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December 27, 2010

Executive Secretary
North Dakota Public Service Commission
State Capitol Building
Bismarck, ND 58505

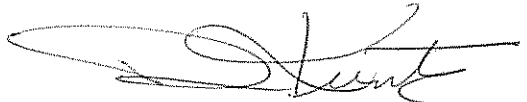
Re: Case No. PU-10-124

Montana-Dakota Utilities Co. (Montana-Dakota), a Division of MDU Resources Group, Inc. herewith submits its Post-Hearing Brief and Proposed Findings of Fact, Conclusions of Law and Order in the above referenced case.

The original and seven (7) copies have been provided to the Commission and one copy has been provided to the parties noted below.

Please acknowledge receipt by stamping or initialing the duplicate copy of this letter attached hereto and returning the same in the enclosed self-addressed stamped envelope.

Sincerely,



Daniel S. Kuntz (ID #03490)
Associate General Counsel
MDU Resources Group, Inc.

Attachment

cc: Mr. Richard Savelkoul
Mr. Jim Roache
Mr. Scott Skokos (on behalf of the Missouri Valley Resource Council)

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

**Montana-Dakota Utilities Co., a
Division of MDU Resources Group, Inc.
Electric Rate Increase Application**

**Case No. PU-10-124
Post Hearing Brief of
Montana-Dakota Utilities Co.**

On April 19, 2010, Montana-Dakota Utilities Co., a Division of MDU Resources Group, Inc., (“MDU” or “Company”) filed an application to increase its rates for electric utility service to provide additional annual revenue of \$15,396,303, or a 14 percent increase, over current rates. The application was filed pursuant to N.D.C.C. Chapter 49-05 and complied with the filing requirements set forth in N.D.C.C. § 49-05-04.1(2):

A public utility selecting a current or future test year shall present the following information:

- a. A comparison of forecast data to historical period data to demonstrate the reliability and accuracy of the utility’s forecast including a comparison of the prior years’ forecast or budgeted data to actual data for those periods.
- b. A statement that the public utility’s forecast is reasonable, reliable, and was made in good faith and that all basic assumptions used in making or supporting the forecasts are reasonable, evaluated, identified, and justified to allow the commission to test the appropriateness of the forecast.
- c. A statement that the accounting treatment that has been applied to anticipated events and transactions in the forecast is the same as the accounting treatment to be applied in recording the events once they have occurred.

On July 6, 2010, MDU filed an update to its application in accordance with N.D.C.C. § 49-05-04.1(3) to reflect removal of the Big Stone II generation development costs that were addressed in Case No. PU-09-733. The amended application requested an annual increase of \$13,300,123 or 12 percent. Exhibits MDU 1, MDU 8.

At the hearing in this proceeding, MDU witness Rita Mulkern presented testimony and supporting schedules to reflect reductions in the request resulting from:

1. A partial settlement agreement reached between MDU and Public Service Commission Advocacy Staff ("Staff") filed June 16, 2010 relating to the rate of return on MDU's rate base which, if the settlement was accepted, effectively reduced the Company's request to \$11,519,000. Exhibit MDU 2.
2. A partial settlement agreement reached between MDU and Staff dated November 8, 2010 relating to certain issues raised in the responsive testimony of Staff witness George Mathai filed October 15, 2010. The partial settlement agreement, if accepted, further reduced the Company's request by \$1,220,000. Exhibit MDU 3.
3. The effect of bonus depreciation allowed by the Small Business Jobs Act which became effective September 27, 2010 including its effect on North Dakota investment tax credit treatment; the correction of an error in the original filing relating to accumulated deferred income taxes (See Exhibit CAS 15); and a reduction in the depreciation rate for the Diamond Willow II and Cedar Hills wind projects. The adjustments reduced the request by \$1,474,000. Exhibit MDU 8R, p. 5-7.

The total of the above adjustments reduced MDU's request to \$8,825,000 or 7.7 percent. Exhibit MDU 8R.

The Staff recommended the Company's rate request be further reduced to disallow recovery of operating expenses and a return on investment for the Diamond Willow and Cedar Hills wind generation projects. The Staff maintained MDU had not met its burden of proof that there was a need for the projects or that they were the least cost generation alternatives at the time of construction. The Staff also recommended the Commission disallow 60 percent of MDU's expenses for employee incentive

compensation and 50 percent of its expenses for board of director's fees and expenses on grounds that such costs benefit both shareholders and customers.

Staff's recommendations are without merit or evidentiary support. The wind projects are used and useful and provide a benefit to MDU's North Dakota electric customers, and MDU's investment in the projects was prudent. Similarly, incentive compensation and director's fees are legitimate business expense within the deference and judgment of MDU's management and Staff failed to show any abuse of management's discretion with regard to these expenses.

The Burden Of Proof

The Staff's recommendation to exclude the expense and investment associated with the wind projects is based upon its position that MDU failed to meet its burden of proof with respect the need for and prudence of those investments. The Staff's position, however, does not reflect a correct application of the burden of proof as an evidentiary standard. The North Dakota Supreme Court summarized the evidentiary principle of "burden of proof" in Helbling v. Helbling, 541 N.W.2d 443, 445-446 (N.D. 1995):

The burden of proof has two components: the burden of going forward with the evidence and the burden of persuasion. (Citation omitted) The burden of persuasion, or risk of non-persuasion, does not shift: it remains with the party having the burden of proof. (Citation omitted) The burden of going forward with the evidence will shift: it may rest . . . at one time upon one party and at another time upon the other. (Citation omitted) The plaintiff or moving party generally bears the burden of proof. (Citation omitted) If the party bearing the burden of proof presents evidence strong enough, if uncontradicted, to support a finding in her favor, that party has made a *prima facie* case. (Citation omitted) When the party with the burden of proof establishes a *prima facie* case, "the burden of going forward with the evidence . . . shifts to the defendant. If the defendant can impair the *prima facie* quality of [i.e., rebut] the case against him, the burden [of going forward] returns to the party having the burden of proof." (Citation omitted) If the party having the burden of proof establishes a

prima facie case, this party will prevail unless the opposing party offers “proof to the contrary.” (Citation omitted)

In Helbling, the District Court held the plaintiff did not meet her burden of proving that a change in the defendant’s child support obligation was justified based upon his net monthly income. The Supreme Court reversed the District Court holding that the plaintiff made a *prima facie* case for increasing the required child support payments when she showed an increase in the defendant’s income and the District Court erred in failing to shift to the defendant the burden of going forward to rebut the *prima facie* case. The Court stated that when a party makes a *prima facie* case, that party will prevail when its opponent fails to offer “proof to the contrary.”

Along with the burden of proof, the Commission must consider the appropriate “standard of proof” in an administrative proceeding under the North Dakota Administrative Agency’s Practices Act at N.D.C.C. Chapter 28-32. As the party with the burden of proof in this administrative proceeding, MDU has the burden of proving by a “preponderance of the evidence” that it is entitled to the requested increase in rates. Sjostrand v. North Dakota Workers Compensation Bureau, 2002 N.D. 125, ¶ 24-30, 649 N.W.2d 537. The function of a standard of proof is to instruct the factfinder concerning the degree of confidence our society thinks the factfinder should have in the correctness of facts or conclusions for a particular type of adjudication. North Dakota State Board of Medical Examiners v. Hsu, 2007 N.D. 9, ¶ 16, 726 N.W.2d 216. The standard of proof serves to allocate the risk of error between the litigants and to indicate the relative importance attached to the ultimate decision. Id. The “preponderance of the evidence” standard of proof is met by evidence which is more convincing or of greater weight than the opposing evidence; namely, evidence which as a whole shows a fact to be proved is

more probable than not. Kraft v. North Dakota State Board of Nursing, 2001 N.D. 131, ¶ 21, 631 N.W.2d 572. As applicable to this proceeding, the preponderance of evidence standard does not require evidentiary proof of irrefutable mathematical certainty as suggested by the Staff. It also does not require evidentiary proof beyond a reasonable doubt, as required in criminal proceedings, or even evidentiary proof of a clear and convincing nature. See Sjostrand v. North Dakota Workers Compensation Bureau, supra. It certainly does require proof of a negative which is the practical effect of Staff's position. Helbling v. Helbling, supra.

The preponderance of the evidence in this proceeding establishes that MDU is entitled to the requested rate relief. Assertions or arguments by Staff that MDU did not meet its burden of proof are not evidence. These assertions and arguments neither contradict the factual evidence presented by MDU nor do they meet Staff's burden of going forward with factual evidence.

MDU Met Its Burden Of Proof By The Preponderance Of The Evidence.

Through its application as supported by the direct pre-filed testimony of its witnesses, MDU established a *prima facie* case for its requested general increase in rates. See N.D.C.C. § 49-05-04.1. In response, the Staff presented the testimony of George Mathai who recommended various adjustments to MDU's application including the disallowance of rate base and operating expenses associated with MDU's Diamond Willow and Cedar Hills wind projects, as well as reductions in MDU's test year expenses for incentive compensation and board of director's fees and expenses. Mr. Mathai's recommendations were largely unsupported by factual evidence. What little factual

evidence that was offered by Mr. Mathai was refuted and certainly did not outweigh the unrefuted evidence offered by MDU on these issues.

Wind Generation Projects

Like most regulatory jurisdictions, North Dakota law has adopted a two step process in the determination of a utility's rate base. First, N.D.C.C. § 49-06-01, requires the Commission to determine the value of the utility's property "used and useful for the service and convenience of the public."¹ Second, § 49-06-02, directs that the value of such used and useful property "is the money honestly and prudently invested therein by the utility. . ." Under this approach, a prudent investment found to be used and useful is incorporated into a utility's rates. Jonathan A. Lester, *The Used and Useful Test: Implications For A Restructured Electric Industry*, 23 Energy L.J. 349 (2002).

