Minnesota Public Utilities Commission

Staff Briefing Papers

Meeting Date: **September 4, 2013 .... Agenda Item # __9**__**

Company: **Minnesota Power (MP)**

Docket Nos. E-015/M-12-1359
In the Matter of a Petition by Minnesota Power for a Modification to its Service Extension Tariff

E-015/M-95-1441
In the Matter of a Request by Minnesota Power for a Modification to its Service Extension Tariff

Issue: Should the Commission accept MP's Petition, filed in Docket No. E-015/M-12-1359, as being sufficient in meeting the compliance requirements ordered by the Commission in Docket No. E-015/M-95-1441?

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Relevant Documents

<u>Docket No. E-015/M-95-1441</u>
PUC - Order Approving Service Extension Tariff As Modified .... October 8, 1996

<u>Docket No. E-015/M-12-1359</u>
MP Compliance Filing (from Docket No. E-015/M-95-1441) .... December 26, 2012
Department of Commerce (Department) Comments .... February 25, 2013
MP Reply Comments .... March 22, 2013
Department Reply Comments .... April 16, 2013

The attached materials are workpapers of the Commission Staff. They are intended for use by the Public Utilities Commission and are based upon information already in the record unless otherwise noted.

August 29, 2013

Table of Contents

Statement of the Issue

Should the Commission accept MP's Petition, filed in Docket No. E-015/M-12-1359, as being sufficient in meeting the compliance requirements ordered by the Commission in Docket No. E-015/M-95-1441?

Introduction

What service extension policies do, i.e. they govern what a utility can charge when new facilities have to be built to serve a new customer.

Utilities have service extension policies so that the cost of extending service to new customer are clear and transparent, the policies are fairly and uniformly administered throughout the Company's service area, and that costs are fairly apportioned between the new customer and the utilities current.

The utility's tariff reflects language and provisions that are designed to be clear and transparent that is reasonably applicable to all customers. As part of MP's tariff, it currently reflects a service line extension allowance of $850 for all service requests. Generally speaking, if MP receives a request for new service or for existing service line relocation, all customers would receive a service line extension allowance of $850. If the service line costs do not exceed $850, the requesting customer does not have to make payment for the service line extension. If the service line costs exceed the $850 allowance, then the customer must pay for the overage.

October 8, 1996, Order Approving Service Extension Tariff As Modified

On October 8, 1996, the Commission issued its ORDER APPROVING SERVICE EXTENSION TARIFF AS MODIFIED, Docket No. E-015/M-95-1441 (the 95-1441 Order). In the 95-1441 Order, the Commission approved MP's service extension tariff and required MP, in its next rate case, to address the following issues:

Order point 3(a). Reduction of the extension cost allowance to $850, affecting all single phase and three phase customers except the lighting class, as approved in this Order;

Order point 3(b). Discontinuance of Schedule A and adoption of a 1/3 cost of extension rule to compute the amount of annual revenues that a three phase customer must guarantee to avoid having to make a lump sum Contribution in Aid of Construction (CIAC); the Company's filing in its next rate case shall include a fully embedded average cost study to provide the cost basis for examining this policy change to determine whether any interclass subsidy has resulted from the change; and

Order point 3(c). Reduction of the maximum extension cost amount eligible for the GAR payment option to $30,000, including information about the revenue impacts and results of the new policy compared to the results under the existing tariff.

In the Commission 95-1441 Order, MP was further directed:

- to file a compliance petition whenever MP's average embedded costs would change its line extension service allowances by 5%. MP was directed to adjust its service line extension allowance to the appropriate level through compliance filing; and

- to review of the $850 cost allowance for the three-phase (or non-single phase) costs in MP's next rate case, and

- to prepare a three-phase average embedded cost study to examine whether any interclass subsidy resulted from the change to the 1/3 cost of extension rule; and

- to provide embedded cost studies for both single-phase and three-phase services in its next rate case, if not, provide before in a separate compliance filing.

Background

MP's original docket number for its service line extension tariff was Docket No. E-015/M-95-1441 (95-1441). MP has filed its compliance to 95-1441 Order Requirement No. 3 in Docket No. E-015/M-12-1359 (12-1359). MP stated that the reason for filing this compliance petition under a different docket than the original service line extension petition (95-1441) was because the original docket predated the eDockets system. The compliance petition made under the new docket number is cross-referenced with the original docket to enable use of eDockets for this petition's filing and review by all interested parties.]

On December 26, 2012, MP filed its compliance petition response to the 95-1441 Order Requirement No. 3 in 12-1359.

On February 25, 2013, the Department filed its comments on MP's 12/26/12 compliance filing.

On March 22, 2013, MP filed its comments responding to the Department's 2/25/13 comments.

On April 16, 2013, the Department filed its comments responding to MP's 3/22/13 comments.

Party Positions

MP has previously complied with Ordering Points 1 and 2 of the Commission's 95-1441 Service Extension Order. Exhibit 2 of MP's compliance petition provided MP's current service line extension rules from its Electric Rate Book – Volume I, Section VI, Page Nos. 4 – 4.5.

