STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Public Service Commission)
Montana-Dakota Utilities Co.) Case No. PU-17-295
2017 Natural Gas Rate Increase)
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)
)

TRANSCRIPT OF PROCEEDINGS
HEARING
VOLUME 1
(Pages 1 to 348)
Taken Wednesday, May 30, 2018
Commencing at 8:30 a.m.

REPORTED BY: CHRISTA A. REESER, RPR, CRR, CRC

Volume 1 of 3, PUBLIC SERVICE COMMISSION HEARING taken on Wednesday, May 30, 2018, commencing at 8:30 a.m. at the North Dakota State Capitol Building, 600 E Boulevard Avenue, Bismarck, North Dakota, before Christa A. Reeser, Registered Professional Reporter, Certified Realtime Reporter, Certified Realtime Captioner, and Notary Public of and for the State of North Dakota.

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PROCEEDINGS, May 30, 2018: 8:30 A.M.

THE COURT: All right. Thanks everyone. Good morning. I guess this is the day we've all been waiting for to see how many people we can squeeze into this room and see how warm it can get. It's the end of May, beginning of June.

This is the Public Service Commission hearing on the application of MDU to increase rates for natural gas service, it's case number PU-17-295. My name is Pat Ward, I'm an administrative law judge pursuant to temporary appointment designated by the Office of Administrative Hearings at the request of the Public Service Commission to serve as the hearing officer for this hearing.

This hearing is on the application of MDU for permission to increase natural gas rates. The record will show it is a little past 8:30 a.m. Central Daylight Time, May 30, 2018. The hearing is located in the PCS hearing room, 12th floor State Capitol, Bismarck, North Dakota, which is the time, date and place set by the Notice of Filing and Continued Notice of Hearing issued by North Dakota Public Service Commission on February 14, 2018.

The Commission's Notice of Hearing for this

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hearing specified the following issues to be considered and determined upon this hearing: Number one, 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. Number two, 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.

Counsel, please state your appearances for the record.

MR. SANDERSON: Thank you, Judge. My name is Paul Sanderson with Evenson Sanderson in Bismarck. I'm here on the applicant, Montana-Dakota Utilities. At the table with me is Nicole Kivitso, President and CEO of Montana-Dakota Utilities, and also Garrett Senger, Executive Vice President of regulatory affairs and gas supply.

THE COURT: Okay. Thank you, Mr. Anderson.

Mr. Armstrong.

MR. ARMSTRONG: Good morning, Commissioners. Mitchell Armstrong and John Schuh, Special Assistant Attorney General on behalf of Advocacy Staff. With us is Victor Schock.

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THE COURT: Thank you. Ms. Jeffcoat-Sacco?

MS. JEFFCOAT-SACCO: Illona Jeffcoat-Sacco, counsel with the Commission on behalf of Advisory Staff. And with me is Jerry Lee.

THE COURT: Now we'll take the interveners. First, Mr. Coffman?

MR. COFFMAN: Good morning. John B. Coffman appearing on behalf of AARP. Dave Chider is not here today but is serving as local counsel. I'm here today with our expert witness, Scott Rubin.

THE COURT: Thank you. And Andy?

MAJOR UNSICKER: Good morning, commissioners. Major Andrew J. Unsicker on behalf of the Federal Executive Agencies.

THE COURT: Okay. Is there anyone else present in the room, other than witnesses for MDU, the Staff or the interveners that may want to testify at some time in this proceeding that's not here on behalf of the one of the parties?

Okay. We'll check that out as we get later into the hearing. And if there is somebody, please identify yourself to me maybe during one of the breaks or at some point so we don't pass anybody over that wants to take a position in this matter.

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Counsel, exhibits and -- let's talk about exhibits and stipulations and where we're at on that.

MR. SANDERSON: If I may, Your Honor, the parties in the case have reached a stipulation on a joint exhibit list I think should -- it was filed and you should have a copy. But at this time we would offer MDU Exhibit 1, its application, direct testimony exhibits, the statements and the depreciation study. We'd offer MDU Exhibit 2, our expert Stephen -- Dr. Stephen Gaske's rebuttal testimony; MDU Exhibit 3, Pat Darras's rebuttal testimony; MDU Exhibit 4, Jim Kaiser's rebuttal testimony; MDU Exhibit 5, Travis Jacobson's rebuttal testimony; MDU Exhibit 6, Jordan Hatzenbuhler's rebuttal testimony; MDU Exhibit 7, Stephanie Bosch's rebuttal testimony.

And those have been agreed to between the parties.

THE COURT: Okay. So those seven exhibits, there's no objection?

MR. ARMSTRONG: No objection.

THE COURT: Okay. Those exhibits will be received. MDU-1 through MDU-7.

Mr. Armstrong?

MR. ARMSTRONG: At this time we would offer PCS Exhibits Number 20 through 27, which is the

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direct and rebuttal testimony -- surrebuttal testimony of Staff's witnesses.

THE COURT: Okay.

MR. SANDERSON: No objection.

THE COURT: Okay. All right. Those exhibits will be received as well, PCS-20 through PSC-27.

And Mr. Cap -- Major Unsicker?

MAJOR UNSICKER: Major Unsicker, that's fine.

THE COURT: Yes, Major. Go ahead.

MAJOR UNSICKER: Yes, sir. We would offer FEA Exhibits 29 and FEA Exhibit 30, which is FEA-29 is the direct testimony of Mike Gorman. And FEA-30 is the surrebuttal testimony of Mike Gorman.

THE COURT: Okay. Any objection?

MR. SANDERSON: No objection.

MR. ARMSTRONG: No objection.

THE COURT: Okay. FEA Exhibits 29 and 30 are also received.

And Mr. Coffman?

MR. COFFMAN: Yes. I would like to offer into evidence Exhibits AARP-41 and AARP-42. I don't know if they got corrected, I think originally there was an oversight. AARP-41 should be the direct

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testimony of Scott Rubin. It had been listed as rebuttal. Mr. Rubin does not have rebuttal. So AARP-41 would be his direct testimony. And AARP-42 should be his surrebuttal testimony.

THE COURT: Okay.

MR. SANDERSON: No objection.

THE COURT: Mr. Armstrong?

MR. ARMSTRONG: No objection.

THE COURT: Okay. There being no objection and that change being noted in the record, those exhibits will be received. AARP-41, direct testimony of Scott Rubin, and AARP-42 surrebuttal testimony of Scott Rubin.

Anything else for the good of the order?

MS. JEFFCOAT-SACCO: Very quickly, there is no AARP-40 then, correct? I'm looking at the list --

MR. COFFMAN: That's correct.

THE COURT: At this time, no.

MS. JEFFCOAT-SACCO: So when it times to certify the record on appeal, there's no number 40.

THE COURT: If something comes up, we could plug something into that.

MS. JEFFCOAT-SACCO: No, let's keep it in order.

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THE COURT: All right.

MS. JEFFCOAT-SACCO: Thank you.

THE COURT: Thank you.

Counsel, any opening remarks or opening statements?

MR. SANDERSON: Yes, Your Honor. I'd like to make an opening statement on behalf of the Company.

Commissioners, again, my name is Paul Sanderson on behalf of Montana-Dakota Utilities. We're here today asking you to consider Montana-Dakota's application to increase its rates for natural gas service in North Dakota. The Company is seeking a revenue increase of approximately $3.5 million with a total increase in rates of about 3.3 percent.

The recent passage of the Tax Cuts and Jobs Act in December of 2017 had a significant impact and resulted in a reduction of nearly 40 percent of the original requested rates as filed in July of 2017. And those -- the impact will be explained by Company witnesses.

Under Montana-Dakota's proposed rate schedule, residential customers will see an increase of approximately 3.6 percent, which would amount to approximately $1.82 a month under the proposed rates.

The primary reason for this increase is due to

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Montana-Dakota's increased investment in distribution facilities to improve safety and reliability in its systems that have occurred since the last rate case.

Throughout the course of this proceeding, Montana-Dakota will present evidence to establish that due to its increase investment in recent years, the existing natural gas rates today are not sufficient to fully recover costs of providing gas service to the North Dakota customers, and therefore the current rates are unjust and unreasonable as they exist today.

At the outset of this case, I'd like to briefly discuss and think it's important to keep in mind the legal standard that a rate case is governed by in North Dakota. The law requires that rates be just and reasonable. And in consideration of a rate case, you must balance the interest of rate payers and ensuring that there's low cost rates. But that interest must also be balanced with the interest of the Company and the utility, that it remains a strong and viable company to provide safe and reliable service to its customers in North Dakota. And we must keep in mind that everyone in this state benefits from having a strong company which is able to meet the service requirements and needs of its customers.

Under the law, a utility has a constitutional

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right to such rates as will permit it to earn a fair return on value of property which it employs for the convenience and service of the public which should be equal to investments in other business undertakings of similar risk.

Now, I'd like to take this opportunity to briefly describe or outline the issues that have arisen or are in dispute between Montana-Dakota, Advocacy Staff, and the Intervenors, AARP and the Federal Executive Agency. The largest amount in dispute in this case between the companies relates to Montana-Dakota's employment compensation program. And that's the incentive compensation or at-risk pay that Montana-Dakota utilizes. Advocacy Staff is request the Commission reduce Montana-Dakota's incentive compensation program by an arbitrary amount of 60 percent. This would be an across-the-board disallowance to every single employee that Montana-Dakota has that provides gas operations in this state.

Now, Montana-Dakota has been utilizing an incentive or at-risk compensation system to compensate its employees for over 20 years, and you'll hear the testimony that this is a critical part of its total rewards philosophy, as will be explained by the Company

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witnesses.

Incentive compensation is recognized in the industry as a critical tool in attracting and retaining a highly-skilled work force. And in fact, the evidence will show in this case that at-risk pay is more economical to rate payers than an equivalent cash compensation that would be necessary to maintain employees at the current rate or a competitive rate.

In essence, what Advocacy Staff is requesting this Commission to do is to step into the shoes of the Company and its management to determine the best way for the Company to compensate its employees. The North Dakota Supreme Court in rate cases has repeatedly held that the Commission is not the financial manager of the Company and should not substitute its judgment for that of the directors of the Company. And in fact, the Court has previously recognized that the overall employment compensation package between a utility and its employees is a matter left to the deference and judgment of management through collective bargaining.

The evidence will establish that Montana-Dakota's incentive compensation for all employees is a reasonable and prudent company expense.

The next biggest issue in terms of the amount in dispute is the authorized return on equity. And as

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with every case, this seems to be the most contentious issue, which is a result of the calculations being so subjective amongst the experts. The U.S. Supreme Court has set forth the standard for determining the appropriate rate of return for a public utility, and that is, one, it must be commensurate with the returns of utilities with similar risk. Two, it must be sufficient to maintain the financial integrity of the Company. And three, it must be adequate to allow the Company to attract capital on reasonable terms.

Montana-Dakota's current return set by this Commission for its natural gas operations is 9.5 percent. The Company will present evidence through its expert witness, Dr. Stephen Gaske, that the appropriate rate of return should be increased, and Dr. Gaske proposes a rate of 10.0 percent, similar to what other utility companies -- natural gas utility companies are earning in this country. Obviously, the Advocacy Staff and the Interveners believe it should be less than that, and you'll hear the testimony on that.

Another critical issue in this case in dispute involves the current main and service replacement projects. And some of that you've probably seen in the testimony is referred to in Montana-Dakota's Information Application as its Systems Safety and

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Integrity Program. But there's one critical distinction that needs to be made here. This case is based on a future -- our application filed in 2017 was based on a future test year of the year 2018, as authorized under North Dakota law. In 2018, Montana-Dakota is already undertaking numerous projects for replacement of mains and pipeline facilities in a number of towns including Taylor, Fairview, Gladstone, New Salem, Eldridge, Barlow and Cleveland.

Now, what's critically in dispute with respect to the SSIP is a proposed new recovery mechanism. But what's the critical distinction is these projects in 2018 in the towns identified are not part of that SSIP recovery mechanism. They're part of what we're requesting for rate base. And why this is important is many of these projects have already begun, and they're all expected to be completed in 2018. And these projects will be used and useful by Montana-Dakota utilities at the time these rates go into effect and become applicable in this case. And therefore, under the legal doctrine of imminent use, they are appropriately included in the rate base, and these costs should be included in the rate base.

And that takes us to the bigger issue in dispute is the SSIP recovery mechanism. And

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Advocacy -- what Montana-Dakota Utilities is proposing is the adoption of a new SSIP recovery mechanism, and that's what Advocacy and AARP object to in their testimony. It's important in this consideration to realize approximately 25 percent of Montana-Dakota's entire natural gas system is over 50 years old, and some well, well older than that.

While Montana-Dakota has continuously been in the process of replacing pipe as necessary, the Company now recognizes the need for continuing safety improvements to an aging gas infrastructure. Montana-Dakota, with this proposal in this case is being proactive about replacing its pipeline infrastructure by implementing its SSIP. It's a risk-based approach focusing on prioritizing safety, asset replacement and mitigating rate impact on customers. The Company's SSIP will help expedite the replacement of Montana-Dakota's aging pipeline system by promoting a timely rate recovery mechanism for the investments it makes in its infrastructure. The proposed SSIP safety recovery mechanism would permit Montana-Dakota to recover specific project costs under that mechanism without the need to file an expensive and full-blown rate case.

Montana-Dakota's witnesses will take the time

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to explain how these projects are selected and will be included in the SSIP program and also how the proposed funding mechanism, if adopted, will be implemented. However, it's very important to note in this entire discussion that no cost recovered under the SSIP program would be permitted without the approval of the Commission in each and every instance.

And this would be a benefit to North Dakota customers. It would be a more gradual rate increase instead of the one-time sticker shock that will come for paying for these increased investments. And the other key benefit, it would avoid these costly rate cases on behalf of the Company and Staff and the Commission.

Ensuring pipeline safety is about more than just replacement and cost recovery. It's about working together with the Commission to establish a long-range strategic plan to ensure a safe and reliable gas pipeline system. You're going to see this is exactly why in July of 2013 the National Association of Regulatory Commissioners adopted a resolution entitled Resolution Encouraging Natural Gas Line Investment and the Expedited Replacement of High-Risk Distribution Mains and Service Lines, which urged state commissions to adopt alternative rate recovery mechanisms to

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accelerate the replacement of the aging natural gas pipeline system in this country. And this is not a unique or novel concept that Montana-Dakota is proposing in this case. Already over 36 states in this country have adopted a rate recovery mechanism to address the issues with the aging infrastructure.

So Montana-Dakota in this case is urging the Commission in this case to take a proactive approach to this critical public safety issue and adopt the Company's proposed SSIP recovery mechanism.

Now, there's other -- there's a few other miscellaneous items that I want to briefly touch on that are in dispute between the Company and Advocacy Staff and the Interveners. One is inflation. As indicated, this case was filed in 2017 based on a future test year. Montana-Dakota is seeking a two percent -- roughly two percent inflation on some minor expenses, and they're basing that on the average of six fully recognized publications on inflation. Advocacy Staff is proposing a complete disallowance of any inflation on its operating expenses. There's also an issue with work and vehicle equipment that Advocacy Staff takes an issue with, and Travis Jacobson on behalf of the Company will talk about these issues and explain why Staff has miscalculated the calculations.

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Then there's also an issue that Advocacy Staff takes with the use of -- the limited use of the Company airplane for Montana-Dakota's North Dakota gas customer -- or gas operations, the employee housing decisions that it made during the Bakken oil boom, and certain advertising and expenses. Again, Montana-Dakota will advocate and argue that these are again examples of the Staff improperly asking you as commissioners to step into the shoes of the management of the Company to make business decisions with respect to these issues. And it's not appropriate in these cases.

The parties are in agreement with the allocation of how the increase and rates should occur between the classes; however, there are some minor disagreements with how the increase should be applied to residential customers. In the last rate case in 2015, this Commission adopted a straight fixed variable rate design in which residential customers will simply pay a flat fee service charge. Advocacy Staff is -- not -- AARP, excuse me, is requesting that the increases be now added as a volumetric charge. Montana-Dakota takes the position that there's no justification to revert back to the previous rate design that existed and proposes that these increases

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continue to be used the straight fixed variable rate design that's a single-service charge.

In addition, there's a dispute regarding the allocation of cost distribution of mains pursuant to a minimum systems approach that the Company is offering where 25 percent of the allocated costs would be assigned or allocated to customers and 75 percent being allocated to demand. While the Federal Executive Agency agrees with this position, AARP opposes this proposal. But those are the issues with rate design.

With respect to the witnesses, I just would like to outline the witnesses we expect to call here. First, we'll call Nicole Kivitso, the president and CEO of Montana-Dakota, to give an overview of the Company and its application in this case. We intend to call Pat Darras, the vice president of gas operations to talk about the SSIP program and how those projects are selected. We'll call Travis Jacobson, our manager of regulatory affairs to discuss the rate base and revenue requirement issues that are in dispute. We'll call Matt Shoemake, he's a regulatory analyst, and he's going to discuss the customer and projected volumes used in our application. Tammy Nygard is our controller, and she will talk about the Company's capital structure. I've already referenced Dr. Stephen

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Gaske who will provide testimony regarding the cost of equity and the required rate of return. We'll call Jim Kaiser, the director of human resources for Montana-Dakota who will discuss the employee compensation program and the importance of the incentive and at-risk pay. Jordan Hatzenbuhler is a senior regulatory analyst who will be called to talk about the class cost of service study. And Stephanie Boss, the regulatory affairs manager, will discuss the tariffs that are being proposed to implement this.

We also have filed the testimony of Earl Robinson, an expert, he did Montana-Dakota's depreciation study. He is -- he'll be available by phone. Nobody -- I'll represent that none of the parties had issues with the depreciation study. So we do not intend to call him. But if the commissioners have any issues they want, we will make him available to testify by phone.

In closing, Montana-Dakota would like to thank you as commissioners for the opportunity to present its case supporting its increase in natural gas rates. The Company looks forward to the open discussion of these important issues over the course of this hearing. Thank you.

THE COURT: Mr. Armstrong.

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MR. ARMSTRONG: Thank you, Judge. Commissioners, I'll be brief because as you just heard we have numerous witnesses to go through. In the room with Staff also are its witness, Karl Pavlovic, Marlon Griffing and Donte Mugrace, who you'll hear testimony from later, as well as Victor Schock.

Overall, I will say that we do not agree with the characterization of Staff's position that was stated in the Company's opening statement. We believe Staff's recommendations completely comply with the law and result in a fair and reasonable rate.

At the outset, I will note that MDU has the burden to show that its proposed rates are just and reasonable. Staff asserts MDU's requested increase is quite simply too much. We believe the evidence will show that the requested increase includes imprudent or unsupported expenditures and is seeking to recover these from rate payers at an inflated return.

As you'll see from the pre-filed testimony and as you just heard from Mr. Sanderson, there are many areas in dispute. We do not intend to address every single area through the course of this evidentiary hearing. That's not because we agree with it or are waiving any argument, but there's pre-filed testimony that we believe fully evaluates those issues and you'll

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have a chance to review that after the hearing if you haven't reviewed it already. But we do rely on that pre-filed testimony and ask you to look at it and consider it carefully.

In addition to the straight dollars in the requested return, one of the major disagreements is the requested implementation of the System Safety and Integrity Program. We'll call that S-S-I-P, sometimes we call it SSIP. That's what we're talking about when we're using those words. Staff strongly disagrees with this program. MDU has operated an overall safe and reliable system basically forever. Now it wants to change the system for certain items and essentially create a rider that will be subject to less scrutiny but will pass significant costs along to customers. Staff believes that type of implementation is not best decided in this rate case. We believe those projects should be reviewed in a rate case type proceeding with experts, interveners, briefing, parties, evidentiary hearings, and just as we're going to do throughout this hearing, to provide the scrutiny that those major expenditures deserve.

At the end of this case, we hope you will see that Staff's recommendation provides a sufficient return for the Company that is just and reasonable,

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does not pass unsupported expenses on to customers, and recognizes the importance of the scrutiny of major projects through a rate case. Thank you.

THE COURT: Thank you, Mr. Armstrong.

Ms. Jeffcoat-Sacco, any opening comments?

MS. JEFFCOAT-SACCO: No, Your Honor. Thank you.

THE COURT: Mr. Coffman, opening statement?

MR. COFFMAN: Thank you. May it please the Commission, Chairman Christmann.

Just briefly, AARP is here on behalf of its 88,000 members in North Dakota. Many of these members are MDU gas customers. And AARP intervenes in rate cases because its members have told it that this is a very high priority for their financial security. Many older customers live on fixed incomes with little hope that their income might increase as much as their energy burden demands. So we do appreciate your scrutiny of this rate case, and we appreciate that you're all here today and hope that you keep -- take with you the knowledge that every dollar matters to many of the people who will be impacted on the residential class which we are here concerned with exclusively.

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We also would like to thank you for the local public hearings that you held in this case. Many of our members appreciate that opportunity to speak directly to you, and it's one of the many reasons that AARP prefers these full rate cases and the thorough scrutiny that they receive as opposed to the surcharge mechanisms that utilities often propose.

Tomorrow we'll have the opportunity to put our witness on the stand, Scott Rubin, who is a nationally recognized rate design expert with considerable experience. We have essentially four issues that we wish to talk about and only two of which I would like to preview for you now. And these are very big issues for us.

I'll just mention the SSIP or mechanism that was discussed by Mr. Sanderson, we oppose this idea along with the Staff and do not believe that it is about providing safe and adequate service. We believe that the current system does a very good job of doing that. We're not aware of any evidence that shows -- that states that applying additional surcharge to the bill have any safer systems with regard to any measurable metric.

We know that the Company is arguing that this will save rate payers money by reducing the number of

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rate cases. Now, the rate case expense for this thorough review is much less in our minds than the amount of cost savings that have been found as a result of this rate case. And one of our many concerns with the surcharge type paradigm is that you lose the opportunity to recognize offsetting factors. Now, main replacements are clearly the major expense that is increasing for the utility, but there are other factors and expenses that are going the other direction. There's also revenue increase that will be recognized in this case that you wouldn't otherwise be able to recognize. It would be a mechanism that would allow for rate increases without recognizes all the other moving parts in the system, and some of those moving parts you cannot anticipate.

In this case, originally it was not known that we would have such a dramatic reduction in the corporate tax rates. So the TCGA is being recognized to the benefit of customers in this case. Had we not had a full rate case and had rates increasing based on an SSIP mechanism, rate payers -- it would be questionable whether or not rate payers would see that benefit. So from our perspective, all relevant factors full review is the way we like to see rates change.

The other issue that is of great importance to

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us is rate design within the residential class. There is no dispute in the record as to allocating the revenues. All the parties have recommended that to the degree that there's a need for an increase that it be applied to the residential and firm general rate.

What we're talking about with the fixed charge for distribution rates is within the residential class. We believe the evidence will show that at least -- or no more than 75 percent of the costs are customer related, and that is, you know, the same for every customer, or fixed. However, the utility is wanting to continue a straight fixed variable rate design that would apply 100 percent of the cost to a fixed fee for the delivery of gas regardless of how much that customer uses. We believe that a just and reasonable rate that is actually based on cost and on the cost study would have some component for usage, some volumetric component. We believe that putting 100 percent in a flat fixed fee is extreme. It's out of the mainstream. And we would recommend that the Commission apply whatever increase comes out of this case to a volumetric part, because as I said, there is no dispute. We believe that it's less than 70 percent, but -- 75 percent, but there's no evidence in the case that shows that any more than 75 percent of the cost to

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delivering gas to the residential customer are customer related.

So based on those issues, we'll address all of our issues tomorrow through our witness. That's all I have and appreciate being here. Thank you.

THE COURT: Thank you, Mr. Coffman. Major Unsicker?

MR. UNSICKER: Thank you, sir. Good morning, commissioners.

The Federal Executive Agencies represents all federal entities within MDU territory, most notably in this case is Minot Air Force Base.

MDU filed a class cost of service study in this case, and the Company's proposed class cost of service study reasonably and accurately measures its cost to providing local gas transmission and distribution services to its various retail rate classes. In fact, the Company's cost of service study results show that the Air Force current rate, which is rate 64, is overcollecting its cost of service by $17,685 at the Company's proposed rate of return.

The Company's cost of service study also shows the Air Force base rate 65 that it pays for the operation and maintenance of the Air Force base distribution system near Minot, North Dakota is

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overcollecting its cost of service by $9,647 at the Company's proposed rate of return. Therefore, the Air Force's current rates result in a total overcollection of $27,332 per year for the Air Force. Hence, the Company's cost structure suggests that the Air Force Base should receive a reduced rate.

It is important to note that MDU proposes to collect its requested increase from only two rate classes, the residential and firm general service class. Therefore a system average increase in this case would be inappropriate as it would result in annual bill increase of $87,000 to Minot Air Force Base.

Now, you will hear from our expert witness, Mr. Gorman, I believe on Friday to talk about return on equity. The Company's claimed revenue deficiency is based on a requested return on equity of ten percent in this case. We believe that this ten percent return on equity is substantially in excess of current capital market costs. A more reasonable return on equity for MDU would be no more than five percent -- 9.5 percent, I apologize -- and possibly lower. Altering the cost of service to reflect a 9.5 percent return on equity would lower the Company's claimed revenue deficiency by approximately $555,000.

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Finally, the money saved by Minot Air Force Base will benefit the local community. In fiscal year 2017, the base's economic impact came to $580 million. Many of these dollars are spent in the Minot community to keep the base running. The amount paid to local schools, including for many airman for off-base education, came to $9.2 million. Construction expenditures were 46 million. These factors help to sustain the economy and jobs in the Minot area.

So in closing, the Federal Executive Agencies would ask that it be required to pay fair and reasonable rate in this case. Thank you, Commissioners.

THE COURT: Thank you, counsel. I guess at this point we'll ask the Commissioners if they have any opening remarks before we get into the witnesses in the hearing. Mr. Kroshus?

COMMISSIONER KROSHUS: Good morning everyone. Thank you for being here. I'll keep this brief because we have a lot of ground to cover, and it's going to be a busy three days.

But rate cases, they're really about creating the balance. It's about protecting consumer interest, it's about balancing that with Company needs also while looking at the safety and reliability of the system as

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well and what is the appropriate mechanism for collecting those dollars, that it obviously takes capital to do those types of projects. And really as we go through this, a lot of -- quite a number of my questions will be centered around the mechanism for collecting if it's appropriate, if it's not appropriate.

But I also recognize from spending a few years in the private sector that attracting capital is also very important. We want healthy companies operating in North Dakota, but we also want households that are doing well at the same time, and we want businesses also to be able to take advantage of low-cost energy. And we're fortunate in North Dakota to have some of the lowest utility rates in the country. So we're very fortunate in that respect.

And I think some excellent points have been made without question, and everyone has a different interest, slightly different angle, oftentimes depending on who you represent. If you're representing low-income households, every little bit matters. And that was one thing that was really -- really struck me when we had our public hearings. The people that showed up and talked about the $2.98 that it originally started at. It shouldn't be surprising to any of us

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that people will show up because social security checks aren't growing and everything else is going up around them. And this is one of the few opportunities they have to come in and to express their concern with the rising cost of just being able to try and live a normal life. So very understandable. And the public input during the course of this rate case was very beneficial to hear.

So really at the end of the day, again, this is about balancing customer interest with company needs and also doing what's right for North Dakota as a whole. So look forward to the witnesses that will be coming across the stand, and I'll save my questions for that point in time. Thanks.

THE COURT: Thank you. Commissioner Fedorchak.

COMMISSIONER FEDORCHAK: Good morning everybody. It's great to be here. First, I want to say thanks to the parties in particular who are taking time to intervene in this. It's really helpful for us to have third parties involved and bring out additional issues that we need to be looking at and thinking about, and it's a big investment of your time and resources to take part in these types of proceedings. So I wanted to make sure that you understand how much

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we appreciate that and value your input. So thank you very much for being here.

Secondly, there's -- I think I counted five members in the media, and I'm not sure if you guys understand the rules for how these rate cases work. But once you're in the room, you don't get to leave. So you got three days to cover. Sorry, James. It's the rules.

No, thank you to you all for being here, too. And hopefully you are getting a good summary. You have everybody's issues here right at the beginning, and maybe you want to come for the closing and see where everything ends up on Friday afternoon. And that might be the simplest way for you to get what you need from these proceedings because there will be an awful lot of detail covered.

Finally, I think it's hard for the public to understand what the Public Service Commission does. I get those kinds of questions a lot when I'm out and about, and especially as we run for office. And so people think really what in the world am I voting for here. And so it's hard to explain a rate case. I mean, you could talk about the rates, but really everything gets involved and it gets so technical, most people just don't have time to care. So I always break

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it down like this: If you care about cold beer and hot showers, then you should care about the Public Service Commission. And most people then go, oh, yes, I do care about those things. And when you're talking to kids, I say, if you care about -- well, we try to make sure that when you plug your phone into the wall there's actually power to charge it. And their eyes get huge and they say, thank you, thank you for that.

And so, you know, it really does, it's that simple. I mean, this is what all of these volumes of paper is about is safe, reliable, affordable utility service, in this case gas, to citizens of North Dakota. And so I will listen intently to all of your arguments. I do care a lot about the SSIP program and how that mechanism would work. I care a lot about the safety. I want to really dig into those issues and understand both the safety pieces, what's driving it, and the recovery mechanism. And so I appreciate all the time that the witnesses have already spent on that and all the testimony on those regards, not that the other issues aren't important. But for me in terms of customer impact and the long-term needs of the system, that's the biggest issue here. So thanks for your time and look forward to spending the next three days with you all.

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THE COURT: Thank you. Chairman Christmann.

CHAIRMAN CHRISTMANN: Well, not probably as enticing of a subject as appropriate recovery or rate base, but for people who are new to the Commission and have never been here and are going to be sitting through full days of hearings, just an announcement, there's a women's restroom right out by the elevators where you came up, hopefully everybody was able to get an elevator with only half of them operational. So that's for the ladies. For the gentlemen, in the northeast corner out there, there's a doorway that takes you to a stairway, you can go up or down one floor and there's men's restrooms by the elevators on the uneven-numbered floors.

I don't know that we ever have had a rate case or anything else with this much detail in opening comments. You guys covered a lot of ground already. And so I think what is clear from that is that we're going to have a very interesting three days, or however long it ends up taking, to get through all the material. I guess the one thing that I think has not been emphasized enough as we kick this off, because I want to give kudos to my fellow commissioners here and our staff for being on top of things months ago

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already. Mr. Sanderson talked about the need for a fair and reasonable return for the Company. I think anyone who's run for office understands the need for the lowest possible rates for the consumers, as well as the reliable service.

But -- and I don't want to jump ahead in the case, but in reading the rebuttal testimony and the surrebuttal testimony as well as listening to the opening comments, it seems like one thing that is pretty much agreed on by everybody is the Tax Cut and Job Act benefits that are being developed into this, whatever the new rates end up being. And they are substantial. And North Dakota, once again, gets left out of a lot of conversations. But in December already this Commission took action to recognize those savings, I think took the appropriate method since we had several rate cases coming, to, instead of just kind of guessing and setting something, account for the money but we will get it back appropriately as we proceed with these rate cases. And although I've seen things coming from all types of publications, including one from the U.S. House of Representatives, that showed North Dakota as being one of a handful of states and not doing anything, I will point out, North Dakota was one of the very first states that took an action to

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make sure to appropriately get the tax savings money back to the consumers. And I'm proud of this agency for doing that.

THE COURT: Okay. Thank you --

CHAIRMAN CHRISTMANN: Oh, and Major, on Memorial Day Weekend, thank you for your service. But would you spell your name please for me?

MAJOR UNSICKER: Yes, sir. It's U-n-s, as in Sierra, i-c-k-e-r.

CHAIRMAN CHRISTMANN: Thank you, sir.

THE COURT: All right. Thanks. The good news is based on our scheduling, we're slightly ahead of schedule at the moment after opening statements and opening comments. We're going to try to keep this on schedule. We've got 16 at least expert witnesses that I can think of to get through in the next three days, and a lot of complicated material but some really good contested issues. I think it's going to be a great hearing. So let's get on with it.

Mr. Sanderson, you can call your first witness.

MR. SANDERSON: Thank you. Your Honor, Montana-Dakota Utility would call Nicole Kivitso.

THE COURT: Ms. Kivitso, I know you've been through this procedure before, and for everyone in the room I'm going to give a perjury admonition that

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I'm required by law to give. If you listen carefully, I won't have to give it to every witness over and over.

I'm required by law to advise you of the law regarding perjury in this state. Perjury is a false statement under oath of a material fact made by a person who knows or does not believe the statement to be true at the time it is made. Perjury is a Class C felony. A Class C felony is subject to a maximum penalty of five years in prison, a fine of $10,000, or in some cases both may be imposed.

Having been advised of the penalty for perjury, please raise your right hand so I can administer the oath.

NICOLE KIVITSO,

duly sworn, was examined and testifies as follows:

THE WITNESS: I do.

THE COURT: Thank you. Mr. Sanderson.

MR. SANDERSON: Thank you, Your Honor.

DIRECT EXAMINATION

BY MR. SANDERSON:

Q. Good morning, Ms. Kivitso. Could you please state your full name and business address for the

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record?

A. Yes. Nicole Kivitso, 400 North Fourth Street.

Q. And whom are you employed by?

A. Montana-Dakota Utilities.

Q. And what is your position with Montana-Dakota?

A. President and CEO.

Q. And could you briefly describe your responsibilities in that role?

A. Sure. I'm possible for the development, coordination and implementation of strategies for our four operating utilities that operate across eight states.

Q. And could you just briefly describe your educational background and work experience for the Commission?

A. Sure. I have a bachelor's degree with a major in accounting from Minnesota State University in Moorhead. I have worked for the Company essentially my entire career, which is about 23 years. Started out at our corporate office at MDU Resources, worked there for a majority of my career, and left there as the chief accounting officer and controller, and then came down to the Utility and worked as vice president of operations for a year before assuming my current role about three and a half years ago.

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Q. And have you testified in other proceedings before state regulatory bodies?
A. I have. I've testified in all eight of our states.
Q. And are you familiar with Montana-Dakota's application for a rate increase in this case?
A. I am.
Q. And could you describe your involvement in this application?
A. Yes. I authorized the filing and ultimate -- had the ultimate decision to file the rate case.
Q. Now, with respect to your testimony here this morning, Ms. Kivitso, have you prepared PowerPoint slides to kind of summarize your testimony?
A. Yes, I have.
Q. And as we go along, feel free to utilize those slides. But first off, can you just provide a brief overview of Montana-Dakota's application for a natural gas rate increase in this case?
A. Sure. I'll turn to my first slide to just give a brief overview on the application. We did file for an increase, that application was filed on July 21st of 2017. The increase at that time we were requesting was 5.9 million, or 5.4 percent overall, which would be a change in our distribution prices. As was mentioned in

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opening statements, we certainly were beneficial to have the Tax Cuts and Jobs Act enacted on December 21st of 2017. That alone decreased our request by 2.3 million. So the current request in front of the Commission is 3.6 million, or an overall increase of 3.3 percent.
Q. Ms. Kivitso, could you just give a general summary of Montana-Dakota's gas operations in North Dakota?
A. Yeah, I point your attention to the map in terms of the slide deck here behind us. Really, when you look at our service territory in North Dakota, on an overall bases on the gas side of our business, we serve around 109,000 customers. 94,000 of those are residential communities. We're in about 74 communities and do this with about 562 dedicated employees.
Q. And Ms. Kivitso, could you just explain why Montana-Dakota has filed a -- or filed this rate application for gas increases?
A. Sure. Again, this slide demonstrates the primary reason for the increase. And it really is investment. When you look at our projected 2018 investment, at the end of the year we're anticipating that to be 275 million in total, which represents an increase of around 41 million or 18 percent compared to

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the last commission review.
What that investment relates to is really the replacement of our aging infrastructure, as was mentioning in opening comment, and then also enhanced reliability. And of course when you add investment to your system, it does increase your operating expenses for things such as depreciation, property taxes, and with labor being a large portion of our operating expenses as well, we did see some wage increases there.
Q. And can you summarize some of the major investments the Company has made since its last rate case?
A. Sure. On this slide we show a couple pictures of some of the major investments. Included in the case are some new town border stations, distribution mains to support our system. We also have included in the case some looping distribution systems around certain communities as well as an interconnection with the northern border and pipeline in Mandan.
Q. And Ms. Kivitso, we've already heard a number of the parties and the commissioners talk about Montana-Dakota's proposed System Safety and Integrity Program, the SSIP. Could you just briefly explain what that is and what prompted the Company to include it in this rate case?

