



400 North Fourth Street
Bismarck, ND 58501
(701) 222-7900

January 23, 2013

Ms. Kate Whitney, Administrator
Utility Division
Montana Public Service Commission
1701 Prospect Avenue
Helena, MT 59620

Re: General Gas Rate Application
Docket No. D2012.9.100

Dear Ms. Whitney:

Enclosed please find Montana-Dakota Utilities Co.'s responses to the Montana Public Service Commission data requests dated December 21, 2012, January 8, 2013, and January 18, 2013. Responses to the following requests are attached:

PSC-024	PSC-050	PSC-102
PSC-034	PSC-052	PSC-106
PSC-035	PSC-096	PSC-111
PSC-036	PSC-097	PSC-112
PSC-037	PSC-100	PSC-138
PSC-047		

Sincerely,

A handwritten signature in blue ink that reads 'Rita A. Mulkern'.

Rita A. Mulkern
Director of Regulatory Affairs

Attachments
cc: Service List

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED DECEMBER 21, 2012
DOCKET NO. D2012.9.100**

PSC-024

Regarding: Key employee severance plan

Witness: Applicable Witness

- a. What was the total severance paid in 2011 for key employees?**
- b. Is the severance amount included in the compensation numbers?**

Response:

- a. Montana-Dakota paid \$153,968 of severance to key employees in 2011.**
- b. The compensation included \$89,924 applicable to Montana gas operations.**

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED DECEMBER 21, 2012
DOCKET NO. D2012.9.100**

PSC-034

**Regarding: 3GIS Company
Witness: Skabo**

- a. Montana Dakota developed and deployed a mobile map product from 3GIS. Does MDU Resource Group or Montana Dakota Utilities receive any royalties or revenues as a result of developing the map product?**
- b. If so please indicate who the revenue is received from and how it is credited to MT natural gas customers.**
- c. If MT natural gas customers do receive a portion of the revenue please explain the reason.**

Response:

- a. Montana-Dakota does not receive any royalties or revenues from 3GIS.**
- b. Not applicable.**
- c. Not applicable.**

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED DECEMBER 21, 2012
DOCKET NO. D2012.9.100**

PSC-035

**Regarding: Combined Office
Witness: Skabo**

- a. Please breakdown the costs the company incurred purchasing or leasing the new combined office.
- b. If the breakdown does not include dollar amounts for office decorating or office furniture please include those costs and the portion allocated to MT natural gas customers.

Response:

- a. The combined office building was constructed. Below is the total cost of the combined office building as of December 31, 2011.

	<u>Total</u>	<u>Montana Gas</u>
Land	\$801,421	\$591,199
Structures & Improvements	4,341,473	3,202,655
Office Furniture & Equipment	170,730	125,945
Total	<u>\$5,313,624</u>	<u>\$3,919,799</u>

- b. There were no office decorating costs and the cost of office furniture is included in the above table.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED DECEMBER 21, 2012
DOCKET NO. D2012.9.100**

PSC-036

Regarding: Call Center

Witness: Gardner

- a. Does MDU receive revenue for using the call center for non-regulated utilities?**
- b. If so please indicate who the revenue is received from and how it is credited to MT natural gas customers.**
- c. If MT natural gas customers do receive a portion of the revenue please explain the reason.**

Response:

- a. Montana-Dakota does not receive revenue from using the call center for non-regulated activities. Any work performed on non-regulated activities by employees is charged to the non-regulated business.**
- b. Not applicable.**
- c. Not applicable.**

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED DECEMBER 21, 2012
DOCKET NO. D2012.9.100**

PSC-037

Regarding: Pension Costs

Witness: Jones

- a. **What does MDU consider normal market returns for pension funding returns? On what logic and information does MDU rely on for its acceptable returns on its pension fund?**
- b. **Provide all work papers, analyses, memos and other documentation that support the logic of MDU's basis for the company's assumptions or normal market returns.**

Response:

- a. Please see Attachment A, for the Statement of Investment Policy. Page 5 of Attachment A provides the Company's Specific Financial Objectives.
- b. Please see Attachment A.

STATEMENT OF INVESTMENT POLICY
FOR
MDU RESOURCES GROUP, INC. PENSION PLANS
July 1, 2005

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STATEMENT OF INVESTMENT POLICY
FOR
MDU RESOURCES GROUP, INC. PENSION PLANS

SCOPE OF THIS STATEMENT OF INVESTMENT POLICY

This Statement of Investment Policy reflects the investment policy, objectives, and constraints of the MDU Resources Group, Inc. Pension Plans.

PURPOSE

The purpose of this Statement of Investment Policy is to establish the underlying philosophy and processes, known as the investment policy for the selection, monitoring, evaluation and management of the investment of the assets of MDU Resources Group, Inc. ("MDU Resources" or "the Company") Pension Plans that is in the best interests of the participants and in accordance with the requirements of the Employee Retirement Income Security Act of 1974 ("ERISA").

DEFINITIONS

1. "Employee Benefits Investment Committee" shall mean the investment committee established by the MDU Resources Group, Inc. Board of Directors.
2. "ERISA" shall mean the Employee Retirement Income Security Act of 1974, any amendments thereto, and any regulations issued thereunder.
3. "Fiduciary" shall mean any individual or group of individuals as defined in ERISA, section 3 (21)(a). The role of a Fiduciary is to manage the overall investment process, including investment policy decisions, asset and investment style allocation decisions, manager selection and review, and tailoring of the investment program to meet the Plan's overall investment policy and objectives.
4. "Investment Horizon" shall be the time period over which the investment objectives, as set forth in this statement, are expected to be met. While the investment horizon for this Plan is long-term in nature, investment performance expectations as detailed in this Statement of Investment Policy will be evaluated over a full market cycle (which typically lasts from 3-5 years).
5. "Investment Management Consultant" shall mean any individual or organization employed to provide advisory services, including advice on investment objectives and/or asset allocation, manager search, and performance monitoring.
6. "Investment Manager" shall mean any individual, or group of individuals, employed to manage the investments of all or part of the Plan assets.

7. "Plan" shall mean all of the pension plans sponsored by MDU Resources Group, Inc. or its affiliates.
8. "Securities" shall refer to the marketable investment securities which are defined as acceptable in this statement.

This Statement of Investment Policy is set forth by the MDU Resources Group, Inc. Employee Benefits Investment Committee ("EBIC") in order to:

1. Define the responsibilities of all involved parties.
2. Establish and communicate to all plan Investment Managers prudent investment goals and objectives regarding Plan assets.
3. Provide guidance and limitations to all Investment Managers regarding the investment of Plan assets.
4. Establish a basis for evaluation of investment results.
5. Establish a relevant investment horizon over which Plan assets will be managed.

The intent of this Statement of Investment Policy is to outline and guide the investment management of Plan assets. It is intended to be deemed sufficiently specific, yet provide the flexibility to be practical.

DELEGATION OF AUTHORITY

The EBIC is a named fiduciary under ERISA, and therefore has responsibility for directing and monitoring the investment management of Plan assets. As such, the EBIC is authorized to delegate certain responsibilities to professional experts in selected areas of investment decision-making. This delegated authorization includes, but is not limited to:

1. Investment Management Consultants. The Investment Management Consultants may assist the EBIC in: establishing investment policy, objectives and guidelines; selecting investment managers; reviewing such managers over time; measuring and evaluating investment performance; and other investment related duties as deemed appropriate.
2. Investment Managers. The Investment Managers will have discretion to purchase, sell, or hold specific securities and vote proxies in compliance with Plan investment guidelines.
3. Trustee. The EBIC may appoint an outside individual or entity, such as a bank trust department, to be Trustee. The Trustee will assume fiduciary responsibility for the administration of Plan assets. The Trustee will comply with the terms of the Trust where Trust is defined as the agreement between MDU Resources Group, Inc. and the Trustee pursuant to which the Plan assets are retained by the Trustee.
4. Custodian. If appointed by EBIC and pursuant to an agreement with the Trustee, the Custodian will physically maintain possession of securities owned by the Plan, collect dividend and interest payments, redeem maturing securities, and effect receipt and delivery following purchases and sales. The custodian may also perform regular accounting of all assets owned, purchased, or sold, as well as movement of assets within Plan accounts.

5. Additional specialists such as attorneys, auditors, actuaries, retirement plan consultants and others may be employed by the EBIC to assist in meeting its responsibilities and obligations to administer Plan assets prudently.

If such experts employed are also deemed to be Fiduciaries, they must acknowledge such in writing. The EBIC will not reserve any control over investment decisions beyond the specific limitations described in these statements. Investment Managers will be held responsible and accountable to adhere to this Statement of Investment Policy and achieve the objectives stated herein. While it is not believed that the limitations will hamper Investment Managers, each Investment Manager should request modifications which they deem appropriate.

All expenses for such related investment services must be customary and reasonable, and will be borne by the Plan as deemed appropriate and necessary.

ASSIGNMENT OF RESPONSIBILITY

Responsibilities of the EBIC

The EBIC is responsible for the establishment of the investment policy, the management of Plan assets through the evaluation of pension investment policy alternatives and making policy recommendations. The EBIC shall discharge its duties solely in the interest of the Plan participants and beneficiaries, with the care, skill, prudence and diligence under the circumstances then prevailing, that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of a business with like character and aims. The specific responsibilities of the EBIC relating to the investment management of Plan assets include:

1. Authorization of the investment policy that will guide the investment of Plan assets.
2. Adhering to the guidelines contained in ERISA and all other applicable regulations.
3. Determining the Plan's risk tolerance and Investment Horizon, and communicating these to the appropriate parties.
4. Establishing reasonable and consistent investment objectives, policies and guidelines that will direct the investment of the Plan's assets.
5. Prudently and diligently appoint qualified investment professionals, including Investment Manager(s), Investment Management Consultant(s), Custodian(s), and Trustees.
6. Regularly evaluate the performance of the Investment Manager(s) and the Investment Management Consultant to assure adherence to policy guidelines and monitor investment objective progress.
7. Implementation of proper control procedures, including asset allocation parameters, and the selection or replacement of investment professionals due to change in investment management objectives, process, or due to a failure to comply with established guidelines.

Responsibilities of the Investment Management Consultant

The Investment Management Consultant's role is that of a Fiduciary to the Plan. Recommendations concerning investment decisions or modifications to investment management policy regarding Plan assets will be presented by the Investment Management Consultants, and will be consistent with the

investment objectives, policies, guidelines and constraints as established in this Statement of Investment Policy. Specific responsibilities of the Investment Management Consultants include:

1. Assisting in the development and periodic review of investment policy.
2. Determining future liability stream of the Plan so that proper funding requirements can be determined.
3. Assisting in determining proper strategic allocation of assets to meet long term earnings expectations.
4. Conducting investment manager searches at the request and direction of the EBIC.
5. Providing "due diligence", or research on the Investment Manager(s).
6. Monitoring the performance of the Investment Manager(s) to provide the EBIC with the ability to determine the status of reaching investment objectives and recommending termination or changes of Investment Managers.
7. Communicating matters of policy, manager research and manager performance to the EBIC.

Responsibilities of the Investment Manager(s)

Each Investment Manager must acknowledge in writing its acceptance of responsibility as a fiduciary and an investment manager under ERISA and other applicable regulations. Each Investment Manager will have full discretion to make all investment decisions for the assets placed under its discretion, while observing and operating within ERISA and other applicable law and all policies, guidelines, constraints and philosophies as outlined in this statement. Specific responsibilities of the Investment Manager(s) include:

1. Discretionary investment management including decisions to buy, sell, or hold individual securities, and to alter asset allocation within the guidelines established in this statement.
2. Reporting, on a timely basis, quarterly investment performance results.
3. Communicating any major changes in economic outlook, investment strategy, or any other factors which affect implementation of investment process, or achievement of the Plan's investment objectives.
4. Inform the EBIC regarding any qualitative change to their investment management organization; such as changes in portfolio management personnel, ownership structure, investment policy, etc.
5. Voting proxies on behalf of the Plan, and communicating such voting records to the EBIC on a timely basis.

GENERAL INVESTMENT PRINCIPLES

Investments shall be made solely in the interest of the participants and beneficiaries of the Plan and for the exclusive purpose of providing benefits accrued thereunder and defraying the reasonable expenses of administration.

Plan investments shall be diversified so as to minimize the risk of large losses, unless under specific circumstances it is clearly prudent not to do so.

The EBIC may employ one or more investment managers of varying styles and philosophies to attain the Plan's objectives. Cash is to be employed productively at all times by investment in short-term cash equivalents to provide safety, liquidity and return.

INVESTMENT MANAGEMENT POLICY

Financial objectives for the Plan have been established in connection with a review of the current and projected financial requirements (liabilities) of the Plan. While there cannot be complete assurance that the defined objectives will be realized, special emphasis should be placed on achieving the following objectives:

1. Preservation and Increase of Plan Assets - Consistent with their respective investment styles and philosophies, Investment Managers should make reasonable efforts to preserve and grow capital, understanding that losses may occur in individual securities.
2. Risk Aversion - Understanding that risk is present in all types of securities and investment styles, the EBIC recognizes that some risk is necessary to produce long-term investment results that are sufficient to meet the Plan's objectives. However, the Investment Managers are to make reasonable efforts to control risk and will be evaluated regularly to ensure that the risk assumed is commensurate with their investment style and objectives.
3. Adherence to Investment Discipline - Investment Managers are expected to adhere to the investment management styles for which they were hired. Investment Managers will be evaluated regularly for adherence to investment discipline.

SPECIFIC FINANCIAL OBJECTIVES

Investment objectives are based on a ten-year Investment Horizon so that interim fluctuations can be viewed in an appropriate perspective.

Over this Investment Horizon, it is the goal of the Plan to meet or exceed:

1. The return of a balanced market index comprised of 50% S&P 500, 10% Russell 2000, 10% MSCI EAFE, and 30% Salomon Brothers Broad Investment Grade Index or other representative benchmark.
2. The EBIC's desired objective to earn a rate-of-return on total fund asset investments that will provide a return 4 percentage points greater than the rate of inflation (measured by the Consumer Price Index for all Urban Consumers for all items, U.S. City Average).

The investment goals above reflect the investment objectives of the Plan, and are not meant to be imposed on each investment account (if more than one account is used). The goal of each Investment Manager, over the Investment Horizon, shall be to:

1. Meet or exceed the market index, or blended market index, selected and agreed upon by the EBIC that most closely corresponds to the style of investment management.
2. Display an overall level of risk in the portfolio which is consistent with the risk associated with the benchmark specified above. Risk will be measured by the standard deviation of quarterly returns.

Specific investment goals and constraints for each Investment Manager shall be incorporated as part of this Statement of Investment Policy. Each Investment Manager shall receive a written statement outlining his specific goals and constraints, as they differ from those objectives of the entire Plan.

ASSET ALLOCATION GUIDELINES

Investment management of the assets of the Plan shall be in accordance with the following asset allocation guidelines:

1. Aggregate Plan Asset Allocation Guidelines (at market value)

<u>Asset Class</u>	<u>Minimum</u>	<u>Maximum</u>	<u>Preferred</u>
Equities	65%	75%	70%
Fixed Income	25%	35%	30%
Cash & Equivalents	0%	10%	0%

2. The EBIC may employ Investment Managers whose investment disciplines require investment outside the established asset allocation guidelines. However, taken as a component of the Plan, such disciplines must fit within the overall asset allocation guidelines established in this statement. Such Investment Managers will receive written direction from the EBIC regarding specific objectives and guidelines.

Permitted Assets

1. Cash Equivalents
 - ◆ Treasury Bills
 - ◆ Money Market Funds
 - ◆ Short-Term Investment (STIF) Funds
 - ◆ Commercial Paper
 - ◆ Banker's Acceptances
 - ◆ Repurchase Agreements
 - ◆ Certificates of Deposit

2. Fixed Income Securities
 - ◆ U.S. Government and Agency Securities
 - ◆ Corporate Notes and Bonds
 - ◆ Private Placement Debt Instruments
 - ◆ Mortgage Backed Bonds
 - ◆ Fixed Income Securities of Foreign Governments and Corporations

- ◆ Collateralized Mortgage Obligations
 - ◆ Taxable Municipals
3. Equity Securities
- ◆ Common Stocks
 - ◆ Convertible Notes and Bonds
 - ◆ Convertible Preferred Stocks
 - ◆ American Depository Receipts (ADRs) of Non-U.S. Companies
 - ◆ Stocks of Non-U.S. Companies (Ordinary Shares)

Prohibited Assets

Prohibited investments include, but are not limited to the following:

- ◆ Commodities and Futures Contracts
- ◆ Equity Private Placements
- ◆ Employer Securities¹
- ◆ Leveraged or Derivative Securities
- ◆ Options
- ◆ Direct Real Estate Investments
- ◆ Precious Metals
- ◆ Venture Capital
- ◆ Limited Partnerships

Prohibited Transactions

Prohibited transactions include, but are not limited to the following:

- ◆ Shortselling
- ◆ Margin Transactions

Diversification

Investment diversification is an investment policy consistent with the intent to minimize the risk of large losses. Consequently, all equity and fixed-income portfolios will be constructed by the respective Investment Managers to attain broad diversification.

Broad diversification for that portion of the equity fund that is actively managed shall mean that no more than 5 percent of the portfolio shall be invested with any one specific issuer, based on the cost of the security at the time of purchase.

Broad diversification for that portion of the equity fund representing equity assets structured to correlate with movements of a selected equity index will permit portfolio structure to correspond with the selected index. Dependent on index composition, this may necessitate an investment with a single issuer that may exceed 5 percent of the total portfolio based on purchase cost. Such investments with a single issuer exceeding 5 percent will be permitted, provided, however that the Plan must be notified in writing of any such commitment.

¹ "Employer Security" shall mean a security issued by an employer of employees covered by the Plans.

For compliance purposes, equity investments in an index managed portfolio will be administered separate and apart from the 5 percent cost basis equity limitation placed on actively managed equity portfolio commitments.

Broad diversification for the fixed income fund shall mean, with the exception of United States Government Issues, no more than 10 percent of the portfolio based on the cost of the security at the time of purchase shall be invested with any one specific issuer.

LIQUIDITY

Each Investment Manager shall maintain liquid reserves equal to at least 1 percent of their managed fund to facilitate the payment of pension benefits. An analysis of the cash flow projections of the Plans indicates that contributions may not equal benefit payments during the next ten-year period.

VOLATILITY

Consistent with the desire for a target commitment of up to 70 percent in equities, with a minimum allocation of 65 percent in equities and a maximum allocation of 75 percent equities, the desire for prudent diversification, and the risk/return guidelines specified for each individual manager, it is expected that the Plan will have above median volatility when compared to a representative universe of balanced fund portfolios.

SELECTION OF INVESTMENT MANAGERS

The EBIC's selection of Investment Manager(s) must be based on prudent due diligence procedures. A qualifying investment manager must be a registered investment advisor under the Investment Advisors Act of 1940, or a bank or insurance company. The EBIC requires that each investment manager provide, among other things, written acknowledgment of fiduciary responsibility to the Plan and certification that the Investment Manager meets the applicable bonding requirements of ERISA.

CONTROL PROCEDURES

Review of Policy

The investment policy will be reviewed on an annual basis by the EBIC, or more frequently should circumstances change to the extent that the policy is ineffective.

Review of Liabilities

All major liability assumptions regarding work force, salaries and wages, benefit levels, and actuarial assumptions will be subject to annual review. This review will focus on an analysis of any major differences between the Company's assumptions and actual experience.

Review of Plan Performance

Performance will be measured quarterly by the Investment Management Consultant(s) on a total rate of return basis and reported to the EBIC.

Performance will be related to overall objectives and capital market returns as evidenced by various market indices and other portfolios operating under similar objectives and guidelines. Consideration will be given to risk/reward relationships.

Investment Manager Performance Review & Evaluation

A review of all Investment Managers investment performance will be conducted by the Investment Management Consultant quarterly to ascertain progress of each Investment Manager versus the return objectives. The quarterly reports cover four basic areas: returns, comparisons of returns to benchmarks and a statistical universe of similar portfolios, diagnostic risk analyses, and compliance with relevant policies and objectives. These results will also focus on:

- administrative and organizational changes;
- the Investment Manager's adherence to the policy guidelines;
- a comparison of the Investment Manager's results against funds having similar policies (in terms of the stock/bond ratio, diversification, and volatility); and the opportunities available in both equity and bond markets.
- Investment Managers may also be evaluated on personnel, strategy, research capabilities, organizational and business matter, and other qualitative factors that may impact their ability to achieve the desired investment results

Investment performance will be reviewed annually with each Investment Manager. In addition an on-site meeting will be held with each Investment Manager on an alternating two-year basis.

The EBIC intends to evaluate portfolio performance over at least a three-year period, but reserves the right to terminate an Investment Manager for any reason, including the following:

1. Investment performance which is significantly less than anticipated given the discipline employed and the risk parameters established, or unacceptable justification of poor results.
2. Failure to adhere to any aspect of this Statement of Investment Policy, including communication and reporting requirements.
3. Significant qualitative changes to the Investment Manager's organization.

PERFORMANCE EXPECTATIONS

The most important performance expectation is the achievement of investment objectives. The primary investment objective for the Plan is to provide long-term capital appreciation through investment in equities and fixed income securities. In addition, to insure that the EBIC is thoroughly evaluating the investment opportunities available over a specific time period, the EBIC will measure the return on the equity portion of the funds that are actively managed to a universe of equity

managers or a universe of managers of similar investment management styles and on the fixed-income portion of the funds to a universe of fixed-income managers or a universe of managers of similar investment management style.

Performance returns for equity or bond funds managed in a passive manner, that is to correlate with movements of a specific equity or bond index, will be measured based upon actual performance deviation from the selected index.

Although the performance will be reviewed each quarter, the primary focus will be on a market cycle which would normally be a period of from 3-5 years.

IMPLEMENTATION

The implementation of this Statement of Investment Policy, through the use of investment managers, shall be formalized in appropriate addenda to this Statement of Investment Policy. Such addenda shall include specific targeted investment return objectives for each manager.

EBIC MINUTES

The EBIC shall document its analysis and decisions in the EBIC minutes.

MDU RESOURCES GROUP, INC.

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR WENTWORTH, HAUSER AND VIOLICH

DATED: August 1, 2009

Through the actions of the Employee Benefits Committee ("EBC"), Wentworth, Hauser and Violich ("WHV") has been retained by the company with the responsibility for the investment management of a separate large-cap international equity portfolio. This addendum defines specific investment objectives and guidelines for the company assets under investment management by WHV and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle, as established in the Statement of Investment Policy, it is expected that WHV will meet or exceed:

- o The return of the Morgan Stanley Europe, Australasia, and Far East (EAFE) Index.
- o A performance ranking in the top one-third (33rd) percentile of a nationally recognized database of managers with similar management styles, or other comparable industry standards for that of a large-cap international equity portfolio.

Volatility (Risk)

WHV is expected to maintain a level of risk commensurate with the risk associated with the index stated above.

Diversification

WHV has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of the security at the time of purchase without the prior written approval of the EBC.

Asset Allocation

WHV is authorized to invest 99 percent of the pension assets in this portfolio. The remaining 1 percent of the WHV portfolio should be maintained in liquid cash equivalents to meet monthly Plan disbursements. WHV may, at its discretion, convert up to 10 percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

**SPECIFIC INVESTMENT GUIDELINES FOR BARROW, HANLEY, MEWHINNEY &
STRAUSS, INC**

Dated: April 1, 2009

Through the actions of the Employee Benefits Committee, Barrow, Hanley, Mewhinney & Strauss, Inc. ("BHMS") has been retained by the company with responsibility for the investment management of a separate domestic fixed-income portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by BHMS and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that BHMS will meet or exceed:

- The return of the Barclay's Aggregate Bond Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized database of fixed-income managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

BHMS is expected to achieve the performance expectations stated above while maintaining a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

BHMS has full discretion in determining the level of diversification in this portfolio. However, with the exception of United States Government securities, no single fixed-income issue may exceed ten (10) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Committee.

