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 the Application of Interstate Power Company for Authority to Increase Its Rates for Electric Service in the State of Minnesota	ISSUE DATE: October 19, 1992 DOCKET NO. E-001/GR-91-605 ORDER AFTER RECONSIDERATION

PROCEDURAL HISTORY

On June 12, 1992, the Commission issued its FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER in the above-captioned matter.

On July 1, 1992, Interstate Power Company (Interstate or the Company) filed an application for rehearing, amendment, reconsideration and reargument.

On July 2, 1992, the Minnesota Department of Public Service (the Department) filed a petition for reconsideration and rehearing.

On July 10, 1992, Interstate filed a response to the Department's petition.

On July 13, 1992, the Department and the Residential Utilities Division of the Office of the Attorney General (RUD-OAG) filed responses to the Company's petition.

On July 21, 1992, the Commission issued an Order granting reconsideration to the Company's and the Department's petitions for purposes of tolling the automatic denial provision of Minn. Stat. § 216b.27, subd. 4 (1990) and allowing the opportunity for meaningful review.

On August 13, 1992 the Company filed a Motion to Strike Staff's Briefing Memorandum, or, in the Alternative, for Leave to File Instanter its Response.

On August 13, 1992, the Commission met to consider this matter and granted oral argument to the parties requesting it, the Company, the Department, and the RUD-OAG.

FINDINGS AND CONCLUSIONS

I. Interstate's Motion

The rule authorizing parties to petition for reconsideration of final Commission Orders also prescribes the process that must attend consideration of that petition. Minn. Rules, part 7830.4100 requires a petition to be served upon all parties to the proceeding with answers to that petition filed by adverse parties within ten days. Reply by the petitioner to the adverse party's answer is specifically prohibited and a hearing is permitted but not required. Since no hearing is required, the scope of any hearing granted is within the sound discretion of the Commission.

The Company's Motion will be denied. The Briefing Memorandum submitted to the Commission by its Staff is not a party pleading but is, rather, an aid to the Commission as a summary of the parties' positions and Staff analysis of those positions. The alternative relief sought (leave to file a written response to the Staff Briefing Memorandum) is likewise unavailable. The process established by the rule does not include more than one written presentation of a petitioner's case for reconsideration. The Motion, in essence, asked the Commisison to vary the rule to permit a second petition. The Commission declines to do so because the Company has not met the requirements for a rule variance. Minn. Rules, part 7830.4400.

The Commision granted the Company an opportunity to give an oral response to the Staff briefing paper at the hearing held on this matter on August 13, 1992. This opportunity satisfied any due process concern raised by the Company.

II. Interstate's Petition for Reconsideration

Interstate argued that the Commission's Order erred in five respects:

A. Capacity Charges: the Commission should have allowed the demand or capacity charges of $1,958,117 relating to the Iowa Public Service (IPS) purchase power contract to be included in its test year cost of service;

B. Rate Case Expenses: the Commission should have allowed the Company to amortize all its rate case expense over a three year period rather than half of that expense over a five year period and allowed the first year average unamortized balance in rate base rather than one-half of that amount;

C. Rate of Return: the Commission should have authorized the Company to earn a 12.9% rather than a 10.9% rate of return on common equity;

D. Dollar Figures for Rate Base Items: the Order should have stated the dollar figures associated with two additions to the rate base: the 70 MW Lime Creek combustion turbines and the Dubuque-Clinton transmission line; and

E. Miscellaneous: the Commission should have ordered the Company to begin applying Conservation Cost Recovery Charge (CCRC) revenues to the tracker account effective with the implementation of final rates rather than as of November 1, 1991, should not have left the Company in a no-refund situation, and should have provided the Company a method of recovering its shortfall on interim rates.

A. Capacity Charges

Interstate stated that the $1,958,117 demand or capacity charges relating to the Iowa Public Service purchase power contact are includible in the test year cost of service under statutes and case precedent relating to prudency and the "used and useful" concept. The Commisison disagrees. The Company argued that the Commission's decision was erroneous for 19 reasons. The Company's arguments are incorrect as the following analysis demonstrates:

1. Basis for Disallowance

Interstate stated that the basis for disallowance is the Commission's belief that Dr. Plorin's load forecast is more accurate than Interstate's. Petition, page 2. This is inaccurate. The basis is the Commission's finding that Interstate imprudently purchased excess capacity. See Order, pages 21-24.

