minnesota power
AN ALLETE COMPANY

30 west superior street / duluth, minnesota 55802-2093 / fax: 218-723-3955/www.allete.com

Christopher D. Anderson
Associate General Counsel
218-723-3961
e-mail canderson@allete.com

May 18, 2016

VIA ELECTRONIC FILING

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

RE: In the Matter of Minnesota Power's 2015 Remaining Life Depreciation Petition
Docket No. E015/D-15-711

Dear Mr. Wolf:

Minnesota Power hereby submits its Reply Comments in the above-referenced Docket. Please contact me at the number above should you have any questions related to this matter.

Yours truly,

Christopher D. Anderson

jmn
c: Service List

STATE OF MINNESOTA
BEFORE THE
MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of Minnesota Power's 2015 Remaining Life Depreciation Petition	Docket No. E015/D-15-711 **REPLY COMMENTS**

Minnesota Power (the Company) files these Reply Comments regarding its 2015 Remaining Life Depreciation Petition (Petition) in response to Comments filed by the Large Power Intervenors (LPI) dated October 30, 2015 and Comments filed by the Minnesota Department of Commerce, Division of Energy Resources (Department) dated October 30, 2015.

On July 9, 2015, Minnesota Power laid out the next steps in its *Energy**Forward*** plan and announced the Company's plan to cease coal operations at Taconite Harbor Energy Center (THEC) units 1 and 2 in 2020 and economically idle THEC units 1 and 2 in the fall of 2016. This action related to THEC was reflected in Minnesota Power's 2015 Integrated Resource Plan (2015 Plan) which is pending approval at the Commission. Minnesota Power has requested in its Petition to continue depreciating THEC over its remaining life of 2026 as it is in the best public interest of customers.

The following are Minnesota Power's reply comments to the LPI's comments and Department's recommendations.

<u>LPI:</u>

LPI questioned in its comments why Laskin Energy Center (Laskin) should have a 15-year remaining life, rather than a 30-year remaining life, which is similar to the life of a new gas turbine peaking plant. Minnesota Power concluded that Laskin only has a 15-year remaining life because it was a conversion of the plant reusing the existing boiler/turbine with additions and changes confined to the firing system and gas supply.

Minnesota Power did not add a new gas turbine; consequently a 30-year remaining life would not be appropriate.

Department:

In Recommendation 1 the Department recommended approving Minnesota Power's proposed remaining lives, except for the lives proposed for THEC and Sappi/Cloquet Generator No. 5 (Sappi).

In Recommendation 2 the Department recommended approving a remaining life of six years (2020) for THEC. Minnesota Power disagrees with this Recommendation and requests the Commission approve the current remaining useful life of twelve years (2026) for the THEC proposed in the Petition for the following reasons:

1. THEC will not be decommissioned in 2020 and refueling, repurposing, and re-missioning opportunities are being considered.

Minnesota Power has no plans to decommission the THEC in 2020 when it proposes to cease electric generation with coal as its primary fuel. Minnesota Power is continuing to develop multiple utility re-missioning and refueling opportunities for THEC to produce electricity that are in the best interests of Minnesota Power customers, and also economically benefit the communities and surrounding region. The Company has dedicated staff working to develop future utility applications of the Taconite Harbor facility. This facility is unique to the Great Lakes as a deep water port served by a private railroad. It is also an important part of the transmission grid reliability of the north shore of Minnesota. There are immediate opportunities including **[TRADE SECRET DATA EXCISED]**. Additional expressions of interest for facility reuse have been received and are being evaluated as options to repurpose the facility that would likely have a material impact on whether and to what extent any decommissioning occurs and the amount of future decommissioning costs. Given Taconite Harbor's many unique site attributes, Minnesota Power continues to explore future site uses that can create utility customer benefits, contribute to local economic development, preserve electric reliability for the north shore and mitigate the socioeconomic impacts from the coal fired power transition that state resource planning is obligated to balance under Minn. Stat. § 216B.2422.

Minnesota Power is recovering the costs in base rates under the existing life. If the life is shortened, either to 2020 or 2017, this would have a significant impact, and would warrant an immediate cost recovery mechanism (like deferral until the next rate case). If the Commission agrees with the Department of Commerce on the shorter life, Minnesota Power requests an immediate cost recovery mechanism. Unlike minor changes to depreciation rates and minor impacts in past depreciation dockets, the Department of Commerce's recommendation would result in major changes and impacts that warrant an immediate cost recovery mechanism.

