Decision No. C20-0372

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF COLORADO

PROCEEDING NO. 19AL-0075G

IN THE MATTER OF ADVICE LETTER NO. 1 FILED BY BLACK HILLS COLORADO GAS, INC. TO PLACE IN EFFECT ITS NEW P.U.C. VOLUME NO. 1 TARIFF ESTABLISHING NEW RATE SCHEDULES AND BASE RATES FOR ALL NATURAL GAS SALES AND TRANSPORTATION SERVICES, INCREASING JURISDICTIONAL BASE RATE REVENUES, COMBINING EXISTING GAS COST ADJUSTMENT ("GCA") AREAS INTO NEW GCA REGIONS, IMPLEMENTING A DISTRIBUTION SYSTEM INTEGRITY RIDER, REVISING THE CONSTRUCTION ALLOWANCE CALCULATION METHOD, AND OTHER PROPOSED TARIFF CHANGES TO REPLACE AND SUPERSEDE ITS P.U.C. VOLUME NO. 3 TARIFF (FORMERLY BLACK HILLS/COLORADO GAS UTILITY COMPANY, INC.) AND P.U.C. VOLUME NO. 7 TARIFF (FORMERLY BLACK HILLS GAS DISTRIBUTION, LLC) IN THEIR ENTIRETY, TO BECOME EFFECTIVE ON MARCH 4, 2019.

**COMMISSION DECISION GRANTING, IN PART,
AND DENYING, IN PART, EXCEPTIONS TO
RECOMMENDED DECISION NO. R19-1033;
PERMANENTLY SUSPENDING TARIFF SHEETS;
ESTABLISHING RATES; AND REQUIRING FILINGS**

Mailed Date: May 19, 2020
Adopted Date: April 14, 2020

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I. BY THE COMMISSION

A. Statement

1. Through this Decision, the Commission grants, in part, and denies, in part, the exceptions filed to Recommended Decision No. R19-1033, issued December 27, 2019, by Administrative Law Judge (ALJ) Conor F. Farley (Recommended Decision). The Recommended Decision permanently suspends the tariff sheets filed by Black Hills Colorado Gas, Inc. (Black Hills or the Company) with Advice Letter No. 1, filed February 1, 2019, as amended by Black Hills, and orders Black Hills to file modified rates and tariff sheets consistent with the terms of the Recommended Decision. Black Hills and intervenors Staff of the Colorado Public Utilities Commission (Staff); the Colorado Office of Consumer Counsel (OCC); Energy Outreach Colorado (EOC); and Bachelor Gulch Village Association (BGVA) filed exceptions seeking to reverse, modify, or amend portions of the Recommended Decision. After considering the filed exceptions, the responses thereto, and the evidentiary record in this Proceeding, we grant, in part, and deny, in part these exceptions.

B. Recommended Decision

2. Black Hills commenced this rate case with the filing of Advice Letter No. 1 on February 1, 2019. Through Advice Letter No. 1, the Company proposes to consolidate the rates, tariffs, and service offerings of its two predecessor gas utilities: Black Hills/Colorado Gas Utility Company, Inc. (BHGU), the legacy gas utility acquired from Aquila, Inc. (Aquila) in 2008; and Black Hills Gas Distribution, LLC (BHGD), the SourceGas companies acquired in 2016. Black Hills proposes to consolidate the three existing base rate areas of BHGU and

BHGD into a single statewide base rate area for purposes of establishing an overall revenue requirement for Black Hills. For purposes of bill mitigation, however, Black Hills proposed to implement two sets of base rates for two newly defined base rate areas. The base rates filed with Advice Letter No. 1 are set to recover a revenue requirement deficiency of approximately $2.5 million. Black Hills subsequently revised the revenue requirement deficiency to $3.5 million but did not propose modified base rates in the consolidated rate schedules. In addition to base rate area consolidation, through Advice Letter No. 1, Black Hills further proposes to: combine the seven existing gas cost adjustment (GCA) areas of BHGU and BHGD into three newly defined GCA areas; implement a Distribution System Integrity Rider (DSIR) to allow current recovery of system safety and integrity investments; and modify its construction allowances for new customer connections.

3. In support of its proposals, Black Hills initially submitted a single statewide Revenue Requirement Study (RRS) and a single statewide Class Cost of Service Study (CCOSS). At the end of the evidentiary hearing, after witnesses for Staff and the OCC testified that the Commission could not determine whether the Company's proposed consolidated and mitigated rates were reasonable, the parties agreed to keep the record open to allow the Company to file four additional CCOSSs. After supplemental direct and answer testimony from Black Hills and the intervenors, the ALJ convened an additional hearing day in October 2019 where the Company provided live rebuttal testimony and parties cross-examined witnesses.

4. The opening paragraphs of the Recommended Decision call this rate case "flawed from the beginning" and conclude that the resulting evidentiary record is "substantially deficient in many areas."[1] The Recommended Decision faults the "atypical" breadth of the issues raised

[1] Recommended Decision ¶¶ 1, 11.

in the Company's Advice Letter No. 1 and the "flaws" in the Company's handling of the case including its "updates" and "corrections" to the RRS and the Company's initial decision to file only a consolidated RRS and CCOSS.[2] The Recommended Decision concludes the evidentiary record is sufficiently developed to allow the ALJ to decide the Phase I issues raised in Advice Letter No. 1, but not to allow the ALJ to find and conclude that Black Hills' proposals on base rate area consolidation and the other Phase II issues, the DSIR, and construction allowances yield just and reasonable rates and are in the public interest.[3]

5. Because of these flaws and deficiencies, the Recommended Decision decides the Phase I issues but denies Black Hills' remaining requests. The Recommended Decision finds the supplemental RRSs and CCOSSs filed after the hearing for each base rate area are "insufficient by themselves" to produce rates that the ALJ can find and conclude are just and reasonable because of the changes made by the Recommended Decision to the inputs to these studies.[4] The Recommended Decision finds the Company "performed little analysis" of the development of cost-based rates generated from the new CCOSSs and that intervenors had "comparatively little time" to review.[5] The Recommended Decision therefore orders the Company to implement a General Rate Schedule Adjustment (GRSA) to adjust current rates proportionally for each of the three existing base rate areas. The ALJ finds the rates resulting from application of a GRSA are just and reasonable as they are based on existing rates with a proportional increase or decrease to implement the necessary changes in revenue requirements.[6] The Recommended Decision orders the Company to file a new Phase II rate case within six months and to provide, at a minimum, a

[2] Recommended Decision ¶ 6-8.
[3] Recommended Decision ¶ 11.
[4] Recommended Decision ¶ 302.
[5] Recommended Decision ¶ 305.
[6] Recommended Decision ¶ 310.

proposal with CCOSSs for each existing base rate area and all rates for each base rate area. The Recommended Decision clarifies that the Company may also propose consolidated rates as an alternative. By approving, in part, a Motion to Approve Partial Stipulation and Settlement Agreement Between Black Hills, Staff, and EOC (Partial Stipulation and Settlement) filed on August 1, 2019, the Recommended Decision grants the formation of three newly defined GCA regions. The Recommended Decision denies Black Hills' request for a DSIR and orders the Company to file a new advice letter and tariff sheets proposing a DSIR within six months addressing the concerns with the Company's proposal identified in the Recommended Decision. Similarly, the Recommended Decision denies Black Hills' construction allowance proposal and orders the Company to file for approval of revised construction allowances within nine months and include in that filing the analysis found lacking in this Proceeding in the Recommended Decision.

C. Black Hills Filing in Response to Interim Decision No. C20-0123-I

6. Black Hills supported through written testimony, a deficiency in its total revenue requirement, calculated on a statewide basis for a single base rate area, of approximately $3.5 million. Following the final hearing day on October 24, 2019, the ALJ scheduled a Technical Conference[7] for the purpose of translating into rates, Black Hills' revenue requirement calculations, the various Phase I proposals, the proposed DSIR, and their combined impacts assuming that not all of Black Hills' requests in this rate case were granted by the Commission. The ALJ ordered Black Hill to model the RRSs, CCOSSs, and bill impacts for the following scenarios: (i) three separate base rate areas plus no post-base period capital additions and

[7] The Technical Conference was scheduled for December 3, 2019 in Decision No. R19-0968-I on December 3, 2019.

adjustments and no DSIR; (ii) three separate base rate areas including post-base period capital additions and adjustments and a separate DSIR for each base rate area; (iii) consolidated base rate areas (Black Hills' proposal) plus no post-base period capital additions and adjustments but with a statewide DSIR (Black Hills' proposal); and (iv) consolidated base rate areas (Black Hills' proposal) plus no post-base period capital additions and adjustments and no DSIR. The ALJ directed Black Hills to calculate the RRSs using an authorized return on equity of 9.0 percent.

7. As explained in the Recommended Decision, Black Hills filed the revised RRSs and CCOSSs in accordance with the scenarios identified by the ALJ prior to the Technical Conference on December 18, 2019.

8. On February 28, 2020, pursuant to Decision No. C20-0123-I,[8] Black Hills filed additional information on RRSs, CCOSSs, GRSAs, and bill impacts calculated in accordance with the conclusions, findings, and directives in the Recommended Decision.

D. Exceptions to Recommended Decision

9. Pursuant to § 40-6-109(2), C.R.S., and Rule 4 *Code of Colorado Regulations* (CCR) 723-1-1505(a) of the Commission's Rules of Practice and Procedure, Black Hills and intervenors Staff, the OCC, EOC, and BGVA timely filed exceptions to the Recommended Decision on January 16, 2020. Black Hills, Staff, and the OCC also timely filed responses to the exceptions on January 30, 2020.

1. Black Hills' Legal Challenges to the Recommended Decision

10. The Recommended Decision finds the record in this Proceeding is not sufficiently developed to decide the consolidation proposal and other Phase II issues, the Company's request for a DSIR, and the Company's requested changes to the construction allowances. The

[8] Decision No. C20-0123-I was issued on February 21, 2020.

Recommended Decision denies these proposals and orders the Company to file a new Phase II rate case within six months, a new advice letter and tariff sheets proposing a DSIR within six months, and a filing for approval of revised construction allowances within nine months.

2. Black Hills Exceptions

11. In its exceptions, Black Hills challenges that the Recommended Decision unlawfully denies the Company's proposals on the Phase II issues, DSIR, and requested changes to the construction allowances. Black Hills asserts: "There is no legal basis for the Commission to reject the Company's filed rates and tariffs on its proposed Phase II, DSIR, and construction allowance initiatives and also to refuse to fashion a just and reasonable resolution based on the expansive evidence in this record."[9] Black Hills argues that "[k]icking out" as deficient and ordering the Company to re-file major portions of its filing is tantamount to rejection of these aspects of the filing, which is unlawful and violates the Company's rights to due process.[10] Citing the statutory provisions §§ 40-6-111(2)(a)(I) and (II), C.R.S., Black Hills contends that, once the Commission acts to suspend a rate filing, it is the Commission's duty and charge to determine whether the Company's proposals are just and reasonable and, if the Commission finds the proposed rates and tariffs are not just and reasonable, to determine the permanent just and reasonable rates and tariffs to be observed thereafter. Black Hills contends that "jettisoning" these issues is an abdication of the Commission's statutory duties and a violation of the Company's statutory and constitutional rights.[11]

12. In its exceptions, Black Hills claims that it "provided substantial evidence in the form of testimony, tables and attachments" in this Proceeding showing that its proposed

[9] Black Hills Exceptions p. 3.

[10] Black Hills Exceptions p. 3.

[11] Black Hills Exceptions p. 4.

mitigated rates are just and reasonable.[12] Black Hills claims it was legal error for the ALJ to deem the Company's failure to provide evidence supporting any alternative to its rate proposals as a "flawed approach" and this improperly influenced the ALJ's determinations regarding satisfaction of the Company's burden of proof. Black Hills claims that "[d]espite the significant record evidence" showing the Company's proposed pipeline safety and integrity programs are in accordance with federal and state regulations and that the proposed DSIR is consistent with riders approved for other Colorado gas utilities, the ALJ determined the record was insufficient to find approval of the DSIR was in the public interest.[13] And Black Hills claims the ALJ incorrectly found there was no record evidence concerning whether the proposed construction allowances result in a subsidy between existing and new customers. Black Hills counters that Company witness Hyatt explained during hearing how to evaluate whether the proposed allowance subsidizes existing customers.[14]

3. Staff Response to Black Hills Exceptions

13. In response to Black Hills' exceptions, Staff argues that denial of these discrete proposals within the Company's filing is lawful. Staff reasons that the Recommended Decision did not outright dismiss Black Hills' Advice Letter No. 1 but rather denied discrete proposals within the larger filing. Staff states the Commission reviewed all admitted evidence and arguments, granted the proposals it found supported by a preponderance of the evidence, and denied the proposals lacking enough support. Staff counters that the case law the Company relies on, *Municipal Light Boards of Reading & Wakefield, Mass. v. FPC*, 450 F.2d 1341, 1345 (D.C. Cir. 1971), is irrelevant. Staff argues the issue of "substantive nullity" decided in the

[12] Black Hills Exceptions p. 16.

[13] Black Hills Exceptions pp. 20-21.

[14] Black Hills Exceptions p. 36 (citing Aug. 7, 2019 Hrg. Trans. (Hyatt) 57:15-58:5; 58:13-61:3).

cited decision is inapplicable because it concerned an order of the Federal Power Commission, with different authority than the Commission as a state agency with constitutional and statutory authority. Staff argues that denial of these discrete proposals for lack of supporting evidence does not violate Black Hills' due process or statutory rights. Staff responds that Black Hills has no statutory right to succeed in litigated proceedings before the Commission and the Company fails to point to any specific instance where the Commission did not provide due process.

14. Finally, Staff responds that the Recommended Decision provides a path to new, just, and reasonable rates for the Company. Staff argues that, through GRSAs for each base rate area, the Company will be able to charge new rates that reflect the new revenue requirement established in this Proceeding. Citing well-established case law, Staff points out the Commission has an independent duty to determine matters that fall within the public interest and therefore is "not bound by the proposals of the parties and may do what it deems necessary to assure that the final result is just, reasonable, and in the public interest, provided the record supports the result, and provided the reasons for the policy choices made are stated."[15] Staff concludes that GRSA riders are a common tool for setting rates in Phase I-only rate cases and the use of GRSAs in this Proceeding is the one path the ALJ had left after denying the Phase II, DSIR, and construction allowance proposals for insufficient supporting evidence.

4. Findings and Conclusions

15. We deny Black Hills' exceptions contending the Recommended Decision unlawfully denied the Company's Phase II, DSIR, and construction allowance proposals.

16. We agree with the discussion in the opening paragraphs of the Recommended Decision that a series of "flaws" in this Proceeding led to a record that is "substantially deficient

[15] Staff Response to Exceptions filed January 30, 2020 at p. 22.

in many areas."[16] As the Recommended Decision identifies, these flaws include that it was predicable the depth and breadth of issues raised by the Company's advice letter would strain the Commission's and intervenors' resources and "lead to a less than fulsome" record;[17] that Black Hills filed updates and corrections to the RRS that, coupled with the cap on the revenue requirement at the original amount, meant the base rates in the tariff sheets were not cost-based and caused confusion about whether the parties and the Commission should focus on the original revenue requirement study or the revised version;[18] and that Black Hills only filed individual CCOSSs for the existing base rate areas late in the Proceeding.[19]

17. By denying these proposals within the Company's Advice Letter No. 1, the Commission does not abdicate its duties or violate the rights of Black Hills. We find the Commission cannot be compelled to formulate just and reasonable rates out of a deficient record. Necessarily, the proponent must first provide a comprehensive factual record to allow the Commission to determine whether or to what extent its proposed changes are just and reasonable and in the public interest. Under the Commission's rules and applicable statutes,[20] the proponent bears the burden to prove its case by a preponderance of the evidence such that the evidence tips in favor of that party.[21] And this evidence must be "substantial evidence," which means such relevant evidence as a reasonable person's mind might accept as adequate to support a conclusion; it must be enough evidence to justify, if the trial were to a jury, a refusal to direct a

[16] Recommended Decision ¶ 11.
[17] Recommended Decision ¶ 6.
[18] Recommended Decision ¶ 7.
[19] Recommended Decision ¶ 8.
[20] Rule 4 CCR 723-1-1500 of the Commission's Rules of Practice and Procedure; *see also* §§ 24-4-105(7) and 13-25-127(1), C.R.S.
[21] *Schocke v. Dep't of Revenue,* 719 P.2d 361, 363 (Colo. App. 1986).

verdict when the conclusion sought to be drawn from it is one of fact for the jury.[22] Here, without Black Hills first meeting its evidentiary burden, the Commission lacks the record evidence needed to determine whether the Company's proposed rates are just and reasonable, as required by statute,[23] and to make a decision properly supported by the record, as required to withstand judicial review.[24]

18. Even Black Hills' own legal challenges assume the Commission has a sufficient record on which to make decisions and formulate new rates. Citing the seven-day hearing before the ALJ, Black Hills argues the hearing record is "*vast* and *fully developed*."[25] Black Hills claims the Commission would abdicate its duties if it declines to "fashion a just and reasonable resolution based on the *expansive evidence* in this record."[26] Black Hills dismisses the ALJ's concerns about additional analyses of alternatives to the Company's proposals as "not a valid basis to refuse to resolve the disputed issues based on the *ample record of evidence*."[27] We disagree with this assumption and uphold the Recommended Decision's conclusion that Black Hills has not met its burden of proof to support its Phase II, DSIR, and construction allowance

[22] *See, e.g., City of Boulder v. PUC*, 996 P.2d 1270, 1278 (Colo. 2000) (quoting *CF&I Steel, L.P. v. PUC*, 949 P.2d 577, 585 (Colo. 1997)).

[23] *See* § 40-6-111(2)(a)(I), C.R.S. (Commission shall establish rates and charges that it "finds just and reasonable").

[24] Pursuant to § 40-6-115(3), C.R.S., the reviewing court will determine whether: the Commission regularly pursued its authority, its decision is just and reasonable, and its conclusions are in accordance with the evidence. Applying this standard, courts examine whether "substantial evidence" supports the decision. *Durango Transp., Inc. v. PUC*, 122 P.3d 244, 250 (Colo. 2005). The reviewing court may not substitute its judgment when substantial evidence supports the Commission's decision. *See, e.g., Colo. Office of Consumer Counsel v. PUC*, 275 P.3d 656, 659 (Colo. 2012).

