

Decision No. C16-0399

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF COLORADO**

PROCEEDING NO. 15A-0867G

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IN THE MATTER OF THE APPLICATION OF BLACK HILLS/COLORADO GAS UTILITY COMPANY, LP, FOR APPROVAL OF PARTICIPATION IN PROPOSED COST OF SERVICE GAS PROGRAM AND FOR ALLOWANCE OF COST RECOVERY.

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PROCEEDING NO. 15A-0868E

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IN THE MATTER OF THE APPLICATION OF BLACK HILLS/COLORADO ELECTRIC UTILITY COMPANY, LP FOR APPROVAL OF PARTICIPATION IN PROPOSED COST OF SERVICE GAS PROGRAM AND FOR ALLOWANCE OF COST RECOVERY.

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**DECISION DISMISSING APPLICATIONS  
WITHOUT PREJUDICE**

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Mailed Date: May 17, 2016  
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**I. BY THE COMMISSION**

**A. Statement**

1. By this Decision, the Colorado Public Utilities Commission (Commission) grants the Motion to Dismiss Verified Applications (Motion to Dismiss) filed by the Colorado Office of Consumer Counsel (OCC) on March 18, 2016. Accordingly, we dismiss the Verified Applications for Approval of Participation in Proposed Cost of Service Gas Program and Allowance of Cost Recovery (Applications) filed by Black Hills/Colorado Electric Utility Company, LP and Black Hills/Colorado Gas Utility Company, LP (collectively Black Hills or Company) on November 2, 2015.

2. The Applications request Commission approval of a Cost of Service Gas (COSG) Agreement between Black Hills and its unregulated parent company Black Hills Utility Holdings (BHUH) establishing a COSG Program. Under the terms of the COSG Agreement, the Company would seek subsequent expedited approval of gas reserve acquisitions of up to 50 percent of the Company's forecasted gas demand.

3. In its Motion to Dismiss, the OCC argues that Black Hills failed to prove in its direct case that the COSG Program will result in just and reasonable rates. Black Hills opposes the Motion to Dismiss arguing it has met its burden of going forward and that it has provided substantial evidence that the COSG Program is in the public interest.

4. We find that Black Hills has failed to provide substantial and reliable evidence, through its direct and supplemental direct testimony, to meet its burden of proof that the Applications are in the public interest. Specifically, Black Hills has failed to provide necessary information to evaluate the costs and benefits to ratepayers of the COSG Program. We therefore grant the OCC's Motion to Dismiss and dismiss the COSG Applications without prejudice, consistent with the discussion below.

#### **B. Background and Procedural History**

5. On November 2, 2015, Black Hills filed two applications for approval of its participation in a COSG Program.<sup>1</sup> Black Hills included the prefiled direct testimony and exhibits of seven witnesses with the Applications.

6. According to Black Hills, its COSG Program would provide customers with a long-term hedge against natural gas price volatility. Black Hills proposes to enter the COSG Agreement with its parent company BHUH. Under the COSG Agreement, the Company would commit to acquiring up to 50 percent of its forecast annual firm demand for its gas and electric utilities each year for the term of the COSG Agreement, based on the life of the reserves acquired.

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<sup>1</sup> Proceeding No. 15A-0867G applies to Black Hills Gas Utility; Proceeding No. 15A-0868E to Black Hills Electric Utility.

7. Black Hills refers to the Applications as “Phase I” where the framework of the program and certain parameters are established. If we approve the COSG Agreement and grant the Applications, Black Hills would later seek approval of gas reserve acquisitions by an unregulated affiliate (“COSGCO”) in future “Phase II” applications. If the Commission approves any gas reserve acquisitions, COSGCO would then provide gas to the Company and its ratepayers based on the costs to acquire the reserves and produce the gas.

8. Specifically, Black Hills requests Commission authorization to: (1) participate in the COSG Program by entering into the COSG Agreement with its parent company, BHUH; (2) revise its Gas Cost Adjustment (GCA) clause under the Company’s PUC Tariff No. 3, to recover the costs incurred by Black Hills Gas Utility under the approved COSG Program; and (3) revise its Energy Cost Adjustment clause under the Company’s PUC Tariff No. 9, to recover costs incurred by Black Hills Electric Utility under the approved COSG Program. Black Hills also requests that the Commission approve the requested 50 percent hedge-participation level in the COSG Program based on the Company’s forecast annual firm gas demand or, in the alternative, a revised percentage that the Commission may determine. To the extent necessary, Black Hills requests that the Commission grant such waivers, conditions, approvals, or such other relief as the Commission deems appropriate.

