MICHAEL J. AHERN
(612) 340-2881
FAX (612) 340-2643
ahern.michael@dorsey.com

March 30, 2009

VIA ELECTRONIC FILING

Burl W. Haar
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-PNG for Approval of a Change in Demand Entitlement for its Great Lakes Gas Transmission System
Docket No. G011/M-08-1330
Docket No. G007,011/MR-08-836

Dear Dr. Haar:

Enclosed please find the Reply Comments of Minnesota Energy Resources Corporation ("MERC") in the above-referenced dockets.

Thank you for your attention to this matter.

Sincerely yours,

/s/ Michael J. Ahern

Michael J. Ahern

cc: Service List

STATE OF MINNESOTA
BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

David C. Boyd	Chair
J. Dennis O'Brien	Commissioner
Thomas Pugh	Commissioner
Phyllis A. Reha	Commissioner
Betsy Wergin	Commissioner

In the Matter of the Petition of Minnesota Energy Resources Corporation-PNG for Approval of a Change in Demand Entitlement for its Great Lakes Gas Transmission System	Docket No. G011/M-08-1330 Docket No. G007,011/MR-08-836

REPLY COMMENTS OF
MINNESOTA ENERGY RESOURCES CORPORATION

Minnesota Energy Resources Corporation-PNG ("MERC" or "Company") submits to the Minnesota Public Utilities Commission ("Commission") these Reply Comments in response to the February 9, 2009 Comments of the Minnesota Office of Energy Security ("OES") in the above referenced matter.

Based on its investigation, the OES concluded that MERC provided a reasonable basis for its proposal. To confirm that MERC's service to its firm customers is reliable, however, the OES requested additional information in the Company's Reply Comments. The OES also noted that its overall conclusion is subject to the Commission's pending decisions regarding the Contracted Demand (CD) units in Docket Nos. G011/M-07-1404 and G007,011/GR-08-835.

A. <u>Design-Day Requirements</u>

1. The OES noted that using the same design-day calculation methodology, the Company proposes significant increases in its design-day requirement for its MERC-PNG Northern PGA system, MERC-PNG Great Lakes PGA system, and for its MERC-NMU PGA system, while at the same time the Company proposes a significant decrease in the design-day

requirement for its MERC-PNG Viking PGA system. The OES requested that MERC provide a detailed explanation of this result in its Reply Comments.

Response

MERC believes the important point to focus on that supports the new methodology is the result when regressing total volumes. The following table indicates the total regressed results for each MERC system utilizing the 2008-2009 methodology for the 2007-2008 season compared to the 2008-2009 season:

System	2007-2008 Total Point Estimate	2008-2009 Total Point Estimate	Variance	Variance %
PNG-GLGT	11,529	12,159	630	5.46%
PNG-NNG	251,200	248,585	(2,615)	-1.04%
PNG-VGT	9,877	10,038	161	1.63%
NMU	84,763	84,632	(131)	-0.15%

As the data shows, there is not a large variance from one season to another utilizing the new methodology. MERC believes this is an important starting point to support the methodology. The major differences are based upon the methodology of deducting interruptible and transportation volumes. The new methodology requires taking the peak month consumption for interruptible and transportation customer and dividing by twenty (20) days, then dividing by ten (10) to convert to Dth. This approach calculates a Maximum Daily Quantity (MDQ) to be subtracted from the total regressed point estimate. In addition, MERC adds back the firm contracted volumes for the Joint Rate customers to calculate design day.

Unfortunately, MERC was not able to simulate the same methodology for calculating MDQ volumes to deduct for the 2007-2008 season because the data was not available in the same format as the data for 2008-2009 season. Without having an equal simulation, MERC cannot adequately address why PNG-GLGT, PNG-NNG and NMU design day increased and PNG-VGT decreased. MERC feels confident that there is adequate capacity to meet customer requirements as filed but would like the opportunity to meet and discuss the new methodology with OES.