Ascertaining a utility's revenue requirement begins with deciding what property is committed to public service. James J. Hoecker, *Used and Useful: Autopsy of a Ratemaking Policy*, 8 Energy L.J. 303, (1987).

Generally speaking, the case law regards costs incurred and investments made used and useful if: (1) there is a direct and immediate benefit to customers; traditionally, the investment is in a plant that is operational now or in a future test year or in the period during which the rates may reasonably be expected to be in effect; (2) the investment or expense, even if not affording an immediate tangible benefit, meets certain secondary benefit criteria, such as reasonably foreseeable plant completion, a necessary cost of continuing business (including land acquisition to enhance gas reserves or other reasonable plans and commitments to dedicate property to public service), or assets held in

¹ For example, under the used and useful test, a distinction is made between investments that provide physical services (used) and those that, while providing physical services, are superfluous (not useful). Id; Denver Union Stockyard Co. v. United States, 304 U.S. 470 (1938). Under the used and useful standard, certain items have been excluded from rate base by regulatory commissions such as: duplicate and unnecessary property; obsolete and inadequate property; abandoned and superseded property; and property used for non-utility purposes. See Charles F. Philips, Jr., *Regulation of Public Utilities Theory and Practice*, Ch. 8 (1984).

reserve to insure service reliability; or (3) the expenditures is necessitated by the projected immediate needs to the ratepaying public. Id.

This Commission most recently applied the used and useful test in Case No. PU-10-18, *Otter Tail Power Company 2010 Renewable Resource Cost Recovery Adjustment Factor Tariff* (August 4, 2010). In that case the Commission determined Otter Tail Power Company's ("OTP") investment in the Luverne Wind Project is used and useful for the service and convenience of the public in North Dakota based upon a finding that the project was completed in September 2009 and the energy from the project partially displaced the amount of purchased energy OTP otherwise needed to serve its retail customers; and therefore, it partially displaced the higher cost energy that customers had paid through increasing fuel cost adjustment charges over the past several years.

The "used and useful" test for ratemaking purposes within an integrated electric system is related to the "benefits and fairness" test recognized in Montana-Dakota Utilities Co. v. Federal Energy Regulatory Commission, 631 F.2d 557 (8th Cir. 1980), and Northern States Power Company v. Hagen, 341 N.W.2d 278 (N.D. 1982). In both cases, the Court was faced with the question of whether high priced natural gas supply purchased primarily to serve one part of a natural gas distribution system should be shared or "rolled in" with lower priced natural gas used to serve a different segment of the natural gas system. In both cases, the Courts' held the "benefits and fairness" test allocates the cost of a given facility or commodity among those customers who derive some measure of benefit from its availability. Northern States Power Company v. Hagen, supra at 282. System integration may justify such cost sharing to the extent it indicates benefits are shared by all customers on the system.

1. The Wind Projects are Used and Useful

Both the Diamond Willow and Cedar Hills wind generation projects are used and useful in providing electric service to North Dakota customers of MDU. Similar to the facts found by the Commission with regard to OTP's investment in the Luverne Wind Project, evidence in this case is uncontroverted that both wind projects are fully operational and available; that both projects are generating electricity that is placed into MDU's transmission system to serve all of the customers within its integrated electric system; that all the customers of MDU's integrated system, including the North Dakota customers, have received the benefit of this electric generation through the displacement of more expensive electric energy that would have otherwise been produced or purchased by MDU; and that the wind generation provides protection against volatility associated with other fuels and the MISO energy market as well as potential carbon control legislation. Exhibit MDU 4R, p. 3-4, MDU 5R, p. 3-4, MDU 6, p. 6-8, MDU 7R, p. 3, 5-7, 12-15, Tr. 69, 152, 176-177, 203, 210, 281-282, 309, 322, 449-450, 455, 496, 538, 547. Approximately seven percent of the Company's 2011 forecasted integrated energy requirements are expected to be obtained from the wind projects. Exhibit MDU 6, p. 11; Tr. 281, 961. The evidence is also uncontroverted that even with the addition of the Diamond Willow and Cedar Hills projects, MDU's electric generation resources are insufficient to meet all of its customer demand such that it is required to purchase both additional energy and capacity to satisfy the needs of its customers. Exhibit MDU 5R, p. 2; Roché 4, Tr. 71, 96, 169, 196, 210, 327, 450, 538, 934. Even Mr. Mathai did not deny the wind projects are being used to supply electricity to North Dakota customers which displaces purchased energy and reduces

fuel costs. Tr. 774-775, 778-779, 830-831. Accordingly, the wind projects are used and useful to provide electric service to customers and are not excess generation.

2. The Investment in Wind Projects was Prudent

The Staff's recommendation to exclude the wind generation projects appears related to the second prong of rate base valuation, i.e., the amount honestly and prudently invested by the utility in its property used and useful for service to the public. The prudent investment test, as initially advanced in the dissenting opinion in Missouri ex. rel. Southwestern Bell Telephone Co. v. Missouri Public Service Commission, 262 U.S. 276, 289 (1923), is a valuation method for utility property based upon its original cost. The test was adopted as an alternative to the reproduction cost method of valuation that was adopted in Smyth v. Ames, 169 U.S. 466 (1898) and used as the valuation method of utility property in the early years of regulation. See Charles F. Philips, Jr., *Regulation of Public Utilities Theory and Practice*, Ch 8, (1984).

The valuation of utility property under the prudent investment test is the original cost minus any fraudulent, extravagant or unwise expenditures. Bonbright, *Principles of Public Utility Rates*, Second Edition (1988). Investments are assumed to have been made in the exercise of reasonable judgment unless the contrary is shown. A prudence review to determine if an investment is appropriate for determining a utility's revenue requirement considers whether a company's actions, based upon what it knew or should have known, were reasonable and prudent in light of the circumstances existing at the time. It is not based upon hindsight nor is it appropriate for the Commission to substitute its best judgment for the judgments made by the company's managers: Re Western Massachusetts Electric Co., 80 PUR 4th 479, 520 (Massachusetts 1986). In

Montana Power Company v. Montana Department of Public Service Regulation, 68

PUR 4th 521 (Montana 1984), the Montana District Court reversed the Montana Public Service Commission disallowance of a coal fired generation station:

The Commission, in making rates, is not bound to give effect to an imprudent or unreasonable management decision to incur an expense, or operate its system in a particular fashion. However, the commission may not ignore the actual management decisions made by the utility, or refuse to give effect to the operational decisions made by the utility, unless it finds that such decisions were imprudent or otherwise unreasonable.

In support of his recommendation that MDU's investment in the wind generation be disallowed, Mr. Mathai offered the following reasons in his pre-filed testimony – Exhibit CAS 17:

- Diamond Willow was built to meet the Montana mandate and not as a prudent investment for North Dakota ratepayers – page 12, lines 23-24.
- MDU has not met its burden of proof as to whether Cedar Hills was necessary or a least cost alternative – page 13, lines 7-8.
- Cedar Hills does not enjoy a presumption of prudence because MDU failed to apply for an advance determination of prudence – page 13, lines 9-10.
- MDU's resource plan and discovery responses rebut any presumption of prudence for Cedar Hills – page 13, lines 11-12.
- MDU has not demonstrated any need for the wind energy projects – page 13, line 17.
- MDU's IRP's do not discuss alternative energy plans compared to the wind projects, and raise concerns about the prudence of such investments – page 13, lines 19-21.
- MDU's IRP's include statements that lead to a conclusion that the wind investments are not least cost, which brings into question any conclusion of prudence – page 13, lines 23-25.
- Because MDU did not utilize the advance determination of prudence law for approval of the wind projects, it can be concluded that MDU built the projects to meet the Montana renewable portfolio standard – page 14, lines 3-8.

- It is cheaper to build wind projects in North Dakota than in Montana; therefore the Diamond Willow II project is not the least cost plant necessary to serve North Dakota customers – page 14, lines 12-24.
- During its audit, Staff did not receive any feasibility studies or cost benefit analysis studies related to the wind energy projects – page 16, lines 10-11.

Of the above reasons offered by Mr. Mathai for exclusion of the wind projects, almost all are simply Mr. Mathai's conclusions or arguments with no factual evidentiary support of imprudence with the possible exception of the evidence he offered regarding the cost relationship between the Cedar Hills and Diamond Willow II projects. Even in that regard, the testimony of Mr. Neigum shows that Mr. Mathai's conclusion is incorrect. Moreover, the conclusions and arguments relied upon by Mr. Mathai are inconsistent with previous decisions of this Commission regarding the ratemaking treatment of wind energy projects for both OTP and Northern States Power Company ("NSP"). Indeed, the conclusions and arguments are inconsistent with prior findings of the Commission regarding MDU.

The law does not impose a burden on the applicant for a general rate increase to prove a negative, i.e., that there were no better alternatives to its investment expenditures. Rather, when presented with evidence challenging the prudence of an investment expenditure the Company is only required to show that it acted prudently and reasonably in undertaking its investment expenditure. In response to the scant evidence offered by Mr. Mathai, MDU presented substantial evidence that its investments in the wind generation projects were prudent and reasonable.

a. Need For The Project

MDU had, and continues to have, a need for additional generation resources to meet its energy and capacity generation requirements. Exhibit MDU 5R, p. 2., Roaché

14; Tr. 71, 96, 169, 196, 210, 327, 450, 496, 501-503, 526-527, 538, 543-544, 546-547, 555-556, 934. Even with the addition of 49.5 megawatts of generation from the Diamond Willow and Cedar Hills projects, MDU's generation deficits require it to purchase capacity through bilateral contracts and energy through the MISO energy market. Tr. 71, 96, 169, 196, 210, 327, 450, 501-503, 526-527, 538, 934 Consequently, there is no excess capacity on MDU's system and no portion of the Diamond Willow and Cedar Hills projects can be considered excess capacity.

