

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Katie J. Sieben	Chair
Dan Lipschultz	Commissioner
Valerie Means	Commissioner
Matthew Schuerger	Commissioner
John A. Tuma	Commissioner

In the Matter of a Petition by Northern States Power Company, d/b/a Xcel Energy, for Approval of the Acquisition of the Mankato Energy Center

ISSUE DATE: December 18, 2019

DOCKET NO. IP-6949, E-002/PA-18-702

DOCKET NO. IP-6949/GS-15-620

In the Matter of Mankato Energy Center II, LLC's Application for a Site Permit for the 345 MW Expansion of the Mankato Energy Center

ORDER DENYING PETITION AND REQUIRING SUPPLEMENTAL MODELING

**PROCEDURAL HISTORY**

On November 6, 2018, Northern States Power Company, d/b/a Xcel Energy (Xcel or the Company), filed a letter informing the Commission of its recent agreement (the Purchase Agreement) with Southern Company (Southern) to purchase the Mankato Energy Center (MEC).

On November 27, 2018, Xcel filed its Petition for Approval of the Acquisition of the Mankato Energy Center (the Petition).

On December 20, 2018, the Commission issued a notice requesting comments on the Petition.

By March 6, 2019, the following stakeholders<sup>1</sup> submitted comments:

- City of Minneapolis
- City of Mankato
- Department of Commerce, Division of Energy Resources (the DOC-DER)
- Greater Mankato Growth
- Institute for Local Self Reliance/Cooperative Energy Futures (ILSF/CEF)
- International Brotherhood of Electrical Workers Local Union 949 (IBEW)
- Laborers District Council of Minnesota and North Dakota (LIUNA)

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<sup>1</sup> Throughout this proceeding, the Commission also received comments from a number of individuals, including Jacob Herbers, Mallory Mitchell, Debbie Meister, Anthony Varriano, Mike Kreuset, Ben Allen, John White, Carol Overland, Pat Foley, Dr. Annette Parker, and a batch of comments from 814 "Clean Energy Supporters." Most public commenters urged denial of the Petition, while a few recommended approval.

- LSP-Cottage Grove, L.P. (LSP)
- Mankato Building Trades
- Office of the Attorney General, Residential Utilities and Antitrust Division (OAG)
- Sierra Club
- Southern
- Xcel Large Industrials<sup>2</sup> (XLI)

On March 29, 2019, Xcel and Southern filed reply comments, and Citizens Utility Board of Minnesota (CUB) filed a letter explaining its intent to file comments.

On April 2, 2019, Xcel filed a letter stating no objection to CUB's late-filed comments.

On April 3, 2019, the Commission issued a notice requesting supplemental comments relating to Xcel's reply comments.

On April 30, 2019, the Department of Commerce, Energy Environmental Review and Analysis (DOC-EERA) filed comments recommending approval of the proposed site-permit transfer.

On May 20, 2019, Xcel filed a Settlement Agreement signed by Xcel, LIUNA, Clean Grid Alliance, Minnesota Center for Environmental Advocacy, Union of Concerned Scientists, Fresh Energy, Center for Energy and the Environment (CEE), and Sierra Club. The Clean Energy Organizations<sup>3</sup> (CEOs) and CEE filed joint comments, and Sierra Club filed a request to withdraw its previous comments.

On May 22, 2019, CUB filed an objection to Sierra Club's request to withdraw its comments.

On June 12, 2019, the City of Minneapolis filed reply comments.

On June 24, 2019, ILSR/CEF filed reply comments, and the Advanced Energy Management Alliance filed a letter regarding the Settlement Agreement.

By July 29, 2019, the following stakeholder groups submitted supplemental comments:

- CUB
- DOC-DER
- LIUNA
- LSP
- OAG
- XLI

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<sup>2</sup> XLI comprises the following companies: Covia Holdings Corporation; Flint Hills Resources Pine Bend, LLC; Gerdau Ameristeel US Inc.; Marathon Petroleum Company LP; and USG Interiors, Inc.

<sup>3</sup> CEOs comprises the Clean Grid Alliance, Fresh Energy, Minnesota Center for Environmental Advocacy, and the Union of Concerned Scientists.

On August 1, 2019, Xcel filed a letter informing the Commission of the Company's intent to move forward with the transaction through an unregulated subsidiary should the Commission deny the Petition.

On August 9, 2019, Blue Earth County filed a letter in support of the Petition.

On August 20, 2019, the Commission issued a notice requesting supplemental comments on the issues raised in Xcel's August 1, 2019 letter.

