

STATE OF MINNESOTA

OFFICE OF THE ATTORNEY GENERAL

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TO: Commissioner LeRoy Koppendraye  
Commissioner Phyllis Reha  
Commissioner Marshall Johnson  
Commissioner Kenneth Nickolai  
Commissioner Tom Pugh

DATE: January 11, 2006

FROM: LISA A. CRUM  
Assistant Attorney General  
445 Minnesota St., #1100  
St. Paul, Minnesota 55101-2128

PHONE: (651) 297-5945  
FAX (651) 282-5832  
TTY: (651) 296-1410

SUBJECT: **Commissioner participation in the Organization of MISO States (“OMS”)**

**LEGAL ISSUE AND RECOMMENDATION**

The Minnesota Public Utilities Commission (“Commission”) inquires whether Commissioner Nickolai’s participation as a board member and secretary of the Organization of MISO States (“OMS”) is a violation of state law.

Based on the facts, legal analysis and discussion below, Commissioner Nickolai’s participation in the OMS as a board member and secretary does not appear to be in violation of state law. By receiving travel reimbursements from OMS, Commissioner Nickolai is neither accepting funds from the regulated utilities nor is he receiving a prohibited gift. Commissioner Nickolai is not violating ex parte communications laws by participating in OMS because the OMS board does not discuss or give advice or recommendations regarding specific docket items before the Commission.

**RELEVANT FACTS**

**Petition**

On January 31, 2005, Laura and John Reinhardt (“the Reinhardts”) filed their Comment Regarding MTO<sup>1</sup> Compliance Filing and Petition to Restore Neutrality to the Minnesota Public Utilities Commission in Docket No. E-999/TL-03-1752 (“petition”).<sup>2</sup> The Reinhardts allege in

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<sup>1</sup> The Commission docket was entitled *In the Matter of the Minnesota Transmission Owners’ Biennial Transmission Projects Report*.

<sup>2</sup> The Reinhardts make a number of allegations and arguments in their petition. Some allegations appear to challenge the validity of the December 2004 CapX Interim Report which found that electricity use in Minnesota will continue to increase with a projected average annual growth rate of approximately 2.5 percent through 2020. The Reinhardts allege that the Commission should (Footnote Continued on Next Page)

the petition that a conflict of interest exists for Commissioner Nickolai to participate as a board member of the OMS because the OMS is funded by the Midwest Independent Systems Operator (“MISO”) which is in turn funded by the regulated utility companies in the Midwest. The Reinhardts allege that because Commissioner Nickolai receives travel reimbursements from OMS he is violating state law by “accepting funds directly from the market participants that the Commission regulates.” Petition at 8. The Reinhardts also allege that, by participating in OMS, Commissioner Nickolai is failing to promote public confidence in the integrity and impartiality of Commission decisions and that Commissioner Nickolai has betrayed the public’s trust and has violated state law by working together with industry participants. Petition at 17. The Reinhardts request that Commissioner Nickolai not be allowed to participate in the OMS.

### **Midwest Independent Systems Operator**

MISO is a non-profit Independent Transmission Systems Operator that serves the electrical needs of the Midwest. Pursuant to regulations of the Federal Energy Regulatory Commission (“FERC”) promoting voluntary formation of Regional Transmission Organizations (“RTOs”), MISO was formed to promote efficiency in wholesale electricity markets and to ensure that electricity consumers pay the lowest price possible for reliable service. *See Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶ 61,285 (December 20, 1999); 18 C.F.R. 35 (2005). In its effort to facilitate formation of RTO’s and ISO’s, FERC “expect[s] that public utilities and non-public utilities, in coordination with state officials, Commission staff, and all affected interest groups, will actively work toward the voluntary development of RTOs.” 18 C.F.R. 35 (2005). Rates charged by MISO are regulated by FERC to ensure the rates are just and reasonable, not unduly discriminatory. 16 U.S.C. §§ 824d, 824e (2000).