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A. Sure. As we continue to look at our system, as has been mentioned again in opening remarks, we've got 2,575 miles of distribution pipe and about 110,000 service lines throughout our territory in North Dakota. As again was mentioned, 25 percent of that was installed before 1970. And we really feel like now is the time to take a look at a more proactive approach for replacing that aging infrastructure to enhance the safety of our system.
Moving to the next slide, really what we're doing here is responding to the United States Secretary of Transportation's call to action that was placed in 2011. As mentioned in opening remarks, 36 other states have a similar mechanism in place, and we have referenced that in an AGA study that has been conducted. On top of that, NARUC has put resolutions together both in 2013 and 2017 encouraging Commissions to work with companies in terms of adoption of safety type mechanisms and trackers. What we base this on is our distribution integrity management plan and program, and we're really focusing our system safety program on early vintage plastic pipe and early vintage steel pipe, and we are prioritizing those projects based on risk.
We request to manage this process by

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establishing projects to be completed annually, which would enhance the safety of our system and gradually increase customer bills verses it all coming in, in one rate case.

Q. Now, the other component of the SSIP is the proposed recovery mechanism. Could you just describe what the SSIP recovery mechanism is and how it will benefit customers?

A. Sure. Similar to other tracking mechanisms, our proposed projects would be submitted to the Commission by March of each year with rate recovery beginning in October of that year. Detailed cost information would be provided for each project, and as mentioned, no recovery would occur prior to Commission approval. We would also have a true-up mechanism in March of the following year where we would true up any costs related to the prior year's project. You know, we believe it would be a very transparent process providing opportunity for thorough review of each particular project.

We do see some customer benefits here. Of course, I'm going to have Pat focus primarily on the safety, which we believe is the number one benefit to our customers. But the mechanism itself certainly provides benefits as well, and we've talked about the

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gradualism and the reduced costs related to fewer rate cases.

When you look at our proposed 2019 investment, what that would result in is a 42-cent per month increase related to this rider mechanism. So again, it's about a $6 million investment that would occur as part of our System Safety and Integrity Program and that investment would result in a 42-cent per month increase if indeed this mechanism was implemented.

Q. Ms. Kivitso, one of the issues that has arisen with Staff is concerns regarding the employee compensation system. As president and CEO of Montana-Dakota Utilities, can you describe why incentive compensation or at-risk pay is important to the Company?

A. Yeah, I think certainly as everyone in this room would recognize, attracting and retaining employees is one of my top priorities in my position. And we really do look at, and as supported by Jim Kaiser's testimony, a total rewards package. We're looking at studies that support our salary structure that reflects a combination of base pay, pay at risk, and benefits. And we look at all of that in total to make sure that we are competitive.

We've employed this similar philosophy for the

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past 20 years, and we believe that if that whole is competitive, if the decision is that incentive pay is not allowed, to replace that with base pay would certainly only increase the cost to our customers because a lot of our other benefits are predicated on base pay, such as a 401k contribution. So to move at-risk pay to base pay we believe would increase the cost for our customers.

Q. Another issue that has arisen with Staff is the use of the Company airplane. Can you briefly explain why the use of the Company airplane is important to Montana-Dakota's gas operations?

A. Certainly. We do take the use of the Company airplane seriously. I approve every request to use our corporate aircraft. And the reason we do that is because we want to make sure that it really is an economic decision. And so our use of that plane primarily would be for out-of-state trips. For example, our customer call center is in Meridian, Idaho. That call center serves all of our customers across an eight-state territory. If we have a need to get employees to the call center and multiple employees are going to travel, we will compare the cost to fly them on the corporate airplane as compared to a commercial flight for those same five people, hotel

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stays, and what not. So we really look at the economics before using that plane.

Certainly we also look at it for use in industry meetings and/or training. And in most cases, it's going to be more economical if more, you know, several people need to go to a location versus we're not using it for single-travel trips.

Q. Now, Montana-Dakota is requesting a rate increase. Can you just explain how the requested rate increase will affect customers and their bills?

A. Sure. In terms of the overall increase, I mentioned the 3.3 percent and rate design. It was also covered in opening remarks. But really this slide just shows how that 3.3 percent would be allocated. As previously mentioned, the residential and general service would be seeing the increases with the residential at 3.6 percent and our general service at 3.3 percent.

When you look at the residential prices, in terms of the basic service charge, we are proposing that this increase goes to the basic service charge. Our current basic service charge is at $19.60, and this proposed increase would take that to $21.42.

On the bottom half of the slide, you can see really how our customer bills break down. And

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currently approximately 61 percent of that bill is still just the pass through on the cost of gas. And so we believe, although with the basic service charge in place, a residential customer still does have and can see benefit by conservation of their use of natural gas. This represents, as previously mentioned, $1.82 per month increase for our residential customers.

And then just lastly, you know, when you look at that increase and where we're proposed, you can see on this graph that really our abundant supply of natural gas across the country and even locally here in the Bakken is certainly helping on our customer bills. When you compare back to 2008, you can see even with our proposal, a pretty significant decrease in the overall cost for your average customer over the last ten years.

Q. And Ms. Kivitso, as president and CEO of Montana-Dakota, are the rates the Company is requesting in this hearing just and reasonable?

A. Yes.

Q. Would you like to make a closing statement?

A. Sure. I guess I would just like to echo the thanks to all the parties. We've heard that before, but it really does take an effort in working with all of our parties in putting these cases together. So I

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want to thank the Commission, the Advocacy Staff and all of our interveners for your interest in this case. Certainly my job is just similar to what the Commission has stated, and that is really striking the balance between all of my interested parties, our customers, our employees, and the shareholders that provide us the capital to invest. And I look forward to the discussion over the next three days.

MR. SANDERSON: Your Honor, before I tender this witness, I'd like to offer exhibit MDU-8. They're just a copy of the PowerPoint slides Ms. Kivitso has presented here today.

THE COURT: Any objection?

MR. ARMSTRONG: No objection.

THE COURT: Ms. Jeffcoat-Sacco?

MS. JEFFCOAT-SACCO: No, Your Honor.

THE COURT: Mr. Coffman? Any objection to the PowerPoint?

MR. COFFMAN: No objection.

THE COURT: Okay. Major Unsicker?

MAJOR UNSICKER: No objection.

THE COURT: Okay. Exhibit 8 will be received.

MR. SANDERSON: And Your Honor, we'd also offer MDU Exhibit 11, 12 and 9 that Ms. Kivitso

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referenced in her presentation. These are the two NARUC resolutions and the AGA report she referenced.

THE COURT: Any objection?

MR. ARMSTRONG: We don't have any objection to the exhibits. I'm not sure I heard a reference, but . . .

MS. JEFFCOAT-SACCO: No, sir.

THE COURT: Mr. Coffman.

MR. COFFMAN: No objection, assuming that, you know, our competing resolution will be treated the same way.

THE COURT: Okay. Major?

MAJOR UNSICKER: No objection, sir.

THE COURT: Okay.

All right. So give me those number again.

MR. SANDERSON: Those were MDU Exhibit 9, 11 and 12.

THE COURT: Okay. So MDU Exhibits 8, 9, 11 and 12 will be received without objection.

MR. SANDERSON: And with that, Your Honor, we'd tender Ms. Kivitso for cross.

THE COURT: Okay. Questions for Ms. Kivitso. Mr. Armstrong?

MR. ARMSTRONG: Thank you, Your Honor.

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CROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. Ms. Kivitso, in your direct testimony you mentioned something about having four companies in eight states. What are those companies, and what states do they operate in?

A. So we have Cascade Natural Gas that operates in Washington and Oregon, Intermountain Natural Gas operating in Idaho, Great Plains Natural Gas operating in North Dakota and Minnesota, and Montana-Dakota operating in North Dakota, South Dakota, Montana, and Wyoming.

Q. And today you're here on behalf of Montana-Dakota, correct?

A. That is correct.

Q. And those other three companies would be your sister or brother companies all under the realm of MDU Resources, Inc.?

A. That is correct.

Q. And you're the president or CEO -- and/or COE of all of those companies, correct?

A. That is correct.

Q. And for all of those company, you would be the person similar to this case the one who authorizes filing of rate increases applications?

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A. That's correct.
Q. Am I correct that MDU is concerned with safety and reliability in all of those jurisdictions?
A. That is correct.
Q. And does MDU provide gas distribution services in all of those jurisdictions? Well, excuse me. Do all of those companies provide gas distribution services --
A. Yes, they do.
Q. -- where they serve?
A. Yes.
Q. And are all of those companies monopolistic publicly regulated utilities where they provide those services?
A. That is correct.
Q. And how long has Montana-Dakota, specifically the Montana-Dakota -- that's how I'll talk about it, company we're here today talking about -- been providing gas distribution services?
A. For many years. Many decades.
Q. Okay. And has it been able to provide a safe and reliable service to the people of North Dakota in that time?
A. Yes.
Q. And regardless of what happens in this rate

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case, you intend to continue to do that; is that correct?
A. That is correct. Although, I would add that we have an aging infrastructure. So what we had decades ago, as I referenced, when we were serving was certainly newer pipe in the ground.
Q. Are you aware of any of Montana-Dakota's replacement or repair projects that have ever been denied recovery in a rate case in North Dakota?
A. I am not aware of any that have been denied.
Q. Do you still have your slides in front of you?
A. Yep.
Q. Could you turn to slide five?
A. Yes.
Q. I had a question for you just for clarification. When you were testifying, you testified that these slides were major investments. Are those major investments since the last rate case?
A. In this case, correct.
Q. So the new town border station, that's been completed; is that correct?
A. The Mandan one has, yes.
Q. Okay. So the Man -- okay.
A. So we have a forecasted test period, so not all investment has been completed at this point.

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Q. And which one of these have been completed?
A. Precisely which ones -- I mean, we've done distribution mains, we have border stations that have been completed. We have a looping system that's been completed. And I believe the interconnection is complete as well.
Q. And mainly what I'm asking, are any of these major investments what you're talking about with the Systems Safety and Integrity Plan program?
A. No. Not specifically, no.
Q. And you're not aware of anybody contesting recovery for those investments in this rate case, are you?
A. I am not.
Q. Would you agree with me that by going through the rate case process for the many years Montana-Dakota has been in business that it has historically provided a safe and reliable system and been able to recover its costs?
A. Yes.
Q. But now the Company wants to implement the SSIP?
A. Correct. And again, I would echo the fact that we have an aging infrastructure. So at some point we have to embark on a program to put a replacement

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strategy in place to minimize risk.
Q. And do your other jurisdictions have aging infrastructure as well?
A. They do.
Q. All your other jurisdictions have early vintage steel and plastic pipe as well, correct?
A. Different versions and -- each system is different. So you can't really compare each system to the next. But each system has aging infrastructure, I would agree with that.
Q. And you said in your direct that 36 states have implemented some sort of recovery mechanism such as you're requesting in this case?
A. That is correct.
Q. Would it be fair to say that all of those states have different level of aging infrastructure as well?
A. And different types of pipe, yep, that would be correct.
Q. Has Montana-Dakota requested SSIP in any of the other jurisdictions it operates in?
A. Yes, we have a -- what I would call a safety tracker in the state of Washington. And we have it in the state of Minnesota. We will be -- well, we filed for it in Idaho. And we also are looking at filing for

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it -- we'll file for it in our next Montana case, Wyoming case. We have already filed for it -- or will file for it in Oregon. So we are looking at the mechanism really across our eight-state territory.
Q. So when you talk about it being in Washington, that's with Cascade, correct?
A. Correct.
Q. And if you talk it being Idaho, that's with Intermountain, correct?
A. We filed for it in Idaho, correct.
Q. And that's through Intermountain, correct?
A. Correct. We do not know -- it's pending.
Q. Okay. And you filed for it in -- have you filed for it in South Dakota?
A. No, not at this time.
Q. Have you filed for it in Montana?
A. Yes.
Q. What's the status of that?
A. We just recently had a settlement in Montana.
Q. How was SSIP affected by that?
MR. SANDERSON: Objection, Your Honor.
THE COURT: Sustained.
MR. ARMSTRONG: Your Honor, I think she's opened the door through the testimony leading up to it.
THE COURT: I disagree.

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BY MR. ARMSTRONG:
Q. You've already said in your testimony that you're waiting for the next Montana rate case to file it again; is that correct?
A. We will be filing in the next Montana case for an SSIP, yes.
Q. You had a pending rate case in Montana up until recently; is that correct?
A. That is correct.
Q. Has the Montana Commission recently ruled on your pending rate case in Montana?
MR. SANDERSON: Judge, I'm going to object to these pursuant to our previous discussion.
THE COURT: Sustained.
BY MR. ARMSTRONG:
Q. Ms. --
MR. ARMSTRONG: Judge, maybe at the conclusion of my other cross, we can take a break and discuss it as we talked yesterday?
THE COURT: Okay.
BY MR. ARMSTRONG:
Q. Ms. Kivitso, in your direct testimony you indicated that the primary reason for the need for increased rates is an increased investment in distribution facilities to improve system safety and

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reliability and the depreciation in taxes associated with the increase in investments; is that still the case?
A. Correct.
Q. And you're talking about the SSIP there, correct?
A. Well, that would be all investment.
Q. Okay. The SSIP though is not something that's being required of MDU by any law, is it?
A. Can you repeat the question?
Q. You're not implementing the SSIP because some federal or state law is requiring you?
A. That is correct.
Q. In fact, it's been done entirely voluntary?
A. We have filed for the SSIP I think for the reasons I stated, and that is that we believe our system is only getting older and at some point we need to take a proactive approach based on risk and assess what the right replacement strategy is to remove that aging infrastructure from our system so we can continue to provide safe and reliable service.
Q. And it's your testimony the time for that is now through this rate case?
A. That is correct.
Q. Even if the SSIP mechanism is not approved, MDU

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would still strive to provide a safe and reliable system, wouldn't it?
A. Yes, we would. But I would say that if we don't have that mechanism, it becomes a balancing act on how long it will take to get that replacement done. So as we've testified, this certainly helps us accelerate that replacement.
Q. Because what it does is allow you to recover the cost of it on an annual basis?
A. That is correct.
Q. So you'll provide a safe system anyway, you just need to recover the cost sooner; is that essentially it?
A. I think it provides us some financial stability and also provides us, you know, the ability to do that over a time frame that is shorter than what it would take if indeed we don't have a recovery mechanism in place.
Q. And that recovery mechanism would not have as much scrutiny as a rate case, would it?
A. The recovery mechanism, in my opinion, as we said, is each project will be completely -- details will be provided, there will be the same level of scrutiny on a regular rate case. I don't see how that would be less scrutiny.

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Q. Will there be interveners?
A. I think the interveners have the right to intervene if they desire.
Q. Will the Commission Staff be able to hire experts and counsel?
A. Legally, I would think so. But I guess I'm not maybe the one to answer that for sure.
Q. So are you envisioning a mini rate case every year then?
A. To me, whether -- how much involvement it takes to analyze the investment would certainly in my mind be less than it would take for a full-blown rate case. So I still believe that a three-day hearing for a full-blown rate case and the costs we'll incur for this hearing will certainly be more than even if you have interveners in your tracker. This case would certainly be more costly than a case predicated just on investment.
Q. And you would agree with me that any replacement project should be reasonable and prudent, would you not?
A. Correct.
Q. And you would agree with me that different subject matter experts often disagree on whether a project is reasonable and prudent?

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A. That would probably be fair.
Q. Moving on to a different area, Ms. Kivitso. Who do you report to? Like, who do you answer to?
A. Dave Goodin, the president and CEO of MDU Resources.
Q. And are you paid under the total rewards philosophy as well?
A. I am.
Q. And is part of your pay based on company earnings?
A. Yes.
Q. And those are earnings that would go on to the shareholders, correct?
A. They are. But again, I think the shareholder -- we need to recognize the importance of shareholder because they are the ones that provide us the capital to invest in our system.
Q. So are all employees part of the total rewards system for Montana-Dakota?
A. All employees are part of our total rewards system at Montana-Dakota, yes. I would say that our employees goals are different than -- the general employees goals are based on what I deem to be customer benefits. And so those goals are customer service and O&M targets, which in my mind go directly to the

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benefit of the customer.
Q. So it sounds to me like there's at least two different levels of employees. Some under the total rewards philosophy are based on the O&M goals and customer service, correct?
A. All employees we believe -- we put all employees under the total rewards philosophy. So all employees, including myself, have base pay, pay at risk and benefits. And we look at total rewards as whether or not that full package is competitive relative to similar positions elsewhere.
Q. Sure.
A. Goals are different. All of our employees goals are based on customer service and O&M containment. My goals are based on earnings and ROIC.
Q. And what is ROIC?
A. Return on invested capital.
Q. And are any other employees' total rewards incentives based on returns or return on invested capital?
A. The only other ones are the executive team.
Q. How many people is that?
A. We have nine executives in total at Montana-Dakota, not all are allocated to North Dakota.
Q. You mentioned in your direct testimony that the

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interested parties in Montana-Dakota are customers, employees and shareholders?
A. Correct.
Q. Would you agree with me that your shareholders also care about Montana-Dakota providing good customer service?
A. I would agree they do care, yes.
Q. Would you agree that your shareholders also care about reaching operations and maintenance goals?
A. Correct.
Q. And are those -- I've seen it referred to in different ways throughout the testimony. Some people say operation and maintenance goals. And some people say operation and maintenance expense goals. Do you know which one is more accurate?
A. It's really -- the goal is to basically it would be a target O&M expense. And to meet the goal we have to end the year under that number.
Q. And that would increase earnings as well, correct?
A. That would help earnings, yes.
Q. Would you agree with me that your shareholders care about staying competitive in the industry?
A. I would agree.
Q. Would you agree with me that your shareholders

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want the company to have a strong community focus and attract business?

A. I would agree. And I also agree our customers care about all five of those things you just asked me about.

Q. I agree as well. Would you also agree with me that your shareholders want to provide safe and reliable service?

A. Correct.

Q. As do customers?

A. Correct.

Q. You talked a bit in your testimony about the use of the private aircraft.

A. Yes.

Q. And you talked about reviewing it. Has MDU provided any documents comparing what commercial flights or anything would be compared to the use of the private aircraft?

A. As part of this case?

Q. Yeah.

A. I am not aware that we have, but that may be a question for another witness.

MR. ARMSTRONG: Judge, subject to a discussion outside the room as discussed and potentially an offer of proof, I have no further

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questions.

THE COURT: All right. Ms. Jeffcoat-Sacco.

MS. JEFFCOAT-SACCO: No questions.

THE COURT: Okay. Mr. Coffman, questions for Ms. Kivitso?

MR. COFFMAN: Yes, I have a few questions. Thank you.

CROSS-EXAMINATION

BY MR. COFFMAN:

Q. Good morning.

A. Good morning.

Q. I'm just going to go through your testimony and see if you can help clarify some things for me. I'm looking at page 5 of your direct testimony where you describe on about line 5 that the Montana-Dakota system has a low load factor where peak gas requirements occurring during the winter. Now, by low load factor, do you agree that there is great variation in usage over the year?

A. Yeah, I think we're getting to the whole, you know, winter peak, yep.

Q. So that's -- a high load factor would be less variable?

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A. Correct.

Q. So is it also true that you have within the residential class a good diversity among different customers amongst how much different customers use?

A. I would say, you know, usage does vary depending on, you know, efficiency of the home, the size of the home and all sorts of considerations, correct.

Q. And are you familiar with a handout that you provided at the public input meetings in this case?

A. Yes.

Q. I don't think this is part of the exhibits here, but do you recall a slide that showed the low, typical and high-use historical bill comparisons?

A. I do recall it. I certainly don't believe I could recite it. But I do recall the slide. I was at the public input meetings.

Q. If I refreshed your memory, would it sound correct that a low-use customer at 50 dekatherms would have about $471 a year where a typical-use customer at 91 dekatherms would have about an annual cost of $636 and a high-use customer of 150 dekatherms would be paying about $873?

A. Okay. That's -- it seems reasonable. The only caveat I would provide is I'm not sure if those numbers

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were based on a proposed increase before the Tax Cuts and Jobs Act or what those numbers were predicated on. But certainly we've had a change with the Tax Cuts and Jobs Act.

Q. Would it help if I showed you a copy of this handout?

MR. COFFMAN: Judge, May I approach the witness?

THE COURT: Yes, you may.

BY MR. COFFMAN:

Q. I believe it shows 2008 and 2013, and what are the last bars there?

A. Yeah, so 2008, 2013 current and proposed. So I believe this proposed would not have reflected the Tax Cuts and Jobs Act.

Q. So it would be somewhat less --

A. Correct.

Q. -- based on that?

THE COURT: You want to mark that and introduce it as an exhibit? Or are you fine with the way it is?

MR. COFFMAN: I could. Would there be any objection?

THE COURT: AARP-45.

MR. SANDERSON: No objection. I mean, is

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it just the one slide, for the record?

THE COURT: Just the one slide?

MR. COFFMAN: Sure. I can just -- or the whole thing?

THE WITNESS: Do we just want to clarify that that might not line up with what we're currently proposing?

MR. COFFMAN: Understood.

BY MR. COFFMAN:

Q. But do you have -- do you have any knowledge about the number of customers that you would find in a low-use or high-use category? What I'm trying to get to is the variability amongst usage within the residential class.

A. So I -- I apologize, but I would not be able to tell you how many customers would represent -- be represented in high use versus low use. I do not have that information in front of me.

THE COURT: Before you go any further, Mr. Coffman, let's mark that AARP-45. And we'll call it Handout of Typical Use For Three Levels of Customers Before the Tax Cut.

MR. COFFMAN: Right. It would be page 12 from the handout at public input hearings.

THE COURT: And if you want to offer that,

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it's been identified.

MR. COFFMAN: I would offer that as AARP-45.

THE COURT: Okay. Any objections, Mr. Sanderson?

MR. SANDERSON: No objection.

THE COURT: Mr. Armstrong?

MR. ARMSTRONG: No.

THE COURT: Ms. Jeffcoat-Sacco?

MS. JEFFCOAT-SACCO: No.

THE COURT: Major Unsicker?

MAJOR UNSICKER: No.

THE COURT: Okay. Exhibit 45 will be received.

BY MR. COFFMAN:

Q. So the -- I believe you testified that the gas portion of the -- the gas cost portion of the bill now is approximately 61 percent for a typical residential customer?

A. That is correct.

Q. And we're only here today talking about the other 39 percent?

A. That's correct as well.

Q. And so when you show the decrease in what a customer pays for their gas bill over time, that's

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almost completely related to the lower cost of the commodity, correct?

A. Correct.

Q. And is it not true that the distribution cost has gone up over the last ten years? Would you have a ballpark of what percentage the distribution portion of the bill has increased up until this rate case since 2008?

A. I do not have that percentage in front of me.

Q. And would you agree with me that the fixed part of the bill has increased more than the volumetric part of the bill?

A. That is correct. As referenced in 2015, the Commission had approved a fixed rate structure at that time.

Q. And you would agree with me that that more detrimentally impacts low-usage customers than high-usage customers?

A. I would agree with that, but I would still contend that there is the ability to manage your bill through the -- you know, conservation and your use of the energy product which still represents 61 percent of the bill.

Q. Yes, but you would agree with me that, would you not, that a low-use customer is someone who's

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paying less than the average is going to be -- has seen a higher increase in percentage base in their bills than the average or high-use customer over that time period?

A. Yeah, if I go back to the design of that, really the --

Q. I mean, is that a yes?

A. That's a yes.

Q. All right.

A. But what we need to keep in mind is our cost to serve a low-use customer and a high-use customer is the same. The amount of pipe we put in the ground, the amount of maintenance that takes place on that service line is the same whether they're a low- or high-use customer, and therefore the design of fixed versus variable.

Q. I think in answer to Staff questions, you did note that you were not aware of any issues that have ever been raised as far as the prudency of MDU's main replacements; is that -- is that accurate?

A. That is accurate.

Q. Okay. And so no prudency issues have been raised in this case or any other cases in your tenure at least?

A. Well, in this case, I would caveat that we have

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the 2018 investment and that discussion between us and Advocacy Staff, as Paul referenced in his opening remarks, that investment was a difference between our -- where we're at from a revenue and where Advocacy Staff was at.

Q. Isn't that question less of a prudency question, more of a timing issue?

A. Well, they've -- in their testimony they kicked that investment out, so . . .

Q. But the basis of that challenge was not prudency?

A. I guess I can't answer to that.

Q. Okay.

A. For sure.

Q. Do you believe that MDU has done a good job under your tenure of managing safety risks?

A. I believe we have done a good job. I would echo though that we do believe now is the time to implement a mechanism that will provide us the ability to look at proactively replacing our aging infrastructure. Our infrastructure is not getting any younger.

Q. Is MDU's natural gas service currently safe and adequate?

A. I believe it is, yes.

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Q. Do you have any reason to believe that it would not be safe and adequate without the SSIP surcharge?

A. I believe to continue the safety of our system, we need to look at a safety program. And Pat will testify to that as well. We need to continue to look at ways to provide safety into the future. You cannot rest on your laurels just because you have a safe system today. Does not mean that if you don't proactively address the safety of your pipeline into the future that you're going to continue to have a safe system.

Q. Well, let me ask you about page 8 under the question that's in the middle of the page there. You talk about your -- you're proposing a structured replacement program, you have early vintage steel, early vintage plastic, low pressure systems and the relocation of inside meters. And are these already -- are these currently priorities for MDU's main replacement program?

A. These are --

Q. Or is this a different priority?

A. These are priorities today. In fact, the dollars included in the case that we are -- have differences in terms of -- you know, those that Paul mentioned in his opening remarks, include projects in

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this category, correct.

Q. So if you were granted an SSIP surcharge, this prioritization would not change, correct?

A. We will continue to focus on this type of pipe for the safety of our system, that is correct, whether we have the mechanism or not. As I described earlier, what the mechanism allows us to do is potentially look at this on a more accelerated basis.

Q. Would the level of investment in main replacements that you are currently planning change? Would it increase the amount or just change the timing of the recovery of the cost for those replacements?

A. So if we are granted the mechanism, what we testified to is approximately what we would spend. We wouldn't increase the amount if we get the mechanism, if that's what you're asking. If we do not get the mechanism, what we will have to manage throughout our entire system, not just North Dakota, is how we adequately look at safety and reliability across our entire system and the recovery of such investment. And if, for example, we have too much regulatory lag or too much consideration, certainly we're going to have to make decisions, again, and the balancing act of our customers, our employees and our shareholders, and there is a chance that we would take this replacement

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plan out over a longer period of time.

Q. The AGA study, which was marked as Exhibit MDU-9, that study lists several different mechanisms from different states and provides some maps. But that particular study doesn't go into the details of those particular mechanisms and analyze them, does it?

A. The study does, but what was provided as part of the exhibit does not have all those details.

Q. Okay. Does the broader study make any conclusion about whether those states have more safe or more adequate gas service than those states that don't?

A. I am not aware of any conclusions drawn such as that.

Q. Isn't it true that in some states that have these accelerated surcharges that there have been explosions and other safety incidents?

A. In some of the states that have the surcharges, yes, there have been natural gas explosions. In fact, I would say that that is in some cases why there was response to implement a surcharge. And in some states where we have seen natural gas catastrophes and explosions, there have also been incentives actually for the companies -- or incentives have been provided to those companies to accelerate their action on safety improvement.

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Q. But what I'm asking is if you are aware of any studies that have analyzed whether such mechanisms have actually increased safety and actually reduced explosions?

A. I think the implementation of these mechanisms are relatively new, so I have not seen a study that has said -- certainly if you've got incentive, financial incentive, to increase the safety of your system, I would think your system is more safe. So I would argue -- but I have not seen a study that particularly calls that out that I'm aware of.

Q. I mean, that's -- I mean, if your main contention is that this is going to help with safety, wouldn't it be good to have evidence that such mechanisms actually are linked to lower leakage rates or to less safety incidents?

A. I guess in my mind, the 36 states that have implemented these mechanisms so far have taken the position that it is the right thing to do to enhance the safety of the system. So if I'm going to provide either a financial incentive, a surcharge, or a mechanism such as the one we're referencing that allows the company to reduce regulatory lag, you are replacing old pipe with newer pipe, and by that very definition you are enhancing the safety of your system.

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Q. So --

A. So I don't know that a study needs to be conducted to determine that.

Q. I assume that you follow other public utility commission cases around the country and follow trends and --

A. Certain of those, yes, I do.

Q. Would you agree with me that these mechanisms have been far from noncontroversial, that there have been quite a bit of controversial disputes?

A. In certain states I would agree with that. But in other states, I think there certainly was -- I guess stepping back in terms of the safety of the natural gas system, in certain states where there has been incidents, I certainly feel the customers have embraced these types of programs.

We are fortunate here in North Dakota that we have operated a very safe and reliable system. And I hope we can continue that into the future. But I certainly don't want to be one of those states that have to come in here after the fact and ask for a safety mechanism because I didn't ask for it before we had an accident or incident.

Q. Would you agree that where there's been controversy, the controversy has been of a financial

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nature. The controversies have generally not been about the projects themselves and whether or not, you know, what the safety priorities have been. The issues have been whether or not the customers are being charged fairly, whether it's a single-issue mechanism or whether or not customers are getting the benefit of a full audit; would that be fair?

A. I haven't seen a whole lot in that regard. I mean, in the states where we have that, I haven't seen a whole lot of that.

Q. All right. Did you review the resolution from the NASUCA, the National Association of State Utility Consumer Advocates, that was marked as an AARP exhibit?

A. I did not specifically read that one, no.

Q. But you understand --

A. I'm familiar with it, but I didn't read it in its entirety.

Q. You're familiar that consumer advocates in many states have raised concerns about single-issue rate pay?

A. I am aware of that, yes.

Q. And -- and I ask you to hypothesize or speculate. If this mechanism, this SSIP mechanism, had been requested and granted in, say, 2015, would rates now be higher than they would have been -- would be

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today?

A. If we would have gotten this mechanism in 2015, in general I would say the answer to that would be no. We've been investing in the safety of our system since 2015, I'm not sure it would look much different. We would have just potentially had the ability to delay this rate case had we seen recovery on those investments sooner.

Q. So customers would have been paying higher rates in 2016, 2017 because they would have had a surcharge on their bill?

A. But by the time you get to today's implemented rates, it would have been approximately the same. It just would have been a more gradual increase as suggested in our testimony.

Q. Can you say what percentage of this rate case -- what the Company's revenue deficiency proposal is that would have been flowed through an SSIP mechanism had you had one granted in 2015? And how much would not have been part of that mechanism?

A. So as part of this case, I think we're looking at around 5 million of investment. And going back in time, I can't tell you the percentage, but I can tell you in 2017, as an example, that number would have been about a $2.8 million investment, in 2016 about 1.7

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million. So I've got each year's total investment that we spent on safety and -- system safety and integrity, which would have correlated with this mechanism had we had it, but I don't know what percentage that represents of the overall increase.

Q. Could you speculate whether or not this rate case would needed to have occurred if you'd had an SSIP mechanism granted in 2015?

A. I don't want to speculate on that. What I could tell you is there's a potential that we could have delayed that or pushed that out. But I don't want to speculate.

Q. And you assert --

A. I don't want to speculate with 100 percent certainty.

Q. And you've asserted that this saves customers money because some rate cases may be delayed; is that --

A. Or avoided.

Q. And do you know what the -- could you estimate what the rate case expense is for this current case that would be included in rates?

A. I believe in this rate case, we have represented that the approximate cost of this case is 350,000. They have averaged between 300 and 500,000 to

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do a full-blown rate case.

Q. And would you agree with me that that's a pretty small amount compared against the TCGA savings that are being flowed through this case?

A. If you compare it to that. But again, if every dollar matters, as suggested by -- you know, we do believe every dollar matters for our customer. So in this case, if we all believe that safety and reliability is in the best interest of all parties, certainly that's what these investments represent. And if we can avoid the costly rate cases, we believe that is the most prudent way to go.

Q. Well, if this rate case were avoided, would residential rate payers see the benefit of TCGA today?

A. Yes, they would, as referenced by Chairman. We -- each state essentially had called us in and asked for our response to the Tax Cuts and Jobs Act. So most states are handling that as a single issue if you didn't have an open case.

Q. On page 14 of your testimony, you reference your witness, Dr. Gaske's, analysis and support of a 10.0 return on equity. And I'd just like to ask you, do you believe that a return on equity is a reflection of business risk?

A. Yes. That is one component, yes.

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Q. And do you believe that business risk and the allowed rate of return should be correlated? In other words, if you are -- if your business is riskier you should receive a higher ROE?

A. Correct.

Q. And would you agree with me that if the company is granted the benefit of an SSIP surcharge, your business risk will be less and your revenue will be more certain?

A. I don't necessarily agree with that philosophy, because our return -- our allowed return is a return on rate base. And whether we've got an SSIP mechanism or not, rolling in that rate base, it's -- that return is what you're allowed to return on your total rate base. So the investment, whether it comes in through a generate rate case or a safety -- system safety tracker, in my mind doesn't really affect the overall return allowed on that ultimate investment in our system.

Q. So you believe if investors are looking at MDU they will care one way or the other whether you have an SSIP mechanism?

A. I would say perhaps our credit analysts may provide -- that may provide benefit to our credit analysts and rating agencies that look at our debt and

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what kind of interest rate makes sense. They may care because it provides a little bit more stability for the Company.

Q. And it -- doesn't revenue stability equal less business risk for MDU?

A. Potentially, I guess. Maybe there's a minor impact there. But I still -- I go back to your ROE is what you're allowed to earn on your investment. So whether that investment came in through a tracker mechanism or a general case, it's still level of return on the investment in your system.

Q. Would you agree with me if MDU's business risk is lessened that the risk to customers is increased? I mean, is it a zero sum game?

A. If MDU -- say that one more time. I'm sorry.

Q. So if business risk changes, is there a corresponding shift of risk to rate payers? Is it a zero sum game or can MDU's business risk be reduced without a corresponding shift of cost risk to consumers?

A. Hmm. If our business risk changes, are you asking if that directly impacts our customers?

Q. Yes.

A. It kind of depends on what component of business risk. There's all sorts of components,

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whether you're a small company, whether you operate in the Bakken, whether you don't. I mean, business risk is comprised of multiple things, so I can't really make a general statement on whether which specific business risks would have a direct impact on our customer.

Q. But would you agree with me that business risk -- that risk to your business doesn't just go away, it's mitigated or it's shifted someplace if it's reduced; would that be fair?

A. Right. If we have inherent business risk, you're right, it doesn't just go away, it's inherent. Yep.

MR. COFFMAN: I'll end there. That's all I have. Thank you very much.

THE WITNESS: Okay. Thank you.

THE COURT: Major Unsicker, questions for Ms. Kivitso?

MAJOR UNSICKER: No questions, Your Honor.

THE COURT: Okay. Ms. Jeffcoat-Sacco, questions for Ms. Kivitso?

CROSS-EXAMINATION

BY MS. JEFFCOAT-SACCO:

Q. I did have a couple and most of them were covered by Mr. Coffman. But I wanted to follow up just

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a little bit because you answered Mr. Armstrong about the financial stability benefit that was coming to the Company if you're granted this SSIP. And the questions that you also talked about I think in that question about how the replacements would then be over a shorter time frame. And I couldn't understand at that time, and I don't know that you got to it with Mr. Coffman, that shorter time frame. Can you explain that a little bit more to me? Because are you saying that your decision of whether or not to perform this upgrade or required maintenance would be different if you were under a SSIP versus a standard rate case?

A. So -- in terms of looking at the safety of our system, we have done I believe a great job of prioritizing our risk. I think that's been demonstrated in testimony and rebuttal testimony that's been provided. So I won't belabor that. But we're going to look at the risk of our system and replace pipe that we believe needs to be replaced, whether we have this mechanism or not. I want to make that clear.

What we would distinguish is over how many years would we replace that infrastructure, and this is predicated on multiple things. In other words, our capital availability, you know, the timing and amount of crews that are available. But if we do not have a

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mechanism that provides for a recovery over a more timely period of time, we may make the decision to instead of look at this over a ten-year period, as an example, look at it over 15. But, again, those decisions are not made in a vacuum, we consider it across our entire footprint and consider other states besides just the state of North Dakota. So those are things we'll take into consideration if we do not have the regulatory mechanism.

Q. But if you have a safety issue or a risk, how can you possibly say that you'd make a business decision not to fix it as quickly as you could based on how you would get recovery? I mean, you have an obligation to do the right thing, and you are guaranteed recovery for the right things you do under the regulatory system as it stands today. I have a real problem making that transition from the recovery mechanism to the business decision to maintain a safe and reliable system. I can't -- I mean, how would you make a decision to go from ten years to 15 years if it needed to be done?

A. If it needs to be done, we're going to do it. Again, I want to be clear on that. But some -- when you're looking at replacing this kind of amount of pipe as demonstrated here, there are -- you know, there is

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some, you know, leeway within that replacement period. Whether you do that over, again, a ten-year period or a little bit longer period, there is some, you know, leeway in that period of time that you do it. We are going to make the investments that we need to make, as we have done for several decades, to maintain the safety of our system. We will do that. It's just a matter of studying what comes out of the studies that we're doing with respect to, for example, the early vintage plastic pipe. You know, what we're doing there is going in and looking at different towns, pulling out samples of pipe. We're going to have -- this is a process that will be fluid as we discover what we have buried in the ground and, you know, what the studies predicate.