By August 30, 2019, the following stakeholder groups submitted additional supplemental comments:

- CUB
- DOC-DER
- OAG
- Xcel
- XLI

On September 3, 2019, the Mankato Clinic filed a letter in support of the Petition.

On September 27, 2019, the Commission met to consider the Petition.

## **FINDINGS AND CONCLUSIONS**

### **I. Introduction and Background**

#### **A. Mankato Energy Center**

The Mankato Energy Center (MEC) is a 720-megawatt (MW) natural-gas combined-cycle power plant located in Mankato. The facility is made up of two units: a 375-MW unit (MEC I) and a 345-MW expansion project (MEC II). MEC I was upgraded and overhauled in 2017, and MEC II began operating in 2019. Southern has owned MEC since 2016.

Since the completion of MEC I in 2006, Xcel has purchased all of MEC's energy and capacity output through a power purchase agreement (PPA).<sup>4</sup> The PPA for MEC I expires in 2026, while the PPA for MEC II expires in 2039.

#### **B. Legal Framework**

Xcel submitted the Petition under Minn. Stat. § 216B.50, which requires a public utility to seek Commission authorization to acquire facilities that cost greater than \$100,000, such as MEC. The Commission will authorize an acquisition if it finds that doing so is consistent with the public interest.

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<sup>4</sup> As stated on page 11 of the Petition, Xcel also makes monthly payments for dispatchability and turbine starts under both PPAs. But unlike the MEC I PPA, the MEC II PPA "does not include a commitment by the Company to dispatch a certain percent of the facility's base capacity."

Xcel also requested a transfer of the MEC site permits under Minn. R. 7850.5000, which requires a Commission finding that the new permittee will comply with the conditions of the permit before a site permit is transferred.

Some stakeholders argued that the Commission should evaluate the proposed acquisition using the criteria from the integrated-resource-plan (IRP) and certificate-of-need (CON) statutes, Minn. Stat. §§ 216B.2422 and .243, respectively. These statutes require the Commission’s consideration of a variety of factors in determining whether to add generation resources to a public utility’s system, including forecasts of energy demand, potential environmental impacts and costs, and possible alternatives to the proposed resource. These statutes also prioritize additions of renewable generation over nonrenewable generation; for example, the IRP statute prohibits approval of a nonrenewable-energy facility unless the utility shows that a renewable-energy facility is not in the public interest.<sup>5</sup>

## II. The Petition

In the Petition, Xcel requested approval of its proposal to acquire MEC and transfer the site permits for the facility. Xcel and Southern negotiated a purchase price of \$650 million, which is \$100 million more than the present value of Xcel’s capacity-payment obligations under the MEC I and II PPAs. Xcel stated that its analysis revealed a number of benefits associated with acquiring the facility, including cost savings for ratepayers, support for the transition to carbon-free generation, acquisition of valuable interconnection rights, risk mitigation of PPA expirations, and economic development for the surrounding community.

Xcel analyzed the effect of the proposed acquisition on system costs using the Strategist resource-planning model. Xcel simulated the operation of its system through 2057 and compared system costs under the ownership scenario and PPA scenario. Xcel explained that “the cost savings under the ownership proposal are achieved by avoiding the costs that would be incurred under the existing PPA as well as utilizing the MEC resource over the expected life of the asset.”<sup>6</sup> Xcel concluded that the acquisition of MEC would save between \$158 to \$251 million in terms of societal costs and \$66 to \$142 million in terms of the Company’s revenue requirement. The Petition included a list of “comparable transactions” to argue that the MEC purchase would be less expensive than other recent natural-gas-combined cycle sale transactions.

Xcel acknowledged that some stakeholders may question why this proposal was not included in its pending IRP, and explained that Southern’s timelines for the transaction precluded that approach. Xcel argued that because MEC is already a resource on Xcel’s system, Xcel viewed the proposal as a change in ownership rather than a resource acquisition.

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<sup>5</sup> Minn. Stat. § 216B.2422, subd. 4. The CON statute prohibits issuances of a CON to a nonrenewable generating facility unless a renewable generating facility is shown to be more expensive, including environmental costs. Minn. Stat. § 216B.243, subd. 3a.