MISO operates pursuant to an Agreement of Transmission Facilities Owners to Organize the Midwest Independent Transmission System Operator (“MISO Agreement”). It is the policy of MISO that its operation shall be conducted in such a manner that it is to be separate from the operations of the owners, members, or users of the electric transmission system. MISO Agreement at Appendix A ¶ II.B.

Membership in MISO is open to utilities which own, operate or control electric transmission facilities in interstate commerce and to eligible customers as defined by MISO’s Transmission Tariff on file with FERC. *Id.* at Article One ¶¶ F, I, K. New members may join MISO by submitting an application for membership and payment of an initial membership fee of \$15,000. *Id.* at Article Two ¶ V.A.1.; Article Six. Each member must pay an annual fee of

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not have approved the report. The Reinhardts also seem to disagree with the establishment and function of the MISO and the OMS. Petition at 11-16. This memo only addresses the Reinhardts’ allegations that Commissioner Nickolai’s participation in the OMS is in violation of state law.

\$1,000 to retain its membership. *Id.* at Article Six. Each member is entitled to one vote. *Id.* at Article Two ¶ V.B.5.

Management of all property, business and affairs of MISO is vested in an independent Board of Directors. *Id.* at Article Two ¶ III.B.1. The Directors shall not, within two years of serving on the Board, be a director, officer, or employee of a member, user or an affiliate of a member or a user of MISO. *Id.* at Article Two ¶ III.A.2. The Directors shall also have no material business relationship or other affiliation with any member or user of an affiliate of a member or user of MISO. *Id.*

### **Organization of MISO States**

The OMS is a non-profit, self-governing Regional State Committee comprised of representatives of each state with regulatory jurisdiction over entities within MISO. OMS Funding Agreement at 1. The OMS makes recommendations as appropriate to MISO, MISO Board of Directors, FERC, other relevant government agencies, and state commissions. *Id.* Membership in the OMS is open to all state and provincial regulatory authorities that regulate the retail electricity or distribution rates of the members of MISO. OMS Bylaws at Article II. The OMS also provides an associate membership that is open to all MISO state and provincial agencies involved in energy planning or electric transmission.<sup>3</sup> *Id.*

Generally, each member regulatory authority is allowed to designate one commissioner to serve on the OMS Board of Directors. Commissioner Nickolai is designated as the board member for Minnesota. Commissioner Nickolai serves as an OMS board member and as secretary on the OMS Executive Committee.

States are not bound by actions or resolutions of the OMS. The OMS bylaws specifically state that “[n]o vote of, or resolution passed by, the Board of Directors has any binding effect upon any state or provincial regulatory authority, or any individual member thereof, in the exercise of the authority’s powers.” OMS Bylaws at Article IX.

The OMS is funded through the MISO Board of Directors. OMS Funding Agreement at 1. The initial budget was set at \$500,000 for the period June 15, 2003 through December 21, 2003. Currently, the OMS has an annual budget of \$630,000. *See* OMS 2006 Budget, approved September 9, 2005. The OMS pays pre-approved travel expenses for its board members pursuant to the OMS Travel Expense Reimbursement Policy (“OMS Travel Policy”), revised May 12, 2005. The OMS Travel Policy is modeled after the Expense Reimbursement Policy adopted by the National Association of Regulatory Utility Commissioners. OMS Travel Policy at ¶ A. It is intended to represent a fair policy that complies with both applicable federal regulations and the Funding Agreement between the OMS and the MISO. *Id.* OMS board members are not compensated for their work on the Board of Directors or any other group or committee of the OMS.

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<sup>3</sup> The Minnesota Department of Commerce is an associate member of OMS.

