

## Staff Briefing Papers

Meeting Date December 20, 2018

Agenda Item **\*\*10**

Company Minnesota Power

Docket No. **E015/M-18-603**

In the Matter of Minnesota Power's Petition for Approval of an Amendment to Electric Service Agreement Between Verso Minnesota Wisconsin LLC and Minnesota Power

Issue Should the Commission approve Minnesota Power's petition to amend the Electric Service Agreement between Verso Minnesota Wisconsin LLC and Minnesota Power?

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651-201-2215



### Relevant Documents

### Date

MP Petition to Amend ESA between Verso and Minnesota Power	September 21, 2018
Verso Comments (John Bastian)	September 27, 2018
Mary Tourville's Comments on Behalf of Verso Duluth Paper Mill	October 10, 2018
Emily Larson, Mayor of Duluth, Comments	October 16, 2018
Department of Commerce – Comments	October 17, 2018
Mark Dylla's Comments on Behalf of Verso Duluth Paper Mill	October 18, 2018
Minnesota Power Reply Comments	October 22, 2018
Department of Commerce – Reply Comments	November 16, 2018

N.B. The Office of the Attorney General requested an extension of the procedural schedule but did not file comments.

The attached materials are work papers of the Commission Staff. They are intended for use by the Public Utilities Commission and are based upon information already in the record unless noted otherwise

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## I. Statement of the Issue

Should the Commission approve Minnesota Power's Petition to amend the Electric Service Agreement between Verso Minnesota Wisconsin LLC and Minnesota Power?

## II. Introduction

Minnesota Power (MP) proposes to amend a contract, approved by the Commission in Docket No. E-015/M-12-1025 in an order dated December 10, 2012, between MP and Verso Corporation. This existing contract is called the "2012 Amendment" and its term extends through at least December 31, 2022.<sup>1</sup> This proposed amendment is called the "2018 Amendment."

The Department of Commerce, Division of Energy Resources (Department) recommends approval of the 2018 Amendment to the Electric Service Agreement between Verso Minnesota Wisconsin LLC and Minnesota Power.

Several employees of Verso Minnesota Wisconsin LLC have submitted letters supporting the 2018 amendment to the agreement as has the Mayor of Duluth.

## III. Relevant Statute

Minn. Stat., Section 216B.1621. Electric Service Agreement.

Subdivision 1. Agreement. When a retail customer of a public utility proposes to acquire power from or construct a new electric power generation facility in the assigned service area of the utility serving the retail customer to provide all or part of the customer's electric service needs, the public utility may negotiate with and enter into an agreement with the customer to supply electric power to the customer in order to defer construction of the facility until the utility has need of power generated by the proposed facility, if the Public Utilities Commission approves the agreement under subdivision 2.

Subd. 2. Commission approval.

- (a) The commission shall approve an agreement under this section upon finding that:
  - (1) the proposed electric service power generation facility could reasonably be expected to qualify for a market value exclusion under section 272.0211;
  - (2) the public utility has a contractual option to purchase electric power from the proposed facility; and
  - (3) the public utility can use the output from the proposed facility to meet its future need for power as demonstrated in the most recent resource plan filed with and approved by the commission under section 216B.2422.
- (b) Sections 216B.03, 216B.05, 216B.06, 216B.07, 216B.16, 216B.162, and 216B.23 do not apply to an agreement under this section.

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<sup>1</sup> The Department notes that the original term expires on December 31, 2022.

#### IV. **Background – “2012 Amendment”**

The “2012 Amendment” was the culmination of a tortuous history involving Duluth Mills. A brief synopsis of it is given in indentation below:

Verso Corporation, an Ohio-based Company, now operates Duluth Mills which makes supercalendered paper (i.e., paper with a high gloss finish) used for magazines, catalogs and miscellaneous retail inserts. Duluth Mills has evolved in a competitive marketplace over the years – it was called Consolidated Papers in 1987; it was acquired by Stora Enso (a Finnish company) in September, 2000; and subsequently acquired by Verso in 2015.

