MINNESOTA DEPARTMENT OF COMMERCE

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May 18, 2017

Daniel P. Wolf
Executive Director
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
Saint Paul, Minnesota 55101-2147

RE: **Response Comments of the Minnesota Department of Commerce, Division of Energy Resources**
Docket No. G002/M-16-891

Dear Mr. Wolf:

Attached are the *Response Comments* of the Minnesota Department of Commerce, Division of Energy Resources (Department) in the following matter:

> In the Matter of the Petition of Northern States Power Company (Xcel), doing business as Xcel Energy, for Approval of a Gas Utilities Infrastructure Cost Rider True-up Report for 2016, Revenue Requirements for 2017, and Revised Adjustment Factors.

The Petition was filed on November 1, 2016 by:

> Amy Liberkowski
> Director, Regulatory Pricing and Analysis
> Xcel Energy
> 414 Nicollet Mall, 7th Floor
> Minneapolis, Minnesota 55401

Based on its review of the Company's *Petition* and *Reply Comments* and the Minnesota Office of the Attorney General, Residential Utilities and Anti-Trust Division's (OAG) *Comments*, the Department continues to recommend that the Minnesota Public Utilities Commission **allow Xcel to recover the costs of its GUIC Rider, with modifications.**

The Department is available to answer any questions that the Commission may have.

Sincerely,

/s/ ADAM J. HEINEN	/s/ JOHN KUNDERT
Rates Analyst	Financial Analyst
651-539-1825	651-539-1740

AJH/JK/lt
Attachment

MINNESOTA DEPARTMENT OF COMMERCE

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

COMMENTS OF THE MINNESOTA DEPARTMENT OF COMMERCE

DOCKET NO. G002/M-16-891

I. BACKGROUND

On November 1, 2016, Northern States Power Company, d/b/a Xcel Energy (Xcel or the Company) filed its *Petition* requesting approval of a GUIC Rider True-Up Report for 2016, revenue requirements for 2017, and revised adjustment factors.

The Minnesota Department of Commerce, Division of Energy Resources (Department) reviewed the *Petition* and filed *Comments* on March 1, 2017 detailing its conclusions and recommendations. The Department observed certain concerns with the Company's proposal including the assessment of costs for its Pipeline Data Project (PDP) and Xcel's proposed Rate of Return (ROR) on rate base for the Rider projects. These concerns led the Department to recommend adjustments to the Company's proposed level of Rider recovery. The Department also recommended that Xcel provide the following in *Reply Comments*:

- Updated schedules reflecting calculation of the GUIC rate based Company's sales forecast before calendar month and DSM adjustments; and
- A detailed analysis comparing the costs of procuring video inspection equipment at the outset of, and each subsequent year until the present, the sewer line inspection plan relative to the expected cost engaging contractors to complete this work.

The Minnesota Office of the Attorney General, Residential Utilities and Anti-Trust Division's (OAG) filed *Comments* on March 1, 2017 and *Reply Comments* on March 13, 2017 which raised concerns regarding the Company's proposed reporting metrics, proposed Rate of Return on Equity (ROE), cost recovery, and size of the GUIC.

Xcel provided responsive information in *Reply Comments*, and the Department provides its review of this information below. The Department also responds to topics raised by the OAG in its *Comments*.

II. THE DEPARTMENT'S ANALYSIS

A. RESPONSE TO XCEL'S REPLY COMMENTS

The Company provided extensive information in response to concerns and requests for clarification raised by the Department in its *Comments*. The Department discusses these responses separately below.

1. Sewer Conflict Inspection

The Department raised potential concerns with the Company's administration of its Sewer Conflict Inspection program; in particular, Xcel's use of outside contractors to perform the inspection work and the cost of this work relative to the Company undertaking it on its own. The Department requested that, given the length and cost associated with this program, Xcel should provide a comparative analysis of the cost of owning the inspection equipment relative to contracting with an outside vendor when the program began and in the years since the program began.

Xcel reiterated its response to Department Information Request No. 6, which stated that the Company did not perform a detailed cost/benefit analysis of the decision to outsource this work when it began. The Company further stated, and described in its original Petition for deferred accounting,[1] that the Company used a competitive bid process to minimize costs and to secure qualified service providers to perform the work associated with the program. In addition, Xcel renegotiated the contract in 2016 to ensure that costs were reasonable. Xcel noted that the Commission found the Company's approach reasonable at the time and approved the program and its accounting treatment. The Company concluded its support of its Sewer Line Mitigation program by explaining that the equipment associated with this program is specialized and that internalizing these costs would involve the training and creation of a new classification of union employees. Xcel also noted its willingness to prepare a cost study comparing contracting this work to internalizing it in its next GUIC Rider Petition.