9. By Decision Nos. C15-1321-I and C15-1322-I, issued December 15, 2015, we deemed the COSG Applications complete and set them for hearing *en banc*. We set a pre-hearing conference for January 22, 2016, and required Black Hills to file supplemental direct testimony to address specific questions.

10. Staff of the Colorado Public Utilities Commission and the OCC intervened as of right in Proceeding No. 15A-0867G and in Proceeding No. 15A-0868E. In Proceeding No. 15A-0867G, we granted permissive intervention to Energy Outreach Colorado (EOC) and Constellation NewEnergy-Gas, and we approved the City of Pueblo's request to participate as *amicus curiae*.<sup>2</sup> In Proceeding No. 15A-0868E, we granted permissive intervention to the Board of Water Works of Pueblo, Colorado, and the Fountain Valley Authority; EOC; Interwest Energy Alliance; Pueblo County; and Western Resource Advocates.<sup>3</sup>

11. By Decision No. C16-0083-I issued February 1, 2016, we adopted the procedural schedule and discovery procedures proposed by the parties. We also consolidated Proceeding Nos. 15A-0867G and 15A-0868E, setting 15A-0867G as the primary proceeding.

12. On February 19, 2016, Black Hills filed supplementary direct testimony and exhibits in response to Decision Nos. C15-1321-I and C15-1322-I.

13. By Decision No. C16-0158-I, issued March 1, 2016, we granted Black Hills's Motion for a Protective Order Affording Extraordinary Protection for Highly Confidential Information and Documents.

14. On March 18, 2016, the OCC filed its Motion to Dismiss. On April 1, 2016, Black Hills filed its response to the Motion to Dismiss.

15. By Decision No. C16-0247-I, issued March 25, 2016, we vacated the April 18, 2016 deadline for the filing of answer testimony to provide sufficient opportunity for parties to address the issues in light of the OCC's Motion to Dismiss.

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<sup>2</sup> See Decision No. C15-1353-I issued December 24, 2015 in Proceeding No. 15A-0867G.

<sup>3</sup> See Decision No. C15-1354-I issued December 24, 2015 in Proceeding No. 15A-0868E.

**C. Findings of Fact**

16. The proposed COSG Program is unprecedented because Black Hills seeks: (1) to enter an entirely new semi-regulated gas supply business; (2) to allow an unregulated affiliate to provide a large part of system supply for Black Hills's gas and electric utilities without traditional bidding or other market cost controls; and (3) approval of a multi-decade contract, that includes a prudence determination, without providing an estimate of the costs and or benefits to ratepayers.

17. On December 15, 2015, the Commission issued to Black Hills, supplemental questions that sought additional information on program costs, market gas price forecasts, and the proposed Commission approval process. Responses were due more than two months later on February 19, 2016, providing adequate time to assemble such information. Although Black Hills provided some degree of response to each of the Commission's questions, the responses were insufficient to address the Commission's core concerns.

18. Black Hills would not or could not provide the additional data for projected costs, confidence intervals for such costs, and details of how the Company would carry out the COSG Program, if approved.

19. Although specifically requested by the Commission, Black Hills did not provide a side-by-side comparison of estimated gas costs using its proposed COSG Program compared to its existing hedging program and a combined program using COSG and hedging. The only relevant program cost data presented, is represented by the Company to be for discussion purposes only and is therefore unsubstantiated.<sup>4</sup>

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<sup>4</sup> Confidential Attachments IV-6 and IV-7 provide costs for acquisitions of a limited number of wells in certain geographic locations, but do not provide overall program costs or ratepayer impacts.

20. Cost incurrence for administrative costs, plus the costs of the Hydrocarbon Monitor and Accounting Monitor, would begin immediately after the Commission approves the COSG Applications. Cost recovery through rates would not occur until a subsequent filing to modify the GCA or the Electric Commodity Adjustment (ECA), but the approval of the proposed cost recovery mechanisms in the COSG Agreement and the requested prudence determination would result in accrued costs to ratepayers.

21. Although Black Hills specifically requested a presumption of prudence for the COSG Program, the Company did not define in specific terms what it meant by such a presumption.

## **II. ANALYSIS AND CONCLUSIONS**

### **A. Dismissal Under Colorado Rules of Civil Procedure 41(b)(1)**

22. The OCC filed its Motion to Dismiss under Colorado Rules of Civil Procedure (CRCP) 41(b)(1), which provides in relevant part:

After the plaintiff, in an action tried by the court without a jury, has completed the presentation of his evidence, the defendant, without waiving his right to offer evidence in the event the motion is not granted, may move for a dismissal on the ground that upon the facts and the law the plaintiff has shown no right to relief. The court as trier of the facts may then determine them and render judgment against the plaintiff or may decline to render judgment until the close of all the evidence.

