MINNESOTA DEPARTMENT OF COMMERCE

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April 20, 2016

Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101-2147

RE: **Comments of the Minnesota Department of Commerce, Division of Energy Resources**
Docket No. G011/M-15-992

Dear Mr. Wolf:

Attached are the Comments of the Minnesota Department of Commerce, Division of Energy Resources (Department or DOC) in the following matter:

> In the Matter of the Petition of Minnesota Energy Resources Corporation for Authorization to Establish Amortization Periods Related to the Pre-Acquisition Pension and Other Postretirement Benefits Costs.

The petition was filed on November 20, 2015 by:

> Amber Lee
> Minnesota Energy Resources Corporation
> 1995 Rahncliff Court, Suite 200
> Eagan, MN 55122

The Department requests that MERC clarify its statement as to the connection of this petition to its concurrent rate case. The Department expects to provide its final recommendations to the Minnesota Public Utilities Commission (Commission) after reviewing Minnesota Energy Resources Corporation's MERC's Reply Comments.

The Department is available to answer any questions the Commission may have.

Sincerely,

/s/ JOHN KUNDERT
Financial Analyst

JK/lt
Attachment

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

COMMENTS OF THE MINNESOTA DEPARTMENT OF COMMERCE DIVISION OF ENERGY RESOURCES

DOCKET NO. G011/M-15-992

I. BACKGROUND

In its July 30, 2007 *Order in the Matter of the Petition of Minnesota Energy Resources Corporation for Authorization to Establish a Regulatory Asset for Pension and Other Postretirement Benefits Acquired from Aquila, Inc.* in Docket G007,011/PA-06-1287, the Minnesota Public Utilities Commission (Commission) authorized Minnesota Energy Resources Corporation (MERC or the Company) to create a regulatory asset for pension and other postretirement benefits acquired from Aquila, Inc. and to amortize the asset over a 20-year period.

In its June 25, 2015 *Order Approving Merger Subject to Conditions* in Docket No. G011/PA-14-664, the Commission approved the proposed merger between MERC's parent Company (Integrys Energy Group, Inc.) and Wisconsin Energy Corporation (WEC). As a result of the merger, generally accepted accounting principles (GAAP) require WEC to assign fair market value to the assets and liabilities acquired in the transaction, including those related to pension and other postretirement benefits and costs.

II. SUMMARY OF MINNESOTA ENERGY RESOURCES CORPORATION'S PROPOSAL

On November 20, 2015, MERC petitioned the Commission for approval of MERC's valuation of pre-acquisition pension and other postemployment benefit assets and liabilities as they existed prior to Integrys Energy Group's acquisition (the Acquisition) by WEC and to permit amortization of those costs over a period that the Company claims will approximate the same annual pension cost level that MERC would have recorded absent the Acquisition.[1]

[1] MERC's petition does not have page numbers, but the statement is on page 4 of 14 of the document, at the end of the first full paragraph.

III. DETAILS OF MERC'S PROPOSAL

MERC is petitioning the Commission for approval to identify and amortize the difference between the accounting (book) values and the estimated current market values of certain retirement-related assets held at the time of the acquisition of MERC (and Integrys) by WEC. The assets in question are regulatory assets that were created at the time of Integrys' acquisition of Aquila's Minnesota assets in Docket No. G007,011/M-06-1287.[2]

WEC is required to assign fair market value to assets and liabilities that were acquired in the Acquisition under generally accepted accounting principles (GAAP). MERC identified the annual financial impact of the proposed change to be an increase in the annual amortization expense associated with these regulatory assets of $45,242.[3] This amount is equal to a 6.4 percent increase in this expense from the current level being charged to ratepayers.

MERC stated on page 7 of its petition[4] that the proposal in this proceeding "will have no impact on the amount MERC proposes to include in rate base in its pending Minnesota rate case" (Docket No. G011/GR-15-736). The Department requests that MERC indicate in Reply Comments whether this statement means that: 1) the costs requested in the instant case are already included in its rate case or 2) these costs are not included in the rate case.[5]

MERC is proposing to continue to use the pre-Acquisition actuarial calculations that were used for the first half of 2015 through December 31, 2015. The Company is then proposing to amortize the remaining pre-Acquisition net regulatory assets over their remaining service lives. The Company is also proposing to vary the amortization period associated with different components of the MERC and Legacy Integrys Business Support, LLC (IBS) benefit plans. The Company is proposing to increase the amortization period from the currently remaining 10 years to 15 years for all the components of the MERC Benefit Plan. MERC is proposing to shorten the current 10-year amortization period for the approved components of the Legacy IBS Benefit Plan from 10 years to 5 or 7 years depending on the component.

