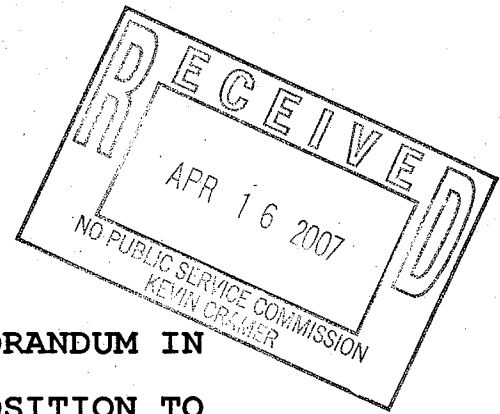


STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION



Otter Tail Corporation
Advance Determination of Prudence
Application

MEMORANDUM IN
OPPOSITION TO
MOTION IN LIMINE TO
EXCLUDE TESTIMONY

Montana-Dakota Utilities Co.,
a Division Of MDU Resources Group,
Inc.

Advance Determination of Prudence Case No PU-06-481
Application Case No PU 06-482

INTERVENORS' MEMORANDUM OF LAW IN OPPOSITION
TO MOTION IN LIMINE TO EXCLUDE TESTIMONY UNDER
NDCC 49-02-23.

SUMMARY OF ARGUMENT

The Public Service Commission should deny the relief requested in the Motion in Limine filed by Otter Tail Power ("OTP") and Montana Dakota Utilities ("MDU") (together "Applicants") on the following grounds:

1. The environmental externalities statute at NDCC 49-02-23 does not apply to Advance Determination of Prudence proceedings under NDCC 49-05-16;
2. Costs related to CO₂ regulation are no longer externalities but a pollutant, regulated by the EPA under the Clean Air Act, subsequent to a recent U.S. Supreme Court ruling; and

3. NDCC 49-02-23 must be stricken upon judicial review. Accordingly evidence relating to environmental externalities must be admitted to prevent a reversal for error of the PSC's eventual ruling in this prudence proceeding.

The PSC will further the stated goals of the North Dakota legislature and the interests of all North Dakota citizens in reaching this determination of the two statutes at issue.

Interveners submit the following:

1. NDCC 49-02-23 applies only to proceedings that existed at the time of its enactment and does not apply to an Advance Determination of Prudence proceeding under NDCC 49-05-16, a separate proceeding created by the Legislature ten years after enactment of NDCC 49-02-23.
2. Even if NDCC 49-02-23 did apply to Advance Determination of Prudence proceedings, the U.S. Supreme Court has declared CO₂ a pollutant and ordered its regulation by U.S. E.P.A. under the Clean Air Act. Massachusetts v. EPA, No 05-1120 (published April 2, 2007). Because the U.S. Supreme Court has classified CO₂ as a regulated pollutant, CO₂ no longer constitutes an environmental externality under the definition created by NDCC 49-02-23(2) ("The alleged costs of complying with future environmental laws or regulations that have not yet been enacted") and the associated costs of regulation must be considered by the PSC.
3. NDCC 49-02-23, the Environmental Externalities statute, must be stricken upon judicial review for the reasons stated below. Therefore evidence in support of an externality theory must be preserved in the evidentiary record and considered by the PSC to avoid reversal of agency decisions upon judicial review.

A prompt decision on Applicants' motion and this responsive brief will assist the parties and the panel by resolving pending discovery objections and trial issues.

Discussion of Legislative History

To assist the panel and all counsel in the matter copies of the legislative history of 49-02-23 and 49-05-16 are attached.

The U.S. Supreme Court has repeatedly explained that the canon of statutory interpretation is triggered only by uncertain statutory text, e. g., Garcia v. United States, 469 U. S. 70, 74-75 (1984); Gooch v. United States, 297 U. S. 124, 128 (1936), and that it can be overcome by, inter alia, contrary legislative history, e. g., Watt v. Western Nuclear, Inc., 462 U. S. 36, 44, n. 5 (1983).

The Motion in Limine argues that a 1995 statute (NDCC 49-02-23) should be applied to proceedings conducted pursuant to a 2005 statute (NDCC 49-05-16) that makes no reference to incorporating the requirements of the older statute. In such a situation the legislative history provides insight into proper interpretation of the statute.

The Partnership

The legislative history of NDCC 49-02-23 reminds the reader that North Dakota has a special relationship with the lignite coal industry. The North Dakota government website describes the partnership between the North Dakota Industrial Commission and the Lignite Research Council. The Legislature enacts legislation and appropriates funding for the program. The Lignite Research Council recommends policies for the funding of projects to the Industrial Commission, which approves policies and funding for projects. The web page describing the partnership is attached with the exhibits. The governor, attorney general and the agriculture commissioner of North Dakota are the three members of the Industrial Commission. An example of the Industrial Commission's work is found in a document available at the Lignite Energy Council Website. The Industrial Council authorized the expenditure of \$250,000 in state monies in 1995-96 to support lobbying and legal effort of the Lignite Energy Council in defeating the effort of Minnesota to apply externality costs on carbon to

North Dakota Lignite Coal. (Document is attached to this memorandum and is available on the Lignite Energy Council Website.)

The Legislature has repeatedly taken measures intended to protect the lignite industry from competition and from costs imposed by other states' regulation. The statutes at issue in this Motion in Limine, however, came about for unrelated reasons and have very different effects on the North Dakota lignite industry.

The Environmental Externalities statute was intended to protect the lignite industry from internalizing the cost of CO₂ emissions. The Advance Determination of Prudence statute was not intended to protect the lignite industry, but to ease access to financing and lower the cost of capital for utilities, regardless of their source of power or whether there was any discernible benefit to North Dakota.

Taken in this light, the Motion in Limine raises simple questions of what the Legislature truly intended to achieve in enacting these two separate statutes 10 years apart. The legislative history plainly shows that the Advance Determination of Prudence statute privileges North Dakota projects (not just lignite projects) by assigning them a presumption of prudence. The Legislature discussed allowing the proceeding only to North Dakota projects, but decided to allow it for any project that would provide power in North Dakota. At no point in the legislative history of NDCC 49-05-16 is there any discussion of the cost of CO₂ emissions, environmental externalities, or even of the lignite industry.

NDCC 49-02-23 Environmental Externalities

According to the testimony filed in support of HB 1312, this statute was proposed by members of the lignite industry in response to Minnesota legislation assigning a value to carbon emissions. Mr. John Dwyer of the Lignite Energy Council says as much:

[T]his statute is brought to protect North Dakota Lignite Coal from adverse effects of a decision of the MNPUC assigning an interim value to carbon dioxide of \$5.99 to \$13.60 per ton for coal fired plants.

Dwyer 1/16/95 testimony ("Dwyer") at 2. Minnesota requires these values to be used in evaluating the selection of resource options in generating electricity. Dwyer 2. Mr. Dwyer continues

Carbon dioxide emissions which occur when you burn any fossil fuel ... [The emissions] are not controlled because they are not classified as a pollutant.... Each ton of lignite generates about 1.4 tons of CO₂ carbon when burned.

Dwyer at 2,3.

See also Dwyer Exhibits 1, "Comparison of Lignite Energy & Wind Energy Without Externality Cost" and 2, "Comparison of Lignite Energy & Wind Energy With CO₂ Externality Cost", concluding that "with externalities, lignite loses."

The legislative history and Mr. Dwyer's testimony reveal that the Legislature, in enacting NDCC 49-02-23,

A. protected a North Dakota industry in competition across state lines and

B. protected a North Dakota Industry with an alternative source of power, wind generated electricity.

The Legislature's explicit intent, fervently supported by Mr. Dwyer and the Lignite Energy Council, was to protect lignite from the competition created by another state's decision to attach a cost to CO₂ emissions. The language of the statute reflects this plain intent:

49-02-23. Consideration of environmental externality values prohibited.

The commission may not use, require the use of, or allow electric utilities to use environmental externality values in the planning, selection, or acquisition of electric resources or the setting of rates for providing electric service. Environmental externality values are numerical costs or quantified values that are assigned to represent either:

1. Environmental costs that are not internalized in the cost of production or the market price of electricity from a particular electric resource; or
2. The alleged costs of complying with future environmental laws or regulations that have not yet been enacted.

The language of 49-02-23 that Applicants would have the PSC apply in this Prudence proceeding is the reference to "planning, selection, or acquisition of electric resources".

The most basic rule of statutory construction is that courts and agencies should look at a statute's plain language. This rule raises the question of how the PSC should read NDCC 49-02-23, which bars consideration of externalities. Yet the 1995-1996 legislature could not have contemplated the Advance Determination of Prudence proceeding, which would not come into existence for another ten years.

Another accepted principle of statutory construction is that an ambiguous statute should be construed in light of the statutory purpose. See Sony Corp. v. Universal City Studios, Inc., 464 U.S. 417, 431-432 (1984); see also United States v. Bacto-Unidisk, 394 U.S. 784, 799 (1969) ("[W]here the statute's language seem[s] insufficiently precise, the 'natural way' to draw the line 'is in light of the statutory purpose'") (quoting SEC v. Ralston Purina Co., 346 U.S. 119, 124-125 (1953)).

The Legislature that passed NDCC 49-02-23 could not have contemplated the Advance Determination of Prudence procedure that another Legislature would create a decade later. The later Legislature (2005) does not reference NDCC 49-02-23 in enacting the Advance Determination of Prudence statute. The PSC must therefore attempt to ascertain the Legislature's purpose in enacting both statutes.

Nothing in the legislative history suggests that NDCC 49-02-23 anticipated or was intended to apply to NDCC 49-05-16, the Advance Determination of Prudence statute, which came into existence 10 years later for reasons unrelated to the enactment of NDCC 49-02-23.

Intervenors shall demonstrate, the Advance Determination of Prudence legislation had an entirely different goal, one that would be undermined - perhaps to the detriment of the lignite industry - if NDCC 49-02-23 were applied to this proceeding.

NDCC 49-05-16 Advance Determination of Prudence

This statute was introduced to the Legislature as HB 1324, a measure intended to provide greater economic certainty to investors in new energy generation facilities. The Advance Determination of Prudence gives investors reassurance that energy generation projects, once financed and built, will be approved by the PSC and allowed to recoup their costs via commercial sales.

The legislative history of NDCC 49-05-16 is critical to determining whether or not the Environmental Externalities statute should apply in such a proceeding. The Lignite Energy Council was silent on the question. MDU, which offered testimony, made no reference to environmental externalities, but instead focused on separating the Advance Determination of Prudence proceeding from ratemaking.

HB 1324, an alternative draft of the present statute, entitled **Advance Determination of Prudence and Ratemaking Principles**, was rejected by the legislature. The adopted present NDCC 49-05-16 makes no reference to the rate making and rate determination powers of the PSC.

There was a deliberate effort on the part of the Legislature to create a separate and new procedure in response to utility concerns about increased costs related to uncertainty in the PSC approval process.

In his testimony, Dan Kuntz, Attorney for MDU, opposed combining the prudence proceeding with the ratemaking proceeding. Kuntz 4-12-05 Testimony on HB 1324 ("Kuntz Testimony") at pp. 2, 3.

The legislature accepted Mr. Kuntz's testimony and removed any requirement for a utility to file a ratemaking request with the Advance Determination of Prudence Application. The Lignite Energy Council expressed no concern with the language of NDCC 49-05-16, which neither incorporates NDCC 49-02-23 by reference nor creates language of its own regarding PSC consideration of environmental externalities in Advance Determination of Prudence.

The utility industry had an opportunity in direct testimony to the Legislature to request that HB 1324 incorporate the

Environmental Externalities statute, or include its own language about consideration of environmental externalities or the cost of anticipated regulation. MDU's Attorney explicitly requested that the Legislature make the Advance Determination of Prudence a new and separate proceeding, unrelated to ratemaking.

It is only just that the PSC should hold MDU to the bargain it made and rule NDCC 49-02-23 applies only to ratemaking proceedings, which it references explicitly, and that 49-02-23 does not apply to an Advance Determination of Prudence.

ARGUMENT

1. NDCC 49-02-23 does not apply to an Advance Determination of Prudence proceeding under 49-05-16. NDCC 49-02-23 explicitly references ratemaking cases and determinations.