Under CRCP 41(b)(1), a dismissal operates as a judgment on the merits.

23. In support of its motion, the OCC argues that Black Hills has submitted all of the evidence it will present at the hearing and, as a result, the Commission, as the finder of fact, can now determine if the Company has met its burden of proof. According to the OCC, Black Hills has not met its burden of proof because it has not provided evidence for the Commission to find that the COSG Program will result in just and reasonable rates.

24. Black Hills argues that dismissal under CRCP 41 is a drastic remedy that must be applied only in extreme situations that are not present here. According to Black Hills, there is no precedent for dismissal under CRCP 41(b) in gas or electric cases before the Commission,<sup>5</sup> and CRCP 41 has been invoked only in transportation certificate of public convenience and necessity application proceedings where there are statutory criteria that an applicant must meet (e.g., financial fitness).<sup>6</sup> The Company argues that there are no specific statutory requirements that apply to the Commission's consideration of the COSG Program. For these reasons, Black Hills asserts that CRCP 41(b) is inapplicable to this proceeding.

25. We find that the OCC filed its motion to dismiss under CRCP 41(b)(1) at the appropriate time in this Proceeding. There are no specific statutory criteria for the Commission to evaluate these Applications because they are novel and unprecedented. Therefore, we review these applications to determine whether they are in the public interest. *See Caldwell v. Public Utilities Commission*, 692 P.2d 1085, 1089 (Colo. 1984) (holding that the Commission has an independent duty to determine whether matters are within the public interest).

26. The Applications are unprecedented gas reserve acquisition proposals. Black Hills has filed direct testimony and supplemental direct testimony; therefore, it has had ample opportunity to provide the Commission with the information necessary to determine whether Black Hills can meet its burden of proof. Because Black Hills has presented its case-in-chief through the filing of its Applications, direct testimony, and supplemental direct testimony, we further find that we may determine, at this time, whether Black Hills has presented sufficient evidence for the Commission to grant the Applications.

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<sup>5</sup> See Black Hills's Response to Motion to Dismiss at 5 (quoting *Cullen v. Phillips*, 30 P.3d 828, 834 (Colo. App. 2001)).

<sup>6</sup> See Proceeding Nos. 14A-0913CP, 13A-1347CP, and 15A-0648CP.



**B. Burden of Proof and Legal Standard**

27. When ruling on a CRCP 41(b)(1) motion to dismiss, the Commission can, among other things, grant the motion if it finds that the applicant has not satisfied its burden of proof. C.R.C.P. 41(b)(1); *City of Aurora v. Simpson (In re Water Rights of Park County Sportsmen's Ranch)*, 105 P.3d 595, 614 (Colo. 2005). In doing so, the Commission need not accept all facts and statements presented in the application as true simply because there is no answer testimony contradicting them. *See In re Water Rights of Park County Sportsmen's Ranch*, 105 P.3d at 614 (citing *Pioneer Constr. Co. v. Richardson*, 176 Colo. 254, 59, 490 P.2d 71, 74 (1971) ("a court, acting as fact finder, is not bound to accept a statement as true because there is no direct testimony contradicting it")). Rather, the Commission may enter a judgment against the applicant if it finds that the applicant did not meet its burden of proof. *See id.*

28. The OCC and Black Hills agree that Black Hills bears the burden of proof, and that it must meet that burden by a preponderance of the evidence. *See* § 24-4-105(7), C.R.S.; Rule 1500 of the Commission's Rules of Practice and Procedure, 4 *Code of Colorado Regulations* (CCR) 723-1; § 13-25-127(1), C.R.S. (in civil cases the burden of proof is by a preponderance of the evidence). The preponderance standard requires the Commission to determine whether the existence of an alleged fact is more probable than its non-existence. *Swain v. Colorado Department of Revenue*, 717 P.2d 507 (Colo. App. 1985). The OCC and Black Hills also agree that Black Hills can satisfy this burden of proof if the evidence—on the whole and however slightly—tips in favor of Black Hills.