2. Prudence Test

Interstate stated that, in applying the prudency test, the Commission should have assumed the accuracy of the deficits forecasted by the Company and asked whether, in light of those perceived deficits, the Company acted prudently. Petition, page 56. In seeking to preclude examination of the reasonableness of the Company's forecast and the prudence of entering into major contracts in reliance upon such forecasts, the Company misstates the prudence test.

3. Differences in Load Forecasts

Interstate stated that the Commission based its decision on a difference of opinion among reasonable people regarding the accuracy of the Company's load forecast. Petition, page 3. In fact, the Commission found that reasonable minds could not differ regarding the accuracy of the Company's load forecast. The Commission found that a utility exercising due care would have checked and revised its demand forecast. Order, page 23.

4. Reserve Margin

Interstate stated that in making its decision the Commission erroneously assumed that 15 percent is the proper reserve margin over which any capacity surplus should be measured and deemed excess. Petition, page 3. The Commission made no such assumption. In its calculations, the Company treated the 15 percent Mid-America Power Pool (MAPP) minimum reserve requirement as if it were demand rather than reserve, thereby significantly understating the amount of reserve capacity that the Commission approved, i.e. declined to label as excess reserve. Using 1992 figures to illustrate, correcting the Company's error reveals that the approved reserve was 22 percent.

5. Company's Prudence Asserted, Not Shown

Interstate asserted that the preponderance of the evidence in the record proved that it acted prudently when it conducted its 1991 and 1990 load forecasts, determined capacity deficits and its need for cheap energy commencing in 1992, and entered into three capacity purchase contracts in August 1991. Petition, pages 34-35. However, the Company pointed to nothing in the record to offset the findings made by the Commission on these points in the Order.

6. Assertion That Commission Relied on Hindsight

Interstate stated that the Commission's finding of imprudence relied on hindsight rather than determining prudence based upon the facts known at the time the utility made its decision to enter into the three long-term purchase power contracts. Petition, page 6. In finding that the Company acted imprudently in relying on its 1990 and 1991 forecasts, the Commission did not use hindsight, i.e did not rely on any information unavailable to the Company at the time it relied upon those forecasts. The Commission specifically found that the Company knew or should have known, at the time it relied on the forecasts to enter the three major purchase power contracts, that the forecasts were unreliable. Flaws in the forecast that would have been apparent at this point to a utility exercising due care were: too few data points, lack of correlation between household income and peak demand, the unrealistic air conditioning market penetration, and the significant change from its previous forecast. Order, page 23.

7. Used and Useful Concept

Interstate argued that its 100 MW IPS purchase power contract may be considered "used and useful" because it displaces older, less efficient production costs. Petition, page 12. That 100 MW of electricity is more efficiently produced does not overcome the fact that the 100 MW is excess, i.e. more than is necessary to meet the needs of the Company's customers. In fact, in proposing to use the new IPS capacity to "displace" 100 MW from one of its

other plants, the Company is idling the other plant, eliminating their costs of producing 100 MW thereby demonstrating the very excess capacity it denies. The Commission addressed this argument in its Order at page 22:

> The Company misunderstands the concept of excess capacity. If the Company, through its current generating capacity and the capacity it has contracted for, has total capacity that exceeds the needs of its customers by 100 MW per year, that amount is excess capacity. If the Company chooses to use the contracted capacity to meet its customers' needs, the Company must necessarily not use 100 MW of capacity available from its current generating facilities. It is not relevant to the "used and useful" analysis which portion of the Company's capacity it chooses to actually use to meet its customers needs; the remaining portion (100 MW) is excess capacity. This amount will not be "used and useful" to meet ratepayer demand.

8. The IPS Contract

Interstate argued that the IPS contract supplied the Company's ratepayers with a cheap source of energy. Petition, page 14. In this argument and recurring throughout its Petition, the Company erred in focusing on the specific IPS contract as if that contract had been disallowed. The Commission was quite clear that it was not disallowing the IPS contract as such, but merely using the price of the IPS contract's 100 MW as a proxy for the value of the 100 MW excess capacity it found. The Commission stated at page 22:

> ...the Commission concludes that the Company's three long-term contracts will result in the Company having excess capacity in the amount of 100 MW per year during each of the next five years. This amount of electricity is not "reasonably necessary to the efficient and reliable provision of utility service" and therefore fails the "useful" prong of the used and useful test. Accordingly, the cost of 100 MW per year must be excluded from the test year cost of service. A convenient and appropriate proxy to indicate the cost of this amount of electricity is the price the Company has contracted to pay IPS for 100 MW per year. The IPS contract amount for 100 MW per year, $1,958,117, will be excluded from the test year cost of service.