MERC's stated goal in this proceeding is to "align its regulatory and GAAP books and minimize the impact on Minnesota customers [of the Acquisition]."[6]

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[2] The Commission allowed MERC to create a regulatory asset for pension and other postretirement benefits acquired from Aquila in that proceeding.
[3] MERC's Exhibit 3 shows the estimated cumulative effect of these changes on annual pension expense to be an increase of $45,242, from $707,449 to $752,691.
[4] Petition at page 7.
[5] The Department notes that, in MERC's rate case, issues regarding MERC's proposed rate base treatment of pension assets are in dispute.
[6] Petition at page 4.

IV. DEPARTMENTAL ANALYSIS

A. INTRODUCTION

In analyzing whether the current petition of MERC is in the public interest, the Minnesota Department of Commerce, Division of Energy Resources (Department or DOC) reviewed:

- MERC's claim that its proposal relative to the treatment of pension and other postretirement benefits is consistent with Commission precedent,
- MERC's claim that its proposal allows it to remain in compliance with the conditions the Commission outlined in its *Order Approving Merger Subject to Conditions*, dated June 25, 2015 in Docket No. G011/PA-14-664, and
- the costs and benefits associated with the Company's proposal on ratepayers.

B. COMMISSION PRECEDENT REGARDING MERC'S TREATMENT OF PENSION AND OTHER POSTRETIREMENT BENEFITS

In its Order dated July 30, 2007 in Docket No. G007, 011/M-06-1287 (the Aquila Docket) the Commission authorized MERC to create a regulatory asset for pension and other postretirement benefits acquired from Aquila; and also authorized MERC amortize the regulatory asset over a period of twenty years, starting July 1, 2006.

MERC subsequently created a regulatory asset equal to $12.1 million by transferring that same amount from goodwill and began to amortize that asset. This decision and the ensuing actions appear to support MERC's claim in the instant docket that the Commission has previously approved a "smoothing mechanism to partially defer certain costs (prior service costs and actuarial gains and losses) of its pension and OPEB plans".[7] The Department's analysis attached to the Commission's Order in the Aquila Docket also appears to support MERC's proposal to adopt amortization periods for the different net regulatory assets that results in an annual cost (amortization) that is similar to the one being recognized prior to the Acquisition.

The Department identified the following components of the regulatory asset created in the Aquila Docket from the information included in Exhibit 3 provided by MERC in the instant docket. Table 1 summarizes this information.

[7] *Ibid* at page 4.

Table 1 – Components of Regulatory Asset Approved in the Aquila Docket*

Benefit Plan	Account Description	Acct. Number
MERC	Pension Expense	926060
MERC	Pension Restoration	926210
MERC	MERC Supplemental Executive Retirement Plan	926220
MERC	Post-Retirement Medical – Admin	926180
MERC	Post-Retirement Medical – Non-Admin	926180
MERC	Postretirement Life	926305
Integrys Business Support	Pension Expense	926300
Integrys Business Support	Peoples Energy Retiree Welfare	926300
Integrys Business Support	Post-Retirement Medical Admin	926300

* *For the purpose of this table, the Department assumed that if the Account had a non-zero pre-existing amortization amount in Exhibit 3 of the filing, it was included as a component in the original regulatory asset approved in the Aquila Docket.*

All of the components of the Commission-approved regulatory asset ostensibly included in Table 1 were amortized over 20 years. This identical amortization period supports the concept of a single regulatory asset that consisted of several different components.

The Department's review of the information in the filing suggests that MERC is proposing to create a new regulatory asset for the components listed in Table 2.

