


MEMO

To: Darrell Nitschke, Executive Secretary
From: Mike Diller, Director of Economic Regulation 
Date: July 16, 2012
Re: Staff Response to NSP's Proposed Reliability Performance Plan
Case Nos. PU-10-657, PU-11-55, PU-11-557

NSP filed its Reliability Performance Plan (RPP) in compliance with the Commission's February 29, 2012 Order in the above referenced cases. While Mr. Sederquist did most of the heavy lifting culminating in this proposal, staff was intimately involved in framing and developing the targets. Even so, staff believes that the SAIDI benchmark is a little light and should be strengthened. We recommend that the Commission approve NSP's plan with the exception that the SAIDI requirement for achieving an award be strengthened by 2 minutes.

SAIDI

In this application, NSP argues for a System Average Interruption Duration Index (SAIDI) of 58.8 minutes (adjusted to exclude major events such as storms). If this had been in place during the last 5 years, NSP would have been entitled to a reward in 2007 when NSP reported a SAIDI of 57 minutes and would have barely missed a reward in 2009 when reporting 59.2 minutes. These low SAIDI reports occurred before the new IntelliTeam switches were installed, the addition of another tree trimming crew, a more aggressive replacement of bad underground cabling and the addition of an engineer to North Dakota's workforce for the purpose of improving reliability as ordered by the commission in these cases. The new products and services should result in lower results in the future arguing for a more strenuous benchmark.

Setting a benchmark is more of an art than a science. In this case, we don't have any history under the new reliability programs. NSP's proposed method averages the actual SAIDI results for the last 5 years and then makes an adjustment for the estimated impact of the IntelliTeam switches plus a 15% improvement goal to arrive at an Excellence Threshold of 58.8 minutes. Absent any major events, less than one hour of electric service interruptions per year is not bad! In the big scheme of things, NSP's proposal may be reasonable but staff recommends strengthening the threshold nonetheless.

If staff is only going to ask for 2 more minutes, why not just accept NSP's proposal? While two minutes does not sound like a lot, consider that the \$2 million investment in the installation of IntelliTeam switches in Fargo is only expected to gain 2.8 minutes per year system wide. Staff believes NSP's IntelliTeam impact estimate is good. A 2 minute increase represents a 19% increase in NSP 15% improvement adjustment beyond the impact of the smart switches. Besides being material, 2 minutes sets the bar higher than what has been achieved in the past. Similar to a handicap in golf, the lower the standard--the more difficult it is to cut 2 more minutes from the score. Staff believes that 2 more minutes is a fair and reasonable position for both ratepayers and the Company.

The SAIDI benchmark is a reward only mechanism and therefore accomplishing it should be very difficult to achieve—but not impossible. Staff is not opposed to a reward only approach but the standard must be sufficiently difficult to attain. NSP should only benefit from this proposal if it achieves the very highest level of reliable service. We believe strengthening the target with the potential to earn as much as \$1 million more in a given year will incent the company to provide reliable service.

Please note that the \$1 million incentive is limited to \$250,000 if earnings in the plan year exceeds the 10.4% return on equity as authorized by the commission in NSP's last electric rate case. The larger payment, in the event earnings are below authorized levels, is acceptable to staff because excellent service should result in an opportunity for NSP to earn a reasonable return on its investment. To keep this in perspective, please note that \$250,000 in additional earnings would increase the return on equity by about .1%. Therefore, the minimum payment of \$250,000 for achieving the goal, even when earnings are above authorized, is relatively small yet still worth chasing after.

The very aggressive proposal to pay \$50 to customers with more than 3 outages is a penalty only benchmark and works to offset the reward only SAIDI benchmark advocated here.

Annual Reporting Requirements

In its application, NSP is ambivalent about how it should file the annual results of RPP. Since the information being reported could impact future earnings and since the level of reward will be determined by NSP's reported earnings to the commission, including the information as part of the normal year end annual reporting requirements seems like the most appropriate and efficient method of filing.