

REVENUE STABILIZATION  
AGREEMENT BY AND BETWEEN  
CITY OF RED WING, MINNESOTA  
AND NORTHERN STATES POWER  
COMPANY D/B/A XCEL ENERGY:

OCTOBER 23, 2006

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FRAMING THE CONTEXT – INSTABILITY AND  
UNCERTAINTY IN PRAIRIE ISLAND NUCLEAR PLANT'S  
(PING) HISTORICAL CONTRIBUTION TO THE LOCAL  
TAX BASE

- The Prairie Island Nuclear Plant first went into service in 1974.
- In the early 1990's PING accounted for approximately 75% of Red Wing's tax base.
- This contribution to the tax base enabled relatively low and stable local tax rates.

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## FRAMING THE CONTEXT – INSTABILITY AND UNCERTAINTY IN PING'S HISTORICAL CONTRIBUTION TO THE LOCAL TAX BASE

(Continued)

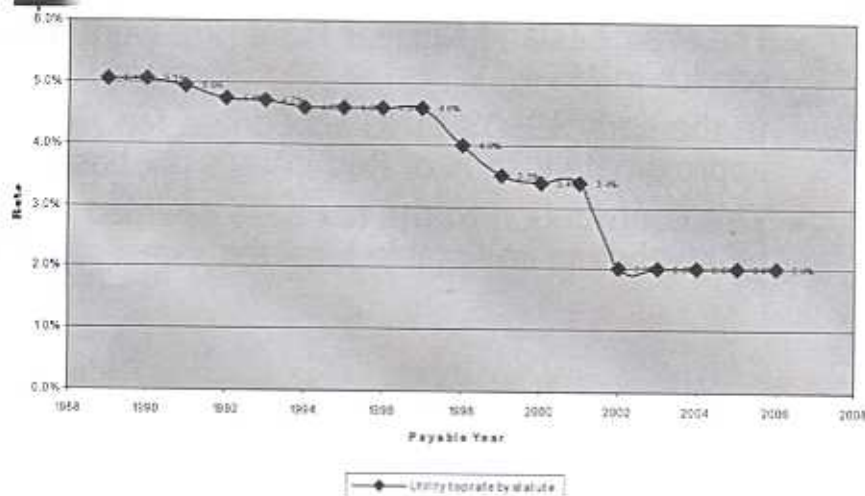
### LEGISLATIVE ACTIONS

- From 1990 to 1997 the Legislature reduced the property tax class rate on utility property by 10% (from 5.1 to 4.6).
- From 1997 to 2001 the Legislature reduced the property tax class rate on utility property by a 26% (from 4.6 to 3.4).
- In 2001 the Legislature reduced the property tax class rate on utility property by 41% (from 3.4 to 2.0).

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## FRAMING THE CONTEXT – INSTABILITY AND UNCERTAINTY IN PING'S HISTORICAL CONTRIBUTION TO THE LOCAL TAX BASE (Continued)

State established tax classification rates by Property Type



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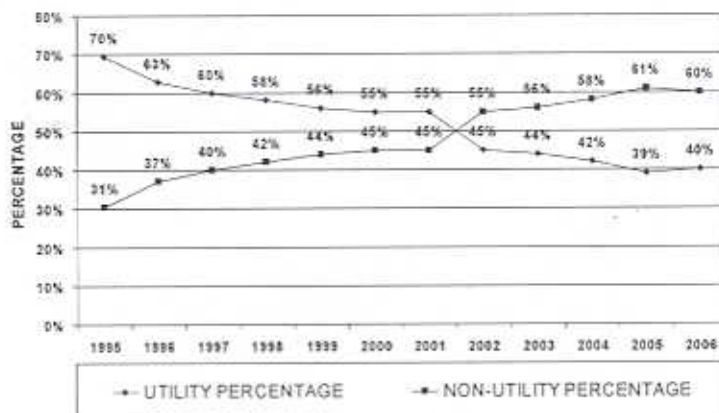
FRAMING THE CONTEXT - INSTABILITY AND UNCERTAINTY IN PING'S HISTORICAL CONTRIBUTION TO THE LOCAL TAX BASE  
(Continued)