The Department appreciates Xcel's detailed discussion of the Request for Proposal (RFP) process it used to select its contractors, and it is satisfied that the Company minimized contractor related costs. However, the information and discussion provided by Xcel in its *Reply Comments* do not alleviate or lessen the Department's concerns regarding its administration of the Sewer Line Mitigation program. Specifically, the Company failed to show that contracting for this work represents a reasonable cost to ratepayers relative to internalizing these functions. Without a cost comparison, as requested by the Department on two separate occasions in this proceeding, the Commission cannot determine whether Xcel appropriately minimized ratepayer costs regarding its decision to outsource this work. The Department also reviewed the Commission's January 12, 2011 *Order* in Docket No. G002/M-10-422 (10-422 Docket) and it appears that Xcel has not complied with this *Order* as it relates to outsourcing work. Specifically, Ordering Paragraph No. 6 stated:

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[1] Docket No. G002/M-10-422.

> 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

The Department reviewed the various annual compliance filings in the 10-422 Docket and observed that Xcel provided significant discussion about its minimization of costs associated with its contracting work but never analyzed whether its decision to contract for sewer line inspection represented a benefit to ratepayers relative to undertaking the work on its own. In other words, Xcel never provided an analysis showing that it completed this work at the lowest cost for ratepayers.

The Department appreciates Xcel's openness to conducting a cost/benefit analysis in its next GUIC filing; however, this commitment does not provide a solution to the issue of cost in this proceeding. Based on its review of previous 10-422 compliance filings and the current and prior GUIC filings, the Department does not believe that the Company has provided evidence that outsourcing sewer line inspection resulted in the least cost to ratepayers. As noted in its *Comments*, the Department understands the potential operating benefits of outsourcing this work, but the Department is troubled as to why Xcel never analyzed whether outsourcing this work was the most cost effective solution, especially given the requirements in the Commission's *Order* in the 10-422 Docket.

As noted in the Company's *Petition*, Xcel budgeted $3.5 million in project costs for its sewer line conflict investigation for 2017 and incurred $3.28 million in project costs for this program in 2016. Despite the lack of comparative analysis in past filings, the Department does not recommend that the Commission adjust prior recovered amounts for the sewer line mitigation program. However, the Department concludes that an adjustment to incurred costs for 2016 and projected costs for 2017 may be appropriate given the lack of support for outsourcing this work in this docket and in previous GUIC and deferred accounting dockets. The decision at hand is the size of this adjustment.

If internalizing these costs is less expensive than outsourcing this work, it is clear that Xcel will incur, and has incurred, some level of reasonable cost associated with these projects; however, the burden of proof is on the utility in this proceeding to show that accelerated recovery of costs through the GUIC Rider is reasonable. As noted in Minnesota Statute §216B.03, doubt must be resolved in favor of the ratepayer. Since Xcel has requested accelerated recovery of these costs and has been unwilling on multiple occasions to show that outsourcing this project is reasonable, relative to internalizing these costs, the Department recommends that the Commission require Xcel to remove Sewer Line project costs from the GUIC Rider. The Department also recommends that the Commission require the Company to provide a cost/benefit analysis in its initial *Petition* in future GUIC Rider filings if Xcel wishes to receive accelerated recovery of these costs on a going-forward basis.

2. *Software Costs*

In its *Comments*, the Department observed concerns with the Company's software costs in relation to Xcel's Pipeline Data Project (PDP). In particular, the Department observed two areas of concern with costs associated with the Company's PDP. First, the Department analyzed the Company's original contract for this work and noted that the contract was executed with all of Xcel's utility affiliates but the entirety of costs were assigned to Minnesota ratepayers. Xcel failed to provide evidence supporting its decision to assign costs solely to Minnesota ratepayers; therefore, the Department recommended that these costs be allocated based on the Xcel company jurisdictional allocator.

Second, the Department identified the presence of duplicative consulting services; in simple terms, Xcel hired consultants to review the work of the original consultant enlisted to undertake the PDP. According to the Company, this additional layer of review was related to quality assurance/quality control (QA/QC) which involved outside contractors, working in Xcel offices, who would review the PDP work before it was entered into the Company's Geographic Information Systems (GIS) software database. Based on these concerns, the Department recommended that QA/QC costs be removed from rider recovery and that remaining PDP costs be allocated on an Xcel operating company basis. In addition, since NSP-Minnesota includes North Dakota, South Dakota, and Minnesota, the Department further allocated these costs using the Company's Transmission Integrity Management Program (TIMP) allocator because Xcel was unable to substantiate that costs for this project occurred only in Minnesota.

The Company provided extensive response on this issue in *Reply Comments*. Regarding the contract being executed for all of Xcel's operating companies, the Company stated that this approach is a standard process at Xcel and is meant to expedite the contract process and avoid potential delays or additional costs. The Company further reiterated that all costs related strictly to work done in Minnesota and, as such, it was appropriate to assign all costs to Minnesota. In support of this assertion, Xcel provided work invoices and a map showing where PDP work was done.[2] As to the QA/QC costs, Xcel continued to conclude that these costs are recoverable through the GUIC. Specifically, the QA/QC contractors served as the primary point of contact for the PDP vendor if responses to questions were necessary. The QA/QC contractors worked as a liaison between the vendor and Xcel and were able to efficiently solve problems and establish a data acceptance and testing process. Xcel also stated that QA/QC inspection is an industry standard and a best practice at the Company and that this layer of review was critical to successful implementation of the PDP.

