

**STATE OF MINNESOTA  
BEFORE THE PUBLIC UTILITIES COMMISSION**

Katie Sieben	Chair
Joseph K. Sullivan	Vice Chair
Hwikwon Ham	Commissioner
Audrey Partridge	Commissioner
John Tuma	Commissioner

In re Commission Evaluation of Changes to Natural Gas Utility Regulatory and Policy Structures to Meet State Greenhouse Gas Reduction Goals

DOCKET NO. G999/CI-21-565

**REPLY COMMENTS OF THE OFFICE  
OF THE ATTORNEY GENERAL—  
RESIDENTIAL UTILITIES DIVISION**

The Office of the Attorney General—Residential Utilities Division (OAG) respectfully submits the following reply comments in response to CenterPoint Energy, Fresh Energy and the Minnesota Center for Environmental Advocacy (MCEA), Center for Energy and the Environment (CEE), and the Citizens Utility Board (CUB). First, the OAG responds to CenterPoint’s claim of a five-year payback period for new customers to pay off the line- and main-extension allowances. Second, the OAG responds to the recommendations in the report attached to Fresh Energy and MCEA’s comments from Javelina Energy. Third, the OAG compares the recommendations for ongoing review from CEE with the OAG’s own recommendations. Last, the OAG appreciates CUB’s recommendation for ongoing discussions on gas utilities’ role in achieving Minnesota’s 2050 net-zero goals, and the OAG would be available to participate in any discussions ordered or encouraged by the Commission.

**I. CENTERPOINT’S CLAIMED AMOUNT OF TIME FOR NEW CUSTOMERS TO PAYBACK THE COST OF THE EXTENSION ALLOWANCES IS INACCURATE.**

Several commenters in the docket, including the OAG, used CenterPoint’s Extension of Free Footage Justification from CenterPoint rate cases to discuss the amount of time it will take

new customers to pay back any line extension allowances and provide benefits to existing utility customers.<sup>1</sup> As explained in the OAG’s initial comments:

A common rationale for line- and main- extension allowances is that adding a new customer will benefit existing customers because the new customer will contribute to the system’s fixed costs, spreading those costs over sales from more customers. But serving the additional customer will require the utility to incur new costs. If the utility socializes those new costs to all customers, it will take time for the new customer to pay back the cost of the extension and start contributing towards system fixed costs.<sup>2</sup>

There are several different ways, however, to measure how much time it will take a new customer to provide a benefit to existing customers—the “payback period.”<sup>3</sup> Some of measures of this “payback period,” however, are more reasonable than others.

CenterPoint claims in its initial comments that new customers provide benefits beginning in the fifth year after installation.<sup>4</sup> As the OAG explained in initial comments, however, CenterPoint uses multiple ways to calculate the payback period.<sup>5</sup> The method that results in the five-year payback period is the shortest. While CenterPoint provides an updated cost calculation to support its payback-period claim,<sup>6</sup> it provides only its preferred payback period of five years in the public version of Attachment A to its initial comments. The trade secret version, meanwhile, includes the two additional methods discussed by the OAG in initial comments.

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<sup>1</sup> See OAG Initial Comments at 11-14, Attach. 4; Fresh Energy and MCEA Comments, Attach. A (Javelina Report). While the OAG used CenterPoint’s cost justification to illustrate various principles, the OAG does not, however, agree that CenterPoint’s cost justification accurately depicts the complete costs to connect and serve new customers or the amount of non-gas revenues.

<sup>2</sup> OAG Initial Comments at 12.

<sup>3</sup> *Id.* at 12-14.

<sup>4</sup> CenterPoint Initial Comments at 6, Attach. A.

<sup>5</sup> OAG Initial Comments at 12-14.

<sup>6</sup> For the reasons stated in the OAG’s initial comments, there are several additional aspects of CenterPoint’s cost justification that the OAG believes are unreasonable. The OAG, however, finds the justification a useful example to illustrate different ways of calculating payback periods.