MDU conducted extensive resource modeling in connection with its study of the Big Stone II project that was presented to the Commission in Case No. PU-06-482. That modeling assumed the addition of 50 megawatts of wind generation by MDU prior to 2012. See Exhibit CAS 4, page 647. The Commission's findings of fact #29 in Case No. PU-06-482 issued on August 27, 2008 and based upon hearings held in June 2007 and April 2008, found MDU was operating the Diamond Willow I project but was nonetheless both capacity and energy deficit:

There was no dispute among the parties concerning the need for additional electric system resources to ensure reliable electric service to customers of Otter Tail and Montana-Dakota.

The Commission further noted at finding of fact #28 that MDU was satisfying its energy deficiency through purchases in the MISO energy market but recognized the price volatility and risk associated with reliance upon that market.

The cost of energy from the MISO market can be uncertain and has been high for both on peak and off-peak demand. In January and February 2002, the average price was \$20/MWh hour of energy. In 2007, the average price was close to \$80/MWh. This is indicative of supply deficiency in the MISO region.

Staff took a predetermined position to exclude MDU's wind projects in this case as imprudent investments based upon a preconceived notion that the projects were constructed solely to meet the Montana renewal energy portfolio standard and Mr. Mathai stubbornly refused to reconsider his position regardless of evidence presented to the contrary. This was particularly evident with respect to the Cedar Hills project in which Mr. Mathai's prefiled testimony concluded that MDU failed to show a need for the project. When presented with evidence that MDU sought and the Commission issued a certificate of public convenience and necessity to own and operate the 19.5 megawatt Cedar Hills project, Mr. Mathai testified that the certificate of public convenience and necessity "is more of a courteous service to the company to expedite their process of building projects. . ." North Dakota law, however, does not provide for the issuance of certificates of public convenience and necessity as a "courteous service." The Commission order granting the certificate of public convenience and necessity for Cedar Hills states that MDU's application indicates the project is needed to provide reliable and economic renewal energy to its customers. Based upon the application, the Commission found public convenience and necessity will be served by construction and ownership of the facilities and the certificate specifically states **that public convenience and necessity require MDU to construct, own and operate the Cedar Hills project.** Exhibit MDU 6R (DJN-2).

Even when presented with the Commission's order, Mr. Mathai refused to change his position that MDU had not shown a need for Cedar Hills:

Sir, I said I cannot even understand about the need unless I have further information. Tr. 818

He later acknowledged, however, that a showing of need was a prerequisite to the issuance of a certificate of public convenience and necessity.

Q. In order to obtain a certificate of public convenience and necessity, is it not a requirement that the company provides sufficient proof to the satisfaction of the Commission that there is a need for the facility?

A. Take your first sentence, yes. Exactly, yes.

It logically follows that if there was a need for the new Cedar Hills generation, then there was also a need for the Diamond Willow I generation that was already built and operating. Despite Mr. Mathai's pre-filed testimony that MDU had not shown the need for Cedar Hills, the Staff did not dispute any of the Company's evidence that it had a need for additional generation, not only when it built the wind projects, but also at the current time. Mr. Mathai agreed on cross examination that even if the Diamond Willow project was built to meet the Montana renewable portfolio standard, that doesn't mean there wasn't a need for the facility. Tr. 765. Mr. Mathai also recognized the need for the wind facilities when he acknowledged that if the wind facilities are excluded from consideration for revenue requirement purposes, there will need to be a greater allocation of other generation resources or purchased power to North Dakota customers. Tr. 830-81.

The evidence is undisputed that MDU had a need for additional energy generation resources when it built the wind generation projects. The construction of the wind generation projects to partially fulfill that need supports the prudence of the Company's investment. There is no evidence that any of the investment was imprudent based upon a lack of need for generation.

The Projects Were Prudent Investments to Meet Renewable Energy Policies

All of the three states in which MDU operates its integrated electric system have adopted renewable energy policies specifying that ten percent of the energy sold within the state be obtained from renewable energy resources. Although the Montana policy imposes penalties if a utility fails to meet the policy, and the North Dakota and South Dakota policies are objectives without monetary penalties, renewable portfolio standards, whether mandatory or objective, are legislatively enacted public policy directives applicable within the respective jurisdiction. MDU is not seeking recovery of penalties assessed under the Montana policy. Instead it is seeking a return upon investments that meet the public energy policies of all three states. It was reasonable and prudent for MDU to comply with these public policy directives regardless of which directive initiated the first investment or whether a directive is mandatory.

With or without the Montana policy, MDU's investments in the Diamond Willow and Cedar Hills projects are needed to meet the North Dakota renewable energy policy objective. The other North Dakota utilities have likewise sought recovery for their wind generation projects based in whole or in part upon the North Dakota renewable energy policy objective notwithstanding more stringent and mandatory requirements imposed by the State of Minnesota that influenced or initiated their projects. In each instance, the Commission has approved rate recovery for those investments as consistent with the North Dakota energy policy objective. In its order of May 21, 2008 in Case No. PU-06-466 (Exhibit MDU 19), the Commission found OTP acted prudently investing in the acquisition of a 40.5 megawatt share of the Langdon wind energy center which became operational in January 2008:

The Commission finds that Otter Tail has responded appropriately to the desires of the North Dakota Legislature encouraging investment in energy conversion facilities in North Dakota. Besides declaring that there is rebuttable presumption that an energy conversion facility built in North Dakota is prudent, the state of North Dakota offers a significant investment tax credit for wind energy development of 5% per year for three years of dollars invested in North Dakota. Further, the legislative assembly has established a state renewable and recycled energy objective that ten percent of all energy sold at retail within the state by the year 2015 be obtained from renewable energy and recycled energy resources.

In Case No. PU-07-776, Staff recommended disallowance of 25 percent of NSP's wind generation projects built in Minnesota in furtherance of the Minnesota renewable portfolio mandate which Staff contended required NSP to move away from least cost resource planning. Nonetheless, the Commission accepted the subsequent settlement between the Staff and NSP in its general rate application that included recovery of the wind generation projects.

On August 12, 2009, the Commission issued an order in Case Nos. PU-08-908 and PU-08-910 for a certificate of public convenience and necessity and advanced determination of prudence for NSP's 150 MW Merricourt wind generation project. Exhibit MDU 18. In its application dated December 3, 2008, NSP stated the Merricourt wind project "was needed to meet the renewable energy policies established by the five upper Midwest states" served by NSP notwithstanding that as of 2008, approximately 10.3 percent of the electricity used by NSP customers already came from renewable generation sources. Exhibit MDU 17, p. 5. The Commission's order determined the project was reasonable and prudent.

On August 4, 2010, the Commission issued an order on OTP's application for approval of its 2010 Renewable Resource Cost Recovery Adjustment Factor to include 49.5 MW of the Luverne Wind Energy Center. The combined nameplate capacity of the

Langdon, Luverne, and Ashtubula wind projects brought OTP's total investment in wind generation to approximately 138 MW. The Commission found OTP acted prudently in investing and constructing the Luverne wind project. The Commission repeated its earlier position that OTP had responded appropriately to the desire of the North Dakota Legislature encouraging investment in wind energy facilities in North Dakota.

In each of the above described cases, the Commission recognized the wind generation projects were reasonable and prudent investments to serve the energy needs of their customers and consistent with the North Dakota renewable energy policy notwithstanding that the projects also met renewable energy policy objectives or mandates in other states. Likewise, MDU's investment in wind generation that assist in its compliance with the state renewable energy policies of the three states in which it operates supports the prudence of its investment.

The Cedar Hills Project Is Presumed Prudent

Mr. Mathai took the position the Cedar Hills project was not entitled to a rebuttable presumption of prudence under N.D.C.C. § 49-05-16(6) because MDU had not sought an advanced determination of prudence for the project. Although the rebuttable presumption of prudence for renewal energy facilities located in the State is contained within the advanced determination of prudence provisions of N.D.C.C. § 49-05-16, the statute does not require an application for an advanced determination of prudence as a condition to the rebuttable presumption of prudence. Mr. Mathai's interpretation of N.D.C.C. § 49-05-16(6) would recognize a rebuttable assumption of prudence for a facility that is not built and not generating energy for customers whereas a facility that is built and generating electricity is not entitled to the same presumption of

prudence. Besides being illogical, this is contrary to the interpretation of the statute previously applied by the Commission. In at least two cases involving wind projects constructed by OTP, the Commission has recognized the rebuttable presumption of prudence for projects that were already constructed or in the process of being constructed. See Case No. PU-08-742 and PU-10-18. Specifically, two months prior to Mr. Mathai making his recommendations in this case, the Commission found OTP's 49.5 megawatt Luverne wind project, which was completed in September 2009 and for which OTP had withdrawn its request for an advanced determination of prudence, was entitled to the presumption of prudence under N.D.C.C. § 49-05-16(6). The Cedar Hills project is similarly entitled to a presumption of prudence.

