

Staff Briefing Papers

Meeting Date	December 19, 2019	Agenda Item 3*
Company	Otter Tail Power Company	
Docket No.	E-017/M-19-411	
	In the Matter of Otter Tail Power Company's Petition for Approval of the Annual Update to its Renewable Resource Cost Recovery Rider Rate, Rate Schedule 13.04	
Issues	Should the Commission approve Otter Tail Power's annual update of its Renewable Resource Cost Recovery Rider rate under Otter Tail Power's Rate Schedule 13.04?	
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Relevant Documents

Date

Docket No. E-017/M-17-279

Order Approving Project Under Minn. Stat. § 216B.1645, Subd. 1,
And Authorizing Cost Recovery January 10, 2018

Docket No. E-017/M-19-411

Otter Tail Power Company – Petition June 21, 2019

Department of Commerce – Comments September 19, 2019

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

 **Relevant Documents**

Date

Otter Tail Power Company – Reply Comments

September 30, 2019

Department of Commerce – Response to Reply Comments

October 16, 2019

Table of Contents

I.	Statement of the Issues	1
II.	Introduction	1
III.	Otter Tail Power’s Petition.....	2
IV.	Department of Commerce Comments	3
A.	Eligibility	3
1.	Langdon and Ashtabula Wind Facilities	3
2.	Merricourt Wind Facility	3
B.	Updated Revenue Requirement and Rate Factor Proposals	4
C.	Updated Rate Design Proposal	4
D.	Proposed Customer Notice	5
E.	Overlap with Potential Rate Case	5
F.	The Use of Two Jurisdictional Factors	5
G.	PTC Flow-Through Methodology for Merricourt PTCs	6
H.	Department Conclusions and Recommendations	6
V.	Staff Analysis	7
VI.	Decision Alternatives	8

I. Statement of the Issues

Should the Commission approve Otter Tail Power's annual update of its Renewable Resource Cost Recovery Rider rate under Otter Tail Power's Rate Schedule 13.04?

II. Introduction

Otter Tail Power Company (Otter Tail, or the Company) is petitioning the Minnesota Public Utilities Commission (the Commission) for approval of its annual update to its Renewable Resource Cost Recovery Rider (RRCRR) rate under its rate schedule 13.04.

This rider was originally established in Docket Nos. E-017/M-08-119 and E-017/M-08-131. In Otter Tail's last general rate case,¹ the Company proposed to recover Production Tax Credit (PTC)-related expenses built into base rates through the RRCRR after the PTCs expire. The Commission approved Otter Tail's RRCRR rate schedule and the RRCRR rate.² The Company's most recent annual update, for the period from November 2018 through October 2019, was approved on August 29, 2018.³

The RRCRR has allowed Otter Tail to recover differences between the PTCs' from its Ashtabula Wind facility (Ashtabula) and its Langdon Wind facility (Langdon) included in base rates and the actual PTCs generated by these facilities. The instant petition proposes to include costs from the Merricourt Wind facility in addition to the cost from the expiring Ashtabula and Langdon PTCs that are in base rates.

For this annual update, Otter Tail Power is requesting approval to recover the annual revenue requirement of \$12,506,339 over a recovery period from November 2019 through October 2020. For a residential customer using 1,000 kWh per month this represents a rate increase of \$2.78 per month.

Overall, Otter Tail Power and the Department are in agreement in recommending that the Commission approve the proposed revenue requirements and rate factors as presented in the Company's September 30, 2019 reply comments.

The main issue the Commission needs to decide is the effective date for the new rate factors and whether the rate factors should be calculated based on a twelve month (annualized) cost recovery time period or a shorter time period.

(In Otter Tail Power's last rate case, in Docket No. E-017/GR-15-1033, the Commission authorized final increase in rates of approximately \$12.3 million, or 5.34 percent.)

¹ Docket No. E-017/M-15-1033, February 16, 2016.

² Ibid, "Findings of Fact, Conclusions and Order", October 30, 2017.

³ Docket No. E-017/M-18-390.