Asset Allocation

BHMS is authorized to remain fully invested with regard to the pension assets in this fixed-income portfolio.

MDU RESOURCES GROUP, INC. PENSION PLANS
ADDENDUM TO STATEMENT OF INVESTMENT POLICY
SPECIFIC INVESTMENT GUIDELINES FOR WEDGE CAPITAL MANAGEMENT
(FIXED INCOME PORTFOLIO)

Dated: April 1, 2009

Through the actions of the Employee Benefits Committee, WEDGE Capital Management ("WEDGE") has been retained by the company with responsibility for the investment management of a separate domestic fixed-income portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by WEDGE and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that WEDGE will meet or exceed:

- The return of the Barclay's Aggregate Bond Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized database of fixed-income managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

WEDGE is expected to achieve the performance expectations stated above while maintaining a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

WEDGE has full discretion in determining the level of diversification in this portfolio. However, with the exception of United States Government securities, no single fixed-income issue may exceed ten (10) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Committee.

Asset Allocation

WEDGE is authorized to remain fully invested with regard to the pension assets in this fixed-income portfolio.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR FRANKLIN PRIVATE CLIENT GROUP

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, Franklin Private Client Group ("FPCG") has been retained by the company with responsibility for the investment management of a separate domestic small-cap growth equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by FPCG and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that FPCG will meet or exceed:

- The return of the Russell 2000 Growth Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized small-cap growth equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

FPCG is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

FPCG has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee. In addition, no more than twenty-five (25) percent of its portfolio may be invested in any one industry sector.

Asset Allocation

FPCG is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. FPCG may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR TEMPLETON PORTFOLIO ADVISORY

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, Templeton Portfolio Advisory ("TPA") has been retained by the company with responsibility for the investment management of a separate international large-cap value equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by TPA and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that TPA will meet or exceed:

- The return of the Morgan Stanley Europe, Australia, Far East (EAFE) Index.
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized international large-cap value equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

TPA is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

TPA has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee.

Asset Allocation

TPA is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. TPA may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR TEMPLETON PORTFOLIO ADVISORY

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, Templeton Portfolio Advisory ("TPA") has been retained by the company with responsibility for the investment management of a separate international large-cap value equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by TPA and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that TPA will meet or exceed:

- The return of the Morgan Stanley Europe, Australia, Far East (EAFE) Index.
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized international large-cap value equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

TPA is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

TPA has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee.

Asset Allocation

TPA is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. TPA may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR NWQ INVESTMENT MANAGEMENT

Dated: August 1, 2005

Through the actions of the Employee Benefits Investment Committee, NWQ Investment Management ("NWQ") has been retained by the company with responsibility for the investment management of a separate domestic large-cap value equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by NWQ and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that NWQ will meet or exceed:

- The return of the Russell 1000 Value Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized large-cap value equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

NWQ is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

NWQ has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee.

Asset Allocation

NWQ is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. NWQ may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR WEDGE CAPITAL MANAGEMENT

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, WEDGE Capital Management ("WEDGE") has been retained by the company with responsibility for the investment management of a separate domestic small-cap value equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by WEDGE and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that WEDGE will meet or exceed:

- The return of the Russell 2000 Value Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized small-cap value equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

WEDGE is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

WEDGE has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee. In addition, the amount of the portfolio that may be invested in any sector is limited to twenty-five (25) percent or the benchmark's weighting for that sector plus five (5) percent, whichever is greater.

Asset Allocation

WEDGE is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. The remaining one (1) percent of the WEDGE portfolio should be maintained in liquid cash equivalents to meet monthly Plan disbursements. WEDGE may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS
ADDENDUM TO STATEMENT OF INVESTMENT POLICY
SPECIFIC INVESTMENT GUIDELINES FOR SANDS CAPITAL MANAGEMENT

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, Sands Capital Management ("Sands") has been retained by the company with responsibility for the investment management of a separate domestic large-cap growth equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by Sands and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that Sands will meet or exceed:

- The return of the Russell 1000 Growth Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized large-cap growth equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

Sands is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

Sands has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed ten (10) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee.

Asset Allocation

Sands is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. Sands may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS
ADDENDUM TO STATEMENT OF INVESTMENT POLICY
SPECIFIC INVESTMENT GUIDELINES FOR MONTAG & CALDWELL

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, Montag & Caldwell ("Montag") has been retained by the company with responsibility for the investment management of a separate domestic large-cap growth equity portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by Montag and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that Montag will meet or exceed:

- The return of the Russell 1000 Growth Index
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized large-cap growth equity database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

Montag is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

Montag has full discretion in determining the level of diversification in this portfolio. However, no single issue of common stock may exceed five (5) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee.

Asset Allocation

Montag is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in equity securities. Montag may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

MDU RESOURCES GROUP, INC. PENSION PLANS

ADDENDUM TO STATEMENT OF INVESTMENT POLICY

SPECIFIC INVESTMENT GUIDELINES FOR DEUTSCHE ASSET MANAGEMENT

Dated: July 1, 2005

Through the actions of the Employee Benefits Investment Committee, Deutsche Asset Management ("Deutsche") has been retained by the company with responsibility for the investment management of a separate domestic fixed income portfolio. This Addendum defines specific investment objectives and guidelines for those company assets under investment management by Deutsche and these guidelines must be incorporated into the Statement of Investment Policy. The policy items included in the Statement of Investment Policy are applicable for the entire Plan, and may not apply to each individual investment manager. Therefore, if a policy item in this Addendum conflicts with a policy item in the Statement of Investment Policy, the specific item delineated in this Addendum shall apply.

Investment Performance

Over a market cycle as established in the Statement of Investment Policy, it is expected that Deutsche will meet or exceed:

- The return of the Salomon Brothers Broad Investment-Grade Bond Index.
- A performance ranking in the top one-third (33rd) percentile of a nationally recognized fixed income database of investment managers with similar investment styles, or other comparable industry standards.

Volatility (Risk)

Deutsche is expected to maintain a level of risk in this portfolio commensurate with the risk associated with the index stated above.

Diversification

Deutsche has full discretion in determining the level of diversification in this portfolio. However, with the exception of United States Government issues, no single fixed income issue may exceed ten (10) percent of this portfolio based on the cost of security at the time of purchase without the prior written approval of the Employee Benefits Investment Committee.

Asset Allocation

Deutsche is authorized to invest ninety-nine (99) percent of the pension assets in this portfolio in fixed income securities. Deutsche is authorized to invest up to twenty (20) percent of this portfolio in Rule 144A Private Placement debt instruments. Deutsche may at its discretion convert up to ten (10) percent of these assets into cash equivalents.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 8, 2013
DOCKET NO. D2012.9.100**

PSC-047

Regarding: Stock Based Compensation

Witness: Jones

Provide all work papers, analyses, memos and other documentation that support the calculated stock compensation cost.

Response:

Please see Attachment A.

MDU Resources Group, Inc.
Stock-based Compensation (Performance Share Awards)

Calculation of Performance Share Award

The compensation expense amounts for stock-based compensation are calculated based on participant target shares, the grant date fair value and forfeiture assumptions based on historical experience. The grant date fair value is based on a Monte Carlo simulation provided by an outside valuation firm.

Compensation expense is determined based on the following formula:

$$\text{Annual compensation expense} = (A * B) / C$$

A = Number of shares granted, less estimated forfeitures

B = Grant date fair value

C = Vesting period (expressed in years)

The annual amount is then prorated throughout the year and monthly compensation expense amounts are provided to the business units.

The associated dividend equivalents for the performance share awards are treated as a reduction to retained earnings in accordance with generally accepted accounting principles and are calculated as follows:

$$\text{Annual dividend equivalents} = (A * B * C)$$

A = Number of shares granted, less estimated forfeitures

B = Annual dividend rate

C = Vesting percentage assumption

The annual amount is then prorated throughout the year and monthly amounts are provided to the business units.

Vesting and entitlement to the performance share awards is based on the company's total shareholder return over designated performance periods as measured against a selected peer group. Performance shares can be earned from 0% to 200% of the original grant.

The Monte Carlo simulation grant date fair value once established does not change based on changes in actual vesting versus the assumptions built into the simulation. Therefore, once the compensation expense at the beginning of the award is established it will not change except for a true up for actual forfeitures. Once the award vests, the adjustment from estimated forfeitures to actual forfeitures will be made.

MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 8, 2013
DOCKET NO. D2012.9.100

PSC-050

Regarding: Lobbying Expenses
Witness: Applicable

Is MDU currently recovering or proposing to recover lobbying expenses from rate payers? If so please provide all work papers, analyses, memos and other documentation that support the lobbying contributions that the Company proposes to include in the gas utility revenue requirement.

Response:

No, lobbying expenses are recorded as a below the line expense.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 8, 2013
DOCKET NO. D2012.9.100**

PSC-052

Regarding: Liability Insurance

Witness: Applicable

- a. When did MDU last investigate the costs of its property and liability premiums?**
- b. What was the result of those quotes compared to the company's current premiums?**
- c. What is MDU's average deductible that must be paid on all insured property and liability insurance policies?**

Response:

- a. Montana-Dakota reviewed its property and liability insurance in December 2012 for renewal in 2013.**
- b. The 2013 premiums for property insurance increased 7.3 percent compared to current premiums and the liability insurance increased 5.2 percent compared to current premiums.**
- c. Montana-Dakota's deductible is \$500,000 for both liability and property insurance.**

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-096

Regarding: Reuse of material

Witness: Mulkern

- a. Please provide the Company's accounting treatment for reuse material.**
- b. Please provide all underlying support and justification for the process employed.**
- c. Please provide the level of plant by account retired during the past 10 years and reused along with the corresponding accounting values by year.**

Response:

- a. Retired natural gas components of property may be reused in limited cases. The items are either salvaged back into general stores materials at the average cost of the stores item or are transferred to another application at the original installed cost and accumulated depreciation. Reinstallation costs of these items at a new application are recorded as an operations and maintenance expense.
- b. Montana-Dakota complies with the FERC Uniform System of Accounts.
- c. Montana-Dakota recorded a total of approximately \$3,000 of reused material salvage from retirements over the last 10 years all of which is related to mains and service salvaged pipe.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-097

**Regarding: Abnormal, atypical and/or unusual historical plant activity
Witness: Mulkern**

Please identify all abnormal, atypical, and/or unusual historical plant activity of the Company's investment that occurred and was:

- a. removed from the historical analysis of MDU's Investment for depreciation purposes; or**
- b. retained in MDU's analysis of historical investment for depreciation purposes.**

Response:

- a. None.**
- b. None.**

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-100

**Regarding: Gross Salvage
Witness: Mulkern**

If dollars associated with the reuse or reimbursement (i.e., all amounts received from an outside party when plant is damaged or relocated, whether replaced or not) are not 100% credited or assigned to gross salvage, then specifically state which portions of the Uniform System of Accounts are specifically relied upon. Provide a copy of each specific definition, instruction, etc., that forms the basis of MDU's opinion.

Response:

Reimbursement from third parties related to damage or relocation are credited to the costs incurred to replace or relocate the facilities. Plant additions and cost of removal less any salvage are offset proportionately.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-102

Regarding: New replacement investment

Witness: Mulkern

- a. Please provide a detailed narrative setting forth which costs are attributable to the new replacement investment and which costs are associated with the retirement of the existing investment when the Company retires a plant and replaces the plant at the same location.**
- b. Please provide the underlying basis and all workpapers associated with any related analyses.**

Response:

- a. All costs such as labor, material, and contract services are directly assigned to either the addition or retirement (cost of removal or salvage) accounts associated with a work order to replace facilities. Instructions are such that any costs incurred related to the removal, disposal, and salvage obtained from those activities are to be recorded in the retirement work in progress accounts. All costs related to the construction of new facilities are to be charged to the addition work in progress accounts.
- b. Please see Attachment A for the Company Policy entitled 'Utility Plant – Purchase and Sales of Units of Property'.



UTILITY PLANT –
PURCHASES AND SALES OF
UNITS OF PROPERTY

AD-6

Page 1 of 3
07/01/07

I. PURPOSE

- A. It is the policy of the Company to account for the purchase and sale of utility plant investments in accordance with the FERC Uniform System of Accounts.

II. SCOPE

- A. For purposes of this instruction, the following definitions are adopted:

Operating unit - A unit or system of electric or gas facilities the construction or purchase of which requires a FERC Certificate of Public Convenience and Necessity and which has an original cost threshold of \$50,000 or more.

Property unit - A unit of property as prescribed in Title 18 of the Code of Federal Regulations, part 216 for which the original cost is accounted for separately within utility plant accounts. The term property unit is synonymous with retirement units.

Cost of removal - The cost of labor, materials and other expenses incurred to demolish, dismantle, tear down or otherwise remove from service and retire electric or gas utility plant retirement units.

Salvage value - The amount received for property retired, less any expenses incurred in connection with the sale or preparing the property for sale or, if the retired property is retained by the Company, the amount at which the material recoverable is chargeable to account 154, Materials and Supplies.

III. PROCEDURE

- A. In accordance with its interpretation of the Code of Federal Regulations, the Company has determined to comply with the instructions for recording salvage values upon the retirement of property units and operating units as follows:
1. The amount received for, or the estimated salvage value of, property units (excluding land or land rights) removed, sold, abandoned, destroyed, or which for any cause has been withdrawn from service and which do not constitute an operating unit as defined above, shall be credited to account 108, Accumulated Provision for Depreciation of Utility Plant - Gas or Electric, as appropriate.
 2. The amount received for property units (excluding land or land rights) withdrawn from service and which constitute an operating unit as defined above, upon conveyance or transfer to another by sale, merger, consolidation, or otherwise, shall be credited to FERC account 102, Electric or Gas Plant Purchased or Sold and the book cost of the property credited to the appropriate utility plant accounts, including amounts carried in account 114, Electric or Gas



**UTILITY PLANT –
PURCHASES AND SALES OF
UNITS OF PROPERTY**

AD-6

Page 2 of 3
07/01/07

Plant Acquisition Adjustments. The amounts (estimated if not known) carried with respect thereto in the accounts for accumulated provision for depreciation, depletion, and amortization and in account 2520, Customer Advances for Construction, shall be charged to such accounts and the contra entries made to account 102. The difference, if any, between (a) the net amount of debits and credits and (b) the consideration received for the property (less commissions and other expenses of making the sale) shall be included in account 4211, Gain on Disposition of Property, or account 4212, Loss on Disposition of Property, as appropriate. The amount received from the sale of land or land rights, less agents' commissions and other costs incident to the sale, and the book cost of such land or rights shall be included in account 4116, Gains from Disposition of Utility Plant or 4117, Losses from Disposition of Utility Plant, as appropriate, when such property has been recorded in account 105, Electric or Gas Plant Held for Future Use or 1051, Production Properties Held for Future Use, otherwise to account 4211, Gain on Disposition of Property or 4212, Loss on Disposition of Property, as appropriate. Proper adjustments of the accounts shall be made with respect to any structures or improvements located on land sold.

- B. In accordance with its interpretation of the Code of Federal Regulations, the Company has determined to comply with the instructions for recording the original cost of utility plant constituting an operating unit, as defined above, which is acquired by purchase, merger, consolidation, liquidation, or otherwise, as follows:
1. The costs of acquisition, including expenses incidental thereto properly includible in utility plant, shall be charged to account 102, Electric or Gas Plant Purchased or Sold. The original cost of the operating unit, estimated if not known, shall be credited to account 102, and concurrently charged to the appropriate electric or gas plant in service account and to account 104, Electric or Gas plant Leased to Others, account 105, Electric or Gas Plant Held for Future Use, account 105.1, Production Properties Held for Future Use, and account 107, Construction Work in Progress--Electric or Gas, as appropriate.
 2. The depreciation, depletion and amortization applicable to the original cost of the properties purchased, shall be charged to account 102, Electric or Gas Plant Purchased or Sold, and concurrently credited to the appropriate account for accumulated provision for depreciation, depletion or amortization. The cost of any property includible in account 121, Nonutility Property, shall be transferred thereto.
 3. The amount remaining in account 102, Electric or Gas Plant Purchased or Sold, shall then be closed to account 114, Electric or Gas Plant Acquisition Adjustments.
 4. Debit amounts recorded in account 114 related to plant and land acquisition will be amortized to account 406, Amortization of Electric Gas Plant Acquisition Adjustments, over a period not longer than the estimated remaining life of the properties to which such amounts relate. Debit amounts related to the acquisition of land only will be amortized to account 406

POLICIES



**UTILITY PLANT –
PURCHASES AND SALES OF
UNITS OF PROPERTY**

AD-6

Page 3 of 3
07/01/07

over a period of not more than 15 years. Credit amounts recorded in account 102 shall be held therein until disposition instructions have been requested and received from the FERC.

IV. RECOGNIZED EXCEPTIONS

- A. The provisions of this policy do not apply to the purchase of utility plant which does not qualify as an operating unit as defined herein. Such purchases of less than an operating unit shall be accounted for as normal additions and retirements in accordance with the FERC Uniform System of Accounts.
- B. The provisions for disposition of debit amounts recorded in account 114 as prescribed in III.B. above may be altered when, in the opinion of the Company, an alternative treatment is desirable and petitions the FERC and receives permission to do so.

V. ADMINISTRATION

- A. The President and Chief Executive Officer of Montana-Dakota Utility Co. and Great Plains Natural Gas Co. has the responsibility for the overall administration of this policy and procedure. Establishment and implementation of procedures to administer the policy is the responsibility of the Executive Vice President, Finance and Chief Accounting Officer of Montana-Dakota Utility Co. and Great Plains Natural Gas Co.

REVIEWED:

EXECUTIVE VICE PRESIDENT,
FINANCE AND CAO

7-16-07

DATE

APPROVED:

PRESIDENT AND CEO

7-16-07

DATE

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-106

**Regarding: Emergency Retirements
Witness: Mulkern**

Please identify the dollars of cost of removal by account by year for the past 10 years associated with retirements that occurred under emergency situations.

Response:

This information is not available. Costs associated with emergency situations are not identified in the construction or fixed asset accounting system.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-111

RE: Board compensation

Witness: Anne Jones

- a. Has MDU used proxy companies to establish its board compensation?**
- b. Is so, please identify them and the compensation they pay board members.**

Response:

- a. Yes.
- b. Please see Attachment A for the list of proxy companies reviewed in 2012 and the 20101 compensation information for the directors of these proxy companies.

APPENDIX B - 2011 PROXY PEER DATA ON SIZE AND PAY FROM EQUILAR

Company Size Statistics

	FY End Mkt Cap (\$MMs)	Revenues (\$MMs)	Net Income (\$MMs)	Total Assets (\$MMs)	Employees
ALLIANT ENERGY CORP	\$ 4,896.6	\$ 3,665.3	\$ 302.3	\$ 9,687.9	4,262
ATMOS ENERGY CORP	\$ 2,932.3	\$ 4,347.6	\$ 198.9	\$ 7,282.9	4,949
BERRY PETROLEUM CO	\$ 2,266.9	\$ 921.3	\$ (228.1)	\$ 2,735.0	317
BLACK HILLS CORP /SD/	\$ 1,475.1	\$ 1,272.2	\$ 40.4	\$ 4,127.1	2,030
COMSTOCK RESOURCES INC	\$ 736.3	\$ 434.4	\$ (33.5)	\$ 2,639.9	124
EMCOR GROUP INC	\$ 1,784.9	\$ 5,613.5	\$ 121.7	\$ 3,014.1	25,000
EQT CORP	\$ 8,190.6	\$ 1,639.9	\$ 479.8	\$ 8,772.7	1,835
GRANITE CONSTRUCTION INC	\$ 917.6	\$ 2,009.5	\$ 51.2	\$ 1,547.8	3,000
MARTIN MARIETTA MATERIALS	\$ 3,440.6	\$ 1,713.8	\$ 78.4	\$ 3,147.8	4,993
NATIONAL FUEL GAS CO	\$ 4,032.9	\$ 1,778.8	\$ 258.4	\$ 5,284.7	1,827
NORTHWEST NATURAL GAS CO	\$ 1,284.1	\$ 848.8	\$ 63.9	\$ 2,746.6	1,050
PIKE ELECTRIC CORP	\$ 306.6	\$ 593.9	\$ 1.4	\$ 493.6	4,600
QUANTA SERVICES INC	\$ 4,468.0	\$ 4,623.8	\$ 132.5	\$ 4,699.1	2,300
QUESTAR CORP	\$ 3,533.7	\$ 1,194.4	\$ 207.9	\$ 3,532.8	1,730
SCANA CORP	\$ 5,871.1	\$ 4,409.0	\$ 387.0	\$ 13,534.0	5,889
SM ENERGY CO	\$ 4,686.8	\$ 1,603.3	\$ 215.4	\$ 3,799.0	639
SOUTHERN UNION CO (from '10)	\$ 3,000.5	\$ 2,489.9	\$ 242.6	\$ 8,238.5	2,437
SOUTHWEST GAS CORP	\$ 1,958.5	\$ 1,887.2	\$ 112.3	\$ 4,276.0	5,754
STERLING CONSTRUCTION CO	\$ 175.8	\$ 501.2	\$ (36.7)	\$ 303.8	1,606
SWIFT ENERGY CO	\$ 1,264.3	\$ 599.1	\$ 83.0	\$ 2,212.5	309
TEXAS INDUSTRIES INC	\$ 1,168.2	\$ 621.8	\$ (64.9)	\$ 1,551.0	2,020
VECTREN CORP	\$ 2,476.9	\$ 2,325.2	\$ 141.6	\$ 4,878.9	4,500
VULCAN MATERIALS CO (from '10)	\$ 5,725.0	\$ 2,558.9	\$ (102.5)	\$ 8,337.9	7,994
WHITING PETROLEUM CORP	\$ 5,484.6	\$ 1,899.6	\$ 491.7	\$ 6,045.6	692
25th Percentile	\$ 1,279.2	\$ 903.2	\$ 30.6	\$ 2,711.2	1,467
50th Percentile	\$ 2,704.6	\$ 1,746.3	\$ 117.0	\$ 3,963.0	2,165
75th Percentile	\$ 4,522.7	\$ 2,507.2	\$ 222.2	\$ 6,354.9	4,687
MDU RESOURCES GROUP	\$ 4,052.1	\$ 4,050.5	\$ 226.0	\$ 6,556.1	8,021
Percentile Ranking	69.7%	85.0%	75.5%	75.7%	95.6%

Non - COB Director Compensation Statistics

Cash Retainer	BOD +		Total Equity	Total Direct Comp.
	Comm. Fees in Cash	Total Cash		
\$ 145,000	\$ -	\$ 145,000	\$ -	\$ 145,000
\$ 75,000	\$ -	\$ 75,000	\$ 102,030	\$ 177,030
\$ 50,000	\$ 7,200	\$ 57,200	\$ 120,000	\$ 177,200
\$ 36,000	\$ 9,000	\$ 45,000	\$ 60,000	\$ 105,000
\$ 78,000	\$ -	\$ 78,000	\$ 172,380	\$ 250,380
\$ 60,000	\$ -	\$ 60,000	\$ 326,964	\$ 386,964
\$ 50,500	\$ 9,000	\$ 59,500	\$ 110,479	\$ 169,979
\$ 70,000	\$ -	\$ 70,000	\$ 82,500	\$ 152,500
\$ 16,250	\$ 8,436	\$ 24,686	\$ 130,328	\$ 155,014
\$ 44,000	\$ 10,800	\$ 54,800	\$ 121,104	\$ 175,904
\$ 90,000	\$ 9,000	\$ 99,000	\$ -	\$ 99,000
\$ 25,000	\$ 6,000	\$ 31,000	\$ 70,000	\$ 101,000
\$ 50,000	\$ 12,000	\$ 62,000	\$ 100,000	\$ 162,000
\$ 50,000	\$ 12,000	\$ 62,000	\$ 100,003	\$ 162,003
\$ -	\$ 39,000	\$ 39,000	\$ 60,000	\$ 99,000
\$ 55,000	\$ -	\$ 55,000	\$ 160,000	\$ 215,000
\$ 90,000	\$ -	\$ 90,000	\$ 149,544	\$ 239,544
\$ 40,000	\$ 9,900	\$ 49,900	\$ 88,941	\$ 138,841
\$ 17,500	\$ 9,000	\$ 26,500	\$ 50,000	\$ 76,500
\$ 55,000	\$ -	\$ 55,000	\$ 130,000	\$ 185,000
\$ 36,000	\$ -	\$ 36,000	\$ 34,940	\$ 70,940
\$ 45,000	\$ 7,500	\$ 52,500	\$ 50,000	\$ 102,500
\$ 45,000	\$ 30,000	\$ 75,000	\$ 89,771	\$ 164,771
\$ 45,000	\$ 9,000	\$ 54,000	\$ 115,000	\$ 169,000
\$ 39,000	\$ -	\$ 48,675	\$ 60,000	\$ 104,375
\$ 50,000	\$ 7,968	\$ 56,100	\$ 100,002	\$ 162,002
\$ 62,500	\$ 9,225	\$ 71,250	\$ 123,328	\$ 177,073
\$ 55,000	\$ -	\$ 55,000	\$ 110,000	\$ 165,000
65.2%	0.0%	43.4%	60.6%	56.7%

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-112

RE: Board compensation

Witness: Anne Jones

Do you agree that the Board simultaneously does work necessary to provide safe, reliable, and economic service to customers, even while it performs tasks that are undertaken for the benefit of MDU's bondholders and stockholders?

