BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Nancy Lange	Chair
Dan Lipschultz	Commissioner
Matthew Schuerger	Commissioner
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In the Matter of a Commission Investigation into Parameters for Competition Among Natural Gas Utilities Involving Duplication of Facilities and Use of Promotional Incentives and Other Payments

ISSUE DATE: September 19, 2018

DOCKET NO. G-999/CI-17-499

ORDER ADOPTING STANDARDS GOVERNING COMPETITION AMONG NATURAL GAS UTILITIES

PROCEDURAL HISTORY

I. Initial Order

On July 12, 2017, the Commission opened this investigation into the appropriate parameters for competition among natural gas utilities.

The investigation arose out of a complaint brought by Minnesota Energy Resources Corporation (MERC) against Northern States Power Company (Xcel) over Xcel's plan to extend natural gas service to a new Minnesota Vikings complex in Eagan (Vikings complaint).[1] MERC claimed that the complex could be served by MERC's existing gas infrastructure and that Xcel's planned service extension was inconsistent with state policy disfavoring the unnecessary duplication of facilities. MERC also alleged that Xcel had offered the Vikings a promotional incentive in violation of Minnesota law.

The Commission dismissed MERC's complaint but also concluded that a review of the appropriate parameters of gas-utility competition could provide useful guidance if and when similar disputes arise in the future. It also required Xcel and MERC to file all existing and future competitive service agreements setting forth the specific terms of the promotional incentives offered to new customers.

II. Notice for Comments

On September 26, 2017, the Commission issued a notice requesting that each natural gas utility file (1) a description of the process it uses to identify opportunities to extend service beyond its existing service borders to new areas or customers, and (2) a description of the promotional

[1] *See generally In the Matter of Minnesota Energy Resources Corporation's Complaint Against Northern States Power Company*, Docket No. G-011,002/C-17-305.

incentives or other payments it offers when extending service to areas or customers outside its existing service area.

The Commission also sought comment from utilities and other stakeholders on the following issues:

- How the Commission should evaluate and set the parameters of inter-gas-utility competition consistent with the provisions of Minn. Stat. § 216B.01;
- What criteria the Commission should use to evaluate whether there is unnecessary duplication of facilities;
- How the Commission should regulate the use of promotional incentives and other tariffed and non-tariffed payments that utilities offer to customers outside their existing service areas;
- What should be considered as other non-tariffed payments, e.g., co-sponsored advertising arrangements; and
- Whether natural gas utilities should be required to file copies of all existing and new competitive service agreements or similar agreements.

III. Stakeholder Comments

On October 31, the following five natural gas utilities filed comments describing how they identify opportunities to extend service and how they use promotional incentives:

- MERC
- Xcel
- CenterPoint Energy Resources Corp. (CenterPoint)
- Great Plains Natural Gas Co. (Great Plains)
- Greater Minnesota Gas, Inc. (GMG)

On November 30, the following parties filed comments addressing the five issues identified in the Commission's September 26 notice:

- MERC
- Xcel
- CenterPoint
- Minnesota Department of Commerce, Division of Energy Resources (Department)
- Office of the Attorney General, Residential Utilities and Antitrust Division (OAG)

In general, MERC and the OAG supported restrictions on competition to ensure fairness and limit the uneconomic duplication of gas infrastructure. The Department and the other utilities argued that the Commission's current framework for reviewing gas-service disputes was sufficient to protect the interests of utilities, existing ratepayers, and competed-for customers.

By January 2, 2018, the following parties had filed reply comments:

- MERC
- Xcel
- CenterPoint
- GMG
- The Department
- The OAG

IV. Second Notice for Comments

On March 30, the Commission issued a *Notice of Supplemental Comment Period* requesting comment on whether gas utilities should be required to stop offering unspecified competitive incentives or show cause why such offers should not be prohibited.

