STATE OF MINNESOTA
IN COURT OF APPEALS
A06-2354

In the Matter of the Application of
Northern States Power Company,
d/b/a Xcel Energy
for Authority to Increase Rates
for Electric Service in Minnesota.

Filed January 15, 2008
Affirmed
Crippen, Judge[*]

Minnesota Public Utilities Commission
File No. E-002/GR-05-1428

Richard J. Johnson, 4800 Wells Fargo Center, 90 South Seventh Street, Minneapolis, MN 55402; and

Megan J. Hertzler, Xcel Energy Services, Inc., 414 Nicollet Mall, Fifth Floor, Minneapolis, MN 55401 (for respondent Xcel Energy)

Lori Swanson, Attorney General, Kari Valley Zipko, Jeanne M. Cochran, Assistant Attorneys General, 1100 Bremer Tower, 445 Minnesota Street, St. Paul, MN 55101 (for respondent Minnesota Public Utilities Commission)

Benjamin H. Frisch, 10369 Huntington Drive, Eden Prairie, MN 55347 (for relator Myer Shark)

Considered and decided by Kalitowski, Presiding Judge; Hudson, Judge; and Crippen, Judge.

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[*] Retired judge of the Minnesota Court of Appeals, serving by appointment pursuant to Minn. Const. art. VI, § 10.

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

CRIPPEN, Judge

Relator Myer Shark contends that the Minnesota Public Utilities Commission's decision to approve an increase in electric utility rates is arbitrary and capricious because it includes a tax cost that the utility may never incur and establishes an effective date that violates conditions imposed under an earlier order of the commission. We affirm.

FACTS

On November 2, 2005, respondent Northern States Power Co. (NSP) filed a rate-increase application with respondent Minnesota Public Utilities Commission (the commission). By order dated December 30, 2005, the commission accepted NSP's filing and allowed an interim rate increase, effective January 1, 2006. After referral to an administrative law judge (ALJ) for contested-case proceedings and lengthy hearings before both the commission and the ALJ, the commission filed an order in September 2006 that permanently approved the proposed rate increase (rate-increase order). Relator now challenges both the rate-increase order and the order allowing NSP to charge increased interim rates.

D E C I S I O N

1.

On certiorari review of contested-case proceedings before an administrative agency, we follow the standard set forth in the Minnesota Administrative Procedures Act at Minn. Stat. § 14.69 (2006). *Minn. Ctr. for Envtl. Advocacy v. Minn. Pollution Control Agency*, 644 N.W.2d 457, 463 (Minn. 2002). We are to sustain the administrative

decision unless it is, among other defects, "in violation of constitutional provisions"; or "in excess of the [agency's] statutory authority"; or "unsupported by substantial evidence"; or "arbitrary or capricious." Minn. Stat. § 14.69(a)-(b), (e)-(f); *see also Erickson v. Comm'r of Dep't of Human Servs.*, 494 N.W.2d 58, 62 (Minn. App. 1992) (quoting Minn. Stat. § 14.69(e)-(f) (1990)). And because ratemaking is a quasi-legislative function, decisions of the commission are entitled to the same regard as enactments of the legislature; thus, rates set by the commission are presumed to be valid until the contrary is shown by clear and convincing evidence. *Computer Tool & Eng'g, Inc. v. N. States Power Co.*, 453 N.W.2d 569, 573 (Minn. App. 1990), *review denied* (Minn. May 23, 1990).

"The legislature has delegated authority to regulate public utilities and to determine the reasonableness of the rates they charge to the Minnesota Public Utilities Commission." *Id.* at 572. By law, the commission must establish "just and reasonable" rates for electric service. Minn. Stat. §§ 216B.03, .16, subd. 6 (2006). Just and reasonable rates provide a fair price to consumers while compensating the utility for the cost of furnishing services plus a fair and reasonable profit. Minn. Stat. § 216B.16, subd. 6; *Minnegasco v. Minn. Pub. Utils. Comm'n*, 549 N.W.2d 904, 908 (Minn. 1996). The cost of furnishing utility service includes taxes. *Minnegasco*, 549 N.W.2d at 909. Thus, the commission must consider NSP's tax obligations, as a service cost, in establishing just and reasonable rates. *See id.* at 908-09.