And what I'm suggesting is if we don't have that regulatory mechanism, perhaps we would adjust that slightly. I'm not talking about a major adjustment to the timetable here. And if there's an immediate need that's immediate this year or next year, we're going to do that.

Q. So it sounds to me like you're saying with the recovery mechanism you may be replacing some things that there isn't an immediate need for. And I think that's part of what Advocacy Staff was saying in its

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testimony that there could be unreasonable replacements that haven't been justified. And if you don't get it, you're going to -- possibly would be stretching it out and perhaps not be meeting your -- I see this as sort of a vicious cycle, I'm not hearing any answers to close it off anywhere. But others can, you know, others can get to that question in a little more detail.

I do want to go back then very quickly to this ROE because we have hundreds of pages of testimony discussing -- maybe not all of it discussing the concept of risk and whether or not a more stable regulatory environment which would include more stable financial recovery for this particular process affects investor expectations and consequently ROE. I just heard you answer Mr. Coffman that it did not. Again, I think you need to explain that a little further to me, because I'm not seeing that based on the rest of the testimony I'm reading.

A. Yeah, I think one factor within the -- when you look at return on equity and what's being requested in the case -- and, you know, I would defer some of this to our expert witness, Steve Gaske. But as I look at the ROE that we're requesting, certainly business risk is a component of that. And -- but that -- of that

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component of business risk, it -- you know, a smaller component of that would be financial risk. So I mean, there's multiple components that go into assessing what the right ROE is for a particular -- you know, could you argue that you get a mechanism such as this? I mean, this is going to cover a small amount of our total capital. Certainly it's not going to cover all the investment that we're putting into the ground. You know, he's arguing that maybe that would reduce the overall risk component. I'm not sure it's enough to affect our overall ROE.

And what I'm saying is whether we get the investment put in the ground as part of a general rate case, or I guess recovery of the investment we put in the ground as a general rate case or as part of a tracker, really what you're looking at is what are you allowed to earn on the investment that you have in the ground. That's what I'm saying. Yeah.

MS. JEFFCOAT-SACCO: Okay. Those are all the questions I have. Thank you.

THE COURT: Okay. We're going to take a break here. It's about 10:13. I'd like the attorneys and the witness and the court reporter back at 10:25 so we can go over the evidentiary issue. And then the commissioners, if you would hold off a little longer

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until we resolve the evidentiary issue, hopefully we can have you back by about 10:30.

(A break was taken at 10:13 a.m.)

(Commissioners not present for the following discussion.)

THE COURT: All right. We're basically off the record -- we're talking to the court reporter on the record now. I want the attorneys to gather around for a little sidebar. You can stay on the witness stand. Just remind you, you're still under oath.

THE WITNESS: Okay. Thank you.

THE COURT: Okay. We're back on the record, but we're not on the video. We're outside the presence of the commissioners. We've had an issue that came up --

MS. JEFFCOAT-SACCO: We're not on the Internet?

THE COURT: No. We had an issue that came up, and we discussed it yesterday on a motion in limine to exclude a settlement agreement in the state of Montana that addressed return on equity, and it addressed this SSIP program. And there were compromises made of those issues. I have ruled based

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on the briefing filed by the parties that that settlement offer is not admissible in evidence in this proceeding. And I will not be allowing that into evidence. If Mr. Armstrong would want to make an offer of proof, that can become part of the overall record that would go to the courts ultimately if this case goes on. I'm afraid we might be inserting appealable record and prefer to try to keep it clean.

And so on that basis, I have denied the admissibility of the exhibit yesterday in the motion in limine. Now, we did start with Ms. Kivitso to get into the some of the subject matter of the Montana settlement agreement. Mr. Armstrong argued that that opened the door for some additional questions. I'm going to allow him to pose his questions at this point that he thinks I'm excluding or denying him under the sustained objections just so we have that on the record in case of an appeal. Go ahead, Mr. Armstrong.

MR. ARMSTRONG: Thank you.

BY MR. ARMSTRONG:

Q. Ms. Kivitso, you were the person who authorized the filing of a rate increase in Montana as well as North Dakota, correct?

A. Correct.

Q. And in Montana, you've agreed to defer the SSI

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program in that case, correct?
A. The SSIP program?
Q. Yes.
A. In the interest of a settlement, we did.
Q. Okay. And that was approved by unanimous vote by the Montana Commission yesterday; is that correct?
A. That is correct.
MR. ARMSTRONG: That's my questions.
THE COURT: Okay. All right.
With that, we'll --
MR. ARMSTRONG: Judge, are you still disallowing that?
THE COURT: Am I allowing that in the --
MR. ARMSTRONG: Can we have some argument on that issue?
THE COURT: Go ahead, Paul.
MR. SANDERSON: Well, he can't argue that she opened the door when he is asking questions trying to get her to open the door. That's ridiculous.
MR. ARMSTRONG: My questions that opened the door were from her direct testimony and the 36 states have approved it, it's in other states. You can't say these 36 states have approved it and then not address the other jurisdictions, especially the ones Montana-Dakota is operating in that haven't approved

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it. So I'm not making her open the door. It's part of her direct testimony, part of the facts of this case.
THE COURT: I'm -- I'm fine with your discussing with her the fact that they -- that the settlement which -- the case in Montana is resolved and that they do not -- did not adopt the SSIP in Montana. I think you've already got that in the record.
But as far as using the contents of that settlement agreement to somehow prove those same facts in this case, either the return of equity, or that the SSIP can be delayed, I am not going to allow it for that purpose.
MR. ARMSTRONG: That's -- Your Honor, I'm not talking about return on equity right now. But she said --
THE COURT: But that's the next --
MR. ARMSTRONG: -- numerous times up here that they need the SSIP now, they need it now and it's for safety and reliability and that's whey they need it now. But they've just deferred it in Montana.
THE COURT: I don't have a problem if you limit your questions to what's going on in other states or that the SSIP was disallowed in Montana. But as far as it being part of a settlement agreement between the Company and Montana, I'm not going to allow that

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because there we get into Rule 408 problem, and I think it's a big problem because Rule 408 realizes what Mr. Sanderson was talking about. It was remodeled recently to get into situations where you attempt to use it to impeach by a prior inconsistent statement or something like that. And still the rule, I think, is fairly -- that offers of compromise are not admissible or that the elements of that offer of compromise, just by the mere fact that it was agreed to for that purpose, is not admissible.
MR. ARMSTRONG: I would just note that it's not a settlement anymore, it's an order of the Montana Commission.
THE COURT: I understand that. But I believe that -- you want to talk about an order of the Montana Commission, I don't have a problem with that. I do have a problem with you talking about it as a Rule -- as an offer of compromise that they entered into.
MR. ARMSTRONG: I understand.
MR. SANDERSON: And Judge, to me the record's been clear on it. Any additional or trying to beat this horse is just cumulative evidence at this point. Mr. Armstrong established that it is not part of their case in Montana and that Ms. Kivitso said we

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will request it the next time.
THE COURT: Yeah, and I think that's already come into the record.
MR. SANDERSON: And it wasn't disallowed, it was -- Montana-Dakota pulled it as part of a settlement agreement. The Commission didn't disallow or rule that we're not going. So continuing to go down this road is improper. The record is clear. Mr. Armstrong's made his record and he's made his offer of proof.
THE COURT: And I think you've made it clear that they don't have it in all states where they do business. There's some that have, some that haven't. And so this is something they're gradually trying to progress in, and I think you've got your record good enough on that. I mean, I think you're running the risk if we let too much in that maybe then he's got a record made that's an appealable error.
MR. ARMSTRONG: That could be, Your Honor, but I do view it -- the Commission is more like a court trial, they can consider the weight and admissibility of it as decided by counsel. It's not fair to Staff or to the Interveners to pretend that all these jurisdictions are pushing this through, pushing this through and it's necessary now but then leave out what

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they've settled in the last month.

THE COURT: I don't think there's any reason why you can't argue the first part of that, that some states are adopting it, some aren't. And that's come out very clearly through Mr. Coffman's cross as well.

But what I do think is that you can't reference the fact that they agreed to that or that that's part of a settlement. You can talk about what they're doing in Montana. I don't have a problem with that. But I don't want that to be referenced as a settlement.

MR. ARMSTRONG: I understand. But if he -- if I'm supposedly beating a dead horse, then I don't want to hear Montana beat the dead horse of everything that's going on around the country.

THE COURT: You can ask your questions when we go come around. We're going to go back around again. First I'm going to give the commissioners a chance to ask a few questions when they get back.

MR. SANDERSON: And I didn't ask --

THE COURT: But I do disagree with you in a sense that I'm the gatekeeper here. The reason I'm here is to preserve the record and to decide which evidence gets in, which evidence doesn't, what's duplicative, what isn't. That's why I'm here.

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Otherwise, I'm just a potted plant and they have no reason to even hire me. So I mean, I -- you know, you can take up an evidentiary question ultimately, maybe at the end of the case, but we're not going to take them piecemeal. That's -- I don't believe that's appropriate.

MR. SANDERSON: Just as far as the order of presentation, I mean, as the applicant, you know, I think under the rules, we get last say on this. So are we -- are we going to go through --

THE COURT: We're going to go around again. First I'm going to let the commissioners ask some questions, then I'm going to go back to you, go around in the same order, and back again. If there's a need for sur-surrebuttal at that point -- hopefully there's not, because now we are fallen behind, we're still on our first witness. But I think everybody wanted to score a few runs in the first couple of innings and try to swing for the fences, and I think we've done that.

So let's go back on the record and bring the commissioners back in. We'll go back on the record when they get here. And on the public video.

(Commissioners present.)

THE COURT: Okay. Back on the record.

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It's about 10:37. Ms. Kivitso is on the witness stand, she's still under oath. For the commissioners' benefit, we had an evidentiary issue involving a document and whether the document should be admitted or not admitted. And I think we've resolved that issue, and there's going to be some additional questioning.

First, we're going to go to the questioning by the commissioners and then the attorneys are going to get one more go round. So I'm not sure which commissioner wants to start. Commissioner Kroshus?

EXAMINATION

BY COMMISSIONER KROSHUS:

Q. Good morning, Nicole.

A. Good morning.

Q. You're lucky in the sense that everyone else that has to testify is watching thinking you'll be done, and they're not.

I want to get -- I want to start with the SSIP, the Safety System and Integrity Program because that's really one of the more significant issues in the rate case for me. Really trying to get a handle on the risk factor. And just for a -- you know, an opening question, if you were a consumer or a household -- owner of a residence, should they be concerned?

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A. No.

Q. So with that being said, and I assumed that was the case, can you talk about -- the plastic pipe that you're talking about, is that -- is that the biggest issue, or is it equal in terms of that and then the steel pipe?

A. Well, essentially what we've done is we've -- in the testimony, and Pat can also reference this when he has the opportunity to testify, but we have presented basically a risk analysis around our aging infrastructure. And really what we're looking at is the likelihood of an event happening and the consequence. And what's factored into that risk analysis is all sorts of data points such as the age of pipe, the type of pipe, leak -- past leak survey. And Pat would be better to give all the details of that. But we've essentially compiled all at that data to develop a risk score then for each of the various pieces of pipe in our system. And what that has done, the culmination of all of that data has produced that what we believe to be our highest risk, which is the early vintage plastic pipe and the early vintage steel pipe.

So depending on -- you know, if you're asking which is the bigger piece, I'm not sure if you're

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asking by in terms of replacement dollars, you know, quantifying would it be more to replace one or the other or which is the --

Q. Risk.

A. Risk, we really deem them -- I don't have the exact scores in front of me, but since we've prioritized them both at the top, they've got to be very close in terms of risk.

Q. Now, Advocacy testimony asserts that the plan lacks detail. Do you agree with that?

A. I believe there is a lot of detail in our plan.

Q. Now, one thing that was alluded to earlier and it's related to timing, the timing of why now, why not doing it as during the course of business as maintenance, there's always replacement, would you agree?

A. Correct.

Q. That you're looking at when you're running a company with a lot of infrastructure. So for me, the timing, that's the hardest part for me to get my arms around. Is the plastic pipe in question, is that good for another five years? Another ten years? How would you answer that?

A. And that's where I would talk to that we are bringing experts in to help us with that analysis. So

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on our plastic pipe, and again Pat will be able to provide additional details here, but we are bringing in folks that are experts in the industry to help us analyze that. And we have been given some guidance from them in terms of even if you did nothing, how much longer would this pipe last in the ground. And so we're relying on our own internal experts, but we're also hiring folks to come in and help us with that analysis.

In terms of the timing, and maybe just to clarify that, as I mentioned before but I want I want to echo again, if we have an urgent, immediate need from the safety perspective, we are going to replace it now regardless of this mechanism. When I suggested about the timing and looking at how long do you replace this pipe over how long will it last, to your questions, that's where we're relying on our internal experts as well as outside experts to help us with that analysis. Because what we do know is to go in and replace this all today and put it in the next rate case would certainly have massive consumer and customer impacts.

And so again, back to my opening statement where we're trying to balance the interests of our employees, our customers and our shareholders, that's

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what we're doing. We're looking at the risk. We're saying now is the time to start a replacement program where we want to work with the Commission, that you can help us identify and prioritize these projects based on what we believe are in the best interest of the Company and over what time period makes sense.

Q. In 1998 as a part of the testimony, and I honestly don't remember which sheet it was on or where I picked it up from, but there was a 1998 report about brittle pipe for pipe put in prior to 1988. So that report was issued 20 years ago. Would you frame it up as the plan, the SSIP plan, in some ways has been under way for a considerable period of time just through -- you've been replacing pipe over the last 20 years, correct?

A. For years, yes.

Q. So is it safe to assume that that report was certainly taken into account as a part of that replacement project or --

A. Correct. Any industry guidance that's provided, as an example on the Aldyl A, which is a piece of our early vintage plastic pipe replacement program, that came out of an PHMSA report. So, yes, we are monitoring industry action and what's taking place in our industry with respect to concerns that pop up.

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And then we identify whether we have them or don't have them in our system. Yes.

Q. Have there been any leaks that you can tie to the old pipe?

A. We do have leaks throughout our system, yes.

Q. But that -- but leaks that would be directly tied to aging infrastructure, not construction techniques, not something outside of now it's old pipe, the joints are failing and -- and I don't want to send a panic wave through because --

A. Right. We do have leaks in our system. Pat can probably better describe exactly where those are, but we do have some in conjunction with some of our older pipe. Again, not to alarm folks, we do a leak survey annually in high consequence areas in that, but yes, leaks have been identified in certain segments of our pipe including the pipe that we're replacing.

Q. At a higher rate?

A. I'm going to defer that to Pat.

Q. Okay. So the pipe stops at the meter; is that a fair statement?

A. Correct.

Q. So from curb to meter or from main to --

A. That's our jurisdictional pipe, correct. In house is the customer.

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Q. Yep. So the problem pipe, if you will, or the high risk infrastructure is outside of the home in most cases?
A. Right. Interior pipe is outside of our jurisdiction, so I can't comment on a customer's -- the shape of any individual's customer interior pipe.
Q. Do you have some inside meters?
A. We do have some inside meters.
Q. So the pipe to the inside meter though --
A. Would be ours, yep.
Q. Do you know offhand what percentage of -- how many shut-off valves is a percent of home -- replace the excess flow valve?
A. Yeah, I do not have that exact percentage. We may be able to get that for you. I do consider it at this point to be relatively low because essentially we have only installed that on new services. One of the advantages certainly of this replacement program would be the installation of excess flow valves on any new replacement that we do.
Q. Right. That ties into a question that I'll check off.
I'm going to jump over to -- there was considerable testimony about the Tax Cut and Jobs Act and how that is impacting utilities across the country,

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not only from lowering rates, but also from a credit ratings standpoint for utilities. Has that negatively impacted MDU's ratings?
A. It has not. We have seen -- certainly we, like other utilities, have seen the impact on cash flow. This change is affecting our cash flow. But we have not seen any credit rating changes because of that.
Q. Now, Fitch and S&P have you rated at triple B plus, correct?
A. Correct.
Q. And how long have you been rated at triple B plus?
A. I don't have the exact timeframe, but for a lot of years.
Q. Okay. So Moody's recently -- and it was toward the end of January -- changed the outlook of 25 U.S. regulated utilities primarily impacted by tax reform, and I think for the majority, if all not, they went from -- well, they were downgraded.
A. Correct.
Q. But just to verify then, you were not included in --
A. We were not included in that, no.
Q. Okay. How do you -- as I've read through a number of rate cases or rate adjustments across the

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country, the average gas utility across the country has lowered customer bills by $2 or more, typically in a range of 2 to 3 dollars. Your numbers came in differently when we adjusted the interim from -- and I don't have that in front of me. But it was, let's see, from 2.44 it went down to $1.82. Was that driven by still leaving SSIP into the equation, or how would you explain -- that's a significant difference compared to what most utilities are granting their customers.
A. So I think if -- I think what you're asking me is the Tax Cuts and Jobs Act, how it impacted us as it compares to other utilities across the nation impact?
Q. Why was it as pronounced for the consumers?
A. Yeah, really I think really that comparison is going to be somewhat difficult because, you know, there were two impacts with the Tax Cuts and Jobs Act. One was taking the current rate from 35 to 21. And when you do that, you're really basing it on the revenue requirement. And it's probably hard to compare what kind of revenue requirement we need relative to another utility. The other piece of that change is going to be the -- basically the repricing of your excess deferreds. And really both of those are predicated on the level of investment you have in the state that you're doing business. So if we've got a different

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level of investment than another utility, it's pretty hard to do a one-for-one comparison on the impact of the Tax Cuts and Jobs Act. But I do know that we have other witnesses that are going to cover the Tax Cuts and Jobs Act in a little more detail.
Q. Okay. First quarter, you had a good first quarter, 45.7 million of terms of earnings in Q1, and that was for the regulated energy portion of your business, correct?
A. That would be for the utility, yes.
Q. The utility. And that's up from 42.2 million last year, so an increase of 3.5 million. So when people see that, consumers see that, they're going to say, well why are they asking for a rate increase when earnings are up. How would you answer that question?
A. I think what we need to consider, and when individuals are looking at either the InView Resources news release or our portion of that new release, the thing that we need to keep in mind is when we're presenting a case in front of a commission, it is for that jurisdiction only. So today what we're here to talk about is North Dakota Gas. What you're looking at is a culmination of our earnings across all of our states. So while we may be at our allowed return in another state, we may not be in this state. And so it

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is really hard to look at our overall earnings and compare that to a need in a particular jurisdiction which is only a subset of our total utility.

Q. Okay. Fair enough. Do you have any concern with your credit worthiness as a result of tax reform? That was one of the factors or points that was made in a number of articles that I read. Any concern with that?

A. It certainly has impacted our cash flow, as I mentioned. At this point in conversations I've had with those that work with our rating agencies, we are not aware of any immediate concerns that they have. But certainly what they will do is monitor our financial metrics. And to the extent that they are deteriorating or that there's indication that because of the reduced cash flow we're not going to be able to meet their -- you know, they have standards that they want you to meet as a regulated utility. So to the extent they see concern or deterioration of those over time, certainly that is something we are very mindful of, and that is one example on, you know, where we're concerned about our credit quality and our debt and equity is -- the credit rating is very important to us.

Q. So --

A. But at this point, we don't have any indication

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from those agencies other than we're going to continue to monitor your metrics.

Q. Okay. I don't want to get into sensitive information on this question, but generally speaking have you found it more challenging to deal with capital markets as a result of the Tax Cut and Jobs Act and the fact that you're a regulated utility?

A. I would say we have certainly seen the conversation change because it does impact regulated utilities different than it affects our unregulated businesses. So as an example, our corporate stock price, there's conversation around the impact of the regulated utilities around tax reform. There's conversation with our credit rating agencies around tax reform. And in general, regulated utilities, the impact, although very beneficial for our customers, has a different impact for the business. And so, you know, there has been, you know, conversation around that.

Q. On -- I believe it was in the Gaske testimony -- and of course, this is -- testimony ages, obviously, and at the time that it was written cited uncertainly in oil pricing slowing customers outside of Bismarck and an increase in late payments. Does that still apply in terms of a slowdown now that oil prices have improved significantly?

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A. Are you specifically asking about late payments or other impacts from the Bakken.

Q. No, we can take the late payment part and just set that aside.

A. Okay.

Q. But customer growth and volume, is that still being impacted?

A. Our customer growth today is certainly different than it was years ago. And so if you're asking whether or not we're seeing, you know, substantial increases in the Bakken, we are not anymore. And so that growth has certainly slowed. I would say it's more stable today than it was as it was, you know, coming off of the highs of the Bakken boom.

Q. Okay. I'm going to go to -- I just want to talk a little bit about households and limited income. What types of savings plans do you promote to a household that -- and the reason I'm asking this is in some of the testimony I think the rationale -- or maybe not rationale, but it was stated that what a customer could do is they could decrease consumption, in effect. But I think if you're a customer that is already struggling financially, you really can't afford to then go out and buy new windows for the house, you may not even be able to afford to put new insulation in the

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attic. So they're certainly impacted because they're just in a tough financial position to do a lot about the house that they're probably fortunate to live in.

What type of plans, educational initiatives do you present to those people, because again, as I mentioned in my opening commentary, it's tough for some people. Every little bit matters. How do you work with that?

A. Yeah, I'd offer up we have two considerations that come into mind here. We've got a balled billing program where you can really look at levelizing your bill instead of, as mentioned previously, where obviously generally on the gas side of the business we're peaking in the winter, we have programs where you can balance that bill over the year. We also have low income assistance programs available as well. And, you know, we will work with customers as needed. So . . .

Q. Do you expect an uptick in low income assistance need?

A. I don't know if I can predict that. I mean, based on this increase, I don't think I would predict a significant increase there. In terms of our bad debt, we have actually seen that come down over the last three years. A piece of that is probably attributed in North Dakota -- I'm talking only North Dakota now -- to

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the Bakken and some of the more levelized -- where that's levelized out, out there. But we have actually seen those write offs come down.

Q. Okay. Would that be similar to just businesses that came for a short period of time --

A. It could be businesses.

Q. -- and decided not to stay and left?

A. It could be businesses, it could have been residential, correct.

Q. Okay. But more stable -- stable business environment. Okay.

I think the -- I have more questions related to the timing of the infrastructure, but I think I will wait -- or the infrastructure request, the SSIP, I have still quite a number of questions on that, but I think I will wait for the witness -- the next witness -- or not next one, but -- I will wait on that. And I don't believe I have any other questions at this point. Thanks.

THE COURT: Commissioner Fedorchak.

COMMISSIONER FEDORCHAK: Typically the Chairman goes next.

THE COURT: Okay. Chairman Christmann.

CHAIRMAN CHRISTMANN: I only have a few.

COMMISSIONER FEDORCHAK: I have my list.

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EXAMINATION

BY CHAIRMAN CHRISTMANN:

Q. Refresh me on who is the witness on the total rewards package.

A. Jim Kaiser.

Q. Okay. Regarding the discussion between building especially the residential rates more toward volumetric or more toward a monthly base flat rate, do you have any statistics on how many meters you have out there that are -- and I don't know what the right term would be -- kind of occasion use things I'm thinking where someone has gas hooked up so they can barbecue in the summer or something like that, or a garage that they only heat rarely over the winter, but for the most part, even in the winter months, either just the base rate or very close to it?

A. I do not have that information in front of me. I apologize. I think we'd be able to get it for you though. Limited use meters is what you're asking.

Q. I would be very curious about that, because if as we would go to a more volumetric system, if that were the case, those people would be the biggest beneficiaries; am I correct?

A. Correct. Those that are using a limited amount

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of gas would benefit from more of that volumetric charge. And again, I guess where we're at with rate design is we really believe the cost, regardless of whether you use our service or not, we still had to put a service line in to get to your meter, we have to maintain that service line. So our argument is similar to if you just were to compare it to a cable company. They don't charge you based on how long you watch your TV, they charge you to install the cable to your home. So we really are -- the cost to serve each customer is really the same.

Q. Things like cabins and such with a gas meter for barbecuing in the summer, that would not necessarily --

A. They wouldn't be sharing their share.

Q. -- the fixed income type people?

A. Correct.

Q. And do you have any statistics -- I think your answer to one of the questions by Mr. Coffman was that usage varies depending on size and efficiency of homes. Which is the bigger factor?

A. I would only be speculating. I'm not sure on that.

Q. So you have no studies or anything that show that some of the typically newer but certainly larger

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homes with all the modern energy efficiencies, how much gas they use in relation to their smaller counterparts that might be older and not have those energy efficiency improvements?

A. Yeah, I'm guessing your more efficient larger home is probably in better shaper than your smaller, but that would be speculation. We probably do have data on that. I just don't have that at the top of my head.

Q. It seems like in this discussion it would be useful data. I just feel like it must be out there or else all the things we talk about all the time with promoting energy efficiency is all just a guessing game, and if that data isn't out there we're just guessing whether it actually works or not. So if that could be provided, I'd sure be interested.

I'm switching now to the SSIP improvements.

A. Okay.

Q. Are there historic pieces of equipment or types of pipe or anything like that within the gas industry that have just been banned that maybe were used years ago and found to be too dangerous and have all been replaced?

A. Well, certainly, you know, the cast iron and bare steel, you know, have been a high priority

essentially across the nation. We don't have that issue in North Dakota here. But completely 100 percent banned, I -- I'm not aware. But there's certainly been studies that suggest, you know, whether certain type of pipe should be on a replacement program such as bare steel, cast iron, you know, the PHMSA came out with the Aldyl A.

Q. And explain why the cast iron and bare steel isn't an issue here?

A. Because we don't really have that in our -- we don't have that type of pipe in the system.

Q. Because it was --

A. That was primarily plastic.

Q. -- when North Dakota was settled; is that --

A. Correct. I mean, I think that's --

Q. -- century old?

A. Right.

Q. Okay. So how would you compare, you know, safety agencies within the government's efforts to see that those types of pipe are replaced compared to what we're seeing -- you mention the NARUC resolution to promote the replacement in kind of a quick manner with the plastic pipe that we're talking about here?

A. Yeah, I think each state is really looking at it in terms of its own -- I don't want to call them

issues. But each state is evaluating what kind of system it has, what risk it has within its system, and, you know, they're making their decisions based on that.

So similar to how we've evaluated what pipe we've got in the state, you know, what type of risk we think it bears and what priority we should put on in terms of the replacement, each state commission is going to be looking at, you know, what's being brought in front of them and evaluating what they deem to be at risk or not, along with obviously the utilities in that state.

Q. But would it be fair to say that nationally where those other types of pipe exist, that there's been a stronger effort to see that those types of pipe are replaced than the type that you're talking about here, or would you say they're comparable as far as safety risks?

A. I would say, you know, nationally in terms of, you know, media and what you saw come out first was probably the bare steel and cast iron, yep.

Q. And you said that if the SSIP program were adopted that all the projects would not go forward without PSE approval, correct?

A. Correct.

Q. The projects that are being worked on right now

in New Salem and Fairview and the whole list of towns, what approval process did they go through?

A. Right now, they are part of this case. So they would --

Q. But you started construction on them without any advance approval?

A. Right. And that's because just like we do with other investments in a general rate case, we make investments that we believe are prudent and we bring them before the Commission. In the case of an SSIP mechanism, we would file those projects with the Commission in March and then we would not get recovery on those prior to approval from the Commission. That's really the way the mechanism works. You know, similar, we've got mechanisms on the electric side of the business in the state of North Dakota that are very similar to what we're suggesting here.

Q. But when you file in March, is it going to be money that's pretty well already spent though because you've already bought supplies and hired contractors?

A. Potentially not all the dollars would be spent, but some of the dollars would be spent. But that goes back to if I really feel it is a safety need, I have to proceed. And so we would be proceeding with some of the projects, you know, certainly in March. We won't

have spent all of the dollars. In fact, it would probably be very minimum considering the construction season in the state of North Dakota. But we would proceed with contractors and getting the worked lined up if we believe it's the right thing to do from a safety perspective, yes.

Q. Okay. No other questions. Thank you.

THE WITNESS: Okay. Thank you.

THE COURT: Commissioner Fedorchak.

COMMISSIONER FEDORCHAK: Thank you.

EXAMINATION

BY COMMISSIONER FEDORCHAK:

Q. Thank you, Nicole.

Just following up where Randy left off on the timing. So you'll file in March, you wouldn't get recovery until October, but you'd be starting on those projects that year?

A. Correct.

Q. So if we deem them to not be prudent, you just wouldn't get the money, or then what?

A. That would be correct, and we'd probably bring them forward in the next general, whatever rate base we're at in the general rate case.

Q. Okay. Is the -- the use -- is this tracker,

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can it be compared to riders for, say on the electric side for transmission or generation? And in what way is it similar and how is it different just in terms of how it would function?

A. It is very similar to what we have on the electric side of the business in terms of environmental and the generation and those types of tracking mechanisms.

Q. Okay. Is the objection then that in those cases where we have the transmission, we have the generation, we have the environmental for all the electric utilities -- well, maybe not the generation for all of them. But is the objection that in those cases we typically do an ADP or have pre-reviewed the projects before they get added to the rider on a separate way and that mechanism isn't allowed here in the tracker you're proposing? Could that be a difference?

A. That would be a difference, I think you're right, on our large projects. But we do not bring all of the dollars forward in the form of an ADP on the electric side of the business. So, you know, you're aware, Thunder Spirit we would have brought forward in an ADP, but not all transmission projects would have been brought forward. So certain of our projects on

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the electric side of the business that we deem to be large enough, we do bring those forward as part of the ADP. But not all dollars that go through the tracking mechanisms on the electric side of our business are brought forward in an ADP before they're put into those mechanisms.

Q. Okay. So is there a way that the Company could provide the big picture, like, here's the whole plan, this is what we need to do, here's what it's going to cost, bring that forward through some sort of process like that and then use a tracker to recover it? Is that feasible? Or does it have to be this year by year kind of constantly changing, perhaps less thorough review of the systematic changes?

A. I think we would be open to bringing forward our plan over a time period. I think we in general provided that as part of the testimony here. We talked about the early vintage plastic pipe and what, if we were to embark on that project, what the cost of that would be over the entire life of that project. We talked about the total project cost as it relates to the early vintage steel and early vintage plastic as part of the testimony here.

But, you know, we would be open to, you know, more dialogue around looking at that plan in its

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entirety. I will say that as part of this plan, as I mentioned earlier, we are going through and working with other experts in the industry that we've hired to evaluate the pipe we're pulling out of the ground to make sure that we are making the right decisions in terms of what to prioritize first. Some of the data that comes out of those studies that are going to be done by GTI and others have the potential of changing the path and, you know, the outcome of what this, you know, long period -- or, you know, what the horizon looks like in terms of that replacement plan. But certainly as we know it today, you know, what we've presented in testimony is kind of where we're at with that plan.

Q. Okay. I do have some more questions like the percent of the system that's been identified at risk and the percent of the system that would be replaced and the percent that's vintage steel and plastic. But we don't want to take away everything from Matt to have to do his job. You've done a lot of his job already, so I think I'm going to save the rest of those specifics for him. But it is helpful to get your kind of view on this approach as a whole, because it's a philosophy.

A. Yep.

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Q. So the -- help me to then -- I think my final question on the specific mechanisms of this tracker as it relates to the mechanics of it. Help me understand the -- functionally how the tracker would be different than if you did this through rate cases? Would you be looking at every year rate cases? Would you be looking at doing this in one big after five years of investment? How would it functionally be different?

A. Yeah, I can't provide 100 percent certainty in terms of what this would mean in terms of would we be filing every year, every other year if we don't have the tracker, but what I know is with the tracker we would have less rate cases than we would if we don't have it. And so to do the investment, so as an example you said five years, would you wait five years and file for something, you know, at the level of investment we incur today and implementing this safety program, certainly waiting five years is not going to produce the financial results we need, you know, to produce a strong financial company.

And talking about the credit metrics and some of the earlier conversation with respect to tax reform, that lag would just probably be too much for us to absorb without some sort of detrimental impact on the financial side of our business. So certainly we

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wouldn't be able to wait five years without a mechanism. It's hard for me to predict exactly how many years that would be with the mechanism, because it really depends on what level of other investment we have, how fast our customer growth, because of course that pays for some of this, is occurring in our communities in North Dakota. There's just a lot of variables there.

Q. And how would you respond to the issues raised by Staff and the AARP about the loss of the opportunity to look at offsetting issues in a tracker versus a rate case? How would the Company address that and assure that you somehow would be able to take that into consideration?

A. Certainly the biggest one that was referenced is the Tax Cuts and Jobs Act. And something that significant, you know, that has that big of an impact, we are going to come in and address that individually. Smaller offsetting items, to the extent that those accumulate, you know, we'll be in for another general. It's not like implementing a tracker, which represents a pretty small portion of our overall investment, is going to eliminate the need entirely for rate cases. What we're saying is it reduces that and saves our consumer costs over time. But those all would be

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factored into an overall general case.

Q. Okay. I got -- I have two other areas. One just again relating to the AARP's testimony about the 100 percent of the cost being allocated to the service charge. Can you really defend that? Is it 100 percent of it appropriately targeted to the -- a basic service charge? Is it any portion related to the usage by the customers from the Company's standpoint?

A. So I would go back to you know, really the rate design we've implemented, and we do have witnesses that will talk in more detail about the rate design as well, but goes back in terms of again the philosophical argument that we have, which is the cost to serve that customer is the same regardless of usage. And that's really how we've predicated our rate design in this case.

Q. So you're saying it is 100 percent the same?

A. 100 percent --

Q. It's all -- there's nothing that's related to usage, it's all -- it's exactly the same regardless of how much they use, the cost to serve them? The customers?

A. Correct. Philosophically, the cost to serve the customer is the same regardless of how much gas they use.

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Q. Okay. All right. Then my final area here is relating to the ROE. How much are you involved in discussions with investors?

A. On a pretty regular basis.

Q. Okay. And is it MDU Resources as a whole that is seeking the capital, or do you guys seek it separately? Do you have separate --

A. So in terms of --

Q. Equity side.

A. On the equity side of the business, we are funded through MDU Resources equity. On the debt side of the business that is imbedded at the utility specifically.

Q. Okay. So how would you characterize the availability of capital for MDU now and the interest by investors in MDU utility?

A. So I would say the availability of capital that -- you know, the interest rates are -- we're seeing an increase in interest rates on the debt side of the business. I think with in terms of our ability to raise debt, I still feel confident that we have the ability to raise the debt we need to fund the projects in our.

On the equity side of the business, in terms of our equity analysts, I was just recently at an AGA

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industry meeting where some of our investors come and certainly they have the opportunity to pose questions of myself, of Dave Goodin, and a lot of their interest does, you know, come around when they're asking around the utility is the regulatory environments in which you operate, are you at your allowed returns. And so there are a lot of questions around regulatory lag and how far behind are you with respect to your allowed returns, what are you earning in your states. And so there is a lot of interest in terms of our ability to earn at our allowed return. And all of that does factor into, of course, the MDU Resources stock price in total which obviously influences our ability to raise equity in the capital market to fund our projects.

Q. So are you earning your authorized return state?

A. In the state of North Dakota, no.

Q. What is it? What's your return?

A. I think in 2018 -- in 2018, we projected our ROE with tax reform to be 6.128 without this increase.

Q. And why -- what would you say are the biggest factors preventing you from earning that return?

A. The investment that we've incurred since the last rate case.

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Q. So your rates are too low?
A. Correct.
Q. Does that affect your ability to attract investors, that return that you're currently getting?
A. Correct. Yes. On an overall basis, I mean, our ability to not be at our allowed return certainly has an impact on MDU Resources in total.
Q. Can you speak to specific issues that's created as in higher interest rates or anything like that that might affect customers? Like, why should customers care about this? Is there any benefit to them to you guys being appealing to Wall Street?
A. Yes, the benefit to our customers and why they should care about our shareholders and our debt holders is because they are the ones that give us the money to invest in our system so that we can provide safe and reliable service for our customers.
Q. And is it -- but you aren't having any trouble attracting that money, and so the difference between a 9.5 and 10 percent ROE matters a lot to customers because it's $500,000 less that they have to pay. How does it -- why should they -- why should we and then therefore the customers, why should that perspective want to allow you a higher return? What benefit would it give them?

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A. Basically a more financially viable company through our ability to at least earn our authorized returns will add value over time to the Company, thus increasing the stock price and reducing the amount of shares needed to be issued to raise the same amount of capital so that we can put investment in the ground.
Q. But would you agree that a 9.5 percent allowed ROE with rates that allow you to achieve that is -- does that? That provides you what you need?
A. I mean, essentially whether we're walking about 10 percent or 9.5 percent, I'm going to defer that to Steve Gaske in terms of our ROE witness. But today with rising interest rates, I believe that, you know, some of the allowed returns in our state have not contemplated the rising interest rate environment that has taken place over the last year.
Q. Okay. And does this SSIP -- how does Wall Street view those mechanisms?
A. Again, I would probably say that when you're looking at our debt analysts, they do take into consideration, you know, what I would call tracking and -- they look at regulatory mechanisms that we have in place. So weather normalization, decoupling, fixed fee, some of those things. And the more stable you are, there is some value there. But again, I would

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come back to that is just one small component in setting the overall ROE for a utility is the, you know, financial and/or business risk of that company.
Q. Okay. I think that's it. Thank you.
THE COURT: Okay. Counsel, I would like to wrap up with this witness soon. But I'll give you one more go round.
Mr. Sanderson, any redirect?
MR. SANDERSON: Yeah, briefly, Your Honor.

