

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE
MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of the Petition of CenterPoint Energy Minnegasco, a Division of CenterPoint Resources Corp., for Authority to Increase Its Natural Gas Rates in Minnesota

**FINDINGS OF FACT,
CONCLUSIONS, AND
RECOMMENDED ORDER**

This matter came on for evidentiary hearing before Administrative Law Judge Richard C. Luis on February 18, 2005 in the Large Hearing Room at the offices of the Public Utilities Commission in St. Paul, Minnesota. Public hearings were held by videoconference on December 2, 2004, between St. Paul, North Mankato, and Willmar.^[1] Additional public hearings were held in Bloomington on December 8, 2004; Minneapolis (Hennepin County Government Center) on December 13, 2004; and Coon Rapids on December 15, 2004.

Due to the interest in this proceeding by persons not able to attend the first Minneapolis public hearing, an additional public hearing was scheduled for the evening of January 12, 2005. This hearing was conducted at the Sabathani Community Center in Minneapolis to afford opportunities for low-income persons to attend and provide testimony.

At the conclusion of the evidentiary hearing, a briefing schedule was established. Posthearing briefs were filed on March 9, 2005, and reply briefs were filed on March 15, 2005. The hearing record closed on March 15, 2005.

Eric Swanson, Attorney at Law, Winthrop & Weinstine, 225 South Sixth Street, Minneapolis, MN 55402; Tracy Bridge, Director of Government and Public Relations, CenterPoint Energy, 800 LaSalle Avenue, Minneapolis, MN 55402; and Brenda Bjorklund, Director, CenterPoint Energy Law Division, 800 LaSalle Avenue, Minneapolis, MN 55402, appeared for CenterPoint Resources Corp. (CenterPoint or the Company).

James Strommen, Attorney at Law, Kennedy & Graven, 200 South Sixth Street, Suite 470, Minneapolis, Minnesota 55402, appeared for the Suburban Rate Authority (SRA).

Julia Anderson and Karen Hammel, Assistant Attorneys General, NCL Tower, Suite 1400, 445 Minnesota Street, St. Paul, Minnesota 55101, appeared for the Minnesota Department of Commerce (Department).

Ron Giteck, Assistant Attorney General, NCL Tower, Suite 900, 445 Minnesota Street, St. Paul, Minnesota 55101, appeared for the Minnesota Office of the Attorney General-Residential Utilities Division (OAG-RUD).

Lon Stanton, Government Affairs Manager, 1650 West 82nd Street, Suite 1250, Minneapolis, Minnesota 55431, appeared on behalf of Northern Natural Gas (Northern).

Sandra Hofstetter, 10157 Ivywood Court, Eden Prairie, Minnesota 55347, appeared on behalf of the Minnesota Chamber of Commerce (Chamber).

Robert Harding, Jerry Dasinger, Stuart Mitchell, Clark Kaml and Kate Kahlert, 121 Seventh Place East, Suite 350, St. Paul, Minnesota, appeared on behalf of the Staff of the Minnesota Public Utilities Commission (Commission).

NOTICE

Notice is hereby given that, pursuant to Minn. Stat. § 14.61, and the Rules of Practice of the Minnesota Public Utilities Commission (“Commission”) and the Office of Administrative Hearings, exceptions to this Report, if any, by any party adversely affected must be filed according to the schedule which the Commission will announce. Exceptions must be specific and stated and numbered separately. Proposed Findings of Fact, Conclusions and Order should be included, and copies thereof shall be served upon all parties. Oral argument before a majority of the Commission will be permitted to all parties adversely affected by the Administrative Law Judge’s recommendation who request such argument. Such request must accompany the filed exceptions or reply (if any), and an original and 15 copies of each document should be filed with the Commission.

The Commission will make the final determination of the matter after the expiration of the period for filing exceptions as set forth above, or after oral argument, if such is requested and had in the matter.

Further notice is hereby given that the Commission may, at its own discretion, accept or reject the Administrative Law Judge’s recommendation and that said recommendation has no legal effect unless expressly adopted by the Commission as its final order.

Under Minn. Stat. § 216B.16, subd. 1a, if the Commission rejects or modifies the Settlement between the Department and the Company, this matter may be extended by 60 days for conclusion of this proceeding.

STATEMENT OF ISSUES

CenterPoint and the Department, either through investigation and responsive testimony, or through a Settlement, a copy of which is in the record that accompanies this Report, have resolved all the issues between them in this matter. The OAG-RUD entered into a separate agreement regarding the exclusion of certain dues expenses

from the rate calculation. OAG-RUD and SRA declined to participate in the Settlement with regard to the following issues:

- Does the agreed-upon change in the residential basic charge unfairly burden low-income, low-usage residential customers, cause rate shock, or discourage conservation contrary to the public interest?
- Should the residential basic charge be retained at the current level of \$5.00 and the remaining revenues allocated to the residential class be derived from adjustments to the delivery rate?

Except for these issues, OAG-RUD and SRA do not oppose the Settlement.

Based on all the proceedings herein, the Administrative Law Judge makes the following:

FINDINGS OF FACT

A. Jurisdictional-Procedural Background

1. On July 14, 2004, CenterPoint filed a Petition with the Commission, under Minn. Stat. § 216B.16, for an increase in natural gas rates of \$21,722,000 (over all, approximately a 1.8 percent increase over the test year (current rates)). CenterPoint also filed a Petition for Interim Rates in the amount of \$16,869,000 (a 1.4 percent increase).^[2]

2. On September 7, 2004, the Commission issued an Order accepting the filing as complete as of August 9, 2004 and suspending the proposed rate increase until the Commission has determined the reasonableness of the proposed rates.^[3] Also on that date the Commission issued a Notice and Order for Hearing, directing that a contested case hearing be convened to determine the reasonableness of the rate changes proposed by CenterPoint.^[4]

3. On September 10, 2004, the Commission issued an Order setting interim rates, authorizing CenterPoint to collect \$16,869,000 in additional annual revenues effective October 1, 2004. CenterPoint is collecting interim rates subject to refund if the interim rates are in excess of the final rates determined by the Commission.^[5]

4. On September 17, 2004, a prehearing conference was held before Administrative Law Judge Richard C. Luis in St. Paul, Minnesota. Petitions to Intervene were filed by and granted to the SRA.^[6] Subsequently, Northern petitioned to intervene and was admitted. The Chamber requested admission to the proceeding as a nonparty participant and was admitted on that basis.

B. Description of the Company

5. In 1997, the Commission approved a merger between the NorAm Energy Corporation (NorAm) and Houston Industries, Inc. (HI). CenterPoint Energy was then a

division of NorAm. HI changed its name to Reliant Energy Inc. in 1999. After a restructuring to spin off unregulated businesses in 2002, the regulated businesses began operating under the name of CenterPoint Energy, Inc. (CNP). CenterPoint Resources Corporation (CPRC) is a wholly-owned subsidiary of CNP.^[7]

6. CenterPoint operates the natural gas utility service known as Minnegasco in Minnesota as a division of CPRC.^[8] In addition to Minnesota, the parent corporation provides natural gas distribution services in Arkansas, Louisiana, Mississippi, Oklahoma, and Texas that serves approximately 5 million customers. The parent corporation's headquarters are located in Houston, Texas.^[9]

7. CenterPoint distributes natural gas to over 750,000 customers in Minnesota. The Company's natural gas service territory encompasses a large part of central and southern Minnesota, including Minneapolis and its northern, southern and western Suburbs. CenterPoint also operates an unregulated energy services business, Home Service Plus®, which offers repair and maintenance for a variety of heating ventilation and air conditioning (HVAC) and other appliances.^[10] The Company's last rate increase in Minnesota was granted in 1996.^[11]

C. Natural Gas Service Areas

8. CenterPoint's natural gas customers are divided between two service areas, denominated the Northern Service Area and the Viking Service Area. These two service areas have historically had modestly different rate structures. The Northern Service Area includes the City of Minneapolis. The Viking Service Area covers portions of the state away from the metropolitan area.

D. CenterPoint Capital Structure

9. Since CenterPoint is a division of a subsidiary, the Company lacks a readily defined capital structure. In similar circumstances, a hypothetical capital structure has been substituted for the assessment of proposed rates.^[12] For the purposes of this rate proceeding, CenterPoint originally proposed the following capital structure:

Minnegasco Proposed Capital Structure

Long-Term Debt	46.17%
Short-Term Debt	3.56%
Common Stock Equity	50.27%

CenterPoint was the only party to file a proposed capital structure.

10. The Department and the Company agree that the capital structure shown in the table in the preceding Finding is appropriate, and urge its adoption.

E. Existing Rate Structure

11. Prior to approval of CenterPoint's interim rate, the Company's natural gas rate structure consisted of the wholesale cost, basic charges, and a delivery rate. The basic charge and delivery rate constitute the delivery charge portion of the customer bill. The wholesale cost to CenterPoint for the natural gas sold to customers is passed through in customer bills without markup. Thus, the delivery charge must account for CenterPoint's costs of providing natural gas service and CenterPoint's return.

