STAFF MEMORANDUM

TO: COMMISSIONERS AND ADVISORS

FROM: PATRICK STEFFENSEN, ERIC PAULSON, & KRISTEN EDWARDS

RE: EL15-030 - In the Matter of the Petition of Northern States Power Company dba Xcel Energy for Approval of its 2016 Transmission Cost Recovery Eligibility and Rate Adjustment

DATE: November 5, 2015

BACKGROUND

On September 1, 2015, the South Dakota Public Utilities Commission (Commission) received a petition from Xcel for approval of a revised Transmission Cost Recovery (TCR) rider adjustment factor for 2016. The filing also requested approval of project eligibility of three new transmission projects and the 2015 tracker report for approved transmission project investments, expenditures, and revenues received.

South Dakota Codified Laws § 49-34A-25.1 through 25.4 authorize the Commission to approve a tariff mechanism for the automatic annual adjustment of charges for the jurisdictional costs of new or modified transmission facilities with a design capacity of thirty-four and one-half kilovolts or more and which are more than five miles in length.

In Docket EL07-007, the Commission approved the establishment of the TCR rider to recover the costs associated with six transmission projects. These costs were incorporated into base rates during Xcel's 2009 rate case, Docket EL09-009. As such, in January 2010, the TCR rider adjustment factor was adjusted to remove the costs related to the six transmission projects and to collect only the remaining balance in the tracker account.

In Docket EL12-035, the Commission approved TCR recovery of the 2011-2012 revenue requirement associated with fourteen new transmission projects and MISO[1] Schedule 26 expenses. The Commission approved the Settlement Stipulation supporting the "refined split method" approach for allocating MISO approved cost-shared projects with company investment.

In Docket EL13-006, the TCR rate was set at $0.00 beginning on July 1, 2013, for the remainder of 2013, due to a projected over-recovery of the 2013 TCR revenue requirements. On December 9, 2013, the Commission issued an Order Granting Joint Motion for Approval of Settlement Stipulation in Docket EL13-006. The approved Settlement Stipulation between Staff and Xcel set forth the estimated 2013 revenue requirements, including eight new transmission projects eligible for inclusion, continuance of

[1] Midcontinent Independent System Operator, Inc.

the “refined split method” for regional transmission investment, and the 2013 rate of return. The rate of $0.00 as set on July 1, 2013, remained unchanged as a result of this settlement.

In Docket EL14-016, the TCR rate was set at $0.002868 beginning on May 1, 2014, for the remainder of 2014, to recover a projected 2014 revenue requirement of $3,941,891. This amount is associated with MISO Schedule 26 expenses and 21 of the 22 transmission projects approved for recovery in Dockets EL12-035 and EL13-006. Per Commission order, all costs related to the Hollydale project were removed due to the Minnesota PUC granting Xcel’s request to withdraw the Hollydale certificate of need and route permit applications.

In Docket EL14-080, the TCR rate was set at $0.002417, effective January 1, 2015, to recover a projected 2015 revenue requirement of $4,949,726 associated with 15 transmission projects and MISO Schedule 26 expenses. This number was comprised of the 21 projects which made up the 2014 revenue requirement less the five projects incorporated into base rates in rate case docket EL14-058 and the Meadow Lake project which was removed due to the Minnesota PUC granting Xcel’s request to withdraw the Hollydale certificate of need and route permit applications. The Company did not seek eligibility determinations of any new projects in Docket EL14-080.

In this filing, Xcel requests to recover a projected 2016 revenue requirement of $5,761,200 associated with the 15 previously approved transmission projects, three new transmission projects, and MISO Schedule 26 expenses. The proposed 2015 revenue requirement results in a rate of $0.002715 per kWh, calculated based on a January 1, 2016 effective date.

Staff’s recommendation is based on its analysis of Xcel’s filing, discovery information, relevant statutes, and previous Commission orders. Staff’s review consisted of, but not limited to, the project eligibility of the three new transmission projects, the 2015 tracker report, the forecasted 2016 revenue requirement, and rate calculation.

NEW TRANSMISSION PROJECTS

In addition to the 15 previously approved transmission projects, Xcel seeks eligibility determination for the Minot Load Serving Transmission Line, Red Wing to Wabasha Rebuild, and Galloping Mitigation Near Nobles County Substation projects. Staff reviewed the eligibility of these projects given the constraints provided through statute and past commission orders and verified that proper efforts were made to ensure the lowest cost to ratepayers.