2. <u>The Department recommendation unfairly penalizes Minnesota Power for early action to reduce carbon emissions</u>

As proposed in Minnesota Power's preferred plan in the Company's 2015 Plan, the most economic resource alternative for THEC, with the best optionality for customers, is to idle the facility until 2020 at which point the Company has proposed to stop using coal to fuel the station. This proposal will be considered and decided by the Commission within the proceedings of the 2015 Plan.

Using normal FERC retirement accounting, had the Company proposed to close and retire the plant immediately, the remaining unrecovered balances on THEC Units 1 & 2 would have been treated as the Company treated Unit 3, and recovered over the original remaining life of 2026. This is illustrated in the "Normal FERC retirement accounting" example below. Minnesota Power and its customers should not be penalized for its "economic idling" proposal, which results in substantial carbon emission reductions, by having the depreciation accelerated for the THEC as a result of shortening the remaining life to six years.

<u>*Normal FERC retirement accounting*</u>

Minnesota Power requests the Commission approve the remaining life of twelve years for the THEC proposed in the Petition. This would be the same life if Minnesota Power retired the unit today following FERC normal retirement accounting.

The Code of Federal Regulations Title 18, Chapter 1, Subchapter C, Part 101 – Uniform System of Accounts Prescribed for Public Utilities and Licensees Subject to the Provisions of the Federal Power Act, Electric Plant Instructions, Section 10. Additions and Retirements of Electric Plant Sections B. (2), D, E and F which reference normal retirement accounting were used when preparing the example below.

For example, if we assumed Taconite Harbor was retired December 31, 2014 an entry would have been made to:

Debit Account 10810 Accumulated Provision for Depreciation for approximately $156 million (the original installed cost of the assets)

Credit to Account 10110 Electric Plant in Service for approximately $156 million (the original installed cost of the assets)

After the entry the balance in electric plant in service would be zero and the debit balance in accumulated provision for depreciation would be approximately $98 million. This $98 million is the undepreciated portion of the retired assets that Minnesota Power is proposing to depreciate over the original useful life of 2026 or proposing to move to Account 182.2 unrecovered plant and regulatory study costs, discussed in the next section below, and amortize these costs over the original useful life of 2026. See additional information in Minnesota Power's 2013 IRP Appendix L: *Accounting for Proposed Retirements and Decommissioning Study Discussion.* Reducing the useful life to 2020, with such a significant balance remaining to depreciate, would result in an increase in depreciation expense of approximately $9 million annually (including decommissioning component of depreciation expense).

<u>*FERC allows recovery of stranded costs*</u>

The Code of Federal Regulations Title 18, Chapter 1, Subchapter C, Part 101 – Uniform System of Accounts Prescribed for Public Utilities and Licensees Subject to the Provisions of the Federal Power Act, Balance Sheet Chart of Accounts, Account 182.2 Unrecovered plant and regulatory study costs Section C. discusses how to account for unrecovered costs of plant facilities which have been prematurely retired.

3. <u>Minnesota Power's proposal for the depreciation and useful life for THEC conforms to Generally Accepted Accounting Principles (GAAP) in Minnesota</u>

In Minnesota utilities are required to follow the Federal Power Commission (FPC) uniform system of accounts and all FPC orders, pronouncement, rules and regulations.[1] This body of pronouncements is generally referred to in the industry as FERC accounting. The FPC defines depreciation expense for FERC accounting purposes. It states that utilities must use a method of depreciation that allocates, in a systematic and

[1] Minnesota Rules Chapter 7825 Public Utilities Commission, Utilities; Financial, Regulatory matters, Uniform System of accounts Minnesota Rules 7825.0200 Subpart 3.

rational manner, the service value of depreciable property over the service life of the property. It also states that the estimated useful service lives of depreciable property must be supported by engineering, economic, or other depreciation studies. And that utilities must use percentage rates of depreciation that are based on a method of depreciation that allocates in a systematic and rational manner the service value of depreciable property to the service life of the property.

FERC accounting, not unlike GAAP for nonutility entities, depreciates the remaining balance of asset over the estimated service life of the asset. This is the method of depreciation that the Department is recommending in its comments in this docket. But FERC accounting alone does not consider the additional authority given to the Minnesota Commission in establishing GAAP for Depreciation Expenses in Minnesota.

In Minnesota, the Commission has additional methods, considerations and authority to directly determine the annual depreciation expense in the Annual Depreciation Certification for utility assets. The Commission, using the standard FERC accounting for depreciation as a framework, can deviate from standard FERC accounting in determining the remaining service life or recovery period of an asset and thereby establishes GAAP for depreciation expense in Minnesota. The Commission can make this determination to deviate from standard FERC methods upon proper review of the appropriateness of a utility's proposal in the annual Depreciation Certification.

