STATE OF MINNESOTA
IN COURT OF APPEALS
A07-0730

In the Matter of Xcel Energy's Petition for Affirmation that MISO Day 2 Costs are Recoverable Under the Fuel Clause Rules and Associated Variances

In the Matter of Minnesota Power's Petition for Approval of Revision to Rider for Fuel Adjustment to Recover Costs and Pass-Through Related to MISO Day 2

In the Matter of Otter Tail Power Company's Petition for Approval of Revision to Rider for Fuel Adjustment to Recover Costs and Pass-Through Related to MISO Day 2

In the Matter of Interstate Power and Light Company's Petition for Approval of Revision to Rider for Fuel Adjustment to Recover Costs and Pass-Through Related to MISO Day 2

Filed April 15, 2008
Affirmed
Stoneburner, Judge

Minnesota Public Utilities Commission
File Nos. E-002/M041970; E-015/M05277;
E-017/M05284; E-001/M05406

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Considered and decided by Stoneburner, Presiding Judge; Toussaint, Chief Judge; and Wright, Judge.

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

STONEBURNER, Judge

Respondents Minnesota public electric utilities petitioned respondent Minnesota Public Utilities Commission (the PUC) for authorization to increase rates using Minn. Stat. § 216B.16, subd. 7 (2006), (the fuel clause) to recover costs assessed against the utilities by the respondent regional transmission organization, which the utilities joined in 2002. The PUC, after requiring an investigation and report concerning the requests, granted the petitions. By writ of certiorari, relator, the Minnesota Office of the Attorney General (the OAG), challenges the PUC's order granting the petitions. Relator argues that the PUC erred as a matter of law by allowing recovery of the assessed charges under the fuel clause and that the decision was arbitrary and capricious. We affirm.

FACTS

Minnesota public electric utilities are required to file schedules with the PUC "showing all rates, tolls, tariffs, and charges which it has established." Minn. Stat. § 216B.05, subd. 1 (2006). Generally, once a rate is established it cannot be changed except through a ratemaking procedure before the PUC in which all of a utility's costs and revenues are reviewed simultaneously. Minn. Stat. § 216B.16 (2006). But the PUC "may permit a public utility to file rate schedules containing provisions for the automatic

adjustment of charges for public utility service in direct relation to changes in: (1) federally regulated wholesale rates for energy delivered through interstate facilities . . . ." Minn. Stat. § 216B.16, subd. 7(1) (2006).

In 2002, with the encouragement of the Federal Energy Regulatory Commission (FERC), which has jurisdiction over the transmission and sale of electricity in interstate commerce, and the conditional approval of the PUC, Minnesota public electric utilities joined a regional transmission organization, respondent Midwest Independent Transmission System Operator (MISO). The purpose of the regional transmission organization is to promote efficiency and reliability in the operation and planning of the transmission system and to ensure nondiscriminatory access to transmission services. 18 C.F.R. § 35.34 (a) (2006). Joining MISO involved the utilities (1) transferring virtually all control over the transmission of electricity to MISO; (2) selling virtually all of the electricity they generated to MISO; and (3) buying the electricity needed to serve customers wholesale from MISO.

MISO created the "Day 2 Market," designed to efficiently deliver electricity. Under this scheme, the utilities notify MISO each day of the anticipated needs of their customers and MISO determines which generators and transmission lines can best serve those needs. When, due to full usage loads, it is not possible to use the most efficient generator or transmission line, MISO chooses the next most efficient option. To fund this operation, MISO assesses charges against the member utilities under 32 categories. The utilities petitioned the PUC for authorization to recover these charges from customers under the fuel clause rather than through the more cumbersome rate-case procedures.

In April 2005, the PUC authorized interim recovery of the MISO charges under the fuel clause, conditioned on a refund of any recovered costs that the PUC subsequently determined should not have been recovered under the fuel clause. In December 2005, the PUC issued a second interim order authorizing recovery through the fuel clause of only those MISO charges that the PUC determined to be energy-specific costs. The order disallowed use of the fuel clause to recover "congestion costs," administration costs, and costs associated with operation of the MISO wholesale market. The order directed the utilities to refund the disallowed costs collected under the April 2005 interim order, but, in recognition of the need for further information, stayed the refund requirement to allow for reconsideration motions, and announced its intention to convene a technical conference to further investigate the nature of MISO costs.

