STAFF MEMORANDUM SUPPORTING REVISED SETTLEMENT STIPULATION

TO: COMMISSIONERS AND ADVISORS

FROM: JON THURBER, BRITTANY MEHLHAFF, AND KRISTEN EDWARDS

RE: EL18-004 – In the Matter of the Petition of Northern States Power Company dba Xcel Energy for Approval of a Proxy Pricing Proposal to Adjust Certain Fuel Clause Rider Power Purchase Costs

DATE: February 12, 2020

Commission Staff (Staff) submits this Memorandum in support of the Revised Settlement Stipulation (Stipulation) of January 17, 2020, between Staff and Northern States Power Company dba Xcel Energy (Xcel or Company) in the above-captioned matter.

BACKGROUND

On January 29, 2018, Xcel filed a Petition for Approval of a Proxy Pricing Proposal (Petition) to address the treatment of certain power purchase costs that flow through the South Dakota fuel clause rider (FCR). The Company submitted its Petition in compliance with the settlement stipulation approved in Docket EL16-037[1], approved by the Commission in its September 19, 2017 order. Staff filed its request to suspend the FCR in order to evaluate whether certain power purchase agreements (PPAs) requested by the Company for cost recovery through the FCR were reasonable and cost effective. Staff subsequently filed a Motion and Brief to Show Cause Why Certain Costs Included in Proposed Fuel Clause Rider Should not be Disallowed. Staff identified several resources to be evaluated. The Commission issued an Order to Show Cause pursuant to Staff's motion. Ultimately, Staff and Xcel were able to come to a settlement agreement, resolving the treatment of many of the PPAs Staff challenged.

The settlement stipulation approved in Docket EL16-037 specified that an additional proceeding (Proxy Pricing Proceeding) was necessary to determine an energy proxy price for Xcel's 187 MW solar PPAs, as well as an energy and capacity proxy price for fifteen Community-Based Energy Development (C-BED) projects, and six Renewable Development Fund (RDF) projects. Such proceeding is the subject of this current docket. The application of the proxy energy and capacity pricing will be retroactive to December 1, 2016, upon completion of the Proxy Pricing Proceeding.

A review of the remaining major elements of the settlement stipulation approved in Docket EL16-037 is as follows:

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[1] In the Matter of Commission Staff's Request to Investigate Northern States Power Company's Proposed Fuel Clause Rider.

- **Aurora Solar PPA** – The actual costs of the Aurora Solar PPA contract will not be recovered from South Dakota customers. The Company is allowed to recover through the FCR a credit equal to the Company's system average cost of fuel and purchased power per kWh for the South Dakota share of the output of the Aurora Solar PPA. The Company will not recover a capacity credit associated with the Aurora Solar project for the term of the PPA.
- **187 MW Solar PPAs** – The recovery of the actual 187 MW Solar PPAs contract costs through the FCR will be replaced with an energy and capacity proxy price. The energy proxy price applicable to the 187 MW Solar PPAs will be established in the Proxy Pricing Proceeding and be applied retroactive to December 1, 2016, subject to refund. The capacity proxy price applicable to the 187 MW Solar PPA is based on MISO's 2014 Cost of New Entry (CONE) escalated on an annual basis at 2% until 2024 and applied to the MISO accredited capacity of these resources. However, no capacity proxy will be applicable to the 187 MW Solar PPAs until 2024.
- **C-BED and RDF PPAs** – The recovery of the actual RDF and C-BED PPA contract costs through the FCR will be replaced with an energy and capacity proxy price. The appropriate energy and proxy price will be established in the Proxy Pricing Proceeding and be applied retroactive to December 1, 2016, subject to refund.
- **Biomass PPAs** – The Company may recover the costs of the Biomass PPAs in the FCR for their term.
- **Natural Gas Generation Capacity PPAs** – No disallowance was reflected in the settlement.
- **FCR Filing Reforms** – For any new PPA with a term of one year or more which is requested for recovery through the FCR, the Company will include the information requested by Staff beginning with the monthly FCR filing immediately following the Commission's adoption of the Stipulation. Xcel Energy will disclose any new resource or cost recovered through the FCR that is acquired pursuant to another state's laws and initiatives in each monthly filing.
- **Net Metered Resources** – The actual costs associated with Minnesota net metering resources currently in the FCR will not be recovered from South Dakota customers.