2. The OES noted that MERC used forecasted changes in sales volumes to estimate its growth rate but did not provide these forecasted volumes in its Petition. The OES recommended that the Company provide these data in its Reply Comments, along with any, and all, models, data, and assumptions necessary to replicate the growth rate.

Response

Please see Attachment 1 (MERC 2009 Design Day Growth Factors) for the growth rate data.

3. Given that the Great Lakes system has no peak shaving ability or available storage, the OES requested that MERC provide information and detailed explanations on whether the Company had sufficient capacity available for firm customers during the recent cold spells experienced in December 2008 and January 2009.

Response

MERC experienced a sustained cold spell from January 12-15, 2009, with adjusted HDD from 86 to 92 experienced. The table below shows the unadjusted/adjusted HDD, MERC contracted firm capacity, MERC nominations, third party nominations and total consumption for all MERC customers (sales and transportation) on GLGT.

Date	Unadj. HDD	Adj. HDD	Contracted Firm Capacity	MERC Nominated Capacity	Third Party Nomination	Total Noms	Actual Usage
1/12/2009	78	86	27,946	14,323	12,947	27,270	32,302
1/13/2009	84	87	27,946	18,785	12,455	31,240	45,951
1/14/2009	83	92	27,946	21,760	10,628	32,388	40,504
1/15/2009	82	87	27,946	21,760	10,117	31,877	37,122
1/16/2009	73	80	27,946	21,760	10,183	31,943	32,838

As the table indicates, during the coldest weather experienced during 2009, MERC's nominated capacity to meet total system requirements was less than actual usage but that was due to working off a long imbalance, which means there was more gas nominated by MERC and third party(s) than had been consumed, which GLGT requires MERC to work off. MERC did not fully utilize all of its firm capacity on any of the days. In addition, MERC has to make sure the total system is balanced on a daily basis, which is why MERC has to factor in third party nominations and compare to total system usage, not just firm usage.

4. The OES requested that the Company identify separately, by service and interstate pipeline contract, the amount of CD units included in the proposed design day and peak-day entitlement levels along with the historical entitlement levels as shown in OES Attachments 1 and 2.

Response

MERC does not separately contract for contracted demand by service or interstate pipeline contract. As stated in the Testimony of Greg Walters in MERC's rate case in Docket No. G007,011/GR-08-835, although MERC includes contracted demand volumes in its firm volumes to calculate peakday requirements, the Company does not separately plan for firm contracted demand capacity in its purchase of firm pipeline capacity. The specific period of time for which a joint rate customer takes contracted firm service from the Company can vary based on the initial contracted term or the cancellation of a contract upon 90 days notice. Because of this variability of firm contracted demand by Joint customers, the Company does not purchase firm pipeline capacity specifically to serve the contracted demand capacity of joint rate customers; nor does the Company allocate a specific amount of firm capacity to meet contracted demand volumes. Instead, because of the historically small volume of firm contracted demand capacity, the Company currently serves firm contracted demand needs out of its reserve margin.

5. The OES requested the Company to recalculate the design day requirements in Docket No. G011/M-07-1404 for the 2007-2008 season using the approach used by the Company in the current docket.

Response

MERC completed design day analysis for the winter of 2007-2008 utilizing the new design day methodology. The data utilized to subtract out the interruptible and transportation for 2007-2008 was not available in the same format as it was in 2008-2009, so MERC was not able to simulate exactly as it did in the 2008-2009 design day. The resulting 2007-2008 design day requirements is 9,060 Dth. MERC's design day requirement for the 2008-2009 winter is 10,299 Dth. MERC believes the important point to focus on that supports the new methodology is the result when regressing total volumes. The total regressed volumes result in a point estimate of 11,529 Dth for the recalculated 2007-2008 winter compared to 12,159 Dth for the 2008-2009 winter. Please see Attachment 2 (MERC 2007&08 Peak Day Forecast Recalculation Using 2008&09 Methodology) and Attachment 3 (PNG-GLGT Winter 2007&08 Peak Day Re-Run).

