

**MPUC Docket No. E-6472-/M-05-1993  
OAH Docket No. 12-2500-17260-2**

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BEFORE THE  
MINNESOTA OFFICE OF ADMINISTRATIVE HEARINGS  
100 Washington Square, Suite 1700  
Minneapolis, Minnesota 55401-2138

FOR THE  
MINNESOTA PUBLIC UTILITIES COMMISSION  
127 7th Place East, Suite 350  
St. Paul, Minnesota 55101-2147

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In the Matter of the Petition of Excelsior Energy Inc.  
and Its Wholly-Owned Subsidiary MEP-I, LLC For Approval of Terms and  
Conditions For The Sale of Power From Its Innovative Energy Project Using  
Clean Energy Technology Under Minn. Stat. § 216B.1694 and a  
Determination That the Clean Energy Technology Is Or Is Likely To Be a  
Least-Cost Alternative Under Minn. Stat. § 216B.1693

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**REBUTTAL TESTIMONY AND EXHIBITS OF  
EXCELSIOR ENERGY INC. AND MEP-I LLC**

**RALPH OLSON**

**OCTOBER 10, 2006**

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1 **EXCELSIOR ENERGY, INC.**

2 **BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION**

3 **PREPARED REBUTTAL TESTIMONY OF**

4 **RALPH OLSON**

5 **Q Please state your name and business address.**

6 A My name is Ralph Olson. My business address is Marston and Marston,  
7 9656 Blake Place, Edmonds, WA 98020.

8 **Q Have you previously provided testimony in this proceeding?**

9 A No.

10 **I. SCOPE AND SUMMARY**

11 **Q What is the purpose of your Rebuttal Testimony in this proceeding?**

12 A The purpose of my rebuttal testimony is, on behalf of MEP-I LLC and Excelsior  
13 Energy Inc. (collectively “Excelsior”), the developers of the Mesaba Energy Project  
14 (the “Project”), to respond to the Direct Testimony and Schedules of Xcel energy, Inc.  
15 (“Xcel”) witness Patrick J. Panzarino and Minnesota Power (“MP”) witnesses Dwight  
16 D. Anderson and Thomas D. Crowley. In particular, I will respond to the following  
17 issues raised by these witnesses:

- 18 1. benefits of fuel flexibility;  
19 2. supply of petroleum coke; and  
20 3. fuel transportation capacity and competition.

21 **Q What general observations do you have with respect to the concerns raised by Xcel  
22 and MP in this proceeding?**

23 A Excelsior Energy Inc has selected the Mesaba Energy Project which, through its  
24 gasification technology, is suitable for a wide range of fuel feed stocks. The Mesaba

1 Energy Project can access fuel sources from multiple coal basins or supply sources.  
2 The preferred site will further allow the delivery of these fuels by multiple delivery  
3 modes, including rail service by two major rail systems and by truck. The optionality  
4 created by this inherent fuel supply and transportation diversity allows for fuel supply  
5 contracting options that should minimize the fuel supply cost to the Project and allow  
6 for a contracting strategy that can incorporate hedging, a ladder of supply contracts of  
7 varying terms and supply quantities and spot market access. At a minimum, the Project  
8 should have a fuel supply cost that is equal to the fuel supply costs of other regional  
9 fossil fueled power plants operated by NSP and Minnesota Power. The optionality  
10 available to Mesaba Energy Project should allow for fuel mixes that are lower in overall  
11 cost than these regional suppliers over the long term.

12 The Mesaba Energy Project, scheduled for operation in 2011, will be able to  
13 take advantage of the changing coal, petroleum coke and rail transportation markets. It  
14 is not feasible or prudent to expect the Project to sign contracts for long-term supplies  
15 of either fuel or transportation 5 to 6 years in advance of project operation (when the  
16 Power Purchase Agreement has not been concluded). As a potential new market for a  
17 broad range of fuel and new transportation revenues, the Mesaba Energy Project will be  
18 able to exercise negotiating power in the marketplace that older, existing power plants,  
19 that are captive to a single transporter and a narrow range of fuel specifications, cannot  
20 expect. The fact that Excelsior has taken prudent steps to ensure that it can implement  
21 an aggressive fuel supply plan and strategy by maximizing its alternatives will allow the  
22 Mesaba Energy Project to offer a long-term fuel supply contracted at a hedged,  
23 predictable cost.

