

# Memo

**To:** Pat Fahn  
**From:** Mike Diller  
**Date:** December 4, 2006  
**Re:** Airforce Gas Distribution Privatization (Case No. PU-06-470)

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I have reviewed the financial projections of Montana-Dakota Utilities Co. (MDU) with regard to acquiring the gas distribution system of Minot Air Force Base (MAFB). I believe the acquisition will not harm existing MDU customers and should be approved. In addition, the commission should require that the low cost debt provided by the MAFB be wholly and directly assigned to North Dakota.

I was initially concerned with the age and quantity of steel pipes (installed in 1961) as staff would not support MDU acquiring a delapidated system that would require funds from existing ratepayers to fix it. However, the deal has been structured to include a transition fee from MAFB for any immediate and necessary improvements. In addition, the new tariff along with the projected cost to provide service will provide an adequate return on investment to cover future improvement needs.

Please note that I have some concern over the tracking of this investment with the low cost of debt provided by the MAFB. If the 6% debt is simply folded into MDU's total capital structure, very little of the low cost debt will be assigned to MDU's North Dakota gas operations. For example, in 2005, MDU's capital structure was \$356 million compared to the gas operations total rate base of \$89 million. Further, North Dakota's rate base is only \$22 million. Without direct assignment of this low cost debt to MDU's North Dakota gas operations, very little of the debt would be assigned to North Dakota gas operations. I estimate that direct assignment of this debt will lower North Dakota's cost of service by \$40,000 in year one.