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January 15, 2021

Will Seuffert
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, MN 55101

VIA ELECTRONIC FILING

Re: Additional Reply Comments of Minnesota Energy Resources Corporation

In the Matter of the Petition of Minnesota Energy Resources Corporation for Approval of the 2019 Gas Utility Infrastructure Cost (GUIC) Rider True-Up Report, 2021 GUIC Rider Revenue Requirements and Revised Surcharge Factors
Docket No. G011/M-20-405

Dear Mr. Seuffert:

Minnesota Energy Resources Corporation (“MERC” or the “Company”) submits these additional Reply Comments in response to the December 29, 2020, Additional Comments filed by the Minnesota Department of Commerce, Division of Energy Resources (the “Department”) on MERC’s Petition for Approval of 2019 Gas Utility Infrastructure Cost (“GUIC”) Rider True-Up Report, 2021 GUIC Rider Revenue Requirement, and Revised Surcharge Factors. MERC thanks the Department for its additional review and comments. As the Department summarized in its Additional Comments, many issues have been resolved between the Department and the Company. While many of the unresolved issues and recommended modifications raised in the Department’s Additional Comments were already addressed in detail in MERC’s November 19, 2020, Reply Comments (“November Reply Comments”), MERC briefly responds to the Department’s additional recommendations.

1. Accuracy of Filing and Process Improvements

With respect to the appropriate adjustment to reflect accurate total invoice costs, the Department, in its Additional Comments, accepted MERC’s recommended adjustment, which was determined based on the Company’s review of all invoices to verify project costs.¹ However, the Department continues to propose that an independent audit to examine the Company’s systems and processes used to determine GUIC costs is warranted, in addition to the Commission putting MERC on notice that future flawed filings will be rejected and may result in the suspension of GUIC rider charges.

¹ Department Additional Comments at 6.

As described in MERC's November Reply Comments, the Company has devoted significant time and resources and has established processes designed to ensure its GUIC projects and costs are accurately reported and accounted for. MERC takes the accuracy and detail of its filings very seriously and fully recognizes the need for and importance of ensuring reliable and accurate data, calculations, and reporting. The Department's assertion that the Company has attempted to divert attention from the concerns raised by the Department² is simply inaccurate. Instead, MERC's November Reply Comments outlined the numerous steps the Company has *already proactively* taken to improve its quality control and review processes to ensure that future calculations and reporting are complete and accurate.³ Given the evaluation and actions already undertaken by the Company, the Department's recommendation of an independent audit is unnecessary. Further, the cost of an independent audit would outweigh any potential benefits; an audit would not be likely to result in additional opportunities for process improvements given the steps already taken by the Company.

Further, MERC's observations regarding the significance of the identified errors holds true—the majority of the errors the Department calls out either had no impact on the revenue requirement, or the impacts are not significant. As reflected in the Company's November Reply Comments, a number of the identified errors involved the incorrect classification of projects as either right-of-way ("ROW") relocation projects or distribution integrity management program ("DIMP") obsolete materials replacement projects. However, the detail for those projects, including costs, installation material and quantity, and retirement material and quantity, were accurately represented, resulting in no impact to the overall costs or rider surcharge calculations. Additionally, the effect of correcting the identified errors with a cost impact on the requested 2021 revenue requirement is generally not significant. For example, the corrections for invoiced costs resulted in an overall reduction to 2019 plant of \$16,703.66, which results in a reduction to MERC's 2021 revenue requirement of \$1,075 or 0.015 percent of the Company's proposed 2021 GUIC Rider revenue requirement. The correction related to accumulated deferred income tax ("ADIT") proration true-up results in an increase to the 2021 revenue requirement of \$488. Further details regarding the revenue requirement impacts were discussed in the Company's November Reply Comments.

² Department Additional Comments at 4.