1 **Q What background and experience do you have to make such observations?**

2 A I have a Bachelor of Science in Chemical Engineering, a Master of Science in  
3 Nuclear Engineering and a Certificate in Business Administration from the University  
4 of Washington in Seattle, Washington. I have also completed advanced studies toward  
5 a PhD in Nuclear Engineering at the University of Washington. I am retired from Puget  
6 Sound Energy where I was Director of Energy Supply. As Director of Energy Supply I  
7 was responsible for Puget's long term energy supply, including coal fueled generation,  
8 natural gas and electrical supply contracts from a number of sources including long  
9 term hydro-electric sourced contracts. The responsibility for coal fueled supply  
10 included managing Puget's ownership, operation, maintenance, fuel supply and contract  
11 output rights and interests in the Colstrip Power Project and the Centralia Steam  
12 Electric Plant. The Centralia Steam Electric Plant purchased coal from the PRB to  
13 supplement local sub-bituminous coal. I was personally responsible for all fuel supply  
14 issues at Colstrip 1&2 and served for a number of years as the Chairman of the Colstrip  
15 3&4 Fuel Subcommittee and as Owner's Representative to the Ownership and  
16 Operating Committees of all units. The Colstrip Project consumed approximately 10  
17 million tons per year of NPRB coal. Small quantities of petroleum coke, sourced from  
18 a local refinery, were burned at Colstrip Units 1&2 for combustion test purposes. Since  
19 my retirement from Puget Sound Energy in 2003 I have worked for Marston & Marston  
20 as a Senior Consultant. My areas of practice, nationally and internationally, have  
21 included coal supply contracts, coal supply development and coal gasification studies.  
22 My resume is attached as Exhibit RO-1.

1 **I. Fuel Flexibility**

2 **Q Do you agree with Mr. Panzarino’s claim that Fuel Switching will not provide a**  
3 **meaningful hedge for the Mesaba 1 Project?**

4 **A** No. The Project’s ability to fuel switch will allow both for aggressive contract  
5 negotiation for fuel and transportation as well as the ability to implement short term  
6 strategies for actual fuel switching utilizing the spot market and contact flexibility. By  
7 having the capability to implement fuel switching, the Mesaba Energy Project will be  
8 able to control fuel costs in a way that many fuel dependant industries, including the  
9 pulp and paper industry, have depended on to limit fuel costs. Based on my  
10 understanding of the E-Gas technology, it is suitable for western sub-bituminous coal as  
11 well as blends with petroleum coke and also can be used for bituminous coal. As a  
12 result, the Project has an inherent advantage because its fuel switching is an actual  
13 capability of its IGCC technology allowing it to realize these benefits. Because not all  
14 fuel costs are linked – for instance high sulfur petroleum coke price is not directly tied  
15 to low sodium, low sulfur coal price – it should be possible to utilize the design  
16 capability of the Mesaba Energy Project to deliver a hedged fuel supply. The fuel  
17 flexibility will also allow for timely and appropriate contract acquisitions to minimize  
18 volatility and fuel cost.

19 **II. Petroleum Coke.**

20 **Q What is your response to Mr. Panzarino’s statement that he does “not believe that**  
21 **Mesaba 1 LLC will be able to enter into long-term agreements for petroleum coke**  
22 **and as such, prices will reflect this volatility?”**

23 **A** Mr. Panzarino’s belief is unfounded and speculative. The depletion of light  
24 sweet crude petroleum as a feedstock for the refining industry has caused a significant

1 increase in the number of coking facilities to be added to existing U.S. refineries to  
2 allow them to process heavy crudes from western Canada and medium crudes from the  
3 deepwater U.S. Gulf. The announced capacity additions for U.S. cokers planning to use  
4 Canadian crudes for the period 2006 through 2010 exceed 15,000 Mt/day. *See Argus*  
5 *Petroleum Coke*, May 9, 2006 Pg 8, Attached as Exhibit RO-2. Additional coker  
6 capacity is planned for development of the tar sands industry in northern Alberta. The  
7 coke produced from these facilities has a typical sulfur content of 6.5% and, as a result,  
8 has a more limited market which in turn causes it to have less price volatility than low  
9 sulfur coal. For example, SO<sub>2</sub> adjusted, Btu Values of Coke and Coal delivered US  
10 Power Trading Hub Cinergy, for April 05-April 06, are Coal \$3.57-\$6.75 per mmBtu;  
11 Coke \$3.20-\$4.12 per mmBtu. The economic benefit of having the ability to fuel  
12 switch and burn petroleum coke is well known to Xcel Energy as they were the number  
13 10 consumer of petroleum coke in the U.S. in 2005 at 222,000 short tons. With the  
14 likely surplus of petroleum coke on the regional North American market, the Mesaba  
15 Energy Project should be able to contract, for short, intermediate and long term periods,  
16 for adequate, low cost supplies of petroleum coke.

