STATE OF MINNESOTA
BEFORE THE PUBLIC UTILITIES COMMISSION

Beverly Jones Heydinger	Chair
David C. Boyd	Commissioner
Nancy Lange	Commissioner
Dan Lipschultz	Commissioner
Betsy Wergin	Commissioner

In the Matter of the Petition of Northern States Power Company for Approval of a Gas Utility Infrastructure Cost Rider

Docket No. G-002/M-14-336

REPLY COMMENTS OF THE OFFICE OF THE ATTORNEY GENERAL - ANTITRUST AND UTILITIES DIVISION

I. INTRODUCTION

The Office of the Attorney General - Antitrust and Utilities Division ("OAG") submits the following Reply Comments regarding the Petition ("Rider Petition") of Northern States Power Company ("Xcel") for approval to establish a cost recovery rider for gas utility infrastructure costs ("GUIC" or "GUI").[1] Xcel seeks rider recovery for deferred costs that the Commission had previously authorized in addition to on-going costs for infrastructure projects.

The recovery of GUI costs are authorized by Minnesota Statutes section 216B.1635, but are limited to recovery of costs for:

> (1) replacement of natural gas facilities located in the public right-of-way required by the construction or improvement of a highway, road, street, public building, or other public work by or on behalf of the United States, the state of Minnesota, or a political subdivision; and
>
> (2) replacement or modification of existing natural gas facilities, including surveys, assessments, reassessment, and other work

[1] According to the Commission's September 30, 2014 Second Notice of Extended Comment Period, reply comments are due by October 27. Although the OAG did not submit initial comments in this docket, it comments now, in part, to reply to the analysis and recommendation of the Department, submitted on October 16.

> necessary to determine the need for replacement or modification of existing infrastructure that is required by a federal or state agency.[2]

These reply comments address Xcel's Petition and the Department of Commerce's ("Department") comments on Xcel's Petition. The OAG recommends denial of the Rider Petition; in the alternative, the OAG recommends that the Commission impose several conditions to protect the interests of ratepayers.

II. BACKGROUND

Xcel submitted its Rider Petition on August 1, 2014, to request an automatic recovery rider for GUI costs. Xcel seeks recovery of costs that it has been granted deferred accounting for plus forecasted costs to address federal and state requirements for pipeline safety. The costs would result in a $14.9 million increase to Xcel's revenue requirement, which equates to a $2.22 increase in the monthly cost for a typical residential customer bill.[3] On an annual basis the increase would be $26.64. According to Xcel, this would be an approximately 3% increase for a typical residential customer bill.

The deferred costs were approved by the Commission in two earlier dockets. In Docket No. G002/M-10-422, Xcel was granted approval to defer costs associated with a Notice of Probable Violation from the Minnesota Office of Pipeline Safety ("MNOPS").[4] The Notice was issued to Xcel in response to a natural gas explosion. Xcel was required to submit a plan for inspection and remediation to MNOPS. The remediation costs that the Commission allowed for deferral were incremental external operating and maintenance expenses that Xcel incurred to comply with the MNOPS Notice.

---

[2] Minn. Stat. § 216B.1635, subd. 1(c)(1) and (2).
[3] Petition, at 2.
[4] Order Granting Deferred Accounting Treatment Subject To Conditions And Reporting Requirements, *In the Matter of the Petition of Northern States Power Company for Deferred Accounting Treatment of Costs Relating to Identifying and Eliminating Sewer/Natural Gas Line Conflicts*, Docket No. M-10-422 (January 12, 2011).

