Minnesota Energy Resources Corporation
Suite 200
1995 Rahncliff Court
Eagan, MN 55122
www.minnesotaenergyresources.com

November 17, 2020

VIA ELECTRONIC FILING

Will Seuffert
Executive Secretary
Minnesota Public Utilities Commission
121 Seventh Place East, Suite 350
St. Paul, MN 55101

Re: In the Matter of the Petition of Minnesota Energy Resources Corporation for Extension of Rule Variances to Recover the Costs of Financial Instruments Through the Purchased Gas Adjustment
Docket No. G011/M-20-____

Dear Mr. Seuffert:

Enclosed please find the petition of Minnesota Energy Resources Corporation ("MERC" or the "Company") for approval of a four-year extension of variances allowing the recovery of costs of financial instruments through the purchased gas adjustment ("PGA"). MERC's current variances to the PGA Rules expire on June 30, 2021. MERC requests the Commission to act to extend its variances before June 30, 2021, to allow the Company to continue to use the PGA to recover the incurred costs of financial instruments used for hedging purposes in procuring natural gas supplies for its Minnesota customers.

MERC has served a copy of this petition on the Department of Commerce, Division of Energy Resources and the Office of the Attorney General – Residential Utilities and Antitrust Division. A summary of the filing has been served on all parties on the Company's attached service list.

Please contact me at (414) 221-4208 if you have any questions regarding the information in this petition. Thank you for your attention to this matter.

Sincerely,

Joylyn C. Hoffman Malueg

Joylyn C. Hoffman Malueg
Project Specialist 3
Minnesota Energy Resources Corporation

Enclosure
cc: Service List

STATE OF MINNESOTA
BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Katie J. Sieben	**Chair**
Valerie Means	**Commissioner**
Matthew Schuerger	**Commissioner**
Joseph K. Sullivan	**Commissioner**
John A. Tuma	**Commissioner**

In the Matter of the Petition of Minnesota Energy Resources Corporation for Extension of Rule Variances to Recover Costs of Financial Instruments Through the Purchased Gas Adjustment

Docket No. G011/M-20-____

SUMMARY OF FILING

Pursuant to Minnesota Rule 7829.3200, Minnesota Energy Resources Corporation ("MERC" or the "Company") hereby petitions the Minnesota Public Utilities Commission ("Commission") for an order granting an extension of variances to Minnesota Rules 7825.2400, 7825.2500, and 7825.2700 (the "Purchased Gas Adjustment Rules" or "PGA Rules") to use the purchased gas adjustment ("PGA") to recover the incurred costs of financial instruments used for hedging purposes in procuring natural gas supplies for Minnesota customers. The Commission first granted the variances at issue to MERC by Order dated July 10, 2007, in Docket No. G007,011/M-06-1358. The Commission subsequently issued an Order extending those variances on June 30, 2009, in Docket No. G007,011/M-09-262; on August 17, 2011, in Docket No. G007,011/M-11-296; on June 21, 2013, in Docket No. G007,011/M-13-207; on May 28, 2015, in Docket No. G011/M-15-231, and on May 8, 2017, in Docket No. G011/M-18-75. The most recent Order extended the Company's variances through the period ending June 30, 2021. With this Petition, MERC requests extensions of the variances to the PGA Rules for four years, through June 30, 2025.

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PETITION

Pursuant to Minnesota Rule 7829.3200, Minnesota Energy Resources Corporation ("MERC" or the "Company") hereby petitions the Minnesota Public Utilities Commission ("Commission") for an order granting an extension of variances to Minnesota Rules 7825.2400, 7825.2500, and 7825.2700 (the "Purchased Gas Adjustment Rules" or "PGA Rules") to use the purchased gas adjustment ("PGA") to recover the incurred costs of financial instruments used for hedging purposes in procuring natural gas supplies for Minnesota customers. The Commission first granted the variances at issue to MERC by Order dated July 10, 2007, in Docket No. G007,011/M-06-1358. The Commission subsequently issued an Order extending those variances on June 30, 2009, in Docket No. G007,011/M-09-262; on August 17, 2011, in Docket No. G007,011/M-11-296; on June 21, 2013, in Docket No. G007,011/M-13-207; on May 28, 2015, in Docket No. G011/M-15-231, and on May 8, 2017, in Docket No. G011/M-18-75. The most recent Order extended the Company's variances through the period ending June 30, 2021. With this Petition, MERC requests extensions of the variances to the PGA Rules for four years through June 30, 2025.

