The Commission met on **Thursday, May 24, 2012,** with Acting Chair Reha and Commissioners Boyd and Wergin present.

The following matters were taken up by the Commission:

ENERGY AGENDA

G-007, 011/GR-10-977
In the Matter of the Application of Minnesota Energy Resources Corporation for Authority to Increase Rates for Natural Gas Service in Minnesota

First Block Motion

Commissioner Wergin moved to take the actions set forth below:

1. ***ALJ's Report* –** Adopt the ALJ's Report and recommendation with modification or clarification to one or more of the following issues. (MERC, DOC, OAG,IWLA/MCEA)

2. ***Sales Forecast* –** Determine that the appropriate sales forecast to use is MERC's initial sales forecast, corrected only as needed to resolve any errors discovered in the audit in favor of ratepayers. If no such errors are found, then MERC's initial sales forecast will be used. Clarify ALJ Proposed Findings 141 and 454 to reflect this determination.

    141. The Administrative Law Judge concludes that MERC's initial sales forecast, adjusted if needed to resolve any errors stemming from the audit in favor of ratepayers, is reasonable and recommends that the Commission use MERC's initial sales Page 2 of 23 forecast, adjusted if needed, for setting rates in this proceeding, noting that it will result in a revenue requirement nearly $1.9 million lower than MERC's revised sales forecast.

    454. MERC has agreed to, and is currently in the process of conducting a full billing system audit. The data existing after this full audit can be used to calculate MERC's RDM, ~~whether the Commission approves~~ based on any corrections from this audit to MERC's original forecast or the later one.

3. ***Vertex/Billing System Audit* –** Adopt the ALJ's findings in paragraphs 134, 135 and 140 Recommendation. [ALJ]

    Paragraph 134 – MERC has agreed to conduct a complete audit of its billing system, as proposed by the Department and the OAG. MERC, the Department, and the OAG have agreed that the parties will reach mutual agreement on the use of an external auditor and the scope of the audit on MERC's billing systems. MERC has agreed that if the audit identifies any understatement of the sales and

> customer counts, the record should be reopened to make any necessary modifications to the final rates in this proceeding.
>
> Paragraph 135 – If significant issues with MERC's data are uncovered during the audit that would result in lower rates for MERC's ratepayers, the Department recommends that the Commission reserve the right to revisit the rates set in this proceeding.
>
> Paragraph 140 – Since MERC has agreed to the proposed billing audit, including the rate revision provision, the data issues identified by the Department and the OAG have been addressed.

The motion passed 3-0.

Revenue Decoupling Motions

Commissioner Wergin moved to deny MERC's request for a full revenue decoupling pilot program.

The motion failed 2-1. Acting Chair Reha and Commissioner Boyd voted no.

Commissioner Boyd moved to take the actions set forth below:

Approve MERC's request for a full revenue decoupling pilot program in the form recommended by the Administrative Law Judge but with the following modifications or conditions:

1. Require MERC to file annual reports to the Commission that specify the Revenue Decoupling Mechanism (RDM) adjustment to be applied to each rate class for the billing period and demonstrate annual progress toward achieving the 1.5% energy efficiency goal set forth in Minn. Stat. § 216B.241.

2. Condition approval of MERC's pilot program subject to MERC stating in its RDM tariff that the Commission has the authority to modify or suspend the rates in this pilot program if warranted by unexpected circumstances. (DOC)

3. Require MERC to use the same billing determinants (customer counts, etc.) used to set final rates to determine the RDM baseline. [MERC, DOC]

4. Clarify that the appropriate sales forecast to use for setting final rates and for decoupling purposes (i.e., in the RDM) is MERC's initial sales forecast, corrected only as needed to resolve any errors discovered in the Vertex billing audit in favor of ratepayers. If no such errors are found, then MERC's initial sales forecast shall be used. [DOC]

5. Clarify that the decoupling pilot program may take effect with the implementation of new rates in this proceeding. [MERC]

6. Clarify that the decoupling program may remain in effect for no more than three years (i.e., thirty-six months), without extension. [PUC Staff]

7. Require MERC, in its thirty-day rate case compliance program, to submit a proposal for implementing its RDM mechanism mid-year, including prorated RDM baseline calculations for the part of the year MERC expects the RDM to be in place at the beginning of the program and at the end of the program. [PUC Staff]

8. Require MERC to submit revised revenue decoupling tariff language that incorporates all of the Commission's decisions in this docket in its thirty-day compliance filing in this rate case. [PUC Staff]

9. Require MERC to explain its revenue decoupling program in its notice to customers about final rates at the end of this case and in another notice when the first annual revenue decoupling rate adjustment is implemented on customer bills. [PUC Staff]

The motion passed 2-1. Commissioner Wergin voted no.