MP stated that its compliance petition (12-1359) addresses the 95-1441 Commission Ordering Point 3 requirements that were not addressed by MP either in a follow-up compliance petition or in its subsequent rate cases. MP had opportunities to address the Order requirements in its 2008 and 2009 rate cases.

MP stated that it has developed a method of tracking Commission compliance requirements; as stated in MP's petition "In order to avoid compliance oversights in the future and to ensure continued compliance going forward, MP has implemented a process to track and monitor compliance requirements resulting from all Commission proceedings."

[Staff Note: MP discovered its omission of the Order requirement through its own review of Rate Department documents, which prompted discussions Commission staff and the Department. These discussions led MP to file its compliance filing in Docket No. E-015/M-12-1359.]

Order Point 3(a) – Line extension cost allowance (95-1441 Order)

Minnesota Power – December 26, 2012 Compliance Petition
The Commission allowed MP to reduce its previous approved line extension cost allowance from $2,800 to $850, and made it applicable to all single-phase and three-phase customers except for the lighting class. The Commission found that the $850 amount was a reasonable proxy for actual three-phase costs, but required the $850 amount to be review in MP's next rate case. The Commission further required compliance petitions whenever MP's average embedded costs for line service extensions change by 5%.

MP stated that its 12-1359 Compliance Filing's Exhibit 3 provides a fully allocated embedded cost study reflecting the average cost for single-phase and three-phase customers based on cost information from the Company's 2011 FERC Form No. 1 and 2009 retail rate case. The average cost per customer for all four rate classes is $992 or an approximate 17% increase over the previous approved level ($850); the study further calculated an allowance for residential single-phase customers of $614, for General Service customers of $1,454, for Large Light and Power customers of $66,904, and for Municipal Pumping customers of $9,124. The three-phase customers' weighted average for all applicable classes is $3,089. The Lighting class is not included in the average because the Lighting class follows specific rules as provided in MP's Electric Rate Book.

MP stated that the existing line extension cost allowance of $850 is higher than the average Residential cost of $614 but lower than the three-phase weighted average cost of $3,089. MP believes that the average residential customer extension cost will be more than covered by the current $850 service line extension allowance amount, while non-residential three-phase customers will typically need to contribute to the extension cost or provide revenue guarantees.

MP is recommending to the Commission that no service line allowance adjustment is necessary and that the current $850 allowance is reasonable.

Department – February 25, 2013 Comments
The Department stated that MP's embedded cost of service for line extension allowance study reflects the average embedded cost based on cost information from the Company's 2011 FERC Form 1 and the 2009 rate case. The MP's embedded costs study results in the following average cost allowance structure:

Customer Class	Average Cost
Residential (single-phase only)	$ 614
General Service (mix of single- and three-phase)	$ 1,454
Large Light and Power (three-phase only)	$66,904
Municipal Pumping (mix of single- and three-phase)	$ 9,124
Weighted average cost (mix of single- and three-phase)	$ 3,089
Average of all Customer Classes	$ 992

MP's current line extension cost allowance is $850 for single and three-phase customers for service line extension requests.

The Department concluded that the 95-1441 Order required MP to file a compliance filing whenever MP's average embedded costs changed by 5% which enables the Commission to establish appropriate allowance level changes. The 12/26/12 MP Compliance filing reflected MP's updated average embedded cost for residential service extensions at $614, or a decrease of about 28% from the current line extension allowance of $850. Further, the average overall line extension cost increased to $992 from $850, which is approximately 17% higher than the current line extension cost.

Department determined that every MP line extension allowance had changed by more than the 5%. The Department calculated that a 5% change in the current $850 line extension allowance results in approximately $42; which translates to a range of $808 to $892.

The Department has concluded that continuing the MP recommended $850 cost allowance for single-phase customers is unreasonable since the average embedded cost has decreased significantly.

The Department stated that MP did not provide a fully embedded average cost study for single and three-phase customers. MP's 12/26/12 Compliance Petition Exhibit No. 3 combines single and three-phase customers' data together when calculating the General and Municipal Pumping service allowances.

Department concluded that setting the cost allowance for three-phase service at $850 is unreasonable for the following reasons:

- MP admitted that the required CIAC for three-phase service would decrease if the extension allowance were set equal to that class' average embedded cost. Thus, new three-phase customers may be subsidizing current customers; and

- The $850 allowance was based on single-phase service rather than three-phase service. As indicated in MP's compliance filing, the three-phase average actual extension costs are $1,454 for General Service and $9,124 for Municipal Pumping.

The Department recommended that continuing the $850 cost allowance for any customer is unreasonable. The Commission should consider the allowances for each service to be based on each class' average line extension costs to reduce interclass subsidies reflected in the embedded cost of service prepared by MP. The Department recommended

1. that the single-phase allowance be set at $615; rounded up from the 2011 average embedded cost of $614.
2. that the Commission require MP to set the extension allowance for General Service three-phase service at $1,455 (rounded up by $1) and $9,125 (rounded up by $1) for Municipal Pumping three-phase service.
3. to the Commission that it should consider ordering MP to study the single and three-phase extension costs, as originally directed in the Order.

