



414 Nicollet Mall
Minneapolis, Minnesota 55401

February 12, 2014

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

—Via Electronic Filing—

RE: REPLY COMMENTS
REGULATORY TREATMENT OF NET OPERATING LOSS
DOCKET NO. E002/GR-10-971

Dear Dr. Haar:

Northern States Power Company, doing business as Xcel Energy, submits to the Minnesota Public Utilities Commission this Reply to the July 31, 2013 Comments of the Minnesota Department of Commerce, Department of Energy Resources.

We submit this Reply to clarify the record regarding our use of our actual Rate of Return to calculate the tax utilization, and ultimately the associated customer refund, and to indicate that it is our understanding that with this clarification, the Company and Department are in agreement regarding the two issues raised in the Department's Comments, as follows:

- *Rate Design of Customer Refund* – We agree with the Department's recommended assignment of the refund amount to class, which is consistent with how taxes were handled in our most recent rate case, and which better matches costs and revenues; and
- *Rate of Return (ROR) Used to Calculate Refund* – The Department now agrees that use of the Company's actual ROR, as reported in our Jurisdictional Annual Report, better represents the Company's actual debt interest tax deduction, is consistent with the Settlement, and results in only a slight timing difference on when dollars are refunded to customers.

We have electronically filed this document with the Minnesota Public Utilities Commission, and copies have been served on the parties on the attached service list.

Please contact Jeff Robinson at (612) 330-5912 or jeffrey.c.robinson@xcelenergy.com or me at (612) 215-4593 or christopher.b.clark@xcelenergy.com if you have any questions regarding this matter.

Sincerely,

/s/

CHRISTOPHER B. CLARK
REGIONAL VICE PRESIDENT
RATES AND REGULATORY AFFAIRS

Enclosures
cc: Service List

STATE OF MINNESOTA
BEFORE THE
MINNESOTA PUBLIC UTILITIES COMMISSION

Beverly Jones Heydinger	Chair
David Boyd	Commissioner
Nancy Lange	Commissioner
J. Dennis O'Brien	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

DOCKET NO. E002/GR-10-971

REPLY COMMENTS

INTRODUCTION

Northern States Power Company, doing business as Xcel Energy, submits to the Minnesota Public Utilities Commission this Reply to the July 31, 2013 Comments of the Minnesota Department of Commerce, Department of Energy Resources.

Since the Commission approved the Tax Normalization and Allowance for Net Operating Losses Agreement (NOL Agreement) in its May 14, 2012 FINDINGS OF FACT, CONCLUSIONS, AND ORDER, we have submitted two annual compliance filings. In both of these *Deferred Tax Asset (DTA) balances associated with the regulatory treatment of Net Operating Losses* filings (Annual Reports), we used the actual results from our May 1 Jurisdictional Annual Reports, which we believe is consistent with the NOL Agreement.

In response to the 2012 Annual Report that we filed May 31, 2013, the Department submitted Comments on July 31, 2013. We appreciate the Department's review of our May 31, 2013 Annual Report. In Comments, the Department: (1) recommended a different methodology to calculate the customer refund amounts; and (2) disagreed with our use of our actual Rate of Return in calculating our DTA utilization. Because we continued to believe that our use of our actual Rate of Return was accurate and consistent with the NOL Agreement, we initiated a meeting with the Department to discuss the issue.

We met with the Department on February 6, 2014 to share the information contained in this Reply, which we believed would clarify the issue. We note that the Company

and the Department are now in agreement on the two issues raised by the Department in their July 31, 2013 Comments, as follows:

- *Rate Design of Customer Refund* – We agree with the Department’s recommended assignment of the refund amount to class, which is consistent with how taxes were handled in our most recent rate case, and which better matches costs and revenues; and
- *Rate of Return (ROR) Used to Calculate Refund* – The Department now agrees that use of the Company’s actual ROR, as reported in our Jurisdictional Annual Report, better represents the Company’s actual debt interest tax deduction, is consistent with the NOL Agreement, and results in only a slight timing difference on when dollars are refunded to customers.

We therefore respectfully request that the Commission:

- Accept the supplemental information contained in this Reply, and clarify that the Company should use its actual ROR from its May 1 Jurisdictional Annual Reports in preparing its Annual NOL Reports;
- Approve our proposed customer refund of \$3.989 million, which is based on our 2012 actual results from our May 1, 2013 Jurisdictional Annual Report;
- Require the refunds be provided to customers in accordance with our proposed Refund Plan, but using the rate base allocation method of assigning refund amounts to customer classes, as recommended by the Department; and
- Require the Company to include with its future Annual Reports, the formulas it uses in its Attachment containing the supporting calculations, as also recommended by the Department.¹

In the remainder of this Reply, we provide the information that we shared with the Department at the February 6 meeting, which we believe will also clarify and supplement the record regarding our use of our actual Rate of Return to calculate the tax utilization, and ultimately the associated customer refund.