Minot Load Serving Transmission Line

Xcel is proposing a new transmission line of approximately 20 miles and a 230kV substation. The existing 115kV lines in the area will be routed in and out of the new substation. Without these facilities, the Minot area voltage cannot be maintained, and Xcel load would need to be shed.

For transmission projects, Xcel energy is able to leverage long-term agreements, established through a competitive bid process, for major materials and construction services. Through this process, they can establish long-term agreements with construction contractors and material suppliers to attain a measure of standardization.

Through planning, Xcel determined this 230 kV line as the better choice compared to their primary alternative of independent construction of a 115 kV system to address the needs in this area. A 230 kV system allowed Xcel to partner with Basin Electric Power Cooperative to address the electrical needs of both companies while jointly developing a robust 230 kV system solution at a greater cost benefit for Xcel customers.

Red Wing to Wabasha Rebuild

The purpose of this project is to maintain system reliability, as the wood structures in this five mile section are at or near their end of life. The existing wooden poles are being replaced with a combination of steel and wood poles, and during the process, the old conductor will be replaced with the company standard 835 amp conductor used on all new or rebuilt 69 kV lines.

Through discovery, it was determined the increased conductor amperage part of this rebuild was not based on need nor to accommodate new or future load growth in the area, as this five mile stretch of line will be constrained by the rest of this line, 436 Amps, which has not yet been rebuilt. Xcel acknowledges this line will not serve a new function after the rebuild, as the line was only replaced for reliability purposes due to the age and condition of the line.

While this project meets the five mile criteria and is needed for reliability purposes, it is Staff's opinion this transmission line rebuild project does not qualify as a "modified transmission facility" under SDCL 49-34A-25.1 and should be removed from the rider. Staff believes for a project to be determined modified it must be functionally different after the modification, meaning a conductor upgrade which is not constrained and is used to serve increased current or future load. Xcel does not object with the removal of this project, which reduces the 2016 revenue requirement by approximately $20,000, or $0.000010 per kWh.

Galloping Mitigation Near Nobles County Substation

Galloping is conductor motion characterized by low frequency, high amplitude "wave-like" movements. The galloping events on this line coupled with the unique regional climatic conditions and terrain in this area have caused multiple outages over the previous five years. This project employs two different methods to take the necessary steps to alleviate the galloping and associated outages on this line. Line segments will either have spacer dampers installed between the two sets of conductor, or for more severe instances of galloping, the conductor will be replaced with a relatively new product to the industry designed to mitigate galloping on the line.

Again, Xcel has acknowledged this project is solely for reliability purposes given the situation described above. The project is not needed to accommodate new or future load growth in the area, and in fact, the new conductor being installed actually has a lower capacity (3,780 amps vs. 3,938 amps) than the old.

Staff believes that although this project is necessary to deal with the outages caused by galloping events, it does not qualify as a "modified transmission facility" under SDCL 49-34A-25.1. Staff recommends removal from the rider as the work done on the lines will not result in a functionally different line, just enhanced reliability. Xcel does not object with the removal of this project, which reduces the 2016 revenue requirement by approximately $49,000, or $0.000023 per kWh.

Staff recognizes the removal of the Red Wing to Wabasha Rebuild and Galloping Mitigation Near Nobles County Substation projects seems trivial in nature, as it will merely shift potential cost recovery to the infrastructure rider. However, Staff believes it is important to adhere to state statute and remain consistent in our treatment and interpretation of modified transmission facilities to be eligible for recovery in the TCR.

OTHER ISSUES

The revised attachments reflect modifications Xcel has agreed to make to correct the following issues found during Staff's review of the model:

Jurisdictional Allocations

The demand allocators used to allocate costs to the South Dakota jurisdiction reflect the actual demand allocation for the given year (i.e. – 2015 revenue requirements based on the 2015 demand allocation). In this year's filing, these allocators got off by one year in the model (i.e. - the 2015 revenue requirements were based on the 2014 demand allocation) resulting in incorrect allocations to South Dakota. The revised attachments use corrected allocations.