Minnesota Power – March 22, 2013 Reply Comments
MP filed its Reply Comments in response to the Department's comments, in which MP revised some of its original recommendation positions; agreeing with the Department on some recommendations, and not agreeing the Department on others. MP provided additional support for its positions that are different than the Department's recommendations.

MP agreed to accept the Department's recommendations on the following:

Single-Phase line extension allowance
MP agreed with the Department to set the single-phase allowance at $615 as calculated in its embedded line extension cost calculation.

Three-Phase line extension allowance – General Service
MP agreed with the Department to set the three-phase allowance for General Service customers at $1,455 as calculated in its embedded line extension cost calculation.

MP disagreed with the Department's recommendations on the following:

Three-Phase line extension allowance – Municipal Pumping
MP disagreed with the Department with respect to the $9,125 Municipal Pumping class line extension cost allowance. MP's revised recommendation is to set Municipal Pumping class three-phase line extension allowance at $1,455, the same as the General Service line extension allowance. MP provides the following in support of its position:

MP argued:

- The number of new Municipal Pumping customers each year is very low; for example, in 2012, only three customers requested service extension compared to more than 100 customers in the General Service rate class. MP believes that changing line extension allowance from the current $850 level to $9,125 would represent such a drastic change where potential Municipal Pumping service customers could be enticed to choose the General Service rate instead, if qualified.

- MP has plans to combine the General Service rates and the Municipal Pumping rates in the future and has taken steps toward achieving this goal in its last retail rate case. MP stated by keeping the Municipal Pumping and the General Service three-phase line extension cost allowances the same is consistent with the planned future combination of these two classes and lessens the chance for customer confusion.

Department – April 16, 2013 Reply Comments
In MP's March 22 comments, MP agreed with some of the Department February 25, 2013 recommendations, however, the Municipal Pumping issue remains unresolved.

Issues that MP has agreed to Department recommendations:

- Agreed with the Department that for new customers the single-phase extension cost allowance could be set at $615 and ;
- Agreed with the Department to set the three-phase allowance for General Service customers at $1,455.

Issue that remain unresolved:

- Disagreement on the extension allowance for three-phase service for Municipal Pumping. The Department is recommending $9,125, while MP is requesting the allowance to be $1,455.

The Department stated that it would not object to MP's Municipal Pumping proposed allowance of $1,455, if the Commission decided to choose that level instead of the Department's recommended level of $9,125.

Order Point 3(b) – Guaranteed Annual Revenue ("GAR") Rule (95-1441 Order)

Minnesota Power – December 26, 2012 Compliance Petition
The Commission allowed MP to change its method of determining the three-phase customer's revenue guarantee necessary to avoid a CIAC payment; the 95-1441 Order approved the 1/3 cost of extension rule . The 95-1441 Order required MP to file in its next rate case a fully embedded average cost study comparing the line extension revenue guarantee necessary to avoid having to make a lump sum CIAC by using the previous approved Schedule A method to the 95-1441 Order approved 1/3 cost of extension rule. MP's 12-1359 Compliance Petition's Figure 1 reflects this comparison.

Figure 1 reflects that the 1/3 cost of extension rule method of calculating the three year guaranteed revenue (GAR) level is approximately the same as the previous Statement A method up to a revenue level of $22,500. After the $22,500 revenue level, the Schedule A method produces a lower required customer guaranteed revenue amount.

MP further supported its use of the 1/3 cost of extension rule by stating that the 1/3 rule is consistent with the line extension revenue guarantee calculations of other investor-owned utilities doing business in Minnesota with the exception of Xcel Energy, which has set its level at 3.5 times the customer's annual revenue.

MP includes revenue from the pass-through of fuel and purchased energy costs in its calculated amount, while the other companies exclude it. MP stated that this policy is more generous.

MP proposed no changes to the current 1/3 cost of extension rule.

Department – February 25, 2013 Comments

The Department stated that the Commission's 95-1441 Order required information about the revenue impacts and results of the new 1/3 cost of extension rule compared to the results under the tariff before 95-1441 implementation, the Schedule A method.

The Department's analysis included a review of MP's 12/26/12 Compliance Filing Figure 1 which compared the required minimum GAR from Schedule A to the 1/3 cost of extension rule. The analysis reflected:

- the 1/3 cost of extension rule is approximately equal to Schedule A for costs up to $22,500; and
- for costs of $22,500 or more, Schedule A resulted in a lower GAR allowance than under the current 1/3 cost of extension rule allowance.

The Department further noted that in the 95-1441 record, MP provided information that demonstrated that Schedule A's allowance credits exceeded or were equal to the 1/3 extension rules allowance credits that were less than $21,100.

The Department concluded that MP's Compliance Petition Figure 1, compares the required minimum GAR as taken from Schedule A and as calculated using the 1/3 cost of extension rule, makes the required 95-1441 Order comparison.