MISO (whose petition to intervene was granted by the PUC), the utilities, the Minnesota Department of Commerce (Department), and a group of Minnesota utility investors moved for reconsideration. The PUC consolidated the motions for hearing and accepted the petitioners' joint recommendation that the PUC (1) cancel the refund obligation; (2) provide the parties with time to develop a joint recommendation on (a) which of MISO's 32 charges should be recovered through the fuel clause and which should be recovered through base rates and (b) the method of allocating MISO charges between retail and wholesale margins; (3) require the utilities to provide specific information regarding wholesale margins; and (4) permit deferred accounting of MISO charges not recoverable through the fuel clause for 36 months or until a utility's next rate case, whichever occurs first. The only party opposing the joint recommendation was the

OAG. The OAG reiterated its previously expressed concern that the PUC's action could lead to restricting the PUC's jurisdiction of the utilities.

The OAG participated in the subsequent preparation of a Joint Report and Recommendation (the joint report) which was filed in June 2006, but the OAG did not support the recommendations contained in the report to expand the definition of energy-related charges to be recovered through the fuel clause. The joint report included congestion costs in its definition of energy-related charges based on the explanation that these charges relate to efficiency in alleviating transmission constraints in a manner similar to the utilities' pre-MISO process in which ratepayers paid for the associated increased costs through the fuel clause. The joint report also explained how other MISO non-administrative costs related to costs that the utilities previously recovered through the fuel clause. The joint report contained the utilities' statement of commitment to challenge any FERC action that would preempt the PUC's jurisdiction.

A summary of the joint report was presented to the PUC at a technical conference in October 2006. Handouts at the conference included numerous examples of pre- and post-MISO-Day-2-Market transactions. In December 2006, the PUC issued a final order adopting the recommendations in the joint report. The order references the PUC's statutory charge to protect Minnesota retail utility customers and reiterates that the utilities' participation in MISO is conditioned on compliance with accounting and operational standards designed to safeguard those protections. The order requires the utilities to accept and adopt practices designed by the PUC to ensure just and reasonable rates to Minnesota consumers and protect and facilitate the PUC's jurisdiction and

oversight of the utilities. Specifically, the order requires the utilities to: (1) use their lowest-cost sources of energy to serve Minnesota ratepayers; (2) refund administrative costs previously collected through the fuel clause; (3) limit participation in the virtual-energy market; and (4) report all virtual-energy transactions that affect the fuel clause. Noting that the OAG continued to object to recovery of MISO costs through the fuel clause, the PUC explained in the final order that it has concluded that granting the utilities the authority to recover certain Day-2-Market costs will not interfere with the PUC's exercise of its full legal authority to promote ratepayer interests with respect to all aspects of retail electric service. The PUC identified certain events that would require it to withdraw its approval of recovery of these costs through the fuel clause.

The PUC declined to act on the OAG's petition for reconsideration of its final order, and this appeal by writ of certiorari followed.

D E C I S I O N

I. Standard of review

Minn. Stat. § 14.69 (2006), provides that on review of an agency decision, this court may:

> [A]ffirm the decision of the agency or remand the case for further proceedings; or it may reverse or modify the decision if the substantial rights of the petitioners may have been prejudiced because the administrative finding, inferences, conclusion, or decision are:
>
> (a) In violation of constitutional provisions; or
> (b) In excess of the statutory authority or jurisdiction of the agency; or
> (c) Made upon unlawful procedure; or
> (d) Affected by other error of law; or

(e) Unsupported by substantial evidence in view of the entire record as submitted; or
(f) Arbitrary or capricious.

"When reviewing agency decisions, we adhere to the fundamental concept that decisions of administrative agencies enjoy a presumption of correctness, and deference should be shown by courts to the agencies' expertise and their special knowledge in the field of their technical training, education, and experience." *In re Excess Surplus Status of Blue Cross & Blue Shield of Minn.*, 624 N.W.2d 264, 278 (Minn. 2001) (quotation omitted). But this court reviews errors of law de novo and need not defer to the agency's determination of a matter of law. *In re Denial of Eller Media Co.'s Applications for Outdoor Adver. Device Permits in City of Mounds View*, 664 N.W.2d 1, 7 (Minn. 2003); *No Power Line, Inc. v. Minn. Envtl. Quality Council*, 262 N.W.2d 312, 320 (Minn. 1977).

II. The OAG has failed to meet its burden to establish that the order contains errors of law.

The OAG seeks reversal of the PUC's December 2006 order and remand with instructions for the PUC to reconsider its decision, make specific findings and clarify its conclusions. The OAG argues that the order contains errors of law and is arbitrary and capricious.

