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Attorneys for NorthWestern Energy

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

IN THE MATTER OF NorthWestern Energy's	)	
2013 and 2014 Applications for (1) Approval of	)	REGULATORY DIVISION
Deferred Cost Account Balances for Electricity	)	
Supply, CU4 Variable Costs, DGGGS	)	DOCKET NO. D2013.5.33
Variable Costs/Credits, Spion Variable	)	
Costs; and (2) Projected Electricity Supply Cost	)	DOCKET NO. D2014.5.46
Rates, CU4 Variable Rates, DGGGS Variable	)	
Rates, and Spion Variable Rates	)	

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**NORTHWESTERN ENERGY'S OPENING BRIEF**

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## CASE SUMMARY

### A. INTRODUCTION

In early July of 2013, an unforeseeable series of events resulted in Colstrip Unit 4 (“CU4”) being off-line for nearly seven months. Due to the forced outage, NorthWestern Corporation, d/b/a NorthWestern Energy (“NorthWestern”), had to purchase additional power in the market to meet its obligation as a public utility to serve its customers’ needs. No one questions in this proceeding – nor could they – that replacement power costs are electricity supply costs.

Unless imprudently incurred, electricity supply costs are to be recovered in rates through a statutorily mandated electricity supply cost tracking adjustment. If a question of prudence does arise, it is to be resolved by an examination of what the utility knew, or should have known, at the time it acted. It is not to be determined with the benefit of hindsight.

In this case, the record clearly establishes that NorthWestern’s actions with respect to CU4, the 2013 forced outage at the unit, and its purchase of replacement power during the outage, were prudent. The two active Intervenors in this case, the Montana Consumer Counsel (“MCC”) and the Montana Environmental Information Center/Sierra Club (“MEIC/Sierra Club”), do not contend that NorthWestern imprudently purchased replacement power, or imprudently paid too much for replacement power. They take the unreasonable positions that the Montana Public Service Commission (“Commission”) should disallow prudently incurred replacement power costs because: (1) NorthWestern did not file a lawsuit seeking recovery of the replacement power costs from Siemens Energy Inc. (“Siemens”), which was responsible for performing maintenance and repair work on CU4, and (2) NorthWestern did not have outage

insurance for CU4 when the forced outage occurred. Neither contention is reasonable, nor supported by substantial credible evidence in the administrative record in this case.

## B. PROCEDURAL HISTORY

On May 31, 2013, NorthWestern submitted its Application for (1) Approval of Deferred Cost Account Balances for Electricity Supply, CU4 Variable Costs, and Dave Gates Generating Station (“DGGS”) Variable Costs/Credits; and (2) Projected Electricity Supply Cost Rates, CU4 Variable Rates, DGGS Variable Rates, and Spion Kop Wind Generation Asset (“Spion”) Variable Rates for the tracker year from July 1, 2012 through June 30, 2013 (“2013 Electricity Supply Cost Tracking Adjustment”).

On June 19, 2013, the Commission issued a Notice of Application and Intervention Deadline setting the intervention deadline for July 31, 2013. By Notice of Staff Action, intervention was granted to the Human Resource Council District XI, Natural Resources Defense Council, and the MCC. As part of the 2013 Electricity Supply Cost Tracking Adjustment, NorthWestern requested interim rates. On June 26, 2013, the Commission issued Order No. 7283, which granted NorthWestern’s request for interim rates.<sup>1</sup>

On May 12, 2014, the Commission issued a Notice of Commission Action that granted NorthWestern’s request to consolidate and hear the 2013 Electricity Supply Cost Tracking Adjustment with the soon to be filed 2014 Electricity Supply Cost Tracking Adjustment (the “consolidated docket”). NorthWestern subsequently filed in the consolidated docket its 2014 Application for (1) Approval of Deferred Cost Account Balances for Electricity Supply, CU4 Variable Costs, DGGS Variable Costs/Credits, and Spion Variable Costs; and (2) Projected Electricity Supply Cost Rates, CU4 Variable Rates, DGGS Variable Rates and Spion Variable

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<sup>1</sup> The Commission removed from NorthWestern’s interim rates \$1,419,172 associated with the replacement regulation services purchased by NorthWestern during the 2012 DGGS outage.

Rates for the tracker year from July 1, 2013 through June 30, 2014 (the “2014 Electricity Supply Cost Tracking Adjustment”).

On June 2, 2014, the Commission issued a Notice of Application and Intervention Deadline noting that those parties who were granted intervention in the docket for the 2013 Electricity Supply Cost Tracking Adjustment were parties in the consolidated docket, and that any other interested party could seek intervention in the consolidated docket by July 18, 2014. Over the objection of NorthWestern, the Commission granted general intervention to the MEIC/Sierra Club.<sup>2</sup> On June 17, 2014, the Commission granted interim rate relief, as requested by NorthWestern, for the 2014 Electricity Supply Cost Tracking Adjustment.

Only two Intervenors actively participated in the consolidated docket and opposed any aspect of NorthWestern’s implementation of its Electricity Supply Cost Tracking Adjustment, the MCC and MEIC/Sierra Club. As noted above, their primary contention is that the Commission should disallow prudently incurred replacement power costs because: (1) NorthWestern did not file a lawsuit to recover the replacement power costs from Siemens, and (2) NorthWestern did not have outage insurance when the forced outage occurred.

The consolidated docket proceeded to a contested case hearing held in Helena, Montana, on October 6-7, 2015. This Opening Brief is submitted in accordance with a Commission established briefing schedule.

