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August 8, 2012

Dr. Burl W. Haar
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101-2147

**RE: Additional Supplemental Comments of the Minnesota Department of Commerce,
Division of Energy Resources**
Docket No. G007,011/AI-10-783

Dear Dr. Haar:

Attached are the Additional Supplemental Comments of the Minnesota Department of Commerce, Division of Energy Resources (Department) in the following matter:

Petition of Minnesota Energy Resources Corporation (MERC or the Company) for Approval of an Affiliated Interest Agreement (Agreement).

The Department's Additional Supplemental Comments are provided in response to additional information filed by MERC on April 25, 2012. The Department recommends that the Commission approve the proposed Agreement with the modifications set forth in these Additional Supplemental Comments.

The Department is available to answer any questions the Commission may have.

Sincerely,

/s/ MARLON GRIFFING
Financial Analyst
651-297-3900

MG/jl
Attachment



BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

COMMENTS OF THE
MINNESOTA DEPARTMENT OF COMMERCE
DIVISION OF ENERGY RESOURCES

DOCKET NO. G007,011/AI-10-783

I. BACKGROUND

MERC filed the petition for approval of an affiliated interest agreement (Agreement) with the Minnesota Public Utilities Commission (Commission) in this matter on July 12, 2010. On September 7, 2010, the Department (then known as the Office of Energy Security) filed Comments analyzing the Company's request. The Department recommended approval of the proposed Agreement with the following conditions:

- that MERC submit a version of the Agreement that requires MERC to seek Commission approval of any changes in the Parties to the Agreement or changes in the services covered by the Agreement, as required by Minn. Stat. § 216B.48, notwithstanding the provisions of the Agreement;
- that MERC agree that the Commission should terminate the affiliated interest agreement approved by the Commission in Docket No. G007,011/AI-06-1052, which currently governs the provision of goods, services, and property between Integrys and its public utility subsidiaries, upon the effective date of the Agreement; and
- that the Commission require MERC to submit a study to the Commission three years from the effective date of the Agreement encompassing the annual Affiliated Interest reports related to transactions carried out under the Agreement, the content of the annual audit reports of the same transactions, the outcomes of the annual fair-market value study between Regulated Parties and Non-Regulated Parties to the Agreement, reports of any changes to Parties to the Agreement, reports of any changes in Services

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covered by the Agreement, and any other information that MERC believes would be helpful for evaluating operation of the Agreement.

In September 17, 2010 Reply Comments, MERC stated that, as recommended by the Department, an Addendum had been added to the Agreement acknowledging that the Company is subject to Minn. Stat. § 216B.48 and, therefore, must seek Commission approval of any changes in Parties to the Agreement or changes in services covered by the Agreement. MERC also agreed in these Reply Comments that the affiliated interest agreement approved by the Commission in Docket No. G007,011/AI-06-1052 would be terminated upon the effective date of the Agreement.

MERC also noted in the September 17, 2010 Reply Comments that it will already provide the Commission with most of the requested information pursuant to the terms of the Agreement, and committed to make available for the Department's, the Commission's or Commission staff's review the fair-market value study results, a submission not required by the Agreement. MERC stated that the Company "would not file or otherwise provide a copy of the study," but would make it available for review. Further, MERC stated that it will be providing the annual updates required under Section 4.4 of the Agreement, an item not specifically identified in the Department's recommendations above. Given these required and voluntary submissions, MERC stated that it was not certain of the value of an additional and separate report to the Commission.

In Supplemental Comments filed on September 22, 2010, the Department clarified its reason for requesting a study from MERC three years from the effective date of the Agreement. The Department stated that the Agreement should not have an open-ended life. Therefore, the Department recommended that the Commission require MERC to provide a study covering the annual Affiliated Interest reports related to transactions carried out under the Agreement, the content of the annual audit reports of the same transactions, the outcomes of the annual fair-market value study between Regulated Parties and Non-Regulated Parties to the Agreement, reports of any changes to Parties to the Agreement, reports of any changes in Services covered by the Agreement, and any other information that MERC believes would be helpful for evaluating operations under the Agreement. In this study, MERC would state its case to the Commission for letting the Agreement remain in effect past three years. The Department noted that the Company could, in the three-year study, summarize the results of the annual reports, audits, and studies required to be filed under the Agreement. Thus, the Department does not envision that this study would force the Company to undertake duplicative efforts. After the Department and any other interested parties comment on the study, the Department would recommend whether the Agreement should continue, be modified, or be discontinued.