## ANALYSIS

As a preliminary matter, it is helpful to review the role of the Commission in regulating electricity, natural gas and telephone service industries in Minnesota. The Commission is unique in that its responsibilities involve all three branches of government. In its quasi-judicial function, the Commission resolves disputes. *See* Minn. Stat. § 216A.02, subd. 4. As an administrative body, the Commission executes statutes and rules. *See* Minn. Stat. 216A.02, subd. 3. Finally, in its legislative function, the Commission sets broad industry policies. *See* Minn. Stat. § 216A.02, subd. 2. The Commission is funded by the state general fund. The general fund is replenished through the Commission's direct billing of the regulated utilities in Minnesota.

The Commissioners are required to abide by strict conflict of interest, ex parte communication, and impartiality laws. In fact, the Commission is not only bound by state laws applicable to all public officials, *see* Minn. Stat. § 10A, but also by state statutes and rules which apply specifically to the Commission and its staff, *see* Minn. Stat. § 216A and Minn. R. ch. 7825.

These provisions set forth, *inter alia*, a prohibition on receiving income or gifts from a regulated utility and a prohibition on ex parte communications. The Reinhardts argue that the Commission should "have nothing to do with MISO" except to address specific docket items. They also argue that it is a violation of the Commission's code of conduct to communicate with project proposers except through open, public dockets. Petition at 8, 11. These allegations are not supported by the facts or the language of the statutes and rules applicable in this case.

### **1. Commissioner Nickolai is not receiving income or a prohibited gift from a public utility and is not in violation of Minn. Stat. § 216A.035 or Minn. R. 7845.0700.**

Minn. Stat. § 216A.035 provides that "no person, while a member of the Public Utilities Commission . . . shall receive any income . . . directly or indirectly from any public utility or other organization subject to regulation by the commission." Also, Minn. R. 7845.0700 prohibits a commissioner or employee from directly or indirectly soliciting or accepting for the commissioner or employee, or for another person, "any compensation, gift, gratuity, favor, entertainment, meal, beverage, loan, or other thing of monetary value from a public utility, telephone company, or party, that exceeds nominal value."

Thus, for a violation to exist, Commissioner Nickolai must be wrongfully receiving funds or a prohibited gift from a regulated utility. The Reinhardts have failed to allege facts to support any such wrongdoing.

As an OMS board member, Commissioner Nickolai is not receiving income or any other item or service from a regulated utility company. Commissioner Nickolai receives reimbursement of travel expenses directly from OMS when attending OMS board and executive committee meetings or other OMS business meetings. The OMS has in place a travel reimbursement policy that is applicable to all OMS board members. The Reinhardts' suggest that the travel reimbursements made to Commissioner Nickolai must be considered payments of money from a regulated utility because OMS receives its funding from the MISO Board of Directors which in turn receives membership dues from the regulated utilities. The Reinhardts

have cited no authority for the proposition that this funding three times removed from Commissioner Nickolai constitutes “income” from a public utility.

A recent FERC decision refers favorably to the current funding arrangement between MISO and OMS and shows that the FCC does not appear concerned about the arrangement. *See FERC Order Encouraging Further Stakeholder Discussions and Denying Rehearing in Part* (July 7, 2005). This FERC decision concerned establishment and funding of the New England State’s Committee on Electricity (“NESCOE”). FERC found that cost recovery from an RTO or ISO for a regional state committee such as NESCOE was not unprecedented. *Id.* at 13-14. FERC specifically referenced the current funding arrangement between the OMS and MISO as a potential mechanism for NESCOE and ISO-NE to explore. *Id.* FERC commented that the process of having the ISO board approve the regional state committee budget “relieve[s] concerns regarding ... independence ....” *Id.*

It is also interesting to note that FERC receives its funding by imposing surcharges directly upon the regulated utilities. *See* 42 U.S.C. § 7178(a)(1) (2000) (requiring FERC to assess and collect fees and annual charges from public utilities equal to all costs incurred by FERC in a fiscal year); 16 U.S.C. § 824(f) (2000) and 18 C.F.R. § 382.201 (2004) (allowing assessment and fee collection from public utilities only); and *Revision of Annual Charges Assessed to Public Utilities*, Order No. 641, FERC Stats. & Regs. ¶ 31,109, at 31,841 n. 4 (2000). A recent discussion of FERC’s funding can be found in *Michigan Public Power Agency v. FERC*, 405 F.3d 8, 8-11 (2005). Similarly, the Commission receives its funding through the state general fund which is replenished through the Commission’s direct billing of the regulated utilities.

