

# NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

## ELECTRIC INDUSTRY COMPETITION COMMITTEE

Tuesday, July 16, 2002  
Woodland East Room, Doublewood Inn  
3333 13th Avenue South  
Fargo, North Dakota

Representative Al Carlson, Chairman, called the meeting to order at 9:00 a.m.

**Members present:** Representatives Al Carlson, Robert Huether, Matthew M. Klein; Senators Duane Mutch, Larry J. Robinson

**Member absent:** Senator Herb Urlacher

**Others present:** See Appendix A

**It was moved by Senator Robinson, seconded by Senator Mutch, and carried on a voice vote that the minutes of the April 15, 2002, committee meeting be approved as distributed.**

### TERRITORIAL INTEGRITY ACT AND REGULATION OF ELECTRIC COOPERATIVES

At the request of Chairman Carlson, committee counsel distributed an excerpt from the report of the Electric Industry Competition Committee submitted to the North Dakota Legislative Council in November 2000 and a copy of 2001 Senate Bill No. 2418. The excerpt concerns the Territorial Integrity Act study conducted by the committee during the 1999-2000 interim and reviews the Territorial Integrity Act; previous studies; 1999 proposed legislation; exclusive electric service area laws of South Dakota, Minnesota, and Montana; and testimony received by the committee. Senate Bill No. 2418 relates to exclusions from limitations on electric distribution line extension and service.

Chairman Carlson recognized Ms. Susan Wefald, President, Public Service Commission. Commissioner Wefald distributed two letters concerning the Territorial Integrity Act--one dated July 15, 2002, and one dated June 7, 2000--addressed to Chairman Carlson, copies of which are attached as Appendix B. A copy of her written testimony concerning the regulation of electric cooperatives is attached as Appendix C. She said the position of the Public Service Commission concerning the Territorial Integrity Act is outlined in the commission's July 15, 2002, letter. She said the investor-owned utilities and rural electric cooperatives generally have opposing views concerning territorial issues and the commission must remain impartial if it is to effectively administer its responsibility to resolve territorial disputes.

Commissioner Wefald said the Public Service Commission's jurisdiction over electric cooperatives includes safety, siting of energy conversion and transmission facilities, the raising and lowering of electric supply lines, and the Territorial Integrity Act. She said the commission does not have jurisdiction over rates, contracts, services rendered, adequacy, sufficiency of facilities, or the rules or regulations of electric cooperatives. She said the fiscal impact on the commission of regulating electric cooperatives may be significant. However, she noted, this fiscal impact may be reduced if provisions in any regulation-enabling legislation assumed the reasonableness of existing electric cooperative rates. If statutory authorization to adopt existing rates was not included in the legislation, she said, implementation would likely require expensive general rate cases to establish initial rates for each cooperative.

In response to a question from Representative Huether, Commissioner Wefald said if municipal electric utilities were included with electric cooperatives under regulatory authority of the Public Service Commission, it would increase the cost of regulation for the commission.

In response to a question from Representative Carlson, Commissioner Wefald said current law allows the commission to assess investor-owned utilities for regulation activity performed by the commission. She said this type of regulatory scheme could be enacted if the Legislative Assembly extended the authority of the commission to regulate electric cooperatives and municipal electric utilities.

In response to a question from Representative Carlson, Commissioner Wefald said the Public Service Commission will provide information on the regulation of electric cooperatives by public service commissions or public utility commissions in Iowa, Kansas, Minnesota, Montana, Nebraska, South Dakota, and Wyoming at a future meeting.

Chairman Carlson recognized Ms. Kathy Aas, Minot Community Relations Manager and North Dakota Governmental Affairs representative, Xcel Energy, Inc., Minot. Ms. Aas discussed the operation of the state's Territorial Integrity Act, including the historical beginnings of the Territorial Integrity Act, conditions of the Territorial Integrity Act, and efforts by

the state's investor-owned utilities to change the Territorial Integrity Act. A paper copy of her Powerpoint presentation is attached as Appendix D.

Chairman Carlson recognized Mr. Loren Laugtug, Director, Legislative and Regulatory Affairs, Otter Tail Power Company, Fergus Falls, Minnesota. Mr. Laugtug discussed the operation of the state's Territorial Integrity Act. A copy of his written comments is attached as Appendix E.