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<sup>2</sup> Siemens Energy, Inc. and PPL Montana LLC requested and were granted limited intervention in this docket. These entities’ intervention was limited solely to the issue of seeking protective orders for information that they had identified as trade secret information subject to protection.

## C. WITNESSES

### 1. NorthWestern presented the testimony of four witnesses in its direct case.

Mr. Kevin J. Markovich, Director of Energy Supply Market Operations.

Mr. Markovich sponsored Ex. NWE-32 and NWE-33. He provided an overview of NorthWestern's electricity supply portfolio, including Demand Side Resources ("DSM") and the off-system hedging program. He showed how the various elements of the portfolio fit into the resource procurement plan previously approved by the Commission.

Mr. Frank V. Bennett, Contract and Regulatory Specialist.

Mr. Bennett sponsored Ex. NWE-1 through Ex. NWE-15. He provided the myriad detail of the various costs included in the consolidated tracking dockets.

Mr. Joe Schwartzenberger, Director of Regulatory Affairs.

Mr. Schwartzenberger sponsored Ex. NWE-16 through Ex. NWE-20. He adopted the pre-filed testimony of Mr. William Thomas, which had been prepared and submitted by Mr. Thomas in the consolidated docket before he retired. Mr. Thomas supported the DSM element in the portfolio, as well as the lost revenue adjustments made in accordance with the Commission's previously authorized Lost Revenue Adjustment Mechanism ("LRAM"). Mr. Schwartzenberger also updated those costs and lost revenues.

Mr. Joseph Janhunen, Senior Analyst, Regulatory Affairs Department.

Mr. Janhunen sponsored Ex. NWE-21 through Ex. NWE-31. Mr. Janhunen adopted the pre-filed testimony of Ms. Cheryl Hansen, which had been prepared and submitted by Ms. Hansen in Docket No. D2013.5.33 before she retired. He also prepared and filed similar testimony on the same subjects in Docket No. D2014.5.46. Mr. Janhunen supported the derivation of the rates developed in accordance with the protocols for the Electricity Supply Cost Tracking Adjustment.

2. The MCC presented the testimony of two witnesses in its case.

Dr. John Wilson, consultant.

Dr. Wilson presented two arguments to the Commission. The first was a proposal to disallow the replacement power costs incurred during the forced outage at CU4, on the grounds that NorthWestern should sue Siemens for recovery of the replacement power costs, and because NorthWestern did not have outage insurance. The second was a proposal to eliminate the LRAM previously authorized by the Commission.

Mr. George Donkin, consultant.

Mr. Donkin proposed that the Commission terminate NorthWestern's off-system Mid-C hedging program and prohibit NorthWestern from acquiring any new firm fixed price contracts effective as of November 18, 2014, when NorthWestern announced that it had closed on the acquisition of the hydroelectric resources previously owned by PPL Montana.

3. MEIC/Sierra Club presented the testimony of one witness in its case.

Mr. David Schlissel, consultant.

Mr. Schlissel echoed Dr. Wilson's proposal to disallow the replacement power costs incurred during the forced outage at CU4, on the grounds that NorthWestern should sue Siemens for recovery of the replacement power costs, and because NorthWestern did not have outage insurance.

4. NorthWestern presented the testimony of seven witnesses in its rebuttal case.

Mr. James Goetz, attorney, retained expert.

Mr. Goetz, one of Montana's premier litigators, explained why NorthWestern had no viable cause of action against either Siemens or Talen Energy ("Talen") for consequential damages, which include replacement power costs. His testimony is Ex. NWE-36.

Mr. Fred Lyon, attorney, retained expert.

Mr. Lyon, a nationally recognized attorney in the field of contracting in the electric power industry, explained that the contract provision in the contract between Talen and Siemens, which barred suit for consequential damages, including replacement power costs, was standard in the industry. He also explained that utility owners of fossil fueled generation stations typically do not contract for outage insurance because it is not a cost effective product over time. His testimony is Ex. NWE-37.

Mr. Ronald Halpern, retained consulting engineer.

Mr. Halpern was one of the two authors of the Root Cause Analysis (“RCA”) which determined the likely cause of the 2013 forced outage at CU4. Both MCC witness Wilson and MEIC/Sierra Club witness Schlissel relied upon the RCA in rendering their opinions that NorthWestern should sue Siemens. Mr. Halpern showed how they misinterpreted and misapplied the RCA. His testimony is Ex. NWE-38.

Mr. Robert Ward, retained consulting engineer.

Mr. Ward was the second of the two authors of the RCA which determined the likely cause of the 2013 forced outage at CU4, and upon which MCC witness Wilson and MEIC/Sierra Club witness Schlissel relied in rendering their opinion that NorthWestern should sue Siemens. Mr. Ward also showed how they misinterpreted and misapplied the RCA. His testimony is Ex. NWE-39.

Mr. Michael Barnes, Superintendent of Joint Owned Thermal Operations.

Mr. Barnes showed how CU4 has been a reliable generating facility since it was put into commercial operation. He prepared and presented a study which showed why outage insurance is not a cost effective product for fossil fueled generating stations owned by utilities. The study

established that NorthWestern would have paid more for outage insurance over time than it would have received as insurance proceeds. His testimony is Ex. NWE-40.

Mr. Pat Corcoran, Vice President of Government and Regulatory Affairs.

Mr. Corcoran explained the mandatory nature of the electricity supply cost adjustment mechanism, and why replacement power costs needed to be reflected in that mechanism. He also addressed the important reasons behind the Commission's previous authorization of the LRAM. His testimony is Ex. NWE-35.

