Volume 2A

Testimony and Schedules of Witnesses:

Bernadeen Brutlag

Depreciation Allocation
Depreciation Expense
Corporate Allocations
Economic Development

Before the South Dakota Public Utilities Commission
State of South Dakota

In the Matter of the Application of Otter Tail Corporation
d/b/a Otter Tail Power Company
For Authority to Increase Rates for Electric Utility
Service in South Dakota

Case No. EL08-_____

Exhibit___

DEPRECIATION ALLOCATION, DEPRECIATION EXPENSE, CORPORATE ALLOCATIONS & ECONOMIC DEVELOPMENT

Direct Testimony and Exhibit of

BERNADEEN BRUTLAG

October 31, 2008

TABLE OF CONTENTS

I. INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Bernadeen C. Brutlag, 215 South Cascade Street, Fergus Falls, Minnesota 56537.

Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR POSITION?

A. I am employed by Otter Tail Power Company ("Otter Tail Power," "OTP" or the "Utility") as Manager, Regulatory Services.

Q. PLEASE SUMMARIZE YOUR QUALIFICATIONS, DUTIES, AND RESPONSIBILITIES.

A. I graduated summa cum laude from Moorhead State University, now Minnesota State University, Moorhead, Minnesota, in 1984 with a B.S. degree in Accounting. I am also a Certified Public Accountant (inactive) in Minnesota. I am a member of the Minnesota Society of Certified Public Accountants and the Institute of Management Accountants. I have been employed by OTP since 1984. From 1984 until 1989 I was Depreciation Analyst, responsible for conducting and obtaining approval for the results of depreciation studies. From 1989 until 1993, I was Senior Regulatory Analyst. My primary responsibilities in this position were preparing annual cost of service studies for the three state jurisdictions where OTP provides service (South Dakota, North Dakota, and Minnesota), and other regulatory and financial analyses. In 1993, I was named Manager of Regulatory Analysis and Compliance. Since 1998, I have been Manager, Regulatory Services, with responsibility for the Utility's revenue requirements, rate administration, regulatory compliance, rate design, load research, and overall regulatory policy.

Q. FOR WHOM ARE YOU TESTIFYING?

A. I am testifying on behalf of OTP.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony has four parts. First, I explain a proposed change in allocation method for accumulated depreciation and depreciation expense. Second, I will discuss adjustments to depreciation expense and accumulated depreciation for known changes in depreciation rates occurring after the 2007 Actual Year. Third, I will explain the corporate allocations used in this proceeding. Finally, I will discuss the Company's economic development program. Mr. Peter Beithon uses the results of my testimony in preparing the overall financial schedules for the rate case.

II. ALLOCATION OF DEPRECIATION

Q. IS OTP PROPOSING A CHANGE IN THE JURISDICTIONAL ALLOCATION OF DEPRECIATION?

A. Yes.

Q. PLEASE SUMMARIZE THE PROPOSED CHANGE.

A. Since OTP's last rate case, for reasons that I will explain, Accumulated Depreciation and Deprecation Expense have been directly assigned to each jurisdiction that OTP serves. I am proposing to allocate both of these items using the same allocation factors used for allocating Electric Plant in Service.

Q. WHY WERE THESE TWO ITEMS PREVIOUSLY DIRECTLY ASSIGNED TO JURISDICTIONS?

A. The property owned by OTP serves all jurisdictions and the allocation of property depends upon usage levels of the customers in the regulatory jurisdictions served by the Utility. OTP's service territory is contiguous, covering parts of the three states in which we provide service. The operating characteristics affecting Utility property are similar throughout OTP's service territory. The property accounting rules and functions performed by the property are uniform throughout the system. All of these factors support using a uniform allocation methodology in each jurisdiction. On the other hand, for a period of time in the past there existed among the three jurisdictions served by the Utility a significant difference in accounting for allowed depreciation expense (recovery of capital), the primary component of accumulated depreciation reserves,. During that prior period, each jurisdiction allowed depreciation expense based upon significantly different depreciation parameters. Consequently, in 1983, the Company adopted a depreciation accounting process that determined the depreciation expense to be assigned to each jurisdiction according to the then allowed depreciation procedures.

