

# Minnesota Public Utilities Commission

## *Staff Briefing Papers*

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Meeting Date: July 1, 2015 ..... Agenda Item\* #3

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Company: Otter Tail Power Company (OTP)

Docket No. E-017/S-15-411

In the Matter of Otter Tail Power Company's Request for Approval of its  
2015 Capital Structure and Permission to Issue Securities

Issues: Should the Commission approve OTP's request to issue securities?

Should the Commission approve OTP's proposed capital structure?

Should the Commission approve OTP's proposed total capitalization?

Should the Commission grant OTP's request for a variance from Minn. Rule,  
pt. 7825.1000, Subp. 6?

Should the Commission require OTP to file additional information?

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### ***Relevant Documents***

Otter Tail Power - Initial Petition ..... May 1, 2015  
Department of Commerce (Department) - Comments ..... May 18, 2015  
Otter Tail Power - Reply Comments ..... May 28, 2015  
Department - Comments ..... June 3, 2015  
Otter Tail Power - Letter ..... June 8, 2015

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## ***Statement of the Issues***

Should the Commission approve OTP's proposed capital structure?

Should the Commission approve OTP's proposed total capitalization?

Should the Commission approve OTP's request to issue securities?

Should the Commission grant OTP's request for a variance from Minn. Rule, pt. 7825.1000, Subp. 6?

Should the Commission require OTP to file additional information?

## ***Relevant Statute***

Minn. Stat. § 216B.49, subd. 3:

It is unlawful for any public utility organized under the laws of this state to offer or sell any security or, if organized under the laws of any other state or foreign country, to subject property in this state to an encumbrance for the purpose of securing the payment of any indebtedness unless the security issuance of the public utility is first approved by the commission, either as an individual issuance or as one of multiple possible issuances approved in the course of a periodic proceeding reviewing the utility's proposed sources and uses of capital funds. Approval by the commission must be by formal written order.

Subd. 4 of the same statute states:

Upon the application of a public utility for approval of its security issuance and prior to the issuance of any security or the encumbrance of any property for the purpose of securing the payment of any indebtedness, the commission may make such inquiry or investigation, hold such hearings, and examine such witnesses, books, papers, documents, or contracts, as in its discretion it may deem necessary. Prior to approval the commission shall ascertain that the amount of securities of each class which any public utility may issue shall bear a reasonable proportion to each other and to the value of the property, due consideration being given to the nature of the business of the public utility, its credit and prospects, the possibility that the value of the property may change from time to time, the effect which the issue shall have upon the management and operation of the public utility, and other considerations which the commission as a matter of fact shall find to be relevant. If the commission shall find that the proposed security issuance is reasonable and proper and in the public interest and will not be detrimental to the interests of the consumers and patrons affected thereby, the commission shall by written order grant its permission for the proposed public financing.

## ***Background***

On May 1, 2015, OTP filed a petition for approval of its 2015 capital structure and soliciting permission to issue securities.

OTP solicited Commission approval of a common equity ratio of 52.1 percent, with a contingency range of 10 percent below the ratio and 10 percent above the ratio (46.95% to 57.3%)<sup>1</sup> such that any change in equity ratio that falls within this range, or outside it for a period not exceeding 60 days, does not require Commission approval.

The other 47.9 percent of the capital structure is proposed to consist of short- and long-term debt. OTP has proposed a short-term debt contingency cap of 15 percent of OTP's total capitalization (roughly \$144 million).<sup>2</sup> OTP has proposed that short term debt exceeding the contingency range for a period not exceeding 60 days would be authorized.

OTP also sought approval of a total capitalization of \$960,273,000, with a contingency cap of 10 percent above that amount, i.e., a total capitalization of \$1,056,300,000. As with the equity ratio, any contemplated securities issuance that would cause total capitalization to exceed the contingency cap for a period not exceeding 60 days would not require Commission approval.

OTP represented that the proposed capital structure contemplated capital expenditures relating to replacement and reliability of current infrastructure, an environmental project at OTP's Big Stone plant and anticipated expansion of transmission capacity in Minnesota (CAPX 2020) and South Dakota.