LEGISLATIVE ACTIONS (Continued)

- Each of these legislated changes had a direct impact on the stability and level of our tax rates.
- The class rate compression has tightened the gap between residential, agricultural and utility property taxes and has shifted property taxes onto non-utility property.
- As a proportion of the tax base, XCEL has dropped from 75% in the 1990's to 38% of the City tax base in 2006.
- The resultant property tax shift has had a disproportional impact on residential properties.

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FRAMING THE CONTEXT - INSTABILITY AND UNCERTAINTY IN PING'S HISTORICAL CONTRIBUTION TO THE LOCAL TAX BASE  
(Continued)



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## RED WING'S RESPONSE TO THE CHANGING UTILITY TAX ENVIRONMENT.

- Red Wing has, and continues to be, extremely active in any endeavor which may reduce the valuation or tax capacity on utility property.
- In 1997 the City of Red Wing was instrumental in forming the Coalition of Utility Cities (CUC). The CUC is a joint powers board formed by seven cities with substantial utility tax base in their communities. The cities are Becker, Cohasset, Granite Falls, Hoyt Lakes, Monticello, Oak Park Heights, and Red Wing. This organization was formed to bring together the resources and talents of its individual members and preserve the host community tax base in the face of tax cuts for utilities. This organization assists its members by providing timely information on current electric utility tax issues, conducting research and analysis on utility tax and regulatory issues, developing options, coordinating activities with other interest groups and governmental agencies, by communicating directly through lobbying and the preparation of advocacy materials.

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## RED WING'S RESPONSE TO THE CHANGING UTILITY TAX ENVIRONMENT.

(Continued)

- The City of Red Wing frequently partners with other local units of governments to preserve the host communities tax base. These partners include the local school district, Goodhue County, Wright County, Sherburne County and other interested governmental entities.
- The City of Red Wing has a long history of coordinating local stakeholders to assist in lobbying key legislators to preserve the utility tax base.

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## RECENT ACTIVITY AT THE MINNESOTA DEPARTMENT OF REVENUE (DOR) INCREASES THE INSTABILITY AND UNCERTAINTY OF THE PING TAX BASE

- In 2003 under pressure from the utilities and on-going litigation over utility market valuation the DOR announced that they were requesting comments on the possible amendment of rules governing valuation and assessment of the property of utility companies, *Minnesota Rules*, chapter 8100.
- In January of 2005 the DOR received their consultant's report which said that the current rules are too rigid and suggested numerous changes to the current rules.
- The precise impact of the rules is unknown because the new rules are not yet finalized.
- DOR staff assigned to this task believe the utility property value may decrease by 18 – 30%.
- The DOR is anticipating that the new rules will be effective for the 2007 utility valuations and Pay 2008 property taxes.

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## POTENTIAL IMPACT OF THE NEW DOR RULES

- Potential 18 to 30% reduction in utility valuation by payable 2008.
- This reduction would equate to a 7 to 13% decline in the tax base.
- A change of this magnitude to the utility valuation will destabilize the property tax rate and shift more of the property tax burden onto non-utility properties including commercial, industrial, agricultural and residential.

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## RED WING'S RESPONSE TO THE ACTIVITY AT DOR

- The City of Red Wing, along with the CUC and other stakeholders, have followed and participated in the DOR's activities to ensure our voice is heard during this process. We have worked with the DOR and presented the DOR with comments, research and analysis which clearly illustrate that the property tax system in Minnesota does not place the Minnesota utilities at a competitive disadvantage and that the rules currently employed underestimate market valuation on utility property. We also participated in the DOR's appointed Utility Rules Advisory Committee.

