0% - 50% 30% 20%	**2013**	**2014**	**2015**	**2016**
Total Annual Revenue Requirement	-	-	(9,629)	48,524
Year over Year Rev Req Change	-	-	(9,629)	58,153
50% 40% 10% - 50% 30% 20%	**2013**	**2014**	**2015**	**2016**
Total Annual Revenue Requirement	-	-	13,104	24,262
Year over Year Rev Req Change	-	-	13,104	11,158

557. The Department summarized the meaning of the above chart to show, among other things, that the reductions occasioned by using theoretical depreciation reserve surplus are temporary, in part as follows:

> [T]his schedule clear shows the "pay me later" concern of the theoretical depreciation reserve amortization. While ratepayers did see benefits of a $32.655 million reduction in 2013 and will likely see benefits of a $78.913 million reduction in 2014, ratepayers will also get an increase of $7 to $30 million more in 2015 depending on the alternative selected, plus a $63 to $121 million increase in 2016 depending on the alternative selected.

The Department showed the differences between a 50/40/10 option and the Company's 50/30/20 option, both with excess DOE payments included for 2015, as follows:

DOC Recommended Rate Mitigation Plans, $ millions, MN jurisdiction

	2014	2015	2016
50/30/20% w DOE	$78.913	$17.084	$63.157
50/40/10% w DOE	$78.913	$5.188	$74.315

Consistent with the text of Ms. Campbell's Direct Testimony, the chart immediately above should show a *reduction* in rates of $78.913 million (rather than the increase shown).[190]

558. Based on its concerns expressed above, including the fact of the Commission's recent action regarding interim rates in this case as well as the fact of the 8-year amortization of theoretical depreciation reserve surplus allowed in the most recent Xcel rate case, the Department recommends the 50/40/10 percent option plus excess DOE payments in 2015, largely due to the lesser rate increase of $5.188 million in 2015, although the Department alternatively recommends the Company's 50/30/20 percent option plus excess DOE payments in 2015. Both options provide significant rate reductions in 2014.[191]

4. DOC recommendation on rate mitigation

559. The Department recommends that the Commission approve the Department's 50-40-10 percent option for the 2014 to 2016 depreciation reserve give-back plus the excess DOE funds. It also agrees that the correct placeholder for DOE funds is now $25.737 million, in light of the Company's support for the $10.1 million lower DOE payment in the Second Supplemental Response to DOC information request no. 1180, as discussed by Xcel witness Lisa Perkett in her opening statement (this amount will be trued-up to actual DOE funds, in compliance with Xcel's requirements to return all DOE refunds to ratepayers). The Department's recommendation results in a net $12.633 million increase in revenue in 2015. In the alternative, the Department recommends the Company's 50-30-20 percent option for 2014 to 2016 depreciation reserve give back plus the $25.737 million in excess DOE funds.[192]

560. In Mr. Lusti's Opening Statement, the DOC's recommendation increased the 2015 STEP operating income by $7,407,000, as shown in DOC Ex. 451 DVL-HE-24, column (h) (Lusti Opening Statement); DOC Ex. 450 at 2 (Campbell Opening Statement).

561. The ALJ agrees that the Department recommendations are reasonable and recommends the 50/40/10 percent option plus excess DOE payments in 2015. In the alternative, and should the Commission choose, the ALJ also agrees that the Company's 50/30/20 percent option plus excess DOE payments in 2015 is reasonable.

---

[190] DOC Ex. 429 at 93-94 (Campbell Public Direct).
[191] *Id.*
[192] DOC Ex. 450 at 3-4 (Campbell Opening); DOC Ex. 435 at 65-69 (Campbell Public Surrebuttal).

NN. 2015 STEP Placeholder -Monticello EPU Prudency (Issue 2, in part)

562. This is solely a placeholder adjustment, and is not a part of the issue for the ALJ to decide in this proceeding. The basis for this adjustment is discussed in the Monticello Cost Overrun Investigation, Docket No. E002/CI-13-754.

563. The DOC's recommendation decreases the 2015 STEP rate base by $53,544,000, as detailed in DOC Ex. 435 NAC-S-1, (Campbell Surrebuttal), and as shown in DOC Ex. 451 DVL-HE-22, column (i) (Lusti Opening Statement). The DOC's recommendation increases the 2015 STEP operating income by $2,013,000, as detailed in DOC Ex. 435 NAC-S-1 (Campbell Surrebuttal), and as shown in DOC Ex. 451 DVL-EH-22, column (i) and DVL-EH-24, column (n) (Lusti Opening Statement). The total revenue requirement adjustment as calculated by the company is $10.237 million reduction for 2015 on a Minnesota Jurisdictional basis, as shown on Attachment A, column (e) in the Company's response to Department IR No. 2148.[193]

OO. 2015 STEP Calculation Monticello EPU 2015 STEP (Issue 2, in part)

564. Ms. Campbell stated in her Direct Testimony that the Monticello EPU is not expected to be in-service in 2014. Thus, she recommended an adjustment to exclude the 2014 costs from the test-year revenue requirements. However, she also stated that the Monticello EPU is expected to be in-service and used and useful in 2015. Thus, it is reasonable to allow recovery of the 2015 Monticello EPU costs in the 2015 STEP revenue requirement.

565. The DOC's recommendation increases the 2015 STEP rate base by $135,597,000, as shown in DOC Ex. 451 DVL-HE-22, column (j) (Lusti Opening Statement). The DOC's recommendation decreases the 2015 STEP operating income by $6,983,000, as shown in DOC Ex. 451 DVL-HE-24, column (o) (Lusti Opening Statement).

566. The ALJ agrees that the Department's recommendation to increase 2015 STEP rate base by $135,597,000 and decrease 2015 STEP operating income by $6,983,000 is reasonable.

PP. 2015 STEP – Cash Working Capital (Issue 49, in part-2015)

567. Mr. Lusti, in his Direct Testimony explained that, as a result of DOC adjustments to the test-year STEP O&M expenses and test-year rate base, Xcel's cash working capital needed to be adjusted. Mr. Lusti calculated this adjustment by applying the DOC's lead/lag days to the DOC O&M expense adjustments. DOC Ex. 437 at 49 (Lusti Direct).

568. In his Opening Statement, Mr. Lusti testified that as a result of the various DOC STEP adjustments, he recommended that the test-year cash working capital requirement be decreased by $3,798,000, as detailed in DOC Ex. 451 DVL-HE-23, Line (51) (Lusti Opening Statement), and as shown in DOC Ex. 451 DVL-HE-22, column (k) (Lusti Opening Statement).

---

[193] DOC Ex. 435 at 32, NAC-S-1 (Campbell Public Surrebuttal).

569. The Department's recommendation that the test-year cash working capital requirement be decreased by $3,798,000 is reasonable.

QQ. 2015 STEP – DOC Total 2015 STEP Rate Base Adjustment Summary.

570. As a result of the various DOC adjustments, DOC recommends that the Commission approve a rate base of $6,833,964,000, as shown in DOC Ex. 451 DVL-HE-21, column (d), line (1) (Lusti Opening Statement). This amount is the result of adding the $332,580,000 of the DOC's 2015 STEP adjustments, including Xcel's 2015 STEP adjustment, as detailed in DOC Ex. 451DVL-HE-22, to the DOC's recommended 2014 test-year rate base of $6,501,384,000 as detailed in DOC Ex. 451 DVL-EH-3 (Lusti Opening Statement).

571. The ALJ finds that the Department's recommendation regarding approval of a rate base of $6,833,964,000 is reasonable.

RR. 2015 STEP – Nuclear Outage Amortization for 2015 (Issue 27)

Resolved between Xcel and the Department: DOC agrees that it incorrectly concluded that this issue related to 2015 capital expenditures. It does not. Thus, DOC no longer recommends a $5.5 million reduction in nuclear outage amortization expense for 2015.[194]

Disputed between Xcel and OAG. DOC does not summarize the disagreement between Xcel and the OAG, but notes that Ms. Campbell disagreed with Mr. Lindell's summary of her position on this issue in his Opening Statement.[195]

572. Based on Xcel witness Mr. Clark's Rebuttal Testimony in which he further explained Xcel's nuclear outage amortization recovery request, the Department now agrees that nuclear outage amortization expense is a non-capital issue, and the Commission allowed the Company to amortize these expenses between fuel outages.[196] Ms. Campbell summarized the basis for her earlier position and why that position was incorrect, as follows:[197]

> I now agree with Xcel. I note that when proposing my adjustment in Direct Testimony I mistakenly believed that the nuclear outage amortization costs were related to capital expenditures. However, as explained above by Mr. Clark, I agree with the Company that the nuclear outage amortization costs are related to O&M fuel outage expenses (for which the Company received special approval so they could amortize these expenses between fuel outages in Docket No. E002/M-07-1489) and are not capital costs. As Mr.

[194] DOC Ex. 450 at 1 (Campbell Opening); DOC Ex. 435 at 14-17 (Campbell Public Surrebuttal).
[195] DOC Ex. 450 at 1-2 (Campbell Opening) (referring to Tr.V. 3 at 196 (Lindell); OAG Ex. 141 at 2 (Lindell Opening).
[196] DOC Ex. 435 at 16 (Campbell Public Surrebuttal).
[197] *Id.*

> Clark correctly noted the capital nuclear costs are excluded from these O&M expenses for nuclear outage amortization. As a result, I am no longer recommending my $5.5 million reduction in nuclear outage amortization expense for 2015.

Ms. Campbell clearly articulated that she mistakenly believed nuclear outage amortization costs to be capital-related and, thus, the basis for her change in position. Mr. Lindell's Opening Statement, page 194 lines 20-21 of Transcript Volume 3, incorrectly summarizes Ms. Campbell's reasoning for her current position.[198]

573. The Department removed the nuclear outage amortization adjustment of $5.5 million for 2015 from Mr. Lusti's financial statements.[199]

574. In his Direct Testimony Mr. Lusti summarized the test-year operating income effect. The DOC recommendation increases the 2015 STEP operating income by $3,225,000, as shown in DOC Ex. 438 DVL-24, column (i) (Lusti Direct Attachments); DOC Ex. 437 at 53 (Lusti Direct).

575. Ms. Campbell notes in her Surrebuttal Testimony at page 16 that she no longer recommends a 2015 STEP adjustment for nuclear outage amortization. DOC Ex. 438 at 43 (Lusti Surrebuttal); DOC Ex. 435 at 16 (Campbell Surrebuttal).

SS. 2015 STEP – Emission Chemicals (Issue 33)

576. In his Direct Testimony, Mr. Lusti summarized the test-year operating income effect. The DOC recommendation increases the 2015 STEP operating income by $1,747,000, as shown in DOC Ex. 438 DVL-24, column (j) (Lusti Direct Attachments); DOC Ex. 437 at 53 (Lusti Direct). With regard to the DOC's adjustment to 2015 STEP operating income for *Sherco 1 and 2* emission chemicals, in Surrebuttal, the DOC's recommendation increased the 2015 STEP operating income by $1,642,000, as shown in DOC Ex. 442 DVL-S-24, column (j) (Lusti Surrebuttal); DOC Ex. 442 at 44 (Lusti Surrebuttal). With regard to the DOC's adjustment to 2015 STEP operating income for *King and Sherco 3* emission chemicals, in Surrebuttal, the DOC's recommendation increased the 2015 STEP operating income by $106,000, as shown in DOC Ex. 442 DVL-S-24, column (k) (Lusti Surrebuttal); DOC Ex. 442 at 44 (Lusti Surrebuttal).

577. In Opening Statements, this matter was resolved. Xcel accepted DOC's recommendation to further reduce the 2015 Step expense related to Emission Control Chemicals by $1.4 million, resulting in a total 2015 Step reduction of $1.580 million. Xcel Ex. 140 at 7 (Heuer Opening Statement); DOC Ex. 451, DVL-EH-24, page 1 of 3, Columns (j) and (j) (Lusti Opening Statement).

---

[198] DOC Ex. 450 at 1-2 (Campbell Opening) (referring to Tr.V. 3 at 196 (Lindell); OAG Ex. 141 at 2 (Lindell Opening).
[199] DOC Ex. 435 at 17 (Campbell Public Surrebuttal).

578. The ALJ agrees that the Departments recommendation to further reduce the 2015 Step expense related to Emission Control Chemicals by $1.4 million, resulting in a total 2015 Step reduction of $1.580 million, is reasonable.

TT. 2015 STEP – PI Admin Building (Issue 29)

579. The Department no longer recommends a 2015 STEP adjustment for the PI Admin Building. DOC Ex. 442 at 41 (Lusti Surrebuttal); DOC Ex. 435 at 20 (Campbell Surrebuttal).

UU. 2015 STEP – Sales Forecast (Issue 13, in part -for 2015)

580. In his Direct Testimony Mr. Lusti summarized the test-year financial operating income effect. The DOC recommendation increases the test-year retail revenue by $670,000 as shown in DOC Ex. 438 DVL-24, column (l) (Lusti Direct Attachments); DOC Ex. 437 at 54 (Lusti Direct).

581. In Surrebuttal, the DOC's recommendation increased the test-year retail revenue by $0 as shown in DOC Ex. 442 DVL-S-24, column (l) (Lusti Surrebuttal); DOC Ex. 442 at 44 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-24, column (l) (Lusti Opening Statement).

582. The Department's recommendation to increase (2015 STEP) test-year retail revenue by $0 is reasonable.

VV. 2015 STEP – Property Taxes (Issue 32)

Resolved between DOC and Xcel: DOC agreed with Xcel's rebuttal proposal to decrease property taxes $3,309,000. DOC Ex. 442 at 45 and DVL-S-24, column (n) (Lusti Surrebutal); DOC Ex. 451 DVL-EH-24, column (m) (Lusti Opening Statement).

560. In his Direct Testimony, as Detailed in DOC Ex. 438 DVL-14, Schedule 1, and as shown in DOC Ex. 438 DVL-24, Column (e) (Lusti Direct Attachments), Mr. Lusti recommended that the test-year property tax be reduced by $14,500,000 to reflect a 9 percent cumulative over-recovery for the period 2001 through 2013. DOC Ex. 437 at 54 (Lusti Direct).

561. In Rebuttal Testimony, Xcel Witness Jeffrey C. Robinson proposed a STEP property tax adjustment. At page 10 of his Rebuttal Testimony, Mr. Robinson recommended an adjustment to decrease property taxes by $3,309,000, such that the STEP level of property taxes only reflects costs directly attributable to the identified STEP projects. DOC agreed to this proposal. As shown in DOC Ex. 442 DVL-S-24, Column (n) (Lusti Surrebuttal), Mr. Lusti in Surrebuttal recommended that the 2015 STEP property tax be reduced by $3,309,000 to allow only for costs directly attributable to the identified STEP projects. DOC Ex. 442 at 45 (Lusti Surrebuttal); DOC Ex. 451 DVL-EH-24, column (m) (Lusti Opening Statement).

