MINNESOTA DEPARTMENT OF COMMERCE

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September 7, 2016

Mr. Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 300
St. Paul, Minnesota 55101

RE: **Response Comments of the Minnesota Department of Commerce, Division of Energy Resources to Xcel Energy's Reply Comments**
Docket No. E002/M-15-891

Dear Mr. Wolf:

Attached are the Response Comments of the Minnesota Department of Commerce, Division of Energy Resources (DOC or the Department) to the Reply Comments of Xcel Energy (Xcel or the Company).

Based on our review of Xcel Energy's Reply Comments, the DOC recommends that the Minnesota Public Utilities Commission (Commission) adopt the DOC's recommendations, as discussed in greater detail herein. The Department is available to answer any questions that the Commission may have in this matter.

Sincerely,

/s/ MARK A. JOHNSON
Financial Analyst

MAJ/ja
Attachment

MINNESOTA DEPARTMENT OF COMMERCE

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

RESPONSE COMMENTS OF THE
MINNESOTA DEPARTMENT OF COMMERCE
DIVISION OF ENERGY RESOURCES

DOCKET NO. E002/M-15-891

I. BACKGROUND

On August 1, 2006, Northern States Power d/b/a Xcel Energy (Xcel or the Company) filed a petition requesting approval of a Transmission Cost Recovery Rider (TCR Rider). The TCR Rider was proposed to replace the existing Renewable Cost Recovery (RCR) Rider and reflect changes required by Minn. Stat. §216B.16, subd. 7(b), a statutory subdivision that was newly adopted during the 2005 legislative session.

On November 20, 2006, the Minnesota Public Utilities Commission (Commission) issued an *Order Approving Transmission Cost Recovery Rider* in Docket No. E002/M-06-1103. The Commission's Order approved Xcel's proposed tariff for the TCR Rider with the condition that Xcel must maintain separate tracker accounts for projects approved under the Renewable Cost Recovery Statute, and those approved under the Transmission Cost Recovery Statute.

The Commission has issued Orders regarding Xcel's TCR Rider in several dockets since its November 20, 2006 Order.[1] Most recently, on June 29, 2015 the Commission issued its *Order Approving 2015 Transmission Cost Recovery Rider Tariff, Adjustment Factors, and 2014 TCR True-Up* in Docket No. E002/M-14-852 (2015 TCR Rider).

On October 1, 2015, Xcel filed the instant petition requesting approval of its 2016 Transmission Cost Recovery Rate Rider Factors (2016 TCR Rider).

On November 6, 2015, Xcel filed an update to its 2016 TCR Rider. The update amended Xcel's 2016 TCR Rider to align with the proposals made by the Company in its 2015 Rate Case (Docket No. E002/GR-15-826). Specifically, Xcel proposed to keep its CAPX2020 Brookings and Fargo projects in the 2016 TCR Rider until implementation of final rates resulting from the 2015 Rate Case. In addition, Xcel proposed to adjust the TCR Rider's

[1] Docket Nos. E002/M-08-1284, E002/M-09-1048, E002/M-10-1064, E002/M-12-50, and E002/M-13-1179.

2016 annual revenue requirement to account for its prorated calculation of plant-related Accumulated Deferred Income Taxes (ADIT) in accordance with Internal Revenue Service (IRS) Section 1.167(l)(h)(6).

On April 21, 2016 the Minnesota Department of Commerce, Division of Energy Resources, (DOC or the Department) filed its initial comments. In summary, the Department:

- concluded that all transmission projects included in Xcel's 2016 TCR Rider are eligible for recovery under the Transmission Statute;

- requested that Xcel explain the forecasted $788,600 reduction in capital costs for the CAPX2020 Brookings project for 2017 in reply comments;

- concluded that Xcel's proposed 2016 annual revenue requirements for the CAPX2020 Brookings and CAPX2020 Fargo projects appear reasonable and recommended that the Commission approve these amounts for recovery through Xcel's 2016 TCR Rider;

- requested that Xcel fully explain in reply comments whether unforeseen or extraordinary circumstances account for the total estimated cost increase for the CAPX2020 La Crosse project from $276.5 million to $326.7 million;

