

Rebuttal Testimony
John J. Reed

State of Minnesota
Before the Office of Administrative Hearings
For the Minnesota Public Utilities Commission

*In the Matter of a Petition by Excelsior Energy Inc. for Approval of a Power
Purchase Agreement Under Minn. Stat. § 216B.1694, Determination of Least
Cost Technology, and Establishment of a Clean Energy Technology Minimum
Under Minn. Stat. § 216B.1693*

OAH Docket No. 12-2500-17260-2
PUC Docket No. E6472/M-05-1993

Financial Impacts

October 10, 2006

1 **I. INTRODUCTION**

2
3 Q. PLEASE STATE YOUR NAME.

4 A. My name is John J. Reed.

5
6 Q. HAVE YOU PROVIDED TESTIMONY IN THIS PROCEEDING?

7 A. Yes. I provided Direct Testimony on behalf of Xcel Energy regarding the
8 Mesaba 1 PPA.

9
10 **II. PURPOSE**

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12 Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

13 A. My Rebuttal Testimony responds to the Direct Testimony and Exhibits of Dr.
14 Eilon Amit, filed on behalf of the Minnesota Department of Commerce
15 (“Department” or “DOC”).

16
17 Q. HAVE YOU ALSO REVIEWED THE PREPARED SUPPLEMENTAL TESTIMONY AND
18 EXHIBITS FILED BY RENEE J. SASS?

19 A. Yes, I have. I agree with the Rebuttal Testimony of Karen T. Hyde regarding
20 the 450-MW PPAs offered by Ms. Sass. These alternatives resolve none of
21 the issues in my Direct Testimony and Exhibits. In fact, as discussed by Ms.
22 Hyde, they exacerbate several of those issues.

23
24 **III. ASSESSMENT**

25
26 Q. DO YOU AGREE WITH DR. AMIT’S ASSESSMENT OF THE MESABA 1 PPA?

1 A. Yes, I agree with nearly all of Dr. Amit's principal conclusions. However, I
2 offer the following qualifications to his assessment. First, his analysis is based
3 on assumptions embedded in the model provided to him by Mesaba 1 LLC.
4 These assumptions are unreasonable and unrealistic in a manner that results in
5 the outputs of Dr. Amit's analysis being more favorable than can reasonably
6 be expected to be achieved. My comments are not critical of Dr. Amit's
7 analysis, but rather are intended to provide necessary context for his results.

8
9 Second, I do not believe that he has accurately interpreted one of the pricing
10 provisions contained in the Mesaba 1 PPA.

11
12 Q. PLEASE DESCRIBE YOUR CONCERNS REGARDING THE ASSUMPTIONS PROVIDED
13 TO DR. AMIT BY MESABA 1 LLC.

14 A. I have two primary concerns. First, the underlying cost data do not include: (i)
15 any incremental transmission costs; (ii) any increment for final Engineering,
16 Procurement, and Construction ("EPC") costs that exceed the 2005 forecast;
17 or (iii) any fixed fuel costs. Even assuming that the EPC costs would not
18 exceed the 2005 forecast, it is clear that there will be incremental transmission
19 costs and fixed fuel costs, and zero value is included for these items in the
20 model that Mesaba 1 LLC provided to Dr. Amit.

21
22 Second, Mesaba 1 LLC's operating assumptions are unrealistic. For example,
23 the model assumes that:

- 24 • Natural gas is used only for start-up, de-slagging and other operational
25 uses, and not as a fuel for generation.
- 26 • The cost of fuel at the burner-tip will increase at the rate of inflation.

- 1 • The plant will operate at an annual capacity factor of 91% from 2015
2 through 2036.

3
4 I believe that each of these assumptions is overly optimistic. Further, given
5 the provisions of the Mesaba 1 PPA, any change in these factors from these
6 assumptions would be borne exclusively by Xcel Energy customers. I believe
7 these assumptions understate the likely costs of the proposal; and accordingly,
8 Dr. Amit's results understate the costs of the proposal.

9
10 Q. DO YOU HAVE ANY COMMENTS REGARDING DR. AMIT'S DISCUSSION OF THE
11 COSTS OF A 450-MW PROPOSAL?

12 A. Yes. The data included in Dr. Amit's testimony appear to recover the entire
13 costs of the 603-MW Mesaba Unit 1 from a purchase of 450 MW. This
14 calculation appears to be an accurate application of the model and data
15 provided by Mesaba 1 LLC, but the calculation does not reflect a reasonable
16 price for 450 MW. While I do not believe that Dr. Amit is proposing this
17 methodology as an appropriate pricing mechanism, it is important to note this
18 qualification on the use of Dr. Amit's testimony so that it is not
19 mischaracterized or misapplied to set the price for 450 MW. Ms. Hyde
20 provides further discussion of this issue in her response to the 450-MW PPA
21 proposed by Ms. Sass.

22
23 Q. PLEASE EXPLAIN YOUR SECOND CONCERN REGARDING DR. AMIT'S
24 INTERPRETATION OF THE MESABA 1 PPA PRICING PROVISIONS.

25 A. Based on his testimony, I do not believe that Dr. Amit fully captured the
26 relationship between capacity price and fuel choice in the Mesaba 1 PPA. Dr.
27 Amit states that the "monthly capacity payments are inversely related to the

1 monthly gas usage.” (Direct Testimony at p 12.) This phrasing suggests that
2 the capacity price is reduced *in proportion* to the use of natural gas. However,
3 my reading of the Mesaba 1 PPA indicates that the capacity price is not
4 reduced proportionally as the use of alternative fuels increases; instead the
5 Mesaba 1 PPA allows *full collection* of the capacity price unless the Mesaba Unit
6 1 plant burns 100% natural gas. In this instance, I do not believe that the
7 Mesaba 1 PPA provides to Xcel Energy the offset to fuel price risk that Dr.
8 Amit describes.

9
10 Q. DO YOU CONSIDER DR. AMIT’S ALTERNATIVE APPROACH TO FUEL PAYMENTS
11 UNDER THE MESABA 1 PPA TO BE A VIABLE OPTION?

12 A. I agree that the fuel price risk that Dr. Amit discusses (pages 10-12) is an
13 uneconomic and unreasonable feature of the contract. Further, the
14 contractual mechanism of partially capping the price by fixing the fuel mix,
15 which he discusses (page 11), is potentially viable in relation to the fuel price
16 risk. However, while this suggestion may solve one problem with the Mesaba
17 1 PPA, it addresses only one of the many significant concerns raised in Xcel
18 Energy’s Direct Testimony. As proposed, the Mesaba 1 PPA does not offer a
19 least-cost resource to Xcel Energy’s system and is not consistent with the
20 public interest.

21 22 IV. CONCLUSION

23
24 Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY.

25 A. I agree with Dr. Amit’s conclusions that the Mesaba 1 PPA is not a least-cost
26 resource for Xcel Energy’s system. Because his analysis was based on
27 information provided by Mesaba 1 LLC and a mistaken assumption regarding

1 the determination of capacity payments, its results present an overly optimistic
2 assessment of the costs of the proposal. This qualification only further
3 confirms the conclusion that the Mesaba 1 PPA is not a least-cost resource
4 and is not consistent with the public interest.

5

6 Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

7 A. Yes, it does.