STATE OF SOUTH DAKOTA	) :SS	IN CIRCUIT COURT
COUNTY OF HUGHES	)	SIXTH JUDICIAL DISTRICT

IN THE MATTER OF THE APPLICATION OF BLACK HILLS POWER, INC. FOR AUTHORITY TO INCREASE ITS ELECTRIC RATES	Civ. No. 15-146 **APPELLEE BLACK HILLS POWER, INC.'S BRIEF**

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PRELIMINARY STATEMENT

The following abbreviations are used in this Brief: Appellee Black Hills Power, Inc. is referred to as "Black Hills Power" or the "Company." Appellants GCC Dacotah, Inc., Pete Lien & Sons, Inc., Rushmore Forest Products, Inc., Spearfish Forest Products, Inc., Rapid City Regional Hospital, and Wharf Resources (U.S.A.), Inc. are referred to as "BHII." The South Dakota Public Utilities Commission is referred to as the "Commission."

JURISDICTIONAL STATEMENT

BHII has appealed from the Commission's Final Decision and Order dated April 17, 2015 ("Final Decision"), which approved the Amended Settlement Stipulation between the Company and Staff of the South Dakota Public Utilities Commission ("Staff"). The Commission affirmed the Final Decision on May 29, 2015, in its Order Denying Rehearing and Reconsideration. This Court has jurisdiction over this Appeal pursuant to SDCL 49-1-9.

STATEMENT OF THE ISSUES

BHII appeals the Commission's Final Decision and raises three issues:

I. **Whether the Commission appropriately allowed post test-year cost adjustments that became known and measureable within 24 months following the test year, when doing so is consistent with applicable statutes, administrative rules, and decades of prior practice, particularly where the Commission's interpretation of these authorities is given "great weight" and where the Commission is afforded "a reasonable range of informed discretion" in interpreting its own statutes and rules.**

Yes, the Commission's interpretation of its statutes and rules was correct, and the Court should affirm the Commission's decision.

II. **Whether the Commission was clearly erroneous in finding that the Company's ongoing pension expenses are properly represented through a normalization period of 2010-2014, as opposed 2011-2015, when substantial evidence was presented regarding appropriateness of the 2010-2014 period, and no evidence was presented regarding appropriateness of the 2011-2015 period.**

No, the Commission's findings were not clearly erroneous, and the Court should affirm the Commission's decision.

III. **Whether the Commission was clearly erroneous in finding that the inclusion of $880,000 in incentive compensation in the Amended Stipulation was proper when substantial evidence showed that such incentive compensation is necessary for the Company to remain competitive and retain employees, which benefits customers.**

No, the Commission's finding were not clearly erroneous, and the Court should affirm the Commission's decision.

STATEMENT OF THE CASE AND FACTS

Black Hills Power filed its Application for Authority to Increase Its Electric Rates ("Application"), including testimony, on March 31, 2014. *Final Decision* at 1, BHII App. A-2.[1] On June 6, 2014, BHII filed a Petition to Intervene. *Id.* On the same date, Dakota Rural Action ("DRA") also filed a Petition to Intervene. *Id.* The Commission issued its Order Granting Intervention to BHII and DRA on June 26, 2014. *Id.*

Staff served over 330 discovery requests, to which the Company responded. *Peterson Direct* at 5, BHII App. A-310. The Company also responded to over 60 discovery requests served by BHII. *Id.* Ultimately, the Company and Staff resolved all issues and entered into a Settlement Stipulation ("Original Stipulation") that was filed with the Commission on December 9, 2014. *Final Decision* at 2, BHII App. A-3. BHII chose to not be a party to the Original Stipulation and filed testimony in opposition. *Id.* DRA also chose to not be a party but did not pre-file opposition testimony. *See id.*

An evidentiary hearing was held on January 27 and 28, 2015 ("Evidentiary Hearing") to afford the Commission the opportunity to resolve two issues: (1) whether the Commission

[1] BHII's appendix will be referred to as "BHII App." The Company's appendix will be referred to as "Co. App."

should approve the Original Stipulation; and (2) if the Commission found that such approval was not appropriate, in the alternative, what rates, terms, and conditions were just and reasonable. *See Order for Hr'g*, BHII App. A-26.

In an effort to address certain issues raised during the Evidentiary Hearing, on February 10, 2015, the Company and Staff filed an Amended Settlement Stipulation ("Amended Stipulation"). *Final Decision* at 1, BHII App. A-2. The Amended Stipulation did not change the overall revenue deficiency that Staff and Black Hills Power agreed to as a term of the Original Stipulation. *Am. Settl. Memo* at 3, BHII App. A-69.

On March 2, 2015, the Commission held its open meeting deliberations regarding the Amended Stipulation. *Order Denying Reh'rg*, BHII App. A-26. On April 17, 2015, the Commission filed and served its Final Decision approving the Amended Stipulation in its entirety. *Final Decision* at 1, BHII App. A-2. The Commission denied BHII's petition for rehearing and reconsideration on May 29, 2015. *Order Denying Reh'rg*, BHII App. A-25-26.

ARGUMENT

Critical to the Court's review is the appropriate standard of review for the Commission's findings of fact and conclusions of law. Thus, as an initial matter, the Company clarifies the relevant standards of review as follows:

The Commission's findings of fact and factual inferences must be reviewed by this Court using the clearly erroneous standard of review. *In re Otter Tail Power Co. ex rel. Big Stone II*, 2008 S.D. 5, ¶ 26, 744 N.W.2d 594, 603; *see also* SDCL 1-26-36.[2] A factual "finding is clearly

[2] BHII incorrectly argues, citing *Tuckek v. South Dakota Department of Social Services*, 2007 S.D. 106, 740 N.W.2d 867, that the Court must apply a de novo standard of review because the Commission's factual findings were based on documentary evidence. This assertion is

erroneous if, after reviewing the entire record, [the Court is] left with the definite and firm conviction that a mistake has been made." *In re Estate of Schnell*, 2004 S.D. 80, ¶ 8, 683 N.W.2d 415, 418. The Court must resolve any conflict in evidence in favor of the Commission's findings. *Id.* Witness credibility, the importance to be accorded to a witness's testimony, and the weight of the evidence must be determined by the Commission, and the Court gives due regard to the Commission's opportunity to observe witnesses and examine the evidence. *Id.* The Court does not substitute its judgment for that of the Commission. *See id.* Instead, the Court considers the evidence in its totality and may only set aside the Commission's factual findings if the Court is definitely and firmly convinced that the Commission made a mistake. *In re Otter Tail Power*, 2008 S.D. 5, ¶ 26.

Conclusions of law are generally reviewed under the de novo standard of review. *Id.* Two relevant exceptions exist, however, for the interpretation of statutes and regulations. First, an agency's interpretation of a statute is given "great weight" when the agency has been charged with the statute's administration. *Matter of Sales & Use Tax Refund Request of Media One, Inc.*, 1997 S.D. 17 ¶ 10, 559 N.W.2d 875, 878. Second, "[a]n agency is usually given a reasonable range of informed discretion in the interpretation and application of its own rules when the language subject to construction is technical in nature or ambiguous, or when the agency interpretation is one of long standing." *Krsnak v. S.D. Dep't of Env't & Nat. Res.*, 2012 S.D. 89, ¶ 16, 824 N.W.2d 429, 436. The South Dakota legislature has charged the Commission with the administration of public utilities. *See, e.g.*, SDCL 49-1-11; 49-34A-4; 49-34A-6; and 49-34A-8; *see also App. of N. States Power Co.*, 328 N.W.2d 852, 855 (S.D. 1983) (the Commission has

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incorrect: Because the Commission's factual findings were based on both live and documentary evidence, the clearly erroneous standard is mandated. *Tuckek*, 2007 S.D. 106, ¶ 13.

