

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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Chair
Commissioner
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In the Matter of Otter Tail Power Company's
2013 Demand-Side Management Financial
Incentives and Annual Filing to Update the
CIP Rider

ISSUE DATE: September 26, 2014

DOCKET NO. E-017/M-14-201

ORDER APPROVING FINANCIAL
INCENTIVE, SETTING CONSERVATION
COST RECOVERY ADJUSTMENT,
REDUCING CARRYING CHARGES,
AND VARYING RULES

PROCEDURAL HISTORY

On April 1, 2014, Otter Tail Power Company filed its annual petition for rate recovery of costs incurred and financial incentives earned in connection with energy-conservation-improvement programs conducted during the previous calendar year. The petition asked permission to take the following actions:

1. Book to the Company's Conservation Improvement Program (CIP) tracker account some \$4,026,600 in demand-side management financial incentives—cash rewards for achieving energy savings at specified levels—earned during 2013 under the financial incentive mechanism adopted by the Commission.¹
2. Increase its Conservation Cost Recovery Adjustment (CCRA), the monthly billing surcharge used to recover amounts booked to the CIP tracker account, from \$0.00175 per kWh to \$0.00209 per kWh.²
3. Adjust its 2013 year-end CIP tracker balance to \$4,835,558, to reflect its 2013 demand-side management financial incentive and its under-recovery of CIP costs in 2013.

¹ *In the Matter of Commission Review of Utility Performance Incentives for Energy Conservation Pursuant to Minn. Stat. § 216B.241, subd. 2c*, Docket No. E,G-999/CI-08-133, Order Establishing Utility Performance Incentives for Energy Conservation (January 27, 2010) and Order Adopting Modifications to Shared Savings Demand Side Management Financial Incentive (December 20, 2012).

² The Company later changed its request to \$0.00263 per kWh. See Otter Tail reply comments of May 16, 2014 and supplemental comments of June 12, 2014.

4. Continue its practice of giving customers a one-time notice of the new CCRA amount and combining the CCRA with other costs recovered through the fuel clause, using a single line item labelled “Resource Adjustment” on customer bills. This practice requires variances to Minn. R. 7820.3500 (K) and Minn. R. 7825.2600, which set calculation and disclosure requirements for the fuel clause.

From May 1 through July 8, 2014, the Minnesota Department of Commerce (the Department), the Minnesota Chamber of Commerce (the Chamber), and the Company filed comments on the petition, as well as alternative rate-recovery proposals.

All parties agreed that the Company had properly calculated its demand-side management financial incentive and CIP tracker account balances; they disagreed on the details of rate recovery.

On September 11, 2014, the case came before the Commission.

FINDINGS AND CONCLUSIONS

I. Summary of the Issues

All commenting parties agreed that the Company had properly calculated and accounted for its CIP expenses, demand-side management financial incentive, previously authorized carrying charges, 2013 rate recoveries, and beginning and ending CIP balances, as set forth below:

Description	Time Period	Amount
Beginning Balance	December 31, 2012	\$ 3,572,621
CIP Expenses	January 1 through December 31, 2013	\$ 5,253,935
DSM Financial Incentive	Approved in 2013 for 2012	\$ 2,681,575
Carrying Charges	January 1 through December 31, 2013	\$ 237,859
Combined Base Rate and CCRA Recovery	January 1 through December 31, 2013	(\$ 6,910,431)
Ending Balance	December 31, 2013	\$ 4,835,558

The Commission has examined the record, concurs with the parties that these calculations are correct, and will approve them.

The parties disagreed, however, on how quickly to permit rate recovery of the \$4,835,558 CIP tracker account balance—i.e., they disagreed on how high to set the CCRA—and on whether to continue permitting the Company to assess carrying charges on the CIP tracker balance. Those issues are addressed below.

II. CCRA Level/Rate Recovery Period

A. Positions of the Parties

The Company originally proposed a CCRA of \$0.00209 per kWh, recognizing that setting the surcharge at that level would mean carrying unrecovered CIP costs for more than the normal one-year term, but considering the delay necessary to moderate the rate impact of significant increases in CIP costs and earned financial incentives. After exchanging comments with the Department, the Company proposed a slightly higher CCRA of \$0.00263, to speed recovery of its CIP tracker account balance while still moderating rate increases.

The Department originally proposed a CCRA of \$0.00350 per kWh, to more closely match costs and revenues and to avoid accumulating high carrying charges in the CIP tracker account. Ultimately, however, the Department concurred in the Company's alternative proposal of \$0.00263 per kWh.