17 **Q How do you respond to MP witness Anderson's claims that there is a finite supply**  
18 **of petroleum coke so that prices will increase if the Mesaba Energy Project uses**  
19 **this fuel at its facility?**

20 **A** As noted above, the supply of petroleum coke is not finite and is expected to  
21 grow significantly. As a result, petroleum coke will be an excellent low cost fuel  
22 allowing the Mesaba Energy Project to minimize fuel costs by utilizing petroleum coke  
23 as an alternative or supplement to coal when market conditions dictate.

### III. Fuel Transportation.

1  
2 **Q Mr. Panzarino makes the claim that “short term rail service is not guaranteed,”**  
3 **what is your response?**

4 A There is some foundation for Mr. Panzarino’s claim since the current Class 1  
5 railroads in the U.S. are undergoing a significant capital expansion program to improve  
6 service and remove constraints on their systems. The most significant constraints on the  
7 transportation system from the Powder River Basin exist on the trackage serving the  
8 Southern PRB (“SPRB”). The magnitude of the transportation issues in the SPRB do  
9 not exist on the northern rail corridor serving the reserves and mines in northern  
10 Wyoming and Montana, despite the unfounded assertion of MP addressed below. In the  
11 past the railroads have shown a willingness to make spot transportation agreements  
12 when surplus capacity exists, which is expected by the time the Project comes on line in  
13 2011. Because Mesaba Energy Project represents new, incremental revenue to the  
14 railroads, the inherent fuel switching capability should allow for both short term and  
15 flexible longer term transportation contracting.

16 **Q How do you respond to Mr. Panzarino’s claim that the Mesaba Energy Project’s**  
17 **fuel plan is limited with respect to deliveries of PRB coal?**

18 A Mr. Panzarino’s claim is again unfounded and speculative. The current Class 1  
19 railroads serving the PRB have experienced service disruptions and constraints on the  
20 line serving primarily the SPRB. These railroads are undergoing a significant capital  
21 expansion program to help solve these issues and increase the transportation capacity  
22 out of the mines in the PRB. The northern route has experienced less congestion than  
23 the central route and as such it is expected that this corridor will continue to provide  
24 adequate delivery capacity to allow for contract and spot deliveries when the plant is

1 placed in operation. With a combination of an upgraded delivery system from the  
2 SPRB and an adequate delivery system from the NPRB, rail capacity should exist to  
3 allow for implementation of a cost effective fuel switching program to help control cost  
4 volatility.

5 **Q Do you agree with Mr. Panzarino that Mesaba I's fuel plan is limited with respect**  
6 **to deliveries of eastern coal?**

7 A. No. The Project's fuel plan includes supplies of eastern coal, primarily from the  
8 Illinois Basin, as an option that, like the other options in the fuel plan, would be  
9 available to exercise when and if the economics favored it. The availability of potential  
10 options increases the likelihood that a cost effective fuel supply source with limited  
11 volatility can be implemented.

12 **Q Mr. Panzarino claims that a long term fuel transportation agreement would**  
13 **improve deliverability and reduce fuel volatility, do you agree?**

14 A No, because at this point in the long term fuel and transportation price cycle, and  
15 without taking into account the many options which are available to the Mesaba Energy  
16 Project for development and implementation of a long term fuel plan, any long term  
17 fuel transportation agreement would likely result in an unnecessarily high delivered  
18 price for fuel. This is assuming that a long term transportation agreement can be  
19 obtained. It has been demonstrated in the past, and indeed the present, that all  
20 commodities, including energy and transportation, have price cycles. It appears that the  
21 cycles have just peaked on these prices and may be heading down. While it is always  
22 possible to eliminate volatility by paying a high price, it has also been shown that  
23 having a long term contract does not guarantee a stable price. Recently the airlines have  
24 found out that timing is everything in hedging fuel prices. United Airline hedged its

1 fuel prices in Q3 of 2006, just before the price of jet fuel started dropping and as a result  
2 have paid more than market price. *See* Airline Fuel Hedging, attached as Exhibit RO-3.  
3 Having real alternatives is a better way to control volatility.