The Department reviewed the Company's additional discussion and information regarding the allocation of costs and continues to conclude that Xcel's proposed assignment of costs is unreasonable. Specifically, the invoices provided by the Company appear to contradict Xcel's claim that work was assigned solely to Minnesota. As noted in the Department's *Comments*, and in the Company's response to discovery,[3] Xcel stated that it used separate invoice numbers so that costs were assigned to the appropriate jurisdiction. The

[2] Xcel *Reply Comments* Attachment B, Attachment C, and Attachment C, Page 1.
[3] Department *Comments*, Page 14.

Department reviewed the invoices provided in *Reply Comments* and observed three significant issues.[4]

First, the Company included work orders with invoice numbers different than the two contracts previously provided in this record;[5] therefore, there is no way to determine which jurisdiction should be allocated these costs. Second, Xcel included work orders with invoice numbers that corresponded to its contract with Public Service Corporation of Colorado (PSCo). If that is the case, it is clear that those costs should be removed from the Minnesota jurisdiction. Third, it appears that some of the work orders included costs associated with projects different than the PDP. At a minimum, this information means that Xcel has logged costs in the incorrect project category or, more significantly, may have booked costs to the wrong jurisdiction. The invoices provided by Xcel do not support the reasonableness of allocating PDP costs strictly to the Minnesota jurisdiction and raise further questions regarding the reasonableness of the Company's proposed PDP costs.

On the topic of QA/QC costs, the Department continues to conclude that these costs are not appropriate for rider recovery. As noted in the Department's *Comments*, the Company already has an amount of professional services included in rate base. Xcel did not provide additional information in *Reply Comments* showing that these QA/QC costs are substantively different from professional service costs already recovered in base rates. In addition, the Department remains concerned that Xcel's internal staff is unable to verify or determine whether data from the original consultant is appropriate for inclusion in the Company's GIS data. The Department does not dispute that quality control is an industry standard and agrees, at least conceptually, that having quality and review standards are important and necessary. However, the Company's application of this standard is inappropriate and not in the interest of ratepayers. Based on the information in this record, Xcel used two layers of consulting which was duplicative and inappropriate for recovery through the GUIC rider.

3. Sales Forecast

The Company forecasted sales in its initial *Petition* to determine the GUIC rates, on a per therm basis, that it will charge ratepayers. The Department analyzed Xcel's forecasting methodology and observed certain deficiencies in the analysis. In particular, the Department discussed two forecasting issues in its *Comments*; 1) the Company's monthly allocation adjustment; and 2) Xcel's Demand Side Management (DSM) adjustment. The Department provided extensive discussion of why these adjustments are inappropriate and call into question the reasonableness of the Company's forecasting approach. To correct these issues, the Department recommended that Xcel provide, in *Reply Comments*, updated GUIC factors based on the Company's sales forecast figures without the monthly allocation and DSM adjustments.

Xcel provided illustrative schedules in its *Reply Comments*.[6] The Company stated that the Department's methodology results in 0.17 percent lower sales than Xcel's forecast over the

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[4] Xcel *Reply Comments*, Attachment B and C.
[5] Department **Trade Secret** *Comments*, Attachment 5.
[6] Xcel *Reply Comments*, Attachments E and F.

proposed recovery period, which could cause a slight increase in the average GUIC rate rider. Xcel also responded to each of the concerns raised by the Department. First, in terms of the monthly allocation, the Company stated that the adjustment is meant to better align forecasted sales with historical actual sales, and the adjustment is done in a manner that ensures that the annual sales for a given calendar year remain unchanged. The Company noted that, while the adjustments are constrained so that annual sales remain unchanged, when a different time period is considered, the adjustments may have a small impact on sales. The Company concluded its discussion by stating that it believes it is appropriate to produce an accurate monthly forecast, so Xcel disagrees with the Department's recommendation.

Second, Xcel responded to the Department's recommendations regarding the DSM adjustment. The Company disagreed with the Department's recommendation to remove the DSM adjustment. The Company responded that no evidence has been presented in this proceeding or any other proceeding that the inclusion of a gas DSM adjustment double-counts DSM. Further, the Company explained that the DSM adjustment is calculated in a manner to avoid double counting and the forecast is only adjusted by the amount of expected future DSM less than the amount of embedded DSM. Xcel also stated that the DSM adjustment is an addition to sales, and DSM-adjusted sales are higher than unadjusted sales.

Xcel's statement that no evidence has been presented in a regulatory record that a DSM adjustment double-counts DSM is misleading. Xcel Electric has previously proposed a DSM adjustment in its electric utility general rates cases. Xcel Electric first proposed a DSM adjustment in its 2012 general rate case (Docket No. E002/GR-12-961). The Department filed extensive testimony on this topic and expressed concern that Xcel Electric's DSM adjustment over-corrected, or double counted, for embedded conservation already reflected in historical data. The Commission agreed with the Department's analysis and, in its *Order*, expressed doubt regarding the appropriateness of a DSM adjustment and set rates based on unadjusted sales (Department Attachment R-1). Xcel Electric also proposed a DSM adjustment its 2013 electric rate case (Docket No. E002/GR-13-868). The Department again filed testimony expressing concern with this adjustment and rates were ultimately set without the inclusion of a DSM adjustment.[7]

The Department's position regarding a DSM adjustment to sales is consistent and has been clear in recent general rate case proceeding. Although, as noted by the Company in its *Reply Comments*, the Department's recommended sales without the DSM adjustment are lower (thus resulting in higher rates), the Department continues to conclude that inclusion of a DSM adjustment is unnecessary. The Department provided significant discussion on this topic in other regulatory proceedings and believes that the decision to calculate rates based on DSM adjusted sales is best analyzed within a general rate case and not an annual rider filing. Thus, the Department recommends that the Commission use the sales figures provided in Attachments E and F of the Company's *Reply Comments* in setting rates.