REDIRECT EXAMINATION

BY MR. SANDERSON:
Q. Ms. Kivitso, I want to go back and address some of the concerns about the timing and then the cost of the SSIP, because specifically with respect to the questions by AARP's counsel and then more importantly by the Commission's counsel this fear of are you telling us you're not going to -- the cost of the factor and you're not going to replace this. Your testimony as shown by the slides was you currently have over 2500 miles of pipe in North Dakota, correct?
A. Correct.
Q. And you're just -- using the round math, you said 25 percent of it is over 50 years old. So roughly 650 miles. Could the Company go out today and replace

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650 miles of early vintage steel and plastic pipe?
A. Well, let's ask Pat Darras that. No, I think to answer your question, certainly that would be a challenge both operationally and more importantly the customer impact of such investment would be quite significant. So the first challenge would be operationally, we certainly could not handle that with our own crews, we would have to hire contractors. And then more importantly is the customer impact of doing that over a one-year time period would be very difficult.
Q. And it gets to the point -- and I think the point you were trying to make, Ms. Kivitso, budget and cost are factors that are weighed into this, the whole picture of what prioritizing projects and safety. Is that a fair representation of your statement?
A. That is correct.
Q. But in addition, you're to -- the recovery mechanism, the SSIP program that Mr. Darras is going to talk about in more detail, that's also trying to prioritize these projects based on risk analysis and other factors as well?
A. That is correct.
Q. Okay. I want to give you a scenario, Ms. Kivitso to maybe address two of these issues on the

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cost to serve and ROE and this issue with the strong company. Let's take the coldest Sunday night in January and we have a gas line break. Is it important to have a strong company out there to serve customers and have the resources in place to provide quality and reliable service to North Dakota customers?

A. It certainly is.

Q. And take that scenario. You have a gas line break, you've got to send out your technicians. Is there a difference in cost to the house that maybe only uses 70 dekatherms versus a house that uses 110 dekatherms?

A. No.

Q. The repair costs that go out to fix that are --

A. Would be the same.

Q. Okay. Ms. Kivitso, I have no further questions. Thank you.

THE WITNESS: Thank you.

THE COURT: Mr. Armstrong.

MR. ARMSTRONG: Thank you.

RECROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. Ms. Kivitiso, I just have a few questions for you. You're aware that yesterday Montana approved

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MDU's requested tariffs and did not include -- or approved MDU's tariffs and did not approve the requested SSIP tariff; is that correct?

A. The SSIP tariff was not a part of the settlement.

Q. And the SSIP is being deferred in Montana until the next general rate case?

A. We will be filing for an SSIP in our next general, yes.

Q. And in North Dakota, the proposed SSIP you said it will be filed in March but you won't get recovery prior to approval, correct?

A. That is correct.

Q. And once you get approval though, there is a return component on to those projects, correct?

A. Correct.

Q. Okay. So you will be earning a return on those before it's ever evaluated in a full rate case?

A. If the dollars are approved as part of the mechanism.

Q. And that process to me does sound a lot similar to what an ADP is; would you agree? An advanced determination of prudence?

A. In an ADP we are not earning on the investment once approved. We would get an advanced determination

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of prudence that it's a prudent project, but we're not going to get recovery on those projects until we roll that through either a tracker on the electric side of the business or do a general rate case.

Q. But you're asking here for the projects to be approved and have a recovery on them, so it's even more than an ADP?

A. Similar to our electric trackers in North Dakota, correct.

Q. But in this case, there is not anything built into the mechanism for any additional review or similar to like we have in this rate case, is there?

A. There is an opportunity to review these projects.

Q. Right. Is there a filing fee?

A. I couldn't -- I don't know the answer to that.

Q. So let me represent to you that I haven't seen any filing fee that allows Commission to hire staff or experts. If that's the case, you would agree there's less scrutiny of that from Commission Staff?

A. I think the Commission has the opportunity to look at the project similar to what's being done on the electric side of our business for those trackers.

Q. And for instance, the estimated 2019 SSIP amount is $6 million to be added to the rate base; is

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that correct?

A. That's correct.

Q. And that's something you would want to pass through that mechanism in that manner?

A. Correct. I think it's 42 cents per month if implemented.

Q. It's not a small amount, is it?

A. 42 cents?

Q. Yeah.

A. Per month? I would call that somewhat minimal.

Q. So if every dollar matters, at some point 42 cents doesn't matter?

A. Every dollar matters. But again, this is an investment in the safety and reliability of our system, and for 42 cents I would say it would be a good investment in safety.

MR. ARMSTRONG: That's all the questions I have. Thank you.

THE COURT: Okay. Mr. Coffman?

MR. COFFMAN: Thank you.

RECROSS-EXAMINATION

BY MR. COFFMAN:

Q. Ms. Kivitso, you were asked questions by Chairman Christmann regarding house size and energy

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efficiency as it relates to the fixed portion of the bill, I believe. And I guess you said you didn't have data based on that. But isn't it true that the more volumetric your rates are, the more incentive there is for a customer to invest in energy efficiency or to engage in energy conservation?

A. And again, I would say that since 61 percent of the bill is based on the cost of gas, there still is incentive to conserve.

Q. But that wasn't my question. My question was, if that was -- if the volumetric portion of your rates were greater, would that not provide a greater reward for energy efficiency?

A. It would, but for all the other reasons of serving that customer is the same whether they use or don't use gas, we would still argue that the fixed rate is the right way to go.

Q. So you just think that's enough? 61 percent is enough to provide an energy efficiency reward to customers?

A. I guess we're trying to look at the fairness across all of our customer classes, and to consider that you have some households that have a meter with limited usage is just equally as unfair to those that are using a lot of gas when the cost to serve those

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customers is the same. So you've got to look at the entire customer base, not just one subset of our customers.

Q. Your testimony here today is that it cost the same to deliver gas to every customer is the same?

A. Our fixed costs are essentially the same to install that service line -- I mean, to a residential customer as an example.

Q. Are you familiar with the cost of service study that your company provided in this case?

A. Yes.

Q. Could I refer you to Exhibit MDU-6, Mr. Hatzenbuhler's rebuttal testimony? Do you have that with you? I just wanted to refer you to page 1 of his exhibits. So that's statement M, as in Montana, page 1, the first page after his Q and A.

A. Okay. I think I'm there.

Q. Okay. On that -- and there, the cost of service is broken down for residential customers into the demand, energy and customer components, correct?

A. Correct.

Q. Do you see those columns?

And the third column, which is the customer charge, that's the cost of the meter and billing and all the costs that are the same for every customer; is

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that fair?

A. You're in which column? Can you say that one more time, please?

Q. That would be the fourth column, the customer column.

A. Okay.

Q. And if you look down at the column to the net distribution cost of service just before the double line, that's about $20 million. But the total residential cost is $26.9 million; is that right?

A. Correct. That's what it looks like, yep.

Q. So those other costs, the difference there are costs that are related either to the demand or energy components. And this is your own study, right?

A. Yes, it is.

Q. Okay. And other witnesses in this case have taken issue with that and argued that the customer portion is even less. But this is your own -- your own witness says that the cost is not the same to serve every customer; isn't that right?

A. I probably would defer this line of questioning to Jordan.

Q. Well, how important is the cost of service study in your opinion when setting rates within the residential class?

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A. I think it's a component of getting to the right rate for our residential customers.

Q. But if you put everything into a fixed fee for the delivery of cost, aren't you disregarding your own cost study?

A. Again, I'll probably defer these questions to Jordan.

Q. Okay. I just have one more question, and it relates, I guess, to Commissioner Fedorchak's question about rate cases. And I guess you said that you might be able to delay rate cases perhaps longer than every five years if you had an SSIP in place. Is that what you said, or could you clarify that?

A. Yeah, I didn't say longer than five years. I don't want to predict that. To say that we could stay out for five years is -- I want to be clear, that's not what I was intended to say if that's how you were interpreting that. It is hard to predict when rate cases will be necessary. But what I do know is a mechanism such as this does allow us recovery that provides consideration for the fact that whether or not we could delay a potential general rate case.

Q. So the benefit to customers in your argument is that, say, $350,000 of rate case expense might be delayed in the future?

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A. Right, 350 to 500 to whatever that number is, yes.

Q. But under the SSIP paradigm, wouldn't you have two more rate cases every year, or two cases of some sort, like limited-issue cases?

A. Right. And as I mentioned earlier, we believe the cost of such a case would be substantially smaller than a fully blown litigated rate case.

Q. Do you have a ballpark estimate of what those cases would cost?

A. I do not.

Q. And isn't the real financial benefit to the utility a reduction of regulatory lag if you were to be granted an SSIP?

A. That would be the financial benefit to the utility and our creditors, correct.

Q. And isn't another way to view regulatory lag from a customer's perspective is that it's the incentive to be cost efficient? Doesn't the regulatory lag provide some incentive for the utility to be more cost efficient in the short term?

A. As part of a general rate case, all of our -- as you have seen by the differences of opinion between us and our interveners, you have seen that expenses are fully scrubbed as part of a general rate case. So I

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believe our incentive to operate efficiently is certainly not reduced by changing the way that we would implement a mechanism such as this.

Q. I appreciate your perspective on that. But under the SSIP mechanism, rate payers would have more frequent rate increases, correct?

A. That would be correct.

Q. But they would be smaller?

A. That's correct.

Q. And there would be -- and there would be pre-approval of projects that are not currently pre-approved; is that right?

A. Pre-approved, I don't necessarily agree with pre-approval. We are going to proceed with the projects that we deem necessary, just like we do today. And it's not that we'll get pre-approval necessarily, other than if we get a decision before we actually execute that specific project. But that would be probably more by happenstance because we're going to continue to proceed with these safety projects. So I don't know that I would necessarily call it pre-approval.

Q. But does it provide some regulatory certainty that you wouldn't have under the current system?

A. To some degree, potentially.

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MR. COFFMAN: That's all I have. Thank you very much.

THE COURT: Major. I was beginning to think you might be a colonel before we get finished with this.

MAJOR UNSICKER: I just have one follow-up.

RECROSS-EXAMINATION

BY MAJOR UNSICKER:

Q. It's the follow-up to Commissioner Fedorchak's questions on ROE. And you said you're generally familiar with other rate cases that go on throughout the country?

A. Correct.

Q. Are you familiar with the ROEs in those cases?

A. I believe Dr. Gaske has testimony with respect to ROE achieved in other cases across the country, yes.

Q. Okay.

A. I don't know if I've got all the specifics in front of me, perhaps I do.

Q. Well, in general over the past ten years would you agree that those ROEs, for both electric and gas, have traditionally been going down on average?

A. I would agree, because the interest rate

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environment was decreasing over the last ten years and now we're heading into an increasing interest rate environment.

MAJOR UNSICKER: That's all I have. Thank you, ma'am.

THE COURT: Ms. Jeffcoat-Sacco.

MS. JEFFCOAT-SACCO: I have no questions.

THE COURT: Okay. Ms. Kivitso, you can step down.

THE WITNESS: All right. Thank you.

THE COURT: Mr. Sanderson.

MR. SANDERSON: Yes, at this time Montana-Dakota would call Pat Darras.

THE COURT: Mr. Darras, I'll have you spell your last name for the record.

THE WITNESS: D-a-r-r-a-s.

THE COURT: And I'll have you raise your right hand. You were here when I gave the perjury admonition?

THE WITNESS: Yes.

PATRICK DARRAS,

duly sworn, was examined and testifies as follows:

THE WITNESS: Yes.

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THE COURT: Okay. You may sit down. Mr. Sanderson?
MR. SANDERSON: Thank you.

DIRECT EXAMINATION
BY MR. SANDERSON:
Q. Good morning, Mr. Darras. Can you please state your full name and business address for the record?
A. Patrick Darras, 400 North Fourth Street.
Q. And whom are you employed by?
A. Montana-Dakota Utilities.
Q. And what is your position with Montana-Dakota Utilities?
A. I am the vice president of operations and engineering.
Q. And could you just briefly describe your responsibilities in that role?
A. Yes. I have executive oversight for both the gas and electric operations.
Q. And Mr. Darras, could you just provide us a brief overview of your educational background and work experience?
A. Yes. I am a graduate of North Dakota State University with a bachelor of science in construction engineering. I've also got a masters in management and

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a masters of business administration from the University Of Mary. Been with the Company approximately 16 years, all in the operations side of the business. Started as an engineer, field engineer, and then was moved up into a region superintendant position overseeing just the gas side. Then from there in 2008 was moved into the position of region director where I oversaw the gas and electric operations for the Dakota heartland region. And in 2015 was moved into the position that I currently hold today.
Q. And Mr. Darras, are you familiar with MDU's application for a natural gas rate increase in this case?
A. Yes, I am.
Q. And what was your role in -- general role with respect to this case?
A. General role would have been really testifying, I guess, as far as the SSIP program itself.
Q. And Mr. Darras, did you submit both pre-filed direct and rebuttal testimony in this proceeding?
A. Yes, I did.
Q. And if asked the same questions as indicated in your pre-filed testimonies, would your answers remain the same?
A. Yes.

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Q. In addition, have you prepared some PowerPoint slides regarding your areas of testimony today?
A. Yes, I have.
Q. And as we go through your questions, if you want to refer to your PowerPoint slides, please do so. But generally, Mr. Darras, can you just describe the challenges in operating a safe and reliable gas system in North Dakota?
A. Sure.
THE COURT: Is that an exhibit, Paul?
MR. SANDERSON: I'll offer it at the end again.
THE COURT: Okay.
MR. SANDERSON: Certainly, Judge, it's MDU Exhibit Number 10. It's in the exhibit book that the Commission has and we provided to all the attorneys. So instead of turning, if you want to look in your exhibit book.
THE COURT: Thanks.
MR. SANDERSON: Thank you.
BY MR. SANDERSON:
Q. So Mr. Darras, just briefly describe the challenges in operating a safe and reliable gas system.
A. Sure. When we look at the challenges, obviously there's a lot of different types of

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challenges. But the ones that we talk about the most I guess or will be talking about really is the aging infrastructure that we see at Montana-Dakota. It's also across the industry wide, it's not something unique to Montana-Dakota, but we'll get into the details of that as far as we're concerned. Changing regulations, again, that is an industry-wide item. And then unknown attributes, and what I say -- I've got pre-code versus post code on there. When I mention pre-code, I'm referencing the PHMSA 192 part that we have to follow, the safety guidelines. And basically post code would be post when that was implemented, which was in the 1970s. Prior to that, obviously there was different regulations, requirements of operators. So when we say pre-code and unknown attributes, that would be that we truly do not know what is in the ground. We were not required to, and to this day we still do not understand what's in the ground.
Q. And Mr. Darras, is that just a problem facing Montana-Dakota, or is that industry wide across the country?
A. That is industry wide. Again, I think each operator is unique in how much of the unknown is out there. But, again, it is something that is required of us to report every year to the federal -- to PHMSA

basically in our 7100 report, we have to put how many miles of pipe that are unknown or have unknown attributes. And that is a requirement of all utilities across the United States.

And then the last one I do mention is the increasing costs. And again, that's construction costs, material costs, really everything related to the operation of the system.

Q. And Mr. Darras, your next slide indicates a typical early vintage steel mechanical fitting. Can you just describe what we're looking at in that picture and why you included that?

A. Yeah, I think throughout my testimony, you'll hear me talk about dresser couplings or mechanical fittings. What you see there, if you look at the pipe, it looks pretty good where it's been cleaned off on the lower left-hand side. That is installed in 1937. We just dug that up last year due to a forced main replacement project.

But when we talk about the potential for leaks -- and again, this was not leaking pipe -- what I like to point out is the dresser couplings themselves, which are the square items there, you can see really at both T's, the one's in a shadow, but there is five dresser couplings on that picture alone. You got a line going

up to, say, the top right and a line going to the top left and then the line to the bottom, right and left. And each one of those connections was put together back in the 30s, we will say, late 30s with those dresser couplings. So they have been in the system for close to 100 years, let's say 80 years.

The way those fittings work, they've got a rubber gasket that basically compresses down on two pieces of pipe. So again, there is the risk, the potential risk, that we see when we're talking about dresser couplings themselves in this older vintage pipe. In this case, this pipe was not leaking, it has been in the system for many years. Is there a risk there? Yes, there is.

Q. Mr. Darras, now I want to turn and focus initially on the various projects included in the 20 -- the Montana-Dakota's 2018 main and service line replacement that are included in this case. Can you just describe to the commissioners those projects and what's happening?

A. Sure. And when we talk about these, again, these are not a part of the SSIP program that we're saying. These are the 18 projects that are in the rate case itself. So basically the towns that we have identified as projects that will go on this year in

2018 are Taylor, Fairview, Gladstone, New Salem, Eldridge, Barlow and Cleveland. And there's really a mix, as you can see after the names of each of those town, on what type of pipe or what type of material is in those systems that we'll be replacing.

To date, I believe -- we have signed contracts for all seven of them. To date, we've got crews on the ground in Barlow, Taylor and New Salem.

Q. And are some of those contractors doing multiple towns for Montana-Dakota?

A. Yes, they are. For those projects, actually the three different towns that they're working are three different contractors and they will be doing multiple towns.

Q. And Mr. Darras, as part of this project in these towns, is the Company testing pipe? Or can you describe what's being done as you do these projects?

A. Sure. And I've got a later slide that I can get into a little bit more of the early vintage plastic pipe study. We will be taking samples out of these towns and sending those in to a third-party contractor. And again, this is the piece of this, the whole SSIP, which I refer to as the program itself, is fluid. When I look at it from an operational standpoint, it is truly fluid. We are changing this thing on a daily

basis based on what information we get in from the field, from different regulation changes, from different studies that are out there beyond what we do internally.

So as part of the plastic pipe that we have slated for this year, the intent is to really take different vintages -- and when I say that, we talk pre-1983, which I'll mention at a different slide, too. But really it's to take that pre-1983, which has been identified in the industry by a higher risk factor, and we're trying to take the lower and the upper limits of that. So one of our towns we'll be studying is in the 1971 vintage for most of the pipe. One of the other towns is in that higher limit, which is 1981 pipe. And then the third town that we'll be doing is the unknown, which a majority of the pipe in that system that we show on our GIS is unknown.

Q. Now, I want to get into, Mr. Darras, the SSIP program. Can you please explain why the Company, Montana-Dakota, needs and developed and implemented the SSIP program?

A. Sure. I think the -- up on the screen, I've got the drivers, or I call them drivers. I would say that one of the -- if you look at it from an industry wide basis, it's probably those top four bullets which

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would be the recent fatal accidents that we talk about or that are known as far as in Allentown, Pennsylvania and San Bruno, California. The other piece is the Integrity Management Program, or the IM Program, that was rolled out and signed into law in 2011. Again, I say aging infrastructure on the slide there, but that's really from an industry wide basis. This is not something unique to Montana-Dakota.

And then really just recently, I would say there has been a large push by federal -- through federal guidelines really to look at systems on a more proactive versus reactive approach. Again, this is industry wide. The one thing I want to point out there that's out there is an API recommended practice. Again, it is recommended, it is not to date a code requirement by PHMSA. They have had many meetings on that to see if they should move that direction. But right now they are trusting industry to take the seriousness of pipeline safety and really look at it from a proactive approach versus the reactive that has been more commonly done in the past.

So that's really the industry wide side. From MDU's standpoint, we are really looking at it, or what's driving it for us is to better understand our threats. Like I said, we have a large percentage of

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our pipe or our system that is unknown to us. That's why we're doing studies like plastic pipe study. It's -- going back to the picture that I had on the slide, those dresser couplings do not show up anywhere on our maps. We have to dig it up. And when we dig it up, we get an e-mail from the field basically saying, look at what we found here. There's five dresser couplings on there. We didn't know that. We show that it goes four different directions. What we don't know is how many dresser couplings are there.

The other thing that we've done is just this more defined systematic approach to identify replacement projects. Again, I look at this as a more formalized approach to how we're doing -- how we're going to replace our pipe going forward. Again, we have replaced pipe for years. It is something we will continue to do based on risks. But this is -- for us to really take it and try and formalize the approach versus a more, I'm going to say, reactive way of handling the way we replace pipe in the past.

And then the last piece I would just throw in there is really the funding mechanism to avoid frequent rate cases. Again, that is a -- there's two different ways that I look at this, obviously from an operation standpoint, I am looking at it from a truly system

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safety standpoint. But as Nicole's testified, there is the funding mechanism that, as she has talked about, how that would help us, I guess, fund some of these projects.

Q. And your focus of your testimony is on the application of the program and mechanical side of this?

A. Correct. The operations side.

Q. Yeah. And Mr. Darras, just for the record, attached to Exhibit -- MDU Exhibit 3, your rebuttal testimony marked as Exhibit PCD-2-2-2-2-2-2, is a copy of the SSIP program as revised as of March 15th of this year, correct?

A. Correct.

Q. Okay. Now, Mr. Darras, can you explain -- you've talked about PHMSA, but can you explain the PHMSA Integrity Management Program and how it relates to what the Company is doing?

A. Sure. So the PHMSA IM Program, again, it falls under part 192 which are the minimum requirements that are required of all operators to operate a gas system. Basically that was rolled out in -- or signed into law in 2011. What I would say is it really followed along the same path as the transmission side of integrity management, which was signed into law in 2006.

Again, integrity management is growing, as you

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can see, that's -- you know, it's ten years and it's got from transmission and five years later it went into distribution. So really when I'm talking this program, we are focused -- or this program just on the distribution side of things, which is what's called the IM versus the D-I-M-P or DIMP Program.

Really the objective of what PHMSA requires us to do is to really develop a model, which we call internally a DIMP model and to better understand our system and identify those threats. Again, once we've identified the threats, now we have to put a risk profile to that and truly determine internally how we want to go about mitigating that risk or that threat.

When you look at it, one thing that is a requirement that all operators have to follow is the eight threat categories that I've got up there, which are corrosion, natural forces, equipment failure, excavation, incorrect operation, joint failure, outside force, and other. So each one of those has a risk score associated with it, and then also the pipe that's associated with that to come up with a risk ratio, basically.

Q. Okay. And Mr. Darras, using your next couple slides, can you just explain the Company's SSIP program and how you intend to implement it and manage it?

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A. Sure. So from a high-level construction replacement plan, or the SSIP program, is really what we focused on is -- we being internally with our SMEs -- is truly what we're calling the early vintage steel pipe. We have drawn the line at pre-1970 or, as I mentioned earlier, pre-code. And then the early vintage plastic pipe, which I'll talk about, basically it's a pre-1983. And again, this comes from some of the documents that were talked about during Nicole's testimony. And then post 1982. And then also as part of the program, we would look to replace basically all associated fittings with that and then also the inside meter sits that are tied to it.

In a little more detail on the early vintage steel pipe, what we're looking at is the higher-risk pipe as identified by a couple of different factors. Number one factor is our DIMP model. And again, what you need to realize is this DIMP model changes on a regular basis. We are required by PHMSA to review that, our program, annually. But the DIMP model can changed based on information we get from the field. We have the ability and the expectation to go into that model as we learn of new information that could affect the risk scores. And then really the other big piece to this is the subject matter expert input, and that's

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our folks in the field that truly understand what they're digging up. As I mentioned with the picture, they know what's in the ground. We bring those type of people when we adjust the model, and really what they do is they look at the data that the model itself puts out based on the risk that we assign to different threats, and they tell us whether they truly feel that that model is giving an accurate picture of our system, and then we adjust that model from there.

And then if you look at the early vintage plastic pipe, again, I had mentioned the study that we've got in place. Really what we've done is through this -- I mean, I think we've -- I testified or there's documents I know through data requests that show that in order to replace all plastic pipe that's that pre-1982 vintage, we quoted $148 million. And again what we're trying to do -- we realize from an operational standpoint, like Nicole testified, that would be a huge task if we were going to do it over a year or two. What we're trying to figure out is what is the true risk based on what we see, plus what other groups are seeing. There has been a lot of data research done, a lot of testing done on this through GTI and others, through AGA -- AGA has got a white paper. And again, they're all recommendations, there's

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nothing required in any of those. They give you more data to basically try and analyze your own system. So that's what we're hoping to do with our study.

We also will be able to determine the presence of the low-ductile inner wall characteristic. That is the potential for a certain resin that was built, or that was used to make this pipe in the early 70s, '71 and '72, that shows the potential for a characteristic of a brittle-like cracking. Basically over time there will be a crack in that pipe. We have not had that in our system to date saying that. There's nothing saying that it can't. And that's what we're trying to determine through this study is if we truly have this low-ductile inner wall characteristic with some of the pipe that we'll be digging up.

The other thing that we've been told we should be able to get from the study is to determine the remaining life expectancy of this pipe. Again, this was installed, I'm going to say, from that '71 to '83 time frame for most of our system. So it's been there a long time already. What we're hoping to get out of it is based on their expertise telling us how many years are left with that. And then obviously the results of this study, then we take that and move it into our model and we'll change and adjust our DIMP

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model itself accordingly.

So when you look at the study itself and the projects we picked, I mentioned this earlier so I'll go through it quick. But basically Eldridge is the town that's mainly 1971 pipe. Barlow is the town that we're doing that's mainly 1981 pipe. And then Cleveland has the mainly unknown vintage. Again, we're working with industry groups on the R and D, the AGA and then GTI.

Q. And Mr. Darras, can you just describe the Company's plans going beyond -- in the future beyond 2018 with respect to its SSIP program?

A. With respect to the plan as it stands with what was submitted -- and again, this is fluid -- is 2019, as it stands today, we would plan to do -- to work on Glen Ullin, which includes both steel pipe and the plastic Aldyl A pipe; the Mandan low pressure system and the Dickinson low pressure system. And then moving on to 2020 through 2022, we would continue with both the Mandan low pressure and the Dickinson low pressure system.

Q. And Mr. Darras, can you explain why early vintage steel pipe low pressure systems pose a safety risk?

A. Yeah, I will -- I guess as far as looking at low pressure itself, it -- you need to look at it as a

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system as a whole. The pipe itself, if we dig it up, like I showed in that picture, the pipe itself is probably going to be in good shape. It's the fittings that tie it together, it's the location of it. Generally what you will see in MDU's system anyway, is this is our oldest vintage pipe in the oldest areas of town which are downtown, which is a high consequence area. So, again, these are all factors when we're looking at how we prioritize projects, that's why we internally have focused on low pressure and said it's a higher risk.

There's other things that, from an operational standpoint, if you do have that leak that you had mentioned in January, this is an ounce system. If you have a pound system that's leaking, the public may or may not, but the public may be able to hear that leak, smell that leak easier underneath this ground. Low pressure, it is a slow leak that's going to migrate and eventually find someplace to come out of that ground. It may be through a crack in the snow or the ice, it may be through a crack in a foundation. And again, when we say where these are located, low pressure is located mainly in downtown areas of cities. So that's really the operational threat or the risk that is out there.

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The other piece that I just want to mention is the potential for cathodic issues. And when I say that, that's the corrosion issues on low pressure. Again, these are put together with dresser couplings, as you saw in that picture. What that does is isolate two pieces of pipe from each other. There is another potential failure that could happen with the cross-examination side of things because you've got an isolated piece of pipe. We protect it either through anodes or direct current, our systems, to basically save that pipe from corroding. So there are systems in place to protect the pipe. What you don't necessarily catch immediately is if there is a short which can be caused from some of these dresser couplings.

And then the last thing I would say is generally low pressure is larger pipe, it's large diameter pipe. Again, it's located in downtown areas for the most part. It's very cumbersome to work around. If you do have issues, you're tearing up a lot more space. A lot of it is in back alleys or streets. Obviously it's not in your boulevards like you see a lot of your plastic pipe or more current pipe today.

Q. And Mr. Darras, industry wide, is there a lot of low pressure systems in the country?

A. There is not. Again, it's unique. I would

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like to mention, I mean, a lot of the projects that are out there, we talk cast iron and we talk bare steel. We've got bare steel, I will correct Nicole on that. We've got protected bare steel, which means that we are protecting it from cross-examination. There's a difference when you put it on the 7100 report. So basically all of ours, to our knowledge is protected from corrosion. There is some bare that we tried to get rid of throughout the years. So ultimately I mean, it's -- we feel there's that threat there, and that's what we are trying to eliminate through the program.

Q. And Mr. Darras, from the operational side of Montana-Dakota's SSIP program, can you explain the benefits to customers of this program?

A. From the operational side, it's safety. Safety is truly the number one thing that I want to point out. It's an improvement. Again, is there a guarantee that we will never have an incident? No, there's not. As Mr. Armstrong mentioned earlier, MDU, as far as he knows, has operated a safe and reliable system in the past or forever. That's something we're very proud of. What I want to point out is just because we've operated a safe system in the past, our past success does not guarantee anything in the future. So we are doing -- we're implementing programs, something like this, to

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try and help us guarantee ourselves that we do not have that one incident.

Q. And finally, Mr. Darras, Advocacy Staff expert's cite the January 2017 U.S. Department of Energy report entitled Natural Gas Infrastructure Modernization Programs at Local Distribution Companies, Key Issues and Considerations.

You, do you feel this report supports the Company's SSIP proposal in this case?

A. I do feel it supports it. When you look at that, again, there's many different -- many different programs that are out there across the United States. Again, I would say some of them are -- many of them are within the very recent past is when they've been implemented. Again, when I look through that, you can go through there and you can see that there may be a company or two that's looked at low pressure. There may be a company or two that's getting recovery through Aldyl A. Again, the majority of them are cast iron. I will say that. We are fortunate that we don't have cast iron. We do have bare pipe. So to me, it supports it because we're not unique. We aren't on that list, or this isn't the first utility that's tried to come for some type of a recovery mechanism for low pressure like we're focusing on, or early vintage

steel.

The other thing it points out is I don't believe -- in my opinion, it does not clarify what early vintage truly is. There's no definition for that. We are clarifying it that we are calling it pre-1970 or pre-code. But early vintage pipe, it could be assumed that it's -- or it's cast iron, or it could be assumed that it's bare steel, but does that mean that if you don't have cast iron or bare steel in your system that your system is risk free or that you don't have early vintage? The one thing I picked up on is it says that there's systems out there that are 800 years old. I showed you a picture of a system that we did you go up last year that's 80 years old. So I think that's why it supports it because there's really no guideline on that, in my opinion, that tells you that it can only be for cast iron or only be for bare steel.

MR. SANDERSON: Thank you, Mr. Darras. Your Honor, we would offer MDU Exhibit 10, the PowerPoint slides of Mr. Darras.

THE COURT: Any objection?

MR. ARMSTRONG: No objection.

MS. JEFFCOAT-SACCO: No.

THE COURT: Mr. Coffman?

MR. COFFMAN: No objection.

THE COURT: Major?

MAJOR UNSICKER: No objection.

THE COURT: All right. Exhibit 10 will be received.

Should we take a break for lunch here?

MR. ARMSTRONG: That would be my preference.

MR. SANDERSON: Yeah.

THE COURT: All right. Can we be back in 45 minutes or so? Everybody back by 1:00 at the latest? Okay. We'll be back at 1:00.

(A break was taken at 12:08 p.m.)

THE COURT: Okay. We're ready to go back on the record here. It's a little after 1:00.

When we took the break, Mr. Darras, you were on the witness stand. You're still under oath. And I think we're going to start cross by Mr. Armstrong.

Go ahead.

MR. ARMSTRONG: Thank you.

CROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. Mr. Darras, am I right that the SSIP in general is a program of scheduled replacements of early vintage steel and plastic pipe? Is that an accurate general

statement of what it is?

A. The SSIP program that I submitted, yes, is generally to look at early vintage steel pipe and early vintage plastic pipe.

Q. And when you talk about the program you submitted, that would be Exhibit PCD-2-2-2-2-2-2 to your rebuttal testimony; is that correct?

A. Yes, that is the North Dakota plan for 2018 through 2022 which falls under the overall SSIP program.

Q. Say that again. This is the plan that falls under the program?

A. We have -- again, when we look at the SSIP, I look at it -- from my position, I look at it across MDU. This is the North Dakota plan that falls under the SSIP program.

Q. This is the part of the SSIP we're here to talk about this week?

A. Yes.

Q. Okay. And you would agree, wouldn't you, that there are other factors besides age in determining overall integrity of a natural gas system?

A. Yes, I would.

Q. And all factors must be considered when considering the safety of your customers, not just the

age of the pipe?

A. Yes.

Q. I assume you would agree that any replacement project should be reasonable and prudent?

A. Yes, I would.

Q. In the past, MDU has replaced pipe based on highest risk through either the DIMP and/or subject matter expert recommendations; is that correct?

A. No, that is not.

Q. That's not correct?

A. Highest I would not necessarily agree with.

Q. Do you have your direct testimony in front of you?

A. Yes, I do.

Q. And that was filed in July of 2017, correct?

A. Yes.

Q. And could you turn to page 24, line 7 through 9? Isn't what I just asked you exactly what you said in that testimony on line 7 through 9?

A. Yes, it is.

Q. You disagree with that now?

A. I disagree that it's -- the DIMP model includes a risk score, but it also includes the subject matter expert which can basically modify what that highest risk is.

Q. And the SSIP, again, includes subject matter experts again, correct?

A. Yes, it does.

Q. What kind of subject matter experts are we talking about?

A. When you -- and again, this changes based on people as they move into different roles. But generally it's our construction supervisor roles that are in that, it's engineering people that are in that, it's some director level. It's really the operation folks that have some type of field experience and then the engineering folks that have some of the design experience or the data research experience.

Q. So it's a slew of different areas, or a bunch of different areas?

A. Yes.

Q. So it would seem to me then that if a bunch of different experts are using or evaluating to figure out what should be included, then in order to review that you would need a bunch of different experts to review that as well, if somebody -- a third party wanted to review that; is that fair?

A. Yes, it's generally the same group that -- I mean, the input is from some experts and then the review is by a separate group.

Q. Going back to how projects were replaced in the past, the Company often did that in coordination with city or state street projects to optimize efficiency; is that correct?

A. That is correct.

Q. Okay. And you would agree that that process was effective?

A. For the cost benefit, yes, I would agree that it's effective.

Q. For the cost purpose?

A. Right, for the -- a cost efficiency, not -- I would not agree that it was the most effective way to look at a system in general.

Q. Okay. And was that because you say it was a reactive approach instead of proactive?

A. Yes.

Q. And now you want to change that process at least with regards to early vintage steel and plastic pipe through this SSIP program?

A. Want to make it more structural, formalized, yes.

Q. And accelerate recovery and replacement?

A. That piece is I think -- that's where -- the acceleration is one piece. The recovery I'm going to say that's the piece where it falls away from

operations.

Q. Okay. But you would agree with me that if you're not worried about recovery then, you could do these projects whenever -- you could do this SSIP without having the mechanism?

A. From an operational standpoint? Yes.

Q. You would just have to get the recovery later in a rate case?

A. Correct.

Q. And by doing the SSIP, it does remove some of the efficiencies -- cost efficiencies of having it tied in with replacement of street and road projects, doesn't it?

A. I think it -- yes, I would say it could. But it does not remove all. There are projects that go on that, again, when you look at the plan that was submitted with my rebuttal, it talks about one of the ways that you can change based on the highest risk and make that a higher risk and change the schedule is based on availability or state street projects, city street projects. You can move that up or back based on a proposed project.

Q. And help me out here, because that's one of the, I guess between you and me and everybody else in the room, one of the hard parts I'm having with

following this SSIP and what you say in your testimony is frankly how fluid it is. It's kind of hard to pin down exactly what it is because it keeps being changed and updated and evaluated; is that fair?

A. That is correct.

Q. Okay. And in fact, the PCD-2-2-2-2-2-2 attached to your rebuttal testimony was actually originally created in January 4th of 2018; is that correct?

A. That is correct.

Q. And then it was updated with minor grammatical changes in March of 2018? If you look at page 3 of 18 I think is the errata sheet?

A. Yes, that's correct.

Q. And that's actually nearly six months after it was requested in the Company's application for a rate increase in this case?

A. And I think -- yes, it is.

Q. So at the time you filed the rate case asking for this program, this document didn't even exist?

A. That is correct.

Q. And this document didn't even exist until after Advocacy Staff's witnesses provided their direct testimony; is that correct?

