

June 4, 2018

Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101

RE: **Comments of the Minnesota Department of Commerce, Division of Energy Resources**
Docket No. G002/M-18-323

Dear Mr. Wolf:

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

In the Matter of the Petition of Northern States Power Company, doing business as Xcel Energy, for Approval of a one-year Rule Variance to the Purchased Gas Adjustment (PGA) Rules to Allow Recovery of Storage-Related Ad Valorem Taxes through the PGA.

The Petition was filed on May 7, 2018 by:

Lisa Peterson
Manager, Regulatory Analysis
Xcel Energy
414 Nicollet Mall, 7th Floor
Minneapolis, MN 55401

The Department recommends that the Minnesota Public Utilities Commission (Commission) **approve the Petition with clarified bounds and conditions** and is available to respond to any questions the Commission may have on this matter.

Sincerely,

/s/ DOROTHY MORRISSEY
Financial Analyst

DM/ja
Attachment



Before the Minnesota Public Utilities Commission

Comments of the Minnesota Department of Commerce Division of Energy Resources

Docket No. G002/M-18-323

I. INTRODUCTION AND SUMMARY OF PETITION

On May 7, 2018, pursuant to Minn. Stat. §216B.16, subd. 7, and related Minn. Rule 7825.2400, subp. 12 (Purchased Gas Adjustment “PGA” rule), Northern States Power Company, doing business as Xcel Energy (Xcel or the Company), filed a request to renew a one-year rule variance beginning November 2018 to allow for the ongoing recovery of certain annual costs. The Company requested the Minnesota Public Utilities Commission (Commission) to approve a one-year variance of Minn. R. 7825.2400, subp. 12 to allow for the inclusion and recovery of Kansas property taxes, related to natural gas storage, in its current cost of natural gas supply. The technical accounting classification of this cost requires use of Federal Energy Regulatory Commission (FERC) Account 408.1; this FERC account is not among those specified in the PGA rule. Xcel requested similar purposed rule variances in prior petitions.¹

As a general matter, ad valorem taxes are state taxes based on the value of property located in that state. Xcel stores natural gas on the Northern Natural Gas Pipeline system (Northern or NNG). NNG’s storage fields include facilities in Kansas, which imposes property taxes on resale gas held in fields located in its state.

II. MINNESOTA DEPARTMENT OF COMMERCE (DEPARTMENT) ANALYSIS

A. BACKGROUND OF KANSAS NATURAL GAS STORAGE TAXATION

The validity of Kansas property taxes has been disputed for many years and has been subject to litigation. Xcel explained that the property tax was challenged in the mid-2000s and the Company, along with other utilities, prevailed in a 2007 Kansas Supreme Court decision overturning the tax.² In 2009, the Kansas legislature modified the enabling statute to allow for the collection of an inventory tax from public utilities based outside of Kansas and ultimately

¹ Docket Nos. G002/M-17-510, M-16-396, and M-15-149 (post-exhaustion of court appeals). Docket Nos. G002/M-05-534 and M-06-905 (during Kansas tax dispute).

² Petition at 5.

reversed the prior ruling that removed the tax.³ Despite the Company, along with other non-Kansas public utilities, disputing and appealing the tax, in October 2014 the Supreme Court of the United States denied certiorari, and thus upheld the ability of states to assess property taxes on out-of-state public utilities.⁴ This decision ended the legal routes for appeal.

Following the exhaustion of court appeals, Xcel petitioned the Commission to grant a rule variance to allow inclusion of the Kansas property tax in its purchased gas adjustment mechanism, which the Commission granted in the following dockets, as discussed below.

1. *Docket No. G002/M-15-149*

On February 6, 2015, the Company petitioned the Commission for recovery of the Kansas natural gas storage tax through the PGA in Docket No. G002/M-15-149. The Commission granted Xcel's request on October 21, 2015 (2015 Order), covering both the retroactive 2009-2014 lump-sum⁵ assessed tax and the one-year prospective variance beginning November 1, 2015. The retroactive lump-sum amount, approved to be amortized over five years, stemmed from the Company legally deferring the taxes applicable during the period of appeals until all legal avenues were exhausted.