[7] Xcel Electric also included a DSM adjustment in its sales forecast for its 2015 general rate case (Docket No. E002/GR-15-826).

4. *Proration of Accumulated Deferred Income Taxes (ADIT)*

In the Department's March 1, 2017 *Comments*, the Department provided background on this issue concerning the Internal Revenue Service (IRS) and concluded:

> Since the current petition involves the use of a rider with forecasted figures, the Department notes that Xcel's forthcoming [Private Letter Ruling] PLR for its 2015 TCR Rider could be used as a guide on how to treat the prorated ADIT issue in the instant proceeding. In the meantime, the Department recommends that the Commission approve Xcel's proposed ADIT proration for the forecasted year in the instant petition, subject to a true-up calculation in the following year using actual non-prorated ADIT amounts.

In support of the recommendation above, the Department notes that in a recent PLR issued by the IRS responding to an investor-owned regulated utility request, the IRS ruled that the utility's Rider True-Up of a now-historical test period, was not subject to the ADIT proration requirement.[8]

Alternatively, the Commission could decide to use only historical test-year periods to avoid the issue of proration of ADIT all together.

B. RESPONSE TO THE OAG'S COMMENTS AND REPLY COMMENTS

The OAG filed *Comments* and *Reply Comments* responding to the Company's GUIC rider request. The OAG's comments focused primarily on the Company's proposed reporting requirements and the appropriate ROE. The OAG also commented on the reasonableness of certain costs incurred by Xcel and proposed a cap on revenue. The Department responds separately to the reasonableness of cost discussion and reporting requirements in this section and to the ROE discussion in Section IV below. The Department does not take a position at this time on the merits of a revenue cap.

1. *Size of the GUIC Rider and Reasonableness of Certain Costs*

In its *Comments*, the OAG provided extensive discussion and expressed concerns regarding the growth in the size of the GUIC Rider relative to base rates approved in Xcel's most recent rate case. In particular, the OAG noted the open-ended nature of the GUIC Rider and the lack of restrictions within the GUIC Statute as to what type of pipes or material are eligible for GUIC recovery, as opposed to other states where these restrictions exist. The Department appreciates these observations, but their relevance is unclear given the wording of the GUIC Statute.

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[8] Internal Revenue Service PLR 201717008 released April 28, 2017.

The OAG also discussed the reasonableness of certain costs and noted that the GUIC Statute provides for rider recovery if costs are not included in existing base rates. In particular, the OAG provided a discussion of Xcel's recovery of costs associated with the replacement of distribution valves, which is a Distribution Integrity Management Project (DIMP). The OAG stated that this project will involve approximately $1 million in costs and is meant to replace existing distribution system isolation valves that have outlived their useful lifespan. The OAG issued addition discovery, and the Company responded that it would have replaced these valves without the GUIC Rider but that the pace and magnitude was changed.[9] The OAG also explained that the Company provided no information on the historical, baseline replacement level and spending that is included in existing base rates. The OAG concluded that the Company has not provided sufficient detail to demonstrate both that Xcel is only seeking recovery for incremental, accelerated replacement of distribution valves, nor that the rate of acceleration is reasonable.

The Department agrees with the OAG's analysis and conclusions regarding the Company's proposed distribution valve replacement costs. The Department reviewed Xcel's response to OAG discovery, and it is clear that the Company included some level of costs for distribution valve replacement in base rates set in its last rate case. The OAG correctly noted that if Xcel is unable to quantify the amount of costs originally included in base rates, the Commission cannot determine what, if any, amount of distribution valve replacement is marginal and eligible for GUIC rider recovery. As noted earlier, Minnesota Statute §216B.03 requires that any doubt must be resolved in favor of ratepayers. Since Xcel has not shown in this record that distribution valve replacement costs are marginal, and not included in currently approved base rates, the Department recommends that the Commission find these costs to be ineligible for GUIC rider recovery. This recommendation results in a $0.72 million ($720,000) decrease in proposed GUIC recovery for 2017.

2. Reporting Requirements

In its August 18, 2016 *Order* in last year's GUIC filing (Docket No. G002/M-15-808), the Commission required Xcel to develop metrics and reporting requirements to analyze the appropriateness of the Company's GUIC expenditures. Xcel presented its proposed metrics to various parties, including the Department and OAG, on November 16, 2016, and the Company filed its proposed metrics in a supplemental filing on January 13, 2017. Xcel noted in its *Reply Comments* that, after discussions with stakeholders, the Company is in the process of seeking input from other utilities on performance metrics through the American Gas Association's SOS forum. Xcel has not received the results of this outreach at this time.

