MINNESOTA
PUBLIC UTILITIES COMMISSION

# Staff Briefing Papers

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| Meeting Date | June 14, 2018 | Agenda Item ***3** |
| Company | Northern States Power Company d/b/a/ Xcel Energy | |
| Docket No. | **E-002/S-17-767**<br>In the Matter of the Petition of Northern States Power Company d/b/a/ Xcel Energy for Approval of its Capital Structure for Issuance of Long-term and Short-term Securities for 2018 | |
| Issue | Should the Commission approve Xcel's petition subject to the modifications proposed by the Department of Commerce? | |

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| ✓ **Relevant Documents** | **Date** |
|---|---|
| Xcel Petition | October 26, 2017 |
| Xcel Supplemental Filing | November 13, 2017 |
| Department of Commerce – Comments | December 1, 2017 |
| Xcel - Reply Comments | December 7, 2017 |

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

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## I. Statement of the Issue

Should the Commission approve Xcel's petition subject to the modifications proposed by the Department of Commerce?

## II. Background

October 26, 2017, Xcel filed a petition requesting the Commission's approval of its proposed 2018 capital structure and permission to issue securities within the scope of the proposed capital structure.

On November 13, 2017, Xcel filed a supplemental filing which contained a copy of the Securities and Exchange Commission Form S-3 registration statement as required under Minn. R. 7825.1500.

On December 1, 2017, the Department of Commerce filed its comments recommending approval of Xcel's petition subject to numerous reporting requirements for future filings.

One reporting condition recommended by the Department requires Xcel, when it issues bonds, to provide a comparison over a six-month period of the results of all bond issuances by other utilities. Another reporting condition recommended by the Department requires Xcel to demonstrate that any bond issuance over the preceding year was cost competitive, including, at a minimum, a detailed comparative analysis of bond issuances by other utilities.[1]

On December 7, 2017, Xcel filed its reply comments. Xcel responded that it had "no objection to the recommended additional reporting requirements," but that it may not always have access to detailed comparative analysis of bond issuances as that information comes from an external source. However, Xcel said it would attempt to provide that information, or very similar information, in future filings.

## III. Summary of Xcel's Petition

Xcel's petition is seeking approval of the following provisions:

(1) total capitalization not to exceed $11.5 billion (including a capitalization contingency of $522 million in case Xcel needs more capital than anticipated);

(2) a consolidated equity ratio of 52.3 percent and a contingency window of ±10 percent (providing a range of 47.07 percent to 57.53 percent);

(3) ability to issue short term debt not to exceed 15 percent of total capitalization;

(4) the 2018 capital structure (including total capitalization) being effective until the Commission approves the next capital structure;

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[1] The Department requires this information to be the same as, or similar to, the information provided by Xcel in this docket. See Attachment 3 to the Department's Comments.

(5) flexibility to issue securities, provided Xcel's capital structure does not go outside approved levels for more than 60 days without Xcel notifying the Commission;

(6) continue to allow Xcel to use risk management instruments that qualify for hedge accounting treatment;

(7) continue to allow Xcel to treat borrowing under multi-year credit agreements as short-term debt, by varying Minn. Rules 7825.1000, subp. 6;

(8) grant Xcel the discretion to enter into financing arrangements to replace outstanding long-term debt instruments with less expensive securities after considering the debt issuance expenses and amortization of redemption premiums; and

(9) grant Xcel the discretion to enter into tax-exempt financing arrangements for pollution control construction programs.

## IV. Summary of the Department's Analysis and Recommendation

The Department reviewed Xcel's petition, including the supplement, and found that the petition complied with all applicable reporting requirements.

The Department has recommended approval of Xcel's petition after a thorough analysis of the nine provisions for which Xcel asked the Commission for approval.

In reference to item (7) above, the Department noted that Xcel has met the requirements for a variance of Commission rules by demonstrating that: (a) enforcement of the rule would be excessively burdensome; (b) granting the variance would not adversely affect the public interest; and (c) granting the variance would not conflict with standards imposed by law. The Department concluded that Xcel's current multi-year credit agreement resembles traditional short-term debt instruments anyhow and classifying multi-year credit agreements as long-term debt could cause credit-rating agencies to react unfavorably, thus imposing an excessive burden on Xcel and hurting ratepayers.

The Department's recommendation of approval is subject to numerous reporting requirements.[2]

In particular, regarding item (6) above, the Department observed that Xcel would likely use risk-management instruments to hedge against the risk of changing interest rates. The Department noted that risk-management instruments such as interest rate swaps can benefit ratepayers as long as Xcel follows prudent corporate guidelines in its usage of such instruments and provides enough information to allow the Commission sufficient oversight. The Department, in view of this objective, has recommended that Xcel include in all future capital-structure filings a summary of its use of risk-management instruments and the resulting effect on ratepayers.