For prospective Kansas natural gas storage taxes, rather than grant Xcel its requested four-year variance, the Commission limited the rule variance term, stating as follows:

The Commission believes, however, that it is appropriate to revisit the ideal method of recovering future gas storage tax costs sooner than five years from now. The Company stated at the Commission meeting that its current storage contracts are set to expire in 2017 and 2018.

The Commission will therefore limit the term of the variance for ongoing tax assessments to one year. While the Company has demonstrated its efforts to resist the application of this tax, now that the tax has withstood all available legal challenges, the Company should consider whether there are unexplored and less-costly alternatives that would serve the same purpose as storing gas in Kansas, without incurring the Kansas tax.

³ K.S.A. § 79-5a01.

⁴ *Missouri Gas Energy v. State of Kansas, Div. of Property Valuation*, 135 S.Ct 151 (2014).

⁵ The 2009-2014 lump-sum for Minnesota jurisdiction, subject to amortization, totaled \$5,006,347. Docket G002/M-15-149, Xcel Reply Comments (April 20, 2015).

Following the issuance of the Commission's 2015 Order, Xcel Gas' November 2015 PGA rates commenced to reflect recovery of both the then-current (i.e., 2015) Kansas natural gas storage tax and an amortized portion of the 2009-2014 sum.⁶ In addition, as of the Company's 2016 Annual Automatic Adjustment of Charges Report (AAA Report), Xcel Gas began to include a summary report of the Kansas tax expensed and recovered during its gas year (July – June).⁷

2. *Docket No. G002/M-16-396*

On May 3, 2016, Xcel filed a request in Docket No. G002/M-16-396 for a one-year extension of the rule variance granted in Docket No. G002/M-15-149. On July 19, 2016, the Commission issued its Order approving Xcel's petition (2016 Order), with the following conditions:

- Granted Xcel a one-year variance to Minn. Rule 7825.2400, subp. 12 to allow recovery in the PGA of ad valorem taxes related to natural gas storage for retail natural gas operations;
- Directed Xcel to include the Kansas property tax as a separate line item in its monthly PGA;
- Required Xcel to list the Kansas property tax costs and revenues as separate line items in the monthly, Annual Automatic Adjustment report and annual PGA True-Up filings as well as in the Company's Schedule C, Schedule D page 1 through 2 of 4 and page 4 of 4;
- Required Xcel to submit a report with its Annual Automatic Adjustment and True-Up report detailing the total amount paid to Kansas and collected from ratepayers during the gas year; and
- Required Xcel, in its next request for a variance to Minn. Rule 7825.2400, subp. [1]2, to provide a discussion of the storage alternatives examined and its efforts to obtain the most cost-effective storage options.

⁶ The Company's annual PGA true-up filed September 1, 2016 (Docket No. G002/M-16-725) shows that the expensing of these two costs amounts began on July 1, 2015, commensurate with the then-current "gas year" (July – June) when inclusion for recovery was approved (15-149).

⁷ See Attachment G of Xcel Gas' AAA report filed in Docket Nos. G999/AA-16-524 and AA-17-493.

3. *Docket No. G002/M-17-510*

On June 28, 2017, Xcel filed a request in Docket No. G002/M-17-510 for a one-year extension of the variance granted in previous dockets. On November 1, 2017, the Commission approved Xcel's petition (2017 Order), with the same conditions set forth in its 2016 Order (listed above).

B. COMPLIANCE WITH THE 2017 ORDER

Based on its review of the instant filing, PGA filings and Xcel's Annual Automatic Adjustment report in Docket No. G999/AA-17-493, the Department concludes that Xcel complied with the 2017 Order.

The Company included as required "a discussion of the storage alternatives examined and its efforts to obtain the most cost-effective storage options" in Section E of this instant petition.⁸ A portion of Xcel's storage portfolio (1.4 million Dths or 11 percent) was up for renewal in May 2018. Following a cost comparison analysis of the available storage alternatives, Xcel concluded that:

Considering all factors, the lower reservation costs (including the pro-rata estimate of Kansas tax payment for the contract quantity being renewed, which in this case is a relatively small \$90,470), the limited available connecting transportation capacity, and the loss of operational flexibility; renewal of the Northern storage entitlements remains the most cost effective option for our customers. The Company notes that we have a large portion of storage entitlements expiring in 2019 (6.5 million Dths) however, given the market conditions, current transportation issues, and other factors we have discussed, we anticipate a similar outcome in the replacement of those entitlements.

