G-002/GR-92-1186 ORDER AFTER RECONSIDERATION

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Don Storm	Chair
Tom Burton	Commissioner
Marshall Johnson	Commissioner
Cynthia A. Kitlinski	Commissioner
Dee Knaak	Commissioner

In the Matter of the Petition of Northern States Power Gas Utility for Authority to Change Its Schedule of Gas Rates for Retail Customers Within the State of Minnesota	ISSUE DATE: December 30, 1993 DOCKET NO. G-002/GR-92-1186 ORDER AFTER RECONSIDERATION

PROCEDURAL HISTORY

On November 2, 1992, Northern States Power Company's Electric Utility (NSP Electric) and Northern States Power Company's Gas Utility (NSP Gas) each filed a petition seeking a general rate increase.

On September 1, 1993, the Commission issued its FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER in the NSP Gas rate case. In that Order the Commission resolved a number of issues which were common to both rate cases, including rate case treatment of incentive compensation.

On September 29, 1993, the Commission issued its FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER in the NSP Electric rate case.

On September 21, 1993, NSP filed a Request for Reconsideration or Rehearing on Common and Gas Issues.

On September 21, 1993, the Residential Utilities Division of the Office of the Attorney General (RUD-OAG) filed a Petition for Reconsideration.

On October 1, 1993, responses to NSP's petition were filed by the RUD-OAG, the Department of Public Service (the Department), Minnesota Energy Consumers (MEC), and the Suburban Rate Authority (SRA). MEC advocated denying the Company's request for reconsideration. The SRA recommended denying reconsideration on the incentive compensation issue.

NSP filed a response to the RUD-OAG's petition on October 1, 1993.

On October 5, 1993, the Commission issued its ORDER GRANTING RECONSIDERATION for the purpose of tolling the statutory 20-day time limit for granting reconsideration.

On October 6, 1993, the Department filed a letter clarifying prior comments.

On November 10, 1993, the matter came before the Commission.

FINDINGS AND CONCLUSIONS

I. COMMON ISSUES

A. Rate of Return

1. The September 1, 1993, Order

In its original Order, the Commission determined that NSP's required return on equity (ROE) should be set at 11.0%. In making this determination, the Commission relied on the testimony of Department witness Dr. Luther Thompson. The Commission found that the discounted cash flow (DCF) methodology was the most appropriate one for determining the Company's required ROE, and that applying the DCF method to NSP produced a dividend yield of 6.0% and a growth rate of 5.0%. The Commission rejected the Administrative Law Judge's recommendation to add a flotation cost adjustment to the DCF result.

2. Positions of the Parties

Two parties to the case requested that the Commission reconsider its decision that the appropriate ROE for NSP is 11.0%. NSP argued that the Commission must adjust the ROE to a level which is more consistent with the Hope/Bluefield[1] criteria and with decisions being reached in other NSP retail rate cases. The RUD-OAG argued that the Commission should reconsider and adopt the recommendation of RUD-OAG witness Mr. Matthew Kahal, who proposed an ROE of 10.6%.

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[1] The Hope and Bluefield criteria are derived from two United States Supreme Court cases frequently cited in the context of utility ratemaking, Bluefield Water Works and Improvement Co. v. P.S.C, 262 U.S. 679 (1923), and FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944). These cases contain the following guidelines for rate of return decisions:

1. The allowed rate of return should be comparable to that generally being made on investments and other business undertakings which are attended by corresponding risks and uncertainties;

2. The return should be sufficient to enable the utility to maintain its financial integrity; and

3. The return should be sufficient to attract new capital on reasonable terms.

In its petition, NSP argued that the Commission erred in using a single method and a single witness's recommendation to determine the appropriate ROE. In addition, NSP contended that the 11.0% ROE is unreasonably low and is inconsistent with the requirements of Hope and Bluefield. NSP argued that if the Commission were to continue to support Dr. Thompson's recommendation, it should consider making the following corrections: the dividend yield should be averaged forward to account for first year dividend growth; the Commission should place little or no weight on volatile earnings per share growth and analysts' forecasts of short-term future growth; and the Commission should add a flotation adjustment to its ROE determination. NSP did not offer an alternative calculation for rate of return.

