

September 5, 2017

Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101

RE: **Comments of the Minnesota Department of Commerce, Division of Energy Resources**
Docket No. E002/D-14-761

Dear Mr. Wolf:

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

Northern States Power Company d/b/a Xcel Energy's Annual Informational Letter and Compliance Filing regarding its Nuclear Decommissioning Trust Fund.

The Letter was filed on April 3, 2017. The petitioner is:

Lisa H. Perkett
Principal Financial Consultant
Northern States Power Company d/b/a Xcel Energy
414 Nicollet Mall
Minneapolis, MN 55401

The Department recommends that the Minnesota Public Utilities Commission (Commission) require Xcel to **change the investment mix, and** is available to answer any questions the Commission may have.

Sincerely,

/s/ EILON AMIT
Statistical Analyst

EA/ja
Attachment



Before the Minnesota Public Utilities Commission

Comments of the Minnesota Department of Commerce Division of Energy Resources

Docket No. E002/D-14-761

I. BACKGROUND

On December 1, 2014, Northern States Power Company d/b/a Xcel Energy (Xcel or the Company) filed its 2016-2018 Triennial Nuclear Plant Decommissioning Accrual with the Minnesota Public Utilities Commission (Commission).

On April 1, 2015, the Minnesota Department of Commerce (Department) filed comments on Xcel's decommissioning filing raising concerns about Xcel's proposed Nuclear Decommissioning Trust (NDT, or Qualified Trust Fund, or Fund) investment portfolio mix.

On May 1, 2015, Xcel filed reply comments attempting to address the Department's concerns regarding Xcel's proposed investment portfolio mix. The concerns remained unresolved, as discussed in the Department's May 11, 2015 response comments.

On October 5, 2015, the Commission issued its *Order Approving Nuclear Decommissioning Study, Assumptions, and Annual Accrual, and Setting Filing Requirements*. In that Order, the Commission required the following:

In its next annual decommissioning filing, Xcel shall include possible benchmarks and methodologies for assessing annual performance of the Qualified Trust Fund. The filing must include, at a minimum, proposals for:

- a. Annual performance benchmarks.
- b. The date the Qualified Trust Fund's achieved returns will be measured against the benchmarks.
- c. The date Xcel will make a compliance filing comparing the Qualified Trust Fund's achieved returns to the benchmarks.

and a discussion of:

- d. The acceptable deviation level between the performance benchmarks and the Qualified Trust Fund's achieved returns. (For example: 100 basis points).
- e. The amount of any true-up, in collars, that falls outside of the acceptable band, if applicable.
- f. The date on which the true-up would take place.

On April 1, 2016, Xcel filed an Annual Informational Letter discussing, among other things, its investment policy and investment asset allocation.

On August 15, 2016, the Department issued Response Comments making various recommendations.

On August 25, 2016, Xcel Energy (Xcel or the Company) issued Reply Comments objecting to the Department's August 15 recommendations.

On September 6, 2016, the Department issued additional Reply Comments making the following recommendations:

1. Require Xcel to re-evaluate its investment mix with the purpose of reducing the Qualified Trust investment management fees and increasing the Qualified Trust annual return on its investment portfolio.
2. Require the Company to file for each year during the triennial period, the average annual return on the NDT portfolio and the return on each individual asset and compare the annual return on the portfolio to the annual return for the S&P 500, 10-year treasury bonds, and the portfolio demonstrated by the Department in Table 2 of its August 15, 2016 Comments.
3. Require the Company to adjust the accruals collected from its ratepayers in the next triennial period by an amount equal to the difference in achieved returns on the portfolio for the Qualified Trust presented in Table 2 of the Departments August 15, 2016 Comments, and the return on Xcel's selected investment portfolio in the event Xcel's selected portfolio falls more than 100 basis points lower than the Table 2 portfolio.

The above calculations should be based on the five-year period ending with the year prior to the next triennial filing. These calculations should be done for each consecutive triennial filing. If at any time under these calculation Xcel's portfolio return exceeds the Department's proposed benchmark by more than 100 basis points, the Company may use this excess against any future deficits in calculating the accrual required.

On February 27, 2017, the Commission issued an Order directing Xcel to re-evaluate its investment mix and retain outside expert. The Commission Order states:

C. Re-evaluation of Investments

Second, the Commission shares the Department's concerns about the low growth and high fees associated with the NDT's investments strategy. Consequently, the Commission will adopt the Department's recommendation to direct Xcel to re-evaluate the fund's investment strategy.

