

Memo

To: Commissioners and Illona
From: Mike Diller
Date: March 6, 2007
Re: BS2 Advance Prudence Cases

Having read the testimony filed by both MDU and OTP, it is clear to me that the utility companies have spent a lot of time and money putting the Big Stone II (BS2) project together. It would be impractical to think that staff's review in this proceeding will be anything but a surface level review to determine the overall reasonableness of the project. I believe this is a fair representation when considering that the power companies themselves have spent a small fortune on consultants to design the generation plant and to conduct site location and transmission studies.

However, it is staff's desire to provide the best analysis we can with the resources we have at our disposal. Regarding resources, the staff assignments for ratepayer advocacy include Annette, Jerry, Bill and me. We also have about \$50,000 in the valuation fund that can be used for these cases.

I have included a draft list of possible areas for review at the end of this memo. The list is not intended to suggest all those areas will be covered by staff's analysis. Instead, I would like us to focus our attention on the areas that fit our skill sets and those areas that are deemed more critical. As you will note, I have organized the possible areas of investigation into one of the following categories:

- 1) Is there a need for additional generation?
- 2) What type of generation facility should be built?
- 3) Where should the plant be located?
- 4) How were agreements and contracts entered into and structured to ensure the financial success of BS2?

Following is a proposed work plan for staff. I would appreciate any input you may have with regard to our review. If you would like to see staff focus on a particular area, please provide that direction as soon as possible. Obviously, the earlier the direction is provided, the better we will be able to address your concerns.

Work Plan for Staff

Given Annette's involvement with MDU's Integrated Resource Plan, she will review both IRP's for MDU and OTP to make sure additional base load generation is needed, that better alternative generation sources or DSM programs do not exist, that there are no environmental externality values assigned and an overall review for the reasonableness of the proposed generation addition.

With Jerry's ever developing expertise in transmission planning and coordination, he will review the Interconnection Study and Delivery Service Study for overall reasonableness. Since these studies are ultimately approved by MISO, it will give Jerry an opportunity to participate and make use of his MISO contacts during the review process. Jerry will also review the cost allocation of the transmission facilities among the participating partners. To the extent possible, he will compare the cost differential between the additional transmission facilities planned for South Dakota and Minnesota for BS2 and the cost of transmission facilities that would be needed if the resource addition was placed next to the existing Coyote station in North Dakota.

Staff will also contract with Terry Deason, a Florida consultant working for the law firm of Radey, Thomas, Yon and Clark to help in its investigation. As you recall, staff issued an RFP for evaluating these cases and none were received. The lack of a response occurred because regulatory consultants are quite busy these days and because advance prudence cases on generation facilities are quite unique and complex. Having received no bids, staff will sole source contract with Mr. Deason for consulting services.

Mr. Deason has spent many years working for the Office of Public Counsel representing consumers before the Florida Public Service Commission; several years as an Executive Assistant; and then as a commissioner for 16 years. He has a Masters in accounting and has presented testimony on the behalf of ratepayers as an expert witness on ratemaking issues. I have attached his professional work experience for your review.

Mr. Deason will be assigned the task of reviewing and evaluating the bid processes, bid selections and contractual arrangements to ensure that best business practices were employed. He will review the overall reasonableness of the total cost projections and the allocation of estimated costs to the participating partners. To the extent possible, his testimony will incorporate and summarize the work of other staff members.

My work will include reviewing the site selection process and helping to coordinate the activities of assigned staff.

Bill will review staff testimony, prepare witnesses and cross-examine the witnesses of the other parties to the case.

Possible Areas for Review

Question 1: Is there a need for additional generation?

Review IRP's to determine need for BS2.

- Reasonableness of demand forecasts
- Consideration of DSM alternatives
- Reasonableness of planning assumptions and reserve requirements

Review monthly fuel clause adjustments to assess the cost and variability of purchased power compared to BS2 projections

Review history of MISO market prices for energy

Question 2: What type of generation facility should be built?

Determine if environmental externality factors have been included

Make sure all energy resources have been fairly considered

Review parameters used to determine that a base load coal plant is the best use of capital

Review sizing (630 MWs) of BS2 and economies of scale

Reasonableness of projected operating parameters of BS2 including heat rates and availability factors

Question 3: Where should the plant be located?

Review decision making models to make sure environmental externality values have not been included in the determination that BS2 represents the least cost resource available

Review inputs to the site selection models for reasonableness. Revise any questionable inputs and rerun the model if necessary

Review the cost of generation using lignite compared to subbituminous coal

Review efficiencies of using an existing site and sharing existing infrastructure

Question 4: How were agreements and contracts entered into and structured to ensure the financial success of BS2?

Review bid processes

Review proposals made by non-selected entities and compare to selected bids

Reasonableness of the Joint Ownership Agreement including governance, operating parameters and cost sharing

Reasonableness of cost projections for BS2 including: capital expenditures; cost of capital (implicit rate of return); O&M expenses; and fuel costs

Reasonableness of coal procurement contract and associated costs

Reasonableness of rail agreement and associated costs

Reasonableness of projected transmission costs and cost sharing among joint participants

Review projected construction time lines of BS2

Impacts of anticipated transmission upgrades on adequacy and overall reliability of the grid

Determine the possible need for some post-decision reporting requirements

Determine the need for any conditions to be placed on the approval of BS2

Determine if there are recommended enhancements to the review process that could be incorporated in future advance prudence determination cases