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January 6, 2012

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**PUBLIC SERVICE COMMISSION**

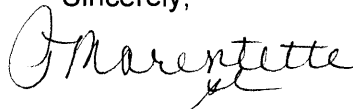
Mark Gruman, Esq.  
North Dakota Public Service Commission  
600 E. Boulevard Avenue, Dept. 408  
Bismarck, ND 58505

Re: In the Matter of the Applications of Otter Tail Power Company and  
Montana Dakota Utilities Co.  
PU-11-163/PU-11-165

Dear Mark:

Enclosed are the original signed copies of the Settlement Agreement. Please feel free to give me a call with any remaining questions or concerns.

Sincerely,



Pamela Marentette

PAM:sl  
Enclosures

cc: Andy Brown (by electronic mail)  
Mark Bring (by electronic mail)  
Daniel Kuntz (by electronic mail)

**88** **PU-11-163** Filed: 1/9/2012 Pages: 15  
**Fully executed Settlement Agreement**

Montana-Dakota Utilities Co., a Division of MDU Resources  
Group, Inc.  
Pamela Marentette, Dorsey & Whitney LLP

**STATE OF NORTH DAKOTA**  
**PUBLIC SERVICE COMMISSION**

MONTANA-DAKOTA UTILITIES CO., A )	
DIVISION OF MDU RESOURCES )	
GROUP, INC. )	DOCKET NO. PU-11-163
APPLICATION FOR ADVANCE )	
DETERMINATION OF PRUDENCE )	
BIG STONE AIR QUALITY CONTROL )	
SYSTEM PROJECT )	
)	
)	
OTTER TAIL POWER COMPANY )	
APPLICATION FOR ADVANCE )	DOCKET NO. PU-11-165
DETERMINATION OF PRUDENCE )	
BIG STONE AIR QUALITY CONTROL )	
SYSTEM PROJECT )	

**SETTLEMENT AGREEMENT**

This Settlement Agreement is entered into this \_\_\_ day of January, 2012, by and between the North Dakota Public Service Commission Advocacy Staff (“Advocacy Staff”), Otter Tail Power Company (“Otter Tail”) and Montana-Dakota Utilities, Co., a Division of MDU Resources Group, Inc. (“Montana-Dakota”) (collectively the “Settlement Parties”). The Settlement Parties agree this Settlement Agreement, if approved by the Public Service Commission (“Commission”) resolves the issues in the above-captioned proceedings in a manner consistent with the public interest.

**BACKGROUND**

These proceedings involve the applications of Otter Tail and Montana-Dakota for an advance determination of prudence (“ADP”) related to the Big Stone Air Quality Control System (“AQCS”) project. Applicants seek an advance determination pursuant to North Dakota Century Code § 49-05-16 that the resource addition of the AQCS at the Big Stone Plant (“Big Stone or

“the Plant”) is prudent in order to comply with the South Dakota Regional Haze Rule, Administrative Rules of South Dakota Chapter 74:36:21. Applicants also seek an ADP for the installation of mercury control equipment at the Plant to comply with National Emissions Standards for Hazardous Air Pollutants for Coal-Fired Utilities proposed by the U.S. Environmental Protection Agency (“EPA”).

The Big Stone Plant is a 475 megawatt coal-fired power plant located near Milbank, South Dakota. Big Stone is jointly owned by the Applicants and NorthWestern Energy. Otter Tail holds a 53.9% ownership interest in the Plant and acts as its operating agent. Montana-Dakota holds a 22.7% ownership interest. The proposed AQCS project consists of a Semi-Dry Flue Gas Desulfurization system to reduce sulfur dioxide emissions, a Selective Catalytic Reduction with Separated Overfire Air to control nitrogen oxide emissions, and balance of plant modifications necessary to install and operate the control technologies (including a replacement baghouse and boiler modifications). The AQCS suite of emissions control technologies has been deemed Best Available Retrofit Technology by the South Dakota Department of Environment and Natural Resources in its Regional Haze State Implementation Plan (“SIP”). The Applicants also propose to install Activated Carbon Injection (“ACI”) at the Plant to control mercury emissions.