A. That, I don't know.

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Q. Was it ever -- do you know if it was ever provided to Advocacy Staff until it was provided in your rebuttal testimony?
A. I don't believe it was, no.
Q. And so have -- now I want to talk to you about the 2018 projects, okay?
A. Okay.
Q. Have those projects remained the same since the application was submitted, or has there been some change to those projects?
A. I would say overall they've remained the same. And when I say that, the towns have stayed the same.
Q. Okay.
A. Depending on what is dug up or what is found in the specific projects, we leave -- I leave those decisions to the project manager on site.
Q. Okay. But in this case -- so you're anticipating that -- what do you mean by that? I mean, could these projects become smaller?
A. They could.
Q. Could they become bigger?
A. They could.
Q. Is it still the Company's position that it's basically the 5.6 million for these 2018 projects?
A. Yes, it is.

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Q. But we really don't know whether it's going to be that or less or more?
A. We don't know. It's not going to be exactly 5.5 million. We did go out for contracts. We have signed contracts that were bid on a unit cost basis. So, again, if that footage changes based on what is found in the ground when they get there, then it could change. But, yes, the goal of the program is to do the 5.5 million.
Q. And I'll come back to some of those projects in a little bit more detail in a bit, but could you just identify for me what the 2018 projects are that we're dealing with as we sit here today? Are they what's listed in PCD-2-2-2-2-2-2?
A. Yes, they are the seven towns that are listed.
Q. And so if I'm looking at page 9 of PCD-2-2-2-2-2-2, that's got six towns on it. Okay. I see. So it would actually be page 10 of PCD-2-2-2-2-2-2 would identify the 2018 projects; is that correct?
A. A combination of 9 and 10, yep. On page 10, it's the steel, early vintage steel. And on page 9 it's your early vintage plastic, which a couple of those towns are on both pages. And I can touch on it on my --

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Q. Okay. So those are the projects --
A. -- slide.
Q. It's slide number four, correct?
A. Yeah, it shows 18 up there, but I think they're combined.
Q. I think they're duplicated.
Okay. So those are the projects we're dealing with for 2018?
A. Yes.
Q. Okay. And on page 9 of PCD-2-2-2-2-2-2, at least for the early vintage plastic pipe replacement, it indicates that a study will be performed on the projects; is that correct?
A. That's correct.
Q. Has there been a study performed on the projects proposed for 2018?
A. Has it been performed? No, it has not. It's in the works.
Q. Okay. But you've already signed the contracts, you've already agreed to go forward with them, but you haven't performed the study that's identified in the plan?
A. Correct. The study itself, I would say, is even fluid based on information that we're getting back.

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Q. I thought the study was to determine which projects to do?
A. The study is to determine whether we need to continue to do the $168 million worth of work.
Q. So how --
A. Do we need -- the study is there to help us with the future. In order to perform the study, we need to do the work that we're doing in 2018.
Q. So what helped you pick the 2018 projects then?
A. It's explained in here. Basically the initial test candidates were selected from the pre-1983 early vintage pipe category due to the higher risks that were calculated by MDU's DIMP model.
Q. So it's solely based by the DIMP then?
A. No, it's not. The SME project selection was based off the upper and lower ends of this identified range of years from '71 to '82.
Q. Okay. So it's the DIMP model plus subject matter plus age?
A. Yes.
Q. Okay. So there's no -- is there some documentation explaining how these projects were selected as a result of that?
A. We could -- I could probably get documentation. I don't know that there's specific documentation. This

is the result of several meetings that were held by the SME group and the DIMP group.

Q. And so those projects anyway are under way, those 2018 projects?

A. Yes, they are. Some of them are.

Q. But contractors have been hired for all of them?

A. Yes, they have.

Q. So I assume the contractor will have to complete one job then move on to the next one?

A. Correct.

Q. Who are the contractors?

A. I have it in one of my files. I can get that for you. Q3 is one, I know. I believe InfraSource is another one.

Q. Let me just ask you this. Are any of the contractors part of MDU Resources group other companies?

A. I don't believe so. Saying that, we do hire contractors that are part of construction services, but I don't believe any of them are from the North Dakota group.

Q. Do you know if MDU has provided the documentation to Advocacy Staff that supports the 2018 replacement projects?

A. Which type of documentation?

Q. The documentation you were just talking about that you could go get.

A. Are you -- the cost piece or are we talking prudency?

Q. Why you're doing those projects now.

A. I don't believe they have. They have access to our DIMP model, which helps -- doesn't necessarily give the authority for us to do it, but the DIMP model does kick out a risk score or risk ratio which then internally we take that risk ratio and decide how we're going to mitigate the risk.

Q. Let me ask you this. If we haven't been able to obtain those documents in this rate case, how are we going to evaluate these projects going forward under the mechanism if we can't even get the information in a rate case?

A. The information is available, and if asked, we can provide that. We did provide the most current DIMP model information for this rate case. We had pipeline safety staff in our office and we went through that. Again, the DIMP model is fluid. When we talk the fluid piece of pipeline safety, that changes, and it could change this afternoon while I'm sitting here based on some information we get back from the field. That is

open to anybody, and we did provide the specifics of the DIMP model. But the specifics of a DIMP model doesn't necessarily provide the specifics for Taylor, North Dakota.

Q. Is there an end date for this proposed SSIP mechanism?

A. There is not.

Q. This is something that if it goes into effect could last forever?

A. Not -- it could, based on risks. I guess right now what we've identified as early vintage steel pipe, early vintage plastic pipe, we do have two accelerated actions. The way they are written today in the DIMP model is that they are our performance metrics, meaning that in order for that accelerated action to go away from the DIMP model, all EVSP and EVPP needs to be removed from the system.

Q. That's, if I understood you correctly, $148 million worth of replacement?

A. In today's dollars. That's just for the -- that's just for the Aldyl A, the plastic pipe pre '83.

Q. Oh, that's just the plastic?

A. That's just the plastic pipe.

Q. So it's even more for the steel?

A. Yes, it's another I think what we quoted was

48.5 million remove all low pressure early vintage steel. That does not account for the early vintage steel of all other pressure systems that are out there. I think that helps show the magnitude of the need to start an integrity project recovery system, however we want to call it, to start removing this riskier pipe than what's put in the ground today.

Q. And all of that would be recovered on an annual basis not subject to a rate case review?

A. Right now what's proposed is to recover it through this mechanism for early vintage steel and early vintage plastic only.

MR. ARMSTRONG: That's all the questions I have. Thank you.

THE COURT: Okay. Mr. Coffman, you're next.

MR. COFFMAN: Yeah, just a couple.

CROSS-EXAMINATION

BY MR. COFFMAN:

Q. Good afternoon, Mr. Darras.

A. Good afternoon.

Q. Just following up on that last line of questions. What kind of assurances if this SSIP surcharge is approved, what assurances can you give

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AARP that the parameters will limit this program to only projects that you've described, I guess, in your rebuttal testimony?

A. I guess the way I would look at that, and I can reword it if you want, but I guess the way I would look at it is the assurance I can give you is that it will be reviewed by the Commission.

Q. And so there's nothing in your -- the proposed plan that's attached to your testimony that limits where this SSIP program may go in the future, right?

A. Other than it limits it to early vintage steel pipe and early vintage plastic pipe, meaning pre '70 steel and pre '83 plastic.

Q. Okay. And that -- is there anything in the tariff that limits this program to only those particular projects?

A. I don't know that I know that answer.

Q. Is there anything in your testimony about the way you would operationally approach main replacements that you would do differently if the Commission did not approve an SSIP mechanism? Operationally.

A. Today I would say probably not, because I'm fairly comfortable with the way the plan stands today. But that could change tomorrow based on an unfortunate incident or something. So today's plan as submitted,

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yes, it would stay the same.

Q. Okay.

MR. COFFMAN: Thank you, that's all I have.

THE COURT: Major?

MAJOR UNSICKER: No questions, sir.

THE COURT: Okay. Commissioners. Commissioner Kroshus.

EXAMINATION

BY COMMISSIONER KROSHUS:

Q. You list two towns where there were accidents, one is Allentown, Pennsylvania, that was related to old vintage steel pipe; is that correct?

A. Correct.

Q. You also list San Bruno, California. What was that related to?

A. I believe it was high pressure old vintage or older vintage. I can't remember the exact vintage on that or when that happened. Again, it was one of the ones that brought it to -- pipeline safety to the attention, I think, or to the forefront of a lot of regulations that are out there.

Q. Okay. Based on the information I read, San Bruno was a 30-inch main that was improperly installed.

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So that would not necessarily be a good example for what you're looking at here in terms of replacing old vintage pipe; is that correct? Or do you have a concern with installation techniques on some of the older infrastructure that's in place right now?

A. I think installation techniques are a -- again, is it a risk that's out there? Yes. Is the pipeline safety group trying to be more proactive in oversight of installation methods? Yes, they are. Quality control is a hot button right now in the industry, and how do you control the installation practices.

Prior to some of this, I think that's the -- that's how -- how do you truly assign a risk to a piece of pipe? How do our SMEs that I mentioned earlier today, how do they truly assign a risk on the installation practice from, say, 1930? And again, that's where I go to the picture that was on my slides. We could have dug that up and it could have been welded. In this case, it was not. It was used with couplings. Welding was a procedure back then. So that's the unknown attribute that we have there. And that's where I think if you look at a transmission side of things or the high pressure where we don't as MDU do not operate a lot of transmission, that, even though it's a risk for the industry, a higher risk because

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there's more of it out there, for MDU that's not a high -- our highest risk just because we do not have as much transmission. We do have some. And fortunately some of what we do have, we have records and we have installation practices that are there.

So that's really the balancing act the way I see it is trying to -- again, when asked the questions of does this go on forever, pipeline safety goes on forever. And does this program go on forever? What we're looking at today, we're focused on just the early vintage steel and early vintage plastic. And we call out specifically low pressure because today our SMEs feel that that is a higher risk than some of the higher pressures, say 40 pounds or 60 pounds, based on the information we currently have, what's in our database. That could change tomorrow.

And that's really where we're trying to -- when I say that it's fluid, it truly is a fluid program. The intent of the program is to begin an accelerated removal of all older vintage high risk pipe. It doesn't have to be the highest. And that's the piece where I called myself out is we may say highest, but if something showed -- if our DIMP model kicks out the highest number out of our entire system and an SME agrees with that, that that could be the highest,

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there's no regulation that tells us that we have to get that pipe out of the ground today or if we can wait ten years. And that's where when I sit in this seat, I really struggle. Is it prudent to let it sit there for ten years since it's the highest risk on our pipe, but it's less risky than a cast iron pipe in New York or Pennsylvania. If we have that incident, one incident is too many for us. Like everything we've been talking about, shareholder, everything, customers, that one incident takes all that away. And that is the burden that I feel, that the folks underneath me feel when we look at these programs.

How do we weigh everything? How do we weigh the cost? How do we weigh the customer, the shareholder and yet try to eventually get this pipe that we feel is a risk out of the system? And again, it's -- it's a true -- it's a true statement that it's not just me, it's the industry as a whole, to try and figure this out. PHMSA is not going to tell us when to remove it, the state is not going to tell us when to remove it. But they will tell us if we were wrong after the fact and that we should have been more aggressive or less aggressive. And that's truly the struggle that we feel. And like I say, this -- the program as -- from the operational side, as proposed,

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changes daily. And we, being myself and the folks that work on the operations design of these systems, truly feel that we need to start a replacement program.

Q. Okay. So on the San Bruno part, and I could be wrong, but based on what I've read, not an applicable example. Pipeline safety, yes. Proper install, yes. But it doesn't seem like it's a material issue.

A. Installation issue is -- now that you've reminded me, I have more recollection of that. But, yes, it's an installation issue. Again, I do not remember the vintage on that. I think, you know, there are -- there are systems, there are programs, there are procedures in place, for instance, the OQ Program that's out there that's been rolled out now for approximately ten years I would say. Again, that was to qualify employees to before they can work on pipe on gas systems they have to be qualified. The big push now is even though they're qualified and can pass a test to do it, is anybody checking that they truly did that right before it was pressurized and put in the system. And there's other checks, too. I mean, you have pressure checks, all systems, lines, have to be pressure tested before they are put into service. But the pressure test that's put on there for an hour or eight hours may not immediately show that defect that

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ultimately is a result of a bad weld or a bad fusion in plastic pipe. Something like that, that shows up over time.

Q. And just for those, well, in the room and listening, my observation certainly isn't to diminish what happened in Allentown where five people perished. So that was a significant -- was significant and obviously a tragedy.

How many times have you sent -- can you -- I think you answered this, but I may have been writing another note at the time. How many times have you sent pipe to a lab for testing that you've pulled from the ground? How often does that happen?

A. In the past I would say not very often. We do more on a reactive approach. So if a piece of pipe is pulled out of the ground due to an incident or a dig-in or some type of a leak, then we would. We would send it in. But, again, that was to determine what could or may have caused that individual leak. We have not had a formal program where we've send it in on a broad basis based on using sampling from areas like we plan to do with this.

Q. Okay. Would it be fair then to characterize the SSIP plan as being based more on anecdotal information from around the country rather than

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specific information that's been garnered from your system?

A. Yes, I would say that's fair today. And again, our hope is as we get more information we are able to make it more specific to our system.

Q. Okay. Is it possible then that after the 5 million, 5.5, is spent on the projects mentioned, the replacements projects, if I have the right number for that?

A. Yes.

Q. Is it possible that you may send the pipe to the lab, have it studied, have it looked at, and through visual and actual lab testing determine that this isn't as pressing as you think it is and that the rest of the money would not have to be spent? And really we're talking about timing --

A. Sure.

Q. -- of this. And you know, I'm not thinking, wow, maybe it's good for another 20 or 30 years. I think that's highly doubtful. However, at what point do we impact rate payers? And also, of course, at what -- how is that metered out so it doesn't hit all at once? So we have to balance that out. But that's why I ask the question.

A. Yeah, and I do -- as I mentioned in my slide

presentation, we do hope to get an expected remaining life expectancy. I will say that I have not been privy to those conversations, but folks that are working on this and working through the plastic study, in their initial conversations, early conversations with GTI, they say -- this is based on their research -- that the northern colder climates are better for Aldyl A. That does not necessarily mean that all of our Aldyl A is good. But the other thing that early on is what I've been told through their conversations is the life expectancy could be 30 to 50 years remaining. So, again, that's more than what you were -- you mentioned as a potential.

The caution thing I want to throw out there is, again, at the current rate that we have in that five and a half million, approximately -- and again, this is moving, but I believe we figured 800,000 of that 500 million was going towards plastic pipe. If you do the simple math on 148 million, this is 165-year project. So whether they tell us 30 or 50, we've missed the boat. If they tell us ten, we really missed the boat.

And again, that's just one example why we need to start accelerating these replacement programs. More power to us if they come back and give us 50 years. Great. That's a yahoo for us. But now we need to come

up with a program internally saying, okay, now, how much do we need to do to get it out of the ground in the next 50 years? And is there one location in Jamestown that to us is a higher risk than Walhalla? And that's really the managing part of this.

So again, it could come back that it's longer than what we expected, or it could come back shorter. We are hoping, for everybody's benefit, that they tell us it's still got 50 years left. That gives us 50 years to replace this. But there's no guarantee that they're going to do that. If it comes back with the LDIW, that raises a whole new risk for us, and we have to accelerate it.

Q. So let's say it is 50 years, you would start replacing infrastructure that still has 50 years of life left on it?

A. I think it would have to be looked at to how do you get it. Because, again, in today's world, to ultimately remove all of that pipe, we can't do it -- we can't wait 40 years and then do it the last 10. We could. But I'm -- the 168 estimate that's out there is today's dollars. So how much is that in 40 years?

So that's the -- again, that's the struggle I have. That's the struggle I believe commissions across the country have is how do you -- how do we balance

this? How do we balance it with everybody's interests? I mean, again, we could get a report saying that it's 50 years and that pipe could stay in the ground for 100. We don't know that. But it could. But if we get a report telling us 50 years, we better, as a prudent operator, have that pipe out of the ground in 50 years.

Q. And then what would the lifespan of the new infrastructure be?

A. I don't think that's proven yet. There's a lot of speculation.

Q. Please tell me more than 50 years.

A. Yeah, I mean, if Aldyl A is a high risk in the industry, and it's lasted -- and ours has been in the ground for close to that and they're saying we got a potential for 30 or 40. The newer poly pipe, it's so new and they continue to make advances on it, I think we would be wrong to even make a guess at that. It's -- it's truly an amazing -- it's truly an amazing material. Again, until we get to that, I don't think we're going to see it in our lifetime. It will be around longer than us, the stuff that's there today, in my opinion, the stuff we're putting in the ground today.

Q. I'll admit the timing just is really a challenge for me in terms of -- you know, I realize it

takes time to get through all of the existing infrastructure, but if you still have infrastructure in the ground that has 30 to 50 years of life expectancy left in it and tell consumers that they're going to start paying for that now, I would have to see more information in terms of just what type of a bottleneck are you talking about in terms of available labor, and this would have to be projected out, the state's going to change a lot between now and 30 or especially 50 years from now.

Well, one final question that I believe I indicated I would ask when you came up on the stand. The leak frequency of the old vintage pipe versus the balance of the system, is it higher or is it the same? What -- where is that at right now currently today?

A. The leak frequency on older vintage pipe is the majority -- I don't know that I can put it in a percentage -- versus newer pipe. Now, saying that, it's what type of leak? Excavation damage is ours and the industry's number one risk. So that, again, is considered a leak. So that's the one disadvantage you maybe have for a plastic pipe, today's plastic pipe, is if you hit it with a piece of equipment you're going to have a gas hazardous leak, whereas you can hit a piece of steel with that same piece of equipment and even

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though you have to repair it, it may not leak. So again, these are all factors that go into leaks.

But overall from a general perspective, our leaks -- we do not have leaks on newer systems. I can -- I can't say never, because we do have perhaps an installation piece that -- it's not necessarily a leak, it doesn't pass a pressure test or something like that, or we may have a -- and I can't -- nothing comes to mind as far as leaks on newer systems, other than excavation damages. Now saying that, it's not that it can't happen.

Q. But in terms of material integrity, which is really what appears to be what is driving SSIP?

A. Right.

Q. You don't have anything specific that you can offer in that regard?

A. Nothing specific. I mean, we have material failures, and it's not necessarily in the pipe itself. You may have fitting failures that are then sent in, or we send them into the manufacturer to see. And again, these are usually industry wide. It's not specific. It could be. We've had in the past a batch of material that comes from the manufacturer and they'll send out a recall. So, again, in today's world, it's easy -- we track that. So we know where that batch of pipe is in

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the ground relatively speaking. We don't know exactly which foot it's on, but we generally know which project it's at and which main, so we can track that and get it out of the ground if it's installed. So you do have that. But you don't -- there's nothing specific that I'm aware of today that's out there.

Q. Actually, one last thing real quick. If the $5.5 million was viewed as a pilot project, would you think -- agree that it would be prudent to do that first before making a determination on next steps and a long-term strategy, because it just seems like there's too much information missing. There's no pipe testing, there aren't any diagnostics to look at to know what the life -- remaining life span is. And that's really what is driving the SSIP program. But to me, it's not a small unknown, even though you say 30 to 50, that's a broad range.

A. I think it's -- I'd like to just explain that that's one piece of the SSIP program. The other piece is the early vintage steel pipe. So we're not planning on testing any type of a test or study for the early vintage steel pipe. We feel that we truly have the information we need -- it's getting better as we gather more information from the field.

So, for instance, pipeline inspection reports.

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Every time an operator is somewhere out in the field, if they expose that pipe, it's a requirement that they get us the information, whatever information is available, on that pipe. This is both regulatory driven, some of it is code, plus we've gone beyond that and said what other information we can gather. We take that data -- and, again, that's the pieces that can change this DIMP model daily, because then we take from our field, put it into our DIMP model, and that spits out that piece of the risk.

So again, our early vintage steel pipe, and more specifically low pressure, is where we are focused a majority of this. When I mentioned the 800,000, again, that's all that's in the 5.5 million for the plastic. And basically that's going to cover the cost of the study this year in 2018. It covers the cost of the study plus the replacement of that pipe that we will be testing, just the plastic. The other 4.7 is going towards early vintage steel pipe, which our DIMP model justifies along with our SMEs.

COMMISSIONER KROSHUS: Okay. All right. Thank you, Pat.

THE WITNESS: Yes.

THE COURT: Chairman Christmann.

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EXAMINATION

BY CHAIRMAN CHRISTMANN:

Q. New replacement distribution pipe, is it pretty much all poly now, or do you still use any amount of steel?

A. It depends on the pressure system. The majority of it of what we operate as far as a distribution system is the poly pipe.

Q. But do you still use steel?

A. We do, yes, for higher pressures.

Q. And so when we look at the guidelines that would be in place for the SSIP, the pre-1970 steel and pre-1983 plastic, how many -- roughly, how many generations of each have there been? What would be -- I'm wondering what the next category of each is, that they make, say, a type of steel then that was used from '71 until the mid-80s and then evolved it to something better?

A. Yeah, it's evolved into something better. Steel has. Plastic has come a long way recently. Like I say, I don't know -- they can continue to improve it, but it's basically the resins and the manufacturing process. Steel for the most part is steel, other than the seams on steel have changed. There's seamless pipe out there. There's the ERW, electro resistance welded

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pipe that was out there. And this is going back years where it's become obsolete in the industry and even recommended that it can't be installed today. Now saying that, is it in systems? That's the unknown piece.

The other piece I just wanted to clarify real quick is the installation practices today to install steel pipe are way higher standards than they were in the past. And when I say that, a welder that installed pipe in 1960 did not have the advantage, not to say that he wasn't a good welder or she wasn't a good welder, but the fact was they didn't have the X-ray, they didn't have the penetration tests, the things that are available and required today, quite frankly, especially on transmission to have -- to have that secondary proof. Before it was the person looked at it and said, yeah, that looks like a nice weld, right. But what you didn't know was what was happening inside. And that's the technology that is there today.

Q. There are multiple generations of improved poly pipe since 1983?

A. Yes, there is.

Q. Is each one safer than the previous one?

A. I would hope that it's making improvements each year, but I don't know that for a fact.

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Q. And what happened from 1969 to 1970? Why this cut off on the steel pipe? You said steel is kind of steel, so why are we concerned about 1969 steel pipe, but this program is not addressing 1970 and 1971 steel?

A. Right. Where we as a company decided to draw the line was what we call pre-code and code. So the code came out in 1970. And the code is when I reference that it's PHMSA's part 192, which was a regulation basically that started putting in some of these installation practices that I'm talking about that are way better than they were. I mean, it's a fact, 1969 didn't have to -- that's the grandfather clause that you maybe heard about is that if it was installed prior to code, we just -- we could assume that that pipe was okay and it didn't have to meet this newer standard. That's the piece where PHMSA right now is debating do they rid themselves of this grandfather clause. And if it truly was documented as grandfathered it's going to need to come out.

Q. Is it safe to say then especially with the poly which has multiple generations and each are hopefully safer than the previous, if you were granted enough recovery to do all of this that then there would just be something else, whatever was the next generation after 1983 is less safe than the rest of it, and so

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this would be a never-ending thing. There's always going to be some way to invest more to achieve some higher level of safety; is that correct?

A. I would agree with that. I think, again, pipeline safety to me is -- it's ongoing. There is no end to it. There's always something new coming up. So and again, it's -- you know, I said the drivers are regulations or an incident. Again, I would love to say that the plastic pipe made today is bullet proof, but if we have one incident anywhere in the country with that pipe tomorrow, there's going to be some type of an advisory bulletin that's going to come from PHMSA to the industry saying we got an issue, what are we going to do with it.

Q. Tell me -- and I lost the page, but I had your -- the photograph marked. Is this something out of a textbook, or is this one of your projects you're working on?

A. It's --

Q. The slide isn't numbered here, but . . .

A. Yeah, and actually that is a -- I don't believe -- I believe it came from one of our towns in Montana. It is our system. It is our folks' feet that you see there. So it's not out of a textbook.

Q. This might be similar to what we're seeing in

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the towns you're at, whichever ones you started work already?

A. Yes. What we do know is that that's the vintage that I called out was 1937. And that pipe, I think, I believe one piece of that picture is 1948. The dresser couplings are standard across our system, so there could be some right outside in the streets here. And again, there's different types of dressers. The pressure class could be different. That wasn't low pressure, it was a medium pressure line.

Q. So as you get to something like this in these towns now, are you boring this in, or is everything being dug up to replace it?

A. A little of both.

Q. Okay. Were you -- is the old infrastructure being removed, or can some of this be abandoned in place?

A. The majority will be abandoned in place.

Q. And so what you're removing is either just what's in the way of something else or enough to get the samplings for doing the testing; is that correct?

A. Correct, yes. As far as the early vintage plastic pipe, we're removing more of that just to do the sampling. The steel, normally is not -- it's not required by code, but there could be certain

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ordinances, cities, that require us to do that if it's in right away, then we'd have to remove it. For the most part we don't see that. But it could happen.

Q. Okay. And now I'm kind of to the point I got to skip my questions because Commissioner Kroshus has asked about the long range future and getting to it.

But in these towns where you started work already, would you be aware of a construction project that's scheduled for this fall in that town to replace a water main or something and you're going to do this now and this fall it's going to be dug back up? And if the answer is yes, what about next year or 2020?

A. The answer is yes, for some. We hope to be involved -- the larger cities, Bismarck for instance, has a planning and zoning commission that does a very good job of knowing longer term. And when I say that, two to five years, what they plan for street projects. We would plan this overall project around information we get from them. When you go to a Taylor, it's really driven by state funding, for one thing. There is a project going on in Glen Ullin this year. There was a project in New Salem last year. Again, these are things that we hope to pick up on. And in some cases we normally know. If we know soon enough, that's the SME part of what drives the proposed plan where we may

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take a Taylor, even though it was scheduled for 2019, and move it to 2022 because Taylor's told us they're going to have this large street project in 2022.

Q. Okay. So if you do this testing on this plastic when you get done with the 2018 projects and it turns out that much of this is worse than expected and very dangerous, okay, that's one thing. If it turns out that it's good for another 20 or 30 or 50 years, you had indicated it would take even longer than that at this pace to replace it all. But in any -- in any scenario where it's, say, decades out, isn't there the likelihood that some of these towns will look much different and have tracks of it that are probably uninhabited by the time you get several decades out and that most all these streets will be dug up for something or another in the next several decades? And so if we're talking about that long-term issue, isn't the solution more to wait and do things as projects are done in those communities?

A. Again, I think it -- it's both. The caution is that even though we could get a report back that tells us 30 years, okay, and then let's go 25 years down the road and now all of a sudden we're five years away, we need to do this and Taylor has a street project. What if we have an incident in two years from that point

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instead of the three years where the project was planned? Is that -- is that our bad? Is that -- should we have done something more proactive? Should we have done it 20 years from now instead of 25? And again, that's the piece I really want to get out there is that there is no exact science to this.

And what I would say is, my personal opinion is if we get that report back and it tells us there's 30 years left in Aldyl A, we will take a pause to the Aldyl A. The intent from my standpoint would be, as Nicole testified, whether we get the rider piece of this or not, we're committed to the pipeline safety piece of it. We've got 6 million is what we're proposing or what's in there, but I look at it as the 800,000 that we talked about that's in 2018 projects. From my operational standpoint, 800,000 now goes to that low pressure, and we can wrap that part of the project up quicker than we had proposed. An extra 800,000 goes a long way, it really does. And that's where we would shuffle that based on the information we get back.

Q. Well, that answer -- one of the early stages of that answer then begs me to ask one more question. So if we approve this, regarding the, well, what if something happens a couple years before it gets

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repaired, what if something happens to some 1984 era plastic and you know that there's been generations of improvements since then and we didn't even address it here today? Isn't that same question applicable for anything?

A. It is. I mean, I think we -- obviously, God forbid that we would have an incident, but if it was '84, again, the struggle we have in my role is just because it was installed in '84, is that '84 material? When was it manufactured? So maybe it still does fall under the pre '81 that we're talking. We don't know -- again, I don't know and the folks that are working on this project have no idea how much inventory we had in each one of our warehouses, for instance, in '81. You know, the code again addresses it recently that you have to keep this protected, the newer poly pipe. Back then, it wasn't that. So it could sit out in a yard for years. And when you finally got it or had wanted to install it, it was there and you used it up. You know, so, again, that's a piece of the puzzle that we have to consider.

CHAIRMAN CHRISTMANN: Okay. No other questions. Thank you.

THE COURT: Commissioner Fedorchak.

COMMISSIONER FEDORCHAK: Okay. Thanks,

Pat.

EXAMINATION

BY COMMISSIONER FEDORCHAK:

Q. Just to -- we're going to backtrack a little bit, but not too terribly much, I don't think. I just want to clarify some things for my own understanding to make sure I'm following this right.

The early vintage plastic pipe, you've got this study going on?

A. Yes.

Q. When does that study -- when do you expect the results of that study?

A. It will be later this year. Again, it's tied to the projects that are up on the board.

Q. So essentially the projects included in this -- in the base rates for this case are the study?

A. The initial -- and I think that's what's in there anyway is the -- it's the initial participants of this study. We could find that, for instance, an example would be Taylor has a higher -- or let's say a lower life expectancy than Walhalla. If that's the case, we would probably do more sampling in the Taylor, Richardton area next year. And again, that's the fluidity of this. We want to -- we want to be able to

take the data we're getting back and truly make our best decision on where we should focus future studies or future dollars spent.

Q. So I don't even see Walhalla listed here.

A. Walhalla would be in the Cleveland, Barlow, Eldridge district.

Q. Oh, okay.

A. And again, we're not going that far north with this study, but it would be in the longer term. We know there's Aldyl A in Walhalla.

Q. Okay. So is there an end point to this study, or are you just talking about this generally like you're constantly going to be looking and evaluating it? I mean, what's the end point of this study?

A. Yes, there's an end point this year. We hope to get a lot of data back. And again, what they're still working on today -- and when I say "they," it's the folks in our engineering group that are working with GTI, and they're working with AGA, is they're trying to really get GTI's information from them and their recommendations on how to do this study.

For instance, I heard the other day was that originally GTI told us in order to get an 80 percent confidence factor on their samples, they needed to do 22 samples per town. Since these are smaller towns,

they've recently told us that 22 samples needs to go up to 35.

Q. Why does the size of the town matter?

A. The size of the town, because you can't get -- what they're saying is based on length.

Q. Okay. It's got a percentage of the whole system?

A. They base it on footage, and there's not enough feet of pipe in that small town of Taylor to get what they consider an 80 percent confidence level with their sampling. So that's the changing piece. So what I could see -- the intent is to finish this study this year, but it could be driven -- it could drive us a different direction next year. We don't intend to do that, but, again, it will evolve, I think, into trying to verify what's found in the study this year.

Q. But this -- it would be -- would it or would it not be accurate to view this as the study on the EVPP?

A. Yeah. And actually if you -- the study itself is in my exhibit, the rebuttal testimony 2.5 talks about a little different. PCD-2-2-2-2-2-2, and then page 9.

So if you look at that, again, this is the study that is out there, but this is the piece that's changing. And this is where when I talk to the folks

that are working on the study itself, we still plan to do the bend-back test, we still plan to do long term hydrostatic stress-rupture tests. What we don't know is how many of those samples we will need to take to truly get an effective --

Q. I'm not finding page 9.

A. Page 9 of 18.

Q. Oh, up on top. Okay. Sorry.

A. Yeah.

Q. Okay. So now I'm with you.

Okay. So I'm sorry. Repeat yourself. I was flipping. What was your point you were going to make on that?

A. So, again, with the study, it's -- we still plan, if you look at the two black bullets there, the bend-back test and the long term hydrostatic, we still plan to do those with the study this year, but that's the changing piece to this as we're getting more information from GTI or GTI is getting more information from us. For instance, where do we operate? When do we think it was installed? If we know that, we can tell them, and then they try and determine, and that's where they're changing the number of samples needed to truly get a confidence level. They shoot for this 80 percent confidence level.

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Q. Okay. So the study is going to direct your future decisions on how and what time frame and how you prioritize the risk of this EVPP?

A. Yes.

Q. And so until you have the results of this study, can you confidently say, I mean, can you even guess what you're going to be doing next?

A. I can confidently say what we do in the next phase, the early vintage steel pipe, and those lines that fall underneath that.

Q. Okay. So can you set this aside until the study is done and start focusing on this? Why wouldn't you think that would be more prudent to just focus on the stuff you know? You've identified you're confident in the way you're approaching the steel replacement, correct?

A. Yeah, I think we could. And I mean, that's really where -- how you -- how commissions or how regulatory agencies, whoever's done this, how they've structured these replacement or these riders has always been different. I think we would be open to any of that. I would, personally. I mean, our design group I think would be, with guidance.

Again, when I look at it and you say how did you -- or we got questioned, I did, through data

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requests -- how did you determine $6 million, and then how did you determine the projects that fall under the 6 million? Again, I looked at it -- and this is me personally -- is we need to start an accelerated program. Is $6 million enough in my operations eyes? No. Okay. In order to eliminate risk in MDU's system, 6 million really doesn't get to where we need to be. Okay. It does not help me sleep well at night knowing that we're not going to have that one incident because we've got $6 million to put toward pipelines in North Dakota.

So my operational mind says we would love to have more. But we have to -- the other part of me says we know we have to take all these other considerations into account. So we can take 800,000 or we can -- the Commission could recommend that we take this 800,000 that was going to this study away, but what that does then is take what we consider a risk, which is our early vintage steel pipe and low pressure, and it drags that out longer.

Q. So the study -- the 800,000 for the study of the plastic -- no?

A. Not necessarily just the study. It's the replacement of all the pipe in those old systems. So all of our plastic pipe that is scheduled for 2018

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projects is come to roughly $800,000 including the study.

Q. Okay. Yep. All right. Well, personally, I think the study is vital. So I don't know why we would take that away. That's the baseline for getting a handle on what the needs are and how safe or not the pipe is. So the study seems like a must.

The question is the, you know, taking a leap to give you guys this new tracker to ongoing -- you know, without a plan for how that plastic is going to be replaced or what the priorities are or what we're looking at in terms of cost. So if we separate that off and focus on the steel, what's -- how much is this -- what's your -- what's the dollar figure on the steel that you're looking at? Was it 45-ish? Was that all steel or just the low pressure steel?

A. That was just low pressure steel.

Q. And are you looking at replacing all the steel? Vintage steel, I should say, not all the steel. Vintage steel? Or is that the vintage steel, the low pressure stuff?

A. The DIMP model will drive that.

Q. Okay.

A. So it could drive us there eventually. There's numerous risks that we feel are a result -- are because

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of a low pressure system that don't exist in a medium pressure system or a high pressure system with us. This is our system, this is our SMEs that look at that. So will ultimately all of the pre '70 or early vintage steel, what we're calling it, have to be replaced? I think it's too early to tell. I mean, again, regulations, new data coming in will really drive that, just like this study would drive it on our plastic pipe.

Q. Okay. So let me go to then the triggers for this. Can you just tick off again what they list them? There was a PHMSA bulletin, there's some issues on the plastic pipe. What have they said -- what have those triggers been outside the incidents? Like the official actions by PHMSA, HA, et cetera?

A. Yeah, I think -- the way I showed it in the slide anyway, it was the recent fatal incidents. It's the PHMSA IM program which was in 2011. It was the call to action that Nicole mentioned. It's, generally speaking, an aging infrastructure. And that's where I push -- I think each one of us in here knows a little bit more about aging infrastructure today, but what is truly aging infrastructure? Is it cast iron in Pennsylvania, or is it 1930s vintage steel here?