The Projects Are Cost Effective

Staff's primary argument for exclusion of the wind projects is its assertion that MDU did not show through modeling or other type of formal study that the wind generation projects were the least cost generation alternatives at the time MDU elected to proceed with the projects; notwithstanding that the Staff offered no factual evidence that any of the costs incurred by MDU for the wind generation projects were excessive, unreasonable or otherwise imprudent. Staff's implied position that MDU was required, as part of this general rate increase application, to present modeling or feasibility studies showing the wind generation projects were the least cost generation projects is incorrect. There is no requirement under the law that a utility must show that an investment was the least cost alternative before the utility is entitled to rate recovery for the investment. North Dakota's renewable energy policy objective certainly does not impose such a requirement. Rather, N.D.C.C. § 49-02-32 provides an exception to the

renewable energy policy objective if the utility determines the use of renewable energy is not cost effective considering other electricity alternatives. The staff attempts to turn this exception on its head by arguing the statute is not an exception but rather a pre-condition that a utility can invest in renewable energy only if it is the least cost generation alternative. Obviously, that was not the intent of the Legislature. **Moreover, the Commission specifically rejected such a least cost analysis with respect to renewable generation investments by MDU in Finding of Fact 116 in Case PU-06-482 made on August 27, 2008:**

Even though a CCGT + wind is not currently the least cost resource, **the resource planning activities by Otter Tail and MDU indicate that wind generation should be a part of the future addition of generation resources for both companies. [Emphasis Added]**

This directive by the Commission to MDU reinforces the prudence and reasonableness of MDU in its investment in the wind generation projects and flies in the face of Staff's position that as a condition to rate recovery MDU was required to conduct and produce in this proceeding a formal feasibility or modeling study showing the wind projects were the least cost generation alternatives.

At the time MDU made its' decision to pursue the Diamond Willow and Cedar Hills projects, its realistic supply alternatives were limited to coal fired steam generation, natural gas fired generation, wind generation, energy purchases through the MISO market, and bilateral capacity purchase agreements. Tr. 363. Each of those alternatives has attributes that make it a prudent inclusion within a diversified generation mix but not necessarily the least cost generation alternative in all circumstances. Tr. 364-365. Following the expiration of the AVS contract with Basin Electric Cooperative and as part of its investigation of the Lignite Vision 21 project and its later involvement

with the Big Stone II generating facility, MDU conducted extensive modeling and cost analysis of generation alternatives. The results of those efforts were discussed in the Commission's order in Case No. PU-06-482. This analysis showed the Big Stone II project was the most cost effective baseload generation project for MDU. Accordingly, MDU pursued the coal fired generation project and the Commission issued its advance determination of prudence for the project. The studies and the Commission's order, however, also provided an analysis of MDU's other generation alternatives. The Commission found the cost of energy from the MISO market can be uncertain and had been high for both on-peak and off-peak demand, including a 2007 average price of nearly \$80 per megawatt hour. Finding of Fact 28. The Commission discussed the 2004 and 2006 RFPs that had been issued by MDU to serve its energy needs following the loss of the AVS contract. Findings of Fact 41 and 42. These RFP's were in addition to the 2006 RFP that MDU issued with respect to renewable resources as testified in this proceeding. Exhibit MDU 15 and MDU 23. The Commission also discussed wind generation as an alternative to Big Stone II. Findings of Fact 101-116. The Commission found that because wind generation facilities are intermittent, they generally are not considered a resource for baseload energy and that cost planning models would generally not pick wind generation as the least cost baseload resource option. Id. However, gas fired combined cycle turbines supplemented with wind generation to reduce natural gas fuel costs could be considered as an alternative to the Big Stone II project. Findings of Fact 112-115. Studies of a CCGT + Wind alternative resulted in a levelized bus/bar cost of \$80.78/ MWh; approximately 11 percent greater than the levelized bus/bar cost projected for Big Stone II of \$77.65. Findings of Fact 96, 112-115.

Based upon that analysis, the Commission made its previously recited directive that wind generation should be a part of MDU's generation mix even if it was not the least cost resource. Approximately two weeks later, MDU signed a contract to pursue the Cedar Hills and Diamond Willow II projects. Tr. 164. If the studies and modeling conducted in conjunction with the planning and analysis around the expiration of the AVS contract and MDU's participation in the Big Stone II project were sufficient for the Commission to conclude that wind generation, in addition to Diamond Willow I, should be part of MDU's future additions to generation resources even if they were not the least cost resources, then it was certainly reasonable for MDU, who had conducted the modeling and analysis, to reach the same conclusion without yet another study in the form desired by Mr. Mathai.

The Staff's position to disallow the wind projects as prudent generation resources begs the question: if not wind then what? Mr. Neigum testified in this proceeding regarding the comparative cost of generation options available to MDU when it made its decision to proceed with Diamond Willow I in 2007:

- The levelized cost of coal generation in the form of Big Stone II was in the \$70/MWh range. Coal generation is a good resource for both capacity, because it is dispatchable, and energy, because it has relatively low and stable fuel prices. Tr. 528-529. Coal generation, however, as demonstrated by the Big Stone II project, presents permitting and environmental difficulties and size requirements needed to achieve efficiency. Tr. 528-529.
- The average price paid by MDU for energy purchases from the MISO energy market in 2007 was \$63/MWh. Tr. 529. Purchases on the MISO energy market provide no capacity and prices are volatile as recognized by the Commission in Case PU-06-482. Tr. 529.
- The levelized cost of natural gas generation was over \$100/MWh. Tr. 529. While gas generation provides both capacity and energy, the cost of energy is reflective of natural gas prices which can make the energy expensive as it was in 2007. Tr. 529.

- The levelized cost of wind was in the \$55 range. Tr. 530. Wind generation provided a lesser percentage of capacity accreditation per nameplate rating than either coal or natural gas but has no fuel cost and therefore, the lowest marginal energy cost.

In the time frame of 2007-2008 when MDU made its decision to add the wind projects, it had recently lost the AVS contract and its own generation was both capacity and energy deficit. Exhibit MDU 6R, p. 3. It was already pursuing development of the Big Stone II project which was identified as the least cost option to meet most, but not all, of its long term capacity and energy needs but the project would not be completed for several years. It was meeting its interim capacity deficits through bilateral capacity contracts, however, it remained energy deficient and was meeting that deficiency entirely through purchases on the MISO energy market. To reduce its dependence on the MISO market, MDU's options were limited to natural gas or wind turbines. While wind generation is an intermittent resource, it was the best choice to provide low marginal cost energy. Selection from this limited menu of choices to address MDU's generation needs did not require any further study beyond the information it already had available. Staff's refusal to recognize the prudence of the wind projects because of the lack of an economic study in a form to the liking of Mr. Mathai, while carefully refusing to identify a better alternative from the limited resources available at the time, (Tr. 785, 789) does not meet Staff's burden of coming forward with evidence to refute the evidence offered by MDU.

Since the issuance of the Commission's order, MDU was forced to end its participation in the Big Stone II project. Case No. PU-10-30. Because of the circumstances that led to the cancellation of the Big Stone II project, investment in new

coal fired generation is not a realistic option at this time. Accordingly, by default wind generation, in combination with natural gas CCGT, are the most cost effective generation alternatives available to MDU unless the risk of price volatility in the MISO energy market and bi-lateral capacity purchases is accepted. The Commission has previously recognized that a utility's investment in generation resources is generally preferable to reliance upon power purchase agreements. Case Nos. PU-06-466 and PU-10-18. Accordingly, wind generation, which was found by the Commission in Case No. PU-06-482 as a cost effective generation resource addition for MDU, becomes even more cost effective as a result of the cancellation of Big Stone II. As MDU's existing capacity contracts expire over the next four years, it appears the Company will need to place greater reliance upon natural gas turbines for capacity and MISO purchases for energy to meet its generation resource needs. In that event, the availability of the existing wind generation resources to supplement or displace energy from the gas turbines or MISO energy purchases will become even more valuable to MDU's customers. Staff's position to disallow such wind generation is both shortsighted and without merit.

The only factual evidence offered by the Staff in support of its position that the wind projects were not the least cost generation alternatives was a schedule contained in Mr. Mathai's testimony purporting to show the cost of the Diamond Willow II project was more expensive than the Cedar Hills project. 1. Exhibit CAS 17, page 14. In actuality, this schedule shows the completed cost of Diamond Willow II of \$2,414 million/MW was slightly lower than the completed cost of Cedar Hills of \$2,425 million/MW. The flaw in Mr. Mathai's analysis was his application of the North Dakota

Investment Tax Credit to reduce the initial cost of the project rather than applying the tax credit to the years in which it is received. Tr. 932. Moreover, it is ironic that Staff would argue that North Dakota tax incentives, which benefit only North Dakota customers, should have driven MDU's decision on the selection of its integrated system wind projects, whereas it objects to recovery of wind projects that may have been influenced by Montana's renewable energy policy.²

The prudence and reasonableness of MDU's decision to construct the wind generation projects is supported by the uncontroverted evidence of the considerations of MDU in its decisionmaking in addition to the modeling and analysis discussed and relied upon by the Commission in Case No. PU-06-482. Those considerations included:

- Its need for generation resources and the opportunity to acquire wind generation resources at costs competitive or favorable to alternative supply resources.
- The availability of transmission on MDU's system that could be accessed without significant network upgrades that might not otherwise be available if the wind projects were delayed. Access to the transmission system at a later date would have made the projects more expensive if significant network upgrades were necessary because of transmission constraints.
- The loss of production tax credits would have significantly increased the cost of wind generation to MDU customers if the projects were delayed beyond the expiration date of the federal production tax credits as scheduled. If carbon control legislation or federal renewable portfolio standards were enacted as proposed, MDU would have been subject to certain criticism if it had failed to construct the projects while the tax credits were available, particularly in light of the state renewable policies and the Commission's directive in Case No. PU-06-482.
- Wind generation is useful in a diversified generation mix as a hedge against volatile fuel prices, particularly natural gas, as well as purchase prices in the MISO energy market. Wind energy displaces the most

²Obviously, Mr. Mathai's comparison does not support his recommended disallowance of the Cedar Hills investment.

expensive energy that would otherwise be purchased from the MISO energy market or produced from MDU's other generation alternatives.

