

Minnesota Public Utilities Commission

Staff Briefing Papers

Meeting Date: August 6, 2015 **Agenda Item # 8

Company: Northern States Power Company d/b/a Xcel Energy (Xcel or the Company)

Docket No. E-002/M-15-515

In the Matter of a Petition for Approval to Share Proceeds from the Sale of
Renewable Energy Credits with Customers

Issue: Should the Commission approve Xcel's proposal to share proceeds from a
recent Renewable Energy Credit sale with customers?

Staff: Andrew Twite | 651.201.2245 | Andrew.Twite@state.mn.us
Dorothy Morrissey | 651.201.5565 | Dorothy.Morrissey@state.mn.us

Relevant Documents

Xcel Energy – Petition May 28, 2015
Department of Commerce – Initial Comments June 29, 2015
Xcel Energy – Reply Comments July 9, 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 noted otherwise.

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Statement of the Issue

Should the Commission approve Xcel's proposal to share proceeds from a recent Renewable Energy Credit sale with customers?

1. Overview

Xcel Energy has recently completed a sale of renewable energy credits (RECs), and it is requesting permission to retain a portion (15%) of the net proceeds as a reward for its efforts and an incentive to complete more REC sales in the future. The Department opposes this proposal, arguing that since Xcel's customers have borne the cost premium of the renewable energy, they should retain all of the proceeds from the sale.

These briefing papers begin with a discussion of recent Commission precedent (Section 2), followed by a summary of Xcel's proposal (Section 3) and the Department's response (Section 4), and conclude with Staff analysis (Section 5) and some possible decision options (Section 6).

2. Background

In order to meet a portion of its obligation under Minn. Stat. §216B.2424 (the Biomass Mandate), which required Xcel Energy to acquire 125 MW of generation from biomass facilities, Xcel entered into a Power Purchase Agreement (PPA) with Fibrominn L.L.C., a 55 MW facility that generates electricity through the burning of poultry litter.¹

In Docket 12-1132, Xcel proposed to sell RECs and share the profits with its customers with an 85/15 percent split. In that docket, the Company was not requesting Commission approval of a specific sale, but rather seeking an advisory opinion for profit sharing in all future sales. In its May 17, 2013 Order, the Commission found proceeds should generally be returned to customers "unless the Commission determines, in response to a specific request, that the circumstances of a particular transaction merit sharing of the proceeds."² Specifically, Order Point 3 states:

The Commission will decide whether to approve a sharing of proceeds based on Xcel's filing, with a focus on the following components:

- a. a demonstration that the net proceeds resulting from credit trading over a designated period are significant and merit a reward;
- b. a documentation of the specific costs of each transaction; and
- c. a demonstration of, and basis for, the appropriate award.

3. Xcel Petition

In 2007, the State of North Carolina established a Renewable Portfolio Standard with a carve-out for production from poultry waste. On March 30, 2015 Xcel sold 20,000 RECs from the

¹ The PPA was approved by the Commission in Docket No. E002/M-00-1169.

² Page 2.

Fibrominn facility to a North Carolina utility at a price of **[TRADE SECRET DATA EXCISED]** for total proceeds of **[TRADE SECRET DATA EXCISED]**. On May 28, 2015, Xcel filed its Petition in this docket, requesting approval to share the net proceeds of this sale, with the Company retaining 15% of the net proceeds and returning the remaining 85% to customers through the RES Rider.

The Company notes that selling RECs is not as simple as one might expect. As Appendix A below displays, Xcel has a large quantity of RECs in its “bank,” projecting surpluses of several million RECs throughout the near future. But, because there is no centralized REC marketplace in which RECs are publically traded, potential buyers and sellers must seek each other out for individual transactions. Xcel claims to have “spent considerable time researching renewable portfolio standards across the United States to identify opportunities for our excess REC inventory,” and it notes that the price agreed to in this transaction is significantly higher than most recent REC sales by Minnesota utilities.³ The Company also noted it may have the opportunity to make additional sales in the future.

Xcel argues its profit sharing proposal provides appropriate reward for these efforts and an incentive for the Company to pursue future REC sales. The Company believes “this is the type of effort that further aligns customer and Company interests in a manner like that supported in the current e21 initiative. This revenue-sharing mechanism will better align utility business model and economic incentives with customer benefits and expectations, and enabling innovation and flexibility.”⁴ Moreover, the Company notes that other states allow it to retain a portion of REC sale profits, stating it retains 10% in South Dakota and 10-20% in Colorado (depending on the transaction type).

