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July 2, 2010

Burl W. Haar
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, Minnesota 55101-2147

RE: **Supplemental Comments of the Minnesota Office of Energy Security**
Docket No. G002/M-09-1287

Dear Dr. Haar:

Attached are the additional supplemental comments of the Minnesota Office of Energy Security (OES) in the following matter:

In the Matter of a Request by Northern States Power Company (Xcel or the Company), a Minnesota Corporation, for Approval of Changes in Contract Demand Entitlements.

Based on the additional information provided by Xcel, the OES recommends that the Minnesota Public Utilities Commission (Commission) **approve** Xcel's proposed contract demand entitlements. The OES is available to answer any questions the Commission may have.

Sincerely,

/s/ MARLON GRIFFING, PH.D.
Financial Analyst

MG/ja
Attachment



BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

COMMENTS OF THE
MINNESOTA OFFICE OF ENERGY SECURITY

DOCKET NO. G002/M-09-1287

I. INTRODUCTION

On November 2, 2009, Northern States Power Company (Xcel or the Company), a Minnesota Corporation, filed a request with the Minnesota Public Utilities Commission (Commission) for approval of changes in its contract demand entitlements. Xcel noted in the request that it would provide the final outcome regarding the costs of the Fargo Lateral Project after the February 11, 2010 true-up for the project. On February 10, 2010, the Office of Energy Security (OES) filed Comments with the Commission. The OES concluded that the Company's requested 2009-2010 demand entitlement level, and the forecast methods and Design-Day assumptions upon which the level is based are reasonable. The OES also recommended approval of the Company's proposed treatments of jurisdictional allocations, supplier reservation fees, PGA cost recovery proposal, and assignment of demand costs to interruptible customers.

In its Comments the OES recommended that the Commission withhold approval of the request until Xcel provided in Reply Comments additional information requested by the OES. Xcel filed Reply Comments on March 1, 2010 addressing the following concerns identified by the OES:

- Final economics of the Fargo Lateral Project;
- Effect of the Fargo entitlement and Chisago realignment on the Company's reserve margins for 2009-2010 and subsequent years; and
- The limits of information filed in November of a given heating season to analyze the cost of employing financial instruments for hedging purposes in a season that runs from November to March.

Xcel also filed an updated version of Attachment 4 of its Reply Comments on June 30, 2010.

II. FINAL ECONOMICS AND UPDATE REGARDING FARGO LATERAL PROJECT

Xcel stated in its initial Petition that the final entitlement terms of the Fargo Lateral Project (Project) constructed for the Company by Viking would not be available until February 11, 2010 according to the Cost-Based Precedent Agreement (Agreement) governing the Project. The true-up on this date resulted in a final cost of \$12,110,175, about \$2.6 million less than the \$14.7 million included in the initial filing.

The reduced cost of the Project in turn reduced the daily entitlement Xcel is required to purchase to pay for the Project from the 89,623 Decatherms per day (Dth/day) to 73,577 Dth/day. However, the Company already purchased a few months of volumes at the assumed higher level. Therefore, after an adjustment for these higher volumes, the daily entitlement volume agreed to by Viking and Xcel to be purchased by the Company is 72,213 Dth/day for the remainder of the Agreement, which runs through October 31, 2017.

The reduced volume that Xcel will purchase from Viking to pay for the reduced cost for the Project causes the annual savings from the Project to decline. This outcome results because the required volume purchased from Viking under the terms of the Project is also a cap. Xcel needs 57,178 Dth/day to meet its demand in Fargo. The Company planned to use the excess purchased under the Agreement to meet demand elsewhere. Because the excess volume is reduced due to the smaller required volume from the Project, Xcel must buy natural gas from other sources to meet the other demand, thereby increasing the total net cost of the Project. See Xcel Trade-Secret Attachment 4, Page 3 of 3, Revised June 2010. However, Xcel has demonstrated that the Project continues to be the least costly alternative compared with other options for meeting the Fargo demand.

In a related issue, Xcel reports that Viking told the Company that the Agreement had to be on file with the Federal Energy Regulatory Commission for 30 days before becoming effective. Therefore, Xcel asserted, the Company will adjust for the Agreement in its PGA on April 1, 2010 rather than March 1, 2010.

The OES concludes that Xcel has shown that the firm entitlement purchase it has agreed to with Viking to pay for the Project is the best option. Furthermore, the OES concludes that an April 1, 2010 date to implement the final cost of the Project in its PGA is appropriate.

III. RESERVE MARGIN EFFECT OF FARGO LATERAL ADDITION AND CHISAGO REALIGNMENT AND REASONABLENESS OF RESERVE MARGIN

Xcel states that pipeline counterparties rarely accommodate capacity additions that just keep pace with increasing customer demand. The more favored approach is to require purchases of increments that may temporarily exceed customer growth for several years. This rule especially

holds for construction projects. Although the added capacity may require several years to grow into, the economies of scale from larger projects are expected to offset this concern.

In the case of the Fargo Lateral Project, an expansion was necessary to meet the design-day capacity requirement for customers served by Xcel on the Fargo lateral. The Company's capacity increase of 57,178 Dth/day does exceed that need and increases its reserve margin. However, Xcel provides analysis that demonstrates the reserve margin for its system will decline by about 1 percent a year through the 2013-2014 as demand increases.

Xcel also states that the Chisago Realignment scheduled for November 2010 has no effect on the reserve margin. This realignment has no effect on capacity. Moreover, the Company has not asked for approval of St. Cloud and Hugo expansions presented in the initial filing, so neither of those proposed projects are included in forecasted reserve margins.

The OES concludes that Xcel has demonstrated that its 7.7 percent reserve margin is acceptable given that anticipated customer demand growth will cause the reserve margin to diminish over the next several years.

Furthermore, the OES stated in its Comments that Xcel was increasing its Minnesota heating season reserve margin by 15,796 Dth/day. The Company brought to the attention of the OES in its Reply Comments that the OES had cited the total increase in Minnesota heating season capacity rather than the reserve margin change. Xcel also reiterated that the correct volume is 6,493 Dth/day. The OES regrets its error and thanks Xcel for the correction.

IV. HEDGING TRANSACTION INFORMATION INCLUDED IN THE FILING

The Company states that the information filed in the instant docket is inadequate for analyzing the costs or benefits of using financial instruments for hedging purposes. No monthly index prices, which the financial instruments are settled against, are available at the time of the filing. The OES agrees with Xcel that the Annual Automatic Adjustment filing made each September is the appropriate vehicle for determining annual hedging costs and benefits.

V. OES RECOMMENDATIONS

The OES appreciates the information provided by Xcel and recommends that the Commission approve Xcel's proposed contract demand entitlements.

/ja

CERTIFICATE OF SERVICE

I, Sharon Ferguson, hereby certify that I have this day, served copies of the following document on the attached list of persons by electronic filing, e-mail, or by depositing a true and correct copy thereof properly enveloped with postage paid in the United States Mail at St. Paul, Minnesota.

**Minnesota Office of Energy Security
Supplemental Comments**

Docket No. G002/M-09-1287

Dated this **6th** of **July, 2010**

/s/Sharon Ferguson

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