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February 11, 2015



Mr. Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
121 7th Place East, Suite 350
St. Paul, MN 55101-2147

**RE: In the Matter of Otter Tail Power Company's 2012-2013 Annual Automatic
Adjustment of Charges Report - Electric
Docket No. E999/AA-13-599
Otter Tail Power Company Additional Reply Comments**

Dear Mr. Wolf:

Otter Tail Power Company ("Otter Tail") hereby submits to the Minnesota Public Utilities Commission ("Commission") its Additional Reply Comments in the above described matter.

Otter Tail has electronically filed this document with the Commission and is serving a copy on all persons on the official service list for this docket. A Certificate of Service is also enclosed.

If you have any questions regarding this filing, please contact me at 218-739-8279 or at stommerdahl@otpc.com.

Sincerely,

/s/ STUART TOMMERDAHL
Stuart Tommerdahl
Manager, Regulatory Administration

wao
Enclosures
By electronic filing
c: Service List

STATE OF MINNESOTA
BEFORE THE
MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of Otter Tail Power
Company's 2012-2013 Annual
Automatic Adjustment of Charges
Report - Electric

Docket No. E999/AA-13-599

**OTTER TAIL POWER COMPANY
ADDITIONAL REPLY COMMENTS**

I. INTRODUCTION

On December 31, 2014, Otter Tail Power Company ("Otter Tail"), the Minnesota Department of Commerce Division of Energy Services ("Department") and the Office of the Attorney General-Residential Utilities and Antitrust Division ("OAG") filed comments in the above captioned docket. Otter Tail submits these Additional Reply Comments in response to recommendations and/or comments and questions raised by the Department and the OAG related to the following items:

- A. Otter Tail's annual compliance filings
- B. Otter Tail's MISO Day 1, Day 2 and Ancillary Services Market Reporting
- C. The Department's recommendations related to replacement purchased power
- D. Business interruption insurance

II. OTTER TAIL RESPONSES

A. Otter Tail's Annual Compliance Filings

In Comments filed December 31, 2014, on pages 23 and 24, the Department recommends the Minnesota Utilities Commission ("Commission") accept all of Otter Tail's compliance filings for the 2012-2013 annual automatic adjustment report ("AAA") related to the following items:

- 1. Enbridge Energy compliance filing.
- 2. Reporting of offsetting revenues or compensation.
- 3. Generation maintenance expense reporting relative to most recent rate case maintenance costs.

4. Plant outage's contingency plans.
5. Sharing lessons learned about forced outages.

Otter Tail supports these recommendations.

B. MISO Day 1, Day 2 and Ancillary Services Market Reporting

The Department concluded that Otter Tail has met the compliance requirements for all MISO Day 1, Day 2 and Ancillary Services Market reporting, but has recommended Commission action on one particular item associated with Real Time ("RT") Revenue Sufficiency Guaranty ("RSG") charges Otter Tail incurred in May 2013.

Otter Tail deployed a software program in 2013 that would reforecast Otter Tail load after the initial Day Ahead ("DA") forecast was submitted to MISO. This update to RT forecasts prior to the incurrence of actual RT values, was done for the purposes of providing a more current forecast prior to RT, to allow for potential netting (reducing) of deviations from the valued initially submitted in the DA schedule, which in turn would reduce RSG charges.

As noted in Otter Tail's November 10, 2014 Reply Comments, a data transfer error resulted in an increase in the deviations between forecast loads and actual loads and consequently an increase in RT RSG charges to Otter Tail. The Department has recommended that the Commission dis-allow at least 50 percent of the difference between the May 2013 RSG level and the average RSG monthly charges for this period or require Otter Tail to identify (and explain) the portion of the amount that is due to the software issue.

Otter Tail worked with its programmers to review the data that was transmitted from its forecasting software through its MISO data interface vendor, OATI, and ultimately to MISO, to confirm the exact days where the issue occurred and develop an estimate of the impact. Otter Tail has identified a mid-afternoon forecast submission that from May 7 to May 16, 2013, was transmitting zeros as the updated RT load forecast.

Otter Tail's initial analysis shows that the total RSG charges for those ten days (inclusive of all settlement statements: S7, S14, S55 and S105 for the affected days) was \$176,770.37 (system basis), or \$17,677.04 per day. The daily average RSG charge for all other days that month was \$3,298.68. The incremental increase in RSG charges (over average) for those ten affected days was \$14,378.36 per day ($\$17,677.04 - \$3,298.68 = \$14,378.36$), or a total of \$143,783.56 of increased RSG charges (system basis). Minnesota's share (51.6 percent) of those

RSG charges is approximately \$74,170. The Department has suggested a disallowance of 50 percent of the excess charges or approximately \$37,085.