I. SUMMARY OF FILING

Pursuant to Minn. R. 7829.1300, subp. 1, a one-paragraph summary of the filing is attached.

II. SERVICE

Pursuant to Minn. R. 7829.1300, subp. 2, MERC has served a copy of this Petition on the Department of Commerce, Division of Energy Resources ("Department") and the Office of the Attorney General – Residential Utilities Division ("OAG"). A summary of the filing has been served on all parties on the attached service list.

III. GENERAL FILING INFORMATION

A. Name, Address, and Telephone Number of Filing Party

Minnesota Energy Resources Corporation
2685 145th Street West
Rosemount, MN 55068

(651) 322-8901

B. Name, Address, Electronic Address, and Telephone Number of Attorney for the Filing Party

Kristin M. Stastny
Taft Stettinius & Hollister LLP
2200 IDS Center
80 South 8th Street
Minneapolis, MN 55402
KStastny@Taftlaw.com
(612) 977-8656

C. Date of Filing

The date of the filing is November 17, 2020. MERC respectfully requests that the Commission grant the requested PGA Rule variances by June 30, 2021.

D. Statute Controlling Schedule for Processing the Filing

No statute controls the schedule for processing this filing. Under Minn. R. 7829.0100, subp. 11, the requested variances fall within the definition of a "Miscellaneous Tariff Filing" because no determination of MERC's general revenue requirement is necessary. Under Minn. R. 7829.1400, initial comments on a miscellaneous filing are due within 30 days of filing, with reply comments due 10 days thereafter.

E. Signature, Electronic Address, and Title of Utility Employee Responsible for Filing

Joylyn C. Hoffman Malueg

Joylyn C. Hoffman Malueg
Project Specialist 3
joylyn.hoffmanmalueg@wecenergygroup.com
2685 145th Street West
Rosemount, MN 55068
(414) 221-4208

IV. DESCRIPTION AND PURPOSE OF FILING

A. Background

On July 10, 2007, in Docket No. G007,011/M-06-1358, the Commission issued an Order granting MERC variances to the PGA Rules. The Commission extended these variances on June 30, 2009, in Docket No. G007,011/M-09-262; on August 17, 2011, in Docket No. G007,011/M-11-296; on June 21, 2013, in Docket No. G007,011/M-13-207; on May 28, 2015, in Docket No. G011/M-15-231, and most recently on May 8, 2017, in Docket No. G011/M-17-85. In that docket, the Commission extended the variances through the period ending June 30, 2021.

The Commission's May 8, 2017, Order in Docket No. G011/M-17-85 authorized MERC to continue to engage in certain limited financial transactions to minimize price volatility of natural gas purchased to serve Minnesota customers, subject to certain limitations and an annual hedging cost cap. In addition to granting this authorization, the Commission:

- Left the cap on the amount of financial hedging set at 30 percent of total projected heating-season sales volumes for the combined MERC system.
- Continue the accounting practices required by the existing variance.
- Required the Company to continue to include information on the costs and benefits of financial instruments in its monthly PGA filings and annual Demand Entitlement and Annual Automatic Adjustment filings.
- Required the Company to provide, in its Annual Fuel Report filed yearly on or about September 1st, a full post-mortem analysis of its hedged volumes for the preceding heating season compared to other hedging strategies and the prevailing market prices strategy.
- Required the Company, in its next request for a PGA rule variance, to demonstrate that ratepayers benefit from hedging and that there is not an undue price penalty.

This Petition is consistent with prior approvals and includes continuation of all prior reporting requirements. Consistent with the Commission's recent Order in Docket No. G011/M-17-85, MERC is requesting a four-year variance extension.

B. <u>Proposed Variances</u>

MERC is requesting an extension of variances to Minn. R. 7825.2400, 7825.2500, and 7825.2700, to continue to recover the costs of financial instruments such as futures and options contracts through the PGA to mitigate the risks of price volatility for retail gas customers.