It could not have encompassed an Advance Determination of Prudence because that procedure did not exist when NDCC 49-02-23 was enacted. The legislative history of 49-02-23 shows plainly that the statute was intended to apply to the type of comprehensive ratemaking proceeding that existed when 49-02-23 was enacted, in which lignite would be at a disadvantage if forced to internalize its environmental externalities.

The Legislature intended to create a separate proceeding independent of the ratemaking and rate determining authority of the PSC to determine prudence. There was every opportunity in 2005 for the Legislature to extend the reach of NDCC 49-02-23 to include Advanced Determination of Prudence proceedings. The Legislature did not do so, and in spite of ample opportunity, neither the utilities nor the lignite industry offered any objection.

The PSC does not have the authority to do what the legislature did not do, simply because it has received this Motion in Limine.

2. The U.S. Supreme Court has declared CO₂ a pollutant and ordered its regulation by U.S. E.P.A. under the Clean Air Act. Massachusetts v. EPA, No 05-1120 (published April 2, 2007). Because the U.S. Supreme Court has classified CO₂ as a regulated pollutant, it no longer constitutes an environmental externality under the definition created by NDCC 49-02-23(2): "The alleged costs of complying with future environmental laws or regulations that have not yet been enacted." The classification of CO₂ as a regulated pollutant means that the PSC is no longer barred from considering the anticipated cost of carbon regulation, which will have a reasonably predictable effect on consumers, an effect on which Interveners wish to offer testimony.

3. Ultimately, upon judicial review, the Environmental Externalities statute must be stricken for the following reasons:

NDCC 49-02-23 denies Interveners their constitutional right to access to the court "for any injury done [Interveners] in [their] lands, goods, person or reputation" for which Interveners have a right to "remedy by due process of law, and right and justice administered without sale, denial or delay." ND Constitution, Art. 1, Sec. 9. The PSC acts in this proceeding as the trier of fact and law, and if NDCC 49-02-23 is applied, Interveners will be denied constitutional rights of access to have their case fully heard.

NDCC 49-02-23 denies Interveners the right to present evidence of harm caused by applicants' proposal and by so doing denies interveners due process of law under the state and federal constitution. ND Const. Art. 1, Sec. 9; U.S. Const., 5th and 14th Amendments.

NDCC 49-02-23 denies Interveners the opportunity to present evidence that alternative energy produced by wind will produce lower rates once the cost of mitigation of carbon dioxide are included in the rate determination process.

NDCC 49-02-23 further sponsors the continued growth of coal-fired power generation without carbon management at

the expense of the development of carbon free electrical generation sources such as wind, which has created significant economic growth in neighboring states with policies more friendly to wind development.

NDCC 49-02-23 interferes inappropriately, harmfully, and beyond the authority of the State of North Dakota in the prudent planning of publicly and privately held corporations, cooperatives, and municipalities for the reasonably predictable future costs of carbon regulation, which will be passed on to shareholders and consumers who shall suffer economic damages thereby.

NDCC 49-02-23 violates the Full Faith and Credit and Commerce clauses of the U.S. Constitution by barring certain activities by corporations registered in other states and bound by laws requiring consideration of environmental externalities, and by usurping Congressional authority to regulate commerce among the states. U.S. Const. Art. IV Sec. I; Art. I, Sec. 8.

The canon of Constitutional avoidance holds that when "a statute is susceptible of two constructions, by one of which grave and doubtful constitutional questions arise and by the other of which such questions are avoided, our duty is to adopt the latter." United States ex rel. Attorney General v. Delaware & Hudson Co., 213 U.S. 366, 408 (1909).

For all of these reasons, an appropriate and lawful standard of review requires the PSC to hear testimony regarding the cost of carbon regulation, now ordered by the U.S. Supreme Court, prior to ruling on the prudence of Applicants' proposed investment.

CONCRETE EXAMPLES OF TESTIMONY PROFFERED

These abstract arguments become clear when applied to the type of evidence interveners seek to present.

As an example, I refer you to testimony of Sandy Tabor, General Counsel to Lignite Energy Counsel before the State Senate in opposition to SCR 4033.

SCR 4033 sought a study to make recommendations to the legislature on a combination of federal and state financial incentives of millions of dollars to enable Lignite Coal to mitigate carbon dioxide. Documents are attached.

Sandy Tabor's testimony announced to the legislature corporate resolutions approved by Lignite Energy on Global warming.

The Lignite Energy Council supports energy policies that encourage cost-effective Global greenhouse gas emission reductions rather than regional or national mandates

The Lignite Energy Council supports public and private investment in research and development on greenhouse gas emission reduction research technologies.

Sandy Tabor's testimony continues to describe the research efforts of Lignite energy including carbon sequestration projects which pipe and sell carbon dioxide to Canadian energy companies.

As an example, I refer you to facts discussed in an article in the Bismarck Tribune, "Carbon Managed Future" published April 15, 2007. The article describes a working carbon sequestration project by the Dakota Gasification Company in Mercer County ND, in which carbon dioxide is sequestered, piped and sold to Canadian energy companies. This article confirms that **this carbon sequestration project is now a \$10,000,000,00 annual sales opportunity.** Such streams of income, if captured, can positively effect ratepayers.

All the parties, attorneys, and panel members in this matter, the General Counsel of Lignite Energy Counsel, members of the legislature and the readers of the Bismarck Tribune know about global warming, carbon dioxide, and carbon mitigation costs. Yet applicants, MDU and OTP, will have us pretend in a prudence hearing that none of this evidence exists and that none of it could reasonably effect the ratepayer and interveners.

MDU and OTP prefer that such testimony be kept in the public forum only, in the Bismarck Tribune or before the legislature, but not in the hearing room record.

Conclusion

The PSC has authority it can exercise to hear the testimony on carbon mitigation and costs and the alternative remedies available to the Big Stone II project and how they effect North Dakota Ratepayers.

Why would North Dakota accept less than is available in North Dakota, from a South Dakota power plant, burning Wyoming coal, who wants to sell its power here?

Granting this Motion in Limine would harm North Dakota ratepayers for the benefit of an out-of-state power plant burning out-of-state coal. There is neither a legal nor a policy reason to exclude Interveners' proffered testimony. The ultimate prudence decision will remain with the PSC, so Applicants will not be harmed by denial of the Motion in Limine.

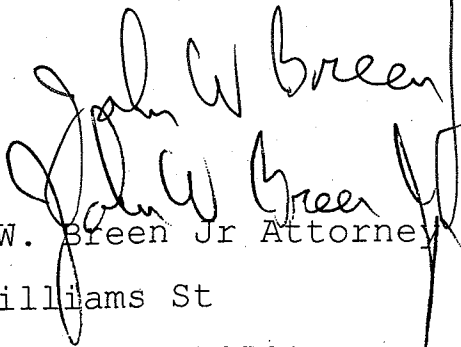
Accordingly the motion to exclude testimony concerning carbon regulation costs in a Prudence hearing should be denied.

Interveners

Mark Trechock and

Dakota Resource Council

By



John W. Breen Jr Attorney

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ND Bar ID 05492

By

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North Dakota

nd.gov Official Portal for North Dakota State Government



North Dakota Industrial Commission

Lignite Research, Development and Marketing Program
State Capitol, 14th Floor, 600 E Boulevard Ave. Dept. 405
Bismarck, ND 58505-0840
Phone: 701-328-3722 Fax: 701-328-2820

The Partnership

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The state/industry partnership includes the Industrial Commission, and the [Lignite Energy Council](#) which have entered into a partnership to administer the Lignite Research, Development and Marketing Program. Following is a quick explanation of how the program works:

The North Dakota Legislature enacts legislation and appropriates funding for the program. The [Lignite Research Council](#) recommends policies and funding for projects to the Industrial Commission. The Industrial Commission approves policies and funding for projects.

The Industrial Commission and the Lignite Energy Council administer the program and all Lignite Research, Development and Marketing Program projects.

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FY94-XVI-55
DEVELOPMENT & PRESENTATION OF EXTERNALITY INFORMATION
RELATING TO LIGNITE-BASED GENERATION
FOR MINNESOTA EXTERNALITY PROCEEDINGS

CONTRACTOR: Lignite Energy Council

PRINCIPAL INVESTIGATOR: John W. Dwyer
Phone: (701) 258-7117
Fax: (701) 258-2755

PARTICIPANTS

<u>Sponsor</u>	<u>Cost Share</u>
Lignite Energy Council	\$300,000
ND Industrial Commission	<u>250,000</u>
Total	\$550,000

Project Schedule - 2 Years

Contract Date - 7/13/94
Start Date - 6/1/94
Completion Date - 8/1/98

Project Deliverables

Status Report - 9/1/94 ✓
Status Report - 3/1/95 ✓
Status Report - 9/1/95 ✓
Final Report - 8/1/98 ✓

OBJECTIVE / STATEMENT OF WORK

The primary objectives of this project are to: 1) provide technical and legal support, 2) provide information and expert witnesses to contest the application of Minnesota externality interim and permanent values on lignite-produced electricity, 3) provide legal assistance to the State of North Dakota and the lignite industry in the Minnesota externality case proceedings, and 4) challenge and appeal inappropriate Minnesota externality values imposed on North Dakota's lignite industry. A goal of this project is to protect the lignite industry and the State from the use of inappropriate public policies, which would adversely impact the development and use of North Dakota's abundant domestic resource.

STATUS

The project involves collecting data, identifying expert witnesses and providing information for contested case proceedings and appeals. The Administrative Law Judge (ALJ) issued his Findings of Facts, Conclusions, Recommendation and Memorandum on March 22, 1996. The Minnesota Public Utilities Commission heard oral arguments on the proceedings on September 16-19, 1996.

The Findings of Fact, Conclusions, Recommendation and Memorandum issued by Administrative Law Judge Allan W. Klein dated March 22, 1996 made the following recommendations:

1. That the Commission establish the following ranges of environmental costs for criteria pollutants, to be used in proceedings subject to Minn. Stat. 216B.2422 (1994). Criteria pollutant values are limited to plants located within 200 miles of Minnesota's borders. These values are found in the table below.
2. That the Commission establish a range of \$0.28 to \$2.92 per ton as the environmental cost of carbon dioxide. The final Order of the Commission on 1/3/97 established a range of \$0.30 to \$3.10 per ton as the environmental cost of CO₂. In its 7/2/97 Order, the Commission confined the application of the values for CO₂ to electric generation located in Minnesota itself.
3. That the Commission specify what escalator should be used to escalate the above figures from 1993 dollars to current dollars at the time of filings under the statute.

Commission's Official Environmental Cost Table

The environmental values adopted by the Commission in its January 3, 1997 Order are stated in terms of 1995 dollars and revised in this Order after reconsideration to show 1) zero values for SO₂ starting after the year 2000 and 2) zero values for CO₂ beyond the borders of the State of Minnesota, as follows:

	<u>Urban</u>	<u>Metropolitan Fringe</u>	<u>Rural</u>	<u>Within 200 Miles of Minnesota</u>
SO ₂ (present to year 2000) \$/ton	112 - 189	46 - 110	10 - 25	10 - 25
SO ₂ (year 2000 and beyond) \$/ton	0	0	0	0
PM ₁₀ \$/ton	4,462 - 6,423	1,987 - 2,886	562 - 855	562 - 885
CO \$/ton	1.06 - 2.27	0.76 - 1.34	0.21 - 0.41	0.21 - 0.41
NO _x \$/ton	371 - 978	140 - 266	18 - 102	18 - 102
Pb \$/ton	3,131 - 3,875	1,652 - 1,995	402 - 448	402 - 448
CO ₂ \$/ton	.30 - 3.10	.30 - 3.10	.30 - 3.10	0

The final order by the Minnesota Public Utilities Commission is being appealed to the Minnesota Court of Appeals and a decision is to be issued sometime in May 1998. In its January 3, 1997 Order, the Commission limited the applicability of the range values established for CO₂ to within 200 miles of the Minnesota border. Major issues on appeal were the CO₂ values and the decision not to apply the CO₂ values to out-of-state generation resources. The State of North Dakota and the Lignite Energy Council asked the appellate court to affirm the Commission decision not to apply the CO₂ values to North Dakota's generation.