6. The OES also requested that MERC reconcile a number in this filing with a number in the Company's rate case. Specifically, when the Company calculated the "Daily Firm Capacity (DFC) customer selections" in its calculations in this proceeding, the number of joint interruptible customers used in the data was for 59 customers. However, in MERC's general rate case the Direct Testimony and Exhibits of Company Witness, Gregory J. Walters, Exhibit GJW-1, Schedule 12 shows approximately 24 joint sales customers in the test year. The OES requested that MERC provide a detailed explanation and reconciliation for the 59 customers DFC data used in the calculation of the firm peak-day estimate calculations and the 24 customers shown in the Company's rate case. If the Company's firm peak-day estimates and calculations change as a result of the reconciliation, the OES requested that the Company update and provide any and all such results in its Reply Comments.

<u>Response</u>

First, MERC believes that the OES incorrectly interpreted Exhibit GJW-1, Schedule 12 in the Direct Testimony and Exhibits of Gregory J. Walters in MERC's rate case. Schedule 12 shows that there were six (6) small volume joint (SJ-5) customers and four (4) large volume joint (LJ-5) customers taking service off of the Great Likes pipeline, in addition to transportation customers that were not distinguished by pipeline, at the time of MERC's rate case filing. MERC-PNG currently has 7 joint rate customers taking service off of the Great Lakes pipeline: one (1) Large Volume customer and six (6) Small Volume transportation customers. Note that the number of sales versus transport customers is not static, as customers may move from sales to transportation service and vice versa.

Additionally, MERC notes that it used the 7 joint customers indicated above to calculate the Daily Firm Capacity (DFC) customer selections for PNG-GLGT, not the 59 customers referenced by the OES. The 59 customers include all joint customers on MERC's system for both MERC-PNG and MERC-NMU.

B. Reserve Margin

The OES noted that since the Viking system has no available storage or peak shaving ability, it may be appropriate for MERC to maintain greater reserve margins in the event of a peak-day event. The OES stated it would review the Company's Reply Comments for further information on this topic.

Response

Although MERC believes that its reserve margin is appropriate, it agrees to monitor this issue going forward and would value the opportunity to meet with the OES to discuss the peak day methodology.

C. Design-Day Deliverability Changes

The OES indicated that MERC's proposal would increase the Company's pending total design-day capacity (total entitlement) by 500 Mcf/day. This proposed increase in total entitlement is caused by an increase of 500 Mcf/day in FT8466 12-month service.

The OES requested that the Company provide the reasons and detailed explanations for this change in entitlement level in its Reply Comments.

Response

Based upon the design day study, the peak day based upon an one (1) in twenty (20) year occurrence, resulted in a design day requirement of 10,299 Dth. MERC previously allocated 10,000 Dth of GLGT capacity to meet the design day of 9,550 Dth, but the new calculated design day left a negative reserve margin. MERC therefore allocated an additional 500 Dth of capacity to meet the design day requirement and have a positive reserve margin of 1.95%.

D. <u>FT0011 Contract</u>

The OES noted that MERC has terminated the FT0011 contract and has refunded costs related to this contract to ratepayers. The Company, however, included volumes related to the FT0011 contract in its base cost of gas calculations in Docket No. G007,011/MR-08-836. Given the concerns noted by the OES about this contract in Docket No. G007/M-07-1402, MERC's agreement with the OES's recommendations in that docket, and the fact that the contract has been terminated by the Company, the OES concluded that inclusion of volumes related to the FT0011 contract in the initial base cost of gas filing is unreasonable. The OES recommended that the Commission require MERC, in its final compliance in Docket No. G007,011/MR-08-836, to remove all costs and volumes related to the FT0011 contract from its final base cost of gas calculations.