The supplemental notice resulted from a second complaint filed by MERC against Xcel regarding a property near the Vikings facility, wherein MERC again alleged that Xcel had offered a developer a promotional incentive to win the right to serve an area that could have been served by MERC's existing facilities (United Properties complaint). In response to this complaint, the Commission suspended Xcel's competitive-agreement tariff and determined that it would seek comment in this docket on whether to bar other utilities from using similar tariffs.[2]

By April 23, the following parties had filed comments in response to the supplemental notice:

- MERC
- CenterPoint
- The Department
- The OAG

MERC and the OAG recommended that the Commission prohibit the use of incentives, while the Department and CenterPoint (and Xcel, in reply comments) supported the continued use of incentives.

By April 30, the Commission had received reply comments from the following parties:

- MERC
- Xcel
- The Department

On July 26, 2018, the Commission met to consider the matter.

[2] *See In the Matter of Minnesota Energy Resources Corporation's Complaint Against Northern States Power Company*, Docket No. G-011,002/C-17-802, Order Dismissing Complaint, Suspending Tariff, and Soliciting Comment (April 10, 2018).

FINDINGS AND CONCLUSIONS

I. Summary of Commission Action

In this order, the Commission (1) adopts criteria for evaluating proposed gas service extensions, and specifically whether an extension would unnecessarily duplicate another utility's existing facilities, and (2) prohibits gas utilities from offering promotional incentives.

II. Duplication of Facilities

A. Introduction

While electric and telephone companies in Minnesota have designated service areas, natural gas utilities do not.

Because gas utilities do not have exclusive service territories, disputes occasionally arise when two utilities seek to serve the same customer or area. The Commission's approach in these situations has generally been to evaluate each dispute on its merits and in light of the statutory admonition that utilities should be regulated "in order to . . . avoid unnecessary duplication of facilities which increase the cost of service to the consumer."[3]

The Commission first examined gas utility competition on an industry-wide basis in the early 1990s. Western Gas Utilities had agreed to construct a pipeline to serve a preexisting customer of Minnegasco, and the Department recommended that the Commission seek input from interested parties regarding the legal and policy issues raised by the proposed pipeline.[4]

After taking comments and convening a study group of interested stakeholders, the Commission concluded that no categorical judgment on gas-utility competition was required.[5] While acknowledging the potential for wasteful duplication of facilities and higher per-customer costs, the Commission reasoned that some level of competition would help promote wider access to natural gas and reduce customers' heating costs.

The Commission concluded that it was capable of balancing the interests of utilities, competed-for customers, and current customers on a case-by-case basis. And it continued using this approach in the years that followed as gas utilities brought forward complaints about other utilities' proposed service extensions.[6]

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[3] Minn. Stat. § 216B.01.

[4] *See generally In the Matter of the Joint Venture Between Rahr Malting and Western Gas Utilities to Construct a Seven-Mile Gas Pipeline in Scott County, Minnesota*, Docket No. G-012/DI-90-227. Western Gas Utilities' system is now owned by Xcel, and Minnegasco was CenterPoint's predecessor.

[5] *In the Matter of an Inquiry into Competition Between Natural Gas Utilities in Minnesota*, Docket No. G-999/CI-90-563, Order Terminating Investigation and Closing Docket, at 5 (March 31, 1995).

[6] *See, e.g.*, *In the Matter of a Complaint of Peoples Natural Gas Against Northern States Power Company Regarding the Construction of Distribution Facilities,* Docket No. G-011/C-96-1062, Order Dismissing Complaint (October 21, 1996) (dismissing complaint of one utility against another for agreeing to serve planned developments adjacent to complaining utility's existing infrastructure); *In the Matter of the Complaint of Great Plains Natural Gas Company Against Peoples Natural Gas Company*

B. Positions of the Parties

1. MERC

MERC stated that it follows the “first-in-the-field” rule when competing with other utilities to serve new customers or areas. According to MERC, this means that “[w]hile utilities may actively compete for new customers in underserved or unserved areas lacking existing infrastructure, the first utility to build new facilities to serve those potential customers becomes the service provider for that area.”

