

E-015/M-91-695 ORDER VARYING RULES TO ALLOW RECOVERY OF CONTRACT
BUYOUT COSTS THROUGH FUEL ADJUSTMENT CLAUSE

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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| Darrel L. Peterson | Chair |
| Cynthia A. Kitlinski | Commissioner |
| Dee Knaak | Commissioner |
| Norma McKanna | Commissioner |
| Patrice M. Vick | Commissioner |

In the Matter of Minnesota
Power's Petition for a Variance
to the Fuel Adjustment Clause
Rules

ISSUE DATE: November 26, 1991

DOCKET NO. E-015/M-91-695

ORDER VARYING RULES TO ALLOW
RECOVERY OF CONTRACT BUYOUT
COSTS THROUGH FUEL ADJUSTMENT
CLAUSE

PROCEDURAL HISTORY

I. Proceedings to Date

On September 18, 1991 Minnesota Power filed a petition for a variance to Minn. Rules, parts 7825.2390 et seq. to allow the Company to use the fuel adjustment clause to pass through the net costs of terminating a long term coal purchase contract with Peabody Coal Company. On September 27, 1991 the Commission solicited comments on the filing from interested persons.

The Department of Public Service, the Residential Utilities Division of the Office of the Attorney General, and an association of taconite producers receiving power under Minnesota Power's Large Power tariff¹ filed comments. All parties recommended granting the variance. (The Department initially expressed reservations, which were resolved by the Company's subsequent agreement to adjust its fuel inventory level in a concurrent rate investigation docket, Docket No. E-015/M-91-654.)

The matter came before the Commission on November 19, 1991.

¹ The members of the association are Eveleth Expansion Company, Eveleth Taconite Company, Hibbing Taconite Joint Venture, Inland Steel Mining Company, National Steel Pellet Company, and USX Corporation.

FINDINGS AND CONCLUSIONS

II. Factual Background

In 1968 Minnesota Power signed a long term coal purchase contract with Peabody Coal. The contract requires the Company to purchase at least 3.15 million tons of Peabody coal per year at prices which are now substantially above the price of coal from other suppliers. The contract also requires the Company to pay the costs of closing the Big Sky Mine, the source of the coal, at the end of the contract term. Those costs would begin in 1993 and would continue at least through 2005.

Minnesota Power has reached an agreement with Peabody that would release the Company from all further obligations under the contract as of December 31, 1991 for a lump sum payment of \$34 million and the transfer of ownership to Peabody of a rapid coal loading facility at the mine. (To transfer ownership of the coal loading facility, the Company would pay the bank from which it has been leasing the facility up to \$1.8 million.) The agreement is contingent upon Minnesota Power receiving regulatory approval of the transaction by November 30, 1991.

Minnesota Power estimates that the buyout agreement would save ratepayers at least \$8.1 million in January 1, 1992 dollars. Most of these savings would result from reduced coal purchase costs; a small portion would result from limiting future mine closing costs. The buyout would also eliminate the risks associated with the Company's obligation to pay mine closing costs by reducing those costs to a sum certain. All commenting parties agreed that the buyout would benefit Company ratepayers.

The Company proposed to recover the total buyout costs, plus a return on the unamortized balance, through the fuel adjustment clause. These costs would be recovered from January 1992 through December 1993. During the same period, the Company would return through the fuel adjustment clause the \$3.4 million collected through rates to pay mine closing costs, plus a return on the unamortized balance of that sum.² Until its next rate adjustment proceeding, the Company would also refund through the fuel adjustment clause the amounts built into current rates for mine closing costs. Finally, the Company would make true-up filings at the end of 1992 and 1993 to correct any over- or under-recovery resulting from differences between actual and projected kwh sales. All commenting parties supported the Company's proposed recovery and refund procedures.

² The Company would reduce this amount by \$580,000 in arbitration costs incurred in an earlier proceeding to determine its mine closing obligation.

III. Commission Action

The Commission agrees with all parties that the buyout agreement will benefit ratepayers, is in the public interest, and should be approved. The Commission also agrees that the most workable and straightforward method of recovering buyout costs, and refunding amounts already collected for mine closing costs, is to use the fuel adjustment clause. Although the buyout costs are not direct costs of purchasing fuel, they are closely related. The fuel adjustment clause offers an economical, administratively simple way to recover them. Furthermore, recovery through the fuel adjustment clause lends itself to easy monitoring by the Department, the Commission, and other interested parties. For these reasons, the Commission will grant the requested variance.

The Commission may grant a variance to any of its rules upon finding that the following conditions apply:

1. Enforcement of the rule would impose an excessive burden upon the applicant or others affected by the rule;
2. Granting the variance would not adversely affect the public interest; and
3. Granting the variance would not conflict with standards imposed by law.

Minn. Rules, part 7830.4400.

The Commission finds that those requirements are met here. Enforcing the fuel adjustment clause rules to prevent recovery of the buyout costs would harm the Company and its ratepayers. In all likelihood it would prevent the execution of the buyout agreement, force the Company to continue buying overpriced coal, and expose the Company to the financial risks of full liability for mine closing costs which have not yet been determined. The first requirement for a variance clearly is met.

The second requirement, that the variance not adversely affect the public interest, is also met. This variance would serve the public interest by allowing a utility to cut fuel costs and protect itself from unknown future liabilities.

Finally, granting the variance will not conflict with any applicable legal standard. The Commission will therefore vary the fuel adjustment clause rules to allow recovery of the Peabody buyout costs through the fuel adjustment clause.

ORDER

1. Minnesota Power's petition to vary Minn. Rules, parts 7825.2390 et seq. to allow the Company to use the fuel adjustment clause to pass through the net costs of terminating its long term coal purchase contract with Peabody Coal Company is granted.
2. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster
Executive Secretary

(S E A L)