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STATE OF MINNESOTA
IN COURT OF APPEALS
A12-0560

In the Matter of a Petition by Minnesota Power
for Approval of a Rider for Facilities Franchise Fee

Filed November 5, 2012
Affirmed
Worke, Judge

Minnesota Public Utilities Commission
File No. E-015/M-11-806

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Considered and decided by Worke, Presiding Judge; Kalitowski, Judge; and Chutich, Judge.

U N P U B L I S H E D   O P I N I O N

WORKE, Judge

Relator city challenges an order of respondent Minnesota Public Utilities Commission (MPUC) allowing the respondent utility company to charge back to city residents franchise fees to be collected by the city based on the utility's high-pressure pipeline. We affirm.

FACTS

Respondent Minnesota Power runs an electric generating facility, the Boswell Energy Center, in relator Cohasset, a city of roughly 2,500 people. The Boswell Energy Center is a coal-fired plant that used fuel oil for an ignition source until 2008, when Minnesota Power received a permit from MPUC to build a natural gas pipeline to the Boswell Energy Center. Minnesota Power uses natural gas only as an ignition source for the Boswell Energy Center; it does not sell natural gas to anyone. Minnesota Power provides electricity from the Boswell Energy Center to roughly 400 customers in Cohasset and to roughly 141,000 customers throughout northern Minnesota.

The city did not object to the pipeline route, which runs under three public roads and a railroad line, but reserved its right to require Minnesota Power to obtain a franchise in order to operate the pipeline. Minnesota Power refused to acknowledge the city's franchise authority and the pipeline was built without concluding a franchise agreement with the city. The city passed an ordinance requiring all operators of high-pressure pipelines within the city limits to be subject to a franchise and a franchise fee. The stated

purpose of the ordinance was to defray emergency first response, fire, and police protection costs occasioned by the presence of a high-pressure pipeline.

Because Minnesota Power refused to enter into a franchise agreement, the city brought a declaratory judgment action in district court, seeking to require Minnesota Power to obtain a franchise and pay a franchise fee. The district court denied the city's request because the pipeline was not providing natural gas to customers and therefore Minnesota Power was not acting as a public utility; this court affirmed. *City of Cohasset v. Minn. Power*, 776 N.W.2d 776 (Minn. App. 2010), *rev'd by* 798 N.W.2d 50 (Minn. 2011). In a unanimous opinion, the supreme court reversed, holding that:

> 1. A municipality is authorized by Minn. Stat. § 301B.01 (2010) to impose a franchise on a public utility that has constructed and operates a gas pipeline located on public property within the municipality, regardless of whether the pipeline itself supplies gas to the public.
> 2. A municipality is authorized by Minn. Stat. § 216B.36 (2010) to impose a franchise on a public utility that serves customers within the municipality or that uses public property within the municipality to serve customers elsewhere.
> 3. The issuance of a permit by [MPUC] for the construction of a gas pipeline along a prescribed route does not preempt pursuant to Minn. Stat. § 216G.02 (2010) a municipal ordinance requiring a franchise for the operation of the pipeline after construction is complete.

City of Cohasset v. Minn. Power, 798 N.W.2d 50, 51 (Minn. 2011). The matter was remanded to the district court. Minnesota Power asked that the city impose an electrical franchise fee so that it could charge the customers within the city the full cost of franchise fees attributable to the pipeline, which the city refused to do, insisting instead that a natural gas franchise was appropriate. Before the matter could be settled in district court, Minnesota Power petitioned MPUC for an amendment to its electrical rates for Cohasset

customers to include a rider imposing the full cost of any franchise fee attributable to the pipeline solely on Minnesota Power customers located within the city. The city objected to the petition, stating that the supreme court's opinion had settled the matter and the matter was not ripe because no franchise agreement had been concluded; the city asked in the alternative for a contested case hearing.