[25] Black Hills Exceptions p. 2 (emphasis added).

[26] Black Hills Exceptions p. 3 (emphasis added).

[27] Black Hills Exceptions p. 4 (emphasis added).

proposals.[28] And because of these deficiencies, we find the Recommended Decision properly declined to approve these proposals within this Proceeding.

19. The Commission has previously denied proposals within a rate case that are unsupported by a preponderance of the evidence. In Public Service Company of Colorado's (Public Service) last three gas rate cases, the Commission denied Public Service's proposals to implement a future test year and multi-year rate plan because Public Service did not meet its burden of proof to support these proposals.[29]

20. Moreover, to the extent the Commission is required under §§ 40-6-111(2)(a)(I) and (II), C.R.S., as the Company claims, to establish the rates that it finds just and reasonable rates after it suspended Black Hills' tariff filing, the Commission has done so here. The Commission fully resolved the Phase I issues presented by the Company. The result of those decisions is an updated revenue requirement for the Company and updated rates through GRSAs that adjust current rates proportionally for each base rate area. That the Commission did not resolve the Phase II issues and rejected the Company's DSIR and construction allowance proposals does not mean the Commission fell short in its adjudication. Rather, the Commission resolved what the evidentiary record allowed for consideration in this Proceeding and provided direction and requirements for resolution of the remaining issues deferred to future proceedings.

[28] *See* Recommended Decision ¶ 11 (finding record not sufficiently developed to allow the Commission to find and conclude the Company's proposals on the Phase II issues, request for DSIR, and requested changes to construction allowances yield just and reasonable rates and are in the public interest).

[29] *See* Proceeding No. 17AL-0363G (concluding Public Service failed to satisfy its burden of establishing its MYP provides an accurate picture of the expected revenue, expense, and investments or generates rates that fairly balance the interests of the utility and ratepayers and are just and reasonable); Proceeding No. 15AL-0135G (finding Public Service provided little information to support a finding that its MYP would serve the public interest); and Proceeding No. 12AL-1268G (finding Public Service's evidence and arguments not well-founded and unpersuasive).

5. Base Rate Area Consolidation

21. The Recommended Decision finds Black Hills did not satisfy its burden to establish that its proposal to consolidate the three existing rate areas of BHGU and BHGD into a single base rate area is in the public interest.

22. The Recommended Decision examines prior Commission decisions concerning rate area consolidations and concludes that none of the factors discussed in those proceedings support the Company's consolidation proposal in this Proceeding. As discussed in the Recommended Decision, these factors are the absence of a substantial rate disparity between the existing base rate areas; evidence of present or future physical connection between systems serving each base rate area; and potential future operational efficiencies from consolidation yielding cost savings. The ALJ finds Black Hills has conceded in this Proceeding that there is no possibility of future physical connection between the three existing rate areas, there is a substantial rate disparity between the existing rate areas, and there are no efficiencies resulting in cost savings that will result from the consolidation of the base rate areas. The Recommended Decision concludes these factors "weigh heavily against granting" Black Hills' proposed base rate area consolidation.[30]

23. In particular, the ALJ finds as undisputed, significant existing rate disparity among the existing base rate areas. The ALJ reasons, as the rate disparity between the base rate areas increases, the degree of inter- and intra-class subsidization necessary to mitigate the highest rates in the consolidation process increases, which decreases the cost-basis of the final rates.[31] The ALJ concludes, if the disparity is substantial, then base rate area consolidation is unlikely to

[30] Recommended Decision ¶ 294.

[31] Recommended Decision ¶ 296.

be in the public interest because of the resulting high degree of subsidization and thus deviation from the cost-based principle.[32] The ALJ finds Staff witness O'Neill persuasively argued that, because the degree of subsidization in Black Hills' proposed rates is high, it will cause ratepayers in high-cost areas to make economically inefficient choices regarding consumption and investment that will, in turn, place upward pressure on overall system costs.[33] The ALJ concludes that the subsidization in the Company's proposed rates will also increase the likelihood of over-collection of revenues, as the proposed rates in the legacy Aquila base rate area substantially exceed the cost of delivering service in that area and the highest anticipated growth is in that area.[34]

24. By denying the Company's proposed consolidation, the Recommended Decision leaves intact the three existing base rate areas of the legacy gas utilities now operated by Black Hills. The ALJ finds Black Hills has not satisfied its burden of establishing the proposed rates resulting from its Phase II analysis are just and reasonable. The ALJ therefore denies the remaining Phase II issues as well as the proposed base rate area consolidation. The Recommended Decision directs Black Hills to modify the existing base rates for the three existing areas through a separate GRSA for each area. The ALJ finds the rates resulting from application of GRSAs are just and reasonable, as they are based on existing rates with a proportional increase or decrease to implement the necessary change in revenue requirement.[35] The Recommended Decision orders Black Hills to: (a) implement a GRSA to adjust current base

[32] Recommended Decision ¶ 296.

[33] Recommended Decision ¶ 297 (citing Hrg. Exh. 408 (O'Neill Answer) 32:3-18); *see also* Recommended Decision ¶ 280 (reviewing Staff testimony that the wrong price signals cause ratepayers in high-cost areas to over-consume and may prevent ratepayers from switching to a less costly fuel source that would reduce the overall system cost).

[34] Recommended Decision ¶ 297.

[35] Recommended Decision ¶ 310.

rates proportionally for each existing base rate area; and (b) file a Phase II rate case within six months of a final decision in this Proceeding.

a. Black Hills Exceptions

25. In its exceptions, Black Hills explains that it seeks base rate area consolidation as a "critical first step to establishing one set of statewide rates for each customer class going forward based on a single statewide revenue requirement and single statewide CCOSS."[36] Black Hills states that its field operations, management, system planning, design, engineering, gas supply, communications, and customer service are all integrated and performed system-wide. Black Hills argues the reliability and quality of its service are essentially the same for all customers. And Black Hills contends all customers benefit from the greater pooling of costs and revenues and allocation of these costs and revenues over a greater customer base.

26. Black Hills objects that the Recommended Decision and intervenors' arguments assume that comparing the actual costs to serve customers within the three existing base areas is a "valid starting point."[37] Black Hills calls the current base rate areas a "historical artifact" and argues they do not reflect a "rational division of the system along geographical lines."[38] Black Hills claims the existing legacy Aquila base rate area resulted from the consolidation of three base rate areas in 1993 and the existing legacy SourceGas base rate areas was the result of a previous consolidation. Black Hills suggests this Proceeding is opportunity for the Commission to continue this progress. Black Hills admits it is "more costly from an investment standpoint to connect communities to supply sources in mountainous areas and in rural areas than in urban locations" but contends the "significant differences" in investments per customer among the

[36] Black Hills Exceptions p. 9.
[37] Black Hills Exceptions p. 13.
[38] Black Hills Exceptions p. 13.

three base rate areas are "simply a reflection of the Company's investment in pipeline infrastructure located upstream of the dedicated mains, services and meters necessary to connect an individual customer to the Company's system."[39] Black Hills concludes that "perpetuating historically developed boundaries…provides no public policy advantage or greater customer benefits than the Company's proposed consolidation."[40]

27. Black Hills challenges the reliance in the Recommended Decision on factors discussed in past Commission consolidation decisions. Black Hills contends these factors were merely recited or referred to in prior decisions and are "clearly not dispositive of the matter."[41] The Company disputes the finding in the Recommended Decision that it is "undisputed" none of these factors support the base rate area consolidation as well as the relevance of these factors.[42] Black Hills concedes it is unlikely its non-continuous systems will become physically connected, but argues that, from an operational standpoint, its physical systems are integrated and operated as part of a single entity. Black Hills concedes it has already achieved most efficiencies from integrating statewide operations and functions but claims further administrative efficiencies can still be gained from having one utility and few base rate and GCA areas. And as to rate disparities, Black Hills concedes rate disparities exist, but argues its proposed mitigated rates are just and reasonable.

28. Black Hills contends the Recommended Decision contains no findings that maintaining the existing base rate areas and determining revenue requirements based on the separate revenue requirements for those separate areas is just and reasonable. Black Hills claims

[39] Black Hills Exceptions p. 13-14.
[40] Black Hills Exceptions p. 15.
[41] Black Hills Exceptions p. 15.
[42] Black Hills Exceptions p. 15-16 (citing Recommended Decision ¶ 300).

that, although multiple CCOSSs were submitted that calculate rates based on both a statewide revenue requirement and separate revenue requirements for the three base rate areas, the ALJ made no determination on which CCOSS should be adopted. The Company reasons the Recommended Decision thus fails to establish the GRSAs will yield just and reasonable rates.

29. Black Hills claims the ALJ erred by applying a "conclusive evidence" standard when finding insufficient evidence to support the consolidation. Black Hills cites the ALJ's statement "finding the record evidence inconclusive" to support consolidation.[43]

30. Black Hills also challenges the ALJ's statement that the Company's decision not to file separate RRSs and CCOSSs for each of the base rate areas was a "flaw" in the Company's case.[44] Black Hills challenges whether it was the utility's burden to present alternatives to its rate proposals as part of its burden of going forward. Black Hills argues that, while Staff and the OCC criticized the Company's proposed rates, both parties failed to provide sufficient evidence supporting any alternative. Black Hills contends the ALJ erred in deeming the Company's failure to provide such information a "flawed approach" and this improperly influenced his finding that the Company failed to meet its burden of proof.

31. Finally, Black Hills claims the Recommended Decision improperly relied on the "no net harm" standard that was applied by the Commission when approving the SourceGas acquisition.[45] Black Hills argues that, although it would not be in position to propose base rate area consolidation and other rate initiatives but for the acquisition of SourceGas, these proposals are not the "'result of Black Hills' acquisition of SourceGas,'" as "incorrectly assumed" by the

[43] Black Hills Exceptions p. 4

[44] Black Hills Exceptions p. 18 (citing Recommended Decision ¶ 8).

[45] Black Hills Exceptions p. 28 (quoting ALJ's statement it is difficult to conclude ratepayers will suffer no net harm as a result of the acquisition particularly when the proposed base rate area consolidation would result in certain rate areas paying some of another rate area's costs).

ALJ in his analysis.[46] Black Hills contends the no net harm standard applied to the SourceGas acquisition in Proceeding No. 15A-0667G was based on the direct impacts of the specific acquisition transactions and did not, and could not, encompass all potential impacts of future rate cases. Black Hills objects that its proposals in this Proceeding do not create opportunity to "reassess" the no net harm standard applied in approving the acquisition.[47]

b. Staff Response to Black Hills Exceptions

32. In response to Black Hills' exceptions, Staff urges the Commission to affirm the Recommended Decision's denial of the base rate area consolidation. Staff argues that Black Hills bears the burden of proof to show and persuade the Commission that consolidation is in the public interest. Staff contends the Company has yet to provide persuasive evidence that the proposed consolidation would satisfy any of the previous factors discussed by the Commission in consolidation decisions and that Black Hills failed to present any of its own different factors in support of consolidation.

33. Staff challenges Black Hills' assertion in its exceptions that "[a]ll customers will benefit from the greater pooling of costs and revenues and allocation of these costs and revenues over a greater customer base provided by a single statewide revenue requirement study[.]"[48] Staff responds that this statement "defies math and logic" because summing the same total dollars and spreading them among the same number of customers creates winners and losers, but is hardly a benefit to all.[49] Staff states that, if all customers were to benefit, then the total cost to serve and thus the total rates paid by customers would decrease under consolidation.

[46] Black Hills Exceptions p. 28 (quoting Recommended Decision ¶ 327).
[47] Black Hills Exceptions p. 28.
[48] Staff Response to Exceptions p. 26 (citing Black Hills Exceptions p. 10).
[49] Staff Response to Exceptions p. 26.

34. Staff cautions that granting the proposed consolidation would depart from the generally accepted ratemaking principle of causation and send inaccurate price signals. Staff contends such departure would "repudiate the Commission's responsibility to consider all customer classes, not just residential customers."[50] Staff contends the significant existing rate disparity between the base rate areas echoes the disparity in the average cost of service in these different areas.[51] And Staff adds that the heavy rate mitigation Black Hills proposes is further evidence of significant cost disparities between the existing base rate areas.

35. Staff also argues that record evidence supports the conclusion that Black Hills' proposed base rate area consolidation is part of Black Hills Corporations' multi-state strategic plan and is not necessarily motivated by any specific or meaningful benefit to Colorado ratepayers. Staff argues that any purported benefit to customers would be ancillary to this plan.

36. Staff disputes the Company's claim that the ALJ applied a "conclusive evidence standard" in denying the proposed consolidation. Staff points to the introductory paragraphs in the Recommended Decision describing the standard of proof to be applied and the ALJ's analytic approach when reviewing the evidence that parties offered into the record.[52]

37. Finally, Staff argues the Recommended Decision provides a path to new rates that are just, reasonable, and in the public interest through GRSAs applied to existing base rates. According to Staff, Black Hills does not explain why a GRSA applied to the Company's underlying rate design for its existing utility services for each rate area is inappropriate or otherwise compromises the public interest. Staff argues that GRSAs are a common tool for

[50] Staff Response to Exceptions p. 28.

[51] Staff Response to Exceptions p. 29. Staff calculates the total revenue requirement for the average BHGD customer is 60 percent higher than the cost to serve the average BHGU customer (citing Hrg. Exh. 401 (O'Neill Answer) 21:14-22:4).

[52] Staff Response to Exceptions p. 18-19 (citing Recommended Decision ¶¶ 73-75; 301).

setting rates in Phase I-only rate cases and that GRSAs are "the one path the ALJ had left after denying Phase II."[53]

c. OCC Response to Black Hills Exceptions

38. The OCC opposes Black Hills' exceptions. The OCC argues the record supports the Recommended Decision's finding that the Company failed to meet its burden to demonstrate the proposed consolidation is in the public interest. The OCC concludes that the finding that the Company failed to carry its evidentiary burden of proof moots contemplation by the Commission of any policy considerations related to consolidation.

d. BGVA Exceptions

39. In its exceptions, BGVA contends that no rate increase via a GRSA rider should be granted pending the outcome of the separate Phase II rate case to be filed after this Proceeding. BGVA objects that the GRSA cannot be presumed to be just and reasonable. BGVA submits that, in the alternative, no rate increase should be allowed in any rate area that initially was given notice of a rate decrease and the Company should absorb any shortfall.

e. EOC Exceptions

40. EOC joins with Black Hills in asking the Commission to reverse the Recommended Decision and approve the base rate area consolidation. EOC contends the proposed consolidation is based on sound policy considerations. EOC argues that consolidation of the base rate areas will "reduce the significant rate shock that is occurring and will continue to occur in the rural, poorer, and less populated areas of the state, and allow the urban, wealthier, and more highly populated centers to absorb some of that shock."[54] EOC presents bill impact

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[53] Staff's Response to Exceptions p. 24.

[54] EOC Exceptions p. 13.

scenarios for the legacy SourceGas rate area BHGD Rate Area 2 and suggests that consolidation of the base rate areas results in a "more manageable" increase.[55] EOC cautions that rate increases for the rural, poor region comprising BHGD Rate Area 2 will have a profound impact. EOC states this area has a lower median household income than the other two base rate areas, a lower median household income than the state as a whole, and 21.5 percent of the population is in poverty compared to 13.1 percent statewide, 7.9 percent in the legacy Aquila rate area, and 10.4 percent in the other legacy SourceGas rate area.[56] EOC argues there are more benefits if costs are spread over a larger number of customers than leaving a smaller number of customers to bear the cost of significant expenditures. EOC cites the Company's testimony that consolidation will benefit customers "'through economies of scale and maximizing the customer base among which the Company's cost of service will be spread in the future.'"[57]

41. Like Black Hills, EOC claims the Recommended Decision overly-relies on the factors discussed in prior Commission decisions. EOC contends the Recommended Decision fails to consider the Company's policy arguments. EOC concludes that denying the consolidation proposal will result in unjust and unreasonable rates now, and more significantly over the next five years.

42. EOC also objects to the GRSAs. EOC asks the Commission to establish a new statewide residential customer charge of $12.25 per month as agreed to in the Partial Stipulation and Settlement among Black Hills, Staff, and EOC. EOC claims the ALJ's GRSA decision amounts to requiring re-litigation of an unopposed settled issue. EOC asserts this "absurd result"

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[55] EOC Exceptions p. 14 (citing Hrg. Exh. 408 (O'Neill Answer) Table ETO-5 "Percentage Bill Impact Based on Staff's Revenue Requirement").

[56] EOC Exceptions p. 15 (citing Hrg. Exh. 401 (O'Neill Answer) Table ETO-3 "Demographic Comparison of Existing Rate Areas"; Oct. 24, 2019 Hrg. Trans. 169:8-170:3).

[57] EOC Exceptions p. 15 (citing Hrg. Exh. 104 (Stoffel Direct) p. 22).

must be overturned.[58] EOC repeats its position that high fixed monthly customer charges for residential customers "is bad policy because it hits low-income customers the hardest and disincentivizes energy efficiency investments."[59] EOC claims the ALJ ignored this argument and the record supporting the residential customer charge in the Partial Stipulation and Settlement.