73123.0200

Sixtieth
Legislative Assembly
of North Dakota

SENATE CONCURRENT RESOLUTION NO. 4033

Introduced by

Senator Potter

Representative Glasheim

1 A concurrent resolution directing the Legislative Council to study federal-state initiatives to aid
2 the energy industry in its efforts to control carbon emissions and pollutants to maintain North
3 Dakota's good air quality.

4 **WHEREAS**, North Dakota currently meets all federal clean air standards; and

5 **WHEREAS**, changing federal policies are requiring installation of advanced air pollution
6 controls at existing and planned coal-fired electrical generating facilities; and

7 **WHEREAS**, there is a compelling federal interest in promoting energy production,
8 maintaining air quality, and lowering carbon dioxide emissions; and

9 **WHEREAS**, the lignite energy industry will be investing millions of dollars to install
10 advanced pollution controls to meet new federal requirements; and

11 **WHEREAS**, the cost of advanced pollution controls are measured in the hundreds of
12 millions of dollars; and

13 **WHEREAS**, federal environmental policies threaten the continued development of North
14 Dakota's coal resources; and

15 **WHEREAS**, there is a compelling state interest in maintaining good air quality and the
16 continued development of North Dakota's coal resources;

17 **NOW, THEREFORE, BE IT RESOLVED BY THE SENATE OF NORTH DAKOTA, THE**
18 **HOUSE OF REPRESENTATIVES CONCURRING THEREIN:**

19 That the Legislative Council study federal-state initiatives to aid the energy industry in its
20 efforts to control carbon emissions and pollutants to maintain North Dakota's good air quality;

21 and

22 **BE IT FURTHER RESOLVED**, that the Legislative Council report its findings and
23 recommendations, together with any legislation required to implement the recommendations, to
24 the Sixty-first Legislative Assembly.

Testimony of Sandi Tabor
Lignite Energy Council

SCR 4033
February 23, 2007

You have heard much in the news recently about global warming and legislative initiatives being pursued in Minnesota. The Lignite Energy Council takes these initiatives seriously. In fact, our board of directors approved the following resolution as our policy regarding global warming and climate change.

The Lignite Energy Council supports energy policies that encourage cost-effective global greenhouse gas emission reductions rather than regional or national mandates.

The Lignite Energy Council supports public and private investment in research and development on greenhouse gas emission reduction technologies.

In light of these policies we are supporting research projects dealing with air quality and carbon capture issues that are being conducted by the Energy & Environmental Research Center (EERC) in Grand Forks. I have included a list of the projects funded by the Lignite Research Council during the past biennium. As you can see, air quality and carbon emissions are a high priority. These studies are funded by the dollars appropriated from the coal severance tax to the Lignite Research Council. During the present biennium approximately \$2.8 million will be spent on research activities. It is important to note that the industry matches this investment dollar for dollar. In fact, in many cases industry's investment is as high as 6 to 1.

Through these efforts, North Dakota is one of only 12 clean air states. In addition, our sulfur dioxide (SO₂) emissions have dropped significantly since 1998, and we anticipate an even greater decrease by 2013.

We are also an active participant in the carbon-related research sponsored by the Department of Energy through the Plains CO₂ Carbon Reduction Partnership, better known as PCOR. The PCOR program is focusing on carbon sequestration issues. This program is funded through a combination of federal, state and private dollars.

We have also joined forces with Canadian public and private stakeholders to work on CO₂ reduction strategies. As part of its mission, the Canadian Clean Power Coalition is conducting research on coal gasification as a clean coal technology that may work with North Dakota lignite. The lignite industry has joined the coalition to support its research into gasification, advanced combustion and retrofit carbon dioxide capture technology. By so doing, our industry will gain access to the results of the coalition's research enabling our utilities to integrate the new data into

existing operations to further reduce CO₂ emissions either by retrofitting or by moving to new combustion technologies.

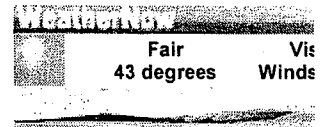
The lignite industry has a history of working to solve environmental issues, and we will continue our efforts. Just Wednesday the industry met with Senator Dorgan to discuss the federal carbon legislation. As our policy emphasizes, the carbon issue is one that must be dealt with at global level. It is far too complicated to have each state attempt to piecemeal a solution. As such, we believe that our work on carbon controls should be focused, and that it makes more sense to work with the Congressional delegation on this issue. As part of our cooperative effort, we will work to secure federal funding for research initiatives involving lignite coal. For that matter we will continue our partnership with the state to jointly fund research initiatives.

SCR 4033 calls for a study of federal-state initiatives to aid the energy industry in its efforts to control carbon emissions. While we appreciate the intent behind this resolution, we feel that our efforts must be focused on a federal initiative. As such, we are proposing to delete the references to carbon emissions from the bill.

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Sunday



News Brief

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• Home/Help

'A carbon-managed future'

Other L

• News

By LAUREN DONOVAN
Bismarck Tribune

These I
that ex

• Sports

COAL COUNTRY - Juries in sensational murder trials are sequestered away from outside contact, herded into the courtroom by day and locked tight in motels by night.

Northe-
enjoyin

• Outdoors

There are plans to do the same thing with carbon dioxide.

Womar
cops th

• Business

It's a gas, though. It won't get to go to courtrooms and motels.

Child a
respon
formin

• Entertainment Instead, it would get deep-sixed into the bowels of the earth, never to be seen again.

• Features

The gas is among those that contribute to the greenhouse effect that some scientists believe is warming the Earth's atmosphere.

More R

• Community

• Classifieds

It's not regulated as a pollutant, at least not yet.

State N

• Customer Service Center

Still, the Environmental Protection Agency estimates that 2 trillion tons of CO2 are emitted every year in this country by power plants, industrial sources and from vehicle exhaust pipes.

Local S

• Hot Deals

Sequestration is viewed as a one-key way to keep a lot of it from ever reaching the atmosphere.

Weathe

• Web Shopping

North Dakota accounts for 48 million of those tons and is relatively low on the CO2 totem pole. It gets higher on the totem pole because three-fourths of those tons come from coal-fired plants, or what's called a "single source," and therefore easier to identify and gather up.

Busine

Web Search:

Search

The millions of tons of CO2 emitted by tractors, semis and pickups in North Dakota and everywhere are impossible to gather.

Births/

Get daily headlines via e-mail:

Submit

Major single sources in North Dakota and across the country are beginning to figure out how they'll gather up the gas and what they'll do with it when the day comes when they have to.

Editori

One industrial source is way out ahead of that curve.

Letters

Sequestration savvy

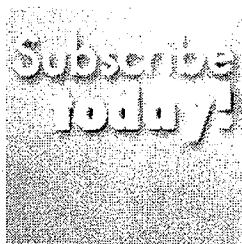
Colum

Dakota Gasification Co., which makes synthetic natural gas from coal in Mercer County, is the world's leader in CO2 sequestration.

That's due to a couple of reasons.

HOT LINKS
• Lottery Results

- Directory
- Horoscopes
- Sudoku
- Forum ***NEW***
- Weather



First, not many sources are sequestering CO2 on a commercial scale.

Second, the process of liquifying coal to make natural gas instead of burning it to make electricity makes it far easier for DGC to get its arms around its CO2.

Carbon gas is a relatively rare and valuable commodity when it's not free-floating around the atmosphere in bad company with methane and other greenhouse gases.

DGC is selling every bit it can to a pair of related oil field operators in Saskatchewan, primarily Encana Corp.

The oil operators send it down oil wells to increase the amount of oil that comes back up.

The carbonated gas works to re-pressurize the oil and is prolonging the life of aging oil fields in what's called "tertiary" recovery, equaling millions of barrels and billions of dollars.

A waste product that DGC blasted into the atmosphere until 2000 is now a \$10 million annual sales opportunity. Because it's injected deep into the oil bearing geology of Canada, it's also sequestered, that increasingly golden word in the industry.

About 8,900 tons of the compressed carbon gas surge through the pipeline to Canada every day.

Bob Fagerstrom, DGC plant manager, said the plant produces another 300 tons to 400 tons a day. But those tons are made on an interruptible basis and not reliable for oil recovery.

The coal-fired power plant right next door - both are owned by Basin Electric Power Cooperative - produces twice as much CO2 as does DGC.

The gas leaves the Antelope Valley Station's emission stack, mixed with other gases and steam.

The process to recover CO2 from the gas stream leaving a coal-fired power plant is very expensive, very complex and still a work in progress in pilot studies and laboratories around the country.

It makes sense, then, that the way to sequestration is proceeding along parallel paths of figuring out to extract CO2 without breaking the consumers' backs and how to sequester it for profit at the same time.

A research giant in North Dakota is making strides on the path of lucrative sequestration.

N.D. projects

The Energy and Environmental Research Center in Grand Forks is deep into CO2 research, in a Department of Energy project called Plains CO2 Reduction, or PCOR, for short.

A number of entities from up and down the Plains, including into Canada, are financial partners.

Phase one involved layout the groundwork for the region, identifying CO2 sources and building a consensus for further research.

In Phase II, the researchers' work now is figuring out to sequester the carbon gas in ways that create either an environmental or financial benefit, or both.

Research chief Ed Steadman and associate John Harju said this will be a big year for experimental sequestration in North Dakota.

They have two major projects in the works, one in far northwestern Burke County and one east of Williston near Tioga.

The first will involve drilling five wells, like the five-dot pattern on a die, into an unminable coal seam 1,600 feet deep in Burke County.

49-02-23. Consideration of environmental externality values prohibited. The commission may not use, require the use of, or allow electric utilities to use environmental externality values in the planning, selection, or acquisition of electric resources or the setting of rates for providing electric service. Environmental externality values are numerical costs or quantified values that are assigned to represent either:

1. Environmental costs that are not internalized in the cost of production or the market price of electricity from a particular electric resource; or
 2. The alleged costs of complying with future environmental laws or regulations that have not yet been enacted.
-

TESTIMONY OF JOHN W. DWYER
PRESIDENT, LIGNITE ENERGY COUNCIL
REGARDING
HB 1312

I. BACKGROUND

A. In 1993, the Minnesota Legislature passed a law effective August 1, 1993, which required the Minnesota Public Utilities Commission (MNPUC) to "....

- "quantify and establish a range of environmental costs associated with each method of electricity generation"
- and required each utility to "use (these values) in conjunction with other external factors . . . when evaluating resource options in all proceedings before the Commission."

B. What are Externalities?

1. EXTERNALITIES are generally defined as those costs or benefits resulting from an economic activity that are not directly reflected in market prices for the goods or services produced by the activity. Such costs or benefits are thus "external" to the market transaction. For the most part, utility commissions who have examined externalities only focus on the negative "cost" aspect of externality theory.
2. What are some examples? What is and what is not an externality cost?
 - a. Coal costs (equipment, taxes, regulatory costs, employee costs) are internalized in the price of energy so it is not an externality cost. Rather, coal costs are internal costs. But the benefits of a lignite industry - the indirect jobs and indirect economic activity it creates are not directly credited to the cost of your electricity, so it is an example of an externality benefit.

B. What are Externalities (cont.)

- b. Air pollution control equipment is internalized in the price of energy so it is not an externality cost. But residual health impacts (if there are any) from emissions of pollutants on the citizens of Jamestown, Fargo, or Grand Forks would be an example of an externality cost that is not reflected in the cost of your electricity.
- c. Carbon dioxide emissions, which occur when you burn any fossil fuel (coal, oil, natural gas, wood, etc.), are not controlled, because they are not classified as a pollutant. In fact, many leading scientists contend CO₂ emissions, which are a key ingredient of life as we know it, are beneficial and necessary and that increased CO₂ emissions are good, not bad.

However, if you believe there is a cost associated with CO₂ emissions from lignite - such as global warming - then the approach the environmentalists have chosen to attack CO₂ emissions is to impose externality costs on coal-fired electricity for its CO₂ emissions, because CO₂ emissions are not now internalized in the cost of energy.

