

m MINNESOTA
PUBLIC UTILITIES COMMISSION

January 15, 2020

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Subject: Triennial Report on the Recovery Costs for Natural Gas Extension Projects under Minn. Stat. § 216B.1638, subdivision 6


Dear Senators and Representatives:

Minn. Stat. § 216B.1638, subdivision 6 requires the Minnesota Public Utilities Commission to report triennially to the Minnesota Legislature on the recovery costs for projects to extend the provision of natural gas services.

The Commission has enclosed its report to fulfill the reporting requirement for this triennium.

Please let me know if I can provide further assistance.

Sincerely,



Ryan Barlow
Acting Executive Secretary

Equal Opportunity Employer



**Triennial Report on the
Recovery of Costs for
Natural Gas Extension Projects under
Minnesota Statutes, Section, 216B.1638**

January 15, 2020

Required General Legislative Report Information

Minnesota Public Utilities Commission
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Minnesota Statutes (2018), Section 216B.1638, subd. 6 requires the Minnesota Public Utilities Commission (Commission) to evaluate and report, beginning January 15, 2017 and every three years thereafter, to the Minnesota Legislature concerning the recovery of costs for projects to extend the provision of natural gas services.

This Report is to fulfill the reporting requirement of this section.

Pursuant to Minnesota Statutes, Section 3.197, the Minnesota Public Utilities Commission estimated costs for preparing this Report are minimal as most if the information is developed in the normal course of business. Special funding was not appropriated for the costs of preparing this report.

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Description of 20015 Legislation

Minnesota Statutes, Section 216B.1638 was enacted in 2015. This section of law allows a utility to petition the Commission for a rider to recover, outside of a general rate case, the revenue deficiency from a natural gas extension project. The statutory section sets forth the information that must be contained in such a petition and establishes the scope and standards for review of the petition by the Commission. Among other requirements for Commission approval, such a rider must not be allowed to recover more than 33 percent of the costs of the natural gas extension project.

Even if the Commission approves such a petition, the utility is not committed to implement a project so approved. The public utility seeking to provide natural gas service must notify the Commission whether it intends to proceed with the project as approved.

Subdivision 6 of this statutory section requires the Commission, beginning January 15, 2017 and every three years thereafter, to report to the Legislature on the following:

1. the number of public utilities and projects proposed and approved under this section;
2. the total cost of each project;
3. rate impacts of the cost recovery mechanism; and
4. an assessment of the effectiveness of the cost recovery mechanism in realizing increased natural gas service to unserved or inadequately served areas from natural gas extension projects.¹

BACKGROUND: RELATED COMMISSION ACTIVITY ENCOURAGING EXPANDED AVAILABILITY OF NATURAL GAS SERVICE

Commission-Authorized New Area Surcharge (NAS) Projects

In 1990, the Commission initiated an investigation and, in 1991, a study group² that asked, among other questions, whether the Commission should encourage the use of natural gas fuel by facilitating the provision of pipelines to more towns. The study group explored how to extend gas service to communities that request gas service but cannot be served economically at tariffed rates.

On March 12, 1992, the Department of Commerce, Division of Energy Resources (Department) and Commission staff submitted their Report on Issues for New-Area Rates. The report covered

¹ Minn. Stat. § 216B.1638. subd. 6.

²ORDER INITIATING STUDY GROUP, In the Matter of an Inquiry into Competition Between Gas Utilities in Minnesota, Docket No. G-999/CI-90-563 (June 4, 1991).

financial issues, rate design and various compliance and reporting issues concerning these new rates. Extensions under these New Area Surcharge tariffs would involve significant costs since the extensions would be to entire towns located in remote areas. Because the proposed surcharges would allow customers to pay the full incremental cost over a number of years (rather than one year), utilities could serve more areas without putting existing customers or stockholders at risk.

Subsequently, the Commission received, reviewed, and approved several New Area Rates proposals. Because these New Area Rates proposals were approved, the Commission decided this issue had been adequately addressed given conditions at that time.³

CenterPoint Energy Resources Corp., d/b/a CenterPoint Energy Minnesota Gas (CenterPoint Energy) completed one large scale project in the 1990s under this tariff in the Alexandria lakes area. Northern States Power Company d/b/a Xcel Energy (Xcel Energy) completed approximately four projects in the 1990s under this tariff. The largest of the four was the Brainerd lakes area project; however, Xcel Energy completed several other smaller projects, for example, in Taylor Falls.