<u>Response</u>

MERC submitted its initial base cost of gas filing in Docket No. G007,011/MR-08-836 on July 31, 2008. At that time, the Company had incurred demand costs related to the FT0011 contract from July through October 2007 and April through June 2008 that were included in the base cost of gas calculations. Moreover, when MERC filed its initial base cost of gas petition on July 31, 2008, MERC continued to disagree with the OES's recommendation that the Company be required to discontinue cost recovery associated with the FT0011 contract and refund to its ratepayers the net difference between the total recovered PGA costs and the total amount received in the capacity release market credited to the PGA for the FT0011 agreement.[1] MERC later agreed to refund this amount to it ratepayers in its Annual Automatic Adjustment report filed September 5, 2008 in Docket No. G999/AA-08-1011.[2] MERC recognizes, however, that the base cost of gas calculations include costs related to the FT0011 contract from July 2007 through October 2009, after the FT0011 contract was terminated.

On September 25, 2008, the Commission issued an Order Setting New Base Cost of Gas in Docket No. G007,011/MR-08-836, setting a new base cost of gas to be implemented with interim rates. In that Order, the Commission directed MERC to file a revised new base cost of gas reflecting the removal of the gas for company use no later than 10 days from the date of that Order and delegated to the Executive Secretary the authority to approve the revised base cost of gas schedules. MERC filed the revised base cost of gas schedules on September 19, 2008, and the Executive Secretary approved the revised base cost of gas on September 26, 2008. The Commission also directed MERC to work with the OES and the Commission to identify acceptable time increments and data sources for updates during the rate proceeding. MERC subsequently filed updates to the commodity cost of gas in both the rate case and base cost of gas proceedings on October 29 and December 22, 2008 and January 27, 2009. The last update was filed just prior to the evidentiary hearing in the rate case proceeding.

The OES now recommends that the Commission require an additional change to the Company's base cost of gas calculations following completion of the rate case proceeding. MERC notes that removing the FT0011 contract costs in the base cost of gas docket has a very small impact on the base cost of gas. The annual FT0011 contract costs for MERC-PNG's Great Lakes pipeline in the base cost of gas filing were approximately $30,500, total estimated demand

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[1] *See* MERC's Reply Comments dated July 9, 2008 and the OES's Response Comments dated July 29, 2008 in Docket No. G007/M-07-1402.

[2] *See* MERC's Letter dated September 23, 2008 filed in Docket No. G007/M-07-1402.

costs were approximately $720,200 and total estimated gas costs were approximately $6,835,368. Using the annual sales projection of 10,886,930 therms from the base cost of gas filing, the approximate effect of removing the costs of the FT0011 contract from the base cost of gas calculation is approximately ($0.00280) per therm

Additionally, the costs associated with the FT0011 contract are not currently included for recovery through the monthly PGA.[3] Therefore the inclusion of the FT0011 contract in the base cost of gas calculations will cause no harm to ratepayers because the costs of this contract will not be charged to ratepayers through the PGA.

MERC, however, agrees to remove all costs and volumes related to the FT0011 contract from its latest update to the base cost of gas dated January 27, 2009, and to submit the revised base cost of gas calculation as part of its rate case compliance filing.

E. Other Demand Entitlement Changes

In addition to terminating the FT0011 contract, resulting in a decrease in its FT0011 7-month non-winter service of 423 Mcf/day capacity, MERC proposed to decrease its Nexen Exchange Agreement by 13,251 units. The OES requested that the Company provide the reasons, and detailed explanations, for the change to its portfolio of other services in its Reply Comments.

Response

MERC allocated the Nexen Exchange Agreements between PNG and NMU on Centra, GLGT and VGT based upon normal winter requirements. Please see Attachment 4 (Nexen Exchange Allocation).

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[3] Although the FT0011 contract was terminated effective June 30, 2008, MERC failed to remove the costs for this contract from its PGA filings for July – September 2008. MERC proposes to refund these costs to its ratepayers in its Annual Automatic Adjustment filing due September 1, 2009.

F. <u>Future PGA and Demand Entitlement Filings</u>

The OES noted that MERC has been using the 2000 rate case volumes in its monthly PGA reports from at least September 2008 and prior periods. The OES stated that it expects MERC, after the end of the Company's general rate case in Docket No. G007,011/GR-08-835, to comply with Minnesota Rule 7825.2700, subpart 5, and Minnesota Rule 7825.2400, subpart 3 in the Company's future PGA and demand entitlement filings. In particular, the Company would use the Commission-approved test year demand volumes for three years after the end of its general rate case test year (2008), and annual demand as defined in Minnesota Rule 7825.2400, subpart 3, in the Company's future PGA and demand entitlement filings.

