

Memo

To: Pat Fahn

From: Mike Diller

Date: January 31, 2007

Re: Air Force Gas Distribution Privatization (Case No. PU-06-470)

On January 10, 2007, the commission held an informal hearing on the above referenced case and I was unable to attend. However, it is my understanding that Rita Mulkern of Montana-Dakota Utilities Co. disputed a conclusion in my memo dated December 4, 2006, claiming the estimated savings of \$40,000 was too high. As you recall, my memo advocates establishing the customer provided debt as wholly belonging to North Dakota.

Rita's conclusion is based on an updated cost of capital structure for 2006, among other things, concluding that the savings would only be \$15,790. I can dispute her conclusions too but from a policy standpoint, the amount of the savings is not relevant. However, to be clear, the savings will vary from year to year and diminish over time as the low cost debt provided by the Air Force is extinguished.

From discussions with Rita after the informal hearing, my understanding is that the Company's angst is not so much with my estimated savings amount but with the precedent of setting aside a particular debt for North Dakota's gas operations. Rita brought to my attention that the low cost pollution control bonds for its electric operations has always been reflected in the total utility capitalization structure benefiting both gas and electric operations and my recommendation in this case departs from past practice.

Staff is not too concerned about departing from past practice when doing so makes sense. However and in the spirit of cooperation, staff is agreeable to putting off the decision until the next rate case proceeding. Doing so would provide a more formal process for fully examining the issue.