Exclusion of Fuel Clause Adjustment (FCA) revenues from the GAR calculation

The Department analysis further concluded that in MP revenue calculation for the 3-times annual revenue rule included revenues from the pass-through of fuel and purchased energy costs (fuel clause adjustment or FCA), while other companies exclude it. MP supported its policy by stating that its policy more generous than other companies that exclude such items.

The Department stated it was concerned that MP incorrectly calculates its marginal revenues and costs. The Order stated "The Company's support for the change to a single formula for computing the requisite GARs (cost = or < 3 times GARs) is based on an analysis of estimated marginal revenues and costs." While MP counts FCA revenues in its calculation of marginal revenues, it appears that the Company does not count the corresponding FCA costs in its calculation of marginal costs. As a result of adding FCA revenue to the GAR, the Department stated that MP is overestimating the revenue included in GAR. Overestimating the required revenues may cause an interclass subsidy from existing customers to new customers.

The Department recommended to the Commission to order MP to discontinue adding FCA revenue to its GAR because of cross-subsidy issues.

Minnesota Power – March 22, 2013 Reply Comments

Exclusion of Fuel Clause Adjustment (FCA) revenues from the GAR calculation

MP currently includes fuel cost and other energy costs in its GAR revenue calculation, which is contrary to how the other utility companies calculate their GAR revenue levels. The Department recommendation was to remove the fuel costs and other energy costs from the GAR calculation. MP Reply Comments state the Department's position as follows:

> "The Department is concerned that the Company incorrectly calculates its marginal revenues and costs, specifically that the Company counts Fuel Clause Adjustment (FCA) revenues in its calculation of marginal revenues, and apparently does not count the corresponding FCA costs in its calculation of marginal costs. Therefore, the Department recommends that Minnesota Power be required to discontinue adding the FCA revenue to its Guaranteed Annual Revenue (GAR)."

MP disagreed with the Department recommendation to exclude the FCA revenues from its GAR calculation. As part of it Reply Comments, MP included Attachment A - its marginal revenue and cost calculations as justification for not being required to remove the FCA revenues from its GAR calculation. Attachment A demonstrates that both MP's marginal revenues and costs are included FCA. MP also notes that the previous Commission Order states that, "The Company's support for the change to a single formula for computing the requisite GARs (cost = or < 3 times GARs) is based on an analysis of estimated marginal revenues and costs." MP believes that the Department's concern regarding inclusion of FCA revenues and costs in the Company's calculation of marginal revenues and marginal costs is therefore resolved with the additional information provided in Attachment A.

MP further argued that on customer's anniversary date of installing an electric service extension, MP's Customer Information System (CIS) automatically bills the customer the difference between the actual revenue for the past year and the GAR. If the recommendation to exclude the FCA/FPE Adjustment revenue were approved, each month MP would have to manually bill an average of three to four customers, with multiple Electric Service Agreements (ESAs). This would require a manual calculation of the monthly FCA Adjustment revenues and a manual comparison of the net revenues to the GAR. This would be a complex and time-consuming manual process.

Department – April 16, 2013 Reply Comments

Exclusion of Fuel Clause Adjustment (FCA) revenues from the GAR calculation

The Department stated that its initial concern with the calculation of GAR was that it appeared that while MP counted FCA revenues in its calculation of marginal revenues, it did not count the corresponding FCA costs in its calculation of marginal costs. In its Reply Comments, MP provided support that the marginal revenue and the marginal energy costs both include MP's 1994 base cost of fuel. Thus, the Department agrees with MP's request to remove its recommendation to exclude FCA revenue from the calculation of GAR.

Order Point 3(c) – maximum extension cost amount eligible for the GAR payment option (95-1441 Order)

Minnesota Power – December 26, 2012 Compliance Petition

The Commission allowed MP to reduce the maximum extension cost amount eligible for the GAR payment option from $280,000 to $30,000 and is applicable to all customers except for the lighting class. The Commission's 95-1441 Order found that the 30,000 cap had merit as an interim measure since most of the Company's extensions cost less than $30,000 and approved the change on a pilot basis.

The $30,000 level is supported by MP's 12-1359 compliance petition, Exhibit 4, Page 1 which reflects that from 2007 through 2010 approximately 99% of MP's line extension costs were under $30,000, the remaining 1% ranged between $30,000 and $280,000.

MP stated that customers whose line extension costs ranged between $30,000 and $280,000 have a choice in options to commit to the GAR option and/or make an advance payment (CIAC) for some or all of the estimated extension cost. A customer may do both a CIAC and GAR option, if either a GAR or CIAC amount alone does not cover the entire extension cost. During the 2007-2010 time periods, for customers in the $30,000 to $280,000 group, the exhibit reflects that eleven customers paid CIAC for the entire extension cost, and five chose the GAR option. If the customers annual GAR revenues do not cover the calculated annual line extension costs, the customers would be billed the difference between the revenue received minus the GAR revenue at the end of the year.