- requested that Xcel explain in reply comments whether it provided any initial cost estimates for the CAPX2020 Big Stone – Brookings project in SDPUC Docket Nos. EL06-002 and EL13-020. If so, the Department requested that Xcel provide these estimates in its reply comments;

- requested that Xcel explain in reply comments whether it provided any initial cost estimates for the La Crosse – Madison project in Docket No. 5-CE-142. If so, the Department requested that Xcel provide these estimates in its reply comments;

- recommended that the Commission require Xcel to recalculate its proposed 2016 TCR Rider annual revenue requirements and resulting 2016 TCR Rider rate factors using the state jurisdictional allocators approved in Xcel's last rate (Docket No. E002/GR-13-868); and

- recommended that the Commission require Xcel to replace its forecasted prorated ADIT balances with actual non-prorated ADIT balances in its beginning-of-month and end-of-month average ADIT balance calculations for true-up purposes in future TCR Rider filings. Alternatively, the Commission could require Xcel's riders to be based solely on historical costs, since the issue applies only in cases with forward-looking rates.

On June 3, 2016, Xcel filed its Reply Comments.

II. DOC ANALYSIS

A. CAPX2020 BROOKINGS

Beginning on page 8 of its Reply Comments, Xcel stated that:

> The Department requested that the Company explain the forecasted $788,600 reduction in capital costs for the CapX2020 Brookings project in 2017. The CapX2020 Brookings project is a 345 kV transmission line, and thus the "By the Farm" (BTF) law applies to the easements needed on surrounding residential and agricultural properties. Landowners who may not want to live by a high voltage power line have the option to sell their homes to the utility, and they have a set timeline by which to elect BTF. This timeline does not always coincide with construction timelines. When BTF is elected by landowners and the properties are acquired by the utility, the properties are marketed for resale and the proceeds are credited to the project, in this case CapX2020 Brookings.
>
> While the actual expenditure to acquire BTF properties was reflected in prior year actual costs, the $788,600 reduction in 2017 capital costs reflects the sales revenue from properties acquired for CapX2020 Brookings project easements. Capital costs in 2017 show an overall reduction because the project is complete and is forecasted to have no positive expenditure, which would otherwise offset these BTF sales. (Footnotes omitted).

The DOC appreciates Xcel's explanation and concludes that the forecasted reduction in capital costs for the CAPX2020 Brookings project appears reasonable.

B. CAPX2020 LA CROSSE

The DOC had asked Xcel to explain in reply comments whether unforeseen or extraordinary circumstances account for the total estimated cost increase for the CAPX2020 La Crosse project from $276.5 million to $326.7 million.

Xcel stated in its Reply Comments that it had identified three areas that contributed to the increased cost estimates for the CAPX2020 La Crosse project. These three areas include cost escalation, length of approved route, and scoping changes. The DOC discusses each of these below.

1. Cost Escalation

Xcel stated the following beginning on page 2 of its Reply Comments::

> The initial estimated project costs at completion were $276.5 million in 2007 dollars, as filed in the CapX2020 projects' Certificate of Need (CON) docket. These initial estimated costs were presented in constant 2007 dollars to evaluate various routing and scoping alternatives. While the use of then-current-year dollars is appropriate for comparing alternatives in the context of a CON docket, it does not account for the actual cost of materials, labor and services in the year those dollars are spent, sometimes many years in the future. It is appropriate to include these normally occurring inflationary cost increases to material, labor and services amounts in TCR recovery as they are inherent to large construction projects, such as the CapX2020 projects, which are planned and constructed over many years.
>
> It is our understanding that the Department did not oppose our calculation of the escalated costs at completion as reasonable in their April 21, 2016 Comments, but requested additional information. In addition, it is consistent with past Commission practice to accept the escalated initial project costs as the cost cap for TCR recovery purposes. Accordingly, we believe it is appropriate to evaluate the project costs in comparison to $330.3 million, which is the initial project cost estimate of $276.5 million as escalated. (Footnotes omitted).