Q. ARE THERE STILL DIFFERENCES IN ALLOWED DEPRECIATION RATES AMONG JURISDICTIONS?

A. There are no longer differences in the salvage and remaining lives used to calculate depreciation rates. The North Dakota Public Service Commission, in Docket PU-401-88-374, by Order dated December 20, 1988, adopted the same parameters that the Minnesota Public Utilities Commission uses to develop annual depreciation rates. Shortly thereafter, OTP began using these same depreciation parameters to calculate depreciation rates for South Dakota. Therefore, since 1989, nearly all of OTP's depreciation expense has been calculated using identical parameters for South Dakota, North Dakota, and Minnesota.

Q. WHY IS IT APPROPRIATE TO USE THE SAME PARAMETERS FOR ALL THREE STATES TO CALCULATE DEPRECIATION RATES?

A. As I mentioned earlier, OTP's electric generating and delivery system is fully integrated and has similar characteristics throughout its service territory. OTP conducts its annual depreciation reviews and the five-year depreciation studies, required by Minnesota Rules,[1] on the property and equipment in its entire system. Therefore, it is reasonable and in fact desirable to use consistent depreciation parameters and methods in all three states covered by OTP's service territory. By using a single set of depreciation parameters for our contiguous, fully integrated system, OTP's regulatory and accounting costs are lower and the South Dakota Public Utilities Commission ("Commission") and its Staff may use their resources for more significant matters.

Q. WHY WAS THE DIRECT ASSIGNMENT OF ACCUMULATED DEPRECIATION AND DEPRECIATION EXPENSE MAINTAINED EVEN AFTER OTP BEGAN USING IDENTICAL DEPRECIATION COMPONENTS FOR ALL THREE STATES?

A. Prior to OTP adopting the Minnesota approved depreciation components for use in the South Dakota and North Dakota jurisdictions, South Dakota and North Dakota had allowed different decommissioning rates and different depreciable lives on some property. It was, therefore, necessary to maintain jurisdictional direct assignments to recognize the fact that our customers in each state had provided different levels of decommissioning funds on common assets.

Q. WHY ARE YOU PROPOSING TO ELIMINATE DIRECT ASSIGNMENT?

A. For nearly 20 years, the depreciation parameters have been identical for all three states. Over time, the remaining life formula used by the states narrowed the differences created by the different depreciation parameters used long ago. While OTP has monitored the relationship of directly assigned reserves to

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[1] Minnesota Statutes § 216B.11 and Minnesota Rules 7825.0600 through 7825.0900 give authority to the Minnesota Public Utilities Commission to review and approve proper and adequate rates and methods for depreciation used by regulated electric utilities in that state. These Rules require utilities to review their depreciable rates annually and conduct depreciation studies at least every five years.

allocated Electric Plant in Service and made periodic adjustments to these jurisdictional amounts, over time, it is more difficult or nearly impossible to identify how much of the jurisdictional difference is because of past regulatory decisions and how much is caused by customer changes among the jurisdictions. I believe any difference in jurisdictional Accumulated Depreciation that may remain is too small to have a material impact on rates. Further, allocating accumulated depreciation and depreciation expense using the same allocation factors as Electric Plant in Service is appropriate and removes administrative requirements to monitor and account for directly assigned amounts.

Q. WHY SHOULD THE SAME ALLOCATION FACTORS USED FOR ELECTRIC PLANT IN SERVICE BE USED FOR ALLOCATING ACCUMULATED DEPRECIATION AND DEPRECIATION EXPENSE?

A. Depreciation expense is the cost of returning the investment in Electric Plant in Service to the shareholders. Accumulated depreciation is the amount of Electric Plant in Service depreciation paid over the life of the assets. Therefore, the jurisdictional factors used to allocate Electric Plant in Service and the associated depreciation and accumulated depreciation expense should all be the same. This change was also requested by OTP and approved in our most recent Minnesota rate case, Docket No. E017/GR-07-1178. If we do not use the same allocation factors for all three states, we will not be able to recover our revenue requirement.

Q. WHAT IS THE AMOUNT OF THE ADJUSTMENT IN THE TEST YEAR FOR THIS CHANGE?

A. The Test Year adjustment includes an increase in South Dakota Accumulated Depreciation of $5,192,394 (which acts to decrease rate base and, therefore, the revenue requirement) and an increase in South Dakota depreciation expense of $115,688. The net effect is a reduction in the revenue requirements.