Mr. Kevin Markovich.

Mr. Markovich, who also testified on direct, explained why the Commission should continue its authorization of NorthWestern's hedging program, even though NorthWestern has not entered into any new firm fixed price contracts off-system at Mid-C, since November 18, 2014. He explained that while the acquisition of the hydro facilities rendered unnecessary additional hedges at the current time, hedge transactions should continue to be part of an overall resource procurement plan on a going forward basis. His rebuttal testimony is Ex. NWE-34.

## ISSUES

The issues in this docket are:

- (1) Whether the Commission can disallow prudently incurred replacement power costs from the Electricity Supply Cost Tracking Adjustment because NorthWestern did not sue Siemens for recovery of the replacement power costs;
- (2) Whether the Commission can disallow prudently incurred replacement power costs from the Electricity Supply Cost Tracking Adjustment because NorthWestern did not have outage insurance when the forced outage at CU4 occurred;

- (3) Whether the Commission should terminate NorthWestern's off-system hedging program, and<sup>3</sup>
- (4) Whether the Commission can expand the category of costs to be included as electricity supply costs.

## FACTS

CU4 is a 740 megawatt (net) coal fired generation station located in Colstrip, Montana. It is one of four mid to large sized coal fired generating stations which make up the Colstrip Project. The total net generating capacity of the Colstrip Project is 2,094 megawatts ("MW"). Five public utilities and PPL Montana, Inc., now Talen, own various shares of the Colstrip Project. Talen has the largest total share and is the operator of the Colstrip Project, including CU4.

NorthWestern has a 30% ownership share in CU4, or 222 MW. Under what is called the Reciprocal Sharing Agreement between the owners of Colstrip Units 3 and 4, each owner has reciprocal rights in the other unit equal to half of its ownership share. Tr. 243-245. Under that agreement, NorthWestern effectively has the right to 111 MW of the output of Colstrip Unit 3, and 111 MW of the output of CU4. *Id.*

CU4 was constructed in the early 1980s and placed into service on December 15, 1985. Ex. NWE-38, internal Exhibit \_\_ (RAH-4) at p. 3. Both the turbine and the generator at the unit were manufactured by Westinghouse, now Siemens. It is standard industry practice to have the original equipment manufacturer ("OEM") do maintenance and repair work on a turbine and generator because of its intimate knowledge of the design and construction of them. Ex. NWE-38

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<sup>3</sup> The LRAM issue addressed by MCC witness Dr. Wilson is now moot, as the Commission adopted the MCC position in a recently issued order in another docket. Order 7375a entered in PSC Docket No. D2014.6.53.

at pp. 11-12, and internal Exhibit \_\_ (RAH-4) at 42. Westinghouse has designed and constructed hundreds of generators like CU4, and the reliability of the units has been very good. *Id.* at 10.

The reliability of CU4 has also been good. Until the forced outage in July of 2013, there had been only one significant problem with the generator, which occurred in 1987. Ex. NWE-39 at pp. 5-6. As is the case for any large scale generator, smaller repair issues occurred through time, but none implicated the generator core. *Id.* at pp. 6-8. In 2009, a blade on one of the steam turbines which drive the generator developed a small crack, which resulted in a lengthy forced outage, but that issue also had no relationship to the integrity of the generator or its core. *Id.* at p. 8.

Because of the Reciprocal Sharing Agreement, NorthWestern's share of the Colstrip Project has had a very favorable Equivalent Availability Factor ("EAF"), even with the 2009 and 2013 forced outages at CU4. Ex. NWE-40 at pp. 5-6. The North American Electric Reliability Corporation's GADS report (Generation Availability Data System) indicates that coal fired generating units similar in size to Colstrip Units 3 and 4 operated with an average EAF of 82.81% during the period 2009 to 2013. *Id.* at p. 8. Because of the Reciprocal Sharing Agreement, during that same period of time, Colstrip Units 3 and 4 operated with an EAF of 81%, even with the 2009 and 2013 outages at Colstrip Unit 4. *Id.*

In 2006, Talen, as the operator of the Colstrip Project, entered into a service contract with Siemens, the OEM of the generator at CU4. Ex. NWE-36 at p. 5. Under the service contract, Siemens performed routine inspection and maintenance work at CU4 beginning May 5, 2013. *Id.* at p. 3. In 2013, its maintenance and inspection routine involved what is called a "rotor out" inspection. The rotor weighs approximately 50 tons. Tr. 178. In a rotor out inspection, the rotor is removed from the core of the generator so that both core and rotor can be examined for

any imperfections that need to be fixed. Tr. 174. It is state of the art testing to test the laminations in a generator core through what is called an “El Cid” test (Electromagnetic Core Imperfection Detector). Tr. 150. After the rotor was removed, three El Cid tests were conducted on the generator core which detected a small number of places in the core laminations which needed repair. Tr. 176. After the necessary repair work was done, the generator was reassembled, including the re-insertion of the rotor into the generator. *Id.*

The withdrawal and re-insertion of the rotor from the generator requires the use of what is called a “skid pan.” Once the rotor is re-inserted using the skid pan, what are called “air gap baffles” must be re-installed in the generator. Once the air gap baffles are installed, it is not possible to conduct an El Cid test. Tr. 177.

