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August 23, 2011

Darrell Nitschke, Executive Director  
North Dakota Public Service Commission  
State Capitol Building, Dept. 408  
600 East Boulevard  
Bismarck, ND 59505-0480

**Re: Otter Tail Power Company  
Advance Determination of Prudence -  
CapX2020 Group 1 Application  
Case No. PU-09-676**

**Northern States Power Company  
Advance Determination of Prudence -  
CapX2020 Group 1 Application  
Case No. PU-09-678**

Dear Mr. Nitschke:

Enclosed for filing as Attachment 1, is the original and seven copies of the executed Settlement on Continued Prudence (“Brookings Settlement”) entered into by Applicants Northern States Power Company, a Minnesota corporation, and Otter Tail Power Company and Commission Advocacy Staff in the above referenced proceedings.<sup>1</sup> The Brookings Settlement amends the original Settlement Agreement (“Initial Settlement”) that was adopted by the Commission in its October 6, 2010 Order (“October 6 Order”).

The Brookings Settlement attempts to address all of the recommendations presented by Mr. Lein at the July 25, 2011 Hearing, including his suggested condition related to

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<sup>1</sup> Consistent with the other settlement agreement in this proceeding, only Applicants and Advocacy Staff are parties to the Brookings Settlement.

potential material modifications of the MVP Order<sup>2</sup>, while still allowing Applicants the opportunity to commence construction of the Brookings Project with an ADP to facilitate a 2015 in-service date. The Brookings Settlement achieves these goals by finding the Brookings Project continues to be prudent but placing a cap on the cost recovery mechanism of N.D.C.C. § 49-05-16 (the “ADP Statute”) if the MVP Order is materially modified. This cap places the appeal risk of the MVP Order on Applicants and thus insulates ratepayers. This is a reasonable resolution to addressing Mr. Lein’s concern while providing Applicants the opportunity to preserve the schedule.

#### **A. Description of the Brookings Settlement**

The following is a brief description of the Brookings Settlement. A section-by-section summary is enclosed as Attachment 2.

The Brookings Settlement amends aspects of the Initial Settlement, but the Initial Settlement remains in effect unless modified. This means Applicants’ waiver of the provisions of the ADP Statute until an Ownership Agreement for the Brookings Project is executed remains in place.

The Brookings Settlement recognizes that Applicants have (a) provided sufficient information of cost allocation applicable to the Brookings Project; and (b) established that the Brookings Project continues to be prudent. This means that the Brookings Settlement (if approved) allows Applicants to execute the Ownership Agreement and maintain an ADP for the Brookings Project, or portion thereof, whenever Applicants deems such execution to be appropriate and without further Commission action.

The Brookings Settlement imposes a cap on the portion of costs incurred by Applicants for the development and construction of the Brookings Project for which the cost recovery mechanism of the ADP Statute would apply (the “ADP Cap”). The ADP Cap would be imposed if the cost allocation methodology applicable to the Brookings Project under the MVP Order is materially modified on rehearing or appeal. The Brookings Settlement defines a material modification of the MVP cost allocation as, in essence, a fundamental change such that the costs of the Brookings

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<sup>2</sup> *Midwest Independent Transmission System Operator, Inc.*, 133 FERC ¶ 61,221 (2010).

Project would no longer be allocated broadly across the MISO footprint. The ADP Cap and the material modification concept are discussed below.

1. *The ADP Cap*

The ADP Cap ensures that only those costs incurred consistent with the broad MVP cost-allocation methodology are considered under the ADP Statute. This shifts the risk of any material modification of that methodology to Applicants. As Applicants' believe this risk is small, we have agreed to apply the cost recovery provisions of the ADP Statute only to those costs that would have been allocated to Applicants under the MVP methodology prior to any material modification.

As a threshold matter, the ADP Cap would be \$0.00 until MISO unconditionally designates the Brookings Project as an MVP. This means if Applicants choose to move forward with the transaction prior to unconditional MVP designation, Applicants would carry the complete cost recovery risk until that designation is made. Once made, the ADP Cap would provide Applicants protection for cost recovery up to the level of the MVP calculation.