The Commission approved a restated electric service agreement between MP and Consolidated Papers in 1997.

This contract was further amended when Stora Ensa acquired Consolidated Papers in 2000.

In 2005, the contract was further amended and restated in Docket No. E015/M-05-1989.

In 2007, NewPage acquired Stora Enso’s paper assets, including the Duluth Mills, and the Agreement was assigned to NewPage. However, in 2011, NewPage filed for Chapter 11 bankruptcy and filed a Plan of Reorganization in 2012.

On September 25, 2012, NewPage filed a petition with the federal bankruptcy court to assume contracts and Minnesota Power concurrently filed a petition with Commission to amend the Agreement and extend the term through at least December 31, 2022 (“2012 Amendment”).

In 2015, Verso acquired NewPage including the Duluth Mills and the Agreement. Verso, in turn, filed for bankruptcy in 2016 but emerged through a successful financial restructuring, which included continuing the “2012 Amendment” with Minnesota Power for Duluth Mills.

#### V. **“2018 Amendment” to the “2012 Amendment”**

MP proposes to amend the 2012 Amendment in three principal ways.

The proposed amendment:

- 1) extends Verso’ agreement to purchase electricity from Minnesota Power through at least the end of 2024 without any prior right of termination; the amendment continues after December 31, 2024 on a rolling four-year basis until a cancellation notice is issued by either party;

2) modifies Verso's Large Power Incremental Production Service (IPS) Threshold<sup>2</sup> by lowering Duluth Mill's predetermined demand level -- to allow more effective management of electric use; and

3) offers additional risk protections for Minnesota Power through a financial corporate guarantee and customer billing modifications:

a) in the proposed amendment, Verso has agreed to a corporate parent guaranty in the event payment is not received under the Agreement – this provision is significant in light of the multiple bankruptcy filings by companies which have owned and operated the Duluth Mills; and

b) the 2012 Amendment provided for voluntary weekly prepayments to Minnesota Power but also provided financial performance criteria to terminate weekly expedited billing; the proposed amendment removes the financial performance criteria.

With respect to the modification of the IPS threshold (2. above), MP notes that the proposed Amendment would allow more effective management of electric use at its Duluth Mills. The IPS Threshold set in the current Agreement does not reflect Verso's current operations and recent energy efficiency improvements. The LP Service Schedule does not address IPS Threshold or energy efficiency improvements. With this Amendment Minnesota Power and Verso are working to support the long term competitive position of the Duluth Mills.

If approved by the Commission, the proposed 2018 amendment will supersede specific provisions in "2012 Amendment."

## VI. Proposed Amendment and Public Interest

Minn. Stat. § 216B.05, subd. 2a requires that any contract between a public utility and a customer involving rates, conditions, or terms not contained in approved schedule should be filed for Commission approval.

At the outset, MP states that Verso's agreement to purchase its electric service requirements for its Duluth Mills from MP Power through at least December 31, 2024 is critically important to MP and its other ratepayers.

MP maintains that the Petition in and of itself will have no effect on MP's base rates.

MP argues that, under the Amendment, it will continue to realize a certain minimum amount of demand revenues between January 2019 and December 2024, but MP also expects Verso to

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<sup>2</sup> Under MP's Large Power Incremental Production Service (IPS) rider, a large customer specifies a pre-determined level (threshold) of demand and the customer's measured demand above the threshold is not subject to any demand charges or ratchet provisions associated with contract demand; further, when the measured demand exceeds the threshold level, the energy associated with the incremental demand above the threshold is subject to an energy charge equal to the Incremental Production Rate. Because of the lowering of the threshold level, Verso will realize savings on its monthly bill. However, MP expects Verso to purchase more electric power and energy than the demand purchases that are minimally guaranteed under the existing Agreement.

purchase more electric power and energy than the demand purchases that are minimally guaranteed under the existing Agreement. MP anticipates that with Verso's expected level of production and power demand level associated with that production, "Minnesota Power will receive more in demand revenues alone during the extended term of the Agreement."