In the annual Depreciation Certification rules[2], utilities are required to file annually and the Commission will consider and approve the specific rates by which utilities depreciate their assets, and these depreciation amounts are used for more than just ratemaking purposes. The resulting depreciation expense is a component of the utility's financial statements, used in its other regulatory and external reports such as its filings with FERC and the Securities and Exchange Commission. The rules state that Depreciation expense is "a process of allocation not valuation." Allocation is an important principle when considering the public interest in establishing the recoverable life of an asset for ratemaking purposes. Further, under the Methods for Depreciation Certification in the Minnesota Rules,[3] the Rules state "No specific methods are prescribed by the Commission in estimating service lives and salvage values." Minnesota

[2] Minnesota Rules 7825.0600 Depreciation Certification Subpart 1 Depreciation practices applicable to all utilities
[3] Minnesota Rules 7825.0800

Power's proposal in the 2015 Depreciation docket, to retain the useful life of the THEC through 2026, is within the methods and authority granted to the Commission to modify traditional FERC accounting for depreciation expense and is thereby allowable GAAP for utilities in Minnesota.

4. The remaining useful life of THEC and the allowance for recovery of the remaining facility investment should be determined in 2015 Plan

The Commission should not take any action on the Department's recommendation until the future of THEC is determined in the 2015 Plan Docket and through exploration of future options for THEC, as this will have significant financial implications on Minnesota Power and its customers. In the 2015 Plan Docket, the Department is seeking that THEC be closed in 2017. If the Commission accepted the Department's recommendation on closing the facility in 2017, Minnesota Power would be required to depreciate the remaining unrecovered balance over a three-year period. This increased depreciation expense of nearly $25 million annually would clearly not be in the best interest of Minnesota Power or its customers. Also, idling THEC 1&2 and being able to call the units back into service will maintain the capability to respond to regional reliability requirements, recognizes the new carbon emission compliance targets in place, and allows consideration of a refuel or remission opportunity in 2020 which the Department's recommendation to shut down the facility in 2017 does not address. This idling action could provide a valuable resource option, considering the substantial energy transformation underway across North America. Future refueling and remission opportunities will be considered in planning and optimization of THEC in Minnesota Power's next resource plan.

5. THEC 2015 Plan proposal warrants allowance to recover costs

Minnesota Power is proactively choosing to cease coal-fired operations at THEC in order to prepare for energy policy changes which will require reductions in carbon emissions. The Commission has the authority to allow the recovery of remaining undepreciated plant balances. The Company believes its current proposal warrants an allowance by the Commission to recover the remaining costs at THEC as the company is proactively choosing to meet the State's energy policy goals of reducing carbon emissions. By taking this proactive approach, the company should be treated in the same manner as would happen if it were ordered to terminate operations before the end of a facility's current remaining useful life. Minn. Stat. § 216B.16, subd. 6 states that if the Commission orders a generating facility to terminate its operations before the end of the facility's physical life in order to comply with a specific state or federal energy statute or policy, the Commission may allow the public utility to recover any positive net book value of the facility as determined by the Commission.

6. <u>The current remaining useful life of 2026 for THEC is in the public interest for customers</u>

The electric industry is in a significant state of change. Reliance on more intermittent energy sources and natural gas as an energy source creates new and different electric system dynamics. These dynamics are further amplified in remote northeastern Minnesota where large electric customers dominate the energy market. Minnesota Power is planning to idle Taconite Harbor and preserve the assets so it can be restarted to protect reliability for electric customers in the event of any unforeseen system developments. The Company's electric customers benefit from having Taconite Harbor available to be restarted during a time of great change to the electric industry.

As well, depreciating THEC over six years, as recommended by the Department, would result in higher depreciation costs for customers. Maintaining the remaining useful life of 2026 protects customers from paying these higher costs and provides for an orderly recovery of invested costs that supports the transition of Minnesota Power's small coal fleet. The Department's recommendations would result in additional annual depreciation expense: approximately $9 million if the useful life is 2020 or $25 million if the useful life is 2017. These are material amounts that do not accurately reflect the remaining value or economic benefits of the economic idling for customers.