If a material modification occurs that is applicable to the Brookings Project, the ADP Cap would limit Applicants' ADP recovery to the costs that would have been incurred without the material modification. For example, under the current MVP cost allocation methodology likely applicable to the Brookings Project, Xcel Energy's ratepayers would be allocated approximately 9% of the costs of the Brookings Project. The ADP Cap would ensure that the ADP Statute would apply to only 9% of the costs of the Brookings Project allocated to Xcel Energy no matter what percentage of the costs of the Brookings Project are actually allocated to Xcel Energy as a result of a material modification to the MVP Order.<sup>3</sup>

2. *Material Modification*

The Brookings Settlement is based on the fundamental premise that the MVP tariff will allocate costs broadly across the MISO footprint and that this would warrant a finding of continued prudence for the Brookings Project. Thus, we agreed that if the

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<sup>3</sup> Under the Brookings Settlement, Applicants do retain the right to seek recovery of any costs of the Brookings Project over and above the ADP Cap in a rate case, but the cost recovery mechanism of the ADP statute would not apply to those costs.

broad based cost allocation applicable to the Brookings Project is overturned, that would be a material modification. However, minor or non-material revisions to the MVP cost allocation methodology would not create a material modification.

The Brookings Settlement attempts to balance the likelihood of minor changes with the low risk that the fundamental principle could be altered. To help bound this concept, we provided examples of the types of changes that could occur on appeal that both Applicants and Advocacy Staff agree would be considered a material modification. Such instances include a modification to the MVP criteria such that the Brookings Project would no longer be deemed an MVP or a change on appeal where the costs of the Brookings Project would be directly allocated to Applicants.

Importantly, because it is not possible to know all the different possible outcomes, the Brookings Settlement defers to the Commission on whether a material modification has occurred, after notice and a hearing. Applicants have agreed to provide timely updates to the Commission as to the status of the MVP Order on rehearing and appeal. Upon notice and hearing, should the Commission deem any order by FERC or the courts to constitute a material modification, consistent with how that concept is defined in the Brookings Settlement, then the Commission could choose to impose the ADP Cap.

## **B. The Brookings Settlement Reasonably Protects Ratepayers**

Both the ADP Cap and the concept of material modification shift the appeal risk onto Applicants. The ADP Cap creates an upper bounds for the amount to which the cost recovery mechanism of the ADP Statute will be applicable. Furthermore, the concept of material modification allows our ratepayers to capture the possibility that the actual cost allocation could be lowered due to the outcome of an appeal for which a material modification is not ordered.<sup>4</sup> Finally, the Brookings Settlement allows Applicants to

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<sup>4</sup> For example, one of the issues in the MVP Order on rehearing is whether the PJM Interconnection (“PJM”) should be allocated some of the costs of MVPs. FERC ordered that no costs be allocate to PJM but many parties have asked FERC to reconsider this issue on rehearing. If FERC reverses itself, and load in PJM is allocated some costs of MVPs, the total amount of the Brookings Project allocated to Applicants would be reduced.

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move forward with the Brookings Project on schedule and with an ADP so that this important system addition can be placed in-service in 2015.

Under the Brookings Settlement, the Commission can actively oversee the impact of the appeal process on the costs to our ratepayers and impose the ADP Cap in its reasonable discretion. The Brookings Settlement, therefore, allows the Commission to find that the Project continues to be prudent without having our ratepayers shoulder the appeal risk that concerned Mr. Lein.

Please feel free to contact Dave Sederquist at (701) 241-8632, or Dean Pawlowski at (218) 739-8947 if the Commission requires additional information or has any questions.

Respectfully,

/s/ James R. Alders  
James R. Alders  
Director of Regulatory Administration  
Xcel Energy Services Inc. on behalf of  
Northern States Power Company

/s/ Dean Pawlowski  
Dean Pawlowski  
Principal Engineer  
Otter Tail Power Company