"broad"regulatory authority). As such, in reviewing the Commission's conclusions of law on statutory and regulatory interpretation, the Court must give great weight to the Commission's interpretations and give the Commission a reasonable range of informed discretion.

In its appeal, BHII asserts as a broad statement that "the Commission misinterpreted and misapplied the law . . . The issues on appeal are questions of law, not fact." *BHII Brief* at 6. A review of BHII's arguments, however, indicates that BHII is disputing the Commission's factual findings. *See, e.g., id.* at 23-25 and 30-34. By incorrectly alleging that its appeal only contests conclusions of law, BHII apparently believes that it can convince this Court that a de novo standard of review is necessary. This assertion is incorrect for two reasons: (1) the Court must give great weight to the Commission's interpretation of statutes and administrative rules; and (2) BHII's allegations regarding allegedly erroneous factual findings by the Commission are subject to the clearly erroneous standard of review.

I. The Commission's interpretations of statutes and rules regarding post-test year adjustments must be given great weight, and the Commission's approval of the Company's adjustments to costs should be affirmed as such approval is consistent with the Commission's statutory and regulatory interpretations.

The Commission found that its statutes and rules allow for adjustments to the historic test year if such adjusted costs are known and measurable within a 24-month period after the last month of the test period. *Final Decision* ¶ 9, BHII App. A-19. As noted above, the Court must give the Commission's interpretation of its statutes and rules great weight.

BHII appeals the Commission's conclusion and asserts an interpretation of five words in an administrative rule that is contrary to South Dakota statutes, administrative rules, case law, and the long-standing policy of the Commission, and that results in an unreasonable interpretation and result. Specifically, BHII argues that under ARSD 20:10:13:44, post-test year

adjustments must be known with reasonable certainty and measurable with reasonable accuracy at the time the utility files its application. This interpretation is directly contrary to the language in SDCL 49-34A-19 (which statute is not even mentioned by BHII in its brief), other administrative rules (including ARSD 20:10:13:01(11), which BHII also does not discuss), and the long-standing Commission interpretation and policy regarding post-test year adjustments. Because the post-test year adjustment issue requires statutory interpretation, a review of the relevant statutes and cases is necessary before analyzing the administrative rules.

A. The rules of statutory construction require the Court to read statutes and regulations as a harmonious unit.

There are two primary goals of statutory interpretation in South Dakota. *Clark Cnty. v. Sioux Equip. Corp.*, 2008 S.D. 60, ¶ 28, 753 N.W.2d 406, 417. First, "the language expressed in the statute is the paramount consideration." *Id.* Second, "if the words and phrases in the statute have plain meaning and effect, [the Court] should simply declare their meaning and not resort to statutory construction." *Id.* Stated differently, "[w]hen the language in a statute is clear, certain, and unambiguous, there is no reason for construction, and this Court's only function is to declare the meaning of the statute as clearly expressed." *Citibank, N.A. v. S.D. Dep't. of Rev.*, 2015 S.D. 67, ¶ 20, --- N.W.2d ---, 2015 WL 4598017, at *7. The same rules of interpretation apply for administrative regulations. *Id.* ¶ 11.

Furthermore, when a case (such as this one) involves the interpretation of a statute and an implementing administrative regulation, the statute and regulation are to be construed "together to make them harmonious and workable." *Id.* ¶ 15. This rule exists because the power of an agency to administer a statute and promulgate regulations is not the power to make law, but rather to adopt regulations to carry out the Legislature's will. *Id.*

B. The plain language of the adjustment rules provide for post-test year adjustments in the 24 months following the test year.

The requirements for a public utility rate case proceeding are set forth in South Dakota statutes (generally SDCL Ch. 49-34A) and administrative rules (ARSD 20:10:13:1 to 107), many of which became effective in the mid-1970s. Shortly thereafter, in 1980, the South Dakota Supreme Court outlined the Commission's procedure for rate making as follows:

> The PUC has adopted the "cost of service" method of rate making. This method entails four steps as follows: (1) Properly determine company's rate base, i.e., investment devoted to public service; (2) determine a fair and reasonable rate of return; (3) multiply the base ((1) above) by the rate ((2) above); and (4) add to company's cost of operations referred to above (including taxes and depreciation). To assist in the computation of the steps above, a historical test year is adopted. The data from this year must be adjusted as to the cost of operations and the rate base to reflect changes which will be in effect subsequent to the historical test year.

App. of Nw. Pub. Serv. Co., 297 N.W.2d 462, 464-65 (S.D. 1980) (emphasis added).[3] This procedure is further clarified in the relevant statutes, including SDCL 49-34A-19, which governs the determination of a utility's revenue requirement:

> In determining the revenue requirement the commission shall consider revenue, expenses, cost of capital and any other factors or evidence material and relevant thereto. The commission may take into consideration the reasonable income and expenses that will be forthcoming in a period of twenty-four months in advance of the test year.

SDCL 49-34A-19 (emphasis added). Under this statute, and the use of the word "may," the Commission maintains discretion to consider adjustments for expenses that will be forthcoming

[3] BHII alleges that *Northwestern Public Service* has limited precedential value. This argument is not relevant as the Supreme Court outlined the Commission's procedure and confirmed that a historic test year does not represent current costs but rather provides a basis for which adjustments may be made to reflect current costs. During the pendency of that case, the Commission promulgated ARSD 20:10:13:44, which sets out, in further detail, the manner in which post-test year adjustments may be made. Thus, *Northwestern Public Service* remains good law for the issues raised in this appeal.

for a period of 24 months. *See also Final Decision* ¶ 9, BHII App. A-19 ("the Commission concludes that the intent of SDCL 49-34A-19 is to permit the consideration of the cost of service evidence that becomes known and measurable during the twenty-four month period following the end of the test year").[4]

The Commission's interpretation is also consistent with the post-test year adjustment requirements, which are set forth in ARSD 20:10:13:44:

> **Analysis of system costs for a 12-month historical test year.** The statement of the cost of service shall contain an analysis of system costs as reflected on the filing utility's books for a test period consisting of 12 months of actual experience ending no earlier than 6 months before the date of filing of the data required by ARSD 20:10:13:40 and 20:10:13:43 unless good cause for extension is shown. The analysis shall include the return, taxes, depreciation, and operating expenses and an allocation of such costs to the services rendered. The information submitted with the statement shall show the data itemized in this section for the test period, as reflected on the books of the filing public utility. Proposed adjustments to book costs shall be shown separately and shall be fully supported, including schedules showing their derivation, where appropriate. However, no adjustments shall be permitted unless they are based on changes in facilities, operations, or costs which are known with reasonable certainty and measurable with reasonable accuracy at the time of the filing and which will become effective within 24 months of the last month of the test period used for this section and unless expected changes in revenue are also shown for the same period.

For purposes of this rule, ARSD 20:10:13:01(11) defines test period as "the test period outlined in ARSD 20:10:13:44, except that if additional material is filed by the utility, a test period is any 12 consecutive months beginning no later than the proposed effective date of the rate application." (emphasis added). Therefore, the reasonable interpretation of "at the time of filing"

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[4] While it may be argued that the phrase, "in advance of," in SDCL 49-34A-19 is not clear, it would be illogical to interpret the statute in a manner that only allowed for adjustments for costs that occurred during the two years prior to the test year. Reasonable interpretation of the statute justifies consideration of expenses that will be forthcoming in the 24 months following the test year. The Commission's interpretation of SDCL 49-34A-19 as meaning "following the test year" is consistent with the plain language and ordinary meaning of the statute.

in ARSD 20:10:13:44 is the time that additional material is filed by the utility as referenced in ARSD 20:10:13:01(11). This interpretation is consistent with the Commission's Final Decision and its interpretation of the adjustment rules for the past several decades.

