

DECEMBER 2017

PUBLIC UTILITIES FORTNIGHTLY

"In the Public Interest"

Brien Sheahan, Bob Frenzel
Marty Lyons, Drew Marsh
Barbara Nick, Chris Gould
Dave Christian, Dave McCurdy
Don Clevenger, Bailey Bearss



Connecticut Takes Command at NARUC and NASUCA

NASUCA's Elin Swanson Katz
and NARUC's Jack Betkoski,
Both from the Nutmeg State

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Leadership Lyceum Podcast

Balanced Leadership in The Heartland



Tom Linquist, Leadership Lyceum,
with Barbara Nick,
CEO, Dairyland Power Cooperative



Barbara Nick became President and CEO of Dairyland Power Cooperative in December 2014. In her thirty-seven-year career in the electric and gas industry, Nick has gained a wide range of professional experience, from investor-owned utilities to her current position in a co-op. She's uniquely qualified to provide critical insight into the differences between the two and the things they have in common.

Nick graciously welcomed us into her office at Dairyland headquarters in La Crosse, Wisconsin, for a discussion about co-ops, IOUs and Green Bay legend Vince Lombardi.

Tom Linquist: What is the history behind the formation of Dairyland Power Cooperative?

Barbara Nick: Dairyland Power Cooperative is a generation and transmission power cooperative. We have twenty-four distribution cooperatives who buy power from us under a long-term wholesale power contract that extends to 2055.

We were formed by our member cooperatives in 1941, encouraged by President Franklin Roosevelt's Rural Electrification Administration to help bring electricity to rural America.

Dairyland was formed to provide centralized power and transmission. Many of the same members are still with us. During that pre-World War II period, the IOUs didn't have enough power or transmission to provide the power to rural areas, or our members couldn't get what they thought was a reasonable price from them. The cooperatives banded together to control their destiny.

Our members serve in five states: a very small part of Michigan, a large portion of western Wisconsin, plus a little bit of Minnesota, Iowa and Illinois. Through our distribution members, we serve about six hundred thousand end members.

We have nearly thirty-two hundred miles of transmission line. Now we have about one and half billion dollars in assets. Once finished with our combined cycle renewable-enabling natural gas unit project in Superior, Wisconsin, we'll have about two and half-billion dollars in assets for our twelve hundred-megawatt system.

Tom Linquist: Tell us more about the renewable-enabling natural gas project.

Barbara Nick: It's the Nemadji Trail Energy Center. The project is a partnership with Minnesota Power, a subsidiary of ALLETE, Inc. For both companies, this is critical. It demonstrates a real partnership and collaboration between a cooperative and an IOU.

We both want to diversify our portfolios in a measured and prudent way. We are both adding wind and solar. We are both migrating away from our dependence on coal. We need an intermediate unit. Something that will enable our reliability. Meet our customers and members' cost objectives.

The natural gas unit is sized right. With the two of us joining together, we get the economies of scale. We have leading edge technology with the required ramp and heat rates.

The site is very valuable. It's Minnesota Power's site, but it's adjacent to gas pipelines owned by Northern Natural and Great Lakes. The site is about six to seven miles away from a 345-kV Arrowhead-to-Weston transmission line.

I've worked with the folks at Minnesota Power for decades. I tell them that while they're an IOU, they have the heart of a co-op.

I know their CEO, Al Hodnik, well. I have a great deal of respect for him. He is president of the Association of Edison

I've worked with the folks at Minnesota Power for decades. I tell them that while they're an IOU, they have the heart of a co-op.

Illuminating Companies. Very well-respected in the IOU industry. Also in the G&T family.

Several of us have partnered with Minnesota Power. We know Al and the ALLETE team to be honorable partners. They are trying to do what is right for their customers as well as their shareholders. In the cooperative model, our mem-

bers are both customers and shareholders. In the long term, we are meeting the needs of our future members.

We don't do it on the backs of our current members. They are also quasi-owners. I say quasi, because it gets complicated when you look at our debt and equity structure. We do borrow money from the Rural Utility Service.

Tom Linquist: Superior is a more densely populated, urban area. You are co-developing this generation facility with an adjacent IOU. Are these partnerships with IOUs a common practice?

Barbara Nick: I know of other G&Ts that partner with their local investor-owned utilities. We've been collaborating with our neighboring IOUs for decades.

At Dairyland, we have also collaborated with Xcel Energy on transmission. The recent transmission buildup of the CapX2020 here in the region, that's a collaborative of investor-owned utilities, public power, co-ops and independent municipalities.

