

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

**Montana-Dakota Utilities Co., a Division
of MDU Resources Group, Inc.
Discontinue Prudence Big Stone II
Application**

Case No. PU-09-731

**Montana-Dakota Utilities Co., a Division
of MDU Resources Group, Inc.
Deferred Accounting - Big Stone II
Application**

Case No. PU-09-733

ORDER ADOPTING SETTLEMENT

June 25, 2010

Appearances

Commissioners Kevin Cramer, Tony Clark, and Brian P. Kalk.

Daniel S. Kuntz, Associate General Counsel, MDU Resources Group, Inc., PO Box 5650, Bismarck, ND 58501-5650.

Annette Bendish, Legal Counsel, Public Service Commission, 600 East Boulevard Avenue, Department 408, Bismarck, North Dakota 58505-0480, attorney for the Public Service Commission Advocacy Staff.

Derrick Braaten, Sarah Vogel Law Partners, 222 North 4th Street, Bismarck, North Dakota 58501-4004, attorney for the Dakota Resource Council and Mark Trechock.

Illona A. Jeffcoat-Sacco, General Counsel, Public Service Commission, 600 East Boulevard Avenue, Department 408, Bismarck, North Dakota 58505-0480, attorney for the Public Service Commission.

Al Wahl, Administrative Law Judge, Office of Administrative Hearings, 1701 North Ninth Street, Bismarck, North Dakota 58501-1882, appearing as hearing officer.

Preliminary Statement

On August 27, 2008, the Commission adopted an order approving the request of Montana-Dakota Utilities Co. (Montana-Dakota) for an advance determination of prudence for its ownership in the proposed Big Stone II generating facility and associated transmission facilities, Case No. PU-06-482.

On December 2, 2009, Montana-Dakota filed an application for a determination that Montana-Dakota's continued participation in the Big Stone II Generating Station is no longer prudent, Case No. PU-09-731.

On December 4, 2009, Montana-Dakota filed an application for authority to use deferred accounting for costs related to Montana-Dakota's efforts in securing new generation, primarily the Big Stone II Generating Station, until disposition of its next general electric rate case, Case No. PU-09-733.

On March 10, 2010, the Commission issued its Notice of Hearings consolidating Case No. PU-09-731 and Case No. PU-09-733 for a public hearing on May 5, 2010, and specifying the issues to be considered:

The issue to be considered in Case No. PU-09-731 is whether Montana-Dakota's continued participation in the Big Stone II Generating Station is no longer prudent.

The issue to be considered in Case No. PU-09-733 is whether authorization for deferred accounting of costs incurred during efforts to secure new electric generation, including participation in the Big Stone II project, is in the public interest.

On March 19, 2010, the Dakota Resource Council and Mark Trechock filed a Petition to Intervene in Case No. PU-09-731 and Case No. PU-09-733.

On March 24, 2010, the Commission issued its Order Granting Intervention to the Dakota Resource Council and Mark Trechock in Case No. PU-09-731 and Case No. PU-09-733.

On April 14, 2010, Commission Advocacy Staff filed a Settlement Agreement between Montana-Dakota and the North Dakota Public Service Commission Advocacy Staff in Case No. PU-09-731 and Case No. PU-09-733. The participants to the Settlement Agreement agree that Montana-Dakota's discontinuation of participation in the project is prudent and Montana-Dakota should be authorized to recover costs related to the Big Stone II generation project, including a monthly carrying charge of 10.016 percent for the period from November 2, 2009 up until the time recovery of costs commences, but excluding a return on investment during the recovery period. The Settlement Agreement provides for recovery of costs over 36 months through the energy adjustment. The settlement is without prejudice to Montana-Dakota's inclusion of recovery of costs incurred during efforts to secure other new electric generation in a general rate filing request.

On May 5, 2010, the public hearing was held in the Commission Hearing Room at the State Capitol in Bismarck, North Dakota.

Montana-Dakota's application and testimony show that the Big Stone II project under Montana-Dakota's original prudency request was a 600 to 630 megawatt electric generation plant planned to meet the reasonably anticipated electric generation needs of

seven utilities. In the fall of 2007, two utilities representing 27.166 percent ownership interest withdrew from the project. The remaining project participants determined that a 500 to 580 megawatt electric generation plant could be supported as cost effective and pursued additional participants for the project. On September 11, 2009, another participant representing 19.333 percent ownership interest, who was also the project operator, withdrew from the project. The intended ownership interest of the remaining participants was 337 megawatts. The remaining participants attempted but were unable to secure commitments for new participants.