³ MERC November Reply Comments at 3. These include improvements to the Company's rider model files to ensure correct accumulated deferred income tax proration calculations and to help avoid the possibility of formula errors as the result of future updates; a review process to ensure the accurate classification of eligible GUIC projects; implementation of a process to ensure retirement quantities are accurately recorded in the field during project construction; additional training for field personnel to ensure complete and accurate tracking of project details; and additional quality control and review of service line project contractor invoiced costs to ensure all invoiced costs are reviewed and accurately reported in future true-up filings.

2. Department Recommended Disallowances

In its Additional Comments, the Department identifies seven remaining disputed adjustments, which the Department is recommending be made to MERC's 2019 GUIC true-up and 2021 GUIC Rider costs.⁴ While MERC addressed each of these items in detail in its November Reply Comments, the Company briefly responds to the new arguments and issues raised in the Department's Additional Comments.

a. Meter-Related Costs

In its November Reply Comments, MERC clarified the scope of meter-related costs included for recovery through the Company's GUIC Rider, stating that "MERC has not included the costs for any new meters in the GUIC Rider."⁵ MERC also provided support for the meter-related costs that are included for recovery as appropriate GUIC-eligible costs related to ROW and obsolete materials replacement projects.

MERC continues to advocate that all of these costs are appropriately included as part of the GUIC service-line replacement projects and no adjustment to remove such costs is warranted. The Department, in contrast, proposes extrapolated adjustments to remove costs related to new meter installations, seemingly on the basis that such costs constitute a betterment.⁶

MERC disagrees that such an adjustment is reasonable or appropriate, given that these costs are appropriate and legitimate GUIC-eligible costs related to ROW and obsolete materials replacement projects. Without having undertaken the ROW relocation or obsolete materials replacement project, no meter-related work would have been performed. The costs proposed for recovery in the Company's GUIC Rider include:

- labor costs to verify meter delivery pressure after installation of the new service line;
- costs to tag a meter to depict if an excess flow valve has been installed on the service line or to designate if a service has been abandoned;
- connection of the new service line to the meter assembly;
- replacement of the meter bar and regulator, if required; and
- the material cost for a sleeve to protect the service riser from corrosion and other damage.

⁴ Department Additional Comments at 8-9.

⁵ MERC November Reply Comments at 12.

⁶ See Department October 26, 2020 Comments at 23 (noting that "[i]n this section of the comments [regarding meter-related costs], we discuss the issue of 'betterment.'").

The included costs are necessary to ensure the meter sets along replacement projects are safe and in compliance with all current regulations and do not constitute a betterment for which GUIC recovery is not allowed.

b. Internal Capitalized Costs

In its Additional Comments, the Department continues to recommend the disallowance of internal capitalized costs on the premise that recovery of internal costs through a rider mechanism may result in double recovery.⁷ In its November Reply Comments, MERC justified why recovery of the proposed internal capital costs would not result in double recovery.⁸ The Department, however, appears to disregard the Company's explanation, instead disagreeing only with MERC's argument that inclusion of these costs is consistent with the Commission's determination in MERC's initial GUIC docket (Docket No. G011/M-18-281).⁹

As explained in MERC's November Reply Comments, the internal costs at issue are incremental costs, as they reflect costs to be incurred for projects, like the DIMP and ROW projects included in the GUIC Rider, that are not currently included in the Company's base rates. While the Department continues to argue that the Commission has "repeatedly and appropriately disallowed the inclusion of internal capitalized costs in rider rate filings,"¹⁰ a proposition that the Company did not disagree with in its Reply Comments,¹¹ the Department fails to recognize the distinguishing circumstances of the internal costs MERC proposes for inclusion in the GUIC Rider, namely that the majority of MERC engineering internal labor costs have historically been capitalized and not included as operations and maintenance ("O&M") expense in base rates. As a result, the Department's concern that "a utility could expense its employee internal labor in a rate case and then later capitalize that same labor in a rider, thus charging ratepayers for those same internal labor costs twice,"¹² is not applicable here.