A lot of the cost sharing agreements on transmission were partnerships and collaborations among neighboring utilities, whether they were municipals, public power, cooperatives or IOUs.

Dairyland is a partner with Wisconsin Public Service



(a subsidiary of WEC) in the Weston 4 power plant. Dairyland is one third owner of that coal facility in central Wisconsin.

I worked with the people at Wisconsin Public Service for thirty-three years. I attest to their dedication to their core mission in service to their customers.

What's core to all our missions and to our business model is safe, reliable, affordable and sustainable generation and delivery of energy.

Tom Linquist: The co-ops, public power, and the investor-owned utilities have their own trade associations. Where do they all come together and collaborate across the boundaries between them?

Barbara Nick: This is my thirty-seventh year in the industry. I worked the first thirty-three years, a good portion of my career, for the IOUs. I sold bulk power to the municipals and cooperatives in the adjacent areas one or two wheels away from our service area.

The IOUs had a view that municipals and cooperatives were the dark side. Now I'm in the co-op world where the IOUs are seen as the dark side.

We have more to gain by working together. Our core business is the same. We'll gain more by collaboration than by competition. Even among the IOUs, there's competition.

There could be competition between co-ops. Our greater interest is in national security, the grid; cybersecurity, grid security. We're all banded together on anything to do with grid security. The same applies to power restoration.

Any time there's a disaster, it doesn't matter if you're a co-op, public power or an IOU. When the lines are down, we are all there helping each other restore power to our customers and members. The differences are more cosmetic than substantive.

Tom Linquist: You refer to "the dark side" with a sense of humor. Can you explain the negative association?

Barbara Nick: The stereotypes probably fall more into the

realm of psychology and sociology than engineering and accounting.

There are natural advantages and disadvantages in each model. The cooperatives have a distinct disadvantage. They are generally in sparsely populated rural areas with one, two, three, four, maybe six members per mile.

The IOUs are historically in very populated urban areas. As urban sprawl migrated into the rural areas, the urban power provider, the IOU, began to annex those areas away from the co-ops. The co-ops are always left with the challenge of operating in those

very sparsely populated areas.

Each entity wants to do what's best and to serve. It creates a little bit of competition or at least a rivalry. Some of that is explained by the differences between our financial structures. IOUs go to the equity markets. They earn a return based on their earnings per share.

Their business, and how they bring value to their shareholders, is a different model. The cooperatives are not-for-profits. Their access to capital is different. They're generally less capitalized in comparison to the IOUs, at least at the G&T level.

An IOU might say co-ops and munis have an advantage because of tax exempt financing or municipal bonding capacity. A co-op would say that IOUs

have the advantages because they can easily tap the capital markets. They draw talent from great population centers. They have great resources available to them because they generally tend to be bigger.

Tom Linquist: You and I were talking about a hypothetical case of a rural IOU and posing a theoretical question about the company. Since it is a rural utility, would it serve better as a cooperative than as an IOU?

Barbara Nick: At the end of the day, we're all bound by our obligation as a monopoly to serve the public interest. The idea was that you would have a franchise territory, meaning exclusive rights to serve in return for acting in the public interest.

That's what the public service commissions are charged to do. They are the proxy for serving in the public interest, especially

when you need to go to the capital markets. All of us are grounded in what's doing right, in the public interest.

Apply that to a very small IOU that must stand on its own, versus a very large IOU that may serve large urban areas along with very distinct rural areas. The large IOU has the benefit of being able to socialize their rates.

When you take away that scale and the ability to socialize rates across a large diverse service area, then you have an entity that has a huge capital burden, lots of miles and very few customers.

It's hardly sustainable. Say you add on the cost of capital in an IOU structure, if it's ten percent, twelve percent, whatever the rate of return is that your shareholders expect. It's a different business model than what you are doing as a not-for-profit. Any margins go back to some kind of patronage or a return to your members over time.

Tom Linquist: Would it be possible to convert an IOU into a cooperative?

Barbara Nick: That's where you would have to understand the underlying cost structure. At the end of the day, we want to be able to provide affordable electricity.

If you don't have a lot of units or members or customers to spread the costs over, figuring out how you do that is tricky. As you get more expensive, you drive more and more of your customers out of business.

As you have less business, you have fewer customers. Then it's a death spiral. Turning the cycle in the virtuous direction, low rates are an ideal economic development catalyst. With low rates, you can attract industry.

As you get more industry that drives the economy and living standards, you get more customers, more members. Then you grow. You are able to spread your fixed costs over more customers. To spin in that virtuous direction, you must figure out how to do that.

