

MEMORANDUM

TO: Commissioners Wefald, Cramer and Clark

FROM: Bill Binek and Jerry Lein

DATE: May 23, 2007

RE: NSP Gas Rate Case Settlement, PU-06-525

Commission advisory staff believes there are three primary issues that the Commission should consider in determining whether or not to approve the proposed settlement: 1) capital structure; 2) asset retirement obligations; and 3) the reasonableness of the settlement as a whole considering revenue requirement, current ROR and the proposed rate moratorium.

The issue regarding capital structure comes down to a question of whether to use a separate capital structure for NSP as has been done historically and is agreed to by the parties in the settlement agreement or whether to use the capital structure of the parent company, Xcel Energy.

The issue of asset retirement obligations (ARO) is not a pressing issue because according to the information provided it only becomes critically important if the company becomes deregulated. There is no suggestion that any deregulation movement is forthcoming.

The reasonableness of the settlement agreement needs to be considered looking at the settlement proposal as a whole. There appears to be no dispute that the company is not earning an adequate return on its investment. There is also no dispute as to the rate base additions that have been made to NSP's distribution system. There is a significant difference in the proposed ROE. Advocacy staff proposes a rate of 9.56% and NSP proposes a rate of 11.32%. Advocacy staff included in its testimony information from a survey undertaken by Regulatory Research Associates for 2005 and 2006 which showed that the highest ROE awarded during that period was 11.5%, the lowest was 9.45% and the average was 10.45%. The settlement proposes an ROE of 10.75% that is slightly higher than the survey average, but includes customer revenue sharing of earnings above that level. Advocacy staff proposed ROE is slightly above the low rate and NSP's proposed ROE is slightly below the high rate.

It appears the rate moratorium and exclusion of automated metering costs are significant considerations as costs continue to escalate between now and the time the rate moratorium expires.