**Attachment 1**  
**Settlement on Continued Prudence**

**Settlement on Continued Prudence**  
**Case Nos. PU-09-676; PU-09-678**

1. This is an amendment (Amendment) to the Settlement Agreement, dated as of September 23, 2010, as adopted by the North Dakota Public Service Commission (Commission) in its October 6, 2010 Order Adopting Settlement in Case Nos. PU-09-676 and PU-09-678 (ADP Settlement). Capitalized terms not otherwise defined in this Amendment have the meaning given them in the ADP Settlement. The parties hereto constitute the Commission Advocacy Staff and Applicants, and their respective successors and assigns, as applicable (the Parties).
2. The terms and conditions of the ADP Settlement remain in effect except as modified by this Amendment.
3. The Parties agree that Applicants have satisfied all requirements of Section 4(a) and 4(b) of the ADP Settlement. Specifically, Applicants have (a) provided a sufficient level of information regarding cost allocation applicable to the Brookings Project; and (b) established that the Brookings Project continues to be prudent. Applicants have obtained all Critical Permits for the Brookings Project.
4. The cost allocation methodology under the MISO Tariff applicable to the Brookings Project has been resolved to the satisfaction of the Parties. Specifically:
  - a) The Federal Energy Regulatory Commission (FERC) has approved MISO Tariff provisions implementing the Multi-Value Project (MVP) category of transmission projects and cost allocation methodology under which the costs of MVPs are broadly allocated to load throughout the MISO footprint (MVP Allocation). The MVP Allocation is in effect as of the date of this Amendment and applicability of the MVP Allocation has not been limited or stayed by FERC or any courts; and
  - b) MISO's Board of Directors has found that the Brookings Project satisfies all of the criteria to constitute an MVP and qualifies as an MVP under the MISO Tariff. MISO's Board of Directors has conditionally approved the designation of the Brookings Project as an MVP and application of the MVP Allocation to it, subject to approval of the larger portfolio of MVP projects of which the Brookings Project is a part.
5. When (or if) the Commission approves this Amendment, Applicants require no further Commission findings or determination to have ADP approval, subject to the terms of this Amendment, to enter into an Ownership Agreement for the Brookings Project. Specifically, upon approval of the Commission of this Amendment, the limitation in Section 4(b) of the ADP Settlement is met and Applicants are free to execute an Ownership Agreement for the Brookings Project, or portion thereof, at a time of their choosing. Applicants' Waiver of the ADP cost recovery mechanism for the Brookings Project, or portion thereof, as provided in Section 2 of the ADP Settlement remains in effect until such time as Applicants execute the Ownership Agreement for the Brookings Project, or portion thereof.

6. Upon Applicants execution of an Ownership Agreement for the Brookings Project, or portion thereof, all provisions of N.D.C.C. § 49-05-16 will be in effect for the Brookings Project, or relevant portion thereof, for all past and ongoing costs, without further Commission action, subject to the following conditions:
- a) Under the existing MVP Allocation, the costs of MVPs, including the Brookings Project, are allocated broadly across the MISO footprint. This broad allocation methodology across the MISO footprint is an important element of the MVP Allocation to both Parties. The Parties believe that the likelihood of a modification to the MVP Allocation that would substantially narrow or eliminate the broad allocation of MVP costs across the MISO footprint is low. Applicants and Advocacy Staff agree that, were there both a change to the MVP Allocation which substantially narrows or eliminates broad cost allocation across the MISO footprint and that such a change is made applicable to the Brookings Project, then such event constitutes a material modification for purposes of this Amendment. Specifically, a material modification would be any of the following outcomes of any FERC order on rehearing or order of a court:
    - (i) Modification to the MVP criteria such that the Brookings Project would no longer be deemed an MVP;
    - (ii) All costs of an MVP being directly assigned to the owner(s) of that MVP resulting in the costs of the Brookings Project being directly assigned to the owners of the Brookings Project, including Applicants, on an ownership percentage basis;
    - (iii) Only a subset of MISO load (*e.g.* only a particular MISO sub-region) would be allocated the costs of any particular MVP resulting in the costs of the Brookings Project being only allocated to a certain subset of MISO load, including Applicants' respective load, and therefore not all load within MISO would be allocated a portion of the costs of the Brookings Project; and/or
    - (iv) Some other change to the MVP Allocation not currently contemplated by the Parties that both fundamentally alters the broad based allocation of MVP costs across the MISO footprint and is made applicable to the Brookings Project, which in the judgment of the Commission would constitute a material modification as contemplated by this Amendment.

The Parties acknowledge that the specific inputs into the MVP Allocation formula or the specific categories of entities to whom costs will ultimately be allocated (*i.e.* allocated only to all load in MISO, to all users of the MISO system such as load located in PJM, some portion to generators and other stakeholders, or some combination) could be changed by FERC or the courts and that such changes may be applicable to the Brookings Project. Such changes would not constitute a material modification so long as

the fundamental principal of cost allocation broadly across the MISO footprint does not change.