The DOC agrees that the Commission has allowed the escalation of initial project costs to determine the appropriate cap for rider recovery purposes. In addition, the DOC agrees with Xcel's cost escalation calculations for the CAPX2020 La Crosse project. As a result, the DOC concludes that the appropriate cost recovery cap for the CAPX2020 La Crosse project should be $330.3 million. As noted in our initial comments, Xcel's total estimated CAPX2020 La Crosse project cost of $326.7 million is below the escalated cost estimate of $330.3 million.

2. Length of Approved Route

Beginning on page 3 of its Reply comments, Xcel stated:

> The CapX2020 La Crosse project costs were also impacted by the final approved project route. When we submit a CON for approval by the Commission, we present a cost range to account for the many possible project routes, line lengths, line voltage and other components of constructing a transmission line that must be taken into consideration to meet the specific need at hand. These cost estimates are further refined when we are able to narrow down the possibilities in order to present, generally, only two route options in a route permit proceeding.
>
> For the CapX2020 La Crosse project, the final route as approved in the route permit proceedings in both Minnesota and Wisconsin was one of the longest routes possible. The selection of this route meant the final approved project cost fell at the uppermost end of the estimated cost range presented in the CON filing.
>
> Of the potential 143 to 159 miles submitted in our CON, the final approved route was 157 miles. Therefore, even before taking into account commodity inflation between 2007 and the actual construction period, the CapX2020 La Crosse project cost projection was very near the initial cost estimate of $276.5 million in 2007 dollars, as filed in the CON.

The DOC agrees that the length of the approved route was near the high end of the range identified in the CON and could account for some of the increased costs associated with the project.

3. Scoping Changes

Beginning on page 4 of its Reply Comments, Xcel stated that the following scoping changes increased its cost estimates for the CAPX2020 La Crosse project:

- 69 kV line upgrades;
- 69 kV substation addition;
- Mississippi River crossing (removal of an existing double-circuit transmission line over the Mississippi River at the request of the United States Fish and Wildlife Service);
- extended 345 kV;
- railway accommodations;
- galloping line mitigation; and
- pipeline issue mitigation.

The Department reviewed Xcel's scoping changes for the CAPX2020 La Crosse project. Based on our review, the DOC concludes that these changes contributed to the increased cost estimates for the CAPX2020 La Crosse project.

4. Conclusion and Recommendation

Based on the above, the DOC concludes that Xcel has reasonably explained the increase in cost estimates for the CAPX2020 La Crosse project. In addition, the DOC concludes that the appropriate cost recovery cap for the CAPX2020 La Crosse project should be $330.3 million. Since the current cost estimate for the CAPX2020 La Crosse project of $326.7 million is below the escalated cost estimate of $330.3 million, the Department recommends that the Commission approve recovery of the costs Xcel proposed for recovery in the instant petition.

A. CAPX2020 BIG STONE–BROOKINGS PROJECT

Xcel stated the following beginning on page 8 of its Reply Comments:

> The Department requested that the Company provide initial cost estimates for the CapX2020 Big Stone – Brookings project as filed with the South Dakota Public Utilities Commission (SDPUC). The total project cost estimate for the complete project of $227 million, including AFUDC, is provided on page 2 of the December 19, 2012 Petition for Order Accepting Recertification of the Big Stone – Brookings project.[2] This estimate includes escalation.
>
> In the original Facility Permit granted to Otter Tail Power Company (OTP) in January 2007,[3] the line segment cost estimates were presented only for the South Dakota portion of the transmission lines. The December 20, 2012 Supplement and Amended Information for Application, Appendix A indicated that the estimated cost for all segments of the original transmission project was approximately $110 million, including AFUDC, in 2006 dollars.
>
> However, the project approved in the original Facility Permit did not go forward as proposed. In the 2012 recertification docket, OTP requested a recertification of only the following three portions of the original project:
> 1. Two 230 kV transmission lines, each 1.5 miles in length;
> 2. The Big Stone South substation; and

[2] SDPUC Docket No. EL12-063.
[3] SDPUC Docket No. EL06-002.

