MONTANA-DAKOTA
UTILITIES CO.
A Subsidiary of MDU Resources Group, Inc.

400 North Fourth Street
Bismarck, ND 58501
(701) 222-7900

September 16, 2019

Executive Secretary
North Dakota Public Service Commission
State Capitol Building
Bismarck, ND 58505-0480

Re: Case No. PU-19-___
Application for Deferred Accounting Treatment

Montana-Dakota Utilities Co. (Montana-Dakota) herewith files an original and seven (7) copies of an application for authority for deferred accounting treatment of costs related to the retirement of the Lewis & Clark 1, Heskett 1 and Heskett 2 coal-fired power plants. This filing is made in accordance with Title 49 of the North Dakota Century Code and the rules and regulations promulgated by the North Dakota Public Service Commission. Montana-Dakota's 2019 Integrated Resource Plan submitted in Case No. PU-19-221 (2019 IRP) provides support for the retirement of the three generating units.

Please refer all inquiries regarding this filing to:

Tamie A. Aberle
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Also, please send copies of all written inquiries, correspondence and pleadings to:

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Montana-Dakota respectfully requests that this filing be accepted as being in full compliance with the filing requirements of this Commission.

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

Sincerely,

Tamie A. Aberle

Tamie A. Aberle
Director of Regulatory Affairs

Attachments
cc: Karl A. Liepitz
Paul Sanderson

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

In the Matter of the Application of	)	
MONTANA-DAKOTA UTILITIES CO. for	)	Case No. PU-19-____
Authority for Deferred Accounting	)	

I. Summary of Application

Montana-Dakota Utilities Co. (Montana-Dakota or Applicant) is the Applicant in the above-entitled proceeding and makes application pursuant to N.D.C.C. Title 49 for deferred accounting for costs related to the retirement of three coal-fired generating stations (Lewis & Clark 1, Heskett 1 and Heskett 2) until disposition of its next general electric rate case.

II. Description of Applicant

Montana-Dakota is a Delaware corporation duly authorized to do business in the State of North Dakota as a foreign corporation and doing business in the State of North Dakota as a public utility subject to the jurisdiction of and regulation by the North Dakota Public Service Commission (Commission) under Title 49, N.D.C.C., as amended. Montana-Dakota's Certificate of Incorporation and amendments thereto have been previously filed with the Commission under Case No. PU-08-710 and such Certificate and Amendments are hereby incorporated by reference as though fully set forth herein. Montana-Dakota provides electric service to approximately 143,000 customers with approximately 93,000 of those customers located in North Dakota.

III. Authority for the Relief Requested

The Commission may authorize deferred accounting and amortization of unusual and non-recurring expenses that were not contemplated at the time current rates were established. By doing so, the Commission allows a utility to designate unusual and infrequent expenses as regulatory assets that will be amortized over future accounting periods.[1] The Commission has allowed deferred accounting when the amounts are sufficiently large that they could accelerate the timing of a rate case [2]. As explained below, this request involves expenditures of that nature as well as the need to accelerate depreciation in order to fully depreciate the Lewis & Clark 1, Heskett 1 and Heskett 2 generating stations upon retirement of the facilities.

IV. Retirement of the Generating Assets

On February 19, 2019, Montana-Dakota announced the Company's decision to retire the Lewis & Clark 1, Heskett 1 and Heskett 2 coal-fired generators at the end of 2020 and 2021, respectively. This decision was based on the age of the coal plants, the availability of low-cost natural gas driving low-cost power on the MISO market, as well as rising coal costs and operating and maintenance expenses (O&M expenses) at each of the units. This decision is fully supported in the Company's 2019 Integrated Resource Plan submitted in Case No. PU-19-221 (2019 IRP). Since the announcement in February of 2019, the Company has determined that March 2021 and March 2022

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[1]ND Admin. Code § 69-09-05.1-03 adopting the accounting practices set forth in the Uniform System of Accounts (USOA) prescribed by the Federal Energy Regulatory Commission, as set forth in 18 U.S.C. § 101; also N.D.C.C. § 49-05-16.

[2] Case No. PU-09-733 Montana-Dakota Utilities Co., a Division of MDU Resources Group Inc. request for authority to use deferred accounting for Montana-Dakota's efforts in securing new generation, primarily the Big Stone II Generation Station.

represent more probable dates for discontinuing operations rather than in December of the prior years.

As detailed in Volume IV, Attachment I of the 2019 IRP, Montana-Dakota undertook an in-depth review of the age and condition, economic competitiveness and future environmental compliance costs for the Lewis & Clark 1, Heskett 1 and Heskett 2 generators as part of the 2019 IRP process. This review indicated that these generating units are no longer economically competitive in the MISO market and that to remain economically viable, unobtainable reductions in operating expenses would be required. For example, O&M expenses would need to be eliminated entirely for all three units while Heskett 1 and Heskett 2 would require an elimination of O&M expenses plus a reduction in fuel costs. Based on a comparison of actual fuel plus variable O&M expenses for calendar year 2018, Heskett 1, Heskett 2 and Lewis & Clark 1 are the highest cost units in Montana-Dakota's generation portfolio with costs on a dollar per MWh generated basis 1.4 to over 2 times Montana-Dakota's 2018 average MISO energy market purchase price of $25.85 per MWh[3].

