

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Gregory Scott	Chair
Edward A. Garvey	Commissioner
Marshall Johnson	Commissioner
LeRoy Koppendrayer	Commissioner
Phyllis A. Reha	Commissioner

In the Matter of the Petition of Otter Tail
Power Company to Implement Personal
Property Tax Savings Credit

ISSUE DATE: September 6, 2002

DOCKET NO. E-017/M-02-515

ORDER DIRECTING REFUND AND RATE
REDUCTION, WITH ASSOCIATED
COMPLIANCE FILINGS

PROCEDURAL HISTORY

On April 11, 2002, Otter Tail Power Company (OTP or the Company) filed a petition proposing to implement personal property tax savings credit of \$236,140 for 2002, with 49.75 percent allocated to Minnesota customers using the revenue method. OTP proposed the refund as a one-time credit on August bills as a separate item.

On May 6, 2002, the Department of Revenue supplied its letter certifying that the tax reduction on generating machinery is \$517,360.76 rather than the \$236,140 figure proposed by OTP in its April 11, 2002 filing. Revenue indicated that amount is to be divided among the states and between customer classes in accord with Commission policies.

On June 10, 2002, Minnesota Energy Consumers (MEC) urged the Commission to use its statutory authority to lower the Company's rates by their total property tax reduction, i.e. on their reduction in property taxes on transmission and distribution assets, as well as generation assets.

On June 12, 2002, the Minnesota Department of Commerce (the Department) filed comments, recommending approval, with modifications.

On June 24, 2002, OTP filed Reply Comments.

The Commission met on July 25, 2002 to consider this matter.

FINDINGS AND CONCLUSIONS

I. OTP'S PROPOSAL

In a plan filed before the Department of Revenue certified the amount of the Company's tax reduction on generating machinery and before the legislature clarified certain aspects of Minn. Stat. § 216B.1646 during the 2002 legislative session, OTP proposed a one-time personal property tax savings credit, 2002 tax savings of \$236,140, with 49.75 percent allocated to the Minnesota customers. OTP proposed to develop the refund rate per revenue dollar using calendar year 2001 retail revenues and to use the revenue method to allocate tax savings to eligible customers, i.e. active retail customers as of March 1, 2002. OTP stated that if the Commission determined that the refund required by the statute was to be on going, it would use a tax tracker to account for any over- or under-crediting.

II. DEPARTMENT OF COMMERCE COMMENTS

The Department recommended modifications to the jurisdictional allocation and customer allocation percentage, but later accepted the Company's proposed revenue method for customer allocation. The Department also recommended that seasonal customers be included in the refund, that OTP take action to begin implementing an on going reduction, and that OTP file a report 30 days after the completion of the refund.

III. OTP'S RESPONSE TO THE DEPARTMENT'S RECOMMENDATIONS

Responding to the Department's recommendations, OTP

- did not object to the Department recommendation that the Company use the 52.7 percent allocation to Minnesota customers that was developed in OTP's most recent rate case;
- opposed the Department's recommendation to return the whole amount of the generation refund to Minnesota retail customers, arguing that it is inappropriate to require OTP to refund more to Minnesota customers than the ratio of tax expense allocated to Minnesota customers;
- opposed the Department's recommendation that the refund should go to all customers receiving service in 2001 but offered to use another date instead of March 1 such as July 1 or the date of the Order;
- opposed being required to refund property tax reductions related to transmission and distribution proper, noting that the statute has been clarified to make any such refunding voluntary;

- agreed to making a report of the refund within 30 days of completion of its proposed refund in this proceeding; and
- recognizing that under the terms of the amended statute the property tax reduction is to be an on going reduction in rates, OTP proposed to make a separate filing to propose a method to implement the on going rate reduction.