Consistent with this practice, MERC recommended that the Commission prohibit a utility from extending natural gas service to a customer or area that is already being served by another utility or can be served by the other utility without the need to cross or duplicate existing infrastructure. If a utility wishes to extend service notwithstanding such duplication, MERC recommended requiring the utility to obtain the Commission’s approval to extend service and show that the duplication is in fact necessary.

MERC argued that resolving the issue on a case-by-case basis, as the Commission has done in the past, creates significant burdens for the agency, utilities, municipalities, and competed-for customers and discourages efficient development. It contended that adopting the first-in-the-field rule would minimize disputes between natural gas utilities, level the competitive playing field, and eliminate customer confusion.

2. The Department

The Department recommended that the Commission continue its current practice of evaluating gas-service disputes on a case-by-case basis. Specifically, the agency recommended that the Commission conduct a cost–benefit analysis of allowing competing utilities to serve a customer, taking into account the impact of either scenario on each of the following groups:

- The competed-for customer,
- The shareholders of the customer’s preferred utility,
- The shareholders of the non-preferred utility,
- The ratepayers of the preferred utility, and
- The ratepayers of the non-preferred utility.

The Department argued that MERC’s first-in-the-field rule could have the unintended consequence of making it more difficult for customers seeking natural gas service to get it. This is because gas utilities have no assigned service areas and are thus under no obligation to serve a customer who requests it. The Department’s argument appears to be that placing undue limits on gas-utility competition could prevent some customers from getting service, or at least increase their costs to do so.

and UtiliCorp United, Inc., Docket No. G-004, 011/C-91-731, Order Dismissing Complaint (December 20, 1991) (dismissing complaint of one utility against another for agreeing to serve expanded load of complaining utility’s existing customer).

3. The OAG

The OAG maintained that the current, complaint-based process for extending natural gas service does not ensure that new infrastructure is built at the lowest possible cost. It recommended that the Commission direct the parties to participate in a stakeholder group to develop a new process, proposing the following framework as a starting point for discussion:

- Every month, each gas utility would submit to the Commission a list of the new natural gas load it wishes to serve;
- Any other utility may make a filing stating its interest in serving that load;
- For an area where multiple utilities are interested, each utility would be required to submit documentation showing the incremental capital expenditures it would incur to serve the new load;
- The property owner would choose whichever gas utility best meets its needs, and the rate would be made public once finalized; and
- In its next rate case, the chosen utility could only put into its rate base capital expenditures up to the level of the lowest "bid" among the final pool of utilities interested in serving that load.

Finally, the OAG stated that if the Commission decides to continue evaluating complaints on a case-by-case basis, it should adopt some formal standards so that all parties know what factors the Commission will rely on in deciding these disputes.

4. Xcel, CenterPoint, and GMG

Xcel, CenterPoint, and GMG recommended that the Commission continue using the case-by-case, fact-specific analysis it has employed to date.

Xcel, in particular, supported the analysis done by the Department in the Vikings complaint proceeding—where the Department itemized and quantified the economic benefits and burdens flowing to the competed-for customer, utility shareholders, and ratepayers under different scenarios. With respect to MERC's first-in-the-field rule, Xcel argued that it would create an incentive for utilities to race into new areas, risking having unused or underutilized facilities if the anticipated demand does not materialize or is ultimately served by another utility. Xcel also contended that there was not a pressing need for this type of bright-line rule, since there have been only four natural-gas competitive complaints in the last 26 years.

CenterPoint and GMG opposed the OAG's proposal, arguing that it was unworkable and likely to have the unintended consequences of frustrating customer choice, significantly delaying construction, and creating an undue administrative burden for the Commission and Department.

C. Commission Action

The Commission appreciates the parties' recommendations regarding the Commission's process for resolving gas-service disputes. The Commission agrees that there is room for improvement, yet it is not persuaded that the circumstances warrant overhauling the current, case-by-case process. But to improve the process, the Commission will clarify the criteria on which it relies in determining whether duplication of natural gas facilities is "necessary," as detailed below.

