

Minnesota Public Utilities Commission

Staff Briefing Papers

Meeting Date: December 6, 2012..... *Agenda Item # 12

Company: Minnesota Power ("MP" or the "Company")

Docket No. E015/M-12-1025

In the Matter of Minnesota Power's Petition for Approval of an
Amendment to an Electric Service Agreement NewPage Wisconsin
System, Inc. and Minnesota Power

Issue(s): Should the Commission approve the Amendment to the Electric
Service Agreement ("Amendment" or "Amended Agreement") with
NewPage Wisconsin System, Inc. ("New Page")?

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Relevant Documents

Minnesota Power Petition..... September 25, 2012
Department of Commerce ("Department") CommentsOctober 17, 2012
Minnesota Power Reply CommentsOctober 30, 2012
Department of Commerce Reply CommentsNovember 8, 2012

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Statement of the Issue

Should the Commission approve Minnesota Power's Amendment to its Electric Service Agreement with New Page?

Relevant Statute

Minn. Stat. § 216.05, subd. 2a. Electric service contract:

A contract for electric service entered into between a public utility and one of its customers, in which the public utility and the customer agree to customer-specific rates, terms, or service conditions not already contained in the approved schedules, tariffs, or rules of the utility, must be filed for approval by the commission pursuant to the commission's rules of practice. Contracts between public utilities and customers that are necessitated by specific statutes in this chapter must be filed for approval under those statutes and any rules adopted by the commission pursuant to those statutes.

Docket No. E015/M-08-1344, addressed issues related to the Commission's authority over rates for Large Light and Power and Large Power customers. The Commission's February 26, 2009 Order in that docket emphasized that fact that the Commission has continuing jurisdiction over and the right to review the LLP and LP contracts at any time and established protocols for future filings seeking approval of LLP of LP electric service agreements.

It also required Minnesota Power to add a provision to its LP Service Schedule stating:

No Public Utilities Commission approval of any of the large power customer electric service agreements required by this Schedule shall act to prevent the Commission from later increasing or decreasing any of the rates or charges contained in this Schedule or shall exempt any customer from the applicability of such increased or decreased charges.

Background

NewPage, Minnesota Power's fifth largest customer, is an affiliate of NewPage Corporation. NewPage is the largest coated paper producer in North America, operating eight paper mills in six states. It owns the Duluth Paper Mill and Duluth Recycled Pulp Mill ("Duluth Mills"). The paper machine produces several grades of supercalendered paper used for catalogs, magazines, advertising inserts and other commercial printing. It has an annual capacity of approximately 250,000 tons.

The Duluth Recycled Pulp Mill started as a Greenfield operation in 1993, producing high-quality recycled pulp. The facility recycles nearly one million pounds of recovered paper per day.

On August 1, 1997, MP and Consolidated Papers entered into a restated electric service agreement.

On November 20, 1997, in Docket No. E-015/M-97-1305, the Commission issued an Order

approving the restated electric service agreement.

On September 2000, Stora Enso purchased Consolidated Papers.

On October 13, 2000, MP filed a petition for approval of an amendment to the Electric Service Agreement between Stora Enso and MP.

On February 8, 2001, the Commission issued an Order approving the Amended Electric Service Agreement.

In 2005, MP and Stora Enso amended and restated their Electric Service Agreement. On March 7, 2006, in Docket No. E-015/M-05-1989 the Commission issued an Order approving the above Amended Agreement.

In 2007, NewPage acquired Stora Enso's paper assets. As part of the acquisition agreement, the Electric Service Agreement between MP and Stora Enso was transferred to NewPage.

On September 7, 2011, NewPage filed for Chapter 11 bankruptcy with the Delaware bankruptcy court ("Court").

On August 13, 2012, NewPage filed a Plan of Reorganization.

On September 25, 2012:

NewPage filed a petition with the Court to assume contracts, including the instant Amended Agreement.