The OAG raised several concerns regarding the Company's proposed reporting requirements. In particular, the OAG voiced concerns as to what information the reporting requirements would provide in terms of determining the reasonableness of costs and whether the proposed reporting requirements are in-line with methods used by other utilities.

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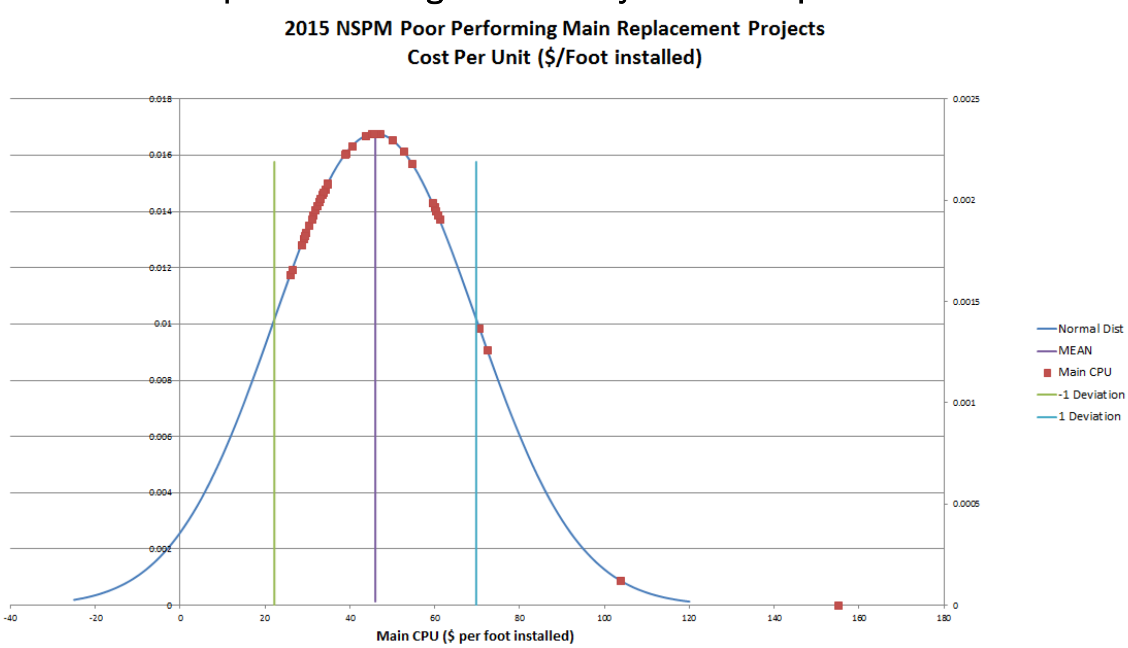
[9] Xcel response to OAG Information Request No. 45, Appendix A to OAG *Comments*.

The Department reviewed the Company's proposed reporting metrics and the concerns raised by the OAG. The proposed reporting metrics appear reasonable as a first step, but the Department identified issues with certain reporting metrics. In addition, the OAG raised important concerns that should be addressed prior to implementing standards. As noted above, the OAG voiced opposition for the proposed reporting metrics because they were unclear as to the benefit these metrics presented. The OAG appeared to express concern that the proposed metrics, in particular the use of the standard deviation, may not provide the Commission with meaningful information to determine whether costs were prudently incurred.

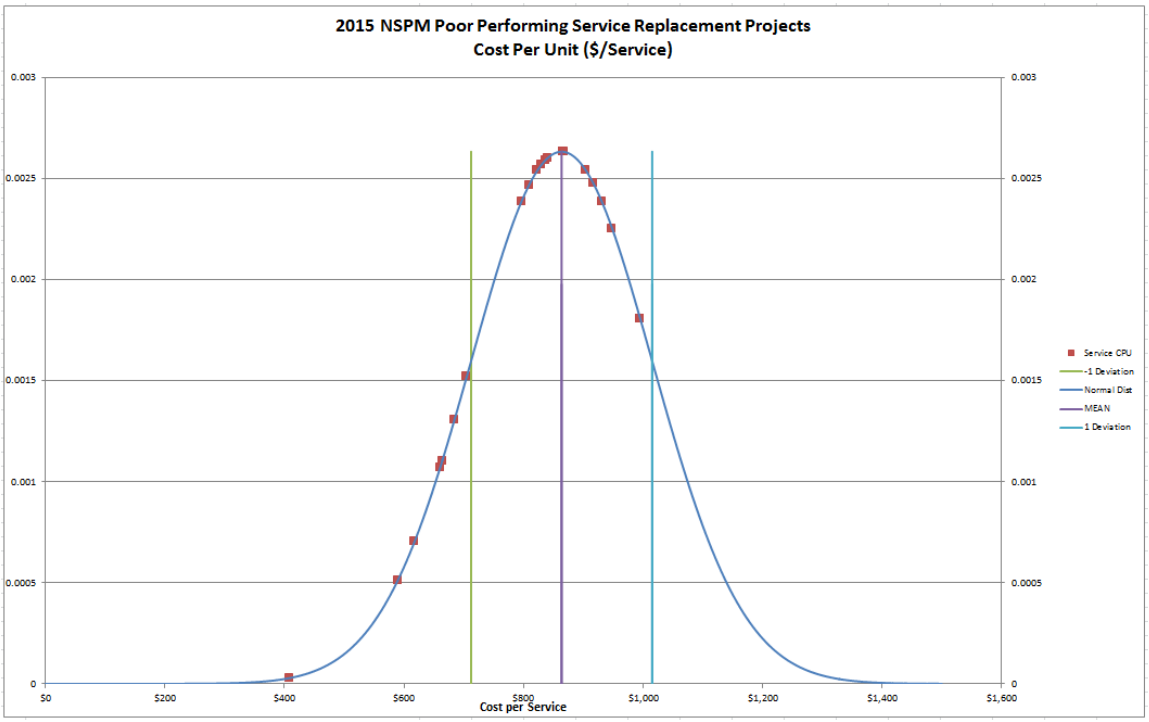
The Department does not necessarily oppose the type of data and use of the standard deviation for review proposed by Xcel, but after reviewing information provided by the Company, the Department believes the proposed method of review, specifically the standard deviation, is potentially flawed. As shown in Graphs 1 and 2 below, Xcel assumed a normal distribution for its data.