C. What has MNPUC done to implement its statute?

1. On March 1, 1994, the MNPUC issued an interim order in writing that established an interim value for Carbon Dioxide (CO₂) of \$5.99 to \$13.60 per ton for coal-fired electricity.
2. In its order, the MNPUC indicated that the use of externality values must be used in the evaluation and selection of resource options "in all proceedings before the Commission, including resource plan and certificate of need proceedings." Furthermore, the use of externality values is mandatory in the selection of new resources, which replace or supplement existing facilities.

II. WHAT DOES THIS MEAN FOR NORTH DAKOTA'S LIGNITE RESOURCE?

- A. Minnesota is 50 percent of present lignite market and is where most future growth will occur.
- B. Additional cost added to lignite from CO₂ externality cost alone is about \$8.50 to \$19.35 per ton. This doubles or triples the present cost of lignite.
- Each ton of lignite generates about 1.4 tons of CO₂ when burned (based on carbon content of lignite).
 - Lignite has higher carbon content than other fossil fuels.
- C. How does application of externality value actually work? (Exhibits 1 & 2 attached)
- D. What happens to lignite resource?
1. Would make lignite non-competitive as resource which replaces or supplements existing facilities.
 2. Would make lignite non-competitive as resource for future facilities (additional units, clean coal projects, etc.).
 3. May limit new firm power sales of lignite capacity between utilities (3/1/94 and later).
 4. Planning process of utilities and cooperatives will begin to limit lignite as viable resource alternative (will be reflected in integrated resource plans filed by utilities and cooperatives after 3/1/94).
 5. Will set detrimental precedent that could be followed in other lignite markets (South Dakota, Montana, etc.) by regulatory authorities.
 6. Artificially raises price of lignite energy to consumers (industrial & residential) and makes our products non-competitive.

III. WHAT HAS NORTH DAKOTA DONE ABOUT MINNESOTA'S EXTERNALITY COST ON LIGNITE?

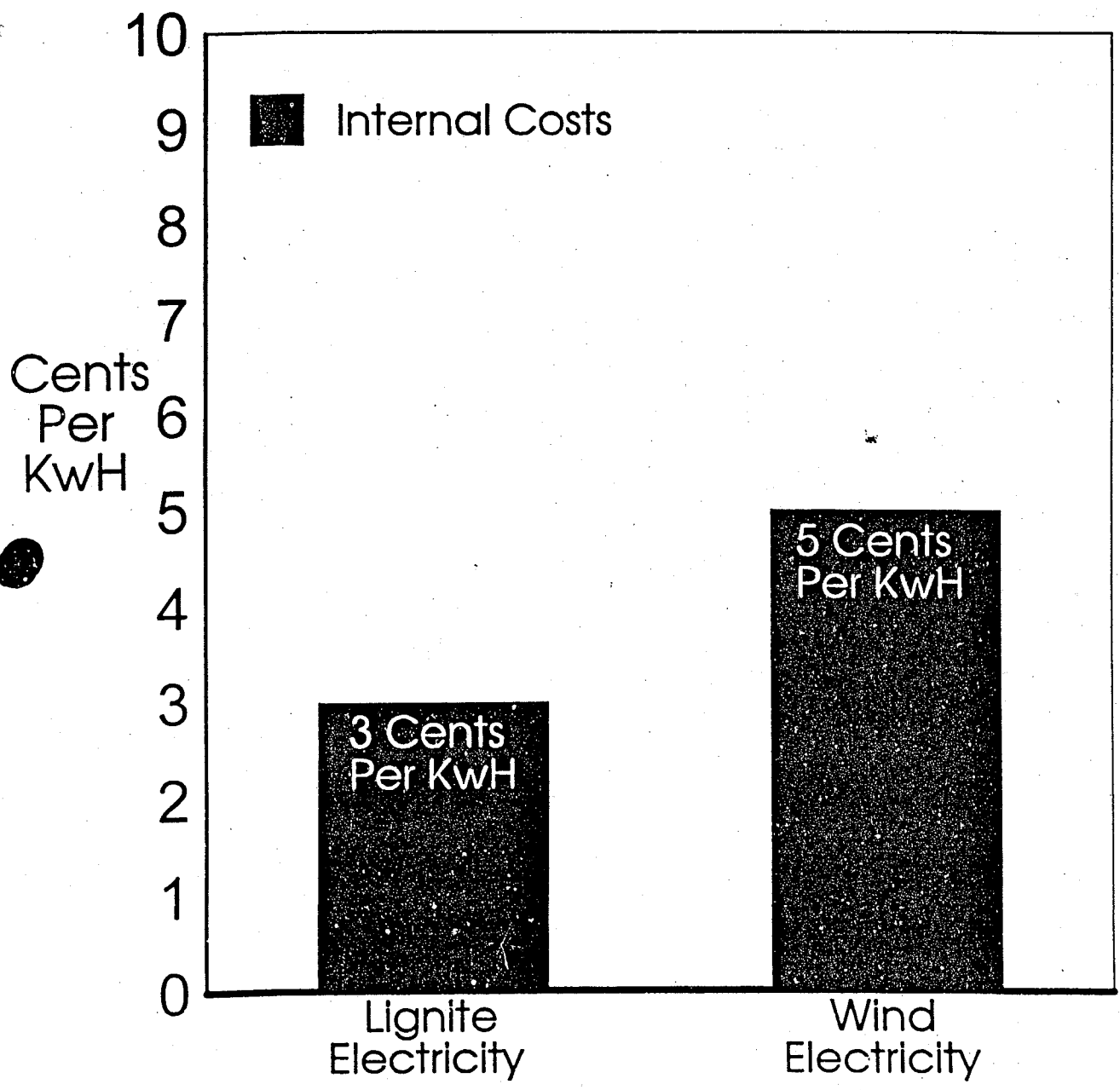
- A. State of North Dakota (through Governor, Attorney General and Agricultural Commissioner - Industrial Commission) and the lignite industry have joined together and intervened in this case to fight the injustice of externality costs on lignite energy.
- B. We are contending that:
 - 1. CO₂ externality costs on lignite energy lack scientific basis.
 - 2. CO₂ externality costs on lignite energy are not appropriate because there is no damage to Minnesota and such regulation is beyond police power of State of Minnesota.
 - 3. CO₂ externality costs on lignite energy place a burden on interstate commerce.

IV. WHAT DOES HB 1312 DO?

- A. Prevents North Dakota Public Service Commission from passing on to North Dakota consumers externality costs imposed by other states.
- B. Sends strong message to Minnesota and other states that State of North Dakota is not going to let other states strangle our lignite industry which provides 18,000 jobs, over \$60 million in annual tax revenue, and \$1.4 billion in business volume for our state.
- C. Protects North Dakota consumers from unreasonable, speculative, and artificial externality costs imposed by other states.

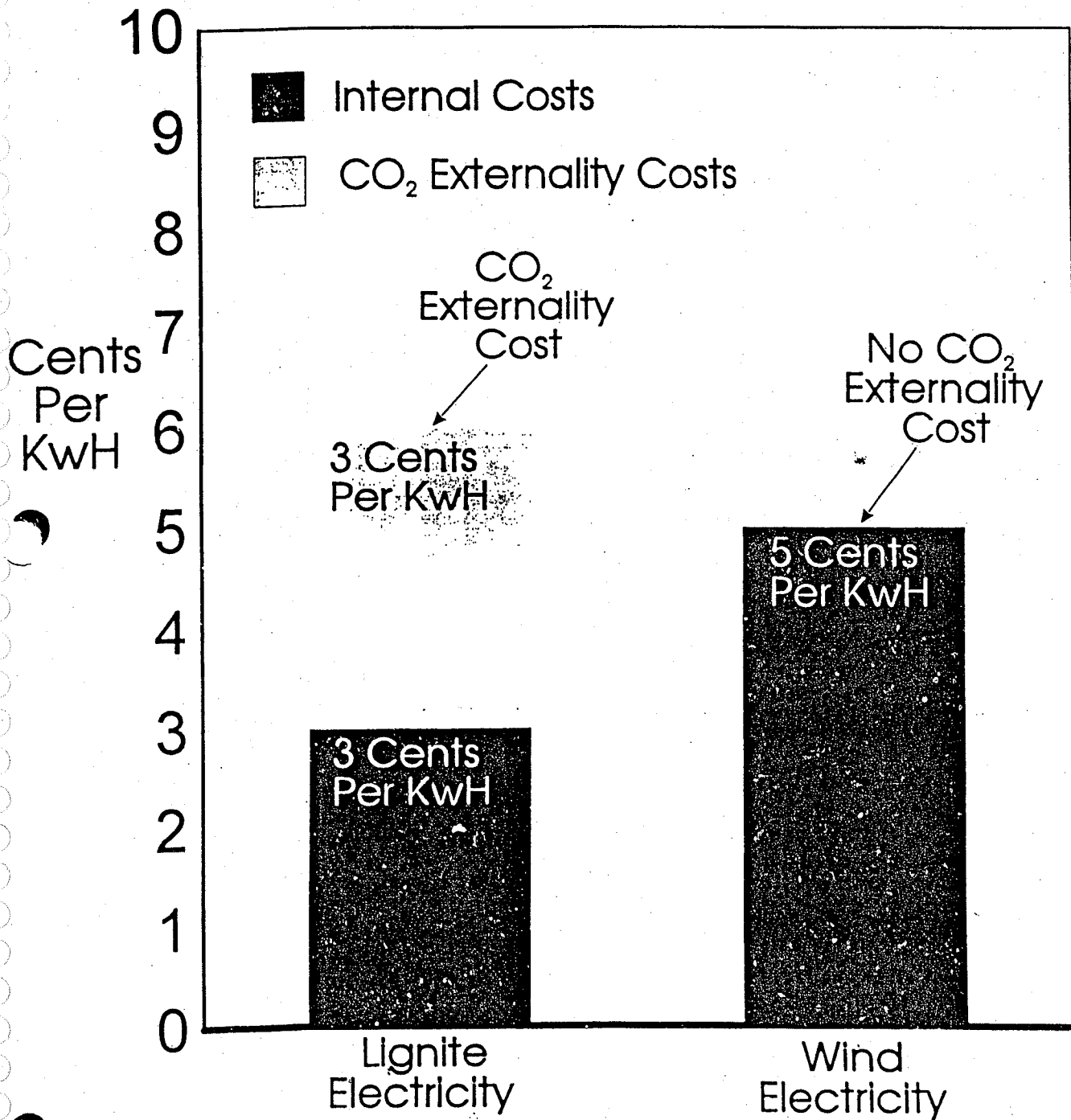
- V. LIGNITE ENERGY COUNCIL AND ITS MEMBERS - our producers (Coteau, Falkirk, BNI, Knife River); our utility members (MDU and Otter Tail Power), our cooperative members (Basin Electric, Cooperative Power, United Power Association and Minnkota Power), and its 200 contractor/supplier members urge a DO PASS on HB 1312.

Comparison of Lignite Energy & Wind Energy Without externality Cost



Without Externalities, Lignite Wins

Comparison of Lignite Energy & Wind Energy With CO₂ externality Cost



With Externalities, Lignite Loses

Excerpts from "Environmental Economics" by Joseph Seneca and Michael Taussig, Used as a textbook for the graduate level "Energy and Environmental Economics" class at the University of North Dakota during the 1970's.

"Chapter 3 extends the elementary theory presented in this chapter by reconsidering the concept of efficiency in a more realistic, sadly familiar world in which the environmental problems of society, such as air and water pollution, are not satisfactorily resolved by an otherwise ideal private market system. These problems are traced to economic factors operating outside the market system, which we term EXTERNALITIES." (pp25 & 26).

"THE CONCEPT OF EXTERNALITIES"

Economists have long recognized that the private market system often produces undesirable spillover effects on man's environments. Typical and too familiar examples of such spillover effects are the noxious smoke and polluted water emissions of modern industrial plants. In such circumstances, the technical nature of the production process generates an output effect distinct from the final marketed product of the firm. The spillover effects of modern industrial production result in deteriorating environmental quality, an output that the firm does not, and, of course, could not sell. On the contrary, households and other firms affected by the pollutant spillages experience real opportunity costs in many different forms and would be willing to pay varying amounts if they could effectively end or lessen the firm's polluting activities.