29. The OCC and Black Hills disagree, however, on the proper legal standard that Black Hills must prove by a preponderance of the evidence. The OCC argues that the Commission should dismiss the Applications because Black Hills has failed to prove by a

preponderance of the evidence that the COSG Program will result in just and reasonable rates. See § 40-3-101(1), C.R.S.; *Cottrell v. Denver*, 636 P.2d 703 (Colo. 1981); *Pub. Utils. Comm'n. v. Dist. Ct.*, 527 P.2d 233 (Colo. 1974). Black Hills disagrees that the legal standard is whether the COSG Program will result in just and reasonable rates because its Applications merely “request[] a determination that the COSG Program ‘is prudent for the Company to pursue and that the amounts associated with the COSG Program are *eligible* for recovery’ through the GCA . . . or the ECA.”<sup>7</sup>(Emphasis in Original) Black Hills further states that it is not seeking cost recovery in this proceeding. Instead, it intends to present the costs associated with the purchase and development of each individual gas reserve property to the Commission in Phase II of the COSG Program when the Company files an application for approval of a specific gas reserve acquisition plan. If an acquisition plan is approved, Black Hills would then seek to recover the associated costs in a subsequent GCA or ECA proceeding. Black Hills argues that the legal standard is whether the COSG Program is in the public interest.<sup>8</sup>

30. We conclude that Black Hills has the burden of proof by a preponderance of the evidence to prove that the COSG Program is in the public interest. Although the legal standard at this stage is not limited to the question of whether the COSG Program will result in just and reasonable rates, we consider the likely costs and benefits of the program when determining whether it is in the public interest to grant the Applications. We must therefore determine whether Black Hills has proven, through its Applications and testimony and by a preponderance of the evidence, that granting the Applications is in the public interest.

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<sup>7</sup> Black Hills’s Response to Motion to Dismiss, 9-10.

<sup>8</sup> *Id.* at 5, 21 (“Black Hills has presented substantial evidence that the proposed COSG Program is in the public interest.”); 24 (“Black Hills has more than adequately met its evidentiary burden by providing substantial evidence that the COSG Program and associated procedures would serve the public interest”).

**C. Parties' Substantive Arguments on the Motion to Dismiss****1. OCC's Arguments Supporting Dismissal**

31. The OCC argues that the Commission should dismiss the Applications because Black Hills failed to meet its burden of proof under Rule 1500 of the Commission's Rules of Practice and Procedure, 4 CCR 723-1. According to the OCC, Black Hills did not meet its burden because it failed to provide sufficient evidence on immediate and future costs. The OCC asserts that, if the Commission grants the Applications, ratepayers will incur certain administrative costs even if the Commission never approves an acquisition plan in Phase II. The OCC contends that Black Hills did not provide sufficient information about future costs, including a forecast of the 20-year program cost, which the Commission specifically requested. The OCC concludes that, because the testimony contains no information about future costs, the Commission cannot determine whether rates resulting from the program will be just and reasonable.

**2. Black Hills's Arguments Against Dismissal**

32. Black Hills argues that approval of its Applications will not commit ratepayers to unavoidable immediate costs unless the Commission approves a future gas reserve acquisition in Phase II. According to Black Hills, there will be no rate impact from this proceeding because Phase I of the program establishes only the mechanism, terms, and guidelines for a long-term gas hedging program. Any "immediate costs" will be subject to Commission approval in a GCA or ECA proceeding (if the Commission approves the acquisition) or in a subsequent rate case (if the Commission does not approve the acquisition).

33. Black Hills asserts that the COSG Program is in the public interest, because it will: (1) provide long-term price stability to customers, with reasonable anticipated savings

for customers over the life of the program; (2) reduce customers' exposure to gas price volatility; and (3) peg a portion of customers' gas costs to today's low gas prices and to stable and predictable production costs. Black Hills also claims that its customers will have a reasonable opportunity for savings over the life of the gas reserves compared to the market prices they would otherwise have to pay for natural gas.<sup>9</sup>

34. Black Hills's remarks that the COSG Program is analogous to Public Service Company of Colorado's Innovative Clean Technology Program (ICT Program), which the Commission approved without reliable cost estimates.<sup>10</sup> Black Hills argues that, similar to the ICT Program, Black Hills is asking the Commission to consider the benefits of the proposed COSG Program in this Proceeding, and asking the Commission to allow Black Hills to present specific costs later in a Phase II gas reserve acquisition proceeding. Black Hills states that, as in the initial Public Service ICT proceeding, the Company cannot forecast the costs associated with the COSG Program here because it does not yet know which gas reserves it will pursue; nor does it know the expected costs of acquisition and production.

35. Finally, Black Hills argues that the Commission has approved other gas-price hedging programs without approving the actual costs, and the costs were later approved in a GCA proceeding.<sup>11</sup> According to Black Hills, the longevity of these hedging programs, and the fact that the Commission changed its rules to allow for cost recovery through the GCA, demonstrates the importance of hedging programs in general.

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<sup>9</sup> Black Hills calculates savings as the difference between the net present value of the COSG cost forecast and the long-term market price forecast of gas prices.

<sup>10</sup> See Decision No. C09-0889 in Proceeding No. 09A-015E issued August 13, 2009.