4. Department Response

The Department opposed Xcel’s profit sharing proposal. As the Department notes, it is Xcel’s customers, not its shareholders, who bear the costs of the Company’s renewable energy investments. This is especially relevant in this sale, as the price paid through the Fibrominn PPA is considerable: the Department cited a recent compliance filing showing Xcel customers pay **[TRADE SECRET DATA EXCISED]** for energy from the Fibrominn facility.⁵ In the Department’s words: “Given the price ratepayers have paid since 2001 for this generation, the Department recommends that ratepayers receive 100 percent of the benefit from the REC sale.”⁶

In addition, the Department argues Commission precedent supports its position. The Department cites Docket 12-1132, in which the Commission stated that it “concurs with the Department that any proceeds from REC trading presumptively belong to the ratepayers who paid for the credits in the first place.”

³ Xcel Petition, May 28, 2015, at page 5.

⁴ Ibid, at pages 1-2.

⁵ Department of Commerce, Initial Comments, June 29, 2015, at page 2, citing Xcel’s most recent compliance filing in Docket No. E002/M-00-1169 (Trade Secret Attachment A).

⁶ Ibid, at page 3.

5. Staff Analysis

5.1 Profit Sharing

Staff agrees that it is Xcel's customers who have paid for the RECs that were sold. The Department points to the relatively high cost paid for the Fibrominn PPA; indeed, in Xcel's current Integrated Resource Plan, the Department argues the Fibrominn PPA is "too costly" and recommends the Commission order Xcel to not pursue an extension of the contract (under current terms).⁷ As Xcel's customers have paid a considerable amount over the life of this PPA, Staff believes the goal should be to maximize the proceeds to customers from REC sales.

However, while the Department's recommendation would provide customers with the highest return in this particular sale, Staff notes that it would not *necessarily* provide the greatest benefit to customers in the long run. The Department's argument does not address the broader point that profit sharing would provide the Company an incentive to pursue more REC sales and to get the best price for the RECs it sells. While 100% of the proceeds would benefit customers for the sales Xcel makes, if a profit-sharing approach results in more sales and higher prices, Xcel's customers will ultimately be better off.

Ultimately, Staff believes the appropriate course of action depends on whether or not the Commission believes additional motivation will result in more REC sales and/or higher prices. On the one hand, the Company may continue to seek out REC sales for its customers even if the Commission awards 100% of the proceeds to its customers, as the Company itself has said it will do.⁸ In this case, customer benefit would be maximized by denying Xcel's request for profit sharing. On the other hand, if the Commission believes additional motivation will lead Xcel to pursue more sales and/or to negotiate better prices, some form of motivation—whether it is an incentive for sales, a mandate for sales, or a penalty for a lack of sales—may produce the greatest customer benefit in the long run.

Finally, should the Commission decide to approve profit sharing for this sale, Staff notes that the split need not be 85/15%. As Xcel notes, the proportion of profit-sharing varies it is allowed in other states varies, from 10% in South Dakota to 10-20% in Colorado (depending on the transaction type). A 2013 draft NRRI report found that states had approved profit sharing from 0-20% for REC sales.⁹ Staff also notes that the percentage need not be the same from sale to sale. For example, the Commission could approve a 95/5% split for this sale, with the understanding that the split for future sales could be increased or decreased depending on the particular sale; this performance-based approach would provide an additional incentive for the Company to negotiate the highest possible sale price.

5.2 Calculation of Profits

If the Commission decides to allow REC sales revenue to be shared between ratepayers and shareholders, only the *profit* from the sale should be subject to sharing. This means the sales revenues must first be reduced by the costs (in current or prior years) that have been or will be

⁷ Department of Commerce, Initial Comments in Docket 15-21, July 2, 2015, at pages 6 and 72.

⁸ Xcel Energy, Petition, May 28, 2015, at page 5.

⁹ NRRI, "U.S. States' Regulatory Treatment for Revenues from the Sale of Renewable Energy Certificates (RECs)," draft for discussion purposes only, March 2013.

paid by customers, which includes the costs incurred in creating and/or acquiring the RECs as well as any transaction-related costs.

Staff believes the Company's proposal did not appropriately net out all of the costs incurred by its customers. In determining the profit subject to share, the only deduction identified in the Company's proposal is a minimal MRETS transfer fee. However, Staff identifies at least two additional customer-paid costs incurred for REC issuance or acquisition that should also be accounted for and included as a deduction to the sales proceeds.

First, to create RECs in MRETS, the Company incurs an issuance fee, which is recovered from ratepayers in base rates. According to Xcel, these REC issuance fees totaled \$100; the Company stated it did not deduct this fee from sales proceeds because it is not a cost specific to the sale.¹⁰ Although minimal, Staff recommends that the issuance fee costs, which were paid by customers, be returned to customers and not subject to profit sharing; this recommendation is included as Decision Option 2A.

Second, any REC acquisition costs should, theoretically, be deducted before dividing profits. Unfortunately, it is difficult to determine the value of RECs transferred through a PPA. In addition to electricity, PPAs for renewable facilities often transfer the corresponding RECs to the purchaser; however, there is rarely an explicit REC value stated in the PPA. In this case, Xcel stated there was no separate REC price listed in the Fibrominn contract, therefore it assigned \$0 for acquisition costs.¹¹ However, given the price of the Fibrominn PPA, Xcel's customers have clearly paid a premium for the "renewableness" of this generation.

