ISSUE DATE: February 4, 1998

DOCKET NO. G-007/M-97-94

ORDER PARTIALLY GRANTING AND PARTIALLY DENYING PETITION FOR MISCELLANEOUS RATE CHANGES

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Edward A. Garvey	Chair
Joel Jacobs	Commissioner
Marshall Johnson	Commissioner
LeRoy Koppendrayer	Commissioner
Gregory Scott	Commissioner

In the Matter of Northern Minnesota Utilities' Petition for Approval of a Miscellaneous Rate Change to Reflect Requested Changes in Gas Transportation Demand Levels

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PROCEDURAL HISTORY

On January 16, 1997, Northern Minnesota Utilities (NMU or the Company) filed a petition to change its demand entitlements. NMU sought permission to change its allocations of firm field transportation service (TFF), firm deferred delivery service (FDD), and system management service (SMS) on the Northern Natural Gas Company system. NMU also asked permission to collect producer demand and upstream pipeline costs in the commodity component of its gas rates (which is charged to both firm sales and interruptible sales customers) rather than the demand component (which is charged only to firm sales customers). As allowed under law, NMU had put this rate design change into effect in November, 1996.

On March 20, 1997, the Department of Public Service (the Department) filed comments. The Department recommended that the Commission grant NMU's request to change its entitlements and grant NMU the necessary related variance to Minn. Rules, part 7825.2910. The Department also recommended that the Commission deny NMU's request to recover producer demand costs in its commodity gas rate. The Department recommended that the Commission require NMU to return to its previous (pre-November, 1996) rate design.

On March 31, 1997, NMU filed reply comments.

On May 22, 1997, the Commission met to consider NMU's petition. After hearing the comments of NMU, the Department, and the Residential and Small Business Utilities Division of the Office of Attorney General (RUD-OAG), the Commission tabled the matter to allow parties to: 1) submit additional comments to clarify (and possibly agree on) the rate impacts of NMU's proposal; and 2) compare NMU's interruptible sales rate and the "market rate" of gas for NMU's interruptible transportation customers.

Between June 13 and December 5, 1997, NMU and the Department filed supplemental comments supporting their respective views.

On January 14, 1998, the Commission again took the matter up.

FINDINGS AND CONCLUSIONS

I. THE REQUEST FOR CHANGES IN DEMAND ENTITLEMENTS

A. Comments of the Department

The Department recommended approval of the Company's requested changes in entitlements for TFF, FDD, and SMS. The Department stated that NMU's design day level is appropriate and should ensure that gas service is reliable for Minnesota customers.

The Department did note particularly the Company's treatment of TFF levels in its petition. NMU had decreased the level of TFF in its November and December, 1996 Purchased Gas Adjustments (PGAs). NMU's petition now stated that NMU's contract with Northern Natural Gas (NNG) did not allow a reduction of TFF; NMU must therefore raise its TFF level. NMU did not indicate how it proposes to recover the amount previously undercharged (which amounts to $80,795 for two months). The Department recommended that NMU include the amount to be recovered as a separate item in the Company's 1997 true-up filing. As with other true-up items, no interest should accrue on this amount.

The Department noted that NMU had reduced its level of TF12 Variable entitlements and increased its level of TF12 Base entitlements by the same amount. Because the Company put the change into effect in its December, 1995 PGA in Docket No. G-007/AA-96-61, the change was not included in NMU's previous demand filing, G-007/M-95-1142, and was not submitted for Commission approval. The Department recommended that the Commission grant a variance to Minn. Rules, part 7825.2910, subp. 2, which requires gas utilities to file for changes in demand, including exchanging one form of demand for another.

B. Commission Action

The Commission agrees with the Department that NMU's requested changes in demand entitlements will not hinder the Company's reliability and should be approved.

The Commission will grant NMU a variance to Minn. Rules, part 7825.2910, subp. 2, which requires gas utilities to file for changes in demand, including exchanging one form of demand for another.

The circumstances fulfill the criteria for granting a variance under Minn. Rules, part 7829.3200:

1. Enforcement of the rule would impose an excessive burden upon the applicant or others affected by the rule.

In this case, not allowing the change in TF levels would burden NMU's customers, who would be forced to pay higher rates retroactively for costs that NMU did not incur.

2. Granting the variance would not adversely affect the public interest.

Granting the variance would be in the public interest because NMU's customers have paid rates reflecting gas costs that have been approximately $180,850 lower than they would have been under the previous allocation of TF levels.

3. Granting the variance would not conflict with standards imposed by law.

Although NMU failed to ask approval of the change in demand levels, it did reflect the rate change in its December, 1995 PGA. The Department stated that it is satisfied that it received technical notice of the change. The Commission finds that granting the variance would not conflict with standards imposed by law.

Finally, the Commission agrees with the Department that NMU should reflect its underrecovery of TFF costs as a separate item in the Company's 1997 true-up filing. This approach will assist the Department in its analysis of the Company's treatment of this cost.

II. THE REQUEST FOR RECOVERY OF PRODUCER DEMAND COSTS AND UPSTREAM PIPELINE COSTS IN THE COMMODITY COMPONENT OF GAS RATES

A. Comments of the Parties

1. NMU

NMU argued that both firm and interruptible sales customers are responsible for producer demand/upstream pipeline costs because producers treat these costs as demand costs and charge them to NMU on a pass-through basis. Interruptible customers should not obtain gas at a commodity rate because that rate does not reflect the full cost of delivering the gas to the point of delivery on NMU's pipeline. NMU should be allowed to recover producer demand/upstream pipeline costs in the commodity charge from firm sales and interruptible sales customers alike.