Reassembly of the generator at CU4 was completed and the generator returned to service on June 27, 2013. Ex. NWE-38, internal Exhibit \_\_ (RAH-4) at p. 3. A ground fault tripped the unit on July 1, 2013. *Id.* at p. 5. The ground fault was caused by melting within the core, which is believed to have begun almost immediately after the unit was returned to service, and eventually caused severe core failure. *Id.* It took seven months and \$26.5 million to repair the damage to the generator caused by the core failure. Ex. NWE-40 at p. 4. The cost of repairing the unit was covered by a policy of property insurance issued by FM Global. *Id.*

Mr. Halpern and Mr. Ward were retained by Talen to investigate the cause of the core failure. Ex. NWE-38 at p. 3. They determined in the RCA which they authored:

The cause of the failure was most likely inadequate interlaminar insulation permitting shorting between laminations caused during the prior outage by rotor insertion, skid pad damage or air gap baffle installation.

Ex. NWE-38, internal Ex. \_\_ (RAH-4) at p. 1.

The 2013 core failure at CU4 was a highly unusual occurrence. Ex. NWE-39 at p. 9. It was likely caused by a combination of inadequate lamination, which would have existed since the generator was manufactured in the 1980s, and damage caused from re-insertion of the rotor, removing the skid pad, or installing the air gap baffles during the 2013 maintenance. The suspected damage from the maintenance work was likely very subtle. Tr. 184. The circumstances behind the 2013 core failure at CU4 were so unusual that Mr. Halpern didn't think Siemens could have done anything differently to avoid what happened. Tr. 145. He testified:

This particular case on [sic] Colstrip has never happened before. Damage to the core happens infrequently. Of the thousands of generators out there, core damage is a very infrequent occurrence. Combined with the interlaminar insulation problem, it's never happened before.

Tr. 167-8.

The service contract under which Siemens performed the maintenance and repair work at CU4 contains a provision which expressly excludes liability for consequential damages such as the cost of replacement power. Ex. NWE-36, internal Exhibit \_\_ (JHG-1) at p. 7. Talen, not NorthWestern, was the plant operator, and the party in privity with Siemens. Ex. NWE-36 at p. 7. Additionally, the service contract expressly excluded third parties as beneficiaries under the contract. Tr. 309. As succinctly stated by NorthWestern witness Goetz:

It is my opinion that no such case [a lawsuit against Siemens] should be filed and, if filed, it would be unsuccessful....It would not have been prudent for NorthWestern to sue Siemens.

Ex. NWE-36 at p. 7. Mr. Goetz also testified that NorthWestern had no viable cause of action against Talen. *Id.* at pp. 9-10. FM Global, which provided property insurance for CU4, also declined to pursue a subrogation claim against Siemens. Ex. NWE-40 at p. 4.

With respect to outage insurance, NorthWestern witness Lyon testified:

Such insurance policies are expensive and may incorporate a large deductible with exclusions, policy limits, and restrictions on recovery based on market fluctuations. In light of the expense and the policy terms, utilities typically do not consider such policies to be cost effective and thus elect not to obtain such coverage in connection with equipment, construction or repair contracts for fossil fuel plants.

Ex. NWE-37 at p. 14. NorthWestern witness Barnes similarly testified that outage insurance was not a cost effective product. Ex. NWE-40 at pp. 8-10. Mr. Barnes prepared and sponsored a study based on quotes that NorthWestern received for outage insurance that showed that the payouts under such policies for the 2009 and 2013 forced outages would have been dwarfed by the premiums paid for such insurance during its ownership of CU4. *Id* at internal Exhibit \_\_ (MJB-2).

## LEGAL STANDARDS

### A. ELECTRICITY SUPPLY COST RECOVERY

The recovery of prudently incurred electricity supply costs does not rest in the discretion of the Commission. It is statutorily mandated: “The commission shall establish an electricity cost recovery mechanism that allows a public utility to fully recover prudently incurred electricity supply costs...” § 69-8-210, MCA. Unless the Commission has an evidentiary basis for determining that the replacement power costs were imprudently incurred, it is legally obligated to allow NorthWestern to fully recover them in its final order in this case.

### B. THE PRUDENCE STANDARD

The Commission has defined prudence as “marked by wisdom or judiciousness[,] circumspect or judicious in one’s dealings; cautious.” In *In re Montana Power Co.*, 218 P.U.R.4<sup>th</sup> 277, 287; Order No. 6382d, Commission Docket No. D2001.10.144, July 21, 2002, (internal quotations omitted). The Commission also has cited to the Montana Supreme Court’s decision in *Sundheim v. Reef Oil Corporation*, 247 Mont. 244, 806 P.2d 503 (1991), for the

definition of prudence. The Supreme Court in that case defined prudence as a reasonable man engaged in a similar business. *Sundheim* at 247 Mont. 255. Recognizing that a prudence determination is not to be made with the benefit of hindsight, the Commission has indicated that “[i]n determining whether NorthWestern acted prudently...the [Commission] must look to what [NorthWestern] knew or should reasonably have known at the time.” Order No. 6921c, ¶ 100, Consolidated Docket Nos. D2008.5.45/D2009.5.62 (May 20, 2010).

The prudence standard has been well described by the Federal Energy Regulatory Commission (“FERC”). In *New England Power Co.*, 31 FERC 61047, 60184 (1985), FERC held:

managers of a utility have broad discretion in conducting their business affairs and in incurring costs necessary to provide services to their customers. In performing our duty to determine the prudence of specific costs, the appropriate test to be used is whether they are costs which a reasonable utility management (or that of another jurisdictional entity) would have made, in good faith, under the same circumstances, and at the relevant point in time. We note that while in hindsight it may be clear that a management decision was wrong, our task is to review the prudence of the utility's actions and the costs resulting therefrom based on the particular circumstances existing either at the time the challenged costs were actually incurred, or the time the utility became committed to incur those expenses.