Response:

Yes. Like any business, the interests of the Company's debt holders and stockholders are indirectly advanced by the sustained ability of the Company to provide safe, reliable and economic service to its customers. Therefore, necessary actions by the Board regarding investment in plant and equipment to assure safe, reliable and economic service for customers are meaningful actions to investors. Similarly, management selection, oversight and compensation are important to the interests of both investors and customers. These are examples of where the Board simultaneously does work that is necessary to provide safe, reliable, and economic service for customers but also indirectly benefits debt holders and shareholders.

**MONTANA-DAKOTA UTILITIES CO.
MONTANA PUBLIC SERVICE COMMISSION
DATA REQUEST
DATED JANUARY 21, 2013
DOCKET NO. D2012.9.100**

PSC-138

RE: Capital Structure

Witness: Morman

Please explain MDU's logic for including short term debt in the Company's capital structure.

- a. Please provide all orders MDU has received allowing the inclusion of short debt within the Company's capital structure.**

Response:

The Company possesses a \$125 million revolving credit agreement facility and uses this line of credit for general funding purposes including the investment in facilities, infrastructure and other capital projects and as such it is included in short term debt. The Company will continue to use this facility until such time that it reaches its credit agreement ceiling of \$125 million and then will seek permanent financing through long term notes. The borrowing rates under this facility are significantly less than long term notes.

- a. Please see Attachment A for the Order in Wyoming Electric Docket No. 20004-81-ER-09.

Response No. PSC-138
Attachment A

Response No. PSC-138
Attachment A

BEFORE THE PUBLIC SERVICE COMMISSION OF WYOMING

IN THE MATTER OF THE AMENDED)
APPLICATION OF MONTANA-DAKOTA)
UTILITIES CO., A DIVISION OF MDU)
RESOURCES GROUP, INC., FOR A GENERAL)
RATE INCREASE FOR ITS WYOMING)
ELECTRIC UTILITY SERVICE RATES OF)
\$5,053,756 PER ANNUM)

Docket No. 20004-81-ER-09
(Record No. 12259)

APPEARANCES

For the Applicant, Montana-Dakota Utilities Co. (MDU or the Company):
BRUCE S. ASAY of Associated Legal Group, Cheyenne, Wyoming.

For the Intervenor, Office of the Consumer Advocate (OCA):
IVAN H. WILLIAMS, Senior Counsel, Cheyenne, Wyoming.

MEMBERS OF THE PUBLIC APPEARING *PRO SE*

STEVE MAIER, Chairman of the Sheridan County Commission
BILL BRADSHAW, Chairman of the Sheridan School District Board of Directors
CRAIG DOUGHERTY, District Superintendent, Sheridan School District
DAVE KINSKEY, Mayor, City of Sheridan
BILL BENSEL, Sheridan, Wyoming
MARYANN BURTON, Trustee of the Sheridan School District No. 2
ED JOHLMAN, CFO, Sheridan Memorial Hospital
LES ENGELTER, AARP, Sheridan, Wyoming
BOB ORRELL, Trustee, Sheridan Public Library
JILL MORRISON, Powder River Basin Research Council
DAVID KANE, Sheridan County Stock Growers
ROB FORISTER, Facilities Manager, Sheridan Memorial Hospital
MIKE NIKE, Sheridan County Commissioner,
and numerous other MDU customers

HEARD BEFORE

Chairman ALAN B. MINIER
Deputy Chairman STEVE OXLEY
Commissioner KATHLEEN A. LEWIS

STEVE MINK, Assistant Secretary, and DAVID J. LUCERO, Attorney Supervisor
Presiding pursuant to a *Special Order* of the Commission

MEMORANDUM OPINION, FINDINGS AND FINAL ORDER
(Issued May 26, 2010)

This matter is before the Wyoming Public Service Commission (Commission) upon the amended application of MDU for authority to increase its Wyoming electric utility service rates in the amount of \$5,053,756 per annum, on the intervention of the OCA and the comments and

representations of the members of the public appearing *pro se* herein. The Commission, having reviewed the original application and attached exhibits, the amended application and attached exhibits, the evidence of record, the *Stipulation and Agreement (Stipulation)*, its files regarding MDU, applicable Wyoming utility law, and being otherwise fully advised in the premises, hereby FINDS AND CONCLUDES:

Findings of Fact: Parties and Procedure

1. On August 14, 2009, MDU filed its original application, together with pre-filed testimony and exhibits and revised tariff sheets, requesting authority to increase its retail electric utility service rates in Wyoming by \$6,198,501 per year, or an overall average increase of 30.7%. MDU stated the proposed rate increase was necessary to recover its 25% ownership interest investment in the Wygen III generating unit (Wygen III or the Plant). MDU noted it received a Certificate of Public Convenience and Necessity (CPCN) to participate in the Wygen III coal-fired electric generating unit in Docket No. 20004-72-EA-08. The certificate authority made no determinations regarding any ratemaking issues associated with MDU's participation in the generating unit. The Company stated that Wygen III was expected to be completed and ready for commercial operation in the second quarter of 2010. MDU stated its investment in Wygen III secures a reliable long-term supply source for a portion of the electric requirements for the Company's Sheridan System. MDU stated that it currently purchases its energy and capacity requirements for its Wyoming electric customers through a purchased power contract with Black Hills Power, Inc. (Black Hills). MDU stated that, when the purchased power contract expires in 2016, its customers will become exposed to uncertain and potentially volatile wholesale power costs. Participation in WYGEN III will help protect its customers from future wholesale market volatility.

2. MDU stated that its net rate base would increase by approximately \$62 million upon completion of Wygen III, reflecting the Company's 25% ownership interest in the Plant, together with increased operation and maintenance (O&M) expenses associated with the Wygen III facility, but net of a reduction in purchased power costs under its current full requirements contract with Black Hills. The Company estimated the rate impact in Wyoming would be approximately \$6,198,501 annually or an overall average increase of 30.7% based on a 2008 pro forma test year. The test year in this case consisted of the 12 month period ending December 31, 2008. MDU stated that its existing rates were unjust, unreasonable, and not compensatory, and therefore should be increased as requested to allow the Company to earn an adequate return on its investment in Wygen III.

3. MDU proposed to recover the requested revenue increase from its various customer classes in the following amounts and percentages:

Class	Increase	Percentage Change
Residential	\$2,968,001	26.1%
Small General Service	\$1,552,124	41.3%
Irrigation Service	\$70,255	26.9%
Large General Service	\$1,579,743	34.5%
Lighting	\$28,378	16.7%
Overall Increase	\$6,198,501	30.7%

4. With its application, MDU filed the prepared direct testimony of David L. Goodin, J. Stephen Gaske, Darcy J. Neigum, Garrett Senger, Rita A. Mulkern, and Tamie A. Aberle, together with supporting exhibits, studies, and other documentation for the case.

5. On August 17, 2009, the Commission issued its *Suspension Order* suspending the Company's rates in this case for investigation and further action for the initial six-month period provided in W.S. § 37-3-106(c), which commences after the 30-day notice term provided in subsection (b) thereof.

6. On August 25, 2009, the Commission issued its *Notice of Application*, providing for an intervention, comment and protest deadline of September 25, 2009. The *Notice of Application* was published once a week for two consecutive weeks in the *Sheridan Press* and a public service announcement was aired five times a week for two weeks on KROE-AM in Sheridan.

7. The OCA filed its *Notice of Intervention* on August 25, 2009, and requested the application be set for public hearing. No other formal -- and timely -- intervention petitions were filed.

8. On September 24, 2009, MDU customers filed with the Commission a petition bearing numerous customer signatures, opposing the proposed rate increase and requesting a public hearing be held in the Sheridan area. Throughout the course of these proceedings, numerous MDU customers filed comments opposing the general rate increase or the proposed increase to the Irrigation class. Some of the customer comments also requested that a public hearing be held in Sheridan. Copies of all customer comments and requests for a public hearing were provided to MDU and OCA.

9. On October 15, 2009, the Commission issued its *Notice of Setting Scheduling Conference* which set a scheduling conference for November 4, 2009, in the Commission's hearing room in Cheyenne, Wyoming.

10. On October 20, 2009, the Commission issued its *Special Order Authorizing One Commissioner and/or Hearing Examiner to Conduct Public Hearing*.

11. The duly noticed scheduling conference was held on November 4, 2009. Bruce S. Asay, local counsel for MDU, participated in person. Rita Mulkern and Tamie Aberle for MDU participated by telephone. Ivan Williams, counsel for the OCA, and David Lucero, Steve Mink and Marci Norby, of the Commission Staff, participated in person.

12. On November 5, 2009, the Commission issued its *Scheduling Conference Order (Scheduling Order)* which established a procedural schedule agreed to by the parties at the scheduling conference, including a public hearing commencing on February 23, 2010, in the Commission's hearing room in Cheyenne, Wyoming.

13. The Commission issued its *Procedural Notice and Order Setting Public Hearing* on November 10, 2009 (*Procedural Order*). It set a public hearing to commence on February

23, 2010, in the Commission's hearing room in Cheyenne, and provided for the filing of written public comments by February 23, 2010. It was published once per week for two consecutive weeks in the *Sheridan Press* and a public service announcement was aired five times a week for two weeks on KROE-AM in Sheridan.

14. To accommodate the requests of MDU customers for a Sheridan public hearing, the Commission issued its *Procedural Notice and Order Setting Public Comment Hearing* on December 9, 2009, setting a public comment hearing to commence on February 10, 2010, at the Sheridan Public Library. It was published once per week for two consecutive weeks in the *Sheridan Press* and a public service announcement was aired five times a week for two weeks on KROE-AM in Sheridan.

15. On December 30, 2009, Dave Kinskey, Mayor of the City of Sheridan (the City), filed a letter offering the Sheridan City Council Chambers as a location for the February 10, 2010, public comment hearing as it is equipped with a camera system which allows for live broadcast, recording and rebroadcasting on the City's local government channel. He stated there was a tremendous amount of interest in MDU's proposed rate increase and it would be beneficial to the public to be able to broadcast the hearing. On January 4, 2010, via electronic mail, the parties were advised that the location of the public comment hearing had changed and would now be held in the Sheridan City Council Chambers.

16. On January 14, 2010, MDU filed its supplement to application (*Amended Application*) together with appendices, exhibits and statements, which had the effect of amending the Company's original application. MDU stated that, after a review of the applicable federal authority, it believed it was entitled to take certain bonus depreciation deductions for Wygen III. The *Amended Application* was filed to reflect bonus depreciation deductions associated with Wygen III expenditures that reduced the revenue increase found in the Company's original application from \$6,198,501 per annum (30.7 % overall) to \$5,053,756 per annum (25.1% overall).

17. The amended rate increase was proposed to be recovered from the various customer classes by the following amounts and percentages:

Class	Increase	Percentage Change
Residential	\$2,414,230	21.2%
Small General Service	\$1,296,410	34.5%
Irrigation Service	\$55,496	21.2%
Large General Service	\$1,263,787	27.6%
Lighting	\$23,833	14.0%
Overall Increase	\$5,053,756	25.1%

18. On January 19, 2010, OCA pre-filed the direct testimonies and respective exhibits of Denise Kay Parrish, Amy J. Zamora and Kimber M. Wichmann.

19. On January 21, 2010, the Commission issued its *Amended Procedural Notice and Order Setting Public Hearings (Amended Procedural Order)*. The *Amended Procedural Order* gave notice that the Company's original application had been amended and the amount of the

proposed revenue increase and the recovery of the proposed increase from the various customer classes had also been revised. Further, the notice provided that the February 10, 2010, public comment hearing to be held at the Sheridan Public Library had been relocated to Sheridan Community College. The *Amended Procedural Order* also provided additional notice of the public hearing already scheduled to commence on February 23, 2010, in the Commission's hearing room in Cheyenne. It was published once per week for two consecutive weeks in the *Sheridan Press* and a public service announcement was aired five times a week for two weeks on KROE-AM in Sheridan. A display ad announcing the Sheridan public comment hearing was also published in the *Sheridan Press* on February 4 and 8, 2010. Copies of the *Amended Procedural Order* were also sent to customers who submitted comments or requests for hearing in this matter.

20. On January 20, 2010, the City filed, via facsimile, a *Petition for the City of Sheridan for Leave to Intervene Out-of-Time (Late-Filed Petition)* stating, *inter alia*, that it did not have adequate notice of MDU's application. The City requested that it be allowed to intervene out-of-time and respond to MDU's application, via pre-filed testimony. A signed hard copy of the *Late-Filed Petition* was filed on January 21, 2010. The City filed a *First Amended Petition of the City of Sheridan for Leave to Intervene Out-of-Time* via facsimile, on January 22, 2010, and a signed hard copy of the *First Amended Petition* on January 25, 2010. The *First Amended Petition* was signed by the City's counsel, Robert P. Warburton of Sheehan, Sheehan & Stelzner, P.A., a licensed Wyoming attorney.

21. On January 25, 2010, MDU filed the *Supplemental Testimony of Witnesses Rita A. Mulkern and Tamie A. Aberle*, in support of the amended application.

22. On January 27, 2010, MDU filed its *Objection of Montana-Dakota Utilities Co. To the Petition of City of Sheridan, Wyoming to Intervene (Objection)*. The City's *First Amended Petition* and MDU's *Objection* came before the Commission for consideration pursuant to due notice at its open meeting of January 27, 2010. Based on the arguments of the parties and its finding that the City had not shown good cause for the failure to timely request intervention, the Commission denied the City's intervention request by *Order Denying Intervention* issued on February 23, 2010. The Commission strongly encouraged City representatives to participate in this proceeding through the presentation of oral comments at the public hearings in this matter or by providing written comments as provided for in Commission Rule Section 103 (g).

23. On February 5, 2010, MDU filed its Electric Division Depreciation Study and its Common Plant Depreciation Study, both as of December 31, 2008, and depreciation testimony of Rita A. Mulkern.

24. On February 9, 2010, MDU filed the rebuttal testimony of Dr. J. Stephen Gaske, Rita A. Mulkern and Tamie A. Aberle.

25. On February 10, 2010, and pursuant to due public notice, a public comment hearing was held in Sheridan. MDU and OCA witnesses provided brief summaries of their

respective positions and members of the public were invited to offer comments. Numerous customers offered their comments during this public comment hearing.

26. Pursuant to the *Scheduling Conference Order* issued on November 5, 2009, the Commission held a pre-hearing conference on February 12, 2010, in the Commission's hearing room in Cheyenne, Wyoming. On that day, [i] OCA filed its *Updated Summary of Contentions, Designation of Exhibits and Summary of Remaining Issues*; and MDU also filed its *Scheduling Conference Memo For Montana-Dakota Utilities Co., A Division of MDU Resources Group, Inc.* The Commission issued a *Prehearing Conference Order* on February 19, 2010.

27. On February 16, 2010, MDU filed its *List of Exhibits and Summary of Contentions*.

28. On February 17, 2010, OCA filed its *Amended Designation of Exhibits*. Transcripts of the February 10, 2010, public comment hearing were also received in the Commission's office on February 17, 2010.

29. A public hearing in this matter was held on February 23-25, 2010, in Cheyenne. MDU and OCA appeared and participated in the hearing. MDU presented its case through six witnesses, David L. Goodin, Dr. John Stephen Gaske, Garrett Senger, Darcy Neigum, Rita Mulkern and Tamie Aberle. OCA presented its case through three witnesses, Denise Kay Parrish, Amy J. Zamora and Kimber Wichmann. Public comments were provided by MDU's customers.

30. On March 3, 2010, MDU filed its Late-Filed Exhibit Nos. 157 and 158. Exhibit No. 157 provides support for the Company's calculation of the allowance for funds used during construction (AFUDC) as of December 31, 2009, shown on MDU Exhibit No. 139. Exhibit No. 158 supports MDU's share of the Shared Assets, Ground Lease and Administrative Fee shown on MDU Exhibit No. 139.

31. On March 5, 2010, MDU filed the *Stipulation*, the affidavit of David L. Goodin, and the testimony of Rita A. Mulkern and Tamie A. Aberle in support of the *Stipulation*; and OCA filed Amy J. Zamora's testimony in support of the *Stipulation*. In the *Stipulation*, MDU and OCA agreed, *inter alia*, to an increase in the Company's Wyoming jurisdictional retail electric service revenues in the amount of \$3,253,726 per annum, effective for service rendered on and after May 1, 2010, with the increase to be phased in over a three-year period.

32. The Commission issued its second *Suspension Order* on March 9, 2010, suspending the Company's rate increase request for the final three-month period provided for in W.S. § 37-3-106(c). Also on this date, the Commission issued its *Procedural Notice and Order Reopening Record and Setting Additional Public Hearing*. It set an additional public hearing to commence on March 22, 2010, in Cheyenne. At this additional public hearing, the Commission expressed its intent to receive into the record [i] the *Stipulation*, [ii] the testimony and exhibits of MDU and OCA in support of the *Stipulation*, and [iii] further public comment. The *Procedural Order* was published on March 13 and 17, 2010, in the *Sheridan Press* and a public service announcement was aired five times on KROE-AM in Sheridan during the week of March 14-21,

2010.

33. On March 12, 2010, MDU filed its Late-Filed Exhibit No. 159 which provides the detailed class of service study and work papers underlying MDU Exhibit No. 130. On March 15, 2010, the OCA and MDU filed their *Joint Responses to Stipulation Data Requests*.

34. On March 16, 2010, OCA filed Exhibit AJZ-1 as referenced in the *Stipulation Testimony of Amy J. Zamora on Behalf of the Wyoming Office of Consumer Advocate*,

35. On March 16, 2010, transcripts of the hearings held on February 23-25, 2010, were received in the Commission's offices. Parties were notified on March 17, 2010, via electronic mail, that the transcripts were received and post hearing briefs were due on or before April 7, 2010.

36. On March 22, 2010, the Commission held an additional public hearing in Cheyenne, reopening the record for purposes of receiving the *Stipulation* and the testimony and exhibits of the parties in support thereof. MDU offered the testimony of its witnesses, Rita Mulkern and Tamie Aberle. OCA offered the testimony of Amy J. Zamora.

37. On April 7, 2010, MDU and OCA filed their *Combined Post-Hearing Brief*.

38. On April 8, 2010, transcripts of the hearing held March 22, 2010, were received in the Commission's offices. Parties were notified on April 8, 2010, via electronic mail, that public deliberations would be held on April 14, 2010, in the Commission's hearing room.

39. Pursuant to W.S. § 16-4-403, the Commission held public deliberations on April 14, 2010, rejecting the *Stipulation* and the rate increase reflected therein, approving *inter alia*, a general rate increase of \$2,651,565 per annum and directing the preparation of an *Order* consistent with its deliberations.

40. As directed by the Commission at deliberations, MDU submitted on April 23, 2010, its compliance tariff sheets consistent with the deliberations of the Commission. The tariff sheets were approved at the Commission's open meeting of April 27, 2010, to be effective for service rendered on and after May 1, 2010.

Findings of Fact: Party Positions

Summary of MDU's evidence

41. Mr. David Goodin, President and CEO of MDU, provided a summary of his prefiled testimony (MDU Exhibit No. 100) in support of the Company's amended application. He discussed the amended application and provided a policy statement and justification for MDU's rate increase request. Goodin testified that the requested general rate increase of \$5,053,746, or 25.1% in the Company's Wyoming electric rates is based on a 2008 test year adjusted for known and measurable changes. Goodin stated MDU was requesting a rate increase to recover its investment in Wygen III explaining the Plant secures a reliable supply source for a

portion of MDU's electric requirements. Goodin explained that the overall rate increase and revenue requirement will reflect customer class percentage rate changes as follows:

Class	Percentage Change
Residential Rates Schedules 10 and 18	21.2%
Small General Service	34.5%
Irrigation Service	21.2%
Large General Service	27.6%
Municipal; Lighting	14.0%
Overall Increase	25.1%

(Tr., pp. 140-141.)

42. Goodin stated MDU currently purchases its energy and capacity requirements through purchased power agreements (PPAs). MDU's current full requirements contract with Black Hills, which commenced on January 1, 2007, was filed in Docket No. 20004-65-EP-06 (Sub 65). This full requirements contract expires December 31, 2016, and contains an option for MDU to purchase up to 25 megawatts from Black Hills' Wygen III generating unit. Goodin stated that MDU exercised that option and purchased a 25% ownership interest in the Plant to serve its Wyoming electric service customers. MDU also filed an application for a Certificate of Public Convenience and Necessity (CPCN) in Docket No. 20004-72-EA-08 (Sub 72) for participation in Wygen III, which has an expected in service date of April 1, 2010. Goodin testified that, upon completion of the Plant, the Company's net rate base will increase by approximately \$62 million to reflect its 25% interest ownership together with the increased O&M expenses associated with the facility, offset in part by a net reduction in power purchase costs under the current full requirements contract with Black Hills. He stated that MDU's participation in the Plant will help protect its ratepayers from the volatile energy market by providing a cost-effective resource and bring diversity to the Company's resource mix by including Company-owned generation with power supply purchases, rather than being totally dependent on PPAs. He discussed how the electric resource modeling process used in the CPCN application took into account possible carbon legislation (cap and trade), carbon costs and pollution considerations. The Company's electric resource analysis demonstrated that a combination of Wygen III, demand side management (DSM) and supplemental purchased power would provide an adequate, reliable and economic electric supply. Goodin also discussed MDU's efforts to employ technological advances to streamline its business practices and its utility integration efforts to become more efficient and save money. He testified to the benefits and risks to the Company in owning a partial interest in the Plant. He also discussed how the Company's ownership and investment of monies increases the risk to ratepayers and the reasons the Company took on the increased risk as a result of its investment in Wygen III. (Tr. pp. 141-144, 150-151, 153-159; MDU Exhibit No. 100, pp. 10-12.)

43. Dr. John Stephen Gaske, Senior Vice President of Concentric Energy Advisors, provided a summary of his prefiled testimony including attached supporting exhibits. (MDU Exhibits 101-102.) Gaske's testimony addressed his analyses in support of his suggested cost of common equity capital of 12.75% for MDU's Wyoming electric utility operations. Gaske stated he calculated the cost of common equity capital based on Discounted Cash Flow (DCF) analyses of a proxy company group with risks similar to those of MDU's Wyoming electric operations.