<sup>6</sup> Petition, at 21. The Petition states that Xcel “expects to be able to utilize MEC I through 2046 and MEC II through 2054.” *Id.*

Xcel requested that the Commission take the following actions:

- Determine [Xcel's] proposal to acquire the existing MEC facility is prudent and in the public interest under Minn. Stat. § 216B.50;
- Approve an FCA variance under Minn. R. 7829.3200 allowing the Company to recover the difference between the 2019 revenue requirement resulting from the transaction and the revenues already in base rates for the capacity portions of the current MEC I and MEC II PPAs;
- Approve the site permit transfer under Minn. R. 7850.5000;
- Issue a Notice setting an appropriate schedule for comments and reply comments from interested parties on this Petition;
- Establish a procedural schedule such that the Commission may issue a written order as close as practicable to June of 2019 so [Xcel] may proceed with the transaction as contemplated by [its] agreement with Southern Power as soon as practicable after the currently scheduled [commercial operation] date for the MEC II PPA; and
- Vary its rules, consistent with past practice, with respect to certain filing requirements referenced in Minn. R. 7825.1800.<sup>7</sup>

At the hearing, Xcel indicated its agreement to a number of customer protections that had been proposed by stakeholders. These protections included caps on the recovery of capital and operations and maintenance expenses with any additional recovery first requiring a showing a reasonableness and prudence by the Company, deferral of ownership expenses that exceed projected PPA costs until 2022, and a future filing evaluating the economics of continuing to operate MEC II beyond the PPA expiration date.

### **III. Stakeholder's Positions**

The comments in this docket cover a number of issues related to the Petition. Below are summaries of the comments regarding the threshold issue of whether Xcel's acquisition of MEC is in the public interest.

#### **A. Supporters of the Petition**

Supporters of the Petition included LIUNA, CEE, Sierra Club, CEO, City of Mankato, Greater Mankato Growth, IBEW, Mankato Building Trades, and Southern.

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<sup>7</sup> Petition, at 46.

## **1. The Settlement**

On May 20, 2019, Xcel submitted a Settlement Agreement between Xcel, LIUNA, CEE, Sierra Club, and CEO. The Settlement Agreement pertained to the Petition as well as “certain aspects” of Xcel’s 2020–2036 IRP. Under the Settlement Agreement, Xcel agreed to pursue a number of actions in its 2020–2036 IRP, including early retirement of certain fossil-fuel generation plants, commitment to energy efficiency targets, and procurement of at least 3,000 MW of solar generation before 2030.

CEE and CEO agreed to submit comments supportive of the Petition and support Xcel’s IRP actions, including Xcel’s requests for regulatory assets for the retired plants and expansion of Xcel’s decoupling pilot. Sierra Club agreed to submit a request to withdraw its comments on the Petition. LIUNA, Sierra Club, CEE, and CEO agreed to support Xcel’s ownership of half of the new solar resources and proposed acquisition process for those resources.

In its comments supporting the Petition, CEO and CEE argued that Xcel’s acquisition of MEC is a “critical component” of the Company’s carbon-reduction goals because MEC ownership would cost-effectively facilitate retirement of coal-fired generating plants.<sup>8</sup> They maintained that, as an existing resource on Xcel’s system, the acquisition would not significantly increase carbon emissions, and it would “reduce or delay” the need for additional gas generation in the future.<sup>9</sup> They also noted that an additional benefit of the acquisition would be Commission jurisdiction over MEC.

## **2. Local Benefits**

Supporters of the Petition from the area surrounding MEC emphasized how Xcel’s ownership of MEC would provide benefits to the local community. They touted Xcel as an excellent community partner and employer, with labor groups highlighting Xcel’s commitment to unionized workers.

Other commenters argued that Xcel’s ownership of MEC would assist Xcel’s transition to clean energy and carbon-reduction efforts. Supporters also argued that Xcel’s ownership of MEC would ensure the continued operation of the facility to provide a reliable energy source to support growth in the region.

## **B. Opponents of the Petition**

The stakeholders recommending denial of the Petition included the Department, OAG, CUB, XLI, City of Minneapolis, ILSF/CEF, and LSP.

### **1. Modeling Issues**

The Department encountered serious issues in analyzing the Strategist modeling that Xcel submitted to demonstrate the benefits of the acquisition. Xcel submitted four rounds of modeling in response to the Department’s concerns, but the Department ultimately came to the following

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<sup>8</sup> CEO and CEE comments, at 2.