9. Accuracy of Load Forecast

Interstate argued that its load forecast was reasonably accurate. Petition, pages 15-28. The Commission's Order analyzed that load forecast in detail and found it invalid, for reasons fully explained in the Order, pages 18-20.

10. Importance of Particular Testimony

Interstate argued that it was of great significance and importance that the Department's witness Dr. Plorin never testified that the Company's load forecast was not accurate. Petition, page 21. This fact has no great importance. The Commission is not restricted to adopting conclusions reached by witnesses, but may draw its own, based on the evidence, as it has done in finding the Company's forecasts invalid. Order, page 20.

11. Record Support for Conclusion

Interstate asserted that the Commission's finding that the Company should have used MAPP purchases to meet its long-term capacity needs was not supported by competent evidence. Petition, page 25. The Company overstated the scope of the Commission's finding on this point which was that the Company's failure to consider the capacity available through MAPP compounded the Company's already defective demand forecast and that the Company should have considered MAPP purchases as an alternative to the capacity purchases. Order, page 20. The record supports the Commission's conclusion. See, e.g. Direct Testimony of Dale Lusti, page 13.

12. Claimed Savings Based on Invalid Forecast

Interstate argued that the IPS capacity costs should be allowed into the Company's test year cost of service because they save ratepayers generation and transmission costs and $147.6 million avoided baseload generation and construction costs during the next 10 years. Petition, page 28. To clarify, $147.6 million is the amount that the Company asserted it saved as a result of all three August 1, 1991 contracts, not simply the IPS contract. More importantly, however, the Company's claimed savings are altogether unconvincing because they are based upon its own load forecast which the Commission has found invalid, as indicated previously.

13. Claimed Savings Not Documented in Record

Interstate alleged that the Commission erred in not crediting Interstate's shareholders with the vast energy savings (avoided fuel costs) due to the IPS purchase power contract. Petition, page 28. The Commission finds that the Company did not document such savings in the record, thereby failing to meet its burden of proving the value of the alleged energy cost savings. In these circumstances, no offset is possible. Furthermore, since Interstate's energy costs are fully recovered in the fuel clause adjustment, its shareholders are not harmed by not receiving credit for purported savings by ratepayers.

In light of the Company's failure to establish these cost savings in the record, it is unnecessary to discuss the Company's assertion (Petition, page 29) that denying Interstate's shareholders recovery in recognition of alleged avoided fuel costs deprives them of constitutional rights.

14. Constitutional Claim Without Foundation

Interstate argued that its constitutional rights were violated because the Commission a) eliminated the IPS capacity purchase, b) failed to allow 100 percent recovery of its rate case expense, and c) adopted a rate of return on equity that was outside the range of reasonableness. Petition, page 32. Each of these issues is discussed elsewhere in this Order: elimination of 100 MW capacity costs at pages 3 to 9; rate case expenses at pages 9 to 10; rate of return at pages 10 to 13. In light of the Company's failure to establish that any of these decisions was unreasonable, the Commission need not discuss the Company's constitutional claim further.

The Commission notes that the United States Supreme Court case Duquesne Light Company and Pennsylvania Power Company v. Barasch, 488 U.S. 299, 109 S.Ct. 609, 102 L.Ed.2d 646 (1989) indicated that proof that some of the component parts of a rate order were unreasonable does not mean that there is an unconstitutional taking of the utility's property. To prevail on such a constitutional claim, the Court indicated that a utility would have to prove that the total overall effect of the rate order was below the range of reasonableness, that the utility was left with unreasonable operating capital or that the utility was impeded in its ability to raise future capital, or that the rate was inadequate to compensate the investor for the risks associated with a modified prudent investment scheme. The Company has made no such showings.

