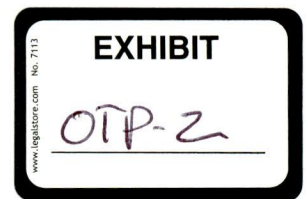


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May 8, 2013



Mr. Darrell Nitschke
Director of Admin./Executive Secretary
North Dakota Public Service Commission
State Capitol
600 East Boulevard, Dept. 408
Bismarck, ND 58505-0408

**RE: UPDATE to In the Matter of Otter Tail Power Company's Application to Establish an Environmental Upgrades Cost Recovery Rider and Tariff.
NDPSC Case Nos. PU-13-84 and PU-13-79**

Dear Mr. Nitschke:

Please find enclosed an update to Otter Tail Power Company's ("Otter Tail's") Application to Establish an Environmental Upgrades Cost Recovery Rider ("ECR") and Tariff (NDPSC Case Nos. PU-13-84 and PU-13-79). Updated Schedules 2-4 are attached to this filing. This update is being made to adjust the application for a lower projected cost for the project and the initial recovery period has been adjusted to reflect that the ECR rates are likely to become effective three months later than originally assumed.

The project has finalized contracts for procurement of approximately 90 percent of the project costs. With a large percentage of the costs under contract, the project has revised its total capital budget significantly from the original \$489 million to \$405 million (Otter Tail's North Dakota share of the project was originally forecast at \$105 million and is now forecast at \$87 million). The new budget is 17.5 percent lower than the original budget for the project. The large reduction in the original budget is a result of the following four factors:

1. Prudent design/engineering modifications is the first factor, accounting for approximately 45 percent of the reduction. Through prudent engineering and hard work there have been a number of changes in the design and specifications, resulting in considerable cost savings without compromising the performance or operability of the project. One example is the changes to the requirements and design of the boiler modifications that eliminated major structural changes originally contemplated. Another example is the reuse of the plant's 13.8Kv switchgear that was recently replaced. This reuse eliminates the need for a new plant substation and transformer to feed the AQCS Project. These and other changes yielded the largest share of the reductions.

23 PU-13-85 Filed 09/17/2013 Pages: 8
Exhibit OTP-2 from Sept. 16 formal hearing
Otter Tail Power Company

An Equal Opportunity Employer
25 PU-13-84 Filed 09/17/2013 Pages: 8
Exhibit OTP-2 from Sept. 16 formal hearing
Otter Tail Power Company

25 PU-13-83 Filed 09/17/2013 Pages: 8
Exhibit OTP-2 from Sept. 16 formal hearing
Otter Tail Power Company

24 PU-13-79 Filed 09/17/2013 Pages: 8
Exhibit OTP-2 from Sept. 16 formal hearing
Otter Tail Power Company

2. The second factor is the project delivery method, timing and market conditions. This accounts for approximately 35 percent of the reduction. With the combination of the project delivery method, General Work Contract target pricing methodology, and a “buyer’s market” we have been able to take advantage of many very competitive situations that have often yielded bid prices below the expected market. This was not coincidental. We selected the project delivery method to allow us to get to the market at the right time, and we have aggressively pushed ahead to try and be in the market during this opportune time.
3. The third factor is project management. Otter Tail Power Company (“Otter Tail”) has taken on the duties of construction management for the project. With a project delivery method focused on having a single contractor for the construction of the AQCS equipment, the partners felt Otter Tail could take on the construction management of the project rather than using a third party. We have added very experienced people to the project staff to ensure that this is a success. This change accounts for approximately 13 percent of the reduction.
4. The final factor is a change to the contingency for the project. Being at a point where so much of the project is under contract, we went through an extensive effort to evaluate the contingency needed for the rest of the project. The outcome was a lowering of the contingency level for the project that accounts for about 7 percent of the reduction.

The attached updated schedules 1-4 also include the impact of a change in the recovery period and in the billing determinants. The schedules are also updated to include actual data through March 2013.

Cost Recovery Impacts of Change in Budget, Revised Recovery Period and Billing Determinants

The original proposal calculated the ECR rates using an effective date of April 1, 2013 and a recovery period of April 2013 - March 2014. Because it appears this case will take a bit longer than originally expected, this update has recalculated rates using an effective date of July 1, 2013, with a recovery period of July 2013 - March 2014. The new implementation date shortens the recovery period by three months. The revised budget decreases revenue requirements from \$4,983,015 to \$4,308,473 (or 13.5 percent) over the period of January 2013 through March 2014 (Updated Attachments 2 and 4). The percent reduction in revenue requirements will not necessarily match the overall reduction in the budget due to the various recovery periods.

The proposed rates are computed assuming the total proposed revenue requirement is effective January 1, 2013 through March 31, 2014. As noted in the original filing, “if the effective date is significantly later than April 1, 2013, OTP requests the option to recalculate the rate in order to recover all approved costs over the remainder of the proposed recovery period.”

