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April 24, 2007

Illona A. Jeffcoat-Sacco, Executive Secretary
North Dakota Public Service Commission
State Capitol Building, Dept. 408
600 East Boulevard
Bismarck, ND 58505-0480

Re: Application of Northern States Power Company, a Minnesota corporation and wholly owned subsidiary of Xcel Energy Inc. for Authority to Increase Rates for Natural Gas Service in North Dakota
Case No. PU-06-525

Dear Ms. Jeffcoat-Sacco:

Attached are an original and seven (7) copies of the fully executed Settlement Agreement between Northern States Power Company (the "Company"), a Minnesota corporation and wholly owned subsidiary of Xcel Energy Inc., and the North Dakota Public Service Commission (the "Commission") advisory staff ("Staff"), along with an original and seven (7) copies of a proposed Order approving the Settlement Agreement.

Approval of the Settlement Agreement would result in just and reasonable rates and would provide other important benefits to the ratepayers and the Company. For ratepayers, approval would result in: (i) a total rate increase of \$506,353 less than the amount (\$2,800,291 million) initially requested by the Company; and (ii) a rate freeze for residential base natural gas distribution rates until January 1, 2010. But for the rate freeze, the Company could file for another rate increase as early as November 2007 in order to recover the planned investment in automatic meter reading equipment. In addition, the settlement further benefits ratepayers because, during the period of the rate freeze, the Company would be required to share 50% of actual earnings in excess of 10.75%, and 75% of earnings above 11.25%. Neither of these benefits would occur if this matter were resolved without a settlement. For the Company, approval would provide a reasonable opportunity to recover its cost of providing natural service in North Dakota.

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North Dakota Administrative Code Section 69-02-05-05 allows parties to enter into a stipulation regarding all or part of the facts involved in a pending proceeding. The Settlement Agreement is such a stipulation for all matters involved in this natural gas rate case.

We respectfully request that the Commission promptly schedule an informal hearing and conduct the necessary working sessions to review the Settlement Agreement and issue an order approving it so that the Commission, Staff and the Company can obtain the regulatory economies that arise through settlement rather than litigated proceedings. These include avoiding the need for the filing of Rebuttal Testimony, conducting an evidentiary hearing, preparation of post hearing briefs and proposed findings of fact and conclusions of law, oral argument, and/or a possible request for reconsideration.

Please address any questions regarding the Settlement Agreement to David Sederquist at (701) 241-8632.

Sincerely,

A handwritten signature in black ink, appearing to read "Megan J. Hertzler", with a long, sweeping underline.

Megan J Hertzler
Associate General Counsel

Encls.

**STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION**

Application of Northern States Power Company,
a Minnesota corporation and wholly owned subsidiary
of Xcel Energy Inc., for Authority to Increase Rates for
Natural Gas Service in North Dakota

Case No. PU-06-525

SETTLEMENT AGREEMENT

This Settlement Agreement is entered into this ____ day of April 2007, by and between the North Dakota Public Service Commission advisory staff ("Staff") and Northern States Power Company ("Xcel Energy" or the "Company"), a Minnesota corporation and wholly owned subsidiary of Xcel Energy Inc., (collectively, the "Parties"). This Settlement Agreement resolves all outstanding issues in the above-captioned proceeding in a manner consistent with the public interest and will result in just and reasonable rates for the Company's retail natural gas operations in North Dakota.

BACKGROUND

Xcel Energy's natural gas operations in North Dakota earned an average return on equity ("ROE") of 6.5% for the ten-year period from 1997-2006.¹ This is below the authorized ROE of 11.5% during the same time period. The earnings deficiency began after the Company reduced rates by \$491,000 in 1996, and then suffered a loss of its natural gas infrastructure and customer base in the city of Grand Forks during the Red River flood of 1997. During this 10 year period, earnings were as low as 3.61%, and never exceeded 8.80%

The Company has implemented two base rate increases since 2000: a 1.2% (\$500,000) increase effective September 1, 2001 (Case No. PU-400-00-521)² and a

¹ Assumes a projected ROE of 5.0% in 2006.