Applying these rules to the facts before the Commission, the Company filed additional material (namely the responses to discovery requests) after the Company submitted its Application, which proposed an effective date of October 1, 2014. Therefore, using the definition of "test period" in ARSD 20:10:13:01(11), the test period referenced in ARSD 20:10:13:44 becomes any 12 consecutive months beginning no later than October 1, 2014.

This interpretation of the adjustment rules by the Commission is not only reasonable, but it is also logical. Section 49-34A-8 provides, in part, that the Commission shall give due consideration "to the need of the public utility for revenue sufficient to enable it to meet its total current costs of furnishing such service[.]" *Id.* (emphasis added). Post-test year adjustments that will become effective in the 24 months following the test year are necessary so that the utility's current costs will be met. Furthermore, the historic test year does not represent current costs, but rather provides a basis for which adjustments may be made to reflect current costs. As such, the test year should be adjusted once more current costs are known with reasonable certainty.

BHII asks the Court to find that ARSD 20:10:13:44 limits adjustments to those that were known with reasonable certainty or measurable with reasonable accuracy at the time that the Application was filed. BHII does not even cite or discuss SDCL 49-34A-19 (which the Commission relied on in interpreting its rules) or ARSD 20:10:13:01(11). Instead, it asks this Court to read ARSD 20:10:13:44 in isolation and without review of other applicable statutes and administrative rules in violation of the statutory construction rules.

The plain language of the adjustment rules does not support the interpretation advanced by BHII. If the Commission took BHII's interpretation to its logical conclusion, then the only adjustments that would be permitted would be those that were known with reasonable certainty and measurable with reasonable accuracy before the Application was filed. Such an interpretation is illogical as there would be no need to include an adjustment later that was already known at the time the Application was filed. Further, an interpretation of this nature is inconsistent with decades of Staff and Commission past practice and the adjustment rules, which permit adjustments for costs that will be effective within 24 months of the last month of the test period. *Thurber Rebuttal* at 4, BHII App. A-371; *Hr'g Tr.* at 278-279, Co. App. A-101-02.

C. Applying the adjustment rules to the facts presented before the Commission confirms that the Commission did not err in approving the post-test year adjustments.

A review of the facts in this matter demonstrate that the Commission followed the adjustment rules in approving the adjustments disputed by BHII. The Company's historical test year ended on September 30, 2013. Therefore, under SDCL 49-34A-19, the Commission may consider reasonable expenses that will be forthcoming within 24 months of the last month of the test period (September 30, 2015), as post-test year adjustments. A comparable permissible adjustment time period is also permitted under ARSD 20:10:13:44. Finally, as stated above, the calculation of September 30, 2015 as the final date for post-test year adjustments is consistent with the calculation of "test period" under ARSD 20:10:13:01(11). Therefore, the adjustment rules all support the inclusion in a settlement of post-test year adjustments which become effective on or before September 30, 2015, and are known with reasonable certainty and measured with reasonable accuracy at the time the Company filed the additional material.

In compliance with the adjustment rules, after filing its Application on March 31, 2014, the Company filed additional material with the Commission in response to over 390 discovery requests from Staff and BHII. *Peterson Direct* at 5, BHII App. A-310. This additional material formed the basis of the adjustments, which were known with reasonable certainty and measurable with reasonable accuracy at the time that Black Hills Power responded to the discovery requests. *Thurber Rebuttal* at 2-3, BHII App. A-369-70. Over 15 months of changes in facilities, operations, and costs occurred and were appropriately adjusted pursuant to the adjustment rules. *Id.* Furthermore, the vast majority of the adjustments relate to costs that Black Hills Power incurred during the 12 months following the historic test year. *Id.* For the few categories of costs that were not incurred during this time period, those costs are known with reasonable certainty and measurable with reasonable accuracy. *Id.* at A-369-72; *Peterson Direct* at 8, BHII App. A-313. Accordingly, the Commission properly approved the post-test year adjustments, as such adjustments were proposed within the 24 months after the Company filed its Application and such post-test year costs were reasonably known and measurable at the time the Company filed the material supporting the adjustments.

D. The Court must give the Commission's interpretation of its rules great weight, and such interpretation is supported by the Commission's long-standing policy.

As noted above, the Court must give the Commission's interpretation "great weight" because the Commission has been charged with the administration of statutes governing public utilities in South Dakota. *Media One Refund*, 1997 S.D. 17, ¶ 10. Furthermore, the Commission has previously interpreted the adjustment rules, which are technical in nature, and such interpretation has been consistent and is long standing. As such, the Court also affords the Commission a reasonable range of informed discretion. *Krsnak*, 2012 SD 89, ¶ 16.

The Commission and Staff have employed a long-standing policy that supports the post-test year adjustments made in this case:

> Staff expert witness Peterson testified that during the four plus decades that he has worked with Staff on rate cases, the consistent interpretation of ARSD 20:10:13:44, read together with SDCL 49-34A-19, has been that because a historic test year is used to set rates for a future period, the analysis and substance of a proposed change in utility rates should include both known expenses during the test year and also adjustments to reflect any changes that occurred after the test year that become known and measurable within the 24-month period provided for in ARSD 20:10:13:44 and SDCL 49-34A-19. . . This is the standard that Staff has relied on for years, and the Commission has approved numerous rate case settlements based on that standard.

Final Decision ¶ 26, BHII App. A-9. Additionally, "[a]s set forth in Conclusions of Law 8 through 10, the Commission concluded that adjustments in the Amended Stipulation are within the allowable adjustment periods set forth in SDCL 49-34A-19 and ARSD 20:10:13:44." *Id.* ¶ 27. The Commission further concluded that

> these provisions have for decades been interpreted together as providing for a historic test year as the cost of service basis period, but also, in part because such cost of service data are used to set rates for a future period, the analysis and substance of a proposed change in utility rates should include both known and measurable expenses during the test year and adjustments to reflect any changes that occurred after the test year that become known and measurable within the 24-month period for case processing provided for in ARSD 20:10:13:44 and SDCL 49-34A-19.

Id. ¶ 9, A-19.

Further, a review of case law indicates that the Commission's long-standing policy to allow adjustments of test year expenses dates to at least 1981. For example, the Memorandum Decision of the Circuit Court in the case of *In re Application of Northern States Power Co. dba Xcel Energy for Authority to Increase its Electric Rates*, No. F-3382 (S.D.P.U.C. 1981), Co. App. A-270-76, includes the following analysis:

> Staff Witness Rislov testified that the purpose of a rate increase application is to derive cost/revenue relationships that will be in effect for the forthcoming period. He

> maintained that historical data reflects actual cost/revenue relationships, and when adjusted, is a better indicator of future relationships than a budget. . . Rislov testified that historical test years are not "backward looking" in a rate case context. It is Witness Rislov's testimony that historical test years adjusted for known and measurable changes are sound for development of appropriate cost/revenue relationship. . .
>
> Witnesses Rislov and Towers additionally testified that NSP could offer known change adjustments occurring prior to the Commission Order[.]

