

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

**Northern States Power Company
Natural Gas Rate Increase
Application**

Case No. PU-400-00-521

FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER

June 27, 2001

Appearances

Commissioners: Susan E. Wefald, Leo M. Reinbold, Anthony T. Clark.

James P. Johnson, Assistant General Counsel, Xcel Energy Services Inc., 800 Nicollet Mall, Minneapolis, MN 55402, appearing for Northern States Power Company d/b/a Xcel Energy.

William W. Binek, Chief Counsel, Public Service Commission, State Capitol, 600 East Boulevard, Bismarck, ND 58505, appearing for the Public Service Commission Staff.

Allen C. Hoberg, Office of Administrative Hearings, 1707 North 9th Street - Lower Level, Bismarck, ND 58501-1882, presiding Administrative Law Judge.

Preliminary Statement

On October 9, 2000, Northern States Power Company d/b/a Xcel Energy (NSP) filed a Notice of Rate Change under N.D.C.C. § 49-05-05. The notice proposed an increase in NSP's natural gas rates of \$1.393 million (3.3 percent) annually, based on a 2000 current test year.

NSP asserted the rate increase was needed to recover (a) the costs of gas distribution system restoration incurred after the 1997 Red River flood, (b) the costs to environmentally remediate the site of a former manufactured gas plant (MGP) in Grand Forks, to facilitate construction of a new permanent dike to prevent future flooding, (c) the costs of substantial distribution system upgrade investments made since the early 1990s to meet increased customer demand for natural gas as a result of the strong economy, and (d) general inflation costs increases since NSP's 1984 gas general rate

case, Case No. 10,523. NSP proposed the natural gas rate change be allowed to go into effect on December 1, 2000, without suspension.

On October 25, 2000, the Commission suspended the rate change under N.D.C.C. § 49-05-06. Under this statute, NSP could place the increased rates into effect on June 9, 2001, unless the Commission issued a final order to the contrary prior to that date.

On December 20, 2000, the Commission issued a Notice of Hearing and Notice of Public Input Session. The notice set forth the following issues for consideration in the proceeding:

1. What is the value of NSP's property, used and useful, for the service and convenience of the public in North Dakota?
2. What is NSP's rate of return on its property, used and useful, for the service and convenience in North Dakota?
3. What is a just and reasonable rate of return on NSP's property, used and useful, for the service and convenience of the public in North Dakota?
4. What rates and charges are necessary to provide a just and reasonable rate of return on NSP's property, used and useful, for the service and convenience of the public in North Dakota?
5. Are NSP's proposed rate schedules designed in such a manner that they result in a basis of charge to its customers that is just and reasonable without discrimination?
6. Other relevant information or proposals concerning the proceeding.

On January 29, 2001, the Commission conducted a Public Input Session via interactive video conference, with hearing sites in Bismarck, Fargo, and Grand Forks. Approximately 20 members of the public attended. The majority of public comments related to high winter gas bills caused by rapid increases in wholesale natural gas prices. NSP and Commissioners stated their concern regarding the impact of high wholesale gas prices on customers, but stated this rate increase request is related to the cost of providing retail distribution service and is distinct from the wholesale market gas costs, which are reflected in gas rates through operation of NSP's purchased gas adjustment (PGA) tariff provisions.

No motions to intervene were filed, and no procedural order was issued. A voluntary procedural schedule was established by NSP and staff.

On February 16, 2001, NSP filed direct testimony supporting the proposed gas rate increase. On March 13, 2001, NSP filed an update to its test year cost of service reflecting (a) increased costs incurred for its MGP remediation project, and (b) reduced costs related to an update to the proposed capital structure to be used to determine final rates. The update increased NSP's asserted 2000 test year revenue deficiency to \$1.644 million.

On March 21, 2001, the staff filed direct testimony contesting various aspects of NSP's rate increase request.

On April 6, 2001, NSP filed rebuttal testimony contesting most of the staff recommendations, but reducing NSP's asserted test year deficiency to \$1.55 million annually.

On April 16, 2001, the staff filed surrebuttal testimony.

On April 19 and 20, 2001, the Commission conducted a formal hearing.

NSP and staff submitted the late-filed exhibits requested during the evidentiary hearing. On May 15, 2001, the Commission held a working session to discuss the issues and clarify whether additional late filed exhibits or information were necessary.