The Commission is convinced from the information provided that resizing, redesigning and re-permitting the plant would result in an anticipated commercial date that would not support the needs of the project participants. Further, that sufficient participation could not be obtained for a project within the design and permit scope of the Big Stone II Project.

At its May 25, 2010 work session concerning these proceedings, the Commission expressed concern about the inclusion in the Settlement Agreement of a monthly carrying charge on the North Dakota share of Big Stone II generation costs from the date on which the company ceased accumulating an allowance for funds used during construction (AFUDC) on the construction work in progress balance, which is November 2, 2009, up until the recovery of costs commences. On May 27, 2010, Montana-Dakota responded that it is amenable to replacing the 10.016 percent rate of return with its average 2009 AFUDC rate of 9.18 percent during the period preceding entry of a Commission order.

The settlement, with the conditions ordered in this Order, results in benefits to consumers. If not for the statute regarding advance determination of prudence and the Settlement Agreement, Montana-Dakota will request recovery of Big Stone II costs as rate base investment in a rate case proceeding. Rate base is typically depreciated over the life of the investment and the company is entitled to a reasonable return on the balance of investment that hasn't been depreciated. The settlement provides a recovery period of 36 months with no return on investment during the recovery period.

The effect of the settlement, with the conditions ordered in this Order, on a typical residential customer consuming 750 kilowatt-hours is approximately \$1.50 per month for three years.

Having considered this matter, the Commission has determined that the Settlement Agreement filed April 14, 2010 is reasonable and should be approved subject to the conditions stated below. Therefore, the Commission makes the following:

Order

The Commission orders:

1. The Settlement Agreement filed April 14, 2010, a copy of which is attached to this Order and made a part of this Order, is APPROVED, subject to the provisions in Ordering Paragraphs 4, 5 and 6, below.

2. Montana-Dakota's discontinuation of participation in the Big Stone II Project is prudent pursuant to the Settlement Agreement and North Dakota Century Code § 49-05-16(5).

3. Montana-Dakota is authorized recovery of the costs incurred in the Big Stone II project, pursuant to the Settlement Agreement.

4. Montana-Dakota shall apply 9.18 percent rate of return on the North Dakota share of Big Stone II generation costs from the date on which the company ceased accumulating an allowance for funds used during construction (AFUDC) on the construction work in progress balance, which is November 2, 2009, up until the recovery of costs commences.

5. Montana-Dakota shall, within 15 days, file a rate schedule and documentation supporting calculation of the rate schedule, consistent with this Order and Settlement Agreement, in order to implement rates to become effective for bills rendered on and after August 1, 2010. The Commission will not suspend the rate schedule, but will promptly issue a Notice of Opportunity for Hearing on the rate schedule submitted by Montana-Dakota. Any amount of over- or under-collection of cost recovery resulting from final implementation of the rate schedule shall be addressed as called for by the Settlement Agreement.

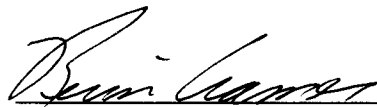
6. Montana-Dakota shall draft a bill insert for Commission approval regarding the recovery of Big Stone II generation costs. Montana-Dakota shall include the approved insert with customer bills every third month during the 36 month recovery period.

7. Montana-Dakota's Application for Deferred Accounting regarding costs incurred during its participation in the Big Stone II Project, Case No. PU-09-733, is rendered moot by this Order and is DISMISSED.

PUBLIC SERVICE COMMISSION



Tony Clark
Commissioner



Kevin Cramer
Chairman



Brian P. Kalk
Commissioner

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SETTLEMENT AGREEMENT

This Settlement Agreement is entered into by and between the North Dakota Public Service Commission Advocacy Staff (“Staff”) and Montana-Dakota Utilities Co., a Division of MDU Resources Group, Inc. (“Montana-Dakota”) (collectively, “the Parties”). The Parties agree that except as expressly provided herein, this Settlement Agreement resolves all outstanding issues in the above-captioned proceedings.