Id. at 2-3 (emphasis added).[5] Based on this evidence, the Court approved the Commission's decision that the adjusted historical test year, as recommended by Staff, was the better method for calculating rates. *Id.* at 35.

Furthermore, Staff was following the Commission's policy as early as 1982, as demonstrated in a Staff memo in another Northern States Power rate case:

> The refined adjustments were included in Company's rebuttal testimony. Other amounts were included initially in Company's rebuttal filing. One was presented for the first time during settlement discussions. All of the amounts reflected as updates would have been accepted by Staff had the case gone to hearing.

In re App. of N. States Power Co., No. F-3422, (S.D.P.U.C. 1983) at 7, Co. App. A-262.

Finally, BHII contends that the Commission's interpretation will "permit a utility to continually update its cost of service in this manner would undermine due process because ratepayers would never know exactly what revenue requirement the utility was proposing." *BHII Brief* at 19. This argument fails to recognize that a utility may never recover from its ratepayers more than the increase proposed by the utility in its application. *See* SDCL 49-34A-21. Ratepayers will always know the maximum increase requested by the utility, and any

[5] By Memorandum Decision dated October 28, 1982, Presiding Circuit Judge Robert Miller of the Sixth Judicial Circuit affirmed the Commission's decision. Memorandum of Decision, *In re App. of N. States Power Co. for Auth. to Est. Increased Rates for Elec. Serv. in S.D.*, Civ. No. 82-6, (S.D. 6th Jud. Cir., Oct. 28, 1982), Co. App. A-277-97.

adjustments must result in some amount less than the increase requested by the utility in its application. Furthermore, in this case, the Company filed its additional material supporting the adjustments in response to discovery requests; as such, BHII had the opportunity to propound additional discovery requests on the Company and cross-examine witnesses regarding this additional material during the Evidentiary Hearing.

As demonstrated by the Commission's Final Decision, and as further supported by Staff's witness, precedent, and Staff's memorandum from the early 1980's, the Commission's decision here is consistent with and affirms its long-standing policy to allow post-test year adjustments that are known with reasonable certainty and measurable with reasonable accuracy at the time the utility filed the information supporting the adjustment. Thus, the Court must affirm the Commission's approval of the post-test year adjustments.

E. BHII's arguments regarding certain adjustments do not provide any reason for this Court to reverse the Commission's interpretation of its rules.

Based on its flawed interpretation of ARSD 20:10:13:44, BHII alleges that the adjustments relating to the Light Detection and Ranging ("LIDAR"), affiliate allocations, and employee additions fall outside the parameter of permitted adjustments. BHII's arguments are based solely and completely on its incorrect interpretation of ARSD 20:10:13:44.[6] BHII's arguments fail under the correct interpretation of the adjustment rules and, as such, the Court should disregard these specific arguments in their entirety. Even if the Court reviews these

[6] BHII's theory is that these items may only be allowed if those adjustments were "fully supported" and known with "reasonable certainty and measurable with reasonable accuracy" at the time Black Hills Power filed its Application. BHII uses its idea of "Pre-Filing Adjustments" and "Post-Filing Adjustments" to distinguish what adjustments should be allowed, using its incorrect interpretation of ARSD 20:10:13:44.

arguments, however, the evidence presented for each of these adjustments affirms that inclusion of these items as adjustments is consistent with the Commission's interpretation of its rules.

1. BHII's own expert recommended that the Commission adopt certain post-test year adjustments, which is contrary to BHII's argument before this Court.

In contradiction to BHII's present legal position, BHII, through its witness Mr. Kollen, fully supported post-test year adjustments agreed upon by the Company and Staff if those adjustments were beneficial to BHII, even though those adjustments were not known and measurable at the time that the Company filed its Application. The post-test year adjustments supported by BHII include the following:

> (1) Neil Simpson Complex Shared Facilities Adjustment (referred to by BHII as the "Neil Simpson Rent Revenue and Expense"): Staff and the Company agreed to a reduction of approximately $219,000 of the allocation of the Neil Simpson Rent Revenue and Expense based upon cost information provided by the Company after filing its Application. *Orig. Settl. Memo* at 8; BHII App. A-45 ("Staff generally agreed with the adjustment but replaced the budgeted costs used by BHP with actual costs. The result of Staff's revisions reduces jurisdictional operating expense by approximately $74,000 and reduces jurisdictional operating revenue by approximately $136,000."). Mr. Kollen recommended that the Commission adopt this proposed adjustment. *Kollen Direct* at 49, BHII App. A-184.
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> (2) Neil Simpson Complex Common Steam Allocation: Staff and the Company agreed to a post-test year adjustment that reduced operating expense by approximately $244,000. *Orig. Settl. Memo* at 9, BHII App. A-45 ("Staff generally agreed with the adjustment but replaced the budgeted costs used by BHP with actual year end August 2014 costs. . . The result of Staff's revisions reduces jurisdictional operating expense by approximately $243,000."). This adjustment was based on actual costs not known until after the date of filing the Application. Mr. Kollen, however, recommended that the Commission adopt this proposed adjustment. *Kollen Direct* at 49, BHII App. A-184.
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> (3) Cost of Debt: In its Application, the Company projected the cost of new debt. After filing the Application, the new debt was issued at a lower rate of interest than projected in the Application. Accordingly, BHII proposed an adjustment to reduce the cost of debt, resulting in a reduction in the revenue requirement of approximately $885,000, which Staff and the Company accepted. *Orig. Settl. Memo* at 15, BHII App. A-52. Mr. Kollen recommended that the Commission approve this

adjustment, i.e., that the actual cost of debt determined after the filing of the Application should be used to reduce the revenue requirement. *Kollen Direct* at 49, BHII App. A-184.

2. The Commission's approval of the adjustments contested by BHII should be affirmed because such approval was consistent with the Commission's interpretation of its rules and the Commission's findings regarding the same were not clearly erroneous.

The Commission also approved three other adjustments, which BHII contests:

(1) The Commission approved the LIDAR adjustment. At the time that Black Hills Power filed this rate case, it planned to perform LIDAR imaging of certain facilities. *Thurber Direct* at 11-12, BHII App. A-378-79. The LIDAR work was completed in the fourth quarter of 2014 pursuant to a fixed price contract. *Id.* at A-380. Staff and the Company included the LIDAR costs as an adjustment to the test year, as the costs were known, measurable, and incurred within 24 months following the historic test year. The Commission's approval of the LIDAR adjustment is consistent with the Commission's interpretation of its rules.

(2) The Commission approved the BHUH affiliate allocations adjustment.[7] Mr. Peterson (Staff witness) addressed this adjustment in his pre-filed testimony. The Original Stipulation reflects increases in the expenses allocated to the Company from its affiliate companies. The Company proposed an adjustment to test year affiliate expenses based on its post-test year operating budget. Staff responded that they were not willing to recommend an adjustment based solely on the Company's budget projections. The Company then provided a detailed summary of its most recent annualized expenses from the two affiliated companies. As Mr. Peterson testified: "The actual annual amounts billed to BHP are included in the settlement. Thus, the amounts billed to BHP from affiliates that are incorporated into the settlement reflect the Company's actual, known costs." *Peterson Direct* at 18, BHII App. A-323. Accordingly, the affiliate allocation costs were known, measurable, and proper as post-test year adjustments, and the Commission's approval of the same was consistent with its interpretation of its rules.

