

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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Chair
Commissioner
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In the Matter of the Petition of Northern States
Power Company d/b/a Xcel Energy for
Approval of a Power Purchase Agreement with
Invenergy Cannon Falls, LLC

ISSUE DATE: March 15, 2005

DOCKET NO. E-002/M-04-1426

ORDER APPROVING POWER PURCHASE
AGREEMENT AS MODIFIED AND
DECLINING TO IMPOSE BIODIESEL
REQUIREMENTS

PROCEDURAL HISTORY

On August 26, 2005, Xcel Energy (Xcel or the Company) filed a petition for approval of a power purchase agreement (PPA) between Xcel and Invenergy Cannon Falls, LLC (Invenergy) for 301 megawatts (MW) of summer peaking capacity (357 MW winter) beginning in 2006.

On October 11, 2004, Xcel filed an amendment extending the date for terminating the PPA without further obligation.

On October 27, 2004, the Commission received a letter from the Minnesota Project. The letter supported the testing and use of blended biodiesel fuels.

On November 24, 2004, the Minnesota Department of Commerce (the Department) filed comments on the Power Purchase Agreement and Minnesota Project's biodiesel proposal. The Department recommended approval of the PPA with significant and substantial modifications and recommended against requiring the testing and use of blended biodiesel fuels.

On December 9, 2004, Xcel Energy filed reply comments accepting some of the Department's proposed modifications and opposing others.

On December 22, 2004, the Department filed supplemental comments. The Department continued to recommend approval conditioned on the same modifications it had proposed in its initial comments.

On February 17, 2005 the Department filed additional information and comments. Based on further analysis, the Department withdrew its recommendation to condition the recovery of the capacity costs on a decision in the 2004 Resource Plan.

The Commission met on February 24, 2004 to consider this matter.

FINDINGS AND CONCLUSIONS

I. Background to the Power Purchase Agreement (PPA)

The PPA at issue in this matter results from Xcel Energy's efforts in the Company's 2001 All Source Request For Proposal. Docket No. E-002/M-01-1618. Invenergy submitted a bid in response to the Company's initial Request for Proposals (RFP) but withdrew from the bid process between the announcement of the short list and the selection of the finalists. After Xcel Energy experienced difficulties with respect to transmission constraints, price issues and other problems with its final selections, the Company went back to the list of bidders and contacted vendors to determine the viability of their projects. At that time Invenergy revived its proposal and began negotiations with Xcel Energy.

The resulting proposed power purchase agreement between Xcel Energy and Invenergy details the location and design of the Invenergy facility (Facility). The Facility would consist of two simple cycle, natural gas-fired, combustion turbine generators and would provide 301 MW of summer peaking capacity and 357 MW winter peaking capacity beginning in 2006.

Xcel requested that the Commission find that the PPA is reasonable and in the public interest, that the PPA is subject only to ongoing prudence review through the ongoing prudence review of the annual automatic adjustment of charges reports, and that Xcel may recover from Minnesota retail customers the Minnesota jurisdictional portion of the amounts incurred for energy-related payments during the full term of the PPA with capacity costs being addressed in the Company's next electric rate case.

II. The Department's Recommendations Regarding the PPA

In its February 17, 2005 comments, the Department revisited the need issue in light of the 2005-2019 Integrated Resource Plan (IRP) that Xcel filed November 1, 2004 in Docket No. E-002/M-04-1752. The Department stated that its analysis of the IRP shows that while the Invenergy facility is not necessary to meet Xcel's peaking needs for the year in which the Facility would be added to the Company's system (2006), the Facility would be used and useful to Xcel customers in other ways as soon as it comes on line due to certain characteristics of the Company's portfolio, as the Department fully described in its February 17, 2005 comments based on its further analysis of the Company's 2004 IRP filing.

The Department found that the data provided as part of Xcel's IRP filing warranted withdrawing

its recommendation that the Commission determine the eligibility for capacity cost recovery based on the outcome of Xcel's current IRP proceeding. Instead, the Department recommended that the Commission approve the PPA between Xcel and Invenergy and allow the Company to recover all capacity costs associated with the PPA.

In addition, the Department recommended that the Commission require Xcel to 1) request the addition of natural gas submetering equipment if the facility is expanded to facilitate wholesale sales to third parties and 2) notify the Commission if it plans to assign the PPA to any of its affiliates.

III. Xcel's Responses to the Department's Recommendations

In comments filed December 9, 2004, Xcel agreed that it would, as recommended by the Department, provide written notice to the Commission and the Department once the owner/operator of the natural gas supply pipeline (New Lateral ¹) that would connect with the Northern Natural Gas interstate pipeline system is known. The Company also agreed to notify the Commission in the event Xcel plans to assign the PPA to any of its affiliates.