In the absence of contract specification, it is ultimately at Commission's discretion to assign a cost to these RECs. There are many possible ways to value the Fibrominn RECs. For example, according to utilities' filings in the most recent Biennial RES Compliance reports (Docket 14-237), the average sale price for RECs (for all Minnesota utilities) was \$0.86. Staff believes this would provide an appropriate proxy for the value of a "generic" REC. This option is included as Decision Option 2B.

5.3 Future Sales

In its Petition, Xcel requests that the Commission approve its profit sharing proposal for potential future REC sales. Staff, on the other hand, believes the process outlined by the Commission in Docket 12-1132 is more prudent; page 2 of the May 17, 2013 Order states:

The Commission concurs with the Department that any proceeds from renewable-energy-credit trading presumptively belong to the ratepayers, who paid for the credits in the first place. The Commission also agrees with both the Department and Xcel that there may be circumstances in which Xcel's efforts would merit an award of part of the proceeds. The Commission is reluctant, however, to set a specific percentage without knowing the details of a particular transaction.

The Commission will therefore order Xcel to return all proceeds from renewable-energy-credit transactions to its ratepayers via the RES Rider unless the Commission determines, in response to a specific request, that the circumstances

¹⁰ Xcel Energy, Response to PUC Information Request No. 4, June 15th, 2015.

¹¹ Xcel Energy, Response to PUC Information Request No. 2, June 15th, 2015.

of a particular transaction merit sharing of the proceeds. The Commission will establish procedures and requirements for this filing as set forth below in the ordering paragraphs.

Xcel's request for an advisory opinion is included as Decision Option 5 below. Though Staff believes an explicit finding that the Commission will continue its current practice for review of REC sales is unnecessary—as the presumption is the Commission would continue its current practice unless it explicitly stated otherwise—this finding is included as Decision Option 6.

6. Decision Options

March 30, 2015 Fibrominn REC sale

- 1) Approve Xcel's proposal to share the net proceeds from this sale, with the Company retaining 15% and the remainder returned to customers through the RES rider. (Xcel)
- 2) Approve Xcel's proposal to share the net proceeds from this sale *with some or all of the following modifications*:
 - A. Require the Company to deduct REC issuance fees from the proceeds before dividing profits.
 - B. Require the Company to deduct a REC acquisition cost of \$0.86/REC from the proceeds before dividing profits.
 - C. Reduce the Company's share of the net proceeds to five percent.
- 3) Reject Xcel's proposal to share the net proceeds from this sale and require the Company to return all of the proceeds to its customers through the RES rider. (the Department)

