Minnesota Public Utilities Commission
Staff Briefing Papers

Meeting Date: November 19**,** 2015 .... **Agenda Item # **9**

Company: Northern States Power Company, d/b/a Xcel Energy

Docket No. G-002/M-15-194

In the Matter of the Petition for Approval of a Modification to the Natural Gas State Energy Policy (SEP) Tariff Rate, 2015 Project Eligibility, 2015 SEP Adjustment Factor, and 2014 SEP Compliance Filing.

Issue(s): Should the Commission approve the proposed 2015-2016 natural gas SEP Rate Rider rate factor?

Should the Commission approve Xcel's 2014 Annual SEP compliance filing, and its proposed Customer Notice and Tariff update?

Should the Commission require Xcel to develop and submit to the Commission a more refined cost estimate and project plan for implementation of a voluntary carbon dioxide and greenhouse gas program for the emissions avoided as a result of the cast iron main replacement activities included in the SEP within 90 days of the Commission's Order?

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Relevant Documents

Xcel Filing.. March 2, 2015
Department Comments ....May 1, 2015
Xcel Reply Comments...May 26, 2015
Department Supplemental Comments ....June 19, 2015

The attached materials are workpapers of the Commission Staff. They are intended for use by the Public Utilities Commission and are based upon information already in the record unless otherwise noted.

November 12, 2015

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Statement of the Issue

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Background and Party Positions

Xcel

On March 2, 2015, Xcel filed its petition requesting approval of its 2015 natural gas State Energy Policy (SEP) Rider rate factor, its 2014 Annual SEP compliance filing, and its proposed Customer Notice and Tariff update. The Company proposed a 2015 natural gas SEP rate factor of $0.001898 per therm for the recovery of $1,817,833 for the 12 month period of July 2015 – June 2016.

Xcel stated that there are three types of expenses currently included for recovery in the SEP Rider: Reliability Administrator, Sustainable Building Guidelines and Greenhouse Gas Infrastructure Costs. The estimated true-up amount from the 2014-2015 SEP Tracker is $(44,883). The primary driver of the true-up is the negative carryover from the 2013-2014 SEP period due to higher collected revenues than forecast.

The Company stated it has not sold any carbon offsets or credits for greenhouse gas emissions associated with the natural gas Cast Iron Pipe Replacement project under the SEP Rider to-date. As a result, there are no carbon offsets and/or credits to report, or proceeds to credit to the SEP Rider tracker account.

Department

On May 1, 2015, the Department filed comments requesting additional information.

The Department recommended that the Reliability Administrator (RA) expenses not be included in the proposed 2015 Natural Gas SEP rider rate because the legislative basis for the inclusion of those costs is scheduled to lapse on June 30, 2015. The Department stated that it is its understanding that language that would extend the Department's authority to recover RA costs through the SEP is contained in proposed legislation currently before the Legislature.

The Department did not have any concerns about the costs related to the cast iron pipe replacement.

According to the Department, in 2008 when it made the recommendation to require reporting the sale of any carbon offset or credit for decreased greenhouse gas emissions associated with gas pipe replacement under the Project, the United States Congress was considering the possibility of implementing a carbon tax. The Department assumed that if the Congress implemented a carbon tax, the EPA would be tasked with implementing some sort of regulatory carbon market. One could also assume that the EPA would award Xcel some level of carbon allowances or credits that would also have some nominal value if that proposed legislation had become law.

The bill that included a carbon tax did not become law. To the Department's knowledge, no other attempt has been made to implement a carbon tax since that effort.

As a result, the Department concluded that the Commission's requirements regarding carbon offsets are not consistent with the current regulatory reality. The inconsistency could be removed by the Commission rescinding those reporting requirements. Another option would be for Xcel to register the project and the carbon reductions on an established carbon registry. The Department requested that Xcel discuss this option in its reply comments in this proceeding.

During the course of the Department's review of the Company's rate calculation, it noted that the forecasts for monthly revenue were much higher than the actuals. According to Xcel's IR response, in early 2015 it discovered that the natural gas SEP adjustment factor is applied to Interdepartmental Gas Sales through a manual billing process. The Interdepartmental Sales are included in the sales forecast to calculate the SEP adjustment factor; however, because of the manual nature of the billing process, the revenues collected under the SEP adjustment factor for Interdepartmental Sales had been inadvertently excluded from total actual revenues reported in the SEP tracker.