The OAG specifically complains that the December 2006 order does not clearly state whether the disputed charges are retail charges or wholesale charges, asserting that the characterization of the charges has critical implications for the PUC's jurisdiction to deny the charges. But the OAG has not explained why the failure to make this distinction in the order constitutes an error of law. The order clearly asserts the PUC's jurisdiction

to deny recovery of the charges under the fuel clause and places conditions on the approval of recovery granted. The OAG's concern about the PUC's continuing jurisdiction over retail-rate regulation appears to be premature and, on this record, we conclude that the PUC did not commit an error of law by failing to characterize the changes in the order. The OAG also complains that the order fails to address the scope of the PUC's authority to review the disputed charges for prudency and deny them if deemed imprudent, but the issue of whether the PUC can review the charges for prudency was not before the PUC in these proceedings.

III. The PUC's order is not arbitrary and capricious

A decision may be deemed arbitrary and capricious if the decision reflects the agency's will and not its judgment, *CUP Foods, Inc. v. City of Minneapolis*, 633 N.W.2d 557, 565 (Minn. App. 2001), *review denied* (Minn. Nov. 13, 2001), or if the agency relies on factors that the legislature did not intend the agency to consider, fails to consider an important aspect of the issue, provides an explanation that is contrary to the record, or renders a decision so implausible that it could not be ascribed to agency expertise. *Trout Unlimited, Inc. v. Minn. Dep't of Agric.*, 528 N.W.2d 903, 907 (Minn. App. 1995), *review denied* (Minn. Apr. 27, 1995). "[An] agency's conclusions are not arbitrary and capricious so long as a 'rational connection between the facts found and the choice made' has been articulated." *Blue Cross & Blue Shield*, 624 N.W.2d at 277 (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168, 83 S. Ct. 239, 246 (1962)). "An agency 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*

Detailing Criteria & Standards for Measuring an Elec. Utility's Good Faith Efforts in Meeting the Renewable Energy Objectives Under Minn. Stat. § 216B.1691, 700 N.W.2d 533, 539 (Minn. App. 2005).

The OAG argues that reversal of the December 2005 interim order without explanation makes the December 2006 order arbitrary and capricious. But the 21-page December 2006 order demonstrates the inaccuracy of the OAG's assertion that the PUC failed to explain the reversal.

The order describes the Day 2 Market and states that

> [i]n theory, the Day 2 Market enables MISO to dispatch generators with lower operating costs to meet the aggregate demand of all customers without regard to which utility owns a given generator or transmission line, or which utility has an obligation to serve a given customer. This process determines the marginal price of electricity—that is, the price of generating the last unit of power required to meet the combined needs of all customers, when all cheaper sources of power are already in use.

The December 2006 order reviews the PUC's prior orders, including the December 2005 interim order and the February 2006 order granting reconsideration and directing the parties to develop a joint recommendation addressing, among other things, which of MISO's 32 charges the utilities should be allowed to recover through the fuel clause. The order addresses the joint report's recommendation that the utilities be allowed to recover all Day 2 Market costs, except administrative costs, through the fuel clause because the charges are type of costs that, prior to MISO, the parties were recovering through the fuel clause. The order specifically addresses and rejects the OAG's fears that the recommendation will lead to the FERC or a court concluding that MISO's federally-

approved tariff would preclude the PUC from continuing to regulate retail electric service in Minnesota. The order states that the PUC "is persuaded that MISO Day 2 costs are sufficiently related to energy costs to warrant cost recovery via the fuel clause . . . [because such] costs are generally the same types of costs that utilities have traditionally recovered through the fuel clause, merely identified with greater precision."

We conclude that the OAG's assertion that the December 2005 order was reversed without explanation is without merit. The December 2006 order contains an explanation of why the PUC reversed a portion of its December 2005 interim order, and authorizes MISO cost recovery through the fuel clause "only on the condition that parties accept and adopt practices designed to 1) ensure just and reasonable rates, 2) protect Minnesota's legal jurisdiction and 3) facilitate [PUC] oversight."

The order states that the PUC "is proceeding based on the legal conclusion that it may continue to exercise its full authority to promote ratepayer interests with respect to all aspects of retail electric service while also granting the utilities' petitions to recover certain Day 2 costs though the fuel clause." The order further provides that any change in that stated legal conclusion "would require reconsideration of this Order," and lists specific contingencies that would require withdrawal of approval to recover Day-2-Market costs through the fuel clause. These contingencies include two specific FERC actions as well as "FERC taking any other action preventing any utility from using its lowest cost generation or resource to serve its native load ratepayers."

The order demonstrates that the PUC thoughtfully considered the issues before it, including the OAG's fears about the PUC's potential loss of jurisdiction over the utilities,

and reached a reasoned decision that is explained in its order. That the order does not answer all of the questions raised by the OAG and does not answer the questions in the manner asserted by the OAG does not make the order arbitrary or capricious.

Affirmed.