15. Benefits Test

Interstate argued that under the "benefits test" adopted by the Commission in previous Orders, the Commission reviews utility operating expenses not specifically covered by statute by requiring them to be reasonable and prudent and then determines whether the expense can reasonably be expected to return benefits that will enure to the benefit of the utility's ratepayers. The Company applied the benefits test to the IPS contract and concluded that the Commission should allow this cost because the contract's cheap energy clearly benefits Interstate's ratepayers. Petition, page 35.

Again, Interstate erred in focusing on the specific IPS contract. As explained previously, the Commission did not disallow the IPS contract. Instead, the Commission 1) found that Interstate's three purchase power contracts imprudently resulted in 100 MW excess reserve, 2) determined that this amount was not "used and useful", and 3) used the IPS contract price as a proxy to

determine the dollar value of the 100 MW capacity that it excluded. Order, page 22-24.

16. Reserve Level

Interstate argued that the Commission exceeded its legislative authority and violated public policy by setting a 15 percent capacity reserve margin level. Petition, page 36. The Company also asserted that the Commission's establishment of a 15 percent reserve margin requirement abandoned its prior precedents in violation of due process considerations (Petition, page 52) and was not supported by the evidence (Petition at page 42). As indicated earlier, the Commission did not adopt such a 15 percent reserve level as alleged by the Company.

17. Standard of Proof

Interstate alleged that the Commission had required a higher standard of proof than preponderance of the evidence with respect to several issues. Petition, page 39. To illustrate the alleged higher standard, the Company stated that the Commission had adopted Department witness Plorin's load forecast as "more accurate" than Interstate's whereas all the Company had to prove was that the Company acted reasonably under the circumstances known at the time and that its forecast was reasonably accurate. Petition, page 40.

The Company is incorrect in asserting that the Commission found that, among two reasonably reliable forecasts (the Departments' and Interstate's), it merely found the Department's the more reliable. The Commission did not simply find the Company's forecasts inferior to the Department's; it found them invalid. The Commission stated:

> The Commission finds that the Department's criticisms of Interstate's forecast[1] are well-founded and demonstrate the invalidity of the Company's forecast. Order at page 20.

Interstate also alleged that the Commission ignored the Company's evidence which, the Company asserted, outweighed the Department's. Petition, page 41. The fact that the Commission found differently from what the Company would like does not demonstrate that the Commission held the Company to a higher standard than preponderance of the evidence.

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[1] The criticisms cited in the Order at page 19 were: (1) the Company's model contains more explanatory variables than the data can support; (2) the model includes an explanatory variable (economic activity as measured by household income) that is not correlated with peak demand and is not stable; (3) Interstate's air conditioning market penetration assumption is not credible.

18. Fuel Adjustment Clause and Sales of Excess Capacity

Interstate requested that the Commission amend it Order to authorize the Company to flow any recovery from any sales of capacity costs through its fuel adjustment clause. Petition, page 55. In its Order, the Commission stated:

> The Commission finds that the mechanism proposed by Interstate to deliver the benefit of the sales of excess capacity to customers is inappropriate. The fuel clause is not a method to offset various costs and revenues unrelated to fuel. The Commission finds that this proposal is unreasonable and conflicts with the intent of the fuel clause.

Interstate provided no argument to dispute those findings.

19. Fuel Adjustment Clause and System Average Energy Cost

Interstate requested that the Commission amend its Order to permit it to use the fuel adjustment clause of the law to permit it to pass through system average energy cost, excluding IPS energy, in place of the $.012 cents/kWh costs from the IPS contract. Again, the Company proposed using the fuel adjustment clause in a manner not contemplated by the legislature when it enacted the fuel adjustment clause statute, Minn. Stat. § 216B.16, subd. 7 (1990). The purpose of the fuel clause is to recover actual fuel costs. Through this clause, the Company recovers exactly what it costs them. To pass additional costs through the clause, as requested by the Company, would result in over recovery of fuel costs and would be contrary to the purpose of the statute.

B. Rate Case Expense Amortization

In its Order, the Commission allowed Interstate to recover one-half of its rate case expenses by amortizing this amount over a five year period. Interstate asserted that it should have been allowed to recover all of its rate case expenses over a three-year period.

1. Five-Year Amortization Period

Interstate did not dispute that there have been five year intervals between the Company's last three rate cases. The Company's suggestion that it will file its next rate case in fewer than five years is insufficient in light of the potential harm to ratepayers. If a three-year amortization were adopted and the historical pattern were maintained, the Company would overcollect for this item beginning in year four. In selecting a five year amortization, the Commission has selected a period that the record indicates is least likely to result in over- or

underrecovery. In these circumstances, a five-year amortization period is clearly reasonable.

