

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Otter Tail Corporation
Advance Determination of Prudence
Application

Case No. PU-06-481

Montana-Dakota Utilities Co., a Division
of MDU Resources Group, Inc.
Advance Determination of Prudence
Application

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ADVOCACY STAFF RESPONSE TO REQUEST
FOR COST CONTAINMENT INCENTIVE

The advocacy staff does not support the idea of constructing additional incentives for cost containment related to the construction of Big Stone II. We believe that the structured bidding processes, multiple co-owners, least cost planning efforts, competition within the energy sector, multiple state jurisdictions, economic development pressures, price pressures, and ultimately profit motivation provides adequate cost control incentives for the construction of Big Stone II without constructing an ad-hoc regulatory incentive.

Unless regulatory plans are properly designed and rigorously examined and tested, the end results may not be positive and could even have an adverse impact on the end cost. Sufficient time has not been afforded in this proceeding to ensure the development of an appropriate incentive, if such is possible.

209 PU-06-482

Pages: 3

Advocacy Staff Response to Request for Cost
Containment Incentive
by Public Service Commission
07/17/2007 Comm. Legal Illona, Annette Mike, ALJ . .

204 PU-06-481

Pages: 3

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Building Big Stone II as the most economical new base load generation source for Montana-Dakota and Otter Tail is based on expert assumptions and best guesses. The difficulty in setting an effective incentive regulation plan in motion can be understood when looking at market price escalations in applicable commodities and wages in just the last few years. The long-term nature of building a power plant makes establishing a reasonable end cost or an inflationary cost standard almost impossible to predict.

The advocacy staff has reviewed the Big Stone II bidding process and the plans to secure other resources as necessary and has noted no exceptions to the proposed course of action. The methods to secure resources in the most cost effective manner are in place for the construction of Big Stone II.

The advocacy staff finds a great degree of comfort in the fact that seven different utilities have reached the same conclusion that Big Stone II is the best source of new generation for their operation. The hardest review of costs will not come from a regulatory body but from those who know the business inside and out.

For too many years, utilities have not invested in new generation facilities in order to avoid the risks associated with cost recovery. The risk is very real not only in terms of advance prudence cases but also in the

political, economical and business side of trying to get rates implemented that are substantially higher than the current rates. The pressure to control costs is extremely important to maintaining industrial customer accounts, attracting new businesses to the area, selling off-system power and standing up to the scrutiny of the general public.

In summary, staff does not support an initiative to develop an incentive plan for cost containment. Staff believes there are sufficient internal, external and market-driven incentives to ensure that Big Stone II is built in a competitive manner.

Dated: July 17, 2007.

Respectfully submitted,



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