WW. 2015 STEP – Interest Synchronization Methodology and Calculation (Issue 49A)

Resolved between DOC and Xcel: DOC accepted Xcel's proposed methodology. DOC and Xcel agreed that final interest synchronization calculation will occur after the Commission determines all cost of debt, rate base and income statement adjustments in this proceeding. DOC Ex. 437 at 43-44 (Lusti Direct) and DOC Ex. 442 at 34 (Lusti Surrebuttal).

562. While the DOC accepted Xcel's proposed methodology,[200] for the 2015 STEP, after all decisions are made, the DOC and Xcel will calculate the 2015 STEP Interest Synchronization, and no decision is needed by the ALJ on the result of the calculation. For the 2015 STEP, DOC Ex. 451 DVL-HE-25, (Lusti Opening Statement) detailed during the evidentiary hearing the calculation of DOC's adjustment to decrease the 2015 STEP test-year income taxes by $1,813,000. This adjustment results from the application of interest synchronization to the various DOC 2015 STEP test-year adjustments.

XX. 2015 STEP–DOC Total STEP Adjustment and Operating Income Adjustment Summary

563. With Mr. Lusti's Opening Statement, DOC recommended that, as a result of the various DOC 2015 STEP adjustments, including Xcel's 2015 STEP adjustment, the Commission decrease the level of operating income that Xcel recommended for the 2014 test year by $12,627,000 as detailed in DOC Ex. 451 DVL-HE-24, Column (p), Line 25 (Lusti Opening Statement). DOC recommended that the Commission approve a level of operating income of $435,721,000, as shown in DOC Ex. 451 DVL-HE-21, column (d), line (4) (Lusti Opening Statement). This amount is the result of adding the negative $12,627,000 of the DOC's 2015 STEP adjustments, including Xcel's 2015 STEP adjustment, as detailed in DOC Ex. 451 DVL-HE-24, to the DOC-recommended 2014 test-year operating income of $448,348,000 as detailed in DOC Ex. 451 DVL-HE-6 (Lusti Opening Statement).

564. In his Opening Statement, Mr. Lusti testified that all the adjustments recommended by the Department, including those identified in the Opening Statement of Xcel Witness Anne E. Heuer that related to Department positions, had been incorporated into the final calculations of revenue requirement that were Attachments to his Opening Statement. DOC Ex. 451 at 1 (Lusti Opening Statement). Mr. Lusti testified that the DOC reviewed many aspects of the Company's income statements, balance sheets, etc., and concluded that the test-year rate base and operating income were reasonable only with the inclusion of the specific adjustments DOC recommended. DOC Ex. 442 at 49 (Lusti Surrebuttal).

565. As a part of his Opening Statement, Mr. Lusti prepared a Summary of STEP Year 2015 Revenue Requirements that summarizes the various elements used to compute the revenue

---

[200] As noted in section FF above, for the 2014 test year, Xcel proposed to calculate its interest-expense deduction for 2014 test-year income-tax purposes by multiplying its rate base by the weighted cost of debt, (DOC Ex. 437 at 43 (Lusti Direct); DOC Ex. 442 at 34 (Lusti Surrebuttal) and the Department accepted Xcel's methodology.

requirements (revenue deficiency) under present rates for the 2015 STEP test year. Column (a), line (7), is the Company's revenue deficiency for the 2014 test year, which was the amount of $192,710,000 under present rates. Column (d) shows the calculation of the DOC's proposed revenue deficiency under present rates for the 2015 STEP test year, assuming an overall rate of return of 7.34 percent per the testimony of Dr. Eilon Amit. Column (c), Line (7), shows that the DOC's proposed revenue deficiency attributable to the 2015 STEP test year was $66,499,000. Thus, for the 2015 STEP test year, the DOC recommended a revenue requirement of $66,499,000. DOC Ex. 451, DVL-EH-21 (Lusti Opening Statement); DOC Ex. 451 at 3 (Lusti Opening Statement).

566. As a result of the DOC's recommended rate of return, rate base and operating income, changes in present rates are appropriate. As discussed above, for the 2014 test year, the Department recommended adjustments decreasing by $146,823,000 Xcel's initial request of $192,709,000, which resulted in a final revenue requirement of $45,887,000. Adding together the DOC-recommended 2014 increase and 2015 STEP increase of $66,499,000 yields a total increase over the two years of $112,386,000.

VII. OTHER COMPLIANCE CONCERNS REGARDING ANNUAL INCENTIVE COMPENSATION PROGRAM, SHERCO 3 INSURANCE CLAIMS AND LITIGATION, AND STEP COMPLIANCE

A. Reasonableness of Xcel's Annual Incentive Compensation Program (Issue 82)

567. The Commission's Ordering Paragraph 30 in its September 3, 2013, FINDINGS OF FACT, CONCLUSIONS, AND ORDER in Docket No. E002/GR-12-961 directed that "Xcel shall evaluate the goals set for its annual incentive program to determine if they are too lenient or if they actually require stretching to meet; the Company shall file the results of the evaluation in its next rate case."

568. The Company provided information regarding its annual incentive program (AIP). Nine witnesses, including Darla A. Figoli, David C. Harkness, Michael C. Gersack, Stephen R. Foss, Steven H. Mills, Timothy J. O'Connor, Gary J. O'Hara, David M. Sparby and Daniel P. Kline commented in their Direct Testimony on Xcel's Key Performance Indicators (KPI); however, they did not address the actual results of those KPI indicators. Mr. Lusti's Direct Testimony addressed the results of the application of the KPI indicators over the 5-year period 2008 – 2012. DOC Ex. 437 at 57 (Lusti Direct). His evaluation on Direct did not include the year 2013 because the Department had not then received Xcel's Incentive Compensation Report for the year 2013. DOC Ex. 437 at 57 (Lusti Direct).

569. Mr. Lusti reported that, from his review of the Annual Incentive Compensation Reports for the years 2008 – 2012, he found that Xcel employees meet their KPI requirement goals nearly always:

- **In 2009,** 15 of the 16 business areas reported KPI's of 100 percent or greater. DOC Ex. 437 at 58 (Lusti Direct) (citing DOC Ex. 437 DVL-19).

- **In 2010**, 17 of 19 business units reported KPI's of 100 percent or greater. One of the business areas in 2010 that did not achieve a KPI rating of 100 percent or greater did achieve a 99.87 percent rating.

- **In 2011**, 13 of the 16 business units achieved a KPI rating of 100 percent or greater. Of the business areas in 2011 that did not achieve a KPI rating of 100 percent or greater, one did achieve a 99.80 percent rating and one achieved a 98.54 percent rating.
- **In 2012**, 10 of 11 business areas achieved a KPI rating of 100 percent or greater. The only business area in 2012 to not achieve a 100 percent or greater KPI rating was the Nuclear business unit, as discussed earlier in his testimony.

570. Mr. Lusti observed that the Company did not report KPI results for the year 2008 because it did not achieve the minimum earnings level to pay incentive compensation. DOC Ex. 437 at 58 (Lusti Direct). Xcel's actual AIP compensation paid as a percentage of AIP Target for the years 2010, 2011, 2012 and 2012 was 103 percent, 94 percent, 118 percent and 120 percent, respectively. DOC Ex. 437 at DVL-37 (Lusti Direct); DOC Ex. 437 at 37 (Lusti Direct) (Xcel's April 25, 2014 Supplemental Response to DOC IR 193). The top twenty Xcel employees in 2013 received, as a group, 192 percent of target level compensation. DOC Ex. 437 at 59 (Lusti Direct); DOC Ex. 438 DVL-20, Schedule 2 (Lusti Direct Attachments). Because some of the AIP plan participants received approximately 200 percent of their target level compensation and all of the Top Twenty recipients received at least 161 percent of their target level, it is reasonable to conclude that the majority of the other AIP plan participants received amounts that were less than the 120 percent of their target level. DOC Ex. 437 at 59 (Lusti Direct).

571. Mr. Lusti stated that ratepayers do not pay for all of the AIP incentive compensation paid to Xcel employees; instead, Xcel ratepayers only pay for AIP amounts up to 15 percent of base compensation, which is referred to as a "15 percent cap." DOC Ex. 437 at 59 Lusti Direct). Mr. Lusti stated that it is reasonable to allow Xcel to recover its AIP compensation up to the 15 percent cap that it has proposed. He explained that DOC sought and provided this information about the results of the AIP and KPI compensation system in anticipation that it would provide a perspective for the Commission to consider when addressing many of the compensation issues discussed in the Department's testimony. DOC Ex. 437 at 59 Lusti Direct).

572. Because this is a compliance issue of the Commission, the ALJ and Commission will need to determine if Xcel 's AIP is reasonable.

B. Sherco 3 Insurance Claims and Litigation

573. In its September 3, 2013 Findings of Fact, Conclusions of Law and Order, in Xcel's last rate case, Docket No. E002/GR-12-961, the Commission issued four Findings with regard to Sherco 3, at Order Points 6 to 9:

> 6. Xcel shall remove all direct costs for Sherco Unit 3, except for property taxes, from the 2013 test year.

7. The Commission approves deferred accounting for Sherco Unit 3 2013 depreciation expense.

8. The Commission accepts Xcel's proposed 21-year remaining life of Sherco unit 3 as a placeholder. Xcel shall have an engineer evaluate Sherco Unit 3 and provide that analysis in its next rate case.

9. Xcel shall provide an analysis and report on the Sherco Unit 3 total costs, insurance recoveries and costs not covered by insurance in its November 2013 rate-case filing and it shall provide the completed accounting and report by December 31, 2013.

DOC Ex. 437 at 60 Lusti Direct). Order Points 7-9 are relevant to this 13-868 rate case. *Id.*

574. The Company addressed Order Point 7 in its rate case filing, with Xcel witnesses, Ms. Lisa H. Perkett at pages 12-13 and 18 of her Direct Testimony and Ms. Anne E. Heuer at Pages 28-29, 81-82 and 90 each discussed the adjustment to recover the 2013 depreciation expense of $14.1 million over the life of the facility beginning in 2014. Ms. Heuer explained that the $14.1 million depreciation expense in 2013 is a total company figure while $10.5 million is for the Minnesota electric jurisdiction net of Interchange billings to NSPW. DOC Ex. 437 at 60 (Lusti Direct).

575. Mr. Lusti agreed that Xcel's proposed treatment of the deferred accounting for depreciation expense is reasonable; the 2013 depreciation expense is being amortized over the 21-year remaining life of Sherco 3. DOC Ex. 438 at DVL-39 (Lusti Direct)(Xcel Response to DOC IR 1182). The effect of amortizing the $10.5 million over the 21-year remaining life of Sherco 3 is an annual expense of $500,000 for the Minnesota jurisdiction. DOC Ex. 437 at 61 Lusti Direct).

576. The Company addressed Order Point 8 in its rate case filing. Xcel Witnesses M. Lisa H. Perkett at Pages 18-20 of her Direct Testimony stated:

> …the Company contracted with Black & Veatch, a firm familiar with the equipment at Sherco Unit 3 to conduct a review for the expected remaining usefulness of the entire unit. ….In addition, Dane Watson of Alliance Consulting Group, an engineer specializing in depreciation analysis, provided an independent review of the remaining life from a depreciation perspective. It was our collective conclusion that the outage did not materially affect the existing remaining life of Sherco Unit 3 and that the 21-year remaining life is appropriate given the current structure of the unit.

Mr. Lusti concluded from this information that Xcel complied with the Commission's requirement. DOC Ex. 437 at 61 Lusti Direct).

577. Finally, Xcel addressed Order Point 9 in its rate case filing in the Direct Testimony of Company witness Mr. Ronald L. Brevig, who provided an analysis and report on the Sherco Unit 3 total costs, insurance recoveries and costs not covered by insurance in its November 2013 rate-case filing. Xcel witnesses Mr. Michael R. Anderson and Ms. Amy Stitt addressed insurance recovery in their Direct Testimonies. DOC Ex. 437 at 62 Lusti Direct).

578. Mr. Lusti had two overall observations, regarding Xcel's insurance settlements and insurance coverage. DOC Ex. 437 at 62 (Lusti Direct).

1. Insurance Settlements

579. The Company's testimony indicates that, at the time it filed its rate case, Xcel had not yet settled all the insurance claims and nor received all of the insurance recoveries, but was continuing to work with its insurers. Xcel stated that some of its costs had been submitted to their insurers and accepted, some are disputed, and some not been approved by insurers. Consequently, Xcel said it had forecasted amounts in the 13-868 proceeding based on its experience with its insurers and its understanding of its insurance policy. DOC Ex. 437 at 62 (Lusti Direct) (citing Xcel Ex. 56 at 50 (Brevig Direct); and Xcel Ex. 36 at 25-26 (Anderson Direct)).

580. After Xcel filed its 13-868 rate case, the Company filed two quarterly compliance reports, on December 31, 2013 and March 31, 2014 that provided updated accounting and reported on cost and insurance recoveries associated with the November 19, 2011 event at Sherco 3. Mr. Lusti indicated the next report was due June 30, 2014. In Xcel's most recent compliance filing, the Company said it had not resolved the insurance claims, and that:

> Our insurance claim is likewise large and complex, involving multiple carriers. We worked with our insurers to ensure cash flow from our insurers while the Restoration project was underway, and our claim continues to evolve as we finalize actual expenditures through monthly reports to our insurers.
>
> We continue to incur some costs, and to work with our insurers to complete all aspects of the claim. Even though most costs submitted to our insurers have been accepted, there are some still being reviewed or not yet approved. Additionally, the Company has not accepted some of the adjustments made initially by our insurers. As a result, we provide this update with the most recent information available and will provide additional quarterly reports until we determine final costs and resolve all matters with our insurers.

DOC Ex. 437 at 63 (Lusti Direct) (citing Xcel Ex. 6 at 2 (March 31, 2014 Sherco 3 Compliance Filing)). Finally, the Company submitted an extensive "Root Cause Analysis" on October 21, 2013, along with compliance filings on December 31, 2013 and March 31, 2014. DOC Ex. 437 at 63 (Lusti Direct).

581. Mr. Lusti testified that, although the total costs of the project were not yet final, each quarterly update provided a closer estimate of the final cost. The estimated total costs submitted with the November 4, 2013 13-868 rate case filing, the December 31, 2013 update, and the March 31, 2014 update provide cost estimates, as discussed in Mr. Lusti's DOC Ex. 439

at 64 (Lusti Trade Secret Direct). Mr. Lusti reported that Xcel had indicated its belief that its more recent estimates of the total cost of the project were getting closer to the final total cost: its March 31, 2014 Sherco compliance filing, at page 4, provided information (marked "trade secret") to support its belief; this trade secret information is set out in DOC Ex. 439 at 64 (Lusti Trade Secret Direct).

