

E-132, 299/SA-88-270 AFFIRMING AND CLARIFYING EARLIER ORDER

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Darrel L. Peterson	Chair
Cynthia A. Kitlinski	Commissioner
Norma McKanna	Commissioner
Robert J. O'Keefe	Commissioner
Patrice Vick	Commissioner

In the Matter of the Complaint Regarding the Annexation of a Portion of the Service Territory of People's Cooperative Power Association by the City of Rochester (North Park Additions)

ISSUE DATE: October 29, 1990

DOCKET NO. E-132, 299/SA-88-270

ORDER AFFIRMING AND CLARIFYING EARLIER ORDER

PROCEDURAL HISTORY

On July 11, 1990, the Commission issued its ORDER DETERMINING COMPENSATION in the above-entitled matter. That Order determined appropriate compensation under Minn. Stat. § 216B.44 (1988) for the City of Rochester's acquisition of a portion of the service territory of People's Cooperative Power Association. The Order set appropriate compensation at \$148,037.

On July 31, 1990, the City of Rochester filed a petition for rehearing, reconsideration, or an amended decision. On the same date the Minnesota Municipal Utilities Association filed a petition for rehearing and other post-hearing relief, and the Minnesota Department of Public Service (the Department) filed a petition for reconsideration and clarification.

On August 10, 1990, People's Cooperative Power Association, the Minnesota Rural Electric Association, and the Minnesota Municipal Utilities Association filed answers to the petitions.

Under Minn. Stat. § 216B.27, subd. 4 (1988), any application for rehearing not granted with 20 days of filing is deemed denied. On August 16, 1990, the Commission issued an Order granting the petitions for purposes of tolling the 20-day time period to afford them careful review.

The petitions came before the Commission on the merits on September 6, 1990.

FINDINGS AND CONCLUSIONS

## **The Nature of Reconsideration**

Most of the issues raised in the petitions were raised, briefed, argued, and considered in detail when this case originally came before the Commission. The Department is correct, however, in pointing out that this does not preclude rethinking any of these issues now.

At reconsideration the Commission directs its attention to specific issues identified by the parties as meriting further evaluation. The Commission does not discourage parties from providing further analysis of already-decided issues at reconsideration. In this case, as in many others, the legal and policy issues are significant and complex enough to warrant a second look, especially one informed by the parties' analyses of the Commission's decision. Having taken that second look, however, the Commission concludes that in this case its original decision was correct, and, for the most part, was adequately explained in its July 11 Order.

Therefore, this Order will not provide another definitive explanation of the Commission's decision. Instead, it will address the new issues raised on reconsideration and will correct an inadvertent mischaracterization of expense residual analysis which appeared in the July 11 Order.

## **The Effect of the Court of Appeals Decision Upholding the Commission's Definition of "Receiving Electric Service"**

The City and the Minnesota Municipal Utilities Association (the MMUA) argued that a recent decision of the Court of Appeals, upholding the Commission's definition of "receiving electric service,"<sup>1</sup> changes their perspective on the case and requires new hearings to allow them to introduce new evidence. The Commission disagrees.

The proper definition of "receiving electric service" was always recognized as a pivotal issue in this case. It was raised early in the proceeding by the City itself in a motion for summary judgment. One of the two claims on which the motion was based was that no compensation was due because the area at issue had not been "receiving electric service" on the date of annexation. The motion was denied by both the Administrative Law Judge and the Commission, clearly indicating that the Commission had not been persuaded to adopt the City's definition. This should not necessarily have dissuaded the City from advancing its own definition. It should, however, have alerted the City to the need to deal with the Commission's definition in presenting its case. ORDER AFFIRMING ADMINISTRATIVE LAW JUDGE'S ORDER DENYING SUMMARY JUDGMENT AND ORDERING RESUMPTION OF CONTESTED CASE PROCEEDINGS ON ISSUE OF COMPENSATION, this docket, March 17, 1989.

Furthermore, by the time hearings began in November 1989, all parties were aware of the

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<sup>1</sup> In the Matter of the Complaint by Kandiyohi Cooperative Electric Power Association against Willmar Municipal Utilities Commission for Extending Electric Facilities in and Adjacent to Westwind Estates, 455 N.W.2d 102 (Minn. Ct. App. 1990).

Commission's definition of "receiving electric service." It had been consistently applied in service area disputes, including several between these parties.<sup>2</sup> It had been implicitly accepted by the Court of Appeals in an appeal from a Commission decision in an interim service rights dispute between the City and the co-op.<sup>3</sup> The City and the MMUA cannot claim surprise to justify their request to reopen evidentiary hearings.

Neither can they claim a failure of due process. All parties had full opportunity to present testimony based on the Commission's definition, as well as alternative testimony based on the definition advanced by the City and the MMUA. The co-op and the Minnesota Rural Electric Association (the MREA) presented expert testimony based on the Commission's definition. The City and the MMUA chose to forego that opportunity. The City and the MMUA also had full opportunity to cross-examine the witnesses who presented testimony based on the Commission's definition of "receiving electric service." The interests of justice therefore do not require further evidentiary hearings.