(3) The Commission approved the employee additions adjustment. As an initial matter, BHII misstates the evidence on this adjustment. The adjustment only

[7] BHII claims that the affiliate allocations adjustments "were based upon informal e-mail communications between BHP and Staff that were not provided to BHII or otherwise included in the record." *BHII Brief* at 20. BHII misstates the record because "the information reflected in the emails is virtually identical to the information that was produced in October 2014 in the Supplemental Response to SDPUC Request 3-96." *Kilpatrick Rebuttal* at 5; Co. App. A-61. Thus, the information was provided to BHII.

> reflects costs for Company positions which were hired and filled at the time of the settlement negotiations between Staff and the Company in December of 2014. Although such costs were not known at the time of the Company's Application in March of 2014, such costs were known, measurable, and proper as a post-test year adjustment in December of 2014. *Thurber Rebuttal* at 15-16, BHII App. A-381-82; *Peterson Direct* at 15, BHII App. A-320. As such, the Commission's approval of the employee additions for positions actually hired at the time of the Original Settlement is consistent with the Commission's interpretation of its rules.

In sum, providing the Commission a reasonable range of informed discretion and giving the Commission's interpretation of its rules great weight as required by South Dakota law, the Court should affirm the Commission's interpretation of the adjustment rules. These rules allow for post-test year adjustments within 24 months after an application is filed if such adjustments are sufficiently known and measurable at the time the material describing the costs is filed with the Commission. Using this interpretation, the Commission properly approved the three above-stated post-test year adjustments which BHII contests (and the three post-test year adjustments which BHII recommended the Commission adopt). The Court should affirm the Commission in all respects regarding the post-test year adjustments.

II. The Commission's approval of the five-year normalization process for pension expenses using the 2010-2014 data is not clearly erroneous as the Commission received substantial evidence on the appropriateness of a 2010-2014 normalization period but no evidence on the appropriateness of a 2011-2015 normalization period.

BHII's contends that, as a matter of law, the Commission was required to calculate the Company's five-year average pension expense based on the normalization of the 2011-2015 costs, rather than the 2010-2014 costs. Importantly, BHII neither argued nor presented any evidence during the Evidentiary Hearing that the Company's pension expenses should be normalized using the 2011-2015 costs. As such, BHII's new argument that, as a matter of law, the Commission had to use a 2011-2015 normalization period is not reviewable by this Court. Even if the Court does review this issue, the Commission's approval of the Company's pension

expenses must be affirmed under the clearly erroneous standard of review because the Company and Staff presented substantial evidence to the Commission on the appropriateness of the 2010-2014 normalization period.

A. Normalization of certain costs, including pension expenses, is necessary for the Commission to ensure that costs match revenues.

In determining whether a rate is just and reasonable, the Commission uses a "matching principle" in which it evaluates whether the test years' costs "establish with a reasonable degree of accuracy the revenue and expenses that a utility will experience during the period when the new rates will be in effect." *App. of Nw. Pub. Serv. Co.*, 297 N.W.2d 462, 469 (S.D. 1980); SDCL 49-34A-8 ("The commission, in the exercise of its power under this chapter to determine just and reasonable rates for public utilities, shall give due consideration . . . to the need of the public utility for revenues sufficient to enable it to meet its total current cost of furnishing such service"). Stated differently, the Commission matches test-year costs to revenues in determining whether the overall rate is just and reasonable. *In re Nw. Pub. Serv. Co.*, 18 P.U.R.4th 291, 294, 1976 WL 419254 (S.D.P.U.C. 1976), Co. App. A-237; *see also Town of Norwood v. F.E.R.C.*, 53 F.3d 377, 380-81 (D.C. Cir. 1995) ("The Commission follows a 'general ratemaking principle' of 'matching,' whereby ratepayers are charged with the costs of producing the service they receive."). This "matching principle" is a "fundamental rate-making principle." *In re Minn. Gas Co.*, 32 P.U.R.4th 1, 4 (S.D.P.U.C. 1979), 1979 WL 461903, Co. App. A-196.

If the test year does not appropriately match costs and revenues, such test year is inappropriate under the matching principle. *Colo. Mun. League v. Pub. Util. Comm'n*, 687 P.2d 416, 422 (Colo. 1984) ("It is fundamental to a proper test year that costs (both investment and operating) and revenues match, i.e., that they be consistent with each other. Unless there is a

matching of costs and revenues, the test year is not a proper one for fixing just and reasonable rates."). Thus, for a volatile cost which varies year to year, the use of a single test year may be inappropriate. In such a situation, the Commission normalizes a volatile cost over a defined period of time. *Final Decision* ¶ 43, BHII App. A-12 ("the Commission has routinely relied on the normalization treatment in prior cases").

For example, weather is volatile and determining the Company's weather-related costs based on one year would be inappropriate. Instead, the Commission approved the normalization for weather-related costs using a thirty-year period. *See Orig. Settl. Memo.* at 10, BHII App. A-47. Similarly, the Commission approved the normalization of costs for the Company's bad debt (using a five-year normalization period from 2009-2013), and storm damage (using a five-year normalization period from 2008-2013). *See id.* at A-42-44.

BHII does not dispute these normalizations or the time period used for these normalizations. BHII, however, disputes the Commission's approval of the normalization of pension expenses from 2010-2014 even though the Company's pension expenses, as stated more fully below, vary significantly from year to year.

B. BHII provided no evidence to the Commission that the Commission must normalize the Company's pension expenses using the 2011-2015 costs, and the Court should decline to review this new argument by BHII.

On appeal, BHII has changed the nature of its argument on the normalization of pension expenses and now argues that, as a matter of law, the Commission had to normalize pension expenses from 2011-2015. A review of the evidence establishes that BHII presented no evidence that a 2011-2015 normalization period would represent the Company's on-going pension expenses better than a 2010-2014 normalization period. Regardless, the Commission's approval

of the normalization of pension expenses from 2010-2014 should be affirmed as such approval was not clearly erroneous.

1. During the Evidentiary Hearing, BHII only offered evidence that the pension expenses should be determined on the 2014 data.

In response to the Settlement Stipulations, BHII argued that the Company should use the actual 2014 pension expense, not the five-year normalization from 2010-2014, as the 2014 pension expense, BHII alleged, was the best evidence of the Company's pension expenses. *Kollen Direct* at 33, BHII App. A-168. Although BHII accepted the normalization of other expenses, Mr. Kollen rejected as "opportunistic" the five-year normalization process. *See id.*

During the Evidentiary Hearing, BHII continued to take the position that only the 2014 pension expense should be used. Further, Mr. Kollen testified that the normalization procedure was a new methodology for the Commission to determine the Company's costs, even though, as stated above, BHII accepted the normalization of other Company expenses and the Commission regularly normalizes volatile expenses.

In its Post-Hearing Brief, submitted after the conclusion of the Evidentiary Hearing, BHII repeated its argument that the Commission should use 2014 in calculating the pension expense costs and that the Company's five-year normalization was "opportunistic." *BHII Post-Hearing Brief* at 40-41, BHII App. A-112-13.[8] Later in that same brief, BHII alleged that "if the Commission is inclined to use the most current information, Mr. Thurber's table on page 21 of his rebuttal testimony should be revised to delete the year 2010 and add the year 2015 for

[8] BHII alleged that "[t]he Commission should accordingly remove BHP's adjustment to increase pension expenses based on a five-year average and require the Company to apply the benefit of the lower pension expenses in 2014 as a reduction to its revenue requirement." *BHII Post-Hearing Brief* at 40-41, BHII App. A-112-13.

purpose of calculating the five year average." *Id.* Importantly, there was no argument by BHII that the Commission must do so as a matter of law. Further, BHII provided no evidence during this proceeding that 2011-2015 is a more appropriate normalization period than 2010-2014.