[2] Staff Note: The reporting requirements are interspersed with analysis in the Department's comments. Staff has attempted to itemize the Departments' recommended requirements.

In reference to item (7) above, the Department has recommended that Xcel file a discussion of how often the risk-management instruments are used, the amount involved, rates and financing costs, the intended uses of the financing, and, for any period in which Xcel sells bonds, a comparison over a six-month period of the results of all bond issuances by other utilities.

The Department recommended approval of items (8) and (9) above because both types of financing would reduce costs to ratepayers. The Department, however, recommended that, in order to ensure adequate oversight, the Commission require Xcel to report on such financings and their impact on ratepayers in its next capital structure filing.

The Department has recommended the following additional reporting requirements:

(a) a schedule showing, for various time periods, the planned investment for each project;
(b) a summary of Xcel's activity in the Utility Money Pool;
(c) a summary of Xcel's use of risk-management instruments and the resulting effect on ratepayers in all future capital structure filings;
(d) to ensure compliance with Order Points 1 and 2 of the Commission's July 9, 2004 Order in E,G-002/AI-04-100,[3] require all future Xcel capital structure filings to include a comparison of the borrowing and lending interest rates from the money pool to alternative interest rates, such as that provided in Xcel's response to Department Information Request (IR) No. 2, shown in Attachment 2 to the Department's comments; and
(e) provide evidence, in all future capital structure filings, that demonstrates that any bond issuances over the preceding year were cost competitive,[4] including at a minimum a

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[3] Staff Note: In docket 04-100, the Commission approved a Money Pool Agreement between Xcel's parent company, its affiliated service subsidiaries, and utility operating subsidiaries for inter-company loans. This agreement provided for a revolving credit facility (i.e., money pool) for the utility subsidiaries by recognizing that the subsidiaries, from time to time, need to borrow funds on a short-term basis, and some of the parties to the contract will from time to time have funds available to loan on a short-term basis. The agreement was structured such that the subsidiary utilities would borrow from the pool only when the interest rate was lower than that offered by a bank or other source; and the operating subsidiaries would lend to the pool only when the return was equal to or higher than returns that the operating utility could expect to receive from elsewhere. In approving this agreement, the Commission required, in part, that Xcel: (1) not use the Utility Money Pool if it can borrow directly from a bank or other financial institution at a lower rate; and (2) lend to the Utility Money Pool only if the returns on investment are equal to or greater than returns Xcel could have received elsewhere.

[4] Xcel notes that, historically, there are two ways of issuing long-term debt securities – Competitive Bidding and Negotiated Placement (Attachment L of Xcel filing). In Competitive Bidding, a limited number of banks competed by bidding the lowest interest rate. Competitive Bidding was common prior to the 1990s and is no longer commonly employed. The standard practice now is Negotiated Placement whereby "the issuing company selects a few banks to serve as underwriters of a bond offering with the goal of creating competition among investors." Further, "[t]he company and selected banks convene a few weeks in advance of the planned issuance to begin preparing the financial and legal documents, monitor market conditions, analyze other utility bond offerings in the market, and discuss potential structures and timing to maximize investor interest to achieve a favorable execution and pricing outcome. The investment banks will undertake a wide-range and in-depth presale effort prior to the formal pricing of the bond. From this effort, investor interest is created, and security prices can be developed through the competitive forces of the supply and demand within the market." Xcel claims

detailed comparative analysis to other bond issuances such as that provided in Xcel's response to Department IR No. 1(c), which is provided as Attachment 3 to the Department's comments;[5] and

(f) a summary of Xcel's use of risk-management instruments and the resulting effect on ratepayers.

that a "negotiated sale provides the company with flexibility regarding structure or market timing" and that "[b]ecause the market is real-time, transparent, and priced in the competitive capital markets, the bond pricing is consistent with other utility transactions with similar credit ratings and bond terms."

[5] The information contained in Attachment 3 (Xcel's response to the Department Information Request (c)) shows bonds issued by utilities with credit ratings similar to Xcel's in 2017, the amount for which bonds were issued, date of issue of bonds, maturity date, coupon rate, and other technical information.