582. The Company had also provided some information on costs of the restoration project that are not covered by insurance. The Direct Testimony of Mr. Brevig identifies six categories of cost not covered by insurance:

1) Insurance Deductible: Costs for which Xcel must pay before the insurance provider will pay any insurance claims.

2) Disputed Items: Costs that Xcel disputes with insurers "for various reasons."

3) Capital Improvements: Costs for capital improvements that Xcel made while the plant was out of service.

4) Expediting Expense Cap: Costs (such as overtime pay and temporary repairs) to minimize the time during which Sherco 3 was out of service that exceeded the policy sublimit for his category.

5) Policy Exclusions: Costs associated with restoring the equipment where the actual cause of the event originated due to disputes about what caused the event.

6) Miscellaneous: Costs for parts and equipment where the cause of the damage cannot be determined and therefore insurance coverage is unclear and is/will be negotiated.

DOC Ex. 437 at 64-65 (Lusti Direct) *(citing* Xcel Ex. 56 at 51-59 (Brevig Direct)).

583. Xcel's most recent estimates of the costs that will not be covered by insurance are set out in each of the two updates (December 31, 2013 and March 31, 2014). Mr. Lusti's Trade Secret Direct Testimony noted that the Company's most recent compliance filing estimates the total cost that would not be covered by insurance, and observes that those higher costs are not included in Xcel's rate case. DOC Ex. 439 at 65 (Lusti Trade Secret Direct). A table at page 66 of DOC Ex. 439 at 66 (Lusti Trade Secret Direct) containing data from Xcel's March 31, 2014 Compliance filing identifies the Company's estimate of these costs at the time of its 13-868 rate case filing, and also includes the December 31, 2013 and March 31, 2014 estimates. DOC Ex. 439 at 66 (Lusti Trade Secret Direct).

584. Finally, Xcel described one other effort to recover the depreciation and return that the Company was unable to recover in its 2013 rate case. Mr. Lusti stated that he was generally aware that the Company and its insurers filed a lawsuit against General Electric (GE), alleging

that GE did not disclose known facts about potential failures. Xcel briefed the Department about this lawsuit, which is also mentioned in a February 6, 2014 article in the Minneapolis Tribune. DOC Ex. 437 at DVL-40 (Lusti Direct); DOC Ex. 437 at 66 (Lusti Direct). That case has not been resolved, according to Xcel's most recent update (March 31, 2014); DOC Ex. 437 at 67 (Lusti Direct).

585. In his Direct Testimony, Mr. Lusti indicated DOC's intent to review the quarterly update due June 30, 2014, in which Mr. Lusti expected Xcel to update the costs, settlements, and the then-current status of the litigation. DOC reserved the right to recommended an adjustment regarding Xcel's proposed recovery of costs not covered by insurance if warranted. DOC Ex. 437 at 67 (Lusti Direct).

2. Insurance Coverage

586. Mr. Lusti's second overall observation was that there appears to be a gap in Xcel's insurance coverage regarding replacement power costs. Specifically, as Mr. Brevig noted in his testimony, Xcel does not have Business Interruption Insurance, which could have helped offset the higher replacement power costs charged to Xcel's ratepayers during the extended outage of Sherco 3. Mr. Brevig stated:

> Q. DID THE COMPANY INCUR COSTS FOR REPLACEMENT ENERGY WHILE SHERCO WAS OFFLINE?
>
> A. Yes. As discussed by Mr. Anderson, we do not carry business interruption insurance for our non-nuclear generation fleet and therefore needed to generate replacement power at another Company facility/unit and/or purchase replacement energy to address any needs to serve our customers while Sherco 3 was offline. We are seeking recovery of the costs of replacement energy through our Fuel Clause Adjustment mechanism and therefore we are not seeking to recover any of these costs in this proceeding. As recommended by the Department of Commerce in their June 5, 2013 Comments in Docket No. E999/AA-12-757, determination of cost recovery of Sherco 3 replacement power costs will be taken up in the most recent AAA docket, E999/AA-13-599.

DOC Ex. 437 at 67-68 (Lusti Direct) (citing Xcel Ex. 56 at 47 (Brevig Direct)).

587. Mr. Lusti concluded his discussion of this compliance topic by noting that Mr. Brevig is correct, that this issue is being discussed further in both E999/AA-12-757 and E999/AA-13-599. DOC Ex. 437 at 68 (Lusti Direct).

C. STEP Compliance (Issue 35 and Issue 36)

Resolved between DOC and Xcel. Xcel accepted DOC's recommendation that, consistent with the Commission's prior Order in Docket No. E,G-999/M-12-587 (MYRP), the Commission should require Xcel to reduce rates for projects that do not occur within the two test years, and refund to its customers all rates that have been over-collected as a result of the cancellation of

projects for which the Company charges its ratepayers. DOC Ex. 437 at 71 (Lusti Direct); DOC Ex. 442 at 49 (Lusti Surrebuttal). Xcel's Compliance Plan is set out in Ms. Heuer's Opening Statement at pages 6-7 of 9.

588. Order Point 23 from the Commission's Order in Docket No. E,G-999/M-12-587 required the Company to provide the following in a multiyear rate plan petition:

> Regarding conditions for obtaining approval for a multiyear rate plan, the application must include or be accompanied by the following:
>
> A. A commitment to provide the Commission, parties, and potentially interested persons with notice of the initial rate change and detailed financial information for the initial rate change at least 60 days before the proposed effective date of the initial rate change.
>
> B. An Acknowledgement that upward rate adjustments during the course of the multiyear plan will be subject to refund if the rate adjustment is later determined to have been imprudent, and a waiver of any claim that such refunds represent retroactive ratemaking.
>
> C. A proposal for a process that ensures that if it became prudent to delay or avoid making a planned investment, the cost of that investment would be removed from the rates arising from the multiyear rate plan, and would be refunded if already collected.

589. Order Point 29 required any utility applying for or operating under a multiyear rate plan to do the following:

> A. File annual status reports confirming that the utility has made investments according to its multiyear rate plan, and affirming that it still intends to make the future investments authorized as part of the plan.
>
> B. If a project included in a multiyear plan is cancelled or postponed, within 30 days inform the Commission and parties, file a proposal to adjust rates to stop collecting any costs related to the cancelled or postponed project, and refund costs already collected.
>
> C. If a utility makes some other ***material*** change in plans, file a status report promptly (e.g., within 30 days of the known change).
>
> D. Within 180 days after the final rate adjustment under the multiyear plan, make a compliance filing verifying that the rates charged under the plan were based only on reasonable and prudent costs of service.

DOC Ex. 437 at 68-69 (Lusti Direct)(emphasis added).

590. Mr. Lusti testified that, while Xcel addressed Order Points 23 (B) and (C), and 29 (B) (DOC Ex. 437 at 69 (Lusti Direct)(*citing* Xcel Ex. 99 at 16-23 (Clark Direct)), the Company's criteria for "materiality" was not consistent with the Commission's above Order points. DOC Ex. 437 at 69-71 (Lusti Direct)(*citing* Xcel Ex. 99 at 20-21 (Clark Direct)). Mr. Lusti rejected the Company's recommendations regarding STEP compliance. DOC Ex. 437 at 69-71 (Lusti Direct)(*citing* Xcel Ex. 99 at 16-21 (Clark Direct)); DOC Ex. 442 at 47-49 (Lusti Surrebuttal) (*citing* Xcel Ex. 100 at 12-14 (Clark Rebuttal)).

591. Mr. Lusti recommended that, consistent with the Commission's prior Order, the ALJ should recommend, and the Commission should require Xcel to reduce rates for projects that did not occur within the two test years, and refund to its customers all rates that have been over-collected as a result of the cancellation of projects for which the Company charges its ratepayers. DOC Ex. 437 at 71 (Lusti Direct). DOC Ex. 442 at 49 (Lusti Surrebuttal).

592. In Ms. Heuer's Opening Statement, Xcel accepted the DOC recommendation as follows:

> We propose the following process in compliance with the Commission's June 17, 2013 Order in Docket No. E,G-999/M-12-587 (Multiyear Rate Plan Order). The 2015 Step rates will be set consistent with the Commission's final order in this proceeding. The Company will provide quarterly compliance reporting during 2015 (April, August, November) to the Commission comparing the most current forecast of each 2015 Step project to the amount included in the 2015 Step. By April 1, 2016, the Company will submit its final compliance report which will include:
>
> - The actual 2015 Step revenue requirement for each project, specifically 2014 actual, 2015 actual and the difference (2015 Step);
> - The revenue requirement difference for each 2015 Step project between the 2015 Step actual and 2015 Step Test Year;
> - Explanations for project additions that are greater than included in the 2015 Step;
> - In the event the total actual 2015 Step revenue requirement is lower than the total Test Year 2015 Step revenue requirement, the Company will include in its compliance filing a proposal for rate refund;
> - In the event the Company becomes aware of a 2015 Step project cancellation or postponement, the Company will provide 30 day notice including a refund plan.

VIII. CLASS COST OF SERVICE STUDY. (ISSUE 51, ISSUE 56, ISSUE 57, ISSUE 59, ISSUE 67)

<u>Amount of Economic Development Discounts (Issue 56)</u>

Resolved between DOC and Xcel: Halve the amount of economic development discounts that Xcel proposed to recover through base rates for the 2014 and 2015 test years to the actual 2013 level. DOC Ex. 408 at 43 (Ouanes Direct); Xcel Ex. 107 at 38–39 (Huso Rebuttal).

Fuel Clause Rider and Base Cost of Gas (Issue 57)

Resolved between DOC and Xcel: Approve the Company's proposed changes to its FCA Rider, with DOC's recommended revised system and class-specific base cost of energy subject to the following requirement: if any significant adjustment to the base cost of energy occurs as a result of the instant 13-868 Rate Case, then the base cost of energy should be reflected in final rates subsequent to the Commission's decision in this 13-868 Rate Case. DOC Ex. 408 at 17 (Ouanes Direct); Xcel Ex. 90 at 13–14 (Heuer Rebuttal).

Resolved between DOC and Xcel: DOC recommended that Xcel use a base cost of energy of $0.02748 per kWh instead of its proposed $0.02780 per kWh. DOC Ex. 408 at 36 (Oaunes Direct); Xcel Ex. 90 at 13–14 (Heuer Rebuttal).

Windsource Rider (Issue 59)

Resolved between DOC and Xcel: DOC recommends that Xcel not change historical data without identifying such changes and providing a justification for such changes in Windsource filings and FCA filings. DOC Ex. 408 at 12 (Ouanes Direct); Xcel Ex. 103 at 42 (Peppin Rebuttal). Xcel also implemented a consistent terminology between the Windsource tracker reports and its monthly fuel clause adjustment (FCA) filings in response to the Department's recommendation. DOC Ex. 408 at 12-13 (Ouanes Direct); Xcel Ex. 103 at 43 (Peppin Rebuttal); DOC Ex. 445 (Ouanes Opening Hearing Statement).

Energy Costs and Incentive Mechanisms (Issue 67)

Resolved between DOC, XLI, and MCC: The Department agreed with XLI that there is a need to change the current energy recovery mechanism. DOC Ex. 412 at 12 (Ouanes Rebuttal). The Department has serious concerns about the monthly rate changes that have been occurring in the FCAs. *Id.* at 13. Because this issue is not limited to Xcel, but also involves Minnesota's three other investor-owned utilities, in the Department's view this issue would be best addressed in the current Annual Automatic Adjustment (AAA) proceeding in Docket No. E999/AA-12-757 (the AAA 12-757 Docket), which specifically relates to fuel adjustment clause issues, and where the Commission would have the opportunity to evaluate the positions of other parties, including the other investor-owned utilities. *Id.*

In addition, the Department agreed with MCC witness Ms. Maini that "the burden of proof should be transferred appropriately to the utility." MCC Ex. 343 at 45 (Maini Direct). This was the basis for the Department's recommended FCA proposal in its June 5, 2013 comments. DOC Ex. 412 at 16 (Ouanes Rebuttal).

CCOSS (Issue 51)

Classification of Nobles and Grand Meadow Wind Farms

Disputed between DOC and Xcel: DOC recommended classifying the costs of the Nobles and Grand Meadow wind farms on the same basis as the other production plant costs. Xcel recommends classifying these plants as 100 percent capacity. *Compare* DOC Ex. 408 at 27 (Ouanes Direct) *with* Xcel Ex. 108 at 27 (Peppin Direct). Alternatively, classify these costs as one-hundred percent energy if the Commission finds that these wind farms were not least-cost resources and that the equivalent peaker method is not a reasonable method to classify the costs of these wind farms. DOC Ex. 414 at 5 (Ouanes Surrebuttal).

Allocation of Other Production O&M Costs

Disputed between DOC and Xcel: Allocate the Other Production O&M costs on the basis of the "location method." Xcel proposed to classify Other Production O&M costs based on the predominant nature method. *Compare* DOC Ex. 408 at 34–35 (Ouanes Direct) *with* Xcel Ex. 102 at 22–23 (Peppin Direct).

Allocation of Economic Development Discounts

Disputed between DOC and Xcel: DOC recommended allocating economic development discounts on the basis of a straight kWh energy allocator. Xcel recommended allocating these discounts on the basis of the present revenue allocator. *Compare* DOC Ex. 414 at 9-11 (Ouanes Surrebuttal) *with* Xcel Ex. 102 at 19 (Peppin Direct).

Updated Costs for Pleasant Valley and Borders Wind Projects

Disputed between DOC and Xcel: Assuming that the use of updated data information in Rebuttal Testimony is appropriate, use plant-specific data for the Pleasant Valley and Borders wind projects and 2013 cost data for all production plant costs in the application of the equivalent peaker method. *Compare* DOC Ex. 414 at 13 (Ouanes Surrebuttal) *with* Xcel Ex. 103 at 3 (Peppin Rebuttal).

A. The Objective and Steps in a Class Cost of Service Study

593. The purpose of a Class Cost of Service Study (CCOSS) is to identify, as accurately as possible, the responsibility of each customer class for each cost incurred by the utility in providing service. DOC Ex. 408 at 18 (Ouanes Direct). The CCOSS can then be used as one important factor in determining how costs should be recovered from a utility's customer classes through rate design. *Id.* DOC witness Ms. Peirce testified as to other factors, in addition to cost (such as competition and rate shock), that must be considered for purposes of determining rates. DOC Ex. 420 at 2–5 (Peirce Direct).

594. There are three steps in performing any CCOSS: 1) functionalizing, or grouping, costs by their purpose; 2) classifying costs by how they are incurred; and 3) allocating costs to customer classes. DOC Ex. 408 at 18–19 (Ouanes Direct); Electric Utility Cost Allocation Manual, 18–22 (Nat'l Ass'n of Regulatory Util. Comm'rs ed., 1992) (hereinafter Electric Manual).