2. The Court should decline to review BHII's argument on pension expense as the issue was not raised prior to appeal.

It was only after the Evidentiary Hearing that BHII suggested that the 2011-2015 data should be used for the normalization of pension expense, and even then stated that 2015 should be used only "if the Commission is inclined to use the most current information." Because the Evidentiary Hearing had concluded at the time BHII argued for inclusion of the 2015 pension expense, there was no evidence in the record regarding whether the use of a 2011-2015 normalization period is a better reflection of the Company's current pension costs than the 2010-2014 period adopted by the Commission. Realizing that there was no evidence supporting this new assertion, BHII now tries to position this as a legal rather than a factual matter and alleges that as a matter of law the Commission must use the 2011-2015 data. *BHII Brief* at 23.

"[A]n issue not presented to the fact-finding tribunal will not be reviewed at the appellate level. This rule applies to administrative agencies as well as trial courts." *Finck v. Nw. Sch. Dist.*, 417 N.W.2d 875, 878 (S.D. 1988). This rule exists because "[f]or an appellate court to consider issues and make a decision on an incomplete record on questions raised before it for the first time would, in many instances, result in injustice[.]" *Cain v. Fortis Ins. Co.*, 2005 S.D. 39, ¶ 22 94 N.W.2d 709, 714. This rule also "exists to permit a [fact-finding tribunal] an opportunity to correct claimed error, prior to appeal." *Sioux Falls Shopping News, Inc. v. Dep't of Rev. & Reg.*, 2008 S.D. 34, ¶ 29, 749 N.W.2d 522, 528. Thus, the Court should reject BHII's position in

its entirety as BHII never presented any evidence before the Commission on the alternate theory it raises in this appeal.

C. Even if the Court reviews BHII's new argument on normalization, the Commission's factual findings are not clearly erroneous.

The Commission's findings of fact are not clearly erroneous and this Court should affirm the Commission on those findings.[9] A summary of the Commission's findings on pension expense follows, with appropriate cites to the record with the evidence supporting the finding:

> The Company's pension expense varies significantly from year to year. *Final Decision* ¶ 41, BHII App. A-12 (*Thurber Rebuttal* at 21, BHII App. A-388; *Peterson Direct* at 16-17, BHII App. A-321-22). The Company's test year pension expense was $2,844,759 but the 2014 pension expense was only $976,122. *Id.* (*Thurber Rebuttal* at 21, BHII App. A-388). The five year average expense for settlement was $2,336,305. *Id.* (*Peterson Direct* at 16-17, BHII App. A-321).
>
> The 2010-2014 data used in the normalization included a low year (2014 at $976,122) and a high year (2012 at $3.25 million). *Id.* (*Peterson Direct* at 16, BHII App. A-321). The Commission is familiar with the normalization process and has used such calculations in other cases and for other costs in this case, namely the weather, bad debt, and storm damage expenses. *Id.* (*Orig. Settl. Memo.* at 10-13, BHII App. A-47-49). Regarding pension expenses, the facts and circumstances surrounding the pension expense make it appropriate to apply normalization treatment in this instance. *Id.* ¶ 43 (*Evid. Hr'g Tr.*, at 132-33, 282-83, Co. App. A-85-84, A-105-06).
>
> The Commission approved the normalization process for pension expense using the 2010-2014 timeframe, which includes a benefit to customers as such calculation saved over $500,000 in expenses. *Id.* ¶¶ 41-43 (*Peterson Direct* at 16, BHII App. A-321; *Evid. Hr'g Tr.* at 282, Co. App. A-105).

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[9] BHII confuses the issue on whether the normalization of pension expenses is a conclusion of law or a factual finding. The Commission made numerous factual findings that the pension expense should be normalized with the 2010-2014 costs and, thus, the clearly erroneous standard of review applies to the Commission's decision. Alternatively, if the de novo standard applies, the Court must give great weight to the Commission's conclusion as such conclusion was the result of the Commission's interpretation of its statutes and rules. Even under that standard, the Commission's decision to approve the normalization of pension expenses from 2010-2014 results in a just and reasonable rate and, as such, should be affirmed.

These above-stated factual findings are fully supported by the substantial evidence the Commission received and reviewed for the Company's pension expense. The Commission reviewed the pre-filed testimony; questioned the Company's witnesses and experts, Staff's witness, and BHII's witnesses during the Evidentiary Hearing; and considered extensive briefing on the pension expense issue. *See, e.g., Evid. Hr'g Tr.* p. 86-87, 132-33, 184, 210, and 282-83, Co. App. A-80-81, A-85-86, A-92, A-96, and A-105-06. There is no evidence in the record that any other period of time was more appropriate for normalization than 2010-2014. There is also no evidence in the record that the normalization using the 2010-2014 data was not a reasonable level of cost for the Commission to use in matching the Company's costs to its revenues under the matching principle. The record further reflects that the Company's 2015 pension expense was not available at the time of filing of the Application or the Original Stipulation.

BHII argues that the Commission ignored the data from 2015. To the contrary, the Commission considered the data from 2015 in determining whether the normalization of pension expense using costs from 2010-2014 was proper. *See, e.g., Post-Brief Hr'g Tr.* at 4-7, Co. App. A-136-39. There was, however, no argument by any party during the Evidentiary Hearing that the Commission had to use the 2015 pension expense cost in the normalization to best match the Company's costs to its revenues.

This Court, resolving any conflict in evidence in favor of the Commission, and considering the evidence in its totality, may only set aside the Commission's factual findings if the Court is definitely and firmly convinced that the Commission made a mistake. Such is not the case here. If the Court reviews the normalization issue raised by BHII for the first time on appeal, the Court should find that the Commission's factual findings are not clearly erroneous.

D. BHII's argument lacks any legal authority and, as such, must be disregarded.

Finally, BHII's new argument that once the Commission adopts an interpretation of ARSD 20:10:13:44 (which permits adjustments), the Commission is allowed no discretion in applying that rule to the evidence in the record is nonsensical. BHII essentially asks the Court to interpret ARSD 20:10:13:44 to require the Commission to adjust a cost every time new data for that cost becomes known.[10]

BHII's argument is wholly unsupported by the plain language of ARSD 20:10:13:44. Rule 20:10:13:44 does not require a utility company to adjust a book cost if such data becomes known after an application is filed. The regulation does require certain actions from a utility company: "The statement of the cost of service shall contain an analysis of system costs as reflected on the filing utility's books for a test period[.]" (emphasis added). The regulation, however, contains no language stating that an adjustment must be proposed at any time. Instead, ARSD 20:10:13:44 provides a mechanism for a company to show a "proposed" adjustment any time that new data becomes available. If adjustments were mandatory, ARSD 20:10:13:44 would not use the word "proposed."

The allowance of post-test year adjustments does not mean that only the most current data should be used for normalization. For example, the Amended Stipulation includes the normalization of bad debt expense, storm damage, and weather using something other than current data, and BHII did not object to the normalization of those items. BHII's argument that

[10] BHII's failure to cite any legal authority in support of this argument constitutes a waiver of the same. *Behrens v. Wedmore*, 2005 S.D. 79, ¶ 55,698 N.W.2d 555, 577.

the pension expense must be normalized from 2011-2015 is another example of BHII picking and choosing its different interpretations of law as necessary to benefit BHII.