In Docket No. G002/M-12-248, Xcel was granted approval to defer costs for its Transmission Integrity Management Program ("TIMP") and Distribution Integrity Management Program ("DIMP") costs. TIMP costs are incurred to comply with federal regulations to establish a baseline inspection program for transmission pipelines, and follow-up inspections are required at least every seven years. The initial inspections were to be completed by 2012.[5] DIMP costs were also being incurred to develop and implement an integrity management program for distribution facilities in accordance with federal regulations. Xcel requested deferral for incremental operating and maintenance inspection and repair expenses for both TIMP and DIMP costs. The Commission approved Xcel's request with conditions.[6]

In Xcel's current Rider Petition, it seeks to recover costs deferred in both of these deferred accounting dockets and also for on-going expenses and capital investments for infrastructure that it believes are permitted by statute in a GUI cost recovery rider. Xcel interprets the conditions in its two deferred accounting authorizations, which require Xcel to address cost recovery in its next general rate case, as also permitting Xcel to recover the costs in a rider. Xcel explained that its attempt to use the GUI cost rider to recover *deferred* infrastructure costs is based on the changes to Minnesota Statutes section 216B.1635 in 2013.[7] Xcel believes the statutory changes for the GUI cost rider allows Xcel to "substitute" rider recovery for the Commission's requirement that it seek recovery for deferred costs in its next "general rate case."

---

[5] Petition, *In the Matter of the Petition of Northern States Power Company for Approval of Deferred Accounting for Costs to Comply with Gas Pipeline Safety Programs*, Docket No. G002/M-12-248, at 4 (Mar. 21, 2012).
[6] Order, *In the Matter of the Petition of Northern States Power Company for Approval of Deferred Accounting for Costs to Comply with Gas Pipeline Safety Programs*, Docket No. G002/M-12-248 (Jan. 28, 2013).
[7] Petition, at 9.

Xcel's revenue requirement calculation for 2015 for GUI costs under the rider is $14.9 million.[8] Xcel compares this incremental revenue requirement to its total revenues authorized in its last case in Docket No. G002/GR-09-1153, of $592.9 million. Xcel also compares the GUI rider revenue requirement to its base revenue of $159.1 million, which excludes revenues for the cost of gas and other operating income.[9] The comparison of the rider revenue requirement of $14.9 million with base revenue shows that the rider revenue requirement is 9.39% of base revenues. The breakdown of the rider revenue requirement between deferred expenses and on-going 2015 costs is $10.2 million for on-going costs and $4.7 million for amortization of deferred costs.[10] A total of $23.8 million of deferred expenses are projected through 2014, which Xcel proposes to amortize over five years.

The Department conducted an initial review of Xcel's Petition. According to the Department, it reviewed Xcel's calculation of its revenue requirement, its tracker proposal, and statutory compliance for the rider. The Department concluded that Xcel's proposal was reasonable, and recommended approval of Xcel GUI Rider Petition with a few conditions. One condition the Department recommended was that the rate of return for the rider be reduced from Xcel's initial request. On October 23, 2014, Xcel filed a letter indicating that it agreed to the Department's recommendation to reduce the rate of return on the costs from 8.28 percent to 7.56 percent.

[8] Petition, at 22.
[9] The comparison of rider revenue with base revenue is relevant because a rate case only considers costs used to develop base revenues.
[10] Petition, at 16.

III. XCEL SHOULD BE REQUIRED TO RECOVER GUIC COSTS IN A GENERAL RATE CASE.

While there is general statutory authorization to recover gas utility infrastructure costs through riders, the traditional rate case approach provides the best protection for ratepayers. A rate case proceeding allows for a more complete of discovery and more thorough analysis. A rate case also allows consideration of all costs to establish rates rather than piecemeal portions of costs in isolation. Without a complete revenue requirement review of all costs, there is a risk that a utility may be overearning yet still be allowed to increase rates by use of a rider. The same is true with deferral of costs. Deferred costs are removed from the determination of operating income for a particular year which may contribute to an overearning situation for that year and at the same time allow higher future revenues when deferred costs are being amortized. Use of regulatory recovery tools such as riders, trackers and deferred accounting allows a utility to preserve or guarantee cost recovery even in situations where the utility's earnings are sufficient to reward investors for their investments.