III. Otter Tail Power's Petition

On June 21, 2019, Otter Tail Power submitted its petition to the Minnesota Public Utilities Commission for approval of its annual update to the Renewable Resource Cost Recovery Rider rate under Otter Tail's Rate Schedule 13.04. Otter Tail requested an effective date of November 1, 2019, for cost recovery of the difference in the production tax credits (PTCs) in base rates and the actual PTCs generated using company-owned renewable generation, specifically, the Merricourt Wind project located in North Dakota.

This RRCRR allows Otter Tail to recover the differences between PTCs included in base rates (many of which are expiring) and actual PTCs. Otter Tail stopped receiving PTC's on Langdon in November 2017 and for Ashtabula in October 2018.

This petition adds the impact of 10 years of Federal PTCs earned for the Merricourt Project. Otter Tail requests the use of these PTCs as a reduction to tax expense as they are generated. The effect of this PTC "flow-through" is a reduction in revenue requirements for 10 years and then no credit to tax expense later. The Company stated that:

Through this approach, Otter Tail's Minnesota customers will receive the rate reduction benefits associated with PTCs even though Otter Tail may not yet utilize the PTCs on current tax returns. The unutilized PTCs are carried forward to offset future taxable income and are part of the deferred tax asset. Through this method, the PTC benefits are not spread over the entire lives of the project; rather, they are incorporated into rates in each year PTCs are generated (based on the kWhs generated in each of the first ten years), regardless of whether the PTCs are used on the then-current-period tax return.

The table below shows the final updated requested revenue requirements.

Table 1: Otter Tail's Requested Revenue Requirement Adjustments⁴

Category	Revenue Requirement
Expiring Production Tax Credits – Langdon & Ashtabula Wind Facilities	\$5,265,493
Return on Construction Work in Progress – Merricourt Wind Project	\$7,338,274
Carrying Costs	\$0
True Up for Projected Over-Recovery of Production Tax Credits	<u>\$(97,428)</u>
Total Requested Revenue Requirement	<u>\$12,506,339</u>

⁴ Department of Commerce's October 16, 2019 Response Comments in Docket No. E-017/M-19-411, page 2. The data for the table was retrieved from Otter Tail's September 30, 2019 Reply Comments.

The table below shows the current and final proposed updated rate factors.

Table 2: Otter Tail's Current and Proposed Rate Factors⁵

Customer Class	Current Rate	Proposed Rate	Proposed % Incr./ (Decr.) in Rate
Large General Service	\$0.21738/kW	\$0.464/kW	113%
	\$0.00164/kWh	\$0.00350/kWh	113%
All Other Service	\$0.00244/kWh	\$0.00525/kWh	115%

In addition, Otter Tail requests the following:

- Continued use of a rate design methodology that incorporates demand and energy components.
- A cost recovery period effective from November 1, 2019 through October 31, 2020.
- Approval of the language in the proposed notice to customers, to be included in customer billings the month that the new rate factors are implemented.
- Future application of a flow-through methodology for PTCs anticipated to be earned through future operation of the Merricourt Wind facility.

IV. Department of Commerce Comments

The Department filed comments on September 19, 2019 and supplemental response comments on October 16, 2019. The following is a summary of the Department's analysis, the issues raised and their resolution.

A. Eligibility

1. Langdon and Ashtabula Wind Facilities

Otter Tail Power is proposing to continue recovering the difference between the PTCs included in base rates and PTC actual earnings. However, the actual PTCs earned for these facilities are zero throughout this recovery period. The Company is zeroing out (i.e. truing up) the difference between the PTCs included in base rates and cost of these two facilities without the PTCs. The Department stated that it verified that the proposed PTC details tied to the cost recovery parameters approved for the 2016 test year in Otter Tail's most recent rate case are correct.⁶

2. Merricourt Wind Facility

The Department noted that cost recovery for this facility is a new element in the Company's RRCRR:

⁵ Ibid, Otter Tail Power's September 30, 2019 Reply Comments, age 4, updated from the Department's September 19, 2019 Comments.

⁶ Mark Johnson's Direct Testimony in Docket No. E-017/GR-15-1033, filed August 16, 2016, at Attachment MAJ-15.

In its January 10, 2018 Order in Docket No. E-017/M-17-279, the Commission approved Otter Tail's Merricourt wind project under Minnesota Statutes §216B.1645, Subdivision 1 and authorized corresponding rider cost recovery under Minnesota Statutes §216B.1645, Subdivision 2a. The Commission also determined in its Order that the Merricourt project qualifies for the renewable energy requirements outlined in Minnesota Statutes §216B.1691.

