IN THE SUPREME COURT

OF THE

STATE OF SOUTH DAKOTA

IN THE MATTER OF THE APPLICATION OF BLACK HILLS POWER, INC. FOR AUTHORITY TO INCREASE ITS ELECTRIC RATES

#27751

Appeal from the Circuit Court, Sixth Judicial Circuit
Hughes County, South Dakota
The Honorable Mark W. Barnett
Circuit Court Judge

APPELLANTS' REPLY BRIEF

Notice of Appeal was filed on February 8, 2016

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I. INTRODUCTION

Black Hills Industrial Intervenors ("*BHII*") appeal from the circuit court's Order affirming the South Dakota Public Utility Commission's (the "*Commission*") decision to approve the Amended Settlement because that decision was contrary to law for the following reasons: (1) the Amended Settlement incorporates adjustments that were submitted after Black Hills Power, Inc. ("*BHP*"), filed its application to increase rates, in violation of the plain language of ARSD 20:10:13:44; (2) if this Court rejects the previous argument, the Amended Settlement uses a pension normalization that does not incorporate the most recent information on pension expense; and (3) regardless of the resolution of the first two arguments, the Amended Settlement incorporates incentive compensation that was not adequately supported by the record. This reply brief addresses matters raised in the Commission's brief (cited herein as "*Comm'n Br.*") and BHP's brief (cited herein as "*BHP Br.*").

II. ARGUMENT

A. Only BHII's interpretation of ARSD 20:10:13:44 conforms to the broad regulatory scheme, the plain language of the rule, and the doctrine of the last antecedent.

BHII's interpretation of ARSD 20:10:13:44 fits seamlessly into the larger regulatory scheme, which is necessary when interpreting a rule. *In re Certification of a Question of Law from U.S. Dist. Court, Dist. of S. Dakota, S. Div.*, 2014 S.D. 57, ¶ 8, 851 N.W.2d 924, 927 ("[I]t is fundamental that the words of a [rule] must be read in their context and with a view to their place in the overall [regulatory] scheme." (internal quotation marks and citation omitted)). ARSD Ch. 20:10:13 is primarily concerned with the contents of the application to increase rates filed by the utility, and § 20:10:13:44

covers the statement of the utility's cost of service, which is a significant component of the utility's application. Understanding how § 20:10:13:44 functions within the chapter and interacts with other rules is critical to interpreting the rule's meaning.

Several rules confirm the proper application of ARSD 20:10:13:44.[1] Reading ARSD 20:10:13:44 together with ARSD 20:10:13:104 makes clear what the rules contemplate, namely, that the utility can include up to three test periods at the time of the filing of its rate case; one historical test-period and two forecasted test periods.[2] Here, BHP chose to include only one historical test-period in the filing of its application. By failing to avail itself of the benefits of § 20:10:13:104, BHP cannot now lawfully maintain that it can "submit post-test year adjustments that become known and measurable within 24 months following the test year," *BHP Br.* at 2; *see also Comm'n Br.* at 10. Permitting BHP to do so would obviate any reason to file a forecast test year under § 20:10:13:104. BHP and the Commission's approach is, in its simplest form, an attempt to create a hybrid of §§ 20:10:13:44 and 20:10:13:104, rendering the second full paragraph of § 20:10:13:104 meaningless. This outcome demonstrates why BHP and the

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[1] BHP erroneously claims that BHII waived arguments relating to ARSD 20:10:13:46, ARSD 20:10:13:104, and SDCL 49-34A-7. *BHP Br.* at 14. BHII discussed these rules in both its post-hearing brief to the Commission, its circuit court opening brief, and during oral argument before the court. *BHII Post-Hrg. Br.* at 13 n.28, 17; *BHII Cir.Ct. Opening Br.* at 13 n.5, 16; *Oral Arg. Tr.* at 30. And BHII discussed the statute at oral argument in circuit court when responding to a question by the court. This argument, therefore, was not "raised for the first time on appeal." *Kansas Gas & Elec. Co. v. Ross*, 521 N.W.2d 107, 116 (S.D. 1994).

[2] For example, if a utility filed for a rate increase on January 1, 2016, using a historical test-period of January 1, 2015 through December 31, 2015, and the utility proposed an effective date for new rates of January 1, 2017, then the utility could, under ARSD 20:10:13:44, submit cost of service information for the non-historical test-period of January 1, 2016 through December 31, 2016, and the non-historical test-period of January 1, 2017 through December 31, 2017.

Commission's interpretation of § 20:10:13:44 is inconsistent with § 20:10:13:104. *See BHP Br.* at 15.