Therefore, Commissioner Nickolai’s participation as a board member of the OMS is consistent with FERC’s guidance that state commissions be involved in policy matters concerning RTOs and ISOs. Commissioner Nickolai is not receiving income or a gift of any kind from the regulated utilities.<sup>4</sup> Instead, Commissioner Nickolai lawfully receives travel reimbursement from the OMS pursuant to the OMS Travel Policy.

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<sup>4</sup> This matter is distinguishable on its facts from *In the Matter of a Commission Investigation of Issues Governed by Minnesota Statutes Section 216A.036*, Commission Docket No. CI-04-1790, heard on October 7, 2005 and order issued on November 2, 2005 (“Order”). In that case, the Commission determined that Former Commissioner Scott violated Minn. Stat. § 216A.035(a) and Minn. R. 7845.0700, subp. 1 by accepting a travel reimbursement of \$706.23 from Integra, an affiliate of a regulated utility company. Order at 10-11. The Commission found that the payment was an ex parte request for reimbursement and constituted income and the solicitation of a thing of monetary value from a public utility, telephone company, or party, that exceeds nominal value in violation of Minnesota Rules 7845.0700, subp. 1. *Id.* The payment was to reimburse Former Commissioner Scott for transportation, meals, lodging and other expenses incurred while visiting Integra at its Portland, Oregon headquarters on May 4, 2004 for purposes of employment discussions. Former Commissioner Scott began employment with Integra on June 16, 2004. *Id.*

**2. Commissioner Nickolai is not communicating directly or indirectly with a participant about a material issue in an open Commission proceeding and is therefore not in violation of state ex parte communications laws.**

The Reinhardts allege that Commissioner Nickolai's participation in the OMS is unlawful because any communication with a regulated utility is prohibited. The Reinhardts' arguments rely on an extremely broad interpretation of the Commission's code of conduct.

Pursuant to Minn. Stat. § 216A.037, subd. 3, the commission adopted its code of conduct rules found at Minn. R. ch. 7845. The purpose of the code was stated as follows:

The purpose of this code is to preserve the integrity and independence of commission decision making and to promote public confidence in the objectivity of commission decisions. Commissioners and employees should maintain high standards of conduct to prevent a conflict or the appearance of a conflict between private interests and official duties. This code must be construed to secure these objectives in keeping with the quasi-judicial function of the commission.

Minn. R. 7845.0300 (2004).

Ex parte communications directly or indirectly between a commissioner and a participant under the commission's rules of practice and procedure are prohibited where the communications involve:

- (1) a material issue during a pending contested case proceeding;
- (2) a material issue in a rulemaking proceeding after the beginning of commission deliberations;
- (3) a material issue in a disputed formal petition; and
- (4) any other communication impermissible by law.

Minn. Stat. § 216A.037, subd. 1 (2004).<sup>5</sup> Commissioners are also prohibited from investing in a public utility, acquiring an interest in a public utility, becoming a director or advisor to a public utility, or actively participating in a public utility's affairs. Minn. R. 7845.0700, subd. 3.<sup>6</sup>

Moreover, commissioners must not have conflicts of interest and must avoid impropriety as set forth in Minn. R. 7845.0400:

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<sup>5</sup> Likewise, a commissioner "shall not communicate, directly or indirectly, with a person or entity who is a party to a pending proceeding before the commission regarding past or future benefits or compensation to be received from that person or entity." Minn. Stat. § 216A.037, subd. 2 (2004).