4 **Q Do you agree with Mr. Panzarino's claim that long term purchase and**  
5 **transportation agreements will be required to obtain the best prices, manage**  
6 **volatility, and ensure reliable deliveries?**

7 A No. The fuel supply diversity inherent in the Mesaba Fuel Supply Plan will  
8 allow for aggressive negotiation of the best available fuel supply, which may include  
9 long-term but flexible supply agreements that allow for response to market conditions  
10 and take advantage of price reductions in project acceptable fuels. I feel that this is the  
11 best way to obtain the best fuel cost, manage volatility and ensure reliable deliveries.

12 **Q Do you agree with Mr. Panzarino's claim that given the infrastructure required**  
13 **for delivery of solid fuels, coupled with the current and expected continued**  
14 **constraints on delivery and volatile fuel prices, Mesaba 1 LLC's plan results in**  
15 **significant price risk and volatility?**

16 A No. The principal transportation constraints today on Class 1 railroads out of  
17 the PRB occurred on the main rail lines from the SPRB. The railroads are making great  
18 strides to remove these transportation constraints by adding new trains and staff and  
19 upgrading trackage. As utilities have rebuilt inventories in 2006 and with the potential  
20 of a mild winter, it is expected that transportation and fuel price volatility will be  
21 dampened on the short term. On the longer term, the EIA forecasts that rail rates will  
22 peak in 2010 and will then fall to 2.2 per cent above 2004 levels in 2030. *See* EIA  
23 Annual Energy Outlook 2006 page 100, attached as Exhibit RO-4. As transportation  
24 constraints are relieved, increased competition among fuel suppliers and transportation

1 providers should allow Mesaba Energy Project to manage its fuel supplies to minimize  
2 price risk and volatility.

3 **Q What is your response to Mr. Panzarino's claim that the limited number of rail**  
4 **suppliers has led to price volatility?**

5 A The recent price volatility can be attributed to a number of causes, including  
6 shipping constraints and high energy prices in general caused by a number of factors.  
7 As noted above, the current constraints are expected to be resolved. In addition, a new  
8 railroad has been proposed that will access the coal reserves in the Northern PRB.  
9 When constructed, this railroad, the Dakota, Minnesota and Eastern ("DM&E"), will  
10 increase access to PRB reserves in the Wyoming and Montana and should increase  
11 competition. In fact, the DM&E may provide another transportation option for the  
12 Mesaba Energy Project if DM&E can interchange with the CN which will have access  
13 to the Project. The existence of additional fuel supply options, including delivery of  
14 petroleum coke by truck haul from regional oil refineries and rail haul from the US and  
15 significant supplies in Canada, should allow the Mesaba Energy Project to control price  
16 volatility and help manage increases in its overall fuel cost.

17 **Q How do you respond to Mr. Panzarino's claim that the UP is currently operating**  
18 **under an embargo that affects its ability to take on new business.**

19 A The Union Pacific is currently operating under a number of system embargos,  
20 including an embargo on shipments from the SPRB. The current UP embargo on  
21 shipments of coal from the SPRB, that was put into place on July 13, 2006, is for a  
22 12-month duration and the embargo period expires on July 13, 2007. The cause of the  
23 embargo is due to track conditions and is anticipated to be lifted when current system

1 upgrades are put into place. It is not anticipated that this particular embargo will be a  
2 long term issue. *See* UP SPRB Embargo, attached as Exhibit RO-5.

3 **Q What is your response to Mr. Panzarino’s statement that due to the UP embargo**  
4 **and the costs associated with a UP and CN route, that the BNSF is the only option,**  
5 **possibly exposing Mesaba 1 LLC to onerous transportation costs and terms?**

6 A As stated above, the UP embargo is anticipated to be resolved as current system  
7 upgrades are put into place. In addition, as MP demonstrated in its successful  
8 negotiations with the BNSF in 2001, even the potential for competition over the UP and  
9 CN resulted in a very successful negotiating strategy, and as Don Shipper, Minnesota  
10 Power Chief Operating Officer said at the time: “Over the next several years, this new  
11 agreement will provide ongoing stability in our fuel delivery costs. In addition, this  
12 contract will keep our generating plants competitive in the wholesale energy market.”  
13 A copy of MP Press Release is attached as Exhibit RO-6. As trackage constraints are  
14 relieved by the UP, this delivery option will be of increasing importance in reducing  
15 fuel price volatility. It should be noted that the source of coal transported by the BNSF  
16 for MP under this transportation agreement is from the NPRB, a supply area not served  
17 by the UP and CN. However, the potential for increased source and transportation  
18 diversity assisted MP in its successful negotiations.