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## RED WING'S RESPONSE TO THE ACTIVITY AT DOR (Continued)

- In 2006, as in 2005, the City of Red Wing was instrumental in getting legislative attention drawn to the DOR's activities.
- In 2006, as in 2005, the City of Red Wing was instrumental in getting various bills related to the proposed utility valuation rules changes authored. The primary piece of legislation was SF 2507 and its companion bill HF 3592. These bills delayed the effective date of any utility valuation rules changes for one legislative session. The legislation was intended to provide the legislature one legislative session to consider the appropriate tax treatment of utilities in Minnesota before any rule changes went into effect. The Senate was supportive and included this legislation in its tax bill. The House however never gave the bill a hearing and the refused to hear it in conference committee. As a result the legislation died.

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## STABILIZATION AGREEMENT PROPOSED

- In 2005 XCEL proposed a stabilization which the City has been negotiating with XCEL and the other host communities now for nearly 1 ½ years.
- XCEL proposed the stabilization to its three largest host communities:
  - Red Wing-Goodhue County
  - Becker-Sherburne County
  - Monticello-Wright Count

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## WHAT PUBLIC INTEREST IS SERVED BY THE STABILIZATION AGREEMENT

- The primary objective of the agreement is to stabilize the utility property tax revenue of the City at an amount certain for a fixed term.
- Reduces the instability and uncertainty in the tax rates created by regulatory, administrative, and judicial actions effecting the valuation and assessment of property taxes upon PING.
- Promotes a stable and controlled revenue stream for the City.
- Provides a basis for long-term budgetary planning of revenues and expenses.
- Reduces the likelihood that substantial property tax burdens will again be shifted from utility property to non-utility property.
- Protects the City's current bond rating.

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## SIGNIFICANT TERMS OF THE STABILIZATION AGREEMENT

- The Stabilization Agreement is legally binding.
- The parties to the Agreement are NSP, D/B/A Excel Energy and the City of Red
- The Stabilization Agreement is terminated if the amended DOR utility valuation rules are not implemented on or before December 31, 2008.
- Subject to termination provisions, the term of the agreement is for a period of 10 years, or through December 31, 2018, whichever occurs first.

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## SIGNIFICANT TERMS OF THE STABILIZATION AGREEMENT (Continued)

- Stabilized property is the state assessed property at the PING facility. Parcels 55.705.0160, 55.705.0161 and 55.705.0162. The property can be loosely identified as the property within the gated perimeter of the PING. State assessed property excludes land.
- The Base Year is the year the rule changes under consideration by the DOR take effect.
- The Base Year Amount is the amount of taxes paid in the base year to the City in the Base Year. The Base Year Amount is the revenue stream stabilized over the term of this agreement.
  - If the DOR rule change occurs as scheduled in 2007 the revenue stream stabilized under the proposed agreement is the amount of property taxes paid on PING in 2007.

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## SIGNIFICANT TERMS OF THE STABILIZATION AGREEMENT (Continued)

- When the property tax assessed on PING falls below the base year amount, a stabilization payment is made directly to the City by XCEL on the date it makes its regular property tax payments.
- When the property tax assessed on PING is above the base year amount, an abatement payment is made to XCEL by the host community the following year.
  - Our modeling indicates that it is unlikely that the City will be placed in an abatement position and that the XCEL stabilization payments will range from \$400,000 to \$2,000,000 annually dependent upon the effect of the DOR rules changes and other factors.

