

February 23, 2017

Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101-2147

RE: **Response Comments of the Minnesota Department of Commerce, Division of Energy Resources**
Docket No. G011/M-16-87

Dear Mr. Wolf:

The Minnesota Department of Commerce, Division of Energy Resources (Department) provides the following *Response Comments* with regards to the following matter:

Minnesota Energy Resources Corporation's (MERC) Petition for Approval of a Variance to the Purchased Gas Adjustment (PGA) Rules to Allow Recovery through the PGA of Amounts Paid for Kansas Gas Storage Taxes Associated with Contracts Acquired from Interstate Power and Light Company (IPL).

Based on our review of MERC's *Reply Comments*, the Department recommends that the Minnesota Public Utilities Commission (Commission) approve the Company's *Petition*, as modified by MERC's *Reply Comments*. The Department is available to answer any questions the Commission may have.

Sincerely,

/s/ SACHIN SHAH
Rates Analyst

SS/lt
Attachment

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

RESPONSE COMMENTS OF THE
MINNESOTA DEPARTMENT OF COMMERCE
DIVISION OF ENERGY RESOURCES

DOCKET No. G011/M-16-87

I. BACKGROUND

On January 27, 2016, Minnesota Energy Resources Corporation (MERC or the Company) filed a variance petition (Petition) requesting approval from the Minnesota Public Utilities Commission (Commission) to include recovery of past and on-going Kansas ad valorem taxes (KAVT) related to natural gas storage in the current cost of natural gas supply. The Company in its *Petition* sought a variance to the Commission's Purchased Gas Adjustment (PGA) rules to allow the Company to recover the taxes.

On November 14, 2016, the Minnesota Department of Commerce (Department) filed its *Comments*. The Department requested that MERC provide in *Reply Comments* additional information and clarification as follows:

- Given the KAVT costs incurred on the storage contracts associated with the Interstate Power and Light (IPL) Northern Natural Gas (NNG) interstate pipeline system (that MERC has assumed from May 2015 onward), the Commission's approval of the consolidation of MERC's Albert Lea (MERC-ABL) and MERC-NNG purchased gas adjustments (PGA), and the timing of the Commission's decision in this matter, please provide the estimated amounts that MERC will seek to recover from the old MERC-ABL and MERC-NNG PGAs and provide the associated bill impacts.
- In its Petition, MERC did not provide a projected amount for the ongoing recovery of costs. The Department requests that, in reply comments, MERC provide, in detail, the amounts MERC seeks to recover on an ongoing basis, the estimated bill impacts, and an explanation of how these specific amounts were determined.
- Given that MERC filed its most recent rate case in 2015 with a 2016 test year, well after the Supreme Court of the United States (SCOTUS) decision upholding the KAVT was made, and well after the IPL Asset Purchase and Sale Agreement was executed and approved by the Commission, please address whether MERC included any (whether past or ongoing) of the KAVT costs associated with the former IPL contracts in its current rate case in Docket No. G011/GR-15-736. If

so, we request that MERC quantify what was included, and if not, to explain why the costs were not included.

- Regarding the \$151,247 of unrecovered KAVT costs, please provide detailed explanations of the following:
 - a) How did MERC determine the figure of \$151,247?
 - b) MERC stated that it executed the Asset Purchase and Sale Agreement on September 3, 2013 and that it acquired a total of \$151,247 in unrecovered Kansas storage costs, yet in its February 4, 2014 Filing in Docket 14-107, MERC stated that it had no deferred tax assets, deferred tax liabilities, regulatory deferrals of tax, or deferred tax credits of IPL included with the sale of assets to the buyer. Once again, please explain in detail how MERC came to its conclusion that it “acquired a total of \$151,247 in unrecovered Kansas storage costs?”
 - c) If the MERC estimated tax liability of \$6,102.17 (for January 2015 – April 2015) is added to the actual amount (for 2009-2014) shown in Attachment A of the Petition of \$148,312.48, it results in a total of \$154,414.51. Once again, how did MERC determine the \$151,247 amount?
 - d) Please explain how the estimated tax liability of \$6,102.17 was determined.

The Department stated that it would offer additional comments and recommendations in subsequent response comments after it had reviewed the additional information.