- The limited opportunity to acquire wind turbines in quantities that allowed MDU to pursue projects of a size appropriate for its system.
- The opportunity to acquire renewable generation resources in compliance with the renewable energy policies of the three states served by its integrated system.
- The opportunity to acquire renewable generation resources with no environmental impacts provided a hedge against potential environmental legislation and regulation or potential carbon taxes and national renewable portfolio standards.
- The opportunity to reduce its dependency upon the MISO energy market and associated price volatility.
- The opportunity for capacity accreditation that was not received on purchases from the MISO energy market.
- The areas of the wind projects were excellent wind resources with available meteorological data.

Exhibits MDU 4R, p. 3, MDU 5R, p. 2-4, 7, MDU 6, p. 9-10, MDU 6R, p. 3-4, 6-11; Tr. 42-45, 119-122, 148-152, 166-168, 281-282, 308-309, 366-367, 377-378, 385-386, 450-452, 487-488, 496, 517-518, 537-538, 543-544, 546-547.

These are the same factors considered by OTP and NSP and recognized by the Commission in support of its determination that investments by those utilities in wind generation were prudent. Case No. PU-06-466; PU-08-742; PU-08-908; PU-08-910; PU-08-862; and PU-10-18.³

The Staff's rationale in support of its recommendation to exclude consideration of the wind projects from the determination of MDU's revenue requirement evolved over the short period of time between the filing of Mr. Mathai's testimony on October 15,

³ It is worth noting that the other utilities, in support of their generation projects, did not provide a least cost comparison between wind generation and other nonrenewable generation alternatives. Rather, their project investments were considered in relation to the cost of other available renewable projects at the time.

2010 and his testimony at the hearing on November 10, 2010. From the previously summarized litany of unsupported conclusions in his pre-filed testimony, Mr. Mathai narrowed the arguments in support of this position to the three presented in Exhibit CAS 18:

- The Company had great difficulty in identifying the total dollar amount applicable to wind included in the current filing.
- The Company did not consider wind investment of approximately \$115 million as being enough of an investment to require an advanced determination of prudence from the Commission and therefore the Staff and Commission did not have an opportunity to scrutinize in detail the used and useful concept and associated cost factors prior to the resources being built or as of the hearing.
- The Company has not established the wind projects are the least cost options and Staff has not been privy to any economic studies conducted by MDU, if they were done at all.

First, in responding to this refined rationale, MDU's application was a general rate increase request and was not based upon the revenue requirement for individual assets. Although cost information relating to individual assets is embedded in the Company's accounting information, MDU does not typically prepare, nor is there any reason for it to prepare, a revenue requirement analysis for individual assets. Tr. 645. Accordingly, MDU did not have such a revenue requirement study available to produce to Mr. Mathai in the form he desired because such a study did not exist. Tr. 645, 786. Nonetheless, MDU provided estimates and substantial other information that it had available related to the wind projects. Exhibit MDU 27. The so-called "difficulty" in not identifying the dollar amount applicable to the wind resulted from the Staff recommendation to exclude the wind generation which was first received by MDU on October 15, 2010. The Staff's recommendation to exclude these assets from the

Company's rate base and operating expense generated the need to calculate the specific dollars of rate base and operating expense applicable to the assets encompassed within the filing. MDU's calculations were in response to Mr. Mathai's calculation of the revenue impact of his recommendation which he readily acknowledged was not accurate. Tr. 780, 831. MDU's calculations were further impacted by the recent enactment of the federal bonus depreciation, its effect on the utilization of the investment tax credits, and the settlement with Staff that was not finalized until November 8, 2010. Exhibit MDU 8R, p. 571-575. While Mr. Mathai recognized the difficulties in making these calculations, he did not identify any errors in the calculations despite their availability to him over the course of the hearing. **Most importantly, and the fundamental flaw in Staff's rationale, difficulty in quantifying the impact of excluding an asset from rate recovery is not justification to exclude the asset.** There first must be on evidentiary basis to exclude some or all of the asset, either because it is not used and useful or because it was an imprudent investment, before a determination is needed as to the revenue requirement impact of such removal. If the basis for exclusion is legitimately established, the calculation of the revenue requirement impact of that removal can be established or verified in a compliance filing.

Second, MDU's investments in wind projects were made in separate time periods; i.e.: the Diamond Willow I project in 2007 and the Diamond Willow II/Cedar Hills projects in 2009-2010. There is no requirement that a utility obtain an advanced determination of prudence for a project and MDU's decision not to seek such a determination is not a basis to exclude a project from rate recovery. MDU explained

why it did not seek advanced determinations of prudence for these projects. Exhibit MDU 5R, p. 6. There was certainly enough time for in this proceeding for Staff to determine if these projects were used and useful in providing electric service to North Dakota customers. Although Mr. Mathai maintained he had inadequate time to examine the projects under the used and useful test, he later testified he didn't understand the used and useful test, and then still later acknowledged that he had no reason to disagree that the wind projects have been used to provide electric energy to North Dakota customers since they began commercial operation. Tr. 773-775. The Staff does not meet its burden of presenting evidence by failing to understand or examine an issue.

Finally, the previous discussion establishes MDU was not required to show the wind projects were the least cost generation option. The Company certainly was not required to prove a negative that there weren't other options that were less costly. While MDU did not conduct and produce formal economic studies specifically directed to each of the wind projects, there was no requirement or need for the Company to create such studies in light of the information and other considerations known to the Company upon which it offered extensive testimony in this proceeding. Even Mr. Mathai acknowledged a company's investment decisions should not be limited to the least cost options and he did not attempt to identify a more cost effective generation alternative. Tr. 767, 768, 770.

Staff's position to exclude the wind projects is not based upon any evidence that the projects weren't prudent, but rather that the Diamond Willow I project was influenced by the Montana renewable energy policy and the inability of the Company to produce a

formal economic study conducted contemporaneously with its decision to pursue the projects. Mr. Mathai acknowledged his recommendations weren't supported by factual information and that even if the projects were constructed to comply with the laws of another state, the projects could nonetheless be used, useful and prudent. Tr. 790. The preponderance of the evidence establishes that the Diamond Willow and Cedar Hills projects are used and useful in providing electric service to North Dakota customers and that MDU's investment in those facilities was prudent and reasonable. Not a single countervailing fact was presented by Staff.

Incentive Compensation and Director's Fees

Staff recommended that 60 percent of the amount included as test year expenses for incentive compensation be excluded from consideration in determining MDU's revenue requirement on the grounds that performance based compensation is beneficial to both shareholders and customers. Exhibit CAS 17, p 23.. Mr. Mathai supported the recommended exclusion percentage based upon his position that the factors under MDU's prior incentive compensation plans were heavily weighted on financial performance. Tr. 750-752. He also commented without any supporting documentation, that MDU's current salaries are at reasonable levels without incentive pay and that incentive pay is not a significant deterrent to employee turnover. Exhibit CAS 18. Finally, he justified his position because other utility commissions have partially disallowed incentive compensation as a compromise position. Exhibit CAS 18.

Mr. Mathai also recommended that 50 percent of the amount incurred by MDU for board of director's fees and expenses be disallowed from ratemaking consideration,

regardless of the amount of those fees and expenses, because the board of directors benefits both shareholders and customers. Exhibit CAS 17, p. 24; Tr. 848-849.

The North Dakota Supreme Court has spoken on at least two occasions regarding the Commission's authority to adjust utility operating expenses for ratemaking purposes. In an early decision regarding the scope of the Commission's ratemaking authority, the Court examined a reduction by the Commission in NSP's legal expense of \$8,476 on the grounds that the Commission felt \$3,000 should be sufficient. In overruling the Commission, the Court stated:

There is no question but that the Company, during that year spent for legal services the amount it claimed should be allowed annually for legal expense. . . . There is no testimony in the record which challenges the prudence or the good faith of the Company's management in the incurring of these charges, nor is there any evidence which indicates that the cost of legal services will be a less sum in the future. It was the duty of the Commission to allow an amount which in its judgment was sufficient for the purpose. In the exercise of that judgment, however, it could not disregard the evidence and substitute for its judgment of the evidence its judgment of what the Company ought to be able to do. The Commission "is not the financial manager of the corporation, and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can ignore items charged by the utility as operating expenses, unless there is an abuse of discretion in that regard by the corporate officers." [Citations omitted]

The Court then reviewed the disallowance of some, but not all of the Company's expenditures for dues and donations. In reviewing the Commission's action, the Court held:

The inconsistency is patent. The finding is that donations for some unstated purposes are not properly allowable as expenses and the allowance is for a reduced sum for all purposes including the unstated improper ones. If the Commission had concluded that some of the donations were improper, it should have pointed them out specifically and if it thought that some of the contributions were so large as to constitute an abuse of discretion on the part of the Company's officers, it should have said so. The action which the Commission did take is simply an attempt to

control the discretion of the Company's management. This was in excess of the powers of the Commission. [Citations omitted]

Northern States Power Co. v. Board of Railroad Commissioners, 298 N.W. 423, 433-434 (1941). To disallow an operating expenditure, the Commission must prove an abuse of discretion on the part of management resulting from a showing of inefficiency or improvidence or from extravagant or unnecessary costs. Charles F. Philips, Jr., *The Regulation of Public Utilities Theory and Practice*, Chapter 7, 1984.