The following table provides a list of residential New Area Surcharge projects approved more recently by the Commission for various communities in Minnesota where natural gas service was not previously available.

Table 1: Recently Approved New Area Surcharge Projects

Utility	Location	Docket No.
Minnesota Energy Resources Corp.	Detroit Lake – Long Lake	G-011/M-15-441
Minnesota Energy Resources Corp.	Ely Lake	G-011/M-15-776
Minnesota Energy Resources Corp.	Fayal Township – Long Lake	G-011/M-16-221
Minnesota Energy Resources Corp.	Balaton	G-011/M-16-654
Minnesota Energy Resources Corp.	Esko	G-011/M-16-655
Minnesota Energy Resources Corp.	Detroit Lake Expansion	G-011/M-17-210
Minnesota Energy Resources Corp.	Ely Lake Expansion	G-011/M-17-211
Minnesota Energy Resources Corp.	Fayal Township Expansion	G-011/M-17-212
Minnesota Energy Resources Corp.	Pengilly	G-011/M-18-460
Xcel Energy - Gas	Barnesville	G-002/M-14-583
Xcel Energy - Gas	Holdingsford	G-002/M-14-583
Xcel Energy - Gas	Pillager	G-002/M-14-583
Xcel Energy - Gas	Barnesville Expansion	G-002/M-15-195
Xcel Energy - Gas	Ulen - Hitterdal	G-002/M-16-40

³ ORDER TERMINATING INVESTIGATION AND CLOSING DOCKET, In the Matter of an Inquiry into Competition Between Gas Utilities in Minnesota, Docket No. G-999/CI-90-563 (March 31, 1995).

Recent Commission-Authorized Exempt Small Gas Utilities

In addition to the five large investor-owned local distribution companies and the municipally-owned distribution companies that serve customers in Minnesota, there are several small natural gas distribution utilities that are exempt from certain aspects of state rate regulation, pursuant to Minn. Stat. § 216B.16, subd. 12.

Small exempt natural gas distribution utilities typically charge higher rates than the larger, state regulated distribution utilities for reasons that are due mainly to their size, but they are providing service to communities that previously did not have access to natural gas.

Over the past several years, the Commission has confirmed, by Order, the exempt status of several of these new, small natural gas utilities that serve customers in previously unserved areas. Several of these projects have required construction of small, intrastate pipelines that provide wholesale natural gas transportation service to the exempt distribution utilities. The rates charged by the intrastate pipelines are set under contracts approved by the Commission, pursuant to Minn. Stat. § 216B.045, subd. 4.

Table 2: Recently Approved Exempt Small Gas Utilities

Company Name	Docket No.	Commission Order Date
Dooley's Natural Gas LLC	G-6915/M-13-672	January 7, 2014
Community Co-ops of Lake Park	G-6956/M-15-856	December 22, 2015
United Natural Gas, LLC	G-6960/M-16-214	May 24, 2016
Dooley's Natural Gas II, LLC	G-6915/M-16-756	July 5, 2017
Lake Region Energy Services, Inc.	G-6977/M-17-186	July 28, 2017

COMMISSION ACTIONS UNDER 2015 LEGISLATION

Minnesota Energy Resources Corporation (MERC) has proposed four projects (Balaton, Esko, Pengilly, and Rochester) under Minnesota Statutes, Section 216B.1638. For three of the proposed projects (Balaton, Esko, and Pengilly), MERC agreed to recover a large portion of project costs through the NAS Rider from project customers, while the remaining costs were deferred to be recovered through base rates in future rate cases, rather than through the Natural Gas Extension Project (NGEP).⁴ The Rochester proposal was approved by the Commission as a Natural Gas Extension Project and is discussed below.

⁴ ORDER APPROVING COST RECOVERY FOR NEW AREA SURCHARGE TARIFFS FOR BALATON AND ESKO PROJECTS, In the Matter of the Petition of Minnesota Energy Resources Corporation for Approval for Recovery of Natural Gas Extension Project Costs through a Rider and for Approval of a New Area Surcharge for the Balaton Project, Docket No. G-011/M-16-654, and In the Matter of the Petition of Minnesota Energy Resources Corporation for Approval for Recovery of Natural Gas Extension Project Costs through a Rider and for approval of a New Area Surcharge for the Esko Project, Docket No. G-011/M-16-655 (February 9, 2017); and ORDER APPROVING NEW-AREA SURCHARGE AND AUTHORIZING DEFERRED ACCOUNTING FOR CERTAIN COSTS, In the Matter of Minnesota Energy Resources

Rochester Natural Gas Extension Project

Initial Request

MERC requested authorization to recover a portion of its Rochester Natural Gas Expansion Project (the Project) costs under this statute. According to MERC, its natural gas distribution system was at capacity in the Rochester area and must be upgraded to meet current needs as well as expected growth in customer demand. The Project includes two phases, which involve improvements to MERC's distribution system and acquiring additional interstate pipeline capacity for delivery to its Rochester distribution system.