43. Finally, EOC requests, if the Commission maintains the requirement for GRSAs, the GRSAs should be applied asymmetrically to only the energy components of the existing base rates, that is, without modifying the existing monthly customer charges.

f. Staff Response to EOC Exceptions

44. In response to EOC's exceptions, Staff challenges that EOC advocates for base rate area consolidation only because the Company presents consolidation as providing the greatest opportunity for intra-class cost subsidization and inter-class cost subsidization for residential customers through rate mitigation. Staff argues that EOC's position is neither good ratemaking nor a reasonable justification for the consolidation. Staff cautions that adopting the Company's proposed ratemaking would require the Commission to "abandon cost-causation as a foundational principle of ratemaking" and place residential customer considerations above all others.[60]

g. Findings and Conclusions

45. We deny Black Hills' exceptions requesting that the Commission approve the Company's proposed base rate area consolidation. We uphold the Recommended Decision's finding that Black Hills failed to meet its burden of proof. Black Hills put forward a case that not only dismisses the tenets of cost-of-service ratemaking but redefines the public interest

[58] EOC Exceptions p. 6.
[59] EOC Exceptions p. 11.
[60] Staff Response to Exceptions p. 33.

entirely within its own judgment about reasonable bill impacts. Although we recognize the Company's argument and EOC's advocacy that the proposed consolidation would provide relief from significant rate shock for customers in the legacy SourceGas rate area BHGD Rate Area 2, we find the record lacks the argument and evidence that we would need in order to find this proposal results in just and reasonable rates and is in the public interest. The Company has shown its proposal would benefit customers in areas otherwise facing significant rate increases but has failed to make a persuasive case why spreading costs to customers in other areas to reduce those bill impacts results in just and reasonable rates or is in the public interest. We find unavailing the Company's conclusory argument that "[a]ll customers will benefit from the greater pooling of costs and revenues and allocation of these costs and revenues over a greater customer base."[61] We agree with Staff that spreading costs among a greater number customers is not necessarily a benefit to all of those customers.[62] We will not depart from the accepted ratemaking principle of cost causation and approve the level of subsidization proposed by the Company on the record put forth by the Company in this Proceeding. We therefore uphold the Recommended Decision's determination to deny Black Hills' consolidation proposal.

46. As an initial matter, we find it justified in these circumstances for the Commission to start with the presumption that the existing base rate areas result in just and reasonable rates. Although these are "historically developed boundaries" as Black Hills criticizes,[63] the fact remains there are significant existing rate disparities among these areas, some of which relate directly to geographical and other differences. At hearing, Black Hills witness Stoffel stated he was "not sure it's surprising" that the average investment to serve a legacy SourceGas customer

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[61] Black Hills Exceptions p. 10.

[62] Staff Response to Exceptions p. 26.

[63] Black Hills Exceptions p. 15.

is more than double the average investment to serve a legacy Aquila customer and he thought "it's accurate."[64] He explained: "If you look at the difference of the systems, and where they are located, and the pit facilities and terrain and extensions, and all of those things … I think that it shows that, the kind of investments, and the relative number of customers, and, so, that results in these differences."[65] Black Hills admits that substantial mitigation is needed to implement its consolidated rates across the existing base rate areas, and that the mitigated rates would as a result not be cost-based.

47. We agree with the Recommended Decision that Black Hills failed to make a sufficient case for why it is just and reasonable and in the public interest for significant costs incurred in one area to be spread to customers in another area, particularly since the Company concedes there exist real differences among the systems serving those customers. Black Hills argues that its proposal is more consistent with the public interest than the current rate structure because the costs of system and future projects will be more evenly spread throughout the Company's geographical footprint.[66] However, we find it appropriate in this case and most rate cases for the Commission to start with the *status quo* and then weigh the pros and cons of any proposed departure. The existing base rate areas and rate structures result from past Commission decisions. If Black Hills had valid concern that the rates in the existing areas are unjust and reasonable and had to be replaced with the move to consolidated rates, Black Hills could have explained why that departure was necessary. Instead, the Company postured its case more as a logical next step following its acquisitions of the legacy utilities. Black Hills urges that

[64] August 5, 2019 Hrg. Trans. (Stoffel) 206:17-23.
[65] August 5, 2019 Hrg. Trans. (Stoffel) 206:22-207:5.
[66] Hrg. Exh. 121 (Stoffel Rebuttal) 12:19-23.

statewide rates will reduce administrative costs and be consistent with the way the Company now operates as a single entity.[67]

48. We find no merit to Black Hills' claim that the ALJ erroneously applied a "conclusive evidence standard." The ALJ's statement that there "are compelling arguments both in favor of, and against, consolidation"[68] does not override the ALJ's thorough articulation at the outset of the decision of the standard of review.[69]

49. We also find no merit to Black Hills' suggestion that the Recommended Decision improperly treats as dispositive factors discussed in prior Commission consolidation decisions. The ALJ only finds these factors "weigh heavily" against granting the consolidation.[70] He recognizes the Commission's past decisions have not all cited or discussed these three factors, which he attributes to the fact these decisions addressed settlements within a larger rate case.[71] Likewise, Staff witness O'Neill clarified at hearing that, although Staff's testimony focused on these factors, use of these factors is "guidance" but not "a requirement incumbent on the Commission,"[72] and past discussions of these factors has always been in the context of settlement.[73] She also explained Staff did not apply these factors only because they had been used previously but also because they were "reasonable and logical" and Staff wanted to see their impact.[74] We agree these factors are relevant, albeit not dispositive, considerations and find the

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[67] Hrg. Exh. 104 (Stoffel Direct) 26:22-27:4.

[68] Recommended Decision ¶ 292.

[69] *See* Recommended Decision ¶ 73 ("The party bearing the burden must prove its case by a preponderance of the evidence."); *Id.* ("This standard requires that evidence of the existence of a contested fact outweighs the evidence to the contrary.").

[70] Recommended Decision ¶ 294.

[71] Recommended Decision ¶ 298.

[72] August 9, 2019 Hrg. Trans. (O'Neill) 103:5-7.

[73] August 9, 2019 Hrg. Trans. (O'Neill) 103:5-10.

[74] August 9, 2019 Hrg. Trans. (O'Neill) 243:24-244:2.

Recommended Decision properly concluded these factors weigh heavily against granting the Company's proposed consolidation.

50. We reject Black Hills' claim that it is not the utility's burden to present alternatives to its own rate proposals. The issue in this Proceeding was the lack of record evidence showing how the Company's proposed consolidation compared to the *status quo*. As Staff witness O'Neill explained at hearing, the Company "boxed" the Commission into only one option by focusing on its own proposals and resisting providing comparative CCOSSs for the existing rate base areas.[75] This was a strategic risk by the Company as it was always possible the Commission would not accept the Company's proposal and would instead consider an approach proposed by another party or one crafted by the Commission. We find Black Hills' all-in approach presenting one comprehensive proposal was indeed flawed. While it is not the utility's burden to present alternatives to its proposals, it is the utility's burden to provide sufficient evidence supporting its proposals.

51. We also reject the Company's protest that the "no net harm" considered in approving Black Hills' acquisition of SourceGas is no longer relevant. In the decision approving the SourceGas acquisition in Proceeding No. 15A-0667G, the Commission required that the settling parties show the proposed merger will result in no net harm to customers, while balancing ratepayer and utility interests.[76] Here, Black Hills' proposed consolidation of the three base rate areas would spread costs among all of its customers despite the undisputed substantial rate disparity between the existing rate areas. In this first rate case following the Company's acquisition of SourceGas, we conclude it is proper to require Black Hills to show why higher

[75] August 9, 2019 Hrg. Trans. (O'Neill) 113:15-17.

[76] Proceeding No. 15A-0667G, Decision No. R16-0058 (issued January 22, 2016).

costs from legacy SourceGas areas should be spread across all of Black Hills' customers despite the Commission's approval of the acquisition relying on a finding of no net harm to the Company's ratepayers.

52. For these reasons, we uphold the Recommended Decision's rejection of base rate area consolidation. Black Hills had ample opportunity to make its case supporting the proposed consolidation of the three base rate areas, relying on the factors discussed in previous Commission consolidation decisions or proffering additional or alternative justifications. The Recommended Decision reviews in detail Black Hills' arguments in favor of consolidation[77] but ultimately finds the Company failed to establish that its proposal is in the public interest. We agree and uphold the finding in the Recommended Decision that the Company's proffered justifications and evidence is unpersuasive, particularly when we consider the rate disparity concerns.

53. We agree with the ALJ that the record is insufficient to establish new rate designs as is commonly achieved in a Phase II rate case. We therefore uphold the Recommended Decision's directive for the Company to implement GRSAs to adjust the current base rates proportionally for each existing base rate area and to file a Phase II rate case within six months of a final decision in this Proceeding. We conclude that the RRSs produced for each of the three existing base rate areas are sufficient to calculate GRSAs. We find the separate GRSAs calculated for application to the existing base rates for each separate base rate area are adequately supported by the record and result in just and reasonable rates. The ALJ reached these same conclusions.[78] We further agree with the ALJ that a Phase II rate case remains

[77] Recommended Decision ¶¶ 272-277.

[78] *See* Recommended Decision ¶ 310 ("The rates resulting from the application of a GRSA are found to be just and reasonable, as they are based on existing rates with a proportional increase or decrease to implement the necessary change in revenue requirements.").

necessary. We therefore uphold the directive in the Recommended Decision that Black Hills file a Phase II rate case within six months of a final Commission decision in this Proceeding.

6. Distribution System Integrity Rider

54. The Recommended Decision denies Black Hills' proposal to implement a DSIR to recover costs of projects in the Company's system integrity programs that accelerate the replacement of higher-risk pipe and improve system data.

55. In Advice Letter No. 1, Black Hills proposed a DSIR with an initial term of four years, effective January 1, 2020, for approved DSIR projects completed in years 2019 through 2023. Through the DSIR, Black Hills would recover the cumulative approved costs of projects completed through 2023, or until the next rate review, when DSIR costs could be rolled into base rates. Black Hills proposed that projects to be pursued and their costs would be filed in a report each November 1. Black Hills would then meet with Staff and the OCC three times a year to discuss projects for that year, any updates, and projects for the next year. Black Hills would provide a report by April 1 detailing the costs incurred the previous year and providing opportunity for interested parties to challenge any of the projects or costs.

56. As discussed in the Recommended Decision, Black Hills anticipates spending \$118 million on DSIR projects through 2023.[79] Of that, \$69.7 million would be spent on projects in the legacy SourceGas rate area BHGD Rate Area 2 including yard line and at-risk meter relocation projects. The Recommended Decision calculates this represents almost 60 percent of the total DSIR spending.[80] The Recommended Decision further calculates that, given this

[79] Recommended Decision ¶ 315.

[80] Recommended Decision ¶ 315 (citing Hrg. Exh. 134 (Gillen Rebuttal) 43:10-44:2 and Table EJG-16 "2019-2023 DSIR Capital Spend by Base Rate Area").

service area has approximately 23,000 ratepayers, Black Hills proposes to spend $3,000 per ratepayer in BHGD Rate Area 2, which would double the rate base in that area.[81]

57. The Recommended Decision notes that Black Hills states it could take over 100 years to mitigate these risks if the replacement programs are not accelerated, but the Company stated at hearing that it would accelerate the replacement of high-risk facilities even if its DSIR program is denied in this Proceeding.[82]

58. The Recommended Decision cites three areas of deficiency that led to denial of the Company's proposal. First, that the Company did not provide adequate evidence to demonstrate all the proposed projects warrant extraordinary DSIR treatment and did not provide a plan to terminate this extraordinary DSIR treatment and resume cost recovery under the ordinary course of business, consistent with recent requirements for Public Service. Second, that the Company did not provide adequate information to justify its proposal to double the rate base in the legacy SourceGas rate area BHGD Rate Area 2, which only has approximately 23,000 ratepayers. Similarly, that the Company did not adequately explain why it is in the public interest for ratepayers to bear 100 percent of these significant costs ($69.7 million) resulting from the acquisition of SourceGas, when Black Hills stated when seeking approval of the acquisition in Proceeding No. 15A-0667G, that the acquisition would cause no net harm to its ratepayers. And third, that the record does not contain any analysis of alternatives to DSIR investments to reduce or eliminate the anticipated costs in BHGD Rate Area 2. The Recommended Decision concludes that, given the proposed doubling of rate base in five years, all possible alternatives should be thoroughly explored before making these investments.

[81] Recommended Decision ¶ 315 (citing Hrg. Exh. 134 (Gillen Rebuttal) 46:6-13; Oct. 24, 2019 Hrg. Trans. 110:25-111:4).

[82] Recommended Decision ¶ 316 (citing August 7, 2019 Hrg. Trans. (Lewis) 141:15-142:13).

59. The Recommended Decision requires Black Hills to re-file its DSIR proposal within six months of a final decision in this Proceeding and, in that new filing, address the concerns identified in the Recommended Decision.

a. Black Hills Exceptions

60. In its exceptions, Black Hills requests that the Commission reverse the ALJ's determination and approve the DSIR. The Company claims that it provided significant evidence demonstrating the DSIR is in accordance with federal and state pipeline safety regulations and is consistent with similar integrity infrastructure riders approved for other Colorado gas utilities. The Company argues that the concerns raised in the Recommended Decision may justify adoption of limitations on what may be recovered through the DSIR, or design modifications, but do not warrant wholesale rejection of the proposal.[83]

61. Black Hills argues that its proposed statewide DSIR is intended to avoid exacerbating rate disparities that were driven by historic investment patterns. Black Hills reasons that the ALJ's concern with the economic impact of the planned DSIR projects on customers in the legacy SourceGas rate area BHGD Rate Area 2 "simply highlights the need for the Commission to resolve the consolidation issues in this proceeding."[84]

62. Black Hills argues that, because of regulatory lag, the Company will likely suffer a shortfall in revenues without a mechanism to allow for timely cost recovery. Black Hills objects that traditional base rate recovery of the significant costs of these initiatives would be delayed as a result of regulatory lag and would require expensive annual rate case filings.

[83] Black Hills Exceptions pp. 4-7.

[84] Black Hills Exceptions pp. 5, 14.

63. More immediate, Black Hills objects that denial of the DSIR in this Proceeding denies the Company an opportunity to recover in 2020 its $8.7 million investment in Distribution Integrity Management Program (DIMP) projects undertaken in 2019. The Company states this amounts to disallowance in this Proceeding. Black Hills argues that its proposed DSIR removes much of the negative incentive related to cost recovery of these initiatives and accommodates the variability in the level of investment the Company expects year-to-year as it evaluates the condition of its pipelines in the ground. Black Hills argues its customers "will obviously benefit from the improvement in the long-term safety and reliability of the gas system" resulting from these efforts and concludes the DSIR is the "most efficient mechanism" to provide for recovery of the highly variable costs.[85]

64. Black Hills argues that it has developed a detailed approach to ranking and prioritizing projects.[86] Black Hills adds that it proposes a true-up mechanism to ensure against over-recovery of costs and an annual 2.5 percent cap and is limited to in-kind replacement of facilities. The Company states its proposal also includes several opportunities for Staff and the OCC to raise any concerns.

65. Black Hills argues that the ALJ's reference to requirements imposed in Public Service's 2015 gas rate case is not dispositive.[87] Black Hills argues that, unlike this Proceeding, Public Service was seeking an extension of its established Pipeline Safety and Integrity Adjustment (PSIA) rider and the Commission granted the extension for three years, provided adequate steps were taken to control the scope of the PSIA. Black Hills objects that the

[85] Black Hills Exceptions p. 23.

[86] Black Hills Exceptions p. 25 (citing Hrg. Exh. 106 (Koca Direct) 34:11-39:7; Hrg. Exh. 107 (Lewis Direct) 23:7-23.)

[87] Black Hills Exceptions p. 26 (referring to Proceeding No. 15AL-0135G).

Recommended Decision denies its proposed DSIR rather than grant the request with conditions to control the scope.

66. Black Hills also argues that, in determining to deny the DSIR, the ALJ improperly reassessed the "no net harm" standard applied by the Commission in the SourceGas acquisition Proceeding No. 15A-0667G. Black Hills contends the factual issues raised in this and future rate cases relevant to establishing just and reasonable rates should not be used to continually reassess the no net harm standard applicable to the acquisition. Black Hills also argues the integrity program costs at issue are not a "result of" its acquisition of SourceGas because the investments would have had to been made regardless of whether Black Hills acquired the system.[88]

67. Finally, the Company contests the requirement that the Company must analyze alternatives to DSIR investment. Black Hills claims the Recommended Decision "stresses the Company study potential changes in the law and whether customers are considering leaving a particular area of Colorado."[89] Black Hills objects that these alternative analyses were not required of other utilities in approving their safety and integrity riders and further no party raised this issue. Black Hills claims it is "wholly inappropriate" to require it to "analyze potential future laws to determine whether to undertake safety projects."[90]

b. Staff Response to Black Hills Exceptions

68. In response to Black Hills' exceptions, Staff states that although it had not advocated for rejection of the DSIR, the requirement for the Company to file a new DSIR advice letter within six months accomplishes Staff's objectives and gives the Company a "valuable opportunity" to incorporate the lessons learned from this Proceeding and achieve a "workable

[88] Black Hills Exceptions pp. 26-27.
[89] Black Hills Exceptions p. 31.
[90] Black Hills Exceptions p. 31.

integrity rider."[91] Staff cautions that an integrity rider "must never constitute a blank check from ratepayers."[92] Staff agrees with the Recommended Decision that the record was not adequately developed on the necessity of the proposed DSIR projects, the impact on ratepayers, alternate method of paying for these projects, and alternatives to the DSIR.

69. Staff disputes the Company's claim that the Recommended Decision disallows the 2019 DIMP costs. Staff states while it is true that rejection of the DSIR in this Proceeding prevents the Company from recovering its 2019 DIMP project costs via the proposed DSIR, that is different from "disallowing" this recovery by deeming the costs "imprudently incurred."[93] Staff states the Company still has an opportunity to recover the projected $8.7 million project costs in its next rate case or through approval of the new integrity rider that Black Hills must file.

70. Staff also requests that the Commission clarify that the required DSIR filing must be separate from the certificate of public convenience and necessity (CPCN) proceeding agreed to by the Company to seek recovery for yard line, farm tap, and at-risk meter replacement, an expected $200 million capital expenditure. Staff reasons a separate proceeding for this issue will allow for an examination of whether Black Hills should fund this project via an integrity rider, through the course of ordinary business, or via some other mechanism.

c. OCC Exceptions and Response to Black Hills Exceptions

71. The OCC opposes Black Hills' exceptions and agrees the deficiencies in the record did not allow for the Commission to find and conclude the DSIR would yield just and reasonable rates or be in the public interest. The OCC further requests that the Commission reject the ALJ's requirement that the Company file for approval of a DSIR within six months.

[91] Staff Response to Exceptions p. 39.

[92] Staff Response to Exceptions p. 40.

[93] Staff Response to Exceptions p. 42.