At the hearing on this matter, Xcel also agreed with the Department's revised recommendation that the Commission approve the PPA without conditioning cost recovery on a subsequent finding of need in the IRP proceeding and only differed with the Department on the rationale for doing so. Xcel continued to assert that the capacity generated by the facility would be required to meet forecasted demand starting as soon as it came on line in 2006 but also stated alternative reasons why it believed the Invenergy generation would benefit ratepayers.

The Company asserted that potential MISO-related² transmission constraints made it uncertain, for example, how available the generation from Angus Anson (South Dakota) facilities would be at a peak period. The Company cited potential difficulty meeting the reserve margin requirement imposed on it by the Mid-continent Area Power Pool (MAPP) and argued that potential transmission constraints imposed by MISO made generation located closer to its load (such as Invenergy's Cannon Falls location) valuable from a reliability standpoint.

¹ New Lateral: Invenergy's plans for the Facility include the construction of a lateral natural gas supply pipeline (New Lateral) that would connect with the Northern Natural Gas interstate pipeline system. Under the PPA, the capacity price can be modified to reflect three events, one of which is the interconnection costs of the New Lateral.

² MISO is the Midwest Independent System Operator, one of the electricity transmission coordinating entities that the Federal Energy Regulatory Commission (FERC) has encouraged electric utilities to join. Xcel is a member of MISO.

As a safeguard against the production of unneeded electricity, the Company also stated that if the Department's forecast of capacity needs is correct, ratepayers would benefit from the availability of Invenergy's generation because the Company could then reduce its purchase of high-priced and volatile spot market electricity (currently purchased by Xcel at the 750 MW annual level) in favor of the relatively less expensive Invenergy generation.

As additional ratepayer benefit from the Invenergy PPA, the Company also assured the Commission that it would propose a mechanism in its next rate case (anticipated to be filed in 2006) to give ratepayers the benefit of revenues received from any sales of surplus Invenergy generation to third parties.

IV. Commission Analysis and Action Regarding the PPA

Having reviewed and considered the written and oral comments of the parties, the Commission will approve the proposed PPA, requiring the Company to give notice as agreed to by Xcel and to add submetering equipment if the facility is expanded to facilitate wholesale sales to third parties. Some of the issues raised in this proceeding merit further comment.

A. Authorization to Recover Capacity Costs

In this case, the only parties to comment on whether Xcel should be authorized to recover capacity costs in rates (Xcel and the Department) ultimately agreed that the PPA should be approved and that Xcel should be allowed to recover in Xcel's next rate case the capacity costs of that PPA in rates from Xcel customers. They only disagreed on the rationale for doing so.

The Commission finds the Department's final comments on this matter persuasive and the Company's assurances and explanation of alternative ratepayer benefits from the PPA reasonable. In short, despite unresolved competing demand forecasts the record supports a finding that the availability of Invenergy generation will benefit ratepayers throughout the 15 year term of the PPA. The Commission believes that its primary obligation to assure the reliability of electric service obliges the Commission to facilitate this project. In light of the gravity of an energy shortfall together with the anticipation that ratepayers will benefit from any sales of surplus Invenergy generation, the Commission believes that ratepayers are likely to receive significant benefit from this PPA, which both parties agree assures that Xcel has a reasonably adequate generation portfolio to supply their energy needs.

B. Selection of Appropriate Pricing Structure Regarding Contingencies

As proposed, the PPA provides that the capacity price would be subject to three adjustments. The Department noted that two of the three adjustments depended on future events and argued that this introduced unreasonable price uncertainty. The Department argued that competitive bidding is used to identify those firms that are capable of providing reliable power at a reasonable and fairly definitive price and noted that the recently approved PPA between Xcel and Mankato Energy Center did not include any such conditional adjustments.

The Department also expressed concern about possibly setting a precedent by approving a contract with multiple provisions that introduce substantial capacity price uncertainty. The Department concluded that approving the PPA with provisions that transfer the degree of price uncertainty risk to ratepayers as proposed would not be appropriate.

Xcel responded that it believed the existing terms of the PPA were the most beneficial to the ratepayer. The Company further stated that the provider (Invenergy) had advised that it could not agree to remove any adjustments to the capacity charge without a compensating change to other terms of the contract. The Company provided two pricing alternatives that it said it would accept.

The Department stated that both alternatives proposed by the Company removed the objectionable price uncertainty while maintaining a reasonable price. The Department did not recommend which pricing alternative the Commission should adopt.

The Commission agrees with the Department that removal of unreasonable price uncertainty is important and will select the first of the two pricing options provided in its December 9, 2004 comments at page 8 because it maintains the initial time frame for this project, 15 years.

C. Selection of Appropriate Backup Fuel

Xcel and Invenergy's PPA identifies fuel oil as the backup fuel for the facility, i.e. the PPA states that the facility will be capable of generation with fuel oil. PPA Section 5.7.