IV. MEC'S RECOMMENDATIONS

MEC recommended that the Commission require OTP to refund and lower rates by the total reduction in property taxes (generation, transmission and distribution). MEC presented several arguments in support of its recommendation, including the following:

- While the statute might not require a lowering of rates for the tax savings associated with transmission and distribution, the statute does not prohibit the Commission from ordering the lowering of rates for the reductions in property taxes associated with transmission and distribution.
- The Commission has great latitude in making rate decisions. The Commission must consider a reasonable return for the utility in establishing a rate for consumers reflecting the cost of service. The interests of the utility must be fairly balanced with the interests of the ratepayers. The utilities' tax liabilities must be taken into account.
- Until the utilities demonstrate a rate increase is necessary, any surpluses that are above and beyond what the Commission originally contemplated when it set the rate should be returned to ratepayers. The Commission should distinguish between those profits derived from economic efficiency and productivity, and those profits resulting from a legislative windfall.
- Any doubt as to the reasonableness of rates should be resolved in favor of the consumer. Minn. Stat. § 216B.03.

V. COMMISSION ANALYSIS AND ACTION

At the outset, the Commission clarifies that the proposal before the Commission is for a part of the refund requirements of Minn. Stat. § 216B.1646, i.e. the lump sum refund for 2002. The refund for 2002 will begin within 60 days of this Order. The Company will provide customers with notice of the refund and, within 30 days of completing the refund, will file a report detailing the amounts refunded and any remaining balances.

To return the tax reduction amount in future years, OTP will be required to file no later than September 15, 2002 new rates to go into effect January 1, 2003, calculated based on the decisions in this Order. The Company will provide notice to its customers of this rate change and should include a copy of its proposed notice with the September 15, 2002 filing.

The Commission will now discuss clarifications of and exceptions to the Company's proposal and parties' comments. OTP will incorporate the Commission's decisions on these several issues into its lump-sum refund and new rates proposal.

A. Refund Generation Tax Reductions Only

Any question whether the legislature intended Minn. Stat. § 216B.1646 to require refund of personal property tax reduction amounts realized with respect to distribution and transmission as well as generation were fully resolved in the negative by the 2002 Legislative Session, which amended the language of Minn. Stat. § 216B.1646, effective July 1, 2001.

MEC accepted that the amended language of Minn. Stat. § 216B.1646 clearly does not require utilities to refund their distribution and transmission-related personal property tax reductions. MEC also acknowledged that, at first blush, its request for the Commission to require OTP to refund their distribution and transmission-related personal property tax reductions may appear to be a request to adjust rates based on a single issue. Nevertheless, MEC argued, the Commission can and should require OTP to refund such amounts. MEC argued that its request is supported by the will of the legislature and the public policy purposes underlying the regulation of Minnesota's utilities.

The Commission has carefully considered MEC's arguments and is not persuaded by them. In addition to clearly not *requiring* refunds beyond generation-related tax reduction, the statute goes on to characterize the utility's refund of any additional tax reductions (i.e. reduction due to lower taxes on transmission and distribution) as "*voluntary*" on the part of the utility. In using this language, the legislature has in effect restricted the Commission from ordering refunds for more than the generation-related tax reductions.

Viewed in light of this clear and specific indicator of legislative intent regarding transmission and distribution-related property tax reductions, MEC's arguments based on more general sources of the Commission's statutory authority (Minn. Stat. §§ 216B.01, .08, and .03) are unavailing. In addition, the Commission follows the traditional ratemaking principle that rates set in the Company's rate case are unaffected by various subsequent cost increases and decreases and remain at that level until there is a showing that the rates have become unreasonable. The record in this matter does not indicate that this is the case.

Further, MEC's argument that the utilities should be required to pass through all the tax savings because, MEC asserted, they agreed to do so during the 2001 legislative session to legislative language does not control. Instead, the Commission is guided by the legislative language actually adopted by the legislature and by traditional ratemaking principles cited previously.

B. Jurisdictional Allocator

Rates for OTP have been established in the past as if the Company operates one system covering portions of Minnesota, North Dakota, and South Dakota. Consistent with that approach, operating costs such as OTP's Minnesota personal property tax liability on generation have been allocated between the states and the rates set for and paid by OTP's customers in North Dakota, and South Dakota, therefore, have been recovering portions of that cost.