The OCC argues that use of a DSIR results in extraordinary treatment of current recovery of costs for approved projects. The OCC concludes the Company is currently operating its system in compliance with federal and state regulations and this activity is being conducted in the normal course of business and without a DSIR. The OCC contends the work the Company proposes to accelerate, and cost recovery through the DSIR, should be performed in the ordinary or normal course of business and recovery of associated costs determined in future rate cases.

d. BGVA Exceptions

72. In its exceptions, BGVA supports requiring Black Hills to file a new advice letter to address DSIR issues. BGVA also asks the Commission to ensure the treatment of synergy savings is addressed separately from the resolution of the issues surrounding the proposed DSIR.

e. EOC Exceptions

73. In its exceptions, EOC argues that deferring the DSIR proposal as well as other Phase II issues to future proceedings wastes resources for ratepayers, the State, and the parties.

f. Findings and Conclusions

(1) *Denial of DSIR*

74. We deny Black Hills' exceptions requesting that the Commission approve the proposed DSIR. We uphold the finding in the Recommended Decision that Black Hills has not met its burden to prove that the proposed DSIR is in the public interest.

75. Our most significant concern with the DSIR is the magnitude of the investment in the legacy SourceGas rate area BHGD Rate Area 2. As the Recommended Decision outlines, Black Hills anticipates spending 60 percent of the total DSIR spending in this area, doubling rate base and spending \$3,000 for each of its 23,000 ratepayers.[94] Yet this extreme level of

[94] Recommended Decision ¶ 315.

investment is supported only with summary-level information. Rather than provide detailed information so the Commission and parties could fully understand the issues in BHGD Rate Area 2, the Company proposed to subsidize these costs through base rate area consolidation. Black Hills has not shown why the Commission should approve its proposal to address this extreme level of investment in a single rate base area through requiring other ratepayers to subsidize these massive costs while the Company receives expedited recovery of its costs as well as a return on the associated investments. Black Hills continues this approach in its exceptions by stating it is not seeking approval of individual projects or rates but rather approval of the general DSIR mechanism.[95] However, we will not approve the DSIR without full information so that we can evaluate the entire impact. Each year's individual projects indicate only a fraction of the total impact. And it will not be possible to consider alternatives to the overall doubling of rate base under the piecemeal analysis of annual project filings. Without more information from the Company, we remain concerned that the proposal to subsidize these massive costs through statewide rate consolidation simply masks the issues in BHGD Rate Area 2 and potentially exacerbates the underlying problems.

76. We find unavailing Black Hills' claim that we should approve the DSIR because the Commission has approved integrity management programs for other utilities. None of these other utility's programs included the extreme level of investment proposed by Black Hills to double the rate base in an area with 23,000 ratepayers within five years.

77. We find no merit to Black Hills' assertion that the Recommended Decision erred in finding that a bill impact analysis including the DSIR for BHGD Rate Area 2 or other existing base rate areas was not provided before hearing and that the financial impact on these customers

[95] Black Hills Exceptions p. 23.

did not become clear until the supplemental post-hearing proceedings. The Company's acquiescence only late in the Proceeding to provide detailed class cost of service information for the existing base rate areas resulted in an inappropriately splintered proceeding that did not provide a reasonable opportunity for parties to consider, investigate, and rebut the information finally provided by the Company.

78. Finally, despite Black Hills' protests, the "no net harm" standard from our approval of the SourceGas acquisition in Proceeding No. 15A-0667G remains relevant in this rate case, as discussed elsewhere in this Decision. In approving the acquisition, the Commission required the settling parties show the proposed merger will result in no net harm to customers, while balancing ratepayer and utility interests.[96] Yet Black Hills' proposal in this Proceeding would spread the costs for massive DSIR investments in BHDG Rate Area 2 to all customers. By Black Hills' own calculations, if the DSIR were approved and the existing base rate areas not consolidated, the ratepayers in BHGD Rate Area 2 would suffer a significant increase in their bills from 2020 to 2023.[97] In this first rate case following Black Hills' acquisition of SourceGas, we find it appropriate to require Black Hills to show why the costs of investments made in a legacy SourceGas rate area should be spread to all customers despite the Commission's approval of the acquisition relying on the finding of no net harm to the Company's ratepayers.

(2) *Requirement to Investigate Alternatives to DSIR Investments*

79. We deny Black Hills' exceptions requesting that the Commission rescind the requirement for the Company to investigate and present alternatives to DSIR investments.

[96] Proceeding No. 15A-0667G, Decision No. R16-0058 (issued January 22, 2016).
[97] Recommended Decision ¶ 274.

80. We disagree with Black Hills' proposed approach for the Commission to approve the DSIR mechanism in this Proceeding and then for the Company, parties, and the Commission to later examine individual projects in future annual filings. We agree with the ALJ that the record does not contain any analysis of alternatives to the proposed DSIR investments that would reduce or eliminate the anticipated costs put forward by Black Hills in this Proceeding, particularly in BHDG Rate Area 2. Given the expected doubling of rate base in that rate area in five years, all possible alternatives should be thoroughly explored before taking steps to implement DSIR-related investments.

81. We find unavailing Black Hills' objection that the Recommended Decision requires the Company to "analyze potential future laws."[98] Although the Recommended Decision refers to § 40-3.2-106(6)(a), C.R.S., a relatively new law effective May 2019, this is simply to provide a definition for the concept of "beneficial electrification," one of the many alternatives identified by the ALJ to be explored before making DSIR investments. The cited statute does not apply to the Company; it requires electric utilities to include in resource plans, certain conversions of customers from a nonelectric source to an electric source. But the definition codifies how the Commission has previously described the concept of beneficial electrification in past proceedings.[99] We agree it is appropriate for Black Hills to investigate whether it would be feasible to convert certain gas service customers to another energy source, including electric service or other available fuels, if it would be more cost effective than DSIR investments.

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[98] Black Hills Exceptions p. 31.

[99] *See, e.g.*, Proceeding No. 17I-0692E, Decision No. C17-0931 ¶ 9 (November 16, 2017) (describing beneficial electrification as powering appliances and machines that have traditionally run on fossil fuels and are instead electrified and explaining that electrifying transportation, water heating, and space heating may produce cost savings and air pollution reductions as well as improved grid management).

82. We also agree with the Recommended Decision that Black Hills did not provide adequate information about the level of subsidy of integrity projects *within* the legacy SourceGas rate area BHGD Rate Area 2[100] and that further analysis is necessary. For example, there may be certain customers or groups of customers served by piping or other facilities that require replacement that would be very expensive per-customer, and it may make sense to convert these customers to a different fuel or energy source so the highest cost DSIR investments can be avoided. And as Staff suggested in testimony, customers may switch to other fuels if they pay the full costs of their service.[101]

83. We also find unavailing the Company's objection that the Recommended Decision requires the Company to investigate whether customers are considering leaving a particular area. Instead, the Recommended Decision requires Black Hills to investigate potential attrition due to customers switching to other fuels as a result of the cost increases as Staff suggests. We find that overall system growth is relevant to future system capacity requirements and potential attrition due to cost increases. Therefore, we require the Company to include an assessment and projection of future system load growth as a part of its DSIR analysis. We do not expect the Company to analyze customer expectations of leaving a particular area, but we do require an assessment of future customer demand based on historic trends and based on potential customer attrition due to integrity project costs.

84. Finally, we find unpersuasive the Company's objection that the Commission did not require these alternative analyses when it approved integrity management programs for other utilities and that no party raised these alternative analysis requirements. None of the other

[100] Recommended Decision ¶ 328.

[101] Hrg. Exh. 408 (O'Neill Supplemental CCOSS Testimony) 32:7-11.

utility's programs included the extreme level of investment proposed by Black Hills to double the rate base in an area with 23,000 ratepayers within five years. These extreme circumstances require that the Company investigate all possible alternatives.

(3) *Requirement to File New DSIR Proposal*

85. We deny the OCC's exceptions requesting that the Commission rescind the requirement for the Company to file a new proposal for a DSIR. We disagree with the OCC's position that Black Hills should recover all integrity costs through the ordinary course of business without any opportunity for the Commission to consider an integrity rider. Although the OCC is correct the Company has operated without such a rider to date, and although the Company has not presented adequate information in this Proceeding to support its proposal, we find further consideration of a DSIR proposal is warranted. In particular, the magnitude of the Company's non-revenue-producing safety investments may warrant a future DSIR program in order to avoid the regulatory lag and expense of continued base rate filings. We set a filing date of six months of a final decision in this Proceeding in order to provide certainty to all parties.

(4) *Requirement to File DSIR Separate from CPCN*

86. We grant, in part, Staff's request to clarify that the required DSIR filing must be separate and apart from the CPCN proceeding agreed to by the Company to seek recovery for yard line, farm tap, and at-risk meter replacement. We note the agreement for the Company to file a CPCN application for these replacement projects assumed that the DSIR would be approved in this Proceeding and the yard line, farm tap, and at-risk meter replacement projects would require separate approval. Since the DSIR now requires separate approval also, it is not clear whether there is any degree of overlap between the two issues. We allow Black Hills the discretion to file for approval of the two issues separately or as a combined filing. However, we

require that, if Black Hills makes a combined filing, it must treat the replacement component as a stand-alone issue, providing all information necessary as if the separate CPCN filing was required.

7. Construction Allowances

87. The Recommended Decision rejects all proposals to modify the construction allowance put forward in this Proceeding by Black Hills and intervenors. The Recommended Decision finds Black Hills did not carry its burden in establishing that its proposed construction allowances are just and reasonable. The Recommended Decision also rejects proposals from other parties for adoption of one of several procedures currently used by one of Black Hills' affiliated companies. The Recommended Decision concludes the Company and the other parties failed to provide a thorough or robust analysis of whether the resulting construction allowances will result in just and reasonable rates, or whether subsidization will occur between existing and new customers. The Recommended Decision finds the existing construction allowances are likely out-of-date and therefore requires the Company to file for approval, in a new proceeding, revised construction allowance rates, terms, and conditions within nine months of a final decision in this Proceeding.

a. Black Hills Exceptions

88. In its exceptions, Black Hills argues that the record contains ample evidence to implement a construction allowance. Black Hills objects that the Recommended Decision orders the Company to file for approval of revised construction allowances in a new proceeding despite the parties largely agreeing in this Proceeding on a construction allowance methodology. Black Hills explains that, after considering the positions of intervenors, the Company largely accepted the recommendation of Staff and the OCC to continue using the construction allowance model of

legacy BHGU. Black Hills states the Recommended Decision needed only resolve one remaining issue among the Company, Staff, and the OCC, the depreciable life of the mains and service lines to be used in the calculation.

89. Black Hills disputes the finding in the Recommended Decision that there is insufficient evidence of whether the proposed construction allowances would result in a subsidy between existing and new customers. The Company responds that Black Hills' witness Hyatt explained at hearing how to evaluate whether the proposed construction allowance results in a subsidy and that Mr. Hyatt demonstrated a new customer would not subsidize existing customers or vice versa.[102] Black Hills contends its proposal balances the impact on existing customers of the increased rate base with future customers' contribution through new load and revenues to reflect the long-term value of new customers.[103]

90. Further, the Company asserts that the requirement to file a new Phase II rate case within six months and a construction allowance application within nine months is problematic. The Company explains that its construction allowance is based on an average of embedded costs of all services and main, as calculated in the CCOSS, which is filed for approval as part of the Phase II rate case.

b. EOC Exceptions

91. In its exceptions, EOC requests that the Commission adopt a construction allowance in this Proceeding rather than require Black Hills to make a separate filing. EOC recommends using the Company's cost of service model, tied to mains and service line investments only, but using a 30-year depreciable life as originally proposed by the Company.

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102 Black Hills Exceptions p. 36 (citing August 7, 2019 Hrg. Trans. (Hyatt) 57:15-58:5; 58:13-61:3).

103 Black Hills Exceptions p. 36 (citing Hrg. Exh. 134 (Gillen Rebuttal) 18:4-19:2; August 9, 2019 Hrg. Trans. (Haglund) 254:4-17).

EOC contends this methodology affords a reasonable allowance to new customers without unreasonably raising Black Hills' rate base and its customers' rates. In the alternative, EOC recommends, if the Commission is inclined to adopt separate construction allowances for separate base rate areas, then the initial proposals of Staff and the OCC would be appropriate.

c. Staff Response to Exceptions

92. Staff responds that the Recommended Decision correctly found Black Hills did not carry its burden in establishing its proposed construction allowances are just and reasonable, or whether they would result in a subsidy. Staff calls the requirement to make a new filing a "valuable opportunity" for the Company to produce a new filing following the "detailed roadmap" in the Recommended Decision.[104] Staff reasons that in that new proceeding the Commission, Black Hills, and intervenors will be able to address the important construction allowance issues "free from a record bursting at the seams with unrelated data and testimony" and without the time constraints of this Proceeding.[105]

d. OCC Response to Exceptions

93. The OCC agrees the record supports the Recommended Decision's denial of proposed changes to the Company's construction allowances. The OCC recommends upholding the requirement for the Company to make a separate filing proposing changes.

e. Findings and Conclusions

94. We deny the exceptions of Black Hills and EOC requesting approval of the Company's construction allowance proposals.

[104] Staff Response to Exceptions p. 44.
[105] Staff Response to Exceptions p. 44.

95. We agree with the Recommended Decision that Rule 4 CCR 723-4-4210(b)(IV) of the Commission's Rules Regulating Gas Utilities and Pipeline Operators, which requires the utility to "ameliorate the rate and service impact upon existing customers," generally requires the utility to address the potential subsidy between new and existing customers caused by setting the construction allowance too high (resulting in a subsidy of the connection of new customers) or too low (resulting in new customers' subsidization of existing customers). The objective of these allowances is thus to equitably balance the expected new revenue stream from the connection of new customers with the cost of that connection without resulting in a subsidy.

96. We agree with Staff and OCC as well as the Recommended Decision that Black Hills failed to provide adequate analysis and information to demonstrate that its proposed construction allowances will result in just and reasonable rates, or whether subsidization will occur between existing and new customers. At hearing, Black Hills witness Stoffel admitted there is nothing in the record of any analysis or calculation to compare the actual cost to connect customers versus the various proposed construction allowances.[106] Black Hills witness Sullivan likewise conceded the Company did not perform that analysis and he was not aware of anyone having that in the record.[107] We reject Black Hills' claim in exceptions that the data in Company witness Hyatt's Hearing Exhibit 132, Attachment DNH-22, provides the missing analysis. Mr. Hyatt testified at hearing that this attachment contains inputs into the construction allowance including the average use per customer for residential customers.[108] We agree with the Recommended Decision that more support is needed than the calculations and inputs in this attachment and Mr. Hyatt's conclusions at hearing.

[106] August 6, 2019 Hrg. Trans. (Stoffel) 59:7-17.
[107] August 7, 2019 Hrg. Trans. (Sullivan) 57:5-14.
[108] August 7, 2019 Hrg. Trans. (Hyatt) 60.

97. We will extend the construction allowance filing date to address the overlap between the new Phase II and construction allowance filings. We extend the construction allowance filing date to 30 days after a final Commission decision in the Phase II rate case ordered by this Decision.

8. Post-Base Period Capital Additions to Rate Base

98. The Recommended Decision disallows the Company's proposed inclusion in the rate base calculation of $35.3 million in post-base period capital additions and adjustments from July 1, 2018 through December 31, 2018. As described in the Recommended Decision, these additions include approximately $6.8 million to support increased system load due to population growth, $7.6 million for general plant additions, $2.8 million for reliability additions, and $18 million for pipeline replacement integrity additions.[109] The ALJ concludes these investments are "ordinary-course-of-business investments for ongoing gas operations" that do not merit a *pro forma* adjustment to cost of service.[110] The ALJ concludes that addition of these investments would be inconsistent with the matching principle "because, given their magnitude in aggregate, they would undermine the integrity of the interrelationship between revenues, expenses, and investments in the test year."[111] The ALJ further concludes Black Hills used different methods to calculate the rate base for the base period versus the post-base period, which added further tension with the matching principle "because they raise questions concerning the integrity of the interrelationship between revenues, expenses, and investments in the test year."[112] The ALJ also analyzes previous Commission decisions regarding significant *pro forma* adjustments

[109] Recommended Decision ¶ 95 (citing Hrg. Exh. 106 (Koca Direct) 39:10-41:9).
[110] Recommended Decision ¶ 114.
[111] Recommended Decision ¶ 115.
[112] Recommended Decision ¶ 116.

related to post-test year capital additions and concludes those decisions contain material factual distinctions and thus “do not dictate a different outcome” in this Proceeding.[113]

a. Black Hills Exceptions

99. In its exceptions, Black Hills requests that the Commission reverse the disallowance of these proposed post-base period capital additions and approve the Company’s $35.3 million *pro forma* adjustment for additions between July 1, 2018 and December 31, 2018. Black Hills objects that the amount of plant disallowed in the Recommended Decision comprises 13 percent of the total rate base requested by the Company. Black Hills contends the regulatory lag of obtaining recovery of this investment that “is now in service and has been providing service to customers for more than a year” through a new rate case is punitive.[114]

100. Black Hills argues that inclusion of these additions is “consistent with similar *pro forma* adjustments approved by the Commission in rate reviews over the past 10 years allowing recovery of significant plant investments placed in service after the end of the Historical Test Year (‘HTY’) adopted in those proceedings.”[115] Black Hills provides a list of decisions it argues demonstrate changing ratemaking policies on “the more general concept of the matching principle” and a “relax[ing]” of the “historical restriction including post-HTY plant in rate base.”[116] The Company argues that upholding the rejection of these additions would “signal a major break in the Commission’s application of its ratemaking policy with regard to post-HTY plant.”[117] Likewise, Black Hills contends that disallowing nearly 13 percent of its rate base is a misapplication of the matching principle. Black Hills concedes the matching principle

[113] Recommended Decision ¶ 122.
[114] Black Hills Exceptions p. 37. (Emphasis omitted)
[115] Black Hills Exceptions p. 39. (Emphasis in original)
[116] Black Hills Exceptions p. 39-40.
[117] Black Hills Exceptions p. 40.