MP recommendations stated that it is appropriate to use a line extension allowance value closer to the single-phase cost, since the overwhelming majority, over 91% of the service line extensions installed by the Company provides service to single-phase customers. MP believes that its current line extension cost allowance level is reasonable and that its Extension Rules are as well reasonable and working to enable extensions of electric service to new customers.

MP proposed no changes to the maximum revenue level eligible for GAR.

Department – February 25, 2013 Comments

The 95-1441 Order directed MP to reduce the line extension cost GAR level where sharing is subject to negotiation between MP and the customer from $280,000 to $30,000. MP stated by lowering the threshold from $280,000 to $30,000 meant that more service extensions where costs exceeded $30,000 were allowed additional tariff flexibility, including giving the customer and MP additional time to pay for or recover the extension costs.

The Department concluded that MP addressed the impact of reducing the maximum line extension cost amount eligible for the GAR payment option to $30,000 by providing its study on line extensions greater than $30,000. MP's study stated that only a small number [1%] of line extensions have costs exceeding the $30,000 level each year." MP analyzed line extensions above $30,000 but under $280,000 from 2007 through 2011. For line extensions where costs were greater than $30,000, the sharing of line extension costs between the customer and MP is determined on an individual customer basis. The historical data provided in MP's Exhibit 4, page 2 reflects the highest extension cost during the five-year period was $184,350.

The Department concluded that lowering the threshold from $280,000 to $30,000 meant that more service extensions that exceeded $30,000 were allowed the flexibility provided for in MP's tariff, by giving the customer and MP additional time to pay for or recover the line extension costs.

The Department concluded that there is no information in the record to support a change in the $30,000 threshold; therefore, the Department concludes that the current $30,000 threshold should remain in place to continue the flexibility benefits to customers and MP as discussed above.

Staff Discussion

Summary of Current Tariff Provisions

The current service line extension tariff provisions were approved in 95-1441 when MP filed its request to modify the service line extension allowance tariff. MP's current line service extension tariff states that the service line extension cost was determined by estimating costs, which included additional or relocation of existing facilities, the addition of new customers or new system loads assuming MP's standard type construction costs.

The Commission's 95-1441 Order approved the change to an $850 service line extension allowance from the $2,800 previous level. The Commission found that "for now this amount is a reasonable proxy for the actual three phase costs." The Commission applied the $850 service line extension allowance to all services. The Commission further discussed its preference to require MP to file a petition whenever the average embedded costs for this allowance changed by 5% instead of requiring an annual review.

MP's current tariff provisions for service line extensions are reflected in Electric Book, Volume I, Section VI, page No. 4.1, Part IV, and are summarized as follows:

Single-Phase service

Where service line extension costs are less than or equal to $850, the customer would not be required to pay MP for any service line extension costs. If the service line extension costs are greater than the extension allowance of $850, and are for single-phase service, the customer must pay MP in advance a Contribution in Aid of Construction (CIAC) for the extension cost in excess of $850 cost allowance.

Three-Phase service

Where service extension costs are less than or equal to $850, the customer would not be required to pay MP for any service line extension costs. If the service line extension costs are greater than the extension allowance of $850, the three-phase customers have additional options for determining any CIAC, the options are as follows:

- To pay the company a CIAC for extension costs in excess of $850; or
- To enter into a five-year Electric Service Agreement (ESA).

If the customer chooses to enter into a five-year ESA agreement and the construction costs do not exceed $30,000 the following determines whether CIAC is required:

- Where the extension costs are equal to or less than three times the customer's GAR, no CIAC is required; or
- Where the extension costs are greater than three times the customer's GAR, CIAC is required for the balance.

For service line extensions exceeding $30,000 in construction costs, each customer's cost obligations are determined on an individual basis and are based on actual line extension costs determined upon completion of the line extension.

The 95-1441Commission Order directed MP to meet certain filing conditions and required MP to remain in compliance with the tariff provisions.

Staff Analysis

95-1441 Ordering Points 1 and 2

MP stated that it had complied with Ordering Points 1 and 2 of the Commission's Service Extension Order. Exhibit 2 of MP's December 26, 2012 compliance petition provides MP's current Service Extension Rules from its Electric Rate Book – Volume I, Section VI, Page Nos. 4 – 4.5.

Department agreed that MP has complied with the Order Requirements 1 and 2 that modify MP's service extension tariff.

Staff agrees

95-1441 Ordering Point 3

MP failed to comply with 95-1441 Order Requirement No. 3 as directed in the Order. The 95-1441 Order directed MP to address certain items as part of its "next rate case." MP failed to address Order Requirement No. 3 in its 2008 rate case, or in its subsequent 2009 rate case. MP discovered its omission while searching files for other rate information. MP self-reported itself for its omission of the 95-1441 Order Requirement No. 3 in its 12-1359 compliance petition.

Is it acceptable for MP to file its compliance petition for the 95-1441 Order Requirement No. 3 in docket 12-1359?