3. Approximately 28 miles of 345kV double circuit-capable transmission line.[4]

Because not all portions of the original project proceeded to the construction phase, the cost estimates presented in the original Facility Permit in SDPUC Docket No. EL06-02 do not provide comparable project costs for the current CapX2020 Big Stone – Brookings Project.

Table 1 below shows the initial project cost estimates as approved in Docket No. EL12-063 and as reported to MISO as part of one of the MISO MVP regional projects. Xcel Energy's portion of the estimated initial project costs is $92.2 million, including AFUDC. These estimated project costs are consistent with the project costs reported to MISO as part of this MVP project in December 2011.

Table 1
CapX2020 Big Stone – Brookings Initial Project Costs

TCR line item	Project Segment	Total Cost Estimated for Facility Permit	NSPM Share	Docket No.
N/A	230 kV Line; Big Stone South Sub; Big Stone Plant Improvements	$52.0 million		EL12-045
Line and Land	T-Line (345kV) and Easements North Half (Approved Route)	$66.0 million	$33.0 million	EL12-045
Line and Land	T-Line (345kV) and Easements South Half (New Route)	$99.0 million	$49.5 million	EL13-020
Sub	Brookings County Substation modifications	$9.7 million	$9.7 million	EL13-020
	Total Estimated Project Cost (w/ AFUDC)	**$226.7 million**	**$92.2 million**	

The May 31, 2013 Application for a Facility Permit for the southern portion of the project[5] provides the project ownership percentages on page 11 and total project costs, including escalation, on page 12, which were approved by SDPUC Order on February 20, 2014.

Attachment 3B of our initial TCR Petition shows Xcel Energy's projected total project expenditure for CapX2020 Big Stone – Brookings to be $81.3 million, below the estimated total project

[4] Of these three project segments, Xcel Energy has shared permit rights with OTP for only the 345 kV portion.
[5] SDPUC Docket No. EL13-020

> costs as submitted to the SDPUC. There are several reasons that our current cost estimate for the CapX2020 Big Stone – Brookings project at completion is less than initially submitted to the SDPUC. The lower cost is reflective of 1) value engineering, whereby we were able to substitute materials and methods with less expensive alternatives without sacrificing quality or functionality; 2) estimate refinement where our actual appropriation cost was less than as originally scoped for the cost estimates; and 3) lower material prices. For example, steel commodity prices were at a 5-year historic low when the structures for this project were purchased, which helped reduce the total project cost. Because there is a true-up mechanism in the TCR Rider, customers will experience these project cost reductions through lower rates.

Based on the above, the DOC concludes that Xcel's total estimated costs of $81.3 million for the CAPX2020 Big Stone-Brookings project is below the total estimated costs of $92.2 million provided to the SDPUC in Docket No. EL12-063. Since Xcel's current estimated costs included for recovery in the instant petition total approximately $47.9 million[6] through December 2016 and are below the total estimated project costs of $92.2 million provided to the SDPUC, the DOC recommends that the Commission approve Xcel's requested recovery of approximately $47.9 million for the CAPX2020 Big Stone-Brookings project.

B. LA CROSSE – MADISON PROJECT

Beginning on page 10 of its Reply Comments, Xcel stated:

> The Department requested that the Company provide initial cost estimates for the Badger – Coulee Project (La Crosse – Madison) in Wisconsin Public Service Commission (PSCW) Docket No. 5-CE-142. In the initial filing, the original project costs were projected to be $576.2 million; however, the project costs presented in the final PSCW Order were slightly higher due to routing changes made by the PSCW. The final, approved project costs of $581.4 million are the relevant initial cost estimates. This estimate includes escalation.
>
> Page 56 of the PSCW's April 23, 2015 Final Decision in the referenced CPCN docket provides a breakdown of total project costs for a total project cost of $581.4 million, including AFUDC. Of this total, Xcel Energy's portion of the approved total project

[6] Per DOC's April 21, 2016 Comments in Docket No. E002/15-891, Page 9, Table 4. Also per Xcel's November 6, 2015 Updated Filing in Docket No. E002/15-891, Attachment 3B - Capital expenditures through 2016.

costs is $206.4 million, including AFUDC. Table 2 below shows the initial project cost estimates and Xcel Energy's portion of the costs.