The Chamber advocated adopting the Company's originally proposed CCRA of \$0.00209, arguing that any larger increase in the CCRA—coupled with expected increases in surcharges for new transmission facilities and possible increases in surcharges for environmental amelioration—would be excessive and could result in rate shock.

B. Commission Action

The Commission concurs with the Department and the Company that setting the CCRA at \$0.00263 strikes the proper balance between the competing goals of moderating the rate impact of these fluctuating costs and ensuring their timely and efficient recovery.

The purpose of having a CIP tracker account and resetting the CCRA annually is to permit the Commission to maintain, as far as possible, equilibrium between CIP costs (including earned financial incentives) and CIP revenues. Equilibrium is optimal for ratemaking purposes—it promotes clarity and fairness by matching the intervals when costs are incurred with the intervals when costs are recovered. It avoids burdening ratepayers with substantial carrying charges, which in the past have been set at the Company's authorized rate of return. And it serves the statutory goal of encouraging conservation and energy efficiency by promptly rewarding utility achievements in these areas.

At the same time, however, the Commission does set CCRA levels that will not zero out tracker balances within a year when necessary, mainly in cases that would otherwise result in excessive rate increases. The Commission took that step when it set the Company's CCRA in its last annual CIP tracker-account filing,³ and it will take the same step in this case. In both cases, rate stability and affordability justify extending cost recovery over a longer time period.

³ *In the Matter of Otter Tail Power Company's 2012 Demand Side Management Financial Incentive Project and Annual Filing to Update the CIP Rider*, Docket No. E-017/M-13-171, order dated October 15, 2013.

The Chamber and the Department pointed out that Otter Tail customers face significant rate increases at whatever level the CCRA is set, since costs passed through the Transmission Cost Recovery Rider and the Environmental Cost Recovery Rider have risen more substantially than CIP costs and will significantly increase rates.⁴ As the following three tables demonstrate, however, the level of the CCRA will still have a substantial impact on customer rates and must be examined in that light.

Customer Bill Impact Resulting from Approved or Proposed Changes in CCRA, TCR and ECRR Since January 1, 2014

Assumes CCRA = \$0.0035/kWh, October – May Rates

Class	Nominal Increase in Avg. Monthly Bill	Percentage Increase in Avg. Monthly Bill
Residential	\$ 7.02	8.8%
Small Commercial	\$ 21.21	9.4%
Large Commercial	\$ 972.21	7.9%

Customer Bill Impact Resulting from Approved or Proposed Changes in CCRA, TCR and ECRR Since January 1, 2014

Assumes CCRA @ \$0.00209/kWh, October – May Rates

Class	Nominal Increase in Avg. Monthly Bill	Percentage Increase in Avg. Monthly Bill
Residential	\$ 5.85	7.3%
Small Commercial	\$ 17.49	7.8%
Large Commercial	\$ 674.65	5.5%

Customer Bill Impact Resulting from Approved or Proposed Changes in CCRA, TCR and ECRR Since January 1, 2014

Assumes CCRA @ \$0.00263/kWh, October – May Rates

Class	Nominal Increase in Avg. Monthly Bill	Percentage Increase in Avg. Monthly Bill
Residential	\$ 6.30	7.9%
Small Commercial	\$ 18.91	8.4%
Large Commercial	\$ 788.61	6.4%

⁴ Supplemental Comments of the Department of Commerce, pages 6-8.

The Commission concurs with the Department and the Company that the mid-level CCRA increase—\$0.00263 per kWh—best balances the need to ameliorate rate increases with the need to move steadily toward full cost recovery and will set the CCRA at that level.

III. Carrying Charges

A. Background

Otter Tail has been crediting/debiting its CIP tracker account with carrying charges, calculated at its authorized rate of return, since the Commission first authorized that action in 1992.⁵ At that point, demand-side-management financial incentives were small and experimental. As the Department pointed out, the financial incentive awarded the Company in 1992 was \$23,714; the financial incentive awarded in this 2013 docket is \$4,026,000.⁶

Further, since 1992, the number of rate riders has grown, as the Legislature has enacted new energy policy initiatives funded by surcharges assessed between rate-case filing intervals. As rate riders have proliferated, so have rate recovery issues, including issues surrounding carrying charges. These concerns led the Commission, in an order dated April 17, 2013, to require Otter Tail to affirmatively justify any future request for carrying charges on any rider tracker-account balance.⁷

The next request for carrying charges came in the Company's 2013 filing to update its transmission-cost-recovery rider. The justification offered by the Company was that those charges were fair and reasonable compensation for the time value of money, protected the Company and ratepayers equally, and had been credited to ratepayers more than once in the past. The Commission disallowed carrying charges prospectively, explaining as follows:

Having considered the issue, the Commission will not allow the Company to add a carrying charge to the tracker balance for its transmission cost recovery rider and its renewable resource cost recovery rider. While the Company's observation about symmetrical treatment is true, it does not go to the heart of the issue. As discussed above, the TCR rider and the renewable resource cost recovery rider are extraordinary cost-recovery mechanisms adopted to expedite the construction of critically needed infrastructure.