<sup>11</sup> See Proceeding No. 99S-293G (Public Service Company of Colorado's first Gas Price Volatility Mitigation Plan proceeding).

**D. Discussion****1. Insufficient Responses to Commission Questions**

36. Because Black Hills's COSG proposal is a case of first impression, the Commission implemented "Active Case Management," a process under which the Commission asked a series of detailed questions to address deficiencies in Black Hills's pre-filed direct case. We explicitly required the Company to provide the best available estimates for any costs not yet fully determined.

37. In response to questions about forecasting costs, confidence intervals for proposed costs, levels of firm demand, and costs for the Hydrocarbon Monitor and Accounting Monitor, Black Hills repeatedly stated that it does not have nor can it reasonably estimate the relevant information.<sup>12</sup> While a level of costs for the first year of the program was listed in Confidential Exhibit AC-2, titled "COSG Model 1," this information is "posed as a hypothetical example and does not provide a reliable cost estimate."<sup>13</sup> Black Hills states that Exhibit AC-2, is for discussion purposes only until the Company knows or can forecast actual cost elements.<sup>14</sup>

38. Additionally, although Black Hills provided confidential financial estimates in response to our request for a detailed record of the accomplishments of Black Hills Exploration & Production, the information shows a wide range of costs, is inconclusive, and is only a small piece of the overall financial model.

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<sup>12</sup> Supplemental Testimony of Ivan Vancas, p.10, ln 1-3.

<sup>13</sup> *Id.*, p. 6, fn 5.

<sup>14</sup> *Id.* p.12, ln 2-4, Q. 1a.

39. Black Hills did not provide a property acquisition or drilling plan. Black Hills states that it is relying on the Commission to provide guidelines for such acquisitions before the Company can file them.<sup>15</sup>

40. Black Hills did not provide a proposal for the financial hedging it plans to pursue if the COSG Program was to be approved. The Company states that it cannot determine its future hedging plans until the COSG Program is approved.<sup>16</sup>

41. Black Hills did not define what it is seeking in a presumption of prudence for the COSG Program. Black Hills states that in approving the Applications, the Commission must indicate the level of participation (percent of future gas load) the Company is allowed to acquire in gas reserves over the life of the program. Black Hills also asserts that, in order for the Company to participate in the COSG Program, the Commission must assure that it will approve the recovery of future costs.<sup>17</sup> On the other hand, Black Hills states that it is not seeking approval of any specific gas reserve acquisitions here, and that the Commission can grant or deny them in future Phase II expedited proceedings.

42. To the extent that the Company is seeking a presumption of prudence, that, under the COSG Agreement, no party can challenge cost recovery in future rate recovery proceedings, or that challenging parties would face a higher burden of proof, we conclude that Black Hills has not provided adequate cost detail and potential ratepayer impact for the Commission to make such a determination. In addition, to the extent that the Company is seeking a presumption of prudence for the criteria, guidelines, and parameters of the

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<sup>15</sup> *Id.* p.8, ln 17-22.

<sup>16</sup> *Id.* p.14, ln 12-14, Q2b.

<sup>17</sup> *Id.* p.20, ln 3-7, Q.6a.

COSG Program, Black Hills asserts that the Commission may not have such expertise, and so, proposes the Hydrocarbon Monitor.<sup>18</sup> But the monitor is not involved in Phase I.

43. Black Hills failed to answer our question as to why it is reasonable to approve Phase II applications for gas reserve acquisitions on an expedited 60-day schedule. Although the Company offered to provide the Commission with limited acquisition data before it files an application, we conclude that an expedited review of Phase II gas reserve acquisitions would be feasible only if Black Hills had provided estimated costs and ratepayer impacts in this Phase I proceeding, where parties and the Commission would have adequate time to thoroughly investigate the proposed COSG Program. However, Black Hills is not seeking approval of such costs nor has it provided estimates of those costs here.

44. Black Hills is unwilling to allow state-specific changes to the COSG Program without reserving the right to decline to go forward with the program in Colorado.<sup>19</sup> Black Hills does not suggest any way for the states where Black Hills is proposing the COSG Program to confer or to work together to implement necessary changes to the proposed program.

45. Black Hills did not substantiate its use of an unusually high level of equity in its capital structure. Black Hills claims that the equity structure falls within a broad range of benchmarks. However, when asked to explain the high level of equity proposed in the capital structure, the Company merely alluded to a “hybrid risk profile” that warranted a “stronger balance sheet,” while in the same paragraph it admitted that the risks “are undoubtedly attenuated” by the provisions of the COSG agreement.<sup>20</sup>

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<sup>18</sup> *Id.* p.28, ln 3-7, Q8b.