1. *Extension of Variance*

The existing variance expires June 30, 2021. MERC is proposing a four-year extension that would apply to financial positions entered into through June 30, 2025. A four-year extension of the variances would enable MERC to use financial instruments for the next four heating seasons (2021-2022; 2022-2023; 2023-2024; and 2024-2025) while also leaving ample opportunity for MERC to request, and the Commission and the Department to review, a subsequent extension petition before the variance ends.

MERC proposes that the extension be conditioned on MERC continuing to provide the reports required in Docket Nos. G007,011/M-03-821, G007,011/M-06-1358, G007,011/M-09-262, G007,011/M-13-207, G011/M-15-231, and G011/M-17-85. These reports allow the Department and the Commission to regularly review MERC's financial instrument practices. If the Commission determines at some point during the extension period that the PGA Rule variance for financial instrument cost recovery is resulting in excessive costs to ratepayers, the Commission has the authority to disallow the costs or terminate the variance prior to June 30, 2025.

2. *Accounting*

MERC proposes to continue the accounting practices required by the existing variance, such that MERC would continue to record the cost associated with all financial instruments to FERC Account 804. MERC will continue to recover these costs through the commodity portion of rates.

3. *Permitted Financial Instruments*

MERC proposes to continue to use the mix of financial instruments permitted in the existing variances, including fixed-price, index-price, and swing contracts. As under the existing variances, MERC would be permitted to use put options in combination with call options to form a "collar," but would not be permitted to use put options for any other reason without Commission approval.

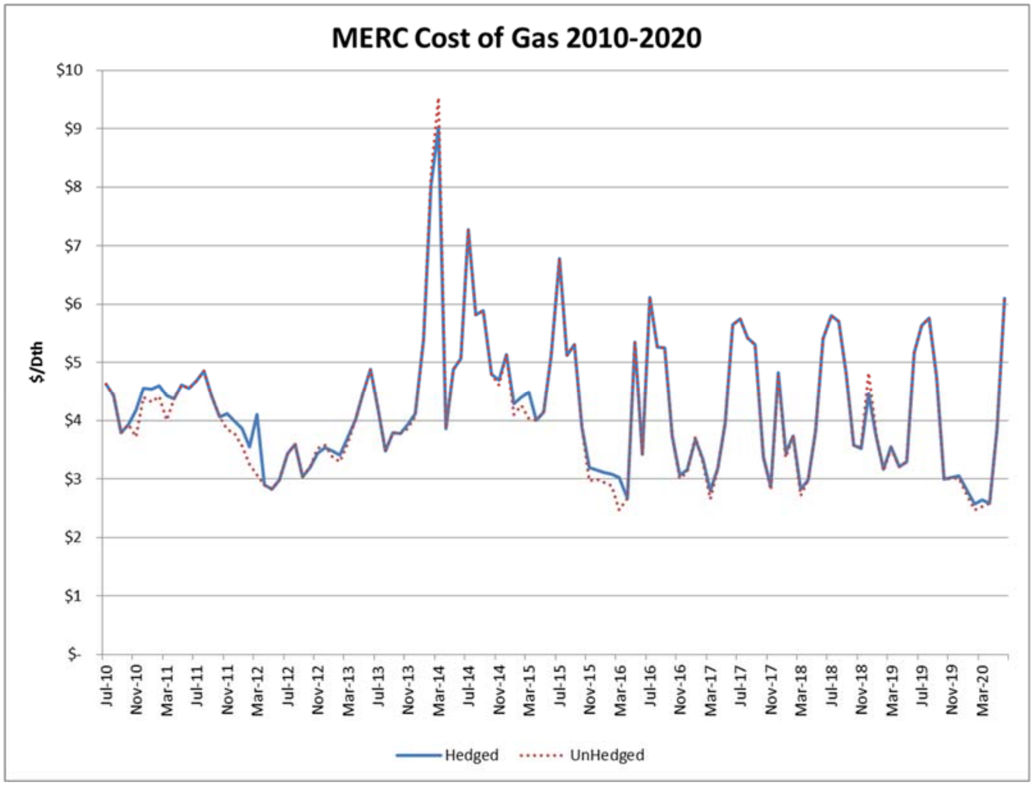
4. *Cap on Amount of Financial Hedging*

MERC proposes that the current cap of up to 30 percent of total projected heating season sales volumes remain in place. It is MERC's strategy to hedge 30 percent of total projected normal winter requirements with the use of financial instruments.