The decision to retire the units was further confirmed with specific retirement modeling analysis as part of the 2019 IRP process as detailed on Volume IV, Attachment I, pages 15-17 of the 2019 IRP. The Electric Generation Expansion Analysis System (EGEAS) model was used to analyze the effect of varying retirement dates (2021, 2024 and 2029) to compare the total net present value of the resource plan over a 50-year period. The results of this analysis showed that the later the retirement date, the higher the net present value of costs to customers. The units were

[3] Volume IV, Attachment I, Page 12 – Figure 11 of the 2019 IRP.

also allowed to be selected as a new resource in another modelling scenario assuming a 5-year life, zero capital costs and current fuel and O&M costs for the units, and the units were not selected as resources by the EGEAS model.

Finally, an estimated revenue requirement, on a total integrated electric system basis, comparing the annual cost of running the three units in 2023 was compared to the cost of retiring Lewis & Clark 1 at the end of 2020 and Heskett 1 and 2 at the end of 2021 including all post retirement costs and the cost of replacing the output of the retired plants with market energy purchases and the addition of a new simple cycle combustion turbine (Heskett 4). The post retirement costs included the amortization of employee retention benefit costs deemed necessary to keep the units running through the retirement dates, a 15-year amortization of the remaining net book values existing at the retirement dates and decommissioning costs. This analysis showed an annual savings of approximately $20 million assuming the units are retired and replaced[4].

V. Accounting Requirements

Montana-Dakota's financial reporting is subject to Generally Accepted Accounting Principles (GAAP) that provides guidance regarding accounting treatment applicable to the retirement of assets in the near future and prior to the previously expected retirement date. Specifically, ASC 360-10-35 requires the Company to accelerate depreciation in order to fully depreciate the asset to the expected early-retirement date for financial reporting purposes.

[4] Volume IV, Attachment I, Figure 14 – Page 17 of the 2019 IRP.

North Dakota's share of the total net plant balances as of August 31, 2019, for the assets to be retired at Heskett Units 1 & 2 and Lewis & Clark 1 are as follows:

	Heskett 1 & 2	**Lewis & Clark 1**	**Total**
Plant In Service	$81,683,172	$54,649,647	$136,332,819
Accumulated Reserve	49,748,972	22,972,378	72,721,350
Net Plant	$31,934,200	$31,677,269	$63,611,469

Montana-Dakota continues to record depreciation expense based on the authorized depreciation rates, which are matched to the authorized revenue, as approved in Case No. PU-16-666. However, the authorized depreciation rates will not provide a net plant balance of $0 upon retirement; therefore, the Company must accelerate the depreciation expense to achieve a net plant balance of $0. The difference between the accelerated depreciation required under GAAP and the authorized depreciation as approved in Case No. PU-16-666 is currently being deferred subject to approval by the Commission.

In addition, the Company is required to recognize a liability for exit and disposal cost obligations associated with the plant closures under the guidance of ASC 420-10. This would include the decommissioning costs and employee retention benefit costs described below. Under the guidance of ASC 980-340, these employee and disposal cost obligations that would be required to be expensed under GAAP are also currently being deferred.

Each cost category along with estimated costs to be deferred is explained in further detail below.

VI. Accelerated Depreciation

Montana-Dakota's electric depreciation study underlying the currently authorized deprecation rates was submitted in the Company's electric rate case filed on October 14, 2016 in Case No. PU-16-666 and was based on electric utility plant balances as of December 31, 2014. In that depreciation study, Lewis & Clark was assumed to be retired in 2025, Heskett 1 in 2021 and Heskett 2 in 2028. Subsequent to the depreciation study based on 2014 balances, the total plant in service balance as of August 31, 2019 has increased approximately $37 million at Lewis & Clark 1 and $14 million at Heskett 1 and 2, primarily related to environmental upgrades associated with the Mercury and Air Toxics Standard, Regional Haze Rule and Coal Combustion Residuals Rule. The accelerated depreciation necessary to depreciate North Dakota's share of the retired generating units by March 2021 for Lewis & Clark 1 and by March 2022 for Heskett 1 and 2 is $54.4 million.

As of December 31, 2017, Heskett 1 & 2 and Lewis & Clark had $38.9 million of accumulated deferred income taxes related to timing differences between book depreciation and tax depreciation. Of that amount, $4.6 million has been determined to be excess deferred income taxes (EDITs) resulting from the change in the federal income tax rate in the Tax Cuts and Jobs Act of 2017 (TCJA). In Case No. PU-18-89, Montana-Dakota reflected a reduction in rates to incorporate the tax savings of the TCJA. The reduction in rates included EDITs associated with Heskett and Lewis & Clark in the amount of $103,000.

The acceleration of the book depreciation and subsequent retirement of the generating units will result in acceleration of the recognition of all EDITs for both Heskett and Lewis & Clark. The amount, in excess of that reflected in rates, through the closure dates of each plant will be included as an offset to the other costs associated with the retirement of the generating units in the amount of $4.1 million The net amount of the remaining EDIT as allocated to North Dakota is $2.9 million.