The Company cited Minnesota Power and Light's 1988 rate case Order[2] and argued that since the Commission allowed MP to amortize its rate case expenses over a three year period even though its previous rate case had been approximately six years ago it was discriminatory not to allow the Company a similar three year amortization period. The appropriate amortization period in any case depends on the Commission's finding of fact regarding the likelihood of when the utility in question is likely to file another general rate case. Such a determination is based on conditions known to the Commisison at that time and will vary over the years and from company to company as conditions change. The Company misperceives such a finding as a precedent which may be mechanically invoked.

2. Rate Base and Operating Income Treatment

Interstate disagreed with the Commission's finding that the burden of defraying its rate case expenses should be shared between ratepayers and shareholders. The Company argued that Minn. Stat. § 216B.16, subd. 6 (1990) required the Commission to allow it to recover all of its prudently incurred expenses. Accordingly, the Company contended that it was entitled to recover all its rate case expenses. It asserted that expense sharing between ratepayers and shareholders was restricted to imprudently incurred expenses or to expenses that, although they were prudently incurred, become no longer used and useful due to subsequent events beyond the control of the parties.

Minn. Stat. § 216B.16, subd. 6 (1990) does not restrict the Commission's discretion to relieve ratepayers of the burden of expenses to the situations described by the Company. The ultimate goal is fair and equitable rates. Inherent in the Commission's responsibility to determine fair and equitable rates is the authority to require that ratepayers not bear the entire burden of costs that provide substantial benefit directly to shareholders. While as recently as its Order in NSP's 1991 rate case[3], the Commission allowed NSP full recovery of its lawful rate case expenses, the Commission is not forever required to

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[2] In the Matter of the Petition of Minnesota Power and Light Company, d/b/a Minnesota Power, for Authority to Change Its Schedule of Rates for Retail Elctric Service in the State of Minnesota, Docket No. E-015/GR-87-223, FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER (March 1, 1988), page 63.

[3] 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 (November 27, 1991), page 14.

allow utilities such full recovery. In this case, the Commission's view of rate case expenses has evolved to an understanding that rate case expenses clearly benefit shareholders as much as ratepayers. In light of this understanding, the Commission finds a 50/50 division of rate case expenses equitable.

C. Rate of Return on Common Equity

Interstate argued that the 10.9 percent return on equity violated the capital attraction test because a) it was not commensurate with returns being allowed other companies in similar circumstances, b) it failed to recognize that the Company would begin a major construction project at the beginning of the next century, c) it was out of line with the FERC benchmark return for the period November 1, 1991 through January 31, 1992, and d) the Commission had not checked the DCF analysis it relied on with reference to any other indicator.

1. Returns Allowed Other Companies

Interstate cited a rate of return allowed it recently by the Iowa Utilities Board (IUB) as a valid check upon the 10.9 percent return on equity approved by the Commission. The Company also cited IUB decisions for other utilities. None of this cited information appears in the record of the case and, therefore, may not be used as the basis for any finding in this case.

> No factual information or evidence shall be considered in the determination ofthe case unless it is part of the record. Minn. Stat. § 14.60, subd 2 (1990).

Nor did Interstate invoke the process established by Minn. Stat. § 14.60, subd. 4 (1990) to, in effect, expand the record to include these facts by the Commission taking official notice of such facts.

Moreover, even if Interstate had made the IUB decisions a part of the record, the Commission does not find them persuasive. It is the returns of comparable companies, not the decisions of other commissions, that form the basis for determining if the return meets the capital attraction test. Federal Power Commission v. Hope Natural Gas, 320 U.S. 591, 603 (1944). The Commission's reluctance to rely on particular rate of return findings of another commission stems from an unwillingness to abdicate its responsibility to evaluate a proper rate of return based on the particular circumstances of the utility before it, circumstances that have been established in the record of that particular case.

Interstate also cited returns that the Commission has approved for other companies. The Commission's own Orders need not be specifically introduced into the record and are available for whatever precedential value they may have. However, regarding return on equity, the Commission finds the cited Orders are

distinguishable from the present case. The return on equity adopted in each case was adopted based on the facts presented in the case. The Commission's decision in each case depended upon its evaluation of the particular company's characteristics and the market conditions prevalent at the specific time period in question. For this reason, rate of return findings are not precedent for future cases.