⁵ *In the Matter of the Proposal of Otter Tail Power Company for a Demand-Side Management Financial Incentive*, Docket No. E-017/M-91-457, Order Establishing Demand Side Management Incentive Pilot Project and Requiring Further Filings (March 12, 1992).

⁶ Comments of the Department of Commerce filed July 8, 2014.

⁷ *In the Matter of Otter Tail Power Company's Request for Approval of its 2012 Renewable Resources Cost Recovery Adjustment Factor*, Docket No. E-017/M-12-708, Order Approving Request to Reduce Rider Recovery Factor, Approving Refund, and Setting Requirements for Future Rider Filings (April 17, 2013).

They offer unique advantages over traditional ratemaking treatment. For example, they permit cost recovery—including recovery of the authorized rate of return—to begin with construction, instead of when the facilities are placed into service. And both riders permit cost recovery to begin before the facilities' costs have been fully scrutinized in a rate case. The additional advantages of a carrying charge are therefore unnecessary either to ensure fairness or to act as an incentive.⁸

B. Positions of the Parties

The Company argued that the Commission should grant carrying charges on the CIP-tracker-account balance at its authorized rate of return. The Company pointed out that this was consistent with past Commission practice, not only as to Otter Tail but as to other Minnesota utilities. And the Company argued that its authorized rate of return was a reasonable level of compensation for the time value of money whose collection was being deferred.

The Chamber urged the Commission to impose no carrying charges on the tracker-account balance, arguing that the Company incurred no risk in collecting the financial incentives and that, in any case, it was equitable for the rate-recovery period to exceed a year, since the benefits of the energy savings for which those incentives were awarded accrued over a period exceeding a year. In the alternative, the Chamber recommended using the Company's authorized short-term cost of debt—instead of its authorized overall rate of return—as the carrying-charge rate.

The Department concurred with the Chamber that the Commission should either reject carrying charges altogether or set the interest rate at the Company's authorized rate for short-term debt. The agency argued there was much less reason to assess carrying charges on unrecovered cash incentives than on unrecovered expenditures and that the CCRA surcharges were generally sufficient to recover the Company's actual CIP expenditures.

The Department also argued that the factual basis for the 1992 decision to grant carrying charges at the authorized rate of return—that the financial incentives were small and the incentive program new—no longer applied. And the Department argued that the cost of short-term debt was a better match than the Company's authorized rate of return for the time-value of the financial incentives whose recovery was delayed.

C. Commission Action

The Commission concurs with the Chamber and the Department that it is no longer appropriate to grant the Company carrying charges on unrecovered CIP costs at its authorized rate of return. The Commission will, however, grant carrying charges at the Company's short-term cost of debt, as explained below.

⁸ *In the Matter of Otter Tail Power Company's Request for Approval of a Transmission Cost Recovery Rider Including the Proposed Transmission Factor for the Recovery Period from May 2, 2013 to April 30, 2014*, Docket No. E-017/M-13-103, ORDER CAPPING COSTS, DENYING RIDER RECOVERY OF EXCESS COSTS, AND REQUIRING INCLUSION OF ALL MISO SCHEDULE 26 COSTS AND REVENUES IN TCR RIDER (March 10, 2014) at 9.

First, as the Department and the Chamber note—and as the Commission explained in the March 10 order quoted above—rate riders are extraordinary cost-recovery mechanisms offering favorable ratemaking treatment to advance specific public-policy objectives. They permit prompt recovery of actual costs outside the normal test-year framework and between normal rate-case filing intervals. And, while rider costs are reviewed for accuracy and reasonableness before rate recovery begins, they do not receive the in-depth scrutiny conducted in a rate case. Granting or denying carrying charges on rate-rider tracker-account balances is therefore a decision that must be made case by case, based on the facts at hand.

Here, the Commission concurs with the Chamber and the Department that granting carrying charges at Otter Tail's authorized rate of return would be excessive. While the CIP financial incentives making up the bulk of the CIP tracker account serve an important public-policy purpose, they are not the kind of costs—out of pocket costs—for which rate-of-return treatment can be most readily justified.