CenterPoint's line extension cost justification includes both a "current" free-footage scenario (with 100' main and 75' service line), and a "proposed" free-footage scenario (113' main and 75' service line).<sup>7</sup> In CenterPoint's five-year payback period claim, as explained in the OAG's initial comments, the fifth year is simply the year when the new customers revenues are greater than their costs.<sup>8</sup> But for several previous years, the new customer was subsidized by existing customers, and to benefit those existing customers the new customers must first pay those subsidies back.<sup>9</sup> Line 22b of Attachment A to CenterPoint's initial comments shows the subsidy incurred in previous years and illustrates a different payback period than CenterPoint's five year claim.<sup>10</sup> In this net present value analysis, Line 22b, the new customer does not begin paying a positive amount, benefiting the existing customers, until year 10 in the current free-footage scenario (Current Tab), and not until year 16 in the proposed free-footage scenario (Scenario Tab).<sup>11</sup>

Under a third measure, the payback period is still different. Line 30 of CenterPoint's Attachment A depicts the net present value using its Traditional Cash Flow analysis. Under this analysis the new customer does not begin to benefit the system until Year 16 in the current free-footage scenario (Current Tab), or until Year 18 in the proposed free-footage scenario (Proposed Tab).

The OAG believes it is unreasonable to consider the new customer as benefiting the system, or paying back the allowance subsidy, by looking to simply the first year where revenues exceed

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<sup>7</sup> CenterPoint Initial Comments at 6, Attach. A (Summary Tab).

<sup>8</sup> CenterPoint Initial Comments at 6, Attach. A.

<sup>9</sup> See OAG Initial Comments at 31 ("If the assumed payback period in the utility's line extension policy only examined when customer revenues were greater than the revenue requirement from the extension, as Line 22 does, it ignores the fact that the new customer had not yet paid back current customers for the cost of the extension.").

<sup>10</sup> See CenterPoint Initial Comments, Attach. A.

<sup>11</sup> See CenterPoint Initial Comments, Attach. A.

costs. Instead, the new customer must also pay back the accumulated subsidy from past years in order to benefit existing customers. While the payback period only accounts for the direct economic benefits to existing customers and does not measure the more qualitative benefits of providing public utility gas service to new customers, the Commission should begin its analysis from a reasonable starting place.

Determining a reasonable period for new customers to pay back the costs of extending service to them is necessary to determine the reasonableness of a utility's extension allowances. The OAG reiterates that it is the Commission, not a utility, that is in the best position to determine what is a reasonable payback period for new customers to return the cost of extending service to them. To accomplish this, the Commission must have accurate information about the full cost of extending and providing service, a reasonable estimate of annual revenues, and a reasonable methodology for estimating the length of the payback period.<sup>12</sup> But the Commission must also exercise its judgment in setting the payback period, whether it be 5, 10, or any number of years. In doing so, the Commission can consider ratemaking principles, current and future concerns about the gas industry, environmental externalities or health impacts of gas service, consumer protection benefits of regulated gas service, and any number of other relevant considerations in making this policy judgement. For that policy judgment to be sound, however, the payback period must be calculated as the time when a new customer not only begins paying more than their costs in that year, but has also paid back any previously incurred subsidies. CenterPoint's assessment of a five-year payback period should not be the starting point for the Commission's assessment.

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<sup>12</sup> OAG Initial Comments at 30-31.

## II. THE OAG AGREES WITH SEVERAL OF THE JAVELINA REPORT'S CRITIQUES OF UTILITIES' EXTENSION ALLOWANCE JUSTIFICATIONS BUT DISAGREES WITH OTHERS.

Fresh Energy and MCEA retained Javelina Energy “to examine the economic analyses used by Minnesota’s investor-owned gas utilities to justify their line extension subsidies.”<sup>13</sup> The Javelina Report includes several critiques of the utilities line extension cost justifications,<sup>14</sup> including:

- Underestimating construction costs
- Omitting metering costs
- Omitting ongoing customer costs
- Overestimating gas usage
- Omitting statutory compliance costs
- Using unreasonably long time periods<sup>15</sup>
- Omitting fixed labor costs
- Omitting service line costs<sup>16</sup>

The Javelina Report also faults the utilities’ extension allowances for not considering societal externality costs—e.g., greenhouse gas emissions and public health costs—resulting from increased gas usage.<sup>17</sup>

Several of the Javelina Report’s critiques utility’s extension allowance justifications or customer extension models match those identified by the OAG. This includes some utilities omission of metering costs and overestimation of gas usage.<sup>18</sup> Several other critiques in the Javelina Report match the OAG’s overall recommendation that gas utilities extension justifications

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<sup>13</sup> Fresh Energy & MCEA Initial Comments at 10.

<sup>14</sup> *Id.*, Attach. A (hereinafter Javelina Report).