C. <u>Ratepayer Benefit</u>

In the May 8, 2017, Order issued in Docket No. G011/M-17-85, the Commission required that MERC demonstrate in its next request for PGA Rule variances that ratepayers benefit from hedging and that there is not an undue price penalty. MERC's use of financial instruments over the July 2010 through June 2020 time period has resulted in a 10.9 percent reduction in winter price volatility while accounting for 1.7 percent of the total cost of gas over the same period. Such reductions in price volatility benefit MERC's ratepayers by providing increased price certainty.

MERC purchases natural gas call option contracts representing up to 20 percent of each winter month's forecast gas requirement. Natural gas future contracts representing up to 10 percent of each winter month's price forecast are purchased as well. The impact of hedging (including gains and costs) on the price of purchased gas is shown in the following chart.



The information in the chart, and in the analysis in Attachment A filed contemporaneously with this Petition, demonstrates that the price increase due to hedging is relatively low when considering the benefit of reduced price volatility and protection from large winter price swings.

Over the period spanning July 2010 to June 2020, the summation of hedging costs represented 1.7 percent of the total cost of gas.

MERC has continually refined its hedging strategy to reduce the premiums paid for call options, while still providing upside price protection. This strategy change has improved results dramatically. The most recent five-year period spanning July 2015 to June 2020 has hedging costs that represent only 1.3 percent of the total cost of gas. Volatility reduction has remained consistent over this period from 10.9 percent (2010-2020) to 10.7 percent (2015-2020).

Financial hedging is unlikely to provide lower costs than not utilizing financial hedging over time. However, the reduction in volatility and corresponding increase in bill certainty is a valuable benefit of hedging for MERC and its ratepayers that has come at a reasonable cost.

V. APPLICATION OF VARIANCE STANDARDS

MERC must obtain Commission approval of variances from three Commission rules in order to recover the costs of its hedging program through the PGA. These rules are:

- Minn. R. 7825.2400, subp. 12, which defines the cost of purchased gas as the cost of gas defined by the Minnesota uniform system of accounts, including specific accounts set forth by the Federal Energy Regulatory Commission ("FERC"), and defines "demand delivered gas cost" as the portion of the cost of purchased gas "other than the commodity-delivered gas costs," including "associated costs incurred to deliver the gas to the utility's distribution system."

- Minn. R. 7825.2500(B), which permits an automatic adjustment of charges for "changes in the cost of commodity-delivered gas cost and demand-delivered gas cost for purchased gas."
- Minn. R. 7825.2700, which permits natural gas utilities to file to adjust retail rates on a monthly basis to reflect changes in the delivered cost of the commodity natural gas, pipeline and contract storage capacity, and peak-shaving supplies purchased for resale.

Minn. R. 7829.3200 provides that the Commission may grant a variance to its rules if it finds that:

1. Enforcement of the rule would impose an excessive burden upon the applicant or others affected by the rule;
2. Granting the variance would not adversely affect the public interest; and
3. Granting the variance would not conflict with standards imposed by law.

A. Enforcement of the Rule Would Impose an Excessive Burden on MERC and Its Customers

The requested extension of variances will allow MERC to continue its current practice of financially hedging 30 percent of forecast winter sales. The cost of hedging, relative to the total cost of gas, over the 2010 to 2020 period was approximately 1.7 percent. Hedging has reduced winter price volatility by approximately 10.9 percent over the same timeframe.

Although natural gas prices have been fairly stable over the last several years, the market is susceptible to events beyond MERC's control. Shifts in energy policy, extreme weather, and physical infrastructure (e.g., pipeline) damage, while rare, have the potential to dramatically affect natural gas prices. The purpose of MERC's hedging strategy is to mitigate price volatility that could arise from events such as these and to do so at a cost that still allows the Company to provide reasonably-priced natural gas. Enforcement of the PGA Rules would prevent MERC from using a widely accepted industry approach to protecting utility customers from undue harm in a fluctuating market. Therefore, enforcement of the PGA Rules would impose an excessive burden on MERC and its ratepayers. The Company's hedging analysis spreadsheet, filed contemporaneously with this Petition as Attachment A, provides support for the conclusion that enforcement of the rules would impose an excessive burden on the Company.