RUD-OAG argued that Mr. Kahal's growth analysis satisfied all of the criteria used by the Commission. According to the RUD-OAG, Mr. Kahal looked at historical information both in his earnings retention analysis and on a stand-alone basis, and he relied on current and future economic trends. Investor analyst projections from Value Line and IBES confirmed the reasonableness of his 4.4% - 4.5% growth formulation.

According to RUD-OAG, the Commission erred in rejecting Mr. Kahal's growth rate due to his use of 1992 data. The Commission had found 1992 data to be unreliable because it was based on conditions which were not expected to reoccur in the near future. RUD-OAG argued that Mr. Kahal acknowledged and discounted 1992 data, both for the Company and for the industry as a whole, in his earnings retention analysis. When performing analyses which excluded 1992 data, the results of those analyses were still below his actual growth recommendation. RUD-OAG concluded that Mr. Kahal's use of 1992 data in some of his analyses did not lower his growth estimate below that which investors require.

3. Commission Action

After reviewing the record, the Commission concludes that a more appropriate ROE for NSP is 11.47%. The Commission continues to find that the DCF method is the most appropriate method for determining required ROE and that the appropriate dividend yield is 6.0%. However, the Commission finds that its original growth determination of 5.0% gave too much weight to certain aberrational factors which investors are not likely to expect in the future. In addition, the Commission will reconsider and reverse its decision to not allow a flotation adjustment to compensate the Company for its equity issuance in the test year.

a. The NSP Petition

i. Adjustment of the Dividend Yield to Account for Growth

The Commission will reject the Company's suggestion to adjust the dividend yield to account for additional growth. The Department demonstrated in the record that Dr. Thompson's dividend yield already accounts for future dividend growth. In addition, RUD-OAG witness Mr. Kahal proposed a forward-averaged dividend yield of 6.0%, and NSP witness Mr. Pender proposed a forward-averaged dividend yield of 6.07%. The Commission concludes that 6.0% represents an appropriate expected dividend yield for NSP.

ii. Weight Placed Upon Earnings Per Share of Growth

In reviewing the growth data, the Commission finds that NSP's earnings per share have experienced little or no growth over the five years ending in 1992. Two sharp declines in earnings per share were experienced by the Company during this five year period, one due to the Commission's denial of the Company's rate increase request in its 1990 rate case, Docket E-002/GR-89-865, and one due to extremely abnormal weather in 1992. In NSP's 1992 rate case, Docket No. E-002/GR-91-001, the Commission noted the 1990 earnings decrease due to the previous rate case decision. The Commission accordingly deemphasized 1990 earnings data when determining the appropriate ROE for NSP in Docket E-002/GR-91-001.

In the final Order in this rate case, the Commission excluded 1992 earnings growth data, because that data would have reflected the earnings decrease due to abnormal 1992 weather conditions. The Commission did not, however, follow its 1992 decision and deemphasize the 1990 earnings decrease when determining the ROE. Earnings per share continues to be an important element in determining the appropriate growth rate for NSP. Dividend growth in excess of earnings per share growth cannot be maintained over the long term at constant payout ratios. All parties agreed that historical earnings per share are likely to be considered by investors when predicting a Company's growth rate.

However, the DCF formula growth rate is designed to be a long-term future growth rate. While historical growth is often a good predictor of future growth, investors tend to discount historical results which are not likely to be sustained in the future. The Commission concludes that NSP's five-year growth data should be accorded less weight in determining the appropriate DCF growth rate for NSP.

The Commission has traditionally considered five- and ten-year averages of historical growth rates when determining the appropriate DCF growth rate. This method places extra emphasis on five-year figures, since the five-year data is also included in the ten-year average. The Commission finds that an appropriate method of according less weight to the five year data in this case would be to consider only ten-year historical growth rates in the average. NSP's ten-year growth data includes periods of both high and negative growth and is likely to represent long-term, average growth expectations of investors.