² In Case No. PU-400-00-521, a \$360,000 per year amortization of the costs to clean up a manufactured gas plant site was also recovered through the Cost Of Gas Rider for an 8-year period.

1.0% (\$745,000) increase effective August 1, 2005 (Case No. PU-04-578). However, these rate increases have not been sufficient to offset the impacts of increased natural gas system investment due to gas main reconstruction and relocation, capacity upgrades, and customer growth. In addition, the Company has continued to see lower distribution margins due to lower commercial sales resulting from customer conservation efforts and response to high wholesale natural gas prices. Finally, operating expense increases due to inflation, new information technology, and other cost increases have also adversely affected the Company's financial results in North Dakota.

Even with the previous two rate increases, Xcel Energy's average residential natural gas delivery charges were *lower* in 2006 than they were in 1984. In 1984, the average natural gas customer paid about \$16.52 for delivery of natural gas on the Xcel Energy system in North Dakota. In 2006, the fixed monthly charge for residential customers was only \$15.69. With the proposed rates contemplated in this Settlement, North Dakota residential consumers will be charged \$18.60 per month for delivery services, approximately a 13% increase over 1984 rates. This compares to an inflationary increase of 95% in the consumer price index ("CPI") over the same 23 year period.

In addition to historically stable rates, progress is being made in other ways to help alleviate high heating bills in North Dakota. The fixed monthly residential charge approved by the Commission in 2005 reduced distribution charges during high natural gas use months (winter) and removed disincentives for the Company to actively promote conservation (Xcel Energy would implement a set of natural gas conservation programs in North Dakota in 2007 under this Settlement to assist residential customers in lowering their natural gas usage and monthly bills through wiser energy use). In addition, the Company annually contributes to fuel assistance programs in the state, and works closely with low-income agencies.

Rates resulting from this Settlement would continue to be reasonable, while allowing the Company the opportunity to recover its costs, avoid another North Dakota rate increase proceeding until at least 2010, and restore financial health for its North Dakota operation.

PROCEDURAL HISTORY

On December 15, 2006, Xcel Energy filed a Notice of Change in Rates for Natural Gas Service with the North Dakota Public Service Commission (the "Commission"), based on a 2007 test year, with interim rates to become effective February 13, 2007. The Notice proposed an increase in natural gas retail and miscellaneous revenues of \$2,800,291, or about 3.0 percent of overall revenues. Xcel Energy proposed to increase residential bills approximately 4.3 percent through a \$3.51 increase in the monthly Delivery Services Charge. The Company proposed to increase commercial firm service revenues by 2.8 percent and commercial interruptible service revenues by 0.7 percent. Filed with the Notice were revised tariffs, direct testimony, exhibits, and supporting statements.

Concurrent with the Notice, Xcel Energy submitted an Alternate Petition for Interim Rates. The proposed interim increase was for \$2,551,000 or 2.74 percent overall, to be effective February 13, 2007 (60 days from filing) in the event the Commission suspended the proposed general increase. The proposed interim increase and rate design were submitted pursuant to the criteria set forth in N.D.C.C 49-05-06.

On December 29, 2006, the Commission issued an order suspending Xcel Energy's general rate increase application and set the matter for investigation and hearing.

On December 29, 2006, the Commission issued a Notice of Filing and Intervention Deadline (the "Commission Notice") that set forth a deadline of February 15, 2007 for other parties to indicate their interest in participating in the case.

On January 10, 2007, the Commission issued a Notice of Hearing and Notice of Public Input Session which set forth the following issues to be considered in this case:

What is the value of NSP's property, used and useful, for the service and convenience of the public in North Dakota?

What is NSP's rate of return on its property, used and useful, for the service and convenience of the public in North Dakota?

What is a just and reasonable rate of return on NSP's property, used and useful, for the service and convenience of the public in North Dakota?

What rates and charges are necessary to provide a just and reasonable rate of return on NSP's property, used and useful, for the service and convenience of the public in North Dakota?

Are NSP's rate schedules designed in such a manner that they result in a basis of charge to its customers that is just and reasonable without discrimination?

