

**Minnesota Public Utilities Commission**  
*Staff Briefing Papers*

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**Meeting Date: May 25, 2017 ..... Agenda Item #4\***

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**Company:** United Natural Gas, LLC

**Docket No.** **G-6960/M-16-317**

In the Matter of a Petition by United Natural Gas, LLC's (UNG) , a subsidiary of United Farmers Cooperative (UFC) for Approval of a Firm Gas Transportation Agreement with the City of Brownton (Brownton)

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**Issues:** Should the Commission approve United Natural Gas, LLC's petition for a Firm Gas Transportation Agreement providing intrastate pipeline transportation services to the City of Brownton (Brownton)?

Should the Commission require United Natural Gas, LLC (UNG) to explain its arrangement with United Grain System, LLC (UGS) in a compliance filing?

- If UNG is providing transportation services to UGS, should the Commission require a transportation agreement between the parties?
- If UNG is purchasing natural gas for either the City of Brownton or UGS, does this arrangement compromise its "intrastate pipeline" status making UNG a "public utility" subject to Minnesota Statute § 216B.48 – Affiliated Interest?

**Staff:** Bob Brill ..... 651-201-2242

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***Relevant Documents***

United Natural Gas, LLC (UNG) – Petition .....April 13, 2016  
Department of Commerce (Department) – Comment.....December 7, 2016

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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.

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*May 15, 2017*

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## Statement of the Issues

Should the Commission approve United Natural Gas, LLC's petition for a Firm Gas Transportation Agreement providing intrastate pipeline transportation services to the City of Brownton (Brownton)?

Should the Commission require United Natural Gas, LLC (UNG) to explain its arrangement with United Grain System, LLC (UGS) in a compliance filing?

- If UNG is providing transportation services to UGS, should the Commission require a transportation agreement between the parties?
- If UNG is purchasing natural gas for either the City of Brownton or UGS, does this arrangement compromise its "intrastate pipeline" status making UNG a "public utility" subject to Minnesota Statute § 216B.48 – Affiliated Interest?

## Introduction

United Natural Gas, LLC (UNG) is seeking Commission approval of its September 13, 2013 Firm Transportation Agreement (Agreement)<sup>1</sup> with the City of Brownton (Brownton).<sup>2</sup> The proposed agreement provides transportation services to Brownton which enables it to provide natural gas distribution services to customers who previously did not have access to natural gas. UNG is a wholly owned subsidiary of United Farmers Cooperative (UFC).

In its January 6, 2017 *Comments*, the Department recommended that the Commission approve the UNG/Brownton transportation agreement. The Department believes the UNG/Brownton Agreement is in the public interest. The Department did not address the services provided by UNG to its UGS affiliate.

PUC staff generally agrees with the Department's recommendation that the UNG/Brownton Firm Transportation Agreement is in the public interest and should be approved, but PUC staff is providing additional discussion on the following:

- The UNG/UGS arrangement – staff is unclear what services UNG provides to UGS and the related rates charged.
- Staff is not sure if UNG qualifies as an "intrastate pipeline" based on statements made in Docket No. 12-250 and if UNG becomes a "public utility" is UNG subject to Minnesota Statute § 216B.48 – Affiliated Interest, which could require UNG to petition the Commission for its approval of an affiliated interest agreement with UGS.

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<sup>1</sup> Pursuant to Minn. Stat. § 216B.045, Subd. 4.

<sup>2</sup> UNG's facilities consist of a 4-mile intrastate pipeline providing transportation services to the City of Brownton and to United Grain Services (UGS) from an interconnection with the Hutchinson Intrastate Pipeline.

## Relevant Statutes

### Regulation of Intrastate Natural Gas Pipeline. Minn. Stat. § 216B.045.

#### Subd. 1. Definition of intrastate pipeline.

....."intrastate pipeline" means a pipeline wholly within the state of Minnesota which transports or delivers natural gas received from another person at a point inside or at the border of the state, which is delivered at a point within the state to another, provided that all the natural gas is consumed within the state.<sup>3</sup>

#### Subd. 2. Reasonable rate.

Every rate and contract relating to the sale or transportation of natural gas through an intrastate pipeline shall be just and reasonable. No owner or operator of an intrastate pipeline shall provide intrastate pipeline services in a manner which unreasonably discriminates among customers receiving like or contemporaneous services.