Basic Charge

12. The basic charge is the amount paid monthly by any customer connected to CenterPoint's gas distribution system. This charge is paid independent of gas usage. For residential customers in the Northern Service Area (Northern customers), the charge is \$5.00 per month. For residential customers in the Viking Service Area (Viking customers), the charge is \$6.00 per month. For commercial classes of customers in both Northern and Viking areas, the customer basic charge is accompanied by a basic transportation service charge ranging from \$106 to \$300 per month, depending on customer class and service area.^[13]

Delivery Rate

13. The remaining portion of the customer bill is the delivery rate. This charge is calculated by multiplying the therms in the natural gas purchased by an established rate.^[14] For Northern customers, the current rate is \$0.12857. For Viking customers, that rate is \$0.10236.^[15] Commercial classes pay a rate (with one exception) ranging from \$0.11025 to \$0.04571. The exception is for large general service customers which pay a demand peak rate of \$0.43405 (Northern) or \$0.52324 (Viking).^[16]

F. Test Year

14. CenterPoint took the actual financial information for the calendar-year base period ending December 31, 2003 as the basis for projecting a test year for the proposed rates. Adjustments were made to remove out-of-period expenses, conform to a normal operating year, address known changes in operating conditions, and correct for inflation. The year ending on September 30, 2005 was used as the projected test year.

15. Heat sensitive sales account for approximately 70 percent of total sales in the test year.^[17] CenterPoint used a ten-year rolling average to derive the temperatures to be applied in the test year. The previous rate matter, conducted in 1995, had used a 20-year rolling average. The 34-year period from 1970 through 2003 showed a statistically significant mean reduction in heating-degree days (meaning the temperature was warmer) over the last decade.^[18] Applying a five-year rolling average would have resulted in an even lower mean number of heating-degree days. The 10-year rolling average provided a more accurate measure of heating-degree days than the 20-year average.^[19] CenterPoint has shown that using a 10-year rolling average is suitable for forecasting temperature-sensitive sales.

G. Test Year Revenue, Expenses and Operating Income

16. The Department and the Company agree that the appropriate test year expenses are \$1,144,783,000 and that the forecast test year operating revenue is \$1,180,936,000, resulting in an operating income of \$36,153,000.^[20]

H. Customer Cost of Service Study

17. In preparation for this rate application, CenterPoint conducted a customer cost of service study (CCOSS). The CCOSS analyzed CenterPoint's administrative and operating costs and attempted to associate identifiable costs with the particular class of customer triggering the cost. The Department filed testimony on the CCOSS studies submitted by the Company, and accepted them. The parties propose that the PUC accept CenterPoint's CCOSS studies.^[21]

18. Based on its CCOSS, CenterPoint concluded that the monthly cost of serving the General Service (Residential and Commercial) customers was \$16, and proposed that amount as a customer charge for the class in its initial filing.^[22]

I. Initial Rate Proposal

19. The Company initially proposed an overall rate increase of 1.8% (\$21,772,000), including a 4.1% increase in rates for the Residential Class.^[23]

J. Summary of Public Comments

20. Substantial public comments were received from attendees at the public hearings, and persons who mailed (or emailed) their written comments. All of those comments have been read and this summary is provided as a representative sampling of those comments.

21. Vincent Guertin, Business Manager for the International Brotherhood of Electrical Workers, Local 949 (IBEW), supported the proposed rate increases. IBEW noted that CenterPoint had not had a rate increase in nine years. Anita Roy, Business Manager for Office & Professional Employees International Union, Local 12 (OPEIU), supported the rate increase as an investment that would result in greater stability for CenterPoint. Michael Everetts, President of Gas Workers Local 340 (GW), also supported the rate increase. IBEW, OPEIU, and GW represent CenterPoint employees.

22. A number of low-usage residential customers commented, either in person or in writing, on the impact of the proposed increase in the basic charge. For one apartment dweller only using natural gas for cooking, the proposed change would increase the monthly bill from approximately ten dollars to twenty dollars. One such comment noted that the \$16.00 basic charge and reduced delivery rate would result in an increase of \$77.00, compared to the CenterPoint estimate of \$38.00 for the average user. A number of commentators objected to the "average" designation, since the methodology tends to obscure the impact on low-usage customers.

23. CenterPoint Energy was represented by Tracy Bridge, Director of Government and Public Relations, at all five public hearings. Mr. Bridge testified in a consistent manner at all hearings. The proposed rate increase for new natural gas distribution by CenterPoint Energy would be the first increase in nine years. CenterPoint Energy seeks to increase revenues by \$21.77 million annually, which is 1.8 percent of the total revenue of approximately \$1.2 billion. Because this increase only affects the costs of providing distribution, only 10 to 30 percent of a typical customer's bill is affected.

24. The Office of the Attorney General (OAG) was represented by Ron Giteck, an Assistant Attorney General in the Residential and Small Business Utilities Division, and Curtis Nelson, a Financial Analyst. The OAG expressed concern regarding the proposed rate increase, which would increase rates relating to non-gas costs of residential customers about 20 percent and decrease rates for big business customers about 18 percent. Specifically, the OAG is concerned that business customer rates will decrease at the expense of residential customer rates. Further, the new rate design will likely increase rates. Under the proposed change, an increase in the customer charge from \$5 to \$16 a month for residential customers, along with a decrease in the usage charge to approximately 3.8 cents would result in a 20 percent rate increase for residential customers. Finally, the proposed highway construction rider that would allow recovery of costs associated with road construction, is of concern to the OAG.

25. The OAG referred the public to its written testimony, which proposes that business class rates should increase by the same percentage as residential customers. Further, the customer charge should remain at \$5 and any increase should be through the variable usage base charge. Finally, the proposed highway construction rider would be inconsistent with traditional rate making concepts and should not be allowed.

26. The Department of Commerce (DOC) was represented by Michelle St. Pierre, Sundra Bender, Jason Bonnett, Vince Chavez, Sachin Shah, Bryan Minder, and Dr. Marlon Griffing. The testimony from the DOC representatives was consistent throughout the public hearings. In essence, the Department's presentation at the public hearings was that it represents the interests of all ratepayers in utility proceedings before the PUC. The DOC was investigating CenterPoint Energy's request for an increase of approximately \$21.7 million to cover non-gas costs. The DOC realizes that any increase in rates imposes a burden on customers and works to ensure that customers pay only for reasonable costs of providing service while preserving the company's financial viability so that it can continue to provide safe, reliable natural gas service.

27. The videoconference in St. Paul obtained testimony from members of the public in Willmar and North Mankato on December 2, 2004. Brainerd was to participate in the hearing, but no members of the public were present. Present in St. Paul were representatives from CenterPoint Energy, the DOC, and the OAG. Several members of the general public were in attendance in Willmar and Mankato.

28. Concerns from the public were in opposition to a residential rate increase. Mr. Bridge responded to the concerns raised by the public. In addition, the OAG and the DOC elaborated on some of those concerns. Lowell James, from Mankato, was opposed to any rate increases, especially the customer charge because people use different amounts of natural gas or therms.

29. Carolyn Gilbertson, from Willmar, inquired why a business would be charged less when they likely use more therms. Ms. Gilbertson was concerned that residential customers could experience rate shock. She suggested businesses should pay for any recovery costs.

30. Eugene Krueger, from Willmar, was opposed to any rate increases. In addition, Mr. Krueger questioned the methodology used to measure therms because the gas meters read in cubic feet.

31. Approximately 25 people attended the proceedings on December 8, 2004 at the John F. Kennedy High School in Bloomington. Representatives from CenterPoint Energy, the DOC, the OAG, and the PUC were in attendance. Handouts were distributed to the public regarding the Cold Weather Rule.

32. Franz Riesterer, from Apple Valley, expressed concern that residential customers who practice conservation measures to keep their usage low would experience unfair rate increases. Mr. Riesterer stated that he actively conserves energy, is a low-use customer, and that his rate increase would be greater than customers who use more energy. Mr. Riesterer submitted written testimony.

33. Marcy Weaver, from Burnsville, stated that small residential users would be unfairly burdened compared to commercial and industrial users. Further, according to available handouts, large-use customers would see smaller rate increases than low-use customers.

34. James Oerichbauer, from Apple Valley, questioned whether the model used for residential customers was inaccurate because it overestimates the amount of therms used. Further, residential customers were not provided any information regarding the need for additional revenue. Finally, the average percentage increase for residential customers would be higher than estimated.

35. Jim Kleven, from Minneapolis, stated that there have been periods where he does not use any natural gas, but must pay the customer charge of \$5. Mr. Kleven opposes the increase of the customer charge to \$16.

36. Peter Freund, from Bloomington, stated that the proposed increase is anti-conservation and a burden on the poor and the elderly. Overall, residential customers would be burdened unfairly.

37. Cindy Lavorato expressed concerns regarding public policy. Specifically, residential customers would not be as encouraged to practice conservation measures due to the increase in the customer charge. Ms. Lavorato concluded that CenterPoint

Energy's new rate design proposal is unfair and a large departure from past practices. She urged the Commission to disapprove it.

38. Approximately 17 people attended in Coon Rapids on December 15. Mike Krueger argued that by increasing the customer charge, customers who are energy efficient would be penalized. Mr. Krueger questioned the need for an increase. In addition, Mr. Krueger expressed concern regarding the fairness of reading meters in cubic feet instead of therms.

39. Alvin Keding, from Big Lake, opposed the customer charge because not only does it place the burden on low-use customers, those same customers must also pay for increases that are passed on by businesses. Any rate increase should be applied evenly to residential and commercial customers. Mr. Keding claims that CenterPoint Energy inflated its average use figures for households and questioned who will pay for the gas used by commercial customers. Residential customers will be forced to pay the increased costs for energy assistance if more low income customers enroll in that program, either through higher taxes or some other means.