The Department appreciates Xcel's response and concludes that the Company has demonstrated that it is reasonable for Xcel to recover the tax in the current year's PGA. However, changes in market conditions could affect Xcel's anticipated outcome of next year's 2019 contract expiration. Therefore, the Department recommends that Xcel continue to be required, in its next request for a variance to Minn. Rule 7825.2400, subp. 12, to provide a discussion of the storage alternatives examined and its efforts to obtain the most cost-effective storage options.

⁸ Petition, Section E. at 12-15.

C. *PROPOSED 2018 PGA RECOVERY*

Xcel proposed to continue the PGA recovery method for ongoing Kansas tax obligations.

1. *Current Year Tax Amount and Bill Impact*

For the initial 2018 rate determination, Xcel proposed to use the actual tax amount billed in the prior year as the estimated cost, then “allocate the annual tax expense to the Minnesota and North Dakota jurisdictions and across all months by the forecasted volumetric sales to retail customers.”⁹ The prior year’s (2017) tax amount was \$813,000 (rounded) of which \$699,000 was Minnesota’s share. Assuming this same cost level for 2018, Xcel estimated the bill impact to be approximately \$0.85 per year (or \$0.07 per month) for the average residential customer using 859 therms.¹⁰

Once the current year’s actual tax becomes known (tax billing occurs in December), the Company calculates a tax adjustment amount and includes this expense adjustment in the production/billing months (December/January, respectively) of the PGA gas year.^{11,12} The Company stated that “any over- or under-recovery of the tax obligations will be captured through the annual PGA True-up factors.”¹³ This approach is consistent with the method used for recovery of the 2017 tax as approved in Docket No. G002/M-17-510. The Department concurs with Xcel’s proposed approach.

2. *Effective Date and Limits for Recovery*

The Company proposed to implement recovery of the 2018 tax amounts on November 1, 2018 to remain consistent with the prior variance.¹⁴ However, the Department observed, and confirmed with Xcel, though prior granted variance periods began on November 1, this stated date does not accurately reflect when the present year’s tax recovery effectively begins.¹⁵ In practice, the Company records and begins recovery of the current year tax expense on a current basis, with a true-up tax adjustment reflected at end of the calendar year period. In other words, Xcel already began recovering its estimated 2018 calendar year taxes in January 2018.

⁹ Petition at 12.

¹⁰ Petition at 12.

¹¹ The 12-month PGA “gas year” reporting spans July 1 – June 30. Minn. Rules 7825.2800, subp. 1, 7825.2820, 7825.2910 subp. 4.

¹² See the annual PGA true-up Docket No. G002/M-17-657, Schedule D, pp. 1, 2, and 6 and Schedule A, p.2.

¹³ Petition at 12.

¹⁴ Petition at 4 and 12.

¹⁵ Response to DOC IR No. 9.B included as DOC Attachment 1.

The Petition's misstatement has raised the question as to whether the extent of the variance being requested is (1) approval for recovery of the 2018 Kansas taxes, or rather (2) approval for inclusion of the Kansas tax expense recorded in the months November 2018 through October 2019, which would consist of an allocable portion of both the 2018 and the 2019 assessed taxes. The Department believes it is the former for the reasons discussed later. Therefore, the Department believes that for this instant docket and for Xcel's future petitions on this matter, the Commission should consider revising the prospective rule variance bounds it may grant.

Absent a Commission order that states otherwise, the duration of a variance is guided by Minn. Rule 7829.3200, subp. 3, which reads:

7829.3200 OTHER VARIANCES.

[...]

Subp. 3. **Duration.** Unless the commission orders otherwise, variances automatically expire in one year. They may be revoked sooner due to changes in circumstances or due to failure to comply with requirements imposed as a condition of receiving a variance.

To clearly frame the granted limit of this rule variance, if it is the recovery of the 2018 tax through the PGA being approved, the Department recommends that the Commission revise the language granting a variance to describe the limitations of the variance. Specifically, the Department recommends that the variance specify that it allows for the inclusion of a *specified year's* Kansas tax assessment in the PGA, which expires upon recovery. This approach would be more clear, rather than granting a rule variance for one year.