Second Block Motion

Commissioner Wergin moved to take the actions set forth below:

1. ***Residential Customer Charge –*** Adopt the recommendation of the Administrative Law Judge and increase the residential customer charge to $8.50. (MERC, DOC, ALJ)

2. ***Small C&I Customer Charge –*** Adopt the recommendation of the Administrative Law Judge and increase the small commercial and industrial customer charge to $14.50. (MERC, DOC, ALJ)

3. ***Capital Structure –*** Use the Company's proposed capital structure comprised of 50.48% common equity, 44.60% long-term debt, and 4.93% short-term debt. (Recommended by the ALJ and the Department.)

4. ***Cost of Long-Term Debt –*** Adopt a cost of long-term debt of 6.55 percent as proposed by the Company and supported by the Department and the ALJ.

5. ***Cost of Short-Term Debt –*** Adopt the cost of short-term debt of 0.1833% as contained in MERC's Initial Brief and its calculations.

6. ***Flotation Costs –*** Determine that the flotation costs have been appropriately reflected in the cost of equity.

7. ***Cost of Equity –*** Determine that the appropriate cost of equity is 9.70, recognizing an anomaly in the comparisons used by the Department and eliminating New Jersey Resources, which differs significantly from the other comparables in the group.

8. ***Overall Rate of Return –*** Direct the staff to calculate, and include in the order, the overall rate of return based on the Commission decisions above.

9. ***Other Employee Benefits –*** Accept the Department's and MERC's agreement to remove $3,905 (Christmas Gift check Expense-Retirees) from Account 926070; $469 (Awassa Lodge) from Account 926100; and $29,639 from Account 926050 (Deferred Compensation amounts that are offset with an equal amount of interest income not included in income in this rate case). This results in a reduction of MERC's test-year expense for other employee benefits by $34,013. (ALJ)

10. ***Other Employee Benefits –*** Accept the Department's and MERC agreement to allow $32,588 from Account 926135 (Fully Insured Long Term Disability Premium Expense); $116,973 from Account 926510 (Profit Sharing Expense); and $3,090 from Account 926270 (Adoption Assistance). (ALJ)

11. ***Gas Storage Balance –*** Authorize the use of a gas storage inventory balance of $12,842,087. (ALJ)

12. ***Plant Adjustment and Accumulated Depreciation –*** Accept the agreement between MERC and the Department that MERC will reduce test year rate base plant-in-service by $1,661,569 and reduce accumulated depreciation by $1,057,096, for a net decrease of $604,473. (ALJ)

13. ***Actual Deferred Tax Balances –*** Require MERC to update its test year deferred tax calculation which results in an increase in the deferred tax balance and a $528,375 reduction in test year rate base. (ALJ)

14. ***Depreciation Expense –*** Reduce MERC's test-year depreciation expense by $35,798. (ALJ)

15. ***IBS Cost Allocation Adjustment –*** Reduce the IBS cost allocation included in MERC's proposed test-year income statement by $18,821. (ALJ)

16. ***Cost Allocations to ServiceChoice –*** Accept MERC's allocation of costs to the non-regulated ServiceChoice program. (ALJ)

17. ***Aircraft Expense –*** Disallow recovery of any corporate aircraft expense in the test-year as agreed by the Department and MERC. (ALJ)

18. ***Lobbying Expense –*** Disallow all lobbying expense, which results in a $20,600 test-year adjustment. (ALJ)

19. ***Interest Synchronization –*** Authorize MERC to recalculate its interest synchronization adjustment in its final, 30-day compliance filing to reflect the Commission's final determinations in this proceeding. (ALJ)

20. ***Asset Retirement Obligation –*** Do not authorize MERC to recover FASB 143 Asset Retirement Obligation (ARO) costs in rates. (ALJ)

