

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

**Montana-Dakota Utilities Co.
Financial Incentive – Power Purchase Agreement
Rates**

Case No. PU-21-373

ADVOCACY STAFF'S POST HEARING BRIEF

INTRODUCTION

Montana-Dakota Utilities Co. (MDU) has requested a financial incentive on two Power Purchase Agreements (PPA's). Advocacy Staff recognizes that the law allows for an incentive if the criteria of the statute is met. However, Advocacy Staff believes that an incentive is something that causes someone to take action and should not be applied to actions already taken by a utility. If an incentive is to be applied, it should not be the weighted cost of capitol along with the previously approved Return on Equity for MDU.

Case Number PU-21-373 deals with a newly enacted provision to North Dakota Century Code (N.D.C.C.) 49-06-02 which reads:

49-06-02. Value of property for ratemaking purposes - Determination.

The value of the property of a public utility, as determined by the commission for ratemaking purposes, is the money honestly and prudently invested therein by the utility including construction work in progress for new facilities that use lignite mined in this state to generate electricity, as well as additions or modifications to existing lignite facilities, less accrued depreciation. The commission shall allow a public utility for those new or existing facilities utilizing lignite mined in this state as its primary fuel:

1. To recover its research and development costs incurred to develop lignite more cleanly, efficiently, or economically, including carbon dioxide capture and sequestration utilization and a reasonable rate of return on capital expenditures;
2. To recover its incremental costs of complying with federal environmental laws, including a reasonable rate of return on capital expenditures. The commission may allow these costs to be recovered by an environmental surcharge that may be added to existing rates;

3. To recover all costs resulting from a coal severance tax pursuant to chapter 57-61 and all costs resulting from a coal conversion tax pursuant to chapter 57-60. The commission shall allow the inclusion of these costs in the base rates and the inclusion in the automatic adjustment clause of any of these costs not in base rates; and
4. To recover costs in rates, including a financial incentive set at a reasonable rate for power purchase agreements of a dispatchable on-demand generating unit, plant, or facility deemed to protect grid reliability.

Statutory Interpretation

MDU has applied to recover rates, including a financial incentive set at a reasonable rate, for a two PPA's they have entered with Minnkota Power Co-op Inc. (Minnkota). MDU's application falls under subsection 4 of 49-06-02.

Under 49-06-02 there are several requirements that must be met per the statute. First, the facility producing the power must utilize lignite mined in this state as its primary fuel. This condition is met as the PPA's are purchasing power from the Milton R Young Unit 1, which is fired with locally-mined lignite coal.

Second, to recover costs in rates which include a financial incentive set at a reasonable rate, the PPA must be of a dispatchable on-demand generating unit, plant, or facility deemed to protect grid reliability. The Milton R Young unit appears to be a dispatchable on-demand generating plant. However, as to the criteria of it being deemed to protect grid reliability, it has not been deemed by this Commission or any other authority.

What does grid reliability mean? The North American Electric Reliability Corporation (NERC) defines reliability as "the degree to which the performances of the elements of the electric system result in power being delivered to consumers within accepted standards and in the amount desired. NERC defines BPS (bulk power system) reliability as a function of adequacy and operating reliability. In this context, NERC

defines adequacy as, “the ability of the electric system to supply the aggregate electric power and energy requirements of the electricity customers at all times, taking into account scheduled and reasonably expected unscheduled outages of system components.” Operating reliability is defined as, “the ability of the electric system to withstand sudden disturbances to system stability or unanticipated loss of system components.” This comes from the Staff Report to the Secretary on Electricity Markets and Reliability from the U.S Department of Energy issued in August 2017.

The report highlights concerns regarding reliability and resilience in regards to the erosion of baseload power compromising a reliable and resilient grid. The Milton R Young generation is a baseload generating facility. While baseload can come from a variety of sources such as nuclear or hydro-electric, baseload generation is a large factor in grid reliability to meet demand. There are many other factors and considerations for grid reliability and the Commission will have to decide if baseload generation alone is enough to deem the Milton R Young facility to meet the criteria to be deemed protecting grid reliability.

If the Commission deems the Milton R Young facility to protect grid reliability, there are still two issues to be decided. First, can an incentive be applied to an existing PPA? Second, what is a reasonable rate to set the incentive at, if one is to be applied at all?

At the hearing, discussion regarding incentive was raised. Specifically, can an action that was previously taken qualify for an incentive?