The Department recommends this alternate language for the variance for at least two reasons. First, in the Commission's 15-149 Order issued October 21, 2015, responding to Xcel Gas' then-requested four-year variance to permit recovery of ongoing tax assessments into the future, the Commission decided to limit the rule variance for prospective tax years to one year. The Commission stated that "the variance for future assessments will be limited to one year" reasoning that "it is appropriate to revisit the ideal method of recovering future gas storage tax costs sooner than five years from now" given that "the Company stated at the Commission meeting that its current storage contracts are set to expire in 2017 and 2018." The Department interprets that the Commission's primary purpose of the limit was to revisit and analyze the prospective year's storage alternatives and their comparative costs, in light of near-term expiration of storage contracts, rather than prescribing a specific twelve-month span.

Second, the recovery mechanism, which includes a true-up, establishes the tax recovery rate that is based on estimates that may not result in accurate recovery within a given period, due to differences between forecasted and actual sales, for example. Further, rider true-ups

typically lead to a carryover/refund balance, which would likely stretch beyond a specific variance period. Therefore, the Department recommends that, if the Commission grants Xcel Gas a variance to Minn. Rule 7825.2400, subp. 12, the Commission's order should specify that the variance granted allows the Company to include recovery of the 2018 Kansas assessed tax, expiring upon its recovery, which would make clear that the variance does not restrict Xcel's effective recovery opportunity to be executed during a particular period.

In addition, the Department believes that any prospective "current year" Kansas tax recovery that Xcel may prematurely include in the overall monthly PGA rate prior to a Commission granted variance would be subject to refund, should the Commission ultimately deny the requested variance. To be clear about this possibility, the Commission may wish to place Xcel on notice of this expectation. Further, should the Commission adopt the Department's recommended refinement of rule variance bounds, Xcel may need to adjust its filing pattern of any future Kansas tax rule variance petitions to allow for prior regulatory processing if it wishes to include 2019 tax year costs beginning in its January 2019 PGA rates.

As a final point, the Department does not oppose current year tax expensing and recovery to be conducted on a current basis; however, Xcel should ensure that its future petition statements accurately describe its recovery and expensing practices. The Department noted that there are also problematic statements and data comparisons related to Kansas storage tax in Xcel Gas' AAA filings, Attachment G, filed in Docket Nos. G999/AA-16-524 and G999/AA-17-493. The Department recommends that the Commission direct the Company to work with the Department to correct the Attachment G narrative and table prospectively and in the pending 2017 AAA docket.

3. Reporting and Future Filing Requirements

The Company also proposed to "continue to reflect the tax cost as a separate line item in our monthly PGA, Annual Automatic Adjustment of Charges (AAA), and annual PGA True-up filings."¹⁶ The Department agrees that such reporting should be required to continue.

The Company stated in its Petition that it will have a large level of storage entitlement expiring in 2019 (6.5 million Dths). Therefore, the Department recommends that the Commission again require Xcel, in its next request for a variance to Minn. Rule 7825.2400, subp. 12, to provide a discussion of the storage alternatives examined and its efforts to obtain the most cost-effective storage options. Restricting the variance granted to its current 2018 tax assessments, as discussed earlier, and requiring this information in future petitions, would provide a reasonable

¹⁶ Petition at 12.

balance, by (1) allowing Xcel certain, but limited recovery assurance, yet (2) incenting Xcel to continue to explore other competitive storage options.

D. RULE VARIANCE DETERMINATION STANDARD

The Department recommends that the Commission grant Xcel's currently approved variance to the PGA rules, with clarified bounds, for the same underlying reasons that prior variances were granted.¹⁷ In these prior dockets,¹⁸ the Commission concluded that: a) the Company or its ratepayers would be excessively burdened by denial of a variance, b) varying the rule would not adversely affect the public interest, and c) varying the rule would conflict with no legal standard (conditions provided in Minn. R. 7829.3200). As discussed below, the Department concludes that these standards are met in Xcel's current request.