"is a general concept that should be applied in ensuring the interrelationships among investments, revenues and expenses are maintained" but argues this is "not a hard and fast principle and is not one that has ever been used by the Commission to disallow actual plant in-service constituting nearly 13% of a utility's total rate base."[118]

101. Black Hills disputes the ALJ's criticisms of the technical methods the Company used to develop its *pro forma* adjustment to cost of service. Although Black Hills admits it did not take into consideration plant replacements and retirements occurring during the same six-month period, July 1, 2018 through December 31, 2018, the Company maintains the adjustment is consistent with the calculation methods used in prior cases.

102. Finally, Black Hills states that, to the extent the Recommended Decision intended to adopt the OCC's partial reversal of the Company's customer growth adjustment as part of the disallowance of the post-base period capital addition adjustment, the Commission should reverse such determination. We construe this as a request for clarification regarding the calculation of the revenue requirement, as the Company states the revenue growth adjustment to reflect the increase in number of customers on the system as of year-end 2018 resulted in a reduction to the requested revenue increase of $708,637.

b. OCC Response to Black Hills Exceptions

103. In its response to Black Hills' exceptions, the OCC agrees with the ALJ and points to the OCC's testimony and argument rejecting the $35.5 million "capital reach." The OCC supports the ALJ's determination that the rate base additions made after June 30, 2018 are not extraordinary but were instead made in the ordinary course of business and thus do not warrant inclusion in rate base in this Proceeding. The OCC reiterates its position that the "capital

[118] Black Hills Exceptions p. 39.

reach" violates the matching principle. The OCC also restates its assertion that Black Hills could have waited 18 days to file its case in order to use full calendar year 2018 per-book data as its test year.

104. The OCC further advises the Commission to conduct a technical conference even if it upholds the ALJ's rejection of the $35.3 million *pro forma* adjustment to rate base. The OCC states the Company's cost of service must be adjusted to achieve a complete reversal of the "capital reach" family of adjustments. The OCC challenges the "revenue growth adjustment" that Black Hills made associated with the $35.3 million of disputed capital additions. When re-calculating its revenue requirement without the $35.3 million of additional capital investments, Black Hills reduces its overall revenue deficiency by roughly $1.3 million. But the Company also eliminates the $708,687 revenue adjustment it made associated with the capital additions, which had caused the net increase in revenue requirements caused by the capital additions to fall from $1.3 million to be about $600,000 on net. In its response to Black Hills' exceptions, the OCC contends that most of the $708,687 adjustment represents a standard "normalization" adjustment rather than a customer growth adjustment. The OCC concludes the "annual normalization" portion of the adjustment, approximately $607,453, should remain in the cost of service.

c. Findings and Conclusions

105. We deny Black Hills' exceptions requesting to include the $35.3 million of post-base period capital additions in the rate base calculation. Black Hills is correct that the Commission does allow post-test-year rate base additions to be included in some form in the cost of service study supporting a request to increase rates. But many factors are generally considered when the Commission allows these additions. In this Proceeding, the ALJ properly

rejected the Company's suggestion that the "significant" size of these post-test year investments, when considered in the aggregate, renders them extraordinary.[119] Black Hills' contentions that rejecting these additions represents a "major break" from "relaxing" the matching principle, and that this principle is a "general concept" but "not a hard and fast principle" mischaracterizes the ALJ's analysis. The ALJ's focus was not on strict adherence to matching but on the actual interrelationship between revenues, expenses, and investments in the test year. The ALJ's disallowance was based on a finding that the post-test year adjustments do not "sufficiently" adhere to the matching principle and therefore would not result in a "just and reasonable outcome."[120]

106. Because we uphold the Recommended Decision's disallowance of these additions, we address the OCC's request in exceptions to require Black Hills to retain a revenue adjustment equal to the amount of $607,453, which the OCC claims is an "annual normalization" unrelated to the capital additions. We deny these exceptions. We find the OCC did not make a compelling case to support its position that $607,453 of the $708,687 revenue adjustment represents a standard "annual normalization" of revenues for the test year. We agree with the Recommended Decision that the OCC raises doubts about whether the full $708,687 ties to a customer growth adjustment in revenues, but we are not convinced that simply subtracting $101,234 from the $708,687 based on an admittedly rudimentary portioning of the adjustment suffices as a measure of "annual normalization." Therefore, since we disallow inclusion of the $35.3 million of capital additions, we find the cost of service should also "reverse" the entire $708,687 revenue adjustment that Black Hills ties to the capital additions.

[119] Recommended Decision ¶ 114.

[120] Recommended Decision ¶ 115.

9. Return on Equity

107. As described in the Recommended Decision, Black Hills requested that the Commission establish a return on equity (ROE) range of 9.6 to 10.9 percent and approve an authorized ROE of 10.15 percent. Black Hills developed its recommendation using a combination of the Constant Growth Discounted Cash Flow (DCF) model, the Multi-Stage DCF model, the Capital Asset Pricing Model (CAPM), the Empirical Capital Asset Pricing Model (ECAPM), the Utility Risk Premium Method, and the Expected Earnings Approach along with economic factors including flotation costs. Black Hills applied these models using data from proxy groups of gas utilities that it considers risk-comparable to Black Hills. Black Hills also used a non-utility proxy group of low-risk companies from various industries.

108. The Recommended Decision describes how Staff recommended an ROE of 9.0 percent or lower. Staff primarily relied on the Multi-State DCF model and encouraged the Commission to give principal attention to this method. Staff argued that its recommended ROE better aligns the Company's ROE with the Multi-Stage DCF model results, recognizes the reduction in risk as an outflow of the approval of the DSIR, and reflects the principle of gradualism in ratemaking. Staff's ROE witness Peuquet used the same criteria as Black Hills to select a proxy group but included four additional criteria in his selection of the companies. Unlike Black Hills, Mr. Peuquet further required the proxy group members to be combination electric/gas utilities. Mr. Peuquet reasoned this was appropriate since Black Hills Corporation issues equity and debt for all its regulated subsidiaries, including Black Hills and Black Hills Corporation's other regulated electric utilities.

109. The Recommended Decision describes that, like Staff, the OCC recommended an ROE of 9.0 percent. The OCC recommended a range of reasonableness of 8.3 to 9.6 percent.

The OCC developed its recommendation based on an average of four models: the CAPM, Constant Growth DCF, the Multi-State DCF, and an analysis of authorized national ROEs. The OCC argued that recent trends in capital markets lead investors to require lower equity premiums. The OCC's ROE witness Fernandez agreed that Black Hills' proxy group was reasonable except for Northwest Natural Gas, which had undergone recent structural and operational changes.

110. The Recommended Decision establishes a range of reasonableness for the authorized ROE of 9.2 percent to 9.6 percent and approves an ROE of 9.5 percent for purposes of determining the revenue requirement.

111. The ALJ concludes the wide range of results and the divergence of positions on inputs and assumptions confirm the need for the Commission to exercise its judgment in considering the various factors that explain the differences in the calculations. The ALJ explains that he examined and considered the quantitative results of each rate of return model presented by the parties. The ALJ concludes that all the methodologies presented by parties are generally accepted by the rate of return analyst community. The ALJ states that, in determining the ROE, no single rate of return model was favored, and the ALJ agrees in principle that each model result has validity and should be appropriately considered.

112. The ALJ explains he also considered the qualitative factors that affect the Company's risk profile. The ALJ states that these include the financial stability afforded to the Company by approval of the DSIR, the historically low level of U.S. Treasury and utility bond yields, the perception of the Company in the marketplace as evidenced by its stock price and credit agency rating, the low likelihood of a credit agency downgrade of the Company, the trends in authorized ROEs for natural gas utilities, and Black Hills Corporation's ability to access

capital. The ALJ concludes that, taken as a whole, these qualitative factors lend credibility to an ROE on the lower end of the spectrum between the positions of the Company and intervenors.

a. Black Hills Exceptions

113. In its exceptions, Black Hills argues that the Commission should increase the authorized ROE beyond the 9.5 percent adopted by the Recommended Decision "to better reflect the upper range of reasonableness."[121] Black Hills objects that the ALJ's findings in support of a 9.5 percent ROE within a range of reasonableness extending from 9.2 percent to 9.6 percent are inconsistent with the factual record. Specifically, Black Hills argues the rate of return models produced by the Company using models other than DCF (*i.e.*, the CAPM, ECAPM, Utility Risk Premium, and Expected Earnings models) significantly exceed the 9.6 percent established as the top of the range of reasonableness. Black Hills concludes that, since the most recent data cited in the record supports an ROE for gas-only utilities like the Company of 9.6 percent, and Black Hills has greater risks than other gas utilities due to its lower credit ratings and lack of regulatory adjustment mechanisms, an ROE above 9.6 percent is justified.

b. Staff Exceptions

114. In its exceptions, Staff recommends the Commission lower the authorized ROE from the 9.5 percent approved in the Recommended Decision to the 9.0 percent Staff advocated for during this Proceeding. Citing findings in the Recommended Decision and Staff ROE witness Peuquet's testimony, Staff concludes the record strongly suggests the Commission can "feel confident" that approving an ROE OF 9.0 percent will not lead to adverse consequences for the Company in accessing capital, maintaining its credit rating, or attracting

[121] Black Hills Exceptions p. 44.

investors.[122] Staff maintains that an ROE of 9.0 percent is just and reasonable in light of current market conditions. Staff points to the modeled results from Staff's DCF analysis, which average 9.0 percent, and results from Staff's Multi-Stage DCF analysis, which range from 7.7 to 8.5 percent, and the Company's own modeled Multi-Stage DCF result, which indicates a 9.0 percent ROE. Staff concludes that an authorized ROE of 9.0 percent does not ignore these important data points and still protects the Company's financial well-being.

115. Staff also asks the Commission to affirm a preference for DCF modelling. Staff warns that the Commission should "refrain from falling for the predetermined-result-seeking alternative modelling" suggested by Black Hills and notes the alternative modelling suggested by Black Hills in this Proceeding produced higher ROEs than those produced by the Multi-Stage DCF.[123] Staff warns that, by not establishing DCF as the preferred approach, the Commission is "opening the door to an explosion of new, unexamined and more easily manipulated approaches to ROE modelling that are not as evidence-based in Colorado rate case proceedings for years to come."[124] Staff argues that the DCF model is the most robust and that continued reliance on this model will promote consistency over time and across utilities. Staff argues that the Commission historically relies on DCF models and the ALJ in this rate case "took the Commission down a new path that the Commission should not travel" because it considered all of the parties' rate-of-return models to have "equal footing."[125] Staff concludes that DCF models work and can foster consistency over time and across utilities.

[122] Staff Exceptions p. 14 (citing Recommended Decision ¶ 185; Hrg. Exh. 100 (Peuquet Answer 106:8-12, 107:9-12).

[123] Staff Exceptions p. 10.

[124] Staff Exceptions pp. 10-11.

[125] Staff Exceptions p. 9 (quoting Recommended Decision ¶ 192).

c. OCC Exceptions

116. In its exceptions, the OCC argues like Staff that the Recommended Decision sets the authorized ROE and range of reasonableness too high based on the record of this Proceeding. The OCC argues the record supports the adoption of the OCC's and Staff's recommended ROE of 9.0 percent. Like Staff, the OCC dismisses the Company's claims of a negative credit rating as unsupported speculation. The OCC argues that the record demonstrates the Multi-Stage DCF models of Staff, the OCC, and the Company all produced an average ROE of 9.0 percent using a selected gas utility proxy group that was essentially the same. The OCC points out that its Multi-Stage DCF result is an ROE of 8.97 percent. The OCC adds that it also presented evidence that recent trends in the capital market are favorable and the Federal Reserve has reduced interest rates multiple times in 2019. In the alternative, the OCC recommends, if the Commission affirms the range of reasonableness established in the Recommended Decision, the ROE should be set at 9.2 percent and in no event higher than the 9.4 percent midpoint in that range of reasonableness.

d. Black Hills Response to Staff and OCC Exceptions

117. In its response to the exceptions of Staff and the OCC filed on January 30, 2020, Black Hills argues the Commission should not ignore the results of models other than DCF. The Company argues that looking only at DCF results would unduly limit the Commission's consideration of other relevant analyses in determining the ROEs for public utilities within its jurisdiction. Black Hills contends the "disconnect between the assumptions" of DCF and "the expectations of real-world investors is demonstrated by the inability of Staff and the OCC to reconcile the results" of DCF analyses against other recognized benchmarks for an appropriate

ROE.[126] Black Hills explains Staff's DCF results ranged from 7.7 to 8.5 percent while the allowed ROEs for Staff's own proxy group average 9.74 percent, and the ROE benchmarks cited by Staff's witness support an ROE of 9.63 percent, at the very top of the Recommended Decision's range of reasonableness.[127] Black Hills responds that even Staff implicitly recognizes the downward bias inherent in the DCF approach by recommending an ROE significantly higher than the 7.85 percent resulting from Staff witness Peuquet's application of this method.[128] Black Hills concludes that consideration of the results of multiple methods, as the ALJ recommends, is consistent with the accepted understanding in the financial community that there is no single model that conclusively determines or estimates the cost of equity.

e. Staff Response to Black Hills Exceptions

118. In response to Black Hills' exceptions, Staff warns that if the Commission opens the ROE analyses beyond DCF models, it risks opening a Pandora's Box, leading to a proliferation of pre-determined and result-seeking alternative modelling. Staff argues that, for consistency's sake, and the sake of sound analytical analysis, the Commission should stick to what works by dedicating itself to exclusive reliance on DCF modelling for the purposes of authorizing ROEs.

f. OCC Response to Black Hills Exceptions

119. In its response to Black Hills' exceptions, the OCC reiterates its support for lowering the established range of reasonableness and the authorized ROE. The OCC reiterates its argument that the cost of equity is less than what the Company presented in its direct or rebuttal cases and that the record supports the OCC's advocacy.

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[126] Black Hills Response to Exceptions p. 10.

[127] Black Hills Response to Exceptions pp. 10-11.

[128] Black Hills Response to Exceptions p. 11 (citing Hrg. Exh. 400 (Peuquet Answer) p. 98, Table JJP-9).

g. Findings and Conclusions

120. The Recommended Decision properly reviews that, in determining a utility's authorized ROE, the Commission considers the standards articulated in *Bluefield Waterworks and Improvement Co. v. Public Service Comm'n. of West Virginia*, 262 U.S. 679 (1923) and *Federal Power Comm'n. v. Hope Natural Gas Co.*, 320 U.S. 591 (1944). We consider whether Black Hills' authorized ROE is similar to the returns to investors who own shares in other businesses having comparable financial characteristics and business risks. And we consider whether the authorized ROE supports Black Hills' financial integrity, including its credit rating that serves as a basis for securing debt at reasonable rates. We agree with the Recommended Decision that setting a utility's authorized ROE is a balancing art. If it is set unreasonably high, ratepayers may be burdened with excessive costs and current investors could receive a windfall. If it is set too low, service quality may be jeopardized, because the utility will not be able to raise new capital on reasonable terms.

121. As an initial matter, we deny Staff's exceptions requesting that the Commission affirm a preference for DCF modelling for purposes of determining the authorized ROE. We find it is generally necessary to weigh the strengths and weaknesses of the various methods brought forward by parties to support their ROE recommendations. We will retain our discretion to apply proper weights to the various methods and results in each rate case before us.

122. We grant, in part, the exceptions of Staff and the OCC recommending that we modify the authorized ROE in the Recommended Decision. The current ROEs of BHGU and BHGD are 9.6 percent and 10.0 percent, respectively. We agree with the findings in the Recommended Decision that a reduction in Black Hills' authorized ROE is supported by the analyses put forward by the intervenors. We affirm the ALJ's range of reasonableness for the

ROE from 9.2 percent to 9.6 percent. However, we find the record supports an even further reduction in the authorized ROE. For the reasons outlined below, we find the record in this Proceeding supports establishing an authorized ROE of 9.2 percent.

123. First, we find more persuasive the advocacy of Staff and the OCC for a reduction in the authorized ROE than the Company's advocacy for an increase. Both Staff and the OCC recommend an authorized ROE of 9.0 percent, which is a marked reduction from current levels and lower than the 9.5 percent in the Recommended Decision. As Staff and the OCC claim in their exceptions, such a reduction is supported by the results of the Multi-Stage DCF models of the ROE witnesses for Staff, the OCC, and the Company, which all produced an average ROE of 9.0 percent.

124. We find the testimony and analysis of Staff ROE witness Peuquet credible and we find Staff makes a compelling case for setting the authorized ROE lower than the 9.5 percent established in the Recommended Decision. The results of Staff's Constant Growth DCF model produced an ROE estimate between 8.77 and 9.01 percent.[129] We further agree with Staff that these results are more reliable than the Company's results because Staff did not have to exclude any calculations, while the Company had to exclude eight calculations as illogically high or low.

125. We also find the testimony and analysis of the OCC's ROE witness Fernandez credible and persuasively supports setting the authorized ROE lower than 9.5 percent. The OCC supports its recommendations with the results of multiple financial models including Constant Growth DCF, Multi-Stage DCF, and CAPM. The OCC comes to the same conclusion as Staff, that it is appropriate to lower the authorized ROE, which we find reinforces Staff's analysis.

[129] Hrg. Exh. 400 (Peuquet Answer) 77:5-8 Table JJP-6 "Summary of Staff's Constant Growth DCF Results."

126. Second, we find that the OCC persuasively argues that other factors support a decrease in the authorized ROE. The OCC provides evidence of a downward trend in authorized ROEs in the United States.[130] The OCC argues this national trend is a reasonable data point to determine what should be set in this rate case. The OCC adds that U.S. Treasury Bond yields, which are the basis for risk free rates, have decreased over that same period.[131] The OCC concludes that equity costs have decreased over the past decade, which has caused a general decrease in authorized utility ROEs for both electric and gas utilities. We thus agree with the OCC that this downward trend in equity costs and average authorized ROEs is grounds to reject the Company's request to increase its ROE and at least set it lower than the 9.6 percent the Commission last authorized for BHGU in 2012.