N.D.C.C. rules of interpretation give guidance as to how to deal with a word that does not have a specific definition. N.D.C.C. § 01-02-02 states: Words used in any

statute are to be understood in their ordinary sense, unless a contrary intention plainly appears, but any words explained in this code are to be understood as thus explained.

The issue of retroactively applying the code is also addressed in the N.D.C.C. Rules of Interpretation in § 1-02-11 which states: No part of this code is retroactive unless it is expressly declared to be so.

In re Ohio Edison Co., 157 Ohio St.3d 73. In re Ohio Edison Co., states:

{¶ 15} The commission relied on a dictionary definition of “incentive” as “‘something that stimulates one to take action, work harder, etc.; stimulus; encouragement.’” Pub. Util. Comm. No. 14-1297-EL-SSO, Fifth rehearing entry, at ¶ 190, quoting Webster’s New World Dictionary 682 (3d College Ed.1988). The commission found that under its preferred definition, the DMR qualified as an incentive under R.C. 4928.143(B)(2)(h) because the rider “is intended to stimulate the Companies to focus their innovation and resources on modernizing their distribution systems.” Id. at ¶ 190.

{¶ 16} Although the commission defined “incentive,” it did not explain how the DMR operates as an incentive. An incentive generally serves to induce someone to take some action that otherwise would not be taken but for the incentive. Moreover, the DMR is a financial incentive and “it is inherent in an incentive payment that the recipient must do something to be paid.” Len Stoler, Inc. v. Volkswagen Group of America, Inc., 232 F.Supp.3d 813, 822 (E.D.Va.2017). That is, the payment of a monetary incentive is generally conditioned upon completion of a particular action.

Id. at ¶ 15, 16

The definition of incentive is important and as stated above an incentive generally serves to induce someone to take action that would not otherwise be taken. In the case at hand, because the PPA’s were entered into prior to the passage of the law, any money awarded is a subsidy or bonus and not an incentive.

The PPA’s were executed prior to the enactment of N.D.C.C. § 49-06-04(4). As stated at the hearing, there is nothing in the law that says expressly that this cannot be applied to an existing PPA. It also does not say that it can be. N.D.C.C. § 1-02-11

states that no part of this code is retroactive unless it is expressly declared to be so. The Commission must decide if applying the "incentive" is applying the law retroactively.

Reasonable Rate for Financial Incentive

If the above statutory requirements are met, the question is: what is a reasonable rate for the Financial Incentive?

MDU is already recovering 100 percent of the cost of the power purchase agreements. Any incentive comes at the expense to ratepayers.

MDU proposes to use the weighted cost of capital, including the authorized return on equity. This is not a reasonable rate for the Financial Incentive.

Most other incentives for utilities appear to be for either demand-side program investment mechanisms (DSIM), or for energy conservation programs. In re Minnesota Power for Approval, a rate of 2.45% was in place and a request to raise it to 3.49% in its 1996 filing for recovery. 2000 WL 1847621. This rate was for the recovery of the Conservation Improvement Programs (CIPs). While the incentives are different from the case at hand, incentives if awarded should be lower than what MDU is asking.

In Montana-Dakota Utilities Co. v. Wyoming Public Service Com'n, MDU had an incentive award based on the decrease of its cost of natural gas. 746 P.2d 1272. This incentive was subject to Commission adjustment so long as the incentive award was between zero and ten percent of savings. This adjustment was built into the statute allowing the incentive.

We don't have an adjustment or a need for it here. However, an incentive award as a percentage of savings of the PPA's vs. construction may be a reasonable way to look at what an incentive might be. This would allow a company to receive its incentive,

and while not passing the full savings on to ratepayers it still allows for the ratepayer to realize some savings that were realized in the PPA vs. building generation and the costs associated with it.

Zero is a rate that could be found to be reasonable for these PPA's and the incentive awarded. If a higher rate for incentive is deemed appropriate, more than five percent of realized savings would be unfair to ratepayers.

CONCLUSION

While N.D.C.C. 49-06-02(4) allows for an incentive for PPA's of a dispatchable on-demand generating unit, plant or facility deemed to protect grid reliability, it should not be applied retroactively. If the Commission does determine an incentive is appropriate, the effect on ratepayers should be considered. A percentage of zero to five percent seems to be a fair and reasonable rate to set for the incentive.