An Interview with
WILL KAUL

Conducted by Marta Monti
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Marta: Today is October 6, and I'm speaking on the phone again with Will Kaul from Great River Energy. Will, can you explain in plain language what the regulatory changes that came with the 2005 Omnibus Energy Bill mean to utilities and to CapX?

Will: Just for a little context, when we kicked off the CapX project, it was a two-pronged approach. One prong was to develop the vision and use that as a communication tool. The other was to get regulatory forms that will actually make it possible to be successful. That required first and foremost that IOUs (Investor-Owned Utilities) would consider transmission a good investment. The way it stood at the time, it was a situation where the IOUs invested in transmission and there would be a regulatory lag, meaning there is a long time between when they spend the money and when they are able to recover it.

Transmission, for a normal integrated IOU, is probably 7% of their overall revenue, so they are not wanting to do a whole rate case on investments in transmission. In fact, they weren't investing in transmission partly for that reason. When we formed CapX, transmission was the least favorite investment for an IOU. We knew we needed to invest, but we wanted to make it so we could raise the capital from the utilities. So that was the most important policy matter that needed to be addressed.

Number two was that the statute didn't have any language in it, under the certificate of need statute, that would recognize the value of regional markets when considering the need for the line. Before it addressed native load in Minnesota. We were able to put in a phrase in there that said "regional" projects could also support a certificate of need.

Another one that was in there was that the need and siting process was disintegrated. Part of it was at the EQB (Environmental Quality Board), and the other part at the PUC. We wanted it all in one place. This is something that we did not propose, because as clients of the EQB and the PUC, we didn't want to offend anybody, but I think it was the Commission that came forward and suggested that we put it all together under the PUC.

The fourth thing was, at that time, Xcel had just pulled the plug on TransLink, their TransCo proposal, and probably the reason why was they were getting pushback from regulators who said they didn't have the authority to do this under state law. So we wrote into the law that it would be legal for utilities to consolidate their assets into a TransCo.

Those were the main things that we sought, and we got all of those things. The reason we got all of those things is we worked with all the other stakeholders. We worked with people like Beth Soholt at Wind on the Wires, we worked with Bill Grant who was with this Izaak Walton League at the time. We worked with the state regulators themselves, the Department of Commerce staff.

Basically, all the stakeholders that were involved were part of the negotiation of the legislative package. We had a bunch of meetings over at the capital. I think Mike Bull at the time--he's worked for everybody--but at the time, he was the lawyer working for the house committee where the jurisdiction for this bill was. So Mike Bull was also involved in this negotiation, as well as his counterpart at the senate. And then Ellen Anderson was the chair of the Senate Energy Committee at the time, and she was also involved. She was the one that said "you guys all work on this really hard and come up with something you can all agree on." so that's essentially what we did.

Marta: Thank you, that's clearing a lot up for me. I think I missed the importance of the change in the certificate of need language to include regional need, so thank you for highlighting that. It is big, and it's not language that you'll find in North Dakota's our South Dakota's PUC/PSC (Public Utilities Commission/Public Service Commission) definition of how need is assessed.

You didn't mention the construction work in progress change in the bill.

Will: That was part of making this a good investment for IOU's. We got forward looking CWIP (construction work-in-progress) formula rates, so we don't have to go into a rate case. They can simply fill out their rider every year, and for transmission investments that qualify, they can put that for what they expect to spend in the coming year. The beauty of this is that it actually reduces the cost of building the project because there is less interest during construction. It also helps to fund the project as you go, and reduces the need to borrow money. It's good for consumers, it's good for the utility, and it gives them certainty, and it took transmission from the least-favored investment to the most favored investment.

Marta: The MOST favored?

Will: Yes

Marta: Okay. So that's big. Jumping from least to most. Is the rider an annual thing that is attached, or is it attached for the length of the project?

Will: It's in place permanently, so anytime you build a project that qualifies, you qualify for this treatment. It's a rate mechanism in place all the time if the situation comes up.

Marta: Without having to actually go through a rate case.

Will: Correct. And it wasn't tied to CapX projects specifically.