<sup>9</sup> *Id.* at 7.

conclusion: “Due to the numerous flaws in Xcel’s Strategist inputs and modeling technique, the Department considers all four rounds of the Company’s modeling analysis to be of no value.”<sup>10</sup>

The Department cited numerous problems with Xcel’s modeling assumptions. For example, Xcel artificially overestimated the value of MEC and undervalued other resources by making unrealistic assumptions about how resources would be used.<sup>11</sup> The Department also considered Xcel’s energy demand forecasts to be too high, which can increase the perceived need for additional generation resources.

The flaws in Xcel’s modeling hindered the Department’s ability to perform its typical review and analysis. When the Department would run scenarios with the inputs provided by Xcel, the results would not match Xcel’s results. The Department asserted that Xcel “failed to employ proper resource planning techniques” by forcing Strategist to perform too many scenarios.<sup>12</sup>

Xcel’s modeling approach precluded the Department from comparing the relative cost of MEC and additional renewables, and the Department accordingly argued that Xcel had not satisfied the renewable-preference provision in the IRP statute.<sup>13</sup> Xcel’s modeling flaws led the Department to conclude that Xcel had failed to demonstrate that acquisition of MEC would be in the public interest under Minn. Stat. § 216B.50.

## **2. Cost-Effectiveness**

Opponents to the Petition argued that purchasing MEC was not a cost-effective decision for ratepayers. Parties noted that the purchase price was \$100 million more than Xcel’s capacity payment obligations under the PPAs, and owning the facility would make ratepayers responsible for a number of additional fixed and variable costs, such as decommissioning costs, property taxes, rate of return, operations and maintenance expenses, and plant outages and failures. Stakeholders questioned the value of MEC’s accredited capacity at a time when there is little need for capacity on Xcel’s system or in the region, and LSP argued that its facility is a lower-cost alternative to MEC.

Stakeholders also noted that Xcel’s analysis shows that MEC is only cost effective for ratepayers if it is operated beyond the expiration of the PPAs, and even past 2050. They argued that early retirement of MEC to align with Xcel’s carbon-reduction commitments would shift considerable stranded costs onto ratepayers, rendering the purchase a bad deal for ratepayers. OAG argued that ratepayers would only begin to experience savings from the purchase starting in the early 2030s. The Department also raised the possible opportunity costs if Xcel is less able to take advantage of new energy technologies because of MEC ownership.

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<sup>10</sup> Department supplemental comments, at 40 (July 26, 2019).

<sup>11</sup> *Id.* Specifically, the Department found that Xcel used “unrealistically low capacity factors for existing nuclear and coal facilities” and impeded renewable resources from competing with MEC. *Id.*

<sup>12</sup> *Id.* at 17.

<sup>13</sup> *See* Minn. Stat. § 216B.2422, subd. 4.

### 3. IRP Process

Many stakeholders argued that the decision to purchase MEC is a long-term resource decision that should be made in Xcel's pending 2020–2034 IRP proceeding, in Docket No. E-002/RP-19-368. They maintained that the issues surrounding the MEC purchase are intertwined with issues raised in the IRP process, and that MEC should be considered alongside all of Xcel's resource options. Some opponents also argued that the two-track bidding process should be used to allow other potential resources to compete with MEC.<sup>14</sup> Opponents criticized Xcel for failing to mention the potential MEC purchase when Xcel requested an extension of the filing deadline for its IRP in December 2018, and they argued that Southern's deadlines for the transaction should not constrain the Commission's review of the purchase.

Opponents noted that operating MEC past 2050, which may be necessary to make the purchase cost effective, would conflict with Xcel's commitment to go 100% carbon-free by 2050. The Department found that the MEC purchase is not needed for future early coal retirements, and ownership of MEC would result in Xcel's system emitting an additional 1.4 million tons of CO<sub>2</sub>.

#### C. Xcel Reply Comments

In its reply comments, Xcel reiterated that it expects significant customer savings resulting from MEC ownership and urged the Commission to focus on the many benefits of MEC rather than modeling issues. Xcel maintained that MEC ownership reduces costs associated with early coal retirements. Besides cost savings, Xcel listed other benefits of ownership, including certainty of future capacity costs, increase in flexibility in future resource planning, regulatory control over the operation and retirement of the plant, transmission and interconnection rights, capacity value after expiration of the PPAs, and a reasonable purchase price considering the range of benefits and recent purchases of similar facilities. Xcel argued that MEC was a better purchase opportunity than LSP Cottage Grove due to the expected life and efficiency of the facilities, as well as the recently lowered capacity payments under the LSP PPA.