III. DEPRECIATION RATES

Q. HAVE YOU MADE OTHER ADJUSTMENTS RELATED TO DEPRECIATION?

A. Yes. Separate from the jurisdiction allocation change discussed above, I am also proposing a total net depreciation expense reduction of $42,449.

Q. WHAT IS THE FIRST COMPONENT OF THAT ADJUSTMENT?

A. As I discussed in Section II above, depreciation parameters used to calculate depreciation rates are reviewed and approved each year by the Minnesota Public Utilities Commission. Those parameters are then used to calculate depreciation rates for all three states. I have adjusted the 2007 Test Year depreciation expense and accumulated depreciation to reflect the depreciation parameters approved by the Minnesota Commission for use in 2008. That adjustment resulted in an increase in South Dakota depreciation expense and accumulated depreciation of $3,487.

Q. DID YOU MAKE AN ADDITIONAL ADJUSTMENT?

A. Yes. I made an adjustment that reduces depreciation expenses by $45,936 to reflect changes proposed by OTP in our five-year depreciation study filed with the Minnesota Public Utilities Commission on August 29, 2008. While that five-year study has not been approved, we expect it be approved and because the changes lower our revenue requirement, it is appropriate that these proposals be reflected in our South Dakota rates. If these proposed parameters are changed by the Minnesota Public Utilities Commission before rates are approved in this proceeding, we request that the actually approved depreciation parameters be used in the rate setting process. Table 1 below shows the proposed changes in depreciation expense by function.

	Depreciation expense change
Production	$ 7,937
Transmission	(23,599)
Distribution	(9,704)
General	(20,570)
Total	($45,936)

Table 1

Q. PLEASE EXPLAIN THE $7,937 PRODUCTION ADJUSTMENT.

A. The primary component of this adjustment is driven by our proposal in the five-year depreciation study to extend the retirement date for OTP's three steam generating plants. The retirement date for Hoot Lake Plant Units 1 and 2 was extended two years to 2019, Big Stone Plant retirement date is proposed to be 2024, four years longer than its previous retirement date, and the retirement date for Coyote Station was also extended by four years to 2029.

Q. WHY HAVE THE EXPECTED RETIREMENT DATES FOR THESE THREE PLANTS CHANGED?

A. These plants provide low cost power for our retail customers; therefore, it is highly desirable to keep these plants in operation. In order to do that, however, it has been necessary to make capital investments in these plants. OTP witness Mr. Kyle Sem discusses several of these investments. Those investments have allowed the lives of these plants to be extended.

Q. IS THERE AN OFFSETTING ADJUSTMENT YOU ARE PROPOSING?

A. Yes. Along with setting new retirement dates for these three plants, OTP conducted a new decommissioning study as part of the five-year depreciation filing. This study showed an increase in expected decommissioning costs. Table 2 below shows the current composite depreciation rates (2008) for each plant, along with the new rates (2009) that include both the later retirement dates and the updated decommissioning costs.

Composite depreciation rate	Big Stone	Hoot Lake	Coyote	Net change
2008	2.89%	3.01%	2.44%	
2009	3.18%	3.01%	2.19%	
Change in annual expense (total system)	$392,848	$403	($377,940)	$15,311

Table 2

The table also shows that, while longer lives and increased estimated demolition costs are significant, the net result of the changes on depreciation expense for the three plants as a group is very small – a total system amount of $15,311 and $1,403 for South Dakota.

Q. WHAT OTHER ADJUSTMENTS CAUSED THE TOTAL PRODUCTION EXPENSE TO INCREASE BY $7,937?

A. In addition to the three steam plants, the Production function includes several small hydro-electric dams and peaking units. The depreciation expense change for all of these units combined makes up the remaining $6,534 for a total increase of $7,937.

Q. WHAT FACTORS CHANGED IN DEPRECIATION EXPENSE FOR TRANSMISSION PLANT?

A. I am proposing a reduction in depreciation expense for transmission of $23,599. The statistical analysis used in the five-year study showed that substation equipment is lasting longer than previously expected. This is the most significant cause for the reduction of depreciation expense for transmission.