<sup>15</sup> The OAG notes that the “unreasonably long time periods” discussed in the Javelina Report appear to refer to the length of time over which the costs of the extension allowance are depreciated. This is distinguishable from the “payback period” discussed above. The “payback period” refers to the amount of time that the new customer will take to benefit existing customers, whereas the depreciation period refers to the number of years over which the capital cost of the allowance estimated to be recovered through rates.

<sup>16</sup> Javelina Report at 3.

<sup>17</sup> Javelina Report at 13-14.

<sup>18</sup> *See* OAG Initial Comments at 25-29.

or extension models should include all costs of extending and providing service to new customers—specifically underestimating construction costs, omitting ongoing customer costs, omitting fixed labor costs, and omitting service line costs. The OAG remains supportive of utilities’ extension allowance justifications including *all* costs to extend and provide service to new customers in and only reasonable estimates of new customer revenues.

However, the OAG differs from the Javelina Report in three respects. First, the OAG does not agree that the utilities should include a 25-year depreciation period in their extension allowance justifications. Instead, the utilities should use the depreciation period authorized in their most recently approved depreciation certifications. Second, the OAG is concerned that it will be too difficult to determine an accurate estimate of future statutory compliance costs. Last, while the OAG agrees that externality costs are important considerations, this is a factor that the Commission could account for when exercising its judgment to determine the appropriate payback period, rather than including these difficult to estimate costs in an extension allowance cost justification calculation. The OAG recognizes, however, that neither the statutory compliance costs nor the externality costs were included in the Javelina Report’s Updated Line Extension Subsidy Calculation.<sup>19</sup>

The Javelina Report critiques the utilities extension allowance justifications for having unreasonably long time periods. As the report notes, these periods range from 29 years to 49 years and align with the relatively long useful life potential of utility assets, but go beyond the year 2050 and Minnesota’s state policy of achieving net-zero emissions.<sup>20</sup> In its Updated Line Extension Subsidy Calculation, the Javelina Report, therefore, uses a 25-year time period (2025 to 2049).<sup>21</sup>

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<sup>19</sup> Javelina Report at 13.

<sup>20</sup> *Id.* at 10.

<sup>21</sup> *Id.* at 12.

The OAG believes that extension allowance justifications are most useful when they compare the actual cost of extending and providing service to new customers with an accurate estimate of revenues from those customers to determine the payback period. The actual costs should include the capital costs of line and main extensions. The cost of utility capital assets, including mains and service lines, is recovered through rates by depreciating the cost throughout the asset's estimated useful life.<sup>22</sup> To determine that useful life, utilities are required to periodically file depreciation studies.<sup>23</sup> By Commission rule, the goal is to distribute the cost of capital assets, less salvage value, over the estimated useful life of the asset.<sup>24</sup>

To accurately represent the length of time until a new customer begins to economically benefit the system, it's important for the extension allowance justification to use the same period over which the capital costs are depreciated as is used in utility rates. For that reason, the OAG does not agree with the Javelina Report that the depreciation period should be over 25-years to match the 2050 net-zero goal. Instead, the depreciation period in the extension allowance justification should match the most recent depreciation certification authorized by the Commission for those assets.

The Javelina Report also critiques utilities' extension allowance justification for omitting statutory compliance costs. As the report explains, "adding a new customer will increase a utility's sales, and thus require additional action to meet its annual energy savings requirement" in addition to other costs that may be needed from gas utilities if Minnesota is to meet its 2050 net zero emissions goal, such as through NGIA pilots.<sup>25</sup> The OAG agrees that meeting energy-savings goals

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<sup>22</sup> Minn. R. 7825.0500, subp. 7.

<sup>23</sup> Minn. R. 7825.0700.

<sup>24</sup> Minn. R. 7825.0500, subp. 7.

<sup>25</sup> Javelina Report at 9.

and the 2050 net-zero goal will likely require additional costs. For example, CenterPoint estimated its initial NGIA plan to have \$195 million in lifetime utility costs.<sup>26</sup>

While the OAG agrees that these costs are likely to increase, it's less clear that an accurate estimate of these costs can be determined that would be reasonable to embed in an extension allowance justification. As described above, the extension allowance calculation should provide accurate estimates of both the costs to extend and provide service to the new customer and the revenues from the new customer. From the OAG's perspective, it would be difficult to estimate with accuracy the ongoing costs of complying with state goals in the face of a dynamically shifting gas market and evolving technologies. The OAG recognizes, however, that the Javelina Report did not attempt to include such an estimate in its Updated Line Extension Subsidy Calculation.<sup>27</sup> That being said, the Commission should consider and account for the potential of rising costs of complying with energy efficiency and gas innovation regulations as it exercises its judgment to determine a reasonable payback period for extension allowances.