Xcel stated that the timing of the Petition was driven entirely by Southern's decision in late 2018 to sell MEC, and that the PPAs contain a right of first offer that allows Xcel to bid on the plant before Southern offers the plant to other potential buyers. Xcel maintained that the risk under the MEC PPAs is that energy and capacity costs will be higher upon expiration, that property-tax and stranded-cost risks had been mitigated, and that the expected operating and decommissioning costs were consistent with industry standards. Xcel argued that the MEC proposal is consistent with its climate goals and that it is "unreasonable . . . to expect the Company to make acquisition decisions in a changing market and industry in perfect lockstep with an IRP process that takes two years to complete and occurs only a few times each decade."<sup>15</sup>

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<sup>14</sup> See OAG supplemental comments, at 1–18 (July 26, 2019).

<sup>15</sup> Xcel reply at 4.



#### **D. Site-Permit Transfer**

DOC-EERA was the only party to submit comments regarding the transfer of the MEC site permits from Southern to Xcel. DOC-EERA noted that the MEC I and II site permits “contain ongoing operational obligations for permittees,” such as compliance with applicable laws, as well as “on-going treatment and handling of cooling water and monitoring of operational and meteorological conditions that could result in fogging or icing on local roads.”<sup>16</sup>

DOC-EERA concluded that, “[b]ased on the record to date and EERA staff’s experience with permits for other Xcel Energy projects, EERA staff has no reason to believe that Xcel Energy will not comply with the conditions in the MEC permits.” DOC-EERA thus recommended that the Commission approve the transfer of the MEC site permits from Southern to Xcel.

#### **E. Affiliate Purchase**

In its August 1 letter, Xcel informed the Commission and stakeholders that if the Petition is denied, it planned to purchase MEC through an unregulated affiliate. In response to the Commission’s subsequent notice, stakeholders agreed that Xcel would be required to gain Commission approval of an affiliated-interest agreement under Minn. Stat. § 216B.48 in order for the affiliate to sell MEC’s energy to Xcel through the PPAs. Xcel noted that it would also need to seek approval from the Federal Energy Regulatory Commission. OAG requested further information from Xcel to determine whether the affiliate’s acquisition requires Commission approval, but all other commenters concluded that only the affiliated-interest agreement would require Commission approval. Xcel acknowledged that any amount collected for payments to the unregulated affiliate are subject to refund until the affiliated-interest agreement is approved.

#### **IV. Commission Action**

Under Minn. Stat. § 216B.50, Xcel bears the burden of showing that its purchase of MEC is consistent with the public interest. In support of its proposal, Xcel argued that purchasing MEC would promote the public interest for a number of reasons, highlighting the potential ratepayer savings as a key benefit of ownership. However, due to multiple serious issues with Xcel’s modeling and forecast, the Department was unable to verify these claims. Even assuming the validity of Xcel’s modeling, ratepayers would not experience savings from the purchase until the early 2030s. This delay raises issues of intergenerational inequity, whereby current ratepayers would pay higher costs for the purchase but future ratepayers would enjoy any potential savings.

That leaves the remaining benefits touted by Xcel, including transmission and interconnection rights, added capacity to support the transition away from coal, mitigation against higher energy and capacity costs when the PPAs expire, and Commission jurisdiction over the MEC facility. But along with these potential benefits, Xcel’s ownership of MEC would introduce significant costs and risks to ratepayers, such as decommissioning costs, property taxes, rate of return, operations and maintenance expenses, plant outages and failures, and \$100 million of the purchase price that exceeds the remaining PPA capacity payments. Operating MEC past the expiration of the PPAs appears to be the only way to make the purchase cost effective, but doing

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<sup>16</sup> DOC-EERA comments, at 2.

so would likely conflict with Xcel's environmental commitments. Retiring MEC early to comply with those environmental commitments could leave ratepayers responsible for stranded costs.

For these reasons, the Commission concludes that Xcel's acquisition of MEC has not been shown to be consistent with the public interest. The potential costs to ratepayers are too high, and the potential benefits too uncertain, to support the purchase. The Commission recognizes the importance of MEC to the surrounding community, and MEC will continue to be an important part of Xcel's system for many years.

### **ORDER**

1. The Commission denies Xcel's request to purchase the Mankato Energy Center and its request to transfer the site permits for this facility.
2. Within 30 days of this order, Xcel shall supplement the modeling in its integrated resource plan with scenarios that reflect the Mankato Energy Center as a power-purchase agreement.
3. This order shall become effective immediately.

BY ORDER OF THE COMMISSION

Daniel P. Wolf  
Executive Secretary



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