Prudence is to be determined by looking at what the utility knew at the time it had to act. *See, e.g. Re Southern California Edison Co.*, 116 P.U.R.4th 365, 374 (Cal. PUC Sept. 25, 1990) (“Namely, the event or contract is to be reviewed based on facts that are known or should be known by utility management at the time. This standard is used to avoid the application of hindsight in reviewing the reasonableness of a utility decision.”); *Re Wisconsin Public Service Corp.*, 86 P.U.R.4th 357, 375 (Wis. PSC July 9, 1987) (“Hindsight may not be relied on by the commission in answering the prudence question.”); and *Re Long Island Lighting Co.*, 71

P.U.R.4th 262, 267 (N.Y. PSC November 16, 1985) (“Thus, in evaluating prudence, we must ask whether the company acted reasonably under all the circumstances at the time.”).

Additionally, in prudence determinations, the Commission must find that it was the imprudent act which caused the harm to the utility’s customers. *See e.g. Atmos Energy Corp. v. Office of Public Counsel*, 389 S.W. 3rd 224, 228 (Mo. App. 2012). Phrased another way, there must be a causal link between the allegedly imprudent act and the costs at issue. *Violet v. FERC*, 800 F.2d 280, 283 (1st Cir. 1986).

### C. BURDEN OF PROOF

The burden of proof in a prudency challenge is on the utility, after an opposing party has made a prima facie showing of a lack of prudence. Costs incurred by a utility are presumed to be prudently incurred until challenged. *West Ohio Gas Company v. Public Utility Commission*, 294 U.S. 63, 72 (1935) (“Good faith is to be presumed on the part of the managers of a business.”) (citing to *State of Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service Commission of Missouri*, 262 U.S. 276, 288 (1923)). The Court of Appeals for the District of Columbia described this holding from *West Ohio Gas* “as a so-called ‘busting bubble’ presumption that vanishes once opponents of the expenditure make a showing of improvidence.” *Potomac Electric Power Co. v. Public Service Commission of District of Columbia*, 661 A.2d 131, 140 (D.C. Cir. 1995). As was aptly noted by Justice Brandeis, in his concurring opinion in *State of Missouri ex rel. Southwestern Bell Telephone Co.*,

[t]he term ‘prudent investment’ is not used in a critical sense....The term is applied for the purpose of excluding what might be found to be dishonest or obviously wasteful or imprudent expenditures. **Every investment may be assumed to have been made in the exercise of reasonable judgment, unless the contrary is shown.**

262 U.S. at 289, n.1 (1923) (Emphasis added).

The FERC and other state commissions have recognized this presumption when determining whether a utility's expenditures were prudently incurred. In *Minnesota Power & Light Company*, 11 FERC ¶ 61,312 at 61,645 (1980), FERC stated that "where some other participant in the proceeding creates serious doubt as to the prudence of an expenditure, then the applicant has the burden of dispelling these doubts and proving the questioned expenditure to have been prudent." The Vermont Public Service Board ("VPSB") also provides for the presumption in prudence cases. In *Re: Central Vermont Public Service Corporation*, 83 PUR4th 532, 566 (Vt. P.S.B. 1987), the VPSB stated that

a utility seeking a rate increase bears the burden of persuasion on the question of whether expenditures claimed to support the rates were reasonable and prudent [citation omitted]. We further noted that a utility enjoys a presumption that its expenditures were, in fact, reasonable and prudent, and that the presumption alone is sufficient to satisfy its burden. The presumption is rebuttable, however, and it is rebutted if an adverse party adduces evidence sufficient to support a finding contrary to the effect of the presumption. Once such evidence is introduced, the presumption entirely disappears and has no further effect. The utility is then left with the task of persuading the [VPSB], as the trier of fact, of the reasonableness of its expenditures through the presentation of evidence of the ordinary sort.

See also *Long Island Lighting Co. v. Public Service Commission of New York*, 134 A.D.2d 135, 144 (3rd Dept. 1987) ("Historically, utility expenditures initially have been assumed to be exercises of reasonable managerial judgment."); *Gulf States Utilities Co. v. Louisiana Public Service Commission*, 578 So.2d 71, 85 (1991).

## ARGUMENT

- I. There has been no challenge to the prudence of NorthWestern's purchase of replacement power.

Neither the MCC nor MEIC/Sierra Club challenged the prudence of NorthWestern's purchase of replacement power due to the 2013 forced outage at CU4. There was no basis for such a challenge. Once the forced outage occurred, NorthWestern was bound by its obligation as

a public utility to acquire the electric power needed to meet its customers' needs. Accordingly, neither the MCC nor MEIC/Sierra Club challenged the amount of replacement power purchased by NorthWestern, or what it paid for the power.

The best estimate of the cost paid by NorthWestern for the replacement power is approximately \$8.2 million. Ex. NWE-34 at pp. 10-12.

II. It was not imprudent for NorthWestern not to sue Siemens or Talen for the cost of replacement power.

Dr. Wilson and Mr. Schlissel both opined that NorthWestern should have given consideration to suing Siemens for the cost of replacement power. Dr. Wilson also threw in a reference to suing Talen. Ex. MCC-4 at p. 13. Dr. Wilson, an economist, has no legal experience or training which would qualify him to provide such an opinion. Although Mr. Schlissel is a lawyer, he is not a practicing lawyer. He is a consultant with no real world experience in litigating damage claims. Tr. 359-64.