We define any costs that are additional to the costs resulting from the production outlays of the firm as EXTERNAL, or spillover, costs. Total social costs (social costs, for brevity) are defined as the sum of the private costs of the firm and any external costs. The use of the word EXTERNAL implies that some costs do not accrue to the firm that produces the good, but are imposed on all society or, at least, on a subset of households or firms in a society. Such costs are outside the market system and are not reflected in relative market prices.

Examples of external costs are easy to find in any modern industrial economy. The paper mill that pollutes a river and destroys the game fish population imposes external costs on fishermen, boaters, and swimmers; so does the chemical plant that plagues the local economy with constant stench. The residential developer who denudes the landscape and constructs row on row of similarly built homes may impose psychic costs on many individuals by affronting their esthetic sensitivities. The individual who misses a number of work days each year due to illnesses caused by impure air bears a personal external cost, equal to his lost wages. Society, which loses the worker's production for the work days lost bears an additional external cost, equal to the net difference between the worker's average product and his wages over the relevant time period. Even the charcoal cookout of the suburbanite that soils his neighbor's drying laundry involves a (perhaps) small external cost. The common theme in all of these hypothetical situations is that firms or households other than those responsible for the

initial act of production or consumption suffer uncompensated monetary or psychic costs.

At the same time, the general term EXTERNALITIES suggests that it is possible for the production or consumption of some commodities to bestow spillover benefits on fortunate firms and households not immediately involved in the actual production or consumption process. The recipients of such external benefits are not charged the monetary value of these benefits. No markets exist that enable the producers of the spillover benefits to exclude potential beneficiaries from consuming the spillovers if they fail to pay the market price. For example, health immunization services provide benefits to all of society in addition to the individual consumer in the form of better protection from contagious diseases. Similarly, everybody in the neighborhood benefits from the beauty of a well designed building, and these benefits are all supplementary to the benefits derived from the owner of the building himself. Because this book is concerned mainly with problems of environmental pollution, our main focus will be on those externalities that have negative spillover effects; that is, external diseconomies. We shall note later, however, that the economic welfare implications of external economies are logically symmetric to those of external diseconomies." (pp 49 & 50).

CORRECTED TESTIMONY ON HOUSE BILL 1312

Presented by: William W. Binek
Chief Counsel, Public Service Commission

Before: House, Industry, Business and Labor Committee

Date January 16, 1995

Mr. Chairman and members of the committee. My name is William Binek and I am Chief Counsel for the North Dakota Public Service Commission. The Commission has asked me to testify in support of House Bill 1312.

"Environmental externality" is a term used to define the assessment of an artificial cost that is arbitrarily assessed as a cost against different types of electric generating facilities. The primary focus of the proponents of this artificial cost is the elimination of coal as a fuel to be used for generation of electricity.

The Commission has taken a proactive role in the fight against the imposition of environmental externality costs. The Commission is providing technical assistance to the Attorney General and the North Dakota Lignite Energy Council in their challenge of the legislation enacted in Minnesota which requires the Minnesota Public Utilities Commission establish environmental costs for CO₂ emissions. The Commission has also aggressively opposed the assessment of environmental penalties against coal fired generating facilities in Northern States Power Company's generic competitive bidding procedure before the Minnesota Public Utilities Commission.

The proposed legislation provides an important tool in the fight against the imposition of environmental externality costs targeted against North Dakota's Lignite

industry. Furthermore, this legislation protects North Dakota's electric ratepayers from artificially increased costs of electricity caused by self-serving and arbitrary actions of other states in the application of externality costs. The Commission realizes that passage of this legislation may adversely affect some utilities, but the interests of North Dakota ratepayers and taxpayers must be protected.

49-05-16. Advance determination of prudence. A public utility proposing to construct, lease, or make improvements to an energy conversion facility, renewable energy facility, transmission facility, or proposed energy purchase contract from another entity or person for the purpose of ensuring reliable electric service to its customers may file an application with the commission for an advance determination of prudence regarding the proposal. The commission may order that expenses associated with investigating the application made by the public utility for prudence of a resource addition be paid by the public utility in accordance with section 49-02-02.

1. The commission may issue an order approving the prudence of an electric resource addition if:
 - a. The public utility files with its application a projection of costs to the date of the anticipated commercial operation of the electric resource addition;
 - b. The commission provides notice and holds a hearing, if appropriate, in accordance with section 49-02-02; and
 - c. The commission determines that the resource addition is reasonable and prudent. For facilities located or to be located in this state the commission, in determining whether the resource addition is reasonable and prudent, shall consider the benefits of having the energy conversion facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased located in this state.
2. The commission order must be rendered no later than seven months after the public utility files its application requesting a prudence determination of an electric resource addition.
3. A resource addition approved by the commission is subject to annual reporting requirements until commercial operation of the resource addition.
4. The commission's order determining prudence of the resource adjustment is binding for ratemaking purposes.
5. If at any time following an initial commission order, the commission, following a subsequent hearing, determines that continuation of a project is no longer prudent or that its prior order should be modified, the public utility may recover in its rates, and in a timely manner consistent with the public utility's financial obligations, the amounts the public utility already has expensed, incurred, or obligated on a project, including interest expense and a return on equity invested in the project up to the time the new order is entered even though the project may never be fully operational or used by the public utility to serve its customers.
6. There is a rebuttable presumption that an energy conversion facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased which is located in the state is prudent.

HOUSE BILL NO. 1324

Introduced by

Representatives Keiser, Kasper, Klein

Senators O'Connell, Robinson, Trenbeath

1 A BILL for an Act to create and enact a new section to chapter 49-05 of the North Dakota
2 Century Code, relating to advance determinations of prudence and ratemaking principles for
3 public utilities.

4 **BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:**

5 **SECTION 1.** A new section to chapter 49-05 of the North Dakota Century Code is
6 created and enacted as follows:

7 **Advance determination of prudence and ratemaking principles.** A public utility
8 proposing to construct, lease, or make improvements to either or both an energy conversion
9 facility or transmission facility or proposing to enter into a contract for the purchase of energy
10 from another entity or person for the purpose of ensuring reliable electric service to its
11 customers may file an application with the commission for an advance determination of
12 prudence regarding the proposal. As part of the application, the public utility also may request
13 that the commission determine ratemaking principles that will be applied to the public utility's
14 investment in the energy conversion or transmission facility or the energy contract cost.

- 15 1. Ratemaking principles a public utility may propose and the commission may use
16 include the following:
 - 17 a. Authorized return on common equity.
 - 18 b. Capital structure to finance the construction, lease, or improvements of the
19 energy conversion facility and transmission facility.
 - 20 c. Estimated service life and depreciation rates for cost of service purposes.
- 21 2. The applicable ratemaking principles to be used in each instance must be
22 determined in a contested case hearing which may be combined with a
23 determination of prudence and an application for a certificate pursuant to chapter
24 49-22.

- 1 3. A commission hearing must be held and an order issued by the commission within
2 one hundred eighty days after the filing of an application by the public utility. If,
3 after hearing, the commission determines that the public utility's decision to
4 construct or lease a facility or make improvements thereto, or to purchase energy
5 is reasonable and prudent, the commission shall issue an order so stating and also
6 shall address the ratemaking principles requested by the public utility. The
7 commission may impose conditions requiring the public utility to monitor and report
8 to the commission pursuant to a specified schedule concerning any significant
9 changes in costs, load, regulatory, economic, or other assumptions upon which the
10 ratemaking principles were decided. Costs to be included in the public utility's
11 electric rates must be in accordance with this chapter, except as otherwise
12 provided in this section.
- 13 4. The commission's order determining prudence and addressing ratemaking
14 principles must be applied in any future rate case to the investment and costs of
15 the facility or contract for the purchase of energy and are binding for ratemaking
16 purposes in all future commission proceedings involving the public utility.
- 17 5. If the commission fails to issue an order determining the prudence of a proposal
18 within one hundred eighty days after filing by a public utility, the facility or contract
19 for the purchase of energy is deemed prudent as proposed and any ratemaking
20 principles requested by the public utility in its application are deemed approved by
21 the commission and are binding in all future rate proceedings involving the public
22 utility.
- 23 6. The commission's order setting forth applicable ratemaking principles must be
24 issued before the public utility's commencement of construction, lease, or
25 improvements to a facility or its execution of the contract for purchase of energy.
- 26 7. If at any time following an initial commission order the commission, following a
27 subsequent hearing, determines that continuation of a project is no longer prudent
28 or that its prior order should be modified, the public utility must be allowed to
29 recover in its rates, and in a timely manner consistent with the public utility's
30 financial obligations, the amounts the public utility already has expensed, incurred,
31 or obligated on a project, including interest expense and a return on equity

Fifty-ninth
Legislative Assembly

1 invested in the project up to the time the new order is entered even though the
2 project may never be fully operational or used by the public utility to serve its
3 customers.

2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1324

House Industry, Business and Labor Committee

Conference Committee

Hearing Date 26 January 2005

Tape Number	Side A	Side B	Meter #
2		X	0-24
Committee Clerk Signature <i>Jean Prindle</i>			

Minutes:

Chairman Keiser opened the hearing of HB 1324.

Dennis Boyd, MDU Resources Group, Inc., introduced the bill. This bill was introduced at MDU's request. (Testimony attached.) He submitted a "hoghouse" amendment to the bill. This amendment is attached to his testimony.

Rep. Ekstrom: On page 2, line 6, would you be subject to annual reporting requirements? I assume those requirements will be detailed.

Boyd: There would be an annual report to the Commission.

Rep. Forseth: With this new amendment would eliminate a need for a fiscal note. The fiscal note was \$70,000.

Boyd: It was one of the concerns that was brought up by the commission when we met with them. We've included a statement that the "commission shall have the authority that the expenses associated with investigating application..., be paid by the public utility in accordance with section 49.02.02." That is the public utility revolving fund. That should eliminate any need for a fiscal note.

Rep. Dosch: Because these things take years what happens if the project itself substantially changes?

Boyd: A protection for us and the fact that we gained pre approval of these expenses and a recognition that things can and do change is if it is determined that the project is not longer prudent or feasible, we would be allowed to collect all those expenses that we incurred up to that point. Any changes would be approved by the Public Service Commission not MDU. Rep.

Keiser: The rate making that gets established is binding if it is based on a 500 megawatt Vs 250.

Boyd: I'm a little concerned about the term "rate making." We're not asking for pre approval of rate making principles. If something did happen that the project changed we would still be able to recover the expenses that we incurred based on original pre approval.

Rep. Kasper: To clarify: What you are asking for is the approval in advance of the opportunity to go ahead, of the prudence of the expenditures or the prudence of the project? If according to the public service commissioner the project makes sense, go for it.

Boyd: Right, I think so. We would determine the need for the project and then go to the Public Service Commission to see if can be approved before we invest in the project.

Illona Jeffcoat-Sacco, executive secretary to the Public Service Commission, testified that the Commission is neutral on HB 1324. (Testimony attached.)

Rep. Forseth: As the bill is written, it's permissive. If you feel it isn't to the benefit of ND you could choose not to use provisions of it.

Jeffcoat-Sacco: In theory, yes. The prudence is a legal regulatory word of art. If the company applied and the commission decided against it because of the fact that it's not in ND, the company could challenge that in the court system. The traditional regulatory standards for prudence probably don't have any statement like instate development as part of the standard. That's not all written out here. That's a lot of body of regulatory law that isn't written in law anywhere. I think you have to put that in this bill to avoid cases being overturned on appeal.

Chairman Keiser: Aren't you really proposing a double standard? The PSC wants the authority to regulate and control and dictate rates to utilities regardless of where the power comes from. If production facility is in SD and that power flows in here, the commission wants the authority to say, "No, you can't do it, you have to bring your construction costs and you have to justify that rate." We are going to say if it's too high or low. Whether it's built out of state or not, you still want the authority to regulate.

Jeffcoat-Sacco: Whether it's built out of state or not, if a portion is allocated to ND, we have the authority to approve those rates today. The prudence is another step. Today whether it's built in or out of state we have the authority to determine the prudence. The only difference is whether in some cases or in all cases you tell us to determine the prudence earlier. Our commission is simply saying that if we determine earlier, it should be in ND.