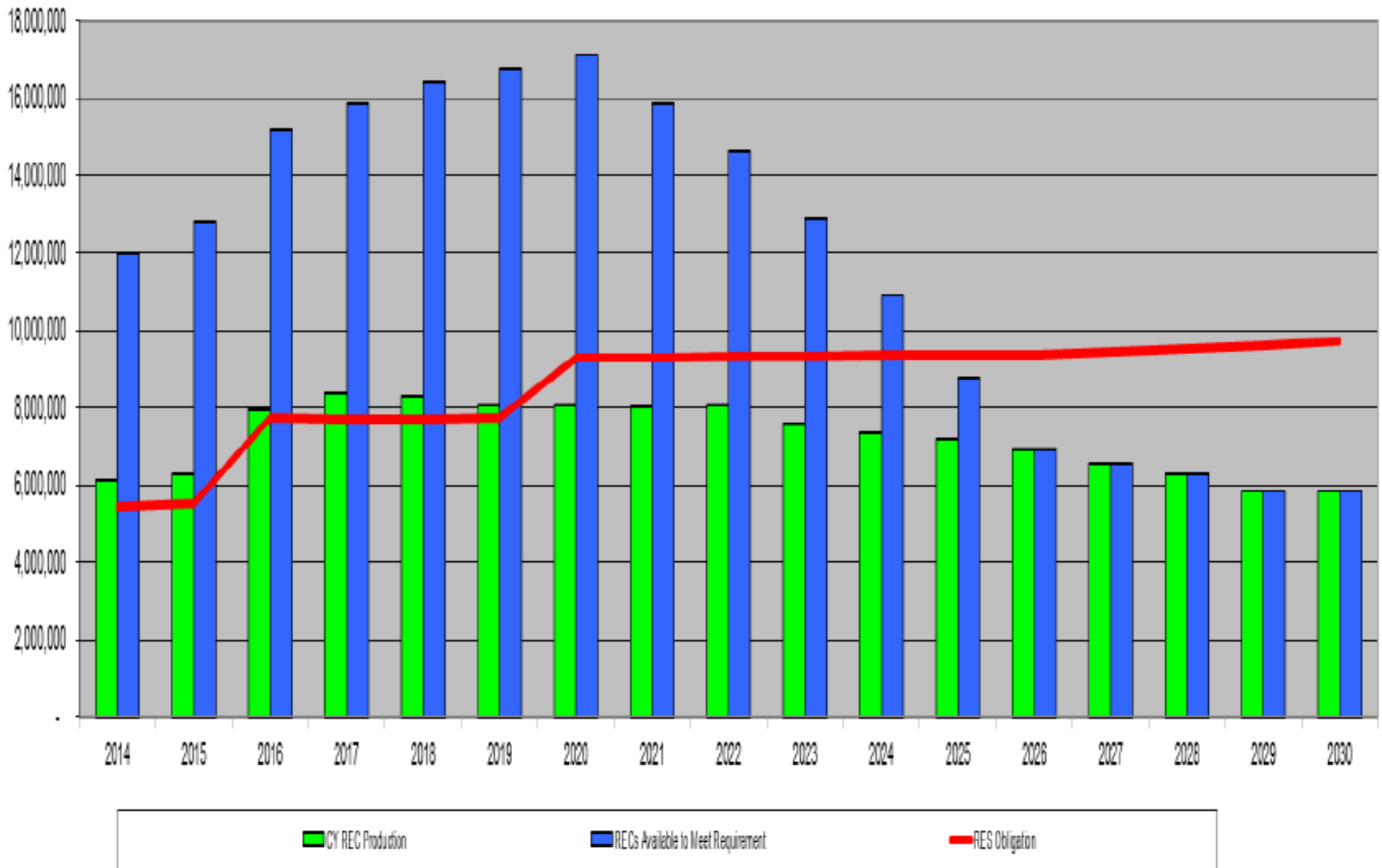
Compliance Filing

- 4) Direct Xcel to make a compliance filing memorializing the Commission's decisions in this docket within 30 days.

Future REC sales

- 5) Approve Xcel's proposed profit sharing mechanism for potential future REC sales. (Xcel) *(Staff note: approval of Decision Option 5 would be a reversal of the Commission's decision in Docket 12-1132)*
- 6) Continue the practice—outlined in the May 17, 2013 Order in Docket 12-1132—of determining the appropriate level (if any) of profit sharing on a sale-by-sale basis. (Staff)

Appendix A



Source: Xcel Energy, Initial Comments, May 28, 2015, at page 8

Appendix B

- ☐ Non Public Document – Contains Trade Secret Data
☐ Public Document – Trade Secret Data Excised
☒ Public Document

Xcel Energy

Docket No.: E002/M-15-515

Response To: Public Utilities Commission Information Request No. 2

Requestor: Dorothy Morrissey

Date Received: June 5, 2015

Question:

Reference Petition, Part C.a, page 6 and Part C.b – Chart 1, page 7. Please provide an accounting for the assigned costs of the Fibrominn RECs sold and explain the Company's basis for assigned cost.

Response:

The assigned cost of the Fibrominn REC is zero. Renewable energy supply contracts will identify a price for the energy and a REC will be awarded to the Company for each megawatt-hour (MWh) of energy purchased. For all of the NSP purchased power contracts, there is no separate price listed in the contract for the REC. Consistent with the industry's practice and accounting standards, where no price is specified in a contract, the REC inventories are recorded at a zero value. Therefore the Fibrominn REC is assigned a zero cost value.

Preparer: Tessa Venetz

Title: Principal Financial Consultant

Department: NSP Commercial Accounting

Telephone: 303-571-2769

Date: June 15, 2015

- ☐ Non Public Document – Contains Trade Secret Data
☐ Public Document – Trade Secret Data Excised
☒ Public Document

Xcel Energy

Docket No.: E002/M-15-515

Response To: Public Utilities Commission Information Request No. 4

Requestor: Dorothy Morrissey

Date Received: June 5, 2015

Question:

Please disclose the M-RETS certificate Issue Fees incurred by, or allocated to, the Company for the specific lots of Fibrominn RECs sold (2014 vintage). Please discuss why certificate Issue Fees are not included when determining net profit from sales of RECs.

Response:

The M-RETS REC issuance fees for the Fibrominn RECs sold (2014 vintage) is \$.005/REC or \$100 for the 20,000 Fibrominn RECs sold. REC Issuance Fees are not included as a cost when determining the net profit from a sale of RECs because they are not a cost specific to the sale. All RECs, whether they are retired for compliance, allowed to expire, or transferred to another party as the result of a sale, have a common issuance fee.

Preparer: Jeff Haskins

Title: Mgr REC Compliance

Department: Commercial Operations

Telephone: 303-571-6454

Date: June 15, 2015