#### Subd. 3. Transportation rate; discrimination.

Every owner or operator of an intrastate pipeline shall offer intrastate pipeline transportation services by contract on an open access, nondiscriminatory basis.<sup>4</sup>

#### Subd. 4. Contract; commission approval.

No contract establishing the rates, terms, and conditions of service and facilities to be provided by intrastate pipelines is effective until it is filed with and approved by the commission. The commission has the authority to approve the contracts and to regulate the types and quality of services to be provided through intrastate pipelines.<sup>5</sup>

### Relations with Affiliated Interest. Minn. Stat. § 216B.48

The affiliated interest statute applies to entities that meet the statutory definition of a public utility and their affiliates as defined in Minn. Stat. §216B.48, subd. 1. No contract or

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<sup>3</sup> Further, an intrastate pipeline does not include a pipeline owned or operated by a public utility, unless a public utility files a petition requesting that a pipeline or a portion of a pipeline be classified as an intrastate pipeline and the commission approves the petition.

<sup>4</sup> To the extent the intrastate pipeline has available capacity, the owner or operator of the intrastate pipeline must provide firm and interruptible transportation on behalf of any customer. If physical facilities are needed to establish service to a customer, the customer may provide those facilities or the owner or operator of the intrastate pipeline may provide the facilities for a reasonable and compensatory charge.

<sup>5</sup> The approval of a contract for an intrastate pipeline to provide service to a public utility does not constitute a determination by the commission that the prices actually paid by the public utility under that contract are reasonable or prudent nor does approval constitute a determination that purchases of gas made or deliveries of gas taken by the public utility under that contract are reasonable or prudent.

arrangement with an affiliate is considered “valid or effective” [for most purposes] “unless and until the contract or arrangement has received the written approval of the commission.”

## United Natural Gas, LLC (UNG)

On March 30, 2012, UNG filed its Information Book for Owners and Tenants of Property (Information Book) for its proposed pipeline project’s route in Docket No. 12-250. UNG constructed a 4-mile intrastate pipeline that interconnects with the Hutchinson Utilities intrastate pipeline (not rate regulated by the Commission) and terminates at the United Grain Systems, LLC (UGS) facility, an affiliate. UNG stated that at the time of construction that UGS was its only customer. Both UNG and UGS are subsidiaries of United Farmers Cooperative (UFC). UFC operates the UNG pipeline as an independent company on an arm-length basis from UFC as a natural gas delivery (transportation) company.

In its April 19, 2012 Comments, the Department recommended the Commission approve UNG’s “Information Book” and proposed pipeline’s route. In its May 16, 2012 Order, the Commission adopted the Department’s recommendations and approved UNG’s proposal. The UNG pipeline was placed in-service in September 2012. UNG did not submit a transportation service agreement for its arrangement with UGS.

In early 2013, UNG and the City of Brownton negotiated their agreement where UNG transports Brownton’s natural gas supply from the Hutchinson interconnection to UNG terminus at the UGS facilities. Brownton constructed its own facilities from its municipal border to the UNG terminus point, approximately 1-mile. UNG had available transportation capacity and entered into an agreement with Brownton. Brownton serves the municipality’s customers and is exempt from Commission regulation.

[Staff note: From UNG’s petition it is unclear if Brownton is serving customers outside its municipality’s borders.]

On June 26, 2013, UNG entered into a firm transportation agreement with the City of Brownton, where Brownton pays \$0.90 per Dth for each volume transported. Pursuant to the contract Brownton is entitled to receive up to 600 Dth per day (the Maximum Daily Quantity), but no more than 60,000 Dth per year (the Maximum Annual Quantity).<sup>6</sup> If Brownton exceeds the Maximum Annual Quantity of 60,000 Dth per year, UNG doubles the existing rate to Brownton.<sup>7</sup> The transportation agreement term runs through 2022 and is subject to extensions. At the time the contract was signed, UNG did not seek Commission approval for the transportation agreement.

On April 13, 2016, UNG filed its Initial Petition seeking Commission approval of the UNG/Brownton transportation agreement. UNG stated that it was un-aware of Minn. Statute § 216B.045 requirements when the Brownton agreement was signed.