B. Xcel's Embedded Class Cost of Service Study

595. The Company filed two embedded CCOSSs: a 2014 CCOSS and 2015 CCOSS, which are both sponsored by Company witness Michael A. Peppin. DOC Ex. 408 at 20 (Ouanes Direct). The Department verified that the CCOSSs were based upon reasonably current data (less than three years old). *Id.* at 21. After review of the Company's proposed CCOSSs, the Department recommended adjustments regarding the following five issues:

- Xcel's proposed change to classifying costs of the two Company-owned wind generation plants, Grand Meadow and Nobles, included in the Production Plant accounts;
- Xcel's proposed change to the classification and allocation of Other O&M costs;
- Xcel's proposed base cost of energy;
- Xcel's proposed allocation of the economic development discounts; and
- Xcel's proposed amount of economic development discounts to be recovered through base rates.

596. While the Company agreed to reduce the proposed base cost of energy and halve the proposed amount of economic development discounts to be recovered through base rates as recommended by the Department, the other issues remain disputed.

597. Other issues identified by the Department during the course of this proceeding include:

- MCC's proposed classification of Production Plant costs;
- MCC's proposed change to the classification of the Nobles and Grand Meadow wind farms;
- XLI's proposed change to the calculation of the power plant costs in the application of the equivalent peaker method;
- Xcel's use of updated plant specific data for the Pleasant Valley and Borders wind projects in Rebuttal Testimony; and
- MCC's proposed allocation of the economic development discounts.

1. Xcel's Proposed Classification of the Costs of the Nobles and Grand Meadow Wind Farms

598. The Company proposed to "classify the costs of the Nobles and Grand Meadow wind farms as 100 percent capacity." Xcel Ex. 108 at 27 (Peppin Direct). In its last three rate cases, Xcel supported the use of the equivalent peaker method (or stratification method) to classify the costs of the Company-owned wind generation plants and argued against the use of classification methods that would not reflect the operational characteristics of wind generation. DOC Ex. 408 at 24-26 (Ouanes Direct).

599. In Xcel's last three rate cases, the costs of the Company-owned wind generation plants were classified as about four to five percent capacity-related and ninety-five to ninety-six percent energy-related. DOC Ex. 408 at 22 (Ouanes Direct). The Company's proposal to classify the costs of Nobles and Grand Meadow Farms as one-hundred percent capacity is a substantial change from the Commission-approved classification method, and is not, as the Company says, a mere refinement. *Id.*; DOC Ex. 414 at 3 (Ouanes Surrebuttal).

600. The Company's justification for changing the classification of the costs of the Nobles and Grand Meadow wind generation plants in the current rate case is as follows:

> Plant Stratification is designed to recognize the fact that peaking plants (with low capital costs and high operating costs) are built to serve customer demand when there are no lower cost resources available and that intermediate and baseload generation resources (with higher capital costs) are added to provide low-cost energy. By selecting an optimal mix of these resources, we are able to minimize total system costs over time.
>
> The Nobles and Grand Meadow wind farms do not fit within this equation. While economical when acquired, these resources were added to the Company's system in order to comply with the 2007 Renewable Energy Plan; they were not added to meet our energy or capacity needs. I therefore recommend an alternative classification and allocation approach for these resources.

Xcel Ex. 102 at 27 (Peppin Direct).

601. The Company's recommendation would classify the costs of the Nobles and Grand Meadow wind farms as if there were peaking plants, which they are not. DOC Ex. 408 at 22-23 (Ouanes Direct). While there would be theoretical arguments against classifying any generation facility as one hundred percent demand, it may be possible to argue that the costs of a peaking facility could be classified as one hundred percent demand if that facility were obtained solely for capacity purposes and not to produce energy. *Id.* Wind facilities, however, only generate electricity when the wind blows. *Id.* It is an intermittent resource and, as such, wind facilities cannot be dispatched and may not produce energy when needed in the same way peaking plants do. *Id.* at 22–23. The Department is not aware of any utility that would consider adding wind capacity merely to address an increase in peak demand. *Id.* at 23.

602. Moreover, the argument that somehow wind resources are acquired, not to meet energy needs, but to comply with a policy mandate and environmental initiatives has already been addressed previously by the Commission. *Id.* at 23 and 25-26. Simply stating that these wind farms were acquired to fulfill the Company's Renewable Energy Standard (RES) obligations is not a reasonable justification to classify these wind farms as if they were peaking plants. DOC Ex. 414 at 3–4 (Ouanes Surrebuttal). In fact, starting with the same premise, OAG-AUD witness Mr. Nelson provided a better articulated justification for his proposed classification method (one-hundred percent energy) that is not as drastically inconsistent with the operational characteristics of wind farms. OAG Ex. 375 at 6–8 (Nelson Direct).

603. Xcel's new argument that the "Nobles and Grand Meadow wind farms . . . were not added to meet capacity needs" conflicts with the Company's proposal to classify the costs of its other owned wind generation plants as 100 percent demand. DOC Ex. 408 at 24 (Ouanes Direct)..

604. Xcel also testified that the Company's proposed classification of the Nobles and Grand Meadow wind farms would be an "offset" to the way Xcel recovers the costs of wind energy that is provided through PPAs. Xcel Ex. 102 at 27 (Peppin Direct). This position is not reasonable: if Xcel believed that the Commission's decisions regarding how the Company recovers the cost of wind obtained through PPAs are in error, Xcel should pursue that issue through appropriate channels. DOC Ex. 408 at 24 (Ouanes Direct). It is not reasonable to assert that the Commission's decisions were in error and then attempt to correct that error by pursuing a ratemaking option that has no basis in fact. *Id.* Moreover, Xcel recovers these costs appropriately, in the same way these resources are acquired, on a $/MWh basis. *Id.* at SO-15.

605. The Department also noted that the Company's statement in its 08-1065 rate case (Zins Rebuttal at 25–26) also conflicts with Xcel's proposed classification of Company-owned wind generation plant costs as one-hundred percent demand in this case:

> The purpose for accelerated development of wind energy is to obtain the environmental benefits of this particular source of <u>energy</u> (not capacity) as compare [sic] to other conventional <u>energy</u> (not capacity) sources. It is also well known that wind energy is intermittent and available only when the wind blows, which is further evidence that it is a source of intermittent <u>energy</u>, which may provide only a small capacity value. This is all reflected in the small 4.7% capacity value resulting for the Grand Meadow resource in the Company's stratification analysis.

Id. at 24–25. Finally, the Department noted that Xcel stated in its last rate case, 12-961 (Peppin Direct at 35):

> Although we believe the Stratification method *appropriately classifies and allocates wind generation*, we acknowledge that the Commission may determine a change is appropriate for policy reasons. (emphasis added).

These recent statements lend additional credence that the change in the way the Company classifies and allocates costs of two of its Company-owned wind farms is unreasonable. *Id.* at 25.

606. In the 10-971 docket, Xcel rejected the Minnesota Chamber of Commerce's criticism that "because wind is not a least-cost resource, and is instead purchased, at least in part, to satisfy a policy preference for clean and renewable energy, company-owned resources should not be treated like least-cost resources in the CCOSS." *Id.* at 25-26 and Commission's May 14, 2012 Findings of Fact, Conclusions, and Order (10-971 Order) at 20. Xcel asserted that "the record does not support the conclusion that wind is not a least cost resource." *Id.* at 26 and 10-971 Order at 20. The 10-971 Order states the following under the "Company-Owned Wind Resources" section: "Xcel's attribution of wind-facility costs primarily to energy needs closely matches the characteristics of wind facilities. Wind resources by and large replace other energy resources, and contribute very little to capacity. Because Xcel's cost-attribution formula [equivalent peaker method] more directly corresponds to the attributes of the resource, the Commission finds that Xcel is treating them appropriately in its CCOSS" *Id.* at 26 and 10-971 Order at 21.

607. The Department recommended that Xcel classify the costs of the Nobles and Grand Meadow wind farms in its proposed CCOSSs on the same basis as the other production plant costs: plant stratification. DOC Ex. 408 at 27 (Ouanes Direct). The ALJ finds that the Department's recommended classification of the Nobles and Grand Meadow wind farms based upon plant stratification is reasonable.

608. Alternatively, if the Commission determines that the Nobles and Grand Meadow wind farms are not least-cost resources and that the equivalent peaker method is not a reasonable method to classify the costs of these wind farms, then these wind farm costs should be classified as one-hundred percent energy since it is the only other reasonable method provided in the record. DOC Ex. 414 at 5 (Ouanes Surrebuttal).

609. The Department requested that the Company rerun its proposed 2014 CCOSS with this adjustment. DOC Ex. 408 at 27 (Ouanes Direct), where the adjustment results in a decrease of about $5.7 million in the Residential class's contribution to Xcel's revenue requirements with a corresponding increase of about $5.6 million in the Commercial and Industrial Demand class contribution to Xcel's revenue requirements.[201] *Id.* Similarly, for 2015, this adjustment results in a decrease of about $5.8 million in the Residential class' contribution to Xcel's revenue requirements with a corresponding increase of about $5.7 million in the

---

[201] For purposes of rate design, this adjustment reduces Xcel's demand-related revenue requirements by about $17 million while increasing Xcel's energy-related revenue requirements by about the same amount. DOC Ex. 409 at SO-16 (Ouanes Direct Attachments).

Commercial and Industrial Demand class contribution to Xcel's revenue requirements.[202] *Id.* at 27–28.

2. MCC's Proposed Classification of the Costs of the Nobles and Grand Meadow Wind Farms

610. The Department also did not agree with MCC's recommendation to classify and allocate Company-owned renewable generation costs by the Percent of Base Revenue method. DOC Ex. 412 at 7 (Ouanes Rebuttal).

611. First, as stated by MCC, the Percent of Base Revenue "approach mimics the current rate design," which would unreasonably include embedded policy judgments as to rate design. MCC Ex. 343 at 23 (Maini Direct); DOC Ex. 412 at 7 (Ouanes Direct).

612. Second, based on the Department's review of Table 6 in Mr. Peppin's Direct Testimony, which indicates that the Percent of Base Revenue method would be similar to (at least) a 57% capacity and 43% energy allocator, using the Percent of Base Revenue method is inconsistent with the Commission's finding that "wind resources by and large replace other energy resources, and contribute very little to capacity." DOC Ex. 408 at 26 (Ouanes Direct).

613. Third, the only justification provided to support MCC's proposed allocation is that the Commission used the present base revenue allocator in Docket No. E002/M-10-1066 to allocate RES Rider costs, including Nobles and Grand Meadow. Reliance on this justification is not reasonable, because the Commission did not adopt this method on the basis of cost causation, but because it reflected the Commission's determination of apportionment of revenue responsibility in Xcel's prior rate case (Docket 08-1065) and it preserved the then-existing rate design in an administratively simple and efficient manner. DOC Ex. 445 (Ouanes Opening Statement).

614. Finally, MCC's proposal is inconsistent with the Commission's past conclusion that:

> Xcel's attribution of wind-facility costs primarily to energy needs [on the basis of the Equivalent Peaker method] closely matches the characteristics of wind facilities. . . . Because Xcel's cost-attribution formula more directly corresponds to the attributes of the resource, the Commission finds that Xcel is treating them appropriately in its CCOSS. *Id.*

---

[202] For purposes of rate design, this adjustment reduces Xcel's demand-related revenue requirements by about $18 million while increasing Xcel's energy-related revenue requirements by about the same amount. DOC Ex. 409 at SO-17 (Ouanes Direct).

3. Xcel Large Intervenors' Proposed Calculation of Power Plant Costs is Not Reasonable

615. Xcel Large Intervenors' (XLI) recommended using power plants' depreciated replacement value in Xcel's application of the equivalent peaker method to develop stratification percentages in the CCOSS. XLI Ex. 260 at 36 (Pollock Direct). XLI's recommended value for the peaking plants is the cost that "NSP would incur to install a new peaking unit." *Id.* at 34–35.

616. The Department did not agree. DOC Ex. 412 at 10 (Ouanes Direct). While XLI's recommended values reflect the depreciated replacement values for most plants, there is a major issue arising from the use of XLI's recommended power plant costs: XLI's recommendation does not provide an "apples-to-apples" comparison. *Id.* XLI's method mixes the costs of a new peaking facility with the costs of existing baseload capacity. *Id.* at 10–11. As a result, XLI's method greatly overstates the relative investment costs of peaking capacity.[203] *Id.* at 11. Because XLI's cost estimates for the plants are not generated in a comparable fashion, the Department recommended that the Commission reject XLI's proposal. *Id.* The ALJ agrees with the Department's recommendation.

4. Proposed Classification and Allocation of Other O&M Costs

617. The Company proposed to classify the "Other Production O&M costs according to the predominant nature method." Xcel Ex. 102 at 22–23 (Peppin Direct). XLI and MCC agreed. XLI Ex. 260 at 16–21 (Pollock Direct); MCC Ex. 343 at 24–25 (Maini Direct). The Company's proposed method placed the 117 detailed cost items that make up Other Production O&M into 15 categories. Xcel Ex. 102 at 22–23 (Peppin Direct). Each category was then analyzed to determine if it was predominantly capacity-related or predominantly energy-related and classified it accordingly. *Id.* All labor costs were assumed to be predominantly "fixed" while material costs were assumed to be predominantly "variable." *Id.* at 23.

618. The overall investment method used by Xcel in its last rate case (12-961) allocated costs on the basis of overall plant investment. The overall investment method, and the refinement of this method (the "location method"), which the Commission required Xcel to use in the current rate case, are reasonable methods (consistent with cost causation) because they reflect the allocation of the generation plants at which these costs are incurred. DOC Ex. 414 at 8 (Ouanes Surrebuttal); DOC Ex. 445 (Ouanes Opening Hearing Statement).

619. The Department's review of Mr. Peppin's Direct Testimony, and in particular Table 9, found that Xcel essentially classified fixed expenses as capacity-related and variable expenses as energy-related. DOC Ex. 408 at 28–29 (Ouanes Direct). Xcel supported the overall investment method and argued against its current proposal in its prior rate cases by disputing the assertion that it is reasonable to assign "fixed" costs (plant labor costs) entirely to demand. DOC Ex. 408 at 29-31 and 34–35 (Ouanes Direct).

---

[203] If all the generator cost estimates were similarly revised, the resulting calculation would classify a larger share of Xcel's production plant cost as energy-related, opposite of the outcome XLI supports.

620. Xcel, MCC, or XLI did not provide any reasonable justification on the basis of cost causation for Xcel's proposed classification and allocation of Other Production O&M costs. DOC Ex. 414 at 8 (Ouanes Surrebuttal).

621. Xcel's proposed method is inconsistent with the Commission's Orders in Xcel's past rate cases. DOC Ex. 408 at 29 (Ouanes Direct). In those cases, Xcel allocated these costs based upon overall plant investment. *Id.* In the 2010 case, the Commission concluded that "the fixed/variable distinction does not correspond to whether those expenses are attributable to energy or demand . . . Xcel's method is preferable, because it does not misallocate the costs on the basis of their fixed or variable nature." Findings of Fact, Conclusions, and Order, Docket No. E002/GR-10-971, 18 (May 14, 2012). In the 2012 case, the Commission required Xcel to refine its allocation method for the Other Production O&M costs on the basis of the Production Plant. Findings of Fact, Conclusions, and Order, Docket No. E002/GR-12-961, Order Point 49 at 53 (Sept. 3, 2013). Xcel defined this refinement as the location method. DOC Ex. 408 at 32-33 (Ouanes Direct).