Likewise, reading ARSD 20:10:13:44 alongside ARSD 20:10:13:46 further supports BHII's interpretation. Section 20:10:13:46 requires that the supporting data relied upon by the utility, other than the data contained in statements A through R, must be limited to the test period. ("Such data shall be limited to the test period prescribed in § 20:10:13:44."). Limiting the other data to the test period and requiring it to be filed with the application fits with BHII's construction of § 20:10:13:44. This construction limits proposed adjustments to those that become known and measurable during the period between the end of the test period and the date the utility files its application and requires those adjustments to be "shown separately" in its cost of service. If, as BHP and the Commission say, the purpose of § 20:10:13:44 is to obtain the most up to date adjustments (without any consideration for the ability of other parties to review those adjustments), then the only way to allow for additional data to come in under § 20:10:13:46 and its specific limitation is to utilize multiple test periods as contemplated by §§ 20:10:13:44 and 20:10:13:104. BHP and the Commission fail to adequately explain this point, and BHP instead argues—without support or analysis—that § 20:10:13:46 is "wholly unrelated to the adjustments passage of § 20:10:13:44." *BHP Br.* at 15. Their interpretation requires that the rules be considered in isolation, contrary to well-established South Dakota law regarding legal construction. *See Klein v. Sanford USD Med. Ctr.*, 2015 S.D. 95, ¶ 13, 872 N.W.2d 802, 806 ("We do not read words or phrases in isolation; rather, the words of a [rule] must be read in their context and with a view to

their place in the overall [regulatory] scheme." (internal quotation marks and citation omitted)).

The definition of "test period" in ARSD 20:10:13:01(11) is also wholly consistent with BHII's interpretation. The second half of the definition states 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." § 20:10:13:01(11). This language mirrors the second passage in ARSD 20:10:13:104: "the utility, in addition, may submit cost of service information for a non-historical test period beginning no later than the proposed effective date of the new rates." § 20:10:13:104. Contrary to BHP's assertion, *BHP Br.* at 14, the "additional material" mentioned in the definition of test period refers to the cost of service information for a non-historical test period contemplated in § 20:10:13:104, not the adjustments discussed in ARSD 20:10:13:44, because the "additional material" is the data projected for the non-historical test period.

Furthermore, when ARSD 20:10:13:44 is read as a whole, the plain language of the rule does not, as BHP and the Commission argue, contain "two distinct passages." In fact, the rule contains one unbroken passage that discusses the "statement of the cost of service," which is a key component of the utility's application to increase rates. The entire rule discusses what must be, and what may not be, included with a utility's statement of its cost of service. Because most of ARSD Ch. 20:10:13, including § 20:10:13:44, is concerned with the contents of the application filed by the utility, the rule need only refer to "the filing" to indicate the application, and need not include the exact word "application." *See Comm'n Br.* at 13-14.

The rule also references data that must be filed with the application as laid out in ARSD 20:10:13:40 and 20:10:13:43 and states that proposed adjustments to book costs must be "shown separately" from the cost of service data filed with the application. ARSD 20:10:13:44. There is no reason for the rule to specify that adjustments must be shown separately from other cost of service data if those adjustments can be filed long after the application is filed.[3] This is why BHP's argument relating to the doctrine of the last antecedent falls flat. The entire rule is about the utility's cost of service included in its application. Hence, "at the time of the filing" refers to the filing of the application, not the filing of a proposed adjustment. It is unnecessary to employ the doctrine of the last antecedent because the meaning of "at the time of the filing" is apparent when the rule is read in its proper context.

But even if the doctrine should be applied, it must be done properly. As this Court previously observed:

> [The Court] "long ago" adopted the rule known as the "Doctrine of the Last Antecedent" which states: "[i]t is the general rule of statutory as well as grammatical construction that a modifying clause is confined to the last antecedent *unless there is something in the subject matter or dominant purpose which requires a different interpretation.*"

Rogers v. Allied Mut. Ins. Co., 520 N.W.2d 614, 617 (S.D. 1994) (emphasis added) (quoting *Kaberna v. Sch. Bd. of Lead-Deadwood Sch. Dist. 40-1*, 438 N.W.2d 542, 543 (S.D. 1989)). The quoted caveat, which was omitted from BHP's responsive brief,

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[3] It would also be inconsistent with ARSD Ch. 20:10:13's overall filing scheme which, as BHII has already shown, requires that all information and adjustments be included at the time of the filing. *See, e.g.*, ARSD 20:10:13:96 ("If the filing public utility claims any adjustments to book figures, the cost of service based upon the claimed adjustments shall be shown on a separate schedule."). Language such as "shown separately" and "separate schedule" are superfluous if such adjustments are filed on a date other than the application date.