19 **Q How do you respond to Mr. Panzarino’s implication that the current constraints**  
20 **on rail shipments from the Power River Basin by the BNSF and UP will continue?**

21 A First, the constraints are being resolved. Second, no industry, especially a  
22 capital intensive one, wants to install more capacity than they can sell in the market  
23 place. However, each market player will want to maximize its revenue for capacity it  
24 has installed to meet its anticipated market demand. To the extent that any competition

1 exists in the transportation market, having access to such competition is recognized by  
2 all market players as better than being captive to one provider. Xcel admits that having  
3 access to two rail carriers is advantageous for siting a power plant in its November 23,  
4 2005 Base Load Development Process Study Options Report (“Xcel Baseload Report”)  
5 on page 10 as a part of its assessment of various self build sites. A Copy of the Xcel  
6 Baseload Report is attached as Exhibit RO-7.

7 **Q Do you agree with Mr. Panzarino’s claim that, given the necessary infrastructure**  
8 **coordination associated with delivering Illinois coal to the Mesaba Unit 1, it is**  
9 **doubtful that this approach would be commercially viable absent long-term**  
10 **contracts with the various suppliers?**

11 A No. At this point in the development of the fuel supply plan for Mesaba Unit 1,  
12 Illinois coal is another potential option. Access to Illinois Basin coal will increase the  
13 options that are available and cause other possible suppliers in the negotiation process  
14 to be uncertain as to the extent of the Projects real options and costs. Having access to  
15 as many options as possible, especially at no cost, increases the negotiation power of the  
16 Mesaba Energy Project. Should a least cost option for a fuel supply from the Illinois  
17 Basin develop during the life of the Project, it will be possible to implement an Illinois  
18 Basin fuel strategy due to the project design and then available transportation  
19 infrastructure.

20 **Q How do you respond to Mr. Panzarino’s claim that Mesada Unit 1 will likely find**  
21 **that it is unable to fully use the fuel-switching capabilities of Mesaba Unit 1 as it**  
22 **will be necessary to commit to a fuel source and delivery services on a longer term**  
23 **basis to obtain reliable service and predictable prices?**

1 A Mr. Panzarino's claim improperly ignores the realities of the marketplace.  
2 Whether Mesaba Unit 1 utilizes all its fuel switching capability will be determined by  
3 the marketplace over the project's life. The fact that the project has the capability to  
4 switch fuel will act as a hedge against volatility in any one market segment, either fuel  
5 or transportation. With anticipated contract flexibility it will be possible to respond to  
6 price increases in one market segment by switching all or part of its fuel supply.

7 **Q Do you agree with Mr. Panzarino that, given the plans for future capital**  
8 **investments by the railroads, that continued upward pressure on delivered prices**  
9 **can be expected?**

10 A No and neither does the Department of Energy. As noted in the EIA Annual  
11 Energy Outlook 2006, attached as Exhibit RO-4, which takes into account future  
12 expansion plans in the energy consuming economy, upward pressure on both mine  
13 mouth prices and transportation rates are expected to moderate after 2010 compared to  
14 2004 prices. By maintaining a flexible fuel supply plan, the Mesaba Energy Project  
15 should be able to respond to pricing changes in different segments of the fuel market.

16 **Q MP witness Crowley takes the position that destination competition is beneficial**  
17 **only if there is competition at the origin of shipment. Is this a correct statement?**

18 A No, as noted above, a fuel plan that provides for transportation competition and  
19 origin competition, as well as fuel type competition, has been developed for the Mesaba  
20 Energy Project. The flexible fuel options available to the Mesaba Energy Project will  
21 provide access to coal reserves and petroleum coke that currently have limited  
22 marketability due to their high sulfur or high sodium. This plan, when implemented,  
23 should provide a system of checks and balances to allow for a long term fuel supply at a  
24 hedged, predictable, stable price.