Marta: Okay, got it. How do riders affect the ratepayers? How much is their bill impacted by this?

Will: Well, as I mentioned earlier, it's beneficial for consumers because it lowers the cost of the project because of the less interest accumulated during construction, and there is less money borrowed. The difference for the consumers is that they are paying as the project is being built rather than waiting for it to be done. With transmission projects like these CapX projects, there might be a 5 year period where we're spending a lot of money. A utility would normally have to wait till the end of those 5 years to submit a rate case to start recovering costs. Instead, starting on year one, the utility is paying as they go, so to speak.

Marta: And then ultimately the price tag is not as high as it would be because you are able to borrow less and accrue less interest.

Will: In the long run, it's the best thing for the consumers. In the short-run, they start paying sooner than they would otherwise.

Marta: So they see impact immediately, but in the long run they are actually saving money.

I learned an interesting fact the other day. Article 11 in the 2005 that relates to eminent domain and landowners called for a Legislative Electric Energy Task Force of 12 people from various stakeholder groups to examine how landowners are compensation for high voltage transmission lines. They were supposed to come up with a report and submit their recommendations a year later. Are you familiar with this?

Will: Well you know, it doesn't ring a bell. I wondering if anyone actually did that.

Marta: No! They did not! Nothing was ever submitted. However, there is a chance that the information was incorporated into the Legislative Energy Commission.

Will: As the projects were going through the permitting and right-of-way acquisition process, there were a number of bills, some of which were passed, that had to do with eminent domain, and you're probably better off chasing that down.

Marta: Yes, that's probably where the effort ended up going to and the issue was addressed that way.

Will: What had happened was, someone came through with a pipeline project, and they got the public really riled up. And there was a legislator down there that became very involved in eminent domain because of it, and that was just when we were coming down the street. So, they were able to take their revenge out on us.

Marta: Lucky you.

Will: I think it was Senator Bly. So there was a legislative initiative that put the landowners in a much better bargaining position. If our offer was more than 20% less than the final offer, then we have to pay for all their costs, and that kinda thing. We have to pay for a property value assessment, and a bunch of other things. Then there were subsequent court cases on the Buy the Farm part which was also very beneficial to landowners. Those were some significant changes in law that occurred because of the project, but it wasn't our initiative. It was more of a reaction to landowners.

Marta: Yes, so it's my suspicion that the issue from the 2005 bill got taken over by the other ways to address it.

I was wondering if you could give me a little more detail about what you mean when you say you were working with stakeholders like Beth Soholt and Department of Commerce staff. What did that look like?

Will: The actual crafting of the language. It started with concept, then it went into drafting. I was involved with a number of those meetings, and my recollection was that the same people were there every time, at each step of the way for each issue. We'd sit down, work through the issue, someone would take homework home and bring it back. It was a bunch of people who were firmly like-minded. We had a shared objective which was to get all this transmission built. And we had some divergent interests. They wanted to build for renewable energy, we wanted to build for renewable energy and reliability and other reasons. But we all had a common shared interest in getting it built.

I would characterize these meetings as a collaboration on getting these regulatory reforms done with an eye towards protecting consumers, protecting the environment, and making sure that utilities saw transmission as a good investment.

That process is typical of the legislature, where a chair of a committee wants to get something done. If you have someone screaming bloody murder, it doesn't move through the legislative process. So the committee chairmen basically tell you to go in a room and don't come out till you figure it out. Our process was like that, but there weren't too many divergent interests.

Marta: Did this effort to change the legislation start before genesis of CapX?

Will: I'm chuckling because, picture the first conference call we had for CapX. There wasn't any real thinking done yet on it. I organized the call, and the call to the group was that we needed a vision and we needed regulatory reform. Everyone was very hot on the vision, they thought it was great. Then I brought up the regulatory reform, and it was like crickets. Of course, I was talking to a bunch of engineers. Someone over at Xcel sent it to their policy and regulatory people who jumped on it and saw it as an opportunity. It took hold then, and then by going through the typical process at the legislature, we got the changes we needed.

