

LINDQUIST & VENNUM P.L.L.P.

4200 IDS CENTER
80 SOUTH EIGHTH STREET
MINNEAPOLIS, MN 55402-2274
TELEPHONE: 612-371-3211
FAX: 612-371-3207

IN DENVER:
600 17TH STREET, SUITE 1800 SOUTH
DENVER, CO 80202-5441
TELEPHONE: 303-573-5900
FAX: 303-573-1956

ATTORNEYS AT LAW

www.lindquist.com

TODD J. GUERRERO
612/371-3258
tguerrero@lindquist.com

August 31, 2007

VIA FEDERAL EXPRESS & EMAIL

Illona Jeffcoat-Sacco
Executive Secretary
North Dakota Public Service Commission
State Capitol
Bismarck, ND 58505

**Re: Montana Dakota Utilities Co., and Otter Tail Corporation; Advance
Determination of Prudence, Big Stone II Generating Station
Case Nos. PU-06-481 and PU-06-482**

Dear Ms. Jeffcoat-Sacco:

On August 28, 2007, pursuant to NDCC § 28-32-25, the Commission advised the parties in the above matter of its intention to take official notice of the Administrative Law Judges' August 15, 2007 Findings of Fact, Conclusions of Law, and Recommendation in the following Minnesota Public Utilities Commission combined dockets: *In the Matter of the Application of Otter Tail Power Company and Others for Certification of Transmission Facilities in Western Minnesota and In the Matter of the Application to the Minnesota Public Utilities Commission for a Route Permit for the Big Stone Transmission Project in Western Minnesota*, OAH No. 12-2500-17037-2, MPUC Dkt. No. CN-05-619 and OAH No. 12-2500-17038-2, MPUC Dkt. No. TR-05-1275 (hereinafter, "ALJs' Order").

The ALJs' Order recommended that the Minnesota Public Utilities Commission (MPUC) grant the Applicants' Petition for a Certificate of Need (CON) for the construction and operation of the Minnesota portions of two jurisdictional high-voltage transmission lines and related facilities that will interconnect the Big Stone Unit II to the regional grid, and thereby recommended authorizing construction of the same. The ALJs' Order further recommended that the MPUC issue route permits for the transmission lines (a 230 kV line from the South Dakota border to the Morris, MN Substation and a 345 kV line from the South Dakota border to the Granite Falls, MN Substation) along the route preferred by the Big Stone II applicants.

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Cover letter w/MN PUC Settlement Agreement and affidavit of
service
Lindquist & Vennum

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The ALJs' Order also recommended, among other things, that the MPUC consider imposing one or more of the conditions suggested by the Minnesota Department of Commerce ("Department") in the CON docket: (a) requiring that the Big Stone II applicants develop and submit to the MPUC a plan to offset the carbon dioxide emissions from Big Stone Unit II associated with serving Minnesota load (i.e., approximately one-half of the plant's expected carbon dioxide emissions); (b) requiring that the Big Stone II applicants develop and issue a request for proposals for at least 120 MW of community-based energy development (C-BED) to be located in the MN counties in which the proposed lines will be constructed; (c) Big Stone II applicants' compliance with various energy conservation measures; (d) requiring that Otter Tail phase out its Minnesota declining block rates in its next rate case; and (e) requiring that the Big Stone II applicants work with the states of South Dakota and Minnesota to resolve and report on water resource issues at Big Stone Lake for Big Stone Unit II. *See, e.g.*, ALJs' Order at pages 88-89.

The Applicants in the Commission's above docket wish to advise the Commission that they, along with their co-owners, have today reached an agreement with the Department under which the Big Stone II applicants and the Department jointly state in the CON docket that the agreement satisfies the Department's concerns expressed in the Minnesota CON docket. Further, under the agreement, the Big Stone II applicants agree to undertake the Department-recommended conditions. In conjunction with the Department, the Big Stone II applicants expect to file the settlement agreement today with the MPUC. The parties are jointly requesting that the MPUC approve the Minnesota CON and route permits, subject to the conditions set forth in the agreement. A summary explanation of the agreement and the agreement itself (without appendices) are attached as Exhibits A and B.

Chiefly among the conditions in the agreement, the Big Stone II Minnesota load-serving entities will offset 100% of the carbon dioxide (CO₂) emissions attributable to the generation of electricity at Big Stone II for customers in Minnesota. Montana-Dakota Utilities Company serves no Minnesota load, and there will be no costs borne by its North Dakota consumers for CO₂ offsetting. Under the settlement agreement, the Department will support Otter Tail's recovery from Minnesota consumers of the costs associated with offsetting the carbon dioxide emissions attributable to the generation of electricity at Big Stone II for customers in Minnesota. Otter Tail will not seek recovery of these costs from its North Dakota (or South Dakota) consumers, nor does the Minnesota Department of Commerce expect that such recovery would be appropriate.

The settlement agreement also calls for the employment of mercury emission technology "most likely to result in the removal of at least 90 percent of the mercury emitted from the [BSP I and BSP II generation units]," to be implemented within four years of the commercial operation date of Big Stone II. (The prudence of this investment in mercury reduction technology, which would be required by the federal Clean Air Mercury Rule (CAMR) in 2018, is part of the rationale that Otter Tail and Montana-Dakota put forth in the above advance determination of prudence docket.)

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In addition, under the settlement agreement, the Big Stone II owners agree to employ groundwater for drought protection at Big Stone II, and undertake various operational and reporting measures designed to address water resource issues and interests. Otter Tail also agrees to propose the phased elimination of its declining block rate program in its next Minnesota rate case, and meet Minnesota energy conservation obligations (Montana-Dakota serves no Minnesota load and therefore is not subject under the agreement to any such conservation obligations).

Last, the Big Stone II applicants with load in Minnesota agree to achieve a percentage of their renewable energy objective from CBED projects in an amount that would have the current Minnesota utilities obtaining 180 MWs from such projects, and which projects are otherwise economic. Again, because Montana-Dakota serves no Minnesota load, it undertakes no obligation for these C-BED commitments. Where Otter Tail pursues CBED projects because of its commitments under the settlement agreement which it would not have pursued based on its least cost planning, the Department also agrees to support Otter Tail's recovery of those incremental costs from Minnesota consumers only.

Otter Tail and Montana-Dakota appreciate the Commission's ongoing interest with respect to the Big Stone II project. Because none of the commitments made in the settlement agreement affects North Dakota consumers or otherwise impacts upon the Applicants' advance determination of prudence application, we are providing the Commission with a copy of the Minnesota settlement agreement for informational purposes and to provide the Commission an opportunity to ask questions of the Applicants about it. Montana-Dakota and Otter Tail are prepared to address any questions the Commission may have about the proposed commitments (contingent upon approval by the MPUC) to be made in the Minnesota CON docket.

Thank you for your consideration.

Very truly yours,

A handwritten signature in black ink that reads "Todd J. Guerrero/ng". The signature is written in a cursive style with a slanted baseline.

Todd J. Guerrero, On Behalf of Applicants
Montana-Dakota Utilities Co., and
Otter Tail Corporation

TJG/kas

cc: Attached Service List (via email and regular mail)