In response to a question from Representative Klein, Mr. Laugtug said the state's investor-owned utilities and electric cooperatives have exchanged or traded territory in the past. However, he said, there are fewer and fewer opportunities to exchange territories because all the growth in the state's electric market is occurring on the fringes of its major cities and thus the investor-owned utilities do not have any desirable areas to trade with the state's electric cooperatives. Also, he said, Otter Tail Power Company has served many of its small cities for many years, would like to continue to do so, and is not interested in trading cities to an electric cooperative.

In response to a question from Representative Huether, Mr. Laugtug said based upon Cass County Electric Cooperative balance sheets reviewed by him, the cooperative's balance sheet is composed of 25 percent member equity and 75 percent debt. Thus, he said, one could argue that the members only own 25 percent of the cooperative.

Chairman Carlson recognized Mr. Dennis Boyd, Senior Governmental Affairs representative, Public Affairs Department, MDU Resources Group, Inc. Mr. Boyd reviewed the operation of the Territorial Integrity Act in North Dakota. A copy of his written comments is attached as Appendix F.

In response to a question from Representative Klein, Mr. Boyd said MDU Resources Group, Inc., has made approximately 65 to 70 acquisitions in the last six or seven years and now operates in 35 to 40 states. However, he said, he could not say that this diversification is a direct result of MDU Resources Group, Inc.'s, inability to grow its business in North Dakota.

In response to a question from Representative Carlson concerning 2001 Senate Bill No. 2418, Mr. Boyd said the investor-owned utilities still believe it is a good bill. However, he said, if changes are recommended to the bill, one area of change may be to increase the population cap and another to mandate joint use agreements between investor-owned utilities and distribution electric cooperatives.

In response to a question from Representative Klein, Mr. Boyd said trading or exchanging electric service areas to form compact service blocks would have been more feasible when the state was electrified in the 1930s. Using the city of Braddock as an example, he said, if Montana-Dakota Utilities Company were to exchange the city of Braddock for service areas around Bismarck, it probably would not

be practical because the area around Braddock is served by KEM Electric Cooperative and the area around Bismarck is served by Capital Electric Cooperative. Thus, he said, Capital Electric Cooperative would lose territory to Montana-Dakota Utilities Company while KEM Electric Cooperative would gain territory from Montana-Dakota Utilities Company. He said this may work for Montana-Dakota Utilities Company, but it would not work for the two rural electric cooperatives involved. Also, he said, Montana-Dakota Utilities Company is not interested in abandoning any of the small communities it serves and has recently affirmed this commitment by pursuing the difficult process of renewing its franchise in Watford City. In addition, he said, although there may be some opportunity for investor-owned utilities and electric cooperatives to trade territories within existing cities, there is very little area left for investor-owned utilities to develop within cities and thus the opportunity for exchange or trade is small.

Chairman Carlson recognized Mr. Harlan Fuglesten, General Counsel and Government Relations Director, North Dakota Association of Rural Electric Cooperatives. Mr. Fuglesten reviewed 2001 Senate Bill No. 2418 and discussed the operation of the state's Territorial Integrity Act. He also distributed a bill draft relating to the purposes, powers, and members of electric cooperatives. A copy of Mr. Fuglesten's written comments is attached as Appendix G and a copy of the bill draft is attached as Appendix H.

In response to a question from Representative Carlson, Mr. Fuglesten said within city boundaries the city has the authority to franchise or not franchise one or more utilities. He said city franchises are nonexclusive, but a city could choose to franchise one utility to serve a given area or one utility to serve the entire city.

Chairman Carlson recognized Ms. Mrg Simon, Director of Governmental Affairs, Missouri River Energy Services, Sioux Falls, South Dakota. Ms. Simon said Missouri River Energy Services is a municipal power agency providing wholesale electricity to municipal utilities in North Dakota, South Dakota, Minnesota, and Iowa. She said the dispute over the Territorial Integrity Act is primarily between the state's investor-owned utilities and rural electric cooperatives, but there is a potential that municipal utilities may be affected. She said municipal utilities would like to continue to have the option of providing their own electricity to the citizens of cities they serve.