specifically directs the reviewing court to consider the "subject matter or dominant purpose" of the rule when applying the doctrine. In the case of ARSD 20:10:13:44, the "subject matter" of the rule is the utility's cost of service, and the "dominant purpose" of the rule is to explain what must be, and what may not be, contained in it. Thus, proper application of the doctrine of the last antecedent also supports BHII's interpretation of § 20:10:13:44.[4]

BHP and the Commission's own description of their interpretation of ARSD 20:10:13:44 demonstrates why they are incorrect. Throughout their briefs, they state that a utility can "submit post-test year adjustments that become known and measurable within 24 months following the test year," *BHP Br.* at 2; *see also BHP Br.* at 12, 14; *Comm'n Br.* at 10, 12, 15, 28. Their interpretation though blatantly conflicts with the plain language of the rule and requires this Court to add the words "of the adjustment" after the phrase "at the time of the filing."

Equally confusing is BHP and the Commission's contorted application of ARSD 20:10:13:44. To make its interpretation workable, the Commission has had to impose a "cut-off date" after which no adjustments are allowed—a procedure that appears nowhere

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[4] BHP also conflates the two distinct standards regarding the proper level of deference an agency should be afforded in interpreting relevant statutes and its own rules. *BHP Br.* at 11. "The construction and interpretation given a statute by an administrative body charged with its administration is entitled to great weight." *In re Sales & Use Tax Refund Request of Media One, Inc.*, 1997 S.D. 17, ¶ 10, 559 N.W.2d 875, 878 (alteration, internal quotation marks, and citation omitted). BHII's appeal does not concern the Commission's interpretation of the relevant statute, but rather concerns the Commission's interpretation of ARSD 20:10:13:44. When interpreting its own rule, an agency is only given deference in certain situations as further explained in BHII's opening brief, and even then the agency is only given a "reasonable range of informed discretion" and not great weight. *Nelson v. Bd. of Dentistry*, 464 N.W.2d 621, 624 (S.D. 1991). Finally, the language in the rule is also not "technical in nature," *BHP Br.* at 11, but rather concerns procedural issues surrounding discovery that are within a court's expertise, not the Commission's.

in the rule, has a dramatic impact on the due process rights of ratepayers and is a violation of South Dakota law. *In re Petition for Declaratory Ruling re SDCL 62-1-1(6)*, 2016 S.D. 21, ¶ 9, 877 N.W.2d 340, 344. As the circuit court acknowledged in its Order, BHII was not aware that the Commission set a cut-off date for adjustments until oral argument before the court. *Order* at 20, App. A-22. Once BHII's counsel learned of the cut-off date, counsel immediately raised the secret nature of the cut-off date in his closing statement. *Oral Arg. Tr.* at 67-68, Reply App. A-4-5. The Commission's citations in its brief to various dates is unhelpful because the Commission does not explain how the particular "cut-off date that the parties agreed to" (which is how counsel for the Commission characterized it during oral argument) was publicized to the two intervenor groups or the general public. *Oral Arg. Tr.* at 59, App. A-103. In fact, there was no notice to anyone (including BHII) of this mysterious date.

BHII acknowledges that adjustments to book costs have the potential to lower as well as increase rates.[5] That is why, in an effort to show the magnitude of the potential rate impact in this case, BHII included in its opening brief a calculation of the impact, excluding both upward and downward adjustments filed after the date of the application. *BHII S. Ct. Opening Br.* at 9 n.4. Importantly, BHII's calculation removes both (1) adjustments to test-year book costs submitted by BHP after filing its application (referred to in BHII's opening brief as "*Post-Filing Adjustments*") and (2) new costs that were not actually adjustments to test-year book costs at all, neither of which are permitted by the provisions of ARSD 20:10:13:44. Contrary to BHP and the Commission's contentions,

[5] A utility has every incentive to adjust costs upward and not downward, which is why BHII is not concerned that its interpretation may prevent a utility from filing certain downward adjustments.

BHP Br. at 22; *Comm'n Br.* at 21, § 20:10:13:44 *does* distinguish between adjusted costs and new costs. The rule only allows "adjustments to book costs" that meet the two tests described above. *Id.* Post-Filing Adjustments are not permitted (and were backed out of BHII's calculation) because they were not known and measurable at the time BHP filed its application. New costs are not permitted (and were likewise excised from BHII's calculation) because those costs do not relate back to book costs reflected in the test period.

In sum, BHII's interpretation of ARSD 20:10:13:44 should be adopted because this interpretation comports with the plain language of the rule, the wider regulatory scheme, and policy concerns.