I think what it took was getting an IOU to embrace the need for change, and run with it. And Xcel was in the lead there.

Marta: Once the bill was signed into law, was there any more selling you guys needed to do to convince the participating utilities that this was a good idea? Or was the group already there, and said "hey, now we've got the regulatory changes we wanted, so let's go!"?

Will: It's kinda like the dog that's chasing the car, and he caught up to it, and then what do you do? Once it was passed we had the chair of the PUC saying to us, "Get that Certificate of Need in here soon!" It was right after the East Coast blackout. We did a great job of selling this thing, and they were getting impatient. That was kind of ironic.

There was no more selling to do, except at the utilities. Now the utilities are looking at a huge commitment, a decade long, billions of dollars….they're going to have to raise the money, they're going to have to talk to their rating agencies and rationalize the CapX project against other capital requirements that they had, and then we had to decide amongst ourselves who's going to invest how much, and in what projects? That was a complicated process. What percent does GRE have to put up? Xcel? Are we going to let all the small muni G&T's get involved? We ended up making it inclusive. We invited Basin, Alliant down in Iowa. We were trying to make it as inclusive as we could.

The muni and cooperative utilities, of course, don't have rate cases, and were not affected by the formula rate thing other than they wanted to make sure that the IOUs were motivated to participate in the project. It had to work for everybody.

I would say that getting that stuff done, it was remarkable. We started in April of 2004, and by the end of the legislative session in 2005 we had everything we needed.

Marta: Right, that's a pretty quick turnaround.

Will: So then it took at least a year or maybe even two before we submitted the CON (Certificate of Need), and that was because a lot of other things. Compiling a regulatory filing like that was a lot of work. Especially when you have $2 billion in 4 different projects packaged in one regulatory filing. It had never been done before.

Marta: Right. And having the one CON for the 3 345 kV lines, that must have been big.

Here's a question. Everyone seems to refer to this as 4 projects, but when you look at it, it's 5 because the Fargo line was split into two projects, and the Brookings to La Crosse is chunked up into a few projects. So depending on how you're looking at it, there are a different number of projects. Am I missing something big here?

Will: Think of it as Phase 1 and Phase 2. The original projects were the 3-345 kV lines and the 230 kV Bemidji-Boswell. The Fargo project were divided into two projects somewhere along the line...I think after the CON but before siting. Then later the MVP (Multi-Value Project) portfolio was approved by MISO (Midcontinent Independent System Operator), and that added the Big Stone-Brookings project and Big Stone-Ellendale, and it also added the La Crosse-Madison project. I think we called the Big Stone-Brookings project a CapX project, but not calling Big Stone-Ellendale or the La Crosse-Madison a CapX project, even though all of those were part of our vision. The original vision had all those projects in it, we just weren't the right utilities.

So in the end we've got the Fargo project, the Bemidji project, the Brookings project, and the Hampton-La Crosse project, and those were the phase 1 projects.

Marta: That clears it up. I guess I must have never distinguished between Phase 1 and Phase 2 projects.

The Big Stone-Brookings line is still considered a CapX project, but the way that it was set up, only Xcel and Otter Tail were the participating utilities.

Will: There's a little backstory on that one. Originally the Big Stone-Brookings project was going to have a number of investors in it. Xcel was essentially sharing its investment rights with participants in the Brookings project. Are you familiar with right of first refusal?

Marta: Yes

Will: So, Xcel owns the Brookings substation, and Otter Tail owned the Big Stone. So technically those two utilities and only those two utilities had a right to invest in it. But Xcel, generously, offered the participants in the Brookings project, a share of the Big Stone-Brookings project. In the end, we took that share and put it into the Brookings project so it increased our percentage of ownership in that, and we got out of the Big Stone-Brookings project so it would be simpler.

So we moved our investment opportunity from Big Stone-Brookings over to the Brookings project.

Marta: Alright, well that clears that up.

Will: More than you wanted to know.

Marta: No, it never is, Will! I called to ask about a 2005 bill, and here we are talking about the projects, so this is perfect for me.