Response

MERC agrees to compute the demand adjustment using test year demand volumes for three years after the end of the Company's general rate case test year (i.e., for 2009 through 2011). After that time, MERC agrees to compute the demand adjustment on the basis of the annual demand volume as defined in Minnesota Rule 7825.2400, subpart 3, in its future PGA and demand entitlement filings.

DATED this 30th day of March, 2009.

Respectfully submitted,

DORSEY & WHITNEY LLP

/s/ Michael J. Ahern

Michael J. Ahern
50 South Sixth Street
Minneapolis, MN 55402
(612) 340-2600

Attorney for MERC

AFFIDAVIT OF SERVICE

STATE OF MINNESOTA)
) ss.
COUNTY OF HENNEPIN)

Sarah J. Kerbeshian, being first duly sworn on oath, deposes and states that on the 30th day of March, 2009, the Reply Comments of Minnesota Energy Resources Corporation were electronically filed with the Minnesota Public Utilities Commission and the Minnesota Department of Commerce. A copy of the filing was delivered by first class mail to the remaining individuals on the attached service list.

/s/ Sarah J. Kerbeshian

Subscribed and sworn to before me
this 30th day of March, 2009.

/s/ Alice A. Jaworski
Notary Public, State of Minnesota

Burl W. Haar
MN Public Utilities Commission
350 Metro Square Building
121 Seventh Place East
St. Paul, MN 55101-5147

Sharon Ferguson
MN Department of Commerce
85 Seventh Place East
Suite 500
St. Paul, MN 55101-2198

Julia Anderson
Attorney General's Office
1400 Bremer Tower
445 Minnesota Street
St. Paul, MN 55101-2131

Ronald M. Giteck
Attorney General's Office-RUD
900 Bremer Tower
445 Minnesota Street
St. Paul, MN 55101

Karen Finstad Hammel
Attorney General's Office
1400 Bremer Tower
445 Minnesota Street
St. Paul, MN 55101-2131

John Lindell
Attorney General's Office-RUD
900 Bremer Tower
445 Minnesota Street
St. Paul, MN 55101-2130

Robert S. Lee
Mackall Crounse & Moore PLC
1400 AT&T Tower
901 Marquette Avenue
Minneapolis, MN 55402-2859

Michael Ahern
Dorsey & Whitney LLP
50 South Sixth Street, Suite 1500
Minneapolis, MN 55402-1498

Ann Seha
Dorsey & Whitney LLP
50 South Sixth Street, Suite 1500
Minneapolis, MN 55402-1498

Michael J. Bradley
Moss & Barnett
4800 Wells Fargo Center
90 South Seventh Street
Minneapolis, MN 55402-4129

Marie Doyle
CenterPoint Energy
800 LaSalle Avenue – Fl. 11
P.O. Box 59038
Minneapolis, MN 55459-0038

Jack Kegel
MN Municipal Utilities Assn.
3025 Harbor Lane N.
Suite 400
Plymouth, MN 55447-5142

James D. Larson
Dahlen Berg & Co.
200 South Sixth Street
Suite 300
Minneapolis, MN 55402

Pam Marshall
Energy CENTS Coalition
823 East Seventh Street
St. Paul, MN 55106

Brian Meloy
Leonard, Street & Deinard
150 South Fifth Street
Suite 2300
Minneapolis, MN 55402

Eric F. Swanson
Winthrop & Weinstine
225 South Sixth Street
Suite 350
Minneapolis, MN 55402-4629

James R. Talcott
Northern Natural Gas Company
1111 South 103rd Street
Omaha, NE 68124

Greg Walters
Minnesota Energy Resources
3460 Technology Drive NW
Rochester, MN 55901