The Department also agreed in its Supplemental Comments that the Commission should defer further consideration of the Agreement until any changes to the Agreement from Illinois and Wisconsin were known and submitted by MERC.

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The Illinois Commerce Commission (ICC) issued its order approving the Agreement on December 15, 2010. The ICC approved the Addendum recommended by the Department in its Comments regarding Minn. Stat. § 216B.48. The Illinois process also resulted in revisions to Sections 4.3 and 4.4 of the Agreement. MERC filed notice of the ICC Order on February 9, 2011, noting the modifications to the Agreement.

On April 25, 2012, MERC submitted a letter noting that the Public Service Commission of Wisconsin (PSCW) had approved the Agreement, as modified by the ICC. The PSCW issued its Final Decision on January 23, 2012, and on February 22, 2012, Wisconsin Public Service Corporation and Integrys Energy Group, Inc. requested a rehearing of that decision. The PSCW issued its Amended Final Decision on April 3, 2012. In the Amended Decision, the PSCW accepted the changes required by the ICC.

II. DEPARTMENT ANALYSIS

The Department has read the ICC and PSCW Orders, and the finalized Agreement filed by MERC on April 25, 2012. In particular, the Department has reviewed the revised sections 4.3 and 4.4 of the Agreement, sections which the ICC and PSCW amended in their respective proceedings addressing MERC's affiliated-interest request.

A. MINN. STAT. § 216B.48

As previously stated, the Department had recommended that MERC submit a version of the Agreement that requires MERC to obtain Commission approval of changes in Parties to the Agreement and changes in services covered by the Agreement. As noted above, MERC provided an Addendum to the Agreement requiring MERC to seek Commission approval of any changes in the Parties to the Agreement or changes in the services covered by the Agreement within 30 days. The Agreement, including the Addendum, was approved by the ICC and the PSCW. Therefore, the Department concludes that the proposed Agreement is consistent with Minn. Stat. § 216B.48.

B. ANNUAL AFFILIATED-INTEREST REPORTS

Section 4.2 of the Agreement would require that MERC submit to the Commission by May 1 of each year the billing reports for the preceding calendar year that reflect its activity as a Providing Party or a Receiving Party under the Agreement. The Department concludes that these annual affiliated-interest reports would provide the Commission with information necessary to monitor transactions carried out under the Agreement.

C. *INTERNAL AUDIT REPORTING*

1. *Modifications to Sections 4.3*

Section 4.3 of the original agreement required MERC to carry out an internal audit of transactions carried out under the Agreement. The ICC required, and the PSCW approved, several changes to Section 4.3. The changes specified several elements to be covered in the audit and dates for when the audit would be reported to the Commissions. The modification addressing the scope of the audit is:

Such audit may be either a discrete audit solely of Services under this Agreement or may be an audit of the Services under this Agreement and other affiliated interest service agreements. The internal audit shall include, but not be limited to, the following:

1) the accuracy of the derivations of costs billed by the Providing Parties; 2) the determination that the costs billed to the Regulated Parties are priced at the lesser of cost or fair market value, based on the studies and updates required by Section 4.4; 3) the determination that Services provided by the Regulated Parties to the Non-Regulated Parties, except Integrys Support, are billed at the higher of cost or market, based on the studies and updates required by Section 4.4; and 4) the accuracy of invoices issued under the Agreement during the year.

The ICC modifications also state that the first such audit report shall pertain to the period ending December 31 of the year in which the Agreement is effective, and shall be due on or before July 1 of the following year, with subsequent audit reports due July 1 following the calendar year that is the subject of the audit.

2. *Modifications to Sections 4.4*

The ICC and PSCW also approved a modification to Section 4.4, which deals with the cost study of the services to be provided under the Agreement. Section 4.4 requires MERC to conduct a new cost study every third year on or before May 1 to determine the fair-market value of services provided between Regulated Parties and the at-cost price for services provided between a Regulated Party and a Non-Regulated Party covered by the Agreement. The study also is to be updated annually to cover changes made between cost studies. The ICC and PSCW also required that MERC should notify the Commissions or Commission staffs of the availability of the study and annual update, and, if requested, make the study and updates available for review at the Commission's offices. Section 4.4 also would require that the first new cost study shall pertain to the period ending December 31, 2011, and be due on or before May 1, 2012.