Following the evidentiary hearing, informal settlement discussions were held between staff and NSP representatives. On May 21, 2001, the parties notified the Commission they had reached a settlement in principle on all issues. NSP submitted a Motion for Extension of Time supported by staff which would allow the parties to submit the Settlement Agreement and supporting findings and other documentation on May 25, 2001, and set a slightly extended schedule for litigation briefs and proposed findings if the Settlement Agreement were rejected or modified. At its regular meeting on May 23, 2001, the Commission granted the motion.

On May 25, 2001, the parties submitted the Settlement Agreement. NSP also submitted proposed Findings of Fact, Conclusions of Law and Order, and a brief supporting approval of the Settlement Agreement. The staff submitted a memorandum supporting approval of the Settlement Agreement.

The Commission, having reviewed the evidence in the record, including the Settlement Agreement and submittals in support thereof, makes the following:

Findings of Fact

1. Northern States Power Company d/b/a Xcel Energy is a Minnesota corporation providing electric and natural gas public utility service in North Dakota. NSP provides retail natural gas service to approximately 37,000 customers in eastern North Dakota.

2. NSP is a utility operating company subsidiary of Xcel Energy Inc., which was created by the merger of Northern States Power Company and New Century Energies, Inc on August 18, 2000. The Commission approved the merger on May 10, 2000, in Case No. PU-400-99-418.

Summary of Undisputed Issues

3. Many of the issues in this proceeding were not disputed in pre-filed testimony or at the hearing. Except for the specific exceptions noted below, the pre-filed testimony of the staff and its consultants did not dispute:

- NSP's test year jurisdictional cost of service study;
- NSP's test year sales forecast;
- NSP's test year rate base;
- NSP's test year average cost of long term debt and short term debt;
- NSP's class cost of service study;
- MGP environmental remediation costs are appropriately recovered in rates;
- the allocation of MGP environmental remediation costs between the North Dakota gas jurisdiction and the Minnesota jurisdiction;
- the inclusion of rate case expenses in the test year cost of service;
- NSP's proposed rate design, including the customer charge for all classes except the residential class and eliminating the declining block rate design for NSP's commodity rate design for residential and small commercial firm services;
- NSP's test year base cost of purchased gas, and NSP's proposal to restate the base cost of gas effective with implementation of final rates;
- NSP's proposed seasonal allocation of certain seasonal transportation and storage demand costs in the PGA to better allocate the costs to the customers who cause the costs to be incurred and to provide more efficient price signals;
- the percentage increase to the interruptible class should be at least one-half the overall increase;
- the proposed bill format change to separate the distribution charge from the cost of gas charge on NSP's gas bill format.

4. In its rebuttal testimony, NSP agreed with the staff consultant proposal to exclude the unrecovered balance of the MGP clean-up costs from rate base, reducing the test year rate base by \$683,000 (net of accumulated deferred income taxes) and reducing test year cost of service by \$90,000 per year. At the hearing, staff agreed to NSP's recommendation to not impose revenue crediting for interruptible service margins above test year levels.

Summary of Disputed Issues

5. The following issues were disputed:

- The return on common equity (ROE) NSP should be allowed on the equity capital component of its capital structure. NSP proposed an ROE of 12.0%. Staff recommended an ROE of 11.3%.
- The capital structure to be used in determining revenue requirement.
- Whether the Commission should make a “merger savings” adjustment to the test year cost of service.
- The timing of MGP clean-up expense recovery.
- The propriety of an adjustment to rate base for accumulated deferred income taxes (ADIT) related to the MGP expenditures if the unrecovered MGP balance is excluded from rate base.
- The depreciation lives and depreciation rates for metallic and plastic gas mains.
- The monthly customer charge for the residential class.

The Settlement Agreement

6. The parties assert the Settlement Agreement comprehensively resolves all disputed issues in the proceeding in a manner consistent with the public interest and just and reasonable rates. The Settlement Agreement may be summarized as follows:

Base Rate Increase

7. Staff and NSP agreed to, and recommend the Commission approve, implementation of non-gas base rates sufficient to increase annual revenue for NSP’s North Dakota gas operations by \$500,000 or 1.2%, exclusive of the PGA recovery of MGP costs.