In approving the normalization process and use of the 2010-2014 costs, the Commission found the following: that the Company's pension expense varies significantly; the remedy is to implement the five-year normalization process; and, based on the evidence presented to the Commission, the 2010-2014 time period was a fair window in which to normalize the Company's pension expense. These findings are not clearly erroneous and must be upheld.[11]

III. The Commission's approval of limited incentive compensation in the Amended Stipulation is not clearly erroneous because the substantial evidence presented to the Commission proved that such compensation is necessary and benefits customers.

The Commission's approval of $880,000 in incentive compensation in the Company's total costs is a factual finding and, therefore, the Court applies the clearly erroneous standard of review. *In re Otter Tail Power*, 2008 S.D. 5, ¶ 26; *see also BHII Brief* at 30 (agreeing that the clearly erroneous standard of review applies). The Court must affirm the Commission's approval of incentive compensation as part of the Amended Stipulation unless the Court is definitely and firmly convinced that the Commission made a mistake.

The Commission did not make any mistake regarding the incentive compensation issue. The Commission received and reviewed substantial evidence, including from Ms. Laura Patterson, Mr. Kyle White, and Staff witness Mr. David Peterson. Ms. Patterson and Mr. White further incorporated numerous studies and market analysis in their testimony regarding the Company's compensation plan. As such, the Commission's decision that the incentive

[11] The Commission, as a matter of law, was not required to use the data from 2011-2015 for the normalization. Thus, even if the Commission's approval of the 2010-2014 costs was a conclusion of law (which it is not), the approval of the 2010-2014 costs results in a just and reasonable rate and should be upheld.

compensation included in the Amended Stipulation did not render the Amended Stipulation unjust and unreasonable is not clearly erroneous.

A. The Commission's finding that the Company met its burden to prove that the rate is just and reasonable is not clearly erroneous.

BHII apparently argues that the Commission improperly approved the inclusion of the incentive compensation because Black Hills Power did not meet its burden of proof before the Commission. Specifically, BHII alleges that the only evidence supporting such inclusion was the allegedly "conclusory" testimony of Kyle White. BHII is correct that Black Hills Power bore the burden to prove before the Commission that its proposed rates were just and reasonable, and that the underlying costs or charges were prudent, efficient, economical, and were reasonable and necessary to provide service to its customers in South Dakota. SDCL 49-34A-11, and 49-34A-8.4. This burden at the Commission level must be proven by a preponderance of the evidence, meaning that the evidence supporting Black Hills Power, "when weighed with that opposed to it, has more convincing force and from which it results that the greater probability of truth lies therein." *Schaffer v. Edward D. Jones & Co.*, 1996 S.D. 94, ¶ 15, 552 N.W.2d 801, 807 n.2.

But BHII is incorrect that the Company failed to meet this burden. BHII alleges that Mr. White did not have sufficient support for his testimony before the Commission on incentive compensation. This is misleading. As stated below, the Company presented substantial evidence to the Commission on the incentive compensation issue:

> BHII completely disregards the testimony of Laura Patterson, which is fatal to BHII's argument. Ms. Patterson was the Director of Compensation, Benefits and Human Resources Information Systems for Black Hills Service Company, a wholly-owned subsidiary of Black Hills Corporation, with over 23 years of experience in compensation and benefits. *Patterson Direct* at 1, Co. App. A-4.
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> The Company must attract, motivate, and retain employees. *Id.* at A-7. To that end, the Company employs a compensation plan that is competitive and promotes

overall performance for the Company. *Id.* at A-7-8. The Company's compensation program includes a base salary and variable pay, which includes the Annual Incentive Plan ("AIP"). *Id.* at A-8. The AIP is consistent and competitive with the market.[12]

One of the Company's long-term incentive programs is a restricted stock award, which is offered to key employees on a limited basis. *Id.* at A-17. The restricted stock program is a retention tool and vests ratably over a three-year period, thereby ensuring retention of the key employees eligible for the program. *Id.* Independent studies support the use of a restricted stock plan. *Id.* at A-18-19. Moreover, public utility commissions in Nebraska, Iowa, Wyoming, and Colorado have approved similar compensation plans. *Id.* at A-25.

The Company also offered the rebuttal testimony of Mr. White, who relied on and explicitly adopted the testimony of Ms. Patterson. *White Rebuttal* at 11, Co. App. A-39. Mr. White disputed BHII's argument that restricted stock and performance plan expenses are tied to the Company's financial performance. *Id.* at A-40. Specifically, the restricted stock has a three-year vesting period and once such stock "is granted to a key employee the only requirement for a pay-out is the employee's continued employment." *Id.*

Mr. White also testified that "[n]o evidence was presented that the total compensation paid to employees was imprudent or unreasonable based upon what the market pays employees for similar positions." *Id.* at A-36. Mr. White testified that the Wyoming Public Service Commission and the Colorado Commission both accepted 100 percent of the requested incentive compensation in the Company's revenue requirement. *Id.* at A-40; *Evid. H'rg Tr.* at 35, Co. App. A-74.

BHII tried, unsuccessfully, through cross-examination, to get Mr. White to agree that the restricted stock is performance-based compensation. *See generally id.* at A-122-27. On redirect, Mr. White clarified the issue and testified that the restricted stock plan is not performance-based compensation but rather a "retention vehicle for key employees." *Id.* A-117 & A-129-30.

In addition to the Company's evidence, Mr. Peterson, who testified on behalf of Staff, rejected BHII's position that the $880,000 should be excluded because "the incentive compensation exclusion embodied in the settlement is essentially the same type of exclusion the Commission has approved for BHP in prior base rate case

[12] For example, in 2009, Towers Watson conducted an independent review of the Company's compensation program to ensure that the program was consistent with the market. *Patterson Direct* at 6, Co. App. A-9. The Company has also used surveys to review its compensation program. *Id.* at A-10. In addition, the Company reviews the pay structure annually to ensure the structure reflects market conditions. *Id.* AIP is essential to meeting these goals because the Company's base pay is lower than market levels. *Id.* at A-14.

settlements and for other South Dakota utilities." *Peterson Direct* at 17-18, BHII App. A-322-23. Mr. Peterson further explained that the incentive compensation had a number of benefits to customers, and the Commission had approved such plans in prior years. *Evid. H'rg Tr.* at 285-88, Co. App. A-108-11. Finally, Mr. Peterson applauded the Company's incentive compensation plan because it does not contain a number of financial triggers (i.e., incentives are paid only if certain corporate financial targets are met) which other utilities' plans have. *Id.* at A-109.

In its Final Decision, the Commission acknowledged but found as unpersuasive BHII's arguments[13] regarding the incentive compensation. *Final Decision* ¶ 39; BHII App. A-11. As findings of fact, the Commission found the following: the Company excluded $660,000 of incentive compensation, which was tied to the Company's financial results; the Company needs to offer incentive compensation plans to remain competitive; and Staff resolved any issues regarding a connection between the incentive compensation and the Company's financial performance. *Id.* ¶¶ 37-40, A-11. Viewing all of the evidence presented, the Commission found "that the incentive compensation plan included in the Amended Stipulation does not render the Amended Stipulation unjust and unreasonable." *Id.* ¶ 40, A-11.

The Commission further found that including the $880,000 in incentive compensation was proper: "No statute or rule precludes the inclusion of employee incentive compensation in the utility's cost of service and revenue requirement. The Commission's decision whether to allow incentive compensation and, if so, subject to what limitations are judgment calls concerning what meets the just and reasonable standard." *Id.* ¶ 12; A-20.

