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PUBLIC SERVICE COMMISSION OF WISCONSIN

Application of Wisconsin Public Service Corporation for Authority to Adjust Electric and Natural Gas Rates — 6690-UR-122

FINAL DECISION

This is the Final Decision in the application of Wisconsin Public Service Corporation (WPSC) for authority to increase Wisconsin retail electric and natural gas rates in 2014.

Final electric rate changes are authorized consisting of a $9,835,000 increase offset against a portion of estimated fuel cost over-collections in 2013 of the same amount and an electric revenue stabilization mechanism (RSM) credit from 2012 over-collections of $12,764,000 returned to RSM rate classes in 2014. The overall rate changes provide a $12,764,000 annual rate decrease for Wisconsin retail electric operations, a 1.32 percent decrease. Final natural gas rate changes are authorized consisting of a $3,881,000 decrease offset against a natural gas RSM charge from 2012 under-collections of $7,877,000. The overall rate changes provide a $3,996,000 annual rate increase for Wisconsin retail natural gas operations, a 1.23 percent increase.

Introduction

On March 29, 2013, WPSC filed a request for authority to increase its Wisconsin retail electric rates by $71,108,000, a 7.36 percent increase, and to increase its Wisconsin retail natural gas rates by $19,010,000, a 5.56 percent increase, to be effective January 1, 2014. These increases are based on a 10.75 percent return on common equity.

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The March 29, 2013, WPSC filing included a request to include the impacts of updated employee benefit costs from actuarial analyses expected in late May 2013. The resulting analyses indicated an additional increase of $4,110,000 on a corporate basis for 2014 electric and natural gas revenue requirements was needed. On June 14, 2013, WPSC requested an additional increase to its 2014 revenue requirements of $1,270,000 expense on a corporate basis for manufactured gas plant remediation costs, $293,000 expense on a corporate basis for electric and natural gas amortization expenses of upfront credit facility fees, and the inclusion of electric revenue requirement associated with additional spending in 2014 for environmental mitigation projects resulting from the U.S. Environmental Protection Agency (EPA) Consent Decree that WPSC entered into in 2013. On August 20, 2013, WPSC requested adjustments to electric and natural gas rate bases and associated revenue requirements related to the deferred tax proration formula that was not included in the March 29, 2013, filing of approximately $700,000. The effects of these requests result in updated rate increase requests in the test year of approximately $75,901,000, a 7.86 percent increase, for Wisconsin retail electric utility operations and $21,236,000, a 6.53 percent increase, for retail natural gas utility operations.

On May 22, 2013, a prehearing conference was held to determine the issues to be addressed in this docket and to establish a schedule for the hearing. On September 27, 2013, public hearings were held in Madison, Wisconsin, for members of the general public and for the parties in this proceeding. On November 14, 2013, the Commission reopened the record in this proceeding to accept further evidence and solicit comments relating to the application of WPSC for authority to adjust its electric and natural gas rates.

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The Commission considered this matter at its open meetings of November 6, 2013, November 14, 2013, and November 22, 2013.

The parties, for purposes of review under Wis. Stat. §§ 227.47 and 227.53, are listed in Appendix A. Others who appeared are listed in the Commission's files.

Findings of Fact

1. WPSC is an investor-owned electric and natural gas public utility as defined in Wis. Stat. § 196.01(5)(a), providing electric and natural gas service to north-central and northeast Wisconsin.

2. Presently authorized rates for WPSC's Wisconsin retail electric utility operations will produce total operating revenues of $1,031,628,000 for the test year ending December 31, 2014, which results in an adjusted net operating income of $128,739,000 and an annual revenue excess of $2,929,000. Presently authorized rates for WPSC's Wisconsin retail natural gas utility operations will produce total operating revenues of $318,768,000 for the test year ending December 31, 2014, which results in an adjusted net operating income of $25,399,000 and an annual revenue deficiency of $3,996,000.

3. For the Wisconsin retail electric utility, the estimated rate of return on average net investment rate base of $1,462,706,000 at current rates subject to the Commission's jurisdiction for the test year is 8.80 percent, which is excessive.

4. For the Wisconsin retail natural gas utility, the estimated rate of return on average net investment rate base of $342,028,000 at current rates subject to the Commission's jurisdiction for the test year is 7.43 percent, which is inadequate.

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5. A reasonable decrease in operating revenue for the test year to produce an 8.68 percent return on WPSC's average net investment rate base for Wisconsin retail electric operations is $2,929,000.

6. A reasonable increase in operating revenue for the test year to produce an 8.13 percent return on WPSC's average net investment rate base for natural gas operations is $3,996,000.

7. WPSC's filed operating income statements and net investment rate base for the test year, as adjusted for Commission decision, are reasonable.

8. Commission staff forecasted electric and natural gas sales are reasonable.

9. It is appropriate to offset $9,835,000 of the 2013 fuel cost over-recovery against the 2014 test-year electric utility revenue requirement and reasonable to approve WPSC's 2014 fuel cost plan upon the condition that such 2013 fuel cost over-collections are used as an offset to the 2014 test-year electric rate increase.

10. It is reasonable in this proceeding to forecast fuel costs based on the New York Mercantile Exchange (NYMEX) natural gas futures prices as of November 4, 2013.

11. It is reasonable to set a 2014 fuel plan-year cost of monitored fuel of $374,213,000, or $27.33 per megawatt-hour (MWh), as shown in Appendix D.

12. It is reasonable to monitor all fuel costs using an annual bandwidth of plus or minus 2 percent.

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13. It is reasonable to allow WPSC to recover any incremental emissions compliance costs associated with the consent decrees that may be incurred during 2014, and to be allowed to include those costs in reported monitored fuel costs.