He stated the purpose of the DCF analysis is to find the discount rate or the cost of capital that is implicit in the stock price of any given utility and reflects what investors expect to receive from their investment in the future. He stated the DCF analysis is a straightforward approach for estimating the cost of capital. Gaske testified he conducted two different DCF analyses: [i] a basic DCF analysis that relies on investment analysts' estimates for the growth rate; and [ii] a two-step growth rate estimation model that combines investment analysts' growth rates with forecasts of the earnings retention growth rates of companies. He also performed Risk Premium and Alternative Equity Investment analyses in establishing benchmarks for a reasonable rate of return. Gaske argued that the results of his DCF analyses must be adjusted by a flotation factor to account for issuance costs for new common equity capital. He used a flotation adjustment factor of 3.7% which he based upon the average cost of a representative sample of flotation costs incurred by electric companies for 81 new common stock issuances during the period 2000-2009. Gaske stated he used a group of 13 proxy companies that have similar risks to those of MDU's Wyoming electric utility operations. He discussed his belief that the OCA's proxy companies were less comparable to MDU than his proxy companies, stating it was more important to have companies as comparable as possible than it is to have a larger group of companies as proposed by OCA. Gaske discussed his 13 proxy companies stating, *inter alia*, he chose companies that [i] have at least 85% of their invested assets dedicated to electric utility operations; [ii] derive at least 25% of their generation from coal-fired plants; and [iii] have investment grade bond rating, [iv] paid dividends and [v] have published growth rate estimates provided by investment analysis services. He acknowledged that a true proxy company does not exist. (Tr., pp. 168-171, 175-176, 188-191; MDU Exhibit No. 101, pp. 3, 9, 16.)

44. Gaske testified that, in a DCF analysis, the dividend yield portion of the equation is simple to calculate but the future growth rate component is more difficult to estimate. His basic DCF analysis, which relied solely on investment analysts' forecasts for determining the growth rate component, resulted in a median cost of equity of 12.73%, an average cost of 12.91%, and a proposed return of 12.95%. Gaske testified that his two-step DCF growth rate estimation analysis, which ascribes two-thirds weight to investment analysts' forecasts and one-third weight to Value Line's retention growth rates for his proxy companies, resulted in a median cost of capital of 11.56% with an average for the group of 12.1% and a 12.62% return. He stated it was his opinion, given the slightly above average risk of MDU's Wyoming electric operations, that the required rate of return on common equity for MDU's Wyoming electric operations is approximately 12.75%. He discussed how the rate of return for MDU's Sheridan system affects the overall Company and he acknowledged that the 12.75% rate of return is higher than normal. Gaske explained that with the stock market down, investors require a higher rate of return because they perceive more risks in investments. Gaske stated the decrease in stock prices in the market increased his current DCF analysis results versus what the result would have been two years ago. (Tr., pp. 172-178, 186-187, 192-195.) He discussed the different risks faced by utilities and investors, the additional risk to a company of having coal-generated resources in its portfolio, and the differences in the risk associated with having an ownership interest in Wygen III and entering into PPAs. He stated that with PPAs more risk falls on the ratepayers and with an investment in its own plant, a company assumes more of the risk than would the ratepayers. (Tr., pp. 179-182, 188-191, 194-203, 206-212.)

45. During cross examination and in his rebuttal testimony (MDU Exhibit No. 135),

Gaske criticized OCA witness Kimber Wichmann's proxy company selection and screening criteria, to include what he termed her failure to limit her proxy group to coal-fired generation assets, and her exclusion of companies with bond ratings above MDU's, while including companies with bond ratings below MDU, and her use of comparable companies with electric operating revenue of 70% or more, whereas his threshold was 85% of electric revenues. Further, he disagreed with her application of the constant growth and two-stage DCF models, her use of the Capital Asset Pricing Model as a method of estimating the cost of common equity capital, and her use of a partial flotation cost adjustment. (Tr., pp. 179-186; MDU Exhibit No. 135, pp. 4-5, 29-39, 53-54.)

46. Gaske also offered a summary of his rebuttal testimony (MDU Exhibit No. 135) responding to OCA witness Denise Parrish's proposal to levelize the cost of the returns on Wygen III over the OCA's recommended expected 50-year depreciable life of the Plant, in contrast to traditional ratemaking wherein the return is earned on the net value of the Company's rate base each year. He stated the OCA's proposal would deny MDU an opportunity to earn a fair return on its investment in Wygen III. He stated, under OCA's proposal, common equity investors would be allowed to only earn a 3.20% return on Wygen III during the first year as compared to the higher returns on equity (ROE) he and Wichmann propose. He argued that ratepayers would be denied the opportunity to earn a fair rate of return on the Wygen III investment until twenty years in the future. He stated that OCA's proposal does not provide: [i] a rate of return sufficient to assure the financial integrity of the Company, [ii] sufficient revenue to cover the financial costs of the utility, or [iii] a return comparable to similar investments of like risk. He stated OCA's proposal deprives common equity investors of approximately \$8.7 million in present value dollars that would otherwise be available to them under a normal rate of return on rate base calculation. Regarding levelization and cash flow, Gaske stated Parrish did not look at what effect levelization would have on the equity holders; she only looked at the overall rate of return. Gaske stated his calculation illustrated that levelization would cover the debt service but would substantially cut the equity return. (Tr., pp. 719-720, 729-731; MDU Exhibit No. 135, pp. 2-3, 6-8, 12.)

47. Gaske stated that Parrish's levelized proposal incorrectly assumes investors will be reimbursed for the cost of their capital 50 years from now. Gaske stated that, during the proposed 50-year levelization period, much of the equipment will be replaced or refurbished because the levelization period exceeds the life of many of the assets. Further, the overall rate of return of 8.45% utilized in her levelization proposal is too low in comparison to the Company's proposed overall rate of return. He stated Parrish failed to recognize that interest on the debt must be paid before the equity investors receive any return. He stated that, under the OCA's proposal, most of the overall return dollars available in the early years will be paid as interest to the debt holder and more equity returns will be pushed out to the later years and will not provide full compensation for the time value of their deferred investment. Gaske stated that, for the equity holders to actually stay whole under Parrish's levelized overall rate of return of 8.45%, the bondholders would have to agree to defer their receipt of interest. He discussed further complications that would need to be considered when considering a levelized approach. (Tr., pp. 719-720, 737-742; MDU Exhibit No. 135, pp. 4.)

48. Gaske noted Parrish's proposal does not recognize or account for the significant

increase in business and regulatory risks that would be caused by OCA's recommendations. He stated that the Company's auditor advised him that OCA's proposal would not qualify for SFAS 71 treatment in the recording of a regulatory asset. He stated MDU's auditor advised him that you can defer an expense item but you cannot record deferrals for revenue items. (Tr., pp. 732-734.)

49. Mr. Darcy Neigum, MDU Systems Operations and Planning Manager, [i] provided a summary of his prefiled testimony (MDU Exhibit No. 103) which offered an overview of Wygen III, [ii] discussed the Company's March 2008 Integrated Resource Plan (IRP) filed as part of its CPCN application in the Sub 72 proceeding, and [iii] described how Wygen III worked in conjunction with the current Black Hills' PPAs. He stated the Plant was expected to be fully commercial and operational on or around April 1, 2010. He discussed the three main areas the IRP encompassed: [i] a load forecasting update; [ii] a Demand Side Management update; and, [iii] a supply-side update which included a market analysis of the estimated energy market. Neigum also discussed MDU's long-term coal supply agreement with Wyodak Resources for Wygen III, its terms and how the coal would be transported from the Wyodak Mine to Wygen III. He discussed the benefits of the Plant, stating they occur over the long term and include, *inter alia*, protection for Wyoming rate payers from wholesale market volatility. He stated participation in Wygen III provides MDU with ownership of a stable and cost-effective resource, brings diversity to its resource mix, and provides a more stable power supply to the customers' benefit. Neigum testified that, in conjunction with MDU's 25% ownership in Wygen III, the Company executed an amendment to its full requirements PPA with Black Hills to service its Sheridan load. The amended PPA runs through December 16, 2016. He stated MDU will be required to use its ownership share of the Wygen III output or rely on replacement power to serve the Sheridan load. Neigum further explained that, following the commercial operation of Wygen III, the PPA will supply all needed resources above those provided by the Company's share of the Plant up to 74 MW. (Tr., pp. 219-224, 226-228, 241, 266-268, 278-280.)

50. Neigum discussed differences in Wygen III construction costs (and the reasons therefor) between those presented in the Sub 72 certification proceeding and those presented in this matter. He testified that MDU's current updated estimate for the total project cost, with the projected AFUDC and remaining capital expenditures for 2010, is \$63,354,500 as of December 31, 2009. (MDU Exhibit No. 139.) He discussed the changes to O&M expenses, and administrative and general expenses (A&G) associated with Wygen III as estimated in Sub 72 and as presented in this case, stating the O&M costs in this case are based on Wygen II costs. Neigum also discussed MDU's ability to oversee the ongoing Wygen III O&M and A&G expenses. He discussed the administrative costs Black Hills charges the Company stating there were two types of costs: [i] directly assigned costs, and [ii] administrative costs. He further stated coal prices related to fuel costs for Wygen III had also decreased from the last update and were projected at \$11.70 per ton for the year 2010. Neigum also testified he believed a 40-year depreciable life for Wygen III was reasonable. He noted that the coal supply agreement for Wygen III is for 50 years. He stated it was hard to predict how long a plant could operate given the technologies used to build it and how it has been run. Neigum noted that MDU has several coal resources that have operated for 50 years. Finally, Neigum described the costs kVARs impose on the Company's system. (Tr., pp. 226-239, 245, 253-255, 263, 280-283; MDU Exhibit

No. 103, pp. 8-9.)

51. Mr. Garrett Senger, MDU's Vice President-Controller and Chief Accounting Officer, provided a summary of his prefiled direct testimony (MDU Exhibit No. 104), in support of the Company's calculation of the overall cost of capital, capital structure, debt and preferred equity cost. He also discussed Statements A, B and F, attached to the Application. (MDU Exhibits 105, 106 and 107.) Statement A is the balance sheet for MDU as of December 31 for the calendar years ended 2007 and 2008, and accompanying notes to the financial statements. Statement B reports the income statement for the 12 months ended December 31, 2008, and March 31, 2009. Statement F shows the utility's capital structure at December 31, 2008, and a pro forma capital structure for 2009, as well as the associated costs of debt, preferred stock, and Gaske's proposed common equity cost. Senger testified that the pro forma capital structure and the associated costs serve as the basis for the overall requested rate of return of 9.62%, which is comprised of:

Component	Percentage	Cost	Weighted cost
Long-term Debt	44.959%	6.793%	3.054%
Average Short-term Debt	2.771%	3.773%	0.105%
Preferred Stock	2.5%	4.594%	0.115%
Common Equity	49.77%	12.75%	6.346%
TOTAL	100.00%		9.62%

He also discussed the pro forma capital structure and the differences between the pro forma and the per books capital structures as of December 31, 2008. (Tr., pp. 287-291.)

52. Senger also addressed the Company's calculation of the AFUDC related to Wygen III, stating it was calculated pursuant to the prescribed FERC Uniform System of Accounts formula which is comprised of two components: [i] borrowed funds used during construction and, [ii] other funds used during construction comprised of debt and equity. He stated that MDU applies AFUDC to construction projects that are greater than 60 days in length. Senger also discussed how the AFUDC was calculated for 2010, stating the AFUDC will be accrued until the Plant is in service. He referenced MDU Exhibit No. 139 which showed AFUDC in the amount of \$1.8 million for 2010. (Tr., pp. 457-462.)

53. Ms. Rita A. Mulkern, MDU's Regulatory Analysis Manager, provided a summary of her prefiled direct and supplemental testimony, including attached supporting exhibits. (MDU Exhibits No. 108 and 126.) Mulkern's testimony addressed [i] the Company's revenue requirement and per books cost of service for the 12 months ending December 31, 2008, [ii] the pro forma cost of service reflecting known and measurable adjustments that would occur by December 31, 2009, including the Company's 25 MW investment in Wygen III, and [iii] the calculation of MDU's revenue deficiency. She also sponsored Statements C-E and G-L. (MDU Exhibits 109-117.) She noted the pro forma cost of service is summarized in Statement L with the supporting detail contained in Statements C-K. Statement L shows the calculation of the revenue deficiency based on the overall rate of return of 9.62% from Statement F, page 1, as supported by Gaske and Senger. She stated the pro forma adjustments to the income statement, Adjustments 1-31, pertain to revenue, expense items and rate base, with Adjustments A-K

pertaining to rate base items. Adjustments relating to Wygen III included: an accumulated reserve for depreciation, accumulated deferred income taxes, fuel and purchased power, O&M, depreciation expense, and other taxes, including income taxes, that are listed separately in the statements. (MDU Exhibit No. 108, pp. 4-14.) Mulkern's testimony also addressed the Company's current power supply cost adjustment (PSCA) tariff given MDU's ownership of Wygen III for a portion of its electric requirements. She stated that MDU's PSCA tariff is an annual adjustment that specifies the procedure to use to adjust rates for fuel and purchased power and amortization of the power supply balancing account. Mulkern stated that, with the addition of Wygen III into MDU's power supply mix, the Company will still be purchasing capacity and energy from Black Hills pursuant to its PPA. The capacity and energy available from Wygen III will displace a portion of the energy and capacity from the Black Hills PPA. She stated MDU would also incur fuel expense for the coal supply required for its portion of Wygen III. Mulkern testified the current PSCA tariff language provides for the inclusion of fuel, purchased energy and capacity and any ancillary services. Mulkern expressed her belief that the addition of Wygen III could be accommodated within the existing tariff language and no changes to the tariff are needed. Mulkern noted the Company was proposing to change the calculation of the PSCA to accommodate the differences in customer class allocations and to clarify the language on the calculation of the PSCA. Mulkern testified that MDU was also proposing to add language to provide the detail of the calculation used to determine the monthly over- or under-recovered amounts placed in the balancing account. (Tr., pp. 294-296; MDU Exhibit No. 108, pp. 15-18.)

54. Mulkern also summarized her supplemental testimony revising MDU's revenue requirement to reflect its proposed bonus tax depreciation adjustment. She testified an accelerated/bonus depreciation deduction was available for federal income tax purposes for certain 2009 qualifying property additions. She stated the deduction was created in February 2008 as part of the Economic Stimulus Act of 2008 which allows for an accelerated tax deduction equal to 50% of the cost of new qualifying property purchased and placed in service in 2008. The bonus depreciation provisions were extended in 2009 under the American Recovery and Reinvestment Act to new qualifying assets acquired and placed in service in 2009. She explained the bonus depreciation accelerates the amount of tax depreciation available thereby affecting current income taxes, deferred income taxes and accumulated deferred income taxes found in rate base. She stated that it does not affect the value of Wygen III or any of its associated expenses. Mulkern testified the revised additional revenue requirement, taking into account the bonus depreciation adjustment, is \$5,053,903 or \$1,144,369 less than the initial requested amount. (Tr., p. 298.) Mulkern testified that at the time MDU filed this rate case, it was not certain if its investment in Wygen III would qualify for the bonus depreciation. However, after research and review of the requirements, Mulkern stated the Company now believes it satisfies the requirements; and the 2009 expenditures for Wygen III should be eligible for the bonus tax depreciation. She stated the Company intends to take the bonus depreciation in its 2009 taxes. If MDU is not eligible for the bonus depreciation, the IRS will review the Company's taxes and advise it that it is not eligible. Mulkern stated an IRS review will not take place for three or four years but the Company stands by its determination to take the bonus depreciation. (Tr., pp. 297-300, MDU Exhibit No. 126, pp. 3-4.)

55. Mulkern also addressed the Company's February 5, 2010, filing of an electric division Depreciation Study and Common Plant Depreciation Study, both as of December 31,

2008. The studies set forth the new depreciation rates for electric and common plant. They were filed in compliance with the Commission's *Order* in the Company's last general rate case (Docket No. 20004-75-ER-08 (Sub 75)) which directed the Company to file a depreciation study with its next rate case. She testified the effect of the proposed revised depreciation rates results in a decrease in the overall revenue requirement of \$220,358 from the January 14, 2010, amended filing, resulting in a decrease in the Company's proposed revised revenue increase of \$5,053,903 to \$4,833,545. (Tr., p. 298; MDU Exhibit No. 142, pp. 2-3.)

56. Mulkern testified on rebuttal and in cross-examination on her adjustment seeking recovery of \$1,683 for institutional advertising expenses from customers rather than shareholders, arguing it was appropriate because customers benefit from this form of advertising. She noted the Company serves small communities in which it is important for MDU to be involved and to demonstrate its support, all of which benefits its customers. She disagreed with OCA's proposed disallowance of this expense, stating it should be recoverable, and the Commission has the authority to consider recovery on a case by case basis. She also addressed the general inflation adjustment and the reasons MDU applied it to various expense categories. She stated the inflation adjustment is applied to smaller dollar amounts and is an aggregate adjustment to expenses using the Consumer Price Index (CPI) as the inflation factor. The CPI used by the Company is a three-year historical average. Regarding the Company's depreciation expense adjustment, she stated the Company used an annual depreciation expense on the plant additions but utilized a six month period in developing the deferred taxes, including tax depreciation, associated deferred taxes and the rate base deduction for accumulated deferred income taxes. Mulkern testified that MDU used six months of depreciation expense for plant additions because they come into service throughout the year. (Tr., pp. 301-306, 743, 753.)

57. Mulkern explained why MDU's proposed three-year amortization period for regulatory commission expense was reasonable, stating three years allows time to recover the cost from customers before the time the company may need to file another rate case. She stated this time frame will help avoid the situation where customers are paying the expenses associated with the current case and the cost of a previous case. Mulkern argued that, should rate case expenses be extended beyond the three years proposed by the Company, it would be appropriate to include the unamortized rate case expense balance in rate base to compensate the Company for the time value of money in delaying recovery of its expenses incurred in 2009. Mulkern also addressed the tariff changes MDU was proposing for its PSCA. (Appendix B to the amended application.) She stated that, under the PSCA Rate 50 tariff, the Company proposes to have three separate classes; it currently has one class applicable to all its customers. The three classes would be: [i] Primary Service for customers taking service under Rates 20 and 39; [ii] Secondary Service for customers taking service under Rates 10, 20, 24, 25 and 39; and [iii] Controlled Rates 11 and 22. MDU proposed to establish a base cost of fuel and purchased power for each of these classes in a general rate case. Then, as part of its monthly accounting, MDU would calculate the over-or-under recovery for each class separately. (Tr., pp. 312-316, 743.)

58. On rebuttal, (MDU Exhibits No. 138 and 139), Mulkern addressed certain adjustments proposed by OCA witness Zamora. She stated MDU objected to Zamora removing the \$3,499 expense relating to transmission expenses. She stated that Zamora eliminated this expense as it related to a one-time occurrence. Mulkern stated that this particular activity might

be non-recurring as reflected in the transmission account, but she explained that it is not a non-recurring expense and that the expense itself, or the dollars associated with it, were not incremental. Mulkern disagreed with OCA's calculation of tax depreciation on plant additions because Zamora used a full year of book depreciation in her calculation rather than the half year used by MDU. Mulkern stated, when calculating book depreciation in the calculation of tax depreciation, the book depreciation portion is based on the actual depreciation expense on those plant additions and is neither a normalized expense nor a theoretical depreciation expense. Regarding the calculation of investment in the Plant, she stated that an update of this investment cost had been provided (MDU Exhibit No. 139), with updated amounts for coal expense and O&M expenses (MDU Exhibits 155 and 156) which are more current than the amounts utilized by OCA. She stated the Company agreed that these most recent updates should be utilized and would match the update of the Wygen III Plant value included in her Rebuttal Testimony. (Tr., pp. 743-748, 760-762.)

59. In opposition to OCA's proposed revisions to the PSCA, Mulkern testified she believed the current tariff language conforms to Commission Rules 249 and 250. She stated that the language in Rules 249 and 250 does not preclude recovery of fuel associated with a generation unit and they do not address what is prohibited. Regarding the use of a dead band, Mulkern stated the Company did not agree with Zamora's recommendation to use a base fuel cost with a dead band and a sharing over/under the dead band. She explained that the components of MDU's PSCA include a contract that was filed with and approved by FERC and this Commission, which contains an escalation factor. She stated it was not appropriate at this time to determine whether the escalation factor is recoverable. The PSCA also includes a transmission component, which is a FERC-regulated tariff with a regulated rate. She stated it was not appropriate to establish a dead band that would preclude recovery of that amount. Mulkern further stated the coal contract (Statement R) includes a price for coal that is not negotiated but is a rate filed with and approved by the South Dakota Commission. Mulkern stated that, because the PSCA contains rates that are established or regulated, it would not be appropriate to establish a dead band that would preclude recovery of the costs. (Tr., pp. 748-754.)

60. Tamie A. Aberle, MDU's Pricing and Tariff Manager, provided a summary of her prefiled testimony and attached exhibits (MDU Exhibits No. 108, 119-125, 130-134), in support of the Company's rate design and the embedded class cost of service study. She discussed the results of the class cost of service study and the proposed design of rates to recover the revenue requirement calculated by Mulkern in her direct and supplemental testimony. Aberle stated the cost allocations in the study are based on cost causation with direct assignments made where possible, with remaining costs being allocated primarily on customer-related, demand-related and energy-related factors, depending on the nature of the cost. She said the class cost of service study is consistent with studies MDU has performed in the past. She stated her proposed rates are intended to recover additional revenues in the amount of \$5,053,756 per annum, as proposed in the Company's amended application. She testified the results of the class cost of service study indicated that the classes are providing returns on the investment necessary to provide service to each of the rate classes. However, every rate schedule is producing a pro forma return below the overall rate of return. MDU is proposing to increase each rate class in an amount necessary to bring each of these classes' revenue responsibility up to the overall rate of return, with the

exception of the private lighting class, which the Company proposes not to change. MDU proposes to allocate the \$15,264 decrease in revenues which would otherwise accrue to this class to all other classes. (Tr., pp. 324-325; MDU Exhibit No. 118, pp. 4-10.)

61. Aberle further stated that, in addition to the rate of return by class, the embedded cost of service study (MDU Exhibit No. No. 130) provided the cost for customer demand and energy-related costs for all classes. She stated the increase in the customer component proposed in this case moves rates toward or to embedded costs as directed by the Commission in the last rate case proceeding. Demand charges for service under the Small General and Large General Service schedules are being adjusted to reflect movement towards recovery of costs as identified in the class cost of service study. The energy rate for each schedule reflects the residual of the revenues required to be collected from each rate schedule after deducting the revenues proposed to be collected from base rates and demand charges. She stated MDU has not proposed any change in rate classes or rate designs in this case. Aberle stated that although the Company filed an inverted block residential rate design as directed by the Commission in its last rate case, the Company prefers to maintain its current rate structure of a monthly base rate and a flat energy charge. However, she stated she would not be averse to implementing an inverted block rate design provided the base rate is set at a minimum level of \$25.00 per month. She stated that, unless the Commission adopts the Company's proposed revenue increase proposal, the Company will have to run its cost of service model and its rate design proposals again to determine the appropriate rates for each rate schedule. (Tr., pp. 325-326, 777; MDU Exhibit No. 118, pp. 11-17.)