622. Classification and allocation of Other Production O&M expenses on the basis of the location method is consistent with cost causation. *Id.* While the Company believed that its proposed methodology is consistent with the Commission's order to refine its allocation method in this case, the Department disagreed. DOC Ex. 408 at 29 (Ouanes Direct); Xcel Ex. 102 at 25 (Peppin Direct). The overall investment method used by Xcel in the 12-961 rate case and refinement of this method, called the "location method," and required by the Commission, are reasonable because they reflect allocation of generation plants at which these costs are incurred. DOC Ex. 408 at 33-34 (Ouanes Direct). Xcel has argued against its current proposal in its last two rate cases and disputed the assertion that it is reasonable to assign "fixed" costs entirely to demand. DOC Ex. 408 at 33-35 (Ouanes Direct). Xcel's entirely new and inadequately supported proposal, which does not, should therefore be rejected. *Id.*

623. Contrary to Xcel's and XLI's assertions, Xcel's predominant nature method is not a refinement of the Commission's previously approved methods. *Id at 7.* Xcel's proposed classification and allocation of Other Production O&M costs is a substantial change from the classification and allocation methods that the Commission previously approved and from the current Commission-required classification and allocation method. *Id.* In addition, Xcel's proposed classification method would result in classifying these costs as 78.4% capacity-related which is much higher than classifying less than 35% of the costs as capacity-related under the location method the Commission required Xcel to use in the current rate case. *Id.*

624. Classifying the Other Production O&M costs on the basis of the location method is the only reasonable method provided in the record. DOC Ex. 414 at 8 (Ouanes Surrebuttal). The ALJ finds that the Department's recommended classification of the Other Production O&M costs on the basis of the location method is reasonable.

625. The Department requested that the Company rerun its proposed 2014 CCOSS based upon the Department's recommended and Commission-supported allocation of Other Production O&M costs on the basis of the "location method." *Id.* at 35. This adjustment resulted

in a decrease of about $12.5 million in the Residential class's contribution to Xcel's revenue requirements with a corresponding increase of about $12.4 million in the Commercial and Industrial Demand class contribution to Xcel's revenue requirements.[204] *Id.*

626. The Department also requested that the Company rerun its proposed 2015 CCOSS with the following adjustment: allocate the Other Production O&M costs on the basis of the "location method." *Id.* at 36. The adjustment resulted in a decrease of about $12.7 million in the Residential class's contribution to Xcel's revenue requirements with a corresponding increase of about $12.6 million in the Commercial and Industrial Demand class contribution to Xcel's revenue requirements.[205] *Id.*

5. Xcel's and MCC's Proposed Allocation of Economic Development Discounts Is Not Reasonable (Issue 56, in part)

627. The Company has proposed to allocate the economic development discounts on the basis of the present revenue allocator. Xcel Ex. 102 at 19 (Peppin Direct). The Company justified its proposal as follows:

> The Company's economic development discount programs are designed to attract new and retain existing large customers. We therefore used the present revenue allocator because it reasonably balances the interests of all classes in a way that is consistent with the overall goal of helping support economic development. That said, we are willing to work with parties throughout this proceeding to further evaluate the proper allocation of economic development discounts.

Id.

628. MCC proposed to allocate the economic development discounts on the basis of the present base revenue allocator. MCC Ex. 343 at 29-30 (Maini Direct). The Department did not agree and recommended that the Company allocate economic development discounts on the basis of a straight kWh energy allocator. DOC Ex. 408 at 39 (Ouanes Direct).

629. The Company's proposal and MCC's proposal are unreasonable for the following two reasons. First, such allocations would include embedded policy judgments as to rate design (from the Company's last rate case) rather than allocating costs based entirely on cost factors.

---

[204] The Department noted for purposes of rate design that this adjustment substantially reduces Xcel's demand-related revenue requirements by about $223 million while increasing Xcel's energy-related revenue requirements by about the same amount. DOC Ex. 409 at SO-18 (Ouanes Direct Attachments).

[205] The Department noted for purposes of rate design that this adjustment substantially reduces Xcel's demand-related revenue requirements by about $226 million while increasing Xcel's energy-related revenue requirements by about the same amount. DOC Ex. 409 at SO-19 (Ouanes Direct Attachments).

DOC Ex. 414 at 10-11 (Ouanes Surrebuttal). Second, as explained in the Direct Testimony of Mr. Nelson, the magnitude of the economic development discounts is based on the kWhs that the beneficiaries consume. DOC Ex. 414 at 11 (Ouanes Surrebuttal).

630. The Department concluded that allocating the economic development discounts on the basis of a straight kWh energy allocator is the only reasonable method in the record. *Id.* The ALJ agrees with the Department's recommendation.

631. The Department requested that the Company rerun its proposed 2014 CCOSS with its proposed allocation method for economic discounts, which resulted in a decrease in the Residential class's contribution to Xcel's 2014 revenue requirements and a corresponding increase in the Commercial and Industrial Demand class contribution. DOC Ex. 408 at 39–40 (Ouanes Direct). There were similar results for a revised 2015 CCOSS. *Id.* at 40.

6. Classification of Production Plant Costs: The Department's Response to the Minnesota Chamber of Commerce

632. MCC recommended that the Company classify and allocate fixed production plant costs on the basis of the peak demand or straight fixed variable (SFV) method. MCC Ex. 343 at 19 (Maini Direct). Under MCC's proposal, fixed production plant costs would be classified entirely as demand-related costs. *Id.*

633. The Department did not agree with MCC's recommendation. DOC Ex. 412 at 4 (Ouanes Rebuttal). First, the Commission chose not to approve this same proposal in Xcel's prior rate case (Docket No. E002/GR-12-961), or prior rate cases for that matter, and MCC provided no new argument that would warrant a change in this approach. *Id.* Second, MCC's recommendation "fails to recognize the dual nature of baseload plants in meeting both the peak demands and the annual energy requirements of customers." Findings of Fact, Conclusions, and Order, Docket No. E001/GR-10-276, 50–51 (Aug. 12, 2011) (hereinafter 10-276 Order)). Importantly, the Department noted that "[t]he Commission has long recognized that production plant costs should be classified based on the determination of what influences a utility's production plant investment decisions." 10-276 Order at 51.

634. The determination of resources needed to meet demand on Xcel's system is made through Xcel's resource planning process, which starts with the need for additional resources—both energy and demand—based on a forecast of its demand load and energy requirements over a fifteen-year period, and then uses a capacity-expansion model (Strategist) to derive the least-cost expansion plan (resource combination) to address the projected need. DOC Ex. 412 at 5 (Ouanes Rebuttal). Such models and decision-making must reflect both capacity and energy costs. *Id.*

635. The equivalent peaker method to classify production plant costs is consistent with the Company's resource planning process. Xcel uses an equivalent peaker method. *Id.* As discussed in the Electric Manual, "[e]quivalent peaker methods are based on generation expansion planning practices, which consider peak demand loads and energy loads separately in determining the *need* for additional generation capacity and the most cost-effective *type* of

capacity to be added." Electric Manual at 52–53. The Company's method is consistent with Xcel's resource planning process as described above. DOC Ex. 412 at 5 (Ouanes Rebuttal).

636. Contrary to MCC's assertion, the SFV method is not "consistent with the notion of least cost planning and minimizing total costs." MCC Ex. 343 at 19 (Maini Direct). By classifying all fixed production plant as demand related, the SFV method ignores the dual nature of baseload plants in meeting both the peak demands and the annual energy requirements of customers. DOC Ex. 412 at 6 (Ouanes Rebuttal). If Xcel were to select generators solely to provide capacity to meet peak customer demand, Xcel would select only generators that have the lowest cost per unit of capacity, the so-called peaking generators. *Id.* The fact that Xcel has actually acquired a variety of generator types undermines MCC's assertion. *Id.*

637. Because it reflects Xcel's decision-making on production plant, the Department recommended classifying the costs of Production Plant on the basis of the equivalent peaker (or plant stratification) method. DOC Ex. 445 (Ouanes Opening Hearing Statement). The ALJ agrees that the Department's (and the Company's) classification of fixed production plant based upon plant stratification is reasonable. The ALJ does not recommend adopting MCC's proposed classification method for fixed production plant.

7. Xcel's Use of Updated Plant Specific Data for the Classification of the Costs of the Pleasant Valley and Borders Wind Farms

638. Xcel proposed changing the replacement cost and summer capacity data the Company used in its proposed Direct 2015 CCOSS as a result of the availability of more current information. Xcel Ex. 103 at 3 (Peppin Rebuttal). Even assuming that it is appropriate in Rebuttal Testimony to use updated data, the Company has not shown its proposed change to be reasonable. DOC Ex. 414 at 13 (Ouanes Surrebuttal). Xcel proposed a limited update of 2012 cost data in its application of the equivalent peaker method. *Id.* For all other production plant costs, Xcel continues to use 2012 cost data in its application of the equivalent peaker method even though 2013 cost data is available for all production plant costs, as provided in Attachment A of Xcel's response to XLI information request number 213. *Id.* If using updated information is appropriate, the Department recommended adjusting Xcel's proposed CCOSSs by using plant-specific data for the Pleasant Valley and Borders wind projects and 2013 cost data for all production plant costs in the application of the equivalent peaker method. *Id.*

639. The ALJ finds that using updated information is reasonable and recommends adjusting Xcel's proposed CCOSSs by using plant-specific data for the Pleasant Valley and Borders wind projects and 2013 cost data for all production plant costs in the application of the equivalent peaker method.

IX. RATE DESIGN

<u>Allocation of Revenue Requirement</u>

Disputed by DOC and Xcel: *See* DOC's Summary of Recommendations, Section D.3. below.

<u>Residential Customer Charges</u>

Disputed by DOC and Xcel: *See* DOC's Summary of Recommendations, Section E.1. below.

C&I Demand Customer Charges

Resolved by DOC and Xcel: DOC Ex. 420 at 22 (Peirce Direct); Xcel Ex. 105 at 20–21 (Huso Direct).

Energy Charge Credit

Resolved between DOC and Xcel: The Department recommended approval of Xcel's proposed energy charge credit (ECC) because it recognizes the lower energy-related cost of high load factor customers. DOC Ex. 420 at 24 (Peirce Direct).

Time-of-Day Rates

Resolved between DOC and Xcel: The Department recommended that the Commission approve Xcel's proposed time of day (TOD) Energy Charge methodology. DOC Ex. 420 at 23 (Peirce Direct).

Interruptible Service Rates

Disputed between DOC and Xcel: The Department proposed a three percent increase in Xcel's Interruptible Discount rates. Xcel proposed to increase the interruptible service discount by approximately 5.1 percent. *Compare* DOC Ex. 420 at 26 (Peirce Direct) *with* Xcel Ex. 105 at 26–27 (Huso Direct).

A. Rate Design Background

640. Without competition, government regulation approximates the results that would be achieved in a competitive environment. Rate design is the second step of the two-step rate making process. In the first step, the Commission determines the revenue requirement, which is quasi-judicial and fact intensive. *See Matter of Request of Interstate Power Co. for Authority to Change Rates* (*Interstate Power*), 559 N.W.2d 130, 133 (Minn. Ct. App. 1997), *aff'd* 574 N.W.2d 408 (Minn. 1998). The second step, designing rates to charge customers, is largely a quasi-legislative function. *Interstate Power*, 559 N.W.2d at 133. While the second step of rate making largely involves facts, it also involves policy decisions. *Id.*

B. Rate Design Goals

641. The Commission has relied on the following principles in designing reasonable and just rates:

a. Rates should be designed to allow the Company a reasonable opportunity to recover its revenue requirement, including the cost of capital;

b. Rates should promote efficient use of resources by sending appropriate price signals to customers, reflecting the costs of serving them. For example, an appropriate price signal encourages conservation by customers;

c. Rate changes should be gradual so as to limit rate shock to consumers. Rate stability and continuity are important to both the utility and the consumer; and

d. Rates should be understandable and easy to administer. Maintaining ease in administration helps ensure that customers understand their utility bills better.

DOC Ex. 420 at 2 (Peirce Direct).

642. The first principle recognizes that Xcel should be afforded the opportunity to recover its revenue requirement, including recovery of its capital costs, which ties into the notion that in the absence of competition, government regulation attempts to approximate the results that would be achieved in a competitive environment. *Id.* at 2–3

643. The second principle reflects the goal that rates should send an appropriate price signal to customers by reflecting the cost of serving them. *Id.* at 3. Rates set at marginal cost (the cost of producing the next increment of service) result in an efficient allocation of resources used to produce the incremental unit of service. *Id.* In other words, an efficient allocation of resources takes place when the value a customer places on a product is equal to the cost of producing the product. *Id.* Although the costs in the current case are based on the embedded or historical cost of the system, setting rates at or near the embedded cost to serve each customer class should provide adequate price signals to customers. *Id.*

644. The third principle reflects that current and proposed rates should have some continuity with past rates. DOC Ex. 402 at 3 (Peirce Direct). Rate stability and continuity are important both to the utility and the consumer. *Id.* Consumers benefit by limiting rate shock associated with wide swings in rates, and utilities are afforded the opportunity to recover a steady revenue requirement. *Id.*

645. Finally, the fourth principle provides that rates should be understandable and easy to administer. *Id.* Maintaining ease in administration will help ensure that customers have a better understanding about the amounts and parts of their utility bills. *Id.*

C. Legal Standards Reflected in Rate Design Principles

646. These four rate-design principles reflect Minnesota law. A fundamental tenet of Minnesota law is that regulated public utilities can only charge just and reasonable rates. Minn. Stat. § 216B.03 (2012). When seeking to change its rates, a public utility has the burden to show that its requested rate change is just and reasonable. Minn. Stat. § 216B.16, subd. 4. Environmentally related, rates must also encourage energy conservation "to the maximum reasonable extent." § 216B.03. In that regard, the Minnesota legislature has found that:

> [I]t is in the public interest to review, analyze and encourage those energy programs that will minimize the need for annual increases

> in fossil fuel consumption by 1990 and the need for additional electrical generating plants, and provide for an optimum combination of energy sources consistent with environmental protection and the protection of citizens.

Minn. Stat. § 216C.05 (2012). Minnesota law also encourages rate designs that promote the use of renewable energy. *Id.* Moreover, if there is any doubt as to the reasonableness of a particular rate design, such doubt must be resolved in the consumer's favor. § 216B.03. In other words, where different rates appear to be equally valid, the Commission must choose the rate design that favors the consumer. *Id.* Minnesota law also prohibits public utilities from charging unreasonably discriminatory rates:

> Rates shall not be unreasonably preferential, unreasonably prejudicial or discriminatory, but shall be sufficient, equitable and consistent in application to a class of consumers.