REPLY COMMENTS

We believe it is important to clarify our understanding of the NOL Agreement, and why it is important to use all actual results in the calculations related to our DTA balances and NOL utilization. In summary, our Rate of Return is our weighted *cost of capital*, comprised of the weighted *cost of debt* and the weighted *cost of equity*. The

¹ Consistent with the Company’s Attachment 1 to DOC Information Request No. 1197.

weighted cost of debt is an essential component of truing-up the DTA for actual results.

In 2012, we were able to achieve a lower cost of debt compared to the weighted cost included in our last authorized ROR. This reduction in debt interest expense reduced the level of tax deductions, allowing the Company to utilize a larger portion of the tax depreciation deductions carried forward from prior periods to offset the reduced level of debt interest expense deduction. A larger utilization creates a larger refund to customers. Specifically, our lower actual ROR that is the result of our lower cost of debt in 2012 *increases* the NOL refund to customers by approximately \$465,000.

We believe the NOL Agreement contemplated that we would apply all actual results to the DTA and NOL calculations to calculate the amount due to customers. Using only a portion, or subset, of our actual results in these calculations would result in an inaccurate representation of the Company's DTA balance and NOL utilization – and ultimately, an inaccurate refund/return of the revenue requirements that result from this utilization. Therefore, the use of selected actual amounts as suggested by the Department in Comments would not accurately reflect the Company's utilization of previously carried forward deductions, as the debt interest deduction would be based on previously established amounts for use in a projected test year rate case, rather than actual interest deductions.

As noted above, the Department recognized the timing issue this mismatch would create, and now agrees that we should use our actual ROR from our May 1 Jurisdictional Annual Report.

A. The NOL Agreement

The NOL Agreement states that the Company will “refund to customers the revenue requirements associated with the consumption of the DTA that is estimated to return approximately \$60 million in aggregate revenue requirements to customers” over the 2012-2015 period.² It goes on to state that:

The amount and timing of the return will be trued up to **actual results**; any change in the total amount will be subject to Commission approval. [Emphasis added]

We believe, and have applied as such, that the Agreement contemplates that we use *all* actual results in our calculations. The ROR, which the Company and the Department

² We note that the current estimate is approximately \$75 million over the 2013-2017 period, as reported in our May 31, 2013 Annual Report.

now agree should be our *actual* ROR, is an essential component to calculating the Company's actual DTA, and therefore, our actual NOL utilization.

If we were to use our last approved ROR instead of our actual ROR, the level of interest expense used to determine taxable income would not reflect actual interest costs and as a result, the level of deductions carried forward from previous years that can be consumed in the current period would be misstated.

We discuss the impact of using our actual 2012 ROR below.

B. Impact of Using Actual 2012 Rate of Return

The Company's last authorized cost of capital was 8.32 percent. Our actual 2012 cost of capital as reported in our 2012 Jurisdictional Annual Report was 8.08 percent. The primary difference between these two amounts is due to the Company's ability to reduce its weighted cost of debt on an actual basis. The weighted cost components for each of these two capital structures are shown on Attachment A to this Reply.

The reduced debt costs, which are tax deductible, resulted in a higher level of previously deferred deductions that could be utilized. As calculated in the Cost of Service Study, the debt interest expense using the 2012 last authorized cost of capital was \$174.8 million. This amount as reported in our 2012 Jurisdictional Annual Report was \$158.9 million, based on the actual 2012 cost of capital. Because of the reduced interest expense realized on an actual basis, we were able to utilize an additional \$15.9 million in previously deferred deductions.

As a result of this additional utilization, deferred tax expense was increased by the composite tax rate times this amount. This caused the ending balance in accumulated deferred taxes to increase by the amount of deferred tax expense and average rate base to decrease by 50 percent of the deferred tax expense. Ultimately, the reduction in rate base caused by this additional utilization caused a decrease in revenue requirements when compared to the same calculations using the last authorized cost of capital.

As illustrated on Attachment B to this Reply, if the Company were required to use its last authorized weighted cost of debt in this analysis in place of actual costs, fewer deductions could be utilized from prior periods for purposes of this calculation, resulting in a reduction to the Company's refund liability of \$465,000 – and the customer refund would no longer be based on the Company's actual results.

CONCLUSION

Xcel Energy respectfully requests that the Commission:

- Accept the supplemental information contained in this Reply, and clarify that the Company should use its actual ROR from its May 1 Jurisdictional Annual Reports in preparing its Annual NOL Reports;
- Approve our proposed customer refund of \$3.989 million, which is based on our 2012 actual results from our May 1, 2013 Jurisdictional Annual Report;
- Require the refunds be provided to customers in accordance with our proposed Refund Plan, but using the rate base allocation method of assigning refund amounts to customer classes, as recommended by the Department; and
- Require the Company to include with its future Annual Reports, the formulas it uses in its Attachment containing the supporting calculations, as also recommended by the Department.