In Recommendation 3, the Department recommended approving a remaining life of two years for Sappi. Minnesota Power disagrees with this Recommendation and requests approval of the remaining life of ten years for the Sappi proposed in the Petition. Minnesota Power requests approval of the remaining life of ten years for Sappi for the following reasons:

1) Minnesota Power has been attempting to negotiate a contract extension with Sappi instead of transferring ownership of the Cloquet Energy Center Generator No. 5 from Minnesota Power to Sappi for a nominal amount on

July 1, 2016. However, it is clear that the contract is not going to be extended and that Sappi will exercise the option under the contract to transfer ownership of the Cloquet Energy Center Generator No. 5. As a result, Minnesota Power will be left with unrecovered costs. Because it is difficult to predict exactly how long an asset will be productive, assets often remain in service for time periods different than their estimated useful lives. In the case of a premature retirement, the Company should be able to recover all of the plant's direct cost even though the plant did not operate as long as expected. As the Company has proposed for THEC Unit 3, Minnesota Power proposes that the remaining plant balance continue to be depreciated over the original useful life of 2024 as a way to recover these costs without significant impacts to ratepayers. MP customers continue to benefit from the capacity of the TG5 unit on the broader capacity system capability.

2) Adjusting the remaining life so that the assets are fully depreciated by December 2016 results in higher depreciation expense over a significantly shorter period, which negatively impacts Minnesota Power's ratepayers. Minnesota Power proposes that the remaining plant balance continue to be depreciated over the original useful life of 2024 to avoid these negative impacts to ratepayers.

In Recommendation 4, the Department recommended approving Minnesota Power's proposed salvage rates, except for the salvage rates proposed for Laskin and THEC. Minnesota Power disagrees with the Department's exception for the salvage rate proposed for Laskin. Minnesota Power requests approval of the salvage rate of negative 15.29 percent for Laskin proposed in the Petition; not the salvage rate of negative 26.02 percent recommended by the Department in Recommendation 5.

In Recommendation 5, the Department recommended approving a salvage rate of negative 26.02 percent for Laskin. Minnesota Power disagrees with this Recommendation and requests approval of the salvage rate of negative 15.29 percent for Laskin proposed in the Petition. Minnesota Power has provided an amended closure plan to the Minnesota Pollution Control Agency (MPCA) and the MPCA will determine the scope of the Laskin ash pond decommissioning through its approval authority. Once the scope is determined, which is expected before we file our 2016 Remaining Life Depreciation Petition, Minnesota Power will have an approved plan. At that time Minnesota Power's decommissioning study will be updated with a known and supportable estimate. As the Department noted in its Comments, there has been volatility in Laskin's ash pond decommissioning cost estimates in the past. That is one reason Minnesota Power is proposing to update the salvage rate in its 2016 filing, instead of changing it in 2015, and then again in 2016, when the final cost estimates are available. The cost estimate of $16 million for landfill and pond closure at Laskin that the Department recommends using is subject to MPCA approval and the final cost estimate is highly dependent on that approval. This cost estimate was the mid-point of a range between $12 million and $24 million. An updated engineering estimate will be completed in 2016, based on the approved MPCA plan, and an appropriate cost estimate will be developed. The Company believes it is reasonable and more appropriate to wait one year and update the 2016 Remaining Life Depreciation Petition with more accurate information.

In Recommendation 6, the Department recommended approving a salvage rate for THEC based on the 2015 Decommissioning Study that includes either (a) an updated coal pile remediation cost estimate or (b) the coal pile remediation cost estimate from the 2013 Decommissioning Study. Minnesota Power agrees with recommendation (a) above. Minnesota Power proposes an updated Taconite Harbor Energy Center salvage rate of negative 5.23 percent based on an updated coal pile remediation cost estimate of $1.1 million. This would increase depreciation expense by $0.1 million.

In Recommendation 7, the Department recommended requiring Minnesota Power to include in future depreciation filings a comparison of the remaining lives used in its depreciation filing to the Company's most recent integrated resource plan and explain any differences. Minnesota Power agrees with this recommendation.

In Recommendation 8, the Department recommended requiring Minnesota Power to include in its next depreciation filing an analysis comparing its depreciation expense using its current decommissioning probabilities to its depreciation expense using 100 percent decommissioning probabilities. Minnesota Power agrees with this recommendation.

In Recommendation 9, the Department recommended requiring Minnesota Power to include in its next depreciation filing a schedule of its supplemental depreciation expense recorded in the prior year as well as the supplemental depreciation expense to be recorded in the future. Minnesota Power agrees with this recommendation.

In Recommendation 10, the Department recommended requiring Minnesota Power to make its next depreciation filing on or before September 1, 2016 to establish depreciation parameters and rates to be effective January 1, 2016. Minnesota Power agrees with this recommendation.