§ 216B.03; DOC Ex. 402 at 4 (Peirce Direct). Similarly, a "public utility [shall not], as to rates or service, make or grant any unreasonable preference or advantage to any person or subject any person to any unreasonable prejudice or disadvantage." Minn. Stat. § 216B.07 (2012). The Commission is also required to consider the ability to pay as a factor when setting public utility rates. Minn. Stat. § 216B.16, subd. 15 (2012).

647. Because rates differ among the various classes of service, DOC concluded that there must be a cost basis for any differences to be deemed reasonable, unless one of the rate-design principles above is used to adjust rates. DOC Ex. 402 at 4 (Peirce Direct).

D. Apportionment of Revenue Responsibility (Issue 53)

1. Apportionment of Revenue Responsibility By Class

648. Xcel provided its proposed 2014 and 2015 apportionment of revenue responsibility in the Direct Testimony of Steven Huso. Xcel Ex. 105 at 7, SVH-1, Schedule 4 (Huso Direct). Xcel proposed to move each of the customer classes closer to their cost of service, with the exception of the Lighting class, for which Xcel proposed no increase in rates, and which remains well above its cost of service. DOC Ex. 402 at 6 (Peirce Direct).

649. The Department did not agree with the Company's proposed apportionment of revenue responsibility for 2014 and 2015. *Id.* In his Testimony, Department witness Dr. Samir Ouanes addressed the Department's concerns with Xcel's proposed CCOSS. The financial impact of Dr. Ouanes's proposed changes to the CCOSS is to increase the cost of service to the Large C&I Demand class and to reduce the cost of service for the Residential and Small C&I Non-Demand classes. DOC Ex. 402 at 6 (Peirce Direct).

650. Regarding impacts of changes to the CCOSS to apportion revenue responsibility, it is clear that Xcel's proposed apportionment of revenue responsibility results in the Residential and C&I Non-Demand classes being apportioned more revenue responsibility than the cost of service for those two classes. *Id.* at 7. For example, Xcel's proposed revenue responsibility

apportioned to the Residential class represents 99.5 percent of the Company's proposed cost of serving the Residential class, but 101.2 percent of the cost of serving this class under Dr. Ouanes's proposed methodology. *Id.* Similarly, C&I Non-Demand customers are apportioned 100 percent of the cost under the Company's proposed CCOSS compared with 102.8 percent under the Department's recommended CCOSS methodology. *Id.* at 7–8.

Table 1: Comparison of CCOSS Outcomes

Customer Class	Current Revenue ($1,000s)	Adj. 2014 Cost ($1,000s)	DOC Prop. CCOSS ($1,000s) DOC IR 715-Revised	Current Rev/ DOC CCOSS	Xcel Proposed 2014 Revenue	Xcel Proposed as % of Proposed CCOSS	Proposed as % of DOC IR-715 Cost
Residential	$1,001,398	$1,093,707	$1,074,955	93.2%	$1,087,898	99.5%	101.2%
C&I Non-Demand	$105,523	$113,274	$110,189	95.8%	$112,274	100.0%	102.8%
C&I Demand	$1,655,346	$1,749,971	$1,770,394	93.5%	$1,753,458	100.2%	99.0%
Lighting	$26,477	$24,154	$25,568	103.6%	$26,477	109.6%	103.6%
Total	$2,788,744	$2,981,106	$2,981,106	93.5%	$2,981,107	100.0%	100.0%

1. Based upon Dr. Ouanes's recommended changes to the CCOSS, the Department recommended the following apportionment of revenue responsibility for 2014 and 2015 respectively. *Id.* at 8.

Table 2: Summary of DOC's Initial Proposed 2014 Apportionment of Revenue Responsibility

Customer Class	Current Revenue	Xcel Proposed 2014 Revenue	DOC Prop. CCOSS ($1,000s)	DOC Proposed Revenue	Percent of Total Revenue	Percent Increase	DOC Proposed as % of DOC Cost
Residential	$1,001,398	$1,087,898	$1,074,955	$1,072,268	36.0%	7.1%	99.8%
C&I Non-Demand	$105,523	$112,274	$110,189	$111,107	3.7%	5.3%	100.8%
C&I Demand	$1,655,346	$1,753,458	$1,770,394	$1,771,220	59.4%	7.0%	100.0%
Lighting	$26,477	$26,477	$25,568	$26,477	0.9%	0.0%	103.6%
Total	$2,788,744	$2,981,107	$2,981,106	$2,981,072	100.0%	6.9%	100.0%

Table 3: Summary of DOC's Initial Proposed 2015 Apportionment of Revenue Responsibility

Customer Class	Current Revenue ($1,000's)	Xcel Proposed 2015 Revenue	DOC Prop. CCOSS DOC IR. 716	DOC Proposed Revenue	Percent of Total Revenue	DOC Prop. as a % of Cost	Percent Increase Current
Residential	$1,001,398	$1,127,053	$1,115,182	$1,107,658	36.0%	99.3%	10.6%
C&I Non-Demand	$105,523	$117,082	$113.982	$114,774	3.7%	100.7%	8.8%
C&I Demand	$1,655,346	$1,808,851	$1,823,647	$1,829,680	59.4%	100.3%	10.5%
Lighting	$26,477	$26,477	$26,651	$27,351	0.9%	102.6%	3.3%
Total	$2,788,744	$3,079,463	$3,079,462	$3,079,463	100.0%	100.0%	10.4%

The Department proposed to move all classes closer to cost while moderating the overall rate increases to all classes. DOC Ex. 402 at 9 (Peirce Direct). Even under the Department's proposed revisions to the CCOSS, however, the Lighting class remains above cost. *Id.* Consequently, the Department agreed with Xcel not to increase the apportionment of revenue responsibility to the Lighting class in 2014. *Id.* The C&I Non-Demand class currently pays for approximately ninety-six percent of the cost of serving that class, and a move to just over cost represents a 5.3 percent increase, less than the 6.9 percent overall rate increase requested by Xcel. *Id.* The Department moved the Residential class to just under cost, and the C&I Demand class to cost which resulted in 7.1 percent and 7.0 percent increases, respectively. *Id.*

651. The Department's proposed 2015 apportionment of revenue responsibility is determined by applying the percentage of total revenue for each customer class from its 2014 recommendation to Xcel's proposed 2015 revenue requirement, which results in a 3.3 percent across-the-board increase for all classes. *Id.* Using this method resulted in an increase in the revenue responsibility apportioned to the Lighting class in 2015, in contrast to Xcel's proposal to hold revenues constant for both 2014 and 2015 for the Lighting class. DOC Ex. 420 at 9–10 (Peirce Direct). Despite the increased apportionment of revenue responsibility to the Lighting class, it moved closer to its cost of service by recovering 102.6 percent of its cost of service in 2015 compared with 103.6 percent in 2014. *Id.* at 10.

652. The Department recommended that the Commission adopt Ms. Peirce's apportionment of revenue responsibility found in Attachments SLP-2 and SLP-3 because it balances the goal of moving toward cost to lessen the impact of inter-class subsidies with the goal of moderating the overall revenue increase experienced by each class. *Id.* The ALJ finds that the Department's recommended apportionment of revenue responsibility is reasonable.

653. If the Commission approves a different revenue requirement than Xcel has proposed, the Department recommended that the Commission adjust the class apportionments proportionally to its recommendation. *Id.* at 11. The ALJ agrees.

2. The Role of Inter-Class Subsidies and Rate Shock

654. An inter-class subsidy occurs when revenue responsibility apportioned to one class of customers fails to recover the cost of serving those customers, with the difference being made up by over-recovering costs from other customer classes. *Id.* at 10.

655. Minimizing inter-class subsidies is important. *Id.* Rates should be fair, and ideally the best way to define "fair" is that each class of customer would pay enough to cover its share of costs. DOC Ex. 420 at 10 (Peirce Direct). Moreover, customers need accurate information about the cost of electricity so they can make informed decisions about how much electricity they use, which is often referred to as "price signals." *Id.*

656. Ideally revenue responsibility apportionment for the classes would completely match the cost allocations by classes that are identified in the CCOSS. *Id.* at 11. While apportionment of revenue responsibility for Xcel's broad customer classes is already close to cost, cost allocations are not perfect, in part, because there is often more than one way to allocate costs to customer classes. *Id.* Moreover, even if cost allocations were perfect, apportioning revenue responsibility should be gradual in order to limit rate shock to the consumers. *Id.* "Rate shock" is a relative concept that reflects the impact of a rate increase on total customer bills. DOC Ex. 420 at 11 (Peirce Direct). In recommending a particular apportionment of revenue responsibility, and customer charge, the Department sought to balance the goal of establishing cost-based rates with the goal of achieving a moderate impact to customer bills. *Id.* This rate-making approach is reasonable.

3. Surrebuttal Update of Revenue Apportionment

657. Xcel witness Mr. Huso provided revisions to Xcel's proposed apportionment of revenue responsibility in his Rebuttal Testimony. Xcel Ex. 107 at 5 (Huso Rebuttal). The following tables summarize Xcel's revised proposal for apportionment of revenue responsibility:

Table 4: Summary of Xcel's Rebuttal Apportionment of 2014 Revenue Responsibility

Customer Class	Revised Current Revenue ($1,000's)	Revised Adj. 2014 Cost ($1,000's)	Xcel Proposed 2014 Revenue	Percent of Total Revenue	Percent Increase
Residential	$983,255	$1,062,672	$1,057,900	36.7%	7.6%
C&I Non-Demand	$101,372	$109,723	$109,200	3.8%	7.7%
C&I Demand	$1,603,456	$1,687,397	$1,690,100	58.6%	5.4%
Lighting	$25,753	$23,508	$25,800	0.9%	0.2%
Total	$2,713,836	$2,883,299	$2,883,299	100.0%	6.2%

Table 5: Summary of Xcel's Rebuttal Apportionment of 2015 Revenue Responsibility

Customer Class	Current Revenue ($1,000's)	Xcel Proposed 2015 Revenue	Percent of Total Revenue	Adj. 2015 Cost ($1,000's)	Percent Increase From Current	Percent Increase From 2014
Residential	$983,255	$1,094,000	36.7%	$1,099,000	11.3%	3.4%
C&I Non-Demand	$101,372	$112,700	3.8%	$113,200	11.2%	3.2%
C&I Demand	$1,603,456	$1,745,400	58.6%	$1,740,600	8.9%	3.3%
Lighting	$25,753	$25,800	0.9%	$25,000	0.2%	0.0%
Total	$2,713,836	$2,977,800	100.0%	$2,977,800	9.7%	3.3%

DOC Ex. 422 at SLP-S-1, SLP-S-2 (Peirce Surrebuttal). Specifically, Xcel's updated apportionment reflected revisions to current revenues as well as changes to Residential and C&I Non-Demand classes. *Id.* at 2.

658. In Rebuttal Testimony, Xcel agreed with Dr. Ouanes's recommendation to reduce the size of the economic development discount, but not with his recommended methodology for allocating the discount among the customer classes. Xcel Ex. 107 at 38–39 (Huso Rebuttal). The Company also disagreed with Dr. Ouanes's other recommended changes to the CCOSS. *See* Xcel Ex. 103 at 7–8 (Peppin Rebuttal); Xcel Ex. 104 at 9 (Peppin Surrebuttal).

659. The Department updated its recommended apportionment of revenue responsibility to reflect the revised revenue requirement provided in the Rebuttal Testimony of Xcel witness Steve Huso, to allow for comparison between the two proposals. DOC Ex. 422 at 3 (Peirce Surrebuttal). The following tables reflect the Department's updated recommended apportionment of revenue responsibility among customer classes:

Table 6: Summary of DOC's Updated Proposed 2014 Apportionment of Revenue Responsibility

Customer Class	Revised Current Revenue	Xcel Proposed 2014 Revenue-Revised	Percent Increase	DOC Proposed Revenue	Percent of Total Revenue	Percent Increase
Residential	$983,255	$1,057,900	7.6%	$1,046,247	36.3%	6.4%
C&I Non-Demand	$101,372	$109,200	7.7%	$106,229	3.7%	4.8%
C&I Demand	$1,603,456	$1,690,100	5.4%	$1,705,070	59.1%	6.3%
Lighting	$25,753	$25,800	0.2%	$25,753	0.9%	0.0%
Total	$2,713,836	$2,883,299	6.2%	$2,883,299	100.0%	6.2%

Table 7: Summary of DOC's Updated Proposed 2015 Apportionment of Revenue Responsibility

Customer Class	Revised Current Revenue ($1,000's)	Xcel Proposed 2015 Revenue	DOC Proposed Revenue	Percent of Total Revenue	Percent Increase Current	% change from 2014
Residential	$983,255	$1,094,000	$1,080,588	36.3%	9.9%	3.3%
C&I Non-Demand	$101,372	$112,700	$109,664	3.7%	8.2%	3.2%
C&I Demand	$1,603,456	$1,745,400	$1,761,002	59.1%	9.8%	3.3%
Lighting	$25,753	$25,800	$26,546	0.9%	3.1%	3.1%
Total	$2,713,836	$2,977,800	$2,977,800	100.0%	9.7%	3.3%

The Department proportionally adjusted the current revenues to reflect its initial proposed revenue responsibility apportionment. *Id.* at 3–4. The method the Department used is consistent with the methodology approved by the Commission in Xcel's prior two rate cases, as detailed in Mr. Huso's Direct Testimony. *Id.* at 4; Xcel Ex. 105 at 13 (Huso Direct).

660. The ALJ finds that the Department's updated apportionment of revenue responsibility is reasonable and recommends that it be adopted by the Commission.

A. Customer Charges

1. Residential and Small General Service Classes (Issue 54)

661. The following table summarizes Xcel's and the Department's proposed customer charges for the Residential and Small General Service customer classes. *Id.* at 12.

Table 8: Summary of Proposed Customer Charges

<table>
<tr><th>Service</th><th>Current</th><th>Xcel Proposed</th><th>Cost</th><th>DOC Proposed</th></tr>
<tr><td>Residential - Overhead</td><td>$8.00</td><td>$9.25</td><td rowspan="4">$15.86 average</td><td>$8.50</td></tr>
<tr><td>Residential – Underground</td><td>$10.00</td><td>$11.25</td><td>$10.50</td></tr>
<tr><td>Res. Electric Heat-Overhead</td><td>$10.00</td><td>$11.25</td><td>$10.50</td></tr>
<tr><td>Res. Electric Heat - Undergrd</td><td>$12.00</td><td>$13.25</td><td>$12.50</td></tr>
<tr><td>Small General Service</td><td>$10.00</td><td>$11.50</td><td>$16.84</td><td>$10.50</td></tr>
</table>

Xcel proposed to increase its Residential monthly customer charge by $1.25. Xcel Ex. 105 at 15 (Huso Direct). The average customer-related cost, according to the Company's CCOSS, is $15.86 per month for a residential customer. *Id.*

662. The Department evaluated Xcel's proposed Residential and Small General Service customer charges. DOC Ex. 420 at 12 (Peirce Direct). While it is reasonable to increase customer charges to reflect the fixed costs of meters, billing, and other related costs of delivering electricity to customers, because Xcel so recently raised its customer charges and because Xcel's proposal would set the residential customer charge higher than the rates for other electric utilities, it would not be reasonable to increase customer charges by the amount Xcel proposes.