MP filed the instant petition ("Petition") with the Commission requesting an amendment to the Electric Service Agreement with NewPage to extend the term through at least December 31, 2022 and incorporate other modifications

On October 16, 2012, the Department filed comments recommending approval with conditions.

On October 30, 2012, Minnesota Power filed reply comments.

On November 8, 2012, the Department filed reply comments recommending approval.

Party Positions

Minnesota Power

Petition

MP filed this Petition for an amendment to its Electric Service Agreement with NewPage under Minn. Stat. §216B.05, Subd. 2a. The Company stated that key provisions of the agreement are:

NewPage's Duluth Mills is required to purchase its electric service from MP through at least

December 31, 2022.

NewPage will have additional operating flexibility and cost reduction potential through modified nomination and maintenance shutdown provisions.

Minnesota Power will recover pre-petition electric service debt and there will be a weekly pre-payment requirement.

MP requested that the Commission issue an order approving an amendment to the Electric Service Agreement with NewPage to extend the term through at least December 31, 2022 and incorporate other modifications.

Motion to Assume Contracts

As noted above, on September 25, 2012, NewPage filed a motion to assume contracts, including the Amended Agreement. Minnesota Power stated that it expects a decision before the end of 2012 on both the Plan for Reorganization and the assumption of power contracts. MP stated that if the Court approves the Amendment and allows the Electric Service Agreement to be assumed, subject to Commission approval, NewPage will be operating under the Amendment going forward. By operation of bankruptcy law, assumption of the Electric Service Agreement requires NewPage to pay its pre-petition debt to Minnesota Power.

If the Court rejects the Amendment, then the Amendment as well as the Electric Service Agreement will be deemed rejected and terminated by operation of law. NewPage would then be required to take service under Minnesota Power's non-contract Large Power Service Schedule, which would not require Commission approval. Minnesota Power stated that would prefer that all Large Power customers take service under a Commission approved electric service agreement.

Minnesota Power requested that the Agreement be effective on the first day of the calendar month following receipt of a written Commission Order approving the Agreement as allowed under Minn. Stat. §216B.16, subd. 1.

Department of Commerce

Based on its review and analysis of MP's petition the Department concluded that:

1. The Amended Agreement is in the public interest because:
 - a. For each year of the Agreement, the revenues received from NewPage would remain higher than MP's variable costs of serving NewPage.
 - b. The extension of the Agreement through, at least, December 31, 2022, would benefit MP's other ratepayers by lowering their share of MP's total fixed costs.
2. The terms and conditions of service under the Amended Electric Service Agreement satisfy the requirements of Minn. Stat. §216B.03 and Minn. Stat. §216B.05.

The Department recommended that:

1. In its reply comments MP provide the following information:
 - a. Clearly identify any terms of the proposed Amended Electric Service Agreement which may be in conflict with the applicable tariff. Where the proposed Amended Agreement has service conditions or terms different from the LP Service Schedule, MP should identify the difference and clarify whether specific Commission approval is required.
 - b. MP must describe any potential conflict between its proposed Amended Agreement and its tariff, and provide a justification as to why the Agreement should control, including relevant Commission precedent. In the cases of unreconcilable conflict between the applicable tariff and the proposed Amended Agreement, MP must resolve the conflict by either changing the proposed Amended Agreement or the tariff.
2. The Commission approve the proposed Amended Agreement provided that MP provides the information specified in 1.a and 1.b. above.

Minnesota Power Reply Comments

In reply comments, Minnesota Power noted that on October 16, 2012, the U.S. Bankruptcy Court in the District of Delaware issued an order authorizing assumption of both the Agreement and Minnesota Power's Steam Contract with NewPage and payment of cure amounts for both contracts.

Minnesota Power explained that it did not request Commission approval of the Steam Contract since steam service is not regulated by the Commission. However, the Steam Contract is an important aspect of Minnesota Power's Hibbard Energy Center operations and NewPage's ability to continue operations at its Duluth Mills. The Court's authorization of the assumption of the Steam Contract will ensure that Minnesota Power can continue to sell steam from the Hibbard Energy Center to NewPage as well as guarantee Minnesota Power receives payment for amounts past due under the Steam Contract.