Open Access Transmission Tariff (OATT) Revenue Credit

To ensure no double recovery occurs from OATT revenue collected from non-native load customers, Xcel applies an OATT revenue credit. The original filing incorrectly used 2013 and 2014 adjustment factors in the calculations. The revised attachments use correct calculations with the 2014 and 2015 adjustment factors. The jurisdictional allocation and OATT revisions combine to reduce the 2016 revenue requirement by approximately $11,000.

Revised Capital Structure

The revised attachments make the standard revision to capital structure in which the 2015 capital structure has been revised to capture actual December 31, 2014 balances. In Staff's review, it was discovered the 2014 capital structure used was incorrect in this year's model. It therefore has been revised to capture actual December 31, 2013 balances. These changes increase the 2016 revenue requirement by approximately $8,000.

Accumulated Deferred Income Taxes

On page 9 of Xcel's petition, they indicate no estimates of the potential impact of IRS regulation section 1.167(1) were available at the time of the filing. These estimates, subject to true-up, have now become available to Xcel, as the IRS has issued a number of Private Letter Rulings (PLR's) on the matter during this past year. These PLR's state that in a forecasted test period such as the TCR, a specific computation must be performed to determine the maximum amount of Accumulated Deferred Income Tax used to reduce rate base. Thus, Xcel has calculated this amount as seen in Staff Exhibit 1 and have included it in Revised Attachment 4 to reflect their current understanding of this requirement and avoid incurring a potential normalization violation from the IRS. This revision increases the 2016 revenue requirement by approximately $15,000.

2015 TRACKER REPORT

The rate approved in Docket EL14-080 was based on the balance in the tracker account and the 2015 estimated revenue requirements. In this docket, Staff reviewed the revised 2015 revenue requirement to determine if the costs were prudent and at the lowest reasonable cost to ratepayers. Staff also reviewed the Company's calculation of the under/over collection of costs incorporated in the new TCR rates, comparing actual recoveries to actual costs.

Attachment 6 summarizes the tracker activity by month for 2015. Individual project detail for the projects is found on Attachment 14.

2016 TCR REVENUE REQUIREMENT

The revised total estimated 2016 revenue requirement of $5,705,060, subject to later true-up to actual costs and recoveries, is based on the 2015 over-collection in the tracker account and the estimated 2016 revenue requirement associated with the 16 transmission projects, MISO Schedule 26 and 26A expenses, and the ADIT Pro-Rate.

Xcel's 2016 TCR continues to apply the provisions set forth in the Settlement Stipulation approved in Docket EL13-006. This includes the methodologies agreed to for each type of project:

(1) New or modified projects, ineligible for cost-sharing through the MISO tariff;
(2) MTEP-approved cost-shared projects without company investment; and
(3) MTEP-approved cost-shared projects with company investment.

For a complete discussion on the methodology applied to each project type and the projects included in Xcel's TCR, please refer to Staff's memorandum filed in Docket EL13-006.

The 2016 revenue requirement continues to apply the other provisions agreed upon in the EL13-006 settlement, including the jurisdictional demand allocators, carrying charge, and rate design. Additionally, the Company will continue to employ the same rate of return method with a true up of the 2016 rider balance calculations to reflect the cost of debt and capital structure at December 31, 2015 levels and use of the return on equity approved in its most recent rate case, Docket EL14-058.

2016 TCR RATE

The revised TCR rate is designed to be implemented effective January 1, 2016. The revised rate is calculated based on forecasted sales from January 2016 through December 2016. The revised TCR rate upon removal of the Red Wing to Wabasha Rebuild and Galloping Mitigation Near Nobles County Substation projects, effective January 1, 2016, is $0.002688 per kWh.

Reasonableness of Overall Earnings from Regulated Rates

Consistent with the terms of the EL13-006 settlement agreement, the Company will continue to file, by June 1 of each year, an annual report with the Commission detailing its South Dakota jurisdictional earnings for the preceding calendar year. Staff believes the report is necessary to monitor the Company's earnings and the potential effect of adding the TCR rider to its South Dakota tariff.

RECOMMENDATION

Staff believes the Company's filing is consistent with the settlement approved in Docket EL13-006 and consistent with prior TCR filings. Staff recommends the Commission approve the revised 2016 revenue requirements and revised TCR rate of $0.002688 per kWh, with an effective date of January 1, 2016.