

E-001/GR-91-605 ORDER SETTING INTERIM RATES

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Darrel L. Peterson	Chair
Cynthia A. Kitlinski	Commissioner
Dee Knaak	Commissioner
Norma McKanna	Commissioner
Patrice M. Vick	Commissioner

In the Matter of the Application of Interstate Power Company for Authority to Increase its Rates for Electric Service in the State of Minnesota	ISSUE DATE: October 11, 1991
	DOCKET NO. E-001/GR-91-605
	ORDER SETTING INTERIM RATES

PROCEDURAL HISTORY

I. Proceedings to Date

On August 15, 1991, Interstate Power Company (Interstate or the Company) filed a petition seeking a general rate increase of \$7,979,327, or 21.3%, effective October 14, 1991. On September 25, 1991 the Commission issued Orders accepting the filing, suspending the proposed rates, and referring the case to the Office of Administrative Hearings for contested case proceedings.

Under Minn. Stat. § 216B.16, subd. 3 (1990), the Commission is required to order an interim rate schedule into effect within 60 days, unless the Commission allows the proposed rates to go into effect. The Company included a proposed interim rate schedule in its filing. On October 1, 1991 the Commission met to set interim rates for the duration of the rate case proceeding.

FINDINGS AND CONCLUSIONS

II. Statutory Requirements

Under Minn. Stat. § 216B.16, subd. 3 (1990), interim rates are established in expedited proceedings conducted ex parte. Except under exigent circumstances, the following principles control.

Interim rates are based on proposed test year cost of capital, proposed test year rate base, and proposed test year expenses. They are calculated using existing rate design and the rate of return on common equity authorized in the company's last general rate case. Only rate base and expense items similar in nature and kind to those allowed under the Company's last general rate case Order can be included in interim rate calculations.

III. Commission Action

The Commission has reviewed the Company's interim rates proposal and finds that it complies with the statutory requirements set forth above in most respects. The Commission has made the following adjustments to bring the proposal into full compliance.

A. Two Step Interim Increase

The Company proposed two interim rate schedules, one to go into effect on October 14, 1991 and one to go into effect on May 1, 1992. On May 1 interim rates would nearly double, to reflect \$3.7 million in additional purchased power costs under new long term firm capacity contracts effective on that date.

The Commission finds it appropriate for interim rates to reflect the additional purchased power costs the Company will begin incurring on May 1. These costs are included in test year expense and were a primary reason for filing this rate case. They are recoverable in interim rates.

The Commission will not approve a two-step interim rate increase, however. It would be confusing and disruptive for ratepayers to have to deal with three rate changes in less than twelve months. Preventing customer confusion and disruption is an important regulatory goal. The Commission will therefore establish a single interim rate schedule, using the weighted average of the annual revenue increases both rate schedules proposed by the Company were designed to collect. This will allow the Company to collect the same interim revenues it would have collected under its proposal, without allowing a second interim rate increase.

B. Rate Case Expenses

The Company included in test year expense \$531,958 in rate case expenses and proposed that that amount be amortized over three years. The Commission will adjust the amount of this expense and the proposed method of recovery.

1. Amount of Rate Case Expenses

The \$531,958 figure was derived by making an inflation adjustment to the Company's expenses in its last general rate case. Although this is a reasonable starting point for estimating rate case expenses, the Commission is not convinced that Company expenditures during the last rate case were typical.

The Company appealed its last rate case decision to the Court of Appeals, which remanded three issues for further consideration. All parties briefed and argued those issues to the Court, and rebriefed and reargued them to the Commission on remand. The appeal and remand imposed substantial costs. Such costs will not be incurred in this case unless it is appealed.

Although an appeal is possible, the Commission will not assume an appeal in computing rate case expenses. The Commission will therefore adjust rate case expenses by \$86,996, the inflation-adjusted amount of rate case expense incurred in the last case between the filing of the appeal and the ORDER AFTER REMAND.

2. Recovery of Rate Case Expenses

The Company proposed to amortize the full amount of its rate case expense over the next three years. The Company's last rate case was filed five years before this one; the rate case preceding that was filed five years earlier. The Company has not shown that it is likely to file rate cases more frequently in the future than in the past. The Commission will therefore extend the amortization period from three to five years, believing five years is a more accurate estimate of the time likely to elapse before the next rate case.

The Commission will also adjust the amount of rate case expenses placed in rate base, using the amortization period average instead of the test year average. Using the amortization period average avoids the overrecovery which would result from using the test year average, assuming a five year interval between rate cases, and is therefore a more accurate and equitable recovery method.

C. Research and Development Expenses

The Company included in test year expense its \$194,122 annual dues to the Electric Power Research Institute (EPRI), an industry-supported research institute. Generally, research and development expenses are recoverable if funded projects can be expected to directly benefit a utility's ratepayers. EPRI projects generally qualify, with one exception.

For non-nuclear utilities, the Commission has consistently disallowed the portion of EPRI dues attributable to nuclear power research. The Commission disallowed 24% of Interstate's EPRI dues in the Company's last rate case, and will do again in setting interim rates. This is consistent with the statutory requirement that expense items must be similar in nature and kind to those allowed in the last rate case to qualify for inclusion in the interim rates calculation. Minn. Stat. § 216B.16, subd. 3 (1990).