The Minnesota Public Utilities Commission uses the "stand-alone" method to calculate NSP's tax obligation for rate-making purposes. This method determines a

regulated utility's taxes irrespective of the activities of affiliated, unregulated companies. But NSP, as a subsidiary of Xcel Energy, Inc., does not file an individual tax return separate from Xcel. Instead, Xcel files a consolidated return, "netting" profits and losses across corporate subsidiaries as provided under federal tax law. *See* 26 U.S.C. § 1501 (2006) (providing for the filing of a consolidated return). The netting process offsets losses from unprofitable subsidiaries against gains from profitable subsidiaries, arriving at a consolidated, company-wide tax obligation, which may be zero if gains from one subsidiary are completely offset by losses from another. This zero-sum result has been the case at Xcel for several years due to substantial losses from investments in NRG Energy, Inc.

Relator argues that the commission's decision to use the stand-alone method was arbitrary and capricious because it attributes to NSP tax costs which may not actually be incurred or otherwise paid to the government. In support of this argument, relator cites *Fed. Power Comm'n v. United Gas Pipe Line Co.*, 386 U.S. 237, 87 S. Ct. 1003 (1967). There, the Federal Power Commission used the "flow-through" method to calculate a utility's cost-of-service tax allowance, allocating to an individual utility its share of the amount of taxes actually paid on a consolidated return—thus including in the utility's tax cost the tax savings or the tax costs of affiliated organizations. *Id.* at 239, 87 S. Ct. at 1005. The Supreme Court upheld the decision to use the flow-through method, concluding that "in the proper circumstances the Commission has the power to reduce cost of service, and hence rates, based on the application of nonjurisdictional losses to jurisdictional income." *Id.* at 245, 87 S. Ct. at 1008. But the Court did not hold that

regulators were forbidden from using the stand-alone method. *See City of Charlottesville v. Fed. Energy Regulatory Comm'n*, 774 F.2d 1205, 1208 (D.C. Cir. 1985) ("The Court [in *United Gas*] thus authorized, though it did not require, the general use of flow-through methodology to calculate tax allowances."). *United Gas* is not dispositive of whether MPUC's use of the stand-alone method was arbitrary or capricious.

"A decision is not arbitrary and capricious if the agency, presented with opposing points of view, reaches a reasoned decision that rejects one point of view." *In re Grand Rapids Utils. Comm'n*, 731 N.W.2d 866, 871 (Minn. App. 2007) (citation omitted). The record indicates that the commission knew the difference between the two tax-calculation methods and heard expert testimony from multiple witnesses arguing for and against each method. The commission concluded that the stand-alone method, which it has applied to all regulated utilities, continues to be the best method to use in setting rates because it is consistent with the commission's policy to deal separately with regulated and unregulated operations of utility companies and insulates Minnesota ratepayers from the turbulence of the unregulated utility market. The commission reasoned that this policy, including the use of the stand-alone method, requires a sharing both of benefits and risks, and that "[i]t is far more important to protect ratepayers from loss than to give them opportunities for windfalls." The commission's decision was not arbitrary or capricious. *See City of Charlottesville*, 774 F.2d at 1216 ("the Commission's stand-alone approach is reasonable enough to survive our highly deferential review").

Relator also argues that the rate-increase order allows NSP to collect taxes for a private purpose, in violation of the commission's statutory authority and the Minnesota

Constitution. *See* Minn. Const. art. X, § 1. But the rate-increase order does not authorize NSP to collect taxes. Rather, it includes NSP's tax obligations as one of the costs associated with furnishing electric service, which the commission is required by law to do. *See* Minn. Stat. § 216B.16, subd. 6 (requiring the commission to consider "the cost of furnishing the service"); *Minnegasco*, 549 N.W.2d at 909 (including "taxes" in the cost of furnishing service).