21. ***Health Care Reform Legislation* –** Defer making a decision until MERC's next rate case on whether MERC may recover in rates the cost of the Medicare Part D subsidy overage and defer the current Medicare Part D subsidy by allowing MERC to record the amount ($88,749) in FERC Account 182.3. (ALJ)

22. ***Marketing Expenses* –** Accept MERC's statements regarding marketing expenses and let the record reflect that MERC did not request cost recovery for test-year marketing expenses. (ALJ)

23. ***Economic Development Expenses* –** Approve MERC's request for $24,148 in test-year expenses for economic development activities. (ALJ)

24. ***Advertising Expense* –** Approve the Department recommendation to include in the test year $143,079 in advertising expenses for MERC-PNG and $39,560 in advertising expenses for MERC-NMU, for a total of $182,639 in test year advertising expenses for the consolidated company. (ALJ)

25. ***Ratepayer-Supplied Funds* –** Accept the ALJ's finding in paragraph 179 of his report that "MERC reduced the rate base by $71,159, and that amount accurately reflects the difference between funding and expenses for its employee benefit obligations. No further adjustment is necessary." (ALJ)

26. ***Cash Working Capital* –** Require Cash Working Capital to be updated to reflect the final decisions of the Commission. (ALJ)

27. ***Long-Term Incentive Compensation* –** Accept the parties' resolution of the long-term incentive compensation issue based on MERC's agreement to remove $88,145 for Performance Shares, $21,080 for Stock Options, and $128,347 for Restricted Stock from the 2011 revenue requirement. (MERC, OAG, ALJ)

28. ***Legal Cost Savings from PGA Rate Area Consolidation* –** Approve the Department adjustment to reduce Administrative and General (A&G) expenses, in Account No. 928, by $11,422. (ALJ)

29. ***Uncollectible Expense Tracking and True-up Mechanism* –** Approve MERC's request to withdraw from consideration its request for an uncollectible expense tracking and true-up mechanism. (ALJ)

30. ***Charitable Contributions* –** Approve MERC's position of including Charitable Contributions of $69,598 in test-year expenses.

31. ***Gift Expenses* –** Accept MERC's position that test-year O&M expense does not include Gift expenses. (ALJ)

32. ***Membership Dues Expense* –** Approve the exclusion of all membership and dues expenses from MERC's test-year revenue requirement. (ALJ)

33. ***Research Expenses –*** Approve MERC's position that its test-year O&M expenses do not include research expenses. (ALJ)

34. ***Labor Increase of Two Additional Employees –*** Accept MERC's position and the ALJ's recommendation that MERC's request for two additional employees at a salary level of $117,600 no longer exists as a separate issue. (ALJ)

35. ***Vertex Billing Service Expense –*** Approve MERC initial filing level of $5,629,466 for Vertex billing service expenses with a test year adjustment of $954,687. (ALJ)

36. ***Capitalization of Repairs and Overhead Costs –*** Accept MERC's statements that its proposal to the Internal Revenue Service to change the way it determines whether repair and maintenance costs will be recorded as capital expenditures or operations and maintenance expense for tax purposes, and the "determinations of repair and maintenance versus capital will not change for regulatory and financial accounting purposes." (ALJ)

37. ***Non-Fuel O&M Expense Methodology –*** Adopt the Department's recommended Non-Fuel O&M expense reduction of $2,215,136, agreed to by MERC, and adopt the ALJ's Finding that the additional six (6) percent reduction to MERC's revised test year non-fuel O&M expenses recommended by the OAG would not accurately reflect MERC's test year costs. (MERC, DOC, ALJ)

38. ***Pension Expense –*** Determine that test year pension expense should be set no higher than 2010 levels and adopt the ALJ findings 142-164. (DOC, ALJ, and OAG with respect to Finding 164)

39. ***Pension Expense in Next Rate Case –*** Require MERC to fully support in its next rate case the reasonableness of having ratepayers pay for 100% of MERC's pension obligation.

40. ***Non-Qualified Pension Plan Costs –*** Require MERC to clearly identify all non-qualified pension plan costs included in its filing and clearly show that all have been removed from the revenue requirement with the exception of the amount associated with the amortization of the regulatory asset created in Docket No. 06-1287.