MP stated that it filed the compliance petition for Order Requirement No. 3 under 12-1359 because the 95-1441 original docket predated the Commission's eDockets system. The petition is cross-referenced to the 95-1441 docket to enable use of eDockets for this petitions.

The Commission and the Department staff held discussions which advised MP on how to proceed after becoming aware of the 95-1441 Order requirement omission and assisted MP in the development of required information to be used for this compliance petition.

Both MP and the Department recommend this compliance petition filing approach.

Staff agrees.

95-1441 Order Point 3(a) – line extension cost allowance

In the 95-1441 Order, the Commission directed MP to change its service line extension cost allowance to $850 from the pre-existing $2,800 amount. The Order further directed MP to file embedded cost studies for both single and three-phase customers in its next rate case and to file for a service line extension allowance adjustment if at any time its embedded cost calculation reflects a 5% change for the current allowances.

The Department concluded that MP's current $850 service line extension allowance is not reasonable for all services and should be adjusted. The Department recommended the following service line extension allowances which would require MP to revise its tariff.

Customer Class	Current Allowance	Department Recommendations
Residential (single-phase only)	$850	$ 615
General Service (mix of single- and three-phase)	$850	$ 1,455
Municipal Pumping (mix of single- and three-phase)	$850	$ 9,125

MP agreed to the Department's residential single-phase allowance of $615 and the General Service allowance of $1,455. But, MP disagreed with the Department's Municipal Pumping allowance of $9,125. MP supports a recommendation of 1,455 for Municipal Pumping.

The Department continued to recommend that the service line extension allowance for Municipal Pumping be set at $9,125. However, the Department stated that if the Commission chooses MP's proposed allowance of $1,455 for Municipal Pumping, it would not object since $9,125 appears to be a drastic change from the current $850 allowance.

On the surface, MP's average embedded cost calculations for service line extension allowances appear to be sufficient. The Commission's 95-1441 Order was specific by requiring MP to provide an embedded cost study reflecting a separate calculation for single and three-phase customers. But, both the Department and staff have concluded that the calculation for General Service and Municipal Pumping reflected in Exhibit 3 of MP's 12/26/12 compliance petition, include both single and three-phase customers in the service allowance calculation, thus creating the possibility that cross-subsidization between customer classes may happen.

MP stated that it does not maintain separate single-phase and three-phase service line extension information for General Service and Municipal Pumping customers. Therefore, MP cannot provide an average embedded cost for single-phase service distinct from three-phase General Service or Municipal Pumping customers to enable an analysis of the difference within these rate classes.

Staff does not believe that MP has met the Order requirements and that MP has not adequately supported its compliance petition position. Pursuant to Minn. Stat. 216B.03, the Commission is required to set just and reasonable rates for utility services that are applicable to all customers. From the record, staff is not able to determine whether MP's proposed revisions to its service line allowances are reasonable because MP has not provided separate embedded cost studies for extending single and three-phase service. The Commission may wish to require MP to provide a recalculation of its embedded cost allowance by separating the single and three-phase costs for certain customer classes that are currently grouped together in determining MP's allowance levels, as directed in the Commission's 95-1441 Order.

If the Commission chooses to accept MP's current embedded cost study, staff generally believes that the Department's recommendations are reasonable and acceptable. The recommended allowance would be as follows:

Customer Class	Revised Cost Allowances
Residential (single-phase only)	$ 615
General Service (mix of single- and three-phase)	$ 1,455
Large Light and Power (three-phase only)	$66,905
Municipal Pumping (mix of single- and three-phase)	$ 9,125

If the Commission decides to accept MP arguments and determines that the General Service and Municipal Pumping allowance amounts should be combined. Staff would recommend that MP be required to combine the costs reflected in the embedded cost study in determining the appropriate combined allowance for this determining this service.

Has MP complied with the 95-1441 Order requirement to file an updated service line extension allowance when the underlying average embedded costs calculation changes the allowances by 5%?

The 95-1441 Order required MP to file a compliance petition whenever MP's average embedded costs calculation changed by 5% which enables the Commission to establish appropriate allowance level.

Department concluded that every MP's line extension allowances had changed by more than the 5%. The Department calculated that a 5% change in the current $850 line extension allowance results in approximately $42; which translates to a range of $808 to $892.

Staff agrees with the Department's calculations, in that every currently effective line extension allowance in MP's tariff has changed by more than 5%, see the following summary:

Customer Class	Current Allowance	Department Recommendation	Percent Change
Residential (single-phase only)	$850	$ 615	(28%)
General Service (mix of single- and three-phase)	$850	$ 1,455	71%
Large Light and Power (three-phase only)	$850	$66,905	7771%
Municipal Pumping (mix of single- and three-phase)	$850	$ 9,125	974%
Weighted average cost (mix of single- and three-phase)	$850	$ 3,090	264%
Average of all Customer Classes	$850	$ 990	17%

From the record, staff cannot determine when these increases occurred, but it seems reasonable to staff to make the assumption that MP surpassed the 5% Order requirement before making this petition.