B. The Public Interest is Not Adversely Affected By Varying the Rule

The public interest would not be adversely affected by granting the requested extension of variances. As the Commission and the Department determined in Docket Nos. G007,011/M-06-1358, G007,011/M-09-262, G007, 011/M-11-296, G007,011/M-13-207, G011/M-15-231, and G011/M-17-85, ratepayers benefit from the use of financial instruments to mitigate natural gas volatility, and the responsible use of such instruments will be ensured by regulatory oversight for the duration of the extension.

C. The Proposed Variances Would Not Conflict With Standards Imposed By Law

The proposed variances do not conflict with any standards imposed by law. The Commission has previously granted the rule variances to MERC in Docket Nos. G007,011/M-06-1358, G007,011/M-09-262, G007,011/M-11-296, G007,011/M-13-207, G011/M-15-231, and G011/M-

17-85, and has granted similar PGA Rule variances to other Minnesota gas utilities. The Commission has therefore previously determined a variance to the PGA Rules does not conflict with standards imposed by law.

VI. EFFECT ON MERC'S REVENUE

The extension would allow recovery of the costs of financial instruments from MERC's retail natural gas customers pursuant to the PGA and annual PGA true-up. The additional revenue would be offset by the costs of the financial instruments and have no net change on MERC's earnings.

VII. CONCLUSION

MERC believes it is in the best interest of its ratepayers to be allowed the flexibility to recover through the PGA the incurred costs of financial instruments used for hedging purposes in procuring natural gas supplies for Minnesota customers. MERC respectfully requests that the Commission grant extensions to PGA Rule variances subject to the reporting requirements and limitations described above. MERC requests Commission action no later than June 1, 2021, so MERC may continue to engage in limited hedging transactions and recover the costs through the PGA.

Dated: November 17, 2020

Respectfully submitted,

/s/ Joylyn C. Hoffman Malueg

Joylyn C. Hoffman Malueg
Project Specialist 3
Minnesota Energy Resources Corporation

Petition of Minnesota Energy Resources Corporation for Extension of Rule Variances to Recover the Costs of Financial Instruments Through the Purchased Gas Adjustment

Docket No. G011/M-20-___

CERTIFICATE OF SERVICE

I, Colleen T. Sipiorski, hereby certify that on the 17th day of November, 2020, on behalf of Minnesota Energy Resources Corporation (MERC), I electronically filed a true and correct copy of the enclosed Petition for Extension of Rule Variances on www.edockets.state.mn.us. Said documents were also served via U.S. mail and electronic service as designated on the attached service list.

Dated this 17th day of November, 2020.

/s/ Colleen T. Sipiorski
Colleen T. Sipiorski

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
Michael	Ahern	ahern.michael@dorsey.com	Dorsey & Whitney, LLP	50 S 6th St Ste 1500 Minneapolis, MN 554021498	Electronic Service	No	GEN_SL_Minnesota Energy Resources Corporation_General Service List
Generic Notice	Commerce Attorneys	commerce.attorneys@ag.state.mn.us	Office of the Attorney General-DOC	445 Minnesota Street Suite 1400 St. Paul, MN 55101	Electronic Service	No	GEN_SL_Minnesota Energy Resources Corporation_General Service List
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Catherine	Phillips	Catherine.Phillips@wecenergygroup.com	Minnesota Energy Resources	231 West Michigan St Milwaukee, WI 53203	Electronic Service	No	GEN_SL_Minnesota Energy Resources Corporation_General Service List
Generic Notice	Residential Utilities Division	residential.utilities@ag.state.mn.us	Office of the Attorney General-RUD	1400 BRM Tower 445 Minnesota St St. Paul, MN 551012131	Electronic Service	No	GEN_SL_Minnesota Energy Resources Corporation_General Service List
Elizabeth	Schmiesing	eschmiesing@winthrop.com	Winthrop & Weinstine, P.A.	225 South Sixth Street Suite 3500 Minneapolis, MN 55402	Electronic Service	No	GEN_SL_Minnesota Energy Resources Corporation_General Service List
Will	Seuffert	Will.Seuffert@state.mn.us	Public Utilities Commission	121 7th Pl E Ste 350 Saint Paul, MN 55101	Electronic Service	No	GEN_SL_Minnesota Energy Resources Corporation_General Service List

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