**Summary of the Department's recommendations**:

1. Approve NSP-MN's requested 2018 capital structure (including total capitalization) effective until the Commission approves NSP-MN's 2019 capital structure;

2. Allow NSP-MN's to issue securities provided that the Company remains within the approved capital structure or does not go outside the approved capital structure for more than 60 days without the Commission's preapproval;

3. Continue to allow NSP-MN to use risk-management instruments that qualify for hedge accounting treatment under Accounting Standard Codification No. 815;

4. Continue to allow NSP-MN to treat borrowing under multi-year credit agreements as short-term debt, by varying Minn. Rules part 7825.1000, subpart 6;

5. Allow NSP-MN to enter into financing arrangements to replace outstanding long-term debt instruments with less expensive securities, and tax-exempt financing arrangements for pollution-control construction programs, provided Xcel's next capital structure filing reports on any such financings entered into and their effect on ratepayers.

6. Additional Permanent Reporting Requirements:

a) a schedule showing, for various time periods, the planned investment for each project;
b) a summary of Xcel's activity in the Utility Money Pool;
c) a discussion detailing how often multi-year credit agreements are used, the amount involved, rates and financing costs, the intended uses of the financing, and, for any period in which NSP-MN sells bonds, a comparison over a six-month period of the results of all bond issuances by other utilities;
d) to ensure compliance with Order Points 1 and 2 of the Commission's July 9, 2004 Order in E,G-002/AI-04-100, require all future Xcel capital structure filings to include a comparison of the borrowing and lending interest rates from the money pool to alternative interest rates, such as that provided in Xcel's response to Department Information Request (IR) No. 2, shown in Attachment 2 to the Department comments;
e) provide evidence, in all future capital structure filings, that demonstrates that any bond issuances over the preceding year were cost competitive, including at a minimum a detailed comparative analysis to other bond issuances such as that provided in Xcel's response to Department IR No. 1(c), which is provided as Attachment 3 to the Department's comments; and
f) a summary of Xcel's use of risk-management instruments and the resulting effect on ratepayers.

## V. Xcel's Reply Comments

Xcel stated that although it does not object to the Department's recommended reporting requirements, it cautioned that it may not always have access to a detailed comparative analysis of bond issuances. Xcel noted that the details of bond issuance analysis come from an external source. Xcel indicated that it would provide the details to the extent it is able to access the information.

## VI. Staff Comment

Staff agrees with the Department's analysis and the need for additional permanent reporting requirements.

However, in light of Xcel's concern that it relies on external data for detailed comparative analysis of bond issuances, staff provides the following simple re-write of condition 6(e), above, which recognizes Xcel's limitation in fulfilling this condition:

> **Condition 6(e) (alternative)**: To the extent practicable, provide evidence, in all future capital structure filings, that demonstrates that any bond issuances over the preceding year were cost competitive, including at a minimum a detailed comparative analysis to other bond issuances such as that provided in Xcel's response to Department IR No. 1(c), which is provided as Attachment 3 to the Department's comments.

## VII. Decision Options

1. Approve Xcel's requested 2018 capital structure (including total capitalization) effective until the Commission approves NSP-MN's 2019 capital structure;

2. Allow Xcel to issue securities provided that the Company remains within the approved capital structure or does not go outside the approved capital structure for more than 60 days without the Commission's preapproval;

3. Continue to allow Xcel to use risk-management instruments that qualify for hedge accounting treatment under Accounting Standard Codification No. 815;

4. Continue to allow Xcel to treat borrowing under multi-year credit agreements as short-term debt, by varying Minn. Rules part 7825.1000, subpart 6;

5. Allow Xcel to enter into financings to replace outstanding long-term debt instruments with less expensive securities, and tax-exempt financings for pollution-control construction programs, provided Xcel includes, in its next capital structure filing, a report on any such financings entered into and their effect on ratepayers.

6. Require Xcel to include the following information in all future capital structure dockets:

   a) a schedule showing, for various time periods, the planned investment for each project;
   b) a summary of Xcel's activity in the Utility Money Pool;
   c) a discussion detailing how often multi-year credit agreements are used, the amount involved, rates and financing costs, the intended uses of the financing, and, for any period in which NSP-MN sells bonds, a comparison over a six-month period of the results of all bond issuances by other utilities;
   d) to ensure compliance with Order Points 1 and 2 of the Commission's July 9, 2004 Order in E,G-002/AI-04-100, require all future Xcel capital structure filings to include a comparison of the borrowing and lending interest rates from the money pool to alternative interest rates, such as that provided in Xcel's response to Department Information Request (IR) No. 2, shown in Attachment 2 to the Department comments;
   e) <u>to the extent practicable,</u> provide evidence, in all future capital structure filings, that demonstrates that any bond issuances over the preceding year were cost competitive, including at a minimum a detailed comparative analysis to other bond issuances such as that provided in Xcel's response to Department IR No. 1(c), which is provided as Attachment 3 to the Department's comments; and
   f) a summary of Xcel's use of risk-management instruments and the resulting effect on ratepayers.