Q. WHAT DID THE STATISTICAL ANALYSIS SHOW FOR DISTRIBUTION PLANT?

A. The analysis resulted in only a small reduction in depreciation expense for the distribution function ($9,704). Within the function were offsetting changes, such as an increase in removal costs for overhead lines that increased expense, higher salvage value for line transformers that reduced expense, a longer life and lower removal costs for underground services that reduced expense, and a shorter life for load management switches that increased expense.

Q. WHAT CAUSED THE $20,570 REDUCTION IN EXPENSE FOR GENERAL PLANT?

A. The reduction in depreciation expense is primarily caused by our proposal to extend the retirement date for our General Office building by ten years.

Q. PLEASE SUMMARIZE THIS SECTION OF YOUR TESTIMONY.

A. The proposed adjustments to 2007 Actual Year depreciation expense are an increase in expense of $3,487 to reflect the 2008 depreciation parameters and a decrease in expense of $45,936 based on the five-year depreciation study recently completed, for a net Test Year reduction of $42,449 from 2007 actual depreciation expense. Corresponding adjustments are made to accumulated depreciation.

Q. FINALLY, ARE THERE OTHER ADJUSTMENTS TO DEPRECIATION EXPENSE IN THIS CASE?

A. Yes. OTP witness Kyle Sem discusses several Test Year adjustments to electric plant in service, which have related adjustments to depreciation expense and accumulated depreciation. OTP witness Peter Beithon will incorporate the results of all of these adjustments into total revenue requirements.

IV. CORPORATE ALLOCATIONS

Q. WHAT IS THE PURPOSE OF THIS SECTION OF YOUR TESTIMONY

A. Mr. Tomas Brause briefly discusses the legal and operational structure of Otter Tail Corporation ("the Otter Tail Corporate Group" or "Corporate") and the pending reorganization to a holding company in his Direct Testimony. I discuss in more detail the functions of the Corporate Group and of the Utility, which does business as Otter Tail Power Company. I also describe the function of the Corporate Group and the proposed method for allocating corporate costs. I also sponsor the Corporate Cost Allocation Manual ("CAM"), a copy of which is included as Exhibit __ (BCB-1), Schedule 1.

Q. HOW ARE OTTER TAIL CORPORATION AND OTP STRUCTURED AT PRESENT?

A. The Utility is the same legal entity as Otter Tail Corporation. However, Otter Tail Corporation is organized and operates in many ways like a holding company even though it is not yet a holding company; and OTP operates like a subsidiary of Otter Tail Corporation, even though it is not yet a subsidiary.

Q. AFTER THE HOLDING COMPANY ORGANIZATIONAL STRUCTURE HAS BEEN FORMED INSTEAD OF THE CURRENT CORPORATE STRUCTURE, HOW, IF AT ALL, WOULD THAT AFFECT THE COST ALLOCATIONS AND MORE BROADLY THE REVENUE REQUIREMENT IN THIS PROCEEDING?

A. When Otter Tail Corporation becomes a holding company, the cost allocations and revenue requirements proposed in this case will remain the same. This is because Otter Tail Corporation and OTP operate as though there were a holding company structure today.

Q. WHAT FUNCTION DOES THE CORPORATE GROUP PERFORM FOR THE UTILITY?

A. Otter Tail's Corporate Group provides a corporate management function for the Utility, as well as for the unregulated subsidiaries that are part of Varistar (the parent company for the corporation's unregulated subsidiaries). The functions performed by the Corporate Group include:

- Pay Corporate taxes and prepare associated returns
- External financial reporting – filing of 10-Qs and 10-Ks
- Corporate accounting – reoccurring journal entries for things like dividends, interest expense, Board of Director expenses, amortization of financing costs
- Shareholder services
- Investor relations – meeting with rating agencies and equity analysts
- Corporate communications – all corporate-related communications including the production of the annual report
- Internal audit
- Corporate financing – debt and equity financings
- Determine executive compensation and benefits
- All legal-related functions
- Oversight of insurance and enterprise risk management

Q. HOW DOES THE CORPORATE GROUP COMPARE IN SIZE TO THE ENTIRE CORPORATION?

A. Otter Tail's Corporate Group is a small part of the total corporation. The Corporate Group has 53 employees out of a total of 4,300 employees for the entire corporation, including all subsidiaries, or about 1.2 percent of the total employees. Expenses of the Corporate Group in 2007 were $21.2 million while total consolidated corporation operating revenues were $1.2 billion dollars, and total consolidated corporation operating expenses were $1.1 billion. Thus, Corporate Group expense is less than 2 percent of either operating revenue or operating expense.