In short, the cases cited by Interstate do not provide useful checks on the return approved for Interstate based on the record in this case.

2. Interstate's Proposed Construction Program

Interstate argued that the Commission failed to give proper weight to the fact that the Company has a plan to build large power plants at the beginning of the next century. According to Interstate, the Commission should have approved a higher rate of return to attract the capital necessary to construct those facilities. The Company's claim is entirely speculative. There is nothing in the record to demonstrate that a higher rate of return will be necessary to attract this capital. Further, the projected construction will not begin for approximately eight years. The Commission finds that it would be inappropriate to allow the Company to earn that higher rate of return during the time that the rate of return authorized in this case is likely to be in effect.

3. The FERC Benchmark

Interstate argued that the fact that the Federal Energy Regulatory Commission (FERC) benchmark in effect when the intervenor direct testimony was filed (November 1991) was 11.47 percent indicated that a 10.9 percent rate of return is unreasonable. Petition, pages 67 and 69. It does not appear that the fact relied on by the Company (what the FERC benchmark was in November 1991) has been made a part of the record. As such, it may not be considered in the determination of this case. Minn. Stat. § 14.60, subd. 2 (1990). Nor did Interstate invoke the official notice process established by Minn. Stat. § 14.60, subd. 4 (1990) to expand the record to include this fact.

However, even if the Company had made the FERC benchmark figure a part of the record of this case, the Commission would not be persuaded that it indicates the unreasonableness of the rate of return figure adopted by the Commission in its June 12, 1992 Order. The Commission's valuation of the FERC benchmark is as follows:

In July 1984, FERC adopted procedures for generically determining a benchmark rate of return for electic utilities and in 1985 began publishing a benchmark rate of return on a quarterly basis. FERC calculated the benchmark cited by the Company by averaging the rates of return of 97 companies. By the time of the hearing

on Interstate's rate case before the ALJ in January 1992, FERC had discontinued the practice of issuing benchmarks. The benchmark was always a very rough check upon the reasonableness of a rate of return. Being calculated without regard to any particular company, it did not compare companies similarly situated to the company whose rate request was being examined. Furthermore, the benchmark was simply an average of 97 companies, so obviously many companies had rates of return below 11.47 percent. Interstate provided no evidence that the companies used by FERC having rates of return higher than 10.9 percent were comparable to it.

In short, even if it were a part of the record, the FERC benchmark would not demonstrate the unreasonableness of a 10.9 percent rate of return for Interstate. If anything, the benchmark would support the reasonableness of the 10.9 percent figure, which is approximately half a point from the benchmark figure. In light of its limitations, the benchmark clearly fails to show that the 10.9 figure is outside the range of reasonableness.

4. CAPM as a Check on the Reasonableness of the 10.9 Percent Return on Equity

Interstate argued that checking the 10.9 percent figure with a Capital Asset Pricing Model (CAPM) demonstrated the unreasonableness of that figure. Petition, page 62. The Company cited the CAPM done by its witness Jackson that produced a 12.68 percent rate for the cost of equity.

The Commission agrees that a CAPM can provide a useful check on the reasonableness of the 10.9 percent rate of return but notes that figures produced by CAPMs vary widely depending on what values are utilized in the standard CAPM formula. A CAPM done by the Department produced a rate of return of 10.35 percent.

The Department's CAPM is a more reliable check upon the reasonableness of the rate selected by the Commission because it utilized a more accurate risk premium factor. In rejecting Mr. Jackson's CAPM results, the Commission notes that his risk premium factor substantially overstated the gravity of the risks and uncertainties facing Interstate during the relevant time period.

5. Comparable Group Studies

Interstate asserted that the Commission should have checked its rate of return against a comparable group study as its witness Jackson had done in choosing his 12.9 percent figure. Petition, page 64.

In fact, the Commission selected the 10.9 percent rate of return for Interstate based on a comparable group study, one submitted by RUD-OAG witness McIntire. The Commission found that

Dr. McIntire's comparable group analysis was a reliable indicator of investor expectations during the relevant time period and based the dividend yield portion of the rate of return calculation on that study. The Commission specifically rejected the comparable group study done by Mr. Jackson in his DCF analysis, finding that unlike Dr. McIntire he had not selected a group of truly comparable companies. The Commission rejected the Company's five other methods because they were not market oriented and did not reflect current market conditions. Order, page 36. In arguing for reconsideration of this issue, the Company noted no flaw in Dr. McIntire's comparable group study and provided no argument to rehabilitate Mr. Jackson's studies.