Id. Rather, the Department recommended increasing the monthly customer charges by $0.50 per month to $8.50 per month for overhead residential customers, and $11.50 per month for underground customers. *Id.* at 12–13. The Department recommended a similar $0.50 per month increase for Residential Electric Heating and Small General Service customers. *Id.* at 13. The ALJ agrees and finds the Department's recommended customer charges to be reasonable.

663. In arriving at its recommended customer charges, the Department reviewed Commission-approved customer charges for other rate-regulated electric utilities. *Id.* As shown below, an $8.50 per month customer charge is consistent with the customer charges of Minnesota Power, Otter Tail Power and Interstate Power & Light in their recent electric rate cases. DOC Ex. 420 at 13 (Peirce Direct).

Table 9: Residential Customer Charges for Minnesota Electric Utilities

Company/Docket No.	Company Proposed Customer Charge	PUC Approved/DOC Proposed
Minnesota Power –E015/GR-09-1151	$9.75	$8.00
Otter Tail Power – E017/GR-10-239	$9.00	$8.50
Interstate Power & Light – E001/GR-10-276	$10.00	$8.50

In recommending a lower Residential customer charge than proposed by the Company, the Department sought to balance the impact of an increase in the fixed customer charge on customers or households with the impact of intra-class subsidies. *Id.* This methodology is reasonable.

664. Like an inter-class subsidy, an intra-class subsidy results when the proposed service rate does not recover service costs. *Id.* at 14. For example, in the Residential class, costs must be recovered either through the customer charge or through the energy charge. *Id.* To the extent customer charges do not recover the full cost of connecting and keeping a customer on the system (including connecting to the system along with ongoing metering, billing, customer service and repair), the costs of providing these services will be recovered through the energy charge. *Id.* As a result, customers who use less energy on average will not pay for their share of customer costs while customers with higher monthly usage will pay not only for their share of customer costs but will also pay for the costs low-use customers did not pay. *Id.* On average, the utility will recover all of its costs, but certain customers within a class will pay in excess of the cost to serve them and subsidize other customers within the same class who pay less than the cost to serve them. *Id.* at 15. Higher-usage customers pay for customer costs through their customer charge, as well as the extra customer costs included in the energy charge for customer costs they do not impose on the system. DOC Ex. 420 at 14 (Peirce Direct). The result is that these customers subsidize the revenue that would otherwise have been collected in a monthly customer charge from low-usage customers. *Id.*

665. Intra-class subsidies are present in Xcel's proposed rates. *Id.* As explained above, Xcel's (and the Department's) proposed customer charges for the Residential Class do not fully

collect fixed costs of customers being connected to Xcel's system, which results in an intra-class subsidy from high-use to low-use customers within the class. *Id.*

666. The Department strongly recommended that the Commission promote goals of fairness and provide appropriate price information by adopting rates that are based on cost, as much as possible. *Id.* In the past, the Commission has been concerned that high customer charges may be burdensome to low-income households. *Id.* The assumption underlying this concern, at least in part, was that low-income households may use less energy than other residential customers, but this may not always be the case. *Id.*

667. Because intra-class subsidies may have a disproportionately greater financial impact on low-income customers, the record should demonstrate whether this assumption about energy use by low-income and other households is correct, in order to verify whether adoption of a particular rate design proposal accomplishes the goal of benefiting low-income customers. DOC Ex. 420 at 16 (Peirce Direct).

668. As shown in the table below, the Department determined that the amount of monthly usage necessary to cover customer costs without any subsidy is approximately 600 kWh.[206] *Id.* at 17. At this breakeven point, customer costs are fully recovered from the combination of customer charges and the energy charge. *Id.* Customers using less than 600 kWh per month do not pay for all of the customer costs they impose on Xcel's system, thereby receiving a subsidy. *Id.* Conversely, households using more than 600 kWh per month subsidize households using less than 600 kWh. *Id.* The breakeven point for recovering customer costs can be determined as follows:

[206] The breakeven usage is calculated by dividing the monthly customer cost recovered through the energy charge by the energy charge ($10.24/$0.01579), or 640 kWh. The Department's witness rounded down to 600 kWh for ease of calculation.

Table 10: Summary of Breakeven Point for Residential Customer Costs Under Xcel's Current and Proposed Rates

		Current Customer Charge/Cost	Xcel Proposed Customer Charge/Cost
1	Residential customer cost (Xcel CCOSS, p. 2 line 17)	$15.86	$15.86
2	Minus: customer charge[1]	$ 8.00	$9.25
3	Monthly customer costs recovered from energy charge, per customer	$7.86	$6.61
4	x 12 months	x 12	x 12
5	Annual customer costs recovered in energy charge, per customer	$94.32	$79.32
6	x Avg. no. of customers (Xcel CCOSS, p. 2, line 14)	1,108,321	1,108,321
7	Total annual customer costs recovered in energy charges	$104,536,837	$87,912,022
8	Divided by kWh sales (Xcel CCOSS, p. 2, line 21)	8,507,873,000	8,507,873,000
9	Per-kWh recovery of customer costs in the energy charge	$0.01229	$0.01033
(3/9)	Breakeven usage amount	640 kWh	640 kWh

The breakeven point estimates the amount of electricity use necessary to recover the remaining customer costs through the energy charge. DOC Ex. 420 at 18 (Peirce Direct). According to Xcel's CCOSS, the Residential customer cost is $15.86 per customer per month. *Id.* The difference between the monthly customer cost and the amount of the customer charge must be recovered from the Residential class by the energy charge. *Id.* Under Xcel's current rates, the $7.86 difference between the monthly customer cost and the customer charge is recovered through a higher energy charge. *Id.*

669. The bill impact on Residential customers of recovering customer costs through the energy charge depends on how much energy a household uses in a given month. *Id.* at 19. Under current rates, an average Residential customer must use approximately 600 kWh to fully pay for the $7.86 in customer costs from the energy charge. *Id.* Customers using less than 600 kWh will be subsidized by households using more than that amount each month. DOC Ex. 420 at 19 (Peirce Direct). For example, a customer using 400 kWh per month would pay only $4.91 (400 * $0.01229/kWh) of their customer costs through their energy usage. *Id.* Consequently, at 400 kWh of usage per month, revenues fall $2.95 short of the necessary $7.86 in customer costs needed to be recovered from the energy charge. *Id.* On the other hand, a multi-member household using 1,000 kWh would pay an additional $4.43 per month above their customer costs ((1,000 * $0.01229/kWh))-$7.86) to subsidize the customers using less than 600 kWh per month. *Id.* The Department is concerned that customers with higher usage levels, some of whom are households with low incomes, are subsidizing the customer costs of lower usage households that may have average or high incomes. *Id.*

670. Mr. Huso supplied the average customer counts, average kWh usage and average bill amounts for all residential customers, customers participating in energy assistance programs and non-energy assistance customers. Xcel Ex. 105 at SVH-1, Appendix A, 2-4 (Huso Direct). The following table summarizes Xcel's Residential customer usage:

Table 11: Summary of Monthly Average Residential Customer Usage

2012:	**All Customers**	**LIHEAP* Participants**	**Non-LIHEAP Participants**
October	501	477	503
November	580	533	584
December	696	638	701
2013:			
January	769	714	773
February	655	623	657
March	621	587	624
April	539	503	542
May	558	495	563
June	544	490	548
July	1,002	857	1,013
August	926	836	933
September	582	527	586
Average kWh	664	607	669
Average customer count	1,116,016	76,957	1,039,059
Average bill	$76.78	$60.85	$77.95

* Low Income Home Energy Assistance Program. *Id.*

671. The Department concluded that, in each month, LIHEAP customers used less energy on average than non-LIHEAP customers. DOC Ex. 420 at 20 (Peirce Direct). In five of the months, however, the average use per low-income household was above the 600 kWh threshold. *Id.* When households use more than 600 kWh in a given month, they are subsidizing households that use less than 600 kWh. *Id.* Such subsidies are not fair when paid by customers who are already struggling to pay their bills. *Id.* The ALJ agrees.

672. Because Residential customer costs are $15.86 per month, while increasing the Residential customer charge to $8.50 per month does not eliminate intra-class subsidization, a fifty cent increase is a very modest and reasonable movement toward cost that will reduce the subsidy. *Id.* at 21.

2. Base Energy Charges for the C&I Demand Class (Issue 62A)

Resolved between DOC and Xcel. DOC accepted the rates proposed by Xcel, as they appear consistent with the results of the modified CCOSS recommended by the Department, the

Department also recommended approval of Xcel's proposed energy rates. DOC Ex. 420 at 22 (Peirce Direct).

673. According to Mr. Huso's testimony, the Commercial and Industrial (C&I) Demand class energy charges were based on the non-fuel, energy-related cost of service including stratified production capacity costs. Xcel Ex. 105 at 20–21 (Huso Direct). In this case, Xcel's proposed CCOSS resulted in an energy charge less than the results of its 2013 rate case compliance CCOSS, and less than the current base energy rate. *Id.* Consequently, Mr. Huso stated that he did not set the energy charge at cost, but rather proposed a small increase in the energy charge to maintain the relationship between the energy and demand charges. *Id.* at 21.

674. In response to DOC IR No. 304, Xcel stated that the decrease in energy costs is the result of changes in its CCOSS methodology, including the plant stratification methodology, and classification of the Grand Meadows and Nobles wind facilities as 100 percent capacity. DOC Ex. 420 at SLP-6 (Peirce Direct). The Department's recommended changes to the CCOSS, however, will not affect the proposed energy rate for C&I Demand customers. *Id.* at 22. In DOC IR No. 318, the Department asked the Company to provide any changes to its proposed rates or rate design that would result from the adoption of the modified CCOSS studies requested in DOC IR Nos. 713, 714, and 715. *Id.* at 22, SLP-7. In response, Xcel indicated that the modified CCOSS requested by the Department would not change the Company's proposed rates because the rates developed from those modifications remained close to rates proposed by Mr. Huso in this case. *Id.*

675. Because the proposed rates appear consistent with the results of the modified CCOSS recommended by the Department, the Department also recommended approval of Xcel's proposed energy rates. *Id.* at 22. The ALJ finds this recommendation to be reasonable.

3. Time-of-Day Energy Charges (Issue 60, in part)

676. TOD energy charges are determined by using the General Service energy charge weighted by the on-peak and off-peak percentages for the C&I Demand class, and the system-weighted average marginal energy costs for on-peak and off-peak periods. Xcel Ex. 105 at 22–23 (Huso Direct). The Company typically uses the forecasted annual marginal energy cost ratio to moderate changes from the combination of TOD base energy rates and TOD fuel cost charges. *Id.* In this proceeding, Xcel used the forecasted marginal energy cost ratio for the summer months of 2013 as the basis for calculating the TOD energy charge rather than the forecasted full-year ratio. *Id.*

677. The Department recommended that the Commission approve Xcel's proposed TOD Energy Charge methodology. DOC Ex. 420 at 23 (Peirce Direct). The calculation change appears to be reasonable and may provide slightly better price signals to customers to shift their usage to off-peak periods. *Id.* The ALJ agrees and so recommends.

4. Energy Charge Credit (Issue 60, in part)

678. The ECC is a credit that applies to customers with higher load factors, and with kWh energy usage above 400 hours of usage in a month. *Id.* A higher load factor indicates that

the customer's energy use is more consistent throughout the year. *Id.* An example might be an industrial customer that operates 24 hours a day, 365 days per year. *Id.* Such a pattern of energy use is less expensive to serve on a kWh basis since the customer uses relatively more energy during less expensive (off-peak) periods. DOC Ex. 420 at 24 (Peirce Direct).

679. Xcel's proposed ECC credit recognizes the lower energy related cost of high load factor customers, and consequently, the Department recommended approval. DOC Ex. 420 at 24 (Peirce Direct). The ALJ agrees.

5. Interruptible Service Customers (Issue 52)

680. Xcel proposed to increase the interruptible service discount by approximately 5.1 percent (though most of the interruptible customer categories is closer to 6 percent). Xcel Ex. 105 at 26–27 (Huso Direct). According to Mr. Huso, the interruptible discount has not increased since Xcel's 2010 rate case (Docket No. E002/GR-10-971) while the monthly firm demand charge increased 6.9 percent in the 2012 rate case, and is proposed to increase by 11.7 percent in this case. *Id.* at 27.

681. Xcel has two tiers of Interruptible Service. *Id.* Tier 1 involves a ten year contract with a three year cancellation notice, and a maximum of 150 hours of interruption, whereas Tier 2 involves a five year contract term with six months cancellation notice with a maximum of 80 hours of interruption. *Id.* The Performance Factors represent the percentage of a customer's maximum Controllable Demand that occurs on average in July and August during the peak period (1 pm to 7 pm). *Id.* The interruptible discount increases as the performance factor increases. *Id.* According to Xcel Witness Mr. Huso, the Company uses a market-based approach to set its interruptible rate discounts. *Id.* In other words, the interruptible rate is set at a level the Company believes will attract an "optimal supply" of interruptible load. *Id.*

682. In response to DOC IR No. 307, Xcel stated that it interrupted load twice in 2013 and twice in 2012. DOC Ex. 420 at SLP-8 (Peirce Direct). Each interruption involved only Tier 1 customers, and interrupted a total load of 44,000 to 45,000 MWs per interruption. *Id.* According to Xcel's response to DOC IR No. 320, the Company does not anticipate that increasing its interruptible service discounts would result in a material increase in its interruptible load. *Id.* at SLP-9.

683. The Department recognized that interruptible customers have seen rates increase in the past couple of years without a corresponding increase in the interruptible discount. *Id.* at 26. Therefore, some increase in the interruptible discount may be appropriate. *Id.* Nonetheless, the Department did not recommend a six percent increase in the discount given the limited interruptions these customers have experienced and Xcel's expectation that it has sufficient levels of interruptible load. *Id.* The Department recommended a more moderate three percent increase to Xcel's interruptible discount rates. DOC Ex. 420 at 26 (Peirce Direct). The ALJ agrees with the Department's three percent recommendation to Xcel's interruptible discount rates.