Table 2
Badger – Coulee Initial Project Costs

TCR Line Item	Project Segment	Total Cost Estimated in CPCN docket as approved	NSPW Share
Land and Line	T-Line (345kV) Line and Easement	$497.5 million	$160.3 million
Sub	Three substations, including Xcel Energy's Briggs Road Substation	$18.5 million	$6.5 million
Line	Environmental Impact Fee, Pre-certification costs and other project costs	$38.1 million	$12.3 million
	Total Estimated Project Cost (without AFUDC)	**$554.1 million**	**$179.1 million**
N/A	AFUDC	$27.3 million	$27.3 million
	Total Estimated Project Cost (with AFUDC)	**$581.4 million**	**$206.4 million**

Attachment 3B of our initial TCR Petition shows Xcel Energy's projected total expenditure for the Badger – Coulee project to be $192.2 million excluding AFUDC, which was Xcel Energy's initial estimate of ownership share. We maintained this level of forecast until the project ownership agreements were finalized on October 30, 2015, after the TCR Petition was filed. We then updated our project forecast to $179.1 million to correspond with the final ownership percentage, as shown in Table 2 above. We will make this adjustment to the forecasted project expenditure in our next TCR petition.

Based on the above, the DOC concludes that Xcel's revised total estimated costs for the La Crosse-Madison project total $179.1 million and match the total estimated costs provided to the PSCW. Since Xcel's current estimated costs included for recovery in the instant petition total approximately $68.0 million[7] through December 2016 and are below the total estimated project costs of $179.1 million provided to the PSCW, the DOC recommends that the Commission approve Xcel's request to recover approximately $68.0 million for the La Crosse-Madison project.

[7] Per DOC's April 21, 2016 Comments in Docket No. E002/15-891, Page 9, Table 4. Also per Xcel's November 6, 2015 Updated Filing in Docket No. E002/15-891, Attachment 3B - Capital expenditures through 2016.

C. JURISDICTIONAL ALLOCATORS

Xcel stated on page 7 of its reply comments that it did not oppose the Department's recommendation to use the state jurisdictional allocators approved in the Company's last rate case (Docket No. E002/GR-13-868). Xcel stated that it had used the state jurisdictional allocators in its currently-pending rate case (Docket No. E002/GR-15-826) for consistency between the rate case and the instant petition. Xcel stated that, in any event, they would true-up the tracker account after the rate case had concluded so the outcome would be the same regardless of the approach taken in the instant petition.

According to Xcel, the use of state jurisdictional allocators approved in the Company's last rate case would increase the revenue requirements in the instant petition from $78,410,459 and $78,599,537 and the residential rate from $0.003131 to $0.003138 per kWh.

The Department agrees that, since the TCR Rider has a true-up mechanism, the outcome would be the same regardless of which state jurisdictional allocators are used. However, for simplicity and consistency reasons, the Department recommends that the Commission require the Company to use the state jurisdictional allocators approved in the Company's last rate case (Docket No. E002/GR-13-868).

D. PRORATED ACCUMULATED DEFERRED INCOME TAXES (ADIT)

Beginning on page 6 of its reply comments, Xcel stated that:

> The Department recommended that the Commission require Xcel Energy to replace our forecasted prorated ADIT balances with actual non-prorated ADIT balances in its beginning-of-month and end-of- month average ADIT balance calculations for true-up purposes in future rate rider filings. Alternatively, the Department recommended that the Commission could require Xcel Energy's riders to be based solely on historical costs.
>
> We note that we plan to address the ADIT issue in our currently pending rate case (Docket No. E002/GR-15-826). Specifically, we plan to address it in a supplement to our response to the Department's Information Request No. 1139 which deals with this same topic. The rate case is a more appropriate forum for this issue for two reasons. First, the potential consequences of the outcome of this complex issue go beyond riders and developing the issue in the rate case will allow further analysis and comments. Second, due to the timing of the true-up, the issue does not need to be decided immediately so the rate case

> procedural schedule will allow a more thorough discussion and perhaps additional clarity on the topic before our next series of annual rider filings are heard at the Commission.
>
> With regard to the Department's alternative solution, using historical test years for riders, we note that there are customer benefits associated with the use of accelerated tax methods in the forecast period that would disappear with the use of a historical test year. If the Commission wishes to explore the use of historical test years for riders, we believe there should be additional record development.