Q. Right. I guess what I'm looking for more

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specifically are the bulletin type items, not the general drivers. Like, just can you list off the -- there was a PHMSA bulletin I've seen these in various places in the testimony. I want a list.
A. Yeah, there's two bulletins from the NCSG for Aldyl A, that are specific for just Aldyl A, and they are in our documentation somewhere. One was in '98, I believe. The other one was 2001, I'm not sure, shortly after that. And then the other thing that we reference, and we're trying to get more information from, AGA's got a white paper out, it's a fairly extensive study on Aldyl A. And we're also going with some of the documentation or the data that's out there through these -- through GTI and their consortium.
Q. Is there anything on the vintage steel? Any bulletins, advisories, that type of industry practices?
A. No, not to my knowledge. Not specific to the vintage steel.
Q. Okay. So to change from your past approach, which has been more you characterize as reactive to this more proactive, do you think that the staff and interveners are appropriately recognizing this changing environment, or what are they missing? Why -- the -- you take a dramatic change from sort of business as usual to now we need to start a more deliberate

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replacement program. So -- and there's been resistance to this. So what's everybody missing?
A. I don't know that they're missing anything. I would just say it's a changing environment for pipeline safety. I don't think anybody missed anything. It's just that there wasn't even a PHMSA integrity management program required until five years ago, six years ago.
Q. Okay. And so now the Company is trying to adapt to this changing environment?
A. Right. You got a DIMP model that was not required until recently, and now this data that's in that DIMP model that drives your -- spits out where your risks are, that -- it's new data. So even though the pipe's been out there for 100 years, the data is what's driving these programs.
Q. Okay. Can you -- can the Company do anything about the fluidity of this? You've been criticized for having too much fluidity. Is any of that within your control?
A. Yes, I think it is. I mean, we can define parameters around it. You know, the question's been thrown out there how many years. I think we can define that. And again, this is from a program perspective. From an operational perspective, I'm very cautious,

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Commissioner, to say that that's not going to continue to be fluid. So what those parameters are, be it cost, be it -- it's so difficult to try and put all encompassing, I don't know, barriers around this, other than time. I mean, there could be a time consideration. I think -- and again, that's where I'm saying, we would be open -- I would be open to some of those parameter discussions anyway and then . . .
Q. Okay. Would you be able to provide a leak history to us, even if it needed to be for some reason confidential?
A. Yes, we do provide -- we provide leak history. It's out there. PHMSA 7100 reports are provided -- they're general documents. Actually they're fairly general, it's broke out by some of the threats that I saw, so it's corrosion, it's a hazardous leak versus not. So I've got all that.
Q. Does it specify the type of pipe? It must.
A. Yes.
Q. So you could quantify the leaks on the Aldyl A and vintage steel? Or don't you know where even all that vintage steel is?
A. Well, that's the unknown piece. That's the unknown parameter that I talk about, or attribute. Our system might call it out as plastic, but we don't know

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is it Aldyl A, or is it a different -- or what year was it installed. That's the new data that's coming in that we're trying to -- for instance, we dug up a piece of Aldyl A a month ago due to an unfortunate incident. The data on that piece of pipe is clear as a bell. We know what we had at that specific location. So we've got that now, and now we put that into our DIMP model and we give that to our experts. But in order to know this, we don't know if that's the same piece of pipe about a block away in Eldridge.
Q. So what could you give us to help determine -- to help quantify the -- to Commission Kroshus's points, the leak history on the vintage steel and vintage plastic? And if not, like, immediately, something that you can file?
A. And what we can give you, and I'm just verifying what's on here. Basically, we can give you the cause of the leak, which is the corrosion, natural force, excavation, for instance. We can say whether it's on mains or services. And I think we could give you more detail than what's on the 7100. Again, that's high level. That's just by the year.
Q. And is that something that your computer can just generate, doesn't require a bunch of manual entry or --

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A. Yes, we have a very -- a lot of information on leaks in our leak repair -- leak management system. So we could get into the specifics of what you're looking for and try and do our best.

Q. Okay. Is that something that you want us to put together, or do you have enough specifics on what we're looking for based on the discussion today to put together some?

A. If you can just repeat that?

Q. I think we should get it, you know -- how many years back do you go?

A. I don't have that off the top of my head. I mean, since PHMSA was --

Q. Well, we always -- in pipeline citing we always do ten years, so I don't know if that's an outrageously huge amount of data? Or five years or something?

A. It's going to be a lot. We should be able to give -- again, it's how much detail.

Q. Yeah. We're interested in the type of pipe, the -- to the extent that you have the type of pipe, the number of leaks, cost, causes. It doesn't have to be each leak, a separate line item, just summarized.

A. Okay.

Q. All right. And so then from your perspective -- actually, you already talked about that.

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So it seems to me that this kind of comes down to a judgment call on urgency. How urgent is it to develop a mechanism to -- a separate mechanism to replace your system?

A. I think the urgency is here for me. That's why we're -- that's why we've got projects in 2018. That's why we've continuously done projects going back. So the sense of urgency is here for me. The recovery of that, again, I think Nicole touched on that piece of it. The system safety piece of it, like I say, my personal opinion is the urgency is here today.

Q. So -- and the recovery piece, I guess we'll have to get more into that because I see the Company's in a bit of a box here because you can't say that you're not going to do -- keep the system safe, and you're saying you're going to keep the system safe and do what you're doing already. So why do you need the recovery mechanism then?

A. My opinion is the recovery mechanism is, again, so I'm not coming in here annually or every two years trying to explain the prudency and why the system is -- why our program is changing. Again, it's the recent --

Q. So the safety will be the same either way, it's just a matter of the Commission's tolerance for rate cases?

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A. And --

Q. Either way, you guys will operate a proactive -- you're going to operate a proactive -- because you have to and PHMSA is requiring it?

A. Yes.

Q. So it's our appetite for rate cases?

A. And cost savings associated with those rate cases.

Q. Yep. Okay I think that completes my question. Thanks, Pat.

THE COURT: Commissioner Kroshus had one more question.

EXAMINATION

BY COMMISSIONER KROSHUS:

Q. When I believe it was Commissioner Christmann was asking about the plastic varying in terms of improvements or in theory getting better with age, what were the controls back when it was first going in, in terms of keeping it out of the sunlight? Could it be stacked and left outside in the elements for a long period of time? And would that impact the long-term integrity of that pipe?

A. I don't know specifically on that. I do know that the recent -- I mean, it was just changed last

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year. Again, that's one of those regulations that changes to where it's actually they extended the period for certain types of plastic pipe where you can keep it out and it can be exposed longer than what the previous two year's regulation was.

Q. Right.

A. So to speak to it back then, I mean, I just don't know. In '71, I mean, I'm assuming, you know, that was you're talking some of that is pre-code even, so there was probably no guidance on the early, early vintage, the '69, '70 vintage.

Q. Could it potentially be an unknown variable or a small variable, large variable?

A. It probably was dependent on your inventory turnover and how quickly some locations were able to turn it over. I don't know personally that there was a requirement out there in the early, early vintage.

Q. Do you think you'll get a good cross section of how pipe may have been handled between the one, two, three, four, five, six -- the seven different towns where some was possibly handled in a better manner than other pipe that was put into the ground? I'm just -- what I'm trying to get at is how consistent will the results be if the tests are implemented?

A. The unfortunate thing at MDU is we did the east

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expansion, that all happened within a two or three-year time period. The good news is that it should have all been pretty much the same type of material. The bad news is it was Aldyl A and it was early 70s. So I think when you look and you talk if we're going to take samples from Eldridge, Barlow, you know, the eastern cities, that should pretty much all be from that same vintage, same time frame for the most part. It's when you get out to some of the western parts where it was just that was the plastic to be used or the poly to be used where you could have difference because there wasn't a large expansion going on like there was in the east.

Q. Okay. All right. Thank you.

THE COURT: Mr. Sanderson?

MR. SANDERSON: Thank you.

REDIRECT EXAMINATION

BY MR. SANDERSON:

Q. Mr. Darras, I just want to respond to Commissioner Fedorchak's request for additional data. Is that something you think we can -- you'd be able to put together in the next two days before this case is over, the leak history and study?

A. I believe so.

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Q. Okay.

MR. SANDERSON: What I would propose, Judge, is that we'll try to put that information together as quickly as possible, mark it as an exhibit, and maybe towards the end of the case on Friday, I'd recall Mr. Darras with that exhibit to introduce that.

THE COURT: Okay. Okay by me. Counsel, any objections?

MR. ARMSTRONG: No, not at this time. I mean . . .

THE COURT: Okay. It makes sense.

MR. SANDERSON: Okay.

THE COURT: Go ahead.

MR. SANDERSON: Thank you.

BY MR. SANDERSON:

Q. Now, I want to follow up and ask you some questions with respect to counsel and specifically Advocacy Staff's counsel's questions that somehow we have not -- the Company has not provided information or we've been hiding information on this. You personally received data requests from Advocacy Staff and the interveners in this case?

A. Yes.

Q. And did you respond to each and every data request that was sent to the Company?

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A. Personally, I did not.

Q. I mean, but the --

A. Through our group, yes.

Q. Yeah. You haven't hidden any data or information regarding the SSIP program?

A. No, I have not.

Q. Okay. And in fact, you were part -- I think it was commission staff came up to look at the DIMP model or go through that; is that correct?

A. Yes, they did. And I think the intent of that meeting, and it was called by us, was because of the numerous data requests that we were getting for information that we felt we could be open and show them on a monitor. We pulled up our DIMP model, we pulled up our leak management system and actually showed them to try and answer some of the specifics they were getting into. For instance, they'd ask us a risk ratio score for a piece of pipe in Taylor, can we show them that. We did our best to say that we can't -- we can do it here, but we can't do it in a data request. We can't tell you what one piece of pipe or one block of pipe's risk ratio is.

Q. And so throughout this case, you've been willing to share and provide any information requested?

A. Yes.

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Q. And as you move forward with Commission, you intend to, on behalf of the Company, continue to respond to any request for information that will be given to you or the Company?

A. Yes.

Q. Okay. Just on the DIMP model computer generation, could you just kind of take us through how long that takes to run the DIMP model that you've been discussing?

A. The most recent one, and I haven't personally done that, but what I was told is just to rerun the model, which we did in the early part of this year, with the new risk scores, just for North Dakota system took two weeks.

Q. So the computer program itself takes two weeks to run this whole model analyzing all the different factors?

A. To give us the input.

Q. Okay. I think we need to clarify some issues regarding the study and the 2018. Could you go to that slide where you have early vintage plastic pipe study project selection. And just to be clear, the 2018 projects, the roughly 5.6 million, only 800,000 of that is to replace plastic pipe, which also includes some costs to do the studies, correct?

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A. Roughly 800,000.
Q. And so that's roughly. I don't want the focus to be on this plastic, that's only 15 percent of the cost of the 2018 projects?
A. Correct.
Q. The other 85 percent of the 2018 projects is early vintage steel pipe, correct?
A. Correct.
Q. Okay. Now, you talked about the testing mechanism. And you specifically, as part of your 2018 project, identified three towns in this project, Cleveland, Barlow and Eldridge where, you know, you're expecting different vintage pipes that you want to test, correct?
A. Yes.
Q. And in your report, you talk about doing the bend-back testing, which that's kind of the brittleness of the walls, that's one part of the testing. And the other part is the long term hydrostatic stress-rupture test, and that's intended to calculate the remaining life of that pipe in those towns, correct?
A. Correct.
Q. And your plan with respect to those three in this study process is to take approximately 35 samples in each of those three towns?

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A. Yes, the way I understand it today, yes.
Q. And then submit it for those testings?
A. Correct.
Q. Now, one thing that I want to make perfectly clear is these towns weren't just pulled out of thin air. Your DIMP model -- a previous version of your DIMP model had identified Barlow, Eldridge and Cleveland as a potential risk ratio?
A. Yeah. Every town's got a risk ratio. So, again, they were identified. Were they the highest? No. Were they the lowest? No. They fell somewhere in between.
Q. And you have in your SSIP that's marked PCD-2-2-2-2-2, on page 9 and 10, you have those risk scores identified with respect to those towns, correct?
A. The risk scores identified with the most recent DIMP model.
Q. And so I just want to make it clear, I mean, these weren't -- prior to 2018, these weren't pulled out of thin air. Your models you'd been running up to that point identified these towns, and then you further identified specific areas to study as part of these projects?
A. Yes.
Q. Okay. Now, more importantly, if you could go

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to your next slide, Mr. Darras? And this -- specifically, I want to ask you questions following up on Commissioner Kroshus and Commissioner Fedorchak's questions as to plastic pipe and why now and do we have to do this. Part of your SSIP has taken the next three years' projects, correct?
A. Correct.
Q. And what is the focus of the next three or four years of the SSIP model, and what type of projects are you focusing on?
A. Early vintage steel pipe and early vintage plastic.
Q. Okay. Now, the man -- like the Mandan low pressure that you're targeting and Dickinson low pressure in 2019 and 2020 through 2022, the majority of that is the early steel -- early vintage steel low pressure pipe?
A. Correct.
Q. Okay. And there may be some components of plastic pipe that as long as you're doing the project, you'll replace those as well?
A. Yes.
Q. But the focus of the Company's SSIP moving forward in the next four years is certainly low -- early vintage steel pipe?

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A. Yes.
Q. Now, we're still -- as part of the 2018, we're still studying the early vintage plastic pipe, but those aren't the focus moving forward in the next four years?
A. Right.
Q. Now, obviously I think you made clear, Mr. Darras, if the study results from Cleveland, Barlow and Eldridge come back with somehow an alarming study, this could all change; is that what you're saying?
A. Yes, it is.
Q. Okay. But I just wanted you to make it clear that the focus moving forward with respect to the SSIP and the recovery mechanism is the steel pipe that you know has issues today and needs to get out of the ground?
A. Yes, it is.
Q. Okay. One of the things, Mr. Darras, that really was not covered in detail, but with respect to that low pressure, could you just talk about inside meters and how that also plays a safety concern with respect to those systems?
A. Sure. The low pressure -- or the inside meter sets, we have had, again, a nonformal program to remove those from our -- anywhere where we have access to the

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facility. For instance, if it's in a home and we are there for another reason, we try and get that out working through the details with the customer.

The reason we're calling it out with the low pressure is that they are tied ultimately to the low pressure system. So, again, as a piece of removing the low pressure, we will also formalize the program to remove the inside meter. And there's an array of reasons why we feel that there's a risk with the inside meter set. That is a -- again, is there -- going back to the Commissioner's question -- is there a specific requirement that all inside meter systems be removed? No, there's not. But are there cases where they've been removed in recoveries like this? Yes, they are. Specific actually in the one -- the one example that's in the exhibit.

Q. Okay. And finally, Mr. Darras, a lot of the questions you got, especially from the Commission, focused on the timing of these projects and, you know, looking at these various components. Do you believe it's prudent as the vice president of Montana-Dakota in charge of the gas operations to start the project now, or should we kick this safety issue down the road and let future generations deal with this?

A. I feel it's prudent to start the project now.

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Q. Mr. Darras, I have no further questions. Thank you?

THE COURT: Okay. Mr. Armstrong, questions for Mr. Darras?

MR. ARMSTRONG: Mr. Darras, I did not think I have any for you, except I think I do have one.

RECROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. I thought the early vintage steel was coming out of the ground was because it was pre-code; is that correct?

A. Pre-code in early vintage in our definition is what we call the same, I guess, because it's pre '70, which is pre-code and what -- where we're drawing the line.

Q. If I understood your testimony before, just a couple minutes ago, it wasn't coming out of the ground because you know it has issues and it needs to come out of the ground, it was because it was pre-code and you're not sure exactly what it is?

A. That is one variable to it.

Q. Okay. I mean, you can't go in there and say this pipe right here has issues because of its cracking or anything like that; is that correct?

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A. That it's --

Q. You can't go in there and say we know the pipe in -- well, let's just use Gladstone. You don't know that there's anything necessarily inherently wrong or unsafe with the pipe in Gladstone; is that true?

A. Again, that's a general statement. I don't know what piece of pipe. For each piece of pipe, if we're talking the town of Gladstone, most likely we've got some data on this piece of pipe and there could be one five feet away that we don't have the same data. To say a piece of pipe --

Q. It seems a little overbroad then to say you know it has issues and needs to come out of the ground?

A. And if I said I know it has issues, I guess I would -- I would assume it has issues and I would say that what we do know is what the data that we have available. What I can say is that my experience in the field, and I think if you were to bring any of those SME experts in this room, if we were to dig up that piece of pipe of a certain vintage at a T, we do know, even though we don't on paper, we know what we're going to dig up.

MR. ARMSTRONG: Thank you. No further questions.

THE COURT: Mr. Coffman?

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MR. COFFMAN: No questions, Your Honor.

THE COURT: Major?

MAJOR UNSICKER: No questions, sir.

THE COURT: Ms. Jeffcoat-Sacco.

RECROSS-EXAMINATION

BY MS. MS. JEFFCOAT-SACCO:

Q. Yeah, I just wanted to sure up this number. Is it five and a half -- well, I should start with this. If the Commission were to approve the concept of the plan and this proactive safety maintenance or replacement -- and/or replacement but not the recovery mechanism, is the number five and a half million or six million, which I heard on previous cross, or what?

A. The five and a half million is what is in the rate case that's filed.

Q. What was the 6 million discussion about then with Mr. Armstrong earlier? Or was that an oversimplification?

A. The 6 million is the proposed span for the SSIP going forward into 2019. 2019 and forward.

Q. Okay. Would the Company be willing to request legislation to create an application fee for the review of the filings if there were a recovery mechanism? Similar to someone previously referenced the electric

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recovery mechanisms for transmission and environment investment. So -- and they include a fee that the Staff and the Commission can use to process the case and do the analysis. So would MDU be willing to propose similar legislation for this purpose with a fee that was then available for reviewing the prudency of the projects?

A. I don't know if I'm the best one to speak to that. I guess my personal opinion is I don't see an issue where we wouldn't. But I think there could be others that may agree or disagree with that.

MS. JEFFCOAT-SACCO: That's all I have. Thanks.

THE COURT: Okay. Let's take ten minutes -- you have another one?

COMMISSIONER KROSHUS: I have another one.

THE COURT: Okay.

EXAMINATION

BY COMMISSIONER KROSHUS:

Q. Okay. So $800,000 on the testing for the plastic pipe, 800,000 to do the plastic, would 800,000 also be adequate to do -- evaluate the steel?

A. I would say no. And again, I want to try and -- I want to clarify the 800,000. The 800,000 is

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to remove the entire Aldyl A system in three of the towns, I believe, and then it's to take samples in some of these other towns. So, again, the study is for the removal of that pipe plus samples from this. So it's not -- even though the 800,000 is being spent, it's not just the study, it's the replacement, the capital side of the replacement, too.

So again, we're working through the details with GTI on how much this will truly cost. The early indication is that we can still do what was planned with these towns and that study can be a piece of that 800,000 is what I'm saying. And again, it's -- we know there's a study needed. But I just want to confirm that this -- if you roll it all together, it's all piece of -- a part of this study. But it's not costing us to work with this third party contractor $800,000 to do that study.

Q. Right. Right. But the same would hold true on the steel side of it as well, the 4.7 million, only a smaller part of that is the actual study?

A. And I think to study steel, I don't know where we would start to study it. And again, because when you dig up the samples, for instance, like with the picture, the steel's not the problem. It's the connections. It's the potential for the coding that's

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around that. Is there a bad coding that's causing the corrosion, potential corrosion pit. So what are you truly -- what are you sending in? If we're going to send up a piece of pipe, I feel that's not prudent, because I feel the piece of pipe itself we're not going to get anything back that's going to tell us one way or the other. It's the construction of that pipe.

Q. Okay.

THE COURT: Okay. Ten-minute break. We'll be back at ten to three. If we need to, can we go until 5:30 or 6:00 tonight?

(A break was taken at 2:40 p.m.)

THE COURT: Okay. Come to order everybody. We're going to go back on the record. We can start with two commissioners.

We're looking at about 2:54 back on the record. Mr. Sanderson, call your next witness.

MR. SANDERSON: Thank you, Your Honor. Montana-Dakota would call Travis Jacobson.

THE COURT: Mr. Jacobson, can you spell your last name for the record, please?

THE WITNESS: J-a-c-o-b-s-o-n.

THE COURT: Okay. And I'll have you raise your right hand.

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TRAVIS JACOBSON,

duly sworn, was examined and testifies as follows:

THE WITNESS: I do.

THE COURT: Thank you. Okay. Mr. Sanderson?

MR. SANDERSON: Thank you.

DIRECT EXAMINATION

BY MR. SANDERSON:

Q. Good afternoon, Mr. Jacobson. Could you please state your full name and business address for the record?

A. Travis R. Jacobson, 400 North Fourth Street in Bismarck, North Dakota.

Q. And whom are you employed by?

A. Montana-Dakota.

Q. And what is your position with the Company?

A. I'm a manager in the regulatory affairs department.

Q. And could you briefly describe what your responsibilities are in that role?

A. I work primarily on the revenue requirement and rate case type settings, as well as the PGA, the cost of gas, and the fuel clause filings.

Q. And before we get into your testimony, Mr.

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Jacobson, could you just give a brief background on your education and work experience?
A. Yes, I have a bachelor's of science in accounting, and I've work for Montana-Dakota for a little over 20 years in financial reporting as well as financial planning and more recently in the regulatory affairs department.
Q. And Mr. Jacobson, have you testified in other proceedings before state regulatory bodies?
A. Yes, I have.
Q. And you're familiar with Montana-Dakota's application for a rate increase in the present case?
A. I am.
Q. And just briefly describe your involvement with that application.
A. My work was primarily related to the development of the revenue requirement in this case.
Q. And Mr. Jacobson, did you submit pre-filed direct and rebuttal testimony in this proceeding?
A. I did.
Q. And if asked those same questions in your pre-filed testimony, would your answers remain the same?
A. Yes, they would.
Q. Okay. And Mr. Jacobson, you've also prepared

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PowerPoint slides regarding your testimony?
A. Correct.
Q. And as we move along, feel free to use those as we proceed here.
Can you briefly summarize how the Company determined its revenue requirements for the present case?
A. Yes. We started with a 2016 base year. And from that base year, we, about a year ago, developed our 2017 projections. And based on those 2017 projections, which we analyzed over 90-plus percent of the entire expense group. And of that, we went through, made any known changes, any changes in business processes or things that we're aware of. And from that, we used that as a benchmark to get to 2018, a projected test period, and that's the test period in this case.
Q. Okay. Can you briefly summarize the Company's projected revenues and expenses? For this case?
A. As you'll see on the screen, so our operating revenues, we built in growth for customers based on customer usage. And then we analyzed the O&M depreciation and all other components to get to a revenue requirement at the time we filed of just under $5.9 million.

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Subsequent to that, the tax reform in late December caused us to reevaluate that request, and I know it was brought up before, but $2.3 million was the savings projected, and that is about 40 percent less than our original request.
There was a mention of a credit metrics. And just to kind of point out in this particular slide, the income taxes plant ARAM and the non-plant, those are non-cash savings to the customer. And those are really what is driving, in part, the lower cash flow. You have to take those, gross them up, and so we collect less revenue, but we don't pay any less actual cash taxes for related to those.
Q. And Mr. Jacobson, could you briefly explain what rate base is and how the Company developed its rate base for this case?
A. Rate base just in general is the investment net of deferred taxes as well as any customer advances. And that is really the level of investment on a net basis that is shareholder contributed, and that is the piece that we try to earn a rate of return on, which is really the shareholders' reward, if you will, for their investment in Montana-Dakota.
Q. And did the Company request interim rates as part of this case?

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A. Yep. Just before we get to that, we also -- on the rate base, we also had an adjustment for the tax impact as well. And that was primarily the bonus tax depreciation. We had intended to utilize bonus tax depreciation in 2018. That's another cash piece of it. The elimination of that you can see on the screen is what we would have intended to have is $1.4 million of additional cash. And it also raises the rate base because there's lower rate, tax rate, as well as the lower bonus tax depreciation, so your deferreds which deduct your rate base.
So getting to the interim request, we did request interim at the time of filing, and we -- we implemented the 60 days afterwards in the amount of $4.6 million in September of 2017. The tax act also affected that. And so we filed that and were granted approval to reduce that by about a million nine, and that reduction then went into effect in February of 2018.
Our intent with the conclusion of this rate case would be to submit a refund plan in order to address the revenue that was collected in 2017 and '18. This will be a little bit unique in that in 2017 we are taxed at the 35 percent federal tax rate whereas in 2018 we'll be taxed at a 21 percent tax rate. So it

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will be a little bit more complicated in terms of a refund plan than what we've seen in the last gas case, for instance, should there need to be a refund.

Q. And Mr. Jacobson, there's already been a bit of testimony from other witnesses as to the issues with Staff and the interveners regarding the revenue requirement in this case. Can you briefly identify those issues in dispute for the Commission?

A. Yes. What I have on the screen now is -- I'll just say that it's based on my high-level analysis comparing the Advocacy Staff revenue requirement -- you'll see that on the bottom of 1.3 million -- reconciling from our $3.6 million. So what I did is I incorporated both the rate base and income statement effects of the two sides. The one additional piece, the nonplant excess deferred taxes, you'll see a $200,000. The issue there is really a philosophical difference between our Company proposal of ten years to amortize our excess deferreds. And our ten year was based on the life of those assets that created the deferred income tax whereas Staff recommended a shorter period primarily to reduce the rate base in a much more expedient manner.

Q. Now, Mr. Jacobson, the biggest amount in dispute between Montana-Dakota and Advocacy Staff

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involves Montana-Dakota's incentive or at-risk pay compensation. Do you agree that the Company's incentive compensation request should be reduced 60 percent as Advocacy Staff is proposing?

A. I certainly do not. The -- I know Nicole covered this a little bit, so I won't spend a lot of time. But there was a disallowance 60 percent, and this again, it's for all employees. It is just one component of our -- of our total rewards. I put a little graph on there, you know, it's a piece of the pie, if you will. There are many options. There are companies out there that have more generous benefits. There are those that have a higher base wage and less benefits. Ours happens to encompass three components.

Just as an example, you know, we've got a customer service agent which is eligible for a six percent bonus assuming we meet all of our targets. And to pull that piece out, it would need to be replaced with something in order to attract and retain those workers. In terms of is it beneficial to the customer, you know, these customer service agents get calls for all of our Montana-Dakota jurisdictions. So they need to be aware of the tariffs in each and every jurisdiction, both gas and electric in those areas we serve. I would argue it's critical that they provide

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sound and quality customer service. And a few things that they can do to control O&M, they can be very well versed in our tariffs and able to answer those questions and get on to the next customer. That reduces the number of agents we need. And, you know, alternatively, servicemen in our local communities, a lot of these guys are not only on the job, but off the job very involved in their communities, and that level of customer service does not go unnoticed.

One of the issues that I have with the adjustment of the 60 percent disallowance, there was an associated payroll tax adjustment, and as the salaries climbed, the percentage of payroll tax decreases. So that adjustment is overstated as well.

Q. Now, I want to move on to the next area. The Advocacy Staff request that the Commission reject all of the proposed cost for the 2018 main projects that Mr. Darras explained. Do you agree that those should be removed from the 2018 case?

A. I do not. And I think Pat talked about it, Nicole talked about it. These are projects that are currently under way. They've all been contracted for. And in some cases, the dirt is actually moving on those. $5.6 million is what is the level of those projects. And, you know, in 2017 in our list of

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capital additions, we didn't classify some of the replacement projects as SSIP. For instance, in Richardton, we did Richardton last year. There was some street work on 13th Street in Bismarck, we timed our replacement program with that. Those are both in 2017 revenue requirement, and there has never been an issue with those given they're similar projects.

One of the things, the reason that we were a little bit more deliberate in 2018 on our capital additions list is as a part of the mechanism, we had indicated we would propose to true up the actual spend of 2017. You know, Pat had mentioned that some of these projects are coming in a little bit less. If we don't spend those dollars, through that mechanism we have proposed to true up those. And hence on our capital additions list, we wanted to make sure that we could go back to those numbers and determine the revenue requirement associated.

Q. The next issue I want to talk to you about, Mr. Jacobson, is Advocacy Staff is also challenging the Company's proposal to include a portion of inflation on its operating expenses. Can you explain that inflation -- or the inflation included by the Company in its application and why it is appropriate in this case?

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A. As I mentioned, we filed the case a year ago, and in that case we analyzed 2017 information to the extent possible. And then for 2017 to get to our projected, and again it's a projected period, we used an inflation factor in several categories. For instance, subcontract labor, we went in and we analyzed the information that we had for 2017, and based on our analysis, we didn't see there was any reason to move those up. There were some subcontract labor costs that had gone away in 2017. We were seeing that. So we only adjusted 2018.

Many of these, you know, materials, for instance, there's thousands of individual purchases of small items for our crews to do their work. We didn't include any kind of an inflation for 2017 on that one either. We did in 2018. It's consistent with all of the rate cases that I've been involved in, and it is a -- it's a practice that's been accepted. We used an adjustment based on the average of six published indexes. And they all had a very tight range, which gives us confidence that it's -- it makes sense, it's what is expected. And again, we're on a projected test period and to get those dollars out that far, it's a reasonable estimate and, again, consistent with past practice.

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Q. Mr. Jacobson, another issue that's in dispute in this case was the Company's inclusion of vehicle and work expense. Could you just explain the dispute and Advocacy Staff's disagreement with our proposal?

A. Yes. In our initial capital budget, Montana-Dakota had included -- and I don't have the numbers right in front of me -- a level of vehicles for replacement as well as work equipment. Through the data request process, we were asked questions about the vehicles and we reanalyzed what our budget dollars were, and we did refine those numbers. So in general, the adjustment by Advocacy Staff was a reduction to our vehicle and work expense. And in general, I don't disagree with the adjustment, except for there were some categories where the level of our vehicle and equipment capital additions increased, but they didn't take -- they only took the decreases. So there's six categories, they picked four of them that decreased. And the two that increased they didn't take.

I'll -- associated with that, they recommended a decrease in depreciation. Our practice long standing, we've not changed any kind of practice, what we do for vehicles and work to more appropriately tie in the use of that cost of the use of the vehicle to

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the type of work they're doing, we put all of the depreciation as well as tires, fuel, oil changes, et cetera, on those vehicles into a clearing account and come up with a per-unit charge. So for 25 cents a mile whenever a serviceman is going -- if he's going out to read a meter, fix a service, change a meter, they record all that, and then that follows the expense.

So we recorded a decrease in depreciation of 38,000. We didn't have it in depreciation. So it's an error. There's also an additional adjustment to O&M. And while I don't necessarily agree with the method of the adjustment, I'm not terribly opposed to the amount of the adjustment.

Q. The next issue I want to address with you, Mr. Jacobson, is the dispute over Montana-Dakota's inclusion of future source charges related to the Company airplane. Can you explain those costs and why they are appropriate in this rate case?

A. Yes. As many of you are aware, Montana-Dakota has access to an airplane. And we record a certain amount of that on our books and records. We've had the aircraft for decades. And for the purposes of this case, we didn't request to add any additional capital. The expenses were trued up to what we anticipate they are for our expense.

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You know, the customers in North Dakota pay for -- they do not pay for trips if we take the plane to South Dakota, for instance. So they're charged the appropriate amount. If there's training, which was brought up, then they would maybe pay a portion of that.

So with the -- the recommendation was to remove all of the expense and the rate base from our request. However, there was no consideration for alternative travel. If we take a company plane, generally speaking, Nicole's reviewing those, it has to be beneficial from a cost perspective. There's a few other items that are also important that may not fall into that. One of them is if we go on a trip, Bismarck is not the best place to get in and out of if you're going on air. So oftentimes there's additional travel costs, meals, lodging, et cetera, in addition to the commercial airfare prices.

The -- one issue that I have in removal of the rate base, the investment was taken out. However, the associated accumulated reserve was not taken out nor were deferred taxes. Those happened to be both rate base deducts. So in sum, the adjustment is certainly overstated.

The other item in the surrebuttal, there wasn't

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an agreement to a recommended adjustment, which I had indicated was doubled. In making that adjustment, the original testimony had a reduction of nearly 13,000. The surrebuttal had an increase of 13,000. So even with the errors that have been identified, the adjustment for the rate base -- or for the aircraft is $110,000.

Q. Mr. Jacobson, the next issue I'd like you to address is Staff is also seeking a disallowance of losses on certain manufactured home in the Bakken. Can you refresh the Commission's recollection on why Montana-Dakota had manufactured homes and why they're appropriate to include in this case?

A. Yes. We had to have employees. And our biggest barrier in the Bakken period was lack of housing. We actually had folks that came up, interviewed, accepted the job, got here, and found out they couldn't get housing or certainly they couldn't get housing. If it was available, it wasn't affordable based on our salaries. We did a number of different incentives, if you will, to try to get employees. The fact is the housing wasn't available. We used housing from the initial period when it was placed in service until the housing became available.

We also at that same time in the same region,

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we had two office buildings that we sold and realized significant gains on those office buildings. We put those gains in our rate base as well and amortizing them back to the customer. Ironically, those weren't pulled out. But these housing units, we are recovering those in our electric jurisdiction right now, and they're the same housing units. We had a lot of folks that were servicemen for gas and electric, and we're recovering it, it's the same units, in our electric rates today.

Q. Now, the next issue I'd like you to address, Mr. Jacobson, is this Advocacy Staff's seeking a disallowance of the Company's advertising expense and Company dues. Can you explain to the Commission what those costs are and why they're appropriate in this case?

A. Right. We belong to a number of -- a number of industry groups, and each of those we pay a membership fee. One of the bigger ones is the AGA, American Gas Association. They have, you know, obviously a lot of national pull.

We also -- I listed kind of the three biggest ones that were excluded -- recommended for exclusion by Advocacy Staff. Consortium for Energy Efficiency, Energy Solution, both are proactive groups regarding

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conservation. And conservation is, you know, something obviously we talk a lot about. We don't have a formal conservation program in North Dakota, but we do believe those are good groups to belong to.

Utility Solid Waste Activities Group, they help us with a lot of environmental issues. PCBs on the gas system, I guess is one of the bigger areas where they're -- and they're very knowledgeable.

A couple of the others were chamber of commerce. One of them was the Cavalier Chamber of Commerce, for instance, disallowance of $160. Ironically, the line above that is Carrington, but there was no disallowance of that one. Each of the membership dues hat we had, it was listed and provided.

On the advertising side, you know, I guess right off the top, we removed all of the promotional advertising. And, you know, any charitable donations and those type of situations, those are all recorded below the line and were never included in the case. This -- the way we requested this, it's very consistent with what we've done in the past in both electric and gas cases, and we provided a list of the types of charges as well as each individual charge. And, you know, those are the main categories. Call Before you Dig and the kid's safety certainly are the lion's share

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of those as well as the telephone directories. And it was a recommendation to remove 50 percent of each and every adjustment -- or each and every advertising expense that we had, including Call Before you Dig.

Q. Now, Mr. Jacobson, I want to move to the Company's revenue requirements supporting the SSIP program, and that's rate 94. Could you describe that?

A. Yes. So included as an exhibit to my testimony, I had included a revenue requirement analysis very similar to what we did on the transmission. We had a couple of transmission projects that we included, Little Muddy and the Kenmare line. Very similar. We put in our asset, any deferred taxes, depreciation, return on that, interest costs, et cetera. At this point, there is no -- we would have the tariff with a zero rate. So it would not show up on the bill. We talked a little bit about the time line. Our intention would be to file in March of 2019 for the projects that would be done in that year with the anticipation to request rates in October. The dates of those are not necessarily inconsequential in March. Generally we've got a lot of the bids back, we're getting ready to send out the contract acceptance. And as you know, the season starts later, and by October most of those projects would be getting

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ready to be placed in service. We generally don't put a lot of them in service early in the year. So it's good timing on that.

I mentioned that the 2018, we identify those separately in our capital additions list so that we could true up that spend in 2018 on the go-forward basis each year we would file, the following year we would true those up to the actual expenses.

Q. Mr. Jacobson, on this SSIP funding mechanism, a question was asked of Mr. Darras, and I believe he said he wouldn't be the appropriate witness regarding a filing fee. Would the Company, Montana-Dakota, support a filing fee to address the concerns by Staff to allow them to investigate and ferret out the issues with the SSIP programs?

A. I think the answer to that is yes, we would. Currently in our other -- we have an environmental generation renewable and transmission, there are filing fees associated, and we'd be open to including a filing fee if there was a request to do that of a set amount within the tariff itself.

Q. The other issue, there was a question raised during cross-examination to Ms. Kivitso of, you know, if an SSIP recovery mechanism was implemented, how could other savings be recognized or investment? How

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would you respond to that question?

A. Yeah, I believe that was Mr. Coffman that mentioned that. So there's a lot of things that change between rate cases. I think everybody would agree to that. The one thing that doesn't change, each and every year, Montana-Dakota provides a -- an annual report, and our earnings are shown in that annual report. If there are savings that are significant enough to move those returns above the allowed return, certainly the Commission has the authority to investigate that.

Q. And finally, Mr. Jacobson, I want to ask briefly, as part of the application, the Company's proposed a change to rate 88, cost of gas and rate 99, cost of propane. Could you just briefly explain those changes?

A. Yes. Each month we prepare based on most recent estimates by the 8th of each month we submit our PGA, our cost of gas filing. And our current tariff, which was established really not all that long ago, moving from an annual tariff to a monthly tariff, was set at 10 cents. At that time, we didn't really have a good magnitude of what would constitute a significant change. What we would request is to move that from 10 cents to 25.

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What we expect to avoid is it will be a little more transparent for the customer if they have fewer rate changes. Certainly the rate changes and they end up with more lines on their bill. We expect the number of filings to reduce by about 50 percent, and it would be a little bit -- it would save both an administrative burden on our end as well as cost.

Q. And with respect to that rate 88, the customer would pay the same amount, correct?

A. Correct. So the mechanism continues the same as it is today in terms of we would still file. Any difference is deferred no different than it is today. The customer will pay that same amount.

Q. Mr. Jacobson, I have no further questions at this time.

MR. SANDERSON: But we would offer MDU Exhibit 13, the PowerPoint slides of Mr. Jacobson used in his direct.

THE COURT: Any objection.

MR. ARMSTRONG: No objection.

THE COURT: Mr. Coffman?

MR. COFFMAN: No objection.

MAJOR UNSICKER: No objection.

MS. JEFFCOAT-SACCO: No objection.