According to Xcel the Interdepartmental Sales discrepancy impacts all of its riders on a small level, though the discrepancy is greatest within the natural gas SEP tracker due to its inclusion of gas Generation Transport. The Company stated it was in the process of quantifying the difference for the SEP Rider and all riders and would update the Department by the end of May.

Recommendations

The Department stated it doesn't have the information necessary to make a recommendation regarding the natural gas SEP rider rate at this time. Once Xcel has filed the additional information that it indicated in its response to DOC information request No. 2 that it would provide, the Department will file additional comments that provide a recommendation.

Xcel Reply Comments

On May 26, 2015, Xcel filed reply comments addressing the Department's questions.

The Company stated that Interdepartmental Sales are included in the sales forecast to calculate the SEP adjustment factor and the SEP adjustment factor was correctly applied to Interdepartmental billed sales; however, because of the manual nature of the billing process, the revenues collected under the SEP adjustment factor for Interdepartmental Sales have been inadvertently excluded from total actual revenues reported in the SEP tracker.

Xcel made a one-time adjustment of $1.124 million to correct for the underreported revenues in its gas SEP tracker. Reflecting the adjustment, Xcel proposed an updated 2015 natural gas SEP rate factor of $0.000724 per therm for the recovery of an adjusted revenue requirement of $693,437 for the 12 month period of July 2015 – June 2016.

The Company stated it participates in the voluntary EPA Natural GasStar program, and it reports CO2-equivalent emissions from the natural gas system annually to EPA under Subpart W of EPA's greenhouse gas reporting program.

According to Xcel, creating registered carbon offset credits from its cast iron pipe replacement activities would require several steps beyond its voluntary reporting to EPA:
1. Identify a carbon offset registry with an approved offset methodology or protocol to quantify methane reduction through pipe replacement in the gas distribution sector;
2. If no registry has such a methodology, secure approval of a methodology;
3. Apply that methodology, using data from the Company's own system, to quantify the CO2 equivalent greenhouse gas avoidance achieved by pipe replacement that reduces natural gas leakage;
4. Prepare and submit project documentation to the carbon offset registry identified in step 1; and
5. Secure third-party verification of its project and the claimed greenhouse gas reductions.

Successfully completing those steps would result in verified offset credits on a registry, but not any offset proceeds that could potentially be returned to customers or used for other purposes. That would require further steps:
6. Identify voluntary or compliance market demand for its cast iron pipe replacement carbon offset credits;
7. Sell the credits; and
8. Reach agreement

The Company considered the feasibility of these steps. Xcel argued that if it were to successfully conduct all of the above steps, including finding a voluntary market buyer for its carbon credits, which is not guaranteed, it could potentially secure on the order of $50,000 per year (11,000 tons CO2e * $4.50/ton). According to Xcel, the combined cost of all the steps could approach or exceed $50,000. Thus, net proceeds from the sale of offsets would be quite small, or negative.

Based on its analysis, the Company recommended:
1. That it not pursue creating, verifying and selling carbon offset credits from its cast iron pipe replacement activities, since the level of effort would be significant and the net proceeds that could be returned to customers would be small or negative.

2. The Company will continue reporting annually to EPA, under Subpart W of EPA's greenhouse gas reporting program, its CO2-equivalent emissions from the natural gas system.
3. The Company agreed with the Department that the Commission's requirements regarding carbon offsets are not consistent with the current regulatory reality, and proposed that the Commission rescind those reporting requirements.

Department Supplemental Comments

On June 19, 2015, the Department filed supplemental comments stating the following regarding Xcel's first recommendation. While the Department agreed that the net proceeds from an effort to create, verify and sell carbon offsets from Xcel's cast iron replacement activities will not be financially significant, the Department noted that requiring Xcel to pursue this activity would provide the Commission, the Department (State Regulatory Agencies) and other interested stakeholders with valuable experience and potentially valuable expertise. Xcel's development of a voluntary emissions program for carbon dioxide and greenhouse gases would allow the Company and the State Regulatory Agencies to explore the concept of greenhouse gas emissions markets in a concrete, albeit small-scale fashion. It may also provide the Company's ratepayers with an opportunity to recover a portion of the costs associated with Xcel's efforts to lower its carbon dioxide emissions on a broader scale.