3. Department Conclusion and Recommendation

The Department concludes that Sections 4.3 and 4.4 as amended by the ICC and PSCW and submitted by MERC are appropriate. The requirement to file the audit report annually and the scope of the elements to be included in the audit report would provide the Commission sufficient data to monitor compliance with the Agreement. The modified sections also are consistent with and go beyond the reporting that the Department suggested, in its Comments and Supplemental Comments, be filed by MERC with the Commission. Therefore, the Department recommends that the Commission approve the Agreement as amended in Sections 4.3 and 4.4. The Department further recommends that the Commission require MERC to make available for study in the Commission offices the cost study and annual updates to the study. The Department recognizes that the Company may want to limit access to the information in the cost study and the annual updates because of its economic value. Therefore, depending upon MERC requesting and demonstrating that access to the documents should be limited, the Commission could grant them trade-secret status or some other level of protection that MERC demonstrates is appropriate.

The requirement in Section 4.4 that the first new cost study covering the period ending December 31, 2011, be due on or before May 1, 2012, is out of date. The Department recommends that the Commission require MERC to file the cost study covering the period ending December 31, 2011, within 30 days of the date of an Order approving the Agreement.

D. COMMISSION THREE-YEAR REVIEW

As stated above, the Department recommended that the Commission require MERC to file a study three years from the effective date of the Agreement. In this study MERC would state its case to the Commission for letting the Agreement remain in effect beyond three years after the effective date. The Department reiterates that this study need not require MERC to develop any data beyond that which it is required to report under the Agreement. MERC could summarize the data provided in the annual affiliated-interest reports, the annual audit reports, and the fair-market value study and its annual updates. Moreover, MERC could summarize the reports that it is required to make to the Commission under Minn. Stat. § 216B.48 of any changes to Parties to the Agreement and changes in services covered by the Agreement during the three years. MERC would have the option to provide any additional information in the study that the Company believes would be helpful to the Commission in evaluating operations under the Agreement.

The Department concludes that the Agreement should not have an open-ended life. Therefore, the Department continues to recommend that the Commission require MERC to file a study with the Commission three years from effective date of the Agreement providing the information set forth above. After the Department and any other interested parties comment on the study, the Department would recommend whether the Agreement should continue, be modified, or be discontinued.

III. SUMMARY OF DEPARTMENT CONCLUSIONS AND RECOMMENDATIONS

The Department concludes that:

- the Addendum to the Agreement protects the Commission's jurisdiction under Minn. Stat. § 216B.48;
- Section 4.2 provides the Commission with information necessary to monitor compliance with the Agreement;
- Section 4.3 as amended provides for annual internal audits of an appropriate scope;
- Section 4.4 as amended provides for triennial fair-market value cost studies and annual updates that ensure charges under the Agreement would be appropriate; and
- the Agreement should not have an open-ended life.

Therefore, the Department recommends that the Commission approve the Agreement as approved by the ICC and PSCW, including the Addendum, provided that the Commission requires MERC to:

- make available for study in the Commission offices the cost study and annual updates to the study, with the documents being granted trade-secret or another protected status, depending upon MERC requesting and demonstrating that access to the documents should be limited;
- file the cost study covering the period ending December 31, 2011, within 30 days of the date of an Order approving the Agreement; and
- file a study with the Commission three years from the effective date of the Agreement providing information sufficient to enable the Commission to determine whether the Agreement should continue, be modified, or be discontinued.

/jl

CERTIFICATE OF SERVICE

I, Sharon Ferguson, hereby certify that I have this day, served copies of the following document on the attached list of persons by electronic filing, certified mail, e-mail, or by depositing a true and correct copy thereof properly enveloped with postage paid in the United States Mail at St. Paul, Minnesota.

**Minnesota Department of Commerce
Additional Supplemental Comments**

Docket No. G007,011/AI-10-783

Dated this **8th** of **August, 2012**

/s/Sharon Ferguson

Docket 10-0408
Attachment

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