THE COURT: It is received. Mr.

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Armstrong.

CROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. Mr. Jacobson, could you keep your slides right out in front of you, please?

A. Yes.

Q. I want to touch on a few things in there right away. And that's slide number five, if you could put it up on the screen?

A. Got it.

Q. So at the bottom of that slide -- and we'll go through some of these items in a little bit. But at the bottom of that slide, you have -- that's 1,329,000 PFC Staff Position, correct?

A. Correct.

Q. And where do you come up with that number?

A. The 1,329,000?

Q. Yeah.

A. From the surrebuttal testimony.

Q. I thought Mugrace's testimony was 867,000?

A. The 867 does not account for the reduction in revenue. So what we're interested here today is what the impact to the customer is, so the amount that needs to be collected from customers. If you would look at

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his exhibit, the top line is a million three. There's an additional revenue adjustment.
Q. And what's that adjustment for?
A. That is related to the aircraft.
Q. Thank you. I just want to make sure we're talking apples to apples.
A. Okay.
Q. So you talked a bit about the incentive compensation reduction recommended by Staff?
A. Correct.
Q. And you're aware that Staff hasn't said you're playing your employees too much, correct?
A. If you remove 60 percent of the incentive, that would reduce the revenue requirement.
Q. How much of the incentive compensation is being paid by shareholders, is being recommended to be paid by shareholders, or be borne by shareholders?
A. You know, I think Ms. Kivitso talked about that. The overall is -- the investment is the shareholders and the expenses are essentially paid by the customers.
Q. So would that be the shareholders are being asked to pay zero dollars?
A. The shareholder invests money to earn a return on it.

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Q. And the incentive compensation is at least partially designed to increase earnings, correct?
A. I believe Ms. Kivitso said that there was a part of the incentive that was tied to earnings.
Q. Okay. And who do those earnings go to?
A. The shareholder receives the earnings.
Q. And -- but the rate payer pays for the incentive associated with earning the shareholder more -- or making more earnings for the shareholder under what's proposed?
A. Can you repeat that?
Q. Yeah. You're not asking the shareholder to bear any of the incentive compensation based on paying for the additional earnings made to the shareholder?
A. So again, if I go back to a revenue requirements model, it's I have a rate base, and what we do is we figure out what's the return, what are the earnings that are needed on that. I add expenses to that to come up with my total revenue requirement.
Q. I understand you might disagree with the concept. But in your rate case, you're not asking the shareholder to bear any of those expenses, correct?
A. To the extent that earnings are higher than what our target is, 100 percent of that would be borne by the shareholder.

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Q. 100 percent of the incentive compensation?
A. 100 percent of the increase over our target.
Q. 100 percent of the earnings would be borne by the shareholder? I don't understand what you mean by that.
A. 100 percent of the expense associated with -- so if our target was X and we earn over that, so that incentive piece goes higher than target, all of that is borne by the shareholder.
Q. Back up a second here. The incentive compensation, correct, there is -- well, basically there's two different tiers of incentive compensation, one for the executives and one for everybody below the executives; is that fair?
A. I think that's reasonable.
Q. And you heard Ms. Kivitso testify that her, along with the executive team, are partially -- one of their criteria is additional earnings for the Company, correct?
A. Correct.
Q. And none of that is being paid by the shareholder. None of that incentive compensation is being paid by the shareholder under your requested rate increase?
A. If they earn the return on the rate base that's

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established in this case, the expense for that would be recovered from the customer.
Q. And then for the other employees, it's customer satisfaction and then operation and maintenance expense goals, correct?
A. Correct.
Q. And if the operation and maintenance expense goals are met, that means there's additional earnings, correct?
A. It would mean -- if you met them exactly, there would be no additional earnings.
Q. Right. But that's what the incentive is for is to come in less, correct?
A. Correct.
Q. So if you come in less, that means there's additional earnings, correct?
A. Correct.
Q. Moving on to the private aircraft. Has the Company produced any evidence in this case of what the commercial aircraft would cost versus a private aircraft?
A. We have provided any and all information surrounding the plane that we were requested.
Q. Okay. So have you provided any information on what the commercial flights would cost?

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A. I'm not aware that we have established a specific comparison between when a company plane was flown versus a commercial aircraft at that same time.
Q. And you know that's one of the issues we raised in our testimony, correct?
A. I -- yes, in reading the surrebuttal, I did see that.
Q. And even with that, we still don't have that information being presented as evidence today, correct?
A. Well, again, what we did is we included the plane.
Q. Just that it exists?
A. The plane? It's -- yeah, it's out there.
Q. No, the comparison between what it costs to fly your employees private versus flying them commercially.
A. I assume someone could do that. I have not --
Q. I assume if every time it's used there's a comparison that's cheaper, somehow there should be something that shows that somewhere.
A. There is an analysis done at the time of the flight. I would say it's probably -- and Ms. Kivitso would be a better one to ask exactly how that works. I'm not sure that we have a transaction history of comparing all the documents.
Q. Wouldn't that be part of trying to make sure

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you're reaching the lowest cost?
A. Maintaining the documents? I would argue that if you were to just do a quick analysis, you would know the answer to that.
Q. I thought -- well, I guess I'll save that for argument.
So then with the aircraft, I know Ms. Kivitso testified earlier about call center flights. You recall that testimony?
A. I do.
Q. And you filed surrebuttal -- or rebuttal on that issue, and I notice you did not list call center flights. Is there a reason for that?
A. No. I just -- it was not something I thought of at that particular point in time.
Q. The things you mentioned were debt and equity analyst meetings?
A. Correct.
Q. And board of director meetings?
A. Correct.
Q. Which board of director meetings would those be?
A. It would be the MDU Resources board of directors.
Q. And where are those meetings held?

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A. I guess they've been in different areas. I'm not sure exactly where they're held each year.
Q. And those -- so the -- as I understand your testimony, you're asking the rate payer to pay for private aircraft to fly to debt and equity analyst meetings and board of director meeting, correct?
A. Those are two instances, yes.
Q. Correct me if I'm wrong, but those sound like shareholder -- more shareholder issues than rate payer issues to me.
A. I would disagree. And so just probably an easy example is based on those analyst meetings, they talked about credit metrics, about credit ratings. Maintaining a strong credit rating certainly is a positive for our customers.
Q. Positive for your shareholders too, correct?
A. It is, absolutely.
Q. But you're asking for all those costs to be borne by the customer?
A. We're doing those for the customer, yes.
Q. Okay. Moving now to inflation. I understand you used a 2018 test year, correct?
A. That's correct.
Q. Would you agree with me that we're almost halfway through 2018?

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A. We'd be close.
Q. Okay. Thank you. Would you agree with me that once we're well into the test year, we should try to identify the known and measurable cost increases versus using an estimate and passing along on every item?
A. To the extent that we had that information available, we did do some of that prior to our rebuttal.
Q. You would agree with me that Mr. Mugrace has accepted those cost increases where they have been identified and are known and measurable, correct?
A. I would agree with that.
Q. The ones he's still contesting are what are just based on a straight across the board 2.2 percent increase, whether they've actually occurred or not?
A. That's correct.
Q. Moving on now to the housing. Am I correct that's in the Watford City area?
A. Watford City, Williston, Dickinson.
Q. Could you turn to your slide on there, it's slide 12? I guess starting off, how much is the loss on this housing that you're asking rate payers to be responsible for?
A. Just under $800,000.
Q. Is it 774,000?

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A. That sounds correct.
Q. And so you're asking the rate payers to be responsible for that entire loss, correct?
A. Correct.
Q. And these were manufactured houses the Company bought during the boom?
A. We bought those during 2011, '10, '11, through 2014.
Q. And part of that was the market caused the housing prices to go up in the area, correct?
A. There wasn't housing available, so that's why we bought them.
Q. Based on the housing market? Being a lack of a market I guess would be more accurate.
A. We needed employees. So one of the things that we saw was the employees that we had could go work in the oil field and make a whole lot more money. We had significant turnover. We had to have something to house those individuals.
Q. Okay. And then you sold them when?
A. '15, '16.
Q. So you owned them for roughly three to four years?
A. Round numbers.
Q. And then lost $774,000 on those sales?

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A. That's correct.
Q. And you talk in your slide here about the gain on the sale of buildings. What buildings were sold?
A. So there was an office in Williston and an office in Watford City.
Q. What were those offices used for?
A. They were the district offices, I believe.
Q. And do you still have district offices in Watford City and Williston?
A. We do.
Q. So those were sold so that Montana-Dakota could move into new facilities?
A. That's correct.
Q. And those buildings had been part of what customers were paying for, for years, correct?
A. They were.
Q. I mean, before 2012, the customers weren't paying for housing, were they?
A. Say that again.
Q. The buildings you had in Watford City and Williston are the types of buildings the Company has used to maintain and have a business in those areas for years and years?
A. Yes.
Q. The Company has not historically paid for

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housing?
A. And typically on those gains on the sales though, those would go below the line.
Q. Okay.
A. And we chose not to because it was in -- they were significant gains and that's why they were included as a reduction for the customer.
Q. And those were buildings the customer had paid for though, correct?
A. Yes. And prior to the Bakken, there wasn't a necessary -- a necessity to have housing for employees. They were able to find their own housing, as they are now.
Q. In your rebuttal -- I'm moving on to advertising now.
In your rebuttal, you indicated that the advertising expenses were necessary to retain a strong community focus and attract business; is that correct?
A. I don't have it in front of me, but that sounds correct.
Q. And that's something you're asking the customer to pay for, those advertising expenses?
A. Yes.
Q. And why does it -- why does community -- let me ask you this. Does having a strong community focus and

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attracting business also benefit the shareholder?
A. It does.
Q. And yet it's all being passed along to the customer?
A. Again, it's in the customer's locations and so on and so forth. It's a cost of doing business.
Q. So if you attract more business, does that necessarily mean every customer's bill goes down?
A. I guess when -- if we were to grow our system and grow businesses, it would certainly reduce the need for any changes in revenue from existing customers. So it has the potential to increase the revenue therefore reducing the amount borne by the customers.
Q. You would agree with me that if you get an additional customer, that doesn't mean the neighbor next door's bill goes down by some level; is that correct?
A. Probably not the next day it wouldn't.
Q. But the Company earnings go up?
A. Potentially. Depends on the customer.
Q. Well, you make money on most of your customers, don't you?
A. We try to.
Q. Now, with respect to the nonplant and its amortization, you've got that amortized over ten years,

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correct?

A. That's correct.

Q. And that allows the Company to receive a return by whatever rate is authorized over those ten years, correct?

A. On the amount that would be included in rate base, I would agree.

Q. And then if that's amortized sooner, the customer still pays back that amount quicker, but the return is less; is that correct?

A. I agree.

MR. ARMSTRONG: No further questions. Thank you.

THE COURT: Mr. Coffman.

MR. COFFMAN: No questions.

THE COURT: Major?

MAJOR UNSICKER: No questions, sir.

THE COURT: Illona?

MS. JEFFCOAT-SACCO: No questions.

THE COURT: Okay. Commissioners. Commissioner Kroshus?

COMMISSIONER KROSHUS: Only a few questions.

EXAMINATION

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BY COMMISSIONER KROSHUS:

Q. In the board meetings are there ever any invited guests that attend those? Potential?

A. I'm not sure. I don't know the answer to that.

Q. On the housing part, did that help drive savings in other areas? I mean, I know that's difficult to quantify because hotel rates were extremely high if you had to put someone up in a hotel room. But overall -- and I know this is very general -- did it help the bottom line by having the housing during that time period available?

A. I'm not sure I would say it helped the bottom line. I do know that there was a facility where some of our folks who went to, you know, the Williston and Watford City, where they were able to use one of the housing units almost like a bunk house, if you will, because the hotels were expensive. But I guess I'm not aware of -- there may possibly be savings that I'm not aware of.

Q. Would expenses have been higher without that, the housing?

A. Well, I think the alternative -- I mean, we had to have people, right. So you could have trucked them in from Bismarck or something. Certainly that would have been more expensive. So the option to not have

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housing was -- would have been logistical issue for us to get the folks that were needed to do the job.

Q. Would it be fair to say that it was not an ideal situation, but it was the lesser of the two evils?

A. I would agree with that entirely.

Q. Okay. On the incentive compensation, you had mentioned targets which I'm assuming would be some percentage that you expect to pay which would not be the entire amount that might be expensed through the year, but then there is a rollback or an adjustment at the end. I don't know how -- I can only relate to my own experience in terms of when that dropped back but then accruals were made along the way.

Without getting into specifics of the plan, how much does that vary from year to year?

A. A couple years ago it was zero. And we have paid out over plan. I guess I'm not sure I know the exact percentage over plan. But it does vary somewhat.

Q. When you say you paid out zero, zero in terms of incentives earned?

A. Correct.

Q. Okay. And then other years have been potentially paid out in a greater amount than -- so it varies greatly, or it can vary greatly?

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A. It can.

Q. Okay. And I have to ask this part. On the -- part of the advertising is for Call Before you Dig, 811?

A. Correct.

Q. What percent?

A. When I look at the Call Before you Dig and the kids safety, just the combination of those two I believe is well over 50 percent of all of our advertising.

Q. Okay. The Call Before you Dig conceivably saves the Company money because you don't have line strikes or you're not trying to chase someone down to pay for hitting a line?

A. It is. It's an awareness for everyone.

Q. Is there -- is the pay -- the pay plan for the utility division consistent with MDU Resources as a whole? Or is it completely different?

A. The -- like, setting the base wages and benefits and such?

Q. Well, what I'm getting at is being competitive in terms of being able to find and attract talent. And I understand the consequences of not having a competitive pay plan. And I think it's been alluded to several times that trying to retain employees. Good

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talent is hard to find. So would you say that the pay plan for the utility division is, generally speaking, similar to if you work for another part of MDU Resources? And I realize the jobs are different, but -- or is it, no, totally different?

A. You know, Jim maybe can expand. So each of the types of employees, an accountant may be very similar if you work at the utility versus resources. You know, it's -- they're very similar type duties. Obviously a lineman on the Montana-Dakota side would -- there wouldn't be a commensurate position at MDU Resources. So each of the positions is analyzed based on the duties. So I think there are some similarities. But I certainly think there are some difference as well.

Q. Same benefits? Same 401k plan?

A. Generally I think the benefits are similar. I do think there are some difference as well.

Q. Okay. I don't have any other questions. I've taken note of the testimony from a number of contributors, and I think it's pretty straightforward outside of making the difficult decision of what to do with each item that's been identified as a discrepancy or a difference of opinion. But I don't have any other questions. Thank you.

THE COURT: Chairman Christmann.

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EXAMINATION

BY CHAIRMAN CHRISTMANN:

Q. My page numbers never match with what's up there, but the reconciliation page. Almost tied for the biggest difference is the ROE. And it almost hasn't been discussed by you. Was that because someone else is --

A. Yes, we have Dr. Gaske. And I built my revenue requirement based on his recommendation.

Q. That's what I figured. Just clarifying a few things so I don't go back later regretting that I didn't ask them.

On vehicles and work equipment, work equipment is like backhoes and trenchers and things like that, I presume?

A. Correct.

Q. Okay. And on the industry dues and advertising, you told Commissioner Kroshus that the Call Before you Dig -- he asked about Call Before you Dig, and then you lumped it in with the kids safety program and said, I can't remember whether it was 40 or 50 percent of the advertising cost, right?

A. Correct.

Q. And how -- what -- on the previous page,

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advertising and industry dues were 74,000, but I don't know when you say that it's 40 or 50 percent of the advertising costs, I don't know if advertising is half of that total or is much more or much less than industry dues?

A. Of the recommended disallowance?

Q. Of the --

A. That --

Q. Right. The reconciliation shows 74,000 for advertising and dues. How much of that is advertising? How much is dues?

A. I believe dues is about 7,000. And the remainder would be advertising.

Q. So mostly advertising?

A. Yes.

Q. And 40 or 50 percent of that is 811 and kids safety?

A. Correct.

CHAIRMAN CHRISTMANN: Okay. No other questions. Thank you.

THE COURT: Commissioner Fedorchak.

EXAMINATION

BY COMMISSIONER FEDORCHAK:

Q. Thank you, Travis. Who pays for the cost of

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the -- what do you guys call it, the at-risk pay for MDU Resources employees?

A. Montana-Dakota receives an allocation of MDU Resources costs, certain costs from there. So --

Q. No, I mean when -- when employees of MDU Resources receive their at-risk pay, who pays for that? I mean, I'm sure you get a share of whatever, but who else pays for that?

A. The shareholder would for any of the nonregulated business.

Q. So why don't the shareholders share the share in the cost of the pay -- the at-risk pay that is targeted toward improving earnings on the utility side?

A. And I guess maybe I'll reclarify my prior comment, the shareholder. To the extent that there's an incentive on a Knife River business, the customer is going to end up paying that. The customer pays 100 percent of their revenue and bears 100 percent of their cost. It's their margin is what the shareholder gets. So if there's an incentive for a nonregulated business, I would argue that the customer pays for that.

Q. So on the utilities side, why doesn't the shareholder share in the cost of at least -- I'm not saying do 100 percent, but we've established that the primary goal for the at-risk pay is reducing O&M which

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increases earnings, and then just increasing earnings in general for the executive team. Why is it not appropriate for shareholders to share in some of the costs of the money that is used to incentivize employees to make them more money?

A. Here's the way I look at it. If I'm an investor and I want to go in and invest in a utility and they -- I expect that they're going to earn a 10 percent return. That 10 percent return is the return on the investment of that -- that the shareholder has made, and it covers all of the expenses. If I take and carve out a portion of expenses and say I can earn 10 percent except for these pieces, I'm not going to earn 10 percent on my investment.

So I guess a couple ways to look at it, you either have to start looking at I'm going to invest in a utility that's going to earn nine percent, their authorized is nine and a half, so I know they're going to be stuck with $500,000 of incentive or other types of costs that they can't recover. But if I'm going in, and Dr. Gaske will talk, the ten percent is the right to attract investors, then every dollar that I don't recover, then -- it doesn't -- it lowers the return; therefore you're not earning your allowed return.

Q. Do -- I mean, it's not a guaranteed return,

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it's an authorized return?

A. It's an authorized return, correct.

Q. And so the investors understand that, that it's not guaranteed, it's authorized?

A. I would agree.

Q. And could not the Company have more wiggle room to earn -- I mean, if you took off a portion of the costs for the pay increase put -- took it off the bottom line, you could still earn more and make -- allow them to meet your 9.5 percent return?

A. But what would you earn it on? You know, we have a regulated business, we don't change rates --

Q. Sometimes do you earn more than your allowed earnings? Sometimes do you earn more?

A. There have been years that we have earned --

Q. And how does that happen then?

A. Generally -- so if you go into the early Bakken, customer growth happened really quickly until such time as our transmission facilities were tapped out, our mains and services were no longer able to deliver the pressure to our customers, we needed to expand. So there are times when that can happen, but it's more outside factors. Montana-Dakota I think strives day in and day out to be the most efficient with our costs. We make prudent investments when

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they're needed and raise rates only when the alternative is that we're significantly under earning.

Q. All right. You mentioned that the profits from the sale of some facilities in the past have gone below the line. So to shareholders, correct? That's what below the line is?

A. Correct.

Q. So has that been kind of norm when there's a profit? A gain on a profit sold, that gain typically goes to the shareholders?

A. So for -- typically for buildings, if there's a gain or a loss, that goes below the line. Others, you know, for -- gas mains, if they're not fully depreciated, it comes -- it just remains in compliant, that's the -- but typically a building, the gain on a sale of a building, would go below the line for typical accounting in our Montana-Dakota service charge.

Q. And you said the loss too. So in this case the loss -- you put the gain and the loss -- you put them both to customers?

A. Correct.

Q. Did you do that because you wanted to do the gain? You wanted to give the gain to the customers, so you had to do the loss too? Or why didn't the gain and the loss both go to the shareholder this time?

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A. We actually had the gain a couple years prior to the loss. So that was put in, in -- as a good-faith measure because we were seeing our rate base increase, you know, there was a lot of things happening. And they were significant. They were significant.

Q. Okay. And so is the loss more or less than the gain?

A. The loss is a little bit more. Or is more, I would say.

Q. Okay. So how come in this case the loss didn't go to the shareholders? We'll leave the gain, you know, that's already been taken care of. So why did you decide to have the loss be covered by customers in this case?

A. And so in our electric -- most recent electric case, we did the same. This is the exact same treatment that we have proposed in this case to what we currently have on the electric side.

Q. Okay.

A. Again, it was a -- we didn't do this but for lack of other options. And we recognize it's significant. And it was the -- really the only option we had at the time was to get these and to get the employees -- they were 1 00 percent to serve our customers. And again, it's consistent with what we're

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doing on the electric side. And the -- in fact, they're the same units.

Q. Yep. I get all that. And I do understand the situation that was occurring out there at those times. I have family members in Williston. So it was crazy.

But I guess if the policy in the past has been for gains and losses to be borne by the shareholders, why did you change? Is there something, some reason why this case should be covered by the customers?

A. And I guess I would just say, you know, the significance of it, the reason behind it was it was very short term in nature and the significance of it. And it was an -- it was our -- it was really our option to serve customers. So we did it 100 percent to serve customers.

Q. Okay. All right. And then my last question, I think, were you -- do you have thoughts on the recovery mechanism, the tracker, versus rate case that you want to add to the mix on the SSIP? Anything that hasn't been covered already?

A. There's not much that hasn't been.

Q. Okay. I agree. We did talk at length about that.

A. You know, I think our experience with the trackers that we currently have. You know, the

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electric we have four different ones in environmental. You know, similar to the pipeline replacement, it's very specific to environmental projects that qualify in certain ways. We have a transmission tracker. We did include transmission assets. Again, we proposed them, we brought them in. We certainly haven't heard negative comments about them. And so it's a method that has -- I guess, I feel has proven itself in North Dakota.

Q. Do you have ideas for ways -- or could you see working on some tools to provide more clarity and certainty to that process?

A. Yeah. We certainly would. I think Pat, you know, mentioned that we would have the projects -- you know, I mentioned the timing of that. You know, in March generally what we've done is we went out for bids and gotten some feedback, maybe even have awarded contracts by that time. So with that, you know, we would see the feet of pipe that they're expecting to include, the cost, that the whole bid process would be available for those. So in terms of the setting the revenue requirement on that, we certainly feel very comfortable that we would have all the information necessary to satisfy the customer.

Q. And you mentioned that there were some errors

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in the calculations of some of Staff's adjustments. Do you have a document that corrects those errors?

A. I've just pointed out the errors themselves.

Q. Uh-huh.

A. I think my slide deck, and there's an appendix to it that does have some additional --

Q. But not by dollar amounts?

A. On the vehicles and work, I would argue that the 38,000 is truly an error.

Q. Okay. It seems like there was a couple others that you mentioned being off, like --

A. On the vehicles and work, the -- you know, we did provide a refinement, and I actually have --

Q. Okay. As long as it's someplace.

A. It's in the appendix to my testimony.

Q. All right. I think that's it, Travis. Thank you.

THE COURT: Okay. Counsel, Mr. Sanderson?

MR. SANDERSON: Thank you, Your Honor.

REDIRECT EXAMINATION

BY MR. SANDERSON:

Q. Mr. Jacobson, I just want to follow up and try to clarify a couple of the issues. And I want to start with the incentive compensation piece that you were

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asked questions on. And one of the things you said is that a shareholder can end up paying for the incentive compensation if the incentive compensation is above the target. Can you just explain by what you meant by that and give an example of how that may occur?

A. So in this case, what we did is we determined what the average incentive compensation target is. So if there are earnings, we had mentioned if you reduce O&M increases its earnings, let's say that's the only thing, rather than 100 percent payout of the target, it went to 102 percent. That affects earnings as well. And that two percent then would be -- that the customer would not be responsible for any of that.

Q. And you also mentioned that in the last three years there was a year that Montana-Dakota did not pay any incentive compensation?

A. That's correct.

Q. Okay. And that would be a situation where the customers were not -- rate payers would not be paying those expenses?

A. That's correct.

Q. Okay. Can you just talk about -- a lot of these questions are directed at somehow trying to pit the shareholder against the rate payer. In this total rewards package, the Company needs to be competitive

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and the shareholder pays, it may improve earnings, but doesn't that also benefit the rate payer? Can you just expand on that?

A. Absolutely. To the extent Montana-Dakota is a strong company, has earnings that are strong, there -- it reduces the need for future rate changes, rate increases. And the customer will always benefit from a strong company. And I think we've talked about that before. And I think it was brought up in a different setting where the power lines southeast of town went down, and at that time Montana-Dakota had the financial ability to go in and put those up. It happened to be in the winter. And those customers were concerned about getting electricity, not necessarily about the cost of that -- of their bill at that particular point in time.

So a strong company and strong earnings are a benefit to the customer as well.

Q. I next want to just touch on the housing situation that was felt. And did you say the housing at issue was purchased in 2010, 2011 all in the Bakken region?

A. That's correct.

Q. And I believe you said these are not -- not only similar to the electric case, but the exact same

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housing units that the Company is treating in this case as it did in its last electric case?

A. That's absolutely correct.

Q. Okay. And the accounting treatment in this case would be consistent -- the accounting treatment to the North Dakota Natural Gas customers in this case would be completely consistent with what was being done and how they -- the North Dakota Electric customers were treated with respect to the same housing units?

A. That's correct.

Q. Okay. Now, let's go back to 2010, 2011, that time frame. And I -- Commissioner Kroshus mentioned this was a difficult time. But going back to that, it was a situation where Montana-Dakota's management determined that it was necessary to purchase these housing units to provide safe and -- to provide a safe and reliable system that benefited customers?

A. That's true.

Q. And certainly from your experience and the research you did in preparing this, was Montana-Dakota the only company that was faced with this housing crunch and put into this situation?

A. No. You know, a lot of the cities couldn't get teachers because they didn't have the housing. There were several cities that went out and actually

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purchased housing on their own behalf for employees for the same reasons we did.

Q. Now, finally, Mr. Jacobson, I want to touch on this little piece of inflation, the 2.2 percent that Advocacy Staff is taking issue with in this case. This is applied only to a small group of expenses that was done for purposes of calculating a future rate year when at the time filed were not known and measurable?

A. That's correct.

Q. Okay. And in fact, through data and other things, like insurance or health insurance or benefits or large expenses, you -- that we knew, we used the actual numbers; is that correct?

A. Yes.

Q. Now, you talked about these -- some of these are, you know, expenses or equipment or the day-to-day tools that are -- thousands of employees are using?

A. That's correct.

Q. And so to go true this up actually, it would just be tens of thousands of documents to try to come up with an actual number on this?

A. It would be a process that would be similar to what we undertook in order to file the case initially.

Q. Now, you were asked, well, we're halfway through the year, you know, we should be able to know.

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Have you looked at what the expenses compared to inflation on some of these issues are and how they compare to the 2.2 percent that the Company has asked for?

A. So we have looked at our actual results, and they came in very -- very close to what our projected 2017 numbers were. And, you know, we are seeing our expense trends are reasonably in line with our projections.

Q. Okay. And again, this is -- the 2.2 percent was an average of six nationally published organizations on projecting inflation?

A. That's correct.

Q. Mr. Jacobson, I have no further questions. Thank you.

THE COURT: Mr. Armstrong, recross?

MR. ARMSTRONG: Thank you.

RECROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. So as I understand your testimony, it's just easier to pass the cost along to the customer than to figure out what it actually is for the inflation?

A. Say that one more time.

Q. You just said it would take too much work to

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figure out what it actually is so you're just going to apply the 2.2 percent to the customer.
A. And again, at the time we built the case we didn't have the benefit of the actual expenses. And we are very consistent with 2017. We do feel our projections still hold.
Q. But even though you could verify it, you haven't done that?
A. We have not verified.
Q. And so let me ask you a couple questions to clarify. If I understood you correctly, you said normally a sale for a profit on a building would be passed through to the shareholders; is that correct?
A. It goes below the line, correct.
Q. Okay. But in this case, you're saying you're passing that building along -- the gain on those buildings along to the rate payers?
A. Correct. It was included as a deduction to the rate payers in an amortization over time.
Q. And actually, you want to pass the housing loss on to the rate payers as well?
A. That's correct.
Q. And the housing loss is more than the gain on the buildings you're talking about, correct?
A. That's correct.

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Q. How much more?
A. And we've been amortizing the gain for a while, so I don't have that in front of me. So 350,000 versus 750 or 774.
Q. So the gain was --
A. A little bit more than double.
Q. Yeah, so --
A. Again, so if you go back in time, the decision for the gain on the sale of the buildings was made well in advance of any housing decisions.
Q. You could probably predict you were going to lose money on those houses, correct?
A. I didn't predict it. I had no idea of knowing.
Q. How many manufactured houses were there?
A. Right off the top of my head, I don't have an exact number. There were about 50.
Q. And I assume you had to buy them at a premium?
A. I'm not sure what the purchase price was compared to what they would have been absent. I don't know.
Q. But we do know they ended up selling for -- and it's actually not the total was wasn't even 774,000, that's just the amount you're putting for the guess in this case, correct?
A. That's correct.

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Q. How much was the amount in the electric case?
A. It would have been a little bit more than 50 percent.
Q. Okay. So we're really talking about a loss of a million and a half?
A. Potentially.
Q. And then the gain would also be a little bit more than half, correct?
A. I'm not sure the allocation of the gain. I assume it would be similar.
Q. Okay. So we're not just talking 350,000, because you said now with the electric settlement, you've also passed those costs along to the customers in the electric part, correct?
A. The loss on the sale of the manufactured homes?
Q. Yes.
A. It's being recovered currently through the electric.
Q. And you talked about that as part of a settlement, and I apologize, but I wasn't able to pull up the settlement quickly. But the settlement in the electric case was actually a black-box settlement, right?
A. It was not part of a settlement. We filed for that. And I guess I'm not sure I would say that there was anything in the settlement.

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Q. Right. Was there anything in the Commission order about the houses?
A. Our initial filing included the treatment of it, and it certainly would have been available for anyone to look at.
Q. Okay. And that's case number PU-16-666, correct?
A. I would agree.
Q. And you filed for this recovery for the houses in that case as well, correct?
A. Recovery, yes.
Q. And we reached a settlement before hearing in that case, correct?
A. There was a settlement in that case.
Q. And you agree with me, the settlement did not discuss the houses?
A. I think I -- that is correct.
Q. Okay. And you agree with me the Commission's order didn't discuss the houses?
A. I don't remember seeing it.
Q. It just happens to be the Company's applied it since the order?
A. That, I would disagree with.
MR. ARMSTRONG: Okay. That's all the

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questions I have.

THE COURT: Okay. Mr. Coffman.

MR. COFFMAN: Mr. Armstrong just asked my questions. I'm good. No questions.

THE COURT: Okay. Major.

MAJOR UNSICKER: No questions, sir.

THE COURT: Okay. Ms. Jeffcoat-Sacco.

MS. JEFFCOAT-SACCO: One question.

RECROSS-EXAMINATION

BY MS. JEFFCOAT-SACCO:

Q. Where is it written that the gain on the sale of an asset bought and paid for by shareholders goes below the line? Where is that precedent? Because it sort of sounds backwards to me. But I'm open to looking it up if you tell me where to look.

A. I'll be honest, I don't know the answer. The accounting treatment would be to, I believe, FERC accounts 42.10 and 11. I'm sorry, 42.11 and 12, which happen to be below the line. FERC accounts.

Q. What were the numbers?

A. 42.11 and 42.12.

Q. Are you familiar with any of the North Dakota cases litigating gains on sales of utility assets?

A. No, I'm not.

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Q. Okay. That's all I have. Thanks.

THE COURT: Okay. Let's call your next witness.

MR. SANDERSON: Thank you. At this time Montana-Dakota would call Matthew Shoemake.

THE COURT: Mr. Shoemaker, would you spell your first and last name for the record?

THE WITNESS: Yes, sir. M-a-t-t-h-e-w, S-h-o-e-m-a-k-e. There's no r.

THE COURT: Oh, okay. Shoemake.

THE WITNESS: Yes, sir.

THE COURT: Okay. Raise your right hand, please.

MATTHEW SHOEMAKE,

duly sworn, was examined and testifies as follows:

THE WITNESS: Yes, sir.

THE COURT: Okay. Thank you. Mr. Sanderson.

DIRECT EXAMINATION

BY MR. SANDERSON:

Q. Good afternoon, Mr. Shoemake. Could you please state your full name and business address for the

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record?

A. Yes, sir. Matthew Shoemake, and I work at 400 North Fourth Street, Bismarck, North Dakota.

Q. And whom are you employed by?

A. Montana-Dakota Utilities.

Q. And what is your position with Montana-Dakota?

A. I am a regulatory analyst in the regulatory affairs department.

Q. You can -- can you briefly describe your responsibilities in that role?

A. Yes, sir. I assist in the preparation of numerous monthly filings to the Commission, the purchase gas cost adjustments, the PGA; the fuel cost adjustment, FCA; I also help prepare the weather normalized volumes for various cases and various other things for the department.

Q. And could you just provide a brief history of your educational background and work experience?

A. Yes, sir. I have a bachelor's of science degree in economics from and Texas A&M. I also have an associates degree in business administration from the college. I have been in my current capacity with MDU for two years. And before that, I was a quality control analyst for Knife River for eight years.

Q. And Mr. Shoemake, are you familiar with

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Montana-Dakota's application in this proceeding?

A. Yes, sir.

Q. And could you just briefly describe your involvement with this application?

A. Yes, sir. I helped prepare and come up with the billing determinates that were used for the normalized volumes.

Q. And in this case, did you file pre-filed direct testimony?

A. Yes, sir.

Q. And if asked the same questions as indicated in your pre-filed testimony, would your answers remain the same?

A. Yes, sir.

Q. I want to then get into your testimony. Can you briefly explain how the Company calculates its customer accounts used in this rate case?

A. Yes, sir. What the Company does is we use information from our Customer Care and Billing System, CC&B. We extract data from that, and we look at monthly customers that get billed and we bill the customer accounts based upon that.

Q. And can you also explain the Company's development of the normalized volumes used in this rate case?

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A. Yes, sir. The normalized volumes are -- they're done at a class level. So we break each customer class out and analyze them individually. The process of whether normalizing volumes is to account for abnormal weather in the year. So what we use is historical data, particularly monthly customer accounts, monthly gas volumes that get billed, and any weather. What we do at that point is we look at each individual class and determine whether a class or a customer subset is heat sensitive. If they are determined to be heat sensitive, we run a 36-month linear regression, OLS or ordinary least squares. Then we get the parameters that are output from that and then we apply those to a normal weather based on 30 years.

Q. Okay. And can you explain how interruptible and transportation class customers and volumes were determined in this case?

A. Yes, sir. The interruptible and transport customers were developed in the same manner as other classes for customers. The volumes were developed a little bit differently because the classes had such a small number of customers, we were able to look at those one by one in some cases, or we did -- we did customer classes by district. So -- and if we go back

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and say -- or if we look at a customer class or individual customer and decided they were heat sensitive, which built them into a linear regression model. If they were not, we would use a three or two-year average depending on how much data they had available.

Q. And finally Mr. Shoemake, can you explain how the projected growth rates the Company used in this case were calculated?

A. Yes, sir. We looked at customer growth over three years originally, but what we saw was there was a -- we were realizing the tail end of that Bakken boom. So there was a diminishing amount of growth. So we determined to use two percent growth rate. But we only applied the two-year average growth rate to the residential customers. All the interruptible transport customers and their volumes were left.

Q. And Mr. Shoemake, I have no further questions. Thank you.

THE COURT: Mr. Armstrong.

MR. ARMSTRONG: No questions.

THE COURT: Mr. Coffman? Not in the room. Major.

MAJOR UNSICKER: No questions, sir.

THE COURT: Illona.

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CROSS-EXAMINATION

BY MS. JEFFCOAT-SACCO:

Q. We were a little concerned with this using the two-year average, although I understand that you've got this anomaly going on with Bakken boom and bust. But everything I hear it's turned around again. Maybe you need those houses again. I just heard a news story the other night about not enough housing in Williston and not being able to ramp up fast enough.

So tell me why this two-year average, which pretty much is flat, I think, is something that we should rely on as of projections for '18 and forward.

A. Yes, ma'am. I would argue that there would probably be a little bit of a lag in the customer growth. So anything that we're -- that you've been hearing about a boom out in that area again, you probably wouldn't realize customer growth for a couple of months. That might be at the tail end of '18, something we might not realize until 2019.

So like I said before, whenever we analyze the three-year growth, that first year, there was a much larger growth. But then over time, it just completely diminished. So if we would have utilized that three-year average growth rate, it would have -- we

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would have ended up with more customers projected.

MS. JEFFCOAT-SACCO: That's all I have. Thanks.

THE COURT: Mr. Coffman, you stepped out of the room. Do you have any questions for this witness?

MR. COFFMAN: Yeah, just one.