OTP is a wholly owned subsidiary of Otter Tail Corporation and OTP does not issue equity securities, but receives equity in the form of equity contributions from Otter Tail Corporation. OTP has assumed an infusion of \$46.5 million of equity from Otter Tail Corporation in 2015.

On May 18, 2015, the Department of Commerce (Department) filed detailed and substantive comments. The Department indicated that OTP has complied with the reporting requirements established in the Commission's Order in the 2014 OTP capital structure and securities issuance filing (Docket E-017/S-14-381). The Department recommended that the Commission approve OTP's proposed capital structure and request for issuance of securities and reiterated the adoption of the reporting requirements in the Commission's August 1, 2014 order in Docket E-017/S-14-381.

On May 28, 2015, OTP filed reply comments accepting the corrections made by the Department (see footnotes on this page). Along with these comments, OTP included a request for the variance from Minn. Rule, pt. 7825.1000, Subp. 6<sup>3</sup> to authorize OTP to treat borrowings under its current multi-year credit facility as "short term debt" as the term is defined in the rule. Otter

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<sup>1</sup> As correctly established by the Department in its May 18, 2015 Comments.

<sup>2</sup> OTP has miscalculated this figure as \$158 million. See p. 16 of OTP's initial filing. Also, see the Department's May 18, 2015 Comments, p. 4.

<sup>3</sup> This rule defines "short term security as "any unsecured security with a date of maturity of no more than one year from the date of issuance; and containing no provisions for automatic renewal or "roll over" at the option of either the obligee or obligor."

Tail indicated that its multi-year credit agreement, scheduled to terminate on October 29, 2019, first referenced in docket E-017/S-12-420, provides it with a \$170 million line of credit which OTP uses for short term working capital and for funding construction in progress. This agreement, OTP noted, has by definition a date of maturity exceeding one year, whereas Minn. Rules, pt. 7825.1000, Subp. 6 limits the maturity date of such securities to one year without provision for automatic renewal or roll over.

OTP argued that granting the request for variance was reasonable as enforcement of the rule would impose an excessive burden upon it; that granting the variance would not adversely affect the public interest; and that granting the variance would not conflict with the standards imposed by law.

On June 2, 2015, the Department filed comments recommending that the Commission grant OTP's request for a variance from Minn. Rules, pt. 7825.1000, Subp. 6.

On June 8, 2015, OTP filed comments requesting that the Commission issue an order consistent with the Department's recommendations regarding OTP's Petition for Approval of 2015 Capital Structure and Permission to Issue Securities.

## ***Summary of Party Positions***

### ***OTP's Petition***

In its request for approval of its proposed 2014 capital structure, OTP is seeking approval of:

- Total capitalization of \$960,273,000 with a contingency cap of 10 percent (or, rounded, \$1,056,300,000);
- An equity ratio of 52.1% with a contingency range of +/- 10%, (resulting in an equity range of (46.9% to 57.3%);
- A request for a variance of Minn. Rules, pt. 7825.1000, subp. 6 to allow the Company to treat borrowings under multi-year credit agreements as short-term debt for approved capital structure purposes;
- The ability to issue short-term debt not to exceed 15% of total capitalization;
- The flexibility to issue short term debt that exceeds the short term contingency range for a period not exceeding 60 days; and
- The flexibility to issue securities provided that the Company remains within the approved capital structure contingency range or does not fall outside the range for more than 60 days.

OTP indicated that it would seek approval from the Commission for any securities issuance as soon as the Company has reason to believe that any such issuance would cause the common equity ratio or total consolidated capitalization to fall outside the approved contingency ranges

for more than 60 days.

## ***Department of Commerce***

The Department's detailed analysis is not repeated in these briefing papers.

In summary, the Department indicated that OTP is in compliance with the reporting requirements contained in the Commission's August 1, 2014 order in Docket E-017/S-14-381; that OTP's proposed range for common equity, the 15-percent contingency for short-term debt, and the total capitalization, including the 10-percent contingency, were reasonable.