40. Sandra Hofstetter, representing the Minnesota Chamber of Commerce (Chamber), gave oral testimony and offered a written statement. The Chamber represents business customers, both small and large, in the state of Minnesota. As such, the Chamber has an interest in the outcome of these proceedings. The Chamber supports a rate structure that closely reflects the cost of providing the service. The Chamber also believes that, to the extent they exist, implicit subsidies should be eliminated or at least made explicit in the rates. Finally, the Chamber believes these pricing objectives send appropriate signals to consumers and will ultimately encourage energy conservation.

41. Two public hearings were held in Minneapolis. The first hearing was held in the afternoon on December 13, 2004, at the Hennepin County Government Center in Minneapolis. Approximately 21 people attended the daytime hearing. The second hearing was held in the evening on January 12, 2005, at the Sabathani Community Center, to accommodate members of the public who were not available during the daytime. Approximately 40 people attended the evening hearing. Representatives from CenterPoint Energy, the DOC, the OAG, the PUC, and the Suburban Rate Authority were present at both hearings. Several handouts were available: a rate case fact sheet; an interim rate fact sheet; a booklet entitled More Comfort, Less Energy; a budget plan brochure; and a energy audit brochure.

42. Annie Young testified on December 13, 2004, on behalf of the Phillips Community Energy Cooperative (PCEC), which is comprised of 2,000 members in the Phillips community. Its mission is to promote energy conservation within the Phillips neighborhood and help its members reduce the burden of their energy bill on their already limited incomes. The position of the Phillips Community Energy Cooperative is that the proposed rate increase is unfair and dramatically shifts costs to residential customers while actually lowering costs for large companies. In addition, this rate shock will disproportionately affect families that are already struggling in an uneven economy.

Public policy should decrease the impact of rising energy prices on families, not increase the impact of those prices. Finally, PCEC is against the rate proposal because it would decrease consumers' incentive to conserve energy. Ms. Young points out that business customers have the ability to pass on any rate increases, while low-income customers cannot. Ms. Young stated that other comments will be submitted from the Phillips neighborhood.

43. Rochelle Scholz, from Minneapolis, stated that she would submit written testimony at a later date and expressed that the rate increase would be unfair. Ms. Scholz stated that the public hearings should be in the evening because people who work cannot attend hearings during the day.

44. Richard Bear questioned why the rest of the Public Utilities Commission was not present at the hearing. Mr. Bear expressed concern that low-income customers would be unfairly burdened by the increase in the customer charge. The infrastructure is already in place, and therefore, residential customers should not have to pay for distribution. Mr. Bear also asked if CenterPoint Energy has a monopoly in any states, whether the company invests in building any terminal sites for unloading liquid natural gas, and if so, whether any of the revenues resulting from the rate increase would be applied toward building additional terminals.

45. Nathan Bloom raised environmental concerns, including air quality and conservation of energy. For example, if an individual uses renewable energy sources and minimizes their use of natural gas, their gas bill would be too high compared to the amount used. By raising the customer charge, conservation or switching to renewable alternative energy sources would be discouraged. Low-use customers would see a disproportionately high increase compared to high-use customers.

46. Christine Ziebold, a pediatrician, is opposed to the rate increase because the price of natural gas has remained stable. Residential customers who consume the least amount of gas would be the most affected by the rate increase. Rate increases should be even across the board. Additionally, Minnesota should be using more renewable energy. Dr. Ziebold speculated that the interim rate increase indicated that this proposed rate increase will be approved despite public comment. Dr. Ziebold explained that residential customers did not receive adequate notice of the proposed rate increase -- only a very small flier in the bill and no information was available on CenterPoint Energy's website. Dr. Ziebold was pleased that there are six public meetings, but expressed disappointment that the meeting in Minneapolis was held during working hours.

47. Orell Jensen, from Northeast Minneapolis, is a renter and only uses gas for cooking and hot water. Ms. Jensen expressed concern that more low-income customers will have to go on assistance if the rates were increased and questioned whether there was an adequate source of funding to pay for all the customers who need assistance.

48. Shanili Gupta, from PCEC, asked if dates and details of the process for this rate case were posted on a website. Ms. Gupta inquired whether there will be an additional hearing in Minneapolis to accommodate members of the general public who are unable to attend hearings during the day.

49. Annie Young appeared also at the Sabathani hearing on behalf of the Phillips Community Energy Cooperative. Renters make up 78 percent of the housing demographic in the Cooperative's area and one third of the population is estimated to have household incomes below the poverty line. PCEC maintains that the proposed basic charge will unfairly impact renters and owners of smaller homes by increasing their share of the overall cost of service. PCEC noted that the highest basic charge in Minnesota is \$6.50.^[24]

50. The Suburban Rate Authority intervened in this case and Attorney Jim Strommen spoke on its behalf on January 12, 2005. The Suburban Rate Authority is a joint powers organization consisting of 34 suburban municipalities in the Twin Cities area. Mr. Strommen raised concerns that the rate increase would fall exclusively on the residential and small business ratepayers, primarily due to the customer charge increase from \$5 to \$16 per resident and the increase to the residential and small business customers of 4.1 percent while business customer rates are decreased. In addition, Mr. Strommen questioned the accuracy of government-imposed relocation costs.

51. Spencer Blaw, board member of the Minneapolis Tenants Union, objected to the change in rate structure, due to its impact on low-income customers. Mr. Blaw also referred to an ongoing investigation into CenterPoint's activities regarding the Cold Weather Rule.^[25]

52. Susan Weinstock, National Coordinator on Economic and Utilities for the American Association of Retired Persons (AARP), stated two objections to the proposed rate changes. AARP opposed the overall increase in rates as unduly burdensome to consumers, especially low-volume users. The change in the basic charge (thereby increasing the share of overall costs borne by residential customers) was opposed by AARP. The commentator also questioned why the commercial customer classes were benefiting through decreases in their share of the overall cost allocation.

53. Dee Long appeared at the Sabathani hearing on behalf of Minnesotans for an Energy Efficient Economy (ME-3), a nonprofit policy organization working toward a fair, efficient, and sustainable energy future. ME-3 is opposed to the proposed rate increase because existing measures encouraging energy conservation and use of renewable energy would be compromised. Increasing the customer service charge by \$11 per month for residential use and reducing the amount of revenue derived through usage charges shifts the revenue obtained away from the volume consumed. ME-3 contends that this shift removes an incentive for residential customers to conserve energy and invest in energy-saving appliances and renewable energy technologies. An example cited by ME-3 is the state sales tax exemption for purchases of some high-

efficiency household goods. ME-3 maintains that the economic incentive to purchase these goods would diminish if the impact on the customer's bottom line was reduced. ^[26]

54. Chris Duffrin, Assistant Director of the Energy CENTS Coalition (Energy CENTS), testified at the Sabathani hearing. Energy CENTS is a statewide coalition of organizations that promote more affordable energy service for low-income and fixed-income Minnesotans through advocacy efforts, regulatory proceedings, and policy and program development. Energy CENTS expressed concern about the impact the proposed rate increase would have on low-income residential customers who conserve and use less natural gas than the average customer. The commentator suggested that 131,000 CenterPoint customers qualify for energy assistance, but do not receive that assistance. Energy CENTS maintains that low-income customers have already been hit hard by the substantial rise in natural gas prices and adding a substantial rate increase will only add to their burden. Energy CENTS proposed that customers on energy assistance should be exempt from an increase in the customer charge.

55. Energy CENTS estimated that the initially proposed increase would result in a 70.7 percent increase in the monthly bills of apartment dwellers (who do not pay for their own heating directly). The commentator questioned whether the proposed rate increase adheres to the intent of Minn. Stat. § 216B.03, which encourages conservation and discourages preferential treatment of a customer class. Energy CENTS opposed the proposed rate design due to its impact on low-income customers. Another suggestion was for new customers in the outer-ring suburbs to pay a higher percentage of the actual costs of new service connections in order to make the system more equitable and reduce subsidies received by that subset of residential customers. ^[27]

56. Sharon Morgan Spencer, of the Minneapolis Urban League, was present at the hearing as an advocate for poor, urban, low and middle income communities of Minnesota that are compromised mostly of people of color. Ms. Spencer raised concerns regarding the impact of the proposed rate increase on people of color, and opposed the rate increase. She maintained the proposed rate increase would not affect people proportionately nor encourage conservation.

57. Mary Busch, representing the Sierra Club's Clean Air Committee, agreed with the testimony of Dee Long regarding the impact on conservation. Ms. Busch urged CenterPoint Energy to revisit, but not reject, the proposed rate increase. The disproportionate impact on residential customers places a hardship on those families trying to sustain a living. Shifting the costs from large industrial customers to residential customers has a great impact on our children. Ms. Busch is a professional social worker and has been on the front lines trying to help people get their kids to school, and energy is very much a part of that. Having clean water to bathe in, clean clothes, and having the ability to sleep comfortably in a warm house all impact the ability of children to attend school, remain healthy, and be attentive. The Sierra Club would like to see the fees structured proportionately throughout the entire customer base.

58. Chris Nisan, a reporter for the *Minneapolis Spokesman* newspaper, had a follow up question at Sabathani regarding the number of customers who had their

service disconnected and whether CenterPoint Energy considered the impact of the rate increase on the those that had been disconnected. Kate Kahlert, a consumer complaint mediator with the PUC, responded that the Commission is informed when someone is disconnected during the cold weather season. Pam Marshall, Energy CENTS Coalition, also asked for clarification on the number of customers who were disconnected.