MPUC concluded that it had primary jurisdiction to determine rate matters between Minnesota Power and its customers and that the record was sufficient, so it declined to postpone its decision or hold a hearing. MPUC further determined that because a franchise fee would be for the sole purpose of raising revenue for the city and because the city had not provided proof of "quantifiable, uncompensated costs due to the construction of the pipeline," it would be "reasonable, equitable, and consistent with past practice for Minnesota Power to recover the franchise fee costs from the ratepayers whose municipality required them, instead of from the general body of ratepayers."

The city asked for reconsideration and MPUC reaffirmed its order. This appeal by writ of certiorari followed.

D E C I S I O N

1. Preemption by Supreme Court

The city argues that MPUC's decision on how to collect a franchise fee imposed by the city was an attempt to avoid the supreme court's decision in *City of Cohasset*. The supreme court held that a city has the right to impose a franchise on a public utility that builds a pipeline within the city, regardless of whether the utility supplies gas to residents of the municipality or serves customers elsewhere, and that this right is not preempted by

the issuance of a permit for construction of a pipeline. *City of Cohasset*, 798 N.W.2d at 51. The opinion analyzes the right of a municipality to require a franchise feeand the obligation of a utility to pay such fee, but it does not discuss how payment will be made.

In contrast, MPUC determined how the franchise fee would be collected by Minnesota Power. This is a ratemaking exercise, which is a legislative function vested in MPUC. *See Schermer v. State Farm Fire & Cas. Co.*, 721 N.W.2d 307, 313 (Minn. 2006) (stating that "ratemaking is a legislative and not a judicial function" and "certain aspects of the ratemaking function, such as the allocation of rates among classes of customers, are peculiarly legislative in nature"). Courts are deferential in their review of the legislative decisions of regulatory agencies, as a part of the separation-of-powers doctrine. *Id.* The supreme court's opinion in *City of Cohasset* does not address allocation of a franchise fee among classes of consumers, nor should it. MPUC, on the other hand, acknowledged that the city has the authority to impose a franchise and franchise fee on Minnesota Power, as instructed by the supreme court, but confined its decision to its regulatory function. There is no conflict between the supreme court's opinion in *City of Cohasset* and MPUC's decision.

2. Contested Hearing

We will reverse an agency decision if it is made upon unlawful procedure. Minn. Stat. § 14.69(c) (2010). The city contends that MPUC wrongfully denied its request for a contested case hearing.

Minnesota Power's petition filed with MPUC sought authority to amend its rates to reflect an anticipated franchise fee. This is a "miscellaneous tariff filing." Minn. R.

7829.0100, subp. 11 (2011) ("'Miscellaneous tariff filing' means a request or notice that does not require determination of the utility's revenue requirement."). Procedurally, after such a filing, a person may submit a comment within 20-30 days, depending on the subject matter, or may request intervention. Minn. R. 7829.1400, subps. 1, 2 (2011). A person may request a contested case proceeding on a miscellaneous tariff filing. *Id.*, subp. 9 (2011). After the time for comments has run, "[i]f the commission finds a contested case proceeding is required, the commission shall refer the matter to the Office of Administrative Hearings." *Id.* "If a proceeding involves contested material facts and there is a right to a hearing under statute or rule, or if the commission finds that all significant issues have not been resolved to its satisfaction, the commission shall refer the matter" for a contested hearing. Minn. R. 7829.1000 (2011). "The burden is on the relator, as the party requesting a contested case hearing, to demonstrate the existence of material facts that would aid the agency in making a decision." *In re Petition of N. States Power Co.*, 676 N.W.2d 326, 335 (Minn. App. 2004).

The city sets forth the items it included in an offer of proof in support of its request for a contested case hearing: (1) Minnesota Power's payments to Cohasset have decreased in real terms because of a variety of public utility strategies; (2) the presence of the pipeline results in public safety costs to Cohasset, which should be shared by all Minnesota Power customers; (3) Cohasset's franchise fee is not intended to pay for a benefit exclusive to Cohasset; (4) Minnesota Power's position would permit utilities to charge cities for all local taxes and fees paid to cities; and (5) the proposed fee structure is not just and reasonable.