6. Growth Rate Factor

Interstate suggested that the 10.9 percent rate of return was unreasonable because Dr. McIntire's DCF method produced that figure using a 3.5 percent growth rate factor rather than a four percent average expected growth rate as contained in the Value Line edition of January 17, 1992. The Commission finds that it would have been inappropriate to use the four percent average expected growth rate proposed by the Company because that figure is financial information from outside the relevant time period.

Dr. McIntire's 3.5 percent growth rate factor is reasonable. Dr. McIntire calculated that rate by averaging the projected per share growth rates in earnings, dividends and book value. He then evaluated that figure in the light of current and expected economic trends and found it appropriate. The Company did not attempt to demonstrate that the 3.5 percent figure was invalid, but simply observed that if the Commission had adopted a four percent growth rate it would have achieved an 11.446 percent ROE, quite close to the FERC benchmark. Due to the irrelevance of the FERC benchmark as demonstrated earlier, the Company's observation provides no basis for rejecting the 3.5 percent growth rate adopted by the Commission.

7. Summary of Interstate's Rate of Return Arguments

Having carefully reviewed Interstate's arguments on this point, the Commission finds that the Company has provided nothing to influence the Commission to reconsider its finding that a 10.9 percent return on equity is fair and reasonable based on the record established in this case.

D. Dollar Figures Associated With Two Rate Base Items

The Minnesota rate base approved by the Commission included the following amounts: $4,107,443 for the combustion turbines and $4,131,375 for the transmission line and substations. Interstate requested that the Commission amend its Order to specifically state the amounts allowed into rate base due to the addition of the 70 MW Lime Creek combustion turbines and the Dubuque-Clinton transmission line.

Because no party contested the inclusion of these items in the rate base and the Commission found them reasonable, the items were included in the rate base without individual comment in the Order. The Commission finds no reason to alter that treatment in this case.

E. Miscellaneous

1. Effective Date for CCRC Charges

The Commission's Order required Interstate to begin recording the revenue received through its Conservation Cost Recovery Charge (CCRC) in the CIP Tracker Account as of November 1, 1991. The Company requested that the Commission modify its Order to require application of the CCRC to the Tracker Account beginning with the implementation of final rates.

In its Order, the Commission approved CIP amounts larger than those used in calculating interim rates. Interstate argued that it is confiscatory to require it to cover those increased CCRC amounts retroactively, i.e. back to November 1, 1991. Petition, page 56. The Commission disagrees.

Interim rates are set exparte, without the benefit of the fully-develped record used to determine final rates. By their very nature and purpose, interim rates and final rates will normally be based on a number of different elements and dollar amounts. Some elements used in setting interim rates in this case were higher than those approved for final rates. For example, interim rates used the full amount of the purchase power contracts, if only for the one and one-half month period, while for final rates 100 MW from those contracts was disallowed. Similarly, the rate of return on common equity for interim rates was figured at 12.43 percent rather than the 10.9 percent figure authorized for final rates. Overall, then, the revenue level collected during the interim period was neither unreasonable nor confiscatory.

2. Lack of Refund Obligation

Interstate complained that it has been damaged because it is not in a refund posture as a result of the Commission's Order. It speculated that if it had been ordered to make a refund, the Commission would have allowed it to recover its rate case expenses dollar for dollar because it would have been able to deduct those expenses from its refund obligation. Petition , page 57. There is no substance to that speculation. As the Commission's discussions in its initial Order and this Order After Reconsideration indicate, the rate case expense issue was decided on its merits, without regard to the Company's refund situation.

Moreover, it is a curious protest by a utility against the Commission that it authorized higher final rates than interim rates and that, as a consequence, the company was not required to

refund any money.

3. Recouping the Shortfall on Interim Rates

Interstate stated that the Commission had not provided the Company a means to recoup its shortfall on interim rates as required by Minn. Stat. § 216B.16, subd. 5 (1990). Petition, page 57. The statutory requirement found at Minn. Stat. § 216B.16, subd. 3 (1990) is not that a utility recover the difference between interim rates and final rates during the entire interim rates period as the Company's term "shortfall" suggests. Instead, the statute authorizes the Commission to prescribe a method for the utility to recover the difference in revenues from the date of the final determination to the date that the new rate schedules are put into effect.