In sharp contrast, Mr. Goetz is one of Montana's premier litigators. He did what any good litigator would do – he examined whether the potential defendant(s) had affirmative defenses which would effectively bar recovery by NorthWestern. He testified unequivocally that NorthWestern did not have viable claims against either Siemens or Talen for its cost of replacement power.

Article 81 of the service contract under which Siemens did the maintenance and repair work at CU4 expressly excludes liability for consequential damages such as replacement power. Ex. NWE-35, internal Exhibit\_\_ (JHG-1) at p. 7. Article 81 expressly defines consequential damages as including the cost of replacement power. *Id.* Moreover, as explained by Mr. Goetz, NorthWestern is not a party to the service contract, and there is no privity between NorthWestern

and Siemens. Ex. NWE-36 at p. 7. Additionally, Article 72 of the contract disclaims any notion of third party beneficiaries. Tr. 309.

Both Dr. Wilson and Mr. Schlissel seem to suggest in their testimony that it was somehow imprudent for NorthWestern not to file a lawsuit instead of filing its Electricity Supply Cost Tracking Adjustment in accordance with Montana statute. If that inference is the real thrust of their advocacy, their testimony flies in the face of Montana statute. As indicated by Mr. Pat Corcoran, the possibility of a lawsuit does not magically render an electricity supply cost, for which there is mandatory recovery under Montana law, into something else. Ex. NWE-35 at p. 6. The Commission does not have the power or authority to ignore a clear statutory mandate based upon a misguided belief that NorthWestern should try and recover its electricity supply costs through ill-advised litigation.

NorthWestern was not imprudent in deciding not to file a lawsuit against Siemens or Talen for the cost of the replacement power.

III. It was not imprudent for NorthWestern not to have outage insurance for Colstrip Unit 4.

Dr. Wilson briefly mentions outage insurance and CU4 in his pre-filed testimony. Ex. MCC-4 at pp. 10-11, 17. Similarly, Mr. Schlissel briefly mentions outage insurance and CU4 in his testimony. Ex. MBIC/Sierra Club-1 at pp. 5, 19-21. Dr. Wilson admitted under cross examination that he had conducted no study into the cost effectiveness of outage insurance for a fossil fueled generating station. Tr. 341-342. Similarly, Mr. Schlissel admitted under cross examination that he had conducted no study into the cost effectiveness of outage insurance for a fossil fueled generating station. Tr. 372.

Implicit in the paucity of support they provided for their own positions is the fact that it is well known in the industry that outage insurance is not a cost effective product for fossil fueled generating stations. NorthWestern witness Lyon testified:

Such insurance policies are expensive and may incorporate a large deductible with exclusions, policy limits, and restrictions on recovery based on market fluctuations. In light of the expense and the policy terms, utilities typically do not consider such policies to be cost effective and thus elect not to obtain such coverage in connection with equipment, construction or repair contracts for fossil fuel plants.

Ex. NWE-37 at p. 14. NorthWestern witness Barnes similarly explained that outage insurance was not a cost effective product. Ex. NWE-40 at pp. 8-10. Mr. Barnes prepared and sponsored a study based on quotes that NorthWestern received for outage insurance that showed that the payout under such policies for the 2009 and 2013 forced outages would have been dwarfed by the premiums paid for such insurance during its ownership of CU4. *Id.* at internal Exhibit\_\_ (MJB-2). Mr. Barnes estimated that NorthWestern would have paid \$25.75 million in premium expense in those years to obtain \$10.6 million in insurance benefits for the 2009 and 2013 outages. *Id.* Mr. Barnes also testified at hearing: “it’s a long-held belief by me and a lot of my colleagues [that] if you hold [outage insurance] over the long term, it doesn’t ever pay because the premiums overwhelm any recovery that you’d otherwise get.” Tr. 254. Mr. Barnes also indicated that none of the other owners of CU4 had outage insurance on their respective shares of the unit when the 2013 outage occurred at CU4. *See* NorthWestern’s Responses to Data Requests MEIC-39 and MEIC-47(c) and (d).

Consistent with the rest of the industry, NorthWestern knew that outage insurance was not cost-effective. Tr., p. 260: (“But over the long term, I [Michael Barnes] don’t believe...that insurance is a good investment over time.”). Even “before Colstrip was

placed [in rates in 2009], we never considered outage insurance either...we never had it when the shareholders were at risk.” Tr. 259.

Both Dr. Wilson and Mr. Schlissel seem to suggest that the cost effectiveness of outage insurance is irrelevant, and that it is the timing of the inquiry which is somehow controlling. That is a celebration of form over substance, and cannot reasonably be elevated to a finding of imprudence. If the existence or non-existence of outage insurance determines the prudence of NorthWestern’s actions with respect to the 2013 outage at CU4, the cost effectiveness of such insurance is necessarily the controlling consideration.

It was not imprudent for NorthWestern not to have outage insurance during the 2013 forced outage at CU4.