Despite the fact that Minnesota ratepayers had not been paying 100% of OTP's Minnesota personal property tax liability on generation, the Department recommended that OTP should be required to return the entire amount saved due to the reduced personal property tax on generation. The Department argued that this was appropriate because the property tax in question 1) is on property located in Minnesota, 2) is payable to the State of Minnesota, and 3) is on generation plants that largely serve Minnesota customers. Further, the Department noted, the Company is likely to keep the tax reductions related to transmission and distribution.

The Commission is not convinced by these arguments. The Commission believes that it would be inappropriate to give to Minnesota ratepayers tax savings related to taxes that were allocated to and paid by customers in other jurisdictions.

The Department also indicated, however, and OTP has agreed, that if any jurisdictional allocator were approved it should be the allocator approved in the Company's most recent rate case. This allocator was used in determining the property tax amounts payable by the various state jurisdictions. Adoption of this allocator increases the tax savings for Minnesota ratepayers by \$15,262, thereby bringing the refund amount to \$272,649.

C. Eligible Customers

1. Eligibility Date

The Commission finds that OTP's original proposal to refund only to customers receiving service on March 1, 2002 unreasonably excludes seasonal customers, customers who have borne their share of the burden of the now-reduced property taxes. At the same time, the Commission agrees with OTP that the Department's proposal that the Company be required to refund to all customers who received service in 2001 would be burdensome and, as a practical matter, would leave a large amount unrefunded because many customers have left OTP's system since then. In addition, a date in 2002 appears consistent with the statute, which directs a refund retroactive to January 1, 2002 and relates to the tax payable in 2002.

Subsequently, OTP proposed to use a date in 2002 other than March 1, 2002, such as July 1, 2002. The Commission finds that the Company's proposal is reasonable and is inclined to allow the Company to use its discretion to select an eligibility date in 2002, provided it chooses a date that does not effectively eliminate seasonal customers from receiving a refund.

2. Competitive Rate Customers

OTP's refund proposal makes competitive rate customers under Minn. Stat § 216B.162 eligible for a refund. This conflicts with the Commission's decision on this subject in Minnesota Power's property tax refund docket. In that docket, the Commission decided that competitive rate customers should not share in the tax-reduction because, unlike other customers, competitive rate customers rates were not calculated to recover property taxes.¹

In this case, however, OTP's failure to exclude competitive rate customers from the refund makes little practical difference since the load on OTP's competitive rate (part of the load of one customer) is so insignificant. In these circumstances, rather than complicating and possibly delaying the refund, the Commission will not require OTP to resubmit a plan to eliminate the one-time competitive rate-related refund. The Commission will, however, direct OTP to achieve this exclusion in calculating the on going rate reduction since there is no assurance that usage of the competitive rate will remain at this relatively insignificant level.

ORDER

1. Within 60 days of this Order, OTP shall begin its proposed lump-sum refund for the year 2002 for the tax savings associated with its generation machinery. To determine the customers eligible for the refund, the Company may restrict refunds to customers receiving service as of July 1, 2002 or as of any other date that includes seasonal customers.
2. The Company shall calculate the refund amount and shall allocate it between the customer classes based on the decisions made in this Order. See discussion at pages 4-7 above.
3. Along with its lump-sum refund, the Company shall include a notice to customers explaining the refund.
4. Within 30 days after completing the refund, OTP shall make a compliance filing with the Commission and parties detailing the amounts refunded by class and any remaining balances.
5. No later than September 15, 2002, OTP shall file with the Commission and parties tariff pages reflecting the new rates calculated based on the decisions in this Order (see pages 3-6, including the decision to exclude competitive rate customers from the on-going rate adjustment as discussed on page 6) and targeted to become effective January 1, 2003. The Company's filing shall include a proposed notice to customers about the rate reduction.

¹ See *In the Matter of the Petition of Minnesota Power to Implement Personal Property Tax Savings Crediting Methodology*, Docket No. E-015/M-01-1957, ORDER DIRECTING RATE REDUCTION AND REQUIRING FURTHER FILING (May 29, 2002) at page 3.

6. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

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