Verso's minimum service requirement commitments are very significant and MP maintains that if it were to face the shutdown of any LP customer, the scenario for all ratepayers would look much bleaker without this Amendment and the corresponding revenue assurances it provides.

MP stresses that when these commitments are coupled with Verso's obligation to purchase its electric service needs from MP through at least December 31, 2024, as provided in the Amendment, all of MP's other ratepayers will be in a better situation than they would otherwise be without this Agreement.

MP notes that the benefits of the proposed amendment to Verso and MP will be realized without any changes to rates provided in its tariffs.

## VII. 2018 Amendment and EITE

Verso, by virtue of its nature and size of operations, is qualified for competitive energy rates under Minn. Stat. § 216B.1696 (Energy-Intensive Trade-Exposed statute). Verso's operations deal with paper mill (specifically noted in the EITE statute) and presumptively meets the requirements of § 216B.1696, Subd. 1 (4).<sup>3</sup>

MP notes that the present Agreement is not conditioned upon or tied to Commission review of MP's EITE docket and any associated tariff filings. MP adds that Verso and MP both recognize that more flexible electric service agreements along with more competitive rates will significantly assist in sustaining Verso's significant paper operations in Duluth.<sup>4</sup>

While Verso's operations are within the definition of EITE statute, MP states, somewhat cryptically, that the Agreement is not otherwise dependent upon or contingent on any EITE related decisions by the Commission. MP notes that it is its intent, to the extent practicable, to evaluate and utilize customized Electric Service Agreements to best match its electric service to its customers' unique needs.

Minnesota Power notes that it intends to continue this practice by making similar terms and conditions available to other LP customers who are similarly situated.

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<sup>3</sup> "a retail customer that (i) collectively imposes a peak electrical demand of at least 10,000 kilowatts on the electric utility's system, (ii) has a combined annual average load factor in excess of 80 percent, and (iii) is subject to globally competitive pressures and whose electric energy costs are at least ten percent of the customer's overall cost of production."  
<https://www.revisor.mn.gov/statutes/cite/216B.1696>

<sup>4</sup> Initial applicability of the EITE Rider is limited to the following customers who have signed EITE Customer Commitment Letter Agreements: ArcelorMittal – Minorca Mine, Blandin Paper Company, Boise Paper, Hibbing Taconite Company, Magnetation LLC, Mesabi Nugget Delaware LLC, Mining Resources LLC, Sappi Cloquet LLC, United States Steel Corporation, United Taconite LLC/Northshore Mining Company, and Verso Corporation. Customers taking service under this Rider should have total power requirement of at least 2,000 kW. See MP Electric rate Book, Vol. 1, Section V, p. 98.0.

## VIII. Department's Initial Comments

The Department concluded that the Amended Agreement is in the public interest and should be approved by the Commission.<sup>5</sup>

The Department noted that the proposed extension of the duration of the Electric Service Agreement (ESA) from December 31, 2022 to December 31, 2024 is in the public interest as it would be beneficial to both MP and its ratepayers. Because Verso's current and proposed rates include contributions to MP's fixed costs, MP's ratepayers would benefit from such contributions that would otherwise have to be collected from them (absent the ESA).

The Department concluded that the proposed reduction to the IPS threshold would allow Verso to lower its energy cost while at the same time allowing MP to recover its incremental energy and transmission costs without negatively impacting MP's other ratepayers.

The Department acknowledged that while the provisions of the amendment could potentially increase the amount of energy that Verso could purchase at the discounted rate, the discount rate itself is set at a level higher than MP's incremental energy cost so that MP's revenues would exceed the incremental cost and contain some contribution towards meeting fixed costs.

However, the Department argued that changes to production by Verso (trade secret information contained at p. 4 of the Department's initial comments) could potentially lower MP's revenues. This potential revenue shortfall would be borne entirely by MP until it files a new rate case.