41. ***Annual Incentive Amounts –*** Allow MERC to include $1,262,723 of annual non-executive incentives, and $45,398 of Executive Annual Incentives, in the revenue requirement. (ALJ)

42. ***Refund of Unpaid Incentive Compensation –*** Adopt MERC's and the Department's refund proposal regarding annual incentive compensation costs and

    a. Require MERC to refund any incentive compensation costs included in the test year revenue requirement that are not paid out in a particular year. However, allow MERC to track the annual amounts to be refunded and make the refunds only after they reach $1 per customer.

b. Require MERC to include, in its thirty-day rate case compliance filing, an explanation of how the $1 per customer refund threshold would be implemented in the refund mechanism. MERC's compliance filing should: (a) explain whether the $1 per customer threshold means "whenever the cumulative amount exceeds an average of $1 per customer" or something else and how that calculation would be made and (b) clarify that all annual incentive compensation costs included in the test year revenue requirement that are not paid out in a particular year (with no netting with years in which more than the test year level of incentive is paid) are to be applied to the tracker account.

c. Require MERC to make an annual compliance filing within 60 days after the incentive compensation awards are or would have been paid,

d. Require MERC to include in its compliance filing sufficient information to determine whether a refund is required and, if so, the amount of the refund, and

e. Use a per dekatherm refund mechanism with any such refund.

43. ***Medical and Dental Expense –*** Adopt the resolution between MERC and the Department on test year medical and dental expenses. (ALJ)

44. ***Additional Property Tax Expense –*** Determine that MERC's 2011 test year revenue requirement should include $5,733,578 of property tax expense ($4,617,000 from the initial filing plus $1,116,578). (ALJ, MERC, DOC)

45. ***Administrative Notice of Tax Appeal Outcomes –*** Take administrative notice of any decisions on MERC's property tax appeals made before the final order in this proceeding. (DOC, ALJ)

46. ***Construction Work in Progress –*** Do not include CWIP in rate base.

47. ***Work Asset Management and PeopleSoft Costs –*** Approve the ALJ recommendation to allow MERC to recover $1,357,410 as amortization expense and to allow the un-amortized balance to be included in MERC's rate base calculation. (MERC, ALJ)

48. ***Bad Debt Expense –*** Approve the ALJ recommendation to calculate the Bad Debt expense by applying the Bad Debt expense factor of 0.776545% to the test year revenue level including the Department's original test year revenue deficiency to determine the revenue requirement. (MERC, DOC, ALJ)

49. ***Travel, Entertainment, and Related Employee Expense –*** Approve the ALJ's recommendation that MERC has met the reporting requirements for Minn. Stat. § 216B.16, subd. 17(c) and that the reported expense levels are reasonable. (ALJ)

50. ***Data Practices and Executive Salaries –*** Approve the ALJ's recommendation to allow MERC's salaries for the sixth through tenth highest paid employees to be confidential, non-public information. (ALJ)

51. ***Regulatory Assets and Liabilities: the Cloquet Plant –*** Adopt the ALJ's recommendation and find that the rate base should include $43,498 that represents the Cloquet plant amortization, labor actuals, and labor loader that were included in the rate base in MERC's last rate case in Docket No. G-007,011/GR-08-835. (MERC, ALJ)

52. ***CIP-Related Filing Requirements –*** Adopt the AJL's finding that MERC has met the requirements of Minn. Stat. 216B.16, subd. 1.

53. ***CIP Expenses –*** Adopt the ALJ finding and allow MERC to recover $8,454,427 ($6,737,189 for MERC-NMU and $1,717,238 for MERU-PNG) in test year CIP expenses.

54. ***CCRC Calculation –*** Require MERC to recalculate its CCRC rate in MERC's thirty-day compliance filing to the Commission's final order in this docket using the Commission approved test year CIP expense and the Commission approved test year sales volumes less the appropriate CIP exempt volumes, but including the three non-exempt CIP customers' volumes erroneously excluded by MERC in its original petition.

55. ***Unamortized CIP Balance –*** Allow MERC to keep its December 31, 2010 CIP tracker balance within MERC's CCRA tracker mechanism and do not require MERC to "roll-in" the December 31, 2010 CIP tracker balance into MERC's CCRC calculation.