8. For purposes of settlement, the parties agreed the capital structure and return on common equity used to establish final rates shall be:

Component	Amount (\$000)	Percent	Component Cost	Total Cost
Long Term Debt	\$1,755,263	51.05%	6.99%	3.57%
Short Term Debt	155,000	4.51	4.65%	0.21
Common Equity	<u>1,528,155</u>	<u>44.44</u>	11.50%	<u>5.11</u>
Total	\$3,438,418	100.00%		8.89%

9. The Settlement Agreement states the settlement capital structure is the capital structure proposed by NSP, except \$105,320,000 of common equity is treated as long term debt to reduce the equity component by the dollar amount of preferred stock held by the parent company Xcel Energy Inc. as of December 31, 2000, the end of the test year. The Settlement Agreement also establishes certain reporting requirements for NSP’s annual financial reports to the Commission.

10. In addition, for settlement purposes only, NSP agreed to adjust the average cost of short term debt for ratemaking purposes from 6.39% to 4.65% to reflect recent reductions in short term interest rates. This adjustment is not supported by any testimony in the record, but reduces the revenue deficiency by \$26,000.

11. The Settlement Agreement states the 11.5% settlement return on common equity ("ROE") is within the range of returns supported by the testimony of Dr. Olson for NSP, who recommended a 12.0% ROE based on a discounted cash flow ("DCF") analysis with a "market to book" adjustment; and Mr. King for staff, who recommended 11.3% based on a DCF analysis. The 11.5% ROE is also 0.5% lower than the 12.0% ROE underlying NSP's present gas rates established in Case No. PU-400-95-559. The Settlement Agreement also states it does not in any way limit NSP or the staff's authority to advocate, or the Commission's authority to establish, a different capital structure or ROE in future NSP natural gas rate proceedings.

12. For purposes of settlement, staff and NSP agreed to reduce the test year cost of service by \$125,000 for merger savings.

13. In its filing update, NSP sought rate recovery of \$50,000 of estimated rate case expenses, amortized over three (3) years at \$17,000 per year, with rate base treatment of the unamortized balance. For purposes of settlement, NSP agrees to no recovery of this cost. In addition, to reach the Settlement Agreement, NSP agrees to further reduce the test year cost of service by \$50,000 annually.

14. For purposes of establishing final base rates, the Settlement Agreement provides the depreciation life for plastic and metallic gas mains shall be 45 years. The Settlement Agreement states it does not in any way limit the staff's authority to advocate, or the Commission's authority to establish, revised depreciation rates in future NSP natural gas rate proceedings.

MGP Remediation Cost Amortization and Recovery

15. The Settlement Agreement provides that NSP may amortize the \$2.88 million of MGP remediation costs over eight (8) years starting September 1, 2001, with no rate base treatment of the unamortized balance or the accumulated deferred income taxes associated with the MGP investment

16. The Settlement Agreement provides the MGP cost recovery shall occur through an adjustment to NSP's annual PGA true-up adjustment for all rate schedules subject to a cost of gas charge. The annual MGP amortization will be included in the calculation of the PGA true-up, which is modified each September 1st and applied as part of the monthly PGA adjustment beginning with the September billing cycle. This would result in an MGP cost recovery billing factor that is unchanged until the next annual PGA true-up calculation. At the end of each PGA year, the MGP cost recovery would be

compared to the amortization, and any under- or over-collections during the previous 12 month period would be included as part of the new PGA true-up factor.

17. The Settlement Agreement also provides that NSP will establish a resource adjustment tariff and billing line item for all current and future transportation service rate schedules at a rate equivalent to the MGP factor included in the effective PGA true-up, so transportation service customers contribute to the MGP cost recovery at a rate equivalent to the cost included in the PGA for comparable sales service. The Commission agrees all customers should contribute to recovery of the MGP cost to the extent possible, and customers should not face incentives to switch from sales service to transportation service to avoid the cost.

18. The Settlement Agreement further provides that NSP will establish a sub-account in Account 182 to record the dollars collected through the PGA and Resource Adjustment. NSP agrees to report the status of the MGP cost recovery in its annual PGA true-up reports to the Commission starting September 1, 2002. The report shall also document any recovery of dollars associated with the Grand Forks MGP clean-up project from third parties (insurance providers, etc.) during such PGA true-up year. Any such recovered dollars shall be accounted to shorten the MGP amortization recovery period.