1 **Q Mr. Crowley also states that true competition will exist only if the competitors cost**  
2 **of service is about the same. Do you agree?**

3 A No. In a competitive world, there are many pricing options available to a  
4 supplier of services. These may include full cost of service as well as incremental  
5 pricing. The only way to ensure that the best price is obtained, no matter how the  
6 supplier of services may evaluate the options, is to be involved in the marketplace and  
7 to have other options. To be held captive to a single supplier, be it for the commodity  
8 or the transportation, has been recognized by Xcel Energy as a disadvantage in their  
9 criteria used for evaluating and ranking sites for base load generation. Indeed, the  
10 potential benefit of accessing two rail systems was recognized in the Xcel Baseload  
11 Report. *See* Exhibit RO-7. This potential advantage accrues to a site without an in-  
12 depth analysis of the current or future competition that may exist between the carriers.  
13 By having an option for fuel supplier by region, quality and type (e.g. coal or petroleum  
14 coke), as well as transportation, there is the maximum assurance that competition will  
15 exist and that the lowest practicable fuel supply cost can be achieved.

16 **Q Mr. Crowley claims that Excelsior will have difficulty negotiating favorable rates**  
17 **from rail carriers. Is this a fair assessment?**

18 A No, this is an unfounded and speculative assessment. The Mesaba Energy  
19 Project represents a new customer for both fuel and transportation services and has the  
20 potential of expanding its fuel use if other projects are built using IGCC given the  
21 incentive under Minnesota Statutes. With the ability to access fuel over potentially  
22 under-utilized transportation corridors, this new load should be an attractive market for  
23 fuel suppliers and rail and motor carriers. Accordingly, the Mesaba Energy Project  
24 should be able to negotiate favorable rates from rail carriers.

1 **Q Do you agree with Mr. Crowley's claim that MP will have lower rail rates for its**  
2 **Boswell plant than will Mesaba?**

3 A No. Many legacy rail transportation contracts have rates that can be either lower  
4 or higher than are currently available from carriers. As these contracts roll off, the new  
5 transportation rates are a function of the current market and the competitive forces that  
6 are in play at the time the new deal is struck. When the Boswell plant's transportation  
7 contract expires in 2011, its new transportation rates will be determined, in part, by the  
8 options the MP has and can realistically implement to supply fuel for that facility.  
9 Indeed, Mr. Crowley states that the lack of competition results in higher prices and MP  
10 will have less transportation and fuel supply options at its Clay Boswell plant than the  
11 Mesaba Energy Project. Mr. Crowley's statement about competition reveals that the  
12 Mesaba Energy Project should have lower transportation and fuel prices since there will  
13 be more competition given the fuel flexibility and transportation alternatives of the  
14 Project.

15 **Q Is Mr. Crowley correct in stating that rail competition will not allow Mesaba to**  
16 **have an unprecedented variety of coals?**

17 A No. In assessing a set of potential fuel supply options that are in competition  
18 with each other to produce the lowest delivered cost, it is necessary to compare sets of  
19 commodity costs and transportation costs. For example, Xcel and the Mesaba Energy  
20 Project, through the Fuel Supply Committee envisioned by the Mesaba Energy Project  
21 PPA, will compare the cost of Montana PRB coal delivered by BNSF against SPRB  
22 coal delivered by UP/CN against petroleum coke delivered by truck or by CN. The use  
23 of a Fuel Subcommittee to manage the fuel supply decisions of a multi-party generating  
24 facility is a common and effective way to manage any risks and unknown issues as they

1 arise. Each of these options has its own internal set of commodity prices based on  
2 demand for that particular coal at the time of evaluation. This plan allows for an  
3 unprecedented variety of coals and supply options that are made available by the design  
4 of the plant and its location with service by three rail carriers and truck haul to be  
5 considered by the Fuel Supply Committee in developing the Supply Plan for Mesaba.