Q. CAN YOU CONTRAST THE FUNCTION OF OTTER TAIL CORPORATION CORPORATE GROUP WITH A SERVICES SUBSIDIARY RESIDING IN SOME UTILITY HOLDING COMPANIES?

A. Yes. Otter Tail's Corporate Group is not a services entity like the corporate services unit in Xcel Energy (Xcel Energy Services Inc.), for example. Otter Tail's Corporate Group does not process the Utility's invoices, customers' bills, nor does it do billing for the Utility. Nor does it manage the Utility's HR, IT, procurement, or provide services other than Corporate management services on behalf of the Utility. OTP contains within its own operating unit functions such as accounting, bill and invoice processing, IT, HR, supply chain, engineering, rates and regulation, payroll, marketing and sales, fuel and energy procurement, and customer service.

Q. HOW ARE THE COSTS OF THESE CORPORATE FUNCTIONS ALLOCATED TO OTP?

A. Costs of the corporate functions are allocated to the Utility using the allocation methodology described in the CAM. The allocations in the CAM are updated annually based on the most recent historic year available and applied to the next 12 months.

Q. HOW WERE THE COST ALLOCATION METHODOLOGIES DEVELOPED?

A. In developing its corporate allocation methodology, OTP considered the following goals:

1) The result should be fully allocated costing;

2) Costs should be directly assigned where possible;

3) If direct assignment is not possible, an indirect allocation will be made if there is a cost causative link to another cost category for which direct assignment is used;

4) When neither direct nor indirect cost causation can be found, a representative general allocator is used;

5) The result is equitable for customers and shareholders;

6) The method is easy to administer – no additional studies or data gathering is needed; and

7) The allocators have components that are based on verifiable public information, to the extent possible.

Q. PLEASE EXPLAIN THE ALLOCATION PROCESS IN MORE DETAIL.

A. Corporate costs can be charged to Varistar, charged to OTP, or kept at Corporate. The allocation process uses three steps. First, all labor and other costs that can be directly assigned to Varistar, Corporate Group, or OTP are identified. Members of the Corporate Group use timesheets to assign labor. Invoices and other costs are assigned as appropriate. In the 2007 Actual Year, 54 percent of all corporate costs were directly assigned to one of the three entities. Second, indirect allocators are used for certain functions. Indirect allocators are used where an indirect-cost causative linkage to another cost category or group of cost categories exists for which direct assignment or allocation is available. In the 2007 Actual Year, about 17 percent of corporate costs were indirectly allocated. The remaining corporate costs (29 per cent in the 2007 Actual Year) do not have an identifiable direct or indirect relationship to Varistar, Corporate Group, or OTP. Those costs are allocated using a General Allocator, which is composed of revenues, assets, and labor dollars, equally weighted.

Q. HOW MUCH OF THE TOTAL CORPORATE COSTS WERE PAID BY OTP IN 2007?

A. In the 2007 Actual Year, OTP was charged 31 percent of total corporate costs. The following Table 3 shows how corporate costs were charged in 2007.

CORPORATE COSTS	ACTUAL YEAR 2007	
Allocated to OTP	$6,599,861	31.07%
Allocated to Varistar	11,210,723	52.79%
Kept at Corporate	3,427,232	16.14%
Total 2006 Corporate Costs	$21,237,816	100.00%

Table 3

Q. HAVE YOU MADE AN ADJUSTMENT TO THE ACTUAL 2007 CORPORATE COSTS TO ARRIVE AT THE 2007 TEST YEAR?

A. Yes, I made two adjustments related to Corporate labor and labor related costs. First, I increased Corporate Group costs allocated to OTP by $216,426 to reflect the increases of salaries and wages that occurred after the end of the 2007 Actual Year. I also reduced the Utility portion of Corporate costs related to cash bonuses of the Corporate executive management by $315,784. This adjustment was made to Corporate labor costs allocated to OTP to be consistent with the proposed 25 percent cap on individual incentives as discussed by Mr. Peter Wasberg. These two offsetting adjustments result in a net decrease of $99,358 from actual 2007 corporate costs. South Dakota's share of this adjustment is a reduction of $9,283.