Further, MERC has excluded all O&M expense associated with internal labor, which ensures the Company will not double recover its O&M costs through both base rates and the GUIC Rider.¹³

⁷ Department Additional Comments at 4-5.

⁸ MERC November Reply Comments at 3-5.

⁹ See Department Additional Comments at 4-5.

¹⁰ Department Additional Comments at 4.

¹¹ MERC November Reply Comments at 4.

¹² Department Comments at 15.

¹³ The Company has only proposed to include third-party contractor incremental O&M expense associated with four unique relocation projects in its 2019 true-up. The Department also continues to recommend disallowance of recovery of the incremental O&M associated with third-party contractor costs for relocations for which no new facilities were installed. MERC responded to this recommendation and provided further support for its proposal in its November Reply Comments. See MERC November Reply Comments at 6-7.

For the reasons discussed in the Company's November Reply Comments, MERC continues to support recovery of the internal costs included in the 2019 GUIC true-up and in the 2021 GUIC Rider.

c. Regulatory Legal Costs

The Department objects to MERC's proposed recovery of actual incremental legal regulatory expense incurred in 2019 related to the Company's GUIC rider, arguing that "a representative recovery amount for outside legal services is built into base rates," and "MERC had ample time to consider and incorporate [GUIC Rider] legal and regulatory costs into base rates if the Company believed they would be unusual or extraordinary."¹⁴

The fact that MERC theoretically could have proposed a known and measurable adjustment to its O&M expense in its last rate case based on plans to file a future GUIC Rider is irrelevant since the Company did not include such an adjustment. Instead, as discussed in MERC's November Reply Comments, MERC's current base rates were set, as proposed by the Department, based on actual 2017 O&M expense. MERC did not have a GUIC Rider, nor any other rider in 2017, so none of the GUIC-related legal regulatory costs proposed to be recovered are included in current base rates.

While the Department correctly notes that expense related to the regulatory work undertaken in 2017 is included in base rates, such base rate recovery does not reflect the incremental GUIC-related legal regulatory costs incurred and now proposed for recovery for 2019. The complexity of GUIC Rider proceedings has been significant relative to other regulatory filings.¹⁵ The regulatory expense associated with filing and obtaining approval for MERC's GUIC Rider cost recovery has allowed the Company to implement multi-year pipeline safety and assessment programs that are comprehensive and cost-effective, rather than undertaking work in a reactionary or immediate threat mode, thus providing substantial cost-savings benefits to MERC's customers beyond increased safety and reliability. Based on these considerations, MERC continues to request approval to recover these incremental costs in its 2019 GUIC true-up, with future actual costs to be recovered in future true-up filings.

d. Betterment

In its Additional Comments, the Department continues to recommend a reduction to MERC's 2019 and 2021 GUIC revenue requirements based on a Rochester ROW relocation project, which the Department asserts constitutes a betterment, based on its judgment that "the growth in the Rochester area *may have been* a factor in the selection of a 6-inch pipe."¹⁶

¹⁴ Department Additional Comments at 2.

¹⁵ In this docket, for example, the Department has issued approximate 50 discovery requests, many with multiple component parts, as well as multiple rounds of comments.

¹⁶ Department Additional Comments at 6 (emphasis added).

The Department alleges that the Company's decision to install 6-inch main resulted in a 300 percent increase in capacity.¹⁷

The Department's conclusion, however, is contrary to the facts in the record in this proceeding. As stated explicitly in the Company's November Reply Comments, "MERC designed the replacement project to use the smallest pipe diameter consistent with prudent engineering practices and standards to safely and reliably serve *existing* customers and demand."¹⁸ MERC also fully justified why replacement of the 3-inch pipe with 4-inch pipe would not have served the existing demand, explaining that "the larger diameter pipe was the result of the overall project design based on the Company's distribution system in this area, is the smallest pipe diameter consistent with prudent engineering practices, *and does not result in increased system capacity or make other system improvements.*"¹⁹

The flow modeling the Company undertook in design of the Rochester ROW project at issue fully supports the conclusion that installation of 6-inch pipe for this replacement was necessary to serve the existing load and that installation of 4-inch pipe instead would not have been adequate to meet that existing demand. MERC's modeling and analysis appropriately reflects the interconnected nature of the Company's distribution system, in contrast to the Department's overly-simplified focus on a single segment of main.