D. Organizational Dues

The Company included in test year expense \$30,287 in dues to different organizations. Like research and development expenses, organizational dues are recoverable only to the extent that the activities they support directly benefit ratepayers. In the Company's last general rate case the Commission disallowed recovery of dues to local commercial clubs, local Chambers of

Commerce, local booster clubs, non-utility lobbying groups, and the portion of the Company's Edison Electric Institute dues attributable to lobbying efforts.

Since the statute limits recovery through interim rates to expenses similar in nature and kind to those allowed in the last rate case, the Commission will exclude the dues and portions of dues listed above. Excluded dues total \$8,782.

E. Competitive Rate Revenues

In projecting test year revenues, the Company calculated revenues from Farmstead Foods, a major customer, using a newly filed competitive rate schedule instead of standard rates. The Commission will not take final action on the competitive rate schedule until after interim rates have been set. This raises the question of how to count revenues from Farmstead Foods for interim rate purposes. Another complicating factor is that the competitive rates statute prohibits recovery of the difference between standard rates and competitive rates until the Commission has approved competitive rates. Minn. Stat. § 216B.162, subd. 6 (1990).

The Commission believes it is more reasonable to use competitive rates to calculate interim rate revenues from Farmstead Foods than to use standard rates. This is not to prejudge the Company's competitive rates filing. The Commission will examine that filing with its usual care and will reject it if it fails to meet statutory standards. On balance, however, the Commission considers it more likely than not that the filing, or a modified version of the filing, will eventually pass muster. The Legislature has determined that competitive rates are in the public interest, and, if Farmstead qualifies for such rates, those are the rates Farmstead should be charged.

Furthermore, the consequences of underestimating interim revenues using competitive rates (overrecovery and refund) are more manageable from a practical standpoint than the consequences of overestimating interim revenues using standard rates (underrecovery and surcharge). Refunds are a normal part of the rate case process, while surcharges pose administrative problems and cause customer confusion. The Commission will therefore base interim rates on revenue projections which assume Farmstead Foods will pay competitive rates.

However, since the competitive rates statute prohibits recovery of the difference between competitive rates and standard rates until the Commission has approved competitive rates, the Commission will impute Farmstead revenues at standard rates until the October 29 deadline for Commission action on Interstate's competitive rates filing. Minn. Stat. § 216B.162, subd. 6. This will reduce proposed interim revenues by \$11,210.

F. Interim Rate of Return

The interim rates statute requires that interim rates be based on the same rate of return on common equity that was approved in the Company's last general rate case. Minn. Stat. § 216B.16, subd. 3 (1990). The Company has proposed to base interim rates on a 12.43% return on common equity, the rate authorized in its last electric rate case. This is appropriate and will be approved.

G. Interim Cost of Capital

The statute requires that interim rates be based on the Company's proposed test year cost of capital, barring exigent circumstances. Minn. Stat. § 216B.16, subd. 3 (1990). The Company based test year cost of capital and interim rates on its current capital structure, which is within industry norms. This is an appropriate interim cost of capital.

H. Rate Design

The Company proposed to calculate interim rates by applying a uniform percentage increase on all rates in its rate schedules. This complies with the statutory requirement that interim rate schedules make no change in existing rate design. Minn. Stat. § 216B.16, subd. 3 (1990). The collection method is approved.

IV. Action Authorized

Based on the findings and conclusions discussed above, the Commission authorizes an overall rate of return for interim rates of 9.85% and a return on equity of 12.43%, calculated as follows:

<u>TYPE OF CAPITAL</u>	<u>RATIO</u>	<u>COST</u>	<u>WEIGHTED COST</u>
Long Term Debt	43.75%	7.91%	3.46%
Short Term Debt	4.77%	7.89%	0.38%
Preferred Stock	8.85%	8.07%	0.71%
Common Equity	<u>42.63%</u>	12.43%	<u>5.30%</u>
TOTAL	100.00%		9.85%

Based on the findings and conclusions discussed above, the Commission finds that the appropriate interim revenue deficiency is \$4,234,000, as shown below.

Rate of Return	9.85%
Income Deficiency	\$2,520,538
Revenue Conversion Factor	1.6798
Revenue Deficiency	\$4,234,000

Accordingly, the Commission will authorize an interim rate increase of \$4,234,000, to be collected for service rendered on or after October 14, 1991. Interim rates are collected subject to refund in the event the interim rate level exceeds the final rate level allowed in the general rate case. Minn. Stat. § 216B.16, subd. 3 (1990).

ORDER

1. Interstate Power Company is hereby authorized to collect \$4,234,000 in additional annual revenues in the form of an 11.3% increase in its retail rate schedules as interim rates, beginning with bills for service rendered on and after October 14, 1991.
2. Within seven days of the date of this Order, the Company shall file with the Commission and the Department of Public Service interim tariff sheets and supporting documentation reflecting the decisions herein.
3. The Company shall keep such records of sales and collections under interim rates as will be necessary to compute a potential refund. Any refund shall be made within 120 days of the effective date of the Commission's final Order in a manner approved by the Commission.
4. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster
Executive Secretary

(S E A L)