56. ***CIP Carrying Charges –*** Allow MERC to apply to MERC-PNG's and MERC-NMU's CIP tracker accounts (except for any portion of the 2005, 2006, and 2007 DSM financial incentives) carrying charges that are equal to the overall rate of return approved for MERC in this general rate case.

57. ***Consolidating CCRC, CCRA, and CIP Tracker Accounts of NMU and PNG Rate Distribution Areas –*** Approve the consolidation of MERC's CCRC, CCRA, and CIP tracker mechanism if the Commission approves consolidation of all other rate aspects in this docket.

58. ***Uncollected CCRC Revenues from Prior Years –*** Modify the ALJ recommendation to require MERC to credit the NMU CIP tracker with the uncollected CCRC revenues from July 2006 through February 2011, the amount to be calculated in consultation with the Department, plus additional revenue amounts from March 2011to the date final rates become effective in this docket. Require MERC to make a compliance filing within thirty days illustrating the necessary calculations for this recommendation. Determine that there will be no carrying charge on these amounts.

59. ***Compliance Filing on Interim Period CCRC and CCRA Collections –*** As part of MERC's thirty-day compliance rate filing, require MERC to demonstrate that the CIP tracker account has been properly credited with the appropriate CCRC amounts during the interim rate period or how MERC plans to do so after final rates have been determined.

60. ***Tax Allocation in the CCOSS –*** Determine that the allocation of income taxes used in the CCOSS should be based on the allocation of rate base.

61. ***Class Revenue Apportionment* –** Adopt the class revenue apportionment recommendation of the Administrative Law Judge and authorize the class revenue apportionment agreed to by MERC and the Department. [MERC, DOC, ALJ]

62. ***Effect of Lower Revenue Requirement on Class Revenue Apportionment* –** If the Commission approves a lower rate increase and lower overall revenue requirement than the amounts MERC initially requested, then the revenue responsibilities for the non-firm classes shall be held constant, and the remaining revenue requirement shall be apportioned proportionately to the remaining firm classes. [DOC, MERC, ALJ]

63. ***Consolidating Rate Distribution Areas* –** Approve MERC's proposed consolidation plan and authorize the consolidation of MERC-PNG and MERC-NMU into a single distribution rate area. [MERC, DOC, ALJ]

64. ***Consolidating Gas Cost Recovery Systems and PGAs of Consolidated Rate Distribution Areas* –** Approve MERC's request to consolidate the four gas cost recovery and PGA systems currently in place (PNG-NNG, PNG-VGT, PNG-GLGT, and NMU) into two new PGAs, the MERC-NNG PGA system and the MERC-Consolidated PGA system. [MERC, DOC, ALJ]

65. ***Timing of PGA Consolidation* –** Approve MERC's request to consolidate PGA rates to be effective on July 1 after final rates go into effect and that consolidation of the true-up factors become effective with the first Annual Automatic Adjustment and True-Up filings made on September 1 after final rates go into effect. [MERC]

66. ***Large C&I Customer Charge* –** Adopt the recommendation of the Administrative Law Judge and increase the large commercial and industrial customer charge from $17.00 to $35.00. (MERC, DOC, ALJ)

67. ***Small Volume Interruptible Customer Charge* –** Adopt the recommendation of the Administrative Law Judge and increase the small volume interruptible customer charge from $80.00 to $150.00. (MERC, DOC, ALJ)

68. ***Large Volume Customer Charge* –** Adopt the recommendation of the Administrative Law Judge and increase the customer charge for all large volume customers from $160.00 to $175.00. (MERC, DOC, ALJ)

69. ***Super Large Volume Customer Charge* –** Adopt the recommendation of the Administrative Law Judge and increase the customer charge for all super large volume customers from $160.00 to $300.00. (MERC, DOC, ALJ)

70. ***Transportation Administration Fee* –** Adopt the recommendation of the Administrative Law Judge and lower the transportation administration fee to $70.00 per month. (MERC, DOC, ALJ)

71. ***Filing and Recordkeeping Requirements Regarding Construction Charges and Disconnection/Reconnection Charges in Cases Involving Tampering –*** Adopt the recommendation of the Administrative Law Judge and

    a. authorize MERC's proposed $260 adjustment for frost charges assessed outside the winter construction charge time period, and

    b. continue the requirement in MERC's next rate case for reporting winter construction charges, abnormal construction charges, and charges for disconnection and reconnection in cases of tampering.