The Department also found OTP's request for a variance from Minnesota Rules, pt. 7825.1000, subp. 6 met the three-part test in Minn. Rules, pt. 7829.3200, which states that:

The commission shall grant a variance to its rules when it determines that the following requirements are met:

- A. enforcement of the rule would impose an excessive burden upon the applicant or others affected by the rule;
- B. granting the variance would not adversely affect the public interest; and
- C. granting the variance would not conflict with standards imposed by law.

Based on its review and analysis, the Department recommended the following:

1. Approve OTP's requested capital structure; this approval to be in effect until the 2016 capital structure Order is issued. OTP shall file its next securities issuance petition no later than May, 2016.
2. Approve OTP's equity ratio of 52.1 percent and a contingency range of minus/plus 10 percent around the approved equity ratio (46.9% to 57.3%). Equity ratios outside this range may not exceed a period of 60 days without prior Commission approval.
3. Approve OTP's proposed total capitalization of \$960,273,000 with a contingency cap of 10 percent (or \$1,056,300,000). The Company may not exceed its total capitalization, including the requested contingency amount, for a period exceeding 60 days without prior Commission approval.
4. Approve OTP's request to issue short-term debt not to exceed 15 percent of OTP's total capitalization (i.e., \$144,040,950). OTP's short-term debt may not exceed 15 percent of its total capitalization for a period exceeding 60 days without prior Commission approval.
5. Approve any securities issuance during this period in which this Order is in place that would not result in an equity ratio outside the approved range. Securities issuances resulting in an equity ratio outside this range may not exceed a period of 60 days without prior Commission approval.
6. Require OTP to provide, within 20 days after each non-recurring issuance of securities, the

following information:

- a. The specific purposes for individual issuances;
  - b. The type of issuances;
  - c. The timing of issuances;
  - d. The amounts of issuances;
  - e. Issuance costs (for common equity issuances, including price per share); and
  - f. Interest rates.
7. Require OTP to provide, in its next capital structure filing, an exhibit showing a general projection of capital needs, projected expenditures, anticipated sources and anticipated timing, with the understanding that such exhibit is not intended to require dollar-for-dollar on the uses identified in the exhibit or to limit issuances to project specific financing. The exhibit need not list short-term, recurring security issuances.
  8. Require OTP to provide in its next annual structure filing, a schedule comparing its actual capital investments in the past year with the capital investments projected by OTP in its previous capital structure filing.
  9. Require OTP to provide in its next annual capital structure filing, the Company's investment plan not only for the next year, but for at least the next five years.
  10. Approve OTP's request for a variance to allow it to treat any loan under its multi-year credit facility as a short-term debt and require OTP to report on its use of such facilities, including:
    - how often they are used;
    - the amount involved;
    - rates and financing costs; and
    - the intended uses of the financing.

### ***OTP's Comments***

OTP thanked the Department for correcting the two numerical errors and requested the Commission to adopt the Department's recommendations.

### ***Staff Comment***

The Department's recommendations are consistent with requirements the Commission has previously applied to securities issuance requests.

In the following discussion, staff offers typographical clarification to the Department's recommendations 1, 7 and 8 for the Commission's consideration:

1. Approve OTP's requested capital structure; this approval to be in effect until the 2016 capital structure Order is issued. OTP shall file its next securities issuance petition no later than May, 1 2016.

7. Require OTP to provide, in its next capital structure filing, an exhibit showing a general projection of capital needs, projected expenditures, anticipated sources and anticipated timing, with the understanding that such exhibit is not intended to require dollar-for-dollar spending on the uses identified in the exhibit or to limit issuances to project specific financing. The exhibit need not list short-term, recurring security issuances.
8. Require OTP to provide in its next annual capital structure filing, a schedule comparing its actual capital investments in the past year with the capital investments projected by OTP in its previous capital structure filing.

In addition, the Commission may consider adding, as a corollary to the Department's recommendation 4, the following requirement:<sup>4</sup>

Require OTP to obtain prior approval for the issuance of any securities in 2015 that would result in an equity ratio outside the approved range or a total capitalization exceeding its approved cap for more than 60 days.

