

**BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN**

Joint Application of American Transmission)
Company LLC and Northern States Power)
Company - Wisconsin, as Electric Public)
Utilities, For Authority to Construct and)
Operate a New 345 kV Transmission Line)
from the La Crosse area, in La Crosse County,)
to the greater Madison area in Dane County,)
Wisconsin)

Docket No. 05-CE-142

**DIRECT TESTIMONY OF KARL HOESLY
IN SUPPORT OF THE JOINT APPLICATION**

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1 **INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. My name is Karl J. Hoesly, and my business address is 1414 West Hamilton Avenue,
4 P.O. Box 8, Eau Claire, Wisconsin 54702-0008.

5 **Q. By whom are you employed and in what capacity?**

6 A. I am employed as Manager, Regulatory Affairs at Northern States Power Company, a
7 Wisconsin corporation (“NSPW”). In that capacity, I am responsible for revenue
8 requirements, pricing (rates), rate cases, fuel cost recovery proceedings, and other
9 regulatory administration functions for the electric and gas utilities of NSPW in
10 Wisconsin and Michigan.

11 **Q. Please describe your educational background, professional experience and current
12 responsibilities.**

13 A. I have a Bachelor of Arts degree in Business Administration - Finance from the
14 University of Wisconsin - Green Bay and have completed post-graduate courses in
15 management at the University of Wisconsin - Green Bay. Prior to joining NSPW, I held
16 a number of positions of increasing responsibility at Integrys Energy Group in the finance
17 and regulatory areas, including Senior Financial Analyst, Senior Rate Planner, and most
18 recently Manager of Regulatory Services for Minnesota Energy Resources Corporation, a
19 wholly owned subsidiary of Integrys Energy Group. I assumed my current position at
20 NSPW in February 2007.

1 **Q. For whom are you testifying?**

2 A. I am providing testimony on behalf of NSPW in support of the Joint Application for a
3 Certificate of Public Convenience and Necessity and Wisconsin Department of Natural
4 Resources Utility Permit (“Joint Application”).

5 **Q. What is the purpose of your direct testimony?**

6 A. My testimony will provide an overview of the Interchange Agreement between NSPW
7 and its Minnesota affiliate, Northern States Power Company, a Minnesota corporation
8 (“NSPM”). I will also provide a discussion of the calculation of present value revenue
9 requirement (“PVRR”) for NSPW for the Badger Coulee 345 kV Transmission Line
10 Project (“Badger Coulee Project” or “Project”) and the use of Allowance for Funds Used
11 During Construction (“AFUDC”) in calculating total capital costs for the Badger Coulee
12 Project.

13 **Q. Are you offering any exhibits or referring to any data request responses in your**
14 **testimony?**

15 A. No.

16 **INTERCHANGE AGREEMENT AND PRESENT VALUE REVENUE REQUIREMENT**

17 **Q. Please provide an overview of the Interchange Agreement.**

18 A. Under the Interchange Agreement¹, NSPW and NSPM (collectively NSPW and NSPM
19 are the “NSP Companies”) plan, build, and operate a single integrated electric generation
20 and transmission system, known as the NSP System. Because of the integrated nature of
21 the NSP System, the NSP Companies entered into an agreement for the sharing of all

¹ The I/A is formally titled “Agreement to Coordinate Planning and Operations and Interchange Power and Energy between Northern States Power Company (Minnesota) and Northern States Power Company (Wisconsin).”

1 production and transmission costs, including capital costs. Both NSPW and NSPM rely
2 on the NSP System to meet the electric needs of their customers, and customers of both
3 companies pay a pro rata share of NSP System capital and operating costs under the
4 Interchange Agreement. The Interchange Agreement, which has been approved by the
5 Federal Energy Regulatory Commission (“FERC”), establishes the charges from each
6 company to the other for the sharing of power, energy, and transmission costs between
7 them. Each company shares in NSP System production and transmission costs by billing
8 the other according to the methodologies authorized by the FERC in the Interchange
9 Agreement.

10 **Q. Under the Interchange Agreement how are costs shared between NSPW and**
11 **NSPM?**

12 A. The Interchange Agreement provides for the separation of production and transmission
13 costs into two components: (1) demand-related costs and (2) energy-related costs.
14 Demand-related costs consist of fixed charges on production and transmission investment
15 (return, depreciation, property taxes, income taxes, and insurance), carrying costs on
16 demand-related nuclear refueling outage costs, net capacity purchases, and the fixed
17 portion of operation and maintenance (“O&M”) expenses. Energy-related costs consist
18 of fuel, purchases, sales for resale, variable O&M expenses, carrying costs on energy-
19 related nuclear refueling outage costs, and fuel stocks. The demand-related costs are
20 shared between the NSP Companies based on the ratio of each company’s respective 36-
21 month contribution to NSP System coincident monthly peak demands. The energy-
22 related costs are shared on the basis of the monthly ratio of the energy requirements of

1 each company to the total NSP System energy requirements. For both demand and
2 energy costs, each company's ratio is adjusted for transmission losses. As a general rule
3 of thumb, NSPW shares in approximately fifteen percent of total NSP System production
4 and transmission costs, with NSPM responsible for the remaining 85 percent.