The scope of the Commission's authority to disallow operating expenses was revisited in Montana-Dakota Utilities Co. v. Public Service Commission, 413 N.W.2d 308, 316 (N.D. 1987) in which the Court reviewed the Commission's disallowance for rate recovery of utility service discounts as a benefit under MDU's employee compensation plans. The Court reversed the Commission holding:

In reaching this conclusion, we recognize that the overall employment compensation package between MDU and its employees is a matter left largely to the deference and judgment of management through its collective bargaining arrangement. See Central Main Power Co. v. Public Utilities Commission, 405 A2d 153 (Me. 1979), cert. denied, 447 U.S. 911, 100 S.Ct. 2999, 64 L.Ed. 2d 862 (1980).

The case of Central Main Power Co. v. Public Utilities Commission, supra relied upon by the Supreme Court is also instructive. In that case, the Supreme Court of Maine cited a line of cases holding that the function of a public service commission is that of control and not management. The matter of employee compensation calls for the exercise of judgment on the part of the management and good faith on its part is presumed. While these expenses are to be scrutinized by the Commission, they should not be disallowed or reduced unless it clearly appears they are excessive or unwarranted or incurred in bad faith. Id. at 175-179. The Court also cited with approval

the concurring opinion in Re General Telephone Co. of Florida, 19 PUR 4th 227, 267 (Fla. P.S.C. 1977) which recognized that regardless of the type of employer, it is almost universal practice that employees receive some part of their total remuneration in a form other than cash:

Whether these forms of remuneration are called concessions, fringe benefits, employee discounts, or some other name, and whether or not they are required by law, all of them accrue to the benefit of the employee. They have a bearing upon whether or not the person (management or craft) will trade his skills and work he can perform for a total package of remuneration (cash plus noncash).

It is uncontroverted that incentive compensation provided by MDU is part of the total remuneration package provided to its employees. Exhibits MDU 4R, p. 4-10; MDU 7; Tr. 45-48, 396-416, 989-1005. There is also no evidence that the incentive compensation package provided by MDU to its employees is excessive or unwarranted or incurred in bad faith. Rather, the evidence is undisputed that such incentive compensation packages are typically offered to employees and that base salary compensation would need to be increased if incentive compensation was removed from the total remuneration package. Exhibits MDU 4R, MDU 7; Tr. 45-48, 396-416, 989-1005. There was no support from Mr. Mathai's opinion that MDU's current salaries are at reasonable levels without incentive compensation and he offered no opinion of whether management abused its deference and judgment with respect to incentive compensation. Tr. 850-851. Rather, testimony shows that MDU routinely compares its compensation packages with those of other employers and that such employee packages are at or near the median of competitive employers. Exhibits MDU 4R, MDU 7; Tr. 45-48, 396-416, 989-1005.

Mr. Mathai's opinion that MDU's incentive compensation is unduly weighted to financial performance was made without recognition of the changes in MDU's incentive compensation plans that became effective 2010. While on cross examination Mr. Mathai retreated to his standard response that he didn't have any information showing how the plans had been changed, he in fact had been provided copies of both the old and new plans in discovery. Exhibit MDU 24. Furthermore, the premise of Mr. Mathai's opinion that financial performance benefits shareholders rather than customers is misplaced in view of the settlement agreement entered into between staff and MDU in this proceeding providing for a revenue sharing mechanism in which any earnings above MDU's required return on equity will be shared with customers through a refund mechanism. Exhibit MDU 2.

With respect to Board of Director fees and expenses, Mr. Mathai acknowledged these are legitimate expenses incurred by MDU as compensation for the services provided by its directors. Tr. 849. He offered no opinion whether management abused its deference and judgment with regard to such fees and expenses. Tr. 849-851. Instead, he acknowledged his recommendation was an arbitrary sharing mechanism which has been adopted by some other utility commissions based on recommendation of Staff in those cases. Tr. 861-862. The analyses' of the Supreme Court in Northern States Power Co. v. Board of Railroad Commissioners, supra, is dispositive. Regardless of what may have been accepted in a proceeding in another jurisdiction, arbitrary exclusion of 50 percent of legitimate expenses without any showing that the amounts included in the test year were excessive or incurred in bad faith is without merit.

Conclusion

As an investor owned public utility, MDU is entitled to earn revenue to allow it to meet its expenses and earn a fair and reasonable rate of return on its investments. Montana-Dakota Utilities Co. v. Public Service Commission, 413 N.W.2d 308, 310 (1987). Arbitrary disallowances of legitimately incurred operating expenses, such as employee compensation and director's fees and expenses, denies MDU a reasonable opportunity to receive revenues adequate to both pay those expenses and earn an adequate return on its investments. Disallowance of MDU's investment in wind generation projects that are currently being used to provide electric service to North Dakota customers, without any showing of imprudence and contrary to North Dakota energy policy and all prior precedent of the Commission with respect to the treatment of similar investments by other investor owned utilities, similarly violates this fundamental ratemaking principle. Id. MDU respectfully requests the Commission to accept the partial settlements between MDU and Staff and reject Staff's proposed exclusion of rate base and operating expense associated with the wind generation projects, as well as Staff's proposed reduction in incentive compensation and board of director fees and expenses.

Respectfully submitted this 27 day of December, 2010.

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

By: 

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STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

**Montana-Dakota Utilities Co., a
Division of MDU Resources Group, Inc.
Electric Rate Increase Application**

Case No. PU-10-124

**PROPOSED FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER
Of
Montana-Dakota Utilities Co.**

_____, 2011

Appearances

Commissioners Kevin Cramer, Tony Clark, and Brian Kalk

Daniel S. Kuntz, Associate General Counsel, MDU Resources Group, Inc., P.O. Box 5650, Bismarck, ND 58506-5650, on behalf of Montana-Dakota Utilities Co.

Richard J. Savelkoul, Felhaber Larson Fenlon & Vogt, Attorneys-at-Law, Suite 2100, 444 Cedar Street, St. Paul, MN 55101-2136, on behalf of the Public Service Commission Advocacy Staff.

Illona Jeffcoat-Sacco, General Counsel, and Mark E. Gruman, Legal Counsel, State Capitol, 600 East Boulevard Avenue, Bismarck, ND 58505-0480, on behalf of the Public Service Commission.

Scott Skokos, Missouri Valley Resource Council, Suite 8, 103½ South Third Street, Bismarck, ND 58504, on behalf of Intervenor Missouri Valley Resource Council.

James D. Roaché, 707 First Street SW, Crosby, ND 58730, Intervenor appearing *pro se*.

Al Wahl, Administrative Law Judge, Office of Administrative Hearings, 1701 North 9th Street, Bismarck, ND 58501-1882.

Preliminary Statement

On April 19, 2010, Montana-Dakota Utilities Co., a Division of MDU Resources Group, Inc. (“MDU” or “Company”) filed an application to increase its rates for electric utility service to provide additional annual revenue of \$15,396,303, or a 14 percent increase, over current rates. MDU filed testimony and supporting statements and exhibits in support of its application.

On June 16, 2010, the Commission issued a notice of hearing and notice of public input sessions scheduling a public hearing on the application to be held beginning November 8, 2010, in the Commission Hearing Room, State Capitol, Bismarck, North Dakota, and public input sessions to be held via interactive television on July 12 and July 13, 2010 at which members of the public were invited to appear and participate at locations in Bismarck, Dickinson, and Williston. The Commission identified the following issues in the notice of hearing:

1. What is the value of MDU's property, used and useful, for the service and convenience of the public in North Dakota?
2. What is MDU's rate of return on its property, used and useful, for the service and convenience of the public in North Dakota?
3. What is a just and reasonable rate of return on MDU's property, used and useful, for the service and convenience of the public in North Dakota?
4. What rates and charges are necessary to provide a just and reasonable rate of return on MDU's property, used and useful, for the service and convenience of the public in North Dakota?
5. Are MDU's proposed rate schedules designed in such a manner that they result in a basis of charge to its customers that is just and reasonable without discrimination?
6. Other relevant information or proposals concerning the proceedings.

MDU's application included a request for an interim rate increase based upon a projected 2010 test year. The request for interim rate relief sought an increase in annual revenue collections of \$7,617,000, an overall increase of 7.04 percent. To accomplish this, MDU filed an interim rate adjustment to increase revenue from each customer class by 7.04 percent and collect the increased revenue using an increase per KWh use charge. On June 7, 2010, the Commission Advocacy Staff ("Staff") filed comments agreeing to the amount of the interim rate increase but recommending the increase be charged to customers on a percentage basis rather than a per KWh basis. MDU agreed to Staff's recommendation to apply a 7.91 percent increase to base rates, energy charges and demand charges with no increase applied to fuel charges and other charges. On June 16, 2010, the Commission issued an order approving MDU's proposed interim increase of \$7,617,000, applied as an equal percentage increase to base rates, energy charges, and demand charges with no increase applied to fuel clause and other charges. The interim rates were effective for service billed on or after June 18, 2010.

On June 18, 2010, the Commission requested designation of an Administrative Law Judge (“ALJ”) from the Office of Administrative Hearings to conduct the hearing. By letter dated June 22, 2010, the Director of the Office of Administrative Hearings designated Al Wahl to conduct the hearing.

On August 24, 2010, the Commission issued an order granting intervention to Jim Roaché, as a customer of MDU. On October 4, 2010, the ALJ issued an order granting intervention to Harvey A. Christian as a customer of MDU. On October 22, 2010, the ALJ issued an order granting intervention to Missouri Valley Resource Council. On November 5, 2010, Mr. Christian advised the ALJ that he was abandoning his intervention.

Public input hearings were held as scheduled on July 12 and July 13, 2010.

On June 16, 2010, the Staff filed a partial settlement agreement between MDU and Staff relating to the overall rate of return (“ROR”) on MDU’s rate base, including the return on equity (“ROE”) component, for use in this proceeding. The partial settlement included a recommended 10.75 percent ROE and 8.699 percent ROR, as well as an earnings sharing mechanism by which MDU would refund to customers revenues corresponding to 50 percent of earnings above a 10.75 percent ROE.