The development and deployment of this software was the result of an initiative to reduce costs to our customers by providing more up to date forecasts based on more current information. There merits and intent of the initiative were sound. The initial phase of implementation, which began in March of 2013 worked well for nearly two months. A modification for submitting updated DA forecasts in May (another attempt to reduce costs), is what triggered this particular issue. This aspect of the program was stopped when the issue was identified through settlement statements.

The development and deployment of technology enhancements and innovations such as these comes with a certain inherent risks. Even with the costs identified by the Department that were associated with the temporary software problem, this was a reasonable effort by Otter Tail with the sole intent of reducing costs for customers over the longer term. While Otter Tail appreciates the Department's recommended compromise regarding disallowance at half of the identified costs, even this recommended disallowance could have a chilling effect that would stifle interest in innovations such as these.

Otter Tail supports the Department's recommendations for approval of all other MISO Day 1, Day 2 and Ancillary Services Market reporting obligations.

C. Replacement Purchased Power

The Department offers a number of recommendations within its December 31, 2014 Comments with regard to lessons learned, as outlined on page 9 of their Comments. Below is a recap of each recommendation made by the Department, followed by Otter Tail's response.

Department Recommendation:

- 1) Utilities seeking to recover replacement power costs due to a forced outage must provide;*
 - a. Information showing the causes of forced outages;*
 - b. Efforts the utility took to prevent the forced outage;*
 - c. Efforts the utility took to minimize the length of the forced outage;*
 - d. Efforts the utility took to protect ratepayers from having to pay for the costs of the forced outage;*
 - e. Efforts the utility took to recover replacement power costs from all potential sources; and*
 - f. The amount by which the replacement power costs exceed the power costs the utility would otherwise have charged ratepayers.*

Otter Tail Response:

The information outlined above by the Department is generally in-line with information typically requested when a forced outage is analyzed by the Department. Otter Tail notes that depending on the nature of the forced outage; the associated analysis and determination of outage causes; and the outcomes from applicable mitigation efforts (insurance, warranties, etc.) an extended period of time may pass before all information is available. Otter Tail understands that this information provides transparency associated with the efforts utilities must often go through to respond and resolve the various issues associated with forced outages as quickly and prudently as possible. Otter Tail is not opposed to providing responses to the questions above but requests clarification as to how the Department would like this information provided (e.g. AAA filings or other filings).

Department Recommendation:

2) IOUs must develop a searchable database applicable to non-nuclear facilities that shares the attributes of the SEE-IN program and provides for a systematic gathering, review, and analysis of operating experience at (Minnesota) IOUs owned non-nuclear facilities.

Otter Tail Response:

In Reply Comments filed on November 10, 2014, Otter Tail provided a table of information¹ that was jointly developed by the utilities, that summarized numerous conferences; trade organizations and industry memberships; consultants, vendors and contractors; and publications which the utilities have found to be the most informative and beneficial forums to share their information given their unique generation portfolios. The table showed both those forums that all utilities utilized, as well as those that were unique to each utility. As Otter Tail has noted in the past, vendor and technology specific forums often provide the most relevant and targeted information sharing.

In addition to the information shared within that table, Otter Tail benefits extensively from information provided by its insurance providers, who act as a conduit of information acquired from their clients that operate similar facilities. The insurance providers also work

¹ Otter Tail Reply Comments filed 11/10/2014, Attachment 1.

closely with Otter Tail in conducting risk assessments and collaborating on various plant maintenance planning efforts, as part of each facility's on-going loss prevention program.

While the SEE-IN program, a nationally developed program, may serve the nuclear industry quite well due to the breadth of participation across the entire industry, Otter Tail questions the benefit of developing a specific database related to just Minnesota utilities that each have their own unique and diverse mix of generation resources.

Department Recommendation:

3) Utilities should adopt Xcel's program, identified in more detail in Attachment D of its November 10 comments, to hold contractors more accountable for replacement power costs, to the extent those practices are not already in place.

Otter Tail Response:

Otter Tail has processes and procedures in place to select its vendors and contractors, and subsequently manage their work. Procurement and contracting processes assist in hiring the appropriate contractor and putting contractual terms in place that appropriately protect Otter Tail. Project management processes and procedures assist in proper project quality-assurance and in holding contractors accountable. Otter Tail believes its current program serves Otter Tail's needs very well and requests that the Commission not require Otter Tail to adopt Xcel's program. A summary of Otter Tail's processes and procedures specifically related to Procurement, Contracting and Quality Assurance are listed below.