Graph 1: DIMP Program Efficiency—Main Cost per Foot[10]



[10] Xcel *Supplemental Filing*, Attachment A, Page 33.

Graph 2: DIMP Program Efficiency—Service Cost per Service[11]



The Company's assumption of a normal distribution is not necessarily correct and, depending on the prevailing data, may result in the wrong data being included in a future analysis of unusual costs. The Department does not necessarily oppose the use of the standard deviation, or a different statistical guideline, to determine unusual circumstances, but Xcel must ensure that it uses the appropriate distribution to filter these unusual data points. The data shown in Graphs 1 and 2 above appear skewed, and it is unclear if the Company's assumption of normal distribution is appropriate. The Department recommends that if Xcel wishes to use the standard deviation as a test metric it needs to show statistically that its data are normally distributed. If its data are not normally distributed, it is the Company's burden to show why the standard deviation, or some other statistical method, is an appropriate screen for unusual data points. Without this additional proof, the metric proposed by Xcel is not valid because the Commission cannot conclude that various data points are in fact abnormal and require additional analysis.

The OAG also recommended a workgroup of all regulated natural gas utilities to aid in the constructing of standard reporting metrics. The Department does not necessarily oppose this approach, but it does make the following observations. First, Xcel is currently the only regulated Minnesota gas utility with an approved GUIC rider.[12] Other gas utilities in the state are undertaking comparable GUIC but they are recovered, and have been recovered,

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[11] *Id.*, Page 34.
[12] Great Plains Natural Gas Company has proposed a GUIC rider in a pending filing (Docket No. G004/M-16-1066).

through the “standard” rate making process. Given the different cost recovery mechanisms employed across the various utilities, it is unclear whether standardized reporting metrics are appropriate. Second, each individual gas utility has different operating and system characteristics, which may make a single set of reporting metrics difficult to develop and administer. The Department, however, would be willing to join in further examination of this topic and, perhaps, seeing some level of standardization if applicable, if the Commission wishes to move in this direction.

As noted above, the Company is currently awaiting responses from other natural gas utilities through the American Gas Association SOS forum. Xcel’s proposed reporting metrics may be reasonable, but, absent the results of the AGA survey, it is unclear if the Company’s proposed metrics are comparable to industry standards or represent the best method to analyze the reasonableness of Xcel’s GUIC rider recovery. The Department recommends that the Commission, at a minimum, withhold its decision on the reasonableness of reporting metrics until the Company receives responses from the American Gas Association SOS forum. In addition, the Department recommends that Xcel provide, in this record, responses from the American Gas Association SOS forum as soon as they are available.

IV. DEPARTMENT COST OF CAPITAL DISCUSSION

The Company continues to support its proposed rate of 7.26 percent. Xcel correctly noted that the Department did not dispute the continuation of the use of the capital structure adopted in Docket No. G002/M-15-808. Also, the Department agrees with Xcel’s proposed costs of short- and long-term debt the Company has proposed. The remaining issue pertains to the Company return on equity (ROE).

Xcel did not update any of the cost of equity information developed using the different models used by its consultant to estimate the Company’s return on equity in its Reply Comments. The Company reiterated its position that a 9.50 percent return on equity was appropriate. Xcel also noted that its proposed 9.50 percent return on equity fell within the range of ROE’s the Department identified in its Comments. The Company also posited, but did not support, a statement that the average authorized ROE for natural gas utilities over the past few months was 9.53 percent. Moreover, without having the facts and relevant law of such proceedings available, such information is not comparable to the situation in this proceeding.

The Department continues to support the 9.04 percent ROE it calculated in its Comments. The Department used the same approach in the instant docket to develop its ROE estimate as it had in Xcel’s 2015 GUIC Rider filing, (Docket No. G002/M-15-808). The Commission appears to have found this approach to be reasonable. In its *Order* dated August 16, 2016 the Commission stated at page 8:

> For the cost of equity, the Commission finds the Department’s analysis persuasive and thorough, is persuaded that the Department’s recommendation relied on the most

> representative proxy group composition and agrees that a 9.64 return best reflects the Company's cost of equity for these rider calculations.