While conducting a review of the forecast billing determinants, the forecasted kWh were discovered to be inconsistent with the kWh forecast used in the recently updated renewable rider. The new billing determinants for the 12-month recovery period originally proposed would have been 1,802,403 MWh versus the billing determinants originally filed of 1,643,885. Due to the shortened recovery period Otter Tail is now proposing, the proposed billing determinants for the now nine-month period

Mr. Darrell Nitschke
May 8, 2013
Page 3

are 1,394,198. The combination of the reduction in the revenue requirements and the change in billing determinants with a shortened recovery period create only a small increase in the rate (Updated Attachment 3). The table below summarizes the change in rate as a result of the updated budget and kWh forecast.

| Rate Type | Original Proposed Rate from 2/08/13 Filing | Proposed Rate based on updated billing determinants and revised project budget |
|-----------|--|--|
| kWh Rate | \$0.00303 | \$0.00309 |

The change in billing determinants combined with the shorter period for which revenue requirement will be collected creates a proposed rate that is only 1.9 percent higher than the rate originally proposed.

While the initial rate increases slightly under the revised proposal, the subsequent 12-month rate (April 2014 – March 2015), which was expected to be \$0.00539 at the time of the initial filing, is now expected to be \$0.00415 or almost 23 percent less due to the budget reduction.

As in the initial filing in this case, Otter Tail proposes that final approved rates and the corresponding rate schedule pages be submitted in a compliance filing in this case.

Please refer all inquiries regarding this filing to Pete Beithon at (218) 739-8607 or pbeithon@otpc.com.

Sincerely,

/s/ PETE BEITHON

Pete Beithon
Manager, Regulatory Recovery

dm
Enclosures
By electronic filing and U.S. mail

Summary of Revenue Requirements

| Line No. | Revenue Requirements | 2013-2014 |
|----------|----------------------|---------------------------|
| 1 | AQCS | \$4,247,862 |
| 2 | Carrying Cost | <u>60,611</u> |
| 3 | Total | <u><u>\$4,308,473</u></u> |

North Dakota Revenue Requirements

\$4,308,473

| | <u>Billing kWh</u> | <u>Rate per kWh</u> | <u>Total Revenue</u> |
|-------------|--------------------|---------------------|----------------------|
| All Classes | 1,394,197,885 | \$0.00309 | \$4,308,473 |

| Line No. | TRACKER SUMMARY Requirements Compared to Billed: | 2013 | | | | | | 2014 | | | | | | January Projected | February Projected | March Projected | Collection Period |
|----------|---|----------------|-----------------|--------------|-----------------|---------------|----------------|----------------|------------------|---------------------|-------------------|--------------------|--------------------|-------------------|--------------------|-----------------|-------------------|
| | | January Actual | February Actual | March Actual | April Projected | May Projected | June Projected | July Projected | August Projected | September Projected | October Projected | November Projected | December Projected | | | | |
| 1 | Revenue Requirements | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 559,118 | 559,118 | 559,118 | 4,247,862 |
| 2 | Air Quality Control System | | | | | | | | | | | | | | | | |
| 3 | Billed (forecast kWh x adj factor) | 0 | 0 | 0 | 0 | 0 | 0 | 391,222 | 404,723 | 405,683 | 390,614 | 458,001 | 525,356 | 599,155 | 596,853 | 536,867 | 4,308,473 |
| 4 | | | | | | | | | | | | | | | | | |
| 5 | Difference | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | 214,209 | (177,013) | (190,514) | (191,474) | (176,405) | (243,792) | (311,147) | (40,037) | (37,735) | 22,251 | |
| 6 | Carrying Charge | | 1,538 | 3,087 | 4,647 | 6,219 | 7,801 | 9,395 | 8,192 | 6,883 | 5,557 | 4,331 | 2,611 | 396 | 112 | (159) | 60,611 |
| 7 | Cummulative Difference | 214,209 | 429,956 | 647,252 | 866,109 | 1,086,536 | 1,308,547 | 1,140,930 | 958,607 | 774,017 | 603,169 | 363,708 | 55,173 | 15,531 | (22,092) | (0) | |
| 8 | | | | | | | | | | | | | | | | | |
| 9 | Carrying Charge Calculation | 1,538 | 3,087 | 4,647 | 6,219 | 7,801 | 9,395 | 8,192 | 6,883 | 5,557 | 4,331 | 2,611 | 396 | 112 | (159) | (0) | |
| 10 | Cumulative Carrying Charge | 1,538 | 4,625 | 9,272 | 15,491 | 23,292 | 32,688 | 40,879 | 47,762 | 53,320 | 57,650 | 60,262 | 60,658 | 60,769 | 60,611 | 60,611 | |
| 11 | Carrying cost | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | 8.62% | |
| 12 | | | | | | | | | | | | | | | | | |
| 13 | | | | | | | | | | | | | | | | | |
| 14 | Forecasted Sales (MWh) | | | | | | | 126,597 | 130,966 | 131,277 | 126,401 | 148,207 | 170,002 | 193,883 | 193,138 | 173,727 | 1,394,198 |

| SUMMARY | Jan 2013 - Jun 2014 |
|---|---------------------|
| Revenue requirements | \$4,247,862 |
| Carrying Charge | 60,611 |
| Total Return on CWIP | \$4,308,473 |
| July 2013 - March 2014 projected sales in mWh | 1,394,198 |
| Average Rate | \$0.00309 |

