

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Nancy Lange	Chair
Dan Lipschultz	Commissioner
Matthew Schuerger	Commissioner
Katie J. Sieben	Commissioner
John A. Tuma	Commissioner

In the Matter of the Application of Northern States Power Company for Authority to Increase Its Rates for Electric Service in the State of Minnesota

ISSUE DATE: August 13, 2018

DOCKET NO. E-002/GR-92-1185

DOCKET NO. G-002/GR-92-1186

In the Matter of the Petition of Northern States Power Company's Gas Utility for Authority to Change Its Schedule of Gas Rates for Retail Customers Within the State of Minnesota

DOCKET NO. E,G-002/M-17-429

ORDER REQUIRING INCENTIVE COMPENSATION REFUND

In the Matter of Northern States Power Company's Petition for Approval of Its 2016 Incentive Compensation Plan Report

PROCEDURAL HISTORY

On May 26, 2017, Northern States Power Company, doing business as Xcel Energy (Xcel or the Company), filed its 2016 Incentive Compensation Plan Report. The requirement to submit this report was originally established by orders in the two above-captioned rate-case dockets.¹

On June 22, 2017, the Minnesota Department of Commerce (the Department) filed comments recommending that the Commission accept the report as compliant with its prior orders.

On March 14, 2018, the Commission issued a notice soliciting comments on the appropriate method by which to determine whether ratepayers were owed a partial refund of Xcel's 2016 incentive-compensation costs.

¹ See Docket No. E-002/GR-92-1185, Order After Reconsideration, at 9 (January 14, 1994) (requiring electric utility to file an annual report on the operation and performance of its incentive-compensation plan); Docket No. G-002/GR-92-1186, Order After Reconsideration, at 8 (December 30, 1993) (imposing same requirement on natural gas utility).

On April 12, Xcel and the Department filed comments in response to the Commission's notice.² Based on its review, the Department recommended that Xcel issue refunds to its electric ratepayers in the total amount of \$1,278,656.

On April 23, Xcel filed reply comments requesting that the Commission accept its report as originally filed and require no refund.

On July 19, 2018, the Commission met to consider the matter.

FINDINGS AND CONCLUSIONS

I. Background

Xcel offers its non-union employees a compensation package that includes both a base salary and incentive payments for achieving Company goals. Its Annual Incentive Program (AIP) defines weighted "key performance indicators," such as reliability, cost management, public safety, and employee safety, by which employees' performance is judged. The Company must achieve specified earnings targets before any payments are made.³

The Commission has imposed two key conditions on Xcel's recovery of incentive-compensation costs from ratepayers. First, the Company is not allowed to recover incentive amounts that exceed 15% of an individual employee's base salary.⁴ Second, to the extent that incentive payouts are lower than the test-year level used to set base rates, Xcel is required to refund the difference to ratepayers.⁵

II. Xcel's 2016 Incentive Compensation Report

Xcel reports that in 2016, it paid approximately \$23.8 million in incentive compensation to employees working in its Minnesota electric and gas operations. According to the Company, this amount exceeds the \$20.3 million approved for recovery through base rates. Xcel concludes that because it paid about \$3.5 million more in incentive-compensation costs than it recovered through rates, no refund is required.

However, the picture changes when the 15%-of-base-salary cap is taken into account. Attachment C to Xcel's report shows that the Company paid incentives totaling \$22,443,649 to employees in its Minnesota electric operations but that the recoverable portion of this amount is only \$18,114,695 after application of the 15% cap. This latter amount is smaller than the test-

² On April 16, the Department filed an attachment that had been inadvertently omitted from its April 12 comments.

³ See Xcel's 2016 Incentive Compensation Plan Report, Attachment A (2016 AIP policy).

⁴ Docket No. E-002/GR-92-1185, Order After Reconsideration, at 7 (electric utility); Docket No. G-002/GR-92-1186, Order After Reconsideration, at 7 (gas utility).

⁵ See *In the Matter of the Application of Northern States Power Company for Authority to Increase Rates for Electric Service in the State of Minnesota*, Docket No. E-002/GR-12-961, Findings of Fact, Conclusions, and Order, at 51 (September 3, 2013) (requiring Xcel to continue its refund practice).

year incentive costs for Xcel's Minnesota electric operations (\$19,393,351), raising the question of whether Xcel should refund the difference to ratepayers.

In its March 2018 notice, the Commission solicited the parties' views on whether the appropriate comparison, for purposes of determining if ratepayers are owed a refund, is between (1) test-year incentive costs and actual incentive payouts or (2) test-year incentive costs and incentive payouts capped at 15% of an employee's base salary.

III. Positions of the Parties

Xcel argued that the appropriate refund comparison is between test-year incentive costs and the amount of incentive compensation actually paid.

The Company stated that its recovery of incentive-compensation costs is already limited in two ways through the ratemaking process: The test-year incentive cost is based on a four-year historical average, to which the 15% cap is then applied. Xcel argued that the 15% cap was not intended to be applied both in ratemaking and to the actual payouts when determining refunds.

Xcel also argued that if actual payouts in excess of 15% of an employee's salary are subject to refund, there would be a negative incentive for the Company to limit payouts to 15% for even its highest-performing employees. In other words, the Company would prefer to have discretion to pay some employees more than 15% while paying others less, such that the total incentive payments to all employees remains at or below 15% of their salaries in aggregate.

The Department maintained that the appropriate comparison for determining refunds is between the test-year incentive cost and actual payouts capped at 15% of each employee's base salary. This is consistent with the Commission's order establishing the cap, which states that recoverable incentive payments are limited to "15 percent of *an individual's* base salary."⁶ Based on the data in Xcel's Attachment C, the Department concluded that Xcel owes its electric ratepayers a \$1,278,656 refund.

IV. Commission Action

The Commission agrees with the Department that the proper comparison for calculating whether a refund is due is between the test-year amount used to set base rates and the amount actually paid out that is eligible for recovery from ratepayers—i.e., excluding incentive pay beyond 15% of an individual's base pay. Accordingly, the Commission will require Xcel to refund electric ratepayers \$1,278,656 for 2016.

This result is consistent with the Commission's order establishing the 15% cap. In that order, the Commission stated that it "continues to believe . . . that the officers' and executives' plans allow too high a proportion of these employees' total wages to come from incentive compensation" and therefore limited recoverable incentive payments to 15% of "an individual's" base salary.⁷

⁶ Docket No. E-002/GR-92-1185, Order After Reconsideration, at 7 (emphasis added).

⁷ *Id.*

Xcel would like to be able to pay certain high-performing employees incentives greater than 15% of their base salaries, offsetting these higher payments by paying other employees less than 15%, to achieve a 15% cap in the aggregate. However, allowing this practice would undermine the purpose of the cap.

The Commission was clear that the reason for the cap was to prevent ratepayers from paying for incentives that represent a very high proportion of an individual employee's overall pay. Incentives beyond that 15% cap may be funded by Xcel's shareholders, but the Commission has made a policy determination that it was not reasonable for ratepayers to fund incentives beyond this level, and the Commission remains convinced that this policy is necessary to ensure just and reasonable rates.

For the foregoing reasons, the Commission will require Xcel to refund its electric ratepayers \$1,278,656, which represents the difference between the Company's test-year incentive costs and its actual 2016 incentive payouts, capped at 15% of each employee's base salary.

ORDER

1. Xcel Electric shall refund its ratepayers \$1,278,656.
2. This order shall become effective immediately.

BY ORDER OF THE COMMISSION

Daniel P. Wolf
Executive Secretary



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