127. Third, and finally, we agree with Staff and the OCC that the evidence in the record does not support the Company's claim that lowering its authorized ROE will adversely affect the Company. For example, as noted in the Recommended Decision, Staff testified that, in August 2018, Standard and Poors upgraded Black Hills Corporation's credit rating from BBB to BBB+ and all credit ratings agencies outlook of Black Hills Corporation was stable.[132] And as the Recommended Decision raises, the Company was able to issue hundreds of millions of dollars in new debt and new equity to finance its $1.9 billion SourceGas acquisition.[133]

10. Cost of Long-Term Debt

128. The Recommended Decision approves the Company's proposed cost of long-term debt of 4.31 percent. This rate is based on the cost of long-term debt that was assigned to Black

[130] Hrg. Exh. 302 (Fernandez Answer) p. 49 Figure RAF-2 "Average Authorized ROEs – Gas Rate Case Decisions."

[131] Hrg. Exh. 302 (Fernandez Answer) p. 49 Figure RAF-1 "10 Year History Treasury Bond Yields."

[132] Recommended Decision ¶ 185 (citing Hrg. Exh. 400 (Peuquet Answer) p. 59, Table JJP-3 "Recent History of BHC Credit Ratings and Outlooks").

[133] Recommended Decision ¶ 185 (citing Hrg. Exh. 302 (Fernandez Answer) 52:9-10).

Hills as of December 31, 2018, and is higher than the 3.85 actual debt cost as of June 30, 2018 (the end date of the Company's HTY used in this Proceeding). The Recommended Decision finds ratepayers will not be prejudiced by the actual cost of debt, as calculated by the Company at 4.31 percent as of December 31, 2018.[134]

129. In addition to establishing the cost of long-term debt for Black Hills for the purpose of calculating the Company's revenue requirement, the Recommended Decision raises concern about Black Hills' approach to obtaining approval from the Commission for its assumption of long-term debt assigned by its parent, Black Hills Corporation. The ALJ notes that Black Hills concedes $101 million of the $136 million in "long-term" debt identified by Black Hills is debt that Black Hills Corporation has been assigning to Black Hills in annual short-term one-year notes. The ALJ explains that, according to Black Hills, only after the Commission has approved using the $101 million in debt for purposes of calculating rates will Black Hills file an application seeking approval for Black Hills Corporation to assign the $101 million to Black Hills on a long-term basis pursuant to § 40-1-104, C.R.S. This statute requires Commission authorization for Black Hills to assume long-term debt unless the Commission finds the authorization inconsistent with the public interest. The Recommended Decision concludes that Black Hills' chosen sequencing "places maximum pressure" on the Commission to approve the application filed under § 40-1-104, C.R.S., since the Commission would have already approved inclusion of the debt in the capital structure used to set rates in a Phase I rate case. The ALJ therefore recommends that the Commission order Black Hills to, in the future, obtain approval of long-term debt assignments pursuant to § 40-1-104, C.R.S., before the Company seeks approval to include such debt in its capital structure as long-term debt in a

[134] Recommended Decision ¶ 207.

Phase I rate case. The ALJ recommends the Commission should otherwise treat the debt as short-term debt and include all short-term debt in the capital structure.[135]

a. **Black Hills Exceptions**

130. In its exceptions, Black Hills argues that the determination of long-term debt is properly made by the Commission in a rate case, where all the revenues, investments, and expenses of the utility can be examined, rather than through a petition filed pursuant to § 40-1-104, C.R.S.[136] Black Hills contends that a petition filed pursuant to § 40-1-104, C.R.S., is an expedited proceeding with a lower standard than a rate review proceeding. Black Hills claims this directive to first obtain approval through a petition departs from how the Commission has in the past applied § 40-1-104, C.R.S., and Rule 4 CCR 723-4-4105 of the Commission's Rules Regulating Gas Utilities and Pipeline Operators, and reasons that such departure would likely first require a rulemaking.

b. **Staff Exceptions**

131. In its exceptions, Staff does not seek to change the approved 4.31 percent cost of long-term debt but does renew its request that the Commission specify that Black Hills' cost of debt shall be set based on the cost of debt of Black Hills Corporation. Staff further requests that the Commission find Black Hills' cost of debt should not be set at any different cost level than the cost of debt of its parent, and thus not "according to the sole discretion of the Treasurer of [Black Hills Corporation]."[137] Staff argues no other utility serving Colorado has its cost of debt allocated in this way and the problems with such system are reflected in the evidence in this

[135] Recommended Decision ¶ 213.

[136] Black Hills Exceptions p. 58-59.

[137] Staff Exceptions p. 15 (citing Recommended Decision ¶ 195).

Proceeding showing that Black Hills Corporation has given more favorable debt assignments to unregulated subsidiaries as compared to its regulated subsidiaries.

c. Black Hills Response to Staff Exceptions

132. In response to Staff's exceptions, Black Hills states there is no controversy between the Company and Staff concerning the cost of long-term debt to be used to develop rates in this Proceeding that would require the Commission to resolve the issues raised in Staff's exceptions. Black Hills contends that Staff's request in exceptions amounts to a request for a declaratory ruling.

d. OCC Exceptions

133. In its exceptions, the OCC contends the record in this Proceeding supports a 4.01 percent cost of debt as of December 31, 2018, and alternatively, the 3.85 percent cost of debt recommended in the OCC's answer testimony, which includes disallowances for selected make-whole and swap lock costs. The OCC argues that the record in this Proceeding demonstrates that Black Hills Corporation has assigned more expensive debt to its Colorado regulated subsidiaries and assigned less expensive debt to its unregulated subsidiaries. The OCC claims that as of June 30, 2018, the end of the test period, Black Hills' cost of long-term debt was 4.01 percent. The OCC contends that Black Hills then increased its cost of debt in the last six months of 2018 through certain allocations of debt by Black Hills Corporation.

134. The OCC further objects to the inclusion of "make-whole costs" that it attributes to the SourceGas acquisition and to the inclusion of "swap lock costs" that the OCC contends reflect derivative transaction hedges not approved by the Commission, and causes the debt to be unreasonably expensive.

135. The OCC supports the ALJ's recommendation requiring Black Hills to obtain approval of long-term debt and/or to assume long-term debt pursuant to § 40-1-104, C.R.S., before seeking approval to include that debt in its capital structure in a Phase I rate case.

e. Black Hills Response to OCC Exceptions

136. In response to the OCC's exceptions, Black Hills counters that the OCC has presented no credible evidence to demonstrate harm or prejudice to the Company's customers from using the cost of debt approved by the ALJ other than to refer to certain other Black Hills Corporation regulated and non-regulated subsidiaries that have a slightly lower cost of debt. Black Hills concludes there has been no showing of any abuse of discretion in this Proceeding.

137. Black Hills responds that the OCC's proposal for a 4.01 percent cost of debt ignores the retirement of a $250 million note due January 11, 2019, at a cost of 2.54 percent, with its replacement, at a cost of 4.53 percent, which occurred in August 2018. Black Hills maintains this retirement constitutes a known and measurable change to the Company's cost of service and reflects the "actual financing" in place when rates take effect. Black Hills argues that the OCC's objections to the debt costs including costs associated with pre-issuance hedges and remarketing costs is unavailing. Black Hills states the fact that the swap lock hedges do not always result in less costs does not make them imprudent when they are put into place when interest rates are volatile and could increase significantly. Black Hills contends the ALJ properly found the remarketing make-whole fees qualify for inclusion in Account 189, Loss on Required Debt, and may be amortized over the life of the notes. According to Black Hills, the OCC has not provided any basis to overturn these findings.

f. Findings and Conclusions

138. We deny these exceptions and uphold in its entirety the Recommended Decision's determination of the cost of debt of 4.31 percent for purposes of setting Black Hills' revenue requirement.

139. We deny Staff's exceptions requesting that the Commission enter a finding that Black Hills' cost of debt shall be set based on the cost of debt of its parent, Black Hills Corporation. The determination of the cost of debt should be made in each rate case based upon all relevant evidence and circumstances. Although the Commission has considered substantial evidence regarding the controversies surrounding Black Hills Corporation's allocation of debt to the Black Hills operating utilities in Colorado, this rate case is not where the Commission should establish a definitive ruling to apply in future rate cases regarding the establishment of long-term debt costs.

140. We uphold the requirement in the Recommended Decision for Black Hills to obtain approval of debt assignments made by Black Hills Corporation for the establishment of the Company's long-term debt. We find the Recommended Decision reasonably concludes that Black Hills should obtain approval for the debt assignments to Black Hills from its parent, Black Hills Corporation, to establish the Company's long-term debt through a separate petition pursuant to § 40-1-104, C.R.S., rather than within this rate case. We make this determination based on the facts and evidence of this Proceeding and decline to enter an express finding on the type of proceeding by which debt assignments are to be made permanent. Rather, we find this issue is another component of the Company's flawed approach in this Proceeding to present many complicated issues within a single rate case. And like the other issues the ALJ denied, we find it reasonable that this component, the long-term debt cost, should be considered on a

separate and more robust record than in this rate case. We thus leave open both options for future consideration based on the facts and circumstances of future cases and, given the processes and different statutory requirements that apply to a petition pursuant to § 40-1-104, C.R.S., rather than to a rate case.

11. Future Wage Increases and Pension Expense Impacts

141. The Recommended Decision finds that Black Hills has carried its burden of establishing that cost recovery should take place in this Proceeding for the Company's proposed adjustments to base period labor costs to reflect wage adjustments in September 2018, planned merit increases of 2.5 percent in March 2019, annual incentive compensation reflecting 100 percent of target but capped at 15 percent, and benefits, overtime, call-out, and standby pay. Staff had recommended disallowing any incentive pay or pension impact associated with salary increases above 2.5 percent. The Recommended Decision finds that Staff has not provided sufficient evidence supporting its requested disallowances.

a. Staff Exceptions

142. In its exceptions, Staff requests that the Commission deny recovery of "incentive pay" and wage increases and their associated impacts on pension expenses greater than 2.5 percent. Staff contends the record shows that, in 2019, Black Hills' wage increases were substantially larger than the 2.5 percent adjustment requested to the booked wages in the revenue requirement. Staff suggests the implications of such increases are "troubling" and "largely unstudied."[138] Staff suggests the Company has itself not determined the full cost of such increases and will likely request recovery in its next rate case. Staff contends the Commission

[138] Staff Exceptions p. 24.

should order that incentive pay and pension impact caused by wage increases in excess of the 2.5 percent authorized by the Recommended Decision will not be recovered from ratepayers.

b. Findings and Conclusions

143. We deny Staff's exceptions requesting that the Commission enter an order in this Proceeding that prohibits cost recovery of incentive pay and wage increases greater than 2.5 percent in a future proceeding. We conclude that our decision setting rates in this Proceeding should not include additional findings on the allowed components of a potential 2019 test year that might be used in a future rate case. We find there is insufficient basis to support a policy of capping cost recovery in the manner proposed by Staff. We also have concern that Staff's proposal is too undeveloped to be implemented in practice. Moreover, we are cautious that it may be improper for the Commission to establish such a prospective policy in this single rate case.

12. Pension and Retiree Expenses

144. The Recommended Decision denies recovery of the amortized costs and actuarial gains and losses in the Company's pension-related and other post-employment benefits (OPEB)-related regulatory assets created at the time of the Aquila and SourceGas acquisitions. Staff advocated in this Proceeding to deny recovery of these regulatory assets and to require that the Company return any dollars already recovered. Staff argued that the Commission had not yet approved creation or recovery of these regulatory assets. Staff also suggested that it was likely these regulatory assets led to an adjustment to the SourceGas purchase price and thus any recovery by the Company would constitute double recovery. The Recommended Decision concludes that, after careful consideration of the arguments of Black Hills and Staff, it is

appropriate to deny recovery and to require the Company to return to ratepayers any dollars already collected, using a three-year amortization period.

a. Black Hills Exceptions

145. In its exceptions, Black Hills requests that the Commission vacate the Recommended Decision's disallowance of pension and retiree medical regulatory assets associated with employees who joined Black Hills through acquisitions of the predecessor utilities. Black Hills argues that the discussion and findings in the Recommended Decision fail to support disallowance of these $265,636 annual costs. Black Hills provides a history of previous rate cases in which such costs were addressed and alleges the ALJ ignored the regulatory principles established in those proceedings. The Company further faults the ALJ for adopting Staff's recommendations without referring to supporting statute, rule, or decision.

146. The Company further urges the Commission to reconsider the Company's proposed accounting tracking mechanism for various cost items including pension and retiree medical expenses. Black Hills states that tracking and amortization of this multi-purpose mechanism should begin upon the effective date of rates from this Proceeding and the balance recorded in the tracker account would be addressed as an expense or credit in the Company's next rate case.

147. Black Hills states that, through its rebuttal testimony, the Company accepted Staff's recommendation to include a base level of pension and retiree medical expenses in the revenue requirement and to set up an accounting tracking mechanism to record in a regulatory asset account the difference between actual expenses incurred and the approved base expense amounts. Black Hills acknowledges that Staff's recommendation was conditioned on the Commission denying Staff's other recommendation to disallow recovery of these costs.

b. Staff Exceptions and Staff Response to Black Hills Exceptions

148. In its exceptions, Staff asks the Commission to clarify that the 15 percent cap for incentive payments relative to eligible earnings applies to the pension costs recoverable from ratepayers. Staff thus asks the Commission to direct Black Hills to remove from the pension expense the impact of incentive payments above 15 percent of base salary. Staff points to recent decisions for other utilities as examples of the Commission adopting this kind of cap.

149. In response to Black Hills' exceptions, Staff alleges that the Company misrepresents the level of detail and transparency involved in prior Commission decisions on the pension and OPEB regulatory assets in order to bolster its criticism of the Recommended Decision. Staff contends the primary reason the Commission should uphold the denial of recovery of the amortized costs and actuarial gains and losses in the pension-related and OPEB-related regulatory assets is because the Company created and started amortizing these regulatory assets without first notifying the Commission so the Commission could approve recovery and define the recovery mechanism. Staff argues that, because there has not yet been this kind of review of these assets, Black Hills is now over-recovering on some of these costs and will continue to over-recover such costs until the Commission acts such as through denial of the cost recovery. Staff states the money collected to pay off these regulatory assets goes to Black Hills as earnings and does not fund the Company's pension or retiree medical trusts.

c. Black Hills Response to Staff Exceptions

150. Black Hills responds to Staff's exceptions by explaining it opposes the 15 percent cap because the amount of any such "excess" pension costs, estimated at $5,000 for 2018, is *de minimis*, while the complexity and burden of attempting to calculate and permanently track

slivers of compensation amounts employee-by-employee is overly burdensome and not cost-justified.

d. Findings and Conclusions

(1) *Pensions and Retiree Medical Expenses*

151. We grant, in part, the request to clarify the treatment of the "periodic" pension and retiree medical expenses. Specifically, we find it appropriate for the Commission to clarify whether an accounting tracking mechanism should be adopted for these expenses. We require that the Company establish separate accounting tracking mechanisms for both items, the balances of which would be addressed in Black Hills' next rate case. We thus deny Black Hills' request for a multipurpose tracking mechanism as set forth in its exceptions.

(2) *Recovery of Amortized Legacy Assets*

152. We disagree with Staff that the absence of a Commission decision approving either the creation or recovery of pension and retiree medical regulatory assets is sufficient cause to disallow recovery of the costs of the pension-related and OPEB-related regulatory assets. We are also unpersuaded that there has been "double recovery" of the costs associated with the purchase price of SourceGas. We also disagree with Staff's request that costs recovered from ratepayers in the past should be returned to ratepayers over a three-year amortization.

153. In this rate case, the cost of service includes unamortized costs associated with the pension and retiree expenses created at the time of the Aquila and SourceGas acquisitions. We find the cost of service includes the amortization expense, except the expense should not include a return. In other words, the regulatory asset should not be included in rate base. We also conclude the amortization periods used by Black Hills and explained in the direct testimony of Company witness Menzel are reasonable. We will require Black Hills to establish an accounting

tracking mechanism for these expenses vis-à-vis the base expense amounts (calculated without any return) starting the effective date of rates from this Proceeding. The balance recorded in the pension and OPEB trackers would be addressed in the Company's next rate case. This accounting mechanism is not to be combined with the accounting of other items.

(3) *Incentive Payments*

154. We deny Staff's exceptions requesting that the Commission direct Black Hills to remove from the pension expense the impact of incentive payments above 15 percent of base salary. Although we share Staff's concern with ensuring that these expenses are reasonable, we are not convinced that the impact of this data-intensive review would result in a meaningful adjustment to the Company's cost of service. Given the complexity of the calculation and the burden of work entailed, we will not impose this directive in this rate case.

(4) ***Equity Compensation***

155. The Recommended Decision directs Black Hills to remove 50 percent of the requested equity compensation expenses from the test period, based on the arguments of Staff and OCC and previous Commission decisions.

e. Black Hills Exceptions

156. In its exceptions, Black Hills argues that the record demonstrates the total compensation the Company pays to its employees, including equity compensation, is reasonable, prudent, and commensurate with the market. Black Hills argues that no party has alleged that the overall compensation for Company employees is excessive or unreasonable. Black Hills cautions that, unless the Company can recover each element of its employee compensation program, it will have difficulty attracting, motivating, and retaining competent and qualified employees.

157. Black Hills also seeks clarification of whether the 50 percent reduction ordered by the Recommended Decision applies to the $426,126 in equity compensation recorded during the Company's base period or instead applies to calendar year 2018 expenses of $790,222.

f. OCC Response to Black Hills Exceptions

158. In response to Black Hills' exceptions, the OCC argues that the record in this Proceeding supports an equity compensation amount of $790,222 for the "disallowance figure" because that is the amount Black Hills stated it included for its equity compensation expense in its 2018 revenue requirement in response to an OCC discovery request. The OCC responds that the record supports the determinations in the Recommended Decision regarding equity compensation. The OCC recommends that the Commission disallow either 50 percent or 100 percent of the amount. The OCC notes that in Black Hills' last two rate cases the Commission ordered the Company to remove equity compensation costs from its cost of service.

g. Findings and Conclusions

159. We deny Black Hills' exceptions requesting that the Commission reverse the requirement in the Recommended Decision to remove 50 percent of the requested equity compensation expenses from the cost of service. We uphold the Recommended Decision's determination that only half of the requested equity compensation amount in the test year should be allowed for recovery from ratepayers. We agree with the ALJ that this result is reasonable and, as explained in recent Commission decisions, we agree with Staff that equity compensation benefits both Black Hills' shareholders and the Company's customers such that a 50/50 cost sharing arrangement is appropriate.