In conclusion, Minnesota Power respectfully requests approval of the remaining life of twelve years for THEC, the remaining life of ten years for Sappi, and the salvage rate of negative 15.29 percent for Laskin proposed in the Petition.

Date: May 18, 2016

Respectfully submitted,

/s/ Debbra A. Davey

Debbra A. Davey
Supervisor, Accounting
Minnesota Power
30 West Superior Street
Duluth, MN 55802
(218) 355-3714
ddavey@allete.com

STATE OF MINNESOTA	)	AFFIDAVIT OF SERVICE VIA
	) ss	ELECTRONIC FILING
COUNTY OF ST. LOUIS	)	

Jodi Nash of the City of Duluth, County of St. Louis, State of Minnesota, says that on the 18th day of May, 2016, she served Minnesota Power's Reply Comments on the Minnesota Public Utilities Commission and the Energy Resources Division of the Minnesota Department of Commerce via electronic filing. The persons on the attached service list were served as requested.

Jodi Nash

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
Julia	Anderson	Julia.Anderson@ag.state.mn.us	Office of the Attorney General-DOC	1800 BRM Tower 445 Minnesota St St. Paul, MN 551012134	Electronic Service	Yes	GEN_SL_Minnesota Power_Minnesota Power General Service List
Christopher	Anderson	canderson@allete.com	Minnesota Power	30 W Superior St Duluth, MN 558022191	Electronic Service	Yes	GEN_SL_Minnesota Power_Minnesota Power General Service List
Sharon	Ferguson	sharon.ferguson@state.mn.us	Department of Commerce	85 7th Place E Ste 500 Saint Paul, MN 551012198	Electronic Service	Yes	GEN_SL_Minnesota Power_Minnesota Power General Service List
Margaret	Hodnik	mhodnik@mnpower.com	Minnesota Power	30 West Superior Street Duluth, MN 55802	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Lori	Hoyum	lhoyum@mnpower.com	Minnesota Power	30 West Superior Street Duluth, MN 55802	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Michael	Krikava	mkrikava@briggs.com	Briggs And Morgan, P.A.	2200 IDS Center 80 S 8th St Minneapolis, MN 55402	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
James D.	Larson	james.larson@avantenergy.com	Avant Energy Services	220 S 6th St Ste 1300 Minneapolis, MN 55402	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Douglas	Larson	dlarson@dakotaelectric.com	Dakota Electric Association	4300 220th St W Farmington, MN 55024	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
John	Lindell	agorud.ecf@ag.state.mn.us	Office of the Attorney General-RUD	1400 BRM Tower 445 Minnesota St St. Paul, MN 551012130	Electronic Service	Yes	GEN_SL_Minnesota Power_Minnesota Power General Service List
Susan	Ludwig	sludwig@mnpower.com	Minnesota Power	30 West Superior Street Duluth, MN 55802	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Pam	Marshall	pam@energycents.org	Energy CENTS Coalition	823 7th St E St. Paul, MN 55106	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
Herbert	Minke	hminke@allete.com	Minnesota Power	30 W Superior St Duluth, MN 55802	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
David	Moeller	dmoeller@allete.com	Minnesota Power	30 W Superior St Duluth, MN 558022093	Electronic Service	Yes	GEN_SL_Minnesota Power_Minnesota Power General Service List
Andrew	Moratzka	apmoratzka@stoel.com	Stoel Rives LLP	33 South Sixth Street Suite 4200 Minneapolis, MN 55402	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Jennifer	Peterson	jjpeterson@mnpower.com	Minnesota Power	30 West Superior Street Duluth, MN 55802	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Susan	Romans	sromans@allete.com	Minnesota Power	30 West Superior Street Legal Dept Duulth, MN 55802	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Thomas	Scharff	thomas.scharff@newpagecorp.com	New Page Corporation	P.O. Box 8050 610 High Street Wisconsin Rapids, WI 544958050	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Ron	Spangler, Jr.	rlspangler@otpco.com	Otter Tail Power Company	215 So. Cascade St. PO Box 496 Fergus Falls, MN 565380496	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Eric	Swanson	eswanson@winthrop.com	Winthrop Weinstine	225 S 6th St Ste 3500 Capella Tower Minneapolis, MN 554024629	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Karen	Turnboom	karen.turnboom@newpagecorp.com	NewPage Corporation	100 Central Avenue Duluth, MN 55807	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List
Daniel P	Wolf	dan.wolf@state.mn.us	Public Utilities Commission	121 7th Place East Suite 350 St. Paul, MN 551012147	Electronic Service	No	GEN_SL_Minnesota Power_Minnesota Power General Service List