The Department recommended that the Commission:

- Approve Xcel Energy's proposed 2015-2016 natural gas SEP adjustment factor of $0.000724/therm;
- Approve the Company's proposed customer notice included in the Petition, adjusted to incorporate the updated adjustment factor; and
- Require Xcel to develop and submit to the Commission a more refined cost estimate and project plan for implementation of a voluntary carbon dioxide and greenhouse gas program for the emissions avoided as a result of the cast iron main replacement activities included in the SEP within 90 days of the Commission's Order.

Staff Analysis

Xcel and the Department did not have any disagreement on the Xcel's 2014 SEP compliance filing. There also was no disagreement on the customer notice. The Department stated that other than a correct adjustment factor, Xcel Energy's proposed customer notice is consistent with the notice approved by the Commission in the Company's previous SEP Rider proceedings. Therefore, Xcel should be required to update the proposed notice to include the adjustment factor approved by the Commission.

SEP Factor

Xcel updated the adjustment factor to reflect the revised deficiency after adjusting for the Interdepartmental Sales error. Both the Company and the Department agreed on the factor of $0.000724 per therm for the 12 month period of July 2015 – June 2016. However, that factor was calculated using the forecasted sales volumes for that 12 month period.

Xcel requested that if actual implementation occurs after July 1, 2015, that the 2015 SEP Rider rate factor be adjusted to recover the approved program costs over the remaining months of the period, through June 30, 2016.

In past cases, the Commission has extended the recovery period if the factor for the remaining months was too large. According to Xcel, the updated factor would cost the average residential customer $0.64 per year. In this case, Staff does not believe it would be necessary to extend the recovery period. Assuming the change was implemented December 1, 2015, the costs would be recovered based on the sales volumes for December through June which should incorporate most of the annual sales volumes for a gas utility because that includes most of the heating season of November through March. The factor should only increase a small amount. Further, while the monthly recovery would increase slightly, the overall amount collected from the average residential customer for the seven month period would remain at $0.64.

Carbon Offsets

The Department proposed that Xcel submit a more refined cost estimate and project plan than the analysis the Company provided in its reply comments. The Department argued that requiring Xcel to pursue this activity would provide the Commission, the Department and other interested stakeholders with valuable experience and potentially valuable expertise. Xcel's development of a voluntary emissions program for carbon dioxide and greenhouse gases would allow the Company and the State Regulatory Agencies to explore the concept of greenhouse gas emissions markets in a concrete, albeit small-scale fashion. The issue for the Commission is to determine if the benefits gained from such a process would justify the time and costs for the Company, the Commission, the Department and other stakeholders. In addition, would the process provide experience and expertise that would be of value to the Commission? If the Commission believes that is the case, then it may wish to approve the Department's recommendation.

Decision Alternatives

SEP Compliance Filing

1. Approve the 2014 SEP compliance filing. (Xcel, DOC)

2. Do not approve the 2014 SEP compliance filing.

Customer Notice

3. Approve the proposed customer notice subject to it including the Commission approved rate factor. (Xcel, DOC)

4. Do not approve the proposed customer notice and require the Company to work with

Commission staff and CAO to develop the notice.

SEP Rate Factor

5. Allow the Company to recover the revenue requirement of $693,437 over the period of December 2015 through June 2016. Require Xcel to submit a compliance filing by November 30, 2015 providing the calculation of the updated factor and revised tariff sheet reflecting the updated factor. (Xcel)

6. Approve the proposed 2015-2016 natural gas SEP adjustment factor of $0.000724 per therm, and

7. Approve the proposed tariff sheet revised in a compliance filing to reflect the Commission approved SEP factor. (DOC)

Carbon Offset Credits

8. Do not require Xcel to pursue, at this time, creating, verifying and selling carbon offset credits from its cast iron pipe replacement activities, since the level of effort would be significant and the net proceeds that could be returned to customers would likely be small or negative and rescind the requirement that the Company to report and credit the SEP Tracker with any proceeds received from the sale of carbon offsets or credits associated with the Project. (Xcel)

9. Require Xcel to develop and submit to the Commission a more refined cost estimate and project plan for implementation of a voluntary carbon dioxide and greenhouse gas program for the emissions avoided as a result of the cast iron main replacement activities included in the SEP within 90 days of the Commission's Order. (DOC)