14. It is reasonable to allow WPSC to defer any minimum tonnage obligation costs incurred during 2014 for possible future rate recovery, with the provision that it is required to submit a detailed analysis documenting its efforts to eliminate or minimize these costs when it seeks rate recovery.

15. It is reasonable to incorporate the ratified union wage increases into estimates for union employee payroll expense and reduce benefits expense associated with union benefits concessions in test-year electric and natural gas revenue requirements.

16. It is not reasonable to include incentive pay plans' costs in test-year electric and natural gas revenue requirements.

17. It is reasonable to include economic development expenses of $304,000 in test-year electric and natural gas revenue requirements.

18. It is reasonable to include deferrals from the settlement in docket 6690-UR-121 in test-year electric and natural gas revenue requirements.

19. It is reasonable to include the revenue requirement impacts of the environmental mitigation project (EMP) costs forecasted to be incurred in 2014 in electric revenue requirement.

20. It is reasonable to terminate the electric RSM and the natural gas RSM beginning January 1, 2014.

21. The reasonable level of expensed conservation costs recoverable in rates for the 2014 test year is $16,644,714 for electric utility operations and $4,263,100 for natural gas utility

settlements to ensure that they are in the public interest. On the other hand, the Commission is not a party to the negotiations and is hesitant to upset negotiated resolutions that may, on balance, be in the best interest of Wisconsin ratepayers. Disallowing recovery of these costs may act as a disincentive for utilities to pursue such settlements and make such settlements more difficult to achieve in the future. As noted previously, it is undisputed that this settlement is in the best interests of both WPSC and its customers. In addition and unlike some of the costs associated with the EMPs, compliance with the more stringent emission limits directly benefits ratepayers. As a result, the Commission will include these costs in the revenue requirement.

Other Deferrals

As a result of the ratemaking process, and with reasonable regulatory assurance of future cost recovery, utilities sometimes include allowable costs in a period other than the period in which those costs would be charged to expense by an unregulated enterprise in accordance with generally accepted accounting principles. These differences usually relate to the timing of the recognition of a cost. The result of these timing differences is the creation of deferred accounts.

As discussed above, the Commission's policy on deferred accounts is set forth in the Commission's Statement of Position, SOP 94-01. Appendix E is a list of those deferred accounts approved for WPSC, the amortization period, and the amount of Wisconsin jurisdictional 2014 test-year amortization expense. It is appropriate to treat all amortizations as normal test-year expenses by recording the full amounts in the test year.

Electric and Gas Revenue Stability Mechanisms

The electric RSM and the natural gas RSM were initially proposed in a stipulation between WPSC and CUB in the fall of 2008 in docket 6690-UR-119. The Commission accepted the terms of the stipulation but also imposed caps on the amounts that could either be recovered in rates due to an under-collection or returned to customers from an over-collection in any year. The RSMs were applicable only to the residential, small commercial and medium-size commercial classes and were in place for four years until the terms of the stipulation expired at the end of 2012. In the fall of 2012, the Commission accepted a settlement proposal made by WPSC in docket 6690-UR-121 that included provisions that replaced the expiring electric RSM and the natural gas RSM with modified RSMs. The modified RSMs have been in place for 2013. These modified RSMs differed from the original RSMs in several ways. First, the modified RSMs included revenue from monthly customer charges and removed consumption per customer as a factor. Secondly, the modified electric RSM changed the way that the margin per kilowatt-hour (kWh) was determined. The original electric RSM subtracted the average LMP from the kWh energy charge for each class over the course of the year to determine margins from energy sales. The modified electric RSM substituted WPSC's monitored fuel cost per kWh for the LMP in the formula.

In this proceeding, WPSC proposed to continue the electric RSM and the natural gas RSM in their current form indefinitely. WPSC also proposed to eliminate the rate adjustment caps. WPSC argued that the RSMs mitigate risks to the utility that result from differences between sales forecasts and actual sales caused by weather, economic conditions and energy efficiency. WPSC also argued that the RSMs remove any financial incentive that the utility may have to maximize sales.

CUB urged the Commission to discontinue the RSMs. CUB stated it had supported the RSMs when they were initially implemented, but that now WPSC wanted the RSMs to continue while offering nothing to ratepayers in return. Commission staff also encouraged the

Commission to reject WPSC's proposal because the utility had little influence on the energy efficiency decisions made by ratepayers and that WPSC had not shown that it would be financially harmed if the RSMs were discontinued.

WPSC has not offered ratepayers anything in return for the risk reduction that the utility would realize if the RSMs were continued. In addition, because Wisconsin has separated the administration of energy efficiency programs from the utilities through FOE, it is not clear that WPSC can influence ratepayer decisions relating to energy efficiency. The Commission is also persuaded by the unwillingness of CUB and WIEG, representatives for the customer classes who are primarily affected by continuation of the RSM, to continue to embrace the decoupling pilot. For these reasons, the Commission does not find it reasonable to continue the electric RSM and the natural gas RSM as proposed by WPSC.

For test year 2014, applicable electric utility customers are credited with $12,764,000 of RSM-related over-collections of 2012 sales. For test year 2014, applicable natural gas utility customers are charged with $7,877,000 of RSM-related under-collections of 2012 sales. Both of these amounts are reflected in the test-year income statements.

Energy Efficiency

Customer Service Conservation

WPSC's proposed 2014 natural gas and electric customer service conservation (CSC) activities are essentially the same as provided to its customers in the recent past. These activities include providing energy efficiency information and education through field and call center staff, advertising campaigns and bill inserts, newsletters, K-12 Energy Education, and annual