6 **Q Mr. Crowley claims that rail carriers will not compete for Mesaba's business and**  
7 **that with only two rail carriers currently operating in the PRB, BNSF and UP each**  
8 **have a large amount of market power and can push prices up, do you agree?**

9 A No, because there is nothing to indicate that the potential incremental revenue to  
10 be derived by a rail carrier through providing transportation services to Mesaba will be  
11 avoided or rejected by any of the rail carriers. Mesaba is a new high volume customer  
12 and as such should be sought after. When the anticipated debottlenecking of the rail  
13 system has been achieved over the next few years, the railroads will be seeking new  
14 business and new revenues to bolster their earnings. For a captive plant like Boswell,  
15 the BNSF will have little incentive to offer an attractive, low price because they know  
16 that they can count on and will get that business. For a plant with multiple options like  
17 the Mesaba Energy Project, carriers will offer their best prices to get the business. MP  
18 realized the benefit of having a second real or potential transportation provider when it  
19 entered into contract negotiations with the BNSF for a 10 year contract in 2001. By  
20 proposing participation in a new short line railroad that would have interconnected the  
21 Boswell plant to the CN and UP, they were able to secure a 10 year rail contract for that  
22 facility and the Laskin Energy Center near Hoyt Lakes, with coal supplied from the  
23 NPRB. While this new transportation link would have resulted in a longer  
24 transportation distance, the mere threat of new competition over the CN and UP resulted

1 in a successful negotiation with the BNSF as noted in MP's press release about the new  
2 Agreement with BNSF. A copy of the MP Press Release is attached as Exhibit RO-6.  
3 However, when the current transportation agreement expires in 2011, Minnesota Power  
4 may actually have to construct the additional rail link to be able to achieve the same  
5 negotiating position that the Mesaba Energy Project will have due to its location and  
6 planned fuel supply diversity. The Mesaba Energy Project has built into its facility the  
7 actual competition that MP only proposed by including rail spurs for both BNSF and  
8 CN and by including fuel flexibility into the design of its IGCC plant. Such built in  
9 competition should help thwart any "market power."

10 **Q How do you respond to the claim by Mr. Crowley that the railroads are reluctant**  
11 **to compete with each other on moves that are theoretically competitive and**  
12 **Mesaba Unit 1 will find it difficult to negotiate favorable contract terms with the**  
13 **railroads, particularly from the NPRB?**

14 A See my response to the previous question. In addition, there is no evidence that  
15 the Class 1 railroads will not compete against each other when a competitive situation is  
16 presented.

17 **Q Do you agree with Mr. Crowley that the Mesaba Unit 1 should not expect rail rates**  
18 **to fall for transporting coal from where he expects coal to be sourced from?**

19 A No. The Mesaba Energy Project has not committed to any sourced fuel supply  
20 but has maintained the optionality of a diverse and flexible fuel supply including  
21 petroleum coke, western sub-bituminous and Illinois Basin bituminous coals. Because  
22 some of these coals have restricted markets, due to their higher sulfur or sodium,  
23 currently available, low cost reserves have not been developed or are not being  
24 produced in the quantities that are forecast to be available. A new high volume

1 customer like the Mesaba Energy Project can allow these dormant resources to be  
2 produced and transportation developed in an existing, non-bottlenecked corridor at  
3 competitive prices. The fuel flexibility and interconnection with two rail carriers of the  
4 Mesaba Energy Project will provide significantly more negotiating leverage than MP  
5 had in 2001 and the potential for better results.

6 **Q How do you respond to the statement by Mr. Crowley that neither the BNSF nor**  
7 **the CN can deliver directly on site to the Mesaba Project without a spur line being**  
8 **built?**

9 A While it is currently correct that neither the BNSF nor the CN currently have  
10 lines that cross the Mesaba Generating Plant site, both of these railroads have mainlines  
11 within 2 miles of the preferred West site. The Mesaba Project contemplates the  
12 construction of rail spurs from both the BNSF and the CN to provide diversity in  
13 transportation systems to ensure a least cost fuel supply.

#### 14 IV. CONCLUSION

15 **Q Does this conclude your prepared rebuttal testimony?**

16 A Yes.

**EXHIBIT NO. \_\_\_\_ (RO-1)**

**Resume of Ralph Olson**

**EXHIBIT NO. \_\_\_\_ (RO-2)**

**Argus Petroleum Coke, May 9, 2006, Page 8**

**EXHIBIT NO. \_\_\_\_\_ (RO-3)**

**Airline Fuel Hedging**

**EXHIBIT NO. \_\_\_\_ (RO-4)**

**EIA Annual Energy Outlook 2006, Page 100**

**EXHIBIT NO. \_\_\_\_\_ (RO-5)**

**UP SPRB Embargo**

**EXHIBIT NO. \_\_\_\_\_ (RO-6)**

**MP Press Release**

**EXHIBIT NO. \_\_\_\_ (RO-7)**

**Xcel Baseload Report**