The Commission routinely provides for such recovery in rate cases where final rates are higher than interim rates. By inadvertence, an Ordering Paragraph executing that statutory responsibility was omitted from the Commission's June 12, 1992 Order. This Order will include the appropriate ordering language. See Ordering Paragraph 4.

III. The Department's Petition for Reconsideration

In its Order, the Commission stated at page 17:

> The Commission finds that when the Company paid dues to local commercial clubs, town Chambers of Commerce, and various other local business, community, civic, development and booster clubs, it incurred those expenses "for economic and community development" within the meaning of Minn. Stat. § 216B.16, subd. 13 (1991) and will exercise its discretion to allow recovery of these expenditures.

The Department requested that the Commission reconsider the basis of its decision to allow Interstate to recover certain economic and community development expenses. The Department disagreed with the Commission's finding that under the new statute [Minn. Stat. § 216B.16, subd. 13 (1991)] expenditures may be considered for recovery regardless of whether they are directly related to providing utility service, or whether they confer a benefit upon ratepayers. The Department argued that the new statute did not override the provisions of Minn. Stat. § 216B.16, subd. 6 (1990) that the Commission give due consideration to the need of the public utility for revenue sufficient to enable it to meet the cost of furnishing the service which, according to the Department, require that the investment and expenses be reasonably related to the provision of utility service. The Department noted that under the broad interpretation adopted by the Commission in its June 12, 1992 Order, it would be legal to allow a utility to recover its investment in hotel franchises as economic development. The RUD-OAG supported the Department's

position.

Interstate argued that the new statute clearly intended to give the Commission the discretion to allow expenses for community and economic development that are likely or possible in the future to provide a benefit to ratepayers, even if no immediate benefit may be shown.

Upon reexamination of the pertinent statutory language, the Commission finds that in adopting the new statute expressly authorizing the Commission to allow recovery of community and economic development expenditures the legislature did not evince a clear intent to repeal the applicability of Minn. Stat. § 216B.16, subd. 6 (1990) as to those items. Accordingly, the Commission will consider the requirements of Minn. Stat. § 216B.16, subd. 6 (1990) (requirements that expenses will be allowed to the extent that they relate to the provision of utility service and benefit ratepayers) in determining the allowability of expenditures identified as economic and community development expenses.

In light of these requirements, the Commission finds that the expenses in question bear a reasonable relationship to the provision of utility service (in light of the expressed purpose of the new statute) and do benefit the ratepayers. However, the Commission also finds that community and economic development in the Company's service area is in the long run benefit of shareholders as well and provides immediate public relations benefits of value to the shareholders. In these circumstances, it is more appropriate that ratepayers and shareholders share the burden of these expenses equally. Therefore, the Commission will allow 50 percent of these expenses, rather than the 100 percent granted in the Commission's June 12, 1992 Order, to be recovered from the ratepayers as test year expenses. Allowing 50 percent of these expenses rather than 1oo percent reduces this expem\nse by $3,200. The overall deficiency is reduced by the same amount, resulting in a revenue deficiency of $4,857,800.

ORDER

1. The petition of Interstate Power Company (Interstate) for reconsideration of the June 12, 1992 FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER in this matter is denied.

2. The petition of the Minnesota Department of Public Service (the Department) for reconsideration of the June 12, 1992 FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER in this matter is granted to the extent described in the text of this Order. Specifically, allowance of the economic and community development expenses allowed in the June 12, 1992 Order is reduced from 100 percent to 50 percent.

3. Ordering Paragraph 1 of the June 12, 1992 Order is amended to read:

> Interstate Power Company is entitled to increased annual revenue of $4,857,800 to produce total annual operating revenues of $42,253,551.

In all other respects, the requirements of the June 12, 1992 Order remain unchanged.

4. Within 30 days of the date of this Order, if Interstate feels it necessary to recover the difference between interim rates and the final increase granted herein in the period from the date of this Order until implementation of final rates, it shall file a proposal for doing so with the Commission, for its review and approval. Parties shall have 15 days to submit comments on the Company's proposal.

5. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster
Executive Secretary

(S E A L)