The DOC also pointed out that the Commission order restricted Merricourt cost recovery to a cost cap, plus Allowance for Funds Used During Construction (AFUDC), and less capitalized internal costs.⁷ In its estimates through 2020, Otter Tail has forecast that overall project expenditures will be less than or equal to the cost cap amount of \$270 million (\$143 million for Minnesota.)⁸ In its revised schedules, the Department found that the Company has correctly calculated Merricourt cost recovery for the period.

B. Updated Revenue Requirement and Rate Factor Proposals

As requested by the Department, Otter Tail removed capitalized internal costs from the Merricourt CWIP balance and then recalculated its entire proposed RRCRR revenue requirements and rate factors. The final revised revenue requirement is \$12,506,339. The final numbers can be seen in Revised Tables 2 and 3, on page 3 of these briefing papers.

The Department pointed out that the rate factors have more than doubled from the previous rates, with Large General Service increasing by 113% and All Other Service increasing by 115%. For an average residential customer using 1,000 kWh per month, the bill impact would be an increase of \$2.81 per month.⁹

The Department concluded that the RRCRR revenue requirements and rate factor proposals are reasonable and recommended approval by the Commission. It also recommended that the Commission require Otter Tail Power to submit the Company's revised tariff sheet 13.04 as a compliance filing within 10 days following a Commission order approving the new rate factors.

C. Updated Rate Design Proposal

In its original proposal, Otter Tail had accidentally used outdated class allocation percentages. Otter Tail corrected them in its reply comments. The Department noted its appreciation for the correction and agreed that the updated class allocation percentages are consistent with the Company's most recent rate case in Docket No. E-017/GR-15-1033. Therefore, the Department recommended that the Commission approve Otter Tail's updated rate design proposal.

⁷ The cost recovery restrictions approved for Otter Tail's Merricourt wind project were originally outlined in the Department's August 16, 2018 Trade Secret Response Comments at page 10 in Docket No. E-017/M-17-279.

⁸ Dollar figures in this sentence are found in the Petition at page 7.

⁹ Otter Tail's September 30, 2019 Reply Comments in Docket No. E-017/M-19-411, page 4. The calculation for this bill impact is: $(\$0.00525 \text{ proposed residential rate} - \$0.00244 \text{ currently approved residential rate}) = \$0.00281 \text{ difference} \rightarrow (\$0.00281 \times 1,000 \text{ kWh}) = \$2.81.$

D. Proposed Customer Notice

According to the Department, on page 13, of its comments,

“Otter Tail proposes to use the following language to notify its customers of approved rate factor updates:

The Minnesota Public Utilities Commission has approved an adjustment to the Renewable Resource Cost Recovery Rider that is part of the Resource Adjustment on your monthly electric service statement. This rider recovers costs associated with owning and operating renewable generation resources. The table below shows the prior and new rates, beginning November 1, 2019, for all classes of customers ... For more information contact Customer Service at 800-257-4044 or place an inquiry from our website at www.otpc.com. [OTP, petition, attachment 6]

The language and format of the proposed customer notification is consistent with that approved in the Company’s most recent renewable rider update in Docket No. E017/M-18-390. Otter Tail indicated that it would notify customers of approved rate factor updates through customer bills in the month that the new RRAR rates are implemented.

Based on its review, the Department concludes that the customer notification language proposed by Otter Tail is reasonable and recommends that the Commission approve the Company’s proposal.”

E. Overlap with Potential Rate Case

In its initial comments, the Department addressed potential issues should Otter Tail file a rate case where any part of the test year overlaps with part of the proposed RRCRR recovery period. As a result, the Department recommended that the Commission direct the Company to stop all rider collections and roll all rider costs and related PTCs into base rates when interim rate become effective, which could require a later true-up filing. In its reply comments, Otter Tail agreed. (Otter Tail has indicated that it may file a rate case sometime in calendar year 2020.)