Xcel explained in its Petition that the impact on a typical residential customer for its rider proposal would be an approximately 3% increase on the customer's bill. In its last gas rate case, in Docket G002/GR-09-1153, Xcel was authorized to increase its revenues by approximately $7.3 million, an increase of only 1.2 percent. Xcel's request to increase revenues by $14.9 million outside of a rate case, in comparison, far exceeds what is typically granted in a general rate case where a thorough review is conducted. It is also worth noting that Xcel is projecting that the GUI Rider revenue requirement will increase each year from approximately $20 million in 2016 to $36 million in 2019.[11] From the OAG's perspective, it would be unreasonable to

[11] Petition, Attachment M, page 1.

allow Xcel to raise its revenues by such a substantial amount without conducting the thorough review that occurs in rate case.

Additionally, the OAG disagrees with Xcel on the important question of whether that its deferred costs can even be included in the GUIC rider. The Commission explicitly stated in both of the deferred accounting dockets that the deferred costs would be subject to review and recovery in Xcel's "next general rate case."

Essentially, Xcel is seeking reconsideration of the two deferred accounting orders to allow it to recover deferred costs in its GUI rider rather than a general rate case. In Docket No. G002/M-10-422, the Commission emphasized the importance of allowing adequate review of deferred costs and consistent with that intent, required that Xcel file a summary of all costs at least 60 days before filing its next general rate case. The ordering paragraphs for this docket are as follows:

ORDER

1. The Commission authorizes the Company to use deferred accounting treatment for the external operating and maintenance costs incurred to implement the inspection and remediation plan submitted to the Minnesota Office of Pipeline Safety in response to that Office's Notice of Probable Violation following the natural gas explosion of February 1, 2010. This authorization applies to costs incurred on and after May 10, 2010.

2. The Company shall include as a separate item in the deferred account any revenues or savings that result from implementing the inspection and remediation plan.

3. Beginning January 30, 2011, the Company shall make an annual filing summarizing costs incurred and deferred under this order, using a format similar to the one used in Attachment C, attached to its petition.

4. The Company shall promptly file an update as a compliance filing in this docket if at any point costs deferred under this order exceed $3,500,000 on an annual basis.

5. At least 60 days before filing its next general rate case, the Company shall file a summary of all costs deferred under this order, using a format similar to the one used in Attachment C, attached to its petition.

6. In any future filing seeking rate recovery of costs deferred under this order, the Company shall include the following information:

   A. Justification for the outsourcing of any tasks required to implement the inspection and remediation plan.

   B. Details of the final resolution of the Notice of Probable Violation and the status of any proposed penalties.

   C. Discussion and explanation of any legal actions or settlements regarding the natural gas explosion that led to the Notice of Probable Violation.

   D. Discussion and analysis regarding any potential third-party recovery for the costs of the plan.

   E. Discussion, analysis, and documentation demonstrating that plan costs were prudent.

   F. Analysis of what it would have cost to conduct the plan over a ten-year period beginning in 2003.

7. This Order shall become effective immediately.[12]

The conditions imposed by the Commission for subsequent cost recovery specifically dictated that cost recovery consideration shall be conducted in Xcel's next rate case and requires extensive disclosures for the purpose of determining whether the deferred costs are recoverable.

Similarly, the Commission specifically required that Xcel seek recovery of deferred TIMP and DIMP costs authorized in Docket No. G002/M-12-248 in Xcel's next general rate case.

[12] Order Granting Deferred Accounting Treatment Subject to Conditions and Reporting Requirements, *In the Matter of the Petition of Northern States Power for Deferred Accounting Treatment of Costs Relating to Identifying and Eliminating Sewer/Natural Gas Line Conflicts*, Docket No. G002/M-10-422 (January 12, 2011).

