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September 16, 2014

VIA ELECTRONIC FILING

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

Re: In the Matter of Minnesota Power's Renewable Resources
Rider and 2014 Renewable Factor
Docket No. E015/M-14-349

Dear Dr. Haar:

Minnesota Power hereby submits the attached Reply Comments, in response to the Comments on Minnesota Power's 2014 Renewable Resources Factor Filing submitted by the Minnesota Department of Commerce on September 3, 2014.

Minnesota Power appreciates both the thorough review of its 2014 Renewable Resources Factor Filing and the opportunity to provide Reply Comments, specifically addressing the Department of Commerce's concerns about Bison 4 Wind Project costs and the potential for delayed cost recovery.

Please contact me at 218-355-3202 with any questions related to this matter.

Respectfully,

A handwritten signature in black ink, appearing to read "Jennifer Peterson".

Jennifer Peterson

JP:sr
Attach.
cc: Official Service List

**STATE OF MINNESOTA
BEFORE THE
MINNESOTA PUBLIC UTILITIES COMMISSION**

In the Matter of Minnesota Power's Renewable
Resources Rider and 2014 Renewable Factor

Docket No. E015/M-14-349

**MINNESOTA POWER'S
REPLY COMMENTS**

On April 29, 2014, Minnesota Power ("the Company") submitted its Petition for Approval of the 2014 Renewable Factor to the Minnesota Public Utilities Commission ("Commission"). Initial Comments on the compliance filing were submitted by the Minnesota Department of Commerce ("Department") on September 3, 2014. Minnesota Power submits these Reply Comments in response to the Department's Comments, specifically addressing the Department's concerns about Bison 4 Wind Project costs and the potential for delayed cost recovery.

Bison 4 Wind Project Costs

The Department stated in its Comments that the estimate of capital expenditures for the Bison 4 Wind Project in the Company's petition is \$1.2 million or 0.4 percent above the project estimate in Minnesota Power's cost eligibility filing. The Department noted that the capital expenditure figure it used to determine this amount was not in the official record and was instead taken from the financial model used to calculate annual revenue requirements. Minnesota Power respectfully disagrees with the Department's statement that the estimate of Bison 4 project expenditures is over the estimate in the cost eligibility filing. In the Bison 4 cost eligibility filing, Minnesota Power stated the estimated total project cost of the Bison 4 project was \$345 million¹, not \$339.7 million, making the \$340.9 million capital expenditure estimate noted in Table 3 of the Department's Comments lower than the total estimated project cost. Table 3 is

¹ Docket No. E015/M-13-907, Minnesota Power's Bison 4 Cost Eligibility Filing; Dated 9/27/13, Page 9.

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misleading because the project costs listed in the “Cost Eligibility Filings” column for Bison 1², Bison 2³ and Bison 3⁴ are derived from the initial cost eligibility filings; while the number the Department used for Bison 4 (within the same table) is from a financial model. Minnesota Power employs multiple steps to help ensure the lowest costs to customers on the Bison Projects and is proud that the Bison 4 Wind Project is currently within budget with only a few months remaining in the project schedule and that the other Bison projects were completed below the original project estimates.

Additionally, Table 3 from the Department’s Comments (shown below) compares the initial estimated total project costs, including net AFUDC, from the eligibility filings with the capital expenditures included for cost recovery. In Table 2 below, Minnesota Power shows the initial estimated total project costs, including net AFUDC, from the eligibility filings, in comparison to the total budgeted project costs and the total costs, after regulatory adjustments, included in the 2013 and 2014 Factor Filings. This demonstrates that Minnesota Power is within the total project costs as estimated in the respective eligibility filings.

² Docket No. E015/M-09-285. Minnesota Power’s Bison 1 Cost eligibility Filing; Dated 3/23/09, Page 16.

³ Docket No. E015/M-11-234. Minnesota Power’s Bison 2 Cost Eligibility Filing; Dated 3/24/11, Page 7.

⁴ Docket No. E015/M-11-626. Minnesota Power’s Bison 3 Cost Eligibility Filing; Dated 6/21/11, Page 7.

Table 1: Table 3 from the Department's Comments

Table 3: Summary of Capital Expenditure Estimates (\$ Millions)			
	Capital Expenditures		
	Cost Eligibility Filings	2013 RRR Filing	2014 RRR Filing
	1/	2/	3/
Bison 1	177.6	172.7	173.2
Bison 2	157.0	144.6	147.7
Bison 3	157.0	146.3	148.7
Bison 4	339.7	n/a	340.9

1/ Cost Eligibility Filings:
 Bison 1 - Docket No. E015/M-09-285
 Bison 2 - Docket No. E015/M-11-234
 Bison 3 - Docket No. E015/M-11-626
 Bison 4 - Docket No. E015/M-13-907 - The Department notes that the capital expenditure figure for Bison 4 in the table is not in the official record in the Bison 4 cost eligibility Docket. The reported \$339.7 million was taken from the financial model used to calculate the annual revenue requirements included in Attachment 2 to the Department's November 12, 2013 Comments in that Docket.