Phase I of the Project was completed in 2015. Phase I cost approximately \$5.6 million, and involved improvements to MERC's delivery system in the Rochester area. The Commission authorized recovery of the Phase I costs in MERC's 2015 rate case.⁵

Phase II of the Project consists of changes to MERC's local distribution system, which are expected to be completed by 2023. This second phase of the project involves upgrading MERC's town border station (TBS) system and constructing a new 13-mile long high-pressure pipeline that will tie together the northern and southern portions of the TBS system. MERC requested approval of the Phase II costs, which are estimated to total about \$44 million. MERC seeks to recover 33 percent of the Phase II costs from all of MERC's ratepayers using its NGEP rider, and to recover the remaining balance of Phase II costs in future rate cases. On May 5, 2017, the Commission issued an Order approving the Rochester project, granting MERC's request for preapproval to recover Phase II costs of up \$44 million through a combination of the NGEP Rider and base rates.⁶

In addition, MERC contracted with its wholesale natural gas supplier, Northern Natural Gas Company (NNG), the interstate natural gas pipeline, to build new interstate pipeline infrastructure that will supply MERC with increased interstate pipeline capacity. MERC requested Commission approval of the NNG costs, which MERC stated would total approximately \$55 million on a net present value (NPV) basis. MERC has proposed to recover these NNG costs through MERC's Purchased Gas Adjustment (PGA) mechanism.⁷ On May 5, 2017, the Commission granted MERC's request for preapproval to recover these additional

Corporation's Petition for Approval of a New Area Surcharge and Natural Gas Extension Project Rider for the Pengilly Project, Docket No. G-011/M-18-460 (March 29, 2019).

⁵ FINDINGS OF FACT, CONCLUSIONS, AND ORDER, In the Matter of the Application of Minnesota Energy Resources Corporation for Authority to Increase Rates for Natural Gas Service in Minnesota, Docket No. G-011/GR-15-736 (October 31, 2016).

⁶ ORDER APPROVING ROCHESTER PROJECT AND GRANTING RIDER RECOVERY WITH CONDITIONS, In the Matter of a Petition by Minnesota Energy Resources Corporation for Evaluation and Approval of Rider Recovery for its Rochester Natural Gas Extension Project, Docket No. G-011/M-15-895, at 18 (May 5, 2017).

⁷ Adapted from the Administrative Law Judge's FINDINGS OF FACT, CONCLUSIONS OF LAW AND RECOMMENDATION, In the Matter of a Petition by Minnesota Energy Resources Corporation for Evaluation and Approval of Rider Recovery for its Rochester Natural Gas Extension Project, PUC Docket No. G-011/M-15-895, OAH Docket No. 68-2500-33191, at 3-4 (November 30, 2016)

interstate natural gas pipeline capacity (transportation) costs through MERC's purchased gas adjustment (PGA) mechanism.⁸

In MERC's most recent rate case, in Docket G-011/GR-17-563, MERC and the Department agreed, and the Commission authorized MERC to include \$19.4 million of Rochester Phase II capital costs in base rates. The remaining Phase II Rochester costs of \$24.58 million are expected to be incurred from 2019 through 2023.

Cost Recovery Request for 2019

On February 28, 2018, MERC requested cost recovery for a forecasted 2019 revenue deficiency of approximately \$1.3 million, subject to true-up. MERC also proposed a 2019 NGEP rider surcharge of \$0.00150 per therm applicable to all customer classes to be effective January 1, 2019.

On June 18, 2019, the Commission approved MERC's petition for a NGEP rider surcharge, allowing the Company to recover a forecasted 2019 revenue deficiency of approximately \$439,955, subject to true up, using a rider surcharge factor of \$0.00050 per therm applicable to all customers. The Commission interpreted Minn. Stat. § 216B.1638 to find that the limitation on recovery of NGEP costs in Subdivision 3(c) of the statute allows MERC to recover no more than 33 percent of the annual costs of an NGEP in any given year.⁹ This interpretation applies the 33 percent limit on annual project costs¹⁰ to the annual incremental revenue requirement as opposed to applying the 33 percent limit to the total, lifetime project costs up front, which the Commission found to be reasonable, and to result in more just and reasonable rates for ratepayers.