The ordering paragraphs from this docket are as follows:

1. Approve Xcel's request for deferred accounting with the following conditions:

   a. Approve deferral of only TIMP and DIMP O&M costs that exceed what is recovered through current rates.

   b. Require the Company to justify any outsourcing of TIMP and DIMP tasks in the annual reports beginning March 1, 2013 and in the summary to be provided 60 days prior to Xcel's next general natural gas rate case.

   c. Approve the Company's implementation of deferred accounting to begin on March 21, 2012 without interest and to continue until the earlier of the time of the utility's next rate case, or March 20, 2015.

   d. Approve the Company's implementation of deferred accounting to begin on March 21, 2012 without interest and to continue until the earlier of the time of the utility's next rate case, or March 20, 2015.

   e. Require that Xcel Energy provide annual reports detailing the amounts deferred for future recovery beginning March 1, 2013.

   f. Require Xcel Energy to provide a filing with a summary of all deferred TIMP and DIMP costs in this same format 60 days prior to the Company's next general gas rate case. [NSP and Department recommendation]

   g. Xcel shall include in the initial filing in its next natural gas rate case, justification and supporting testimony regarding all deferred TIMP and DIMP costs for which it seeks rate recovery.

   h. The Commission notes that granting deferred accounting neither guarantees rate recovery nor creates a presumption of rate-recoverability; it merely reflects a Commission finding that the costs in question warrant deferral for consideration in a later rate-setting proceeding.[13]

Again, the Commission specifically dictated that cost recovery consideration would be conducted in Xcel's next general rate case.

[13] Order, *In the Matter of the Petition of Northern States Power Company for Approval of Deferred Accounting for Costs to Comply with Gas Pipeline Safety Programs*, Docket No. G002/M-12-248 (Jan. 28, 2013).

The purpose of a review of deferred costs, whether they are GUI costs or not, in a general rate case is that it allows sufficient time to conduct adequate discovery and provide testimony to justify recovery in rates. The deferred costs that Xcel seeks recovery for in its GUI Rider are substantial and were incurred over a number of years. Simply making annual compliance filings in each docket does not constitute the review that the Commission anticipated to determine cost recovery.

It is also unclear whether Xcel properly accounted for the deferred costs. Generally, deferral authorizations must reach a determination that costs for deferral are unusual and significant. A more in-depth review, in a rate case, would show whether Xcel is deferring normal O&M expenses as GUI expenses that are not incremental to normal O&M expenses. While TIMP and DIMP costs should be connected to the formal, documented and mandated programs, the activities themselves would also be considered normal operating repairs and maintenance without having the mandated programs in place. The fact that Xcel is subject to a federal mandate requiring that a formal safety program be established does not mean that Xcel was not already doing those types of safety inspection and maintenance activities that were treated as normal O&M expenses in the past.

The OAG also believes that Xcel could have requested rider recovery under the statute at the time that it had requested deferred accounting. The statute was initially enacted in 2005, with subsequent revisions in 2013. Xcel asserts that it could not have requested recovery of the TIMP and DIMP costs until the 2013 amendment, but given that Xcel did not even attempt to request recovery under the 2005 law it is, at least, unclear whether the recovery would have been allowed.

Regardless of the 2013 amendment, however, the OAG does not agree with Xcel that the revisions in 2013 triggered a substitution alternative to recover these deferred costs in a GUIC rider. The Commission's orders clearly indicated that the costs could be recovered in Xcel's "next general rate case." The standard for recovery of deferred costs is intentionally high and requires a comprehensive rate case review to determine whether the deferred costs are appropriate for recovery. Xcel chose to request deferral of costs in anticipation of a subsequent rate case to justify recovery. Xcel should not now be allowed to seek a less stringent cost recovery review.

For these reasons, the OAG recommends that the Commission deny Xcel's Rider Petition because the proposal would inappropriately increase revenues without an opportunity for a review of Xcel's total costs, including cost of capital,[14] and revenues under current rates which are likely much different than what was approved in Xcel's last rate case filed five years ago.

IV. IF THE COMMISSION APPROVES THE GUIC RIDER, IT SHOULD IMPOSE CONDITIONS TO PROTECT THE INTERESTS OF RATEPAYERS.

If the Commission approves some or all of the costs that Xcel proposes for rider recovery, the Commission should impose several conditions in order to protect the interests of ratepayers.