IV. The termination of NorthWestern’s off-system hedging program proposed by MCC witness Donkin is likely moot.

MCC witness Mr. George Donkin proposed in these consolidated dockets that the Commission end NorthWestern’s off-system hedging program, effective November 18, 2014, the date that NorthWestern announced that it had closed on the acquisition of PPL Montana’s hydroelectric facilities. Ex. MCC-3. NorthWestern opposed his advocacy in this docket. Ex. NWE-34 at pp. 3-10. However, NorthWestern acknowledged that the need to mitigate price volatility through hedging had declined because of the hydro acquisition and indicated that it had not entered into any new firm fixed price purchases at Mid-C since it had acquired the hydros. *Id.* at p. 9. NorthWestern’s opposition to Mr. Donkin’s advocacy was based on NorthWestern’s belief that the hedging program, which has consistently been part of NorthWestern’s Commission approved resource

procurement plans, should be maintained in principle to accommodate future changes in loads and resources. *Id.* at pp. 7-8.

This issue is now likely moot. Because of the length of time these consolidated dockets have been pending, another Electricity Supply Cost Tracking Adjustment has been filed. Docket No. D2014.7.58. NorthWestern and the MCC have executed and filed a Stipulation in that docket (Appendix 1 attached) which includes an agreement that the Commission can end NorthWestern's hedging program, despite it being part of the resource procurement plans. The Stipulation is structured such that if it is approved by the Commission in that docket, it would have the same effect as if ordered in this docket.

V. The Commission has authority to expand the category of expenses that can be included in the Electricity Supply Cost Tracking Adjustment.

The question has arisen whether the Commission can expand the category of expenses that can be included in the Electricity Supply Cost Tracking Adjustment. Two positions of the parties have apparently raised the question. First, the MCC and MEIC/Sierra Club complained that the savings in labor costs arising from the furlough of Talen employees because of the 2013 forced outage was not reflected in the Electricity Supply Cost Tracking Adjustment. Ex. MCC-4 at pp. 16-17. Ex. MEIC/Sierra Club-1 at pp. 21-23. As explained by NorthWestern witness Corcoran, the theory of their complaint is contradicted by a prior Commission decision when NorthWestern unsuccessfully tried to include an upward change in labor costs related to electric supply in an Electricity Supply Cost Tracking Adjustment. Ex. NWE-35 at pp. 7-9. Order No. 6682d, FOF 70-72, entered in Docket No. D2005.5.88.

Secondly, Mr. Corcoran indicated in his testimony that if the Commission was truly worried about NorthWestern trying to double recover the cost of replacement power

– first from its customers in these consolidated trackers, and later in a subsequent lawsuit against Siemens – all it had to do was to include in its final order in the case a provision that any subsequent recovery from Siemens has to be credited back to ratepayers through the deferred account in the Electricity Supply Cost Tracking Adjustment. Presumably, neither the MCC nor the MEIC/Sierra Club would be opposed to such a provision.

The narrow question of whether the Commission has the power to expand the category of costs to be included in the Electricity Supply Cost Tracking Adjustment must be answered in the affirmative. It clearly does: “The commission may include other utility costs in and expenses in the cost recovery mechanism if it determines that including additional costs and expenses is reasonable and in the public interest.” § 69-8-210(1), MCA. The broader question of whether the phrase “additional costs and expenses” can be interpreted to mean on a net basis is interesting, but is not necessary to answer in this case. Clearly, the MCC and the MEIC/Sierra Club will not object to the Commission following NorthWestern’s suggestion that the Commission include an express provision in its final order requiring NorthWestern to include in the deferred account for the Electricity Supply Cost Tracking Adjustment any subsequent recovery from Siemens. Just as clearly, NorthWestern would be equitably estopped from later challenging the validity of such a provision, having expressly proposed it in this case.

## CONCLUSION

NorthWestern is entitled under the provisions of § 69-8-210(1), MCA, to the recovery in this consolidated docket of the replacement power costs it incurred because of the 2013 forced outage at CU4. Neither the MCC nor MEIC/Sierra Club challenged the prudence of NorthWestern's purchase of the replacement power.

It was not imprudent for NorthWestern not to file a lawsuit against Siemens or Talen for the recovery of the replacement power costs. Moreover, even if it had a viable claim against Siemens or Talen, the existence of such a claim would not change the character of the replacement power costs as recoverable electricity supply costs.

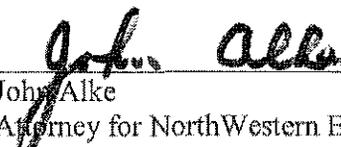
It was not imprudent for NorthWestern not to have outage insurance for CU4. Outage insurance is not a cost effective product for a utility's fossil fueled generating stations. The cost of the insurance over time quickly eclipses the benefits of any recovery under the insurance.

NorthWestern is entitled to a final order of the Commission in the consolidated docket which makes final the interim rate relief previously granted.

Respectfully submitted this 24<sup>th</sup> day of November 2015.

NORTHWESTERN ENERGY

By:

  
John Alke

Attorney for NorthWestern Energy



Docket, authorizing interim rates as requested in NorthWestern's Application.

4. On October 15, 2015, the Commission issued Final Order No. 7375a in Docket No. D2014.6.53 (the "LRAM Order"). In the LRAM Order, ¶ 67, the Commission ordered that "[e]ffective December 1, 2015, NorthWestern may not recover any lost revenues through electric and gas supply rates." NorthWestern is permitted to "propose to true-up lost revenues that were actually and prudently incurred from July 1, 2015 through November 30, 2015." LRAM Order, ¶ 69. As required by the LRAM order, NorthWestern will make a compliance filing which removes lost revenues from its electric rates effective for service rendered on and after December 1, 2015. A one-time true-up of LRAM revenues for the period July 1, 2015, through November 30, 2015, will occur in the next annual true-up of the electric supply cost tracking adjustment.