Request to Suspend Surcharge for Direct Connect Customers

On June 28, 2019, MERC reported that certain large customers on its system (MERC's Direct Connect Customers) have demonstrated the ability and intent to bypass MERC and instead contract directly with the interstate pipeline to acquire natural gas. To make MERC's service more attractive to these customers, MERC asked the Commission to suspend the collection of two surcharges from these customers, and to refund the surcharge amounts already collected from these customers. Specifically, MERC proposed to suspend and refund collections of:

⁸ORDER APPROVING ROCHESTER PROJECT AND GRANTING RIDER RECOVERY WITH CONDITIONS, In the Matter of a Petition by Minnesota Energy Resources Corporation for Evaluation and Approval of Rider Recovery for its Rochester Natural Gas Extension Project, Docket No. G-011/M-15-895, at 18 (May 5, 2017)

⁹ ORDER APPROVING NGEP RIDER SURCHARGE WITH MODIFICATIONS, In the Matter of the Petition of Minnesota Energy Resources Corporation for Approval of a Natural Gas Extension Project (NGEP) Cost Rider Surcharge for the Recovery of 2019 Rochester Project Costs, Docket No. G-011/M-18-182 (June 18, 2019).

¹⁰ The NGEP statute does not specifically define "costs" for purposes of recovery.

- MERC’s Gas Utility Infrastructure Cost (GUIC) Rider, and
- MERC’s Natural Gas Extension Project (NGEP) Cost Rider.

The Commission concurred with parties that MERC’s Direct Connect Customers can credibly threaten to bypass MERC’s system, and the combined effects of the GUIC and NGEP surcharges were sufficient to potentially motivate a Direct Connect customer to bypass MERC’s system.

Ultimately, however, the Commission granted MERC’s request to suspend the GUIC Rider surcharge for Direct Connect Customers but determined that because the NGEP statute requires all customers to be charged the NGEP surcharge, the NGEP Rider surcharge would not be suspended.¹¹

Cost Recovery Request for 2020

On September 30, 2019, MERC submitted its request for \$796,167 of costs to be recovered through its NGEP Rider for a 2020 revenue deficiency of approximately \$2.4 million based on projected 2020 investments related to the Rochester project.¹² Comments on MERC’s request are expected in early 2020. A Commission meeting on this matter will occur later in 2020.

NEW PROJECTS PENDING COMMISSION APPROVAL UNDER 2015 LEGISLATION

To date, only one public utility other than MERC has requested authorization to recover costs associated with natural gas extension projects under Section 1638 of Minn. Stat., Ch. 216B. On December 31, 2019, CenterPoint Energy Resources Corp., d/b/a CenterPoint Energy Minnesota Gas (CenterPoint Energy) submitted its request for authority to recover costs for a project in the community of Nowthen in Anoka County, Minnesota.¹³ CenterPoint Energy asked to recover costs for this project either in its next rate case or through an NGEP Rider and to establish a 16-year New Area Surcharge to finance the remainder of the project costs.

¹¹ ORDER SUSPENDING GUIC RIDER SURCHARGE FOR DIRECT CONNECT CUSTOMERS, AND DECLINING TO REOPEN NGEP COST RIDER; In the Matter of the Petition of Minnesota Energy Resources Corporation for Approval of a Natural Gas Extension Project (NGEP) Cost Rider Surcharge for the Recovery of 2019 Rochester Project Costs, Docket No. G-011/M-18-182; In the Matter of Minnesota Energy Resources Corporation’s Request for Approval of a Gas Utility Infrastructure Cost (GUIC) Rider, Docket No. G-011/M-18-281; In the Matter of the Petition of Minnesota Energy Resources Corporation for Approval of 2020 Gas Utility Infrastructure Cost (GUIC) Rider Revenue Requirement and Revised Surcharge Factor, Docket No. G-011/M-19-282; and In the Matter of the Application of Minnesota Energy Resources Corporation for Authority to Increase Rates for Natural Gas Service in Minnesota, Docket No. G-011/GR-17-563; at 7 (August 26, 2019).

¹² Docket No. G-011/M-19-608.

¹³ In the Matter of the Petition by CenterPoint Energy for Approval of Recovery of Natural Gas Extension Project Costs through a Rider or in the Alternative for Regulatory Asset Treatment and for Approval of a New Area Surcharge for the Nowthen Project, Docket No. G-008/M-19-840.