The Commission may wish to reconsider the latitude it gave MP in its 95-1441 Order by changing the compliance petition requirement reflected in the Order that required MP to make to file a petition whenever its service line extension allowance embedded cost calculation reflects a change that exceeds 5%. The Commission may want to consider requiring MP to file its embedded cost study annually or make the determination to use some other basis or method in making the allowance calculation.

95-1441 Ordering Point 3b – Guaranteed Annual Revenue ("GAR") Rule

In the 95-1441 Order, the Commission directed MP to change its method of calculating the Guaranteed Annual Revenue ("GAR") from the Schedule A method to the 1/3 cost of extension rule method. The Order required MP to prepare an average embedded cost study reflecting the separation of all service phases (one and three phase) to examine whether any interclass subsidy resulted from the change to the 1/3 cost of extension rule from the previous Schedule A method.

Does MP's 12-1359 compliance petition include an average embedded cost study that provides the basis for examining whether any interclass subsidy has resulted from the change to the 1/3 cost of extension rule method from the previous Schedule A method?

MP stated that it has met the Order Requirement No. 3 in its compliance petition on Page 4, Figure 1. Figure 1 illustrates that the GAR revenue requirement would be approximately the same under both the 1/3 cost of extension rule and Schedule A up to $22,500 after which Schedule A method would produce a lower GAR revenue requirement.

MP further stated that its use of the 1/3 cost of extension rule is consistent with the GAR calculations of other investor-owned utilities doing business in Minnesota with the exception of Xcel Energy, which has set its level at 3.5 times the customer's annual revenue. MP proposed no changes to the 1/3 cost of extension rule method of calculating the guaranteed annual revenue (GAR) level.

The Department does not make any recommendation on MP's GAR revenue calculation method. However, the Department recognizes that the GAR revenue from either method is approximately the same up to $22,500 and the Schedule A method does produce a lower GAR with larger amounts.

The 95-1441 Order, required MP to address discontinuance of Schedule A and adoption of a 1/3 cost of extension rule and required MP to compare the amount of GAR annual revenues that a three-phase customer must guarantee to avoid having to make a lump sum CIAC contribution to an equivalent Schedule A amount. The Order also required MP to include a fully embedded average cost study to provide the cost basis for examining whether this policy change resulted in any interclass subsidy.

From the information provided in the record, it appears that MP's Figure 1 does provide the required 95-1441 Order information. The 1/3 cost of extension rule method appears to be comparable to the previous Schedule A method in determining the GAR revenue requirement up to $22,500. Thus, staff generally believes that MP has met the 95-1441 Order requirements and that the 1/3 cost of extension rule GAR method does not need to be changed at this time.

Should MP's GAR calculation include its Fuel Clause Adjustment (FCA) revenues?

In its 12/26/12 compliance filing, MP stated that its GAR amounts include the pass-through of fuel and purchased energy costs (Fuel Clause Adjustment (FCA) revenues) amounts, while the other companies exclude it. MP stated that by doing this, its GAR calculation under this policy is more generous. The Department recommended making no GAR calculation methodology changes in its 4/16/13 Comments.

Staff generally agrees with the Department's recommendation. But, from the record, staff cannot determine if MP is properly accounting for its fuel costs included in its monthly fuel clause adjustment (FCA). Staff is concern that MP's reported fuel costs may be distorted and somehow the fuel costs may be under/over stated. The Commission may wish to discuss this with MP.

95-1441 Ordering Point 3c – maximum extension cost amount eligible for the GAR payment option

In the 95-1441 Order, the Commission directed MP to reduce the maximum extension cost amount eligible for the GAR payment option to $30,000 from the pre-existing $280,000 amount. The Order further required MP to include information about the revenue impacts and results of the new policy compared to the results under the existing (previous) tariff in its compliance filing.

Does MP's 12-1359 compliance petition meet the 95-1441 requirements to provide a study comparing the revenue impacts and results of using $30,000 new policy amount compared to the results of the previous $280,000 amount?

MP proposed no changes to the $30,000 maximum revenue level eligible for GAR.

The Department concluded that by lowering the threshold from $280,000 to $30,000 meant that more service extensions where costs exceeded $30,000 were allowed additional tariff flexibility, including giving the customer and MP additional time to pay for or recover the extension costs. The Department recommended that the current $30,000 threshold should remain unchanged to continue to provide the flexibility benefits to customers that MP has discussed above and that there is no information in the record to support a change in the $30,000 threshold at this time.

Staff generally agrees with the Department's recommendation.

Is MP consistently calculating its service line extension costs for all requesting customers?

During the review of this docket, an individual filed an informal complaint with the Commission's Consumer Affairs Office which stated that MP provided several different cost estimates for the same service line extension request. The customer complaint was filed on 3/19/13 and was assigned a Consumer Record number of 61614.