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<sup>6</sup> See UNG’s Initial Petition - Transportation Agreement, pp. 6-7, Article VII (Sections 7.1.1 and 7.3).

<sup>7</sup> The \$0.90 per Dth rate will become \$1.80 per Dth for each volume transported over the 60,000 Dth Maximum Annual Quantity.

UNG justified its intrastate pipeline status with the following:

- UNG is un-aware of any other similarly situated distribution entities that could request similar cooperative arrangement that would serve the public interest. UNG stated that it would willingly enter into negotiations with other similarly situated distribution entities to discuss similar cooperative arrangements that would serve the public interest in other respective communities, thus there was no discriminatory element to the Agreement; and
- The negotiated Agreement reflects a partnership between the entities working together to serve the public interest. The Agreement benefits Brownton and its customers, the community, and their local economy; and
- The Agreement will benefit UNG and its parent (UFC) by contributing to UNG's economic viability and its ability to serve historically underserved populations.

## Department of Commerce

### Requirements of Minnesota Statutes and Rules

The Department concluded that UNG was an intrastate pipeline subject Minnesota Statute §216B.045 where the Commission has authority to approved the UNG/Brownton Agreement.

UNG agreed in its initial petition that it was an intrastate pipeline and was subject to Minnesota Statute §216B.045. The Department stated that UNG must meet the conditions listed in Minnesota Statute §216B.045, which requires that an intrastate pipeline provide service under the following conditions:

- Contract at rates that are just and reasonable and do not unreasonably discriminate among customers receiving like or contemporaneous services (Minnesota Statute § 216B.045, subd. 2);
- Offer services by contract on an open access, nondiscriminatory basis (Minnesota Statute §216B.045, subd. 3); and
- Obtain Commission approval for each contract where service is provided as an intrastate pipeline (Minnesota Statute §216B.045, subd. 4).

### Contract at Reasonable Rates

The Department noted that most regulated utility rates are cost of service based and the reasonableness of the rate can be determined by reviewing its revenue requirement. However, reasonable rates may be negotiated as part of an arm's length transaction. In simple terms, the reasonableness of the rate could be determined because all parties involved have agreed to the negotiated rates.<sup>8</sup>

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<sup>8</sup> The Department assumed that UNG's management set a rate that is reasonably recovering the facility's costs, including the design of charging higher rates if the City's use of UNG's pipeline exceeds the level identified in the Agreement.

### Obligation to Offer Service

UNG is required to offer services on an open access, non-discriminatory basis.<sup>9</sup> UNG's petition indicated that it would be willing to enter into negotiations with other similarly situated entities to discuss similar agreements to serve other communities. The Department concluded that UNG was offering its intrastate transportation services on an open-access, non-discriminatory basis.

### Approval of the Transportation Agreement

UNG and Brownton entered into the Agreement on September 10, 2013. The Agreement stated that UNG begin providing service on August 1, 2013. UNG formally submitted the Agreement to the Commission for approval on April 13, 2016 and also asked that the Commission approve the Agreement retroactively to June 26, 2013.

UNG stated in its Initial Petition that it was unaware of Minnesota Statute §216B.045 and its requirements and that its delay in petitioning the Commission for its approval was not intentional. Further, UNG noted that the Agreement has provided benefits to both UNG and Brownton by resulting in natural gas development in the city.

The Department agreed with UNG that the introduction of natural gas service in Brownton provided societal benefits. The Department stated that if UNG provides similar future transportation services, UNG would be expected to file a more-timely petition, indicating that the proposal provides service on a non-discriminatory basis for similarly situated customers.

### **Department Recommendation**

The Department recommended the Commission approve the UNG/Brownton Transportation Agreement, where UNG provides intrastate pipeline transportation services to Brownton who provides retail distribution services.

### **PUC Staff Comment**

#### **United Natural Gas (UNG)/City of Brownton (Brownton) Firm Gas Transportation Agreement**

PUC staff reviewed UNG's petition and appreciates the Department's December 7, 2016 *Comments*. PUC staff is in agreement with the Department that the UNG/Brownton transportation agreement and resulting Brownton distribution project serves the public interest for the following reasons:

#### Arm's Length Transaction

After reviewing UNG's Petition and the Department's comments, PUC staff believes that parties have acted independently in developing the UNG/Brownton agreement, but staff cannot make this determination without receiving additional information from UNG regarding its UGS arrangement. The jointly signed UNG/Brownton Agreement could be considered proof that the

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<sup>9</sup> Minn. Stat. § 216B.045, Subd. 3.

parties have negotiated in good faith and to serve the public interest. Staff is unsure about the UNG/UGS arrangement.