Based on the above, the Department observes that Xcel would like to implement the 2016 TCR Adjustment Factor in the instant docket (a cost recovery docket) while having the ADIT discussion in its pending general rate case in Docket No. E002/GR-15-826. However, subsequent to Xcel's *Reply Comments* in this proceeding, a settlement has been filed in the rate case proceeding. Due to this settlement, which resolved all financial issues between the DOC and Xcel, and should the Commission accept the settlement, the policy surrounding the prorated ADIT will not be considered precedential. Thus, to avoid having this important financial issue overlooked, the Department discusses the issue in this proceeding.

Pages 12-25 of Ms. Nancy Campbell's June 14, 2016 Direct Testimony in Xcel's most recent rate case (Docket No. E002/GR-15-826), along with Attachments NAC-6 through NAC-9 of her testimony, all of which is attached to these *Response Comments*, addressed the issue of accounting for ADIT in ratemaking. The Department notes that in Xcel's most recent rate case, the Department took a stronger position on the ADIT Prorate issue based on a better understanding by the Department of this ADIT Prorate issue than we had at the time of our initial comments in the instant proceeding. The Department recommended that no changes/adjustments proposed by Xcel for the ADIT Prorate be allowed in Xcel's most recent rate case. Specifically, pages 16, 24-25 of Campbell Direct stated:

> **Q. Why are you concerned that the Company is changing a long standing position on how it treats its ADIT balance for ratemaking purposes and using private tax rulings as support?**
> A. I am concerned because ratepayers are continuing to pay the same depreciation and related taxes on investment, and now ratepayers will not be receiving the full ADIT offset or credit to rate base.
>
> **Q. Do these private letter rulings even apply to Xcel?**
> A. No. At the end of all private letter rulings, the IRS provides the following statement, which basically says this IRS decision is only to be used by the entity requesting the decision:

> This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides it may not be used or cited as precedent.[8]
>
> …
>
> - Fourth, since Xcel's proposed ADIT changes will harm ratepayers and change the way ratemaking is handling accelerated depreciation for rate cases without demonstrating adequate support to show that the ADIT change is required under the Internal Revenue Code or Treasury Regulations (only supported by private letter rulings that are entity specific), because Xcel failed to meet its burden of proof to show its proposed change to be reasonable, and because the Company failed to provide the adjustment the Department requested for the ADIT issue as discussed above, I recommend that no ADIT changes be allowed in this rate case at this time.

Additionally, on July 25, 2016 (after the Department and other intervenors filed Direct Testimony in the Xcel Rate Case) the Company submitted a Compliance Filing on behalf of Xcel Energy Transmission Development (XETD) Company LLC, in FERC Docket No. ER14-2752-004. The Department observes that, the Company's Note D of Attachment 4 page 2 of 2 stated the following regarding ADIT:

> ADIT is computed using the average of the beginning of the year and end of the year balances.

The Department notes that, in the FERC proceeding, the Company is *not* pro-rating its ADIT credit for rate base for XETD. This fact is inconsistent with Xcel's claims that NSP-M needs to pro-rate its ADIT balance. Since Xcel Energy does taxes on a consolidated tax basis, the Department does not see how the Company can claim non-prorated ADIT for XETD and prorated ADIT for NSP-M, except to conclude that the Company's claim that the IRS private ruling requires them to pro-rate the ADIT balance is not supported.

