

E-002/M-92-2 Order from the Commission Stating that NSP Can Recover Through Its Retail Fuel Adjustment Clause Certain "Option Payments," or a Waiver of the Commission's Rules Governing Automatic Adjustments ISSUE DATE: June 16, 1992

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Don Storm	Chair
Tom Burton	Commissioner
Cynthia A. Kitlinski	Commissioner
Dee Knaak	Commissioner
Norma McKanna	Commissioner

In the Matter of a Petition by Northern States Power Company for Either a Declaratory Order from the Commission Stating that NSP Can Recover Through Its Retail Fuel Adjustment Clause Certain "Option Payments," or a Waiver of the Commission's Rules Governing Automatic Adjustments

ISSUE DATE: June 16, 1992

DOCKET NO. E-002/M-92-2

ORDER GRANTING VARIANCE

PROCEDURAL HISTORY

On December 10, 1991, Northern States Power Company (NSP or the Company) filed a petition with the Commission. In the petition NSP sought alternative relief from the Commission: either a declaratory Order confirming that NSP may recover certain option payments through its fuel adjustment clause (FAC); or a waiver of Commission rules governing automatic adjustments to allow the recovery.

On April 10, 1992, the Department of Public Service (the Department) filed its report. The Department recommended that the Commission approve NSP's petition and issue the requested declaratory Order.

The matter came before the Commission on May 27, 1992.

FINDINGS AND CONCLUSIONS

The Fuel Adjustment Clause

Minn. Rules, part 7825.0300 states that the Uniform System of Accounts (USOA) adopted by the FPC (Federal Power Commission, now known as the Federal Energy Regulatory Commission, or FERC) shall be implemented as the Minnesota USOA.

The USOA provides that receipts of fuel by electric utilities shall be recorded in Account 151, Fuel Stock, which is an inventory account. The cost of fuel consumed is then recorded in Account 501. The USOA describes Account 151 as follows:

This account shall include the book cost of fuel on hand.

Items

1. Invoice price of fuel less any cash or other discounts.
2. Freight, switching, demurrage and other transportation charges, not including, however, any charges for unloading from the shipping medium.
3. Excise taxes, purchasing agents' commissions, insurance and other expenses directly assignable to the cost of fuel.
4. Operating, maintenance and depreciation expenses and ad valorem taxes on utility-owned transportation equipment used to transport fuel from the point of acquisition to the unloading point.
5. Lease or rental costs of transportation equipment used to transport fuel from the point of acquisition to the unloading point.

The FAC is an adjustment to the customer's bill which is calculated as the difference between the cost of fuel consumed and the base cost of fuel. The base cost of fuel is defined in Minn. Rules, part 7825.2400, subparts 4 and 5 as the cost per kilowatt-hour in the base period where the FAC is set to zero. Minn. Rules, part 7825.2400, subpart 8 defines the cost of fuel as the current period withdrawals from Account 151.

Various Minnesota statutes and rules define the parameters of the FAC. Minn. Stat. § 216B.16, subd. 7 allows the Commission to permit the automatic adjustment of rates for the costs of fuel used in the generation of electricity. Minn. Rules, parts 7825.2390 et seq. implement the automatic adjustment of charges, known as the FAC when referring to the provision of electric service. Minn. Rules, part 7825.2920, subpart 2 requires that errors in the FAC will be refunded to the consumer.

Factual Background

NSP entered into a long term contract with Westmoreland Resources, Inc. (Westmoreland) in 1972. Under the contract Westmoreland provides a portion of the coal used at two NSP generating stations.

NSP and Westmoreland entered into an amendment to the contract which became effective July 1, 1986. Under the terms of the amendment, the parties reduced the minimum take provision, the quality of the coal was improved, and the price of coal was reduced approximately \$1.00 a ton.

The contract amendment called for a fixed payment of \$625,000 to be paid quarterly by NSP to Westmoreland. The quarterly payment was termed an "option payment." The amendment also provided that NSP would pay quarterly true-ups following the option payments to adjust for the effects of applicable indices. In return for the option payments, Westmoreland guaranteed the Company the right to negotiate for up to 200 million additional tons of coal at market price for delivery prior to December 31, 2050.

NSP's accounting treatment of the coal option payments changed from the effective date of the amendment until the present. From July 1, 1986 until December 31, 1987, the Company flowed all costs associated with the option payments through the FAC. On January 1, 1988, interim rates for the Company's 1987 rate case¹ went into effect. From that date the Company included the option payments in the base cost of fuel, and the costs were recovered in rates. The true-up costs were passed through the FAC until March 29, 1991, when interim rates went into effect in NSP's 1991 rate case.² Since that date, true-ups have not been included in the FAC.

On April 1, 1991, FERC auditors issued a report regarding NSP's wholesale operations. FERC stated that NSP should not include coal option payments in the wholesale FAC calculation because option payments are not part of the current cost of fuel. NSP disputes this conclusion and has filed a response with the FERC.

In its December 10, 1991 petition, NSP requested a declaratory Order approving NSP's recovery of payments through the FAC from July 1, 1986 through March 29, 1991.³ NSP requested a declaration that NSP's coal option payments are among the costs of fuel allowed in Account 151 and are therefore recoverable

¹ In the Matter of the Application of Northern States Power Company for Authority to Increase Its Rates for Electric Service in Minnesota, Docket No. E-002/GR-87-670, FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER, (August 23, 1988).