5. NorthWestern has represented in PSC Dockets D2013.5.33 and D2014.5.46 that it has not entered into any new off-system hedge transactions since November 18, 2014 when the PSC issued its PSC Order 7323k entered in PSC Docket No. D2013.12.85.

6. A fair and equitable resolution of the issues in this Docket, which would result in the establishment of just and reasonable rates, would be:

- a. The Commission's issuance of a final order in this Docket approving NorthWestern's Application, subject to the modification set forth in subparagraph 6 (b), and subject to the conditions set forth in subparagraphs 6(c) and 6 (d).
- b. The requested increase in rates set forth in NorthWestern's Application will be decreased by \$650,430, to implement the proposal of the MCC to reduce the requested rate increase by the difference between the amount of PTCs actually received by NorthWestern in 2012 through 2014, and claimed in its income tax returns for those years, and the amount of PTCs reflected in NorthWestern electric

rates during the same period of time. The reduction will be implemented by a one-time reduction of the deferred account for Spion K.op, to be reflected in the earliest practical monthly tracking adjustment filing occurring after the issuance of a final order in this docket.

- c. NorthWestern will make the compliance filing described in paragraph 4 above.
- d. NorthWestern will not make any new purchases of fixed price, firm power, for purposes of hedging the costs of purchased power, without first seeking and obtaining the approval of the Commission to make such purchases. However, nothing in this subparagraph prohibits NorthWestern from either selling power at Mid-C under power purchase agreements executed prior to November 18, 2014, or from purchasing power at Mid-C for use by its end use customers if economical to do so. For purposes of this subparagraph, the term "new purchases" shall mean after November 18, 2014.

7. NorthWestern and the MCC present this Stipulation as a reasonable settlement of the contested issues in this Docket. No party's position in this Docket is accepted by the other party by virtue of their entry into this Stipulation, nor does it indicate their acceptance, agreement, or concession as to the validity of any particular theory or rate making principle or legal principle embodied, or arguably embodied, in this Stipulation. Furthermore, no parties hereafter shall be deemed to be bound by any asserted position, and no finding of fact or conclusion of law, other than those agreed to herein, shall be deemed to be implicit in this Stipulation.

8. The entry of an Order by the Commission approving this Stipulation shall not be deemed to work any estoppel upon any party or to otherwise establish or create any limitation on or precedent of the Commission.

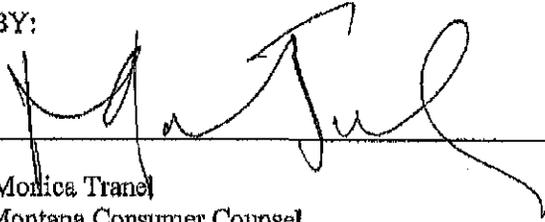
9. This Stipulation shall not become effective and binding upon the parties and shall be of no force and effect unless and until accepted and approved by the Commission as to all of the terms and conditions contained herein, without modification. If the Commission declines to approve this Stipulation as agreed to herein by the parties, or if the Commission adds or removes any terms or conditions not agreeable to the parties, either party shall, at its sole option, have the right to withdraw from this Stipulation with all of its rights reserved. The Stipulation and all its parts shall then be null and void, and the parties shall not be bound by any provision of it, and it shall have no force or effect whatsoever. In such event, the existence or terms of this Stipulation shall not be admissible in any proceeding before the Commission or any court for any purpose.

10. This Stipulation is a settlement between the parties and is not and shall not be used as evidence in other proceedings regarding any issue involved in this Stipulation.

11. This Stipulation may be executed in one or more counterparts and each counterpart shall have the same force and effect as an original document, fully executed by the parties. Any signature page of this Stipulation may be detached from any counterpart of this Stipulation without impairing the legal effect of any signatures thereon, and may be attached to another counterpart of this Stipulation identical in form hereto but having attached to it one or more signature page(s).

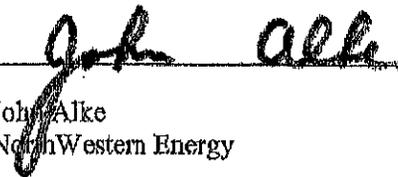
IN WITNESS WHEREOF, the parties hereto below have executed this Stipulation on the  
17th day of November, 2015.

BY:



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Monica Tranel  
Montana Consumer Counsel



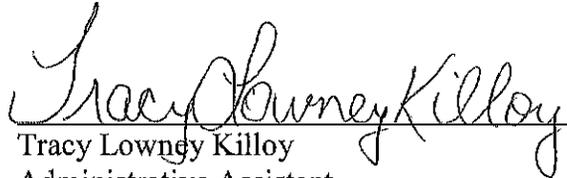
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John Alke  
NorthWestern Energy

**CERTIFICATE OF SERVICE**

I hereby certify that a copy of NorthWestern Energy's Opening Post-Hearing Brief in Docket Nos. D2013.5.33/D2014.5.46 has been hand delivered to the Montana Public Service Commission and to the Montana Consumer Counsel this date. It has been e-filed on the PSC website, emailed to counsel of record, and served on the most recent service list by mailing a copy thereof by first class mail, postage prepaid.

Date: November 24, 2015

A handwritten signature in cursive script that reads "Tracy Lowney Killoy". The signature is written in black ink and is positioned above the printed name and title.

Tracy Lowney Killoy  
Administrative Assistant  
Regulatory Affairs

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D2013.5.33/D2014.5.46  
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