NSP witness Mr. Pender proposed a DCF growth rate of 5.32%, based on ten-year average historical growth rates. The Commission finds that this growth rate appropriately reflects investor growth expectations for the future for NSP.

iii. Flotation Cost Adjustment

The flotation adjustment was first proposed by RUD-OAG witness Matthew I. Kahal and was supported by the Company. In his report, the Administrative Law Judge recommended that the Commission add 15 basis points to NSP's ROE to compensate the Company for flotation expenses. The ALJ concluded that this was a reasonable adjustment because NSP had issued equity during the test year. The Department did not except to the ALJ's recommendation that NSP's ROE be adjusted to reflect flotation costs.

In its September 1, 1993 Order, the Commission rejected the ALJ's recommended flotation adjustment on the grounds that NSP did not request a flotation adjustment in its ROE calculation. On rehearing, the Commission will reconsider and reverse that decision.

The record shows that the Company supported the addition of flotation costs if the Commission determined that the ROE should be calculated using the DCF method. The Company's ROE request of 12.5% was not directly calculated, but instead represented an estimate within a range of possible returns. Therefore, it would not have been appropriate for the Company to add a flotation cost adjustment to the Company's request. Flotation costs should have been implicitly considered when selecting the appropriate point within the range.

However, the calculation of the dividend yield and the growth rate in the DCF method does not take flotation costs into account. In order to reflect flotation costs, a separate adjustment must be made. In the past, the Commission has adjusted ROE to reflect flotation expenses when a company is planning to issue equity in the test year. The record shows that NSP issued $100 million in equity in May of 1993. The Commission finds that it is appropriate to add a flotation cost adjustment to its DCF determination of ROE. The Commission also finds that the adjustment of 15 basis points recommended by the ALJ is reasonable.

b. The RUD-OAG Petition for Reconsideration

The Commission does not agree that it was in error in rejecting Mr. Kahal's growth rate in its original decision. Although Mr. Kahal may have excluded 1992 data in his earnings retention analysis, he included it in his historical growth data. Because the Commission has decided to place primary weight on historical growth data to determine the appropriate growth rate, its decision to reject Mr. Kahal's growth rate is reasonable.

4. Conclusion

Using the DCF method to calculate the appropriate ROE for NSP, the Commission finds that the appropriate dividend yield is 6.0%, the appropriate growth rate is 5.32%, and it is reasonable to add a flotation cost adjustment of 0.15%, for an ROE of 11.47%.

Based upon the Commission's findings and conclusions on return on equity, cost of debt and preferred stock, and capital structure herein, the Commission finds the overall rate of return for NSP in the test year to be 9.31%, calculated as follows:

Capital Employed	Percent	Cost	Weighted Cost
Long-term Debt	38.80%	8.05%	3.12%
Short-term Debt	4.55	4.00	0.18
Preferred Stock	8.26	5.57	0.46
Common Equity	48.39%	11.47	5.55
Total	100.00%		9.31%

B. Incentive Compensation

In its original Order, the Commission disallowed recovery of the full amount of incentive compensation costs sought by the Company. The Commission accepted and adopted the Administrative Law Judge's findings that NSP's overall employee compensation levels were unreasonably high and that the amount by which they exceeded market medians was equal to the cost of the incentive compensation plan. Having also found significant deficiencies in the plan, the Commission took the most straightforward course of action and disallowed recovery of all incentive plan costs. The Commission will rethink this decision on reconsideration.

Having again reviewed the record and having heard the arguments of the parties on reconsideration, the Commission concludes the public interest would be better served by modifying the incentive plan than by disallowing its costs entirely.[2] First, the record shows that incentive compensation plans are widely used, respected tools for managing employee performance. The Commission expects utilities to stay abreast of management trends and experiment with promising new approaches. Penalizing the Company for implementing incentive compensation imperfectly could discourage the kind of innovative management necessary to control costs in an increasingly competitive environment.