62. Aberle's direct testimony and exhibits addressed the Company's Irrigation Service – Rate 25, proposal. She stated the rate design retains a base rate and time differentiated demand charge as adopted in the last rate case. The Company is proposing to recover the revenue increase allocated to this rate class by increasing the base rate from \$25.00 to \$50.00 per month; with no change in the on-peak demand charge of \$9.50 per kW or the off-peak demand charge of \$3.00 per kW. The remainder of the increase would be recovered through the energy charge. MDU proposed to continue the current peak period of Noon to 8:00 p.m.. (MDU Exhibit No. 118, pp. 15-16.) On cross-examination, Aberle stated that Irrigators who operate on a 24 hour/seven day schedule contribute to the peak because they are poor load factor customers who typically operate four to five months a year. She also discussed the effects of having a shorter peak demand period, stating a shorter peak period would only move the peak to the next hour. She noted the majority of irrigator kWh were billed off peak with approximately 54% of the kWhs billed off peak and 46% of the kWhs billed on peak. She discussed the demand charge for the Irrigation customers, how it works, and the Company's efforts to work with customers to establish an alternative to the mandatory time-of-day schedule to help customers move off peak. She also described the Company's alternative irrigation rate proposal that she offered in her rebuttal testimony (MDU Exhibit No. 140), which included an optional time-of-day irrigation schedule that would provide an incentive to irrigation customers to move load off-peak, in addition to the standard schedule that includes a non-time differentiated flat demand charge. The standard irrigation rate would include a demand charge of \$6.25 for the monthly peak demand regardless of the time the peak demand is established. The optional time-of-day schedule would include the current on-peak charge of \$9.50 per kW and the off-peak charge of \$3.00 per kW. She assured the Commission that an irrigation customer taking service during the on-peak period

and off-peak period and would not pay a rate of \$12.50 per kW but would be billed for each period separately at the applicable \$9.50 or \$3.00 per kW rate. (Tr., pp. 329, 354, 360, 362-365, 770; MDU Exhibit No. 140, p. 4.) However, an irrigator taking energy during both on-peak and off-peak hours would pay both demand charges, or a total of \$12.50 per kW for all hours during the month. (Tr., pp. 385-387.)

63. Aberle also addressed MDU's inclusion in its revenue requirement of approximately \$55,000 a year for kVar penalties. Aberle stated the Company believes that a \$2.50 per kVar penalty [i] provides an incentive to customers to make a change to their equipment to avoid supplying kVars to the system; [ii] is sufficient to cover the identified potential impacts to the system; and [iii] will provide a revenue stream to cover capacitors and the losses and the other costs associated with kVars being introduced into the system. (Tr., pp. 345-347, 374.)

64. In her rebuttal testimony, Aberle offered an alternative to Zamora's recommendation to use separate demand and energy rates for purchased power and fuel recovered under a tracking mechanism in the PSCA. MDU Exhibit No. No. 141 illustrated her alternative proposal that the demand costs associated with the PSCA be moved to the cost of service component of each rate with only the prospective changes in demand under the contract being billed through an energy charge in the PSCA. Aberle suggested the demand component included in the purchased power agreement is relatively stable; and therefore, prospective changes in demand-related costs under the PSCA mechanism should be minimal. (Tr., pp. 778-783; MDU Exhibit No. 140, pp. 4-5.)

65. Aberle's rebuttal testimony addressed certain rate design-related proposals made by OCA witness Zamora. (MDU Exhibit No. 140.) She discussed Zamora's proposal to introduce a \$4.00 per kW charge for the first ten kW billed under the Small General Service Rate 20, Secondary Service, and a \$4.50 per kW for the first ten kW billed under Small General Service, Primary Rate 20, schedule. She stated these changes would result in a significant change to a large group of very small use customers taking service under Small General Service Rate 20. The current rate design for the Rate 20 Class provides the first ten kW at no charge with a demand charge being imposed on all kW over ten kW. She stated OCA's proposal would require the purchase and installation of approximately 17,000 demand meters at a cost of approximately \$484,500. She recommended the current rate structure be maintained. (Tr., p. 764, MDU Exhibit No. 140, p. 3.)

Summary of OCA's Evidence

66. Ms. Kimber Wichmann, Rate Analyst for the OCA, provided a summary of her prefiled direct testimony, including attached supporting exhibits, which addressed OCA's position on the appropriate ROE, cost of debt, and capital structure that should be used in the computation of MDU's overall rate of return. (OCA Exhibits 201-208.) Wichmann testified her analyses supported a ROE for MDU's Wyoming electric utility operations of 10.4%, resulting in an overall rate of return for the Company of 8.45%. In performing her analyses, she identified a group of twenty-two proxy companies from publicly available financial data which were comparable to MDU's regulated electric utility operations. She stated the filters used in

selecting her comparable companies were that they should have [i] a Baa rating as MDU's issuer rating was Baal, [ii] at least 70% of revenues from regulated electric operations, and [iii] had to pay dividends in 2009. All but one of Gaske's 13 comparable companies were included in her group of comparable companies. Wichmann stated she utilized a constant growth rate DCF model, a non-constant growth DCF model and a capital asset pricing model (CAPM) in conducting her ROE analyses. She stated the two DCF models provide an estimate of cost of equity capital by examining expected dividends and market prices, but the non-constant growth DCF analysis provides a more realistic estimate of future growth. She stated that she used the CAPM not as a primary model but as an objective measure of risk for regulated electric utilities with the same investment as MDU, in comparison to other securities available to investors. (Tr., pp. 473-475, 483,507-510; OCA Exhibit No. 201, pp. 6-8.)

67. Wichmann testified she and Gaske used similar information sources in performing their respective analyses and in their selection of comparable companies but differed in their application of the information, including their calculation of flotation costs and size adjustments. She stated that, although she supported a flotation cost adjustment, she utilized a conventional flotation cost calculation, which assumes that flotation costs are incurred only when new stock is sold and not when earnings are retained. Under the conventional calculation the flotation adjustment is applied only to the dividend yield of the DCF calculation and not to the growth component. She stated her use of MDU's actual flotation factor of 3.50%, which was lower than an industry average of 3.70% used by Gaske, was appropriate as it was a known factor, and customers should only have to pay the actual cost. As to utilizing a size adjustment as advocated by Gaske, she rejected such an adjustment on the basis that MDU's utility operations do not share the same risk as a small business in a free market, given MDU's status as a regulated monopoly with certain mechanisms such as the PSCA tariff which mitigates the risk of cost recovery. Wichmann identified other areas of disagreement with Gaske's ROE analyses, including his averaging of stock prices in his DCF models, his use of an "unconventional" growth adjustment in his DCF analysis, resulting in an overestimated cost of capital, and the results of his Risk Premium analysis, which fail to support or legitimize the results of his DCF analyses. (Tr., pp. 475-476, 517; OCA Exhibit No. 201, pp. 14-15, 31-34.)

68. Wichmann concluded that her ROE analyses supported a range of reasonableness of 9.05% to 10.93%, with a midpoint of 9.9%. After considering the macroeconomic environment, financial and business risks, growth forecasts and MDU's ability to recover many of its costs through regulatory and tariff provisions she recommended a conservative ROE of 10.4% as providing a reasonable balancing of shareholder's interests with the customer's interests, although she acknowledged that any ROE number falling within her range would be supported by her analysis. Using the Company's pro forma capital structure for 2009, its calculated costs of long-term debt (6.79%), short-term debt (3.77%), preferred stock (4.59%), and OCA's recommended cost of common equity (10.4%), Wichmann recommended an overall rate of return of 8.45%:

Component	Percentage	Cost	Weighted cost
long-term debt	44.959%	6.79%	3.05%
average short-term debt	2.771%	3.77%	0.104%
preferred stock	2.5%	4.59%	0.115%

common equity	49.77%	10.4%	5.18%
TOTAL	100.00%		8.45%

(Tr., pp. 475-477, 521-522; OCA Exhibit No. 201, pp. 23-29, 36; OCA Exhibit No. 208.)

69. Ms. Denise Kay Parrish, OCA's Deputy Administrator, provided a summary of her prefiled direct testimony, including attached supporting exhibits (OCA Exhibits 216-218), in support of OCA's proposal to levelize the cost of the return on MDU's 25% ownership interest in the Wygen III generation Plant over the expected depreciable life of the Plant. Parrish stated the concept behind her levelization proposal was to assure that all generations of MDU's Wyoming electric customers benefiting from the Wygen III Plant pay their proportional share of the return MDU is entitled to earn on its share of the Plant. Through this levelization approach, the impact of adding the Wygen III Plant to rate base would be lessened during the initial years the rates are in effect. Levelization would address generational inequities existing today under more traditional methods of front-loaded return on new plant placed in rate base, wherein early generation customers benefiting from the plant pay more return than later generation customers. She stated the total value that MDU would earn over the depreciable life of the Plant is summed; with the total value being divided by the expected Plant life to arrive at an equal dollar amount of return to be recovered from customers during each year of the Plant's operating life. She stated her proposal in addition to not disadvantaging generations of customers is also intended to not disadvantage investors over the life of the Plant by making sure they receive the same amount of return over the life of the Plant by using present value calculations. (Tr., pp. 622-623; OCA Exhibit No. 216, pp. 3-4, 8.)

70. Parrish described the calculation of her levelization proposal (OCA Exhibits 217 and 218), stating she developed a rate base for the Plant based on the 50-year depreciable life that OCA was recommending for Wygen III; but she acknowledged she had not updated her gross Plant numbers as brought up to date by MDU. Based on her calculations, the Company, on behalf of its investors, would have to receive \$2.8 million each year for fifty years. Parrish stated that, for purposes of her calculation, she assumed that investors should have the opportunity to receive the same total present value amount that they would receive under current regulatory practices. She testified that, over the 50-year life cycle of the Plant, investors would receive the same dollar value in return that they would receive over the life of the Plant using the more traditional front-loaded method. Her analysis further showed the total amount of return collected by MDU would be approximately \$55 million more under her levelized approach as compared to the amount that would need to be collected using a nominal levelized return. She justified this result as being fair because customers will be deferring some of the higher payments to a later time period when the funds they pay will have a lesser value than if they were paying the higher and more traditional cost today. She stated her levelized approach assumes the Company would continue to receive the \$2.8 million over the life of the Plant, without modification, even if there were subsequent rate case filings submitted over the course of the 50-year period. (Tr., pp. 624-631; OCA Exhibit No. 216, pp. 8-20.)

71. In Gaske's rebuttal, he argued that her levelization proposal requires future commissions to be bound by the determinations of this Commission regarding this issue over the 50-year period. Parrish responded, acknowledging that, although one commission cannot bind

future commissions, it was her experience that this Commission and prior commissions have been reasonable and have not backed out of prior commitments. She further expressed her disagreement with Gaske's argument that recording the deferral as a regulatory asset would only be acceptable if MDU's customers entered into a 50-year contract to ensure the Company's recovery of its Wygen III investment. Parrish testified that, although her levelization approach would affect cash flow streams for the Company differently than more traditional approaches, because levelization would result in less cash being collected during the earlier years with more cash becoming available in later years, she believed OCA's approach did not violate the standards set out in the *Hope* and *Bluefield* cases, as was argued by Gaske, because the levelization proposal provides OCA's recommended overall rate of return of 8.45% over the life of the Plant. She stated the *Hope* and *Bluefield* cases do not require that regulatory commissions provide specific cash flow streams on a specific schedule. Finally, Parrish stated that, although she did not believe OCA's proposal created more risk for MDU, she provided several options for consideration to mitigate the regulatory risk that might be attributed to the adoption of her levelization proposal. (Tr., pp. 631-635, 637; OCA Exhibit No. 216, pp. 21-24.)

72. Parrish expressed OCA's concerns over possible Commission approval of MDU's latest depreciation studies, which were filed very shortly before the commencement of the hearings in this matter, stating that OCA had only a limited opportunity to review the studies and had many unanswered questions, including: [i] the need to review the Company's rationale for significant differences between present and proposed depreciation rates for various accounts; [ii] issues regarding interim retirement rates; and [iii] other aspects of the depreciation studies that require further review. She recommended the depreciation studies be considered in more detail in a separate docket or in the next rate case. Parrish testified it was reasonable to accept MDU's depreciation adjustment as identified in Mulkern's depreciation testimony (MDU Exhibit No. 142, pp. 2-3), which results in decreasing the Company's revenue increase request by \$220,358. (Tr., pp. 639-646, 679-680.)

73. Ms. Amy Zamora, Senior Rate Analyst for the OCA, provided a summary of her prefiled direct testimony, including attached supporting exhibits. (OCA Exhibits 209-215.) Zamora's testimony provided background for the Company's application, including its entry into a new all requirements purchased power contract with Black Hills Power in 2006, which provided MDU with the option, which it exercised, to purchase 25% of Wygen III. She stated MDU will be obligated to pay 25% of the investment cost of the Plant, O&M costs, the costs associated with 25% of the coal needed to fuel the Plant, and certain administrative expenses to Black Hills Power as the Plant operator. Zamora also addressed her review of the Company's revenue requirement, the class cost of service study and rate design, which were incorporated in the OCA revenue requirement recommendation, proposed rate spread and proposed rate design. Zamora stated she reviewed the per books amounts contained in the Company 2008 test year and the Company's pro forma adjustments, whereupon she made her own adjustments to the Company's results to normalize and annualize the test year numbers to remove prior period expenses, one-time expenses, expenses that did not need to be incurred in providing utility service, and expenses that were not known and measureable. She further stated that she separated her adjustments between non-Wygen III-related expenses and Plant, and only Wygen III-related expenses and Plant. Her separation of Wygen III-related expenses and investment

costs from the rest of the revenue requirement was done to accommodate Parrish's proposed levelized return proposal for the Wygen III Plant. (Tr., p. 528; OCA Exhibit No. 209, pp. 3-6.)

74. OCA Exhibit No. 211 sets forth OCA's non-Wygen III-related adjustments to revenues, purchased power and fuel costs, O&M expenses, depreciation expense, Taxes Other Than Income, deferred income taxes and current income taxes. Zamora's revenue adjustment was comprised of an MDU-provided correction to the pro forma usage and revenue calculations for Large General Service Class Rate 39, which increases pro-forma revenues by \$18,726. In all, OCA made six adjustments to O&M expenses, including increasing the purchased power expense by \$18,714, to reflect the correction in the Rate 39 usage calculation, and increasing expenses by \$6,782,183 to remove the MDU calculated Wygen III-related purchased power and fuel costs, for a net expense increase adjustment of \$6,801,897. She stated the changes are included in the Wygen III-related adjustments. An adjustment was made to remove Wygen III-related O&M expenses of \$2,681,907, which would be included in the Wygen III adjustments. Zamora made an additional adjustment to remove institutional advertising and industry dues expenses of \$2,413 on the basis these expenses need not be incurred in providing service. Zamora supported her adjustment by stating institutional advertising should be shareholder funded. Recovery of these expenses has been denied by the Commission in past cases, and are here precluded from rate recovery under OCA's interpretation of Commission Rule Section 248. OCA proposed to amortize regulatory commission (rate case) expense over a ten year period to reflect the historical length of time between past Company general rate filings, as opposed to the three years proposed by the Company. OCA also proposed an O&M expense reduction of \$6,551 to remove MDU's general inflation adjustment for other miscellaneous expense items. Zamora testified that adjusting these other expenses by a blanket percentage, based upon the consumer price index, is not a known and measurable adjustment, and has been disallowed by the Commission in cases involving other utilities. Finally, OCA removed certain one-time expenses occurring in the test period, prior period adjustments, and costs recovered through the Company's Load Management Program resulting, after a correction to OCA's computations, in an O&M expense reduction of \$30,994. (Tr., pp. 528-532, 561, 584-585, 589; OCA Exhibit No. 209, pp. 6-8.)

75. Zamora discussed her removal of MDU's calculation of Wygen III-related depreciation expense of \$1,744,988, saying it would be offset by inclusion in her Wygen III adjustments. Regarding the Company's filing of its most recent depreciation studies that had the effect of reducing depreciation expense, she stated OCA accepted the adjustment in this case but requested additional time to allow a more thorough review of the studies and the proposed depreciation rates in the context of a future proceeding. Regarding her adjustments for Taxes Other Than Income Taxes, she annualized franchise and gross revenue taxes by applying OCA's adjusted revenues to the appropriate tax factors, and removed MDU's pro forma ad valorem taxes related to Wygen III stating they would be added in later as part of her Wygen III adjustments, for a net decrease of \$100,327. Zamora also proposed an annualized adjustment to deferred income taxes for all other plant by using a full year of book depreciation for all assets regardless of when they went into service, as opposed to the Company's use of one-half year's depreciation. She supported this adjustment by stating use of one-half year's depreciation is inappropriate as it would not reflect a normal year of depreciation for ratemaking purposes, and it does not match the full year of depreciation used for depreciation expense. This adjustment

also recognizes MDU's applying of the IRS-authorized 50% bonus depreciation rate and the accumulated depreciation rate toward plant additions placed in service in 2009 or for expenditures incurred in 2009. She removed the calculated deferred income taxes for Wygen III which resulted in a decrease of \$817,322, for a net reduction for these two adjustments of \$822,626. She proposed an interest synchronization adjustment of \$1,534 to synchronize interest expense with OCA's calculated rate base, excluding Wygen III. She also removed interest expense for the Wygen III rate base. The net effect of these two adjustments amounted to a \$1,947,215 decrease in interest expense. Based upon the above-described adjustments, as corrected, MDU's adjusted operating income is reduced by \$2,103,062. (Tr., pp. 532-534; OCA Exhibit No. 209, pp. 10-12.)

76. Zamora also proposed adjustments to the Company's rate base (OCA Exhibit No. 213) which included the removal of Wygen III costs related to the investment, accumulated depreciation and accumulated deferred income taxes and updates to accumulated deferred income taxes for all other investments, resulting in a total revised rate base, without Wygen III, of \$18,902,960. Zamora stated that with OCA's revised adjusted test year return of approximately \$1.6 million, the resulting rate of return without Wygen III is 8.587%, which exceeds OCA's recommended overall rate of return of 8.45%, resulting in the need for a revenue decrease. (Tr., pp. 538-539.)

77. Zamora testified to OCA's adjustments related to and including Wygen III, for purchased power and fuel, O&M expenses, Taxes Other Than Income and deferred income taxes. Regarding purchased power and fuel costs, she stated OCA's adjustment for decreases in energy capacity and transmission costs were the same as MDU's adjustment, but she adjusted fuel costs by \$1,902,225 based on the gross tonnage of coal estimated by Black Hills Power to be used in Wygen III. She stated she used a more current estimate of gross tonnage provided by Black Hills Power in its currently pending rate case, which resulted in a net adjustment decrease of approximately \$6.9 million dollars in purchased power and fuel expenses. In addition, she made adjustments to Wygen III-related O&M expenses, and to Wygen III-related depreciation expense. Zamora stated her gross Plant cost as reflected in her prefiled testimony was \$61.7 million, but acknowledged that MDU had provided an updated gross Plant cost on rebuttal, which she wished to verify prior to accepting it. She also adopted a depreciation expense adjustment to reflect a 50 year Plant life, testifying that it is appropriate, reasonable and consistent with depreciable lives used by other utilities for similar generating plants. Zamora made additional adjustments to Wygen III-related ad valorem taxes to reflect the most current 2009 mill levy, and the use of a full year of depreciation for deferred income taxes. She stated the tax depreciation for Wygen III had been adjusted to reflect the use of the special 50% bonus depreciation rate. She stated that she had included certain costs that were not incurred in 2009 in calculating tax depreciation which might require further revision. (Tr., pp. 539-541, 557, 596; OCA Exhibit No. 209, pp. 12.)

78. Zamora testified that her calculation for the Wygen III only portion of the revenue requirement is based on OCA's levelized return at present value for Wygen III of \$2,825,952. The decrease in expenses of \$1,871,213 per OCA's adjustments, when subtracted from the \$2,825,952 recommended return for Wygen III results in the need for additional revenue of \$954,739. Adjusting this amount by the federal income tax factor results in the need for

additional revenues for Wygen III of \$1,485,693. OCA's total recommended additional revenue requirement, taking into consideration OCA's recommended decrease in revenues without Wygen III of approximately \$40,000, when combined with the revenue requirement for Wygen III, results in a total revenue increase of approximately \$1.45 million or 7.852%. (Tr., p. 542; OCA Exhibit No. 209, p. 18.)

79. Zamora provided testimony regarding MDU's class cost of service study, stating she found it to be reasonable, with the methodologies and allocations being comparable to other studies that have been accepted by the Commission. She utilized MDU's cost of service study in performing two model runs for each piece of her revenue requirement and then added the results of the two runs for the revenue requirement without Wygen III and with the Wygen III-only revenue requirement to determine total costs to serve each customer class. (OCA Exhibit No. 214.) Zamora stated that after allocation of OCA's proposed additional revenue increase, each rate class will be providing the same percentage increase on each piece of the revenue requirement, i.e., non-Wygen III and Wygen III-only, with the effective rate of return for each class being slightly different and ranging from 5.857% to 7.564%. In doing so, OCA moved each class toward (but not to) recovery of its full cost of service-based revenue responsibility, with all classes receiving an increase except the Private Lighting Class which is currently exceeding its cost of service, and therefore will see a 36.9% decrease. (Tr., pp. 545-546; OCA Exhibit No. 209, pp. 19-23.)

80. Zamora addressed OCA's proposed rate designs for the various customer classes, stating she utilized the Company's class cost of service model in developing her rate design recommendations, the results of which are set out in OCA Exhibit No. 215. She described her rate design proposals for the various customer classes. (OCA Exhibit No. 209, pp. 26-30.) She proposed an inverted block energy charge for Schedule 10, Residential Class, with a monthly customer charge of \$25.50. OCA's initial proposed rate design for Schedule 20, Small General Service, included demand rates for all customers in the class; but she discovered that customers in the class using less than 10 kW did not have demand meters, and stated her rate design would not work for the entire class because demand could not be measured for the entire class. Therefore, she withdrew her recommendation of a demand charge for Rate 20 customers using less than 10 kW. Zamora stated the Schedule 25, Irrigation Class, is the only class whose rate components are not recovering their respective full costs. She testified the cost of service study supports a monthly charge of \$105.64; but, to avoid rate shock, she proposed a monthly charge of only \$50.00, which is about twice the current monthly charge. In addition, OCA is proposing a reduction in the on-peak demand rate of \$9.50 per kW to \$8.30 per kW, with the off-peak rate remaining at \$3.00, which will bring this rate element to cost of service. Regarding Aberle's proposal on rebuttal of offering a time-of-use rate and a non-time-of-use rate to irrigation customers, Zamora deemed it a reasonable alternative. She acknowledged that, [i] if the revenue increase ultimately approved differs from that proposed by OCA, the rate design will have to be revised, and [ii] if the amount of the increase is significant, it might impact her proposal to move to cost based rates. (Tr., pp. 547-549, 552-553, 556 & 611; OCA Exhibit No. 209, pp. 26, 29-30.)

81. Zamora described OCA's proposed revisions to the Company's current PSCA to reflect its change in status from a purchaser of all its power requirements to, in part, a self-

generator. It is OCA's position that as a self-generator of a portion of its power requirements, the provisions of Commission Rule Sections 249 and 250, which currently apply to MDU, will no longer be applicable. She testified that these rule provisions have not been interpreted in a manner which would allow a self-generator to accumulate its production costs and pass them on to customers. Recovery of these production costs is typically addressed in computing base rates. Her proposed tariff language to revise the PSCA is similar to the language used by Cheyenne Light, Fuel and Power Company, which she recommended as an appropriate starting point for PSCA revision. OCA proposed a deadband of \$290,000, based on a proportion of kWh sales, to assure that some portion of the system power cost changes are borne by the Company's shareholders rather than placing all the risk and reward of changing system power costs on ratepayers. In addition, ratepayers would only receive 95% of the cost changes that fall outside the deadband. Zamora testified this approach will incent the Company to make operational decisions for the benefit of customers. She also recommended further tariff language changes to the PSCA. She advocated changing the term "Base Rate" in each rate schedule to "Basic Service Charge" to reduce confusion. She noted the "Energy Charge" reference in the rates in the tariffs is actually comprised of two components, and argued they should be separately identified by the base purchased power and fuel cost rate component and the energy rate component, to arrive at the "Energy Charge" in an effort to provide more transparency in demonstrating how the energy charge in the PSCA is calculated. (Tr., p. 550; OCA Exhibit No. 209, pp. 32-34, 37-38.)

Summary of Parties' Testimony on Stipulation

82. The Commission reopened the record at its hearing of March 22, 2010, to receive into the record the *Stipulation* (MDU/OCA Joint Exhibits No. 1 and 2) and the parties' testimony and exhibits in support of the *Stipulation*. Mr. Bruce S. Asay, MDU counsel, offered certain late-filed exhibits in addition to the exhibits to the *Stipulation*. The offered late-filed exhibits included: [i] Exhibit No. 157, an explanation of the Company's AFUDC calculations; [ii] Exhibit No. 158, a document identified as the shared assets administrative fee and ground lease; and [iii] Exhibit No. 159, the detailed class cost of service study and work papers. Provided in support of the *Stipulation* were Goodin's affidavit (MDU Exhibit No. 60); Mulkern prefiled testimony (MDU Exhibit No. 161) and Aberle's prefiled testimony and exhibits (MDU Exhibit No. 162).