19. The Settlement Agreement further provides that NSP shall terminate the PGA commodity gas cost recovery charge on the date NSP completes recovery of the \$2.88 million of MGP costs. NSP shall notify the Commission of the termination of the PGA cost recovery by filing appropriate tariff revisions.

20. Finally, the Settlement Agreement provides that any customer who had in effect a transportation service agreement for a fixed term at a fixed rate under the negotiated transportation service provisions of NSP's interruptible transportation service rate schedule as of May 1, 2001, shall not be subject to the resource adjustment for the remaining term of the customer's fixed rate transportation service agreement. Unless otherwise authorized by the Commission, however, the resource adjustment shall apply to any future transportation service agreements with such customer(s) during the eight year amortization period. However, if NSP must discount its commodity distribution charge from the maximum per therm rate, the resource adjustment component shall be discounted pro rata with the distribution charge.

Cost Allocation/Rate Design

21. For purposes of Settlement, NSP and Staff agree the residential customer charge shall be \$5.50 per month, as proposed by staff. Both staff and NSP's testimony supported the separation of the distribution charge from the cost of gas charge, elimination of the declining block commodity rates for residential and commercial classes, the seasonal PGA demand cost recovery, and restatement of the base cost of gas in the cost of gas charge.

22. In testimony, the staff and NSP agreed the overall base rate increase should be allocated so the increase to the interruptible class will be at least one-half the overall increase. The percentage increase to other customer classes shall be the pro-rata share of the overall percentage by class proposed by NSP.

23. As part of the overall Settlement Agreement, NSP agreed not to place the filed rates into effect on June 9, 2001, when the Commission's October 25, 2000 suspension notice would otherwise expire, but agreed to delay the effective date of the rate increase by 30 days to July 9, 2001. The Settlement Agreement contemplates that the revised rates would be effective for gas usage on and after July 9, 2001 and NSP agreed to submit a compliance filing containing revised rates and tariffs at least 10 days before the new effective date to allow the Commission and staff time to review the compliance filing. The Commission recognizes that this ten day time frame requires NSP to make its compliance filing by June 29, 2001, only two days after the date of this order. The Commission recognizes that NSP may need additional time from the date of this order to produce and file its compliance filing. The Commission understands that NSP also recognizes the potential need for additional time and agrees to make its compliance filing at least 10 days before the effective date of the new rates.

24. The Settlement Agreement includes standard provisions stating the Settlement Agreement does not establish principle or precedent, and is not binding if rejected or modified by the Commission.

Findings Regarding Settlement Agreement

25. The Settlement Agreement is a negotiated settlement, subject to Commission approval, and does not establish any principle or precedent, except as expressly provided therein.

26. The written Settlement Agreement, together with the information provided to the Commission prior to and at the hearing and in post hearing exhibits and submittals, provide adequate support for finding the Settlement Agreement is fair and reasonable.

From the foregoing Findings of Fact, the Commission makes its:

Conclusions of Law

1. The Commission has jurisdiction over the subject matter in this proceeding under N.D.C.C. Chap. 49-02 and 49-05.

2. The existing level of NSP's natural gas rates is inadequate to produce a reasonable rate of return on NSP's natural gas property, used and useful, for the service and convenience of the public in North Dakota.

3. NSP is entitled to a rate level adequate to provide it an opportunity to earn a reasonable rate of return on its North Dakota natural gas property, used and useful, for the service and convenience of the public in North Dakota.
4. The Settlement Agreement is fair and reasonable and in the public interest.
5. The level of NSP's natural gas rates filed in compliance with this Order will provide NSP with opportunity to earn a reasonable rate of return on its North Dakota natural gas property, used and useful, for the service and convenience of the public in North Dakota.