Second, the record shows that the incentive compensation plan has helped the Company reduce overall compensation costs. The Company concedes that current salary levels exceed corporate

[2] By "modifying the incentive plan" the Commission means changing the parameters of the plan as eligible for rate recovery, not requiring the Company to make changes in the plan as actually administered.

goals and that one of its purposes in introducing incentive compensation is to gradually reduce wage rates by avoiding the compounding effect of base salary increases. This strategy appears to be working; total test year labor costs were some $10 million below what they would have been had the Company been using a base-pay only system. It would be anomalous to disallow as excessive the costs of the mechanism being used to bring salaries into line with market medians.

Third, all expert testimony in the record agrees that the Commission should expect the Company to deviate slightly from compensation market medians; the only disagreement is over how much deviation is reasonable. Both compensation levels and market medians are snapshots in time; it would be more coincidental than probative if they happened to match one another exactly. The Commission concludes its original decision to limit recoverable compensation to the market median -- and the accompanying decision to disallow all incentive compensation costs as a useful proxy for the excess -- was a bit too facile.

After all, the Commission has more precise tools at its disposal than total disallowance. It can allow partial recovery of incentive compensation costs. It can disallow cost recovery for plan features it considers unreasonable. It can limit recovery of total employee compensation costs to an amount it considers reasonable, based on all the evidence in the record.

All these considerations together lead the Commission to conclude that granting partial recovery of incentive compensation expenses would be a better course than totally disallowing them. The Commission will therefore allow recovery of incentive compensation costs as outlined below.

1. Recoverable Payments Limited to 15% of Base Salary

The Commission continues to believe, for the reasons set forth in the original Order, that the officers' and executives' plans allow too high a proportion of these employees' total wages to come from incentive compensation. (These plans provide for incentive payments of up to 40% of base pay.) The Commission will limit recoverable incentive payments to 15% of an individual's base salary.

2. Shortfall to be Held for Ratepayers

In the original Order, the Commission expressed strong disapproval of the Company's retention of the right not to make incentive payments earned under the plan. The Commission continues to view this as an inappropriate transfer of risk from shareholders to ratepayers and as inconsistent with the test year concept on which rates are based. The Commission will therefore require the Company to record all earned but unpaid incentive compensation recoverable in rates under this Order for future return to the ratepayers. This will adequately protect ratepayers' interests and prevent erosion of the test year concept.

3. Total Amounts Recoverable Limited to 2.2% of Base Wages

Utilities provide essential services to captive ratepayers and must be held to a high standard of prudence and reasonableness when seeking rate recovery of any cost. In its original Order the Commission denied rate recovery of all employee compensation amounts exceeding the market median. Upon further reflection, the Commission agrees with the Administrative Law Judge, the Company, and the Department that it is more reasonable to expect and allow minor differences between actual compensation levels and market medians. Although industry averages are a good starting point for analyzing reasonableness, reasonableness depends upon the specific facts of the case before the Commission.

On the record before it in this case, the Commission agrees with the Administrative Law Judge and all parties except the Company that the 7.5% by which current compensation levels exceed market medians is unreasonably high. (Without conceding that current compensation is too high, the Company itself has made bringing wage levels closer to market medians a corporate priority.) The Administrative Law Judge accepted and recommended that the Commission accept the Department's position that rate recovery of compensation costs should be limited to 105% of the market median. This would result in authorizing recovery of incentive compensation costs equalling 2.2% of total Company base pay and corresponding pension costs. The Commission finds the reasoning of the Department and the Administrative Law Judge persuasive and will accept and adopt it.

4. Other Concerns Raised in Original Order

The major concerns that led to the original disallowance of incentive compensation costs have been dealt with above. The original Order also raised several less critical concerns, discussed below.

The original Order expressed disapproval of the earnings-per-share components of the executives' and officers' plans. Although the company did not expect to meet the earnings-per-share threshold in the test year and did not seek recovery of amounts attributable to meeting those goals, the Commission was concerned about appearing to concur in the plans' earnings-per-share design. Similarly, the original Order found arbitrary the plan's goal of keeping NSP rates low in comparison with the rates of other utilities, since inter-utility rate differences result from so many factors besides employee productivity. Here, too, however, the Company reports it does not expect to meet the goal in the test year and does not seek recovery of amounts attributable to meeting that goal.