Chairman Carlson recognized Mr. Bob Graveline, President, Utility Shareholders of North Dakota. A copy of Mr. Graveline's written comments is attached as Appendix I. He said that as rural electric cooperatives continue to serve more and more customers inside city corporate limits, competing utility organizations serving those cities should be treated the same, with both rural electric cooperatives and

shareholder-owned utility companies under the same regulatory body. He said all rural electric cooperatives that provide service within corporate city limits should be under the full jurisdiction of the Public Service Commission because taxpayer money is being used to build urban rural electric cooperative infrastructure and there is no third-party oversight of those cooperatives; taxpaying, shareholder-owned utility companies are ready, willing, and able to take on the burden of providing energy and services to new residents as cities expand and thus there is no need to involve taxpayer investments; lack of Public Service Commission oversight gives cooperatives a competitive advantage over shareholder-owned and regulated utility companies; and without Public Service Commission oversight of cooperatives, many city consumers are being served by an unregulated monopoly unfairly competing with a regulated shareholder-owned utility company.

Chairman Carlson recognized Mr. Fuglesten. A copy of Mr. Fuglesten's written comments concerning the regulation of electric cooperatives by the Public Service Commission is attached as Appendix J. He said electric cooperatives are operated on a nonprofit basis for the benefit of their consumer-owners and locally elected boards of directors adopt policy, set rates, and represent the interests of electric consumers and thus oversight by the Public Service Commission is not needed. He also distributed a survey of state regulation of electric cooperatives, a copy of which is attached as Appendix K.

Chairman Carlson recognized Mr. Thomas Mund, Director, Dakota Valley Electric Cooperative, Milnor. A copy of Mr. Mund's written comments is attached as Appendix L. He discussed cooperative governance and cooperative ratesetting.

Chairman Carlson recognized Mr. George Berg, President and Chief Executive Officer, Nodak Electric Cooperative, Grand Forks. A copy of Mr. Berg's written comments is attached as Appendix M. He discussed regulation of electric cooperatives by the Public Service Commission and the merger between Nodak Electric Cooperative and Sheyenne Valley Electric Cooperative.

In response to a question from Representative Klein, Mr. Berg said the 94 percent approval of the merger by members of the Sheyenne Valley Electric Cooperative occurred because even though that cooperative was smaller, its members realized lower electric rates as a result of the merger.

In response to a question from Representative Klein, Mr. Fuglesten said under North Dakota law, cooperatives are allowed to retain unclaimed capital credits as donated capital.

In response to a further question from Representative Klein, Mr. Fuglesten said he would supply information on capital credits retained by electric cooperatives at a future meeting.

In response to a question from Representative Carlson, Mr. Fuglesten said if electric cooperatives were subject to regulation by the Public Service Commission, it would increase their cost of doing business and the increased cost would have to be passed on to their members which would result in increased electricity rates for those members.

In response to a further question from Representative Carlson, Mr. Fuglesten said if a member is dissatisfied with electricity rates the member can work through the cooperative and its board of directors to resolve the complaint or question. He said cooperatives have a number of meetings and numerous opportunities for members to present their views to the management and directors of the cooperative and provide a greater opportunity for member input than would regulation by the Public Service Commission.

In response to a question from Senator Mutch, Mr. Jay Jacobson, Manager, Dakota Valley Electric Cooperative, Milnor, said electric cooperatives use cost-of-service studies to determine their rates, which is the same method used by the Public Service Commission. Thus, he said, it would duplicate information that must be supplied to the commission which would increase the cost of doing business for cooperatives.

Chairman Carlson recognized Ms. Simon. Ms. Simon said municipal electric utilities are locally controlled by the elected officials in the community they serve. She said if citizens of that community do not agree with how the electric municipal utility is being managed, they can voice their opposition through the electoral process. She said regulation of investor-owned utilities came about because there is an inherent conflict of interest between investor-shareholders and consumers. Thus, she said, regulatory bodies were created to oversee this conflict. She said rural electric cooperatives and municipal electric utilities are not-for-profit consumer-owned utilities that are self-regulated.

## **TAXATION OF ELECTRIC UTILITIES**

At the request of Chairman Carlson, committee counsel distributed a letter from Mr. John W. Dwyer, President, Lignite Energy Council, concerning the taxation of transmission lines. A copy of the letter is attached as Appendix N.