Xcel timely filed its proxy pricing proposal within 120 days following the Commission's adoption of the stipulation. The Company identified several proxy pricing methods for the Commission's consideration and provided recommendations for application of specific proxy pricing methods applicable to the resources at issue.

On May 3, 2018, the Commission issued an Order Authorizing Executive Director to Enter into a Consulting Contract. On December 18, 2019, Staff and Xcel filed a Joint Motion for Approval of Settlement Stipulation. On January 17, 2020, Staff and Xcel filed a Joint Motion for Approval of Revised Settlement Stipulation. The Revised Settlement Stipulation amends the original Settlement Stipulation to remove an incorrect reference to C-BED regarding the proxy price agreed to for RDF PPAs and clarifies the treatment for certain C-BED PPAs.

STAFF'S ANALYSIS AND SETTLEMENT RESOLUTIONS

Staff and the Company (jointly the Parties) held several negotiating sessions to discuss Party positions regarding various proxy pricing alternatives. As a result, some Party positions were modified and others were accepted where consensus was found. Ultimately, the Parties agreed on a comprehensive resolution of all issues. Staff believes the Stipulation is based on sound regulatory principles and avoids costly litigation.

Staff's analysis of the settlement regarding the proxy pricing for each resource is discussed below.

187 MW SOLAR PPAS

In Docket EL16-037, Staff determined the 187 MW Solar PPAs were acquired to comply with the Minnesota Solar Energy Standard (SES) and there was no evidence to support these resources as cost effective compared to other resource alternatives. The EL16-037 Settlement Stipulation established a capacity proxy price beginning in 2024 with the energy proxy price to be established in the Proxy Pricing Proceeding.

Xcel proposed to apply the Company's Fall 2014 on-peak market price forecast for the MISO Minn Hub. The Company argued that using a fixed price forecast provides for a hedge against market price fluctuation, similar to the benefit a solar facility would provide. The Company utilized an on-peak price forecast as solar generally provides energy during peak hours. Xcel chose the Fall 2014 Forecast because it reflects the energy and gas prices in effect at the time the Company conducted its Strategist analysis and made the solar portfolio acquisition decisions.

Given Staff's analysis in Docket EL16-037 indicated the solar portfolio was not economic at the time the decision was made to acquire these resources, Staff did not agree with the Company's decision to use the Fall 2014 on-peak market price forecast for the MISO Minn Hub. However, Staff does recognize there is an energy value associated with these resources. Staff and the Company held several meetings to discuss different proxy pricing options that would best represent the marginal energy impact to the NSP system. The Parties discussed two alternative options to that proposed by the Company: 1) a proxy price based on Xcel's system average marginal costs and 2) a proxy price based on day-ahead locational marginal prices (LMPs).

Ultimately, the Parties agreed to a proxy price based on day ahead LMPs. The agreed upon proxy and the fixed price proxy initially proposed by Xcel are both market based proxy prices. However, utilizing the day-ahead LMPs eliminates the concern Staff has with associating the proxy with the time the decision was made to acquire the resources. While there is some pricing risk by using LMPs rather than a fixed price for the energy proxy, customers are subject to very minimal energy price risk with the existing NSP system because Xcel meets its resource needs through Company owned generation and long-term PPAs and is not reliant on short-term market purchases. In addition, these solar resources represent a very small portion of the overall NSP system resources. While the Parties also discussed use of a proxy price based on Xcel's system average marginal costs, Staff agrees the LMP method appropriately reflects the incremental energy impact of the 187 MW solar resources on the NSP system. The LMP method compensates the Company for the price Xcel would pay for market purchases absent the generation from the 187 MW solar resources and recognizes the 187 MW solar generation could be sold on the market absent use for Xcel's native load. Furthermore, Xcel will continue refunding South Dakota customers 100 percent of asset based margins through the FCR, including the margins due to the addition of Marshall and North Star. The margins ensure South Dakota customers realize the benefits associated with the asset being a part of the NSP system in the event the Company has market sales associated with these resources.

A market based proxy price could use LMPs at the generation nodes or the load nodes. Xcel receives revenue at the generation node for all generators dispatched in MISO in a particular hour. Xcel then pays for the energy to serve its load at the NSP.NSP node. While a proxy using the LMPs at the NSP.NSP node (load node) would be simpler and easier to implement, using the generation nodes (NSP.MARSHSOLAR node and NSP.NSTRSOLAR node) more precisely aligns the revenues from the additions of those projects and eliminates the risk associated with the differential between the LMPs at generation and load due to congestion.