NMU argued that their request is a rate design proposal for which the Commission, acting in its quasi-legislative capacity, may examine both cost and non-cost factors. The Commission should note that a return to NMU's pre-November, 1996 rate design would result in a rate increase of approximately $25 per year for firm customers (residential and small commercial) and a decrease of approximately $4800 per year for interruptible sales customers (industrial entities). NMU stated that the rate it is currently charging interruptible customers is well below market rate.

NMU argued that it should be allowed to charge interruptible customers a rate that is as close to market rate as possible; a rate decrease for interruptibles would result in firm customers subsidizing interruptible customers.

2. The Department

The Department argued that interruptible customers should not be charged producer demand/upstream pipeline costs because they do not contribute to the costs of reserving gas supplies and transport to serve firm gas to firm customers. If there were no interruptible customers on the system, the Department argued, NMU's demand costs would be the same. Interruptibles have made a bargain with the system, under which they agree to be subject to curtailment in exchange for a lower rate. The retention of interruptible customers benefits the system; if all interruptible customers became firm customers and no longer subject to curtailment, NMU would need to build a bigger line and charge all firm customers more.

The Department argued that requiring NMU to return to recovering producer demand charges through its demand costs would minimize rate shock and promote rate stability. NMU's current practice of recovering producer demand charges through commodity costs increases rates for interruptible customers by 21%, risking a conversion of interruptible sales customers to transportation customers. If customers switch to transportation, there will be fewer sales volumes over which to spread recovery of fixed costs. The result will be higher rates for the remaining sales customers.

The Department disagreed with NMU's argument that it must be charging appropriate rates for interruptible customers because it did not lose interruptible sales customers in 1996-1997 (after it had effected its proposed rate design change). According to the Department, the full impact of the change has not yet been felt because NMU unintentionally undercollected its producer demand costs by more than $1 million during that time.

The Department further argued that the appropriate venue to consider major rate design change is in a rate case.

B. Commission Action

Until November, 1996, NMU had recovered its producer demand costs from its firm sales customers in the demand component of gas rates. Since November, 1996, NMU has recovered producer demand costs from both firm sales and interruptible sales customers through commodity charges. NMU is now asking the Commission to authorize this method of recovery through a miscellaneous rate design change. For the reasons it will articulate, the Commission finds that this set of facts does not warrant such a requested change in rate design.

In 1995, the Commission addressed a similar request for a rate design change from NMU's affiliate, Peoples Natural Gas Company (Peoples). In Orders dated March 13 and August 8, 1998, in Docket No. G-011/M-94-960,[1] the Commission determined that Peoples should continue recovering pipeline demand costs[2] solely from the Company's firm sales customers in demand charges. In the August 8 Order, the Commission stated that Peoples' request for a significant change in rate design (to recovery of pipeline demand costs from both firm sales and interruptible sales customers in commodity charges) should be addressed in a rate case: "Major rate design decisions must be examined in the context of the Company's overall rate design, financial picture, and rate of return." Order at p. 4.

For the same reason, the Commission finds that NMU's request for a change in recovery of its producer demand costs should not be granted in a miscellaneous rate design proceeding.

The Commission also agrees with the Department that requiring NMU to recover producer demand costs solely from firm sales customers, as it had done prior to November, 1996, will minimize rate shock for NMU's customers and contribute to rate stability. Under NMU's current practice of recovering producer demand costs from firm sales and interruptible sales customers, the latter customers are experiencing average rate increases of $4800 per year. Logic supports the notion that interruptible customers, who by definition have an alternative means of obtaining gas supply, may migrate from the NMU system as a result of this level of rate increase. It is also reasonable to presume that, after migration of interruptible customers takes place, fewer customers will be available to absorb fixed costs, and costs to firm customers will rise.

Because NMU incorrectly implemented 1996 gas rates, resulting in significant underrecovery, it is hard for the Company to support its argument that it can sustain a $4800 increase for interruptibles without losing customers off the system through rate shock. The Department has offered data which indicates that NMU's corrected rate would have been *higher* than the spot-market price in all three months in which the Company provided data. The Department also questioned the accuracy of the market price "comparables" offered by NMU to support its theory that its present interruptible rate is properly placed just below market rate. Given the uncertainty of the evidence presented by NMU, the Commission finds that the Company failed in its burden of supporting the requested rate design change.

For these reasons, the Commission will deny NMU's request for a rate design change to recover producer demand costs in the commodity component from firm sales and interruptible sales

[1] In the Matter of a Petition from Peoples Natural Gas Company, a Division of UtiliCorp United, Inc., for a Variance from Minn. Rules, Part 7825.2700, Subpart 5, ORDER GRANTING VARIANCE WITH CONDITION (March 13, 1995) and ORDER DENYING REQUEST FOR RECONSIDERATION (August 8, 1995).

[2] Pipeline demand costs should be distinguished from producer demand costs, the subject of the instant petition.

customers.

ORDER

1. The Commission grants NMU's request to restore its TFF level. NMU shall include the undercharge of $80,795 for November and December, 1996, in the 1997 true-up, and identify the recovery separately in the true-up. NMU shall not collect interest for the undercharge.

2. The Commission grants NMU's requests for changes in its FDD reservation, FDD capacity, and SMS levels.

3. The Commission grants NMU a variance from Minn. Rules, part 7825.2910, sub. 2.

4. The Commission denies NMU's request for permission to collect producer demand and upstream pipeline costs in the commodity component of gas rates.

5. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

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