Q. WHAT PERCENT OF TOTAL CORPORATE CHARGES IS CHARGED TO OTP IN THE TEST YEAR, AS REDUCED BY $9,283?

A. In the 2007 Test Year, as adjusted, OTP is charged 30.6 percent of total corporate costs.

Q. PLEASE DESCRIBE THE GENERAL ALLOCATOR USED BY OTP.

A. The General Allocator used to allocate Corporate Group costs, not otherwise directly assigned or indirectly allocated, uses three equally weighted components: revenues, assets, and labor dollars.

Q. PLEASE DESCRIBE THE COMPONENTS OF THE GENERAL ALLOCATOR, BEGINNING WITH REVENUES AND ASSETS.

A. The source and items included in these two components are shown on Appendix A to the CAM (my Ex __ (BCB-1), Schedule 1). The revenues included are from continuing operations of the total corporation and OTP. The assets included are those reported in the business segment section of the 2007 Annual Report to Shareholders.

Q. BEFORE YOU DISCUSS THE LABOR DOLLARS COMPONENT, WHY WEREN'T EMPLOYEE FULL-TIME EQUIVALENTS USED INSTEAD?

A. I explained earlier the goals that OTP believes important. Besides the obvious goal that the resulting allocation must be equitable, the components used in the allocator should be auditable, relatively easy to obtain, and not create unnecessary additional administrative work. In order to calculate full time equivalents (FTEs), labor hours would need to be gathered from each subsidiary. That is not data currently gathered. Otter Tail Corporation operates as a very decentralized organization. Each of the 11 subsidiaries (and their subsidiaries) operates quite independently, keeping its own accounting and payroll system. Gathering this data from the diverse systems, and finding a way to ensure that the data is complete and accurate, would be a challenge, difficult to verify and time-consuming. In addition, some of the non-utility subsidiaries have operations that experience seasonal fluctuations that would interfere with the consistent application if FTEs rather than labor dollars were used as a component of the General Allocator.

Q. WHY NOT USE EMPLOYEE COUNT?

A. Employee counts are available, but OTP proposes instead using labor dollars as a component of the General Allocator. We do so for several reasons. First of all, we can reliably obtain labor dollar data easily without additional administrative work – it is data already being collected for reporting purposes. A second advantage is that it is part of the accounting information used in external financial reporting and, therefore, subject to review and audit. As mentioned above, each of Otter Tail Corporation's subsidiaries use their own accounting systems. The Corporate Group performs the consolidation process needed for external financial reporting using a consolidation software tool. As part of this process, the Corporate Group has defined a corporate chart of accounts. Each subsidiary maps (assigns) its individual accounts to accounts in the corporate chart of accounts. The mapping is reviewed annually by Corporate employees. This allows for a consistent set of accounting data in a format that is used to complete external financial statements.

Another advantage of using labor dollars is that each subsidiary's labor dollars have a better relationship to the costs of Corporate management than do FTEs or employee count. Labor costs are an important part of manufacturing and construction companies, as well as the Utility. Efficient management of labor dollars, while primarily done at the subsidiary level, is a concern of overall Corporate management to ensure the financial success of each company. Therefore, the relationship of labor dollars to Corporate management is a third advantage for using labor dollars.

Q. WHAT TYPES OF COSTS ARE INCLUDED IN ARRIVING AT LABOR DOLLARS?

A. The following types of accounts for each subsidiary are included in the definition of labor dollars: labor (direct and indirect), salaries, sales commissions, management bonuses, payroll taxes and employee benefits. Some items like management bonuses and payroll taxes need to be included because some subsidiaries include those in labor and some report them separately. The goal is to have consistent costs for each subsidiary in order to calculate an appropriate ratio.