On December 8, 2016 MERC filed a response to the Department’s requests. The Department discusses the responses below.

II. PGA CONSOLIDATION, TIMING AND BILL IMPACT

With regards to the requests on PGA consolidation, timing and bill impact, MERC stated the following:

MERC proposes that the lump sum amount for the period 2009 through 2014 be recovered from the Albert Lea PGA before PGA consolidation on July 1, 2017. As shown on Attachment A to this filing, MERC paid IPL \$145,147 for the 2009-2014 storage taxes allocated to IPL’s Minnesota customers. Assuming MERC receives approval of the requested variance effective February 2017, MERC proposes to recover the past tax costs for the period 2009 through 2014 from the Albert Lea PGA, prior to consolidation with the MERC-NNG PGA. Recovery of this historic

tax amount from the Albert Lea PGA is reasonable and appropriate because these costs are attributable to that PGA.

... MERC believes recovery of the historic 2009-2014 costs from the Albert-Lea PGA prior to consolidation would be appropriate and that the rate impacts would be reasonable. MERC acknowledges that under its proposal it would begin collecting the Kansas ad valorem tax at or near the same time final rates will be implemented in MERC's pending rate case. MERC believes the overall bill increase is reasonable and that the expense should be recovered from the former IPL customers who benefitted from the storage from 2009 through 2014.¹

In its *Comments*, the Department had stated the following:²

In Docket 15-149, the Commission approved, for the past lump-sum assessment, a 5-year variance for Xcel to match the amortization period. The Department notes that, in this case, amortizing the 2009 through April 2015 KAVT amounts over a 4- or 5-year period may not be appropriate since the Commission approved consolidation of MERC's Albert Lea and NNG PGA systems effective July 1, 2017. Thus, allowing most of the costs to be recovered by MERC's Albert Lea (legacy IPL) PGA customers is appropriate given that MERC's Albert Lea (legacy IPL) customers received the benefits of the storage during that time period.

MERC also provided a Table in its Reply Comments³ showing the total and monthly impact if the \$145,147 is recovered from the Albert Lea PGA during the period February 1, 2017 – June 30, 2017 (over five months). The Department reviewed MERC's calculations provided in its *Reply Comments*, and concludes that they are reasonable. The Department agrees with MERC that it is appropriate for the Company to recover only those tax amounts from and attributable to the natural gas storage used by MERC's Albert Lea (legacy IPL) PGA customers.

¹ MERC *Reply Comments* pages 2-3.

² Department *Comments* at page 18.

³ MERC *Reply Comments* pages 2-3.

III. RECOVERY OF ONGOING COSTS

As mentioned above, the Department in its *Comments* sought clarification on the amounts MERC sought to recover on an ongoing basis, the estimated bill impacts and an explanation on how these specific amounts were determined.⁴

In its *Reply Comments*, MERC stated the following:⁵

At the outset, MERC notes that it is withdrawing its request for a variance to recover the ongoing Kansas ad valorem taxes attributable to the former Interstate Power and Light (IPL) customers. As discussed below, the administrative burden of collecting the ongoing expense through the PGA outweighs the benefit and MERC will absorb the ongoing Kansas ad valorem taxes as a shareholder expense until the filing of our next rate case. MERC continues to request a variance to recover the lump sum of \$145,147 for the Kansas ad valorem taxes paid from 2009 through 2014.

... At the time MERC filed its Petition in this docket, the amount of ongoing Kansas tax costs was not known because final tax bills had not yet been received from the Kansas taxing authorities for the year 2015. MERC has since received the Kansas invoices for 2015 and the tax expense related to the Albert Lea storage is approximately \$13,000. See Attachment B, attached to this filing. In light of the administrative challenges and expense associated with recovery of these ongoing costs through the PGA, MERC withdraws its request as it relates to the recovery of costs for the years 2015 and onward. Although these amounts were not included in MERC's most recent rate case expense for the Albert Lea storage, the amount of this expense is anticipated to be relatively small and the administrative burden of collecting the expense through the PGA and obtaining additional annual variance extensions does not justify the recovery. MERC proposes to treat the Albert Lea storage expense as a shareholder expense until MERC files its next rate case, at which time MERC will calculate the Kansas storage tax expense based on the consolidated storage contracts, including the Albert Lea contracts.