Neither does the public interest favor reopening evidentiary hearings. This case began in April of 1988. It was referred to the Office of Administrative Hearings for contested case proceedings and remained there for 17 months. It consumed two days of public hearings and ten days of evidentiary hearings. It has made substantial claims on the resources of all parties, the Commission, and the Office of Administrative Hearings. The Commission does not believe it would be in the public interest to extend this proceeding any longer.

### **The Significance of Proceedings Before the Wisconsin Commission**

The Commission found that the co-op had been damaged in the amount of \$11,644 in increased

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<sup>2</sup> The Willmar case, which set forth the Commission's definition of "receiving electric service" and was ultimately upheld by the Court of Appeals, was decided August 9, 1989. In the Matter of the Complaint by Kandiyohi Cooperative Electric Power Association Against Willmar Municipal Utilities Commission for Extending Electric Facilities in and Adjacent to Westwind Estates, Docket No. E-118, 329/SA-89-502. Following that case, the Commission set forth and applied its definition of "receiving electric service" in at least eight Orders involving service area disputes between the City and the co-op. See ORDER DISMISSING COMPLAINT, August 31, 1989, docket number E-299, 132/C-89-519, and seven Orders titled ORDER DENYING INTERIM SERVICE RIGHTS TO THE CITY OF ROCHESTER, dated September 1, 1989, in docket numbers E-299, 132/SA-89-419, E-299, 132/SA-89-420, E-299, 132/SA-89-421, E-299, 132/SA-89-422, E-299, 132/SA-89-423, E-299, 132/SA-89-368, and E-299, 132/SA-89-457.

<sup>3</sup> In the Matter of a Complaint of People's Cooperative Power Association, Inc. Against the City of Rochester, 447 N.W. 2d 11 (Minn. App. 1989). In that case the Court found contested case proceedings necessary to resolve disputed material facts before a municipality could be awarded interim service rights to an area "receiving electric service" from an assigned utility. There were no actual customers within the area at issue when the City extended service, implying the Court's acceptance of a more expansive reading of the statute than the City's "actual customer" test.

incremental wholesale power rates due to its loss of the North Park load. The City and the MMUA argued that evidentiary hearings should be reopened because evidence in two proceedings before the Wisconsin Public Service Commission indicates there may be opportunities for the co-op's wholesale supplier to sell the power it would have sold to the North Park Additions to other utilities.

From the descriptions presented in the City's petition, one proceeding appears to be a least cost planning proceeding involving Wisconsin Public Power, Inc. The other is apparently a consolidated construction docket, in the nature of a certificate of need proceeding. The issues in both proceedings involve the need for additional generating capacity on the part of various public and private utilities operating within the state of Wisconsin.

The Commission sees no reason to reopen evidentiary hearings in light of the Wisconsin proceedings. Neither of them focuses solely, or even primarily, on the co-op's wholesale supplier, Dairyland Power Cooperative. Both proceedings are wide ranging in scope. They are designed to yield reliable conclusions on the overall capacity situations facing the involved utilities, not on the specific power contracts these utilities should execute. The Commission considers it unlikely that these proceedings will yield information specific to Dairyland Power Cooperative's incremental cost of producing wholesale power.

Furthermore, the Wisconsin proceedings appear to have been in progress in February 1990 when the record in this case closed. They were clearly in progress during briefing and argument to the Administrative Law Judge and the Commission. If the City and the MMUA believed the Wisconsin proceedings would yield information relevant to this case, they could and should have requested its introduction before this lengthy proceeding reached the reconsideration stage.

### **The Appropriateness of Basing Damages on a 1988-89 "Test Year"**

The City and the MMUA objected to the Commission's, and the Administrative Law Judge's (ALJ's), use of the twelve month period from August 1, 1988 to July 31, 1989 to determine sales, revenues, and expenses in assessing the co-op's damages. These parties argued that the appropriate date for determining damages was the date of annexation (March 1987) or the date the City extended distribution facilities into the area (June 1987). The Commission disagrees.

The goal of the compensation provisions of Minn. Stat. § 216B.44 (1988) is to place the displaced utility in the same position it would have occupied but for the municipal utility's acquisition of its service territory. As the Commission noted in the July 11 Order, in theory the loss of revenues sustained by the co-op is perpetual. There is therefore no "magic date" for purposes of determining compensation. Whether the Commission assumed a date of taking of March 1987, June 1987, or July 1989, the damages would have been the same. The ALJ and the Commission properly used the most recent, most reliable data available on sales, revenues, and expenses attributable to serving the annexed area, to determine what the co-op lost when it lost the right to serve it.

### **The Order's Observations on the Potential for Selective Annexation**

The City and the MMUA objected to the compensation award on grounds that it was based on the erroneous finding that the City had annexed selective portions of the surrounding area to avoid paying compensation to People's. The Commission made no such finding.