As for the Company's discussion regarding its 9.50 percent estimate falling within the Department's range of values for the cost of equity, the Department notes that the selection of a value above the mean average cost of equity developed increases the probability that the Commission approved ROE falls above the Company's actual ROE. A statistical example may help illustrate this point. If one assumes that the cost of equity developed using the Department's approach is normally distributed and the standard deviation is equal to the average of the two standard deviations for the mean average estimates for the Department Proxy Groups, the probabilities associated with Xcel approach would be the following:

Table 1: Department ROE Probability Analysis

Range	Probability
Department Mean high estimate(less than 10.79%)	0.997
Xcel's recommended ROE (less than 9.50%)	0.762
Department's Mean average estimate (less than 9.04%)	0.500
Greater than Xcel proposed ROE (9.50%)	0.238
Between Department's and Xcel's proposed ROE's (9.04% and 9.50%)	0.262

This example suggests that approval of an ROE of 9.50 percent would be higher than Xcel's cost of equity over 75 percent of the time. The Department would not consider that level of probability to provide for an equitable outcome to ratepayers and continues to recommend that the Commission adopt its proposed 9.04 percent estimate for Xcel's return on equity for this proceeding.

The OAG also provided a recommendation regarding the appropriate ROE for Xcel's GUIC rider for 2017. The OAG recommended an ROE of 7.13 percent in its *Comments* and then lowered its recommended ROE to 7.00 percent in its *Reply Comments*. The OAG's recommended ROE is based on its multi-stage Discounted Cash Flow model. While the Department agrees with the OAG's analysis that the Commission has historically preferred the DCF approach for determining a utility's cost of equity, the Department does not agree that the OAG's multi-stage DCF model provides a reasonable estimate of the cost of equity for Xcel's Gas utility.[13]

The Department also continues to support the overall rate of return for Xcel's Gas utility of 7.02 percent it identified in its *Comments*.

[13] Department witness John P. Kundert reviewed the OAG's multi-stage DCF model in detail in his Rebuttal Testimony in Docket No. E017/GR-15-1033. The Department refers the reader to that discussion for additional support for its recommendation regarding the appropriate ROE for Xcel's Gas utility in this proceeding.

V. THE DEPARTMENT'S RECOMMENDATIONS

Based on its review of the Company's *Petition* and *Reply Comments* and *Comments* of the OAG, the Department continues to recommend that the Commission allow Xcel to recover the costs of its GUIC Rider, with modifications. Specifically, the Department recommends, in addition to the recommendations already noted in *Comments*, that the Commission:

- remove Xcel's Sewer Ling project costs, approximately $3.5 million per year, from the GUIC rider;
- require Xcel to provide a cost/benefit analysis in its initial *Petition* in future GUIC Rider filings if Xcel wishes to receive accelerated recovery of Sewer Line costs on a going forward basis;
- establish rates based on unadjusted sales provided in Attachment F of Xcel's *Reply Comments*;
- remove Xcel's proposed distribution valve replacement costs from the GUIC Rider since the Company has not shown that these costs are in addition to replacement costs already included in base rates; and
- withhold its decision on the reasonableness of reporting metrics until the Company receives response from the American Gas Association's SOS forum.

The Department also recommends that Xcel provide, in this record, responses from the American Gas Association SOS forum as soon as they are available.

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Ultimately the ALJ concluded that a five-year amortization period was too short. The ALJ then recommended amortizing the reserve surplus over the average service life of the plant—but acknowledging that countervailing considerations might justify a shorter period, she also suggested a 15-year period.

The Commission concurs that a five-year amortization period is too short, giving insufficient consideration to rate stability. But the Commission also finds that amortizing the surplus over the life of the plant would give insufficient consideration to issues of rate shock mitigation and intergenerational equity. While the ALJ suggested a 15-year amortization period, the Commission favors a period of roughly half that duration. Balancing the competing considerations, the Commission will direct Xcel to amortize the depreciation reserve surplus for its transmission, distribution, and general plant accounts over eight years.

2. Production Plant

Finally, the Commission concurs in the ALJ's recommendation regarding Xcel's production plant depreciation reserves, especially regarding Xcel's nuclear generating units. The preponderance of the evidence indicates that these reserves appropriately reflect the cost of production plant retirements, including interim retirements, as explained by Xcel and the Department. Because the Commission finds insufficient reason to conclude that this reserve has a surplus, the Commission will decline XLI's proposal for amortizing the surplus.

However, this decision is not intended to preclude continued monitoring and analysis. The Commission will direct the parties to explore this matter more fully in Xcel's next rate case.

IX. Sales Forecast

A. Introduction and Background

The Commission requires a reasonable test-year sales forecast as the foundation for determining just and reasonable rates. Test-year sales volumes are important factors in calculating a utility's revenue requirement, rate design, and conservation cost recovery charge because sales levels affect both revenues and expenses. Lower sales levels will normally result in higher rates since costs are spread over fewer units.