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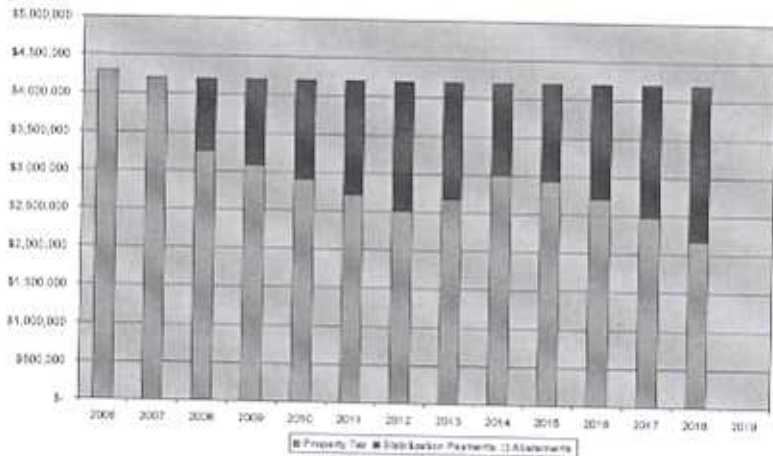


## SIGNIFICANT TERMS OF THE STABILIZATION AGREEMENT (Continued)

- Extraordinary investment clauses protect the City from abatement payments due as a result of projects initiated at PING which increase its state assessed valuation.
- Extraordinary divestiture clauses could result in a reduction of the Base Year Amount. Extraordinary divestitures could arise from the sale or destruction, or material impairment, of the Stabilized Property or from an event that renders a plant generating unit substantially non-operational.
- Dispute resolution procedures are contained in the contract to avoiding litigation.

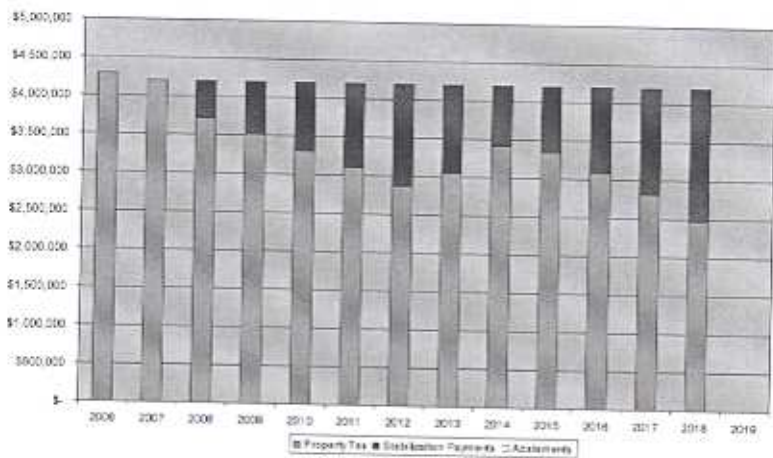
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PROJECTED OUTCOME OF STABILIZATION AGREEMENT IF THE DOR RULES CHANGES RESULT IN A 30% DECREASE IN PING'S VALUATION



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PROJECTED OUTCOME OF STABILIZATION AGREEMENT IF THE DOR RULES CHANGES RESULT IN AN 18% DECREASE IN PING'S VALUATION



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## EXAMPLES OF HOW THE STABILIZATION AGREEMENT PAYMENTS WOULD FLOW

	A. Property Tax paid (total for 10 years)	B. Stabilization payments (total 10 years)	C. Abatements paid out (total 10 years)	Net dollars to City over 10 years (A+B-C)
30% value reduction, 2% class rate	\$38,289,128	\$16,494,625	\$0	\$54,783,753
18% reduction, 2% class rate	\$43,395,277	\$11,388,475	\$0	\$54,783,752
30% reduction, State raises rate to 3%	\$50,077,252	\$4,706,499	\$0	\$54,783,751
18% reduction, State raises rate to 3%	\$57,204,223	\$1,140,505	<b>-\$1,766,906</b>	\$56,577,822

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## KEY ASSUMPTIONS IN PREVIOUS GRAPHS AND CHART.

- Base Year is 2007.
- Base Year Amount is \$4,207,218.
- Annual tax capacity growth is 5.5%.
- Annual tax levy growth is 2.5%.

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## QUESTIONS OR COMMENTS

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Questions or Comments.