Dated: February 12, 2014

Northern States Power Company

Respectfully submitted by:

/s/

CHRISTOPHER B. CLARK
REGIONAL VICE PRESIDENT
RATES AND REGULATORY AFFAIRS

2012 Actual Capital Structure

	<u>Rate</u>	<u>Ratio</u>	<u>Weighted Cost</u>
Long Term Debt	5.7072%	45.3838%	2.5900%
Short Term Debt	0.9830%	1.8365%	0.0200%
Preferred Stock	0.0000%	0.0000%	0.0000%
Common Equity	10.3700%	52.7797%	5.4700%
Required Rate of Return			8.0800%

2012 Last Authorized Capital Structure

	<u>Rate</u>	<u>Ratio</u>	<u>Weighted Cost</u>
Long Term Debt	6.0936%	46.8780%	2.8600%
Short Term Debt	2.4326%	0.5604%	0.0100%
Preferred Stock	0.0000%	0.0000%	0.0000%
Common Equity	10.3700%	52.5616%	5.4500%
Required Rate of Return			8.3200%

**Net Operating Loss (NOL) Related Deferred Tax Asset Balance Reporting
Balance Build-Up, Forecast Utilization and Annual Revenue Requirement Reduction**

Dollars in thousands

2012 Jurisdictional Annual Report

EOY Unused Deduction Balance
Tax Effect of Deduction Balance
EOY Unused Credit Balance
Total (EOY Rate Base)

Balance	2012 Annual Activity				Balance
2011 Year End Ann Rpt	2012 Sec 172(f) Utilization	2012 Filing of 2011 Return	2012 Annual Amount	Total Annual Activity	2012 An Rpt Balance
588,687	(73,694)	(29,132)	(70,803)	(173,629)	415,058
240,222	(30,051)	(11,880)	(28,959)	(70,890)	169,332
<u>27,036</u>	<u>0</u>	<u>0</u>	<u>18,482</u>	<u>18,482</u>	<u>45,518</u>
267,258	(30,051)	(11,880)	(10,477)	(52,408)	214,850

Capital Structure

Weighted Cost of Debt	2.61%
Weighted Cost of Equity	<u>5.47%</u>
Composite Cost of Capital	8.08%
Current Tax Rate	41.37%
RR Conversion Factor	1.70561146

NOL/DTA Return to Customer Amount	2012 CB	2012 Other
NOL Deferred Tax Asset Utilization	30,051	22,357
Impact on Average Rate Base	(15,026)	(11,178)
Required Operating Income	(1,214)	(903)
Deferred Tax	-	22,357
Debt Return	(392)	(292)
Current Tax	162	(22,740)
Operating Income	(162)	384
Operating Income Deficiency	(1,052)	(1,287)
Total Annual Revenue Requirement Reduction	(1,794)	(2,195)
	2012 Total	(3,989)

2012 @ Last Authorized COC

EOY Unused Deduction Balance
Tax Effect of Deduction Balance
EOY Unused Credit Balance
Total (EOY Rate Base)

Balance	2012 Annual Activity				Balance
2011 Year End Ann Rpt	2012 Sec 172(f) Utilization	2012 Filing of 2011 Return	2012 Annual Amount	Total Annual Activity	2012 An Rpt Balance
588,687	(73,694)	(29,132)	(54,881)	(157,707)	430,980
240,222	(30,051)	(11,880)	(22,447)	(64,378)	175,844
<u>27,036</u>	<u>0</u>	<u>0</u>	<u>18,482</u>	<u>18,482</u>	<u>45,518</u>
267,258	(30,051)	(11,880)	(3,965)	(45,896)	221,362

Capital Structure (Last Authorized)

Weighted Cost of Debt	2.87%
Weighted Cost of Equity	<u>5.45%</u>
Composite Cost of Capital	8.32%
Current Tax Rate	41.37%
RR Conversion Factor	1.70561146

NOL/DTA Return to Customer Amount	2012 CB	2012 Other
NOL Deferred Tax Asset Utilization	30,051	15,845
Impact on Average Rate Base	(15,026)	(7,922)
Required Operating Income	(1,250)	(659)
Deferred Tax	-	15,845
Debt Return	(431)	(227)
Current Tax	178	(16,180)
Operating Income	(178)	335
Operating Income Deficiency	(1,072)	(995)
Total Annual Revenue Requirement Reduction	(1,828)	(1,696)
	2012 Total	(3,524)
	Net Change in Refund	(465)

CERTIFICATE OF SERVICE

I, SaGonna Thompson, hereby certify that I have this day served copies of the foregoing document or a summary thereof on the attached lists of persons:

xx by depositing a true and correct copy or summary thereof, properly enveloped with postage paid, in the United States Mail at Minneapolis, Minnesota; or

xx via electronic filing

Docket No. E002/GR-10-971

Dated this 12th day of February 2014

/s/

SaGonna Thompson

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