83. Mulkern summarized her testimony, stating the *Stipulation* represents the parties' efforts to arrive at negotiated agreements regarding various adjustments initially advocated in the parties' respective direct and rebuttal cases. She stated the Company believed the *Stipulation* is in the public interest and should be approved. Mulkern summarized the various terms and conditions of the *Stipulation* including an identification of the various stipulated adjustments, which result in a stipulated increase in MDU's revenue requirement of \$3,253,726 per annum. The *Stipulation* provides, *inter alia*, for the implementation of the stipulated revenue increase over a three-year phase-in period. Mulkern testified the phase-in approach addresses the concerns expressed by many MDU customers at the Sheridan public comment hearing that the immediate implementation of the 25% revenue increase was excessive, caused rate shock, and precluded customers' ability to budget for such a large increase. In the phase-in plan, a Year 1, increase of \$1.8 million or 8.9% would be implemented on May 1, 2010. The remaining \$1.4 million or 6.6% would be implemented in Year 2 on May 1, 2011, and would also include a separate surcharge of \$0.0029 per kWh which would be amortized over a two-year period or

until the remaining deferred amount, including interest, is amortized to zero. She stated the interest component is based on the overall stipulated return of 8.68%, explaining the 8.68% was not really an interest rate but rather the rate of return or a carrying charge. Adding together the deferred amount and the surcharge, the Year 2 total increase would be \$2,261,726 or 10.3%. She acknowledged the overall increase of 10.3% in Year 2 was on top of the 8.9% increase in Year 1, essentially resulting in an increase of 20.1%. She stated customers will experience an increase in the first and second year; but there would be no change in rates in the third year. In the fourth year, customers would see a decrease in rates due to the elimination of the surcharge. She agreed customers would still be paying the 20.1% increase in Year 3 because of the amortization of the amount deferred in the first year. She also acknowledged the stipulated increase would be 16.1% if it were implemented in its entirety this year rather than being phased in as proposed in the *Stipulation*. (Transcript of March 22, 2010, Stipulation Comment Hearing, hereinafter Stipulation Comment Tr., pp. 16-17, 19, 36-39, 41-44; MDU/OCA Joint Exhibit No. 1, pp. 5-6.)

84. Mulkern stated that to address irrigation customers' concerns, MDU will bifurcate the Rate 25 irrigation rate into two rate schedules; [i] the optional time-of-day irrigation rate; or, if preferable, [ii] a more traditional non-time differentiated rate with a flat demand and energy charge. The optional time-of-day tariff will utilize an on-peak period of 3:00 p.m. to 7:00 p.m. She stated the *Stipulation* also includes a revised PSCA Rate 50 which includes a sharing of costs symmetrically above and below the base cost of power supply of 90% to the customer and 10% to the Company. She also stated the parties had agreed to a negotiated 45-year depreciated life for Wygen III. (Stipulation Comment Tr., pp. 17, 24, 29.)

85. Ms. Tamie Aberle provided a summary of her prefiled testimony and exhibits in support of the *Stipulation*. (MDU Exhibit No. 162) She testified that the stipulated increase of \$3,253,726 was allocated to each of the rate classes based on the results of the embedded class cost of service study. (Exhibit No. TAA-1 to MDU Exhibit No. 162.) Regarding the phase-in of the rate increase, Aberle stated the Years 1 and 2 increases were allocated to each rate class based on the revenue requirement for each particular class as derived from the embedded class cost of service study. The surcharge needed to collect the deferred portion of the revenue increase was spread to all customer classes based on energy usage. She stated the revenue increase was allocated so each class would produce the overall rate of return of 8.68%. Going forward with those revenues, she agreed, would produce a rate of return for all classes of 8.68%. (Exhibit No. TAA-2 to MDU Exhibit No. 162.) She acknowledged that, depending on the customer's usage, the surcharge could affect a Rate 39 large service customer differently than a residential customer. She discussed the \$0.00290 per kWh surcharge, stating under the proposed *Stipulation*, the residential class would experience an increase of approximately \$3.95 per month in Year 1 and \$7.70 per month in Year 2. (Stipulation Comment Tr., pp. 61-62, 69-71, 82-88.)

86. Aberle stated the *Stipulation* will result in changes to Small General Service Rate 20 in that it had been split into separate schedules for demand and non-demand metered customers. She discussed the irrigation service rate, stating the schedule was bifurcated into Rate 25, non-time differentiated rate, and Rate 26, for customers who choose the option of using time-differentiated service. Aberle testified that irrigation customers can choose a new rate schedule at the beginning of their irrigation season but prior to any usage for that season. Under the *Stipulation*, the irrigation tariff provides that customers may choose a rate schedule through

May of 2010. Aberle stated the Company does not want irrigation customers to change rate schedules during the season because of the additional administrative burden and the need to reprogram meters. She said MDU would probably inform its irrigation customers of this change and the options available to them by sending a letter to its customers. Under the *Stipulation*, the negotiated time-of-use irrigation peak period is from 3:00 p.m. to 7:00 p.m. Aberle acknowledged the evidence presented in this case demonstrated the peak periods fall between 4:00 p.m. and 6:00 p.m. with the majority occurring at 5:00 p.m. (MDU Exhibit No. 122.) She also discussed costs to serve irrigation customers and how the demand charge was calculated. The *Stipulation* proposes a demand charge of \$6.25 per kW for non-time-of-use irrigators. (Stipulation Comment Tr., pp. 62-69, 75-77, 79-82, 89-97.)

87. Zamora provided a summary of her prefiled testimony and exhibits in support of the *Stipulation*. (OCA Exhibits No. 219, 220, and 221.) Zamora's testimony explained how the *Stipulation* resolved the issues identified in OCA's direct case regarding revenue requirement, rate design and tariff issues, and why she believed approval of the *Stipulation* was in the public interest. She stated [i] the parties had stipulated to an ROE of 10.9%, resulting in an overall rate of return of 8.68%; and [ii] the Company adopted OCA's adjustments, or agreed to revise OCA's adjustments with updated information. The *Stipulation* further provides for an increase in revenues of \$3,253,726 per annum to be effective May 1, 2010, to be phased-in over a three year period (an explanation of the phase-in increases is found in the *Stipulation* at ¶¶ 16-20). She stated the phase-in approach was intended to address the concern expressed by MDU's customers at the Sheridan public comment hearing over the significant size of the proposed rate increase and would give customers an opportunity during the first year of implementation to plan and budget for the additional increase to occur in the second year. She also addressed the proposed interest on the deferred amount of 8.68%, which was based on the overall stipulated rate of return. She found them appropriate and reasonable.

88. Zamora stated other significant issues in the *Stipulation* included, but were not limited to, a stipulated depreciation life of forty-five years for Wygen III, and rate design issues for residential, small general service and irrigation customers. She also testified that the *Stipulation* provides for a revised Rate 50 Schedule applicable to the PSCA that provides for a deadband or sharing mechanism based on a 90/10 ratio, wherein MDU would recover 90% of its purchased power and fuel costs above the base rate costs and will return 90% of purchased power and fuel costs below the base rate costs. (Tr., pp. 103-105, 115-116, 137; OCA Exhibit No. 219, pp. 3-4, 7.)

Findings of Fact: Public Comments

89. The Commission heard numerous comments from MDU ratepayers at the February 10, 2010, hearing in Sheridan. City and county officials and representatives from the Sheridan County School District and Board of Directors, Sheridan Memorial Hospital, Sheridan County Public Library, AARP, Powder River Basin Resource Council and the Sheridan County Stock Growers expressed concerns that the amount of the increase would negatively impact their respective budgets and would result in the loss of jobs and programs. Numerous MDU residential customers opposed the proposed rate increase because of current economic conditions, inflation and the financial burden it would place on ratepayers. Ratepayers generally

questioned [i] the magnitude of the proposed increase, [ii] the effect it will have on their electricity bills, [iii] the prudence of MDU's investment in Wygen III, [iv] the proposed ROE, and [v] the depreciable life of the Plant.

90. Mr. Bill Bensel, Chairman of the Wyoming Water Development Commission and an MDU irrigation and residential customer, provided comments generally opposing the irrigation demand charge and rate structure changes for the Irrigation class, stating the peak hours needed to be adjusted to allow irrigators to irrigate their fields consistent with state water laws. Bensel also discussed the prudence of MDU's investment in Wygen III and offered several alternatives for MDU and the Commission to consider when seeking to meet future electricity demands. He discussed the difficulty irrigators will face when trying to shut down their systems to avoid watering during peak times, and he questioned whether the proposed increases will cause irrigators to discontinue doing business because they no longer can afford to irrigate their lands. Bensel expressed concern that MDU's proposed peak hours were not compatible with state water laws or the way irrigation is managed and used and could result in a loss of the irrigators' water and water rights. He stated that the demand rate option of a \$6.25 per kW demand charge would not be a workable alternative. Bensel also explained that flood irrigation has become less common in the Sheridan area, so most irrigators pump constantly. (Tr., pp. 63-67, 438-456.)

91. The Commission wishes to express its gratitude to the Sheridan ratepayers for their participation in the public comment hearing. The Commission was impressed with the high level of rate payer participation and the thoughtful quality of their comments and questions. The public raised a substantial number of issues which are worthy of comment; and we will address these issues to help MDU's customers better understand the regulatory process and the decisions of this Commission. Some of the questions posed by MDU's customers and the answers are as follows:

a. Question. When and why did MDU decide to purchase a 25% share in Wygen III Plant? Why did MDU not consider wind as an alternative? Has MDU lost the flexibility of competitive bidding for supply contracts?

Answer. MDU had an option which expired December 31, 2008, to purchase a portion of the Wygen III facility. Because the Company was faced with the expiration of favorable long-term supply contracts in 2016, it was concerned that long-term supply and demand trends would make Sheridan ratepayers vulnerable to wholesale market volatility, including unstable prices and sharp price increases. Its analysis showed that the best option for protecting Sheridan ratepayers was to purchase a share in Wygen III. Black Hills had a proven record of being able to construct similar plants on time and on or under budget.

MDU did not specifically consider wind as an alternative. However, the Commission is aware that wind is generally more expensive. Although costs are coming down as the technology matures, wind is somewhat expensive; and it is, by its nature, an intermittent resource. Complete reliance on wind power poses considerable service and economic risks to a utility with a relatively small service population. Wind integration cost is discussed in a Black and Veatch paper found under the Hot Topics section of the Commission's web site at

<http://psc.state.wy.us>. Interested persons should also review the Western Wind and Solar Integration Study prepared for the National Renewable Energy Laboratory in Golden, Colorado. It may also be found under Hot Topics/Wind Integration on the PSC's web site.

b. Question. Has the economic downturn lowered the cost of equity capital?

Answer. In general, this appears to be the case. However, the cost of equity capital for a public utility must be considered in comparison to similar companies. Both parties submitted evidence on this question, and the Commission decided on a return on equity capital less than that originally proposed by either party. However, the Commission is not free to ignore established legal standards (found in statute, Wyoming and federal Supreme Court cases) which address the type of evidence the Commission must consider in reaching conclusions on capital costs.

c. Question. Could the Commission require MDU to rely entirely on debt, with no equity?

Answer. When a utility's capital structure is out of balance, i.e., when it relies too heavily on debt, the Commission may order the use of a hypothetical capital structure for ratemaking purposes and has done so in the past. As a utility approaches a 100% debt capital structure, it becomes much riskier for itself and bondholders. If all of its financing is done with fixed obligations (bonds), it must pay for all of its financing on a regular basis in fixed amounts. This increases the chance of default and bondholders would rightly demand higher and higher returns on their investments, to the point at which small companies might become so risky that they could be denied access to capital markets. Similarly, a 100% common equity capital structure would lessen the ability of a utility to raise needed money through issuance of more common stock. Potential stockholders would be buying a heavily diluted portion of the company. Issuance costs would rise and perhaps stock would remain unsold. A balanced capital structure gives the utility the ability to access capital markets on generally reasonable terms. Given our statutory charge under Wyoming law that rates may not be unfair, discriminatory, unjust, unreasonable or unremunerative, ordering reliance on 100% debt would be contrary to law.

d. Question. Could the Commission require 60-year depreciation on the Plant?

Answer. The Commission theoretically could, but doing so would not be supported by the evidence of record in this case. Such action outside of the record would be arbitrary on its face under the Wyoming Administrative Procedure Act and subject to being overturned on appeal.

e. Question. Could the Commission authorize a return on equity in the mid-single digits?

Answer. It could do so if the evidence of record supported it. However, such a decision would not be supported by the evidence in this case and or requirements of law (including the United States Supreme Court cases discussed below). As in ¶ 93d above, if the Commission were to act arbitrarily, its decision could be set aside after judicial review.

f. Question. Is the return on equity based on good comparables?

Answer. As the case is decided, yes.

g. Question. Can the irrigation rate be adjusted?

Answer. The irrigation rate has been adjusted, consistent with the principle that each class of service must bear its own costs. On the last day of the hearing, devoted principally to the *Stipulation*, the Commission reviewed details of MDU's cost of service study as it relates to irrigation service. The Commission is satisfied with the results of the cost of service study and notes that the new optional irrigation tariff reduces the daily peak hours from an eight-hour window to a two-hour window when the actual MDU system peaks occur. The Commission also notes that OCA did not question MDU's cost of service study.

h. Question. Has MDU addressed its own cost structure?

Answer. That issue was more directly addressed in last year's rate case. Until 2008, MDU's management had successfully operated under a rate structure which had been in place since 1993. The Commission believes MDU is competently managed, and there has been no evidence offered to show that MDU has incurred excessive or imprudent costs. The need for this rate case rests principally on the purchase of a 25% share of Wygen III.

i. Question. Has MDU accounted for the savings it will realize by not having to purchase all of its power?

Answer. Yes. The purchased power costs are decreased in this case to account for the power generated by the Wygen III Plant.

j. Question. Why are we guaranteeing MDU a return on equity when the healthiest companies in the nation are losing money and private citizens' investments and businesses do not have guaranteed returns?

Answer. The Commission does not guarantee MDU a return on its equity. It only gives MDU an opportunity to earn a return on equity, and in doing so, sets a maximum allowable return. Utilities commonly fail to earn the authorized rate of return. We have to determine a fair rate of return as noted above. Also see the *Hope* and *Bluefield* cases discussed below. They are the standard for utility regulators throughout the United States.

k. Question. Can MDU do better with demand side management?

Answer. The Commission will address this question in another docket, already in progress. The Commission notes that the cost of demand side management measures are typically passed on to ratepayers as a surcharge, which means that benefits of proposed measures must be thoughtfully scrutinized and tested to see whether they provide real value for consumers.

l. Question. Are the ratepayers bearing the risk of MDU's investment in Wygen III?

Answer. There are different forms of risk. However, as we understand the original question, we believe the answer is that ratepayers are not guaranteeing a return to MDU or otherwise limiting MDU's own risks in a manner uncommon for utilities in Wyoming or elsewhere in the United States. In this regard, we note that under Wyoming law, public utilities like MDU are granted exclusive service territories, and so are insulated from competitive risk. Also, it is important to understand that, in areas of the country where utilities are free to compete, lower prices do not always result.

m. Question. How does MDU compare with Rocky Mountain Power, which was reported to be asking for a 3% decrease in its power costs?

Answer. The newspaper accounts were a bit misleading since they addressed only the portion of Rocky Mountain rates which were driven by purchased power and fuel costs. Its overall rates have been rising. Rocky Mountain has advised the Commission that it intends to file rate cases on a yearly basis for the near future.

For the past four years, Rocky Mountain Power normally has had two proceedings a year, one to increase general rates, and one to pass on power costs. In this year's general rate case proceeding, Rocky Mountain Power requested a rate increase of \$70 million per annum. Rocky Mountain Power and the parties in those two cases have proposed a combined settlement that would cut this increase in half.

Rocky Mountain Power's plans for the coming ten years call for \$10 billion of new investment a substantial portion of which is driven by environmental standards and new transmission to serve its customers. Rate increases every year are likely, in addition to whatever proceedings there may be to adjust power costs. MDU does not have similar plans.

n. Question. Did MDU responsibly forecast its need for the next ten years before it decided to invest in Wygen III?

Answer. Yes.

o. Question. Should MDU have been directed to discuss its investment decision with the customers before it went ahead?

Answer. The Commission considered MDU's decision to become involved with Wygen III in a public hearing for a proposed certificate of public convenience and

necessity. That proceeding, which forecast a rate increase of 17%, drew far less attention than the Company's eventual proposal to increase rates by nearly double that amount. We note that the Stipulation here proposed an increase of 16.1%, and the Commission approved an increase that was even smaller. The Commission is charged with regulating utilities, not managing them. We cannot require the public to pay active attention to a Company decision, even one which may have long term effects; and such discussions would be outside of the record of this case. That is, the Commission could not use such meetings in making its decision here.

Legal Standards Applicable in This Case

92. W.S. § 37-3-101 states:

All rates shall be just and reasonable, and all unjust and unreasonable rates are prohibited. A rate shall not be considered unjust or unreasonable on the basis that it is innovative in form or in substance, that it takes into consideration competitive marketplace elements or that it provides for incentives to a public utility. * * * The commission may determine that rates for the same service may vary depending on cost, the competitive marketplace, the need for universally available and affordable service, the need for contribution to the joint and common costs of the public utility, volume and other discounts, and other reasonable business practices. * * *

93. The Commission has broad powers to inquire into the facts surrounding the determination of rates. They include W.S. § 37-2-119, which articulates the "used and useful" test and allows wide latitude in the Commission's investigation of rate-related matters. It states, in part:

In conducting any investigation pursuant to the provisions of this act the commission may investigate, consider and determine such matters as the cost or value, or both, of the property and business of any public utility, used and useful for the convenience of the public, and all matters affecting or influencing such cost or value, the operating statistics for any public utility both as to revenues and expenses and as to the physical features of operation...

94. W.S. § 37-2-120 requires the Commission to afford due process in its cases, stating, in part:

No order, however, shall be made by the commission which requires the change of any rate or service, facility or service regulation except as otherwise specifically provided, unless or until all parties are afforded an opportunity for a hearing in accordance with the Wyoming Administrative Procedure Act.

95. W.S. § 37-2-121 gives the Commission latitude to determine the actual rates to be charged by a utility, stating, in part:

If upon hearing and investigation, any rate shall be found by the commission to be inadequate or unremunerative, or to be unjust, or unreasonable, or unjustly discriminatory, or unduly preferential or otherwise in any respect in violation of any provision of this act, the commission may fix and order substituted therefore such rate as it shall determine to be just and reasonable and in compliance with the provisions of this act.

96. W.S. § 37-2-122(a) reinforces the Commission's ability to exercise its sound informed discretion in rate making cases. It states:

In determining what are just and reasonable rates the commission may take into consideration availability or reliability of service, depreciation of plant, technological obsolescence of equipment, expense of operation, physical and other values of the plant, system, business and properties of the public utility whose rates are under consideration.

97. W.S. § 37-2-122(b) gives similar necessary latitude to the Commission regarding utility services, stating:

If, upon hearing and investigation, any service or service regulation of any public utility shall be found by the commission to be unjustly discriminatory or unduly preferential, or any service or facility shall be found to be inadequate or unsafe, or any service regulation shall be found to be unjust or unreasonable, or any service, facility or service regulation shall be found otherwise in any respect to be in violation of any provisions of this act, the commission may prescribe and order substituted therefore such service, facility or service regulation, as it shall determine to be adequate and safe, or just and reasonable, as the case may be and otherwise in compliance with the provisions of this act, including any provisions concerning the availability or reliability of service. It shall be the duty of the public utility to comply with and conform to such determination and order of the commission.

98. At W.S. § 16-3-107, the Wyoming Administrative Procedure Act sets parameters for due process in Commission cases, including the giving of reasonable notice. In accord are W.S. §§ 37-2-201, 37-2-202, and 37-3-106. See also, Sections 106 and 115 of the Commission's Rules.

99. Read in *pari materia*, these statutes articulate the basic mechanism of the public interest standard which the Commission is to follow in its decisions. The public interest must come first in the Commission's decisions, as the Wyoming Supreme Court has stated; and the desires of the utility are secondary to it. *Mountain Fuel Supply Company v. Public Service Comm'n*, 662 P.2d 878 (Wyo. 1983). Construing W.S. § 37-3-101, which requires rates to be reasonable, the Court in *Mountain Fuel*, *supra*, at 883, commented:

This court cannot usurp the legislative functions delegated to the PSC in setting appropriate rates, but will defer to the agency discretion so long as the results are fair, reasonable, uniform and not unduly discriminatory.

Later, 662 P.2d at 885, the Court in *Mountain Fuel* observed:

We agree that if the end result complies with the 'just and reasonable' standard announced in the statute, the methodology used by the PSC is not a concern of this court, but is a matter encompassed within the prerogatives of the PSC.

100. In accord are *Great Western Sugar Co. v. Wyo. Public Service Comm'n and MDU*, 624 P.2d 1184 (Wyo. 1981); and *Union Tel. Co. v. Public Service Comm'n*, 821 P.2d 550 (Wyo. 1991), wherein the Supreme Court stated, 821 P.2d at 563, that it "...has recognized that discretion is vested in the PSC in establishing rate-making methodology so long as the result reached is reasonable."

101. Consistent with the discretion given to the Commission in examining cases and reaching a just result, there are no precise bases in Wyoming law to guide the Commission in determining a utility's rate of return. Therefore, the Commission must apply its informed

judgment to all of the evidence in the case. In this work, we are guided by the earnings and capital attraction standards of *Bluefield Water Works & Improvement Co. v. Public Service Commission of West Virginia*, 262 U. S. 679 (1923); and *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U. S. 391 (1944); accepted in Wyoming in *In re Northern Utilities*, 70 Wyo. 275, 249 P.2d 769 (Wyo. 1952). Taken together, these cases stand for the principle that a public utility is entitled to rates which will permit it a reasonable opportunity to earn a return on its investment properly reflecting the risk of the business and which will reasonably preserve the financial soundness of the company and allow it to raise the capital needed to provide service in the public interest. Having said that, we also acknowledge that the measurement of the required level of return is not a matter of simple mathematics but is a matter requiring judgment and the employment of discretion. The United States Supreme Court, in *Hope, supra*, noted that a "just and reasonable end result" is the desired outcome and that it is the end reached, rather than the method employed in achieving it, that should control.

102. Under Section 119, Settlements, of the Commission's Rules, "...informal disposition may be made of any hearing by stipulation, agreed settlement, consent order or default upon approval of the Commission."

103. In *Willadsen v. Christopulos*, 1987 WY 5, 731 P.2d 1181, (Wyo. 1987) the Wyoming Supreme Court discussed the standard of proof to be used in Wyoming administrative hearings. Construing Wyoming Statutes (W.S. §§ 41-3-911(b) and 41-3-911(c)), neither of which names the standard to be applied in matters coming before the State Board of Control, the Supreme Court stated, 1987 WY 5 at ¶13, with regard to W.S. § 41-3-911(c):

Under that statutory section and the applicable provisions of the Wyoming Administrative Procedure Act, the standard applicable to an adjudicatory hearing before the Board of Control, unless otherwise stated, is the "preponderance of the evidence" standard customarily used in civil cases. *Amerada Hess Pipeline Corporation v. Alaska Public Utilities Commission*, Alaska, 711 P.2d 1170, 1179 n. 14 (1986); *Intermountain Health Care, Inc. v. Board of County Commissioners of Blaine County, Idaho*, 107 Idaho 248, 688 P.2d 260, 263 (1984), quoting E. Cleary, McCormick on Evidence § 357 (3d ed. 1984).