Other relevant information or proposals concerning the proceeding.

On January 16, 2007, Staff filed comments taking issue with the level of interim rates requested by the Company, contending that Xcel Energy's interim rate petition did not comply with N.D.C.C 49-05-06. Specifically, staff argued that the ROE to be used for interim rates should be based on a consideration of the imputed ROE from the previous rate case Settlement, and that interim rates should not include the unamortized balance of manufactured gas plant ("MGP") remediation costs in rate base, nor should it reflect additional expenses resulting from a change in the derivation of the Company's "customer allocation factor". Staff proposed that the interim rate increase be \$1,788,000. On January 18, 2007, The Company provided a response to Staff's comments, opposing those adjustments as being inconsistent with the interim rate standards of Section 49-05-06.

On January 24, 2007, the Commission conducted an informal hearing on the Company's interim rate petition. Both Commission Staff and the Company presented their positions on the interim rate increase amount that should be allowed in this case.

On February 5, 2007 the Company sent a letter to the Commission outlining a proposed resolution to the disagreement regarding interim rates. The resolution called for an interim rate increase of \$2,158,000, reflecting: (1) an ROE of 11.5% (the last commission authorized ROE); (2) exclusion of the unamortized balance of MGP remediation costs; and (3) exclusion of additional expenses related to the customer allocation factor change. In an email note sent to the Commission on the same day, Staff endorsed the proposal.

On February 7, 2007, the Commission issued an order allowing interim rates of \$2,158,000, as agreed to by the Parties, to be placed into effect February 13, 2007, subject to refund.

On February 8, 2007, the Commission conducted a public input session as provided in the Commission Notice. The session utilized interactive video-conferencing capabilities to include participants in Fargo, Grand Forks, and Bismarck. However, the session was closed shortly after its scheduled start time due to lack of participation.

Under the Commission Notice the deadline for filing a Petition to Intervene was February 15, 2007. No party filed such a petition in this proceeding.

On March 13, 2007, a settlement meeting was held between the Company and the Commission advocacy staff. Follow-up discussions were held by phone and email in the months of March and April. As a result of those discussions, the Parties reached this Settlement Agreement.

On March 20, 2007 a second public input session was conducted to provide the public with another opportunity to participate in the case. The session utilized interactive video-conferencing capabilities to include participants in Fargo, Grand Forks, and Bismarck.

The administrative record supports the Settlement Agreement. Accordingly, the Parties jointly recommend the Commission issue an Order approving this Settlement Agreement without conditions or modifications.

TERMS OF SETTLEMENT AGREEMENT

The Parties agree to the provisions as defined below and supported by Schedules A, B, C, D, E, F, and G attached to this Settlement.

Increase in Natural Gas Revenue

The Parties agree to, and recommend the Commission approve, a net increase in Xcel Energy's natural gas rates for retail customers in North Dakota to yield an annual retail sales and miscellaneous revenue increase of approximately \$2,293,938, or 2.5%, effective for service rendered on and after July 1, 2007. Rates have not been increased since August 2005, and consequently this represents an annual increase of about 1.2 percent, which is well below the rate of inflation.

The Parties further agree, and recommend the Commission approve, the following revenue requirement apportionment. Total residential test year revenues would increase \$1,294,275 or approximately 3.6 percent, Commercial firm service revenues would increase \$872,588 or 2.2 percent, and interruptible service revenues would increase \$124,475 or 0.7 percent overall, as shown on Schedule B. This apportionment reflects the assignment to the residential class of 53 percent of the Settlement decrease in revenues from the original rate increase request. At the same time, the apportionment helps align rates for each customer class more closely with the class costs as derived in the class cost of service study filed in this proceeding.

The Company shall file compliance tariff pages setting forth the revised gas rates and tariffs provided by this Settlement Agreement rate option at least 30 days prior to the effective date.

Reduced Return on Equity

The Parties agree to, and recommend the Commission approve, a return on equity of 10.75 percent.