These two issues have no rate impact. They did not and do not compel disallowance of cost recovery on their own. The Commission concludes development and analysis of such issues should be deferred to a proceeding in which they have a practical impact.

Finally, the Commission was originally concerned that the performance goal requiring departments to spend within 2% of their allocated budgets could be counterproductive or meaningless. The Commission thought the requirement would discourage cost-cutting at best and encourage frivolous spending at worst. These concerns have been allayed in part by Company explanations that departmental budgets are set after exacting inquiry; that it is Company policy to explore cost-cutting measures in the budget setting process, not the spending process; and that spending shortfalls are not encouraged because of their potential to affect quality of service. This is a plausible explanation which the Commission will not second-guess at this time.

5. Annual Report Required

The Commission will require the Company to file an annual report on the operation and performance of its incentive compensation plan. The report will include an accounting of all amounts paid under the plan, all amounts recorded as earned but not paid, and an evaluation of the plan's success in meeting its stated goals, including controlling overall employee compensation costs.

C. Change in Federal Income Tax Rate

The Revenue Reconciliation Act of 1993 increased the federal corporate tax rate from 34 to 35 percent, retroactive to January 1, 1993. In its petition for reconsideration, the Company stated that the tax change would increase test year expense by $4.5 million for NSP Electric and by $0.4 for NSP Gas. In calculating the increase for NSP Gas, NSP used the gas utility's revenue deficiency in the Commission's September 1, 1993, Order. For the electric utility, the Company applied its requested return on equity of 12.5 percent to calculate the increase, rather than the 11 percent approved in the rate cases.

NSP stated that the change in federal tax law may be officially noticed by the Commission and applied to the rate case upon reconsideration. According to NSP, there is no need for a contested case hearing since there is no factual dispute regarding the tax change or its effect on NSP's revenues. The Company argued that failure to include the retroactive increase in rates would result in final rates which would be insufficient to recover test year expenses.

The Department had no objection to incorporating the federal tax change into the calculation of final rates. The Department did note that further legislation which would repeal the retroactive effect of the tax has been considered. If such legislation resulted in repeal of the tax during the 1993 test year, NSP should be required to refund the difference to ratepayers.

No other party commented on the Company's request to apply the federal tax change to adjust NSP's final rates.

The Commission agrees with NSP that the change in federal tax legislation should be applied when calculating the Company's final rates. This change was beyond NSP's control and will directly affect the Company's revenues. NSP has acted promptly to notify the Commission and parties of the change. It would be unfair to require the Company to absorb the decrease in net revenues, simply because the legislation did not pass until after the Company's rate cases were filed.

The Commission will apply the new federal corporate income tax rate to determine final rates for both NSP Electric and NSP Gas. The Commission will require NSP Electric and NSP Gas to refund the additional amount collected under this adjustment, should the tax be repealed for 1993.

II. ISSUES RELEVANT ONLY TO THE GAS UTILITY

A. CNG Vehicle Conversion Kits

1. The September 1, 1993 Order

In the rate case filing, NSP Gas included the cost of 14 compressed natural gas (CNG) vehicle conversion kits in rate base. The gross cost of the kits was $48,396; the net, after depreciation, was $30,800. NSP included only the net amount in rate base.

In the rate case the Department argued that NSP had not provided enough record evidence to allow a cost/benefit analysis of the CNG vehicle conversion kits to take place. The Department also claimed that the Company had included non-regulated use of the CNG vehicle refueling station in its Operations and Maintenance (O&M) costs. The Department therefore recommended that the gross cost of the CNG kits be deducted from rate base as a proxy for the combined net CNG kit costs and the improper O&M costs. The Commission agreed with the Department's recommendation in the September 1, 1993, Order.