² In the Matter of the Application of Northern States Power Company for Authority to Increase Its Rates for Electric Service in the State of Minnesota, Docket No. E-002/GR-91-1, FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER (November 27, 1991).

³ The final estimate of option payments recovered through the FAC from July 1, 1986 through March 29, 1991 was \$3,512,749.

through the FAC. In the alternative, the Company requested a variance to the rules governing automatic adjustments to allow NSP recovery through the FAC.

Positions of the Parties

NSP argued that the option payments were properly flowed through the FAC because they represent compensation for current coal deliveries and are thus correctly recorded in Account 151. The Company stated that the true nature of the "option" payments was revealed in the economic benefits they confer rather than the title of the accounting treatment. According to NSP, the option payments were part of an overall negotiating strategy which resulted in substantial benefits to **current** ratepayers through lower coal prices and improved coal quality. Benefits to future ratepayers are speculative because the future contracts will be negotiated at the market price then outstanding.

The Department agreed with the Company's position. The Department stated that the term "option payment" is a misnomer because the payments have the effect of bringing current, not future, benefits. There is no future guaranteed price and little need for a guaranteed future source of coal, given the abundance of coal reserves. For these reasons, the Department recommended that the Commission find that the option payments were a part of the direct cost of current coal consumption and thus properly recovered through the FAC.

Commission Analysis

The Commission is unpersuaded that the quarterly payments known to the contracting parties as "option payments" are clearly part of the cost of fuel used for the generation of electricity under the meaning of Minn. Stat. § 216B.16, subd. 7 and the USOA list of allowed items under Account 151. The Commission is reluctant to expand the scope of Account 151 to include an item which is not on the USOA list and which on its face seems directed to future benefits rather than current costs. Because Account 151 ultimately affects the costs that are recovered under the FAC, and because the FAC allows cost recovery without prior regulatory approval, the Commission has been strict in its interpretation of allowed items. The Commission will continue with the same policy in this case. The Commission also notes that the FERC did not find that the option payments are a current cost of fuel and did not allow their recovery through the wholesale fuel clause adjustment. The Commission will not issue a declaratory Order confirming NSP's recovery of option payments through the FAC. Neither will the Commission allow the Company a variance to its automatic adjustment rules to allow such recovery.

Since the Commission as a matter of policy is not allowing NSP to include the Westmoreland contract option payments in the FAC, the issue of refunds arises. Minn. Rules, part 7825.2920, subpart 2 reads in part:

Errors. Errors made in [automatic] adjustment [of charges] must be refunded by check or credits to bills to the consumer in an amount not to exceed the amount of the error plus interest computed at the prime rate upon order of the commission

Although a refund is appropriate for most errors in automatic adjustments, the Commission is reluctant to require one in this case. The circumstances here are unique and do not form a pattern of practice. NSP has been excluding the option payments from the FAC since March 29, 1991. NSP was not ignoring prior Commission Orders on the subject, because the Commission has not previously addressed this particular set of circumstances. For these reasons, the Commission will consider granting the Company a variance to the refund requirement of Minn. Rules, part 7825.2920, subpart 2 as follows.

The Variance

Variances are governed by Minn. Rules, part 7830.4400. The Commission must grant a variance to any of its rules in an instance where it appears to the satisfaction of the Commission that:

1. Enforcement of the rule would impose an excessive burden upon the applicant or others affected by the rule;

Here, the Company had been flowing the option payments through the FAC from July 1, 1986 through March 29, 1991. Because of the passage of time it would be difficult both to account for the refund amounts and to match the refunds to the proper customers. Enforcing the refund would also mean that the benefits derived from the amended contract would have accrued to the ratepayers, yet the costs related to procuring those benefits would have been borne by the shareholders.

2. Granting of the variance would not adversely affect the public interest.

Ratepayers have received substantial net savings plus a better quality of coal as a result of the terms of the renegotiated contract. The option payments were one part of the negotiating process and resulting contract. Ratepayers have been benefitted rather than harmed overall by the existence of the renegotiated contract. Further, the Company has changed its accounting practice since the time the potential refund amount accrued. For

these reasons, granting of the variance will not adversely affect the public interest.

3. Granting the variance would not conflict with standards imposed by law.

The Commission is unaware of any legal standard which would be violated if the variance were granted.

The Commission will grant a variance to Minn. Rules, part 7825.2920, subpart 2. NSP will not be required to refund any amounts flowed through the FAC in error due to inclusion of the Westmoreland contract option payments in Account 151.

Future Treatment of Costs

The Commission notes finally that in the future NSP should consult with the Department and with Commission staff before including any item in Account 151 which is not specifically listed as a permissible item under Account 151.

ORDER

1. The Commission denies NSP's December 10, 1991 request for a declaratory Order confirming that NSP may recover option payments through its FAC, or in the alternative a waiver of Commission rules to allow such recovery.
2. The Commission grants NSP a variance to Minn. Rules, part 7825.2920, subpart 2 so that NSP is not required to refund any part of the \$3,512,749 in option payments recovered through NSP's FAC between July 1, 1986 and March 29, 1991.
3. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster
Executive Secretary

(S E A L)