Table 2 – New Regulatory Assets or Components Requested**

Benefit Plan	Account Description	Reg Asset (Liab) @ 12/31/2015	Acct. Number
MERC	Integrys Supplemental Executive Retirement Plan	$40,990	926210
Integrys Business Support	Pension Restoration	$120,223	926300
Integrys Business Support	Integrys Supplemental Executive Retirement Plan	$960,338	926300
Integrys Business Support	Peoples Energy Supplemental Plan	($186,395)	926300
Integrys Business Support	Post Retirement Life	$17,687	926300

***For the purpose of this table, the Department assumed that if the Account did not have a pre-existing amortization in Exhibit 3 of the filing, it was not included as a component in the original regulatory asset approved in the Aquila Docket.*

If one accepts the Company's premise that it is merely "updating" the costs of the different components included in the pre-existing regulatory asset the Commission approved in the Aquila Docket, then MERC did not provide an adequate basis to create regulatory assets for these components listed in Table 2. MERC appears to have adopted the aforementioned premise in this docket in that the Company stated that it was not seeking to establish a new regulatory asset.[8] Thus, based on the information provided in the record, the Department concludes that MERC did not support its proposed inclusion of the Legacy IBS components identified as Pension Restoration, Peoples Energy Supplemental Plan and Post Retirement Life. At a minimum, MERC would need to provide adequate support to include these items as regulatory assets to be incorporated.

In addition, the Department recommends that the Commission deny MERC's proposal to create a regulatory asset for Integrys Supplemental Executive Retirement Plan (SERP) in either the MERC or IBS Legacy Benefit Plans.[9] The Department's reason for recommending that Integrys' SERP costs not be allowed to be included as regulatory assets in this docket is based on the Commission having denied the recovery of SERP costs in several recent general rate cases:

- In Otter Tail Power's 2010 general rate case (Docket No. E017/GR-10-239), the Commission affirmed the Administrative Law Judge's recommendation to disallow $931,141 in supplemental executive pension costs.[10]
- In MERC's 2010 general rate case, (Docket No. G007,011/GR-10-977) the Commission affirmed the ALJ's recommendation to disallow the non-qualified pension costs included in the test year.[11]
- In Centerpoint Energy's 2013 rate case (G008/GR-13-316), the Commission at its May 8, 2014 Commission agenda meeting confirmed the ALJ's recommendation to disallow the non-qualified pension costs in the test year.[12]
- In Xcel Energy's 2012 general rate case, (Docket No. E002/GR-12-961), the Commission affirmed the ALJ's recommendation to disallow the non-qualified pension costs included in the test year.[13]

Similarly, the Department recommends that the Commission deny MERC's proposal to create a regulatory asset for SERP costs for either MERC or IBS Legacy Benefit Plans.

[8] Page 4 of MERC's petition.
[9] SERP costs are non-qualified pension expenses as defined by the Internal Revenue Services (IRS) rules. Employees whose earnings are above the qualified IRS limit are taxed on that amount. The SERP costs at issue in MERC's filing essentially would put ratepayers at risk for paying higher costs to override the effects of the IRS rules for those executives.
[10] See page 27, footnote 26 of the Commission's April 25, 2011 Order.
[11] See page 29 of the Commission's July 13, 2012 Order.
[12] See page 3 of the Commission's revised briefing papers.
[13] See page 7 of Commission's September 3, 2013 Order.

C. COMPLIANCE WITH THE COMMISSION'S ORDER IN DOCKET NO. G007/PA-14-664

The Department reviewed the conditions included in the Commission's Order dated June 25, 2015 in the aforementioned docket and identified the following two topics as being germane to this proceeding – push-down accounting and transaction or transition costs.

The Company stated in the filing that "no push-down accounting or transactions costs are assigned to MERC through this proposal".[14] The Department could not find any changes in asset values included in the filing that might be attributable to push-down accounting. As a result, the DOC believes MERC's assertion is correct.

> Regarding transition costs, in DOC Information Request No. 6, the Department asked: "Does the Company consider the costs identified in the Petition as being transition costs related to the merger?"

MERC responded:

> No. None of these costs were incurred to integrate or reorganize the utilities after the transaction was closed. . . .
>
> More specifically, Generally Accepted Accounting Principles require such costs be deferred and expensed over a period of years, a process known as 'smoothing." Before the acquisition, MERC was required by GAAP to smooth these costs over a number of years. Thus, at the time of the acquisition, MERC had not fully recovered all of the costs associated with the pension and benefits earned by its employees. The unrecovered costs were already deferred on MERC's books and the proposed amortization would permit recovery of previously-incurred costs.