59. State Representative Neva Walker, representing the district that includes the Sabathani Center, questioned the timing of the disconnections of customers.

60. Hennepin County Commissioner Peter McLaughlin attended the hearing as Chair of the Phillips Community Energy Cooperative and submitted a petition signed by 103 of its members in opposition to the proposed rate increase to residential consumers. Commissioner McLaughlin highlighted that low-income customers also tend to use less energy and they will be unfairly burdened. Customers that live in small rental units would likely see a 67 percent increase in their distribution charge and about a 15 percent increase in their overall bill. The PCEC urged the Commission to reject the proposed rate increase.

61. Carl Nelson, energy project manager for The Green Institute and a staff person for PCEC, also urged rejection of the proposed rate increase. Mr. Nelson echoed the concerns of Commissioner McLaughlin and questioned some of the data presented by CenterPoint Energy regarding its estimate of the net increase. If a need for a rate increase is determined, it should be proportional among the different customer classes.

62. Gary Alexander inquired about the costs of distribution for new customers as a result of new construction in the suburbs and whether existing customers would be subsidizing the costs of installing new distribution.

63. Todd Reubold commented that in one of the handouts, customer usage had decreased due to conservation measures and other improvements. As a result, the proposed increase has the effect of penalizing those that employ conservation measures.

64. State Representative Keith Ellison, representing part of North Minneapolis (House District 58B), expressed concern over the effect of the rate increase on children in low-income households. Further, energy conservation and more advancement of renewable energy should be encouraged.

65. Over 75 written comments and emails were received. Three comments, all from labor unions mentioned earlier, favored the increase as proposed, stating the rate increase supports safe and reliable service. The remaining comments were in opposition to the proposed rate increase.

66. The majority of the written comments focused on two interrelated issues. Many low-income customers take measures to conserve energy and believe the proposed increase in the customer charge would negate those measures. Further, low-income and low-use customers would pay a disproportionate share because they are

using less natural gas, but their customer charge would be increased the same amount as residential customers who consume much more natural gas. Therefore, the proposed increase would discourage conservation measures and penalize low-use, low-income customers. Many commentators advocated to increase rates based on usage by increasing the cost per therm, not by increasing the customer charge. One commentator recommended an exemption for people who do not use natural gas as their primary heating source to promote alternative energy sources.

67. Many commentators noted that the increase in the customer charge would result in a percentage increase much higher than the estimated 4.1 percent. Most found that estimate to be approximately 19 percent.

68. Several commentators rented apartments and pay only for the natural gas used in cooking, which is minimal. The proposed rate increase would be unfair on renters who would likely see the largest percentage increase in their bill.

69. AARP commented that older Americans are particularly vulnerable because they spend a higher portion of their income on home heating costs. The proposed rate increase is unfair because it burdens residential customers while lowering rates for large-use businesses. The proposed rate increase discourages conservation and disproportionately increases the rates of low-use customers.

70. The Franklin Area Business Association opposed the proposed rate increase because small business owners would see an increase while large business owners would see a decrease. The increase to small business owners is unfair. One small business owner did not oppose the increase for residential customers, but opposed the decrease to large business customers because it would be at the expense of smaller business owners.

K. Department/CenterPoint Settlement

71. Prior to the hearing in this matter, the Department and CenterPoint comprehensively settled the issues between them. Any issues involving other parties not resolved by this settlement will be discussed in subsequent Findings. In general, CenterPoint agreed to reduce its overall revenue increase, from \$21,722,000 to \$8,987,000.^[28] The Department agreed that CenterPoint's residential basic charge could rise to \$8.00 per month. CenterPoint agreed to retain the existing customer class structure. The Department agreed to the proposed consolidation of the Northern and Viking services areas. Specifics regarding these and other parts of the settlement will be addressed in subsequent Findings.

Cost of Capital (Settlement)

72. The parties agreed that the initially proposed capital structure describing the hypothetical division between CenterPoint's long-term debt, short-term debt, and equity would be used for setting rates in this proceeding.^[29] CenterPoint originally requested a return on equity (ROE) figure of 11.25%. The Department proposed ROE of 9.79%. Each proposal was based on a range of results, relying on a discounted cash

flow analysis and a comparable group of companies. The differences arose from differing projections of growth rates and interest rates. The parties agreed to an ROE of 10.18%.^[30]

73. CenterPoint proposed that the long-term cost of debt be set for rate purposes at 6.17% and the short-term cost of debt be forecast as 1.77%. The Department's figures essentially agreed (the only differences being due to rounding methodology). The cost of capital agreements result in an overall cost of capital for CenterPoint of 8.03%, derived as follows:

Cost of Capital Calculation			
<u>Component</u>	<u>Percent of Total</u>	<u>% of Cost</u>	<u>Weighted Average</u>
Long-Term Debt	46.17%	6.17%	2.85%
Short-Term Debt	3.56%	1.77%	0.06%
Common Stock Equity	50.27%	10.18%	5.12%
Total			8.03% ^[31]

Rate Base (Settlement)

74. Due to anticipated additions to plant and some extraordinary expenditures late in the test year, CenterPoint maintained that using an end-of-year plant balance for calculating the rate base was appropriate. The Department disagreed with this methodology, asserting that the recognized method for calculating plant balance was the average test-year balance. CenterPoint agreed to use the average test-year balance method, thereby reducing its rate base by \$17,637,824 and the associated property tax expense by \$1,049,984.^[32]

75. CenterPoint proposed that \$6,762,000 be included in its rate base for the cost of initial margins on forward contracts (for the purchase of natural gas). The Department agreed that the rate item was appropriate for inclusion in the rate calculation, but objected to the amount. The Department noted that CenterPoint had purchased no contracts for the 2004-2005 heating season and asserted that the item should be reduced by \$3,488,000. The parties agreed that only contracts purchased from April 2005 onward would be considered, that the average cost was \$6,750 per contract, and that the 13-month balance should be used. This calculation results in \$4,678,000 to be included in CenterPoint's rate base for the cost of initial margins on forward contracts.^[33]

76. Unamortized rate case expenses were proposed for inclusion in the rate base by CenterPoint. The Department disagreed with this approach, contending that some of the costs would occur outside of the rate year and the amount claimed was

overstated. The parties agreed to substitute carrying costs identified in a lead/lag study.^[34] The agreement reduced CenterPoint's rate base by \$539,145.^[35] The parties also agreed to use the lead/lag study figures to determine CenterPoint's working capital requirement.^[36]

77. The agreed-upon test-year rate base for CenterPoint totals \$516,076,000.^[37]

Revenue Items (Settlement)

78. CenterPoint forecasted that the total volume of natural gas delivered to customers would amount to 154,824,000 Dth in the test year.^[38] This forecast was based on 764,358 customers, with econometric modeling done for small service classes (residential and small commercial) and individual customer forecast sales for large volume customers.^[39] CenterPoint used eight years of customer data and the 10-year rolling average for weather. The Department generally agreed with the methodology, only asserting that its model was somewhat more accurate. The Department also proposed that sales to large volume dual fuel (LVDF) customers be reclassified as transportation. The parties agreed to use the Department's forecast and reclassify LVDF customers to the transportation category. These changes result in a net required revenue reduction of \$1,106,185.^[40]

79. Two transportation customers signed contracts with CenterPoint after this rate case was filed. The Department proposed, and CenterPoint agreed, to adjust the test-year operating revenues by increasing them by \$234,801 to account for the additional revenue obtained from these customers.^[41] CenterPoint also increased its test-year operating revenues to account for an additional \$14,795 in rental income.^[42]

80. CenterPoint originally proposed forecasting late fee revenue by taking the actual ratio of 2003 late fees to 2003 revenue and applying the percentage derived to the forecast test-year firm revenue. The Department agreed with the methodology, only suggesting an adjustment to account for the Department's estimate of lower revenue. CenterPoint noted that its actual 2004 late fee revenue was higher than that of 2003. The parties agreed to average the late payment fee percentage over the two years of actual revenues. This approach increased test-year revenue by \$177,798.^[43]

Expense Items (Settlement)

81. The parties' agreements on sales forecast and test-year plant triggered a decrease of \$12,547,369 to the anticipated cost of natural gas in the test year and a decrease of \$1,049,984 to the anticipated depreciation and property tax expenses. These changes were agreed to between the Department and CenterPoint.^[44]

82. CenterPoint initially proposed to recover \$1,891,001 for increased information technology (IT) expenses. The additional IT expenses arose from upgrading from existing computers and software (referred to as "legacy systems") to new computer systems with enhanced capabilities.^[45] The Department objected to the entire expense, asserting that the costs were not justified or were not appropriately

calculated. After providing supporting documentation for the IT upgrades and correcting some of the supporting calculations, the parties agreed to reduce the test-year IT expense by \$408,119 and reduce the test-year rate base by \$384,592.^[46]

83. Expenses for four marketing programs promoting energy efficiency were included in CenterPoint's proposed recovery. These programs were: residential water heaters, customer additions, food service, and commercial & industrial incentives (C&I). CenterPoint prepared cost/benefit analyses to support each of these programs. The Department suggested that a 50% baseline market penetration test be used to determine if natural gas was already being used by the persons being marketed. The Department also suggested that a societal benefits test be applied to assess the utility of these marketing programs.