<sup>6</sup> Certain exceptions apply to this provision at Minn. R. 7845.0700, subp. 3(A)-(D).

Subpart 1. General behavior. A commissioner or employee shall respect and comply with the law and shall behave in a manner that promotes public confidence in the integrity and impartiality of the commission's decision making process.

Subpart 2. Actions prohibited. Commissioners and employees shall avoid any action that might result in or create a conflict of interest or the appearance of impropriety, including:

- A. using public office for private gain;
- B. giving preferential treatment to an interested person or entity;
- C. impeding the efficiency or economy of commission decision making;
- D. losing independence or impartiality of action;
- E. making a commission decision outside official channels; and
- F. affecting adversely the confidence of the public in the integrity of the commission.

The Reinhardts accuse Commissioner Nickolai of "formulating our state's policies in concert with market participants...." and acting as an advisor to the public utilities. Petition at 11, 16-18. However, the Reinhardts have not presented specific facts to support their allegations.

OMS makes recommendations on relevant energy policy-related issues as appropriate to MISO, MISO Board of Directors, FERC, other relevant government agencies, and state commissions. OMS board members do not take on the role of "advisor" to the public utilities. To the contrary, the OMS board members work as a group separate and apart from MISO members and the MISO board. Likewise, MISO itself operates separate from the owners, members or users of MISO.

As a board member and secretary, Commissioner Nickolai does not act to bind the Commission as a whole. The purpose of OMS is not to address pending dockets before this Commission or any state commission. The OMS bylaws specifically require that states are not bound by actions or resolutions of the OMS.

For example, the OMS passed a resolution in March 2004 stating that the OMS Board of Directors will not take a position on the MISO Transmission Expansion Plan for 2003 ("MTEP-3") because "individual state commissions may have siting cases before them that result from the plan." OMS President Susan Wefald briefing memo on May 13, 2004 OMS agenda.

Likewise, the OMS Transmission Planning and Siting Work Group ("Work Group") recognized in its March 24, 2005 resolution ("Work Group Resolution") that:

[S]tate commissioners, siting authorities, and administrative law judges may hear or decide contested cases regarding approval or rejection of particular transmission line projects; parties in contested cases before state agencies have a constitutional right to due process; due process includes, among other things, the right to an impartial decision-maker who has not prejudged any issues in the case; and OMS States generally have rules or guidance about state commissioners, siting authorities, and administrative law judges, and other advisory staff involvement in decision-making and they generally cannot be

biased in favor of or against any party in these contested cases or have prejudged or had the appearance of prejudging issues that may arise in these contested cases.

Work Group Resolution at 1.

The Work Group Resolution also stated that commissioners will not give their opinion regarding the likelihood of approval of a project, and commissioners will not prejudice specific projects that may become the subject of a contested case before a state commission or siting authority. Work Group Resolution at 2.

Commissioner Nickolai has not violated the Commission's code of conduct by participating in the OMS. Open, pending Commission matters are not discussed or decided by the OMS. Commissioner Nickolai is not acting in a role of advisor to public utilities or in any way participating in the utilities' affairs. By offering his time and expertise to RTO establishment as encouraged by FERC, Commissioner Nickolai behaves in a manner that promotes public confidence in the integrity and impartiality of the commission's decision making process here in Minnesota.

**3. Commissioner Nickolai has no conflict of interest nor has he received a prohibited gift under Minn. Stat. § 10A.**

State conflicts of interest laws require state public officials<sup>7</sup> to disclose potential conflicts in writing when the official's duties would require action or decision-making that would "substantially affect the official's financial interests." Minn. Stat. 10A.07. Likewise, Minnesota law prohibits state officials from receiving certain gifts by lobbyists and principals.<sup>8</sup> Minn. Stat. § 10A.071.