The Commission's criteria are in essence a framework for applying Minn. Stat. § 216B.01. The statute requires this agency to regulate utilities "to provide the retail consumers of natural gas . . . with adequate and reliable services at reasonable rates . . . to avoid unnecessary duplication of facilities which increase the cost of service to the consumer[,] and to minimize disputes between public utilities which may result in inconvenience or diminish efficiency in service to the consumers."

By using the qualifier "unnecessary" before the word "duplication," the statute contemplates that some duplication of facilities may be necessary to provide adequate and reliable service at reasonable rates. Moreover, the absence of legislative action to assign exclusive gas-utility service territories allows a certain amount of competition among them, and likely some duplication of infrastructure. The Commission's primary task is to define as clearly as possible what constitutes "necessary" duplication.

With these considerations in mind, the Commission will adopt the following principles with respect to the duplication of natural gas facilities where utilities are competing for an established customer.

A Commission-regulated utility is prohibited from extending natural gas service to any customer who is already being served by another Commission-regulated utility through its existing facilities unless (1) the utility with the existing infrastructure does not seek to serve the customer, or (2) the utility seeking to extend service can demonstrate that it would not be duplicating the existing facilities of the other utility or that its duplication of the existing facilities is necessary to serve the customer or further the public interest.

Determining whether a utility is duplicating the facilities of another will be based on the nature, size and physical proximity of the new facilities relative to the other utility's existing infrastructure, as well as the extent to which the existing facilities need to be expanded to serve the customer.

To establish that its duplication of existing facilities is *necessary*, a utility must show that (1) customers cannot obtain the natural gas service they need from the utility with the existing facilities; or (2) such duplication furthers the public interest based on:

- the needs of the customers who would be served by the utility extending service;
- the incremental capital expenditures associated with duplicating the existing facilities compared to any incremental capital expenditures needed to expand the existing facilities to serve the customers in question;
- any safety concerns associated with constructing and operating the duplicative facilities; and
- any other factors showing that the duplication would advance the public's interest in adequate, reliable and economical access to natural gas service.

The Commission will continue to decide gas-service disputes on a case-by-case basis. However, the Commission will institute an additional protection to help prevent unnecessary duplication of facilities: Upon the filing of a complaint, the respondent utility will not be allowed to engage in any construction activity related to the allegedly duplicative facilities while the complaint is pending unless the Commission otherwise issues an order specifically allowing construction to proceed.

The Commission appreciates MERC's effort to develop a "first-in-the-field rule" to minimize disputes among utilities. The Commission also appreciates the OAG's thoughtful proposal for minimizing system-wide infrastructure costs. However, the Commission is not persuaded that either proposal is consistent with the statutory scheme. Moreover, in light of the infrequency of these disputes, the Commission agrees with CenterPoint and GMG that the administrative burdens of the OAG's proposal are likely to outweigh any benefit gained.

The Commission is satisfied that the criteria outlined above will allow it to protect ratepayers without unnecessarily stifling competition. And while no criteria or standard, however clear, can entirely foreclose the possibility of future disputes, the Commission is confident that these criteria will provide gas utilities with a clear legal framework when evaluating whether to file a complaint before the Commission.

III. Promotional Incentives

A. Introduction

Another important issue raised by MERC's recent complaints against Xcel is the propriety of a regulated utility using incentives to win prospective customers' business. In its September 2017 notice, the Commission asked utilities to describe the promotional incentives or other payments they offer when extending service to areas or customers outside their existing service area.

MERC and Great Plains stated that they do not offer promotional incentives or other payments to potential customers, although MERC does have a "flexible rate" tariff under Minn. Stat. § 216B.163, which allows it to lower its rates within a Commission-approved range in the face of competition from unregulated gas suppliers.

The other three regulated gas utilities—Xcel, CenterPoint, and GMG—all stated that they offer some form of promotional incentive on occasion. The incentives typically take the form of one-time cash payments to a customer or land developer, paid out of shareholder funds, and in some cases are conditioned on the consumption of a specified amount of natural gas.