CROSS-EXAMINATION

BY MR. COFFMAN:

Q. With the occasional booms or spurts in growth, customer growth, would that -- that type of a change in the factors, would that be taken into account in any of the SSIP surcharge increases on an annual basis?

A. I wouldn't be able to comment to that, sir.

MR. COFFMAN: All right. Thank you. That's all.

THE COURT: Okay. Questions from the commissioners. Commissioner Kroshus.

EXAMINATION

BY COMMISSIONER KROSHUS:

Q. How does the current, the projected growth rate, how would you say that compares to the rest of the country?

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A. I couldn't really comment on that. I would -- I would say that due to the nature of the area and with respect to the oil industry, I think that North Dakota might be a little bit more susceptible to any growth that we see. As has been noted throughout the day at different times, oil prices are coming back. I don't know how soon that North Dakota would realize that. And like I say, if it was realized, it would probably be later if the oil prices continued to rise or stay at the same level. But I would believe that North Dakota would probably be more susceptible than the rest of the country to that.

Q. Do you think as susceptible though, because when you look back at what happened during the last -- well, the oil boom itself when it really took off, and it was driven by a number of factors, oil prices were extremely good, but producers also had to secure lease holds. So we had a lot of drilling rigs operating in the state, and I think it was in part due to pricing and in part due to securing lease holds. But that was really a unique period of time. And now I think there's a significant amount of stability in the Bakken, significantly more, because there are more gas plants, there are more value-added components that have been put in place, there are more wells which require

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more maintenance, which is an essentially permanent job. It's not going to go away if oil prices go to 30, the well is still pumping, or producing, I should say.

So I guess I'm just wondering if the possible downturn or the Bakken factor is being overweighted because really when you compare North Dakota to the rest of the country, it's not a bad place to do business in, would you agree?

A. Yes, sir, I would agree.

Q. Okay. So I know there can be some ups and downs, but in a normalized situation I would rather live here than -- well, I'd rather live here than anywhere else, so that's why I'm here.

A. Yes, sir.

Q. Despite January.

Then one final thing. On the growth as well, you said a lot of the -- there's going to be a lag, but a lot of that infrastructure is available in subdivisions, for example, the lines have been laid. But the homes may not have been built, so you can't obviously just generate a customer because the line's going up to the curb but there's no house on the lot yet. But that, as things start to take off again, that should be an opportunity as well, don't you think?

A. Yes, sir, I do.

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COMMISSIONER KROSHUS: Okay. No other questions. Thank you.

THE COURT: Chairman Christmann.

EXAMINATION

BY CHAIRMAN CHRISTMAN:

Q. Is this your first time testifying here?

A. Yes, sir.

Q. Good job. Thank you. I have no other questions.

MR. SANDERSON: That's what we call a softball.

THE COURT: Commissioner Fedorchak.

EXAMINATION

BY COMMISSIONER FEDORCHAK:

Q. Okay. So just kind of following up with Illona, what Illona was talking about. So your customer levels are basically an average from 2014, '15 and '16. Did I get that correctly?

A. Yes, ma'am, that's correct.

Q. And the downturn really started -- I mean, those are the years where things really went flat?

A. Yes, ma'am.

Q. Haven't you already seen those turn around? I

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mean, how come you're not using 2017 and 20 -- you know, some of the more recent numbers, to have the first half of 2018 to at least check those projects?

A. Yes, ma'am. So the customer growth that we used was a very small rate, it was for residential, it was 1.4 percent growth year to year. So of the 9,000 residential customers, you're talking another couple thousand. But whenever we look at 2017 that we just finished up, the numbers are about in line with what we projected, they're not that different.

Q. Okay. All right. That's all. Thank you.

A. Thank you, ma'am.

MR. SANDERSON: Nothing further, Your Honor.

THE COURT: Mr. Armstrong.

MR. ARMSTRONG: Nothing, thank you.

THE COURT: Ms. Jeffcoat-Sacco.

MS. JEFFCOAT-SACCO: Nothing.

THE COURT: Mr. Coffman.

MR. COFFMAN: No more. Thank you.

THE COURT: Major?

MAJOR UNSICKER: Nothing, sir.

THE COURT: Okay. You may step down.

MR. SANDERSON: Montana-Dakota would call Tammy Nygard.

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THE COURT: All right. Just to be safe, Ms. Nygard, I'm going to have you spell your first and last name.

THE WITNESS: Tammy, T-a-m-m-y; Nygard, N-y-g-a-r-d.

THE COURT: Just one a?

THE WITNESS: Just one a.

THE COURT: Thank you. Raise your right hand, please.

TAMMY NYGARD,

duly sworn, was examined and testifies as follows:

THE WITNESS: I do.

THE COURT: Thank you. Mr. Sanderson?

MR. SANDERSON: Thank you.

DIRECT EXAMINATION

BY MR. SANDERSON:

Q. Good afternoon, Ms. Nygard. Could you please state your full name and business address?

A. Tammy Nygard, 400 North Fourth Street, Bismarck, North Dakota.

Q. And whom are you employed by?

A. Montana-Dakota Utilities.

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Q. And what is your position with the Company?

A. I am controller of MDU Utilities Group, which includes Montana-Dakota Utilities, Great Planes Natural Gas, Cascade Natural Gas, and Intermountain Gas.

Q. And could you briefly describe your responsibilities as controller?

A. Yes. I provide leadership and management for our accounting and financial forecasting and planning functions. This includes the analysis of reporting -- analysis and reporting of all financial transactions.

Q. And could you briefly describe your educational background and work experience?

A. Yes. I have a bachelor of science degree from the University of Mary with majors in accounting and computer information systems. I've been with the Company for over 16 years. Started at Montana-Dakota as a financial analyst and then went to Cascade Natural Gas as director of accounting and financing, and now in my current role as controller of MDU Utilities Group.

Q. And you've filed testimony in other proceedings before state regulatory bodies?

A. I have.

Q. Okay. And are you familiar with Montana-Dakota's application for natural gas rate increase in this case?

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A. Yes, I am.

Q. And could you just briefly your role in the application?

A. Yes. I am responsible for presenting Statement D, which is the capital structure and associated costs.

Q. And in this case, you filed pre-filed testimony?

A. Yes, I did.

Q. And if asked the same questions in your pre-filed testimony, would your answers remain the same?

A. Yes, they would.

Q. And can you briefly summarize the Company's capital structure?

A. Yes. The projected capital structure in this case, the ratio is about 43 percent long-term debt, 6 percent short term debt and 51 percent common equity. The average embedded cost of the long-term debt is 5.282 percent, which has dropped 67 basis points from the last North Dakota gas rate case when the percent was 5.969 percent.

Q. And Ms. Nygard, has the Company made recent changes to its capital structure?

A. Yes, it has. On April 1st of 2017 Montana-Dakota redeemed all preferred stock issued and

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outstanding. The redemption of this preferred stock reduces the administrative burden of those associated costs as well as reduces the overall cost of capital that was replaced with lower cost long-term debt.

Q. And can you just briefly explain how the Company finances its gas utility operations and determines the amount of common equity debt and preferred stock to be included in its capital structure?

A. Yes. Through our financial planning process, we determine the amount of financing required to support the cost associated with providing safe and reliable service. We target 50 percent common equity ratio. And our capital expenditure investments are financed through a mixture of internally generated funds, use of our short-term credit line, as well as issuance of debt and equity.

Q. And you indicated you sponsored Statement D of the application. Can you just briefly summarize Statement D?

A. Yes. Statement D is the average utility capital structure for the 12-month period ending December 31, 2016, as well as projected 2017 and 2018. It also shows the associated cost of debt as well as the common equity as supported by Dr. Gaske in this

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case. And those two pieces serve as the basis for the overall rate of return in this case of 7.542 percent.

Q. Ms. Nygard, I have no further questions. Thank you.

THE COURT: Mr. Armstrong.

MR. ARMSTRONG: No questions.

THE COURT: Mr. Coffman?

MR. COFFMAN: No questions.

THE COURT: Major?

MAJOR UNSICKER: No questions, sir.

THE COURT: Ms. Jeffcoat-Sacco.

MS. JEFFCOAT-SACCO: No questions.

THE COURT: Mr. Kroshus?

COMMISSIONER KROSHUS: No questions.

THE COURT: Chairman.

CHAIRMAN CHRISTMANN: I'm good as well.

THE COURT: Ms. Fedorchak.

COMMISSIONER FEDORCHAK: None for me either.

THE COURT: You got off easy.

Okay. Next witness.

MR. SANDERSON: Thank you. At this time Montana-Dakota would call Jim Kaiser.

THE COURT: Jim, please spell your last name for the record, please.

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THE WITNESS: Kaiser, K-a-i-s-e-r.

THE COURT: Okay. Raise your right hand.

JIM KAISER,

duly sworn, was examined and testifies as follows:

THE WITNESS: I do.

THE COURT: Thank you.

Mr. Sanderson.

MR. SANDERSON: Thank you.

DIRECT EXAMINATION

BY MR. SANDERSON:

Q. Mr. Kaiser, could you please state your full name and business address?

A. My name is Jim Kaiser, and my business address is 400 North Fourth Street in Bismarck.

Q. And whom are you employed by and what is your position there?

A. I'm employed by Montana-Dakota Utilities, and -- actually I'm employed by MDU Resources, but my time is devoted to Montana-Dakota as director of HR.

Q. And could you briefly describe your responsibilities as director of human resources?

A. Sure. I'm responsible for basically the human

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resources strategy, the compliance and delivery of all the HR services for Montana-Dakota. This also includes compensation programs, the benefit programs, talent acquisition, talent development, and also the retention of that talent, along with the labor and employee relations programs.

Q. And Mr. Kaiser, could you just provide a brief overview of your educational background and your work experience?

A. Sure. I have a bachelor's degree in management from the University of North Dakota. I have 36 years of human resource experience in three different regional utilities. I've been with Montana-Dakota for 16 years, and I've been in my current role as director of human resources since 2013.

Q. And are you familiar with Montana-Dakota's application in this proceeding?

A. I am.

Q. And could you briefly describe your role in the application?

A. I'm here to talk about incentive compensation. In my role, I am responsible for the compensation programs for the utility.

Q. And in the present case, did you submit pre-filed rebuttal testimony in this proceeding?

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A. I did.

Q. And if asked the same questions as indicated in your pre-filed testimony, would your answers remain the same?

A. Yes.

Q. Now, can you briefly describe the Company's -- Montana-Dakota's employee compensation system?

A. Yes. The -- Montana-Dakota has a total rewards philosophy that we outline the different components of our compensation programs that we use to compensate our employees. Those three different components are base pay, incentive compensation or the pay that's at risk, and the employee benefit programs. We participate in numerous salary surveys, we -- and analyze those results. We use outside consultants, and we help use all those resources to help us establish competitive total rewards in those three components, again, base pay, incentive compensation and benefits.

Our goal is really to be competitive in the labor market so that we can attract and that we can retain a highly skilled work force. We have a philosophy, and we've -- you've heard from others that have testified, this philosophy has been in place for 20 plus years, that we believe it's effective for the customer, it's effective for the organization to have a

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portion of an employee's targeted total cash compensation, again cash compensation is base pay and incentive comp, to have some of that at risk.

Compensation budgets are established, assuming a satisfactory employee performance. If an employee's performance doesn't meet the results, then they don't receive a portion of that compensation. Also, if the incentive plan goals are not met in customer service or in the O&M expenses, the employee loses a portion of their total compensation as well.

Q. And Mr. Kaiser, as director of the Company's human resources, do you believe Montana-Dakota's incentive plan -- employee incentive compensation plan and incentives are an appropriate part of the total employee compensation package?

A. Yes, I do. Again, we believe that having those incentive compensation programs with those metrics in place help employees be more aware and engaged in cost awareness and the overall efficient operation of our business. We believe that every employee can impact these metrics, and that's the reason why we have every employee in our organization eligible for incentive compensation.

In other words, every employee does have some pay at risk. When the goal -- when the goals are not

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met, then the customers don't have to pay that portion of the compensation plan.

Q. And can you explain how Montana-Dakota's incentive plan assists in recruiting and retaining highly qualified employees?

A. Yes. Well, we've talked about it a lot here, the challenges that we've had in the Bakken and some have referenced the fact that the Bakken, you know, that there may be some ramping up of the work force. And as recent as last week, we saw articles in the Bismarck Tribune about the challenges that employers are having in western North Dakota, and recruitment is at the forefront of some of their concerns.

Employers are looking for individuals that have experience and they have training, and that fits very well with the work force that we have at Montana-Dakota. We're a prime target if we're not going to be competitive in our total rewards strategy. I see it in my work on a regular basis. When we're making job offers, if we don't have a package that is competitive, we aren't going to be able to get that employee to come to work for us.

So in my experience in working with compensation programs, an example is some companies only have one component to their total cash

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compensation, and that's basically the base pay program. Other companies, and really in the utility industry, it's very common practice -- it's most common that employers would have the two components which are the base pay and the pay at risk or variable pay and incentive comp.

Today it's Montana-Dakota's incentive compensation programs that keeps our total rewards package in a competitive level. Without that opportunity for incentive comp, our total compensation would not be competitive, which is going to have an impact on the acceptance of job offers and, more importantly, the retention of our highly skilled work force that we have today.

Q. And Mr. Kaiser, what alternative means are available to maintain adequate compensation without the use of incentive or at-risk pay?

A. Well, as far as alternatives, we are very deliberate and we do participate in a lot of market studies, and we compare both the base pay, the total of the base pay and an incentive compensation opportunity to our competitors in the labor market. And so really, the alternative would be to add that incentive compensation to be competitive to our base wages.

Q. Do you believe that adding -- going straight to

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a base pay system without incentives is in the best interest of rate payers?

A. No, I do not, because if we would put that -- those dollars -- if we take the dollars from the incentive compensation and put those -- if we would -- if we'd move away from that, then really the alternative is to put it into base wage. And when we put that into base wage, there's an incremental cost. And I think you've heard from others testifying today, the main source of the incremental cost really comes in the form of the 401k contributions, and that would be about another half percent in incremental costs right off the bat.

Q. Now, Mr. Kaiser, what procedures does the Company utilize to ensure it is not paying more than the minimum necessary to attract and retain a qualified work force?

A. Again, we participate in many outside surveys, from reputable consulting firms. We also contract with an independent consultant. We last did this in 2013. We had a consultant come in, do a thorough review. I believe that was submitted as an exhibit. And now we're under way with another compensation study this year, we're renewing that study. So we really do a look -- a review of all those components of our total

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rewards philosophy to be sure that we are competitive in that marketplace.

Q. Now, Advocacy Staff has asserted that rate payers should not be required to pay incentive compensation costs because they don't provide any benefit to rate payers. Do you agree with Staff's assertion?

A. No, I don't agree with that.

Q. And could you explain why you believe the total rewards package or how that does benefit North Dakota rate payers?

A. Our approach to compensation is really with the total reward philosophy that we have, it's cost effective for the Company, but it's also beneficial to the rate payers, because as I said earlier, it engages our work force in those important goals. And those goals of customer service and certainly the goals of O&M costs are things that benefit our customers.

If we are not competitive in our total rewards package, we're not going to have the work force that we need to provide that reliable and safe customer service. And by having a competitive total rewards package, we retain those highly skilled technical and professional individuals that we need to have to serve our customers.

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Q. Mr. Kaiser, I have no further questions. Thank you.

THE COURT: Mr. Armstrong?

MR. ARMSTRONG: Thank you.

CROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. Mr. Kaiser, you do understand that it's not Staff's position to take out all of the incentive pay. You're aware of that, correct?

A. I'm aware that the Staff is -- has categorically said 60 percent of incentive comp would be disallowed.

Q. And can you tell me on the incentive comp what the goals are for the executive level and then for the other level?

A. Certainly. For 99 percent of our employees, the goals are customer service goals and meeting -- being in the top 35 and a select group of utilities, and that's through J.D. Powers and Associates. That's one of the metrics. And then the other metric is our O&M and coming in under our O&M goal. And again, that's 99 percent of the employees. The other --

Q. We'll get to the other.

A. Okay.

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Q. As I understand that, is that 50 percent, 50 percent?

A. It's 50 percent, 50 percent, yes.

Q. So 50 percent is customer service and 50 percent is O&M goals for 99 percent of your employees?

A. Yes.

Q. And that O&M goals relates with coming in with lower expenses than some sort of set number?

A. Yes.

Q. And then for I think you're moving on to executive level employees?

A. That's correct.

Q. Can you explain that, please?

A. So the executive level employees, and I believe Nicole referred that there are nine in the executive incentive plan. And with that executive incentive compensation plan, that is measured on 50 percent on earnings and 50 percent on ROIC. And the thought process there is that the executive team is in a position that they have the ability to control and they have the ability to drive the outcomes of the business in a much better position to do that, that's why they've got more of the financial metrics.

Q. So the ROIC and the earnings -- and I forgot what the acronym --

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A. Return on invested capital.

Q. Return on invested capital. I mean, those are all things about how the Company is performing, like its bottom line, correct?

A. That's correct.

Q. So the executive level is almost 100 percent, you know, earnings or making money type of incentive compensation?

A. Well, the earnings is 50 percent, the return on the investment --

Q. That's getting a higher return?

A. Right.

Q. Okay. And then with the 99 percent other employees, there's the 50 percent customer service and 50 percent for the O&M expense goals?

A. That's correct.

Q. Now, in your rebuttal testimony, you talked about a -- well, let me back up one second. Has it always been the Company's goal to pay market level for its employees?

A. Yes, it has.

Q. And in your rebuttal testimony, you talked about a change in the incentive plan, and I'm assuming you didn't identify executive or the other -- is there a name or the other 99 percent, or --

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A. The employee incentive plan.
Q. So that's just -- okay. So that's employee incentive, and the other one would be the executive --
A. Executive incentive plan.
Q. So in your rebuttal testimony you talked about a change in 2017 to the employee incentive plan, correct?
A. That is correct.
Q. And that change was to remove customer earnings as a portion of the regular employee incentive plan, correct?
A. That -- previously that was a metrics in the plan, and that was removed.
Q. When that was a metric in the plan, what was the breakdown between that and customer service and O&M expense goals?
A. I believe it was one-third, one-third, one-third.
Q. So now the Company -- the earnings would be more by meeting the O&M expense goal, correct? You would agree with that? The Company earnings would be more by meeting an O&M expense goal?
A. I've -- our goals are really to -- I don't agree with that. Our goals are really focused -- to focus our employees on the metrics of serving our

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customer and also to operate the utility in an efficient manner. And every employee, whether it's a service technician and how they approach their job, or the manager, has the opportunity to expend and impact the budget.
Q. Would you agree with me in general that if expenses are lower, then earnings are more?
A. It would contribute to earnings by having lower O&M.
Q. Thank you. So when you removed the Company earnings as a specified part of the employee incentive plan, did incentive compensation go down?
A. The target percentage that we --
Q. No, the overall Company incentive compensation, did it go down by removing Company earnings from the plan?
A. This -- in 2017 was the first year of our plan, and, no, it -- I need to understand your question. Would you repeat it again, please?
Q. So before 2017, you were trying to pay employees at market level, correct?
A. That's correct.
Q. And after you were trying to pay employees at market level?
A. That's correct.

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Q. And that includes whatever incentive plan they may be under, correct?
A. Umm-hmm.
Q. And before 2017, you had customer service, O&M expense goal and Company earnings, correct?
A. Yes.
Q. And you paid incentives based on that, correct?
A. Yes.
Q. And after 2017, you took out Company earnings and put a greater share on customer service and O&M expense goal?
A. That is correct.
Q. Did it change the amount of incentive compensation that was paid out? Did it lower it?
A. I can't answer that question, because there are other factors that have an impact on the -- in the way the plan is designed, what the payout percentage would be.
Q. I'm looking at the Company's work papers. Were you involved at all in preparing those?
A. I was not.
Q. Okay. And I don't know if the companies are like that, but I've got -- I guess it's the summary of O&M, and it's the first page after the summary of O&M, and it says, "for the 12 months ending in December 31,

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2016, incentive comp was $741,346. And the projected for '17 was $794,431."
Does that sound right to you what has actually occurred?
A. I -- my -- and I'm not an accountant or I didn't prepare these financial papers, but my understanding would be is that when this case was prepared, we had the history from 2016. And when the case was built, it was built on the target percentages being paid out for the incentive compensation plans, which would be a higher number because our payouts were not at target, I believe, in 2016.
Q. And as I understand it, you've said that if the shareholders are responsible for any portion of incentive compensation, then we should just convert it to base wages to be market level; is that -- am I understanding that correctly?
A. Repeat your question for me, please.
Q. I think you said something about, we have incentive plan because wages are expenses, but we could just convert it all to base wages and then we wouldn't even be having this discussion about incentives.
A. In my rebuttal testimony, I provided a response that what was the alternative to incentive compensation, and that would be to have a competitive

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total cash comp program, the only viable alternative that I saw would be to put it into base wages.

Q. And that's really the only alternative if you want rate payers to pay for it all?

A. Rate payers are -- you know, as Travis illustrated in his example, the customer are paying for the wages in a manufacturing or construction type business. In a utility business I think it's common practice that the customers would be paying the cash compensation. That's a cost of delivering the service. I think Travis also said that if our incentive compensation plans would pay out above the target, at that point in time, those things are borne by the shareholder.

Q. I guess we'll just have to rely on Mr. Jacobson's testimony for that then, huh?

Those employee compensation would be paid by the shareholder?

A. That -- yes, that's how the -- based on the case, yes.

Q. Can you identify for me anywhere in this case where you're asking the shareholder to pay for any of the compensation?

A. My understanding of how this case was prepared was that the revenue requirements were established

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based on a target incentive compensation opportunity. Anything that's paid out above target, so above what's a market competitive wage, that is 100 percent borne by the shareholder.

Q. But part of determining what a market competitive wage is, is part of that pay is to increase earnings, correct?

A. I'm talking about our compensation total reward philosophy. I think -- I'm not sure I understand your question.

Q. Let me ask this. Is the Company still paying retention bonuses?

A. Is -- we do not pay retention bonuses today.

Q. You did at some point, correct?

A. Yes. We would have paid -- in very limited circumstances we would have paid retention bonuses. I'm not sure if we called them retention bonuses, but they were to get people to take assignments in hard-to-fill locations such as Williston.

Q. You called them retention incentives, correct?

A. I'm not sure what's reflected in the case, sir. I need to see that.

Q. Anyway, as we sit here today, you're no longer having to pay any retention bonuses or incentives to any employees to keep them employed at MDU?

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A. We do not pay them today, and any retention bonuses that we paid in the past -- I'm going to back up. I think I know what you're referencing. And what we called the retention bonuses, back in -- and I think those came to an end back in 2015, basically those were our location allowances. We -- we didn't increase employees' base wages, we didn't -- some companies would call it a location allowance, I think it's commonplace still in that area. We called them a retention bonus. And those were phased out. And those were in place to cover some of the higher costs in those communities of just in living in those communities.

MR. ARMSTRONG: Thank you. I have no further questions.

THE COURT: Mr. Coffman?

CROSS-EXAMINATION

BY MR. COFFMAN:

Q. Good afternoon.

A. Good afternoon.

Q. John Coffman for AARP. I wanted to ask in your survey, are there other utilities that place safety as a criteria for incentive compensation?

A. In the past, I have seen that as a metric. And

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frankly, OSHA has really frowned upon safety as being a metric in incentive compensation plans. So we have moved away from that in the utility.

Q. Did it used to be an incentive criteria?

A. It was a metric at the utility until probably seven or eight years ago. And it was -- but we had more goals as part of the incentive plan at that point in time.

Q. What about other criteria that might be safety related for customers, say leakage rates or incidents? Has that ever been considered as a criteria for incentive comp?

A. It hasn't been brought to my attention, so I'm not aware of that being considered.

Q. Okay. Can you explain the rational for why top executives would not have a component of customer service as part of their incentive package?

A. I think it's really -- that's focused with all the other employees. I mean, I'm not responsible for all the design of the executive incentive compensation program. But I think the thought process is that going back to having a healthy business, they are focused on that they have the ability to control a lot of the outcomes in the business, and so that's -- and they're contributing to multiple lines of business.

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Q. Don't their decisions have an impact on customer service and safety and all the other criteria?
A. Certainly they would.
MR. COFFMAN: Okay. That's all I have.
THE COURT: Okay. Major?
MAJOR UNSICKER: No questions, sir.
THE COURT: Ms. Jeffcoat-Sacco.
MS. JEFFCOAT-SACCO: I have a few.

CROSS-EXAMINATION

BY MS. JEFFCOAT-SACCO:
Q. The work papers that Mitch was referring to that had the 2016 and the 2017 payouts, those are in the application filed work papers as opposed to data requests? I just want to confirm from someone here so we can look them up. Were they data request responses work papers?
A. I believe they were the work papers.
Q. Okay. We were hoping that maybe we could get one or two more years. Could we get, like, 2015 and possibly 2014? Would that be possible? The numbers?
A. That wouldn't be -- that wouldn't be something that I would provide, but I don't see a reason why we couldn't provide that information.
Q. Oh, well, whoever provided this.

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A. Right.
Q. If we could get one or two more years maybe before Friday, that would be helpful.
And then the payout in 2017, was that after the change -- like, did the change -- was the change applied for 2017 and then the payout was 50,000 more?
A. The change was applied for 2017.
Q. '17. Okay.
A. But I believe when that case -- when the revenue requirement was established, it was established based on target. We didn't know the actual results for the year.
Q. Right. I understood that.
A. Okay. I'm sorry.
Q. And then I just wanted a little more explanation since at the state we don't have incentive pay. And so when we talk about incentive, I see it as a carrot, and when we talk about at risk, I see it as a stick. Okay. So if I were to get a job offer from MDU, would the number that I am offered be that full amount that's subject to being lost if I don't make the target, or is it some lesser amount that's subject to growing if I do meet the target? Or is there some combination? Can you just explain how it works?
A. Yeah. So if you were to be offered a position

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at Montana-Dakota, your job offer would contain a base pay offer. It would contain information on what your incentive compensation eligibility is and what that target payout percentage is, along with a brochure that you would have that would go through all the employee benefits. And I can guarantee you -- again, this is an example of the mix of total rewards, different companies have different philosophies. The State of North Dakota has a fully paid medical plan, which is attractive to many. That isn't the case at the utility. That isn't the same philosophy.
Q. Not anymore anyway.
A. Right.
Q. But, okay. So the total amount that's considered incentive and/or at risk, is that -- okay. There's not like two components? I mean, there's a base pay. But as far as a motivating pay, it's one component? You -- with a chance to earn it?
A. You have the chance to earn it. You have the chance to actually earn, you know, more than that amount in some cases.
Q. Right. I was just trying to find out if there's a chance of losing some of that other number?
A. Base pay -- base pay is not at risk.
MS. JEFFCOAT-SACCO: That's all I have.

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Thank you.
THE COURT: Okay. Commissioners. Commissioner Kroshus.

EXAMINATION

BY COMMISSIONER KROSHUS:
Q. Okay. I don't want to get -- I don't want to lose sight of what we're -- well, at least what I'm really looking at, and that is are you competitive in terms of market conditions for attracting talent? Are you too generous? Because I just don't want to get -- personally, I don't want to get too far into the style of how you're compensating employees. To me it's more about market value. So with that being said, how is turnover today compared to turnover two years ago? Five years ago? And if you just have to tell me anecdotally, that's fine as well.
A. Actually, I have those numbers. As far as our turnover, numbers have improved to some extent. We're pretty much consistent with the industry norms right now, so that's a good thing. We're at about eight percent for last year was our turnover. The year prior to that was ten percent, and the year prior to that was 14 percent. So we -- we are doing much better with turnover. And that's the way we hope to keep it.

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Q. Sure. Would you attribute that to just what most businesses and entities operating in North Dakota are experiencing with less volatility out in the western part of the state?

A. There would be -- there's not just one factor that impacts it. I mean, certainly work culture affects it. Certainly total rewards would affect retention. But there's no question the Bakken slow down, you see the numbers at 14 percent, we had higher turnover at that point in time.

Q. When you say compared to industry, you're talking compared to other utilities?

A. That's correct.

Q. Okay. How about compared to just North Dakota as a whole?

A. I would be -- I would be guessing if I would -- if I would state that number. I don't know what that would be.

Q. But eight percent, that's --

A. Yeah, I'd say --

Q. It's not a bad number.

A. No, that's right.

Q. So really when I'm looking at the present and projected market requirements for compensation, how you get there I think is really -- it ties into the overall

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question of the incentive pay on what to allow, what not to allow.

A. Umm-hmm.

Q. Would you say based on the improvement that the improvement and turnover has been driven by the new plan design or just more related to market conditions?

A. That would be -- that would be a bit speculative on my part. Certainly having a good total rewards package is important, as I see when I'm making job offers to individuals or my team is. I mean, they are -- it is a competitive labor market out there. And so I want to be sure I answer your question. Is it -- is turnover lower? Repeat your question for me, please.

Q. Well, let me break it down. Would you say that it appears to be working or the jury's still out?

A. The change in plan design, I'm not sure that that impacts our ability to retain. The fact that we do offer incentive compensation is what really helps us be competitive, because if we don't -- because, again, we look at total cash compensation. And total cash has two components, the base pay and the variable pay and the pay at risk. And we do market studies, our outside consultant has looked at those things, the feedback we get is as outlined in the exhibit, we take actually a

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conservative approach to compensation.

Q. Okay. Do you go on investor calls and explain the impact or how the new comp plan, the new incentive pay -- or maybe I shouldn't call it new -- but the incentive pay model is driving results? Do you ever explain that?

A. That's not a part of my role.

Q. Not a part of your role. Okay.

No other questions for me.

THE COURT: Chairman Christmann.

EXAMINATION

BY CHAIRMAN CHRISTMANN:

Q. I think we're asking the same thing, but I'm still I'm not sure I understood your explanation to Illona. The three components are base pay, incentive pay and benefits, correct?

A. That's correct.

Q. And incentive pay and at-risk pay, is that the same thing?

A. That is the same thing, because if we don't --

Q. So if I was hired on there, the base pay I would get regardless. I'd either get terminated or I'd get that pay?

A. That's correct.

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Q. And so the at-risk pay, that really isn't a real thing, it's more of an incentive pay. If you meet certain goals, you get it, but nothing gets taken away out of your base pay?

A. Nothing gets taken away. What's at risk is because --

Q. Your bonus.

A. Your bonus, and that is part of your offer.

Q. Okay. I think Ms. Kivitso said there was something like 562 employees. If you had to estimate the total, I'm going to call it compensation, if that's the right word, the total of base pay for those 562 people, incentive pay, and benefits, about what percentage would you say is base pay and what percentage is benefits and what percentage is incentive pay?

A. This is a bit speculative, but the -- about eight -- I think it's about 8.4 percent would be incentive comp.

Q. 8.4?

A. 8.4. You have the numbers there, so we could easily calculate the percentage without that in front of me for the benefits. But I assume that's a line item that's separate from -- and then the remainder of that number would be base wages.

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Q. Okay. But --
A. Is there a line item on the work papers you're looking at?
Q. I'm not even on that page right now. But the 8.4 is plenty close, even if it's 7 or 8 or 9 or somewhere in there. Close enough for the purpose of my question, maybe not for the ultimate answer.
A. Okay.
Q. I sensed a bit of criticism from someone earlier that Staff's recommendation of only allowing 40 percent, of reducing it by 60 percent, was arbitrary. So whatever the total dollars that is budgeted to come up with that 8.4 percent, is that arbitrary? How is it determined that that was the correct amount for incentive pays?
A. I believe Travis testified to that, that that 8.4 percent is basically taking every employee that's eligible for the plan and placing their target incentive opportunity, and then calculating that off of their base wages to come up with a total amount. And so whatever that dollar amount is, divide that by the total payroll and that is your percentage.
Q. But if someone's potential incentive plan, let's say they exactly met all their goals and got a -- and maximized their incentive plan, and let's say that

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were $10,000.
A. Okay.
Q. Why not $11,000?
A. Oh, how do we establish the targets?
Q. You could do even better.
A. That's a very good question. Those targets -- really, I talked earlier about the surveys that we participate in, and most of the market studies that you do, they list a -- they list a median base pay and they list a median incentive opportunity. And that's what we're looking at, and that's how we establish the target for each of those positions.
Q. I think in some other subject matter we've heard or did I read it earlier that, regarding ROE, that MDU probably has -- is more at risk than some other gas companies it could be compared to. So wouldn't the -- because of that, the environment that you operate in, wouldn't that suggest that your incentive package might need to be different than the other companies that you participate in the surveys with?
A. When we set our establish -- I guess to answer that, I -- no, I don't think that's the case. And what's important -- again, you're trying it attract talent and retain talent. And what's important is that

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we are aware of what the labor market is paying and what's competitive, and that we're able to maintain a competitive level of compensation or offer that in our total rewards package.
So factors relating to, again, the 99 percent of the employees that are covered under the employee incentive plan, I think being market competitive is most important for those individuals. For the executives, one could argue what's important there.
Q. And I recognize that you said the 8.4 percent was an estimate.
A. Right.
Q. But let's just use that as the base, assuming that that is exactly what it is. Do you believe if it was 10.4 percent that was allowed that you would have even better performance and better retention?
A. Again, it seems a bit speculative to me because the way we're establishing, you know, we're establishing -- the way we've built this case is based on market competitive compensation. So it's market competitive base pay, it's market competitive incentive compensation, it's market competitive benefits. And our total rewards philosophy is not to be at the 75th percentile of the labor market, it is to be at the median of the market. And so that's our objective. So

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I'm not sure if the labor market is saying 8.4 is appropriate why we would -- that's not consistent with our philosophy to set it at something higher.
CHAIRMAN CHRISTMANN: Okay. No other questions. Thank you.
THE COURT: Commissioner Fedorchak.
COMMISSIONER FEDORCHAK: I don't have any questions. Thank you.
THE COURT: Counsel, any follow up?
MR. SANDERSON: Yeah, just briefly.

REDIRECT EXAMINATION
BY MR. SANDERSON:
Q. Mr. Kaiser, I wanted to follow up, and you had mentioned, you know, being comparable to the industry standard. And in your filed testimony, you talked about a 2017 American Gas Association compensation survey. And they surveyed the employee compensation programs of various utilities in different parts of the country, correct?
A. That's correct.
Q. And I think in your testimony, it showed that 13 of the 15 public utilities that reported in the north central region provide incentive compensation?
A. That's true.

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Q. Okay. And then to Commissioner Kroshus's questions on how do we know you're in the market or what are you doing to check to make sure you're there, is this -- when you said you had third party review, would that be the 2013 Aon Hewitt survey, a third party independent survey of our employee compensation program?

A. Yes, that's the study.

Q. And is that something that Montana-Dakota does on a regular basis?

A. Yes.

Q. And currently in 2018, they're doing another -- five years later doing another, you know, complete review of our system to make -- or our employee compensation system to make sure it's competitive in the market?

A. That's correct.

Q. Okay. And then finally, Mr. Kaiser, there was some talk about the targets and the 8.4 and the past history. Am I correct that in -- I think you mentioned, in 2015 the Company did not meet its thresholds and zero incentive bonuses were paid?

A. That is correct.

Q. Okay. And in 2016, the level of bonuses was under the target -- some bonuses were paid but it was

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under the target in 2016?

A. Yes.

Q. And then last year in 2017, bonus were paid, but they were above the projected target line used in this case?

A. Yes, they were.

Q. Okay. So in the three years we have a situation where no bonuses were paid, below target and above target?

A. That's correct.

Q. And does that kind of indicate to you that your target range is probably appropriate and certainly for projecting a 2018 test year?

A. It does.

MR. SANDERSON: I have no further questions.

THE COURT: Mr. Armstrong.

RECROSS-EXAMINATION

BY MR. ARMSTRONG:

Q. That would also indicate to you that removing the earnings portion didn't really have any effect on the amount paid, wouldn't it?

A. It would -- the earnings -- I'm not sure I can draw that correlation. I -- I'm sorry.

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MR. ARMSTRONG: Nothing further.

THE COURT: Mr. Coffman.

MR. COFFMAN: No more questions.

THE COURT: Major.

MAJOR UNSICKER: No questions, sir.

THE COURT: Ms. Jeffcoat-Sacco.

MS. JEFFCOAT-SACCO: No questions. Thanks.

THE COURT: Okay. We're going to adjourn here for today. We'll go off the record.

(The hearing was adjourned at 5:19 p.m.)

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REPORTER'S CERTIFICATE

I, Christa A. Reeser, a Registered Professional Reporter, Certified Realtime Reporter, and Certified Realtime Captioner, do hereby certify that the foregoing pages of typewritten material constitutes an accurate verbatim stenographic record taken by me of the proceedings aforementioned before Patrick J. Ward, Esq., Administrative Law Judge, on the 30th day of May, 2018, at the times and place specified.

DATED: July 2, 2018 Christa Reeser

Christa A. Reeser
Registered Professional Reporter
Certified Realtime Reporter
Certified Realtime Captioner
Notary Public, Cass County

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