Procurement and Contracting

Standardized contracts are used as much as possible, with formal legal review required of all contracts over \$250,000. Otter Tail believes that the use of competition in the supplier selection process helps Otter Tail achieve reasonable pricing and contractual terms.

Otter Tail strives to have appropriate contractual assurances in place for each transaction by using standardized base contracts as much as possible for the purposes of warding off supplier dilution of the terms during the bid and negotiation process. A required step in Otter Tail's contracting process is the development of a Contract Risk Assessment ("CRA"). The CRA is a worksheet listing the main risks in the particular transaction(s) the contractor is hired for, what sections of the contract the risk is covered, and a narrative describing how each particular risk is addressed in the contract. The CRA allows for an appropriate contract to be developed as the

transaction is negotiated with the supplier. The CRA documentation enhances the risk assessment of a project and is a useful tool in the discussions between Subject Matter Experts (“SME”), Sourcing personnel, Legal, and Insurance in developing risk mitigation strategies. The CRA helps ensure the SME is aware of the risk associated with the work being done by the contractor; the risk is addressed in the contract; and assists the SME in holding the contractor responsible.

Depending on the nature of the project, additional financial assurances are also sought when needed. These assurances can include retainage, liquidated damage clauses, performance guarantees, letters of credit, bonds, etc. For instance, Retainage - the withholding of a portion of each invoice during a large construction project - is an excellent way to ensure performance². The leverage that retainage provides helps ensure Otter Tail’s work remains priority, which is especially critical if there is an issue on a particular project. In the end, this a key strategy that help’s Otter Tail hold contractors accountable.

The contract approval process ensures the contract is reviewed at the appropriate levels up the organizational structure. The CRA is included with the contract as the contract moves through various levels of organizational approvals, to ensure the risks are flagged up for each reader to analyze and understand.

For major procurements on large construction projects, Otter Tail will often hold pre-Request For Proposal and pre-contract execution meetings between the SME, Project Management, Sourcing, Legal and Insurance personnel. These meetings allow for robust discussion regarding the project risks and ultimately help to more efficiently acquire the best vendor and execute the best contract possible.

Quality Assurance (“QA”) Quality Control (“QC”)/ Project Management

Each SME is responsible for quality of the work of the contractor. The size and nature of the project will often dictate what resources are used to ensure quality work is completed. On large projects, Otter Tail uses a separate QA SME and a QA firm. For the smaller construction projects, Otter Tail uses the SME and possibly an outside firm. Formal QAQC programs are

² Not only does the supplier suffer cost of capital expenses for amounts withheld during a long period of time, but (more importantly) the outstanding amounts affect the supplier’s Days Sales Outstanding financial metrics. Any nonperformance of work will be more evident to not only supplier’s operations groups, but also their financial and executive groups.

developed for the larger projects. These plans are vetted heavily by Otter Tail's engineering staff, outside QA firms, and Sr. Engineering Management.

The scope of Project Management ("PM") required depends on the size and complexity of the project / transaction. Otter Tail's larger projects require that a Risk Register is completed by the Project Manager. The Risk Register is a worksheet or table listing the risks associated with the respective project as a whole. These are items that, if they occur, may cause the project to be delayed, cost more than expected, or to be postponed altogether. Each risk is analyzed and an estimated cost as well approximate probability of occurring is listed. The Risk Register assists Project Management in proactively managing the project and increasing the quality of work performed by all involved, including contractors. If needed, items identified in the Risk Register are incorporated into the contractual terms of the supplier. There are other requirements, all of which assist in the project being well run and the respective contractors held accountable.

Given the size and nature of Otter Tail's business and the types of projects Otter Tail is involved in, the sourcing strategies and resources outlined above help Otter Tail to prudently scale and deploy resources as needed to effectively manage contractor performance and achieve desired performance outcomes. While Otter Tail's program may not be identical to that of Xcel's, Otter Tail believes its sourcing and contracting program achieves similar protections and outcomes as Xcel's program does for them.

Department Recommendation:

4) Xcel and other utilities should add language to the "Supplier Warranties" section of the contracts as discussed above to indicate that contractors may be liable for a limited amount of replacement power costs.

Otter Tail Response:

As summarized in Otter Tail's response above, Otter Tail uses numerous strategies and tools to enhance contractor performance. However, as Otter Tail previously stated in Comments submitted earlier in this docket, obtaining a warranty from a vendor for purposes of covering the costs of replacement power, as suggested by the Department, is generally not possible with most vendors without incurrance of significant cost relative to the amount of warranty coverage.

Otter Tail also would have a concern if the Commission were to require such a term without also indicating what amount of cost would be reasonable to add to a procurement

contract to get this additional warranty. It should also be noted that the negotiation of terms and conditions for many procurement contracts can be complex and require the weighing of numerous terms including price, warranty, and other terms.