Based on the record, MERC has demonstrated that the identified project does not constitute a betterment under the GUIC statute and prior Commission decisions interpreting that statute.

e. Geographic Information System ("GIS") Service Line Mapping Project

Finally, the Department continues to recommend that MERC's proposed 2021 GIS Service Line Mapping Project spending be reduced by \$178,563, the amount authorized for recovery in MERC's current base rates for the compilation of paper main and service line documentation and information, and scanning paper documentation into a comprehensive database (the "Documentation Project"). The rationale for this recommendation is not clear, given the fact that the scope of these projects are independent and that both projects are planned to be worked on in 2021.²⁰

The proposed \$1 million in O&M expense for the GIS Service Line Mapping Project is separate from and in addition to the authorized expense that continues to be incurred for completion of the Documentation Project. Both of these projects allow MERC to more accurately document and access its system design, material characteristics, operating

¹⁷ Department Additional Comments at 6.

¹⁸ MERC November Reply Comments at 11 (emphasis added).

¹⁹ MERC November Reply Comments at 11 (emphasis added).

²⁰ It is unclear from the Department's comments whether the Department is suggesting that MERC utilize a portion of the \$1 million proposed for 2021 to begin the GIS Service Line Mapping to instead complete the Documentation Project.

conditions and environment, and maintenance and operating history, in accordance with the Pipeline and Hazardous Materials Safety Administration's Integrity Management Program for Gas Distribution Pipelines Rule (49 C.F.R. Part 192, Subpart P), and work on both projects is proposed in 2021. Finally, in order to ensure ratepayers are protected from any possible double recovery, MERC committed, in its November Reply Comments, to account for any underspending on the Documentation Project in 2021 as an offset to actual GUIC GIS Service Line Mapping Project costs in the Company's 2021 true-up to be filed in 2022.

3. Magnitude and Timing of Future GUIC Recoveries

Finally, the Department continues to recommend that the Commission consider a measurable rider-recovery limit as a "public interest safeguard."²¹ The Department also continues to raise questions as to whether the Company has adequately satisfied the GUIC statute's requirement that the utility report "the magnitude and timing of any known future gas utility projects that the utility may seek to recover under this section."²²

With respect to the application of a cap on GUIC recoveries, as MERC illustrated in its November Reply Comments, the Company's forecasted GUIC spending is decreasing in 2021 rather than increasing as the Department suggests.²³ Given the importance and necessity of the gas utility infrastructure projects being undertaken, capping recovery for such projects is not reasonable or appropriate at this time.

Regarding compliance with the GUIC statute filing requirement to address the magnitude and timing of any known future gas utility projects, the Department appears to ignore the Company's extensive response in its November Reply Comments.²⁴ Contrary to the Department's claim that MERC merely references a recap of its 2021 projections,²⁵ MERC

²¹ Department Additional Comments at 8.

²² Minn. Stat. § 216B.1635, subd. 4(2)(vi).

²³ MERC November Reply Comments at 17-18 and Table 3 (showing total capital and O&M expenditures in 2021 of \$14.186 million as compared to \$16.495 million in 2020 and \$15.3 million in 2019).