The Applicants prepared a capital cost estimate that included a projection of costs to the date of the anticipated commercial operation of the AQCS project. The estimated capital cost to install the AQCS is \$489,397,400 (2015 dollars) with an accuracy of +/-20%. The South Dakota SIP and its implementing rules provide that the AQCS be installed as expeditiously as practicable but not later than five years from the EPA’s approval of the SIP. South Dakota submitted the SIP to the EPA on January 21, 2011. The EPA recently published its intent to

approve and promulgate the SIP in the Federal Register on December 8, 2011. The comment period closes on February 6, 2012. The Applicants expect the EPA to issue a final decision on the SIP by March 29, 2012. The implementation schedule for the AQCS anticipates a commercial operation date by the end of 2015. The implementation schedule was designed to reduce project costs by taking advantage of favorable market conditions and coordinating tie-in of the AQCS equipment during a scheduled outage at the Big Stone Plant in 2015.

The EPA has proposed National Emissions Standards for Hazardous Air Pollutants from Coal-Fired Electric Utility Steam Generating Units, also known as the utility maximum achievable control technology (“utility MACT”) rule, which would require mercury emissions reductions at the Plant. The rule was proposed on March 16, 2011. The compliance timeline of the proposed rule requires coal-fired utilities to install mercury controls to meet mercury emissions limits by early 2015. Applicants anticipate the utility MACT rule will become effective within the timeframe of the installation of the AQCS project. Installation of the ACI at the Plant is estimated to cost \$5,012,700 (2015 dollars).

Otter Tail and Montana-Dakota filed applications and testimony in support of an ADP for the AQCS and ACI projects at the Big Stone Plant. Advocacy Staff reviewed the Applicants’ submissions, conducted discovery and independent analysis, and filed testimony regarding its assessment and recommendations. The Commission held a hearing on the Applications on November 29, 2011 in the Commission Hearing Room. Administrative Law Judge Al Wahl presided at the hearing.

At the hearing, the Commission heard testimony from the Applicants regarding the importance of the Big Stone Plant as a baseload resource, the regulatory need for the AQCS and ACI projects, the cost of the proposed projects, the reasonableness of the cost estimates, and an

analysis of the cost of the AQCS project as compared to the cost of the viable alternatives for compliance. Mr. Jeffrey Kopp of Burns & McDonnell testified that the AQCS is the least cost option by a significant margin as compared to the natural gas alternatives studied. Mr. Richard Hahn, testifying on behalf of Commission Advocacy Staff, stated that the component technologies of the AQCS and the project cost estimate were reasonable, and Mr. Hahn recommended the AQCS as the preferred option. The Commission also heard testimony regarding the need for a timely advance determination of prudence to assist the Applicants in achieving the lowest cost for ratepayers.

Following the hearing, the Applicants and Advocacy Staff conferred for settlement negotiations. In consideration of all the record evidence of these proceedings, the Settlement Parties agree to the following subject to approval of this Settlement Agreement by the Commission.

#### **TERMS OF SETTLEMENT**

1. Prudence Determination. Integrated Resource Plans submitted by the Applicants, additional analysis conducted by or on behalf of the Plant co-owners, and analysis conducted by the Advocacy Staff's consultant demonstrate the AQCS is a reasonable and prudent project that will provide cost effective and reliable electric generation for the Applicants and their customers in compliance with state and federal law.
2. BART Approval. An order for ADP for the AQCS project is contingent upon the EPA's approval of the same suite of emissions control technologies required by the South Dakota Regional Haze SIP as currently proposed.
3. Utility MACT Finalization. An order for ADP for the proposed ACI to control mercury emissions is contingent upon issuance by the EPA of a final utility MACT rule.