BACKGROUND

These proceedings involve two separate but related matters: (1) Montana-Dakota’s request for a determination that its continued participation in the Big Stone II project is no longer prudent, filed with the Commission on December 2, 2009; and, (2) Montana-Dakota’s request, filed with the Commission on December 4, 2009, for authority for deferred accounting of costs related to Montana-Dakota’s efforts in securing new electric generation, primarily the Big Stone II Generating Station, until disposition of its next general electric rate case.

The Big Stone II project was a proposed multi-owner coal-fired generating plant to be located at the site of the existing Big Stone Generating Plant near Big Stone city, South Dakota. Prior to Otter Tail Power Company’s (OTP) withdrawal from the project in September 2009, Montana-

Dakota had a 26.54% share of the project and a corresponding responsibility for shared project costs.¹

In June of 2005, Montana-Dakota entered in to project agreements with six other utilities for purposes of pursuing the project.² At that time, the participants applied for the necessary permits, began preliminary engineering work, and began other development work for the project. The Commission issued an Advance Determination of Prudence for Montana-Dakota's participation in the project in August 2008, in Case No. PU-06-482, for a minimum of 121.8 MW up to a maximum of 133 MW and proportionate ownership share of the associated transmission electric resource additions. The Commission's order was based on an updated analysis by the Big Stone II participants for the cost of a 500 MW to 580 MW facility with an on-line date of mid-2013. Also, other permits were received from the South Dakota Public Utilities Commission ("SDPUC"), who approved the project Site Permit in July 2006, and the Minnesota Public Utilities Commission ("MPUC"), who issued a Certificate of Need ("CON") for the Big Stone II transmission lines in March 2009. The project also obtained a Water Allocation Permit, Air Permit, and other necessary permits, and completed a Federal Environmental Impact Statement for the project. Where applicable, these permits were generally based upon a generating plant capacity of between 500 and 600 MW. Montana-Dakota has incurred approximately \$13.9 million for the permitting, engineering and other development activities for the project to date. The North Dakota jurisdictional share of the total costs is 69.351586% or approximately \$9.6 million.³

On September 11, 2009, OTP withdrew from further participation in the project. Montana-Dakota was one of four remaining participants after OTP's withdrawal. The remaining

¹ Or more precisely 26.544622425% based on Montana-Dakota's proportion of committed off-take: 116 MW of a total of 437 MW committed. Montana-Dakota's share of the project increased after Great River Energy ("GRE") and Southern Minnesota Municipal Power Agency ("SMMPA") withdrew from the project in September 2007. Without new participants to make up for GRE and SMMPA, Montana-Dakota's proportionate share of off-take was larger than its original share of 19.3333% of a total 600 MW committed.

² Preliminary investigation of the feasibility of a second unit at the Big Stone site and other project activities had been undertaken before the project group agreements were finalized and executed.

³ The jurisdictional allocation percentage is based on the system twelve month peak demand factor, or 69.351586% to North Dakota.

participants sought but were unable to obtain commitments from new project participants largely because of regulatory, legislative and environmental concerns affecting the project as well as the economic downturn. On November 2, 2009, Montana-Dakota and the other remaining participants determined it was no longer feasible to continue the development of the Big Stone II project as the project size, reflecting the remaining participants' combined MW shares, was smaller than the designed and permitted plant size. Thus, the project lacked the envisioned economies of scale, and the validity of the permits issued for a larger size plant was in question. The costs related to Montana-Dakota's efforts in securing new electric generation fall generally into the following cost categories: Engineering, project development, permitting, legal, other expenditures, and Allowance for Funds Used During Construction ("AFUDC"). In addition to the Big Stone II project costs, the costs include \$2.1 million associated with the Lignite Vision 21 Project and \$332,000 associated with the Milton R. Young III Project.

TERMS

Montana-Dakota and the Commission Advocacy Staff (collectively "the Parties") agree to the provisions as defined below and supported by this Settlement Agreement.

I. Recovery of Costs related to the Big Stone II Project

The Parties agree that:

- A. Montana-Dakota's discontinuation of participation in the project is prudent and therefore Montana-Dakota should be authorized to recover the portion of costs related to the Big Stone II generation project ("Big Stone II Generation Costs") as detailed in this Section I.
- B. Approximately \$13.9 million represents the total amount of Big Stone II Generation Costs incurred by Montana-Dakota to date; of which \$9.6 million represents North Dakota's jurisdictional share of such costs.⁴

⁴ Id.