⁴ Department *Comments* at page 19-20.

⁵ MERC's *Reply Comments* at pages 1, and 3-4.

The Department appreciates MERC's clarification regarding the amounts MERC sought to recover on an ongoing basis. The Department appreciates MERC's proposal to withdraw its request to recover the ongoing KAVT associated with the former IPL contracts and for MERC "to treat the Albert Lea storage expense as a shareholder expense until MERC files its next rate case, at which time MERC will calculate the Kansas storage tax expense based on the consolidated storage contracts, including the Albert Lea contracts."

The Department notes that MERC's KAVT obligation for 2015 was approximately \$267,866 (inclusive of the approximately \$13, 233 costs attributed to the former IPL contracts and as a result, the corresponding MERC-NNG portion would be approximately \$254,633). In Docket No. G011/GR-15-736 (Docket 15-736), MERC requested recovery of \$286,509 of KAVT costs. No party opposed the Company's request; the Commission approved the request through its October 31, 2016 *Findings of Fact, Conclusions, and Order*.

Thus, depending on the actual weather, the Company's operating conditions and the associated natural gas usage and storage inventory at year-end, to the extent the actual total MERC KAVT costs are at or below \$286,509, MERC's shareholders will not be required to cover the ongoing costs associated with the former IPL contracts, since current rates would be sufficient to recover MERC's total KAVT costs.

IV. RECOVERY OF PAST OR ONGOING COSTS IN BASE RATES

The Department in its *Comments* stated and observed the following:⁶

... Given that MERC filed its most recent rate case in 2015 with a 2016 test-year, well after the SCOTUS decision was made, and well after the IPL Asset Purchase and Sale Agreement was executed and approved by the Commission, the Department requests that, in Reply Comments, MERC explain whether it included any (whether past or the on-going assessments) of the KAVT costs associated with the former IPL contracts in its current rate case in Docket No.G011/GR-15-736. If so, we request that MERC quantify what was included, and if not, to explain why the costs were not included.

In its *Reply Comments*, MERC stated the following:⁷

MERC responds that none of the Kansas storage tax costs associated with the former IPL storage were included in MERC's calculation of test year property tax expense in Docket No. G011/GR-15-736 because of the timing of MERC's rate case filing in Docket No. G011/GR-15-736. At the time MERC prepared its rate case filing, it did not have information regarding

⁶ Department's *Comments* at pages 13-14.

⁷ MERC's *Reply Comments* at page 4.

the test year (and ongoing) expense for the IPL Kansas storage. MERC's rate case was filed September 30, 2015, based on MERC's historical experience with Kansas property taxes, which did not include any taxes associated with the IPL gas storage, and no assumption for the IPL taxes associated with gas storage was made or included in the rate case. The 2015 Kansas tax bills (the first bills reflecting MERC's ownership of the IPL storage) were not received from the taxing authorities until November of 2016.

The Department appreciates MERC's explanations above. As mentioned previously, the Department observes that to the extent the actual total MERC KAVT costs are below \$286,509, ostensibly MERC will be recovering the costs associated with the former IPL contracts.

V. CALCULATION OF KAVT COSTS

The Department in its *Comments* stated and observed the following:⁸

... a) How did MERC determine the figure of \$151,247?

b) MERC stated that it executed the Asset Purchase and Sale Agreement on September 3, 2013 and that it acquired a total of \$151,247 in unrecovered Kansas storage costs, yet in its February 4, 2014 Filing in Docket 14-107, MERC stated that it had no deferred tax assets, deferred tax liabilities, regulatory deferrals of tax, or deferred tax credits of IPL included with the sale of assets to the buyer. Once again, please explain in detail how MERC came to its conclusion that it "acquired a total of \$151,247 in unrecovered Kansas storage costs?"

c) If the MERC estimated tax liability of \$6,102.17 (for January 2015 – April 2015) is added to the actual amount (for 2009-2014) shown in Attachment A of the Petition of \$148,312.48, it results in a total of \$154,414.51. Once again, how did MERC determine the \$151,247 amount?

d) Please explain how the estimated tax liability of \$6,102.17 was determined.

In its *Reply Comments*, MERC stated the following:⁹

⁸ Department's *Comments* at page 21.