84. CenterPoint responded that a baseline test was unnecessary as two of the programs were directed at areas with demonstrated low natural gas penetration. The parties agreed to disallow the customer additions program expenses and reduce the C&I and residential water heater programs. These reductions total \$664,844, leaving \$550,000 in the water heater program. The parties agreed that the resulting water heater marketing program cost passes the ratepayer test. The parties also agreed that the food service and adjusted C&I programs were recoverable expenses.^[47]

85. In its application, CenterPoint proposed pension expenses of \$4,902,965 before allocations. Centerpoint relied upon the actuarial analysis in FAS 87 to arrive at this figure.^[48] The Department proposed a five-year average expense amount, instead of the FAS 87 methodology, that would result in a reduction of \$1,202,245. CenterPoint made a substantial contribution to the pension fund after the period for prefiled testimony closed. With the contribution, the actuarial analysis results in a reduction in \$972,584. The parties agreed to that reduction, the use of the FAS 87 actuarial study, and that CenterPoint would provide an annual summary of activity in the pension fund.^[49]

86. CenterPoint used a similar actuarial study to determine the expenses of other postretirement benefits.^[50] Under the 2005 FAS 106 analysis, CenterPoint's expenses for other postretirement benefits increased by \$348,663 due to changes after the last prefiled testimony. The parties agreed that the postretirement benefits expense should be increased by \$348,663.^[51]

87. Based on projections of increased line location requests, CenterPoint applied for an increase of \$666,782 for additional line location expenses. The Department proposed disallowing the entire increase. The actual number of line locations appears to have fallen below projections. Gopher State One Call (a line location referral service) has increased its rates, resulting in an actual increase of \$62,484. The Parties agreed that CenterPoint would forego its projected increase in cost, and the increase of \$62,484 (for the Gopher State One Call expense) would be allowed.^[52]

88. CenterPoint proposed that its expenses for this rate matter be recovered over a two-year period. The Department asserted that \$10,000 in administrative expenses be disallowed, a portion of the expense be allocated to the nonregulated operations, and that allowable expenses be amortized over a five-year period. The parties agreed that 7% of regulatory agency costs should be allocated to nonregulated operations, no deductions to the expenses be made, and that the costs be allocated over a three-year period. These adjustments result in a reduction of the test year expenses by \$216,647.^[53]

89. CenterPoint operates Conservation Improvement Program/Demand Side Management projects (CIP) as part of its efforts to improve customer conservation. The costs incurred in these projects, less the revenue recovered through rates is set out in the CIP tracker balance.^[54] The actual CIP tracker balance at the beginning of the test year was (\$351,126), a negative balance. The parties agreed that the balance should be trued-up and reset at the beginning of the test year and that the true-up amount be applied to the interim refund. These changes result in a test-year expense reduction of \$391,159.^[55]

90. Because CenterPoint operates regulated and nonregulated businesses, the costs incurred must be allocated between these businesses. By prior Commission Order, CenterPoint has incorporated allocation methods into a Cost Allocation Manual (CAM) that governs the division of expenses between regulated, nonregulated, and capital accounts.^[56] In its Application, CenterPoint proposed adjustments to the CAM to conform test-year methodologies to their treatment in the CAM. The Department opposed these adjustments, which increased the allocation to regulated operating expenses. The parties agreed to decrease the test-year allocation to regulated operating expenses by \$294,229.^[57]

91. General liability and automobile claims were proposed for inclusion in the rate base using a three-year average of actual claims from April 2001 to March 2004. In its application, CenterPoint identified \$493,940 as the three-year average cost of claims. CenterPoint experienced increased claims over the remainder of 2004.^[58] The parties compromised by allowing the adjustment of the historical claims period to include 2004 and increase the averaging period to four years. The parties agreed that the allowable claims cost for the test year is \$583,737.^[59]

92. CenterPoint proposed an expense adjustment to cover anticipated increases in costs caused by compliance with the Pipeline Safety Improvement Act of 2002.^[60] In its application, CenterPoint proposed \$195,387 as increased pipeline safety expenses. The parties agreed to increase the costs by \$84,487 to cover the cost of a Project Engineer position filled to comply with the increased safety regulation.^[61]

93. CenterPoint proposed calculating a test-year bad debt expense by taking the actual 2003 bad debt expense as a percentage of 2003 firm revenue and applying that percentage to the test year firm revenue. The Department suggested averaging the bad debts over two years to derive the percentage. Averaging the actual bad debt expenses from 2003 and 2004 and applying the resulting percentage results in an

increase in the allowable bad debt expense of \$695,055 over the requested expense.^[62] The parties agreed that the increase was appropriate.^[63]

94. Corporate allocation costs and fleet operating expenses were identified for rate base inclusion in CenterPoint's application. The Department analyzed the costs and questioned the methodologies on these two expense items. The parties agreed that these two items would be reduced by \$145,337 and \$140,777, respectively.^[64]

95. Advertising expenses of \$809,967 were identified for inclusion in the rate base as relating to safety, conservation, utility services, and environmental protection. The Department disputed whether the content of the advertising met the statutorily-established categories authorizing inclusion in the rate base.^[65] The parties agreed to shifting some expenses from different accounts to advertising and disallowing \$11,521 for a newsletter expense.^[66] The effect of these changes is to increase the allowable advertising expense by \$59,080.^[67]

96. Some corporate functions (known as "shared services") of CenterPoint are performed by a division of the parent company, CNP. In its Application, CenterPoint proposed an increase of shared services expenses of \$69,463 reflecting CNP's performing CenterPoint's accounts payable function.^[68] The Department disputed the reasonableness of the proposed expense, noting that the identified costs increased when performed by shared services and the costs had not been allocated between regulated and nonregulated businesses.^[69] The parties agreed that the shared services cost would be reduced by \$69,463.^[70]

97. A Highway and Street Infrastructure Cost Rider (ICR) was proposed for inclusion in CenterPoint's billing structure. The ICR would allow CenterPoint to recover relocation costs arising from street and highway construction by means of an annual adjustment to customer bills. The adjustment would be derived by estimating the upcoming year's capital costs arising from such construction and arriving at a monthly surcharge, allocated across customer classes.^[71]

98. SRA, the Department, and the OAG-RUD objected to the addition of the ICR to CenterPoint's billing structure. OAG-RUD noted that the frequent new charges on bills would likely cause confusion among customers regarding the charges.^[72] The Department maintained that the absence of a statutory provision authorizing the ICR requires the Commission to treat the proposal as a fundamental change to rate setting.^[73] The Department distinguished other riders that had been previously approved as being voluntary adjustments to avoid passing costs on to the general rate base for payment by customers system-wide.^[74]

99. As part of the settlement, CenterPoint dropped its request for the ICR.^[75] CenterPoint will continue to pass these costs along to customers in its rate base. The difference lies in CenterPoint's adjustment of the cost recovery. CenterPoint is foregoing an annual adjustment of this cost, instead treating this item as part of its general rate adjustment, which happens less frequently (only when it files for rate increases).

100. Outside of the settlement between CenterPoint and the Department, the OAG-RUD objected to the allocation percentages of dues in certain trade organizations that were proposed for inclusion in the rate base. CenterPoint agreed to make the allocation adjustments recommended by the OAG-RUD. These adjustments result in a decrease of \$32,561 from the membership dues expense requested by CenterPoint.^[76]

Rate Design Issues (Settlement)

101. The core dispute over rate design in this matter was CenterPoint's proposal to change the manner in which the residential delivery charge was calculated. As set out in the application, the residential basic charge would increase from \$5.00 per month to \$16.00 per month. The originally proposed design for this customer class significantly reduced the rate per therm to calculate the delivery rate. The effect was to radically change how the burden of that charge was distributed. Customers who use little natural gas (such as renters who only use natural gas for cooking) would see a large increase in their delivery charge (by some calculations, up 20% of their total bill). Residential customers who use above average amounts of natural gas could actually see their delivery charge **decrease** as a result of CenterPoint Energy's rate **increase**.

102. Many members of the public, ME-3, the Sierra Club, Energy CENTS, the Department, the OAH-RUD, SRA, PNEC, AARP and others objected to this outcome. They maintained that CenterPoint's use of an "average" increase in the residential class masked the true impact of these charges, particularly as they affect low-income, low-usage residential customers. As noted earlier, the comments at the public hearings and written comments filed focused largely on this issue.

103. OAH-RUD has maintained consistently throughout this case that the residential customer charge should stay at \$5.00. The SRA agrees, but noted in its Briefs that it would not oppose a compromise position of \$6.50 if the MPUC is persuaded of the need to move toward cost-based rates.

104. CenterPoint maintains the low-income, low-usage residential customer is an "urban legend."^[77] This assertion is supported, CenterPoint maintains, by the statistics from the Low Income Home Energy Assistance Project (LIHEAP) showing that low income customers use volumes of natural gas similar to average residential customers.