Although the city made an offer of proof, it did not provide a basis for its claim that its public safety costs increased because of the pipeline, nor did it demonstrate that the amount of the proposed franchise fee was reasonably tied to those increased costs. "There must be some showing that evidence can be produced that is contrary to the action proposed by the agency." *Id.* In addition, the city acknowledged in its brief that MPUC accepted the statement of facts submitted with the city's comments. ("Cohasset submitted a statement of facts based on the record developed before the Supreme Court. The MPUC found no disputed issue of fact, thereby accepting Cohasset's proffered statement.") If the facts are undisputed, a contested case hearing would serve no purpose.

Because the material facts are not disputed and the city failed to establish what concrete facts it could submit that would support its position, MPUC did not err by refusing to hold a contested hearing. We thus conclude that MPUC did not act upon unlawful procedure. Minn. Stat. 14.69 (c); Minn. R. 7829.1000 (2011).

3. Review on the Merits

We may affirm, reverse, or modify an agency decision if "the substantial rights of petitioners may have been prejudiced" because the agency's decision was, among other things, unsupported by substantial evidence, in excess of its statutory authority, or arbitrary or capricious. Minn. Stat. § 14.69 (2011). Agencies act in both quasi-judicial and quasi-legislative capacities; an agency acts in a quasi-judicial capacity when it "hear[s] the views of opposing sides presented in the form of written and oral testimony, examin[es] the record, and mak[es] findings of fact." *St. Paul Area Chamber of Commerce v. Minn. Public Serv. Comm'n*, 312 Minn. 250, 259-60, 251 N.W.2d 350, 356

(1977). When an agency acts in a quasi-judicial capacity, we review its findings to determine if they are supported by substantial evidence. *Id.* at 260, 251 N.W.2d at 356. Rate allocation, however, is a quasi-legislative function; we will uphold an agency's legislative determination unless the party opposing the allocation shows by clear and convincing evidence that the allocation is unreasonably preferential or prejudicial, or discriminatory. *Id.* at 260-61, 251 N.W.2d at 357.

The issue before us here is MPUC's legislative action: its allocation of rates among Minnesota Power's customers. Because the disputed issue here involves rate allocation, a quasi-legislative function, the city has the burden of showing by clear and convincing evidence that the proposed allocation was unreasonable or discriminatory.

We will affirm an agency's ratemaking decisions, "unless shown to be in excess of statutory authority or resulting in unjust, unreasonable, or discriminatory rates by clear and convincing evidence." *In re Interstate Power Co. Rate Change Request*, 574 N.W.2d 408, 413 (Minn. 1998) (quotation omitted). We presume that rates fixed by an agency are reasonable and just. *St. Paul Area Chamber of Commerce*, 312 Minn. at 254, 251 N.W.2d at 354. Recently, the supreme court has reaffirmed this deferential standard, based on the "filed rate doctrine." *Hoffman v. N. States Power Co.*, 764 N.W.2d 34, 43 (Minn. 2009). The filed rate doctrine, grounded in justiciability and separation-of-powers concerns, "recognizes that rate-setting is a legislative function [of an agency] and that courts are 'ill-suited' to determine the reasonableness of rates established by the agency." *Id.* at 42. The supreme court noted that a filed rate is based on an intricate process of agency decisionmaking that includes balancing rights of both ratepayers and the regulated

industry, and may be based on more than purely economic factors. *Schermer*, 721 N.W.2d at 313-14; *In re Interstate Power Co. Rate Change Request*, 574 N.W.2d at 413.

