

Councilmember Cowles and other members of Council:

Please see responses to your questions posed in your July 14 memo to city staff. Hopefully this adequately addresses the issues you raised.

The valuation of the Distribution System failed to include the value of the meters. Is this true? If so, why did we not include that cost, and how much is it?

Answer:

A cost associated with the purchase of meters was not included in the acquisition figures. Xcel will not grant access to current distribution system data. Without access to the distribution system, there is not enough information or consistent data to derive an estimate of meters, whether energy or interval, single-phase or three-phase, secondary, primary or transmission voltage level.

To defray potential meter costs, the asset valuation does include an estimate of the Xcel service yard on 63rd Street. Although the service yard is located outside of Boulder's city limits and, technically double-counted in the municipal utility's \$32.5 million start-up cost, RBI and staff thought it would be prudent to include quantifiable assets in the valuation in order to offset potential unknowns such as the meters.

Bob Bellemare estimated the value of the meters at about \$5 million. RBI omitted the meters but included the service yard with an estimated RCNLD of \$7.2 million. Implicitly, the meters have been accounted for as the service yard may end up being excluded from the asset valuation.

Additional points:

- Xcel reports for 2009 a total of 47,095 accounts (ref.: Boulder 2009 Annual Report) but 119,444 meters (ref.: 2000 - 2010 Electric Distribution Trend Sheet, includes active and inactive meters). The discrepancy commands further investigation.
- Of the 47,095 accounts, 7,820 are commercial accounts. It is unknown at this time how many are served by primary voltage (more expensive meters than secondary voltage).
- Of the 39,260 residential accounts, approximately 60% have smart-meters, which would be captured in the SmartGridCity acquisition cost.

The FS failed to account for the benefit that Boulder receives from Xcel's tax payments, specifically:

Property Taxes paid to BVSD	\$2,778,644
Sales Tax paid to City	\$4,180,397
Use Tax paid to City	\$96,736

What would be the plan of the Muni to compensate for these amounts that would be lost to the City and to BVSD?

Answer:

The amounts for PILOT (payment in lieu of taxes) and P3 equal approximately \$6.5 million annually in the initial year and increase thereafter. There are no amounts included in the model specifically for Property Taxes paid to BVSD. While noting that there was enough money available, Staff informed Council on June 14 that it did not specifically account for the amount of property tax paid because it would be the decision of the Council (or other Utility Board) how it wanted to handle that aspect of monies now being paid by Xcel Energy. Staff did, however, recommend that the amounts be covered.

He argued that the method used to calculate the cost of acquiring the Distribution System (DS) by a court in condemnation would include a value for it as a going concern. The DS is not a going concern by itself. However, he argues that discounting the cash flow to present value rather than assessing the cost and accumulated depreciation would be the more likely way for a court in condemnation to value the DS. If discounted cash flow method were used, would it not substantially increase the cost to purchase the DS? Is there precedent for predicting which method a court would use in coming up with a final value?

Answer:

As a general matter, in Colorado “going concern value” is not a compensable element in eminent domain proceedings. The “measure of damages” in an eminent domain proceeding is the “fair market value” of the property taken in light of the property’s highest and best use. Going concern damages are permitted when a municipality condemns an electric cooperative’s distribution system. There is a different scheme in Colorado that applies to cooperatives which would not apply directly to municipalization of the electric distribution facilities of an investor-owned utility. It is fair to assume, however, that Xcel Energy will argue any and all methodologies that provide the highest value.

He argued that separation costs would be substantially more than \$15MM because of county enclaves within the City’s boundaries. How would the

enclaves be treated? Clearly, it makes no sense for Xcel to set up parallel infrastructure to serve the enclaves. But could they insist that they serve the enclaves, and thus force us to pay for parallel infrastructure to serve them?

Answer:

Should the city choose to condemn Xcel Energy's distribution facilities, the City would select which components of the system it wants to acquire. Separation costs are those costs that Xcel Energy will necessarily incur to separate its remaining electric distribution system from that of the City's newly acquired electric distribution system.