Further, the factual context that led to setting carrying charges at the overall rate of return no longer applies. As the Department pointed out, in 1992—and for years thereafter—demand-side management financial incentives were small, the financial-incentive program was new, and it was important to use whatever tools were at hand to encourage its success. The incentives are now sizeable, the program is well established, and Otter Tail itself stated at hearing that reducing or eliminating carrying charges would not affect its conservation commitment or efforts, just its approach to rate amelioration.

Still, the Commission is concerned about perceived reductions in the value of financial incentives when recovery is delayed and about ensuring fair treatment to utilities, which factor financial incentives into their financial decision-making processes. Further, the CCRA set in this case will spread tracker-account recovery over two years instead of one; some recognition of that additional twelve months is warranted.

While there is no exact match between this additional twelve-month recovery period and a standard interest rate, the Commission concurs with the Department and the Chamber that the authorized cost of short-term debt is the closest match contained in the record. The twelve-month term typical of short-term debt corresponds to the twelve-month period CIP costs are typically carried in the tracker account. And, while the additional twelve months of recovery necessitated by the moderated CCRA level is anomalous, the short-term debt rate is still more consistent with the public interest than the overall rate of return, given the nature of these costs—cash financial incentives—and the relatively short term—two years—within which they will be recovered.

For all these reasons, the Commission will grant carrying charges on the CIP tracker account balance at the Company's authorized cost of short-term debt.

IV. Rule Variances

A. Introduction

Like other Minnesota utilities, Otter Tail gives customers notice when it changes the amount of the CCRA and then combines the CCRA with other costs recovered through the fuel clause. Instead of identifying the CCRA separately on customers' bills, the Company combines it with other

fuel-clause costs in a single line item labelled “Resource Adjustment.” This practice requires variances to Minn. R. 7820.3500 (K), which requires that customer bills separately itemize the fuel clause, and Minn. R. 7825.2600, which sets calculation and disclosure requirements for fuel clause components.

The Company has been granted variances to these rules since 1995, when it first began recovering CIP costs through a rate rider. It states that these billing practices have avoided customer confusion without compromising the full disclosure anticipated by the customer billing rules, both because of its annual CIP customer notice and because of the comprehensive CIP information on its website. The Company also stated that its current customer-billing software will not permit it to separately itemize the CORA without substantial expense.

No one opposed granting the variances, and the Department supported granting them.

B. Commission Action

Under Minn. R. 7829.3200, the Commission is authorized to vary any of its rules upon making the following findings:

1. Enforcing the rule would impose an excessive burden upon the applicant or others affected by the rule;
2. Granting the variance would not adversely affect the public interest; and
3. Granting the variance would not conflict with any standards imposed by law.

The Commission will vary Minn. R. 7820.3500 (K) and Minn. R. 7825.2600, making the following findings:

1. Enforcing the separate itemization requirements of the rules would impose an excessive burden on the Company, by forcing it to incur substantial unnecessary expense, and on its ratepayers, by forcing them to adjust to an unfamiliar billing format, without meaningful benefit.
2. Varying the rules would not adversely affect the public interest, since the purpose of the disclosure requirements would be served by the annual customer notice provided by the Company and by the comprehensive CIP information on its website.
3. Varying the rules would not conflict with any standards imposed by law, since the itemization and disclosure requirements are set by rule, not statute, and may therefore be varied under Minn. R. 7829.3200.

ORDER

1. The Commission approves Otter Tail’s 2013 CIP tracker account balance at set forth above, including its 2013 financial incentive of \$4,026,600.

2. The Commission grants Otter Tail's request to record its 2013 financial incentive in a lump sum fashion following the issuance of this order.
3. The Commission sets the Company's Conservation Cost Recovery Adjustment at \$0.00263 per kWh.
4. As of the date of this order, the Commission modifies the carrying charge on the CIP tracker-account balance to the short-term cost of debt set in the Company's last rate case, E-017/GR-10-239.
5. The Commission varies Minn. R. 7820.3500 (K) and Minn. R. 7825.2600 to permit Otter Tail to continue giving customers a one-time notice of the new Conservation Cost Recovery Adjustment and combining the Conservation Cost Recovery Adjustment with other costs recovered through the fuel clause, using a single line item labelled "Resource Adjustment" on customer bills.
6. This order shall become effective immediately.

BY ORDER OF THE COMMISSION



Burl W. Haar
Executive Secretary



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