According to statute, "[r]ates shall not be unreasonably preferential, unreasonably prejudicial, or discriminatory, but shall be sufficient, equitable, and consistent in application to a class of consumers." Minn. Stat. § 216B.03 (2010). Also, "[n]o public utility shall, as to rates or service, make or grant any unreasonable preference or advantage to any person or subject any person to any unreasonable prejudice or disadvantage." Minn. Stat. § 216B.07 (2010). Even considering the deferential standard of review, if a party can demonstrate by clear and convincing evidence that a utility's rates are discriminatory or preferential, we will reverse or modify an agency decision. *See City of Moorhead v. Minn. Pub. Utils. Comm'n*, 343 N.W.2d 843, 846 (Minn. 1984). "Any doubt as to reasonableness should be resolved in favor of the consumer." Minn. Stat. § 216B.03.

To determine if a rate is discriminatory or preferential, the supreme court approved the use of the "benefits and fundamental fairness" test. *City of Moorhead*, 343 N.W.2d at 848. This focuses on the relationship between the utility and its customers, a balance of cost and non-cost factors, and a weighing of competing interests. *Id.* at 848-49. Here, MPUC noted that (1) its policy was to allocate the cost of a municipal franchise fee to residents of the particular municipality; and (2) although the city claimed it had increased public safety expenditures, it declined to identify those costs to the commission, the proposed franchise fee was not tied in any identifiable way to the "magnitude of costs allegedly arising from the pipeline," and the purpose of the franchise

fee appeared to be to raise revenue for the city. Because the purpose appeared to be solely for the purpose of enhancing city revenue, MPUC concluded that the franchise cost should be borne by city residents.

The city argues that its residents receive no particular benefit greater than any other customer of Minnesota Power: the pipeline serves only the Boswell Energy Plant and presumably makes the transmission of power more efficient for all of its customers, not just city residents. The city compares the increased public safety costs to the typical costs of running a utility plant, such as the property taxes that a utility must pay to the municipality within which it is located; the amici also stress this point. This is an appealing argument, but the city failed to produce concrete evidence of those costs. The MPUC's decision is based not so much on evidence that the city does not have extraordinary costs, but on the city's failure to prove that it does. Although the city correctly points out that franchise fees imposed on residents of a municipality usually reflect a special benefit to the municipality, whereas the proposed fee here reflects a particular hardship imposed on the city by Minnesota Power, the city failed to provide clear and convincing evidence of those costs and only demonstrated that the franchise fee would be a revenue-enhancing measure. *Cf. N. States Power Co. v. City of Oakdale*, 588 N.W.2d 534, 543 (Minn. App. 1999) (suggesting that utility companies could recoup costs of burying overhead lines by charging residents of municipalities benefitting from this service because it provided a special benefit to those residents).

MPUC staff acknowledged that the issue here, whether a "franchise fee imposed on an electric utility [that] does not provide retail natural gas service in the city for a natural

gas pipeline," is one of first impression; it is possible that a fuller presentation of public safety costs could have influenced the outcome. But the city had the opportunity to present more concrete information and failed to do so. Under our standard of review, the city bears the burden of demonstrating that the rate allocation was unreasonable or discriminatory by clear and convincing evidence. The city has not meet this burden.

Finally, the city argues that this matter is not ripe for determination, because the city and Minnesota Power have not actually entered into a franchise agreement. But according to the record, it is not unusual for MPUC to "approve a petition for a rider before costs flow through that rider." Further, the city's ordinance establishing its right to demand a franchise appears to impose a fee with or without an agreement:

> As part of any franchise granted pursuant to this Ordinance, the City of Cohasset shall impose a fee of 1% of the fair market value of the gas or liquid delivered via [the pipeline] plus an additional 1% of the fair market value of the transportation of such gas or liquid within the City of Cohasset.

The ordinance goes on to state, "If, for whatever reason, a franchise ordinance . . . is not in force, a franchise fee shall nonetheless be due and payable to the City. The franchise fee, in such circumstances, shall be calculated by the City Administrator in a manner consistent with [the above-quoted section]." This provided specific terms for MPUC to use as a basis for its decision.

Affirmed.