2.

Relator's second argument is that the commission's decision to accept NSP's November 2 rate-increase application and allow NSP to collect increased interim rates violated stipulations contained in a 2000 agreement between NSP and the Office of the Minnesota Attorney General (OAG agreement). The OAG agreement was incorporated into a commission order approving the merger between NSP and New Century Energies, Inc., as a condition to the merger, which allowed for the formation of the parent company Xcel Energy. Relator contends that these stipulations prohibited NSP from applying for increased interim rates before January 1, 2006. The commission interpreted the stipulations only to prohibit increased interim rates from taking effect before January 1, 2006, allowing the application to be filed at any time.

Relator argues that the OAG agreement is analogous to a private contract, the terms of which we review de novo. *See Info Tel Commc'ns, LLC v. Minn. Pub. Utils. Comm'n*, 592 N.W.2d 880, 884 (Minn. App. 1999) (noting that the commission's interpretation of a contract is subject to de novo review on appeal), *review denied* (Minn. July 28, 1999). Respondents correctly argue that because the stipulations were

incorporated into the merger order, the commission's subsequent interpretation is entitled to substantial deference.

When issuing the 2000 merger order, the commission acted pursuant to Minn. Stat. § 216B.50, subd. 1 (2000), which requires the commission to investigate any proposed merger of regulated utilities and issue an order approving the merger if the commission finds the merger to be "consistent with the public interest." As an exercise of the commission's expertise in regulating public utilities consistent with the public interest, the merger order is more closely analogous to an administrative regulation than a private contract. And when the language of an agency's regulation is reasonably capable of more than one meaning, we afford "considerable deference . . . to the agency['s] interpretation" of the regulation, which "will generally be upheld if it is reasonable." *St. Otto's Home v. Minn. Dep't of Human Servs.*, 437 N.W.2d 35, 40 (Minn. 1989); *accord Udall v. Tallman*, 380 U.S. 1, 4, 85 S. Ct. 792, 795 (1965) (deferring to administrative interpretation of administrative and executive orders); *Schuster v. Comm'r of Pub. Safety*, 622 N.W.2d 844, 847 (Minn. App. 2001) (deferring to the commissioner's construction of department rule).

Additionally, deferring to the commission's interpretation of its own order is consistent with the state's policy of emphasizing the "maximum flexibility for the regulated party and the agency" in meeting regulatory goals, Minn. Stat. § 14.002 (2006), and our practice of recognizing "a presumption of correctness" in administrative decisions. *Reserve Mining Co. v. Herbst*, 256 N.W.2d 808, 824 (Minn. 1977).

Applying this standard, we must determine whether the language of the merger order is ambiguous, and, if so, whether the commission's interpretation was reasonable. *See In re Cities of Annandale & Maple Lake NPDES/SDS Permit Issuance*, 731 N.W.2d 502, 515 (Minn. 2007) (stating that "when the relevant language of the regulation is unclear or susceptible to different reasonable interpretations, i.e., ambiguous, we will give deference to the agency's interpretation and will generally uphold that interpretation if it is reasonable"). A writing is ambiguous if its language is subject to more than one reasonable interpretation. *Am. Family Ins. Group v. Schroedl*, 616 N.W.2d 273, 277 (Minn. 2000).

The relevant terms of the OAG agreement provide that NSP's base rates will be reduced "for the calendar years 2001 through 2005" and that rates will remain at the reduced level "after the agreement ends, but that NSP may file to increase or decrease its base rates effective at any time thereafter." Later, the OAG agreement provides that "NSP will not increase or petition the Commission to approve an increase in its retail electric rates" before January 1, 2006.

Emphasizing the latter passage, relator argues that the order prohibits NSP from filing a rate-increase application before January 1, 2006. The commission contends that the provisions only restrict when increases could become effective. Both interpretations find support in the text and are reasonable; thus, the meaning is ambiguous. And because the commission's interpretation of the ambiguity is reasonable, we defer to that interpretation.

Affirmed.