The city has had reports from electric utility engineers whom have reviewed the physical electric distribution system that separation costs would not be significant because of the nature of the City's physical boundaries. Xcel Energy, through UtiliPoint, is apparently suggesting otherwise. Importantly, until the boundaries are drawn and the utility engineers from both sides engage, there is simply no way to estimate accurately what amounts will be required to "separate" the two systems.

When determining the facilities the city wants to acquire, engineers will balance the total cost of acquiring certain facilities (e.g., asset value plus separation costs) versus the cost of building certain assets and/or decreasing the facilities to be acquired. This analysis will be done initially at filing of any condemnation action and then refined later during the actual prosecution of the condemnation action.

Xcel's consultant argues that the FS fails to include \$38.5MM in solar rebates and \$5.5MM in DSM rebates in 2010 in calculating the cost of the DS. Is that true? How would the repayment of these rebates be handled by a Boulder Muni?

Answer:

Staff considered the possibility that Xcel would require the repayment of rebates offered to its Boulder customers and provided city council with a "worst case scenario" figure for these possible repayments. (REC payments, which are made on an annual basis, would not have the same repayment issue.) However, until staff is able to obtain specific information from Xcel, it will be unable to fine tune its analysis of the repayment issue to derive a more realistic figure. The Boulder municipal utility could pay these rebate repayments on behalf of the individual who received the rebate. This repayment program would be similar to other demand side management programs the city funds through the CAP tax.

Have we priced into the costs of operating a Muni the annual cost of DSM rebates in the future that would provide incentives similar to existing incentives for people to install energy conservation measures?

Answer:

Yes. As mentioned above, the amounts for PILOT (payment in lieu of taxes) and P3 equal approximately \$6.5 million annually in the initially year and increase thereafter. The cost model includes 5% (in the original model) for the public purpose fund and 4% for PILOT. Staff is running additional scenarios to increase these and determine the impact. In addition, the cost model was programmed to retain \$5 million in reserves (increasing with inflation) that could be earmarked for other costs such as an increase in incentives.

A concern that I would like to have addressed has to do with energy supply, hedging energy costs and stranded assets. Currently, there is excess generating capacity in our region. That means that it is a good time to be, like the City of Boulder, a purchaser of power.

Answer:

Currently, yes. The prices in the market are currently depressed because of the low price of natural gas and the excess of hydropower in the Northwest has depressed overall energy prices, even in our region. Of course, these market conditions can and will change.

Does that excess current capacity in the system strengthen Xcel's argument that they are entitled to stranded costs?

Answer:

Not necessarily. The current market circumstances are a "snap shot" of the market conditions as they exist now. The determination of stranded costs is complicated and FERC has not reviewed many such determinations; none for some time. The determination of stranded costs involves whether Xcel Energy reasonably invested in generation in anticipation of having Boulder as a customer, and if so, how long is it a reasonable assumption. Staff believes the City has some strong arguments, among which is that Xcel Energy should not have anticipated having the City as a customer.

It may also be interesting to consider the legal issue this may cause. If Boulder pays Xcel the SCO resulting from excess capacity then a Boulder utility should, theoretically, be entitled to this very excess capacity from

Xcel at no cost. Xcel could not collect a stranded cost and then sell Boulder the same capacity a second time.

Would a Muni, purchasing power on the open market, be at more disadvantage than Xcel in hedging against the price volatility of energy? Another way of phrasing the question would be this: to what extent would a Muni be more subject to purchases on the spot markets and less able to hedge against short term price hikes than Xcel?

Answer:

No. A municipal utility would not be at a disadvantage. While a utility (whether Xcel or a muni) does a portion of its energy trading on the spot market (day-ahead and real-time markets), the muni can hedge itself against energy price volatility (both electricity and gas) by purchasing futures.

In addition, Xcel's advantage is that it has a larger fuel mix than the City and can use coal as a hedge against gas/oil prices. This "advantage" may disappear if a carbon tax is enacted. The City also has plans for localization which will reduce transmission expenses over time. The City may be able to coordinate its purchases with other public utilities to assist it in obtaining better deals.