²⁴ See MERC November Reply Comments at 17-20. As discussed in the Company's November Reply Comments, the proposed Farm Tap Project is the one new project MERC identified in Exhibit H to the Company's GUIC Rider petition as a potential future gas utility project. MERC referred the Department to the detailed data and analysis that has been provided and evaluated in that proceeding in response to its request for additional quantification of potential future GUIC Rider cost impacts. See *In the Matter of the Petition of Minn. Energy Res. Corp. for Approval of Farm Tap Customer-Owned Fuel Line Replacement Plan, Tariff Amendments, and Deferred Accounting*, Docket No. G011/M-17-409, DEPARTMENT COMMENTS at 23-25 (Sept. 14, 2020) (providing analysis of the cost and rate impacts of full replacement and replacement within one mile of the Company's system, assuming recovery through the GUIC Rider, based on data and analysis provided in response to discovery).

²⁵ Department Additional Comments at 8.

has provided a discussion of both the magnitude and timing of known future gas utility projects the Company intends to potentially seek recovery of through the GUIC Rider.

As explained in the Company's November Reply Comments, MERC's DIMP projects will necessarily be a multi-year effort and the pace of the work completed can be controlled while balancing the need to mitigate known risks on the distribution system with the associate rate impacts. MERC also included discussion and references to the various alternatives under consideration with respect to its Farm Tap Replacement Project and considerations that are likely to impact the level of ROW relocation spending in the near term, noting that, ultimately, the Company does not receive advanced notice regarding ROW relocation projects and therefore is not able to provide precise forecasts for future costs. The Commission has consistently approved MERC's forecasted ROW costs based on historical ROW project spending, recognizing that the Company is not informed of future ROW relocation work with enough lead time to include specific projects in its forecasts and that actual costs can appropriately be accounted for through the true-up mechanism.²⁶

MERC fully recognizes the need to ensure that rates continue to be reasonable, and has and will continue to undertake efforts to mitigate the magnitude and timing of its investments in order to help smooth customer rate impacts. Continuation of GUIC Rider recovery is critical, however, to allow MERC to implement multi-year pipeline safety and assessment programs and to ensure the continued safety and reliability of its natural gas system.

CONCLUSION

MERC respectfully requests that the Commission approve its 2021 GUIC revenue requirement inclusive of 2019 true-up of \$6,965,675 to be recovered through GUIC surcharge rates based on the Company's proposed rate design, effective following Commission approval and to continue until the Commission either authorizes new GUIC rider rates or implementation of interim rates in a future MERC rate case proceeding.

Please contact me at (414) 221-4208 if you have any questions regarding the information in this filing. Thank you for your attention to this matter.

²⁶ *In the Matter of Minn. Energy Res. Corp.'s Request for Approval of a Gas Util. Infrastructure Cost Rider*, Docket No. G011/M-18-281, ORDER APPROVING GAS UTILITY INFRASTRUCTURE COST RIDER WITH MODIFICATIONS AND REQUIRING COMPLIANCE FILING at 6-7 (Feb. 5, 2019).

Mr. Will Seuffert
January 15, 2021
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Sincerely,

A handwritten signature in black ink that reads "Joylyn C. Hoffman Malueg". The signature is written in a cursive style with a large, stylized initial "J".

Joylyn Hoffman Malueg
Project Specialist 3
Minnesota Energy Resources Corporation

cc: Service List

Petition of Minnesota Energy Resources
Corporation for Approval of the 2019 Gas
Utility Infrastructure Cost (GUIC) Rider True-Up
Report, 2021 GUIC Rider Revenue Requirements
and Revised Surcharge Factors

Docket No. G011/M-20-405

CERTIFICATE OF SERVICE

I, Colleen T. Sipiorski, hereby certify that on the 15th day of January, 2021, on behalf of Minnesota Energy Resources Corporation (MERC), I electronically filed a true and correct copy of the enclosed Reply Comments on www.edockets.state.mn.us. Said documents were also served via U.S. mail and electronic service as designated on the attached service list.

Dated this 15th day of January, 2021.

/s/ Colleen T. Sipiorski

Colleen T. Sipiorski

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