Q. ARE HEAD COUNTS USED FOR ANY PURPOSE IN THE ALLOCATION PROCESS?

A. Yes, an employee-ratio based on head-count is used in two indirect allocators – human resources (HR) and risk management (RM). Employee count is appropriate for these two indirect allocators because the costs to which these allocators are being applied tend to be tied to how many employees are involved. Employee count is also more appropriate in those two applications than the alternative of using labor dollars because of the specific costs to which the allocators are applied. The cost of administering HR benefit costs, for instance, relates more to the number of employees than to the compensation of individual groups of employees. The employee ratio is not used alone in the two indirect allocators and a relatively small proportion of Corporate Group dollars are allocated on these indirect allocators. Therefore, these components of the indirect allocators remain appropriate. However, OTP is less inclined to use employee count in the General Allocator because, as I explained, the number of employees in the regulated and unregulated parts of the business has little relationship to general corporate management.

Q. IN SUMMARY, WHY IS THE GENERAL ALLOCATOR USED BY OTP APPROPRIATE?

A. The non-utility subsidiaries of Otter Tail Corporation are almost completely unrelated to the electric utility business. They are also quite diverse in business characteristics. OTP's General Allocator is broadly based, stable, and verifiable. Using a General Allocator comprised of revenue, assets, and labor dollars has the advantage of being comprehensive and balances the characteristics of Otter Tail Corporation's varied lines of business. Some subsidiaries have significant assets, while others have few assets; some are high revenue, low margin businesses, while others are low revenues but high margins; and some are more labor intensive businesses. Using these three components (revenues, assets, and labor), recognizes this diversity.

Q. USING THE ALLOCATION METHOD AND FACTORS SUGGESTED, IS OTP PAYING MORE THAN ITS FAIR SHARE OF CORPORATE MANAGEMENT COSTS?

A. No. It is paying an appropriate share of corporate costs. As can be seen in the business segment section of the 2007 annual report to shareholders, the Utility had 56 percent of the consolidated corporation's assets, 46 percent of the consolidated corporation's income before income taxes, but paid just over 30 percent of the corporate management costs. This comparison indicates that the Utility is not paying more than its equitable share of corporate costs.

V. ECONOMIC DEVELOPMENT

Q. PLEASE DESCRIBE THE PURPOSE OF THIS PORTION OF YOUR TESTIMONY.

A. This portion of my testimony supports our request to recover OTP's South Dakota economic development expenses. More specifically, I will explain our proposal to modify our South Dakota program to mirror the very effective program we have in place in North Dakota, including a matching grant program that we have not previously offered in South Dakota.

Q. PLEASE DESCRIBE OTTER TAIL'S NORTH DAKOTA ECONOMIC DEVELOPMENT PROGRAM.

A. The North Dakota program has two components that we are proposing to incorporate into the South Dakota economic development proposal.

Under the North Dakota program, OTP is required to spend a minimum amount of $315,557 annually on economic development in OTP's North Dakota service territory (that amount is included in OTP's North Dakota rates). Since the North Dakota program's inception, OTP has actually spent, on average, well over half a million dollars annually. The program includes guidelines for the type of expenditures made. The four types of expenditures and the target expenditure amounts for each component are as follows:

PURPOSE	AMOUNT
Community matching grants	$160,000
Labor dedicated to economic development	100,000
Loan pool loss provision	35,000
Miscellaneous economic development expense	20,557
Total	$315,557

Table 4

It should be emphasized that the target amounts for each category of expenditure were approved in 1989 by the North Dakota Public Service Commission as guidelines and not as rigid individual spending requirements. Under the North Dakota program OTP may spend more or less than the guideline for any category in any given year, but its spending over time should approximate the guidelines for each category.

Q. WHAT MINIMUM SPENDING LEVEL ARE YOU PROPOSING FOR SOUTH DAKOTA?

We propose to spend a minimum of $100,000 annually on economic development in our South Dakota service territory. The total program amount proposed for South Dakota recovery is roughly proportional to the North Dakota approved amounts based on the relative size of our electric business in each state. The guideline amounts proposed for the South Dakota rate recovery are as follows:

PURPOSE	AMOUNT
Community matching grants	$50,000
Labor dedicated to economic development	41,000
Loan pool loss provision	1,000
Miscellaneous economic development expenses	8,000
Total	$100,000

Table 5

Q. WHAT HAS OTP TYPICALLY SPENT ON ECONOMIC DEVELOPMENT IN SOUTH DAKOTA?

A. In the last five years, OTP has typically spent about $45,000 annually on economic development in South Dakota. The amount spent in any given year varies because of the level of assistance requested, the health of the economy, and the provision for loan losses.