Similarly, the Javelina Report notes that utilities extension allowance calculations do not include societal externality costs, such as the cost of greenhouse gas emissions or costs to public health.<sup>28</sup> As with statutory compliance costs, the Javelina Report did not include externality costs in its Updated Line Extension Subsidy Calculation.<sup>29</sup> Externality costs are complex to estimate in comparison to the relatively simple extension allowance justifications. Including accurate externality costs in these calculations would be contentious and complex to calculate—particularly since the externalities of additional natural gas emissions would fairly need to be viewed in

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<sup>26</sup> See Docket No. 23-215, CenterPoint Reply Comments, Ex. A at 2.

<sup>27</sup> Javelina Report at 13.

<sup>28</sup> *Id.* at 13-14.

<sup>29</sup> *Id.* at 13.

comparison to the externalities of alternative heating options. Instead of attempting to perform such a calculation, the Commission may consider impacts to greenhouse gas emissions and public health as it exercises its judgment to determine a reasonable payback period.

In sum, the OAG agrees with the Javelina Report that several known costs to extend and provide service to new customers should be included in any extension allowance calculation. However, the OAG disagrees that a 25-year period should be used to depreciate these costs, and instead utilities should use the depreciation period for these capital assets set in their most recent depreciation certification. Regarding statutory compliance costs and externalities, the OAG is concerned that it would be difficult to accurately estimate these costs. Instead, the Commission should consider future costs of meeting state goals and impacts to the environment and public health in exercising its judgment to determine an appropriate payback period.

**III. THE OAG APPRECIATES CEE’S PROPOSAL TO REVISIT THESE ISSUES PERIODICALLY, BUT EMPHASIZES THAT UTILITIES MUST CONTINUE TO SHOW THAT EXTENSION ALLOWANCES BENEFIT EXISTING CUSTOMERS WITHIN A REASONABLE TIME PERIOD.**

In initial comments, the OAG recommended that the gas utilities update their tariffs to establish new free footage allowances or customer extension models that do not include unreasonable assumptions about costs and customer usage or include discretionary CIAC waivers. This initial update could either occur within the Future of Gas docket, or utilities could be ordered to file miscellaneous tariff filings in new dockets within a certain timeframe. In addition to this initial update, the OAG recommended the Commission periodically revisit extension allowances to review the policies with updated cost and usage information, but also address several ongoing questions.<sup>30</sup>

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<sup>30</sup> See OAG Initial Comments at 36-40.

CEE similarly recommends new criteria to apply in utility specific proceedings in the form of questions that utilities filing new or modified line extension tariffs must demonstrate.<sup>31</sup> CEE’s recommended questions are provided in the right-hand column and the OAG’s recommended issues are provided in the left-hand column for comparison below:

#	OAG	CEE
1	Whether the utility’s free footage or service extension allowance included the majority of all new extensions with only the extremely long extensions requiring a CIAC.	How does the tariff support and serve Minnesota’s greenhouse gas emission reduction goals?
2	Whether the utility’s free footage or extension allowance ensures that existing customers will benefit from new customers additions to the system within a reasonable time period. Utilities should include a determination that: <ul style="list-style-type: none"> <li>a. The assumed revenues from the new customer include a reasonable estimate of use per customer that accounts for potential declining customer usage from energy efficiency and electrification of heating and appliances.</li> <li>b. All costs of serving the new customer are included in the calculation.</li> <li>c. The length of the payback period and the methodology used to calculate it are reasonable.</li> </ul>	How does the tariff consider actions taken by the Commission and the Department in other proceedings, including but not limited to Gas Integrated Resource Plans, Natural Gas Innovation Act Plans, Energy Conservation and Optimization Plans, and other utility pilots, programs, and rate design offerings?
3	If offered, whether the utility’s extension charge refund policy is appropriate.	How does the tariff consider affordability and ratepayer protections related to both existing and new customers?
4	Whether the utility’s extension allowance should be measured in number of feet (i.e. free footage) or be based on an estimate of the customer’s estimated usage (taking into account square footage, number of gas appliances, non-gas heating equipment, etc.).	How does the tariff consider the differences in serving different customer types, such as whether service is being extended to new structures or existing structures without gas service?