Department concludes that none of the newly proposed provisions would negatively impact MP's other ratepayers; the risk of potential revenue shortfall will be borne by MP until it files a rate case, but until then, MP's other ratepayers will not feel a rate impact.

The Department acknowledged in a footnote that Verso is one of MP's EITE customers and that the Commission's April 20, 2017 Order Authorizing Cost Recovery with Conditions, Docket No. E-015/M-16-564, would require any increases in revenues from Verso due to an EITE rate to be refunded to other ratepayers between rate cases. However, the Department added, that there would be no effect on other ratepayers due to decreases in Verso's revenues due to the proposed changes in this ESA.

## IX. Department's Reply Comments

In its reply comments, the Department assured that none of the provisions in the Amended Agreement between MP and Verso is in conflict with existing terms of the large power (LP) tariff and all the new terms of the Amended Agreement were reasonable.

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<sup>5</sup> The Department pointed out that MP, in its initial petition, did not provide the information required in the Commission's February 26, 2009 order in Docket No. E015/M-08-1344: (1) identification of any terms of a proposed agreement that may be in conflict with the applicable tariff; and (2) description of any potential conflicts between agreement contracts and tariffs, and in case of potential conflict, justification of how the agreement should control the tariff; and, in case of irreconcilable conflict, resolution of the conflict through changes to the agreement or tariff. In its reply comments, MP stated that the Amendment does not conflict with the applicable tariff or provide any conflicts between the Electric Service Agreement ("ESA") and tariffs.

Section V, p. 24.0, of MP's Electric Rate Book, Vol. 1, requires that

Unless otherwise specifically approved by the Commission, each ESA shall have an initial minimum term of ten (10) years and shall continue in force until either party gives the other party written notice of cancellation at least four years prior to the time such cancellation shall be effective.

The instant Amendment provides that the term shall be extended from December 31, 2022 to December 31, 2024. Since this term is an Amendment to an existing contract, the Department concluded that the ten-year requirement is not applicable (the requirement is only applicable to initial contracts).

The modification of Large Power Incremental Production Service provision is not in conflict with tariffed requirements as it already exists as a Rider for the LP customers.

The Department concluded that Corporate Guarantee which provides for the parent guaranty of due payments from Verso to MP is not in conflict with any of MP's tariffs.

Finally, the Weekly Expedited Billing provision, although not consistent with the existing Rider for Expedited Billing Procedures, was previously approved by the Commission in Docket No. E-015/M-12-1025 and thus, does not require further specific Commission action. The Department agrees with MP regarding this issue.

## **X. Comments of Other Interested Parties**

Verso Duluth Mill manager, John Bastian, filed comments stating that the Amendment provides the Duluth Mill with critical operating flexibility and associated energy cost reduction, which would allow the Mill to be more cost competitive in this very challenging global market.

Mark Dylla, a 24-year employee of Verso Duluth Paper Mill, filed brief comments supporting MP's petition and noted that it was in the public interest.

Emily Larson, Mayor of Duluth, files comments noting that the amendment provided Verso with operating flexibility and potential to reduce energy costs, enabling Verso to remain competitive and maintained that the amendment was in the interest of the parties and the public as a whole.

Mary Tourville, a 30-year employee of Duluth Paper Mill, filed comments soliciting Commission approval of the Amendment and noting that the proposed amendment gave her company critical operating flexibility and energy cost reduction.

## **XI. OAG's Petition for Extension of Procedural Schedule**

On October 16, 2018, the OAG filed a petition requesting an extension of the procedural schedule for this matter. The OAG indicated that it had initiated discovery requests upon MP and needed extra time to receive MP's response and then determine whether it should file comments. However, as it turned out, the OAG did not file comments.

## **XII. Staff Comments**

Staff is generally in agreement with the Department's conclusions.

The revenue impact of the proposed amendment is ambiguous.

Although MP is hopeful that additional sales will result from the restatement of Verso's Large Power Incremental Production Service Threshold in the 2018 Amendment, the Department has pointed out that the change in the threshold value, along with any operational changes to Verso's production function, could potentially lower MP's revenue (compared to what it is getting from Verso now).