Xcel's tariff includes a "Natural Gas Competitive Agreement," which gives Xcel the exclusive right to transport natural gas to a development in exchange for a "Natural Gas Promotion Allowance," with a blank space provided for the parties to indicate the amount of the allowance. Xcel stated that, on average, it uses promotional incentives about twice a year, for a total expenditure of $50,000 annually.

CenterPoint's tariff contains a "New Market Development Agreement." The agreement provides that CenterPoint will have the exclusive right to be the sole natural gas provider to a new development under the conditions specified in an attached "Exhibit A," which contains blank lines to be filled with the specific terms for a project. CenterPoint stated that it has entered into ten such agreements in the past five years. Among the residential development projects, the weighted average payment per lot or apartment was $233; commercial development projects were awarded an average incentive of $7,200.

GMG has no specific tariff terms that govern promotional incentives. It stated that it occasionally offers incentives to developers of high-density developments, on the theory that such projects bring economic benefits with relatively small main-extension costs.

B. Positions of the Parties

1. Arguments Against Incentives

MERC and the OAG both opposed the use of promotional incentives by regulated utilities, deeming them inconsistent with several key statutes:

- **Minn. Stat. § 216B.03**, which requires that rates "shall not be unreasonably preferential, unreasonably prejudicial, or discriminatory, but shall be sufficient, equitable, and consistent in application to a class of consumers";
- **Minn. Stat. § 216B.05, subd. 1**, which requires each public utility to file with the Commission "schedules showing all rates, tolls, tariffs, and charges which it has established and which are in force at the time for any service performed by it within the state";
- **Minn. Stat. § 216B.06**, which prohibits a public utility from charging a rate greater or less than what is set forth in the utility's filed tariffs; and
- **Minn. Stat. § 216B.07**, which prohibits a public utility from granting any person an unreasonable preference or advantage or subjecting any person to any unreasonable prejudice or disadvantage.

MERC argued that promotional incentives lead to impermissible discrimination in favor of new customers in violation of sections 216B.03 and .07. And it contended that promotional incentives offered in the absence of a corresponding tariff, as with GMG, or where the tariff omits material terms such as the amount of the incentive, as with Xcel and CenterPoint, violate sections 216B.05 and .06.

MERC stated that the Legislature has created one exception to the non-discrimination principle embodied in these statutes—the flexible-rates statute, Minn. Stat. § 216B.163—and thereby foreclosed any other exceptions.

Finally, as a matter of policy, MERC contended that the use of promotional incentives and discounted rates undermines competition and creates an uneven playing field among regulated utilities when one utility offers gas service in accordance with its approved tariff and another utility is allowed to fill in the amount of the discount without any meaningful oversight.

For these reasons, MERC recommended that the Commission immediately suspend utilities' use of promotional incentives.

2. Arguments for Incentives

The Department, Xcel, CenterPoint, and GMG all supported the continued use of promotional incentives in one form or another, emphasizing that they are funded by utility shareholders, not ratepayers, and generally do not make up a large portion of a utility's costs.

Xcel and CenterPoint argued that an incentive payment is distinct from a rate—it is a one-time payment and not an per-unit discount or adjustment to a customer's tariffed rate—and therefore does not impact the competed-for customer's bill. Further, they contended, incentives funded by shareholders do not increase existing customers' rates and in fact tend to reduce rates by attracting new customers who share the burden of paying the utility's fixed costs.

The Department agreed with Xcel and CenterPoint that a one-time payment is not a "rate" and therefore does not violate the "filed rate" doctrine embodied in Minn. Stat. §§ 216B.05 and .06. It also disagreed with MERC's view that the existence of the flexible-rates statute bars regulated utilities from offering incentives in competing with each other, stating that the statute pertains to competition between utilities and *unregulated* gas suppliers. The Department argued that shareholder-funded incentives benefit existing ratepayers and that barring them across the board could hamper utilities' efforts to compete with nonregulated suppliers.

For these reasons, the Department recommended that the Commission allow gas utilities to offer shareholder-funded incentives that the utilities can demonstrate to be cost-effective. The Department also recommended that the Commission require utilities to provide information on the effects of promotional incentives on their rates and quality of service, and to file copies of all their existing and new competitive service agreements.