In addition, the Commission will direct Xcel to retain a third-party expert in long-term institutional investment strategies to also evaluate Xcel's investment strategy. This expert will analyze how the fund's assets could best be invested to ensure that the trust amasses sufficient funds to meet the decommissioning costs by the time they will have to be borne, and maximize the return from the investment consistent with the appropriate risk level. The expert will be charged with the duty of filing a report on his or her conclusions within six months.

By pursuing these two paths—acquiring objective information about alternative investment opportunities, as well as receiving more subjective recommendations of knowledgeable parties—the Commission will lay the foundation for making further decisions about the NDT in the future.

ORDER

1. Xcel shall include in its annual compliance filings in this docket the following information:

- A. the average annual return on –
- 1) the Nuclear Decommissioning Trust Fund (NDT) portfolio, including the return on each individual asset,
 - 2) the Standard & Poor’s 500 stock market index,
 - 3) 10-year treasury notes,
 - 4) other qualified nuclear decommissioning trust funds,
 - 5) any other benchmarks proposed by Northern States Power Company d/b/a Xcel Energy, or jointly by Xcel and the Minnesota Department of Commerce, and
 - 6) Vanguard Exchange-Traded Funds (ETFs) invested according to the Charles Schwab Moderately Aggressive Asset Allocation as set forth below:

Fund Name	Weight
Vanguard Large Cap ETF	45%
Vanguard Small Cap ETF	15%
Vanguard Total World Stock ETC	20%
Vanguard LT Corporate Bond ETF	20%

- B. calculated over the five-, ten-, and twenty-year periods ending in the calendar year preceding the filing.
2. Regarding the investment strategy of the NDT:
- A. Xcel shall re-evaluate its investment mix with the purpose of reducing the NDT’s investment management fees and increasing the annual return on its investment portfolio.
 - B. Xcel shall retain a third-party expert in long-term institutional investment strategies to evaluate Xcel’s investment strategy with respect to the NDT with a goal of assuring sufficient funding to meet the decommissioning obligations at the time they are expected to come due and maximize return from the investment consistent with the appropriate risk level. The expert shall file a report on the matter with the Commission within six months of this order.

3. This order shall become effective immediately.

On April 3, 2017, Xcel filed a Compliance Filing providing information on the Fund Composition and the Fund Performance.

On July 14, 2017, the Commission issued a *Notice of Comment Period* requesting comments on the following:

- Does Northern States Power Company's (Xcel's) April 3, 2017 compliance filing comply with the Commission's October 5, 2015 *Order Approving Nuclear Decommissioning Study, Assumptions, and Annual Accrual, and Setting Filing Requirements* and February 27, 2017 *Order Directing Xcel to Analyze Fund Investments and Retain Outside Expert*?
- Why is there such a large variance in income taxes paid by each nuclear facility's fund when compared to the income each fund generated?
- How does the Nuclear Decommissioning Trust's (NDT's) financial results compare against other benchmarks over time?

II. DEPARTMENT ANALYSIS AND RECOMMENDATIONS

A. COMPARISON OF NDT'S FINANCIAL RESULTS WITH OTHER BENCHMARKS

The Department appreciates that the Commission shares the Department's concerns about the low growth and high fees associated with the NDT's investments strategy. The required comparison of the NDT portfolio return with the Vanguard Exchange-Traded Funds (Order Point 1.A.6) appears to reflect support for a change in investment strategy. The Department notes, however, that the 80/20 percent composition was used by the Department to show that, based on various measures, the Fund has significantly underperformed various market portfolios.

The Department provided an in-depth analysis of the Fund's performance in its August 15, 2016 Response Comments and its September 6, 2016 Reply Comments, which demonstrated that the Fund significantly under-performed relative to various market indices. In particular, the Fund significantly under-performed in comparison to a diversified portfolio that consists of 45 percent large Cap ETF, 15 percent of small cap ETF, 20 percent international ETF and 20 percent fix income ETF (see Table 2 of the Department's Response Comments dated August 15, 2016).

This conclusion is confirmed by Xcel's Compliance Filing dated April 3, 2017. Xcel's filing shows that the five-year return for the Fund averaged 7.29 percent compared to 11.80 percent for the Department's proposed portfolio. Neither Xcel's Reply Comments dated August 25, 2016 nor Xcel's Compliance Filing dated April 3, 2017 provide any new analyses to show either that the Company's portfolio are reasonable or that the Department's conclusions and recommendations are invalid.

B. VARIANCE IN INCOME TAXES

As noted above, the Commission's Notice of Comment Period asked a question about why there is such a larger variance in income taxes paid by each nuclear facility's fund when compared to the income each fund generated.