Chairman Keiser: I understand. I'm also suggesting to you that ties the hands of a business making a prudent investment decision. We're interfering.

Jeffcoat-Sacco: Yes, you're correct But I see that regulation step as equal.

Steve Schultz, Otter Tail Power, testified "I don't know" on the bill. I believe we will be fine with the hoghouse amendments. I really appreciate, Mr. Chairman, you leading into what I really wanted to preach about. The request by the commission to say only ND projects in Ottertail Power's standpoint would be a bad thing. As many of you know we're looking at a sizable project in SD that would have rate affects to our customers in ND and MN. If you take the pre approval piece way from our project, 40% of Ottertail's customers now are denied the benefit. How much that would save or cost them, I don't know. It would seem to me we are being penalized for making a business decision what makes the best sense. We are very concerned about the "ND only." Otherwise from a first blush we would support this bill.

Chairman Keiser: Ms. Jeffcoat-Sacco, we would appreciate you drafting the amendment so we could have that.

Rep. Thorpe: You mentioned energy producing projects in SD. How did ND miss out that?

Schultz: The way it ended up being looked at in SD is when Bigstone One was built in SD it was built with the idea of there being a second unit there. There were a number of infrastructure type works that were begun.

Rep. Kasper: Clarify where you were at on the bill before the hoghouse amendment. I'm shocked that some of the rest of the industry didn't get up and support the bill as it makes a lot of sense to me. Were you in support of the bill as it was written? Now you want to double check the amendment?

Page 5

House Industry, Business and Labor Committee

Bill/Resolution Number **HB1324**

Hearing Date **26 Jan 05**

Schultz: Yes, we were supporting the previous bill.

Chairman Keiser closed the hearing on HB 1324.

2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1324

House Industry, Business and Labor Committee

Conference Committee

Hearing Date 26 January 2005

Tape Number	Side A	Side B	Meter #
3	X		572 - 839
Committee Clerk Signature <i>Jan Prindle</i>			

Minutes:

Chairman Keiser opened discussion of HB 1324. He said that was the hog house amendment. He said he visited with Rep. Kasper and asked if he supported the hog house. Rep. Kasper said he didn't have any problems with it. He asked the wishes of the Committee. If the Committee feels comfortable, we can pass it out. If he comes back with a problem, we'll just get the bill back.

Rep. Ekstrom: I don't see any reason why this project should be developed in ND.

Rep. Keiser: All right. They were going to offer that amendment. If the committee wants to proceed with this the first action will be to adopt the hog house amendment.

Rep. Kasper: I so move.

Rep. Nottestad: I second

A voice vote was taken. The motion carried.

Rep. Keiser: The amendment is on the bill what would the Committee like to do?

Page 2

House Industry, Business and Labor Committee

Bill/Resolution Number HB 1324

Hearing Date 26 Jan 05

Rep. Ruby: I move a Do Pass as Amended.

Rep. Vigasaa: I second

Rep. Keiser: This is one of the best pro business things I've seen come before this committee.

Occasionally the state does things backwards but with this one we were right at the top of the class in terms of doing it backwards. You make people go through hundreds of thousands of dollars of expenditures and then come in and have them say no. It's a lot better just to say here's our concept if you like it or not and then we're gonna go forward. I believe this is the right thing.

Rep. Ekstrom: One question. If we have gotten all the way down to brass tax and the PSC says eh eh.

Rep. Keiser: It has happened and then had to go back and retool and have to do a bunch of things. This should be doing it at the front end.

Rep. Kasper: Who would be responsible to get the bill redrafted?

Rep. Keiser: Our clerk will take up the amendment to get it refined and then we'll go from there.

A roll call vote was taken.

Yes: 14 No: 0 Absent: 0 The bill passed as amended.

Rep. Kasper will carry the bill.

FISCAL NOTE

Requested by Legislative Council
01/28/2005

Amendment to: HB 1324

1A. State fiscal effect: *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2003-2005 Biennium		2005-2007 Biennium		2007-2009 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues	\$0	\$0	\$0	\$0	\$0	\$0
Expenditures	\$0	\$0	\$0	\$0	\$0	\$0
Appropriations	\$0	\$0	\$0	\$0	\$0	\$0

1B. County, city, and school district fiscal effect: *Identify the fiscal effect on the appropriate political subdivision.*

2003-2005 Biennium			2005-2007 Biennium			2007-2009 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts
\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0

2. Narrative: *Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.*

We estimate the engrossed bill causes no fiscal impact

3. State fiscal effect detail: *For information shown under state fiscal effect in 1A, please:*
A. Revenues: *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

No revenue impact is expected from this bill.

B. Expenditures: *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

We estimate no substantial expenditures under the engrossed bill.

C. Appropriations: *Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.*

We have not estimated any need for an additional appropriation because we would expect to employ such outside experts under our existing appropriation. However, it is possible that if operating expenses are tight, we will need to obtain Emergency Commission approval for these expenditures, and a corresponding increase to our appropriation to cover the cost.

Name:	Illona Jeffcoat-Sacco	Agency:	PSC
Phone Number:	701-328-2400	Date Prepared:	01/28/2005

FISCAL NOTE
 Requested by Legislative Council
 01/12/2005

Bill/Resolution No.: HB 1324

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2003-2005 Biennium		2005-2007 Biennium		2007-2009 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues	\$0	\$0	\$0	\$0	\$0	\$0
Expenditures	\$0	\$0	\$70,000	\$0	\$70,000	\$0
Appropriations	\$0	\$0	\$0	\$0	\$0	\$0

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2003-2005 Biennium			2005-2007 Biennium			2007-2009 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts
\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0

2. **Narrative:** *Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.*

The only aspect of the bill which could cause fiscal impact is the need to process any case and all issues raised by the applicataion within the prescribed time frames. It is likely that under some circumstances this would require hiring outside assistance. We estimate that this might cost about \$35,000 for one filing, and we estimate one filing requiring this outside assistance per year, or two per biennium.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*

A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

No revenue impact is expected from this bill.

B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

We estimatated expenditures because it is likely that under some circumstances this bill would require hiring outside assistance, in order to process the filings within the required time frame, especially if cost of capital is involved in the application. We have no cost of capital expert on staff. We estimate that hiring a consultant for this purpose might cost about \$35,000 for one filing, and we estimate one filing requiring this outside assistance per year, or two per biennium. Consequently, the expenditure number is \$70,000 per biennium. The expenditures would be general fund expenditures because the bill does not provide for use of the Valuation Fund for these filings.

C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.*

We have not estimated any need for an additional appropriation because we would expect to employ such outside experts under our existinig appropriation. However, it is possible that if operating expenses are tight, we will need to obtain Emergency Commission approval for these expenditures, and a corresoponding increase to our appropriation

to cover the cost.

Name:	Ilona Jeffcoat-Sacco	Agency:	PSC
Phone Number:	701-328-2407	Date Prepared:	01/23/2005

REPORT OF STANDING COMMITTEE

HB 1324: Industry, Business and Labor Committee (Rep. Kelsner, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (14 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1324 was placed on the Sixth order on the calendar.

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 49-05 of the North Dakota Century Code, relating to advance determination of prudence for a public utility's proposed new construction, lease, or improvement of an energy conversion facility, renewable energy facility, transmission facility, or proposed energy purchase contract.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. A new section to chapter 49-05 of the North Dakota Century Code is created and enacted as follows:

Advance determination of prudence. A public utility proposing to construct, lease, or make improvements to an energy conversion facility, renewable energy facility, transmission facility, or proposed energy purchase contract from another entity or person for the purpose of ensuring reliable electric service to its customers may file an application with the commission for an advance determination of prudence regarding the proposal. The commission may order that expenses associated with investigating the application made by the public utility for prudence of a resource addition be paid by the public utility in accordance with section 49-02-02.

1. The commission may issue an order approving the prudence of an electric resource addition if:
 - a. The public utility applies for a prudence determination before commencement of construction or purchase of an electric resource addition;
 - b. The public utility files with its application a projection of costs to the date of the anticipated commercial operation of the electric resource addition;
 - c. The commission provides notice and holds a hearing, if appropriate, in accordance with section 49-02-02; and
 - d. The commission determines that the resource addition is reasonable and prudent.
2. The commission order must be rendered no later than seven months after the public utility files its application requesting a prudence determination of an electric resource addition.
3. A resource addition approved by the commission is subject to annual reporting requirements until commercial operation of the resource addition.
4. Before commercial operation of the resource addition, the public utility shall make a general rate case filing with a full cost of service analysis including the resource addition in accordance with section 49-05-05. The commission's order determining prudence of the resource adjustment is binding for ratemaking purposes.

5. If at any time following an initial commission order, the commission, following a subsequent hearing, determines that continuation of a project is no longer prudent or that its prior order should be modified, the public utility may recover in its rates, and in a timely manner consistent with the public utility's financial obligations, the amounts the public utility already has expensed, incurred, or obligated on a project, including interest expense and a return on equity invested in the project up to the time the new order is entered even though the project may never be fully operational or used by the public utility to serve its customers."

Renumber accordingly

2005 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1324

Senate Industry, Business and Labor Committee

Conference Committee

Hearing Date 03-02-05

Tape Number	Side A	Side B	Meter #
1		xxx	900-1930
Committee Clerk Signature <i>Jana Van Berkom</i>			

Minutes: Chairman Mutch opened the hearing on HB 1324. All Senators were present.

HB 1324 relates to advance determination of prudence for a public utility's proposed new construction, lease, or improvement of an energy conversion facility.

Dennis Boyd, Montana Dakota Utilities, introduced the bill. See written testimony.

Senator Klein: Do the consumers save as well?

Boyd: That's correct. Any way that we can save cost in a constructional plan is going to eventually transfer down to lower cost for the consumer.

Chairman Mutch: Is this proposal unique to North Dakota?

Boyd: I can't answer that.

Senator Espegard: This doesn't allow the cost of the plant to be put onto the bill early, it just allows the determination to be made as feasible product.

Boyd: This has nothing to do with covering the cost during the construction faze of the plan.

Sen. O'Connell stated his support for the bill.

Page 2

Senate Industry, Business and Labor Committee

Bill/Resolution Number HB 1324

Hearing Date 3-02-05

Bob Graveline, Utility Shareholders of North Dakota, stated his support for the bill.

The hearing was closed. No action was taken.

On the 8th of March, the committee met to make a recommendation on this bill.

Senator Epegard moved a DO PASS AS AMENDED.

Senator Klein seconded.

Roll Call Vote: 5 yes. 0 no. 2 absent.

Carrier: Chairman Mutch

REPORT OF STANDING COMMITTEE

HB 1324, as engrossed: Industry, Business and Labor Committee (Sen. Mutch, Chairman) recommends AMENDMENTS AS FOLLOWS and when so amended, recommends DO PASS (5 YEAS, 0 NAYS, 2 ABSENT AND NOT VOTING). Engrossed HB 1324 was placed on the Sixth order on the calendar.

Page 2, after line 19, insert:

- "6. This section applies only if the energy conversion facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased is located in this state."

Renumber accordingly

2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1324

House Industry, Business and Labor Committee

Conference Committee

Hearing Date 4-6-05

Tape Number	Side A	Side B	Meter #
1		x	7.9-8.5
Committee Clerk Signature <i>Jody Bender</i>			

Minutes:

Chairman Kasper: Opened the conference committee on HB 1324.

Chairman Kasper, Representative Ruby, Representative Boe, Chairman Mutch, Senator Nething, Senator Heitkamp were present.

Chairman Kasper: Let me share with you a word that I just received, it appears that the people involved, the governors office and the PSC are working a on some type of a compromise amendment that they would like to propose to this committee, but as we sit here they do not have that amendment prepared and they asked if they would adjourn our meeting and reschedule it for tomorrow? Meeting adjourned.

2005 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1324

House Industry, Business and Labor Committee

Conference Committee

Hearing Date 4-12-05

Tape Number	Side A	Side B	Meter #
1	x		12.8-34.8
Committee Clerk Signature <i>Jody Bente</i>			

Minutes:

Chairman Kasper: Opened the conference committee on HB 1324.