If you would mind, could I ask you another question or two about the CapX participation agreement? You were talking about how the group decided what percentage each group would invest. How did these percentages change from the participation agreement to the project agreements?

Will: There are two things going on here. One is the participation agreement was an agreement that covered, for lack of a better term, the early development work of CapX. It was not specific to any particular project.

Marta: More towards getting studies in order?

Will: Right. At that time we had Terry Groves from GRE, and Xcel had somebody, and those key people were spending a lot of time, or even full time, on CapX. The participation agreement was an agreement to cover those costs, study costs, and other costs associated with development. Communications, salaries, things like that.

When it came to projects, we had a day where we all came in, and somebody coined the term "poker chip exercise". If GRE's got $300 million to invest, where are we going to put it? Let's see...we'll put $100 million in Brookings, we'll put $150 million in Fargo, and we'll put $50 million in Bemidji. And we choose those projects because they are in our service territory, we have some other reasons why we like those projects. And each utility walked around the room and put their poker chips, literally, into the projects they liked. When we were all done, we looked at the way things panned out and found that, for example, Brookings still needed another $20 million. So a little re-arranging was done. And as it turned out, by happenstance, each project ended up having 5 participants. It wasn't planned, it's just the way it worked out.

Each participant had whatever their share was of that project, and it was different for each one.

In the investment obligation, because at that time transmission was not a desired investment, was based on the load-ratio share of the system peak. So, on the hottest day of the year, let's say Xcel is 50% of the load, GRE is 15%, MP might be 8%, etc. Each utility had investment in proportion to their use of the system. That's how many poker chips they got.

Not all the utilities participated fully. They didn't invest up to their load ratio share. They were skeptical, or didn't have the capital, had other concerns, competing interests, that sort of thing. There was one case, one utility that wasn't quite on board.

Marta: That wouldn't by any chance be a utility that exited the group and was replaced by another, would it?

Will: Who exited the group?

Marta: As I was examining the route permit applications, I noticed Dairyland was added to a project after the certificate of need but before the route permit application. They replaced Missouri River Energy Service (MRES).

Will: This an interesting part of the history. Dairyland was invited. They were very unwilling to put a lot of money into it. They were interested and they wanted to be part of it, but they didn't want to pay for it during the developing stage. That was part of the La Crosse project. We kinda let them sit in, sort of, and then later on they joined, and they are a member now. But they had trouble anteing up the funds.

Minnkota was another one that was on the periphery the whole time. I don't think they ever quit, but like Dairyland, they too wanted a piece of the Bemidji project. So, they weren't a dues-paying member, but they were involved in those two projects individually, and those were the only projects they were involved in. So there's not actually a group that left.

Marta: What I think I'm remembering is the legalize-speak at the beginning of the project documents that names the participants, and I remember one name being changed out saying that "from here forward this company will now be referred to as Dairyland" etc…

Will: I know what you're talking about. This is another situation. Missouri River Energy Services (MRES) was one of the participants almost from the very beginning. Their assets reside in some other organization I've never heard of, and I couldn't tell you what the name is. Somewhere along the way they changed who the official legal participant was from what MRES services to what this asset holding company was. So they didn't actually leave, they just changed their name.

Marta: Okay. Clear as mud, I got it now! The give and take has been fun to follow as I've been going through these projects.

One last question about voting with the vision team. I noticed that there are different levels of voting, depending on what is being voted on. Was it complicated getting that worked out?

Will: We had the original participation agreement that was essentially a handshake. Then as the CapX initiative started construction and it became more complicated, we felt we needed to make our agreement process more sophisticated. There are some things that are a simple majority vote, and others that required a unanimous. Depending on what it was we were voting on--some things were fine with a simple majority, and some not. New members had to be a unanimous vote, for example.

Marta: So once that structure was agreed upon, people were more or less happy with the system? You didn't have some of the larger companies like Xcel-or GRE even-feeling as though their vote should count for more because they are investing more?

Will: Everyone was happy with the result. Xcel was one of the leading voices in shaping the governance policy of the group.

Marta: Okay. Thank you for your time again today, Will.

Will: No problem, my pleasure.