- b) In the event FERC or a court of competent jurisdiction (i) orders a material modification of the MVP Allocation as described and defined in 6(a); and (ii) the material modification of the MVP Allocation is applicable to the Brookings Project, then the cost recovery provisions of N.D.C.C. § 49-05-16 will apply only to those costs for which Applicants would have been responsible under the MVP Allocation applicable to the Brookings Project immediately prior to the effective date of the material modification, calculated as if such material modification to the MVP Allocation had not occurred (ADP Cap). By way of example only: pursuant to the currently effective MVP Allocation, Applicant Xcel Energy is responsible for approximately 9% of the costs of the Brookings Project; should there be a material modification to the MVP Allocation, the terms of N.D.C.C. § 49-05-16 would apply to only 9% of the costs of the Brookings Project for Applicant Xcel Energy.
  - c) Until MISO unconditionally designates the Brookings Project as an MVP, the ADP Cap will be \$0. Once MISO unconditionally designates the Brookings Project as an MVP, the MVP Cap will be determined pursuant to the terms of paragraph 6(b), above.
  - d) Applicants will provide updates to the Commission on the status of any proceedings related to the MVP Allocation which may arise before FERC and the courts. Based upon the updates, if the Commission believes a material modification to the MVP Allocation, as described in paragraph 6(a), above, has occurred, Applicants and Advocacy Staff will provide the Commission with sufficient information, upon notice and hearing, to determine on the record whether a material modification to the MVP Allocation has occurred and the extent of Applicants recovery of any costs exceeding the ADP Cap. Notwithstanding the forgoing, Applicants and Advocacy Staff may request that, upon notice and hearing, the Commission make a determination as to whether a material modification to the MVP Allocation has occurred.
  - e) Should either Applicant file a rate case, rate rider, or other cost recovery mechanism after the Brookings Project, or portion thereof, is in-service but before any appeals or FERC determination on the MVP Allocation are completed, the terms of this Amendment will apply to the costs prudently incurred for the Brookings Project by the Applicant making the filing and included for recovery as part of the rate case, rate rider, or other recovery mechanism. Upon the final disposition of the rate case, rate rider, or other cost recovery mechanism proceeding, the terms of this Amendment will cease to be applicable to the Applicant making the filing and any future outcome of any appeal or final FERC determination on the MVP Allocation on a going forward basis will be addressed in a subsequent rate case, rate rider, or other cost recovery proceeding.
7. Applicants and Advocacy Staff jointly recommend the terms of this Amendment be accepted as a package.

8. Applicants retain their right to recover any and all costs of the Brookings Project, or portion thereof, including the costs of the Brookings Project, or portion thereof, over and above the ADP Cap, in a rate case, rate rider, or other cost recovery proceeding if the Applicant filing the rate case, rate rider, or other cost recovery proceeding (Filing Applicant) establishes that the costs incurred in the construction and development of the Brookings Project were appropriately incurred pursuant to the applicable legal standard in the rate case, rate rider, or other cost recovery proceeding. Filing Applicant may rely on the terms of this Amendment in any rate case, rate rider, or other cost recovery proceeding as may be applicable.
9. Applicants do not forgo or waive any other rights they may have under state or federal law.
10. Applicants and Advocacy Staff reserve the right to withdraw from this Amendment if the Commission rejects or modifies any element of this Amendment.
11. Applicants and Advocacy Staff agree that nothing in this Amendment addresses, takes a position on, decides, or asks the Commission to decide the extent or application of federal jurisdiction to the investments Applicants make or have made in the Brookings Project.
12. Pursuant to N.D.C.C. § 49-05-16(4), the Commission's Order determining the prudence of the Brookings Project is binding for such ratemaking purposes as are within the Commission's jurisdiction.

**[Signature Pages Follow]**

Otter Tail Power Company

By:   
Charles S. MacFarlane, CEO & President

Dated this 23 day of August, 2011

[SIGNATURE PAGE TO SETTLEMENT ON CONTINUED PRUDENCE  
CASE NOS. PU-09-676; PU-09-678]

**Northern States Power Company, a Minnesota Corporation**

By: Laura McCarten, Regional V.P.