2. Positions of the Parties

In its petition for reconsideration, NSP did not challenge the Commission's decision to remove CNG investments from rate base. The Company asserted, however, that the deduction should have equalled the net cost of the kits, not the gross cost. NSP had properly included the net cost in rate base, pursuant to Minn. Stat. § 216B.16, subd. 6. The Company stated that it would be a dangerous precedent to disallow the gross cost, based upon the Department's unproven assumptions.

The Department reiterated its position that the gross cost is a reasonable proxy for the amount of costs that are properly excluded from rates.

3. Commission Action

Upon reconsideration the Commission finds that the net, not the gross, cost of the CNG vehicle conversion kits should be deducted from rate base. The Company properly included the net amount, after depreciation, in its rate case filing. This is the usual rate case practice, and the Commission will not depart from it without a good reason. In this case, the Department's nonspecific charge of Company misallocations is not sufficiently concrete to justify a departure from accepted rate case practice.

B. Marketing Program Expense

1. The September 1, 1993, Order

In its rate case filing, NSP Gas included costs for four marketing programs focused on improvement of base load utilization through nonheating uses. The Commission found that the Company had not shown that the four programs are cost-effective or that they benefit ratepayers. The Commission disallowed the costs associated with the four marketing programs.

2. Positions of the Parties

In its September 21, 1993, petition, the Company asked the Commission to reconsider its position on one gas marketing program, the Gas Cooking Incentive Program. The Company argued that this program met cost/benefit analyses previously favored by the Commission. The incentive program has a positive net present value and a simple payback period of one year.

The Department opposed any reconsideration of the rate case disallowance of Gas Cooking Incentive Program expenses. According to the Department, the Company failed to provide information necessary to demonstrate that the program is beneficial to ratepayers.

3. Commission Action

NSP has provided no information or analysis which convinces the Commission that reconsideration of this item is advisable. The Commission remains unpersuaded that the costs of the Gas Cooking Incentive Program should be recovered in rates. The Commission will deny NSP's request for recovery of Gas Cooking Incentive Program expenses.

C. Minimum Distribution Study

1. The September 1, 1993, Order

A minimum distribution study is used to set customer-related costs. The study uses the minimum average cost of provision of gas service to a class of customers, under the assumption that the customers will only be connected and will not consume any gas. In the September 1, 1993, rate case Order, the Commission required NSP to file a minimum distribution study in its next gas rate case.

2. Positions of the Parties

In its petition for reconsideration, NSP requested Commission approval of deferred accounting treatment for costs of the study. NSP stated that these costs were not included in the 1993 test year or in NSP's budget for 1994. NSP anticipated using unbudgeted overtime labor or an outside engineering firm to prepare the minimum distribution study. Since these unbudgeted costs would be significant, NSP sought deferred accounting.

The Department stated that NSP's request for deferred accounting was not the proper subject of a petition for reconsideration. A request for deferral should not be considered until the costs of the study are more certain and the Company can provide a deferral time frame.

3. Commission Action

The Commission agrees with the Department that this reconsideration proceeding is not the proper forum for the Company's request for deferred accounting. If the Company wishes to pursue this request further, it is free to do so in a separate miscellaneous filing. The Commission will deny NSP's request for approval of deferred accounting for costs of the minimum distribution study.

III. ISSUES REQUIRING CLARIFICATION BETWEEN THE RATE CASES

A. Purchasing and Contracting Practices

1. The Rate Case Orders

Parties raised concerns regarding NSP's purchasing and contracting practices in both the gas and the electric rate cases. The Department questioned the Company's policies of competitive bidding for goods and services.

In the September 1, 1993, gas rate case final Order, the Commission ordered the Company to file a report on its purchasing practices and procedures within six months of the date of the Order. The Company was told to work with the Department in setting the criteria for the report.

In the September 29, 1993, electric rate case final Order, the Commission directed the Department to analyze NSP's purchasing practices, beginning with the Company's Purchasing Department Policy and Procedure Manual. The Commission ordered the Department to report on NSP's policies, procedures and compliances within six months of the date of the Order.