The customer complaint stated that MP had provided numerous service line extension cost estimates in 2012 and 2013 for the same proposed service line extension route. In 2012, the cost estimate was calculated at $15,250 and in 2013 the customer received a cost estimate of approximately $38,000. The customer stated that it later complained to MP about the difference between the 2012 and 2013 estimates, and received another estimate of approximately $16,000. Confused by the different cost estimates, the customer contacted the Commission and subsequently filed an informal complaint. After involving the Commission, the customer received another cost estimate of approximately $15,300. After the Commission reviewed this cost estimate, the customer received another estimate from MP of approximately $11,000.

Staff believes that this complaint has revealed some inconsistencies in how MP applies its extension policy and how its representatives in the field calculate service line extension cost estimates. Staff believes this customer ultimately paid the correct service line extension charges, but the process described above caused alarm about the possible lack of consistency and uniformity in the way MP applies its tariff and treats new customers. The Commission may wish to require MP to revise its extension policy in a compliance filing to ensure that MP's administrators and field representatives are provided better guidance on a company-wide basis on how to accurately, consistently and uniformly calculate estimates of service line extension costs. This would ensure that potential new customers are provided with accurate information about the charges they will be assessed for new service and they will not have to go through the process that the previous new customer went through.

Decision Alternatives

95-1441 Order Point 3a – line extension cost allowance

1. Accept the Department preferred alternative (recommendation) and the MP embedded cost studies as satisfying 95-1441 Order Point 3 (a) – line extension cost allowance embedded cost study requirement and change MP's Section VI, page No. 4.1, Part IV tariff to reflect the following service line extension allowances:

    - $615 for Residential Customer Service
    - $1,455 for General Customer Service
    - $66,905 for Large Light and Power Customer Service
    - $9,125 for Municipal Pumping Customer Service <u>or</u>

2. Accept the Department second choice alternative (recommendation) and the MP embedded cost studies as satisfying 95-1441 Order Point 3 (a) – line extension cost allowance embedded cost study requirement, change MP's Section VI, page No. 4.1, Part IV tariff to reflect the following service line extension allowances, and allow MP the combine the General and Municipal Pumping Services:

    - $615 for Residential Customer Service
    - $1,455 for a Combined General Customer and Municipal Pumping Services
    - $66,905 for Large Light and Power Customer Service <u>or</u>

3. Accept the Department recommendation <u>as modified below in the bullet points</u> and the MP embedded cost studies as satisfying 95-1441 Order Point 3 (a) – line extension cost allowance embedded cost study requirement, change MP's Section VI, page No. 4.1, Part IV tariff to reflect the following service line extension allowances, and allow MP the combine the General and Municipal Pumping Services:

    - $615 for Residential Customer Service
    - Require MP to combine data from the two services and re-calculate the service line extension allowance for General Customer and Municipal Pumping Services
    - $66,905 for Large Light and Power Customer Service <u>or</u>

4. Do not accept the Department recommendation and require MP to provide a revised embedded cost studies separating the one and three-phase customers for General and Municipal Pumping Services line extension allowances.

95-1441 Order Point 3a – MP requirement to adjust its service line extension allowance if the average embedded costs change by 5%.

5. Continue the current 95-1441 requirement to file a compliance petition with Commission whenever the average embedded costs change the line extension service allowances by 5% (or more) from the currently effective allowances. <u>or</u>

6. Continue the current 95-1441 requirement to change the service line extension allowances when the average embedded costs change the line extension service allowances by 5% (or more), but in the event MP's costs have not changed, require MP to file an annual letter stating that the allowance have not changed by more than 5%. <u>or</u>

7. Discontinue the current 95-1441 requirements and require MP to file an annual compliance petition with Commission that includes updated average embedded costs adjusting its service line allowances.

   <u>And</u>

8. Continue the requirement that MP, in its next rate case, include a fully embedded average cost study separated by single and three-phase service and by customer class to provide the cost basis for examining MP's extension policy.

95-1441 Ordering Point 3b – Guaranteed Annual Revenue ("GAR") Rule

9. Allow MP to continue to use the 1/3 cost of extension rule method to determine its GAR level and that MP satisfied the 95-1441 embedded cost study requirement. <u>or</u>

10. Determine that MP has not met the 95-1441 embedded cost study requirement and require MP to file a new embedded cost study.

95-1441 Ordering Point 3c – maximum extension cost amount eligible for the GAR payment option

11. Allow MP to continue to use $30,000 as the maximum extension cost amount level eligible for a GAR payment and that MP satisfied the 95-1441 Order study requirement. <u>or</u>

12. Determine that MP has not met the 95-1441 Order study requirement and require MP to file a new embedded cost study.

Fuel Clause Adjustment (FCA) revenues in the GAR calculation

13. Allow MP to continue its current practice of including the Fuel Clause Adjustment revenues in its GAR calculations for customers. <u>or</u>

14. Require MP to discontinue including the Fuel Clause Adjustment revenues in its GAR calculations for customers.

Revision to MP's service line extension tariff for determining costs

15. Require MP to file a compliance petition revising its service line extension tariff reflecting changes in how MP will determine costs charged to customers. <u>or</u>

16. Do not require MP to make any tariff changes for how MP calculates its service line extension costs.