B. Response to Energy CENTS Coalition Witness Roger Colton and the OAG

1. The Department Considered Ability to Pay

684. Energy CENTS Coalition witness Roger Colton testified that the Department did not consider ability to pay in recommending a rate design in this proceeding. ECC Ex. 237 at 1 (Colton Rebuttal). The Department did not agree. DOC Ex. 422 at 4 (Peirce Surrebuttal). Long before rate design is even considered, the issue of affordability was addressed by the DOC financial witnesses in the evaluation of Xcel's proposed revenue requirement and rate of return. *See, e.g.*, DOC Ex. 439 at 12 (Lusti Direct); DOC Ex. 438 at DVL-2 (Lusti Direct Attachments). The most significant benefit to all customers comes from a thorough evaluation of the reasonableness of the requested revenue increase. DOC Ex. 422 at 4 (Peirce Surrebuttal). With respect to rate design, while the Department did not cite specifically to Minn. Stat. § 216B.16, subd. 15 in its Direct Testimony, which directs the Commission to consider ability to pay as a factor in setting utility rates, two aspects of the Department's analysis reflected consideration of ability to pay. *Id.* at 4–5. First, the Department considered rate shock in an effort to avoid excessive rate increases for all customers. *Id.* at 5. Second, the Department analyzed of how the impact of a change in the customer charge would impact customers differently depending on their usage levels. *Id.*

685. The Department agreed with ECC that ability to pay is an important part of rate design. *Id.*

686. The ALJ finds that the Department fully considered ability to pay in evaluating the Company's proposals and in making its own recommendations.

2. Low Income Customers

687. ECC and the OAG both argued that low-income customers are largely low-usage customers, and if low-income customers happen to have high-usage, they are being adequately assisted by energy assistance programs. OAG Ex. 377 at 34 (Nelson Rebuttal); ECC Ex. 238 at 2 (Marshall Rebuttal). In contrast, the Department recognized that low-income customers, as evidenced by the usage data summarized in the table below, exist across all usage levels and will be affected by changes in fixed or usage based rates in different ways depending on their usage levels. DOC Ex. 422 at SLP-S-3 (Peirce Surrebuttal). LIHEAP non-space heating customers are represented, albeit in fairly small numbers, at all usage levels. *Id.*

Table 12: Summary of Customer Usage

Usage Block (monthly kWh)	Total Customer 2013		Residential Non-Space Heating 2013		LIHEAP Non-Space Heating 2013	
	% of Total Meters	% of Total kWh	% of Total Meters	% of Total kWh	% of Total Meters	% of Total kWh
0-300	23.1%	6.0%	23.3%	6.1%	25.0%	7.7%
301-600	30.8%	19.4%	31.0%	19.9%	34.4%	23.5%
601-1,000	25.7%	28.2%	25.7%	28.7%	23.7%	28.3%
1,001-1,500	12.9%	21.9%	12.7%	22.1%	10.9%	20.4%
1,501-2,000	4.3%	10.5%	4.2%	10.4%	3.6%	9.6%
2,001-2,500	1.6%	5.1%	1.5%	4.9%	1.3%	4.4%
2,500+	1.6%	8.9%	1.4%	7.9%	1.2%	6.1%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

As a result, the Department advocated a balanced approach to recovery with a modest increase in fixed and variable charges. *Id.* at 6. By taking this balanced approach, the Department considered the affordability impacts on all customers. *Id.*

3. Residential Customer Charges (Issue 55)

688. The OAG, ECC, CEI, and AARP all recommended no increase in the current $8.00 per month residential customer charge, in contrast to the Department's recommended $0.50 increase per month and the Company's $1.25 increase per month. DOC Ex. 422 at 6 (Peirce Surrebuttal). Xcel witness Mr. Huso maintained that his recommendation to raise monthly customer charges to $9.25 will move customer charges closer to cost without overly burdening lower usage customers. Xcel Ex. 107 at 26 (Huso Rebuttal). Both the OAG and ECC argued that usage patterns for customers receiving LIHEAP assistance are likely biased toward higher usage customers. OAG Ex. 327 at 34 (Nelson Rebuttal); ECC Ex. 238 at 2 (Marshall Rebuttal). Because they believe that the larger population of low-income customers is likely to have lower usage levels than LIHEAP recipients, they favor maintaining the customer charge at current levels, and recovering any increase in the revenue requirement through energy charges. *Id.*

689. The Department did not agree with the OAG and ECC's contention. DOC Ex. 422 at 7 (Peirce Surrebuttal). Information from the most recent LIHEAP Home Energy Notebook prepared by the Administration for Children and Families of the U.S. Department of Health and Human Services[207] indicates that LIHEAP recipients use less electricity (both for heating and all electricity uses) than other low-income households. *Id.* at 7.[208] Although LIHEAP recipients

[207] *http://www.acf.hhs.gov/sites/default/files/ocs/fy2009_liheap_notebook.pdf.*

[208] On this point, the Department noted that in his Direct Testimony, Mr. Colton incorrectly cited the LIHEAP Home Energy Notebook's energy consumption data for all fuels (natural gas, (Footnote Continued on Next Page)

consume more energy overall from all fuel sources than general low income households, they consume slightly less electricity. *Id.*

690. Furthermore, the LIHEAP Home Energy Notebook reviewed the findings of the Census Bureau Survey of Income and Program Participation (SIPP) in order to analyze energy affordability problems for low income households and the findings of the Energy Information Administration's Residential Energy Consumption Survey (RECs), and found that both studies concluded that "low income elderly households are significantly less likely to experience energy affordability problems than other types of low income households." *Id.* at 8, SLP-S-4. This finding suggests that low-income seniors may have lower usage levels, in part due to smaller household size, income, or dwelling size, and they are less likely to have problems paying their bills than other low income households. *Id.* All of this information supports the Department's conclusion that low income customers exist across all usage levels, and therefore, a balanced approach to rate design is reasonable.

691. The ALJ agrees that the Department's analysis and conclusion on low income customers is reasonable.

692. ECC witness Mr. Colton also argued that the Department's analysis of intra-class subsidies is flawed because it compared de-averaged customer charge revenue with average customer charge costs. ECC Ex. 237 at 4 (Colton Rebuttal). Furthermore, Mr. Colton asserted that if the Department had de-averaged the costs, low-income, low-usage customers would likely be imposing fewer costs on current ratepayers. *Id.* Mr. Colton assumed that low-income customers live in older housing with older more depreciated investment to argue that low-income customers likely impose fewer utility infrastructure costs than non-low-income customers. DOC Ex. 422 at 8 (Peirce Surrebuttal). First, his assumption that lower-income customers live in older housing is not supported by his data, which shows customers of all incomes living in all ages of housing. *Id.* at 8–9. In addition, the contention that older housing stock results in lower costs is unsupported. *Id.* at 9. Mr. Colton ignored that older investment may impose more maintenance expenses, and that Xcel makes ongoing investment to replace aging equipment. Xcel Ex. 69 at 30 (Foss Direct). The basic point is that if customer costs are not recovered through a customer charge, any remaining customer costs will be recovered through the energy charge. DOC Ex. 422 at 9 (Peirce Surrebuttal). As a result, customers who use a higher amount of energy than the average residential customer will typically pay for more customer costs than they impose on the system.

693. In addition, Mr. Colton stated that the Department concluded that there "is a customer charge 'subsidy' flowing from higher-use, higher-income customers to lower-use, lower-income customers." ECC Ex. 237 at 8 (Colton Rebuttal). The Department did not reach this conclusion. DOC Ex. 422 at 9 (Peirce Surrebuttal). Because some low-income customers

---

(Footnote Continued from Previous Page)
electricity, fuel oil, kerosene and liquefied petroleum gas) to argue that LIHEAP customers use more electricity, not less than the larger group of low income customers. ECC Ex. 234 at 7, RDC-2 (Colton Direct).

use higher amounts of energy than the average residential customer, the Department is concerned that recovery of customer costs through the energy charge will result in customers with limited means having to pay for more customer costs than they impose on Xcel's system.[209] *Id.* at 9–10.

694. As low-income, higher-usage customers are most affected by the recovery of customer costs through the energy charge, that is precisely why the Department preferred a balanced approach to increasing the customer charge and the energy charge. *Id.* at 10. Because low-income customers exist across all usage levels as shown in the table above (and at DOC Ex. 422 at SLP-S-3 (Peirce Surrebuttal)), the Department recommended that the Commission address the impacts that increases in fixed and variable rates have on different customers by modestly increasing the customer charge. *Id.* The ALJ agrees with this recommendation.

695. In a similar vein, ECC witness Ms. Marshall asserted that the Department's concern for high-usage, low-income customers is misplaced and ignores the availability of existing and proposed assistance programs. ECC Ex. 238 at 4–7 (Marshall Rebuttal). The Department did not agree. DOC Ex. 422 at 11 (Peirce Surrebuttal).

696. LIHEAP recipients are a subset of a broader group of LIHEAP-eligible low-income customers. *Id.* Because the receipt of LIHEAP assistance is generally required to access many of these additional assistance programs, the broader group of LIHEAP-eligible customers would not have access to these assistance programs. *Id.* For instance, at this time the Power On Program is generally available only to LIHEAP recipients, not to the broader group of LIHEAP-eligible customers. *Id.* In addition, funding for low-income assistance programs is not always sufficient to address the needs of all eligible customers. *Id.* Consequently, the Department concluded that not all high-usage, low-income customers will receive assistance from these other assistance programs. *Id.* at 11–12. The ALJ agrees with the Department's conclusion.

697. Ms. Marshall focused her concern on rate design measures that will most benefit low-income, low-usage customers, but does not address expanding outreach programs so that more customers could benefit from LIHEAP assistance. *Id.* at 12. Such an approach would target benefits to customers who need the assistance, whereas the approach of keeping customer charges low would require all Xcel customers, including those who have low incomes, to pay higher energy rates, and higher energy bills, to pay for a portion of the customer costs of all low-usage customers, some of whom are not low-income. DOC Ex. 422 at 12 (Peirce Surrebuttal). This is why a balanced approached to setting rates is reasonable. *Id.*

698. Finally, Ms. Marshall proposed a new CIP program geared toward rental properties with one to four units.[210] ECC Ex. 235 at 27–31 (Marshall Direct). To the extent the

---

[209] Attachment SLP-S-3 summarize Table 5 and usage levels for LIHEAP non-space heating customers for 2013, and clearly demonstrates that some low-income customers have high usage levels, and they will be hurt by the recovery of customer costs through the energy charge. DOC Ex. 422 at SLP-S-3 (Peirce Surrebuttal).

[210] Department Witness Bill Grant responded to Ms. Marshall's proposal. DOC Ex. 416 (Grant Rebuttal).

needs of rental properties with 1-4 units can be addressed by existing CIP programs or modifications to those programs, those programs should do so in order to support administrative efficiency. DOC Ex. 422 at 13 (Peirce Surrebuttal). If a need is found to develop an additional CIP program aimed specifically at renters in one-to-four unit dwellings, the Department recommended that the Commission direct Xcel (and other interested parties) to work with Department of Commerce CIP staff in developing such a program, as well as appropriate participation and energy-savings goals for the program. *Id.* The ALJ agrees.

C. Inclining Block Rate (Issue 80)

1. Initial Rebuttal Inclining Block Rate Recommendation

699. In general, an IBR structure increases the energy charge over successive blocks of energy usage. DOC Ex. 416 at 1 (Grant Rebuttal). For example, in a two-block IBR structure with monthly usage of 300 kWh as the dividing point, customers using up to 300 kWh would pay one rate per kWh for that usage. *Id.* at 1–2. When a customer uses over 300 kWh, those customers would pay the same rate for the first 300 kWh, but would pay a higher rate for the incremental amount of usage over 300 kWh. *Id.* at 2.

700. CEI proposed a four-block IBR structure for Residential customers on the Standard Residential Tariff. CEI Ex. 280 at 17–25 (Chernick Direct). The proposed IBR varies by season, consistent with Xcel's current seasonal rate structure. *Id.* CEI proposed to exclude Residential Space-Heating customers during the winter months and recommended no increase to the customer charge. *Id.* at 18.

701. The Department initially recommended studying CEI's proposed IBR and determining what its benefits would be. DOC Ex. 416 at 3 (Grant Rebuttal). In that regard, to effectively communicate the IBR proposal to Xcel's customers, the Department recommended that the Commission require Xcel to begin collecting data about the impact of an inclining block rate (IBR) structure on customer bills by providing parallel billing for one year, which would teach customers the rates they would pay under an IBR structure. *Id.* at 6. The information would be used by the Department to identify all impacts from billing implementation of IBR. *Id.* Based on the analysis, the Department will make a recommendation to the Commission on whether to adopt CEI's IBR proposal, and if so, whether the rate structure should be adopted as proposed, or with modifications. *Id.*

2. The Parties' IBR Agreement

702. At the evidentiary hearing, Xcel, CEI, Energy CENTS, and the Suburban Rate Authority entered into an agreement regarding a proposed IBR structure (Stipulation). *See* Xcel Ex. 135 (Stipulation on Inverted Block Rate). The Stipulation urges the Commission to open a new docket and require Xcel to file a proposal for an IBR structure in the form of a compliance filing within 120 days of the Commission's decision in this matter. *Id.* The purpose of the new docket is to allow for further development of a rate structure and give all parties additional time to discuss related issues. *Id.*

703. The ALJ finds the Stipulation to be reasonable and recommends that the Commission incorporate the Stipulation into its final decision.

D. A New CIP Program for Low Income Renters (Issue 81)

704. The Department generally agreed with Energy CENTS witness Ms. Marshall that a CIP program targeted at one-to-four unit dwellings is needed. DOC Ex. 416 at 7 (Grant Rebuttal). To the extent that existing programs can be used to reach this particular population of customers, the Department recommended using them for efficiency reasons. *Id.* The Department's understanding is that Xcel's existing Home Energy Savings and Low-income Home Energy Squad are both available to renters, so it is not clear whether these programs are unable to target the renters in question, or if there are program changes that could better enable the existing programs to reach low-income renters in smaller unit dwellings. *Id.*

705. If a need is found to develop an additional CIP program aimed specifically at renters in one-to-four unit dwellings, the Department recommended that the Commission direct Xcel to work with Department of Commerce CIP staff in developing such a program, as well as appropriate participation and energy-savings goals for the program. *Id.* These low-income recommendations should be pursued whether or not the Commission ultimately orders IBR rates for Xcel customers. *Id.*

706. The ALJ agrees with the Department's recommendations.

Dated: October 14, 2014

Respectfully Submitted,

s/ Linda S. Jensen

Linda S. Jensen
Assistant Attorney General
Attorney Reg. No. 0189030

s/ Peter E. Madsen

Peter E. Madsen
Assistant Attorney General
Attorney Reg. No. 0392339

s/ **Julia E. Anderson**
Julia E. Anderson
Assistant Attorney General
Atty. Reg. No. 0138721

445 Minnesota Street, Suite 1800
St. Paul, MN 55101-2131
Attorneys for the Minnesota Department of Commerce