Chairman Kasper, Representative Ruby, Representative Boe, Chairman Mutch, Senator Nething, Senator Heitkamp were present.

Chairman Kasper: OK committee, the parties of this bill are working on some type of a compromise which they now claim they have done so.

Dennis Boyd, Resources Group, MDU: Appeared in support of the amendments, and stated that this bill was introduced at our request, and I want to thank the committee and the chairman to take some testimony, as you correctly indicated, the 3 investor owned utilities companies, the Governors office, PSC office have come to an agreement of some additional amendments that we would ask you to put on this bill.

Dan Kuntz, Attorney, MDU: Appeared in support of the amendments, the purpose of HB 1324 was to allow public utilities to come to the commission and get pre approval for prudence and

reasonableness of construction projects, leases and so forth, the purpose for that pre approval was to give the utilities some assurance that they were going to be able to recover the cost of those projects and rates at some future point. The Senate amendments would have restricted the ability of the commission to consider those pre approval applications and facilities built in North Dakota the amendments that you have before you do a couple different things, the first is on line 18 and 19 would currently provide the utility must apply for before entering into a purchase contract or before construction of the facility starts, the amendments would remove that requirement because of power purchase contracts. leases, and so forth that is really not practical the PSC proceedings will take 6-7 months in all likely hood, some of these things are going to require quicker action to that. If the company waits to long after it starts construction the only risk is on itself, that it may not get prudency determination. the amendment on page 2 line 2, will allow the commission to consider reviewing prudence application facility be located in North Dakota, the benefits of having the facility located in North Dakota what that would do is the facility that is located in North Dakota if someone were going to argue that it might be more beneficial to locate that facility out side the state, that the commission could none the less consider the benefits of having the facility located in North Dakota and there by determine that even though there might be a cheaper alternative located out side the state, when you consider the benefits of having it located in the state, the project is none the less prudent and reasonable. It would provide the companies to build in North Dakota but not penalize utilities for having facilities located outside the state. They would have to stand under their own weight in terms of prudence without the benefits of being able to consider what would otherwise apply to facilities located in North Dakota. the amendments were suggesting remove the requirement of 8, 9, 10,

that would require the utility to file a rate case before commercial operation of the facility, in essence this requirement would of always forced utility to file for a rate case before it could put the facility into place smaller projects, purchase contracts, there really would be no reason you would be forcing utility to file that it may not need at that particular point, we suggest removing that requirement, the utility would be able to file for a rate increase whenever it felt necessary under present law, and then finally, the Senate amendment to HB 1324, put a requirement on that these applications could only be made for facilities located in North Dakota, the proposed amendments would not limit it, the pre approval application to just facilities in North Dakota, but instead allow facilities in North Dakota to be entitled to a rebuttable presumption of prudence.

Senator Heitkamp: Other states are allowing this?

Dan Kuntz: I'm not sure what other states are doing in this regard.

Chairman Kasper: Give us an overview of why we need these amendments to this bill?

Dan Kuntz: The bill itself and why we need to bill, is for utilities to come to the commission have the commission involved in that decision making that will give the utility some comfort level, that what they are doing, they will not be second guessed, it may even help with their financing. These amendments provides a little bit of a plus if you will for the North Dakota facilities, the commission considers employment benefits, tax benefits, and so forth in weighing this particular alternative being built in North Dakota verses a facility outside the state. This will just make the process smoother for those facilities which they aren't really controversial.

Kevin Cramer, Public Service Commission: Appeared in support of the bill. I want to express my appreciation to these folks, what we have come up with is a good of a product as we can hope for. The commission has not taken a position on the amendments, although all three of us have

Page 4

House Industry, Business and Labor Committee

Bill/Resolution Number HB 1324

Hearing Date 4-12-05

talk about them, and this is a very good compromise, however it provides that regulatory certainty that the utilities need to go to the market to get a better rating, to lower financing, and that certainty is beneficial not only for investors, the companies, the state of North Dakota, but also for the rate payers. I'm very pleased with the product that has turned out.

Ron Rasenberger, Governors Office: Appeared in support of amendments and appreciate all the work that has taken place on this bill.

Kathy Aas, Excel Energy: We are also in support of the amendments.

John Olson, Otter Tail Power Company: We are also in support of the amendments.

Senator Mutch: I move that the **SENATE RECEDE** from the **SENATE** amendments and **ADOPT** the amendments as presented.

Senator Nething: I **SECOND** the motion.

Motion carried **VOTE: 6-YES 0-NO 0-ABSENT**

Representative Kasper will carry the bill on the floor.

REPORT OF CONFERENCE COMMITTEE

HB 1324, as engrossed: Your conference committee (Sens. Mutch, Nething, Heitkamp and Reps. Kasper, Ruby, Boe) recommends that the **SENATE RECEDE** from the House amendments on HJ page 1001, adopt amendments as follows, and place HB 1324 on the Seventh order:

That the Senate recede from its amendments as printed on page 1001 of the House Journal and page 756 of the Senate Journal and that Engrossed House Bill No. 1324 be amended as follows:

Page 1, remove lines 18 and 19

Page 1, line 20, replace "b." with "a."

Page 1, line 22, replace "c." with "b."

Page 2, line 1, replace "d." with "c."

Page 2, line 2, after the period insert "For facilities located or to be located in this state the commission, in determining whether the resource addition is reasonable and prudent, shall consider the benefits of having the energy conversion facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased located in this state."

Page 2, line 8, remove "Before commercial operation of the resource addition, the public utility shall make"

Page 2, remove line 9

Page 2, line 10, remove "addition in accordance with section 49-05-05."

Page 2, after line 19, insert:

"6. There is a rebuttable presumption that an energy conversion facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased which is located in the state is prudent."

Renumber accordingly

Engrossed HB 1324 was placed on the Seventh order of business on the calendar.

Testimony on HB 1324
Dennis Boyd
MDU Resources Group, Inc.
January 26, 2005

Good morning, Mr. Chairman and members of the committee. My name is Dennis Boyd. I am with MDU Resources Group, and appearing this morning in support of HB1324. This bill was drafted and introduced at the request of Montana-Dakota Utilities and started out with a simple concept. That concept is to obtain from the North Dakota Public Service Commission a pre-approval or predetermination of the prudence of expenditures for the construction of generation and transmission facilities before construction begins and the ratemaking principles which will be utilized when those facilities are completed and added to the rate base of the company. What started out as a simple concept, has become rather convoluted and in a sense, humorous. Before I explain, let me begin by explaining how the current process works when a regulated company determines it needs to build a generating plant or transmission facility.

Currently and in very general terms, after a company has determined it needs additional generation or transmission facilities AND after it has obtained all of the various permits needed – air quality permits, water permits, siting permits, etc. etc. , it proceeds to build the facility. Usually those facilities take several years to complete and expenses run into the hundreds of millions of dollars. After the facility is completed, the utility then files a rate case with the PSC to recover the costs. After the PSC determines the facility was needed and the expenditures were prudent, the costs are then added to the utilities rate base and rates are adjusted accordingly. When the Coyote plant at Beulah was built in the early 1980's, the costs ran about \$1million per megawatt. Coyote is a 400 megawatt plant and the cost was about \$400 million. Today those costs are even higher.

HB1324 seeks to place the approval of the prudence of the expenditures at the front end of the process, rather than at the end of the process. We are seeking advance determination of the prudence because there is always the risk that the Commission might determine after the expenses have been incurred that there might have been a better option. That makes investors nervous and could lead to higher costs for the consumer.

I said earlier this has become somewhat convoluted and humorous. During the development of the concept of HB1324, we had been in contact with the PSC staff and I had at least one conversation with one of the PSC Commissioners. In response to suggestions from them, the bill you have before you was developed. Confident we would not meet with Commission resistance, I recruited bill sponsors and the bill was dropped into the House hopper. Shortly thereafter, I was informed the PSC would like us to meet with them to explain the bill, which we were happy to do. After meeting with the Commission for an hour and in a further effort to address their concerns, we decided the bill needed extensive amending and the easiest way to accomplish that was to re-write the entire bill.

If there is anything humorous about this entire process, it the fact I am now offering a HOGHOUSE AMENDMENT to my own bill. Usually hoghouse amendments are something you do to somebody else, not to yourself. HAND OUT AMENDMENTS.

Mr. Chairman and members of the Committee, the hoghouse amendment you have before you would create a new bill. All references to ratemaking principles contained in HB1324 have been eliminated, and what remains is simply the authority for the Public Service Commission to issue a pre-approval or predetermination of the prudence of expenditures for new construction, leases or improvements to existing facilities, renewable energy facilities, transmission facilities, or energy purchase contracts AND to establish a process.

Section 1 of the amendment allows the utility to file an application with the PSC for an advance determination of the prudence regarding the proposal (line 13). It then allows the PSC to utilize NDCC section 49-02-02 to bill the utility for the expenses associated with the prudency determination.

Subsection 1 sets forth the procedure and parameters of the request. In Subsection a, the utility files an application for predetermination. Subsection b requires the utility to include with the filing a projection of the costs to the date of commercial operation of the project. Subsection c authorizes the Commission to provide notice and to hold a public hearing, if appropriate. Subsection d authorizes the Commission to predetermine the reasonableness and prudency of the proposal.

Subsection 2 (line 3, page 2) requires the Commission to issue its determination no later than 7 months after the application.

Subsection 3 (line 6, page 2) requires the utility to file an annual report until the project is ready for commercial operation.

Subsection 4 (line 8, page 2) requires the utility to file a general rate case prior to commercial operation of the project which shall include a full cost of service analysis, BUT the Commission's order determining prudence shall be binding for ratemaking purposes.

And finally Subsection 5 (line 13, page 2) allows the PSC to change their predetermination, if AFTER HEARING, the PSC determines the project is no longer prudent. HOWEVER, IF THE PSC REVERSES ITS INITIAL ORDER, the utility is allowed to recover in its rates all of the expenses incurred up to the time the order is reversed.

That is the bill, Mr. Chairman and members of the committee. It still is a fairly simple concept - approve the prudency of the expenses before they are incurred, not afterward. We have worked hard to placate the Public Service Commission's concerns; there are safeguards in the bill for the consumer, for the company, and for the Public Service Commission. We believe passage of this bill will allow us to remove investor uncertainty on projects which cost hundreds of millions of dollars and perhaps allow us to borrow money at a lower interest rate, which in turn, translates into reduced cost for the consumer.

1 A BILL for an Act to create and enact a new section to chapter 49-05 of the North
2 Dakota Century Code, relating to advance determination of prudence for a public utility's
3 proposed new construction, lease or improvement of an energy conversion facility,
4 renewable energy facility, transmission facility or proposed energy purchase contract.

5 **BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:**

6 **SECTION 1.** A new section to chapter 49-05 of the North Dakota Century Code
7 is created and enacted as follows:

8 **Advance Determination of Prudence.** A public utility proposing to construct,
9 lease or make improvements to an energy conversion facility, renewable energy facility,
10 transmission facility or proposed energy purchase contract from another entity or person
11 (hereinafter referred to as an electric resource addition) for the purpose of ensuring
12 reliable electric service to its customers may file an application with the commission for
13 an advance determination of prudence regarding the proposal. The Commission shall
14 have the authority to order that expenses associated with investigating the application
15 made by the public utility for prudence of a resource addition be paid by the public utility
16 in accordance with section 49-02-02 of the North Dakota Century Code.

17 1. The Commission may issue an order approving the prudence of an electric
18 resource addition if:

- 19 a. The public utility applies for a prudence determination prior to
20 commencement of construction or purchase of an electric resource
21 addition;
- 22 b. The public utility files with its application a projection of costs to the date
23 of the anticipated commercial operation of the electric resource addition;
- 24 c. The commission provides notice and holds a hearing, if appropriate, in
25 accordance with the provisions of section 49-02-02 of the North Dakota
26 Century Code and

1 d. The commission determines that the resource addition is reasonable and
2 prudent.

3 2. The commission order shall be rendered no later than seven months after the
4 public utility files its application requesting a prudence determination of an
5 electric resource addition.

6 3. Any resource addition approved by the commission is subject to annual
7 reporting requirements until commercial operation of the resource addition.