In sum, it is inappropriate and inconsistent to require ratepayers of a fully regulated utility such as Xcel to pay for higher income tax expenses based on an assumption of straight-line depreciation (rather than accelerated depreciation used for tax purposes) *and* to lose the long-standing offsetting ADIT credit to rate base. Instead of treating ADIT as the timing issue it has always been, Xcel now proposes to charge higher rates to ratepayers by charging ratepayers a tax expense that is higher and to no longer provide a matching ADIT credit for rate base because of the one-sided proration to only the rate base credit and not the tax expense.

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[8] See last page of Department information request no. 157, DOC Ex. ___ NAC-6 (Campbell Direct).

Since the Company is also not agreeing to the true-up in the following year when amounts become actual, the Company is inappropriately keeping for its shareholders the benefits of tax expense being higher than the ADIT credit. Charging ratepayers for a full tax expense that is not prorated and at the same time lowering the credit for ADIT due to proration without a true-up in the following year when costs become actual results in the Company unreasonably overcharging ratepayers. Thus, Xcel's proposal does not meet the requirement of Minnesota Statute section 216B.03, that rates must be just and reasonable.

Moreover, as this proceeding is a rider petition, Xcel's proposal would not meet the requirements of Minnesota Statute section 216B.1645, subdivision 2 since the Company is charging ratepayers a tax expense amount that is higher than the prorated ADIT credit, which is one-sided to the detriment of ratepayers and is not consistent with long-standing ratemaking principles:

> Subd. 2.**Cost recovery.**
> The expenses incurred by the utility over the duration of the approved contract or useful life of the investment and expenditures made pursuant to section 116C.779 shall be recoverable from the ratepayers of the utility, to the extent they are not offset by utility revenues attributable to the contracts, investments, or expenditures.

For all of the reasons identified in the Department's testimony in the concurrent rate case and in the Department's *Comments* in this proceeding, the Department recommends that the Commission either:

1. not allow Xcel to use any prorated ADIT balances, since the proposed changes to ADIT would:
   - harm ratepayers,
   - be inconsistent with the way ADIT has been handled for many years for ratemaking purposes,
   - inappropriately allow Xcel to use private letter rulings that don't even apply to the Company,
   - contradict the statement below in the IRS letters (even if the private letter rulings applied to Xcel) that there is no need for normalization if rates are based on historical data,
   - be inconsistent in Xcel's application, as a consolidated tax entity, of its pro-rated ADIT between NSP-M in Minnesota and XETD at FERC, and
   - contradict Xcel's assertion that the Company must pro-rate ADIT since Xcel, the consolidated tax entity, did not do so in its compliance filing with FERC,

OR

2. require Xcel's RES rider to be based solely on historical costs.

Requiring Xcel's TCR Rider (and other riders) to be based solely on historical costs would fully address the ADIT issue, as described in the Private Letter Ruling of the IRS:

> Congress was explicit: normalization "in no way diminishes whatever power the [utility regulatory] agency may have to require that the deferred taxes reserve be excluded from the base upon which the utility's permitted rate of return is calculated." H.R. Rep. No. 413, 91st Cong., 1st Sess. 133 (1969).
> …
> [T]he second interpretation of section 1.167(l)-1(h)(6)(ii) of the regulations [that "the historical period is that portion of the test period before rates go into effect, while the portion of the test period after the effective date of the rate order is the future period"] is consistent with the purpose of normalization, which is to preserve for regulated utilities the benefits of accelerated depreciation as a source of cost-free capital. The availability of this capital is ensured by prohibiting flow-through. But whether or not flow-through can even be accomplished by means of rate base exclusions depends primarily on whether, at the time rates become effective, the amounts originally projected to accrue to the deferred tax reserve have actually accrued.
>
> If rates go into effect before the end of the test period, and the rate base reduction is not prorated, the utility commission is denying a current return for accelerated depreciation benefits the utility is only projected to have. This procedure is a form of flow-through, for current rates are reduced to reflect the capital cost savings of accelerated depreciation deductions not yet claimed or accrued by the utility. Yet projected data is often necessary in determining rates, since historical data by itself is rarely an accurate indication of future utility operating results. Thus, the regulations provide that as long as the portion of the deferred tax reserve based on projected (future estimated) data is prorated according to the formula in section 1.167(l)-1(h)(6)(ii), a regulator may deduct this reserve from rate base in determining a utility's allowable return. In other words, a utility regulator using projected data in computing ratemaking tax expense and rate base exclusion must account for the passage of time if it is to avoid flow-through.