The Commission may also wish to order, in the interest of uniformity of action regarding electric utilities' annual capital structure filings, the following requirement which the Commission also applied to Minnesota Power:<sup>5</sup>

Require OTP to provide, in its next annual capital structure filing, a report of actual issuances and uses of the funds from the prior year. The report will be for information purposes only and need not cover short-term security issuances.

Finally, the Commission may consider applying the disclaimer that the capital structure approved herein is not a determination concerning the appropriate capital structure for ratemaking purposes:

Clarify that approval of securities issuance and the resulting capital structure, within this proceeding, is not a determination of the appropriate capital structure for ratemaking purposes.

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<sup>4</sup> The Department applied this requirement to Minnesota Power. Please see: ORDER, In the matter of a Petition by Minnesota Power for Approval of its 2015 Capital Structure and Authorization to Issue Securities, Docket No. E-015/S-15-168 (May 22, 2015).

<sup>5</sup> Ibid.

## ***Decision Alternatives***

### ***A. Adopt only the Department's recommendations with the typographical changes:***

1. Approve OTP's requested capital structure; this approval to be in effect until the 2016 capital structure Order is issued. OTP shall file its next securities issuance petition no later than May, 1 2016.
2. Approve OTP's equity ratio of 52.1 percent and a contingency range of minus/plus 10 percent around the approved equity ratio (46.9% to 57.3%). Equity ratios outside this range may not exceed a period of 60 days without prior Commission approval.
3. Approve OTP's proposed total capitalization of \$960,273,000 with a contingency cap of 10 percent (or \$1,056,300,000). The Company may not exceed its total capitalization, including the requested contingency amount, for a period exceeding 60 days without prior Commission approval.
4. Approve OTP's request to issue short-term debt not to exceed 15 percent of OTP's total capitalization (i.e., \$144,040,950). OTP's short-term debt may not exceed 15 percent of its total capitalization for a period exceeding 60 days without prior Commission approval.
5. Approve any securities issuance during this period in which this Order is in place that would not result in an equity ratio outside the approved range. Securities issuances resulting in an equity ratio outside this range may not exceed a period of 60 days without prior Commission approval.
6. Require OTP to provide, within 20 days after each non-recurring issuance of securities, the following information:
  - a. The specific purposes for individual issuances;
  - b. The type of issuances;
  - c. The timing of issuances;
  - d. The amounts of issuances;
  - e. Issuance costs (for common equity issuances, including price per share); and
  - f. Interest rates.
7. Require OTP to provide, in its next capital structure filing, an exhibit showing a general projection of capital needs, projected expenditures, anticipated sources and anticipated timing, with the understanding that such exhibit is not intended to require dollar-for-dollar spending on the uses identified in the exhibit or to limit issuances to project specific financing. The exhibit need not list short-term, recurring security issuances.
8. Require OTP to provide in its next annual capital structure filing, a schedule comparing its actual capital investments in the past year with the capital investments projected by OTP in its previous capital structure filing.



9. Require OTP to provide in its next annual capital structure filing, the Company's investment plan not only for the next year, but for at least the next five years.
10. Approve OTP's request for a variance to allow it to treat any loan under its multi-year credit facility as a short-term debt and require OTP to report on its use of such facilities, including:
  - how often they are used;
  - the amount involved;
  - rates and financing costs; and
  - the intended uses of the financing.

***B. Adopt A above and some or all of the following:***

11. Require OTP to obtain prior approval for the issuance of any securities in 2015 that would result in an equity ratio outside the approved range or a total capitalization exceeding its approved cap for more than 60 days;
12. Require OTP to provide, in its next annual capital structure filing, a report of actual issuances and uses of the funds from the prior year. The report will be for information purposes only and need not cover short-term security issuances; and
13. Clarify that approval of securities issuance and the resulting capital structure, within this proceeding, is not a determination of the appropriate capital structure for ratemaking purposes.