As the above evidence demonstrates, Mr. White's testimony is not conclusory. BHII, ignoring this evidence, cites *In re One-time Special Underground Assessment by Northern States Power Co. in Sioux Falls*, 2001 S.D. 63, 628 N.W.2d 332 ("*NSP*") as being "instructive" to this Court's determination on incentive compensation. *NSP*, however, confirms that the Commission's approval of the incentive compensation was not clearly erroneous.

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[13] BHII argued that the entire $1.554 million in incentive compensation should be excluded because the incentive compensation plan, including restricted stock, is tied to operating and financial performance. *Kollen Direct* at 37, BHII App. A-170. Mr. Kollen provided no analysis on whether the restricted stock plan is essential to recruit and retain key employees or the financial ramifications for the Company and customers if the Company has to increase base salaries instead of offering incentive compensation. *Id.*; *Evid. Hr'g Tr.* at 184, Co. App. A-92.

In *NSP*, the Commission found that NSP was not entitled to recoup a surcharge to all Sioux Falls customers to cover the cost of burying overhead electrical lines. The Company's only evidence before the Commission was conclusory testimony by an NSP executive stating simply that the burial benefited all Sioux Falls customers. *NSP*, 2001 S.D. 63, ¶ 11. Contrary evidence offered by both Staff and customers found that the burial of lines did not improve safety or the reliability of services. In upholding the Commission, the Supreme Court found that NSP failed to prove that the burial of the lines benefitted all customers. *Id.* ¶ 12.

The facts in this case are not like those in *NSP*. As shown above, Mr. White's testimony was not conclusory as he incorporated the testimony of Ms. Patterson and relied on numerous studies finding that incentive compensation plans are necessary and proper expenses for companies such as Black Hills Power. Indeed, the Commission regularly approves costs which are supported by independent studies. *See, e.g.*, *In re Nw. Bell Tel. Co.*, 68 P.U.R.4th 436, 448, 1985 WL 1205459 (S.D.P.U.C. 1985), Co. App. A-174 (finding that the utility should be allowed to recover the costs of management bonuses when such bonuses were found to be necessary from a study); *see also In re Otter Tail Power Co.*, 30 P.U.R.4th 26, 1979 WL 461902 (S.D.P.U.C. 1979), Co. App. A-143 (finding that the rate was reasonable based on studies reviewing the company's capital structure). Staff also testified in favor of approving the incentive compensation. Other evidence indicated that the Commission (and other public utility commissions) have approved similar compensation plans.

After reviewing all of this evidence, the Commission found that the Company met its burden to prove that the greater convincing force of the evidence established that the rate, as a whole, was just and reasonable, and the Company's costs were efficient, economical, and reasonable and necessary to provide service to its customers in South Dakota. Indeed, no

contrary evidence supported by any facts showed differently. As such, the Commission's decision regarding incentive compensation is not clearly erroneous.

B. BHII's argument that the incentive compensation is a performance-based incentive is irrelevant.

BHII also argues that the incentive compensation is a performance-based incentive and, as such, the Commission's decision to approve the Amended Stipulation with the incentive compensation was clearly erroneous. Importantly, BHII has offered no legal basis to challenge the inclusion of incentive compensation regardless of whether such compensation is based on the Company's performance.

The Legislature has instructed the Commission to determine whether a utility has presented sufficient evidence that the overall rate is just and reasonable. SDCL 49-34A-6. The Commission need not follow any particular formula so long as the methods it uses, as a whole, do not produce an arbitrary result. *SDPUC v. Otter Tail Power Co.*, 291 N.W.2d 291, 293 (S.D. 1980); *App. of Montana-Dakota Util. Co. for Auth. to Est. Increased Rates for Elec. Serv.*, 278 N.W.2d 189, 191 (S.D. 1979). There is simply no legal authority that the Commission cannot approve a settlement which includes some incentive compensation, regardless of whether it is performance-based in nature.

Regardless, the Company's incentive compensation is a retention tool, not a performance-based incentive. *Patterson Direct* at 14, Co. App. A-17; *White Rebuttal* at 11-12, Co. App. A-40-41, *Evid. Hr'g Tr.* at 285-86, Co. App. A-108-09. The restricted stock program itself confirms this because the stock vests ratably over three years, at which time the only requirement for pay-out is the employee's continued employment. *Patterson Direct* at 14, Co. App. A-17; *White Rebuttal* at 12, Co. App. A-40. The Staff agreed with the Company that the

incentive compensation is not a performance-based incentive. *See, e.g.*, *Evid. Hr'g Tr.* at 285-86, Co. App. A-108-09. Besides the self-serving testimony of Mr. Kollen, who provided no analysis for his conclusion that the incentive compensation was tied to performance, BHII presented no evidence before the Commission that the incentive compensation is tied to performance.[14]

C. The Commission is not required to make a specific determination on each cost submitted in the Company's Application.

Finally, BHII contends that the Commission was required to make a specific determination whether the Company met its burden of proof on incentive compensation. *BHII Brief* at 26. This argument lacks any legal basis. Indeed, the statutes relating to public utility rates contain no such mandate for the Commission. *See generally* SDCL Ch. 49-34A. As stated above, the Commission must only determine whether the rate, as a whole, is just and reasonable.

Common sense also dictates this result. It would not make sense to require the Commission to determine that the Company has met a burden of proof on each and every expense contributing to a rate. A rate is arrived at only after considering a number of factors, costs, adjustments, expenses, and related items.[15]

Thus, the Commission's reasoning that no statute or rule precludes the inclusion of incentive compensation and that its decision to approve such a cost lies within its judgment in determining a just and reasonable rate must be upheld. Moreover, the inclusion of incentive

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[14] Before this Court, BHII argues that the restricted stock incentive is linked to performance because the Company's Omnibus Compensation Plan uses the word "award." *See BHII's Brief* at 31-33. The use of the word "award" is irrelevant to the actual terms of the restricted stock plan, which, as stated above, provides that the restricted stock vests in a three-year period after which the employee only needs to continue working to receive a pay-out.

[15] Further, even if the Court finds that the Company has to meet a burden of proof for each cost included in a rate, the Company certainly met that burden here, as stated in the summary of the evidence on incentive compensation.

compensation in the Amended Stipulation is fully supported by the record. As such, the Commission's decision to approve the Amended Stipulation, which included the incentive compensation cost, was not clearly erroneous and must be affirmed.

CONCLUSION

Black Hills Power, in conjunction with Staff as a co-settling party, produced evidence to the Commission sufficient to satisfy the Company's burden of proof pursuant to SDCL Ch. 49-34A. In particular, during the Evidentiary Hearing, the parties to the Amended Stipulation established that the underlying costs of the rates and charges that result from the Amended Stipulation are prudent, efficient, economical, and are reasonable and necessary to provide service to the Company's customers in South Dakota. The adjustments made to the test year were appropriate and proper under the South Dakota statutes and rules and were in conformance with the decades old practice of Staff and the Commission. The resulting rates are just and reasonable and the Company is entitled to approval of the rates as filed in the Amended Stipulation.

Black Hills Power respectfully requests that the Court affirm the Commission's Final Decision.

Dated this 18th day of September, 2015.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 18th day of September, 2015, a true and correct copy of Appellee Black Hills Power, Inc.'s Brief and Appendix in the above-entitled matter, was electronically mailed and/or electronically served and a courtesy hard copy of Appellee Black Hills Power, Inc.'s Brief was placed in first-class U.S. Mail, postage prepaid, to the following persons:

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Appellee Black Hills Power, Inc.'s Brief and Appendix was also electronically filed this date with the Hughes County Clerk of Courts, 104 East Capitol Ave., Pierre, SD 57501.

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