From the foregoing Findings of Fact and Conclusions of Law, the Commission makes its:

Order

The Commission orders:

1. The Settlement Agreement filed May 25, 2001 by NSP and Staff is approved and accepted.
2. NSP shall file revised tariff sheets, reflecting (a) rate increases required to produce a total annual base rate revenue increase of \$500,000, (b) a restated base cost of gas, and (c) implementing the rate design, as provided in this Order.
3. NSP shall file revised tariff sheets, effective for natural gas usage on and after September 1, 2001, reflecting the PGA true-up recovery of the annual MGP cost amortization described herein and implementation of the resource adjustment for transportation service rate schedules, as provided in this Order.
4. For natural gas bills rendered after the effective date of the natural gas rates as provided in this Order, monthly gas usage shall be prorated to determine the volume provided under NSP's present gas rates and new final gas rates and billed accordingly.
5. NSP shall file the revised tariff sheets for Commission approval at least ten days prior to their effective date.
6. NSP shall file annual reports providing information regarding the status of MGP cost recovery activity and any recovery from third party sources, for each July to June annual period starting with NSP's September 1, 2002 PGA true-up report.

7. NSP shall terminate the MGP cost recovery mechanisms effective on the date NSP has recovered the allowed MGP costs.

PUBLIC SERVICE COMMISSION

Anthony T. Clark
Commissioner

Susan E. Wefald
President

Leo M. Reinbold
Commissioner

STATE OF NORTH DAKOTA
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Natural Gas Rate Increase
Application**

Case No. PU-400-00-521

**Concurring Opinion
Commissioner Susan E. Wefald**

June 27, 2001

It is never easy to pass along a rate increase to customers. The Commission took a very close look at this settlement since natural gas customers have had to bear higher commodity prices for natural gas recently. This is the first time that NSP has requested an increase in distribution costs of natural gas since 1984. I concur with the Commission's findings in this case.

The Commission has made a major change in rate design in this proceeding. In the past NSP customers have used a declining block commodity rate, which means that customers paid more for their first 30 therms of gas than they did for additional gas. In this order the Commission is approving a flat commodity rate, which is better because it encourages conservation of natural gas. All gas purchased by a specific customer class will have the same rate. Due to these changes, the main change that the typical NSP residential customer will notice on their bill is the fifty cents per month increase in their customer charge, from \$5.00 to \$5.50 per month.

The Commission took a very close look at the request to bill customers for cleaning up the site of a former manufactured gas plant in downtown Grand Forks, near the Red River. The plant closed in the late 1940s, and prior to that time, the company was following legally acceptable practices for the site. However, new federal requirements for the environment made it essential that this site be cleaned up prior to this spring. NSP took care of this problem in a timely manner.

The rate increase originally asked that customers pay a rate of return on the costs of cleaning up the site of the Grand Forks former manufactured gas plant. The settlement the Commission is approving does not allow any return on the clean up costs. The \$2.8 million clean up costs are being handled in a special account through the purchased gas adjustment. Although the Commission in this order is allowing the company to bill customers for 100% of the costs of the cleanup, the costs will be billed over a period of 8 years and no interest will be allowed during this time period. Spreading the collection of this expense over 8 years, rather than 5 years as originally proposed by NSP, will encourage the company to more aggressively pursue insurance proceeds on this project.

In this settlement, the Commission is approving use of a 11.5% return on equity. Over the past few years, the Commission has used a 12% return on equity as a benchmark. However in this case, I believe that the 11.5% return is reasonable.

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**Concurring Opinion
Commissioner Anthony T. Clark**

June 27, 2001

The question before us today is whether the Commission should approve the settlement between commission advocacy staff and Xcel Energy. I believe the settlement offers a fair and reasonable conclusion to this proceeding.

The settlement is fair to consumers in that the impact will be minimal. A typical Xcel residential customer will see an increase of just over \$1 per month, averaged annually.

Although the time span between rate actions is, in and of itself, irrelevant to the necessity of changes in rates, the reasonableness of this increase is underscored by the fact that this is the first such increase in the regulated portion of consumers' rates in 17 years.

In fact, this Commission lowered rates in 1996 by \$486,000. When this is taken into account and compared with the annual revenue requirement increase of \$500,000 found in this settlement, the net effect on consumers is basically to set rates at the 1984 level.

Additionally, the justification for the settlement is sound. The natural disasters our state suffered in 1997 created costs for North Dakota. A significant portion of this settlement reflects those costs.

It is unfortunate that the recovery of these disaster related costs comes in close proximity to the volatile price swings in the commodity cost of gas we saw last winter but

it cannot be helped. Nonetheless, I believe this settlement allows for the recovery of those disaster-related costs, but does it in such a way that minimizes the effect on consumers still recovering from the increases in the unregulated portion of their natural gas bill.