The 2019 average day ahead LMP was $20.79/MWh for Marshall Solar and $22.34/MWh for Northstar Solar.

C-BED WIND PROJECTS

Xcel proposed an index proxy for the C-BED wind resources to account for any premium above the market price at the time the resources were acquired. The 2016 Lawrence Berkley Lab (LBL) Market Report for wind resources provides levelized PPA prices by region and by the year the PPA was executed. Xcel proposed to apply the levelized wind PPA prices using a 2009 PPA execution date for the Interior region for each C-BED PPA that exceeds the LBL Market Report price. The application of the LBL Market Report proxy provided an all-in proxy, including the energy and capacity value, for wind resources acquired in the interior region.

Staff agreed that the index proxy method proposed by Xcel is reasonable for the C-BED resources and limits administrative complexities. However, the Parties agreed to two modifications to Xcel's proposed method. First, Staff recommended using a 2010 execution date for the proxy instead of 2009 because the majority of the C-BED PPA execution dates were 2010 or later[2]. Second, Staff recommended converting the LBL values from 2016 dollars to 2010 dollars to reflect the dollar value at the time of the resource decision.

As additional support for the 2010 Interior Region PPA proxy, Staff compared the LBL index proxy to the actual resource cost of other, non-CBED wind resources owned by the Company. The Nobles Wind Farm, evaluated in Docket EL11-019, was constructed during the same general time period as the C-BED resources. The levelized cost of the Nobles Wind Farm is greater than the LBL index proxy.

The resulting C-BED proxy price is $41.98 per MWh for all C-BED PPAs with a levelized cost of energy or average $/MWh greater than $41.98/MWh. Two C-BED PPAs are less than the proxy price of $41.98/MWh and therefore, the actual PPA price applies.

RDF PROJECTS

The RDF resources include four solar PPAs, two wind PPAs and one biomass PPA. Xcel proposed that the capacity and energy proxy price established for the 187 MW Solar PPAs also be applied to the RDF solar

[2] Staff's review of the MN PUC dockets associated with the C-BED projects indicated that while certain projects were approved late in 2009, these approvals were amended in 2010, therefore these projects should be considered as 2010 execution dates instead of 2009.

PPAs, and the proxy price established for the C-BED PPAs also be applied to the RDF wind PPAs. The remaining biomass RDF PPA, Diamond K Dairy, is a small 350 kW facility and the PPA expires in 2024. Xcel proposed to use the Company's Fall 2014 7x24 average market price forecast for the MISO Minn Hub as the energy proxy for Diamond K Dairy, and no capacity proxy price was proposed in the Application for the biomass resource.

Staff agreed with Xcel's wind RDF proposal and recommends applying the proxy pricing method established for the wind C-BED projects to the wind RDF resources. Since the price of both wind RDF resources is below the 2010 Interior Region PPA proxy price of $41.98 per MWh, no adjustment is proposed to the actual PPA price.

During settlement negotiations, the Parties agreed to an alternative proxy pricing method for the solar and biomass RDF projects. Due to the relatively small size of the resources, the Parties agreed using the energy rate currently in effect for small qualifying facilities under the Company's Occasional Delivery Energy Service tariff is a reasonable proxy and is administratively efficient. The small QF rate in effect as of 01/01/2020 is $23.70 per MWh.

CUSTOMER REFUND

Pursuant to the stipulation in Docket EL16-037, the Company shall refund the difference between the proxy prices and the amounts recovered from South Dakota customers since December 1, 2016. This refund will be in the form of a reduction to future FCR rates and will occur no later than 60 days from the Commission order approving this Stipulation.

The refund due to South Dakota customers for the time period December 1, 2016 through December 31, 2019 is $3,239,554.80. Details regarding the refund amount per year and project type are provided in Attachment 2 to this memorandum. The Company will calculate the final refund amount following Commission approval of the Stipulation. The credit will be refunded to customers over a period of three months.

RECOMMENDATION

Staff recommends the Commission grant the Joint Motion for Approval of Revised Settlement Stipulation and adopt the Stipulation without modification.