Later, the Court emphasized the necessity of applying this standard, 1987 WY 5 at ¶14, saying:

Because the Board of Control failed to apply the preponderance of the evidence standard and instead applied the substantial evidence test applicable to appellate review of an agency decision, we find that petitioners were denied due process.

Although one of the statutes on which we rely in this case, W.S. § 37-1-121, specifies the substantial evidence standard, the other sections do not. We must therefore agree with the Court in *Willadsen*, that the correct standard to apply to this case is the higher preponderance of the evidence standard. We would be remiss in even colorably denying due process in this case and will not do so.

Additional Findings of Fact

104. Many of the particular facts necessary to the decision of this case have been stated above and will not be restated here.

105. MDU filed its initial general rate case filing seeking additional revenue relief in the amount of \$6,198,501 per annum (30.7% overall increase). The Company subsequently filed its supplemental or amended application reducing the amount of its requested revenue increase to \$5,053,756 per annum (25.1% overall increase) to reflect its accelerated/bonus depreciation deduction adjustment related to Wygen III, as provided for under federal law for certain qualifying property additions. The Company subsequently filed its updated electric division Depreciation Study and Common Plant Depreciation Study in which it proposed certain revised depreciation rates; the net effect of which is a further decrease in the Company's revenue request to \$4,833,545 per annum. The OCA offered its testimony through expert witnesses supporting its initial proposed revenue increase of \$1,430,794 per annum (7.773% overall). (OCA Exhibit No. 210.)

106. At the conclusion of the contested portion of the public hearing in which MDU and OCA presented their positions on an appropriate revenue increase, they advised the Commission they were in the process of negotiating a settlement which culminated in the filing of the *Stipulation*. An additional public hearing was held in which Company and OCA witnesses provided testimony in support of the *Stipulation* which provided for a negotiated revenue increase of \$3,253,726 per annum based upon a 10.9% return on equity, which when applied to the Company's proposed capital structure results in an 8.68% overall return on rate base. Generally, the *Stipulation* provided for a three year phase-in of the revenue increase including interest on the amount of the increase deferred in the first year of the phase-in. Other major provisions in the *Stipulation* included depreciation expense and other depreciation-related calculations based on a negotiated 45 year Wygen III depreciation life, the offering of Rate 25 and Rate 26 irrigation schedules, the filing of a rate case within five years of the date of the order in this case, and a revision to the Power Supply Cost Adjustment tariff mechanism to provide for a sharing mechanism as advocated by the OCA. (MDU/OCA Joint Exhibit No. 1.)

107. Based upon the preponderance of the evidence offered in this proceeding, the Commission finds that the *Stipulation*, although offering certain reasonable terms and conditions, must be rejected for the reasons set forth below. Further, the Commission finds the evidence of record supports additional rate relief for MDU in the amount of \$2,651,565 per annum (13.1% overall), as supported by the Commission findings below.

The Stipulation

108. Witnesses Mulkern and Zamora testified that one of the major benefits of the *Stipulation* was the proposal to phase-in the stipulated revenue increase over a three-year period, offered to mitigate rate shock concerns expressed by MDU's customers at the public comment hearing in contemplation of the 25% increase proposed. The phase-in approach was justified as a mechanism which would provide customers with the ability, during the first year of the phase-in, to plan and budget for the additional increase which would come in the second year and continue through the third year. Zamora acknowledged OCA had made concessions to the Company in the *Stipulation* regarding the return on equity and the Wygen III depreciation rate to obtain the phase-in provision. She also expressed her belief that the phase-in provision was an integral part of the *Stipulation* and that if the Commission had concerns and rejected the phase-in

provision it should reject the *Stipulation*. (Stipulation Comment Tr., pp. 142, 152.)

109. The *Stipulation* specifies 8.68%, the overall rate of return agreed to by the parties, as the interest rate for the deferred portion of the phased-in rate increase. The Commission finds this proposed interest rate on the deferred portion of the revenue increase to be excessive. If this rate reflects the time value of money, the Commission finds it highly unlikely that, if the Company needed to borrow money in the interim, it would have to pay an interest rate of 8.68%, given current economic and financial conditions. Below, the Commission will discuss its determination of an appropriate return on equity for this Company which will decrease the overall rate of return on rate base.

110. The phase-in proposal was ostensibly offered to mitigate the rate shock to come from implementation of the full revenue increase in 2010, by implementing a \$1.8 million (8.93%) increase in the first year, and a \$1,453,726 increase in the second year (6.6%) and continuing into the third year. (MDU/OCA Joint Exhibit No. 1, ¶¶ 16-17.) On closer inspection of the proposed phase-in and its associated interest on deferred revenues, it is clear that, in exchange for the transitory illusion of less rate shock in the first year of implementation, the net result is that customers will pay more overall than if the phase-in were not allowed. Zamora acknowledged this fact. (Stipulation Comment Tr., pp. 123-124.) Rather than ameliorating rate shock in the first year, the phase-in has the effect of continuing the rate shock effect for at least two years. Mulkern acknowledged on cross-examination that, in Year Two and Three of the phase-in, and taking into account the interest on the unamortized balance, customers would experience an increase of approximately 20.1%, (in comparison to current revenue levels), as opposed to the 16.1% increase they would realize in the first year if the *Stipulation's* revenue increase were put into effect with no phase-in. Only in Year Four would the increase decline to 16.1%. (Stipulation Comment Tr., pp. 42-43.) The phase-in proposal will also cause customers to experience rate instability as rates would be adjusted in Years One, Two and Four (and remaining high in Year 3). This will contribute to unnecessary customer confusion and may serve little purpose than to remind customers that rates continue to increase in subsequent years as a lingering effect of approval of the *Stipulation*. The Commission finds the provisions regarding the handling of possible under-recoveries or over-recoveries of the deferred balance at the end of the two-year amortization period, as referenced in ¶ 19 of the *Stipulation*, is unclear and leaves unresolved the appropriate rate treatment for an over-recovered balance. Based upon the findings set forth herein, the *Stipulation* provides no tangible rate relief benefits to customers, is not in the public interest and must be rejected. Simply put, the ratepayers will pay more if the phase-in is accepted, and it should not be. We further reject the notion, expressed at ¶ 25 of the *Stipulation*, that MDU should bind itself to file another rate case in five years. MDU is capable of deciding when it wants to file for additional rate increases without an arbitrary deadline, just as the Commission is fully capable of ordering MDU to file another case should we determine the need has arisen.

OCA'S Levelization Proposal

111. OCA witness Parrish offered a proposal to levelize or equalize the cost of the return on MDU's 25% Wygen III ownership interest over the expected depreciable life of the facility, as a mechanism to make all generations of MDU customers pay the same proportional

share of return MDU is entitled to earn on its portion of the Plant. The levelization proposal would lessen the rate impact of adding Wygen III to rate base during the initial years of its inclusion. Utilizing a fifty-year depreciable life for Wygen III, and a discount rate for the present value of 8.45% (OCA's recommended overall return on rate base) over the life of the Plant, levelization results in a return to the Company's investors of \$2.8 million each year over the fifty-year life of the Plant. Parrish further testified that her levelization proposal assumes no change in the \$2.8 million return to investors, regardless of future MDU general rate case filings. It also does not account for the costs of any additions to or repairs of the Plant during its useful life. Traditional depreciation methods would front load the return on the new Plant, resulting in early customers paying more than later generation customers, as the value of the Plant is depreciated over time. (Tr., pp. 626, 630-631.)

112. Parrish acknowledged this is the first case in which she has offered a levelization proposal and she was unaware of any prior Commission decision which addressed or approved a similar proposal. (Tr., p. 650.) She conceded that there is some uncertainty surrounding her proposal and that, over the first year of the Plant's operation, the return on the Plant would be less than 8.45%. (Tr., pp. 651, 657.) She further conceded the inherent unevenness in the plan: during the first ten years, customers would pay a lower return, with the return paid in later years being greater. She acknowledged implementing an 8.45% return over the fifty-year period could be problematic if certain events occurred, such as [i] debt and equity costs increasing into double digits which would make the discount rate insufficient in the marketplace, or [ii] the Company being unable to attract capital in the event the market did not accept her methodology. (Tr., p. 686.) Further Parrish noted in her summary testimony that the result of her levelization approach would be that MDU will collect about \$55 million more from customers than it would if a nominal levelized return were used. (OCA Exhibit No. 216, p. 15.)

113. The Commission finds, based upon its review of Parrish's testimony and Gaske's rebuttal testimony in which he expressed a number of concerns regarding OCA's levelization proposal, that the proposal relies on too many assumptions to be approved. For example, to implement OCA's proposal, which is premised on a return of 8.45%, set at a time of historically low interest rates, we would be required to assume that this return will be reasonable over the 50-year life of Wygen III (an asset which was estimated by Parrish to quadruple the size of MDU's Wyoming electric rate base). The proposal may impose unreasonable constraints on future commissions who may feel compelled to maintain the fixed return level in the face of market conditions which may suggest otherwise. It could jeopardize the Company's ability to attract capital in the market place under such circumstances. It would have the effect of shifting part of the recovery of the return on Wygen III from the current generation of customers to later generations who will incur additional significant costs (approximately \$55 million under the OCA's proposal). In addition, as noted by Gaske, the return earned during the initial year of Wygen III's inclusion in rate base and in subsequent years, under the levelization proposal, may be insufficient to provide a reasonable return to common equity investors, as interest on debt must first be paid to bondholders. (Tr., p. 737-739.) In all, in return for lower, and possibly inadequate initial returns on the Wygen III investment, in contemplation of \$55 million of additional costs to be imposed on ratepayers over the years, accepting that we are in a time of low inflation and that it might not remain so over the 50-year life of the Plant, acknowledging that it is not only bad public policy but also not possible to attempt to bind future commissions,

either actually or morally, to a decision made today, and understanding that adopting the plan could make it difficult for MDU to raise needed capital in the future, we find that OCA's levelization proposal must be rejected as being unreasonable and contrary to the public interest. This finding is supported by the preponderance of the evidence of record in this case.

Overall Cost of Capital and Return on Common Equity

114. MDU witness Senger offered [i] the pro forma MDU capital structure as projected for the twelve month period ending December 31, 2009; [ii] the pro forma costs of long and short term debt; [iii] the costs of preferred stock, as projected through 2009; and [iv] the recommended cost of equity capital of 12.75% as determined by Gaske. (MDU Exhibit No. 107.) Using these figures to derive weighted average costs, the Company recommended an overall rate of return of 9.62%. OCA witness Wichmann adopted the Company's proposed pro forma capital structure and associated weighted costs of long and short term debt, and preferred stock. (OCA Exhibit No. 208.) She applied her recommended cost of equity capital of 10.4% to the pro forma capital structure and weighted costs of debt and preferred stock in arriving at her recommended overall rate of return of 8.45%. The uncontroverted testimony supports the use of the Company's pro forma capital structure and pro forma cost of debt and preferred stock, and we will do so in calculation of the authorized overall rate of return below.

Component	Percentage	Cost	Weighted cost
long-term debt	44.959%	6.79%	3.05%
average short-term debt	2.771%	3.77%	0.104%
preferred stock	2.5%	4.59%	0.115%
common equity	49.77%	10.4%	5.18%
TOTAL	100.00%		8.45%

115. MDU witness Gaske and OCA witness Wichmann provided their respective testimony and analyses in support of their calculations of a reasonable cost of common equity capital for MDU's Wyoming electric utility operations as summarized, *supra*. Both Gaske and Wichmann selected their respective group of comparable companies utilizing similar information sources and certain criteria or filters they believed would provide a sampling of companies that would reasonably serve as proxies for MDU's Wyoming electric operations. We note that twelve of Gaske's thirteen comparable companies were included in Wichmann's group of twenty two proxy companies. Both Gaske and Wichmann relied on several different DCF analyses as their primary methodologies in arriving at their recommended returns on common equity. Wichmann's ROE analyses resulted in a range of reasonableness of 9.05% to 10.93%. She recommended a ROE of 10.4%. In contrast, Gaske utilized the results of his two DCF analyses in arriving at a range of reasonableness of 11.56% to 12.95% and concluded that because of MDU's slightly above average risks a ROE of 12.75% was appropriate. (Tr., p. 174.)

116. The Commission finds Wichmann's testimony and analyses presented in calculating a range of reasonableness for MDU's ROE to be the most thoroughgoing, persuasive, and supported by the preponderance of the evidence. Gaske's explanation of his criteria in selecting his comparable companies, and notably his use of companies with at least 25% of generation from coal-fired plants, unreasonably narrows the group of comparable companies,

making the results of his analyses vulnerable to manipulation. He assigned additional risk to the Company because of its use of coal-fired generation in meeting a portion of its supply requirements, which he contrasted to its prior total dependence on purchased power contracts and the associated market volatility in serving its load requirements. This, on its face, appears to conflict with the Company's underlying rationale for purchasing a 25% interest in Wygen III, i.e., the mitigation of wholesale market volatility and its associated higher risks. The Commission is not persuaded by Gaske's argument that current economic conditions and the decline in the stock market have resulted in investors requiring a higher rate of return as they perceive more risk in common stock investments. (Tr., pp. 193-194.)¹ In contrast, Wichmann's determination of an appropriate ROE took into consideration the results of her DCF analyses and an identification and analysis of macroeconomic, financial and business risks facing MDU's regulated utility operations. (OCA Exhibit No. 201, pp. 23-28.) Taking these factors into account and recognizing [i] the narrowing of credit spreads between Aaa and Baa rated company securities and 30-year Treasury bond yields in 2009 (which suggests reduced risk and lower premium expectations by investors), and [ii] the regulatory paradigm in which MDU operates (which allows a significant portion of its costs to be recovered under tariffs, including the PSCA mechanism), Wichmann concluded the risks to MDU's Wyoming utility operations are average in comparison to other utilities, with the business risk being low to average. (Tr., p. 521.)

117. Although Wichmann recommended a ROE of 10.4%, the midpoint of her range of reasonableness is 9.9%. Chairman Minier asked her, given his concerns that the fed fund rate has been low for an extended period of time and the investment climate has been poor, whether it was unreasonable to consider a 9.9% ROE as being appropriate. She stated that any point within her range of reasonableness of 9.05% to 10.93% would be supported by her analysis. (Tr., p. 522.) Taking into consideration current economic conditions (as reflected in historically low interest rates which appear poised to continue, and indications that investors are returning to the equity market), the Commission finds and concludes that Gaske's recommended ROE of 12.75% is excessive and that a more reasonable ROE is appropriately closer to the midpoint of OCA's range of reasonableness. The Commission finds that a ROE of 10.0% for MDU's Wyoming electric utility operations is reasonable and appropriate. It meets the standards and requirements of the *Hope* and *Bluefield* cases. Based on our determination, that a 10.0% cost of common equity is supported by the preponderance of the evidence, we find the appropriate and reasonable overall rate of return for MDU's Wyoming electric utility operations to be 8.25%, calculated thusly:

Component	Percentage	Cost	Weighted cost
long-term debt	44.959%	6.79%	3.05%
average short-term debt	2.771%	3.77%	0.104%
preferred stock	2.5%	4.59%	0.115%
common equity	49.77%	10.0 %	4.977%

¹ The Commission's concerns regarding Gaske's credibility were further underscored by his willingness to testify under oath about an unrelated issue based on a text message received by another person in the hearing room. (Tr., pp. 732-736.) The Wyoming Administrative Procedure Act does not prohibit the Commission, as a learned tribunal, from accepting hearsay evidence, but, in this instance, acceptance would be far enough beyond what is reasonable that it would undermine the Commission's process.

TOTAL	100.00%		8.25%
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Wygen III Depreciation Life

118. In its application, MDU proposed a 40-year depreciable useful life for Wygen III, stating the Company utilized the depreciation rate assigned by Black Hills Power & Light to the facility. The Company did not present an independent analysis of an appropriate depreciable life or corresponding depreciation rate for Wygen III and stated its recently completed depreciation studies did not include Wygen III because it was not constructed at the time the depreciation studies were prepared. (Tr., pp. 309-310.) Also, the Company originally proposed an annual depreciation rate for the Plant of 2.72% which translates to a 36.7 year life for the Plant. Mulkern subsequently testified on rebuttal that she was updating the depreciation rate for the Plant to 2.5% to reflect the 40-year life which the Company maintained was reasonable. (Tr., p. 756.) MDU witness Neigum acknowledged on cross examination that the Company had several older coal plants that have operated in excess of 50 years. From a technological standpoint, he was unaware of any reason which would limit a coal plant's life to 50 years. He stated a 40-year life for Wygen III was a "safe" estimate. (Tr., pp. 253-254, 281.)

119. OCA witness Zamora testified in support of a depreciable life of 50 years for Wygen III, basing her recommendation on the depreciation rates and lives assigned to similar coal-fired power plants by Rocky Mountain Power and Black Hills (which possesses plants similar to Wygen III). She stated that a 40-year life was a good starting point but that it was logical to extend the lives of these plants to address continued capacity deficits. (Tr., pp. 541, 563.) In discussing the depreciable lives of other vintage coal-fired plants in MDU's inventory, Parrish noted the current updated MDU depreciation studies reflect depreciation lives ranging from 48 to 66 years. (Tr., p. 645.)

120. The Commission finds the evidence presented on this issue supports a depreciable life of 50 years and a corresponding depreciation rate for MDU's share of Wygen III of 2.0% per annum. The Company presented no independent analysis to support its 40-year depreciable life, and based its decision on nothing more than the 40-year life assigned to Wygen III by Black Hills. We note the 40-year life assigned to Wygen III by Black Hills has not been brought before this Commission for consideration or approval. It will, however, be an issue for consideration in the pending Black Hills general rate increase filing. Our determination, based on the evidence in this case, is, we note, also consistent with the representations of OCA regarding useful coal plant lives in excess of 50 years for other coal-fired plants operated by Rocky Mountain Power and Black Hills. The use of a 50-year depreciable life for Wygen III is further supported by the Company's acknowledgment that the actual coal contract to serve the Wygen III Plant is set to run for 50 years. A 50-year life is within the range of reasonableness as developed in this case. (Tr., pp. 245, 254.) In addition, the Commission finds OCA's concession to accept a 45 year depreciation life for Wygen III understates the reasonable useful life of this generating facility, which will also be addressed herein.

Revenue Requirement

121. The OCA recommended a number of adjustments to the Company's proposed pro

forma revenues, O&M expenses, federal income taxes, other taxes and depreciation expenses. In her revenue requirement analysis, Zamora separated Wygen III expenses and investment costs from the rest of the revenue requirement to accommodate the OCA levelization proposal. Because the Commission rejects OCA's levelization proposal, it is unnecessary for us to consider Zamora's Wygen III adjustments separately from non-Wygen III-related expenses and investment costs.

122. OCA proposed an adjustment to usage which corrects an error identified by the Company regarding the revenues associated with the Rate 39 – Large General Service Class. This increases the Company's pro forma revenues by \$18,726 to reflect additional revenue from demand and energy charges collected from the class due to an upward adjustment to usage. This adjustment simply corrects errors and was not contested by the Company. It is adopted by the Commission.

123. The Commission finds OCA's adjustment to purchased power and fuel costs associated with Wygen III is appropriate. It reflects updates in the gross tons of coal (629,355 tons) and uses a more updated cost of coal of \$11.70 per ton. MDU witness Neigum testified to these statistics as representing the most current 2010 projections. (Tr., p. 237.) Mulkern provided updated coal expense information agreeing that the most recent updates should be utilized and stated they would match the update of the Wygen III Plant value she identified in her rebuttal testimony. (Tr., p. 746; MDU Exhibit No. 155.) Zamora agreed the most current Statement R price regarding the coal price should be used. (Tr., p. 558.) OCA's adjustment also incorporates a purchased power adjustment to reflect the correction to the Rate 39 usage.

124. In its initial testimony, OCA proposed an adjustment to Wygen III-related O & M expenses. During the course of the hearing, the parties agreed that updated information regarding Wygen III available at the time of the hearing should be incorporated into these adjustments. As to this specific adjustment, Zamora stated that she did not disagree with the updated amounts provided by Mulkern on rebuttal and said they should be adopted; and MDU agreed to the inclusion of the update. (Tr., p. 746.) The Commission finds the updated O & M expense total associated with Wygen III in the amount of \$2,668,722 (as reflected in Commission Exhibit C), are appropriate and should be incorporated in the calculation of the revenue requirement.

125. OCA proposed to exclude \$2,413 in advertising expense and industry dues, stating the expenditure of these funds are not needed in the provision of utility service and should more appropriately be shareholder funded. Company witness Mulkern, on rebuttal, testified the Company disagreed with the exclusion of the advertising expense in the amount of \$1,683, arguing that institutional advertising benefits the communities it serves, thereby benefiting customers. (Tr., p. 743.) Commission Rule Section 248 addresses the issue of "promotional", "political" and "institutional" advertising and sets out the general prohibition of cost recovery in rates for these types of advertising, stating that such costs should be recovered by shareholders or owners of the utility. Commission Rule Section 248(e) specifically excludes certain forms of advertising from the general prohibition of cost recovery through customer rates, allowing recovery of the costs of advertising required by the public interest, as determined on a case-by-case basis. The Commission finds the advertising for which the Company seeks rate recovery

does not fall within the exceptions in Section 248(e). We do not find that the Company has supported its argument for recovery of these advertising expenses in this case. The denial of rate recovery for these advertising expenses and industry dues in the amount of \$2,413 is in the public interest and is consistent with past Commission practice.

126. The OCA proposed to amortize regulatory commission (rate case) expenses over a ten year period, stating the normal time frame between MDU rate case filings is 8-15 years. (OCA Exhibit No. 209, p. 9.) Company witnesses proposed a three-year amortization period. The Commission finds the shorter amortization period of three years for recovery of regulatory commission expense is more reasonable and should be adopted as it provides for a more timely recovery of these expenses. The Commission anticipates that the historically lengthy period of time between MDU rate case filings may no longer be possible given the rapidly changing financial markets, which may require a more frequent review and evaluation of a reasonable cost of capital for MDU's Wyoming utility operations. It is also possible that carbon emission legislation and other regulatory issues might arise, which could necessitate further rate case filings. Many such issues may arise at the federal level -- beyond the power of the Commission or MDU to ignore or defer.

127. The Commission finds the Company has failed to support by a preponderance of the evidence its proposed generalized inflation adjustment to certain O&M expense accounts it had not individually adjusted for inflation. The Commission concurs with the position advocated by OCA that the adjustment of these specific expenses by a blanket percentage inflation factor is inconsistent with general past Commission practice of allowing adjustments for known and measurable changes. Therefore, the Commission adopts OCA's downward adjustment in the amount of \$6,551.

128. OCA proposed to adjust O&M expenses to exclude certain costs related to one-time occurrences and prior period adjustments from 2007, and costs recovered through the Company's Load Management Program. Zamora corrected an error in the calculation of her prior period expense adjustment, reducing the total adjustment from \$46,454 to \$30,994. (Tr., p. 587.) Mulkern, on rebuttal, testified the Company did not take issue with OCA's adjustments regarding Account 902, Prior Period Adjustments from 2007, as corrected by Zamora; Account 925, the one-time occurring Wrench Ranch Fire expenses; or Account 908, Refrigerator Round Up Program Costs. Mulkern however, took issue with the exclusion of \$3,499 associated with the Basin Electric Facilities Addition, which were related to transmission substation expenses, on the basis that even though the specific expense activity was non-recurring, such expenses regularly recur. (Tr., p. 744-745.) The Commission concurs with the Company's rationale that inclusion of the \$3,499 in expenses associated with the Basin Electric Facilities Addition is appropriate and reflects the recovery of a recurring expense. The Commission finds the OCA's other adjustments to O&M expense accounts, as corrected, are uncontested, and therefore an adjustment in the amount of \$27,495 is adopted.