2. Positions of the Parties

In its petition for reconsideration the Company requested that the Commission require a single report for both gas and electric rate cases, to be conducted on the lines of the report ordered in the electric case. The Department would thus prepare and submit the single report.

The Department replied that it had no objection to NSP's filing a single report on purchasing and contracting practices for both the electric and the gas utilities.

3. Commission Action

The Commission agrees with the Company and the Department that a single report should be filed on the purchasing and contracting practices of the electric and the gas utilities. As NSP stated, the issues would be identical and the same Company personnel would be involved in both the purchasing practices and facilitating the report.

The Commission will require the Department to report on the Company's purchasing policies, procedures, and compliance within six months of the date of this Order.

B. Conservation Cost Recovery Charge

1. The Rate Case Orders

In the September 1, 1993, gas rate case final Order, the Conservation Cost Recovery Charge (CCRC) was calculated by dividing test year Conservation Improvement Program (CIP) expenses by test year sales, **including** Interdepartmental Sales. In the September 29, 1993, electric rate case final Order, the CCRC was calculated by dividing CIP expenses by test year sales, **excluding** Interdepartmental Sales.

2. Positions of the Parties

In its petition for reconsideration NSP noted the discrepancy between the two rate cases. NSP stated its belief that the CCRC calculation in the electric rate case was more correct. NSP therefore requested that the Commission modify the gas CCRC to exclude Interdepartmental Sales. This would change the gas CCRC from $0.022901/Mcf to $0.022907/Mcf.

The Department did not oppose NSP's request.

3. Commission Action

The Commission agrees with the parties that the calculation of the CCRC should be consistent between the two rate cases. The Commission finds that modifying the gas CCRC to exclude Interdepartmental Sales would be appropriate and will so order.

IV. Rate Base Summary

The Commission's findings and conclusions on reconsideration relating to the Company's rate base result in a Minnesota jurisdictional average rate base of $213,455,000 for the test year as show below (000's omitted):

Utility Plant in Service	$395,044
Less: Accumulated Depreciation	155,741
Net Utility Plant in Service	$239,303
Construction Work in Progress	8,011
Accumulated Deferred Income Taxes	-39,948
Working Capital:	
Cash Working Capital	-7,395
Gas in Storage	12,517
Materials and Supplies	3,343
Prepayments	609
Customer Advances & Deposits	-496
Misc Def Debits & Credits	-1,144
Pension Funding Liability	-596
FAS 106 Provision & Amortization	-903
Unamortized Rate Case Expense	154
Total Working Capital	$ 6,089
TOTAL AVERAGE RATE BASE	$213,455

V. Operating Income Statement Summary

The Commission's findings and conclusions allowing recovery of a portion of incentive compensation and of the increased federal income taxes revises the Minnesota jurisdictional operating income for the test year under present rates to $13,992,000 as shown below (000's omitted):

Operating Revenues	
Retail Revenues	$249,617
Unbilled Revenues	1,994
Gross Earning Revenue	4,107
Other Revenues	3,332
Total Operating Revenues	$259,050

Operating Expenses	
Purchased Gas Cost	$166,456
Other Production	2,263
Transmission	898
Distribution	14,590
Customer Accounts	5,918
Customer Service & Information	1,465
Sales Expense	432
Administrative & General	14,188
CIP Expense	1,507
Depreciation Expense	14,039
Taxes	
Real Estate, Pers Prop, Other	13,995
Misc - Tax Benefit Transfer	-79
Gross Earning Tax	4,107
Federal & State Income Taxes	5,770
Deferred Income Taxes	3
Def ITC Amort to Taxes	-403
Total Operating Expenses	$245,149
Operating Income before AFUDC	$ 13,901
AFUDC	91
Net Operating Income with AFUDC	$ 13,992

VI. GROSS REVENUE DEFICIENCY

The above Commission findings and conclusions result in Minnesota jurisdictional gross revenue deficiency for the test year of $10,031,000 as shown below (000's omitted):

Rate Base	$213,455
Rate of Return	9.31%
Required Operating Income	$ 19,873
Test Year Operating Income	13,992
Operating Income Deficiency	$ 5,881
Revenue Conversion Factor	1.705611
Gross Revenue Deficiency	$ 10,031

In the test year income statement, the Commission found that the Minnesota Total Operating Revenues at present rates is $259,050,000. Adding the gross revenue deficiency of $10,031,000 to this amount results in total authorized revenue from Minnesota customers of $269,081,000.