<sup>31</sup> CEE Initial Comments at 8-9.

5	Whether offering free footage or an extension allowance continues to be reasonable in light of current and forecasted gas-system utilization, advances in technology, state and federal policy, and risks to ratepayers of stranded assets or an overbuilt system.	How does the tariff consider the viability and affordability of alternative heating methods?
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The OAG believes CEE’s criteria are helpful considerations. The OAG supports the considerations that the OAG provided in initial comments in addition to whichever of the considerations above the Commission would find helpful.<sup>32</sup>

There is some overlap in the considerations proposed by CEE and the OAG, such as with the question regarding gas conservation and innovation and affordability and ratepayer protections for new and existing customers. But the OAG emphasizes that there should be ongoing analysis of whether existing customers will benefit from the addition of new customers within a reasonable time period. And that consideration requires detailed analysis of utilities’ extension-of-service models or cost justifications for their extension policies. For that reason, it is important to require periodic consideration of whether the utility’s free footage or extension allowance ensures that existing customers will benefit from new customer additions to the system within a reasonable time period. This should include a determination that (a) the assumed revenues from the new customer include a reasonable estimate of use per customer, (b) all costs of serving the new customer are included in the calculation, and (c) the length of the payback period and the methodology used to calculate it are reasonable.<sup>33</sup>

The OAG’s final issue is not addressed in CEE’s criteria. While the OAG does not believe that it is currently time for the Commission to order all gas utilities to cease offering extension

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<sup>32</sup> OAG Initial Comments at 37.

<sup>33</sup> *See id.*

allowances in a broad policy determination, this may change depending on how gas usage and extension costs shift in the coming years.<sup>34</sup> For this reason, if the Commission continues to permit extension allowances, gas utilities periodically must show these extension allowances continue to be reasonable in light of forecasted gas-system utilization, advances in technology, state and federal policy, and risks to ratepayers of stranded assets or an overbuilt system.

#### **IV. THE OAG SUPPORTS CUB'S RECOMMENDATION FOR STRUCTURED CONVERSATIONS TO ENCOURAGE GAS UTILITIES TO PURSUE THE 2050 NET-ZERO GOAL.**

On the topic of other issues the Commission should consider, CUB recommends exploring additional ways the Commission can encourage and measure gas utilities progress in meeting the statewide greenhouse gas reduction goals. Minnesota Statutes section 216H.02, subdivision 1 provides a goal to reduce statewide greenhouse gas emissions across all sectors producing emissions from 2005 amounts by 30% in 2025, 50% in 2030 and to net zero by 2050.

While the OAG does not believe that eliminating line and main extension allowances is presently in the public interest, the OAG agrees with CUB that the Commission has a central role in ensuring that gas utilities operate in light of the goals laid out in section 216H.02.<sup>35</sup> From the OAG's perspective, the statewide greenhouse gas reduction goals, while not mandatory, are an important state policy. Minnesota's gas utilities, which contribute both direct and indirect emissions, must be central and willing participants in these reductions for the state to meet this goal. If the gas utilities fall behind, this could create not only societal costs but also significant ratepayer costs if abrupt reductions in gas usage become necessary to meet either the current state policy or potential future regulations.

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<sup>34</sup> Applying these modifications to calculate a reasonable extension allowance may result in a utility offering no or very little free footage. OAG Initial Comments at 38 n.115. But going through this cost based exercise for each utility is necessary to make this determination.

<sup>35</sup> CUB Initial Comments at 22.

CUB suggests one method for encouraging the gas utilities to move more deliberately towards the 2050 net zero goal—setting benchmarks with interim goals specific to the utilities. CUB focuses on the need for ongoing stakeholder input and utility modeling in this endeavor. To this end, CUB recommends the Commission request the Great Plains Institute (GPI) to engage with the Gas Utility Innovation Roundtable to consider “what decarbonization benchmarks the gas utility sector must meet in order to enable the state to reach its statutory net zero goal, and that GPI report its process and conclusions to the Commission.”<sup>36</sup> The OAG defers to GPI on whether it has the resources or interest in taking on this endeavor. The OAG will gladly engage on the subject and participate in whatever stakeholder process the Commission sets forth.

### CONCLUSION

The OAG appreciates the ongoing dialogue on this important issue. The OAG will provide its final recommendations for Commission consideration in supplemental comments.

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Respectfully submitted,

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<sup>36</sup> *Id.*