129. The Commission finds OCA has supported its proposed adjustments related to Taxes Other Than Income, which included, [i] adjustments to Franchise Taxes of \$125 and Gross Revenue Taxes of \$57 to reflect OCA's Rate 39 revenue adjustment, and [ii] an adjustment to ad valorem taxes of \$3,503 for Wygen III based on 2009 mill levies. The correct mill levy amounts

were not available to the Company at the time of the filing. We thus adopt a total net adjustment of \$3,321.

130. MDU witness Mulkern offered a depreciation expense adjustment to reflect updated depreciation rates and associated expenses as shown in the Company's updated and very recently filed Electric Depreciation Study and Common Plant Depreciation Study. She stated the effect of utilizing the new depreciation rates would be to reduce her pro forma depreciation expense by \$218,211 per annum. Mulkern stated factoring the effects of the revised depreciation expense on rate base, O&M expenses, and income taxes has the effect of reducing the Company's revenue increase by \$220,358. (MDU Exhibit No. 142, pp. 2-3.) OCA witnesses accepted the Company's adjustment but recommended the Commission not accept or approve the updated depreciation studies because the OCA had insufficient time to review the studies in detail. OCA suggested that a more thorough review and full consideration of the studies would be best handled in the context of future rate proceedings. (Tr., pp. 564-566, 639-646.) Mulkern testified the Company did not object to the utilization of the revised depreciation expenses as set forth in the studies or allowing the OCA and Commission staff adequate additional time to review and inquire into the depreciation studies. (Tr., p. 759.) Based upon the concurrence of the parties in the adjustment to depreciation expense which reduced the Company's revenue requirement by \$220,358 per annum, and general agreement that additional time for review of the updated depreciation studies is appropriate, the Commission finds the adjustment to depreciation expense should be accepted and factored into the calculation of the Company's revenue requirement. Further, the Commission finds the Company should be directed to refile its updated depreciation studies, as a separate docketed matter, so they can be reviewed, noticed, and additional proceedings can be held, if necessary, and a final determination can be made by this Commission regarding their reasonableness and possible approval of the studies.

131. In her supplemental testimony in support of the Company's amended application, Mulkern proposed an additional decrease to the Company's revenue request to recognize the impact of a proposed 50% bonus tax depreciation adjustment available for federal income tax purposes for certain qualifying property additions. The Company presented testimony to support its belief that its investment in Wygen III qualified for the bonus depreciation deduction. (Tr., pp. 297-300; MDU Exhibit No. 126, pp. 3-4.) Mulkern testified that the head of the Company's tax department, its internal auditors, and external tax experts had come to the common conclusion that the Company qualified for the bonus tax depreciation adjustment. (Tr., pp. 470-471.) OCA witness Zamora also recommended the bonus tax depreciation adjustment be adopted and incorporated in the calculation of the Company's revenue requirement. Zamora incorporated this deduction in her adjustments to deferred income taxes. She agreed her proposed adjustment, as reflected in her prefiled direct testimony, should be revised to reflect the update of MDU's Wygen III investment. (Tr. p. 559.) Mulkern's bonus depreciation adjustment was updated to reflect the updated estimate of MDU's Wygen III investment, as reflected in MDU Exhibit No. 139. OCA and MDU concurred that the most current updated numbers should be utilized for many of the Wygen III adjustments. The Commission concurs with the parties' position that an adjustment to reflect the 50% bonus tax depreciation deduction for the Company's Wygen III investment is appropriate and should be adopted.

132. The Commission further finds that OCA's testimony supports its adjustment to

deferred income tax expense to reflect the use of a full year of book depreciation -- in contrast to MDU's use of a half year -- in the calculation of the 50% bonus depreciation. The Commission concurs with OCA's adjustment. The use of a full year of depreciation is consistent with the normalizing of book depreciation in general and with specific reference to the calculation of deferred income tax expense. This adjustment increases book depreciation in the calculation and the annual tax effect of the difference between book and tax depreciation in the calculation, as depicted in the OCA calculation, is applied to deferred income tax expense and accumulated deferred taxes in the rate base calculation. The changes in book depreciation in the calculation are included in the current tax calculation.

133. The Commission accepts the OCA adjustment to synchronize interest expense in calculating current income taxes to reflect the interest deduction and the recovery of the interest expense necessary to finance the utility plant needed to provide service to the public. The Commission also agrees with OCA's adjustment to ad valorem taxes, which reflects the use of the 2009 mill levy for Wygen III, consistent with updated information. In addition, the Commission adopts the OCA adjustment to Bad Debt Expense based on a five year average of the bad debt expense ratio, which is applied in the revenue requirement calculation.

Rate Base

134. In its initial application, MDU presented a pro forma rate base for its Wyoming utility operations of \$80,489,334, which it lowered in its amended application to \$71,779,243, after taking into account the 50% bonus depreciation deduction. (MDU Exhibit No. 128, p. 7 and revised p. 7.) In her supplemental testimony, Mulkern calculated a revised pro forma rate base of \$72,038,689 that took into account the depreciation rates in MDU's updated depreciation studies. (MDU Exhibit No. 150, 2nd revised p. 7.) During the hearing, the parties provided their respective calculations of MDU's Wygen III investment costs, which must also be factored into the calculation of an updated rate base. Zamora calculated the capital cost for Wygen III at \$61.7 million. (Tr., p. 559.) Both Mulkern and Zamora agreed the most updated Wygen III capital costs should be used in determining the appropriate rate base. Zamora testified that, with an asset the size of Wygen III, it is appropriate to use the most current data. She further stated she had verified the Company's AFUDC calculation for 2010 but needed to verify the Company's AFUDC calculation for 2009. (Tr., pp. 559, 604.) The 2009 AFUDC calculation was subsequently provided in MDU late-filed Exhibit No. 157. On rebuttal, Mulkern provided an updated capital investment amount for Wygen III of \$63,354,500, which includes AFUDC for 2009 and 2010. (Tr., pp. 312; MDU Exhibit No. 139.) The Commission concurs with the parties that the most current numbers must be used in calculating MDU's Wyoming rate base. Factoring in the adjustments to accumulated deferred depreciation to reflect the Commission use of a 50-year depreciation life for Wygen III (2.00% per year), the effects of the updated depreciation studies, and the accumulated deferred income tax, the Commission finds MDU's Wyoming electric utility rate base to be \$71,863,966, as reflected in the following table which illustrates the Commission's calculated revenue deficiency of \$1,703,954. We must thereafter make provision for payment by MDU of federal corporate income tax at the rate of 35%, which required the application of a "tax gross up" factor of 1.55612 to the revenue deficiency, yielding an additional revenue requirement of \$2,651,565, all as based on the Commission's findings as set forth above.

Operating Income and Adjustments		
A	MDU Initial Filing - Revenues	\$ 3,726,284
Commission Adjustments		
B	Add Revenues	18,726
Deduct (or add) Expenses		
C	Purchased Power and Fuel	(134,010)
D	Wygen III O&M Expenses	6,817
E	Advertising and Dues	(2,413)
F	Regulatory Commission Expense ²	0.00
G	Remaining O&M Expenses (Inflation)	(6,551)
H	Miscellaneous O&M Expenses	(27,495)
I	Depreciation expense	(731,581)
J	Taxes Other Than Income	(3,321)
K	Deferred Income Taxes	8,557,461
L	Income Taxes ³	(8,138,783)
M	Total Expense Adjustments	(479,876)
N	Adjusted Test Year Operating Income	\$ 4,224,823

Rate Base		
O	MDU Initial Filing - Rate Base	\$ 80,489,334
Commission Adjustments		
P	Plant Costs & Accumulated Depreciation	(67,907)
Q	Accumulated Deferred Income taxes	(8,557,461)
R	Commission Determined Rate Base	\$ 71,863,966

Revenue Requirement for This Case		
S	Commission Determined Required Return on Rate Base at 8.25% [R x 8.25%]	5,928,777
T	Return Deficiency [S - N]	1,703,954
U	Commission Determined Additional Revenue required [T x 1.55612]⁴	\$ 2,651,565

Rate Spread/Rate Design

135. Aberle described the Company's proposed rate spread. She testified the Company proposes to increase rates so that each customer class would produce revenue at the overall rate

² The Commission ordered no change from present practice.

³ Includes Interest Synchronization

⁴ The federal income tax gross-up factor. See discussion directly above this table.

of return with the exception of Schedule 24, the private lighting class, which is currently contributing more than the overall rate of return. The Company proposes to maintain Schedule 24 rates at their current levels. (Tr., p. 324.) She further stated the Company's proposal to move the customer charges and energy components of the various rates closer to their respective embedded costs, consistent with the results of its embedded cost of service study. She said this movement complies with the Commission's prior directives that such movement toward actual cost be made. (Tr., p. 325.) The OCA concurred with the use of the Company's class cost of service study results in apportioning its proposed revenue increase between the various classes, concurring that the Schedule 24 Class was exceeding the overall rate of return. OCA used the Company's model in developing its proposed rate design for each customer class with the objective of continuing movement toward recovery by each class of its respective cost of service, and movement towards, or recovery of, cost of service for the individual rate components for each class. (Tr., p. 544-546.) The Commission concurs with the general objectives of the parties in continued movement to cost of service based rates in developing their respective rate proposals. The Commission finds generally that setting rates with the objective of recovering the actual embedded costs incurred in providing service to the respective customer classes, and the rate components within the classes, is consistent with the past policy directives of this Commission.

136. MDU offered an alternative inverted block rate design for the Residential Rate Class, Schedule 10, as directed by the Commission in the prior rate case. The Company, however, recommended continuing its current rate design which contains a monthly base rate and a flat energy charge, but agreed that an inverted block rate design was acceptable as long as a minimum base rate of \$25.00 was incorporated. MDU proposed an initial energy block of 1,000 kWh with the second block of energy use having an additional \$0.02 per kWh differential. (MDU Exhibit No. 118, p. 12.) OCA proposed the use of an inverted block rate design with a minimum base rate/monthly charge of \$25.50 and a similar \$0.02 per kWh differential for all energy above the initial block of 1,000 kWh. (OCA Exhibit No. 209, pp. 26-27.) The Commission finds the use of an inverted block rate design for Schedule 10 will provide better pricing signals to customers and will promote conservation. The use of a \$25.00 base rate/monthly charge is consistent with the results of the embedded cost of service study and provides additional movement towards recovery of the fixed costs associated with this rate component.

137. The OCA proposed a rate design for the Small General Service Class, Schedule 20, that provided for a \$4.00 demand charge for the first 10 kW of usage and \$10.00 per kW for usage over 10 kW for primary customers and a \$4.50 demand charge for the first 10 kW of usage and \$10.50 per kW for usage over 10 kW for secondary customers. MDU's current rate design does not provide for a separate demand charge for the first 10 kW of usage. MDU witness Aberle testified that OCA's proposal to implement a demand charge for the first 10 kW of usage for small use Schedule 20 customers would require the use of approximately 1700 demand meters at an installed cost of approximately \$485,500, which she recommended not be implemented. (Tr., p. 764.) OCA witness Zamora subsequently acknowledged that her proposed rate design was not workable if demand meters were not in place for all customers in this class. (Tr., p. 548.) The Commission finds acceptable the proposal of the parties in the *Stipulation* at ¶ 21, that a Small General Service Rate 20 Non-Demand Metered provision is added and charged

separately under Schedule 20, with this provision being applicable to customers that do not currently have a demand meter. The proposal is reasonable and supported by the preponderance of the evidence. Given the small benefit to be derived, the expenditure of approximately \$485,500 to purchase and install demand meters for small use customers in this class to track their demand usage is not supportable.

138. Members of the Irrigation Class, Schedule 25, raised concerns at the public hearings regarding the negative impacts of the current Irrigation rate design on their farming operations and their rates. In response, the Company proposed on rebuttal to bifurcate the current Irrigation Rate Schedule and offer an optional rate schedule under which Irrigation customers could take service under a time differentiated demand rate (time-of-day), or a more traditional non-time differentiated rate with a flat demand and energy charge. The Company witness testified that the optional schedule would provide an appropriate price signal due to an increase in demand charges and an incentive to customers to move their loads to off-peak periods. (MDU Exhibit No. 140, p. 4.) OCA proposed continuation of the current Schedule 25 with an increase in the monthly charge to \$50.00, a reduction in the on-peak demand rate from \$9.50 per kW to \$8.30 per kW, continuing the off-peak rate of \$3.00 per kW, and an increase in the energy charge. (OCA Exhibit No. 209, pp. 29-30.)

139. The Commission finds that a proposed bifurcated Irrigation Rate Schedule which offers optional time-of-day rates, with an on-peak hours period⁵, and the use of a non-time-of-day rate design⁶ which uses a flat demand charge, will provide irrigation customers with the ability to control their respective costs by determining which rate schedule is most compatible with their usage characteristics. Adoption of a bifurcated rate schedule proposal is consistent with and supported in the rebuttal testimony of Aberle. (Stipulation Comment Tr. p. 79-80.) The Company initially proposed continuation of a 12:00 noon to 8:00 p.m. on-peak period which it subsequently shortened to the four hour period proposed in the *Stipulation*. In response to cross-examination, Aberle expressed her reluctance to move off the 12:00 noon to 8:00 p.m. on-peak period as she did not have available data to support another time period. However, we find the Company failed to offer any evidence which would support continuation of the current eight hour peak period. (Tr., pp. 790-791.) On the contrary, the Company provided actual data which showed its system peaks occurring between 4:00 p.m. to 6:00 p.m., with the majority occurring at 5 p.m. (MDU Exhibit No. 122.) The Commission finds that use of a peak period that runs from 4:00 p.m. to 6:00 p.m. for Rate Schedule 26 is supported by the evidence and should be adopted. The Commission further finds a monthly Basic Service Charge of \$50.00, an on peak demand rate of \$8.30 per kW, and an off-peak demand rate of \$3.00 per KW under Rate Schedule 26 are reasonable and supported by the evidence. The Commission Staff will monitor the use of Schedules 25 and 26 and their impact on irrigation customers.

140. The Commission also finds that irrigation customers should be allowed to select at any time the irrigation schedule under which they wish to be served; however, once the customer selects an irrigation schedule service must continue to be taken under that schedule for at least a one year period. The Company agreed this selection process which required the

⁵ Rate Schedule 26 offered in the *Stipulation*

⁶ Rate Schedule 25 offered in the *Stipulation*

customer to be bound for at least a year was acceptable and would address prior concerns expressed by the Company regarding the administrative burden and costs associated with having to reprogram its irrigation meters if customers were able to switch schedules more frequently. (Public Comment Tr., pp. 64, 88.) We expect some confusion among irrigation customers as a result of the adoption of Schedules 25 and 26. Consequently, at the public deliberations on April 14, 2010, the Commission directed the Company to send a letter to its irrigation customers prior to May 1, 2010, describing the new Schedules 25 and 26 and scheduling a meeting with its irrigation customers for the purpose of explaining, *inter alia*, how the schedules operate and how the rates were calculated and providing a full understanding of the possible consequences of adopting a particular schedule. We also directed that a customer making a selection prior to the date of the customer meeting shall not be bound by his initial election. The meeting must include a Commission staff member.

141. Based upon the above rate design and rate spread findings the Company is directed to file compliance tariffs that recover the approved revenue requirement from the various customer classes as follows:

Rate Class	Revenue Increase	
	\$	%
Residential Service		
Rate 10	1,113,404.00	10.1%
Rate 11	<u>10,968.00</u>	<u>2.8%</u>
	1,124,372.00	9.9%
Small General Service		
Rate 20	803,672.00	21.5%
Rate 22	<u>348.00</u>	<u>2.9%</u>
	804,020.00	21.4%
Irrigation Service		
Rate 25	23,950.00	9.2%
Rate 26	new tariff: insufficient data ⁷	
Large General Service		
Rate 39	726,901.00	15.8%
Lighting		
Rate 24	(29,889.00)	-34.9%
Rate 41	<u>2,525.00</u>	<u>3.0%</u>
	(27,364.00)	-16.1%
Total Wyoming Electric	2,651,879.00	13.1%

Tariff Revisions

142. The Commission finds OCA has supported the use of separate demand and energy components for purchased power and fuel recovered under the PSCA mechanism. On rebuttal,

⁷ Rate 26 is newly created. There is therefore no "revenue increase" for this class and no data upon which to base a percentage of increase. See the discussion of the rates for this class at ¶ 139.

Aberle provided an alternative proposal to collect the demand charges associated with the power purchase agreement from the cost of service component of each rate with only the prospective changes in the demand component billed through the energy charge, stating the demand costs do not fluctuate significantly from year to year. The Commission finds the base cost of power supply, including the demand, energy and transmission components are those established in this case as a result of the Commission's determinations. The demand and transmission components that change as a result of changes to MDU's power purchase agreement, and filed under the Company's PSCA tariff pursuant to Commission Rule Sections 249 and 250, will be reflected in the energy or demand components, as applicable, and will be allocated to the primary and secondary service customer classes.

143. The Commission further finds OCA has supported its recommendation that the use of the term "Base Rate" in all applicable retail rate schedules be replaced with the term "Basic Service Charge," as it will eliminate confusion that currently arises from the use of the term "base rate" in other contexts in the calculation of various rates.

Power Supply Cost Adjustment (PSCA) Mechanism

144. In its initial testimony, OCA proposed a revised PSCA mechanism which would accommodate the purchased power and fuel costs associated with MDU's interest in Wygen III. OCA argued that Commission Rule Sections 249 and 250, which provide for the recovery of commodity and commodity-related costs by utilities that purchase all their power requirements from a wholesale provider, do not provide for the recovery of accumulated production costs from self-generation and the subsequent passing of them on to customer. Zamora stated these production costs are usually addressed at the time base rates are computed in a general rate case. (OCA Exhibit No. 209, p. 33.) She recommended the adoption of a revised PSCA mechanism that incorporates a dead band and sharing mechanism as more fully described in the summary of her testimony, above. The Company argued that its current PSCA tariff language would accommodate its partial self-generation status and that Rules 249 and 250 do not preclude recovery of production or fuel costs. The Company further disagreed with the incorporation of the dead band and the sharing mechanism as proposed by the OCA. (Tr., pp. 748-754.) As shown in the *Stipulation* at ¶ 26, the Company and OCA negotiated a revision to the PSCA mechanism consistent with OCA's proposal of incorporating a dead band and sharing mechanism. The Commission rejected the *Stipulation*, and with it, the above-described mechanism. We therefore infer that MDU retains its initial opposition to OCA's revised PSCA mechanism.

145. The Commission finds OCA's proposal of a revised PSCA mechanism which incorporates a dead band and a sharing mechanism falls under the innovative and non-traditional ratemaking provisions contained in W.S. § 37-2-121, which states in part:

Any public utility may apply to the commission for its consent to use innovative, incentive or nontraditional rate making methods. In conducting any investigation and holding any hearing in response thereto, the commission may consider and approve proposals which include any rate, service regulation, rate setting concept, economic development rate, service concept, nondiscriminatory revenue sharing or profit-sharing form of regulation and policy, including policies for the encouragement of the development of public utility infrastructure, services,

facilities or plant within the state, which can be shown by substantial evidence to support and be consistent with the public interest.

This statute sets up a mechanism whereby it is the utility which must apply for innovative, incentive or nontraditional rate making methods. The Commission is limited to consenting (or not) based on substantial evidence that the public interest is thereby served. MDU has neither applied for nor proposed the adoption of OCA's revised PSCA mechanism. The Commission finds that we are precluded under W.S. § 37-2-121 from imposing such a mechanism on the Company. MDU may make such a filing in the future. However, the Commission advises the Company that it will not be receptive to a filing under Rule Sections 249 and 250 which seeks recovery of items or costs for which we have not previously allowed recovery under these Rules.

Net Metering Tariff

146. In response to the Commission's inquiry regarding the need for an updated calculation of the Company's avoided cost for purposes of its net metering tariff, the Company expressed its belief that the Company's avoided cost would not change as a result of its acquisition of an interest in Wygen III in meeting its load requirements. Aberle argued the Company's current avoided cost is based on its Black Hills PPA. Any power needed over and above its Wygen III production will be purchased under the PPA; and this, she offered, establishes the marginal cost MDU avoids. (Tr., p. 335.) Aberle subsequently conceded the inclusion of the generation costs of Wygen III in its avoided cost calculation would result in a decrease in its current avoided costs. (Tr., pp. 338, 344-345.) We note that, when the MDU system is not utilizing its entire share of Wygen III's output, and a net metering customer is producing electricity, MDU avoids nothing with reference to the PPA. The Commission finds the evidence of record clearly supports the need for the Company to recalculate its avoided cost and submit a revised net metering tariff. The Company is directed to submit its proposed revised avoided cost and net metering tariff for Commission consideration within sixty (60) days of the issuance of this *Order*.

Conclusions of Law

147. MDU is duly authorized by the Commission to provide retail electric public utility service in its Wyoming service territory under certificates of public convenience and necessity issued by the Commission. MDU is an electric public utility as defined in W.S. § 37-1-101(a)(vi)(C); and, as such, the Commission has the general and exclusive jurisdiction to regulate MDU as a public utility in Wyoming under W.S. § 37-2-112.

148. Proper public notice of these proceedings was given in accordance with the Wyoming Administrative Procedure Act, W.S. § 37-2-203 and the Commission's Rules, especially Section 106 thereof. The public hearings were held and conducted pursuant to W.S. §§ 16-3-107, 16-3-108, 37-2-203, and applicable sections of the Commission's Rules. The intervention petition of the City of Sheridan was properly denied. Intervenor OCA became a party to the case for all purposes.

149. The Commission concludes, based on its findings above, that the offered *Stipulation* must be rejected as not being in the public interest.

150. The preponderance of the evidence of record, as shown in the Commission's findings above, supports the Commission's conclusion that MDU's current rates for electric service are inadequate and unremunerative, and should be increased in the amount of \$2,651,565 per annum, the same to be effective for usage on and after May 1, 2010.

151. The Commission concludes an overall rate of return on rate base of 8.25%, based upon a reasonable return on equity of 10.0%, for MDU's Wyoming electric utility operations is just and reasonable and in the public interest. We conclude that these rates satisfy the capital attraction standards of the *Hope* and *Bluefield* cases, discussed, *supra*.

152. The Commission further concludes the rates approved herein will allow MDU to continue to provide adequate, safe and reliable service. The rates approved herein are just and reasonable, and the recovery of the rates pursuant to the rate spread and rate design adopted herein will not result in undue discrimination as between customer classes because they are based on the respective cost of serving each customer class consistent with the provisions of W. S. § 37-3-112.

153. The Commission concludes the tariff modifications approved herein are supported by the preponderance of the evidence of record and should be approved as being in the public interest.

IT IS THEREFORE ORDERED:

1. Pursuant to the Commission's deliberations held on April 14, 2010, Montana-Dakota Utilities Co. is authorized to implement a general electric rate increase of \$2,651,565 per annum, effective for usage on and after May 1, 2010, and done in the manner approved hereinabove.

2. Based on the Commission's deliberations, MDU filed compliance tariffs to reflect the approved general rate increase, the rate spread, the rate design and the tariff modification findings set forth above. The compliance tariffs were approved by open meeting action taken on April 27, 2010, to be effective for service rendered on and after May 1, 2010.

3. The Company is directed to refile its updated depreciation studies within thirty (30) days of the issuance of this *Order* for consideration in a separate docket.

4. The Company is directed to submit its proposed revised avoided cost and net metering tariff for Commission consideration within sixty (60) days of the issuance of this *Order*.

5. With its compliance tariff filing, the Company submitted a proposed letter to Irrigation customers as described above in ¶ 140. Having directed several needed revisions to

draft letter notice, the Commission directs that the Company use the revised letter and shall hold the scheduled informational meeting as directed by the Commission.

6. This *Order* is effective immediately.

MADE and ENTERED at Cheyenne, Wyoming, on May 26, 2010.

PUBLIC SERVICE COMMISSION OF WYOMING

Alan B Minier

ALAN B. MINIER, Chairman

Steve Oxley

STEVE OXLEY, Deputy Chairman

Kathleen A. Lewis

KATHLEEN A. LEWIS, Commissioner



David J. Lucero

DAVID J. LUCERO, Assistant Secretary