On July 6, 2010, MDU filed an amendment to its application. The amendment eliminated from the application the Big Stone II generation development costs that were addressed in Case No. PU-09-733. The amended application, which did not include the effect of the partial settlement agreement between MDU and Staff filed on June 16, 2010, reduced MDU’s increase request to \$13,300,123 or 12 percent.

On October 15, 2010, the Staff filed responsive testimony to MDU’s application. The Staff’s testimony included recommended adjustments to MDU’s rate base and income statements, including the removal of MDU’s investment in wind generation projects. Staff’s testimony asserted that MDU’s current rates provide excess revenues of \$2,804,000.

On November 4, 2010, the ALJ held a pre-hearing conference with the parties.

On November 5, 2010, MDU filed rebuttal testimony to Staff’s responsive testimony. MDU’s rebuttal testimony also reflected the effect of a tentative partial settlement agreement with Staff that was finalized and received as a hearing exhibit on November 8, 2010. The partial settlement agreement revised the earlier settlement on ROR to 8.736 percent and resolved various adjustments recommended by Staff. The settlement of these adjustments reduced the Company’s request by \$1,220,000. MDU’s rate request after adjustment for the June 16, 2010 and November 8, 2010, partial settlement was \$10,299,000. MDU’s rebuttal testimony also reflected the adjustment of investment and expenses related to the wind generation projects as a result of the enactment of the Small Business Jobs Act in September 27, 2010; a reduction in depreciation rate for the 2010 wind projects from 5.17 percent to 5.0

percent; and the correction of an error in the original filing related to accumulated deferred income taxes. These adjustments lowered the revenue requirement associated with the wind generation from \$8,582,000 to \$7,108,000. The total rate increase request as effectively reduced by the settlements and adjustments for the wind projects resulted in a total increase request of \$8,825,000 or 7.7 percent.

The Commission held a hearing on the application on November 8, 9, 10, and 12, 2010, in the Commission Hearing Room. The ALJ presided at the hearing. The Commission heard testimony regarding the proposed settlements, as well as the remaining contested recommendations of the Staff to exclude from the Company's test year revenue requirement: (1) the investment and expenses associated with the Company's wind generation projects, (2) sixty percent of the Company's employee incentive compensation expenses, and (3) fifty percent of the Company's Board of Director's fees and expenses.

Having allowed all interested persons the opportunity to be heard and having heard, reviewed and considered all testimony and evidence presented, the Commission makes the following:

Findings of Fact

1. Montana-Dakota Utilities Co., a Division of MDU Resources Group, Inc., is a Delaware Corporation authorized to do business in the State of North Dakota as a foreign corporation. MDU is doing business in the State of North Dakota as a public utility. MDU operates an integrated electric system in portions of Montana, North Dakota and South Dakota. Approximately 65 percent of MDU's customers are located in North Dakota.
2. Jim Roaché is a customer of MDU and resides in Crosby, North Dakota.
3. Missouri Valley Resource Council is an affiliate of Dakota Resource Council and is an environmental group organized in the State of North Dakota.
4. The settlement agreement between MDU and Staff filed June 16, 2010, as modified by the settlement agreement dated November 8, 2010, which provides for a ROE of a 10.75 percent and a ROR of 8.736 percent, for ratemaking purposes, is fair and reasonable. The proposed earnings sharing mechanism under the settlement by which the Company will refund to customers revenues corresponding to 50 percent of earnings above 10.75 percent ROE as reflected in the annual report of jurisdictional regulated electric earnings for any fiscal year prior to either: (i) January 1, 2013; or (ii) the base period included in the Company's next electric general rate case (whichever occurs sooner), is fair and reasonable.
5. The proposed settlement agreement dated November 8, 2010, between the Staff and MDU regarding the resolution of issues set forth therein is a fair and reasonable resolution of those issues. The effect of this settlement agreement is to reduce the

Company's rate request by \$1,220,000. Resolution of the issues includes agreement that customers, upon the effectiveness of the rates authorized by this proceeding, will be credited through the Fuel Clause Adjustment for 100 percent of North Dakota's portion of asset-based wholesale margins received by MDU. MDU will, starting with the month final rates go into effect, include in its fuel clause adjustment calculation, the actual amount of wholesale sales margins for the applicable month. The Company also agrees to fund up to \$125,000 for a study to be completed prior to the filing of the Company's next general rate case to review issues regarding MDU's accounting system and jurisdictional allocation process, minimum standard filing requirements for rate cases, and MDU's corporate allocation process and affiliate transactions. Finally, the settlement agreement provides the rate design as a result the revenue requirement change determined in this proceeding shall be as MDU proposed in its request, modified to reflect adjustments to the revenue requirement and class allocations described in the agreement.

6. With acceptance of the settlement agreements of June 16, 2010 and November 8, 2010, issues remaining in dispute are Staff's recommendations to exclude the following from consideration in determining the Company's test year revenue requirement:

- Investment and expenses associated with the Company's Diamond Willow and Cedar Hills wind generation projects.
- Sixty percent of the Company's test year expenses for employee incentive compensation.
- Fifty percent of the Company's test year expenses for Board of Director's fees and expenses.

7. MDU operates an integrated electric system in the states of North Dakota, South Dakota and Montana. Both the Diamond Willow and Cedar Hills generation facilities are operational. Both projects have been generating electricity since their commercial operation dates. The Diamond Willow I project began commercial operation in 2008 and the Diamond Willow II and Cedar Hills projects began commercial operation in 2010. All the electricity generated from both projects is placed into MDU's transmission system to serve all of the customers within its integrated electric system. All of the customers of MDU's integrated system have received the benefit of the electricity generated from these projects through the displacement of more expensive energy that would have otherwise been produced or purchased by MDU. Electricity generated from these projects has been reflected in lower fuel costs included within MDU's fuel clause adjustment for its North Dakota electric rates since the projects began commercial operation. The wind generation projects provide protection against volatility associated with other fuels and the MISO energy market, as well as potential carbon control legislation.

8. Following the expiration of the Company's AVS contract with Basin Electric Cooperative in 2006, MDU's generation resources were insufficient to meet the load demands of its customers. Even with the addition of 49.5 megawatts of generation from the Diamond Willow and Cedar Hills projects, MDU's electric generation resources are insufficient to meet all of its customer demand, such that it is required to purchase both additional energy and capacity to satisfy the needs of its customers.

9. Approximately seven percent of the Company's 2011 forecasted integrated energy requirements are expected to be obtained from the Diamond Willow and Cedar Hills wind generation projects.

10. The Diamond Willow and Cedar Hills wind generation projects are used and useful to provide service to MDU's North Dakota electric customers.

11. MDU needed additional generation resources to meet its energy and capacity generation requirements when it decided to construct the Diamond Willow and Cedar Hills wind generation projects. The construction of the wind generation projects to partially fulfill its need for additional generation supported the prudence of the Company's investment in those projects.

12. If the Diamond Willow and Cedar Hills projects were excluded from consideration for ratemaking purposes in this proceeding, there would need to be a greater allocation of other generation resources or purchased power to North Dakota customers which supports the need for and the prudence of these projects as generation resources.

13. All three states in which MDU operates its integrated electric system have adopted renewal energy policies specifying that at least ten percent of the energy sold within the state be obtained from renewable energy resources. The Montana policy imposes penalties if the utility fails to meet the policy while the North Dakota and South Dakota policies are objectives without monetary penalties. The Diamond Willow and Cedar Hills projects are consistent with these policies. It was reasonable and prudent for MDU to construct wind generation projects consistent with these legislatively enacted public energy policies. MDU responded appropriately to the desires of the North Dakota legislature encouraging investment in wind energy conversion facilities.

14. The comparative cost and other considerations of generation options available to MDU when it made its decision to proceed with the Diamond Willow I project in 2007 were:

- The levelized cost of coal generation in the form of the Big Stone II project was in the \$70 per MWh range. Although coal generation is a good resource for both capacity and energy because it is dispatchable and has relatively low and stable fuel prices, it presents permitting and environmental difficulties, as well as economy-of-scale size requirements for efficiency.

- The average price paid by MDU for energy purchases from the MISO energy market in 2007 was \$63 per MWh. Purchases from the MISO energy market provide no capacity and energy market prices are volatile which was recognized by the Commission in Case No. PU-06-482.
- The levelized cost of natural gas-fired generation was over \$100 per MWh. While gas generation provides both capacity and energy, the marginal costs of the energy is a function of natural gas prices which can make the associated energy price expensive as it was in 2007.
- The levelized cost of wind from Diamond Willow was in the \$55 per MWh. Wind generation provides a lesser percentage of capacity accreditation per nameplate rating because of its intermittent nature than either coal or natural gas; but has no fuel costs, and therefore, the lowest marginal energy cost.
- Montana-Dakota issued a Request for Proposal (RFP) for wind resources in 2007 which led to selection of the Diamond Willow project as the least cost renewable energy option available to the Company.

15. Following the expiration of the AVS contract with Basin Electric Cooperative and as part of its investigation of the Lignite Vision 21 Project and its later involvement with the Big Stone II generation facility, MDU conducted extensive modeling and cost analysis of generation alternatives. The results of this modeling and analysis were presented to the Commission and discussed in its order in Case No. PU-06-482. These studies showed the cost of gas turbine generation in combination with wind generation was approximately 11 percent greater than the levelized cost projected for the Big Stone II project which was the least cost generation alternative identified by the Company's modeling.