8 4. Prior to commercial operation of the resource addition, the public utility shall
9 make a general rate case filing with a full cost of service analysis including
10 the resource addition in accordance with section 49-05-05 of the North
11 Dakota Century Code. The commission's order determining prudence of the
12 resource adjustment shall be binding for ratemaking purposes.

13 5. If at any time following an initial commission order, the commission following
14 a subsequent hearing determines that continuation of a project is no longer
15 prudent or that its prior order should be modified, the public utility shall be
16 allowed to recover in its rates, and in a timely manner consistent with the
17 public utility's financial obligations, the amounts the public utility already has
18 expensed, incurred or obligated on a project, including interest expense and
19 a return on equity invested in the project up to the time the new order is
20 entered even though the project may never be fully operational or used by the
21 public utility to serve its customers.

H. B. 1324

Presented by: Illona A. Jeffcoat-Sacco
Executive Secretary
Director, Public Utilities Division
Public Service Commission

Before: House Industry, Business and Labor
Honorable George J. Keiser, Chairman

Date: 26 January 2005

TESTIMONY

Mr. Chairman and committee members, my name is Illona Jeffcoat-Sacco. I am Executive Secretary of the Public Service Commission and Director of the Public Utilities Division. The Public Utilities Division implements the Commission's jurisdiction over telecommunications, gas and electric utilities. The Commission asked me to appear here today to testify on HB 1324. The Commission is neutral on HB 1324.

However, the Commission strongly recommends that the benefits conveyed to the investing utility by HB 1324 should only be realized if the investment that is the subject of the pre-approval is an investment in North Dakota.

Under traditional regulatory concepts, the prudence of a utility's investment is determined when that utility seeks to recover the cost of that investment in rates, which is when the investment becomes used and useful to ratepayers, or in other words, when the plant is up and running. This process has worked well here and across the country

for decades. This process can continue to work well in the future and is in no need of change.

Under HB 1324, a utility could ask the Commission to determine the prudence of an investment earlier in the process, when the investment was in the planning stages, thereby providing the utility with an additional measure of comfort as it proceeds with its investment. We can see why utilities would want this pre-approval, but we strongly believe such a benefit should not be loosely granted. Simply, the added measure of comfort provided by HB 1324 should not be available to a utility for an investment outside North Dakota. The benefit should be reserved only for North Dakota investments.

The type of process envisioned in this bill is an incentive for shareholders to develop generation. One state that we are aware of that has created a process somewhat like this is Iowa. But in Iowa they have very specifically targeted this incentive to only Iowa projects. In fact, the Governor of Iowa recently touted the incentive in his state of the state speech as a major reason six new facilities are locating there. South Dakota is aggressively targeting incentives to power development this year as well. And the state of Minnesota has never been shy about encouraging in-state power source development. We are concerned that if every state in our region is targeting incentives, but North Dakota is not, other states will use that fact to lure away projects that would otherwise be feasible here.

We would be happy to prepare a proposed amendment to implement this recommendation.

This completes my testimony. I will be happy to answer any questions you may have.

Testimony on HB 1324
Dennis Boyd
MDU Resources Group, Inc.
March 2, 2005

Good morning, Mr. Chairman and members of the committee. My name is Dennis Boyd. I am with MDU Resources Group, and appearing this morning in support of HB1324. This bill was drafted and introduced at the request of Montana-Dakota Utilities and started out with a simple concept. That concept is to obtain from the North Dakota Public Service Commission a pre-approval or predetermination of the prudence of expenditures for the construction of generation and transmission facilities before construction begins and the ratemaking principles which will be utilized when those facilities are completed and added to the rate base of the company. What started out as a simple concept, has become rather convoluted and in a sense, humorous. Before I explain, let me begin by explaining how the current process works when a regulated company determines it needs to build a generating plant or a transmission facility.

Currently and in very general terms, after a company has determined it needs additional generation or transmission facilities AND after it has obtained all of the various permits needed – air quality permits, water permits, siting permits, etc. etc., it proceeds to build the facility. Usually those facilities take several years to complete and expenses run into the hundreds of millions of dollars. After the facility is completed, the utility then files a rate case with the PSC to recover the costs. After the PSC determines the facility was needed and the expenditures were prudent, the costs are then added to the utility's rate base and rates are adjusted accordingly. When the Coyote plant at Beulah was built in the early 1980's, the costs ran about \$1 million per megawatt. Coyote is a 400 megawatt plant and the cost was about \$400 million. Today those costs are even higher – almost double.

HB1324 seeks to place the approval of the prudence of the expenditures at the front end of the process, rather than at the end of the process. We are seeking advance determination of the prudence because there is always the risk that the Commission might determine after the expenses have been incurred that there might have been a better option. That makes investors nervous and could lead to higher costs.

I said earlier this has become somewhat convoluted and humorous. During the development of the concept of HB1324, we had been in contact with the PSC staff and I had at least one conversation with one of the Commissioners. In response to suggestions from them, the bill was developed. Confident we would not meet with Commission resistance, I recruited bill sponsors and the bill was dropped into the House hopper. Shortly thereafter, I was informed the PSC would like us to meet with them to explain the bill, which we were happy to do. After meeting with the Commission for an hour and in a further effort to address their concerns, we decided the bill needed extensive amending and the easiest way to accomplish that was to re-write the entire bill.

If there is anything humorous about this entire process on the House side, it is the fact I ended up offering a HOGHOUSE AMENDMENT to my own bill. Usually hoghouse amendments are something you do to somebody else, not to yourself. Those amendments were accepted by the House, and the result is the bill you have before you this morning. Very simply, the bill gives the authority to the Public Service Commission to issue a pre-approval or predetermination of the prudence of expenditures for new construction, leases or improvements to existing facilities, renewable energy facilities, transmission facilities, or energy purchase contracts AND to establish a process. It puts the approval process at the beginning of construction.

Section 1 of the amendment allows the utility to file an application with the PSC for an advance determination of the prudence regarding the proposal (line 13). It then allows the PSC to utilize NDCC section 49-02-02 to bill the utility for the expenses associated with the prudency determination.

Subsection 1 sets forth the procedure and parameters of the request. In Subsection a, the utility files an application for predetermination. Subsection b requires the utility to include with the filing a projection of the costs to the date of commercial operation of the project. Subsection c authorizes the Commission to provide notice and to hold a public hearing, if appropriate. Subsection d authorizes the Commission to predetermine the reasonableness and prudency of the proposal.

Subsection 2 (line 3, page 2) requires the Commission to issue its determination no later than 7 months after the application.

Subsection 3 (line 6, page 2) requires the utility to file an annual report until the project is ready for commercial operation.

Subsection 4 (line 8, page 2) requires the utility to file a general rate case prior to commercial operation of the project which shall include a full cost of service analysis, BUT the Commission's order determining prudence shall be binding for ratemaking purposes.

And finally Subsection 5 (line 13, page 2) allows the PSC to change their predetermination, if AFTER HEARING, the PSC determines the project is no longer prudent. HOWEVER, IF THE PSC REVERSES ITS INITIAL ORDER, the utility is allowed to recover in its rates all of the expenses incurred up to the time the order is reversed.

That is the bill, Mr. Chairman and members of the committee. It still is a fairly simple concept – approve the prudence of the expenses before they are incurred, not afterward. We have worked hard to placate the Public Service Commission's concerns; there are safeguards in the bill for the consumer, for the company, and for the Public Service Commission. We believe passage of this bill will allow us to remove investor uncertainty on projects which cost hundreds of millions of dollars and perhaps allow us to borrow money at a lower interest rate, which in turn, translates into reduced costs for everyone.

Within the past several days, additional concerns have been raised by the Public Service Commission. We have been meeting with Commissioners and their staff in an effort to address those concerns. Consequently, I would ask that your committee not take any action on this bill today to see if we can resolve their concerns.

That concludes my testimony. I would be happy to answer any questions.



Public Service Commission

State of North Dakota

COMMISSIONERS

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E. Wefald
Cramer

Executive Secretary
A. Jeffcoat-Sacco

8 March 2005

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Honorable Duane Mutch, Chairman
Senate Industry, Business and Labor
600 E. Boulevard Avenue
Bismarck, ND 58505

Re: Proposed Amendment to Engrossed H.B. 1324

Dear Senator Mutch:

The Commission is neutral on HB 1324. However, the Commission strongly recommends that the benefits conveyed to the investing utility by HB 1324 should only be realized if the investment that is the subject of the pre-approval is an investment in North Dakota. A proposed amendment to accomplish this is attached.

The type of process envisioned in this bill is an incentive for shareholders to develop generation, and a protection for shareholders against some of the risk associated with doing so. One state that has created a process somewhat like this is Iowa, but Iowa has very specifically targeted this incentive to only Iowa projects. A similar focus for the North Dakota bill is appropriate. The added measure of comfort provided to the utility by HB 1324 should not be available to a utility for an investment outside North Dakota, but should be reserved only for North Dakota investments.

Thank you for the opportunity to provide this information and the proposed amendment. If you have any questions, please do not hesitate to call or e-mail.

Sincerely,

Illona A. Jeffcoat-Sacco
Executive Secretary
Director, Public Utilities Commission

Enclosure

cc: Senator Jerry Klein, Vice Chair
Senator Karen K. Krebsbach
Senator April Fairfield

Senator Duaine C. Espeland
Senator Dave Nething
Senator Joel C. Heitkamp

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1324

Page 1, remove lines 18 and 19

Page 2, line 2, after the period insert "For facilities located or to be located in North Dakota, the commission, in determining whether the resource addition is reasonable and prudent, shall consider the benefits of having the energy conversion facility, renewable energy facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased located in North Dakota."

Page 2, remove lines 8 and 9

Page 2, line 10, remove "addition in accordance with section 49-05-05."

Page 2, after line 19, insert:

"There is a rebuttable presumption that an energy conversion facility, renewable energy facility, transmission facility, or facility generating the energy to be purchased which is located in the state is prudent

Prepared by Public Service Commission
8 March 05

PROPOSED AMENDMENT TO ENGROSSED HOUSE BILL NO. 1324

Page 2, after line 19, insert:

"6. This section only applies if the energy conversion facility, renewable energy facility, transmission facility or facility generating the energy to be purchased is in North Dakota."

Renumber accordingly

411-05

Prepared by Dan Kuntz for
Montana-Dakota Utilities Co.

Summary Explanation of Proposed Amendments to First Engrossed HB 1324 with Senate Amendments

Background

Engrossed HB 1324 with the Senate Amendments would allow public utilities to apply to the Public Service Commission for an advanced determination of whether a power purchase contract, or the construction or lease of a generating facility or transmission line, will be deemed prudent by the Commission. The determination that a project is prudent gives a utility some assurance that it will be allowed to recover the costs of the project in its future rates.

Proposed Amendments

The proposed amendments would remove a requirement at lines 18 and 19 of Engrossed HB 1324 that the utility must apply for a prudence determination before entering into a power purchase contract or before construction of a facility commences. For power purchase contracts, leases, and small construction projects this may not be practical because the Public Service Commission proceeding may last six to seven months.

The proposed amendment to page 2, line 2 of Engrossed HB 1324, would allow the Commission, in reviewing prudence applications for facilities located in North Dakota, to consider the benefits of having the facility located in North Dakota. For example, with this amendment, a facility located in North Dakota that might be somewhat more expensive than an alternative facility located outside the state, could

nonetheless be determined to be prudent. This should provide an incentive to locate facilities in North Dakota without penalizing utilities for facilities located outside the State.

The proposed amendments would remove the requirement at lines 8, 9 and 10 of Engrossed HB 1324 that the utility must file a rate case before commercial operation of a facility. This requirement would force a utility to file for a rate change even for relatively small projects or purchase contracts.

The current language of subsection 6 of Engrossed HB 1324 would allow the Commission to consider prudence applications only for facilities located in North Dakota. The proposed amendment to page 2, lines 20 through 22, would allow for prudence applications for a facility regardless of its location. Facilities located in North Dakota, however, would be entitled to a rebuttable presumption that they are prudent. This should provide a further incentive to locate facilities in North Dakota without penalizing facilities located outside the state.