1. Enforcement of the Rules Would Impose an Excessive Burden upon the Applicant or Others Affected by the Rules

The Company argued that not granting the variance would impose an excessive burden to the Company and ratepayers since, without storage, it would be deprived of a critical tool for "securing a prudent natural gas supply portfolio, which is necessary to provide reliable and cost-effective natural gas service to our customers."¹⁹ Xcel further stated, "[t]o require the Company to absorb this cost until it can be included in base rates would unfairly penalize the Company for a direct cost of gas over which the Company has no control."²⁰

As stated by the Commission in its 2015 Order,

[d]enying PGA recovery of *future* storage tax costs would unreasonably burden ratepayers. It would temporarily disguise from ratepayers the true cost of their natural gas, resulting in inefficient natural gas use—with the costs borne by ratepayers and the public. Denying a variance could also discourage the Company from moderating price volatility with storage, which benefits ratepayers.

Moreover, when considering the Company's analysis results of alternative storage options, denying the variance may discourage optimal storage selection.

¹⁷ Xcel Gas Docket Nos. G002/M-15-149, M-16-396, and M-17-510.

¹⁸ *Ibid.*

¹⁹ Petition at 10.

²⁰ Petition at 10.

The Department concludes that enforcement of the rules may impose an excessive burden on Xcel and its ratepayers.

2. Granting the Variance Would Not Adversely Affect the Public Interest

Xcel claimed that the public interest is served when the Company engages in prudent resource strategies.²¹ Xcel stated that granting the variance would encourage the Company to continue to use storage – “providing customers price stability and a hedge against the risk of supply disruptions from unforeseen circumstances.”²² Also, Xcel argued that the tax is a direct cost of natural gas delivered so it would not adversely affect the public interest.

The Department concludes that having the storage resource proposed by Xcel is in the public interest since it would enable price stability and assist with reliability. The Company’s discussion of alternative storage options indicates that the variance would facilitate optimal use of storage. Therefore, granting a variance would not adversely affect the public interest.

3. Granting the Variance Would Not Conflict With Standards Imposed by Law

Xcel stated that the variance is not in conflict with standards imposed by law. The Company contends that the Kansas property tax is a cost directly tied to the cost of gas. Although the tax is not specifically outlined in Minn. R. 7825.2400, subp.12, the Company suggests that it could be included as a “cost of purchased gas.”²³

The Commission has previously granted this rule variance in Docket Nos. G002/M-15-149, G002/M-16-396 and G002/M-17-510, in which it determined that a variance to the PGA rules did not conflict with any standards imposed by law. The Commission has authority to vary its own rule designating accounts included in the cost of purchased gas. As such, the Department concludes that the variance is consistent with the purpose of the PGA statute and rules and does not conflict with any other laws.

III. DEPARTMENT RECOMMENDATIONS

The Department recommends that the Commission approve a variance to the PGA rules with clarified bounds and with the same conditions established in the 2017 Order:

²¹ Petition at 7.

²² Petition at 10.

²³ Petition at 10.

- grant Xcel Gas a variance to Minn. Rule 7825.2400, subp.12 to allow recovery through the PGA of the 2018 Kansas ad valorem taxes related to natural gas storage for retail natural gas operations, which expires upon recovery of the 2018 tax;
- direct Xcel to include the Kansas property tax as a separate line item in its monthly PGA report;
- require Xcel to list the Kansas property tax costs and revenues as separate line items in the Annual Automatic Adjustment report and the PGA True-Up filings, including the Company's Schedule C and Schedule D;
- require Xcel to submit a report with its Annual Automatic Adjustment and PGA True-Up report detailing the total amount paid to Kansas and collected from ratepayers during the gas year;
- require Xcel, in its next request for a variance to Minn. Rule 7825.2400, subp. 12, to provide a discussion of the storage alternatives examined and its efforts to obtain the most cost-effective storage options; and
- direct the Company to work with the Department to correct the Company's Annual Automatic Adjustment Report Attachment G narrative and table, prospectively, and in the pending 2017 AAA docket G999/AA-17-493.