B. BHII's pension-expense normalization more accurately reflects current costs and thus leads to more reasonable rates.

If the Commission prevails in its interpretation of ARSD 20:10:13:44, BHII asserts, in the alternative, that the Commission should use the most recent pension expense data in calculating the utility's cost of service. BHII has argued for the use of a 2011-2015 normalization of pension expense because that average is closer to the 2015 actual expense than the 2010-2014 normalization average the Commission adopted.[6] BHII submits that this approach is more consistent with the Commission's emphasis on up-to-date costs in this case. In fact, the Commission claims that, "[t]he rates charged to customers should reflect the costs incurred by the utility on a prospective basis so that the rates, when they go into effect, provide sufficient revenue to cover the actual prudent

[6] BHP's actual pension expense for 2015 was $2,056,581. *Thurber Rebuttal Test. & Ex.* at 22 (Jan. 15, 2015) ("*Thurber Rebuttal*"). The five-year average for 2010-2014 is $2,336,305, *Thurber Rebuttal* at 21, which is $279,724 greater than the 2015 expense. The five-year average for 2011-2015 is $2,162,451, *BHII Post-Hrg. Br. to the Commission* at 53, which is $105,870 greater than the 2015 expense.

costs incurred to supply safe, reliable electric service to ratepayers." *Comm'n Br.* at 22. But when it comes to this pension-expense decision (that could decrease the revenue requirement, and accordingly decrease customer rates), the Commission is apparently not interested in the most up-to-date costs, even though those costs were introduced in rebuttal testimony and thus were part of the record and available for the Commission to consider.[7] If the Commission's interpretation of § 20:10:13:44 prevails, then the pension normalization that best reflects the most current year's pension costs is the amount that would produce the most just and reasonable rates, and is therefore the normalization period that should be used.

BHP states that ARSD "20:10:13:44 does not require a utility to adjust a cost if data becomes known after an application is filed." *BHP Br.* at 27. This statement demonstrates the unreasonable level of control that a utility has over the information in a rate proceeding under BHP and the Commission's interpretation of the law. In their view, a utility is able to file adjustments to its cost of service until the Commission's fictional cut-off date, and the utility gets to decide which costs it chooses to adjust or not adjust.[8] Under this scenario, parties are only given a limited opportunity to be heard and review adjustments to ensure such adjustments are reasonable and lack any ability to test whether other adjustments should have been proposed by the utility. By contrast, if all adjustments to book costs are filed with the application, parties are able to fully review

[7] And even though the normalized 2011-2015 pension expense would be in excess of the 2015 actual pension expense. *Thurber Rebuttal* at 22-23.

[8] BHII agrees with BHP in footnote 11 of its responsive brief that there is "no distinction" between the Wyodak expense adjustment and the pension normalization, because both were submitted after the Commission's cut-off date. This is why those adjustments should have been treated equally by the Commission in either adjusting or not adjusting the revenue requirement.

those adjustments for reasonableness. In addition to its consistency with the plain language of § 20:10:13:44, BHII's interpretation also leads to a more fair and equitable rate case proceeding for all parties.

C. BHP did not meet its burden of proof for the amount of incentive compensation it sought to recover through rates.

As BHII argued in its opening brief to this Court and to the circuit court, all three issues on appeal should be reviewed *de novo*. *BHII Cir. Ct. Opening Br.* at 4, 23-27; *BHII S. Ct. Opening Br.* at 29 n.10. The incentive compensation issue is subject to *de novo* review because the Court must determine "whether the uncontroverted facts or the facts as established satisfy the legal standard of proof," which is a "mixed question of law and fact, reviewable de novo." *Erdahl v. Groff*, 1998 S.D. 28, ¶ 30, 576 N.W.2d 15, 21 (reviewing agency decision); *BHII S. Ct. Opening Br.* at 29.

BHII's argument regarding incentive compensation concerns the amount of compensation that BHP seeks to recover in rates, and whether BHP met its burden to submit sufficient evidence to support that cost. BHII agrees that BHP can recover the cost of incentive compensation from ratepayers, if that cost is adequately supported in the record. That is why BHII does not cite to the testimony of Laura Patterson, who testified about the need for an incentive compensation program, a fact that BHII does not dispute. But in order to justify recovering its incentive-compensation adjustment from ratepayers, BHP must provide more evidence to support the amount of compensation than a table of unsubstantiated figures that contained no underlying work papers and did not reference any other documents. ARSD 20:10:13:44 ("Proposed adjustments to book costs . . . shall be fully supported, including schedules showing their derivation, where appropriate."). Because BHP failed to carry its burden of proof on the issue of incentive compensation,

BHII requests that the $0.888 million in compensation be excluded from rates. If this Court agrees, then BHP would still be allowed to recover approximately $2,235,297 in incentive compensation expenses.

III. CONCLUSION

For the reasons discussed herein and in BHII's opening brief, this Court should reject BHP and the Commission's arguments, reverse the circuit court's Order and remand the case for further proceedings. BHII renews its request for oral argument.

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