<sup>19</sup> *Id.* p.26, ln 5-7, Q7a.

<sup>20</sup> *Id.* p. 35, ln 7-19, Q12a.

46. Finally, Black Hills failed to provide specific risk factors that differentiate the COSG Program from other regulated utility operations. Instead, the Company suggests that it needs a higher rate of return in order to create “a stronger balance sheet” because investors are likely to determine that the risks of acquiring gas reserves are greater than the risks of investing in regulated utilities.<sup>21</sup>

## 2. Immediate Costs

47. We find that approval of the Phase I Applications will result in Black Hills’s customers incurring immediate costs as required by the COSG Agreement, even if the Commission does not approve any subsequent Phase II acquisitions.

48. Black Hills states “there will be no rate impact” to customers if the Commission grants the COSG Applications, because they “merely to establish the mechanism, terms and guidelines” for the COSG Program.<sup>22</sup> Although Black Hills argues that it does not seek rate recovery in these Applications, the Company seeks approval of the COSG Agreement, a prudence determination, approval of the framework for future gas reserve purchases (including employing a Hydrocarbon Monitor and Accounting Monitor), and provisioning for recovery of future costs through the GCA and ECA tariffed rates.

49. If the Commission approves the Phase I Applications, Black Hills must carry out the actions prescribed in the COSG Agreement to pursue the acquisition of reserve interests, thus incurring costs. For example, to propose a single reserve interest to the Commission in a Phase II application, costs would be incurred—at a minimum—for administration of the program, evaluating potential resources, and fulfilling Hydrocarbon Monitor requirements.

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<sup>21</sup> *Id.* p. 37, ln 1-2, 6-8, Q12b.

<sup>22</sup> *Id.* p.7, ln 4-6.



Black Hills estimates that it would incur costs of approximately \$225,000 for all program administration fees in the first year of the existence of COSGCO, the new unregulated affiliate that will own and manage the gas reserves.<sup>23</sup>

50. Black Hills states that it would ask the Commission to approve rate recovery in a “rate case or other subsequent proceeding before the Commission”<sup>24</sup> for costs incurred in pursuing the reserve interests as described in the COSG Agreement. Therefore, if we approve the COSG Agreement with the requested prudence determination, Black Hills would likely argue that the costs expended to pursue all gas reserve acquisitions were prudently incurred, and the Company would pursue recovery of such costs even if we deny all Phase II reserve acquisition applications.

### **3. Insufficient Information About Future Costs and Benefits**

51. Black Hills has failed to provide an adequate estimation or forecast of program costs. Because Black Hills has not provided any details associated with costs or the likely economics of its proposed program, the Commission cannot assess the viability and potential benefits of the program, including the claimed reduction in gas supply price volatility and the potential for reduced gas costs compared with market purchases.

52. For example, Black Hills states that it intends to “peg a portion of customers’ gas costs to today’s low gas prices and to stable and predictable production costs.”<sup>25</sup> However, Black Hills provides no evidence whatsoever that it is possible to achieve such objectives. Even after the Commission specifically questioned Black Hills about this aspect of its case,

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<sup>23</sup> *Id.* p.16, ln 12-14 (Black Hills describes this exhibit and information as “hypothetical” and “for discussion purposes only,” so the certainty of this value is highly speculative. In any case, it is likely that the costs of the monitors and administration are significant.).

<sup>24</sup> Black Hills’s Response to Motion to Dismiss, at 11.

<sup>25</sup> Direct Testimony of Ivan Vancas, p.4, ln 1-2

it was unable or unwilling to provide any forecast data, estimates, or other evidence in support in its testimony.

53. Black Hills proposes in its COSG Applications to enter into a contract with its unregulated affiliate for an unspecified length of time—likely extending for decades—to supply up to 50 percent of system gas requirements, at a substantial cost. It is not appropriate for the Commission to consider the specific costs of the program only after the COSG Agreement is approved, because it would be too late to make meaningful changes to the Agreement or to consider whether the Agreement is in the public interest. Even if the Commission and the parties could adequately review a Phase II acquisition application on the proposed highly expedited 60-day timeline, the COSG Agreement and prudence determination would have already been made, and the Commission could not alter the primary terms of the Program, even after it receives complete information on how the Program will affect rates.