Tom Linquist: Is there a common objective that's important at all times, beyond providing safe, reliable, affordable, sustainable energy and helping your members grow? Or are you constantly balancing the interests of the members?

Barbara Nick: At the most fundamental level, their interests are aligned. In the co-op world here in Wisconsin, our rates are not regulated by the public service commission, although we certainly follow their rules and have a great deal of respect for that body. Our rates are set by our board. The board is independently elected by our members.

Do they have different interests? Yes. But they all agree that we are going to share in this pot of expenses, fixed costs, our generation and our transmission because this is what they formed Dairyland to do.

When it comes to how you divide up the fixed and variable costs – that is where it gets dynamic. For those who really love rate design, what do you charge to your demand rate? What



Barbara Nick with Roger Tjarks,
Board Chairman for Dairyland
Power Cooperative

The impact of energy efficiency technology has been huge. When you are capital intensive, that means a lot.

charge goes to energy utilization?

Those with low load factors have a very different view on that than those with high load factors. Those who would like to have a lot of flexibility and member distributed energy resources have a different view than those who don't want that.

Tom Linquist: In this era of new technology and distributed energy resources, those conversations become more and more interesting.

Barbara Nick: It is a very pivotal point in our industry. We've been talking about change. There's something that's fundamentally different now than in the '70s and the '80s.

Two things: one, we were growing then. If you go back to the '70s, we were moving off an eight percent growth rate to a four percent growth rate. Now, when it's organic growth, we are looking at almost flat growth rates, maybe 0.6% to 0.8%. The impact of energy efficiency technology has been huge. When you are capital intensive, that means a lot.

The flattening of the growth and electricity demand is a real game changer, a new development since the inception of our industry in the industrial age.

The other is the fact that our customers have choices. They have tangible choices with the price points of solar. We are not quite there with batteries. They are able to make choices now that can continue to cannibalize the load.

Tom Linquist: You've led in both the IOU world and the cooperative world. Is there a better alignment with the customer in the cooperative structure? What's the magic formula in their

(Cont. on page 57)

natural gas are those users. The chemical folks, steel folks and fertilizer folks see the benefits of a low cost, abundant, domestic, clean resource that no other country really has the way we do. We have high demand, but also a phenomenal supply.

PUF's Steve Mitnick: Who are the other trade associations

who will take part in the World Gas Conference?

Dave McCurdy: EEI, API, INGAA, the Natural Gas Supply Association, and the Natural Gas Council, are all involved. It's not just an AGA event. This is a real opportunity for the entire energy sector. **PUF**

Barbara Nick

(Cont. from p. 35)

ability to stay relevant, on the cutting edge, and to consistently provide high-quality services?

Barbara Nick: I've seen service providers in the IOU space and some of the public power space. Sometimes they are shared providers. They might provide services to public power, to cooperatives or the IOUs.

It depends on who is leading the organization, how true they are to their mission. Those cooperative organizations that leverage the advantage do so by living and demonstrating our cooperative principles. There is an allegiance among the cooperatives, all things being equal. At the end of the day, they are going to go with what's best for their members.

While IOUs might have started out very coalesced in their needs, over time leadership changes or the changes in shareholder expectations might cause service levels to change. You



don't have that same risk of short-term views in cooperatives. They are cooperative by their definition.

They are not-for-profit. Their mission is to serve their members. There's some skin in the game to make it successful. Unlike an IOU, members are a part of the governance. Members have a vested interest in making sure that it survives.

Tom Linquist: For an entity that's self-governed, what are the vulnerability points of governance?

I'm from Green Bay. How can I end any conversation if I don't quote one of our great coaches?

profession. Effective leadership rests on the commitment to do the right thing, and having the intelligence, judgement, and good common sense to execute on the right thing. I'm from Green Bay. How can I end any conversation if I don't quote one of our great coaches?

Green Bay Packers coach Vince Lombardi once announced to his players, "Gentlemen, this is a football." He wanted the players to start with the fundamentals of the game. That's what this is about. This is recognizing the fundamentals of how you run a business. How you do the right things for the right reason at the right time. For our industry, the goal is safe, reliable, affordable, and sustainable energy. **PUF**

From 2010-2016, the nation's residential electric bills rose 5.9%. That's around one percent per year. The nation's residences took 2.7% fewer kilowatt-hours in 2016, compared to 2010. Bills up. Kilowatt-hours down. Average rates consequently rose 8.8%. That's around one and a half percent per year.

If the trend continues, with the same dominance of variable line items in electric bills, average rates will keep going up, and become even less indicative of what consumers pay for electric service.