A. The Commission Should Update Xcel's Rate of Return for Any Costs Recovered through a GUIC Rider.

Xcel agreed with the Department's recommendation to use an adjusted rate of return from Xcel's last general rate case in Minnesota. The authorized return granted in that case was 8.28%, with a cost of equity of 10.09%. The Company and the Department agree that there

[14] A rate case proceeding would very likely reduce Xcel's overall cost of capital including debt and equity with the result that a lower rate of return applied to total rate base may offset the total the revenue requirement that Xcel is proposing for its GUI Rider proposal.

should be some adjustment to cost of debt for this filing, as Xcel's borrowing costs have decreased significantly since its 2009 general rate case. The adjustment, according to DOC, in the cost of debt brings the overall cost of capital down to 7.56%.[15]

The OAG supports an adjustment to the cost of capital for this rider proposal if it is approved, and agrees the cost of debt adjustment is appropriate and reasonable for this case. The OAG also believes that the Commission should consider adjusting Xcel's cost of equity for any rider recovery, as it has not been updated since the Company's last rate case. Xcel's authorized return on common equity in its last rate case was 10.09%, but the financial climate and experience of other gas utilities indicate that Xcel's cost of equity is likely lower in the present day.

The cost of equity for the other large gas utilities in Minnesota, CenterPoint Energy and MERC are considerably lower at 9.59%[16] and 9.34%[17] respectively. Both utilities were granted these authorized returns in 2013 rate cases. Given that Xcel has not had its return on equity adjusted for five years, and that the trend has been lower authorized returns on common equity for both gas and electric utilities in Minnesota since 2009, the OAG believes that the Commission should lower Xcel's authorized rate of return for this rider, should it decide to approve the rider.

It is reasonable for the Commission to consider reducing Xcel's cost of equity for any rider recovery because the cost of equity would have received a thorough review if Xcel had requested recovery of the costs through a rate case as it was ordered to do by the Commission. Without such a review to ensure that Xcel's cost of equity is reasonable, the Commission cannot

[15] Department Comments, at 20.
[16] Findings of Fact, Conclusions of Law, and Order, Docket No. 13-316 (June 9th, 2014) at 32.
[17] Findings of Fact, Conclusions of Law, and Order, Docket No. 13-617 (Order Pending).

be certain that the resulting rates are just and reasonable. Should the Commission decide to grant the rider, the OAG believes that the return on equity used in cost of capital calculations for this proceeding should fall between 9.34% and 9.59%, which would be representative of other authorized cost of equity for gas utilities in Minnesota. Using a 9.34% cost of equity would equate to a weighted cost of capital of 7.07% and a 9.59% cost of equity would equate to a 7.20% cost of capital, assuming the same capital structure and cost of debt as the Department proposed.

In the event that Xcel is allowed to forgo a rate case and generate recovery through a rider instead, it would also be concerning that the OAG, the Department, and the Commission would be denied the opportunity to assess rate of return requirements for Xcel's gas operations as a whole. Given that Xcel has not had a rate case since 2009, and rates of return for gas utilities have generally fallen since then, it would appear that Xcel benefits by not having its rate of return scrutinized in a new rate case. If Xcel were to return for a rate case in 2014 or 2015, the rate of return awarded would likely be in line with other gas utilities rates of return and costs of equity awarded in 2014. Given that the Commission established a rate base of roughly $438 million in Xcel's 2009 general rate case,[18] a drop in rate of return from 8.28% to 7.07% would reduce the required return by $5.3 million for Minnesota ratepayers. The Commission's decision regarding the return on equity is a significant variable in determining whether or not approving a GUIC rider is in the best interest of ratepayers.

[18] Findings of Fact, Conclusions of Law, and Order , Docket No. 09-1153 (Dec. 6, 2010) at 29.