#### **4. Distinguishable from the ICT Program**

54. Despite Black Hills's contention to the contrary, we find that the proposed COSG Program is indeed distinguishable from Public Service's ICT Program. The ICT Program is structured to allow the Commission to approve potential electric generation resources that are small in scale and have a minimal customer rate impact, analogous to a pilot project.<sup>26</sup>

55. The normal process for the Commission to consider new energy technology electric resources is through the electric resource plan procedures, where we consider all resources on a cost and production basis. Public Service's Electric Resource Plan typically includes thousands of megawatts of potential resources. The ICT Program allows Public Service

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<sup>26</sup> See Decision No. C09-889 in Proceeding No. 09A-015E.

to apply for approval of smaller resources, typically just a few megawatts, without the expense and time constraints associated with the Electric Resource Planning process.

56. The large scale and potential rate impacts of the COSG Program places it in an entirely different category from the ICT Program. Further, the expedited review of ICT projects must be preceded by stakeholder review. We are not aware that a stakeholder review process is proposed here, and the Hydrocarbon Monitor and Accounting Monitor proposals are not an adequate substitute for a stakeholder review.

### **5. Distinguishable from Other Hedging Programs**

57. We also find that the proposed COSG Program is distinguishable from other hedging programs approved by the Commission. We find Black Hills's arguments unavailing that other hedging programs provide an example of why the COSG Program costs do not need to be considered until a Phase II gas reserve acquisition application is filed.

58. Black Hills failed to provide any testimony or evidence with which to compare the COSG Program to the existing hedging program under its Gas Mitigation Plan. We asked Black Hills to provide a side-by-side comparison of the estimated gas costs of its proposed COSG Program, its existing hedging program, and a combined program using COSG and existing hedging. However, Black Hills did not provide the requested comparisons, insisting that it could not do so until the COSG Program was essentially up and running.<sup>27</sup> Although the Company referenced the Aether price scenario models, which compare hedging scenarios,<sup>28</sup> the Company did not address the Commission's request to compare the proposed COSG Program to the existing hedging program.

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<sup>27</sup> Supplemental Testimony of Ivan Vancas, p.18, ln 3-6.

<sup>28</sup> *Id.*, p.18, ln 17-23.

59. We also find that the approved financial hedging programs are significantly different from the COSG Program.<sup>29</sup> For example, under the approved financial hedging programs, utilities do not apply for pre-approval of contracts or predetermination of prudence and utilities do not earn a profit on such gas costs. Gas supply and hedging contracts are typically awarded, based on bidding or participation through established markets rather than the sole-source unregulated affiliate transaction as proposed by Black Hills. Hedging provisions typically have one to three year terms with occasional five to ten year fixed contracts, rather than a term equal to the life of the wells, as proposed under the COSG Program. Further, the proposed acquisition of 50 percent of system gas requirements under the COSG Program sets an unprecedented level of hedging for one contract, and even the vague details that Black Hills did present for the program indicate a very large immediate rate increase for customers in the early years of the program if resources are ultimately acquired.<sup>30</sup>

60. Additionally, we are not persuaded by Black Hills's assertion that the recent approval of programs in Utah and Wyoming, such as Questar Gas Company's acquisition of property under the Wexpro II agreement in 2013, provide an example of how its proposed approval structure can be approved.<sup>31</sup> Those approvals were generally a continuation of long-standing programs, which were enacted in substantially different circumstances with higher market gas prices, lower supply levels, and different production methodologies. Further, the Commission is not required to follow precedent established by another state.

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<sup>29</sup> See, e.g., Decision Nos. R99-1094 and C03-0588, in Proceeding No. 99S-293G; Decision No. C11-1132 in Proceeding No. 11A-580E; and Decision No. C15-0447 in Proceeding No. 15A-0199E.

<sup>30</sup> See Exhibit AC-2.

<sup>31</sup> See Direct Testimony of Ivan Vancas, p. 13, fn 3 (citing *In the Matter of the Application of Questar Gas Company for Approval to Include Property Under the Wexpro II Agreement*, Dkt. No. 13-057-13, Report and Order (Jan. 17, 2014)).

## E. Conclusions

61. We conclude that Black Hills was unwilling or unable to provide evidence demonstrating that its proposed COSG Program is in the public interest. The fundamental lack of cost information and other evidence makes it impossible to determine tangible customer benefits. Likewise, without a meaningful analysis of likely costs and benefits, the Commission is unable to make a public interest determination.

62. Black Hills provided essentially no information to substantiate its claim that the program will “peg a portion of customers’ gas costs to today’s low gas prices.”<sup>32</sup> The limited information Black Hills did provide indicates that ratepayers would see a significant rate increase in the early years of the program and that Black Hills would immediately enjoy what amounts to a guaranteed profit margin. Any benefits to ratepayers will be delayed and are questionable because they are based on the speculative long-term forecast of increased market gas prices.<sup>33</sup> Without substantially more information concerning likely program costs and operations, we cannot determine the likelihood that the COSG program can supply gas at prices that would provide a benefit to ratepayers.