4. Semi-annual Reporting. The Applicants will submit reports to the Commission at least semi-annually regarding the status of EPA's review of South Dakota's Regional Haze SIP, the amounts and types of costs incurred with respect to the AQCS project, and any changed circumstances that will materially affect the cost, schedule or installation of the AQCS project.
5. Cash Return on CWIP. The Settlement Parties agree a cash return on Construction Work In Progress ("CWIP") for the AQCS and ACI projects is appropriate to minimize the final base rate increase and to provide for a gradual rate increase over the life of construction. The Applicants shall each file proposed tariffs for recovery of federal environmental mandate costs in accordance with N.D.C.C. § 49-05-04.2, and any appropriate compliance filings under the proposed tariffs for a return on CWIP for the AQCS and ACI projects.
6. Billing Statements. Until the project is complete and rolled into base rates, the cash return on CWIP will be reflected as a single line item on customers' bills labeled "Req. Environmental Upgrades."
7. ADP Amendment. An order for ADP will be issued and interpreted pursuant to N.D.C.C. § 49-05-16 as amended by Chapter 347, § 1 of the 2011 North Dakota Session Laws notwithstanding that the applications for ADP were filed prior to the effective date of Chapter 347, § 1 of the 2011 North Dakota Session Laws.
8. No Precedential Effect. The Settlement will have no precedential effect on any existing or future ADP determinations.
9. Reservation of Rights. Applicants reserve any rights under state and federal law or equity not specifically waived in the Settlement.

10. Basis of Settlement Agreement. It is agreed this Settlement Agreement is a negotiated Settlement Agreement subject to approval by the Commission.
11. Effect of the Settlement Negotiations. It is understood and agreed that all offers of settlement and discussions related to this Settlement Agreement are privileged and may not be used in any manner in connection with the proceedings in this case or otherwise, except as provided by law. In the event the Commission does not approve this Settlement Agreement, the Settlement Agreement will not be admissible as evidence in this or any other proceeding and no part thereof may be used for any purpose in this case or in any other.
12. Applicability and Scope. This Settlement Agreement is binding on the Applicants and Advocacy Staff, and their successors, assigns, agents, and representatives. This Settlement Agreement does not set policy or overturn precedent. Except as specifically provided herein, this Settlement Agreement does not constitute an agreement, admission or determination by Applicants or Advocacy Staff as to the merits of any specific allegation or contention made by Applicants and Advocacy Staff in this proceeding. This Settlement Agreement supersedes all prior settlement negotiations and agreements between Applicants and Advocacy Staff in these proceedings.
13. Effective Date. This Settlement Agreement is effective on the date of the Commission Order approving the Settlement Agreement.
14. Modification. If the Commission Order modifies or conditions approval of this Settlement Agreement, it shall be deemed terminated if either the Applicants or the Advocacy Staff files a letter with the Commission within five (5) business days of the date of such Order

stating that a condition or modification to the Settlement Agreement is unacceptable to such party.

### CONCLUSION

Applicants and Advocacy Staff have agreed to the forgoing terms to resolve the contested issues in the captioned proceedings. These terms are a result of negotiations between the Settlement Parties, are in the public interest, and will result in prudently incurred costs for the benefit of North Dakota ratepayers. For these reasons, Applicants and Advocacy Staff respectfully urge the Commission to approve the Settlement Agreement.

Dated this \_\_\_\_\_ day of January 2012.

Otter Tail Power Company

By: \_\_\_\_\_

Its: \_\_\_\_\_

Dated this 4 day of January 2012.

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

By: David Stanley

Its: VP Electric Supply

Dated this \_\_\_\_\_ day of January 2012.

North Dakota Public Service Commission

By: \_\_\_\_\_

Its: \_\_\_\_\_

**STATE OF NORTH DAKOTA**  
**PUBLIC SERVICE COMMISSION**

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Dated this \_\_\_\_\_ day of January 2012.

Otter Tail Power Company

By: \_\_\_\_\_

Its: \_\_\_\_\_

Dated this 4 day of January 2012.

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

By: [Signature]

Its: UP Electric Supply

Dated this 4<sup>th</sup> day of January 2012.

North Dakota Public Service Commission

Advocacy Staff  
By: [Signature]

Its: Legal Counsel