2/ Docket No. E015/M-13-410
 3/ Petition, Exhibit B-3

Table 2: Minnesota Power's Adjusted Capital Expenditure Table

	<u>2013 RRR</u>			<u>2014 RRR</u>	
	Cost Eligibility	Budget	Cost Recovery	Budget	Cost Recovery
	Filing Total Project Cost Estimate /1	Total Project Costs 2/	Project Costs 3/	Total Project Costs 2/	Project Costs 4/
Bison 1	177.6	176.9	171.2	177.5	171.7
Bison 2	157.0	146.2	142.9	149.3	145.9
Bison 3	157.0	147.6	145.2	150.1	147.5
Bison 4	345.0	n/a	n/a	345.0	337.9

1/ Total project costs (capital expenditures plus net AFUDC)
 Bison 1 - Docket No. E015/M-09-285
 Bison 2 - Docket No. E015/M-11-234
 Bison 3 - Docket No. E015/M-11-626
 Bison 4 - Docket No. E015/M-13-907

2/ Total Project Costs MP Budget (capital expenditures plus net AFUDC)

3/ Total Project Cost MP Budget less regulatory adjustments
 (Less wholesale AFUDC, less internal costs) Docket No. E-015/M-13-410, Exhibit B-3

4/ Total Project Cost MP Budget less regulatory adjustments.
 (Less wholesale AFUDC, less internal costs, less AFUDC on internal costs) Petition, Exhibit B-3

The Department cited the Commission’s decision in Docket No. E002/M-09-1048 as the basis for its recommendation to limit Bison 4 costs to \$339.7 million. The order language from the docket cited is as follows, “In setting guidelines for evaluating project costs going forward, the TCR project cost recovered through the rider should be limited to the amounts of the initial estimates at the time the projects are approved as eligible projects, with the opportunity for the Company to seek recovery of excluded costs on a prospective basis in a subsequent rate case.⁵” Minnesota Power interprets the “amount of the initial estimate at the time the projects are approved” to be the total project cost, which in the case of Bison 4 is \$345 million. The Company disagrees with the Department’s interpretation of the cost cap being any number other than the total project cost as stated in the initial eligibility filing.

Proposed Extended Recovery Period

In its Comments, the Department also recommended that the Commission consider requiring the Company to stretch the recovery of its tracker balance over a period of two years, in order to mitigate the proposed rate increase and smooth some of the volatility expected in Minnesota Power's RRR rates over the next few years. The Department acknowledged that this may be harmful to the Company financially, as it does not earn a return on the tracker balance.

The Department cited concerns about the impact of significant, but short lived, rate increases related to renewable energy investments on customers. The Department noted that the tracker balance, which accounts for nearly 40% of all 2014 RRR costs, is likely to be paid off within the next two or three years. While Minnesota Power certainly understands the concern over spikes in customer rates, the Company is currently expending more capital on renewable and environmental retrofit projects than ever before (including the Bison 4 Wind Project, the Boswell Energy Center Unit 4 Mercury Emissions Reduction Project and the Thompson Hydroelectric Restoration Project). **[TRADE SECRET DATA EXCISED]**⁶. Project planning for these large investments was based upon the expectation of timely current cost recovery.

Additionally, Minnesota Power's current credit rating is, in part, predicated upon the anticipation of current cost recovery for eligible investments. This rating has been challenged by the timing of the cost recovery process. Timing delay related to the Renewable Resources Rider is primarily due to the postponement of establishing updated billing factors in the 2013 RRR docket⁷. Prior to the submission of the 2013 RRR factor filing, Minnesota Power was working with the Department in the Company's 2011 Transmission Cost Recovery ("TCR") docket⁸ to resolve issues related to tax handling in the calculation of annual revenue requirements. Without certainty on the correct treatment of the same tax matter in the RRR filing, the Company refrained from filing its

⁵ Docket No. E002/M-09-1048. Xcel Energy's 2010 TCR. Order Dated 4/27/14.

⁶ **[TRADE SECRET DATA EXCISED]**

⁷ Docket No. E-015/M-13-410. Minnesota Power's Petition for Approval of its 2013 Renewable Resources Rider Factor.

⁸ Docket No. E-015/M-11-695. Minnesota Power's Petition for Approval of its 2011 Transmission Cost Recovery Rider Factor.

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2013 RRR billing factor until the issue could be resolved in the TCR docket. Upon resolution of the issue, the Company filed a petition requesting an update to its 2013 RRR and TCR billing factor calculations. This is the primary cause of an increase in the RRR tracker balance on December 31, 2013, which would have been billed to customers in a prior period. This also creates a larger increase percentage over the previous year; however, the delay in collection was also a benefit to Minnesota Power's customers at that time. Furthermore, regulatory timing is also a factor in the current docket as the 2014 RRR Factor Filing was submitted in April 2014 with Initial Comments filed in September 2014. For each month it takes to establish the new 2014 renewable factors as filed, Minnesota Power is forgoing an additional \$3.4 million in cash collections⁹.