⁹ MERC's *Reply Comments* at page 4.

... This calculation consists of \$145,147 of allocated tax liability for the years 2009-2014 and \$6,102 as the estimated amount due for January thru April 2015, for a total of \$151,249. As mentioned, MERC is amending its petition to seek a variance to recover only the amount paid to IPL for tax liability through 2014 (\$145,147).

... Under the Asset Purchase and Sale Agreement, the purchase price paid by MERC for the acquisition of IPL's Minnesota natural gas assets and operations included the PGA over/under collection and gas storage. While the Agreement expressly excluded pre-closing tax liability, the amount of Kansas storage costs for the period 2009-2015 were included in the PGA under-collection amount that was transferred.

... In particular, the final Minnesota tax allocation for 2009-2014 was \$148,312 whereas the tax allocation recorded and included in the sale was \$145,147. The slight difference results from the fact that the tax allocations were estimates until the actual tax bills were issued by the Kansas taxing authorities. Because the amount paid by MERC to IPL for the 2009-2014 Kansas tax costs was \$145,147, that is the amount that properly should be approved for recovery from former IPL customers, and for simplicity sake MERC is no longer seeking the \$6,102 attributable to January-April 2015.

The Department appreciates MERC's explanations for the calculations and agrees with MERC that it should only recover the amounts paid to IPL for the KAVT costs from 2009 through 2014.

VI. REPORTING REQUIREMENTS

The Department in its *Comments* stated and observed the following:¹⁰

... MERC has not proposed to report the tax costs as separate line items in the monthly PGAs, AAA report and annual PGA true-up filings. To clarify, the Department recommends that MERC provide, in the Company's AAA report and PGA True-Up filings filed in September each year, the actual amount paid in ad valorem tax as well as recovered from ratepayers by state. Additionally, the costs and revenues should be listed as separate line items.

¹⁰ Department's *Comments* at page 20.

In its *Reply Comments*, MERC stated the following:¹¹

Because MERC is proposing to withdraw its requests for recovery of ongoing Kansas ad valorem tax expense and is requesting approval to recover only the lump sum Kansas tax expense for the period 2009-2014 from the MERC-Albert Lea PGA, MERC believes much of the Department's recommendation for ongoing reporting is no longer necessary. MERC would propose to list the Kansas tax expense on the monthly PGA as a separate line item and would track the amount of recovery on a monthly basis relative to the total expense of \$145,147. MERC would then propose to roll any over- or under-recovered amount into the MERC-NNG PGA with the 2017 AAA and True-Up filings effective September 1, 2017.

The Department appreciates MERC's explanations and agrees with MERC that reporting for the ongoing KAVT expense amounts is not necessary given the Company's request to forego recovery for future storage assessments. The Department also agrees with MERC that the Company should report the tax costs as separate line items in the monthly PGAs, Annual Automatic Adjustment (AAA) reports and annual PGA true-up filings.

In addition, the Department notes that MERC's proposal "to roll any over- or under-recovered amount into the MERC-NNG PGA with the 2017 AAA and True-Up filings effective September 1, 2017" appears reasonable given the PGA consolidation approved by the Commission. However, the Department clarifies that MERC should ensure that, to the extent feasible, the costs to be recovered by MERC's Albert Lea (legacy IPL) PGA customers are appropriate given that MERC's Albert Lea (legacy IPL) customers received the benefits of the storage during that time period.

The Department recommends that the Commission approve a variance to include recovery in the PGA of ad valorem taxes as set forth in MERC's *Reply Comments*.

¹¹ MERC's *Reply Comments* at page 6.

VII. RECOMMENDATIONS

Based on our review, the Department recommends that the Commission approve MERC's *Petition*, as modified in its December 8, 2016 *Reply Comments*.

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CERTIFICATE OF SERVICE

I, Sharon Ferguson, hereby certify that I have this day, served copies of the following document on the attached list of persons by electronic filing, certified mail, e-mail, or by depositing a true and correct copy thereof properly enveloped with postage paid in the United States Mail at St. Paul, Minnesota.

**Minnesota Department of Commerce
Response Comments**

Docket No. G011/M-16-87

Dated this 23rd day of February 2017

/s/Sharon Ferguson

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