105. LIHEAP is a federally-funded program administered in this state by the Minnesota Department of Commerce. As part of the State's obligations under the program, the administering agency must adopt a plan indicating how the LIHEAP program will be implemented and the funds disbursed. Minnesota's plan for 2005 states in pertinent part:

The State of Minnesota agrees to:

(1) use the funds available under this title to--

(A) conduct outreach activities and provide assistance to low income households in meeting their home energy costs, **particularly those**

with the lowest incomes that pay a high proportion of household income for home energy, consistent with paragraph (5);

* * *

(5) provide, in a timely manner, that **the highest level of assistance will be furnished to those households which have the lowest incomes and the highest energy costs or needs in relation to income**, taking into account family size, except that the State may not differentiate in implementing this section between the households described in clauses 2(A) and 2(B) of this subsection;^[78]

106. Since low-use customers will, by definition, have lower energy costs than higher use customers, the LIHEAP program is far less likely to assist low-use customers. Put another way, the LIHEAP program's focus on alleviating the energy problems of customers with large energy bills biases the program towards low-income customers who heat single-family residences. The LIHEAP program information does not support CenterPoint's contention that low-income, low-use customers are an "urban legend." To the contrary, there is no dispute that a segment of CenterPoint's residential customers are renters in buildings where the customers' only gas usage is for cooking. There is no dispute that some portion of that segment are low-income persons. Some of these persons submitted comments in this proceeding. Left unanswered by the record in this matter is how many customers are low-income, low-usage customers.

107. The impact of the proposed rate design change on low-income, low-usage customers is an appropriate concern of the Commission in determining whether rate shock will occur and whether the change is in the public interest. The settlement between the Department and CenterPoint addresses this issue by agreeing to a basic charge of \$8.00 per month for residential customers. This agreed-upon amount is one-half the initially requested total basic charge. The increase proposed is 27 percent (3/11) of that initially requested. CenterPoint notes that this agreed-upon amount is one-half of the actual costs incurred by CenterPoint to deliver services as measured by the CCOSS.^[79] The Department maintains that the \$8.00 charge appropriately balances the interests of both CenterPoint and ratepayers.^[80]

108. The approved residential customer basic charges for five other natural gas utilities in Minnesota are cited by the OAG-RUD. These charges range from \$5.00 to \$6.50 per month. From this evidence, the OAG-RUD maintains that the existing \$5.00 charge should be maintained.^[81] But in recent filings for rate increases by two of those utilities, a part of the requested rate increases has been to increase the residential customer charge to \$8.50 and \$8.00.^[82]

109. The reason for imposing a basic charge is to more closely correlate the costs of providing a service (in this case, delivery of natural gas to consumers) to the price paid by customers who are receiving that service. The record is undisputed that the approximate cost of providing service to residential consumers is \$16.00. An intra-class subsidy of 50% in the identifiable cost of service for residential customers is a

reasonable balance between the interests of large consumers of natural gas and low-income, low-usage consumers.

110. A factor to be considered in any rate increase is the effect of rate shock on consumers.^[83] OAH-RUD asserts that the change in cost from the current bill under the settlement disproportionately increases the costs to low-usage customers. In support of this argument, examples of ultimate delivery charges under various scenarios were charted. The ultimate delivery charge under the settlement increases **annually** by \$32.40 for low-usage customers, \$22.15 for small use customers, \$9.93 for LIHEAP customers, and \$8.83 for average use customers. The ultimate charge decreases annually by \$5.51 for residential customers using 1,500 therms per year.^[84]

111. Stated as a monthly charge, the largest increase in a customer bill under the settlement is \$2.70.^[85] The average monthly bill will see an increase of 70 cents. At the public hearings, many commentators opposed to the \$11 increase in the customer charge proposed by the Company recognized that some level of cost increase was appropriate.

112. The OAG-RUD points out that in 1991, the Commission found an increase of \$2.07 in the monthly bill to low-usage customers to be “substantial.”^[86] The OAH-RUD also cited a Florida utility decision where the basic charge was increased by only 50 cents and to a Wisconsin utility rate decision where the proposed increase was deemed to constitute rate shock.^[87]

113. What was not mentioned about the Florida decision was that the existing residential basic charge was \$7.50 per month.^[88] With the allowed increase, the Florida monthly basic charge was \$8.00. In the Wisconsin decision, the existing monthly basic charge was \$8.55 (and the utility was seeking an increase to \$13.08).^[89] The increased bills arising from this settlement do not trigger rate shock. Rate shock is not a factor that requires retaining the existing \$5.00 customer charge in this instance.

114. Ensuring that the rate structure does not discourage conservation is another consideration in the approval of a particular rate design. An argument made throughout this proceeding is that increasing the residential basic charge acts as a disincentive to conservation. CenterPoint responded that the entire delivery charge is significantly smaller than the wholesale charge portion of an average customer’s bill.

115. There is no practical conservation effect arising from the increase of the basic charge to \$8.00 on low-usage consumers. Essentially, these customers have reached the irreducible minimum of natural gas consumption. For the average use and average LIHEAP customers (consuming approximately 1,000 therms per year), the annual increase is approximately \$9.00. The wholesale cost of gas dwarfs this modest increase. Conservation incentives persist in both the wholesale cost (which is directly passed through to the customer) and the per therm rate portion of the delivery charge (which is higher under the settlement than in the Application). For large volume residential consumers, the modest decrease in the delivery charge constitutes no disincentive to conserve energy, since the wholesale cost per therm is large and

significant reduction in consumption (and thereby increased savings) is possible for these customers.

116. Under the settlement, CenterPoint’s proposed revenue requirement increase totals .8%. Apportioned by customer class, the burden of the increase is as follows: ^[90]

Class	Total Revenue	Non-gas Costs
Residential	0.90%	4.33%
Comm. & Ind. A	1.30%	5.02%
Comm. & Ind. B	0.72%	3.66%
Comm. & Ind. C	0.39%	2.42%
Small Vol. Dual Fuel A	1.30%	10.08%
Small Vol. Dual Fuel B	1.30%	11.55%
Large Vol. Dual Fuel	0.00%	0.00%

Consolidations (Settlement)

117. CenterPoint had proposed to consolidate the Commercial & Industrial A class with the residential class, due to similarities between the classes. Similarly, the usage rates for Commercial & Industrial classes B and C were proposed to be merged. These proposed adjustments in the rate structure were opposed by the Department and OAG-RUD. The parties agreed to retain the current class structure and usage rate mechanism.

118. Due to the company’s operational changes, CenterPoint proposed to merge the Viking and Northern service areas. The Department agreed to the merger in the settlement. No other party filed testimony on this subject or objected to the merger. ^[91]

119. CenterPoint also proposed a partial consolidation of rates between the Viking and Northern service areas. CenterPoint estimated that full consolidation would require attribution of \$100,000 to the Viking Service Area. ^[92] In its Application, CenterPoint proposed attribution of \$70,000 to the Viking Service Area as a step toward consolidation. As part of the settlement, the parties agreed that Northern and Viking Service Areas would receive the same percentage increase in the distribution margin. ^[93]

Miscellaneous Tariff Changes (Settlement)

120. With respect to Market Service Riders, the Company proposed to clarify that the Demand Charge on Large General Firm Sales Service and Transportation Service may be flexed upward or downward. The Department agreed with this clarification. The parties urge adoption of the Company's proposed tariff change to its Market Service Rider.

121. With respect to Transportation Service Balancing Penalties, the Company proposed to equal the amount charged to CenterPoint by the interstate pipelines as provided in the Company's tariffs. The Department agreed with updating, but did not agree that future updates should occur automatically as the pipeline companies changed their charges. The parties now propose that the tariff language regarding transportation service balancing penalties will specify that any changes in such charges will be effective only after Commission approval, as recommended by the Department.

122. Due to a change in Minnesota law, the Company proposed a change in the language in its tariffs related to interest and deposits, to track the new law. The Department agreed that such a change was necessary, and the parties urge adoption of the Company's proposed tariff change in this regard.

123. With respect to service disconnection and reconnection charges, the Company proposed initially to modify its Rate Book regarding service reconnection charges to require customers to pay all costs of reconnection and to increase the additional charge for situations involving meter tampering from \$50 to \$100. The Department agreed with the Company's proposal so long as the Company agreed to retain records relating to the actual cost of each disconnection and reconnection, which the Company has agreed to do. The parties urge the Commission to approve this approach.

124. The Company proposed a minor word change to the Cost Justification Formula for its commercial and industrial (C & I) main line extension projects at subsection 4.04 of its tariffs, and proposed annually to update the cost of service factor used in that formula. The Department agreed, with two qualifications. The Company agreed with the Department's proposed modifications, and the two parties proposed to the Commission that the company will withdraw its proposed multiplier of 1.4 and that the cost of service factors will be included in the gas rate book. Going forward, the Company agrees to update annually the cost of service factors pursuant to a miscellaneous tariff filing.

125. The Company proposed to modify subsection 5.10 to reduce the free footage allowance from 75 to 50 feet for residential customers not installing gas water heaters, maintaining that a 75 foot allowance cannot be justified economically in those cases. The Department disagreed initially, maintaining that the Company should create a separate class of residential non-water heater customers if it wanted to draw such a distinction. The parties agree now to propose to the Commission that the Company will maintain a free footage allowance of 75 feet for all residential customers.

126. The Company proposed to delete its water heating allowance for gas main extensions (currently in Section VI, part 4.06), because information regarding gas water heaters is not known at the time the main extension occurs. The Department was opposed to the change, arguing that the Company could apply overall market penetration data to estimate gas main allowances. As part of the settlement, the parties agreed to delete the water heating allowance for gas main extensions currently at Section VI, part 4.06, which results in similar treatment for all residential customers.

127. The Company proposed to update its service line extension tariff, in part by increasing the per foot charge from \$2 to \$4 for service lines in excess of the free footage allowance. The Department agrees with this change, and the parties urge adoption by the PUC to change the excess footage charge in Section VI, part 5.0 of the Company's tariffs to \$4.