Dated this 19<sup>th</sup> day of August, 2011

**[SIGNATURE PAGE TO SETTLEMENT ON CONTINUED PRUDENCE  
CASE NOS. PU-09-676; PU-09-678]**

**North Dakota Public Service Commission Advocacy Staff**

By:   
Illona A. Jeffcoat-Sacco (ID# 03315)

Special Assistant Attorney General  
600 E. Boulevard Avenue, Dept. 408  
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(701) 328-2407

Dated this 23<sup>rd</sup> day of August, 2011

**[SIGNATURE PAGE TO SETTLEMENT ON CONTINUED PRUDENCE  
CASE NOS. PU-09-676; PU-09-678]**

**Attachment 2**  
**Summary of Settlement**

**Summary of Settlement on Continued Prudence  
Case Nos. PU-09-676; PU-09-678**

The following is a summary of the terms and conditions of the Settlement on Continued Prudence entered into by Northern States Power Company, a Minnesota corporation (“Xcel Energy”), Otter Tail Power Company (“Otter Tail” and collectively with Xcel Energy, “Applicants”) and Commission Advocacy Staff in the above referenced proceedings (the “Brookings Settlement”). Numbered paragraphs in this summary correspond to the numbered paragraphs in the Brookings Settlement.

1. Introductory information.
2. Carries forward the terms of the ADP Settlement unless modified by the Brookings Settlement.
3. Provides that Applicants have met all of the requirements in the ADP Settlement related to the Brookings Project and that the Brookings Project continues to be prudent.
4. Provides that the status of the cost allocation methodology applicable to the Brookings Project has been reasonably resolved and recites the procedural status of the MVP Order and MISO’s actions related to the designation of the Brookings Project as an MVP.
5. Provides that upon approval of the Brookings Settlement, Applicants may enter into the Ownership Agreement for the Brookings Project and restates that Applicants Waiver of the cost recovery mechanism of the ADP Statute remains in effect for the Brookings Project until such time as the Ownership Agreement is executed.
6. Provides that upon execution of the Ownership Agreement for the Brookings Project, all provisions of the ADP Statute are applicable to all past and ongoing costs of the Brookings Project subject to an agreed-upon cap in the event that the MVP cost allocation is materially modified:
  - a) Defines material modification as any change to the MVP cost allocation methodology that (1) substantially narrows or eliminates the broad allocation of costs of MVP projects across the MISO footprint, and (2) is applicable to the Brookings Project. This paragraph provides several examples of what a material modification would be and provides a catch all provision for the Commission to determine what would constitute a material modification under the circumstances.

b) Creates the ADP Cap which would be triggered by a material modification to the MVP cost allocation methodology. Under the ADP Cap, the cost recovery provisions of the ADP Statute would be applicable only to those costs of the Brookings Project for which Applicants would have been responsible under the MVP cost allocation methodology prior to the FERC or a court ordering a material modification.

c) Sets the ADP Cap at \$0.00 unless and until MISO unconditionally designates the Brookings Project as an MVP.

d) Requires Applicants to provide updates to the Commission on the status of the MVP Order to determine, upon notice and hearing, if a material modification has occurred. Applicants also reserve the right to request that the Commission make such a determination.

e) Provides that the terms of the Brookings Settlement continue into the next rate, rate rider, or other cost recovery proceeding for which Applicants seek to recover costs of the Brookings Project. Upon completion of those proceedings, the Brookings Settlement terminates as to the Applicant filing the rate case, rate rider, or other cost recovery proceeding and any unresolved issues will be handled on a going forward basis in any subsequent rate case, rate rider, or other cost recovery proceeding.

7. Provides that Applicants and Advocacy Staff will recommend the Brookings Settlement be accepted by the Commission.

8. Provides that independent of the granting of an ADP, Applicants have a right to seek recovery of any costs of the Brookings Project over and above the ADP Cap.

9. Provides that Applicants do not forgo any rights they may have under state or federal law.

10. Allows Applicants and Advocacy Staff the right to withdraw from the Brookings Settlement if the Commission rejects or modifies it.

11. Clarifies that the Brookings Settlement does not address any issues related to federal jurisdiction of transmission costs.

12. Restates that the ADP Statute makes the Commission's finding of prudence binding for rate-making purposes.