### Negotiated Rates

UNG's rates reflected in the Agreement *were not* based on an underlying cost of service calculation, but have been negotiated based on an arm's length transaction with UNG for a 9-year contract term. The Department stated that it believes the rates were negotiated fairly based on the information in the record - PUC staff agrees.

### Subsequent New UNG Contracts using the Facilities

Because the Commission must approve all subsequent UNG intrastate pipeline customer agreements, PUC staff is not concerned that UGS and Brownston customers could subsidize new customers, if added.

## **United Natural Gas (UNG)/United Grain System (UGS) Arrangement**

PUC staff believes the Department's analysis may not have adequately addressed the service arrangement between UNG and UGS. The Department concluded that UNG's intrastate pipeline was not a public utility, subject to Minnesota Rules and Statutes as a regulated Local Distribution Company (LDC) that provides retail sales and transportation services. (The definition of a public utility is in Minn. Stat. § 216B.02, subd. 4. The definition of an intrastate pipeline is in Minn. Stat. § 216B.045, subd. 1.)

However, staff has the following concerns:

- UNG made certain statements in its 12-250 petition, it is unclear to staff if UNG purchases the natural gas for UGS or if UGS purchases its own natural gas supply. UNG made the following statement in its 12-250 petition:

*"UNG can purchase up to 5000 Mcf per day."*<sup>10</sup>

- Previously, UNG stated that it operated as an intrastate pipeline, subject to Minnesota Statute § 216B.045 requirements. If UNG is an intrastate pipeline, natural gas supply cannot be purchased by UNG for resale to retail customer, UGS. If UNG is purchasing natural gas for either UGS or Brownston, staff believes that this could make UNG a natural gas retailer subject to Commission regulation.<sup>11</sup> If UNG is subject to Commission regulation, it would become a "public utility." At this point, staff believes the UNG/UGS arrangement could be subject Minnesota Statute § 216B.48 – Affiliated Interest, which could require UNG to petition the Commission for its approval of an affiliated interest agreement.

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<sup>10</sup> See UNG's Initial Petition dated March 30, 2012 in Docket No. 12-250, p. 1.

<sup>11</sup> To staff knowledge, UNG does not have a Purchased Gas Adjustment (PGA) recovery mechanism for the cost of gas.



- The record in this docket does not contain an explanation of the service arrangement between UNG and UGS, who are both owned by UFC. Therefore, staff cannot determine what services are provided by UNG to UGS. The information required of UNG would be the services provided to UGS, including the rates charged, construction costs of the intrastate pipeline, the time period of the arrangement, and any other relevant terms of the arrangement. Because this information is not in the record, staff cannot compare the rates charged to UGS to the rates charged to Brownton, thus, staff cannot determine if one entity is subsidizing the other.

The Commission may wish to direct UNG to explain its arrangement with UGS during the Commission's Agenda Meeting or in a compliance filing.

## Decision Alternatives

### United Natural Gas (UNG)/City of Brownton (Brownton) Firm Gas Transportation Agreement

1. Approve the UNG/Brownton Firm Transportation Agreement retroactive to June 26, 2013. (UNG, DOC) or
2. Approve the UNG/Brownton Firm Transportation Agreement retroactive to June 26, 2013 based on the facts of UNG's and Brownton's circumstances in this docket but without setting precedent and allow future petitions to be decided on a case-by-case basis. or
3. Do not approve the UNG/Brownton Firm Transportation Agreement. or
4. Take no action.

### United Natural Gas (UNG)/United Grain System (UGS) Arrangement

5. Require UNG to provide a discussion of the services provided to UGS, such as transportation services and purchasing of gas, the construction costs of the intrastate pipeline, the rates charged to UGS, the time period associated with the UGS arrangement, and any other relevant terms of the arrangement in a compliance filing within 30 days of the Commission Order. or
6. Take no action.