F. The Use of Two Jurisdictional Factors

In its initial comments, the Department requested an explanation for the Company’s use of two different Minnesota jurisdictional allocation factors in its petition. Otter Tail responded that it used an Electric-Plant-in-Service allocation factor for Langdon and Ashtabula as approved in its most recent rate case, Docket No. E-017GR-15-1033. Since these wind facilities’ PTCs are built into Minnesota base rates using this factor, the Company uses this same factor for these facilities in the PTC true-up in this RRCRR. Typically, the Company would use its E2 allocator for projects contained entirely in the RRCRR and that is the factor that was used for Merricourt.

The Department concluded that Otter Tail Power's use of these two factors is "logical and appropriate under the circumstances".

G. PTC Flow-Through Methodology for Merricourt PTCs

The Department explained Otter Tail's proposed use of a flow-through methodology as opposed to a levelized methodology in accounting for the future Merricourt PTCs.

The flow-through methodology would allow the Company to apply PTCs to the Company's revenue requirement calculation as the credits are earned, thereby reducing the revenue requirement amount and incorporating this tax credit benefit into rates each year in which Otter Tail earns PTCs. Under a levelized approach, the Company would allocate estimated Merricourt PTC benefits evenly over the depreciable life of the facility, resulting in a tax credit benefit distributed over a 25-year period (i.e. the currently estimated depreciable life, rather than the 10-year period over which Merricourt would be eligible to earn PTCs).

The Department concluded that Otter Tail's proposed use of the flow-through method is reasonable and recommends that the Commission approve this proposal.

H. Department Conclusions and Recommendations

The Department recommended that the Commission:

- Approve Otter Tail's proposed revenue requirement of \$12,506,339, as presented in the Company's September 30, 2019 Reply Comments.
- Approve Otter Tail's proposed rate factors of (1) \$0.464 per kW and \$0.00350 per kWh for Large General Service customers and (2) \$0.00525 per kWh for all other customers, as presented in the Company's September 30, 2019 Reply Comments.
- Approve Otter Tail's proposed rate design, as outlined in Revised Attachment 5 of the Company's September 30, 2019 Reply Comments.
- If and when the Commission approves new Renewable Resource Cost Recovery rate factors:
 - Authorize the new rate factors to become effective on November 1, 2019 and remain in effect through October 31, 2020, if the Commission issues an order in this matter before November 1, 2019.
 - Authorize the new rate factors to become effective on the first of the month following Commission approval and remain in effect through October 31, 2020, if the Commission issues an order in this matter after November 1, 2019.
 - Grant Otter Tail the option to recalculate its rate factors, if the new rate factors are approved more than 45 days later than November 1, 2019.
- Approve Otter Tail's proposed customer notification language to be included with customer bills in the month that new rate factors are implemented.

- Approve Otter Tail's proposal to use a flow-through methodology to account for future Merricourt Production Tax Credits.
- Require Otter Tail to submit as compliance filings (1) the Company's revised tariff sheet 13.04 and (2) the Company's customer notice, updated with any newly approved RRCRR rate factors, within 10 days following Commission's order approving new RRCRR rate factors.

In addition, if Otter Tail files a rate case with a test year that overlaps with any part of the recovery period proposed for this rider, the Department recommends that the Commission do the following:

- Require Otter Tail to discontinue all rider collections and roll all rider costs and related PTCs (if any) into base rates once interim rates become effective, with subsequent PTC true-ups in future riders. Rolling in all rider costs at the beginning of the rate case could be accomplished as follows:
 - The rider is suspended at the beginning of the utility's test year in the rate case (such as January 1, 2020).
 - Unrecovered rider costs, such as undepreciated rate base and operation and maintenance expenses, as of the end of the day before the test year (e.g. December 31, 2019), are folded into interim rates.
 - The subsequent true-up for the rider would resolve any under- or over-recovery (tracked through the rider tracker account) as of the day before the test year in the rate case (e.g. December 31, 2019).

V. Staff Analysis

Staff notes that there are no disagreements between the Department and Otter Tail Power regarding recommendations. The only remaining issue involves the timing of the implementation of the updated rider rate factors. As noted by the Department, the proposed rates are 113% to 115% higher than the current rate and would result in an increase of \$2.81 per month for an average residential customer using 1,000 kWh per month.