Minnesota Power stated that under the Amendment, Minnesota Power will continue to realize a minimum amount of fixed cost recovery between January 2013 and December 2022. If NewPage was not a customer, Minnesota Power would lose the demand revenues. Minnesota Power stated that the MISO market may mitigate some of the lost revenues, currently sales into the MISO market are less predictable and at lower prices than Minnesota Power's sales to firm retail customers such as NewPage. Therefore, Minnesota Power believes there are benefits for all ratepayers from having NewPage continue as a customer.

Minnesota Power stated that in response to the Department and the Commission's directive in Docket No. E015/M-08-1344, it was providing the following additional comments related to how the terms of the Amendment integrate with Minnesota Power's LP Service Schedule.

1. Term of Agreement

The Amendment provides that the Agreement shall be extended through December 31, 2022, without any prior right of termination. The Agreement continues thereafter on a rolling four-year basis until a cancellation notice is issued by either party. Depending on the effective date of the Amendment, the initial term complies with the standard LP Service Schedule language requiring a minimum ten-year agreement since assuming a January 1, 2013 effective date the Agreement's term would be exactly ten years. Currently, the NewPage electric service agreement is on a rolling four-year term. The "rolling" four-year notice of cancellation would be triggered from the date of a written notice of cancellation, making the current earliest possible termination date October 2016.

Minnesota Power stated that even if the effective date of the Amendment is after January 1, 2013, the tariff language should not be applied to NewPage because of the Duluth Mills' long history on Minnesota Power's system and the fact that previous electric service agreements did not have the same requirement. Minnesota Power stated that it is reasonable to offer existing LP customers who are extending contracts less than a ten-year term. The negotiated additional six years to the term of the Agreement is six years longer than NewPage's existing four-year obligation. This contract term is comparable to the terms Minnesota Power obtained from other existing Large Power customers in similar circumstances. With this new commitment, Minnesota Power gains additional certainty regarding its ability to manage generating capacity and plan for future needs of all its ratepayers.

Minnesota Power requested that the Commission approval, if necessary, to continue to waive the minimum ten-year contract term provision in the LP Service Schedule.

2. Modified Paragraph 3(G). Allowance for Scheduled Maintenance

The Amendment modifies NewPage's allowance for scheduled maintenance provision. The LP Service Schedule does not have a provision related to Scheduled Maintenance, but the Commission has previously approved scheduled maintenance provisions for NewPage and other LP customers.

3. Revised Paragraph 3(J). Large Power Incremental Production Service

The Amendment modifies NewPage's IPS Threshold under the Rider for Large Power Incremental Production Service. This Rider is applicable to customers taking service under the LP Service Schedule that have electric service agreements with "a minimum term of at least four (4) years". As discussed above, NewPage's current Agreement has a four-year term and the Amendment would extend that term to ten years. In addition, the LP Service Schedule requires that every electric service agreement shall include "An Incremental Production Service Threshold as defined in the Rider for Large Power Incremental Production Service, as applicable." NewPage's current Agreement includes an IPS Threshold that is just modified by the Amendment. As noted in the Service Conditions in the Rider, the IPS product is available to a customer "to increase production or throughput above historic and contractual Service Requirement levels". NewPage has met this requirement through an extensive energy efficiency

and productivity effort that has resulted in NewPage lowering its electrical demand while maintaining historic production levels.

4. New Paragraph 3(N). Decreases in Service Requirement

New Paragraph 3(N) allows for reductions in the take-or-pay Service Requirement. The LP Service Schedule does not address decreases in service requirement for permanent facility shutdowns.