B. Any Costs Recovered Through a GUIC Rider Should Use the Same Apportionment as Xcel's Last Rate Case.

In its Petition, Xcel seeks to apportion the costs of the GUIC rider based on the results of the CCOSS it conducted in its last rate case.[19] But in its last rate case, Xcel agreed to use a different apportionment than the one developed from its CCOSS. This apportionment schedule was agreed upon by the Department and the Company, and is detailed in DOC's Mr. Christopher Shaw's Direct Testimony.[20] Xcel has not presented any reason for using the results of its CCOSS rather than the apportionment that it agreed to, and that the Commission approved, in the last case. Given that Xcel expects to recover more than 60% of the costs in the rider from the residential class in 2015, and even more in 2016 and 2017, using the results of the CCOSS, rather than the apportionment that was agreed upon in the previous case, would place an unreasonable burden on the residential class.[21] The OAG recommends that any costs collected through the rider be collected using the apportionment that was ordered by the Commission in Xcel's last natural gas rate case.

Additionally, the OAG also has concerns related to the type of equipment being used in the DIMP and TMIP and its relation to revenue apportionment. The OAG would like to see the Company detail what size equipment is being replaced and what size of equipment is replacing it. If Xcel is taking this opportunity to increase the size of distribution and transmission infrastructure, there should be additional consideration and discussion about how to apportion the revenues. Any increase in size of distribution or transmission equipment would be solely

---

[19] Petition, at 23.
[20] Christopher Shaw Direct Testimony, *In the Matter of the Petition of Northern States Power Company for Authority to Increase Rates for Natural Gas Service in Minnesota*, Docket No. 09-1153, at 15, Table 2 (May 3, 2010).
[21] Filing, Attachment K, pages 2-3.

demand related, and the proposed revenue apportionment of rider revenue requirements would not be appropriate for that reason.

C. A GUIC Rider Should Only be Approved for 2015.

The GUIC rider, if approved, should sunset at some point when on-going TIMP and DIMP costs stabilize. If the Commission approves recovery of the GUIC costs through a rider, the rider should only be approved for 2015 and continued only if Xcel can demonstrate that its normalized costs for rider recovery cannot be fairly estimated and recovered in base rates.

IV. CONCLUSION

The OAG recommends that Xcel's GUI Rider Petition be denied. The statutory authorization for a GUI rider does not supersede the Commission's obligation to establish just and reasonable rates, and Xcel's proposal does not demonstrate that its cost recovery will establish just and reasonable rates.

If the Commission does approve a rider for GUI costs, the OAG recommends that deferred costs accumulated in Dockets Nos. G002/M-10-422 and G002/M-12-248 not be included for recovery in the rider. Rather than attempting to circumvent the standard practice for deferred accounting, Xcel should seek recovery of the deferred costs in its next rate case as the Commission ordered.

Additionally, if the Commission approves the GUIC rider it should attach conditions to protect the interests of ratepayers. First, the Commission should adjust the rate of return for any costs recovered through a GUIC rider as Xcel's cost of debt and equity has not been updated since its last rate case. Xcel should not be permitted to earn a higher return on any costs recovered through a rider than it would earn by requesting recovery in a rate case. Second, any costs recovered through a GUIC rider should be apportioned on the basis of the revenue apportionment used in Xcel's last rate case. Third, if the Commission approves a rider for GUI costs it should be limited in duration. The OAG recommends that the rider only be authorized for 2015 unless Xcel can demonstrate that an extension is warranted.

Dated: October 27, 2014

Respectfully submitted,

LORI SWANSON
Attorney General
State of Minnesota

s/ Ryan P. Barlow
Ryan P. Barlow
Assistant Attorney General
Atty. Reg. No. 0393534

445 Minnesota Street, Suite 1400
St. Paul, Minnesota 55101-2131
(651) 757-1473 (Voice)
(651) 297-7206 (TTY)
ryan.barlow@ag.state.mn.us

ATTORNEYS FOR OFFICE OF THE ATTORNEY GENERAL – ANTITRUST AND UTILITIES DIVISON