128. The parties urge adoption of the Company's proposed tariff change regarding deletion of financing plans, as modified by the Department. The Company had proposed to delete a section of its tariff allowing applicants to finance their contribution-in-aid-of-construction over a period of up to three years, due to non-use by customers. The Department agreed, recommending that the remaining 90 day financing option be interest free. CPE settled on the Department's final proposal, and the parties recommend it to the MPUC.

129. The parties have agreed to a change in CPE's tariff for winter construction charges, as proposed initially by the Company. They agree further that the Company will retain information regarding the number of winter construction projects, total costs charged to customers for such projects and total winter construction charges incurred by the Company, and to provide that information with its Annual Jurisdiction Report. The Company's initial proposal was to modify its tariff regarding assessment of winter construction charges, changing the word "will" to "may", in recognition that the Company may not need to apply the winter construction charges during winter months (depending on actual weather conditions).

130. The Company proposed initially to modify language in Section VI, part 4.06 of its tariffs to clarify that a cash advance must be received prior to construction and to delete a provision for a 15 percent discount for advance payments, due to non-use by customers. The Department agrees with both proposed modifications, and the parties urge adoption thereof.

131. The Company proposes three miscellaneous tariff charges on which no other party filed testimony and for which the Company requests Commission approval. The Department of Commerce agrees that these proposals, regarding Small Volume Firm-Interruptible Service Tariffs, Large Commercial and Industrial Credit Policy and the daily balancing service rider be adopted.

Non-Financial Issues (Settlement)

132. In its supplemental testimony, the Company provided a proposed service quality plan. The Department also filed testimony on the plan, supporting it along with two recommended additions – reporting on adjusted data for telephone response time and providing quarterly reports (as opposed to semiannual). The Company agrees with the DOC recommendations and the parties urge adoption of CenterPoint’s proposed plan as modified by the Department’s recommendations.

133. Regarding Main and Service Line Extensions, the Company filed a required report with the Commission, the results of which were disputed by the Department, which indicated that it did not believe the Company had demonstrated consistent and correct applications of its tariffs. The Company provided substantial additional information in response to that concern. In its Surrebuttal Testimony, the Department stated that based on further review and the additional information provided, that CenterPoint “has shown it consistently and correctly applied its tariffs since the last rate case”.^[94] The parties urge that the Company has shown that it has consistently and correctly applied its Commission-approved extension tariffs since its last rate case, and urge the Commission to adopt that position.

134. The Commission’s order in the Company’s 1995 rate case also asks the parties to examine whether a rate case applicant’s tariffs were “appropriately cost and load justified”. The Company made a number of recommendations for updating its tariffs in this case to address that point, noted at pages 46 and 47 of Exhibit 44. In this connection, the parties agree that the Company has shown that it has consistently and correctly applied its Commission-approved extension tariffs since its last rate case. The Department and the Company agree that the Company’s investment in extension projects has been reasonable, and further agree that the resolutions set forth in Sections 4.8.5 and 4.8.8 to update the Company’s tariffs addressing the issue of cost and load justification should be adopted.

135. The Department questioned initially whether the Company had demonstrated that it had not engaged in wasteful addition of plant.^[95] The Department had concerns with the Company’s demonstration of consistent and correct application of its tariffs, with the alleged use of an “Allowable Investment Formula” and with the Company’s economic study of a project known as “The Lakes”. The Company responded to the Department’s concerns with substantial additional information and the parties now agree that the Company has demonstrated a consistent and correct application of its extension tariffs. The Department also agrees that the Company has explained adequately its “Allowable Investment Formula”. Regarding The Lakes project, which is a rapidly-growing development area in Blaine, the Company maintains it properly applied its tariffs for this multi-year project. The Department initially disagreed, arguing that CPE was requiring other ratepayers to subsidize The Lakes Project. As detailed on pages 49-51 of Exhibit 44, the parties now agree that the addition of plant by the Company has not been wasteful. Rather, it is agreed that the Company has shown it has consistently and correctly applied its Commission-approved extension tariffs since its last rate case, including with respect to The Lakes project. The parties agree that the economic analysis of The Lakes project shows it falls well within the parameters of reasonableness established by Commission-approved tariffs.

136. The Commission has required the Company to study the impact of the demand smoothing factor on demand costs in its CCOSS. The Company and the Department agree that demand smoothing has had no effect on the Company's CCOSS. As a result, the Company asked initially for a permanent variance from the study requirement. The Department objected to the permanency of the variance, and the parties agree now that demand smoothing does not impact the CCOSS but the company will withdraw its request for a permanent variance.

137. Regarding transportation costs, the Department recommended in its direct testimony that the Company account separately for costs associated with transportation customers in its next rate case. In connection with the settlement, the parties now agree that the Company will provide information in its initial filing in its next rate case regarding the costs associated with serving transportation customers, and that it is appropriate for the Commission to order that accordingly.

138. In its direct testimony, the DOC recommended certain information requirements for future rate cases filings as well as annual reports related to large customer sales. The Company responded that it recommended that parties meet to discuss information needs for future rate cases and objected to the recommendations relating to large customer sales. The Department agreed that the parties should meet further to discuss rate case information requirements and then inform the Commission of any agreement reached. The parties now agree that with its Annual Jurisdictional Report, the Company will provide a listing of new large customers and projected annual throughputs and margins associated with those customers. The parties agree to meet to discuss future information needs, including providing billing cycle data in future rate case filings.

Based on the foregoing Findings, the Administrative Law judge makes the following:

CONCLUSIONS

1. The Minnesota Public Utilities Commission and the Administrative Law Judge have jurisdiction over the subject matter of this proceeding pursuant to Minn. Stat. Ch. 216B and section 14.50.

2. Any of the foregoing Findings which contain material which should be treated as a Conclusion is hereby adopted as a Conclusion.

3. CenterPoint and DOC have demonstrated that an increase in the residential basic charge to \$8.00 per month is an appropriate adjustment to balance the need to recoup the costs of serving the residential class of customers with the need to encourage conservation, avoid rate shock, and account for other external factors that favor business customers.

4. There is insufficient evidence in the record to support the OAG-RUD's contention that the residential basic customer charge should remain at \$5.00 per month or the SRA's contention that \$6.50 per month is an acceptable residential basic charge.

5. The record supports all the uncontested matters, whereby the amount sought in additional revenue is reduced to \$8,987,000, constituting a revenue requirement increase of 0.8%, and these uncontested items may be adopted.

6. The capital structure proposed in the settlement is reasonable, resulting in an overall rate of return of 8.03%.

7. The record supports the joint recommendation to use a rate of return on equity of 10.18 percent without further adjustment.

8. The record supports that modifying CPE's natural gas rates in the manner described in the Settlement and in the Findings and Conclusions above results in just and reasonable rates that are in the public interest within the meaning of Minn. Stat. § 216B.11.

9. The rate finally ordered by the Commission should be compared to the interim rate set in the Commission's September 10, 2004 Order, and a refund be ordered to the extent that the interim rate exceeds the final rate.

10. In the event that the Commission rejects the agreement of the parties, this matter may be extended by 60 days for conclusion of the contested case proceedings under the terms of Minn. Stat. § 216B.16, subds. 1a and 2.

Based on the foregoing Findings and Conclusions above, **IT IS RECOMMENDED** that the Public Utilities Commission issue the following:

ORDER

1. CenterPoint is entitled to increase gross annual revenues by \$8,987,000 in accordance with the terms of this Order.

2. Within 30 days of the service date of this Order, the Company shall file with the Commission for its review and approval, and serve on all parties in this proceeding, revised schedules of rates and charges reflecting the revenue requirement for annual periods beginning with the effective date of the new rates, and the rate design decisions contained herein. The Company shall include proposed customer notices explaining the final rates. Parties shall have 14 days to comment.

3. (If the Commission orders an Interim Rate Refund) within 30 days of the service date of this Order, the Company shall file with the Commission for its review and approval, and serve upon all parties in this proceeding, a proposed plan for refunding to all customers, with interest, the revenue collected during the Interim Rate period in excess of the amount authorized herein. Parties shall have 14 days to comment.

Dated this 25th day of March, 2005.

/s/ Richard C. Luis

RICHARD C. LUIS
Administrative Law Judge

Reported: Shaddix and Associates
Transcripts Prepared

MEMORANDUM

Most of the parties who did not participate in the Settlement, and many persons who made comments on the subject of the basic charge, asserted that any increase in the basic charge was inappropriate. They asserted that increasing the basic charge would result in rate shock. But public utilities must make significant investments in infrastructure to provide necessary services. These investments are constant and directly associated with providing customer service, independent of the consumption of natural gas. CenterPoint and the Department have attempted to balance the need for a consistent stream of revenue with the need to avoid rate shock resulting from changes to rate design affecting residential customers. To that end, CenterPoint has agreed to a reduction amounting to more than 70% of its proposed increase to the basic charge.

Some prior decisions of the Commission have established a low threshold for increases to the basic charge that constitute rate shock. Recently approved basic charges have reached (or exceeded) \$8.00 in Florida and Wisconsin. In Minnesota, two utilities with higher basic charges than CenterPoint's are currently seeking to increase their basic charges to at least \$8.00. In this case, the \$8.00 basic charge appears to be a natural plateau upon which the competing interests of utilities and residential customers are appropriately balanced.