5. New Paragraph 5. Precedent Conditions

The language in new Paragraph 5 establishes a number of conditions which must be met by NewPage including Court authorization for full payment of \$2.19 million to cure monetary defaults arising under this Agreement. These conditions are separate from the required Commission approval of the Amendment and are not addressed in the LP Service Schedule.

6. New Paragraph 6. Weekly Prepayment

NewPage agreed to weekly prepayments for the life of the Agreement. There is not an applicable tariff that applies to NewPage since the existing Rider for Expedited Billing Procedures is applicable to ‘taconite producing customers’ only. NewPage internal accounting procedures could not be modified to accommodate the provisions of the existing Rider for Expedited Billing Procedures.

Conclusion

Minnesota Power stated that the Amendment does not conflict with the applicable tariffs and these reply comments meet the Commission’s directive in Docket No. E015/M-08-1344. The Amendment provides benefits to Minnesota Power and its ratepayers by assuring Minnesota Power that it will provide NewPage’s electric service requirements, through at least December 31, 2022.

Minnesota Power and its ratepayers benefit from an extension to an existing agreement, in this case from an LP customer, which provides continued revenue assurance to Minnesota Power and its ratepayers from an important industrial customer. Minnesota Power respectfully requests that the Commission issue an order approving this Amendment.

Department of Commerce Reply Comments

In its reply comments the Department concluded that:

MP provided the information requested by the Department in its initial comments.

None of the provisions in the Amended Agreement between MP and NewPage is in conflict with existing terms of the LP tariff

All the new terms of the Amended Agreement are reasonable.

The Department recommended that the Commission approve the proposed Amended Agreement between MP and NewPage.

Staff Analysis

Minnesota Power's large Power Service, Rate Schedule 74 requires that the customer and the Company have executed an Electric Service Agreement for service to be taken under this schedule. The Agreement being discussed in this filing meets that requirement. The rates that will be charged are tariffed rates and subject to Commission jurisdiction. On page 24.1 the tariff clearly states:

No Commission approval of any ESA shall act to prevent the Commission from later increasing or decreasing any of the rates or charges contained in this LP Schedule, any Rider or any other tariff applicable to Large Power Service. Nor shall any Commission approval of any ESA except any Customer from the applicability of any such increases or decreased charges.

Staff generally agrees with the Department's analysis and is not going to repeat specifics in this briefing paper. However, staff is concerned with the DOC statement that "[s]ince NewPage's rates include contribution to MP's fixed costs, MP's ratepayers benefit from such contribution that would otherwise have to be collected from them."

The addition of a new large customer or the retention of one that might otherwise leave the system is not necessarily beneficial to other customers.

Whether other ratepayers would pay more without the contract with NewPage is dependent on the existence of surplus capacity and the market for that capacity and on supply of energy and demand for the energy.

The Amendment extends the duration of the Electric Service Agreement to December 31, 2022. A review of current forecasts indicates that there may be a need for additional capacity during that period. According to Minnesota Power's most recent resource plan, Docket No. E015/RP-09-1088, the Utility's expected forecast shows resource deficits for both summer and winter beginning in 2016. At this point, if Minnesota Power needs to pay more for the additional capacity and energy than the rates being paid by NewPage, other customers would be harmed by the contract.

Minnesota Power also has the option of selling surplus power and energy. If the Company is able to sell that power or energy at rates higher than what is being paid by NewPage, other customers will not be benefiting from the contract. According to the Midwest ISO's September 2012 study, 6 gigawatts of capacity may be needed by 2015 to maintain an appropriate planning reserve margin. This would indicate that there will be a market for capacity in the near future.

The rates for NewPage are tariffed under the Large Power Service schedule and are subject to future Commission review, as a result, the Commission does not need to make a specific finding regarding the benefits to other customers.

Decision Alternatives

Some Commission options are:

- I. Approve the Amended Agreement.
- II. Approve the Amended Agreement and note that the Commission is not making any specific findings as to the benefits to other customers.
- III. Deny Minnesota Power's request to approve the Amended Agreement.