160. With respect to the request for clarification on the amount of expenses to be cut in half, we confirm that the Company-wide cost of service proposed by the Company includes the

amount of $790,222 of equity compensation expenses and that 50 percent of such an amount may be included in the revenue requirement for establishing rates.

13. Property Tax Expense

a. Black Hills Exceptions

161. In its exceptions, Black Hills asserts that the Recommended Decision does not address certain disputed Phase I issues regarding the appropriate level of property taxes to be included in the revenue requirement and the Company's proposed treatment of property taxes and other amortizations through an accounting tracking mechanism. Black Hills states that it proposed to include $3.6 million of property tax expense in the revenue requirement, consisting of the Company's per-book property tax expense adjusted to remove out-of-period costs and to reflect updated mill levy rates. The Company also included additional estimated property tax attributable to the $35.3 million of plant additions placed in service in the second half of 2018.

162. Black Hills requests that the Commission reconsider the appropriateness of the multipurpose accounting tracking mechanism discussed above, that would include pension and retiree medical expenses, property taxes, and other approved amortizations. Black Hills proposes that, in the Company's next rate case, the recorded balance of the multipurpose tracker would be amortized as an expense or revenue credit.

163. Due to Black Hills' proposed tracker, the Company also asks the Commission to reverse the ALJ's rulings requiring the filing of negative GRSA riders in the future when the amortization period terminates.

b. Staff Response to Black Hills Exceptions

164. In response to Black Hills' exceptions, Staff recommends that the Commission set property tax rates at the amount owed for tax year 2018 and paid in 2019 and order the Company

to track the under- or over-collection of property taxes for recovery in the Company's next rate case (without a carrying cost).

c. Findings and Conclusions

165. We grant these exceptions, in part. We agree that clarification is needed regarding the level of property expense that Black Hills may include in its revenue requirement. We therefore direct Black Hills to calculate the property tax expense for the 2018 tax year, but exclude property taxes associated with the $35.3 million of plant additions that are not allowed to be recovered through rates established in this Proceeding. The property tax amount shall be adjusted to remove other out-of-period costs and to reflect updated mill levy rates.

166. Consistent with the conclusions and findings set forth elsewhere in this Decision, we decline to adopt the Company's proposed multipurpose tracker. We instead order Black Hills use a separate tracking mechanism to account for differences in property taxes paid versus the property tax expense established by the Commission in this Proceeding. The balance of this tracker may be addressed in the Company's next rate case.

14. Rate Case Expenses

167. The Recommended Decision disallows recovery of 20 percent of the Company's estimated $950,000 of rate case expenses. The Recommended Decision concludes this 20 percent disallowance appropriately reflects the amount that Black Hills' mistakes and flawed approach to this Proceeding contributed to increasing the Company's rate case expenses. The Recommended Decision concludes it would be unfair to expect ratepayers to shoulder these additional costs.

a. Black Hills Exceptions

168. In its exceptions, Black Hills argues that rate case expenses are a legitimate cost of providing service, necessitated by the Commission's regulation, and the Company has a right to recover all reasonable operating expenses including rate case expenses. Black Hills contends the Recommended Decision effectively caps the potential rate case expenses at $950,000 and disallows 20 percent of the estimated expense. Black Hills requests that the Commission remove this "$950,000" cap as such cap is "contrary to well-established Commission policy to allow utilities to recover their actual rate case expenses."[139] Black Hills further argues the 20 percent disallowance is not based on the factual record but instead reflects the "revisionist history permeating the [Recommended Decision] that assigns blame solely to [Black Hills] for the 'mistakes and flawed approach to this proceeding.'"[140]

b. Staff Response to Black Hills Exceptions

169. In response to Black Hills' exceptions, Staff counters that the ALJ's disallowance of 20 percent of the estimated rate case expenses is supported by the Company's mistakes and flaws in this Proceeding. Staff states the first 11 paragraphs of the Recommended Decision: "painstakingly and accurately detail the mistakes and flaws committed by [Black Hills] resulting not only in inordinately high rate case expenses, but also, a colossal waste of the Commission's valuable time."[141] Staff thus concludes the Recommended Decision was right to impose a deduction. Staff concludes the Company's $950,000 projection of rate case expenses constitutes a remarkably high amount considering the Company only requested a $3.5 million revenue requirement increase (capped at $2.5 million). Staff concludes the 20 percent deduction "is quite

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[139] Black Hills Exceptions p. 54.

[140] Black Hills Exceptions pp. 54-55 (quoting Recommended Decision ¶ 371).

[141] Staff Response to Exceptions p. 49.

generous to the Company in light of the mistakes and flaws" such that "[f]rankly, the Company is lucky the deduction wasn't larger."[142]

170. Staff requests that the Commission more clearly define the recovery mechanism for the collection of allowed rate case expenses. Staff requests the Commission amortize rate case expenses over two years through a separate rider. Staff argues that amortization through base rates risks over-recovery by the Company. If the Commission disagrees with the proposed rider, Staff asks the Commission to adopt the same treatment for rate case expenses as established by the Recommended Decision for the Company's "Synergy Regulatory Asset."

c. OCC Exceptions

171. In its exceptions, the OCC also agrees the record supports the ALJ's findings to disallow 20 percent of the $950,000 in rate case expenses. The OCC argues that a Black Hills witness previously supported the $950,000 estimate as accurate and that the 20 percent disallowance is supported by the flaws in Black Hills' case that contributed to the total rate case expenses incurred during the Proceeding. The OCC seeks clarification that rate case expenses will be recovered over a three-year amortization period with a negative GRSA at the end of that period to ensure over-recovery does not occur. The OCC requests that the Commission also require Black Hills to make a compliance filing after the amortization period to halt recovery.

d. BGVA Exceptions

172. In its exceptions, BGVA argues that the rate case expenses associated with this Proceeding have been greatly inflated due to the way Black Hills presented its case and that Phase II issues must now be relitigated in future proceedings. BGVA agrees with Black Hills that the 20 percent reduction in recoverable rate case expenses is "unexplained" in the

[142] Staff Response to Exceptions pp. 50-51.

Recommended Decision; however, BGVA recommends the Commission go even further and order at least a 50 percent reduction in recoverable expenses. BGVA points to procedural hurdles caused by Black Hills and notes that another Phase II proceeding could have been avoided if Black Hills had agreed in advance to separate both phases.

e. Findings and Conclusions

173. We deny these exceptions. We uphold the ALJ's determination that Black Hills may recover $760,000 of rate case expenses. We find the ALJ's recommendation to disallow recovery of 20 percent of the estimated amount of $950,000 is reasonable and supported by the record of this Proceeding. We agree with the response of Staff and the OCC that Black Hills' flawed case contributed to higher than necessary expenses and that it is reasonable to disallow recovery of a portion of these additional costs. We clarify that the revenue requirement should reflect a three-year amortization of $760,000 (or $253,333 per year). After the end of the three-year amortization period, we direct Black Hills to file a negative GRSA to discontinue the recovery of these expenses from customers.

15. Credit Card Processing Fees

174. The Recommended Decision denies Black Hills' proposal to include transaction costs for credit card and Automated Clearing House (ACH) fees in rates and be paid collectively by all customers, instead of on an individual basis. At present, customers in the BHGU rate area pay these fees individually, while customers in the BHGD rate areas do not. Black Hills had argued that "socializing" the fees over the entire customer base would result in small rate impact but would improve the overall customer experience.[143] Staff and the OCC opposed the

[143] Recommended Decision ¶ 351 (citing Hrg. Exh. 120 (Gillen Direct) 21:19-23:5).

Company's proposal, reasoning that customers who do not pay their bills with credit cards should not be required to subsidize customers who use credit cards or ACH transfers.

175. The ALJ found the existence of two different methods between the rate areas inconsistent and concluded the continued disparity would prejudice ratepayers that bear the burden of socialized costs. The Recommended Decision concludes that Black Hills has not carried its burden that socializing the costs of credit card and ACH fees is in the public interest. The Recommended Decision therefore requires Black Hills to use consistently across its system a "pay-as-you-go" method.

a. Black Hills Exceptions

176. In its exceptions, Black Hills agrees that the Recommended Decision properly found a common policy across rate areas that is in the public interest but objects to the "pay-as-you-go" method adopted by the Recommended Decision. Black Hills repeats its argument that the elimination of credit card transaction fees is consistent with the general widespread use of credit cards for making payments of goods and that service and would improve the customer experience and allow more customers to schedule automatic payments, which would in turn promote timely payment of bills and lower the Company's bad debt expense. Black Hills states the credit card fees should be treated the same as the expenses for processing payments received by U.S. Mail.

b. Staff Response to Black Hills Exceptions

177. Staff responds to Black Hills' exceptions that the holdings in the Recommended Decision mirror Staff's position in this Proceeding. Staff urges the Commission to prevent the Company from subsidizing the transaction fees incurred by credit-card and ACH-paying

customers with funds from customers who do not pay their bills these ways. According to Staff, customers incurring such charges should be the ones paying them.

c. OCC Response to Black Hills Exceptions

178. The OCC responds that the Recommended Decision properly found these fees should be borne by the cost causer and Black Hills' proposal to socialize the fees should be denied. The OCC agrees with the finding in the Recommended Decision that the Company failed to meet is burden of proof to demonstrate socializing these costs are in the public interest.

d. Findings and Conclusions

179. We deny these exceptions. Although we see merit in both positions on credit card and ACH fees, we agree with the Recommended Decision that the "pay-as-you-go" method is reasonable based on the advocacy of Staff and the OCC in this Proceeding.

16. Accumulated Deferred Income Tax Tracker

180. The Recommended Decision rejects the Company's proposals to separate the non-protected excess Accumulated Deferred Income Taxes (ADIT) into two pieces: property-related and non-property-related, and to delay collection of the non-property-related non-protected ADIT until its net operating loss ADIT has been reduced to zero, when the Company will then apply an average rate assumption method to the remaining non-plant ADIT. The Recommended Decision instead adopts Staff's proposed approach to amortize the non-protected ADIT over three years and to net the non-protected property-related with the non-protected non-property related so that both the regulatory asset and the regulatory liability are extinguished.

a. Black Hills Exceptions

181. In its exceptions, Black Hills proposes to address the termination of the amortization of the excess ADIT tracker through the combined tracker described above for the

amortization of pension and retiree medical expenses, property taxes, rate case expenses, and other amortizations.

b. Findings and Conclusions

182. We deny these exceptions. We share the concern of the ALJ that the Company proposes returning the non-protected plant excess ADIT of $3.7 million to ratepayers over decades, while having ratepayers pay the non-protected non-plant excess ADIT of $1.4 million over a much shorter period. We affirm the ALJ's adoption of Staff's proposal to amortize the non-protected ADIT over three years and to net the non-protected property-related with the non-protected non-property related so that both the regulatory asset and the regulatory liability are extinguished. Consistent with the conclusions and findings regarding Black Hills' proposed multipurpose tracker as set forth above, we direct Black Hills to establish a separate accounting tracking mechanism for these ADIT-related elements in Staff's proposal. The balance of the tracker will then be examined in the Company's next rate case.

17. Depreciation Rates

183. In its exceptions, Black Hills requests, for clarity and purposes of internal accounting and future rate reviews, that the Commission identify the specific depreciation rates approved for use by the Company with a specific reference to certain tables set forth in the depreciation studies filed by the Company in this Proceeding. The tables are identified in Black Hills' exceptions as those in Table 1 in Part VI of each of the depreciation studies, except for the amortization period for the Unrecovered Reserve Adjustment. For that, the Company seeks approval of a ten-year amortization instead of the five years recommended in the study.

184. We grant these exceptions and approve the depreciation rates proposed and supported by Black Hills in this Proceeding.

18. Whitewater System Rate Condition

185. The Recommended Decision denies Black Hills' proposal to eliminate a special rate condition put in place when the Commission approved the CPCN for the Whitewater system, near Grand Junction in 2005, then owned by Kinder Morgan. The Recommended Decision notes this condition was established by the Commission to "'protect ratepayers from the risk of unrealized, optimistic assumptions about, *e.g.*, the number of customers, … capital costs, [and] expenses.'"[144] The Recommended Decision notes that Black Hills acknowledges project costs have exceeded expectation while customer numbers and revenues have been less than expected. The Recommended Decision agrees with Staff that it is appropriate to continue to hold Black Hills to this obligation. The Recommended Decision does allow, however, that investments made to improve reliability of the system are reasonable costs for recovery in this Proceeding.

a. Black Hills Exceptions

186. In its exceptions, Black Hills requests that the Commission reverse the Recommended Decision and allow the Whitewater system rate condition to now be terminated. Black Hills contends this was a condition imposed on Black Hills' predecessor, Kinder Morgan, 14 years ago applicable to the 370 customers on the Whitewater system. Black Hills contends this rate condition was not intended to be permanent and it has served its purpose by ensuring rates for other Western Slope customers did not make up for any deficiency that resulted from the economics of the initial construction of the Whitewater distribution system in 2006. Black Hills reasons that the Whitewater system is part of Black Hills' integrated statewide gas distribution operations and not a separate operating division or area. Black Hills concludes that, in "view of

[144] Recommended Decision ¶ 257 (quoting Proceeding No. 04A-113G, Decision No. R05-0269 ¶ 85 (March 4, 2005)).

the passage of time and changes to the system" in this and other areas, this condition should be terminated.[145]

b. Staff Response to Black Hills Exceptions

187. Staff urges the Commission to deny Black Hills' exceptions. Staff states that the Commission, in enacting the special rate condition, sought to protect ratepayers if the Whitewater system ultimately cost more than the forecast, or the number of customers was lower than expected. Staff argues that nothing has occurred since the Company willingly inherited this obligation from Kinder Morgan that warrants abandoning this condition at this time.

c. Findings and Conclusions

188. We deny Black Hills' exceptions requesting that the Commission reverse the Recommended Decision and allow the Whitewater system rate condition to be terminated. We agree this special rate condition is functioning as intended, to protect ratepayers from harm if actual costs of the Whitewater system exceed forecasted costs, and that this condition should continue in place for the time being.

19. Cost Savings Resulting from GCA Area Consolidation

189. The Recommended Decision finds the Partial Stipulation and Settlement among Black Hills, Staff, and EOC with respect to the GCA area consolidation is in the public interest and therefore approves this portion of the settlement. The settlement provides for consolidation of seven GCAs into four GCAs by combining the BHGU and Arkansas Valley GCAs into a Central GCA, and combining the North Eastern, North Central, and Southwestern GCA regions into a North/SW GCA.

[145] Black Hills Exceptions p. 56.

190. The Recommended Decision notes the OCC only supports the GCA area consolidation if the Company monetizes the resulting cost savings and includes them as a known and measurable *pro forma* adjustment in the Company's revenue requirement. The Recommended Decision notes the OCC did not state that such consolidation is contrary to the public interest.

a. OCC Exceptions

191. In its exceptions, the OCC requests that the Commission require an adjustment for cost savings that result from the GCA area consolidation. The OCC objects that the Recommended Decision denied without explanation its request to include the cost savings as an adjustment to the Company's revenue requirement. The OCC points to the Company's testimony that there would be reductions in noticing requirements and avoided labor hours if the GCA areas were consolidated.[146] The OCC requests, in the alternative, that the Commission order such cost savings be reflected in the Company's GCA amount or reverse the ALJ and reject this portion of the Partial Stipulation and Settlement and thus preserve the *status quo* of GCA areas and filings.

b. Black Hills Response to OCC Exceptions

192. In response to the OCC's exceptions, Black Hills claims the OCC's recommended adjustment is neither quantifiable nor certain. The Company represents that, in addition to a reduction in the number of legal notices that would need to be published, reducing the number of GCA filings under the Company's proposed GCA area consolidation would result in approximately 422 less labor hours per year devoted to GCA filings by the Company's regulatory administration staff. However, the Company anticipated there would be no immediate labor cost savings because its regulatory administration personnel are salaried employees thus any time

[146] OCC Exceptions p. 20 (citing Hrg. Exh. 300 (Skluzak Answer) at 38:8-12).

saved on GCA matters would be spent instead on other Black Hills matters. The Company acknowledges that increased efficiencies could eventually result in the Company being able to defer hiring new staff. The Company adds that, likewise, the fact it may incur less GCA noticing costs due to less annual GCA filings does not necessarily mean the Company's total annual noticing costs will be reduced.

c. Findings and Conclusions

193. We deny the OCC's exceptions requesting that the Commission require an adjustment for cost savings that result from the consolidation of the GCA areas. We agree with the arguments raised by Black Hills that the GCA area consolidation will not likely result in an immediate and certain cost savings for the Company. We conclude that, although the GCA area consolidation may result in minor cost savings over time, it is not appropriate to make an adjustment to the Phase I revenue requirement in this Proceeding.

20. Synergy Regulatory Asset

194. In this Proceeding, Black Hills estimated approximately $36 million in overall savings from the SourceGas acquisition. Of that amount, Black Hills contends that $2 million accrues to the Company and is now embedded in its test year cost of service. Black Hills took the position in this Proceeding that it had made no representation that the synergies would translate into a rate reduction for ratepayers. Black Hills maintained that, instead, it had expected synergies would offset inflationary effects on utility costs and help defer rate filings. Black Hills therefore opposes any imputation of these cost savings into the revenue requirement.