C. Commission Action

The Commission finds that the offering of promotional incentives—tariffed or untariffed—by regulated utilities is inconsistent with Minn. Stat. §§ 216B.03, .05, .06, and .07 and will prohibit their use on a prospective basis.

Section 216B.05, subdivision 1, requires each public utility to file with the Commission "schedules showing all rates, tolls, tariffs, and charges which it has established and which are in force at the time for any service performed by it within the state." Subdivision 2 is even more expansive, requiring that every utility file "any contracts, agreements, or arrangements" that relate to the service being offered.

These provisions are broad enough to cover the types of competitive agreements employed by Xcel and CenterPoint. And while Xcel and CenterPoint have filed template competitive agreements as part of their tariffs, the Commission has already determined that a template agreement that omits essential terms such as the amount of the incentive payment does not meet the requirements of section 216B.05.[7]

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[7] *See In the Matter of Minnesota Energy Resources Corporation's Complaint Against Northern States Power Company*, Docket No. G-011,002/C-17-305, Order Dismissing Complaint, Requiring Filings, and Opening Investigation, at 7 (July 12, 2017).

In response to MERC's Vikings complaint, the Commission required Xcel and MERC to file all their existing and future competitive agreements, and has asked stakeholders in this proceeding whether other natural gas utilities should be required to do likewise. However, the Commission is not persuaded that the after-the-fact filing of competitive agreements cures their fundamental flaw—disparate treatment of customers.

Sections 216B.03 and .07 establish clearly the principle that customers in the same class are to be treated the same, and that no unreasonable preference or advantage is to be given to any person. An incentive payment to a new customer that is not available to existing customers constitutes just such an unreasonable preference or advantage, regardless of whether it is part of a filed tariff.

Finally, the Commission clarifies that the prohibition on promotional incentives applies irrespective of whether such incentives take the form of cash payments or noncash incentives such as co-sponsored marketing events that benefit a single customer. All parties agreed that there is no material difference between a cash payment and other kinds of valuable consideration tied to the provision of natural gas service.

For the foregoing reasons, the Commission will prohibit promotional incentives as inconsistent with Minnesota law.

ORDER

1. Commission-regulated natural gas utilities are prohibited from offering cash or noncash promotional incentives on a prospective basis.

2. The Commission adopts the following principles with respect to the duplication of natural gas facilities:

> A Commission-regulated utility is prohibited from extending natural gas service to any customer who is already being served by another Commission-regulated utility through its existing facilities unless (1) the utility with the existing infrastructure does not seek to serve the customer, or (2) the utility seeking to extend service can demonstrate that it would not be duplicating the existing facilities of the other utility or that its duplication of the existing facilities is necessary to serve the customer or further the public interest.
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> - Determining whether a utility is duplicating the facilities of another will be based on the nature, size and physical proximity of the new facilities relative to the other utility's existing infrastructure, as well as the extent to which the existing facilities need to be expanded to serve the customer.
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> - To establish that its duplication of existing facilities is necessary, a utility must show that (a) customers cannot obtain the natural gas service they need from the utility with the existing facilities; or (b) such duplication furthers the

public interest based on (i) the needs of the customers who would be served by the utility extending service; (ii) the incremental capital expenditures associated with duplicating the existing facilities compared to any incremental capital expenditures needed to expand the existing facilities to serve the customers in question; (iii) any safety concerns associated with constructing and operating the duplicative facilities; and (iv) any other factors showing that the duplication would advance the public's interest in adequate, reliable and economical access to natural gas service.

- Disputes regarding the duplication of facilities will be determined by complaint on a case-by-case basis. Upon the filing of a complaint, the respondent utility shall not engage in any construction activity related to the allegedly duplicative facilities while the complaint is pending unless the Commission otherwise issues an order specifically allowing construction to proceed.

3. This order shall become effective immediately.

BY ORDER OF THE COMMISSION

Daniel P. Wolf

Daniel P. Wolf
Executive Secretary

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