63. Approval of the Phase I Applications and the COSG Agreement creates a presumptive expectation that the Commission will approve subsequent Phase II applications for reserve interests (and resulting costs) as long as the Company follows the guidelines in the COSG Agreement.<sup>34</sup> Although Black Hills argues that the Commission can analyze costs

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<sup>32</sup> *Id.*, p.4 ln 1-2

<sup>33</sup> Further, Black Hills’s confidential forecast gas price for 2016 is nearly double the actual market prices to date. We therefore question the accuracy of forecast prices 10 to 20 years from now and any estimates of ratepayer benefits based on that forecast.

<sup>34</sup> For example, the COSG Agreement contains a specific Acquisition Criteria that, if met, guarantees that a reserve interest will qualify under the Program. *See* Exhibit A to Attachment IV-1.

when the Company proposes specific resources in Phase II, we conclude that it is not in the public interest for the Commission to approve the Phase I Applications if Black Hills fails to provide any useful analysis of the likely costs and benefits of the program until Phase II.

64. Further, without a detailed examination of the anticipated costs and ratepayer impacts of the program in Phase I, the Commission could not adequately evaluate a Phase II reserve acquisition on an expedited 60-day schedule. We thus conclude that approval of the framework for a highly expedited 60-day Phase II application is unreasonable without a full analysis of potential costs and customer impacts in Phase I.

65. Black Hills seeks an unusually high level of equity and a higher rate of return because it asserts that there is a high risk profile for the COSG Program. However, Black Hills fails to provide any protection from the risks to ratepayers if the Commission were to grant these Applications. Black Hills did not identify and substantiate specific risk factors that differentiate the COSG Program from other regulated utility operations. Black Hills therefore failed to provide a reasonable basis for its use of an unusually high level of equity and higher rate of return in its capital structure, and the Company asserts that the contract cannot be modified since it has been proposed in other states.

66. Black Hills did not identify and substantiate specific risk factors that differentiate the COSG Program from other regulated utility operations. Black Hills therefore failed to provide a reasonable basis for its use of an unusually high level of equity and higher rate of return in its capital structure, and the company asserts that the contract cannot be modified since it has been proposed in other states.

67. Finally, we find that an inherent conflict of interest exists between the Accounting and Hydrocarbon Monitors, the Company, and ratepayers because Black Hills's parent company, BHUH, would hire and pay the Monitors.

68. We provided Black Hills with an opportunity to give us the information necessary to determine whether the COSG Program is in the public interest by issuing supplemental questions. In response, the Company provided only a fraction of the information we requested. The only relevant information the Company provided was characterized by the Company as "hypothetical" and, "for discussion purposes only."

69. Black Hills has failed to present, in its case-in-chief, sufficient and reliable evidence to quantify or otherwise permit a reasonable analysis of the COSG Program as proposed. Black Hills also failed to present evidence to support its fundamental premise that the COSG Program will provide long-term price stability through a physical hedge and provide an opportunity for customers to pay less than market prices.

70. Black Hills has therefore failed to meet the required burden of proof to defeat a motion to dismiss under CRCP 41(b)(1). We grant the Motion to Dismiss and dismiss the COSG Applications without prejudice.

### **III. ORDER**

#### **A. The Commission Orders That:**

1. The Motion to Dismiss Verified Applications filed by the Colorado Office of Consumer Counsel on March 18, 2016, is granted, consistent with the discussion above.

2. The Verified Application for Approval of Participation in a Proposed Cost of Service Gas Program and For Allowance of Cost Recovery filed by Black Hills/Colorado Gas

Utility Company, LP on November 2, 2015, is dismissed without prejudice, consistent with the discussion above.

3. The Verified Application for Approval of Participation in a Proposed Cost of Service Gas Program and For Allowance of Cost Recovery filed by Black Hills/Colorado Electric Utility Company, LP on November 2, 2015, is dismissed without prejudice, consistent with the discussion above.

4. The procedural schedule established by Decision No. C16-0083-I is vacated.

5. The 20-day time period provided by § 40-6-114, C.R.S., to file an application for rehearing, reargument, or reconsideration shall begin on the first day after the effective date of this Decision.

6. This Decision is effective upon its Mailed Date.

**B. ADOPTED IN COMMISSIONERS' WEEKLY MEETING  
April 27, 2016.**

(S E A L)



ATTEST: A TRUE COPY

Doug Dean, Director

THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF COLORADO

JOSHUA B. EPEL

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GLENN A. VAAD

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FRANCES A. KONCILJA

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Commissioners