/ja

- Not Public Document – Not For Public Disclosure
 Public Document – Not Public Data Has Been Excised
 Public Document

Xcel Energy

Docket No.: G002/M-18-323

Response To: MN Department of Commerce Information Request No. 9

Requestor: Dorothy Morrissey

Date Received: May 16, 2018

Question:

Topic: Purchase Gas Adjustment – Kansas Tax Recovery design

Reference(s): PGA Dockets 16-725 (PGA annual true-up), 15-950 (Nov. 2015 PGA), 17-657 (PGA annual true-up)

- A. Reference Annual PGA True-Up dockets (16-725 and 17-657), Schedule D: Please explain why Schedule D, reported 12-month span on page 1 (June – May) differs from the 12-month span (July – June) on the remaining pages of this schedule.
- B. Please explain and clarify the 12-month span designed for recovery of Kansas Tax (Current Year). In response, also identify the “Current Year” tax year in relation to its 12-month tax recovery period.
- C. Reference Annual PGA True-Up Docket 17-657, Schedule C, page 2: (1) Regarding “Current Year Factor”, columns August 2016 – February 2017, please explain underlying reasons for the changing factor rates; (2) Likewise, please explain underlying reason for change in the “2009-2014 factor” during the August - October months.
- D. Reference Dockets 15-950 (November PGA – Letter and Schedule A) and 16-725 (Annual PGA True-Up – Schedule D). Post-Commission Order in Docket 15-149 (issued October 21, 2015), please confirm that though Xcel did not resume Kansas natural gas storage tax recovery in its PGA rates until November 2015, it reported this tax as a gas commodity expense effective July 1, 2015.

Response:

- A. Natural gas purchases are recorded on a calendar month basis, but customers are billed on multiple billing cycles throughout the month. The Company’s Annual PGA True-up reports gas purchases expenses for calendar months of June through May, and gas sales revenues for billing months July through June.

Gas purchase expenses on each page of Schedule D are reported for the 12 calendar months of June through May, originating from the gas expenses reported on Schedule H of the PGA True-up filing. Gas revenues on each page of Schedule D are reported for the 12 billing months of July through June. The Company notes that the billing month labeling convention (July through June) is used throughout Schedule D pages 2 through 6. We apologize for the confusion, and will update the PGA True-up schedules as appropriate in future reports.

- B. The annual Kansas Tax expense is recorded on a current basis, and included in the current month's PGA for recovery. For example, the 2018 Kansas Tax expense estimate is allocated to the 12 month period January 2018 through December 2018, and included in the PGA for recovery over those months. The estimated expenses are trueed-up to the actual Kansas Tax bill in the annual PGA true-up calculation.
- C. (1) In the PGA, the "current year" Kansas Tax factor is updated each September with a sales forecast update. It is also updated in January to incorporate the new level of billed taxes. The Kansas Tax factors on Schedule C, page 2 of the PGA True-up filing are prorated in order to be applied to billing month sales. For example, September 2016 billed sales included 49.07% of August sales and 50.93% of September sales, so the Kansas Tax rate is weighted at 49.07% of the August factor and 50.93% of the September factor. Changes to the Kansas Tax rate in September would be included in the September, October, and possibly the November billing month prorations. Changes to the Kansas Tax rate in January would be included in the January, February, and possibly March billing month prorations.
- (2) As described in more detail in Part D below, per Commission Order, the 2009-2014 Kansas taxes were amortized over a five year period, starting in 2015. In the PGA, the "2009-2014" Kansas Tax factor is updated each September with a sales forecast update. The Kansas Tax Factors on Schedule C, page 2 of the PGA True-up filing are prorated in the same manner as described above for the "current year" Kansas Tax factors, and a rate change in September would be included in September, October, and possibly November billing month prorations.
- D. In our February 6, 2015 petition in Docket No. G002/M-15-149, we requested a variance to recover the Kansas Tax lump sum for 2009-October 2014. We also requested a four year variance to recover Kansas Tax on an ongoing basis starting with the November 2014 expenses. The October 21, 2015 Commission Order in the same docket approved a five year amortization for

the 2009-2014 lump sum, and a one year variance for the current year's assessed Kansas Tax. The Company interpreted the Order to mean that we had authority to recover current and 2009-2014 lump sum taxes in the current AAA gas year. Accordingly, we began putting Kansas Tax expenses in the first PGA following the Order (November 2015), and also represented the tax expenses from the beginning of the current gas AAA year (July 2015).

Preparer: Lisa Peterson
Title: Regulatory Analysis Manager
Department: Regulatory Affairs
Telephone: 612-330-7681
Date: May 31, 2018