16. In its Finding of Fact #116 in Case No. PU-06-482 issued on August 27, 2008, the Commission found that even though gas turbines in combination with wind generation were not the least cost generation resource, the resource planning activities by MDU indicated that wind generation should be a part of its future addition of generation resources. Approximately two weeks after the Commission made this finding, the Company entered into contracts for the development of the Cedar Hills and Diamond Willow II projects and in December 2008, MDU filed its application for a certificate of public convenience and necessity for the Cedar Hills project.

17. MDU sought and the Commission issued a certificate of public convenience and necessity to own and operate the 19.5 megawatt Cedar Hills project in Case PU-08-942. The application for the certificate of public convenience and necessity included the estimated levelized cost per megawatt hour, as well as an estimated revenue requirement based upon the projected cost of the project and associated operating expenses, depreciation and taxes offset by production tax credits. Exhibit MDU 6R. The

Commission found public convenience and necessity would be served by the construction and ownership of the Cedar Hills project.

18. The Cedar Hills project, which was constructed in North Dakota, is entitled to rebuttable presumption of prudence under N.D.C.C. § 49-05-16(6).

19. There was no requirement that MDU file for an advanced determination of prudence with respect to either the Diamond Willow or Cedar Hills projects, nor is there a requirement that a specific feasibility study or revenue impact study be conducted by a utility as a condition of prudence.

20. In the time frame of 2007-2008 when MDU made its decision to add the wind projects, it was already pursuing development to the Big Stone II project which was identified as the least cost option to meet most of its long term capacity and energy needs. It was meeting its interim capacity deficits through bilateral capacity contracts, however, it remained energy deficient and was meeting that deficiency entirely through purchases from the MISO energy market. While wind energy is an intermittent resource, it is a cost effective choice of providing low marginal cost energy. Selection of reasonably sized wind generation projects, from the limited generation alternatives available to MDU, supports the prudence of its investment in these projects.

21. The Commission has previously recognized that investment in generation resources is generally preferable to reliance upon power purchase agreements or energy market purchases. See Case Nos. PU-06-466 and PU-10-18.

22. The Big Stone II coal generation project was cancelled in 2009. As MDU's existing capacity contracts expire over the next four years, the Company will likely need to place greater reliance upon natural gas-fired alternatives to meet its generation resource needs. In that event, the availability of the existing low marginal cost wind generation resources, as a hedge to natural gas price volatility, will become an even greater benefit to MDU's customers.

23. The following considerations used by MDU in its decision to build the Diamond Willow and Cedar Hills wind projects support the prudence of those investments:

- MDU's need for additional generation resources and the opportunity to invest in available wind generation resources at costs competitive or favorable to alternative supply resources.
- The average price paid by MDU for energy purchases from the MISO energy market in 2007 was \$63 per MWh and in 2008 was \$55 per MWh.
- The levelized cost of natural gas-fired generation was over \$100/MWh.

- The levelized cost of wind from the Cedar Hills and the Diamond Willow wind projects was in the range of \$55 to \$57 per MWh.
- Available synergies and cost savings achieved through the construction of Cedar Hills in the vicinity of the Diamond Willow wind project.
- The availability of transmission on MDU's system for these projects that could be accessed without significant network upgrades and that might not otherwise be available in the future if the wind projects were delayed. Access to the transmission system at a later date would have made the projects more expensive if significant network upgrades were necessary because of transmission constraints.
- The loss of production tax credits would have significantly increased the cost of wind generation to MDU customers if the projects were delayed beyond the expiration date of the federal production tax credits as scheduled. MDU would have been subject to likely criticism if it had failed to construct the energy projects while the tax credits were available, particularly in light of the state renewable policies and the Commission's directive in Case No. PU-06-482.
- Wind generation is beneficial in a diversified generation portfolio as a hedge against volatile fuel prices, particularly natural gas prices, as well as market prices in the MISO energy market. The zero marginal energy cost of wind displaces the most expensive energy that would otherwise be purchased from the MISO energy market or produced from MDU's other generation alternatives.
- The limited opportunity to acquire wind turbines in quantities that allowed MDU to pursue projects of a size appropriate for its system and generation portfolio.
- The opportunity to acquire renewable generation resources consistent with the renewable energy policies of the three states served by MDU's integrated system.
- The opportunity to acquire renewable generation resources with no environmental impacts as a protection against potential environmental legislation and regulation as well as potential carbon taxes and national renewable energy portfolio standards.
- The opportunity to reduce its dependency upon the MISO energy market.

- The opportunity for capacity accreditation that was not received for purchases from the MISO energy market.
- The location of the wind projects with excellent wind resources and available meteorological data.

24. The preponderance of the evidence establishes the Diamond Willow and Cedar Hills projects were reasonable and prudent investments by MDU.

25. MDU provides incentive compensation plans as part of the total remuneration package for its employees. MDU routinely compares its compensation packages with those of other employers and MDU's employee compensation packages are at or near the median of competitive employers. There is no evidence the incentive compensation packages provided by MDU to its employees are excessive or unwarranted or incurred in bad faith.

26. MDU changed its incentive compensation packages effective for 2010 to reduce their weighting on financial performance. With the adoption of the revenue sharing mechanism provided in the partial settlement of June 16, 2010 and approved by this Order, financial performance incentives provide additional benefit to customers.

27. The Company's Board of Director's fees and expenses are legitimately incurred expenses for the operation of MDU's utility business. No evidence was offered in this proceeding to show the amounts paid for the Company's Board of Director's fees and expenses are excessive or that management abused its deference and judgment with regard to the amount of such fees and expenses.

28. There was no evidence presented to support disallowance of the amounts included within the Company's test year for employee incentive compensation or Board of Director's fees and expenses.

29. The Commission finds the following test year revenues, expenses and rate base are reasonable:

	(000's)			
	2009 ¹	2010 Test Year As Filed ²	2010 Test Year Adjustments ³	2010 Test Year Adjusted
Operating Revenues				
Sales	\$105,442	\$110,925		\$110,925
Sales for Resale	4,698	0		0
Other	<u>4,684</u>	<u>5,075</u>		<u>5,075</u>
Total Revenues	114,824	116,000		116,000
Operating Expenses				
Operation and Maintenance				
Cost of Fuel & Purchased Power	32,069	33,267		33,267
Other O&M	<u>39,364</u>	<u>40,485</u>		<u>40,485</u>
Total O&M	71,433	73,752		73,752
Depreciation and Amortization	15,705	18,757	(136)	18,621
Taxes and Other Than Income	4,338	4,636	(2)	4,634
Current Income Taxes	(3,811)	1,794	181	1,975
Deferred Income Taxes	<u>8,806</u>	<u>0</u>		<u>0</u>
Total Expenses	96,472	98,939	43	98,982
Operating Income	<u>\$18,351</u>	<u>\$17,061</u>	<u>43</u>	<u>\$17,018</u>
Rate Base	<u>\$210,903</u>	<u>\$276,885</u>	<u>(10,805)</u>	<u>\$265,880</u>
Rate of Return	<u>8.701%</u>	<u>6.166%</u>		<u>6.401%</u>

1. Exhibit MDU 8 – Statement L, Page 1 of 3.

2. Exhibit MDU 8 – Statement M, Page 1 of 44.

3. Difference between Exhibit MDU 8R-RAM–2, Page 3 of 6 (Total) and RAM-3, Page 1 of 8 (Wind Generation)

30. The Commission finds MDU's 2010 test year revenue requirement is \$8,825,000 as follows:

<u>Description</u>	<u>Test Year</u> (000's)
Average Rate Base	\$265,880
ROR Required (10.750 ROE)	<u>8.699%¹</u>
Return Required	\$ 23,129
Return Earned	<u>\$ 17,018</u>
Difference	\$ 6,111
Tax Factor (1-.3916 ²)	1.6437
Revenue Deficiency	\$ 10,045
Settlement Adjustments	<u>\$ 1,220³</u>
Revenue Increase Requirement	\$ 8,825

¹Exhibit MDU 2.

²Exhibit MDU 8, Statement L, Page 3 of 3.

³Exhibit MDU 3.

The effect of the above increase is mitigated by the pass through of future wholesale sales margins in the Company's fuel clause adjustment.

From the foregoing findings of fact, the Commission makes it:

Conclusions of Law

1. The Commission has jurisdiction over the parties and the subject matter of this proceeding.
2. MDU is entitled to rates and charges necessary to provide it an opportunity to earn a reasonable return on its North Dakota electric property, used and useful, for the service and convenience of the public in North Dakota. MDU is entitled to an increase in its existing electric rates to yield additional revenues of \$8,825,000 per year, or \$1,208,000 above the interim rates that became effective on June 18, 2010.

From the foregoing findings of fact, the conclusions of law, the Commission makes its:

Order

1. The Commission orders:

1. The partial settlement agreement between Staff and MDU filed June 16, 2010, as revised by the settlement agreement dated November 8, 2010, is approved.

2. The partial settlement agreement between Staff and MDU dated November 8, 2010, is approved.

3 MDU is authorized to implement an increase in its electric rates sufficient to produce a total annual revenue increase of \$8,825,000 in accordance with the rate design provided in the settlement agreement dated November 8, 2010. MDU shall file compliance tariff pages setting forth the revised electric rates and tariffs provided by this order at least 30 days prior to the effective date of the rates. Such compliance filing shall also provide for the Commission's consideration, a separation of the revenue requirement associated with North Dakota's allocated share of the Diamond Willow and Cedar Hills generating facilities to be recovered from customers as part of the Renewable Resource Cost Recovery Rider rather than through base rates.

Public Service Commission

Anthony T. Clark
Commissioner

Kevin Cramer
Chairman

Brian P. Kalk
Commissioner