This reduction in ROE from the 11.3 percent proposed in the original filing decreases the test year revenue requirement by about \$215,000. It is below the average return granted to natural gas utilities since December 2005, as shown on Attachment A.³ The Parties agree that a 10.75% ROE will be used for purposes of determining interim rates in the Company's next natural gas rate case.

Residential Rate Freeze Until 2010

The Parties agree to, and recommend the Commission approve, a prohibition against further increases in residential natural gas delivery rates any time prior to January 1, 2010.

Customer Refunds for Earnings Above Threshold

The Parties agree to, and recommend the Commission approve, an earnings

³ All orders listed on Attachment A are for natural gas rate orders issued after December 1, 2005, for cases with a 2005 or 2006 test year.

sharing mechanism that will result in customer refunds if the Company's net income exceeds a 10.75 percent return on equity.

If the Company earns in excess of 10.75 percent ROE during the 2007, 2008, or 2009 calendar years, the Company will refund to customers revenues corresponding to earnings as shown below:

50% of earnings above 10.75% up to and including 11.25%

75% of earnings above 11.25%

Earnings sharing credits would be applied to customer accounts as soon as practical after July 1st, after the annual report of natural gas earnings for the given fiscal year has been filed with the Commission (typically on May 1st). A refund would be administered as a one-time bill credit.

A 10.75 percent ROE sharing threshold is reasonable because this Agreement freezes residential rates until January 1, 2010, imposing an additional risk on the Company. The ROE is lower than previously authorized and, as demonstrated by Attachment A, is lower than the average ROE granted in recent utility rate proceedings across the country.

No Change in Customer-Based Allocation Factor

The Parties agree to, and recommend the Commission approve, a \$291,000 *reduction* in test year revenue requirements to reflect a reinstatement of Xcel Energy's previous method of allocating common utility costs.⁴

In its original application, the Company had estimated a \$363,000 increase in test year revenue requirements as a result of a new customer allocation method. This estimated impact was based on a comparison of the cost allocation using the new method to the cost allocation determined by the previous method using 2004

⁴ In its rate application, Xcel Energy had proposed that, for purposes of determining the customer-based allocator used to allocate common utility costs to the gas utility, a customer receiving both gas and electric service from the Company would be counted as 1 gas and 1 electric customer (previously, combination customers were counted as a ½ gas and ½ electric customer). This change was driven by limitations in the combination customer count reporting of the Company's billing system ("CRS") installed in 2005. However, the Company has recently verified the existence of a computer program that enables

customer data (the most recent year in which the old method had been calculated).

In reinstating the previous method, both Parties agree to use 2006 customer counts (instead of 2004 counts) to determine the cost allocation. The use of updated 2006 customer counts increases the test year revenue requirement by \$72,000. The net result of reinstating the previous method of counting combination customers (a \$363,000 decrease) and updating the customer count data with 2006 data (a \$72,000 increase) is a reduction in revenue requirements of \$291,000.

Exclusion from Rate Base of Automated Meter Reading Investment

For purposes of determining the overall revenue requirement, the Parties agree to, and recommend the Commission approve, the filed test year average rate base amount of \$46,631,000. The rate base does not include a significant investment in automated meter reading ("AMR") equipment that the Company plans on making in North Dakota in the fourth quarter of 2007. However, this amount does include \$721,000 related to the remaining balance of the unamortized manufactured gas plant ("MGP") remediation costs.

For purposes of settlement, the Parties agree that the Company's recent decision to install either longer-life replacement batteries (at an estimated cost of \$1.0 million) or replacing both AMR modules and batteries (at an estimated cost of \$2.4 million) will not be included in the test year operating expense, rate base, or calculation of test year revenue requirements. A \$2.4 million investment in AMR equipment would increase annualized revenue requirements by approximately \$500,000 (about \$90,000 of this is offset by the inclusion of unamortized MGP costs in rate base, however). The Company agrees not to seek an increase in its test year rate base and revenue requirement through a supplemental filing in this proceeding, as would otherwise be permitted by NDCC § 49-05-04.1 paragraph 3.