ORDER

1. Rate recovery of the costs of the incentive compensation plan shall be limited to 2.2% of total base salary costs, to individual payments not exceeding 15% of the individual's base salary, and corresponding pension costs.

2. The Company shall record for future refund all incentive compensation payments earned under the terms of the plan and recoverable in rates under this Order but not paid.

3. The Company shall file a report on or before April 1, 1995 and annually thereafter evaluating the operation and performance of its incentive compensation plan. The report shall include, but shall not necessarily be limited to, an accounting of all amounts paid under the plan, an accounting of all amounts recorded as earned but not paid, and an evaluation of the plan's success in meeting its stated goals, including controlling overall compensation costs.

4. The return on equity for NSP is 11.47%, which combined with other factors results in an overall rate of return of 9.31%, calculated as shown in the body of this Order.

5. Final rates for both NSP Gas and NSP Electric shall be adjusted to reflect the increase in the federal corporate income tax rate from 34 to 35 percent, retroactive to January 1, 1993. If this federal tax change is repealed retroactive to 1993, NSP shall refund the amount collected which reflects the increase from 34 percent.

6. Final rates in the NSP Gas rate case shall be adjusted to reflect the exclusion of the net cost of CNG vehicle conversion kits ($30,800) rather than the gross cost ($48,396).

7. NSP's request to reconsider the disallowance of Gas Cooking Incentive Program expenses is denied.

8. NSP's request for approval of deferred accounting for the costs of the minimum distribution study is denied.

9. Within six months of the date of this Order, the Department shall submit a report on NSP's purchasing policies, procedures, and compliance.

10. The calculation of the CCRC in the NSP Gas rate case shall be modified to exclude Interdepartmental Sales, resulting in a CCRC of $0.022907/Mcf.

11. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

DISSENTING OPINION

Commissioners Kitlinski and Knaak, dissenting

On September 1, 1993, the Commission issued its FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER in the NSP Gas rate case, which included issues common to the Company's gas and electric rate cases. In that Order, the Commission set NSP's rate of return at 11.0% and disallowed recovery of the full amount of incentive compensation costs sought by the Company. The Commission's findings and conclusions on these issues were well reasoned and grounded firmly in the evidence presented.

In the short time between its initial decision and reconsideration in this case, the majority has seen fit to change its decision on these two critical issues. The majority did not have the benefit of new evidence or arguments; yet it revised two fundamental decisions that had been made after months of review and days of argument and deliberation. This, in our view, exceeds the limits of the appropriate use of reconsideration. We must, therefore, respectfully dissent.

The Commission has used reconsideration very judiciously in the past, rarely changing its findings or conclusions except to correct obvious technical errors which come to light after the original Order has been issued. Absent the introduction of significantly new and persuasive arguments, the Commission should continue its tradition of restraint and not cast aside major decisions made after long and careful consideration. Failure to limit the scope of reconsideration in this way renders the Commission's initial Order something approaching a rough draft which, upon brief reflection, becomes subject to major revision. Reconsideration becomes a forum to rehash old arguments and rethink well-considered findings and conclusions.

The Commission's proceedings were never intended to operate in this manner. The Commission's Orders are generally expected to be final and the availability of reconsideration should not suggest otherwise. In this case, the majority's change of view on reconsideration will cost NSP's gas customers approximately 1.3 million dollars annually; it will cost electric customers some 14 million dollars per year. The Commission's September 1, 1993 Order set out a very detailed and compelling case for an 11.0% rate of return and for disallowing the full amount of the Company's incentive compensation costs. The Commission should have reaffirmed those decisions here.

Signed
Cynthia Kitlinski
Commissioner

Date:

Signed
Dee Knaak
Commissioner

Date: