MINNESOTA DEPARTMENT OF COMMERCE

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July 28, 2015

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-15-539

Dear Mr. Wolf:

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

Minnesota Energy Resources Corporation's (MERC) 2015 Evaluation of its Gas Affordability Program (GAP).

The evaluation was filed on June 1, 2015 by:

Jim Phillippo
Program Manger Energy Efficiency
Minnesota Energy Resources Corporation Programs
1995 Rahncliff Court, Suite 200
Eagan, Minnesota 55402-1498

As discussed in greater detail in the attached *Comments*, the Department recommends that the Minnesota Public Utilities Commission (Commission) **approve with modifications** MERC's proposals for the GAP. The Department is available to answer any questions the Commission may have in this matter.

Sincerely,

/s/ JOHN KUNDERT
Financial Analyst

JK/lt
Attachment

MINNESOTA DEPARTMENT OF COMMERCE

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

COMMENTS OF THE MINNESOTA DEPARTMENT OF COMMERCE DIVISION OF ENERGY RESOURCES

DOCKET NO. G011/M-15-539

I. INTRODUCTION

On June 1, 2015, Minnesota Energy Resources Corporation (MERC or the Company) submitted its 2015 *GAP* [Gas Affordability Program or Program] *Evaluation Report* (*Report*) consistent with the Commission's requirement at Ordering Paragraph 2 at page 3 in the Commission's ORDER ACCEPTING REPORT, EXTENDING PROGRAM, AND INCREASING GAS AFFORDABILITY SURCHARGE dated December 29, 2011 in Docket No. G007,011/M-07-1131. The *Report* includes the following sections:

- background information;
- a general description of the GAP;
- information on GAP participation and expenses;
- an evaluation of the GAP tracker account balance and the proposed GAP surcharge for 2016;
- an evaluation of the program in light of its statutory requirements;
- an evaluation of other issues and challenges; and,
- the Company's proposals for the GAP on a going-forward basis.

II. THE DEPARTMENT'S ANALYSIS

The Minnesota Department of Commerce, Division of Energy Resources (Department or DOC) discusses MERC's GAP participation and expenses, the Company's GAP evaluation, and the Company's proposed modifications to the GAP below.

A. GENERAL DESCRIPTION OF MERC'S GAP

In its 2015 *Report*, MERC listed the general characteristics of the Company's GAP, including:

- qualified customers must agree to be placed on a levelized payment plan and a payment schedule;

- customers are automatically removed from the GAP after a non-payment period of two consecutive months;

- the GAP has an affordability component that consists of bill credits determined by calculating the difference between the estimate of the customer's annual natural gas bill and the applicable income limit of the customer's household income (*e.g.*, limiting a customer's payment to six percent of the customer's household income);

- the GAP has an arrearage forgiveness component that applies a monthly matching credit to the customer's balance after payment is received, and the application of this monthly credit retires pre-GAP arrears over a period of up to 24 months;

- the GAP is currently funded through a charge of $0.00441 per therm and this charge is billed to all firm customers;[1] and

- the GAP is administered by the Salvation Army.

The DOC notes that MERC maintains a tracker account to record expenses and revenues associated with its GAP.

B. GAP PARTICIPATION AND EXPENSES

In its *Report*, MERC provided GAP participation data, summarized in Table 1 (following page).

[1] MERC identified the firm customer classes as follows: GS-NMU General Service; GS-1 General Service; GS-4 General Service; and GS-5 General Service.

Table 1: GAP Participation Data

	2011	2012	2013[2]	2014
Enrolled at Year End	NMU=425 PNG=808 Total = 1,233	NMU=414 PNG=737 Total = 1,151	1,080	1,750
Removed - Customer Request	NMU=20 PNG=54 Total = 74	NMU=15 PNG=42 Total = 57	74	63
Non-Pay Default	NMU=12 PNG=48 Total = 60	NMU=18 PNG=30 Total = 48	59	161
Number of Participants who Received a Credit	1,367	1,256	1,248	2,060
Default Rate, Delinquency (%)	NMU=3% PNG=6%	NMU=4% PNG=4%	5%	9%

According to the data in Table 1, participation in MERC's GAP decreased slightly from 2011 through 2013 and then increased significantly in 2014. The Department also notes that the default rates remained fairly constant for the first three years of the study period and increased in 2014.

In order to provide a little more context to this discussion, the Department developed Chart 1 that provides the number of MERC ratepayers enrolled in GAP at year-end since 2008.

The information in Chart 1 (following page) suggests that the decline in the enrolled number of customers at year end began in 2009 and continued through 2013. Under most circumstances, the Department would be concerned with these results. In isolation, this information could suggest that MERC is not dedicating a sufficient level of resources to market or administrate the GAP.

While that still may be the case, the decrease in the price of natural gas during this same time period may have had some influence on MERCs ratepayers' willingness to participate in the GAP. Chart 2 (also following page) uses the information in Chart 1 as a starting point. The Department then included the annual United States Department of Energy's Energy Information Agency (EIA) Average Annual City Gate Price ($/MCF) on a second y-axis over this same time-period.

[2] MERC consolidated its PNG/NMU rate areas in Docket No. G007,011/GR-10-977. The Commission recognized this change in its ORDER ACCEPTING REPORT, EXTENDING PROGRAM, AND INCREASING GAS AFFORDABILITY SURCHARGE dated December 29, 2011 in Docket No. G007,011/M-07-1131 at Ordering Paragraph 7 on page 4.

Chart 1 – Number of GAP Participants Enrolled at Year-End – 2008 through 2014

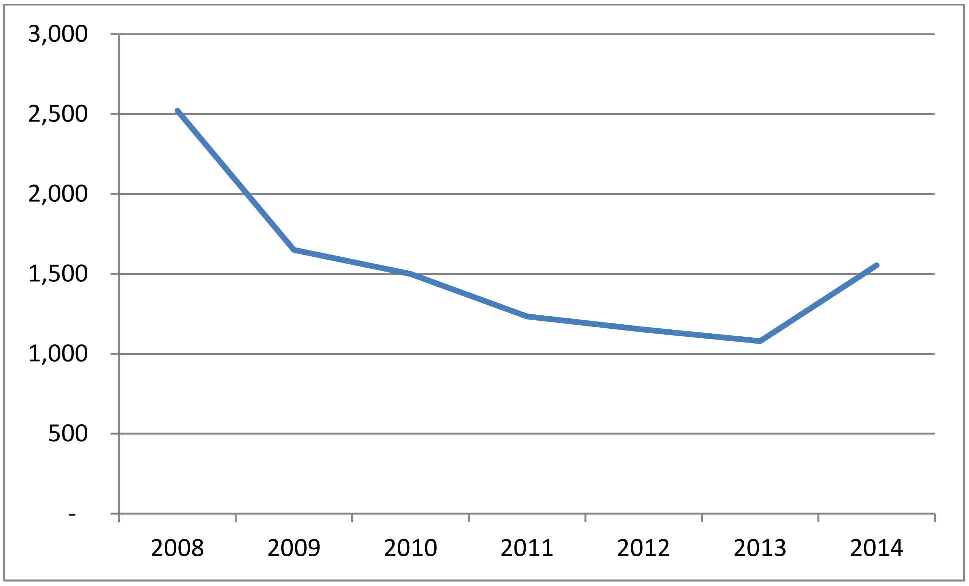
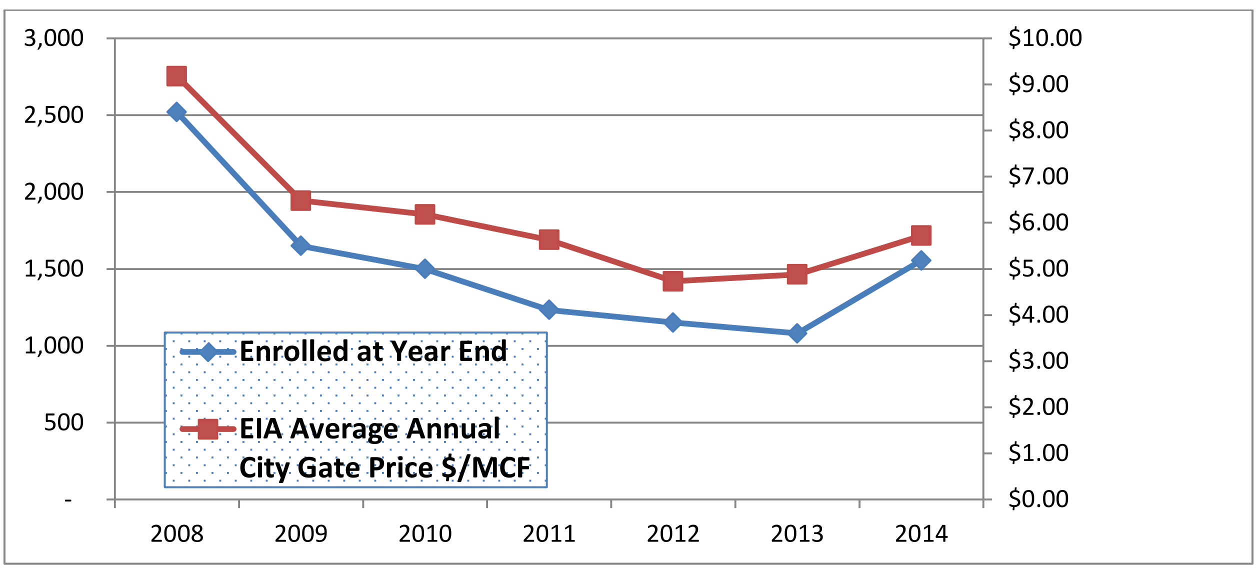


Chart 2 – Comparison of Enrolled Customers at Year-end versus EIA Average City Gate Price ($/MCF)



The information in Chart 2 suggests that there may be some correlation between the price of natural gas and the number of customers enrolled in MERC's GAP at year-end. There is some intuitive appeal to this explanation. A lower price for natural gas would lead to a lower bill (ceteris paribus) which could decrease a low-income ratepayer's need for financial assistance or arrearage forgiveness. The Department is exploring this issue further to determine whether MERC's experience with its GAP program is consistent with that of other similarly situated natural gas local distribution companies. The Department will report on its findings to the Commission and other interested parties if the Commission believes it would be of value.

MERC also provided information regarding the affordability and arrearage credits provided to participants. Table 2 provides this information.

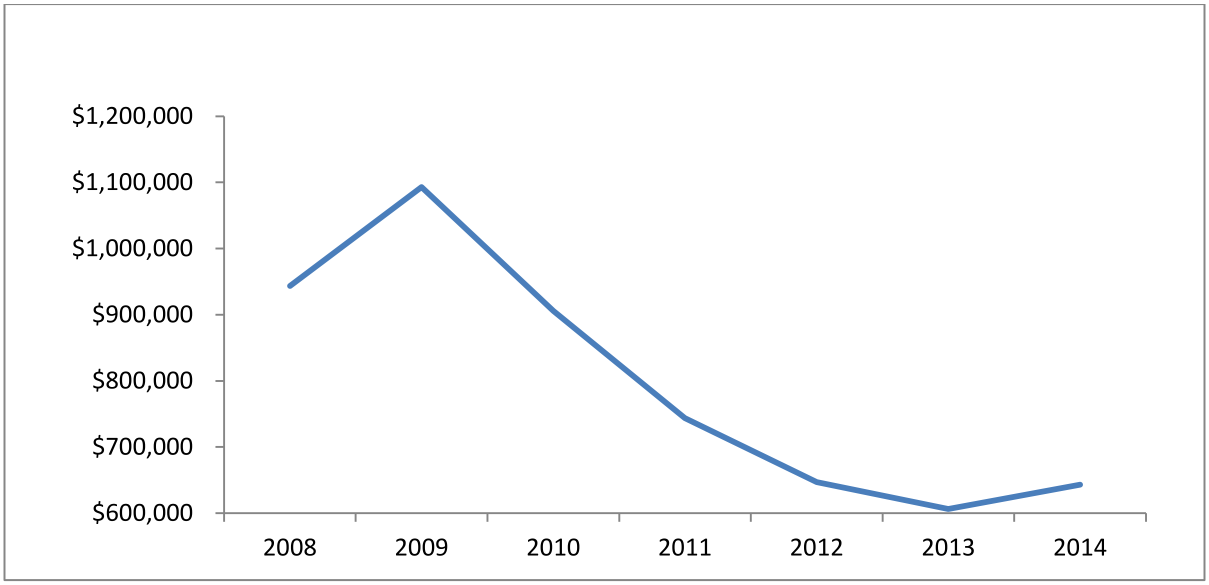
The data in Table 2 is largely consistent with that contained in Table 1. GAP spending on total credits declined from 2011 through 2013 and then increased by roughly 6 percent in 2014. Spending during this time period was well below the annual $1 million Program, budget. Annual average arrearage credits also demonstrated a similar pattern, although the increase from 2013 to 2014 was much higher in percentage terms (239 percent increase).

Table 2: Credits to Participants

	2011	2012	2013	2014
Affordability Credits	NMU=$267,946 PNG=$470,538 Total = $738,484	NMU=$239,558 PNG=$402,830 Total = $642,388	$602,149	$628,002
Arrearage Credits	NMU=$2,237 PNG=$3,081 Total = $5,318	NMU=$1,894 PNG=$2,603 Total = $4,497	$4,439	$15,062
Total Credits	NMU=$270,183 PNG=$473,619 Total = $743,802	NMU=$241,452 PNG=$405,433 Total = $646,885	$606,588	$643,064
Arrearage Credits as a % of Total Credits	NMU=Less than 1% PNG=Less than 1%	NMU= Less than 1% PNG= Less than 1%	Less than 1%	2%

Chart 3 summarizes the annual outlays for affordability and arrearage forgiveness credits since the program's inception.

Chart 3 – Annual Total Affordability and Arrearage Credits ($/yr)



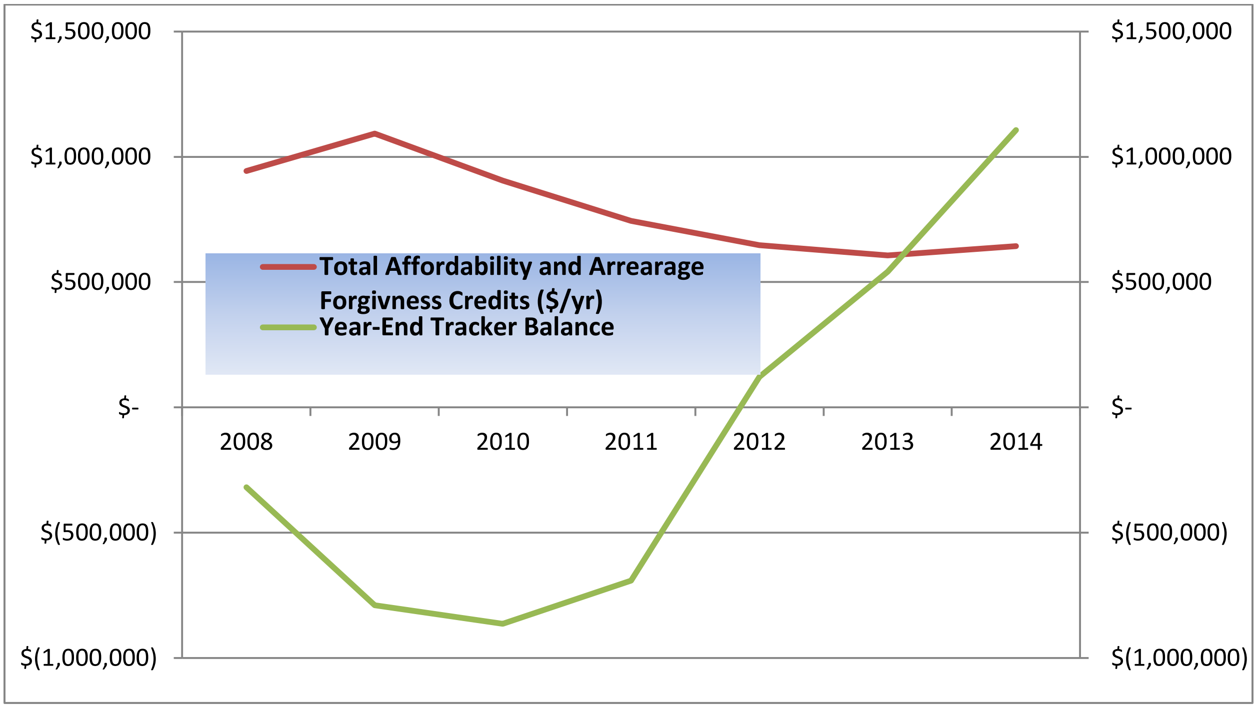
The information in Chart 3 is consistent with the balance of the information included in MERC's *Report*. The annual amounts of affordability and arrearage credits declined as the price for natural gas declined.

C. GAP COST RECOVERY

1. GAP Tracker Balance

MERC's 2014 year-end GAP tracker balance was over-recovered by $1,106,456.37. This over-recovered balance represents a significant change (a positive $1.8 million approximately) from the $687,542.60 under-recovered balance it forecasted for year-end 2011 in the Company's initial evaluation report. Chart 4 attempts to represent this change visually and to place it in context with the information provided in Chart 3 on the annual affordability and arrearage credits awarded to customers.

Chart 4 – Comparison of Annual Affordability and Arrearage Credits and Year-End Tracker Balance 2008 – 2014



The information in Chart 4 suggests that MERC has addressed the annual under-recovered balances associated with the first four years of the Program (2008-2011) and has now increased the GAP tracker balance to the point where it is substantially larger than is appropriate.

The Company recognizes this situation and has proposed several changes to the Program beginning in 2016 that would lower the tracker balance on a going forward basis.

- a decrease in the current GAP surcharge of $0.00441 per therm to $0.00158 per therm.
- a 4-year amortization of the 2015 forecasted year-end GAP tracker balance of $1,179,308.76; and
- a 25 percent decrease in the GAP's annual budget (from $1 million to $750,000).

MERC proposed that the new surcharge be effective January 1, 2016. The proposed surcharge is 64 percent lower than the currently effective surcharge.

While the Department appreciates the balance included in the Company's proposal, the DOC recommends a different approach. Given that the 2015 year-end GAP tracker balance is forecasted to exceed the proposed 2015 annual budget by 157 percent ($1,179,309/$750,000), the Department recommends that the surcharge be set at $0.00 per therm and that the $0.00 per therm surcharge become effective the month following the Commission's Order in this matter.

There are a number of public policy reasons the Department can reference to support this recommendation. First, due to churn in MERC's customer base, the ratepayers receiving the benefit of the lower GAP surcharge in 2019 would be somewhat different from the set of ratepayers whose contribution lead to the over-recovery in the tracker balance from 2012 through 2014. Second, MERC will be filing a general rate case in the fall of 2015. Customer's rates and bills will be increasing shortly thereafter due to the likely approval of interim rates. Lowering the GAP surcharge to $0.00 would provide an admittedly small offset to the likely increase in MERC's base rates. Finally, this change may provide the Company with an incentive to manage the tracker balance more proactively in the future.

As for the bill impact of the proposed change, the Department estimates that lowering the GAP surcharge to $0.00 per them would lower an average residential customer's bill by $0.35/month.

D. GAP LEGAL AND LEGISLATIVE REVIEW

There are a number of statutory and regulatory requirements that outline the criteria and timing of the review of the GAP. The Department uses certain statutory criteria and the tariffed financial evaluation in its analysis. The Department also addresses additional issues concerning the GAP that were raised by the Company.

1. GAP Tariff

MERC's approved GAP tariff includes the following provision:

> The Program shall be evaluated before the end of the four year term and may be modified based on annual reports and on a financial evaluation.[3]

2. Statutory Criteria

Minnesota Statutes, section 216B.16, subd. 15 (b) provides the following criteria for evaluating gas affordability programs approved by the Commission:

> (b) Any affordability program the commission orders a utility to implement must:
> (1) lower the percentage of income that participating low-income households devote to energy bills;
> (2) increase participating customer payments over time by increasing the frequency of payments;
> (3) decrease or eliminate participating customer arrears;
> (4) lower the utility costs associated with customer account collection activities; and

[3] See 1st Revised Sheet No. 7.11 of the Company's tariff.

> (5) coordinate the program with other available low-income bill payment assistance and conservation resources.

In addition to the five statutory criteria discussed above, Minnesota Statutes, section 216B.16, subd. 15 (c) states the following with respect to gas affordability programs:

> (c) In ordering affordability programs, the commission may require public utilities to file program evaluations that measure the effect of the affordability program on:
> (1) the percentage of income that participating households devote to energy bills;
> (2) service disconnections; and
> (3) frequency of customer payments, utility collection costs, arrearages, and bad debt.

The list above is nearly identical with the list of five statutory criteria above, with the inclusion of service disconnections in Part (c) immediately above and the requirement in Part (b) that the utility must coordinate with other low-income and conservation resources.

MERC stated that it reported on certain of these criteria as part of its annual compliance report and discussed them as part of the overall evaluation *Report* as well.

a. Lower the Percentage of Income that Participating Low-Income Households Devote to Energy Bills

i. MERC's Response

MERC stated that, by design, the Program reduces the natural gas bill to participants from what the bill would have been without the Program.[4] The amount of this reduction is equal to the total monthly affordability and arrearage forgiveness credits provided to participants. For this reason, the Company concluded that the Program reduced the amounts billed for natural gas service to participating customers. MERC also stated that, while it is not possible to know definitively whether the Program lowered the percentage of income participants to devote to energy bills due to a number of variables, including, for example, the impact of other energy bills (*i.e.,* electricity) and any changes in participants' income, assuming these other factors remained constant, MERC's GAP did satisfy this statutory requirement.

ii. The Department's Conclusion

The DOC agrees with MERC that other variables identified by the Company affect the percentage of income devoted to energy bills for each participating households.

[4] MERC noted that changes in usage due to conservation or weather-related demand and changes in the price of natural gas also contribute to changes in the total amount of natural gas bills to participants.

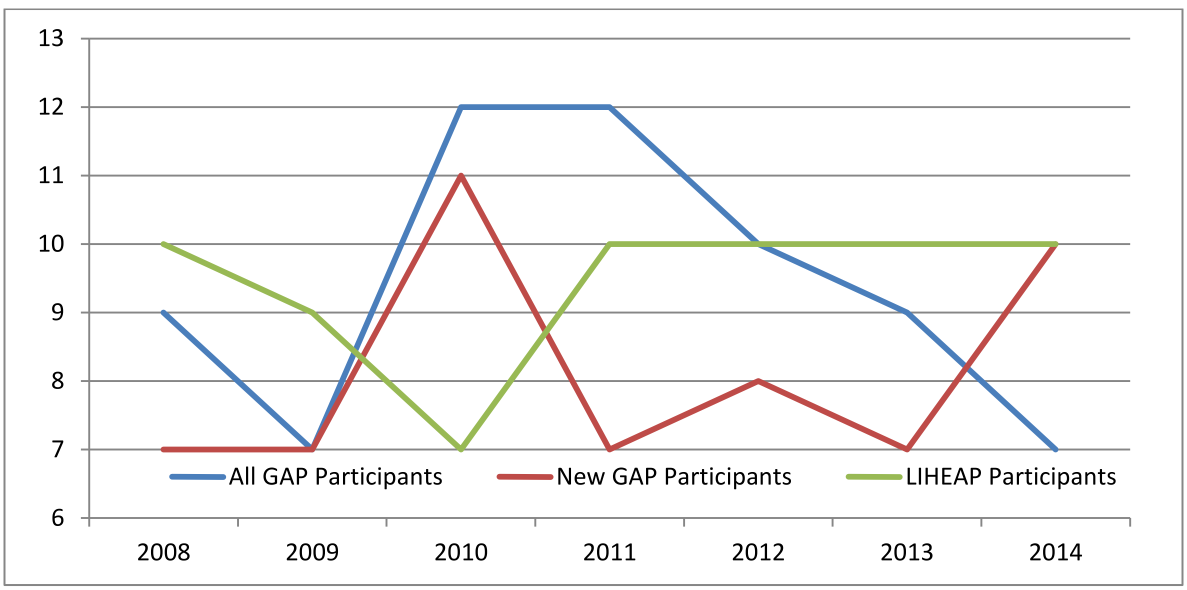
b. Increase Participating Customer Payments Over Time by Increasing the Frequency of Payments

i. MERC's Response

The result of MERC's analysis with respect to customer payment frequency is provided on page 10 of the *Report.* Specifically, MERC compared customer payment frequency of GAP participants on an annual basis for the period from 2011 to 2014. MERC also separated out the payment frequency for the new enrollees in the Program in each year between 2011 and 2014. The Company also provided payment frequency information for LIHEAP recipients during this period. The Company's information states, "The payment data for the 2014 GAP enrollees is difficult to compare with overall payments the last few years because of the increase in enrollments."

Chart 5 attempts to provide a visual representation of this information.

Chart 5 – Comparison of Average Number of Payments/Year for GAP and LIHEAP Participants 2008 through 2014



In its *Report*, MERC explains that the annual number of payments is dependent on a number of different factors and that it has been difficult to draw conclusions regarding payment frequency due to these factors.

ii. The Department's Conclusion

The Department cannot identify any discernible positive trend in the payment information for any of the three groups identified during the 2011 through 2014 time period. The average number of payments per year for all GAP participants declined from 2011 through 2014. The same information for new GAP participants appeared to show a slight uptick. At the same time, the average number of payments per year for LIHEAP participants remained constant. These mixed results suggest that the analysis developed relative to this decision criterion may need to be revised on a going forward basis.

The Department's conclusion regarding this statutory requirement is that the information provided by the Company was insufficient to determine whether the GAP was a contributing factor in increasing the frequency of customer payments from participating customers for the period from 2011 through 2014.

The Department requests that MERC discuss in reply comments potential reasons for the relatively stable payment frequency among LIHEAP customers compared with the declining payment frequency of GAP customers, and identify any potential GAP design changes that could improve payment frequency.

c. Decrease or Eliminate Participating Customer Arrears

i. MERC's Response

Table 3 below indicates the change in arrearage levels for the average GAP customer compared to LIHEAP customers (who were not enrolled in GAP) at the end of each of the program years from 2011 through 2014. The table also compares the average level of arrearage for all of the utility's residential customers for the same time period.

Table 3: Comparison of Average Arrearage Levels

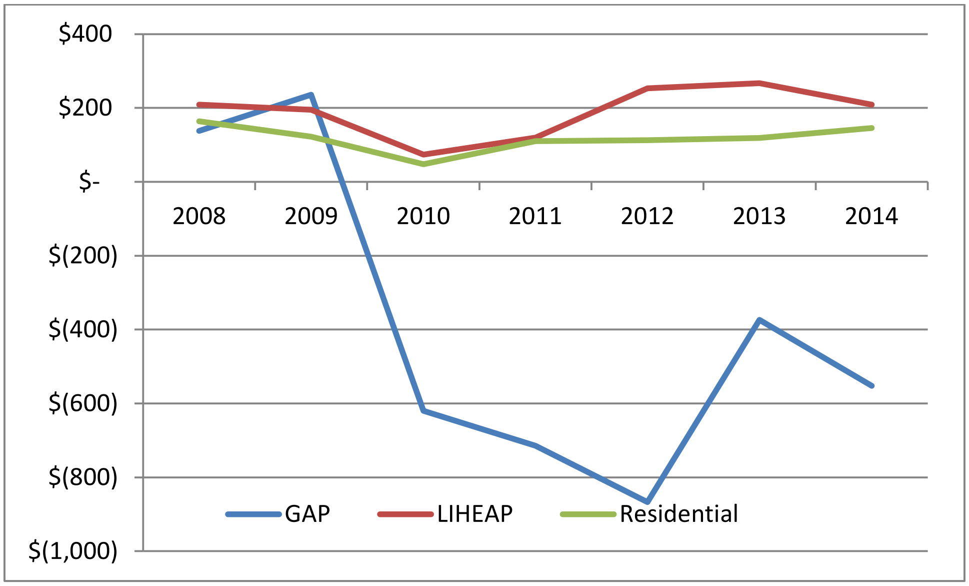
	2011	2012	2013	2014
GAP*	($714)	($867)	($374)	($552)
LIHEAP (Non-GAP)	$120	$253	$267	$209
Residential (Non-LIHEAP, Non-GAP)	$110	$113	$119	$146

**A negative arrearage amount equates to a credit balance for the ratepayer/participant.*

MERC stated that the average credit balance for all GAP customers at the end of 2014 was quite substantial because the majority of the enrolled customers no longer had any arrears. Overall, MERC stated that the Program has been very successful in reducing and eliminating the arrears of a great percentage of GAP participants during the 2011 through 2014 time period.

Chart 6 (following page) provides the average arrearage information for the three customer sub-groups in question for the 2008 through 2014 time period.

Chart 6 – Average Year-End Arrearages for GAP-only, LIHEAP-only and Residential Non-GAP and Non-LIHEAP Customer Groups 2008 through 2014



The information in Chart 6 suggests that the Program has clearly decreased participants' arrearages relative to year-end average arrearages for both LIHEAP-only and Residential non-GAP, non-LIHEAP customer groups during the 2011 through 2014 time frame.

ii. The Department's Conclusion

The Department concludes that, for 2011 through 2014, MERC has shown that the GAP was a factor in decreasing arrears for program participants. Thus, for this period, the GAP satisfied the statutory criteria that the GAP decrease or eliminate customer arrears.

d. Lower the Utility Costs Associated with Customer Account Collection Activities

i. MERC's Response

On page 14 of its *Report,* MERC provided information indicating the number of disconnections of:

- all firm customers;
- LIHEAP recipients, and,
- GAP participants during the 2011 through 2014 timeframe.

The data shows that, during 2011 through 2014, an average of less than one percent of GAP participants were disconnected per year.[5]

By contrast, for LIHEAP recipients the percentage of customers disconnected ranged from 24 to 27 percent per year during the same time period. Thus, compared to LIHEAP participants, GAP participants experienced fewer disconnections.

MERC also identified the following estimated savings of $25,110 of avoided costs associated with prevented disconnections for 2011 through 2014 and approximately $1.2 million in savings from avoided write-offs due to the Program.[6] MERC concluded that overall collection costs have been reduced for GAP participants in each year of the four-year study period.

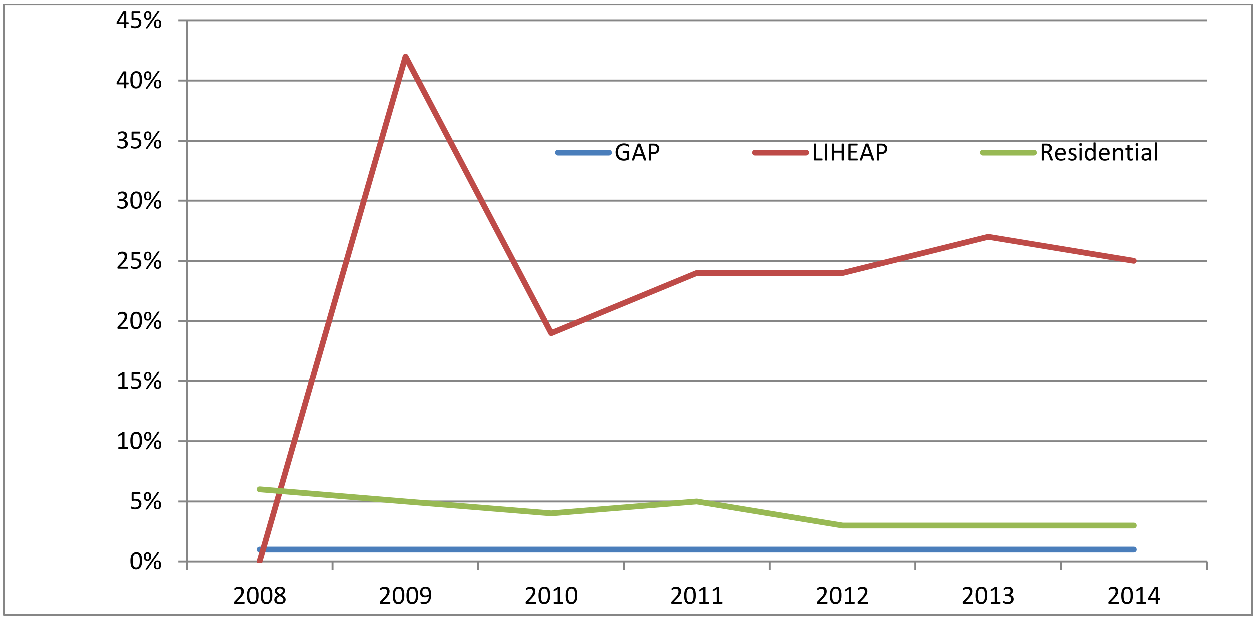
Chart 7 (following page) provides the disconnection percentage information for the three customer sub-groups in question for the 2008 through 2014 time period.

ii. The Department's Conclusion

The information in Table 7 highlights the difference between GAP participants' disconnection rate (less than 1 percent), non-GAP LIHEAP participants' disconnection rate (around 25 percent) and residential customers' disconnection rate (around 3 percent) during the 2011 to 2015 timeframe.

[5] MERC noted that the numbers/percentages of GAP customers represent GAP customers who defaulted from the GAP and had gas service disconnected within 90 days.
[6] The Company stated that, since MERC does not track write-offs specifically for GAP participants, MERC had assumed in this analysis that GAP participants' accounts were written off at the same percentage as write-offs for MERC's LIHEAP customers.

Chart 7 – Percentage of Annual Firm Customer Disconnections for GAP-only, LIHEAP-only and Residential Non-GAP and Non-LIHEAP Customer Groups 2008 through 2014



MERC has shown that, during the period 2011 through 2014, the existence of the GAP has lowered its costs associated with customer account collection activities. The information in Chart 7 clearly identifies a benefit associated the Program relative to the difference between the percentage of firm disconnects for non-GAP LIHEAP and non-GAP, non-LIHEAP residential customers and GAP participants. Thus for this period, MERC's GAP has satisfied the requirement in Minn. Stat. §216B.16, subd. 15, part (b)(4).

e. Coordinate the Program with Other Available Low-income Bill Payment Assistance and Conservation Resources

i. MERC's Response

MERC discussed several resource coordination efforts, including the following:

- the Company works with its partner, the Salvation Army – Northern Division, to administer the Company's GAP and to ensure that GAP customers are being properly enrolled and provided assistance, as needed and available;
- the Salvation Army has access to a variety of support programs internally (including HeatShare) and proactively refers over-income customers or customers with a wide array of needs to a number of external programs that can assist many families and individuals;
- the Salvation Army offers food assistance, rent assistance, medical clinics, seasonal and disaster assistance, and many other services for those in need;

- MERC has regular contact with all of the energy assistance agencies and many community agencies in its service territory.

- MERC has been able to refer a number of its GAP customers to its Conservation Improvement Program for weatherization and other energy efficiency measures.

The Company concluded that the GAP has satisfied this statutory criterion.

ii. The Department's Conclusion

The Department concludes that MERC has shown that, during the period covered in the *Report*, the Company coordinated the GAP with other low-income bill payment assistance and conservation resources, as required by Minn. Stat. §216B.16, subd. 15, part (b)(5).

3. Financial Evaluation

a. MERC's Response

The Company's approved tariff states, in part, with respect to the GAP:

> The financial evaluation will include a discounted cash flow of the Program's cost-effectiveness analysis from a ratepayer perspective comparing the 1) total Program costs, which includes the Affordability component, Arrearage Forgiveness component and total company incurred administration costs, to 2) the total net savings including cost reductions on utility functions such as the impact of the Program on write-offs, service disconnections and reconnections and collections activities. The discounted cash flow difference between total Program costs and total net savings will result in either a net benefit or a net cost to ratepayers for the program. Any net benefit after the initial four-year term of the Program will be added to the Tracker for refund to residential ratepayers.[7]

To comply with this tariff provision, MERC conducted a cost-effectiveness analysis of the GAP from the ratepayer perspective. Table 4 (following page) summarizes the Company's analysis.

[7] See Original Sheet No. 7.11 of the Company's tariff.

Table 4: Summary of MERC's Financial Evaluation of the GAP[8]

Savings	Total 2011-2014	2011-2014 Average
Avoided Write-offs	($1,236,960)	($309,240)
Avoided Disconnects, Reconnections, and Collections	($25,110)	($6,278)
Total Ratepayer Savings	($1,262,070)	($315,518)
Costs		
Program Cost, excluding Excess Administrative Costs	$2,840,339	$710,085
Total Ratepayer Cost	$1,578,271	$394,568
Net (Savings) Cost	$1,578,271	$394,568

As indicated in Table 4, MERC's financial evaluation shows that there was a net cost to ratepayers of approximately $1.6 million in nominal dollars for the Company's GAP. Thus, the GAP was not cost effective from the ratepayer perspective.

In addition to the Company's cost-effectiveness analysis from the ratepayer perspective, MERC discussed the following societal benefits associated with the GAP:

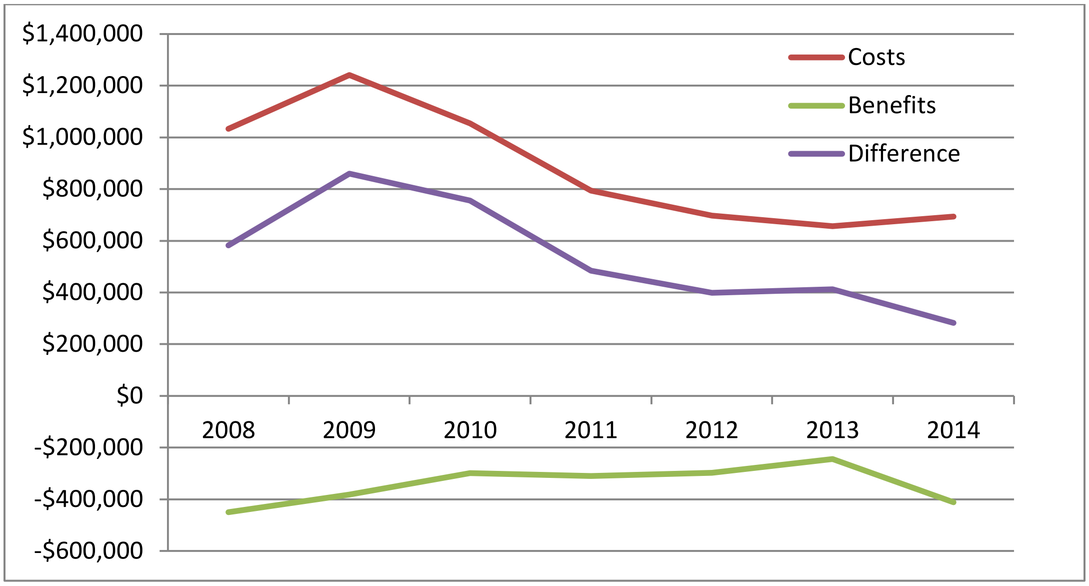
- household budget management;
- stabilizing household mobility;
- growing the safety net; and
- new program development to help offset the growing energy burden.

b. The Department's Conclusion

Similar to its other analyses in these comments, the Department included information for the Program since its inception in 2008 in its review. Chart 8 (following page) provides the information in Table 4 for the 2008 to 2014 time period.

[8] See pages 19 through 20 of the Company's *Report* for a description of each category of savings and costs listed in Table 4.

Chart 8 – Average Annual GAP Cost, Benefit and Difference



The information in Chart 8 is somewhat positive from a ratepayer perspective. The GAP's annual costs appear to be declining at a faster rate than the annual benefits. Consequently, the difference between the two is declining as well. Put another way, the net annual cost of the Program appears to be declining. In 2008 the Company estimated the net annual cost or benefit as a cost of $582,478. By 2014, that net annual cost had declined to $282,517.

MERC did not specifically quantify any of the identified potential societal benefits or costs. Thus, the Department recommends that the Commission exclude these potential societal benefits or costs from any cost-effectiveness analysis of the GAP. Rather, the Department recommends that the Commission continue to use the Company's tariffed financial evaluation as an indication of the GAP's cost effectiveness.

4. Evaluation of Other Issues and Challenges

In addition to the evaluation based on statutory criteria, the Company discussed certain other issues related to the Program.

a. GAP Impact on LIHEAP Grants

MERC discussed the relationship between GAP and LIHEAP in general and the changes in LIHEAP funding to its customers since 2011. MERC differentiated between regular energy assistance grants and emergency energy assistance benefits, the latter of which are targeted towards customers who have higher arrears and are making regular payments, but may be falling further behind and are potentially facing disconnection. MERC stated that emergency energy assistance benefits of GAP participants have been impacted due to GAP benefits. However, MERC stated that it cannot make a fair and accurate analysis of the overall reduction of emergency benefits to GAP customers because too many variables affect customers' ability to qualify for emergency benefits and the actual amount of potential assistance.

MERC also provided annual data for:

- the number of GAP customers that received LIHEAP funds,
- the total amount of LIHEAP funds awarded to those GAP participants.
- the total number of LIHEAP participants, and
- the total amount of LIHEAP grants received by those LIHEAP participants.

Conceptually, the Department can understand that GAP participants might not be eligible for LIHEAP emergency assistance benefits in certain situations. The DOC also recognizes that this potential for a portion of LIHEAP benefits to not be awarded to those GAP participants could be considered a cost associated with GAP participation from the customer's perspective. The Department requests that MERC discuss the magnitude of those "foregone LIHEAP emergency benefits" in its reply comments.

Chart 9 summarizes this information for the GAP participants who receive LIHEAP funds.

The information in Chart 9 suggests that the number of GAP participants who receive LIHEAP grants has been increasing since 2011 as has been the total amount of LIHEAP funds awarded to those GAP participants.

Chart 9 – Comparison of Annual amount of LIHEAP Grants Awarded to GAP Participants ($/yr) and annual number of GAP Participants Receiving LIHEAP Grants 2008 -2014

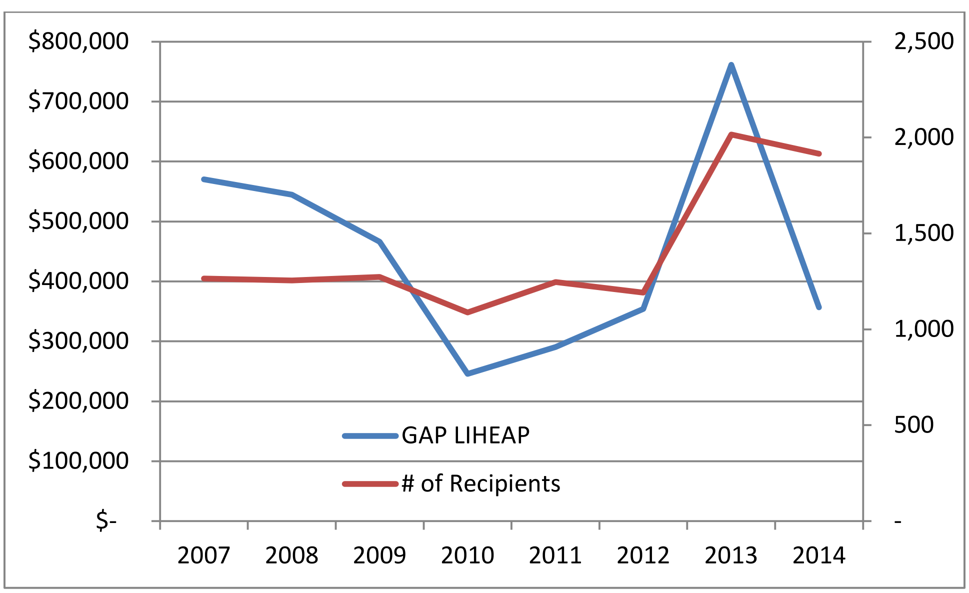
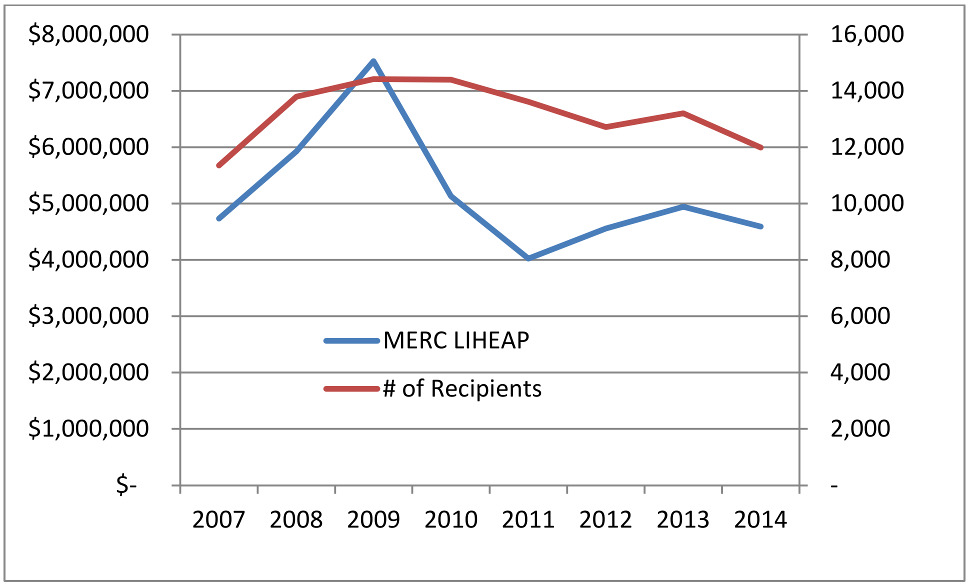


Chart 10 (following page) presents the same categories of information as Chart 9 except the population consists of all of MERC's ratepayers who were awarded LIHEAP grants.

A comparison of the information in the two charts suggests that GAP participants represent an increasing percentage of LIHEAP program participants, (from 11% in 2007 to almost 16% in 2014). The Department also requests that MERC address the drivers of this increase in its Reply Comments.

Chart 10 – Annual Number of LIHEAP Recipients (cust/yr) and Annual Amount of LIHEAP Grants Awarded ($/yr)



b. Spending Challenges

MERC provided a discussion of the development of the large over-recovered tracker balance in the *Report* as well. The Company identified two drivers – higher than forecasted gas consumption during the winter of 2014 and lower than forecasted expenses due to lower levels of participant arrears among long-term participants. MERC also noted that is planning to promote the Program to more customers with the highest arrears at the end of the Cold-Weather Rule (CWR) cut-off of April 1st.

The Department appreciates the information provided. While there are drivers beyond the Company's control that can impact forecast accuracy, the DOC believes that the Company's proposal for a more targeted promotional approach may help to partially alleviate the spending challenge identified in the *Report*.

c. Appropriate Carrying Charge Rate on the GAP Tracker Balance

In the Commission's ORDER ACCEPTING REPORT, EXTENDING PROGRAM, AND INCREASING GAS AFFORDABILITY SURCHARGE dated December 29, 2011 in Docket No. G007,011/M-07-1131 at Ordering Paragraph 9 at page 4 the Commission stated:

> The Commission authorizes a carrying charge on the consolidated gas affordability program tracker balance effective January 1, 2012 at MERC's currently authorized rate of return. MERC shall update the rate of return applied to this tracker account at the end of its pending rate cast in Docket No. G-007, 011/GR-10-977.

The Company filed a clarification to information included in Attachment C in its original Petition on July 24, 2015. This information is consistent with the requirement included in the Commission's Order.

On a going-forward basis, the Department recommends that the Commission approve a carrying charge on the GAP tracker account that is set equal to MERC's Commission-approved cost of short-term debt (2.3487% in this instance). This approach would be consistent with recent Commission precedent regarding the appropriate carrying charge for Conservation Improvement Program (CIP) Tracker balances. The rationale for requiring MERC to use its short-term cost of debt to calculate the carrying charge in its GAP tracker balance is the same as the rationale the Commission approved for using a utility's short-term cost of debt to calculate the carrying charge on its CIP tracker.

Regarding that precedent, in its ORDER APPROVING FINANCIAL INCENTIVE, SETTING CONSERVATION COST RECOVERY ADJUSTMENT, REDUCING CARRYING CHARGES, AND VARYING RULES, dated September 26, 2014, the Commission determined that the short-term cost of debt was the appropriate basis for the carrying charge on the CIP tracker account for Otter Tail Power Company. The Commission followed similar logic in Xcel Energy's 2014 CIP and Interstate Power and Light's 2014 CIP filings.[9]

The Commission's rationale supporting this decision, delineated in its ORDER in Docket No. E017/M-14-201 at page 7 is also relevant to MERC.

> While there is no exact match between this additional twelve-month recovery period and a standard interest rate, the Commission concurs with the Department and the Chamber that the authorized cost of short-term debt is the closest match on the record. The twelve-month term typical of short-term debt corresponds to the twelve-month period CIP costs are typically carried in the tracker account. . . . the short-term debt rate is still more consistent with the public interest than the overall rate of return, given the nature of these costs . . .within which they will be recovered.

[9] Docket No. E002/M-14-287 ORDER APPROVING TRACKER ACCOUNT, APPROVING FINANCIAL INCENTIVE, SETTING CONSERVATION COST RECOVERY ADJUSTMENT AND REDUCING CARRYING CHARGES, issued December 17, 2014. Docket No. E001/M-14-284 ORDER APPROVING TRACKER ACCOUNT, APPROVING FINANCIAL INCENTIVE, SETTING CONSERVATION COST RECOVERY ADJUSTMENT AND REDUCING CARRYING CHARGES issued December 17, 2014.

> For these reasons, the Commission will grant carrying charges on the CIP tracker account balance at the Company's authorized cost of short-term debt.

The Department also requests that MERC provide in its Reply Comments an updated estimate of its 2016 year-end tracker balance assuming the Commission approves the Department's recommendations that, effective the first month following the Commission's Order in this matter, the Company use its current short-term cost of debt as the carrying charge on the CIP tracker account and set the GAP surcharge at $0.00 per therm.

5. Evaluation of the Company's GAP Proposal

MERC made the following proposals with respect to its GAP:

- maintain the Company's "percent of income" credit component (*i.e.*, one-twelfth of the difference between MERC's estimate of the qualifying customer's annual gas bill and six percent of the qualified customer's monthly household income as provided by the customer);
- maintain the Company's arrears forgiveness component (*i.e.*, a matching credit of 1/12 of the pre-enrollment arrears, which is applied to a qualified customer's account each month after receipt of the customer's 1/12 monthly arrears being paid over a period of up to 24 months);
- allow customers without arrears at the time of enrollment to participate for 12 months and customers with arrears at the time of enrollment to participate for 24 months;
- extend the Program for four years, or until December 31, 2019, at which point the Commission would again review MERC's GAP;
- lower the annual budget from $1 million to $750,000;
- authorize the Company to recover the projected tracker balance as of December 31, 2015, amortized over the four-year extension period plus the $750,000 proposed annual budget through a revised GAP surcharge of $0.00158 per therm to be effective January 1, 2016.

The Department notes the proposals contained in the first three bullet points are merely a continuation of the Company's current Program. The proposals included in the fourth through the sixth bullet points represent modification to the existing Program.

The Department supports the proposals included in the first five bullet points. The Program appears to be consistent with the Legislature's intent and is operationally sound. For these reasons, the DOC supports the four year extension. Further, it appears that the decrease in the annual budget to $750,000 is reasonable given that MERC's actual annual spending has hovered around $650,000 in recent years and that Interstate Power and Light's annual spending for that same time period was roughly $50,000 per year. Both MERC and IPL's programs also had fairly stable participation levels during this time period. As noted earlier, the Department is recommending that the GAP surcharge be set at $0.00 per therm beginning the month following the Commission's Order in this proceeding. Consequently, the DOC doesn't support MERC's proposed four-year amortization or GAP surcharge of $0.00158 per therm.

III. THE DEPARTMENT'S CONCLUSIONS AND RECOMMENDATIONS

1. Statutory Criteria

The Department concludes the following:

- Other variables identified by the Company affect the percentage of income devoted to energy bills for each participating household as required by Minn. Stat. §216B.16, subd. 15, part (b)(1). However, given the Program's affordability and arrearage components, MERC has shown that, for 2011 through 2014, the GAP was a contributing factor in decreasing the percentage of income that participating households devoted to energy bills;

- MERC has shown that for 2011 through 2014, the GAP was a contributing factor in the decrease in arrears for GAP. For this period, the GAP has satisfied the criteria that the GAP decrease or eliminate customer arrears, as required by Minn. Stat. §216B.16, subd. 15, part (b)(3);

- MERC has provided a credible analysis that shows that, during the period 2011 through 2014, the Company experienced estimated avoided costs of $25,110 due to prevented disconnection and $1.2 million due to avoided write-offs because of the GAP; For this period, the GAP has satisfied the requirement in Minn. Stat. §216B.16, subd. 15, part (b)(4); and

- MERC has shown that, during the period covered in the *Report*, the Company coordinated the GAP with other low-income bill payment assistance and conservation resources, as required by Minn. Stat. §216B.16, subd. 15, part (b)(5).

- MERC has not shown that, for 2011 through 2014, the GAP was a contributing factor in the increased frequency of GAP customer payments for GAP participants. The GAP may not be satisfying the criteria of increasing participant customer payments over time by increasing the frequency of payments, as required by Minn. Stat. §216B.16, subd. 15, part (b)(2). The Department requests that MERC discuss in its reply comments potential reasons for the relatively stable payment frequency among LIHEAP customers compared with the declining payment frequency of GAP customers, and identify any potential GAP design changes that could improve payment frequency.

2. Financial Evaluation/Other Issues

The Department recommends that the Commission exclude potential societal benefits or costs identified by the Company from any cost effectiveness analysis of the GAP; and use the tariffed financial evaluation as an indication of the GAP's cost effectiveness. The Department also requests MERC discuss the magnitude of the "foregone LIHEAP emergency benefits" it identified and the drivers of the increase in the number of GAP participants receiving LIHEAP grants in its reply comments. In addition, the Department requests that MERC provide an updated estimate of its 2016 year-end tracker balance assuming the Commission approves the Department's recommendations that the Company use its current short-term cost of debt as the carrying charge on the CIP tracker account effective and that the GAP surcharge be set at $0.00 per therm in its reply comments.

3. Proposed GAP Modifications

The Department recommends the Commission set the GAP surcharge at $0.00 per therm and authorize a carrying charge on the GAP tracker balance equal to MERC's short-term cost of debt approved in its most recent general rate proceeding. The Department also recommends that both changes be effective beginning the month following the Commission's Order in this matter

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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-15-539

Dated this 28th day of July 2015

/s/Sharon Ferguson

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