The Department expressed concern that Xcel's forecast underestimates test-year sales. It challenged Xcel's methodology based on four claims:

- Xcel underestimated its total number of customers;
- Xcel overestimated energy prices;
- Xcel improperly used a binary factor to account for the loss of two large industrial customers; and
- Xcel overadjusted for the effect of demand-side management (DSM).

The Department recommended modifications to address each of these issues. The ALJ accepted the Department's modifications with respect to the first three issues but found that a DSM adjustment was proper.

The Commission concurs in the ALJ's analysis of customer count, energy prices, and sales to large commercial and industrial customers and adopts the ALJ's findings and conclusions on those issues. However, the Commission respectfully disagrees with the ALJ's resolution of the DSM-adjustment issue, as discussed below.

B. Positions of the Parties

1. Xcel

Demand-side management, or DSM, refers to measures taken by a utility to reduce customer demand for energy, such as promoting the use of efficient appliances. Xcel argued that, without an adjustment to account for a recent upward trend in energy savings from DSM, its forecast will overestimate energy sales. Xcel calculated a DSM adjustment by taking the difference between the Company's expected DSM savings in 2013 and a five-year historical average (2007–2011).

2. The Department

The Department argued that a DSM adjustment would underestimate 2013 sales, harming ratepayers through the resulting higher rates. The Department maintained that a DSM adjustment is unnecessary because the past sales data on which Xcel's projections are based already reflect historical DSM levels. No additional adjustment is needed since Xcel expects its DSM savings to level off in the future.

C. Recommendation of the Administrative Law Judge

The ALJ found that Xcel's proposed adjustment risks double-counting some of the DSM savings already reflected in historical sales data. The ALJ recommended using a four-year average of DSM savings instead of Xcel's five-year average as a baseline for calculating a DSM adjustment.

The ALJ also recommended several requirements for Xcel's next rate-case filing to aid the Department's analysis of the sales forecast.

D. Commission Action

The Commission concurs with the Department that Xcel has not shown the reasonableness of a DSM adjustment in this case. A DSM adjustment would underestimate test-year sales for several reasons. First, historical DSM efforts are already reflected in the sales data used in the forecast. Second, data provided by the Department show that Xcel's yearly DSM savings are leveling off, rather than increasing. Finally, Xcel's sales forecast with the DSM adjustment is consistently lower than actual data for five out of the last six months of 2012. For these reasons, the Commission will adopt ALJ Finding 252, revised as follows:

> 252. As shown by the Department, <u>the Company has not proven the reasonableness of a DSM adjustment in this proceeding. The inclusion of a DSM adjustment will under-estimate test-year sales and should not be applied to the sales forecast in this proceeding.</u> ~~the best method of accounting for DSM related savings beyond the first year of a device's implementation, while avoiding an overestimation of the impact of these savings, is to use a four~~

~~year average to calculate embedded DSM. This approach would increase the sales forecast by 51.161 MWh or $3.0 million in revenue above the forecast resulting from the five-year average advocated by the Company.~~

Overall, the Commission finds that the Department's recommendations result in a sales forecast that is reasonable, well designed, and appropriate for ratemaking in this case. The Department's recommendations increase the test-year retail revenue by $26,163,000.

Finally, the Commission concurs with the ALJ's recommendations for improving the transparency of Xcel's sales forecast. The Commission will require Xcel to include the following items in its next rate case:

1. Forecasting data at least 30 days prior to the initial rate case filing;
2. A comparison to the forecast information in this docket and the Baseload Diversification Study filed on or around July 1, 2013;
3. Large industrial customer account data in a format that allows interested parties to readily access historical data for all customers;
4. A spreadsheet, with all links intact, identifying any data inconsistencies with the Company's raw weather data and any modifications made to the raw weather data;
5. A detailed step-by-step explanation as to how test year revenue was calculated and what commands should be changed if a party wishes to adjust test year sales, adjust customer counts or calculate revenue;
6. A detailed description of the changes the Company has made to simplify its test year revenue calculation so that persons outside of the Company may verify the accuracy of the calculation; and
7. A report on the meetings Company representatives have had, prior to filing, with interested parties to explain its revenue calculation process and to cooperatively discuss methods for streamlining the revenue calculation.

X. Residential and Small General Service Customer Charges

A. Introduction

The monthly customer charge is a fixed monthly charge assessed without regard to usage levels. It is designed to help recover fixed customer-related costs such as the cost of meters, service lines, meter reading, and billing

Xcel's current monthly customer charges are $7.11 for overhead residential customers, $9.11 for underground customers, and $8.61 for small general service customers. The average customer-related cost, according to the Company's revised Class Cost of Service Study (CCOSS), is $17.35 per month for a residential customer.

CERTIFICATE OF SERVICE

I, Linda Chavez, hereby certify that I have this day served copies of the following document on the attached list of persons by electronic filing, e-mail, or by depositing a true and correct copy thereof properly enveloped with postage paid in the United States Mail at St. Paul, Minnesota.

MINNESOTA DEPARTMENT OF COMMERCE – RESPONSE COMMENTS

Docket Nos. **G002/M-16-891**

Dated this **18th** day of **May, 2017**.

/s/Linda Chavez

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