On October 28, 2004, the Minnesota Project filed comments supporting the use of fuel oil blended with biodiesel as the backup fuel for the Facility. The Minnesota Project referred to various Minnesota Statutes that it stated promoted the use of renewable fuels such as biodiesel. The Minnesota Project also asserted that the use of a biodiesel blend would not pose any technical difficulties for the facility's operation and argued that because the amount of biodiesel fuel used in a fuel blend would be minimal, any cost increase due to the use of biodiesel would be negligible.

Specifically, the Minnesota Project recommended that the Commission advance the goals of Minnesota's renewable energy policies by requiring the PPA to include a biodiesel content for all fuel oil used at the plant or at least to impose on Invenergy the same obligation the Commission imposed on Calpine/Mankato Energy Center in Docket No. IP-6345/CN-03-1884, i.e. to make its test facilities available for testing and evaluation of fuels and to work with those interested in order to continue to investigate the technical feasibility and economic viability of the use of a biodiesel blend for those times when the facility does not have access to natural gas as fuel.³

³ See *In the Matter of the Application of Mankato Energy Center, LLC, a Wholly-Owned Subsidiary of Calpine Corporation, for a Certificate of Need for a Large Electric Generating Facility*, Docket No. IP-6345/CN-03-1884, ORDER GRANTING CERTIFICATE OF NEED (September 22, 2004) at page 8.

Having considered this matter, the Commission will not impose any obligation on Invenenergy regarding biodiesel.

First, despite the number of statutes that the Minnesota Project cited promoting the consideration of renewable fuels, none of them preclude the Commission from taking into account concerns regarding cost, reliability, and technical feasibility.

Second, the Minnesota Project quotes a witness in the Calpine/Mankato Energy docket asserting that “there do not appear to be any technical reasons that biodiesel cannot be used in such application [combustion turbines] in blended form.” However, the Administrative Law Judge who heard all the testimony did not recommend that the Commission require a biodiesel blend be used as the backup fuel for the facility. Instead, he specifically concluded, there is “insufficient reliable information in the record to support [such a recommendation]”⁴ and in its Order the Commission likewise declined to require use of a biodiesel fuel blend as back-up-fuel.⁵ In the current docket, the Minnesota Project has provided no additional information to support its contentions.

Third, the Calpine Order in Docket No. IP-6345/CN-03-1884 provides no precedent for requiring a non-volunteering supplier such as Invenenergy to make testing facilities available to investigate the technical feasibility of a biodiesel blend. In the Calpine/Mankato Energy Order, the Commission did not impose testing obligations on Calpine/Mankato Energy that the company had not voluntarily undertaken to do.⁶ The record in the current matter provides no basis for imposing similar requirements.

In short, the Commission agrees with the Department’s un rebutted analysis and conclusion that based on the information available at this time, there is no basis for approving the biodiesel blended fuel backup proposed by the Minnesota Project.⁷

⁴ *In the Matter of the Application for a Certificate of Need and a Site Permit by Mankato Energy Center, LLC, a wholly owned subsidiary of Calpine Corporation*, FINDINGS OF FACT, CONCLUSIONS OF LAW, AND RECOMMENDATION, OAH Docket No. 6-2500-15869-2 and PUC Docket No, IP-6345/CN-03-1884 (August 20, 2004) at page 46.

⁵ *In the Matter of the Application for a Certificate of Need and a Site Permit by Mankato Energy Center, LLC, a wholly owned subsidiary of Calpine Corporation*, ORDER GRANTING CERTIFICATE OF NEED, Docket No, IP-6345/CN-03-1884 (September 22, 2004) at page 9.

⁶ *Supra* at pages 9-10.

⁷ See Department of Commerce Comments filed November 24, 2004 in this matter at pages 21-22.

ORDER

1. The Commission hereby approves the power purchase agreement (PPA), with the following additions and clarifications:

Notice Requirements: 1) Xcel shall provide written notice to the Commission and the Department once the owner/operator of the New Lateral is known; and 2) Xcel shall notify the Commission if it intends to assign the PPA to any of its affiliates.

Submetering Equipment: if the facility is expanded to facilitate wholesale sales to third parties, Invenenergy shall add submetering equipment.

Pricing: Xcel shall use the fixed “risk” premium described in the first of two bulleted alternatives proposed by the Company on page 8 of its comments filed December 9, 2004.

2. The Minnesota Project’s request that the Commission proposal to require Invenenergy to use biodiesel as a back-up fuel for the facility is denied. Its request that the Commission require Invenenergy to evaluate biodiesel blended fuels in the manner undertaken by Calpine/Mankato Energy in Docket No. IP-6345/CN-03-1884 is also denied.
3. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

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