VII. Decommissioning the Plants

Montana-Dakota retained Burns & McDonell Engineering Company (BMcD) to assist with the decommissioning required upon retirement of the plants. BMcD provided the Company with a cost estimate necessary to develop a cost budget and timeline for decommissioning and demolishing each of the generating stations. Based on the cost estimates prepared by BMcD, Montana-Dakota plans to issue Requests for Bids to demolition contractors the 2nd quarter of 2020 for Lewis & Clark 1, and the 3rd quarter of 2021 for Heskett 1 and Heskett 2.

BMcD is developing a plan for continuity of operations at each plant site. This is necessary because Lewis & Clark 2, consisting of two natural gas fired Wärtsilä 20V34SG simple cycle reciprocating internal combustion engines (RICE) with a combined nameplate rating of 19 MW shares systems and facilities with Lewis & Clark 1. At the Heskett site, Heskett 3, the natural gas fired General Electric (GE) simple cycle combustion turbine generator (SCCT) with a nameplate rating of 88 MW that went on-line in 2014 and the new SCCT nominally rated at 88MW (Heskett 4) share systems and facilities currently a part of Heskett 1 and 2. BMcD will be providing assistance in the evaluation of modifications, replacements, and additions to these systems and facilities necessary to minimize major outage impacts to the operations of Lewis & Clark

2 and Heskett 3, and to construction and commissioning of Heskett 4 during the decommissioning and demolition of the retired units and to ensure standalone operational capability of Lewis & Clark 2 and Heskett 3.

Montana-Dakota plans to use Lewis & Clark and Heskett Station staff to perform pre-decommissioning activities. BMcD will be preparing a project schedule and a plan that will define the anticipated duration of pre-decommissioning activities. The schedule for work to decommission and demolish the units to be completed by the contractor will not be known until the work is awarded. Montana-Dakota anticipates that the contractor(s) will mobilize and start work shortly after pre-decommissioning efforts are complete. Based on a range of cost estimates provided by BMcD, Montana-Dakota estimates a cost of $11.3 million to decommission and demolish Lewis & Clark 1 and a cost of $8.7 million to decommission and demolish Heskett 1 and 2.

Montana-Dakota began recovering $500,000 in decommissioning costs annually beginning in August 2017 upon the implementation of rates approved in Case No. PU-16-666. The Company has incurred decommissioning costs in excess of the amount of decommissioning collected to date and expects to have a balance of $110,750 at March 31, 2022, resulting in an accelerated decommissioning cost in North Dakota of $14.1 million to be deferred.

VIII. Employee Related Costs

The Company has created employee retention benefit plans to maintain a work force necessary to operate the units to be retired through the plant closure dates. Upon closure of the Heskett and Lewis & Clark Coal plants, some employees will be retained to operate the existing and new natural gas units and the Company will offer training for employees who wish to fill open positions in other areas of the Company. Those employees who remain employed through the last day of coal operations or until released by the Company and subsequently do not have another position with the Company have been offered a severance package. The Company is requesting to also defer these employee related costs with an estimate for the severance, retention, retraining and job search assistance costs at $6.1 million in total with $4.4 million allocated to North Dakota.

In summary, Montana-Dakota requests that the Commission issue its order authorizing deferred accounting for the retirement related expenses, net of the EDIT, applicable to the Lewis & Clark 1, Heskett 1 and Heskett 2, until disposition of its next general electric rate case. The total deferred costs, as allocated to North Dakota, are expected to total approximately $70.0 million as shown in the table below:

	Million $
Accelerated Depreciation	$54.4
Excess Deferred Taxes	(2.9)
Decommissioning Costs	14.1
Employee Retention	4.4
Total Deferred Costs	$70.0

As discussed in the 2019 IRP, the annual cost to retire assuming an amortization of the accelerated depreciation costs and decommissioning costs over 15 years and the Commission authorized rate of return and an amortization of the employee related costs over a 5-year period, is more than offset by the O&M expenses and fuel savings that occur upon retirement of the facilities resulting in a net benefit to North Dakota electric customers.

IX. Conclusion

Applicant respectfully requests that the Commission:

1. Give Notice of Opportunity to request a hearing to interested parties and, if no hearing is requested within twenty days, to waive the hearing in accordance with N.D.C.C. § 49-03.1-05.

2. Enter an Order authorizing deferred accounting for Montana-Dakota's costs related to the retirement of the Lewis & Clark 1, Heskett 1 and Heskett 2 generating stations.

3. Grant such other relief as the Commission shall deem appropriate.

Dated this 16th day of September 2019.

Tamie A. Aberle

Tamie A. Aberle
Director of Regulatory Affairs

Subscribed and sworn to before me this 16th day of September 2019.

Caitlin Straabe

CAITLIN STRAABE
Notary Public
State of North Dakota
My Commission Expires August 28, 2023

Caitlin Straabe, Notary Public
Burleigh County, North Dakota
My Commission Expires: 08/28/2023

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