Chairman Carlson recognized Mr. Fuglesten. A paper copy of Mr. Fuglesten's Powerpoint presentation concerning taxation of electric utilities is attached as Appendix O. He presented a history of the committee's review of electric industry taxes and presented a proposal concerning electric industry taxation. Under the proposal, the public utility property tax paid by investor-owned utilities would be eliminated, but the locally assessed land tax would be retained. The 2 percent gross receipts tax, city privilege tax, and high-voltage transmission line tax paid by rural electric cooperatives would be eliminated, but

the locally assessed land tax would be retained. Concerning the generation function, the current coal conversion tax would be left in place and the conversion tax would be made applicable to all generation plants of five megawatts or more. Concerning the transmission component, the rural electric cooperative tax proposal would tax all transmission facilities on a line mile basis with transmission lines of less than 50 kilovolts taxed at \$75 per mile, lines of 50 to 99 kilovolts taxed at \$150 per mile, lines of 100 to 199 kilovolts taxed at \$300 per mile, lines of 200 to 299 kilovolts taxed at \$450 per mile, lines of 300 to 399 kilovolts taxed at \$600 per mile, and lines of 400 kilovolts or more taxed at \$900 per mile. Concerning the distribution function, the rural electric cooperative tax proposal would impose a two-part formula composed of a flat tax of 54 cents per megawatt hour of delivered power and a tax of .92 percent of revenue collected on the retail sale of kilowatt hours of electricity.

In response to a question from Representative Carlson, Mr. Fuglesten said the Association of Rural Electric Cooperatives did not develop the taxation proposal to serve any one interest but has attempted to reach a compromise and develop a proposal that in the long run will be beneficial for all electricity providers.

In response to a question from Representative Klein, Mr. Fuglesten said the proposal was approved by the Association of Rural Electric Cooperatives Board of Directors at its July 8, 2002, meeting.

Chairman Carlson recognized Mr. Boyd. He said Montana-Dakota Utilities Company does not support the tax proposal put forward by the Association of Rural Electric Cooperatives because deregulation is not imminent and thus there is no reason to proceed any further with changing the tax structure of the electric industry. He said one area of interest would be for the committee to study incentives to build transmission facilities in North Dakota to promote the state's lignite and electricity generating industries. Concerning property taxes, he said, one problem experienced by Montana-Dakota Utilities Company is allocating assets between electricity and natural gas for property tax valuation purposes. Also, he said, the Association of Rural Electric Cooperatives taxation

proposal does not address the issue of corporate income taxes paid by the state's investor-owned utilities. He said Montana-Dakota Utilities Company pays from \$2.4 million to \$2.5 million in corporate income taxes annually. Finally, he said, altering the state's property tax system may cause revenue shifts at a time when the Legislative Assembly is facing revenue issues.

Chairman Carlson recognized Mr. Danny E. Kvenvolden, Supervisor, Property Taxes, Otter Tail Power Company, Fergus Falls, Minnesota. A copy of Mr. Kvenvolden's written comments is attached as Appendix P. He discussed electric utility property taxes and said Otter Tail Power Company, Montana-Dakota Utilities Company, and Xcel Energy, Inc., do not feel now is the time to consider a complete overhaul of North Dakota's property tax system.

### **COMMITTEE DISCUSSION AND STAFF DIRECTIVES**

Representative Carlson requested that representatives of the state's investor-owned utilities respond at the next meeting to the tax proposal presented by the Association of Rural Electric Cooperatives.

Representative Carlson requested that committee counsel invite representatives of the cities of Bismarck, Fargo, Grand Forks, and Minot to discuss the role of cities in developing franchise agreements with electricity providers in those cities.

Representative Carlson requested that committee counsel contact the Lignite Energy Council and invite the council to provide an update of the Lignite Vision 21 Project.

Representative Carlson requested that the Legislative Council staff prepare the electric industry taxation proposal submitted by the Association of Rural Electric Cooperatives in bill draft form.

No further business appearing, Chairman Carlson adjourned the meeting at 3:30 p.m.

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Jeffrey N. Nelson  
Committee Counsel

ATTACH:16