This increase could be even higher if the new rates cannot be implemented until 45 days after a Commission order is issued approving Otter Tail's request. Assuming the order could be issued by mid-January 2020 with an effective date of February 1, 2020 and a recovery period through October 31, 2020, this would result in the revised rates shown in the following comparison table below.

Table 3: Otter Tail's Current and Revised Rate Factors for Recovery from February 1, 2020 through October 31, 2020¹⁰

Customer Class	Current Rate	Revised Rate	Proposed % Incr./ (Decr.) in Rate
Large General Service	\$0.21738/kW	\$0.61883/kW	185%
	\$0.00164/kWh	\$0.00467/kWh	185%
All Other Service	\$0.00244/kWh	\$0.00700/kWh	187%

The implementation shown above would result in a billing impact of a \$4.56 per month increase for an average residential customer using 1,000 kWh per month.¹¹

If the Commission allows a 12 month recovery period from February 1, 2020 through January 21, 2021, then the revised rate factor would revert to the calculations shown in Table 2 on page 3 of these briefing materials. This would mitigate rate shock, but could result in additional under/over recovery in a future time period depending on the revenue requirements necessary for the next annual update.

VI. Decision Alternatives

2019 Annual Update to Otter Tail Power's Renewable Resource Cost Recovery Rider – Revenue Requirement and Rate Factors

1. Approve Otter Tail's proposed revenue requirement of \$12,506,339, as proposed in the Company's September 30, 2019 Reply Comments (*OTP, DOC*) **AND**
2. Approve Otter Tail's proposed rate factors to become effective January 1, 2020: (a) \$0.464 per kW and \$0.00350 per kWh for Large General Service customers and (b) \$0.00525 per kWh for all other customers, as proposed in the Company's September 30, 2019 Reply Comments (*OTP preferred alternative, DOC*) **OR**
3. Approve Otter Tail's proposed rate factors to become effective February 1, 2020: (a) \$0.464 per kW and \$0.00350 per kWh for Large General Service customers and (b) \$0.00525 per kWh for all other customers, as proposed in the Company's September 30, 2019 Reply Comments (*OTP, DOC*) **OR**
4. Authorize Otter Tail to recalculate new rate factors based on a nine month recovery period to become effective on February 1, 2020. (This assumes the Commission issues its order in January 2020.) (*OTP 2nd preferred alternative, DOC*)

¹⁰ The calculations assume that billing units are three-fourths of Otter Tail's proposed number and the revenue requirement remains the same.

¹¹ Staff calculates this bill impact as: (\$0.00700 revised residential rate - \$0.00244 currently approved residential rate) = \$0.00456 difference → (\$0.00456 x 1,000 kWh) = \$4.56.

Proposed Rate Design

5. Approve Otter Tail's proposed rate design, as presented in Revised Attachment 5 of the Company's September 30, 2019 Reply Comments. (*OTP, DOC*)

Tariff and Customer Notification

6. Approve Otter Tail's proposed customer notification language (updated as needed to include the correct implementation date and revisions to the rate factors), to be included with customer bills in the month that new rate factors are implemented. (*OTP, DOC*) **AND**
7. Require Otter Tail to submit as compliance filings (1) the Company's revised tariff sheet 13.04 and (2) the Company's customer notice, updated with any newly approved RRCRR rate factors, within 10 days following Commission's order approving new RRCRR rate factors. (*OTP, DOC*)

Merricourt PTCs

8. Approve Otter Tail's proposal to use a flow-through methodology to account for future Merricourt Production Tax Credits. (*OTP, DOC*)

If Otter Tail files a rate case with a test year that overlaps with any part of the recovery period proposed for this rider

9. Require Otter Tail to discontinue all rider collections and roll all rider costs and related PTCs (if any) into base rates once interim rates become effective, with subsequent PTC true-ups in future riders. Rolling in all rider costs at the beginning of the rate case could be accomplished as follows:
 - The rider is suspended at the beginning of the utility's test year in the rate case (such as January 1, 2020).
 - Unrecovered rider costs, such as undepreciated rate base and operation and maintenance expenses, as of the end of the day before the test year (e.g. December 31, 2019), are folded into interim rates.
 - The subsequent true-up for the rider would resolve any under- or over-recovery (tracked through the rider tracker account) as of the day before the test year in the rate case (e.g. December 31, 2019). (*OTP, DOC*)