The proposed modification of the basic charge exceeds increases held by prior Commissions to constitute rate shock. But the length of time since the prior increase

supports the conclusion that the change is not excessive in this instance. The Commission could conclude that the record supports raising the basic charge by \$3.00 per month, but there are still concerns over the impact on low-income customers. The suddenness of the change, increasing the basic charge by 60% at one time, could be viewed, standing alone, to impose rate shock on these particular customers. If that conclusion is reached by the Commission, it may wish to consider a mechanism to ameliorate the speed of the change to residential customers. The increase could be phased in over two years, with the delivery rate being adjusted in a compliance filing in year two. The utility would benefit from the certainty derived from the modest increases in the basic charge and consumers would not have the entire increase occurring at one time. The overall revenue increase would remain the same, allocated between classes to the same extent, but more revenue would be drawn from higher volume users of natural gas in the first year.

R.C.L.

^[1] A location in Brainerd was identified in the public hearing notice of this proceeding, but that location was unable to connect due to technical difficulties. No persons appeared at the Brainerd location to provide testimony. Videoconference Transcript, December 2, 2004, at 29.

^[2] Ex. 1, Binder 1, Notice of Change in Rates.

^[3] ***In the Matter of the Petition of CenterPoint Energy Minnegasco, a Division of CenterPoint Resources Corp. for Authority to Increase Natural Gas Rates in Minnesota***, PUC Docket No. G-008/GR-04-901 (Order Accepting Filing, Suspending Rates, and Requiring Further Filings issued September 7, 2004).

^[4] *Id.* (Notice and Order for Hearing issued September 7, 2004).

^[5] *Id.* (Order Setting Interim Rates issued September 10, 2004).

^[6] The Department and the OAG-RUD were admitted as of right.

^[7] Ex. 5, Hammond Direct, at 2-3.

^[8] CenterPoint issues no common stock, since it is a division of CPRC. Ex. 27, Griffing Direct, at 21. Effective December 1, 2004, CPRC directed that its division formerly known as CenterPoint Energy Minnegasco would be known only as CenterPoint Energy.

^[9] Ex. 1, Binder 1, Tab G.

^[10] Ex. 1, Binder 1, Tab G.

^[11] ***In the Matter of the Application of Minnegasco, a Division of NorAm Energy Corp., for Authority to Increase Its Natural Gas Rates in Minnesota***, PUC Docket No. G-008/GR-95-700 (Findings of Fact, Conclusions of Law, and Order issued June 10, 1996).

^[12] Ex. 27, Griffing Direct, at 12.

^[13] Ex. 21, TheBerge Direct, at 3-4.

^[14] One therm is equal to 100,000 BTU's. CenterPoint calculates the therm value of gas provided by sampling delivered gas for its BTU content per cubic foot and multiplying that value by the cubic feet actually delivered to a customer.

^[15] Ex. 21, TheBerge Direct, at 3-4.

^[16] *Id.*

^[17] Ex. 5, Hammond Direct, at 5.

^[18] Ex. 16, Yang Direct, at 9-10, Schedule 4.

^[19] *Id.*

^[20] Ex. 44, Table 3.6.

^[21] Ex. 44, at 30.

^[22] Ex. 21, pp. 13-14, Ex. 5, pp. 15-21.

[23] Ex. 44, p. 32.

[24] Minneapolis Tr. at 17-21.

[25] Sabathani Tr. at 23-26. The circumstances surrounding CenterPoint's actions regarding the Cold Weather Rule are outside the scope of this proceeding, and no findings can be made here regarding that controversy.

[26] Sabathani Tr. at 28-31.

[27] Sabathani Tr. at 33-46.

[28] CenterPoint Brief, at 4 (including the revenue decrease from the OAG-RUD settlement).

[29] Ex. 44, at 4. The numbered outline format (e.g. 3.1) used in the settlement is followed in the headers to assist in directing attention to the portion of the settlement being discussed.

[30] Ex. 44, at 6. The agreement to the ROE number was conditioned on acceptance of the \$8.00 per month residential basic charge.

[31] Ex. 44, at 7.

[32] Ex. 44, at 8.

[33] Ex. 44, at 9.

[34] Included in the record in Ex. 44, Schedule 3.2.6.

[35] Ex. 44, at 10.

[36] *Id.*, at 10-11.

[37] *Id.*, at 11.

[38] Ex. 44, at 11. "Dth" stands for dekatherm, with a conversion factor of 1 Dth equaling 10 therms.

[39] Ex. 44, at 11.

[40] Ex. 44, at 13, Schedule 3.3.1 (since the decrease in the cost of natural gas is greater than the decrease in revenue).

[41] Ex. 44, at 13-14.

[42] *Id.*, at 14.

[43] Ex. 44, at 14-15.

[44] Ex. 44, at 15.

[45] *Id.*

[46] Ex. 44, at 16.

[47] Ex. 44, at 18.

[48] Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions" (FAS 87), was published by the Financial Accounting Standards Board (FASB) in December 1985.

[49] Ex. 44, at 19.

[50] Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" (FAS 106), was published by the FASB in December 1990.

[51] Ex. 44, at 20.

[52] Ex. 44, at 20.

[53] Ex. 44, at 21.

[54] Ex. 12, Ostazeski Direct, at 45-47.

[55] Ex. 44, at 22.

[56] Ex. 7, Nesvig Direct, at 78-80.

[57] Ex. 44, at 23.

[58] Ex. 44, Vol.2, Schedule 3.4.12 C.

[59] Ex. 44, Vol. 1., at 24; Ex. 44, Vol. 2, Schedule 3.4.12 D.

[60] Pub. L. No. 107-335 (2002)(amending 49 U.S.C. § 6103, *et seq.*).

[61] Ex. 44, Vol. 1, at 24.

[62] Ex. 44, Vol. 2, Schedule 3.4.12 D.

[63] Ex. 44, Vol. 1, at 25.

[64] Ex. 44, Vol. 1, at 26.

[65] See Minn. Stat. § 216B.16, subd. 8(b).

[66] Ex. 11, Peterson Rebuttal, at 37.

[67] Ex. 44, Vol. 1, at 27.

[68] Ex. 7, Nesvig Direct, at 34.

[69] Ex. 24A, Bender Direct, at 15.

[70] Ex. 44, Vol. 1, at 27.

[71] Ex. 5, Hammond Direct, at 23-24; Ex. 12, Ostazeski Direct, at 63-67.

- [72] Ex. 42, Nelson Direct, at 22.
- [73] Ex. 26A, St. Pierre Direct, at 6.
- [74] *Id.* at 7-10.
- [75] Ex. 44, Vol. 1, at 28.
- [76] Ex. 46, Nelson Supplemental Surrebuttal, at 3; CCN-3, Schedule 3.
- [77] CenterPoint Brief, at 18.
- [78] Minnesota Department of Commerce website (http://www.state.mn.us/mn/externalDocs/Commerce/2005_State_Plan_120304015409_StatePlanFinal2005.pdf)(emphasis added). The 2004 plan has identical language.
- [79] CenterPoint Reply Brief, at 2.
- [80] Department Brief, at 2.
- [81] OAG-RUD Brief, at 8.
- [82] ***In the Matter of an Application by Northern States Power Company d/b/a Xcel Energy for Authority to Increase Rates for Natural Gas Service in the State of Minnesota***, Docket No. G-002/GR-04-1511 (Notice and Order for Hearing issued November 12, 2004) (<http://www.puc.state.mn.us/docs/orders/04-0149.pdf>); ***In the Matter of a Petition by Great Plains Natural Gas Company, a Division of MDU Resources Group, Inc., for Authority to Increase Natural Gas Rates in Minnesota***, Docket No. G-004/GR-04-1487 (Notice and Order for Hearing issued November 1, 2004) (<http://www.puc.state.mn.us/docs/orders/04-0143.pdf>).
- [83] ***In the Matter of the Application of Midwest Gas, a Division of Iowa Public Service Company, for Authority to Change Its Schedule of Gas Rates for Retail Customers within the State of Minnesota***, Docket No. G-010/GR-90-678, at 35 (Findings of Fact, Conclusions of Law, and Order issued July 12, 1991).
- [84] Ex. 46, Nelson Supplemental Surrebuttal, CCN-3, Schedule 2.
- [85] This is calculated for Northern customers. Viking customers already pay a \$6.00 basic charge and will see a smaller monthly increase. Theoretically, a Northern customer could see a \$3.00 per month increase, but only if that customer used no natural gas under the existing rate structure, which is unlikely.
- [86] ***Midwest Gas***, *supra*, at 48.
- [87] OAH-RUD Brief, at 7 (citing ***In Re Application for Rate Increase by City Gas Company of Florida***, Florida Public Service Commission Docket No. 030569-GU, (Order No. PSC-04-0128-PAA-GU issued February 9, 2004); ***Application of Madison Gas and Electric Company for Authority to Change Electric and Natural Gas Rates***, Wisconsin Public Service Commission Docket No. 3270-UR-111 (Final Decision issued February 28, 2003).
- [88] ***City Gas Company of Florida***, *supra*, at 54.
- [89] ***Madison Gas and Electric Company***, *supra*, at 35.
- [90] Ex. 44, Vol. 1, at 34. The percentages listed are the percentage of increase over the current cost. The apportionment is an estimate, with the final allocation to be determined in CenterPoint's compliance filing. *Id.*
- [91] Ex. 44, Vol. 1, at 35.
- [92] *Id.* at 36.
- [93] Ex. 44, Vol. 1, at 36.
- [94] Ex. 39, pp. 33-37, 45.
- [95] Ex. 37, Vol. II, p. 37.