72. ***Miscellaneous Tariff Charges –*** Adopt the recommendation of the Administrative Law Judge and approve MERC's request for miscellaneous tariff changes as described in paragraphs 330 to 334 of the ALJ's Report.

73. ***Farm Tap Inspection Program –*** Adopt the recommendation of the Administrative Law Judge and approve the continuation of the farm tap inspection program and clarify that MERC

    a. shall continue to send farm-tap safety and information brochures to new farm tap customers before they take service and to all existing farm customers annually.

    b. shall continue to file annual reports on its farm tap inspection program on or before April 1 of each year.

    c. Within 90 days of the end of each five-year inspection cycle and in each general rate case, shall file with the Commission, the Department, and the Minnesota Office of Pipeline Safety a five-year report including cumulative results of the inspection program and any recommendations for future improvements. [PUC Staff recommendation]

74. ***Gas Affordability Program –*** Adopt the recommendation of the Administrative Law Judge and approve the agreed upon adjustments to rate base to remove $244,305 in gas affordability program start-up costs and to remove $148,555 in deferred debt-LT arrearage regulatory asset. (MERC, DOC, OAG, ALJ)

75. ***Housekeeping Issues –*** State that the final order in this docket shall contain summary financial schedules including: a calculation of MERC's authorized cost of capital, a rate base summary, an operating income statement summary, a gross revenue deficiency calculation, and a statement of the total allowed revenues. Direct parties to work with Commission staff to prepare such schedules for inclusion in the Order, should modifications be necessary to reflect the Commission's final decision.

76. ***Compliance Filings –*** Require MERC to make the following compliance filings within 30 days of the date of the final order in this docket:

a. Revised schedules of rates and charges reflecting the revenue requirement and the rate design decisions herein, along with the proposed effective date, and including the following information:

i. Breakdown of Total Operating Revenues by type;
ii. Schedules showing all billing determinants for the retail sales (and sale for resale) of natural gas. These schedules shall include but not be limited to:

1. Total revenue by customer class;
2. Total number of customers, the customer charge and total customer charge revenue by customer class; and
3. For each customer class, the total number of commodity and demand related billing units, the per unit commodity and demand cost of gas, the non-gas unit margin, and the total commodity and demand related sales revenues.

iii. Revised tariff sheets incorporating authorized rate design decisions;
iv. Proposed customer notices explaining the final rates, the monthly basic service charge, rate area consolidation, and, if approved, the revenue decoupling pilot program.

b. A revised base cost of gas and supporting schedules incorporating any changes made as a result of this rate case, and automatic adjustments establishing the proper adjustments to be in effect at the time final rates are implemented.

c. If final authorized rates are lower than interim rates, a proposal to make refunds of interim rates, including interest calculated at the average prime rate, to affected customers.

77. ***Comments on Compliance Filings –*** Authorize comments on all compliance filings within 30 days of the date they are filed. However, comments are not necessary on MERC's proposed customer notice.

The motion passed 3-0.

Motion on Alternative Decoupling Proposal

Commissioner Boyd moved to reject MERC's SFV rate design proposal for residential and small commercial and industrial customer charges as an alternative to revenue decoupling.

The motion passed 3-0.

Motion on Rate Case Expense

Commissioner Boyd moved to approve the ALJ's recommendation for amortized rate case expense level of $397,677, which is amortized over a three year period, and to require MERC to track rate case expense recoveries exceeding the authorized test-year expense, for possible crediting against the revenue requirement in the next rate case. (CenterPoint 2008 rate case)

The motion passed 3-0.

Motions on Class Cost of Service (CCOSS) Study

Commissioner Boyd moved to make no determination on the precision or usefulness of MERC's CCOSS and to take no action on the treatment of income taxes in future CCOSSs.

The motion passed 3-0.

Commissioner Boyd moved to determine that the Commission will not adopt the language in the ALJ's proposed finding 52.

The motion passed 3-0.

There being no further business, the meeting was adjourned.

APPROVED BY THE COMMISSION: July 18, 2012

Burl W. Haar

Burl W. Haar, Executive Secretary