On August 30, 2017, Xcel responded to this question raised by the Commission. Xcel reproduced Table 5, Market Value Change by Component for 2016, in its comments and provided two reasons for why the actual calculation of taxes will not align with the amounts on Table 5. First, taxes paid in 2016 are based on estimated earnings for each fund. Second, the income tax line on Table 5 includes both income tax expenses for the current year, as well as prior year tax refunds or remaining tax payment due for the previous year. Basically the prior-year refunds or payments can differ by unit/fund.

The Department reviewed Xcel's response and is generally satisfied with the income taxes reconciliation and related explanation. However, the Department recommends further information to support the 42.6 percent of 2016 estimated tax expense for Monticello. The Department notes that the nuclear decommissioning fund's federal income tax rate is a flat rate of 20% and Minnesota State's applicable corporate income tax rate is 9.8%, resulting in a total effective tax rate of approximately 27 to 28 percent. Xcel noted tax expenses for 2016 of 27% and 30.4% for Prairie Island Unit 1 and Prairie Island Unit 2, respectively, look more reasonable than the Monticello's 42.6% estimated tax expenses.

The Department also noted that on page 3 of Xcel's August 30, 2017 comments Xcel stated that it has requested some Private Letter Rulings in 2016. The Department recommends that the Commission require Xcel to provide these IRS 2016 Private Letter Rulings (PLRs) and explain the reason(s) for these PLRs.

Finally, the Department is concerned that, since income taxes for decommissioning funds are stand-alone and the incomes taxes are deducted from the decommissioning fund, it does not appear to be reasonable for decommissioning costs that are included in rate cases to be grossed up for tax purposes. The Department recommends that the Commission require Xcel

to explain this concern about possible double income tax recovery related to nuclear decommissioning and indicate how the Company will address this issue.

III. SUMMARY AND CONCLUSIONS

1. *Summary*

Based on its review and analysis of Xcel's filing in these and previous comments, the Department concludes the following:

- a. Over the last 20-year, 10-year, and 5-year periods, Xcel's NDT failed to provide competitive returns when compared to well-diversified portfolios.
- b. While Xcel's portfolio is based on financial theory, the ultimate test of the theory is how it actually performs over the long run. Xcel's investment portfolio failed this ultimate test.
- c. Xcel's low Sharpe ratio (a measure of return per unit of risk) indicates the inefficiency of Xcel's portfolio compared to the Sharpe ratio for the Department's portfolio.
- d. Using a forward-looking approach, the Department's portfolio results in a higher return than Xcel's portfolio. Such higher returns could save ratepayers over \$5 million per year.
- e. Xcel's April 3, 2017 compliance filing complies with the Commission's October 5, 2015 Order Approving Nuclear Decommission Study, but does not demonstrate that the Company's portfolio is reasonable.

2. *Recommendation Regarding the Qualified Trust Investment Mix*

The Department recommends that the Commission continue to:

- a. Require Xcel to re-evaluate its investment mix with the purpose of reducing the Qualified Trust investment management fees and increasing the Qualified Trust annual return on its investment portfolio.
- b. Require the Company to file for each year during the triennial period, the average annual return on the NDT portfolio and the return on each individual asset and

compare the annual return on the portfolio to the annual return for the S&P 500, 10-year treasury bonds, and the portfolio demonstrated by the Department in Table 2 of its August 15, 2016 Comments

- c. Require Xcel to use the portfolio in Table 2 of the Department's August 15, 2016 Comments as a benchmark to measure the Fund performance.
- d. Require the Company to adjust the accruals collected from its ratepayers in the next triennial period by an amount equal to the difference in achieved returns on the portfolio for the Qualified Trust presented in Table 2 of the Department's August 15, 2016 Comments, and the return on Xcel's selected investment portfolio in the event Xcel's selected portfolio falls more than 100 basis points lower than the Table 2 portfolio. This requirement should be implemented on a going-forward period based on a date to be decided by the Commission.

3. *Variance in Income Taxes*

The Department recommends that Xcel address the following in its reply comments:

- a. Further information to support the 42.6 percent of 2016 estimated tax expense for Monticello.
- b. Copies of the IRS 2016 Private Letter Rulings (PLRs) and explain the reason(s) for these PLRs.
- c. Address the concern about possible double-recovery of income taxes related to nuclear decommissioning.

/ja

CERTIFICATE OF SERVICE

I, Sharon Ferguson, hereby certify that I have this day, served copies of the following document on the attached list of persons by electronic filing, certified mail, 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
Comments**

Docket No. E002/D-14-761

Dated this 5th day of September 2017

/s/Sharon Ferguson

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