Additionally, altering the cost recovery from the standard practice of twelve months to twenty four months may cause credit analysts to lose faith in the credibility of the current cost recovery system and consider downgrading the Company's credit rating. If Minnesota Power's credit rating is lowered it would result in increased costs to borrow funds that are currently needed to meet the ongoing construction needs of the Company, thereby affecting customers. These increased borrowing costs would result in increased customer rates. [TRADE SECRET DATA EXCISED]¹⁰.”

[TRADE SECRET DATA EXCISED]¹¹.

Minnesota Power is committed to meeting the state's Renewable Energy Standard while maintaining the affordability and reliability of service for its customers. The Company also recognizes that cost recovery petitions must undergo regulatory review. However, while recovery of the current tracker balance over the standard twelve month period will cause a rate increase for customers, the potential downgrading of Minnesota Power's credit rating could cause the cost of capital to rise – thereby also harming customers. If the Company does not receive current cost recovery it is forced to finance additional capital, which results in an additional cost. Low financing rates for necessary capital are beneficial to customers overall, not exclusively for renewable and environmental projects alone.

⁹ 2014 Revenue Requirements: \$85,798,725/12 minus 2013 revenue requirements \$44,615,189/12 equals \$3,431,960/month

¹⁰ [TRADE SECRET DATA EXCISED]

¹¹ [TRADE SECRET DATA EXCISED]

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While the RRR rate increase is viewed as significant by the Department, and Minnesota Power itself is sensitive to customer cost impacts, the increase should also be viewed within the context of Minnesota Power's overall rates to its customers. Minnesota Power offers some of the lowest utility rates in the nation. As mentioned in the Company's 2013 Integrated Resource Plan, based on 2012 statistics¹² compiled by the Edison Electric Institute ("EEI"), Minnesota Power's total average retail electric rate was the fourth lowest in the United States among the 169 providers surveyed. Additionally, Minnesota Power's rates were determined by EEI to be the second lowest in the West North Central region and the lowest in the state of Minnesota. In a more recent EEI study which covered the previous twelve month period ending in April 2014, Minnesota Power had the lowest average total electric rates of any Investor Owned Utility in the nation. So while the recovery of the 2014 RRR tracker balance will result in an increase to customers, Minnesota Power will still provide electric power to customers at some of the most competitive rates in the country.

If the Commission agrees with the Department and supports an extended cost recovery period, Minnesota Power then requests that it earn a rate of return on the tracker balance to offset the additional costs that will be incurred as a result of delayed recovery. The Commission established a precedent in allowing a rate of return on deferred cost recovery in Otter Tail Power's 2012 Renewable Resource Cost Recovery Adjustment Factor, in which Otter Tail Power was allowed to add a carrying cost of 8.33 percent to the unamortized balance during the extended recovery period.¹³ Minnesota Power would respectfully request the Commission consider a similar arrangement if it determines the Company should extend its cost recovery period.

¹² "Typical Bills and Average Rates Report Summer 2012", dated 7/1/12. Also referenced in MP's IRP, Docket No E015/RP-13-53, dated 3/1/13, on Page 1.

¹³ Docket No. E-017/M-08-1529. Order Approving Otter Tail Power Company's Renewable Resource Cost Recovery Factor. August 10, 2009.

CONCLUSION

Minnesota Power appreciates both the thorough review of its 2014 Renewable Resources Rider Factor Filing and the opportunity to provide Reply Comments. Minnesota Power would like to reiterate that the cost of the Bison 4 Wind Project is currently within the initial project estimate of \$345 million, as approved by the Commission, with only several months of the project remaining. Additionally, with the large number of ongoing capital renewable, transmission and environmental projects, delaying cost recovery from one to two years would be financially harmful to Minnesota Power. The Company has acted aggressively in developing and incorporating renewable energy assets into its generation portfolio, with Bison 4 being the most recent wind development, and expects to meet the state's Renewable Energy Standard by 2015 – ten years ahead of schedule. Minnesota Power respectfully requests timely cost recovery on its approved renewable energy investments.

Dated: September 16, 2014

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Jennifer J. Peterson", with a long horizontal flourish extending to the right.

Jennifer J. Peterson
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STATE OF MINNESOTA)
) ss
COUNTY OF ST. LOUIS)

AFFIDAVIT OF SERVICE VIA
E-FILING AND
FIRST CLASS MAIL

Susan Romans, of the City of Duluth, County of St. Louis, State of Minnesota, says that on the 16th day of September, 2014, she e-filed Minnesota Power's Reply Comments in Docket No. E015/M-14-349 on the Minnesota Public Utilities Commission and the Minnesota Department of Commerce via electronic filing. The remaining parties on the attached Official Service List were served as indicated.

Susan Romans

Susan Romans

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