Xcel Energy to access the CRS customer count data needed to support its previous customer allocation methodology. Under the terms of this Settlement, Xcel Energy will return to this previous method.

Use of Operating Company Capital Structure

For purposes of determining the overall revenue requirement, the Parties agree to, and recommend the Commission approve, the filed capital structure and cost of capital for Northern States Power, a Minnesota corporation and wholly owned subsidiary of Xcel Energy Inc. ("NSP(MN Co.)").

The Parties agree that it is not necessary for the Company to adjust its NSP(MN Co.) regulated capital structure by decreasing common equity and increasing long-term debt by the amount of preferred equity held at the holding company level. It is agreed that the NSP(MN Co.) operating company capital structure will be used for purposes of determining interim rates in the Company's next natural gas rate case.

Transportation Service Tariff Improvements

The Parties agree to, and recommend the Commission approve, three changes to Large Commercial Interruptible Transportation Service tariff. The first is to allow for nominations in the final a.m. cycle on Northern Natural Gas Company interstate pipeline. The second is to shorten the nomination deadline from two hours to 10 minutes prior to the standardization nominate deadlines. These changes to the nomination terms will provide transportation customers additional ability to ensure that their nominations match their expected usage and provide them greater opportunity to react to an unanticipated change in usage. The final change is to clarify the language regarding the calculation of Monthly Undertake/Overtake charges to ensure the calculation is based upon the amount of natural gas actually delivered on the customer's behalf by the upstream pipeline. This change makes the tariff language more understandable to customers.

The tariffs filed in compliance will also reflect the more accurate legal name Northern States Power Company, a Minnesota corporation and wholly owned subsidiary of Xcel Energy Inc.

Accounting for Conservation Programs

The Parties agree to, and recommend the Commission approve, a requirement for the Company to keep track of annual conservation program expenses that deviate from the amount allowed in the test year (\$138,000). Any accumulated differences will be considered in the next rate case proceeding.

Interim Rates Remain in Effect

The parties agree the interim rates will remain in effect for all customer classes for the period February 13, 2007 to June 30, 2007. No interim rate refunds will be issued.

OTHER TERMS AND CONDITIONS

Basis of Settlement

It is agreed this Settlement Agreement is a negotiated settlement agreement subject to approval by the Commission. Except for the purpose of setting interim rates in the Company's next natural gas general rate case, the Settlement Agreement does not establish any principle or precedent, nor adopt or recommend any specific type or amount of expense or rate base, for this or any future proceeding.

Effect of the Settlement Negotiations

It is understood and agreed that all offers of settlement and discussions related to this Settlement Agreement are privileged and may not be used in any manner in connection with proceedings in this case or otherwise, except as provided by law. In the event the Commission does not approve this Settlement Agreement, it shall not constitute part of the record in this proceeding and no part thereof may be used by any party for any purpose in this case or in any other.

Applicability and Scope

This Settlement Agreement shall be binding on the Parties, and their successors, assigns, agents, and representatives. Consistent with the Commission's

settlement guidelines, this Settlement Agreement does not set policy or overturn precedent. This Settlement Agreement shall not in any respect constitute an agreement, admission or determination by any of the Parties as to the merits of any specific allegation or contention made by the Parties in this proceeding.

Effective Date

This Settlement Agreement shall be effective on the date of the Commission Order approving the Settlement Agreement. The revised rates and tariff agreed to by this Settlement Agreement shall be effective on the dates specified in Section I of Terms of Settlement Agreement.

Modification

If the Commission Order modifies or conditions approval of this Settlement Agreement, it shall be deemed terminated if either Party files a letter with the Commission within three (3) business days of the date of such Order stating that a condition or modification to the Settlement Agreement is unacceptable to such party.

Dated this 24 day of April 2007

Northern States Power Company,
A Minnesota corporation and wholly owned subsidiary of Xcel Energy Inc.

By: Scott M. Wilensky
Scott M. Wilensky
Vice President, Government and Regulatory Affairs

Dated this 23 day of April 2007.

Northern Dakota Public Service Commission Staff
By: Annette M. Bendish
Annette M. Bendish
Counsel to the Commission