The Department largely agrees with the concepts noted in MERC's response to DOC Information Request No. 6 for the components of the regulatory asset that was created as part of the Aquila Docket. The regulatory asset in question was created in 2007 using an estimate of fair value at the time. The book value of the components of that regulatory asset and the market value likely diverged to a certain extent during the seven year period between the creation of the regulatory asset and Integrys' acquisition by WEC. The Acquisition required those assets to be evaluated using a Fair Value Appraisal.[15] This filing represents something of a "true-up" relative to the value of the net regulatory asset approved in the Aquila Docket. The Department finds that the Company's proposal for identifying and amortizing the net regulatory assets approved in the Aquila Docket is not in conflict with the requirements contained in the Commission's Order in the Acquisition Docket.

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[14] *Ibid* at page 4.
[15] The term Fair Value Appraisal is defined as "Fair Value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

D. ESTIMATED COSTS AND BENEFITS ASSOCIATED WITH THE PROPOSAL FROM A RATEPAYER PERSPECTIVE

MERC explained in the Petition that Commission approval of its proposal "will then result in a regulatory cost recognition that aligns with historical actuarial cost recognition and GAAP; properly reflects on MERC's books and records the value of pension and OPEB costs allocated to MERC; and does not increase MERC's administrative and actuarial costs."[16]

The Department asked the Company in DOC Information Request to support its statement:

> Please provide the analysis that supports the Company's statement, "this proposal will reduce the administrative costs of otherwise requiring WEC to conduct multiple actuarial valuations of pension and OPEC assets to reflect regulatory requirements differently from GAAP."

MERC replied:

> That statement was based on a conversation with the Company's independent actuary, Wills Towers Watson, which indicated that the incremental annual cost of preparing a second set of actuarial valuations for MERC alone would be approximately $150,000.

A copy of this information request is included as Attachment A.

V. RECOMMENDATION

The Department requests that MERC indicate in Reply Comments whether or not any of the pension amounts identified in the instant proceeding are included in the Company's concurrent rate case. In either case, the Department concludes that MERC's proposal to include the Legacy IBS components identified as Pension Restoration, Peoples Energy Supplemental Plan and Post Retirement Life should be denied. In addition, the Department recommends that the Commission deny MERC's proposal to create a regulatory asset for SERP costs for either the MERC or IBS Legacy Benefit Plans.

The Department expects to provide its final recommendations to the Commission after reviewing Minnesota Energy Resources Corporation's MERC's Reply Comments.

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[16] *Ibid* at page 5.

State of Minnesota

Department of Commerce
Division of Energy Resources

Nonpublic [ ]
Public [X]

Utility Information Request

Docket Number: G011/M-15-992 Date of Request: 3/21/2016

Requested From: Minnesota Energy Resources Corporation Response Due: 3/31/2016

Analyst Requesting Information: John Kundert

Type of Inquiry:

[ ]......Financial	[ ]......Rate of Return	[ ]......Rate Design
[ ]......Engineering	[ ]......Forecasting	[ ]......Conservation
[ ]......Cost of Service	[ ]......CIP	[ ]......Other:

If you feel your responses are trade secret or privileged, please indicate this on your response.

Request No.	
2	Reference: Page 4 of the petition Please provide the analysis that supports the Company's statement "this proposal will reduce the administrative costs of otherwise requiring WEC to conduct multiple actuarial valuations of pension and OPEC assets to reflect regulatory requirements differently from GAAP." **MERC Response:** That statement was based on a conversation with the Company's independent actuary, Willis Towers Watson, which indicated that the incremental annual cost of preparing a second set of actuarial valuations for MERC alone would be approximately $150,000.

Response by: Christine Hans

Title: Manager – Benefits Accounting

Department: Benefits Accounting

Telephone: (312) 240-4009

List sources of information:

CERTIFICATE OF SERVICE

I, Sharon Ferguson, hereby certify that I have this day, served copies of the following document on the attached list of persons by electronic filing, certified mail, e-mail, or by depositing a true and correct copy thereof properly enveloped with postage paid in the United States Mail at St. Paul, Minnesota.

Minnesota Department of Commerce
Comments

Docket No. G011/M-15-992

Dated this 20th day of April 2016

/s/Sharon Ferguson

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