- C. The recovery of Big Stone II Generation Costs will occur over 36 months, beginning with the first day of the first calendar month by which implementation can practically be achieved by Montana-Dakota following the Commission's approval of this Settlement Agreement.
- D. Montana-Dakota's recovery will be in the form of an annual rate that shall be established based on an amount equal to one-third of the estimated total recovery, divided by the estimate of retail energy sales (in kWh) over the twelve-month period for which the rate will be in effect, to arrive at a rate per kWh. This rate will be applied to all customer bills as part of the Fuel Clause Adjustment ("FCA") based on kWhs consumed.
- E. At least 30 days prior to the end of each annual period, Montana-Dakota shall make a report to the Commission to show the total amount to be recovered, as well as the amount recovered and the amount of actual kWh retail energy sales for the period (up to the time of the report). Montana-Dakota will also calculate any amount of over- or under-collection (based on actual amounts up to the time of the report and estimated sales for the remainder of the annual period), and that amount (the "True-up Amount") shall be added to or subtracted from the amount to be recovered in the next annual period. Any True-up Amount remaining at the end of the 36 month recovery period shall be collected from customers (for any under-collection) or refunded to customers (for any over-collection) through the FCA surcharge adjustment.
- F. Montana-Dakota shall include in its total recovery amount a monthly carrying charge on the North Dakota share of Big Stone II Generation Costs for the period from November 2, 2009 (the date in which it ceased accumulating AFUDC on the construction work in progress balance) up until when the recovery of costs commences as described in paragraph C. above. The carrying charge shall be Montana-Dakota's rate of return as approved in its most recent rate case (10.016 percent).
- G. An estimate of the rate described above based on an assumed implementation date of June 1, 2010, a North Dakota balance of \$10.2 million including carrying charges

through May 31, 2010 and projected kWh sales is \$0.00214 per kWh, or \$1.61 per month for a typical residential customer using 750 kWh.

II. Recovery of Costs related to the Lignite Vision 21 Project and Milton R. Young III Project

The Parties agree this settlement is without prejudice to Montana-Dakota's inclusion of recovery for costs related to the Lignite Vision 21 Project and the Milton R. Young III Project in its next general rate filing request. It shall be Montana-Dakota's burden of proof in any such proceeding to show that cost recovery is appropriate.

III. Miscellaneous

A. Basis of Settlement Agreement

It is agreed this Settlement Agreement is a negotiated settlement agreement subject to approval by the Commission.

B. Effect of the Settlement Negotiations

It is understood and agreed that all offers of settlement and discussions related to this Settlement Agreement are privileged and may not be used in any manner in connection with proceedings in this case or otherwise, except as provided by law. In the event the Commission does not approve this Settlement Agreement, the Settlement Agreement will not be admissible as evidence in this or any other proceeding and no part thereof may be used by any party for any purpose in this case or in any other.

C. Applicability and Scope

This Settlement Agreement shall be binding on the Parties, and their successors, assigns, agents, and representatives. Consistent with the Commission's settlement guidelines, this Settlement Agreement does not set policy or overturn precedent. This Settlement Agreement shall not in any respect constitute an agreement, admission or determination by any of the Parties as to the merits of any specific allegation or contention made by the Parties in this proceeding.

D. Effective Date

This Settlement Agreement shall be effective on the date of the Commission Order approving the Settlement Agreement.

E. Modification

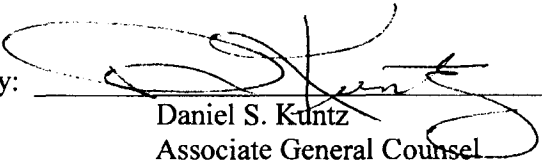
If the Commission Order modifies or conditions approval of this Settlement Agreement, it shall be deemed terminated if either Party files a letter with the Commission within three (3) business days of the date of such Order stating that a condition or modification to the Settlement Agreement is unacceptable to such Party.

CONCLUSION

The Parties have agreed to the forgoing terms to resolve the contested issues in the above-captioned proceedings. These terms are a result of negotiations between the Parties, are in the public interest and will result in reasonable electric rates. For these reasons, the Parties urge the Commission to approve the Settlement Agreement.

[Signature Pages Follow]

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

By: 
Daniel S. Kuntz
Associate General Counsel

Dated this 14th day of April 2010.

North Dakota Public Service Commission Staff

By: Annette Bendish
Annette Bendish
Counsel to Advocacy Staff

Dated this 14 day of April 2010.