> But **if rates go into effect after the end of the test period, the opportunity to flow through the benefits of future accelerated depreciation to current ratepayers is gone, and so too is the need to apply the proration formula**. In this situation, the only question that is important for the purpose of rate base exclusion is the amount in the deferred tax reserve, whether actual or estimated. Once the future period, the period over which accruals to the reserve were projected, is no longer future, the question of when the amounts in the reserve accrued is no longer relevant (at the time the new rate order takes effect, the projected increases have accrued, and the amounts to be excluded from rate base are no longer projected but historical, even though based on estimates). (Emphasis added).[9]

III. CONCLUSIONS AND RECOMMDATIONS

In summary, the Department:

1) concludes that Xcel's forecasted reduction in capital costs for the CAPX2020 Brookings project appears reasonable;

2) concludes that Xcel has reasonably explained the increase in cost estimates for the CAPX2020 La Crosse project. In addition, the DOC concludes that the appropriate cost recovery cap for the CAPX2020 La Crosse project should be \$330.3 million. Since the current cost estimate for the CAPX2020 La Crosse project of \$326.7 million is below the escalated cost estimate of \$330.3 million, the Department recommends that the Commission approve recovery of the costs Xcel proposed for recovery in the instant petition;

3) concludes that Xcel's total estimated costs of \$81.3 million for the CAPX2020 Big Stone-Brookings project is below the total estimated costs of \$92.2 million provided to the SDPUC in Docket No. EL12-063. Since Xcel's current estimated costs included for recovery in the instant petition total approximately \$47.9 million[10] through December 2016 and are below the total estimated project costs of \$92.2 million provided to the SDPUC, the DOC recommends that the Commission approve Xcel's cost recovery request; and

[9] https://www.irs.gov/pub/irs-wd/201541010.pdf pages 6-8.
[10] Per DOC's April 21, 2016 Comments in Docket No. E002/15-891, Page 9, Table 4. Also per Xcel's November 6, 2015 Updated Filing in Docket No. E002/15-891, Attachment 3B - Capital expenditures through 2016.

4) concludes that Xcel's revised total estimated costs for the La Crosse-Madison project total $179.1 million and match the total estimated costs provided to the PSCW. Since Xcel's current estimated costs included for recovery in the instant petition total approximately $68.0 million[11] through December 2016 and are below the total estimated project costs of $179.1 million provided to the PSCW, the DOC recommends that the Commission approve Xcel's cost recovery request.

In addition, the Department recommends that the Commission:

1) require the Company to use the state jurisdictional allocators approved in the Company's last rate case (Docket No. E002/GR-13-868); and
2) not allow Xcel to use any prorated ADIT balances, since the proposed changes to ADIT would:
   - harm ratepayers,
   - be inconsistent with the way ADIT has been handled for many years for ratemaking purposes,
   - inappropriately allow Xcel to use private letter rulings that don't even apply to the Company,
   - contradict the statement in the IRS letters (even if the private letter rulings applied) that there is no need for normalization if rates are based on historical data,
   - be inconsistent in Xcel's application, as a consolidated tax entity, of its pro-rated ADIT between NSP-M in Minnesota and XETD at FERC, and
   - contradict Xcel's assertion that the Company must pro-rate ADIT since Xcel, the consolidated tax entity, did not do so in its compliance filing with FERC.

   OR

   - require Xcel's TCR Rider to be based solely on historical costs.

/ja

[11]Per DOC's April 21, 2016 Comments in Docket No. E002/15-891, Page 9, Table 4. Also per Xcel's November 6, 2015 Updated Filing in Docket No. E002/15-891, Attachment 3B - Capital expenditures through 2016.

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
Response Comments

Docket No. E002/M-15-891

Dated this 7th day of September 2016

/s/Sharon Ferguson

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