The conflicts of interest law under Minn. Stat. § 10A.07 does not seem applicable in this case since the Reinhardts do not allege that Commissioner Nickolai has a conflicting financial interest. The gift prohibition under state law likewise seems inapplicable in this case. Even though the Reinhardts allege that by accepting travel reimbursement for OMS business Commissioner Nickolai is "accepting funds from market participants," they do not specifically argue that Commissioner Nickolai received and accepted a "prohibited gift" as defined under the statute.

As discussed above, OMS reimburses Commissioner Nickolai's travel expenses, pursuant to OMS's Travel Policy, when traveling on OMS business. These expenses are not a gift as defined in 10A.071, subd. 1(b) (2004). A "gift" is specifically defined as "money, real or

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<sup>7</sup> Commissioners of the MPUC are "public officials" as defined under Minn. Stat. § 10A.01, subd. 35 (2004).

<sup>8</sup> A lobbyist or principal may not give a gift or request another to give a gift to an official. An official may not accept a gift from a lobbyist or principal. Minn. Stat. § 10A.071, subd. 1 and 2 (2004).

personal property, a service, a loan, a forbearance or forgiveness of indebtedness that is given and received without the giver receiving consideration of equal or greater value in return.” Certainly, travel expenses could be considered “money” but the definition does not stop at identifying the thing received. The definition specifically requires that the giver of the money not receive any consideration of equal or greater value in return.

In Advisory Opinion #234, the Minnesota Ethical Practices Board addressed a similar question of whether a public official could serve on a board and receive actual and reasonable expense reimbursement for his work. In that opinion, the Board found that the public official could serve on the board of directors of a company that was a lobbyist principal. The Board also found that the public official could receive reimbursement for his “actual and reasonable expenses incurred on behalf of the corporation” and that this would not constitute a prohibited gift “since the corporation would be receiving consideration of equal or greater value in return, that is, the board member’s services and the value of any cost incurred.”

Here, Commissioner Nickolai provides his expertise and time to the OMS board and the executive committee. The OMS reimburses the board members for the expense of traveling for meetings and other OMS business. The Reinhardts have not alleged that Commissioner Nickolai does not provide time and expertise to OMS nor would the facts support such a statement. Thus, the travel reimbursement provided by OMS is not a prohibited gift under state law.<sup>9</sup>

In addition, even if the travel expenses could be considered a gift under state law, the giver of the gift must be a lobbyist or principal as defined by the statute. OMS is neither. While not explicit in their petition, the Reinhardts appear to suggest that OMS and electric utility companies are one in the same because of the way MISO is structured and operated. It is true that some or all Minnesota electric utility companies or their agents are registered as lobbyists or principals. It certainly does not follow in law or fact, however, that OMS must also be categorized as such. To the contrary, OMS is an independent, self-governing organization. OMS is not an organization that engages in lobbying efforts and it is not registered as a lobbyist or principal in any state. OMS serves strictly as a recommending board on energy policy issues faced by FERC, MISO and governmental agencies.

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<sup>9</sup> The law also states that “prohibitions in this section do not apply” if the gift is given “because of the recipient’s membership in a group, a majority of whose members are not officials, and an equivalent gift is given to the other members of the group.” Minn. Stat. 10A.071, subd. 3(b)(1) (2004). Thus, due to Commissioner Nickolai’s membership in OMS which is a specified group; the fact that only one or several members of the group are state officials as defined by the statute; and all board members and executive committee members receive travel reimbursements under the same policy, the travel reimbursement is specifically exempted under the law.

Thus, Commissioner Nickolai's participation on the board and executive committee of the OMS is not a violation of Minn. Stat. chapter 10A because (1) he does not have a conflicting financial interest requiring disclosure, and (2) he has not received a prohibited gift as defined under the statute.<sup>10</sup>

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<sup>10</sup> Pursuant to Minn. Stat. § 10A.02, subd. 12 (2005), Commissioner Nickolai also has the option of requesting an advisory opinion from the Campaign Finance and Public Disclosure Board regarding the Reinhardts' allegations.