The City and the MMUA advocated an interpretation of Minn. Stat. § 216B.44 (1988) which would limit compensation to cases in which a municipality physically acquired facilities belonging to another utility. The Commission rejected this interpretation, in part because it could lead to the absurd result of awarding no compensation when a municipality selectively annexed all portions of its surrounding area except parcels on which the facilities of

other utilities were located. This was a proper consideration. When construing a statute, it is standard practice to consider the effects of alternative interpretations in light of the policies underlying the statute. Here, the Commission properly concluded it should not adopt an interpretation which could defeat the statutory purpose of compensating utilities which lose service territory to expanding municipalities.

### **The Order's Findings of Fact and Policy Discussions**

The MMUA objected that the July 11 Order failed to make necessary findings of fact and instead based its conclusions on "broad, unsubstantiated policy statements." The Commission disagrees.

The most hotly contested issues in this case were issues of law and policy: whether the area at issue had been "receiving electric service" within the meaning of the statute, whether a municipality must physically take possession of facilities to be liable for compensation, whether a displaced utility's right to serve was a compensable property right, and whether a city's franchise authority could defeat a displaced utility's right to compensation. These were issues of statutory interpretation. To resolve them, the Commission was required to use its institutional expertise in regulatory law and policy. It was entirely appropriate, then, for the July 11 Order to reflect the Commission's understanding of the public policies underlying the Public Utilities Act, Minn. Stat. § 216B.01 et seq.

The Order also made findings on the disputed factual issues. Since the Order was in narrative form, these findings were not segregated and numbered, as they were in the ALJ's report. The Commission reiterates, however, that it accepts and adopts the findings of the ALJ in regard to the loss of revenue damages sustained by the co-op. The Commission reiterates that the August 1988 to July 1989 data which the ALJ used to compute compensation were accurate and reliable, and that expense residual analysis was the proper analytical tool for converting those data into damages.

The Commission also found and finds that the data underlying MREA's and People's' calculations of increased wholesale power costs were accurate and the best available measure of those damages.

### **The City's and the MMUA's Alleged Reliance on Judge Klein's Order**

The City and the MMUA alleged that they reasonably relied to their detriment on the finding by Administrative Law Judge Allan W. Klein that damages in this case could not be awarded for loss of revenue, but only on the basis of "other appropriate factors." If such reliance occurred, it was unreasonable.

The Commission's Order affirming Judge Klein's denial of summary judgment made it clear that the Commission did not rule out the possibility of awarding damages under any of the four factors listed in Minn. Stat. § 216B.44 (1988):

The Commission believes that full evidentiary hearings may develop facts that could justify compensation on some or all of the [four statutory] factors listed above. For that reason, the Commission will affirm the ALJ's Order and order the resumption

of contested case proceedings on any of the statutory factors the parties may choose to address.

The decision the Commission makes today is to resume contested case proceedings; this decision does not prejudge whether compensation is due or define any specific basis for that compensation. This Order simply affords parties an opportunity to develop an evidentiary record supporting their positions.

ORDER AFFIRMING ADMINISTRATIVE LAW JUDGE'S ORDER DENYING SUMMARY JUDGMENT AND ORDERING RESUMPTION OF CONTESTED CASE PROCEEDINGS ON ISSUE OF COMPENSATION, March 17, 1989, this docket.

It was obvious from the language of the Order that the Commission would entertain arguments for compensation under any of the statutory factors, including loss of revenue. The co-op and the MREA introduced evidence of loss of revenue damages. This evidence was duly admitted by the ALJ. The Commission rejects the contention of the City and the MMUA that their alleged reliance on Judge Klein's Order requires reopening of evidentiary hearings.

### **Clarification of Expense Residual Analysis**

Through inadvertence, the July 11 Order mischaracterized expense residual analysis, treating that analytical method as if its reference point were revenues instead of expenses. Actually, expenses are the starting point, since the purpose of the analysis is to determine what portion of system-wide joint and common costs service to the area at issue would have contributed. The method is based on the assumption that expense residuals based on cost of service principles approximate net revenue loss.

The expense residual method first determines the expenses which would be allocated on a system-wide basis to sales within the area at issue. From this amount expense reductions, realized because the area is not being served, are subtracted, yielding the expense residual.<sup>4</sup> The expense residual is then adjusted for inflation and reduced to present value, assuming damages are being computed over time and into the future.

The discussion above is intended to correct inadvertent mischaracterizations of expense residual analysis which appeared in the July 11 Order and to clarify the application of the methodology to this case.

### **Commission Action**

The Commission concludes, for the reasons set forth above, that its original compensation

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<sup>4</sup> In this case, People's' operation and maintenance expense, depreciation expense, interest expense, and billing costs were reduced. The amount of the reductions was subtracted.

determination was correct. It will affirm that determination and will clarify the operation of expense residual analysis in calculating the compensation amount.

ORDER

1. The Commission affirms and clarifies its Order of July 11, 1990 as set forth above.
2. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster  
Executive Secretary

(S E A L)