195. The Recommended Decision finds that, contrary to the Company's position, Black Hills did state in the SourceGas acquisition, Proceeding No. 15A-0667G, that the resulting

savings would lead to a rate reduction for ratepayers.[147] The Recommendation Decision states it appears that no clear rate reduction has materialized and Black Hills has instead put forward a case in this Proceeding that a rate increase is warranted for a significant portion of its ratepayers. The Recommended Decision raises concern about the evidence of Black Hills Corporation's strategy of acquisitions followed by delayed rate reviews that ensured shareholders, not ratepayers, benefitted from the cost-savings. The Recommended Decision concludes the result is that ratepayers have not seen the promised savings and will now suffer the consequences of the delayed capital investment, particularly in the legacy SourceGas rate area BHGD Rate Area 2. The Recommended Decision concludes it would "defy logic" to conclude that Black Hills Corporation did not know or should have known of these needed capital investments and factored that into the acquisition price.[148]

196. In this context, the Recommended Decision denies Black Hills' proposal to amortize a "Synergy Regulatory Asset" of $880,484 over two years. This asset consists of severance costs resulting from a reduction in a headcount of 152 employees in the 18 months following the SourceGas acquisition. The severance costs were allocated by Black Hills Corporation to Black Hills and then reduced 50 percent, pursuant to the settlement in the SourceGas acquisition Proceeding No. 15A-0667G. Through rebuttal testimony, Black Hills states that as part of that settlement, the Company was permitted to establish a regulatory asset to collect the cost of severances resulting from the acquisition. Black Hills states such severance costs were to be included in this rate case for recovery and amortization. Black Hills reasons

[147] Recommended Decision ¶ 76.

[148] Recommended Decision ¶ 85.

that, because the Commission approved the settlement, the Commission has approved recovery over a two-year amortization period.

197. The Recommended Decision agrees that the Commission approved, in principle, amortization of the regulatory asset for severance costs as set forth in paragraph 10.C. of the settlement in the SourceGas acquisition Proceeding No. 15A-0667G.[149] The Recommended Decision states the plain language in the settlement authorizes amortization over two years for purposes of determining the revenue requirement. The Recommended Decision, however, agrees with the concerns raised by Staff and the OCC about recovery extending beyond the two-year amortization period and therefore requires Black Hills to make a compliance filing after the end of the two-year amortization period to halt recovery and remove the "Synergy Regulatory Asset" from rates.

a. Black Hills Exceptions

198. In its exceptions, Black Hills explains that the Company proposed in its rebuttal testimony an alternative to address the termination of the amortization of the "Synergy Regulatory Asset" through the multi-use cost tracker described above. Black Hills requests that the Commission reject the Recommended Decision's requirement that the Company make a compliance filing and accept the Company's agreement that the associated amortized amounts be included in the Company's "overall" proposed accounting tracking mechanism (that we deny in this Decision) to ensure there is no under- or over-recovery of costs when the amortization ends. Black Hills argues this offer represents a material concession by the Company in that this is inconsistent with the terms of the settlement in Proceeding No. 15A-0667G.

[149] Proceeding No. 15A-0667G, Decision No. R16-0058 (issued January 22, 2016).

b. **Findings and Conclusions**

199. We deny these exceptions and affirm as reasonable the Recommended Decision's directive to the Company to make a compliance filing to reduce rates after two years. We find the discrete rate reduction at the end of the amortization period should not be subject to the uncertainties of deferred accounting associated with pension, retiree medical expenses, and property tax expenses. The elimination of the "Synergy Regulatory Asset" should thus not be addressed by the combined tracker proposed in Black Hills' exceptions.

200. In our decision referring this Proceeding to the ALJ, we directed the ALJ "to examine whether the consolidation of Black Hills/Colorado Gas Utility Company Inc. and Black Hills Gas Distribution, LLC resulted in efficiencies and cost savings as reflected in the overall annual revenue requirement of $73.2 million at issue in this Proceeding."[150] We conclude that the ALJ properly places the "Synergy Regulatory Asset" as the top of the series of his analyses in the Recommended Decision. In that initial analysis, he contradicts the Company's witnesses in this Proceeding by reminding them that Black Hills had presented the SourceGas acquisition to the Commission as leading to a savings-driven rate reduction for ratepayers. At a high level, the ALJ identifies Black Hills Corporation's strategy of acquisitions followed by delayed rate reviews to ensure that shareholders, not ratepayers, receive the benefits of any cost savings. And the ALJ juxtaposes that strategy—now clearly revealed in this Proceeding—against the consequences of the settlement terms that Black Hills negotiated to its benefit with Staff and the OCC regarding rate case stay out and the request to recover severance costs through rates.

[150] Proceeding No. 19AL-0075G, Decision No. C19-0194 ¶ 18 (Feb. 22, 2019).

201. We conclude the ALJ satisfied the Commission's directive to examine the financial benefits to ratepayers of the SourceGas acquisition. It appears no rate reduction has materialized for ratepayers due to the acquisition. Rather, the disaggregation of the Company's overall revenue requirement instead reveals the possibility that the three-year rate case moratorium advanced in the acquisition proceeding as a benefit to ratepayers may have instead delayed significant rate relief due to most of Black Hills' customers in adherence of basic cost of service principles.

21. Sharing of Anticipated SourceGas Acquisition Tax Savings

202. The Recommended Decision denies Staff's proposal to require Black Hills to split between shareholders (10 percent) and ratepayers (90 percent) the anticipated $24 million in income tax savings to accrue to Black Hills Gas Holdings, LLC, an affiliate of Black Hills, as a result of the SourceGas acquisition over the next 15 years. Staff advocated that shareholders should retain 10 percent of the tax benefits as a reward for engaging in tax planning that benefits ratepayers, but ratepayers should receive the remaining 90 percent. The Recommended Decision finds the record in this Proceeding does not support Staff's sharing proposal. The Recommended Decision concludes that Staff failed to persuasively argue that ratepayers receiving gas service from Black Hills should receive tax savings accruing to a different entity from which those ratepayers receive their gas service.

a. Staff Exceptions

203. In its exceptions, Staff requests that the Commission reverse the Recommended Decision and require Black Hills to share a significant portion of the anticipated $24 million in income tax savings with ratepayers.

204. Staff reasons that Black Hills Corporation exclusively benefited from the tax savings due to the way the SourceGas acquisition was structured using a subsidiary holding company. Staff ties the tax benefits accruing in the first instance to the holding company to Black Hills Corporation's strategic initiatives to grow its earnings through acquisitions and by purposely avoiding rate reviews that would cause sharing of savings with ratepayers.

205. Staff posits that, if the Commission agrees with the Recommended Decision that Staff did not provide sufficient argument to support its sharing proposal, then the Commission should revisit this issue after reversing the ALJ's denial in Interim Decision No. R19-0655-I[151] of Staff's motion to compel Black Hills to produce certain documents relevant to this issue. Staff challenges that the Deloitte & Touche report and related documents requested by Staff, but claimed as protected by the Company, could have provided evidence to persuade the ALJ that the income tax savings resulting from the acquisition measurably and purposefully benefitted Black Hills. Staff argues that its discovery request was for more than a single "memo" and there could be other reports and documents that describe the tax strategies to maximize benefits from the SourceGas acquisition, even if the consultant report itself is protected from discovery. Staff also argues the mere fact of a future tax audit should not be a blanket protection from disclosing all documents regarding income tax strategies. Finally, Staff argues, even if the documents were prepared in anticipation of litigation, they are discoverable because Staff has a substantial need for these documents and Black Hills is the only party to this Proceeding with access to information regarding what was planned regarding income tax savings. Staff offers that the Commission could order additional hearings once the documents are produced and the Commission can gauge their possible evidentiary value.

[151] Decision No. R19-0655-I was issued in this Proceeding on August 1, 2019.

b. Black Hills Response to Staff Exceptions

206. In response to Staff's exceptions, Black Hills reiterates that the $24 million in anticipated income tax benefits derive from a portion of the non-deductible goodwill originally recorded as part of the SourceGas acquisition becoming tax deductible through future amortizations over the next 15 years. According to the Company, this goodwill is recorded at a holding company level and thus does not affect Black Hills' books and records. Black Hills argues that this benefit is exclusive to shareholders because it derives directly from goodwill and because such goodwill is not included in rate base or reflected in Black Hills' revenue requirement pursuant to the settlement in the SourceGas acquisition in Proceeding No. 15A-0667G.

207. Black Hills contends that Staff's reasoning for imputing 90 percent of the tax benefit to ratepayers as a credit is not grounded on any ratemaking principle but rather on Staff's own reassessment of the "no net harm" standard applied in the SourceGas acquisition Proceeding No. 15A-0667G.

208. Black Hills goes on to argue that there is no evidence showing, had the Company filed a rate case within the first three years following the acquisition, that the acquisition transactions would have resulted in a rate decrease. Black Hills adds that Staff fails to explain why it was unreasonable for the Company to not make capital investments in its newly acquired systems to the extent such investments could be temporarily deferred until after the integration was complete and the new organization finalized. Black Hills notes that legacy SourceGas customers received $800,000 of bill credits associated with the terms of the settlement in Proceeding No. 15A-0667G. Black Hills contends that customer costs associated with the acquisition transactions cannot be viewed in isolation but rather in conjunction with the

offsetting customer benefit from being spared rate increases for years. Finally, Black Hills makes two technical objections, arguing first that the allocation of tax benefits to ratepayers would likely be viewed by the Internal Revenue Service as an indirect income tax normalization violation, and second, that a greater percentage of rate base is being financed through ADIT than in prior rate cases for the separate utilities before the acquisition.

209. In response to Staff's request that the Commission overturn the ALJ's Interim Decision No. R19-0655-I denying Staff's motion to compel discovery of the Deloitte & Touche documents, the Company argues such documents: (1) are in the exclusive possession, custody, and control of Black Hills Corporation, and not the Company; (2) constitute attorney work product and attorney-client communication privileges and are therefore not subject to discovery; and (3) are further subject to protection from an accountant-client privilege. Black Hills states that, even assuming the information sought could be relevant, the Company provided in this Proceeding income tax and accounting witnesses who addressed the basis for the $24 million tax benefit, the resetting of a portion of the Company's ADIT balances resulting from the SourceGas acquisition, the income tax effects of the Tax Cuts and Jobs Act, and income tax normalization violations. Black Hills charges that Staff's renewal in exceptions of its motion to compel "is nothing more than an extension of its fishing expedition in this proceeding."[152]

c. BGVA Exceptions

210. In its exceptions, BGVA asks the Commission to address the questions surrounding the tax savings separately from any decision regarding the Company's proposed DSIR. BGVA contends the ALJ erroneously linked two unrelated issues in rejecting Staff's tax sharing proposal. BGVA appears to support the relief sought by Staff's exceptions regarding the

[152] Black Hills Response to Exceptions p. 31.

proposed sharing. BGVA does not object to consideration of the DSIR in a new proceeding as required by the Recommended Decision.

d. Findings and Conclusions

211. We deny Staff's exceptions requesting that the Commission require Black Hills to share with ratepayers the income tax savings resulting from the SourceGas acquisition. We are cautious that implementation of such a directive as requested by Staff would be an extraordinary extension of ratemaking. We therefore deny these exceptions and uphold the Recommended Decision.

212. We share the ALJ's concerns about Black Hills Corporation's strategy acquisitions followed by delayed rate reviews to ensure shareholders receive the benefits from the acquisitions. We also share the ALJ's doubts of whether Staff and the OCC would have reached settlement with Black Hills in the SourceGas acquisition Proceeding No. 15A-0667G had they known more about how the acquisition strategy would play out over time for Colorado ratepayers. However, we find the ALJ has carefully considered the merits of the Company's numerous requests for rate relief in this Proceeding without intent of punishment, and the Commission will do the same. And while the no net harm standard remains relevant in this Proceeding, we find it unnecessary to use the rate setting process in this rate case to correct any revealed shortcomings of the settlement approved in Proceeding No. 15A-0667G or to rebalance the "no net harm" findings the Commission made in the past.

213. We also deny Staff's exceptions requesting that the Commission amend Interim Decision No. R19-0655-I to compel Black Hills to produce the Deloitte & Touche report and related documents requested by Staff. We affirm the Recommended Decision properly finds

these documents protected work-product[153] and that Staff has not shown a substantial need that would overcome this protected status.

214. Staff's arguments in exceptions do not provide good cause to reverse the ALJ's determinations. Staff's main argument in exceptions is that, because Black Hills used the term "memo" in its response to Staff's motion to compel, there may be discoverable related documents, even if the consultant report itself is protected. Although Black Hills' response to Staff's motion to compel refers at times only to the "memo," reading the response as a whole makes clear that the Company claims protection for the memo and related documents. Likewise, we find Staff's challenge that the fact of a future tax audit should not provide blanket protection ignores the explanation by Black Hills that "[Black Hills Corporation] is routinely audited by the IRS" and "[d]ue to the complexity and significant dollar amount associated with the tax issues surrounding these restructuring transactions, the Company expects to have to defend its position with the IRS in an upcoming audit."[154] Finally, Staff argues these documents are discoverable because Staff has a substantial need and Black Hills is the only party with access. Yet Staff failed to make these arguments to the ALJ. Now on exceptions, with the record closed, we find Staff's claim of need unpersuasive. As Black Hills raised in its response to Staff's motion to compel, and again in its response to exceptions, the Company provided direct and rebuttal testimony through Company witnesses on the tax impacts related to Black Hills. Staff suggests these documents may still be useful toward Staff's case and in future related proceedings, but that would require re-opening the record and possibly additional hearings on the potential that

[153] The applicable Colorado Rule of Civil Procedure 26(b)(3) (2012) provides that a party may discover documents prepared in anticipation of litigation or for trial by that party's representative, including the party's attorney, consultant, or other agent, only upon a showing that the party seeking discovery has a substantial need of the materials in the preparation of the case and is unable without undue hardship to obtain equivalent materials by other means.

[154] Black Hills Response to Staff Motion to Compel ¶ 32.

these documents "may still be useful" to Staff's case. We will not delay resolution of this rate case so that Staff can continue to argue this single issue.

22. Required Updated Calculations and Bill Impacts

215. Through Ordering ¶ 9 of the Recommended Decision, the ALJ requires Black Hills to file with any exceptions, an updated revenue requirement, updated CCOSSs, updated GRSA calculations, and corresponding bill impacts for each of the three existing base rate areas that reflect the determinations made in the Recommended Decision.

216. In its exceptions, Black Hills disputes whether a Recommended Decision can require the filing of additional information with a party's exceptions filing; Staff's exceptions also raise the issue of whether the Company properly complied with this provision of the Recommended Decision.

217. We clarify that a party's ability to file exceptions to a recommended decision is conferred by statute and therefore cannot be modified through a condition imposed in a recommended decision. Section 40-6-109(2), C.R.S., states plainly that parties may file exceptions to the ALJ's recommended decision. Further, a recommended decision, and the ordering paragraphs therein, remain recommendations of the ALJ until they become a decision of the Commission, through operation of law if no exceptions are filed, or through adoption by the Commission. In this case, the Recommended Decision was stayed by the filing of Black Hills' and intervenors' exceptions.

218. We make these findings for clarification only. We agreed with the ALJ's intent that these updated calculations should be filed in this Proceeding to assist the Commission in addressing the filed exceptions. We already resolved this matter by issuing a separate Commission decision, Interim Decision No. C20-0123-I, issued February 21, 2020, requiring

the Company to file the information sought by Ordering ¶ 9 of the Recommended Decision, and the Company timely complied. The Company's filing in response to Interim Decision No. C20-0123-I is discussed above.

II. ORDER

A. The Commission Orders That:

1. The effective date of the tariff sheets filed by Black Hills Colorado Gas, Inc. (Black Hills) on February 1, 2019 under Advice Letter No. 1, as amended, is permanently suspended and shall not be further amended.

2. The tariff sheets filed under Advice Letter No. 1 are permanently suspended and shall not be further amended.

3. The exceptions to Recommended Decision No. R19-1033, issued by Administrative Law Judge Conor F. Farley in this Proceeding on December 27, 2019 (Recommended Decision), filed by Black Hills on January 16, 2020, are granted, in part, and denied, in part, consistent with the discussion above.

4. The exceptions to the Recommended Decision filed by Staff of the Colorado Public Utilities Commission on January 16, 2020, are granted, in part, and denied, in part, consistent with the discussion above.

5. The exceptions to the Recommended Decision filed by the Colorado Office of Consumer Counsel on January 16, 2020, are granted, in part, and denied, in part, consistent with the discussion above.

6. The exceptions to the Recommended Decision filed by Energy Outreach Colorado on January 16, 2020, are denied, consistent with the discussion above.

7. The exceptions to the Recommended Decision filed by Bachelor Gulch Village Association on January 16, 2020, are denied, consistent with the discussion above.

8. Black Hills shall file modified rates and tariff sheets within a consolidated Colo. PUC No. 1 consistent with the terms of this Decision and the Recommended Decision, as adopted or modified through this Decision.

9. The Colo. PUC No. 1 compliance tariff filing shall include tariff sheets and rate schedules that continue the implementation of Black Hills' three separate base rate areas and set forth the existing Commission-approved base rates for each of the three base rate areas to be modified by three new separate General Rate Schedule Adjustment (GRSA), consistent with the Phase I determinations in this Decision and in the Recommended Decision, as adopted or modified by this Decision.

10. The Colo. PUC No. 1 compliance tariff filing shall be filed on a consolidated basis, provided that the tariff book includes the three existing base rate area schedules and the newly established GRSA riders for each base rate area.

11. The Colo. PUC No. 1 compliance tariff filing shall reflect the settled terms of the Partial Stipulation and Settlement Agreement among Black Hills, Staff of the Colorado Public Utilities Commission, and Energy Outreach Colorado regarding: (i) consolidation of gas cost adjustment areas; and (ii) late payment charges.

12. The Colo. PUC No. 1 compliance tariff filing shall reflect the terms of the Partial Stipulation and Settlement Agreement between Black Hills and AM Gas Transfer Co.

13. Black Hills shall file the Colo. PUC No. 1 compliance tariff filing in a separate advice letter proceeding on not less than 21 days' notice.

14. Black Hills shall file a Phase II rate case within six months from the Mailed Date of this Decision, consistent with the discussion above.

15. Black Hills shall file for approval of a Distribution System Integrity Rider no later than six months from the Mailed Date of this Decision, consistent with the discussion above.

16. Black Hills shall file for approval of construction allowances no later than 30 days after a final Commission decision in the Phase II rate case ordered by this Decision, consistent with the discussion above.

17. 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.

18. This Decision is effective upon its Mailed Date.

B. ADOPTED IN COMMISSIONERS' DELIBERATIONS MEETING April 14, 2020.

(S E A L)

ATTEST: A TRUE COPY

Doug Dean

Doug Dean,
Director

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

JEFFREY P. ACKERMANN

JOHN GAVAN

MEGAN M. GILMAN

Commissioners