Staff's main concern is whether MP clearly distinguishes between changes in revenue received from Verso from the IPS Rider and changes in revenue received from Verso from the EITE Rider. Staff is seeking express assurance that revenues (and discounts) from the two riders are treated separately. MP has not addressed this issue except to note that "the Agreement is not otherwise dependent upon or contingent on any EITE related decisions by the Commission."

Staff has not found any provision in MP's Electric Rate Book that prevents the concurrent application of two riders. The Rider for Large Power Incremental Production Service (IPS) applies to Verso in addition to the Rider for Energy-Intensive Trade-Exposed (EITE) Customers at the same time. MP's Rate Book provides that the IPS Rider and the EITE Rider are applicable to an eligible customer taking service under Large Power Service Schedule 74.<sup>6</sup>

Under the EITE Rider, Verso is entitled to a credit of 1.15¢ per kWh for all Firm Energy, Excess Energy, and Incremental Production Service (IPS) Energy in excess of a monthly energy usage threshold. MP's Rate Book establishes this threshold to be 450 hours times Verso's expected peak electric usage. The Commission's April 20, 2017 Order Authorizing Cost Recovery with Conditions in Docket E-015/M-16-564 authorizes Minnesota Power to collect a surcharge from non-EITE customers to recover the cost of providing credits to EITE customers by allowing MP to create a "tracker account" to track the difference in revenue between that which would have been collected under MP's applicable standard tariff and the EITE rate schedule.

Under the IPS rider, Verso establishes a threshold demand. When the measured demand exceeds this threshold demand (but not greater than 110-percent of the threshold), Verso will not be subject to any demand charge for that amount of demand which exceeds the threshold (but not to exceed 100-percent of the threshold). The energy charge applicable to the energy level associated with this amount of demand is subject to a lower energy rate – "subject to an energy charge equal to the Incremental Production Rate."

The incremental production rate consists of the incremental energy cost plus an energy surcharge. The incremental production rate varies between curtailable-demand and non-curtailable-demand. There is no tracker account with regard to this rider and, as the

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<sup>6</sup> Other requirements also apply. MP's Rate Book, Vol. 1 provides that the EITE Rider is applicable to any eligible Large Power Service Customer (Rate Code 54/74) or Large Light and Power Service Customer (Rate Code 55/75). The IPS Rider is applicable to any customer taking service under Large Power Service Schedule 74.



Department has noted, any reduction in revenue, compared to existing level, is borne by MP until it files the next rate case.

MP anticipates Verso to purchase more electric power and energy than the demand purchases that are minimally guaranteed under the existing Agreement. Staff's main concern is that if Verso is receiving relief from demand and energy charges pursuant to the "2018 Amendment," in addition to the EITE credit, any increase in Verso's EITE revenue could potentially be minimized and could result in less revenue accruing to the EITE tracker account, potentially leaving the tracker account in arrears to be made whole by the application of EITE surcharge.

Also, if, because of the provisions of the 2018 Amendment, Verso accounts for less revenue than the "current" revenue stream, is there any assurance that the short fall will not be recouped through an EITE surcharge?

The Commission may seek assurance from MP that there is no cross-allocation of revenue from the IPS and EITE riders by requiring MP to include a schedule in its annual EITE tracker account report that shows the change in revenue from EITE customers due to the increased use of IPS energy since the 2016 EITE base year.

### **XIII. Decision Options**

#### **2018 Amendment**

**A.** Adopt the Department's recommendation to approve the proposed Amended Agreement between MP and Verso (MP, DOC).

Or,

**B.** Reject the proposed amendment.

#### **Compliance Filing**

**C.** Require MP to update its tariff book as necessary to reflect the 2018 amendment to the agreement between MP and Verso.

#### **EITE Tracker Account Report**

**D.** Require MP to include a schedule in its annual EITE tracker account report that shows the change in revenue from EITE customers due to any increased use of IPS energy since the 2016 EITE base year.