D. Business Interruption Insurance

Both the Department and the OAG have advanced the idea that the utilities should be exploring further, the use of business interruption insurance for purposes of covering replacement power costs associated with forced outages.

Otter Tail has worked with its insurance provider to understand the Business Interruption (“BI”) products available. Coverages are generally specific to each location, based on each location’s unique factors. In addition Otter Tail found that BI, if available for a location, can be purchased in a range of coverages for a range of perils or exposures. The lowest cost coverage typically insures the differential cost between power generated at the location and power purchased on the open market with coverage for limited perils or exposures (for example equipment breakdown only, natural hazards, contingent BI for offsite assets such as transformers or power lines owned by others, etc...). The highest cost coverage insures 100 percent of the financial impact had the asset not been impaired and would cover the broadest range of perils and exposures.

For its evaluation, Otter Tail has relied on insurance industry rate ranges, as provided by the insurer, for business interruption insurance. Costs range from \$0.55 to \$1.20 per \$100 of limit purchased with a minimum 60 day deductible. The range in pricing is due to varying levels and types of business interruption insurance available and location-specific factors that would be considered in underwriting (as described above). Based upon these premium levels and Otter Tail’s historic performance experience, it was determined that purchasing such insurance would not be a reasonable value. Our insurer notes that less than 5 percent of regulated utilities purchase business interruption insurance.

Otter Tail also notes that the OAG made the following statement in their December 31, 2014 Comments, claiming that Otter Tail had previously stated it had never had an interruption longer than 60 days:

Utilities that found BII (other than pass-through of fuel costs to ratepayers) to be too expensive must provide sufficient explanation as to how they reached that conclusion. One company stated that an interruption of 60 days had never occurred previously in its system, so it did not find it financially feasible to purchase BII.²⁴

What Otter Tail actually stated in its Reply Comments submitted on November 10, 2014 was:

During Otter Tail's 2014 property insurance renewal process, Otter Tail investigated business interruption insurance with its insurance carrier. Otter Tail requested a quote for this type of coverage. The minimum deductible for such coverage was not tied to a dollar value, but was instead tied to the length of time of the business interruption. In this particular case, the time element was 60 days. In other words, the coverage for business interruption would not start until after the forced outage or outage extension went beyond 60 days.

Based on past experience with the durations of forced outages, Otter Tail determined that the cost of the additional premium for such coverage outweighed the benefit of adding that coverage. Otter Tail will likely revisit this or similar types of coverage again in future renewals.

While Otter Tail has historically had very few forced outages that exceeded 60 days, Otter Tail wants to be clear that Otter Tail did not claim that it has never had a forced outage longer than 60 days, as the OAG Comments suggest.

Otter Tail's risk management process associated with plant maintenance and operations includes two primary components. The initial focus is on minimizing the probability of equipment breakdown by implementing maintenance programs focused on engineering out losses before they occur. The second focus is to minimize the financial consequences of losses that do occur. Otter Tail's insurance program is instrumental throughout the risk management process. In addition to providing insurance on physical assets, Otter Tail's insurer provides loss preventions services including site evaluations, risk quality benchmarking, client training and impairment management. Otter Tail attributes its historically low frequency and duration of outages to its loss prevention activity.

Otter Tail knows the probability of a loss exceeding 60 days is something greater than zero however Otter Tail believes the expense required to maintain the loss prevention component of its risk management program is a better use of funds than the purchase of insurance to finance the consequence of losses that its history indicates have a low probability of occurring.

III. CONCLUSION

Otter Tail appreciates the opportunity to provide these Additional Comments in this docket and respectfully requests approval of Otter Tail's 2012-2013 AAA report.

Dated: February 11, 2015

Respectfully submitted,

OTTER TAIL POWER COMPANY

By: /s/ STUART TOMMERDAHL
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CERTIFICATE OF SERVICE

**RE: In the Matter of Otter Tail Power Company's 2012-2013 Annual Automatic
Adjustment of Charges Report - Electric
Docket No. E999/AA-13-599**

I, Wendi A. Olson, hereby certify that I have this day served a copy of the following, or a summary thereof, on Mr. Daniel P. Wolf and Sharon Ferguson by e-filing, and to all other persons on the attached service list by electronic service or by first class mail.

**Otter Tail Power Company
Additional Reply Comments**

Dated this **11th** day of **February 2015**

/s/ WENDIA. OLSON

Wendi A. Olson
Regulatory Filing Coordinator
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Minnesota Docket No. E999/AA-13-599
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