5 **Q. How was the Interchange Agreement used in preparing the Joint Application for the**
6 **Badger Coulee Project?**

7 A. The Interchange Agreement was used to calculate the PVRR for NSPW and the net
8 benefits of the Badger Coulee Project to NSPW's customers and customers of American
9 Transmission Company LLC, by its corporate manager, ATC Management Inc.
10 (collectively "ATC") as part of the Badger Coulee Planning Analysis Addendum
11 (Appendix D to the Joint Application). As described on page 331 of Appendix D, the
12 PROMOD analyses calculated total adjusted production cost and energy loss savings for
13 the Xcel Energy zone for six possible future scenarios, and then allocated the total
14 savings from such results to NSPW according to the standard allocation of the
15 Interchange Agreement.

16 The PVRR reduction to NSPW customers as a result of the Badger Coulee Project
17 was then calculated and used to assess the net benefits of the Project for each of the
18 future scenarios. Table G3 in Appendix D includes the results of these calculations. I
19 provided the calculations for columns (g)-(n) of Table G3 that relate to the cost of the
20 Badger Coulee Project for NSPW's customers.

1 **Q. Briefly describe how you conducted the net PVRR analysis contained in the original**
2 **planning analysis in Appendix D of the Joint Application.**

3 A. A detailed description of my methodology is included in Addendum G in Appendix D of
4 the Joint Application. A general overview of the steps are as follows: First, I calculated
5 the change in NSPW's annual revenue requirement associated with the Project for the
6 years 2012 - 2058. I then calculated the Incremental Interchange Agreement revenue
7 requirement for the same period of time; this is the amount of the Project that will be
8 billed to NSPW through the Interchange Agreement pursuant to the sharing arrangement
9 discussed above. Next, I calculated the impact of the Midcontinent Independent System
10 Operator, Inc. ("MISO") allocated revenue requirement under the Multi Value Project
11 ("MVP") designation, as well as the charge back from ATC's portion of the Project.
12 Finally, I discounted this annual net cost to calculate the PVRR of the Project using a
13 discount rate of 6.7%.

14 **Q. What do these PVRR calculations show as the impact of the Badger Coulee Project**
15 **on NSPW's customers?**

16 A. The PVRR calculations show that NSPW's customers would receive substantial net
17 benefits as a result of Badger Coulee Project. This is because the Badger Coulee Project
18 will reduce NSPW's total revenue requirement and provide a corresponding reduction in
19 the transmission charges paid by NSPW's customers. This occurs because the Badger
20 Coulee Project qualifies as a MISO MVP project, meaning the costs are shared among
21 the entire MISO region and are not just paid for by NSPW's and ATC's customers.

1 **Q. Was the net PVRR for ATC's ratepayers calculated and, if so, who conducted that**
2 **analysis?**

3 A. Yes, the net PVRR for ATC's ratepayers was calculated by Mr. James Hodgson. Mr.
4 Hodgson's direct testimony describes his calculations and includes a discussion of why
5 the net PVRR is an important metric to compare the economic benefits of the Badger
6 Coulee Project to other alternatives.

7 **ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION**

8 **Q. What is AFUDC?**

9 A. NSPW uses AFUDC to recover finance costs during construction of its transmission
10 projects. AFUDC represents the cost of borrowed funds, both equity and debt, in
11 accordance with rules prescribed by the FERC and state public service commissions.
12 This mechanism recognizes the financing costs a utility incurs while building a facility as
13 part of the overall cost of the facility and these charges are accrued during the
14 construction period. Once construction is completed and the asset is placed into service,
15 AFUDC accruals cease. At that time, AFUDC becomes part of the transmission project
16 asset and is capitalized in the same manner as construction labor and material costs and
17 placed into rate base. More specifically, AFUDC is recorded on the income statement
18 and the balance sheet.

19 **Q. Was AFUDC included in the costs for the Badger Coulee Project?**

20 A. NSPW uses AFUDC to recover the finance costs during construction of its transmission
21 projects. However, in Table 4.1-1 of the original Joint Application filed in October 2013,
22 AFUDC was not included in total Project cost estimates as noted in Ex.-Applicants-

1 Henn-2 (Incompleteness Response No. 01.96). As NSPW intends to use AFUDC for its
2 investment in the Badger Coulee Project, Table 4.1-1 was revised in the Joint Application
3 filed in March 2014 to include AFUDC.

4 **CONCLUSION**

5 **Q. Does this complete your testimony?**

6 **A. Yes.**