Q. PLEASE EXPLAIN THE DIFFERENCES BETWEEN OTP'S HISTORIC ECONOMIC DEVELOPMENT ACTIVITIES AND THE PROPOSAL IN THIS CASE.

A. The differences are: 1) the inclusion of the new matching grant program costs and 2) the inclusion of the costs associated with loan pool losses. As stated above, the amounts are roughly in proportion to the approved costs of the North Dakota program. The cost of loan pool losses (which occur when the recipient of a loan is unable to repay the loan) is higher than recent average annual losses, but reflects the credit exposure associated with the loan pool program.

Q. PLEASE EXPLAIN THE COMPONENT PARTS OF THESE PROGRAMS BEGINNING WITH THE COSTS INCLUDED IN LABOR COSTS?

A. We currently employ two full-time economic development specialists, one that is dedicated to South Dakota and Minnesota and another dedicated to North

Dakota. Personnel from our customer service operations are, at times, also involved in economic development activities.

Q. PLEASE EXPLAIN HOW THE COMMUNITY MATCHING GRANTS WORK AS PART OF THE OVERALL ECONOMIC DEVELOPMENT PROGRAM.

A. The matching grant program is a critical component of the overall economic development program. The matching grant program was designed to provide entrepreneurs, both start up companies and existing companies, the additional equity dollars needed to secure financings to complete projects. Often, one of the biggest hurdles for rural projects is securing sufficient equity funds to get projects off the ground. Our grant program in North Dakota has allowed numerous projects to obtain conventional financing, without which they would fail. Making matching grant funds available in South Dakota would similarly help projects leverage necessary financing.

These grants are not given without a substantial demonstration of the likelihood of a project's success. Also, grants are not given unless applicants can also obtain matching grants at least as large from local government sources, and/or regional economic development funds. This "matching" requirement insures that the local communities also support the projects, and creates a partnership among the local community, the project, and OTP. This matching requirement also helps to ensure that no one source of equity funds is burdened.

These principles have been in effect since OTP started its grant program in North Dakota in 1989, and, if approved, they would apply to the South Dakota matching grant program.

Q. PLEASE EXPLAIN WHAT THE LOAN POOL PROGRAM IS AND HOW THE LOAN POOL LOSS PROVISION FIGURES INTO THE AMOUNT YOU INCLUDED IN THE TEST YEAR.

A. Under the loan pool, OTP lends funds as part of a "pool" of lenders in order to assist projects that are in need of financing beyond what they may be able to obtain from conventional sources. Typically, a conventional lender (i.e. a bank) serves as lead lender and the other pool participants serve to provide their funds through that lead lender, often in a position subordinated to the lead lender. The loan pool program is not a low interest program. The borrower pays all pool lenders the same interest rate as the lead bank. Lender pools usually have between two and six participant lenders and historically have been made up of banks, community development commissions, local business interests, telephone companies, and rural cooperatives. Because other lower interest loans have become available in recent years, the amount that OTP has currently in loan pools in South Dakota is quite small.

The loan pool loss provision in our proposal is only a guideline that recognizes that such losses, if they occur, are to be included in economic development expenses. While OTP currently has low exposure because of the amount loaned, concern for economic conditions supports the proposed guideline of $1,000 annually for loan losses.

Q. PLEASE EXPLAIN WHAT COSTS MIGHT BE INCLUDED IN THE MISCELLANEOUS CATEGORY?

A. These costs include such things as cell phone costs, travel expenses including mileage, meals, and lodging (we have a lot of territory to cover).

Q. WHAT IMPACT HAS OTP HAD WITH ITS ECONOMIC DEVELOPMENT EFFORTS IN SOUTH DAKOTA?

A. Beginning in 1989 and through 2007, OTP has assisted in creating 1,630 jobs and assisted in saving an additional 40 jobs in South Dakota. In recent years, OTP has worked with about a half dozen South Dakota cities that requested assistance each year. The work covered a variety of business development projects. In 2007, these efforts helped create 66 jobs. We believe that our success will be greater with the addition of the grant program we are proposing in this case.

Q WOULD YOU BE MORE SPECIFIC ABOUT OUR ECONOMIC DEVELOPMENT ACTIVITIES?

A. The communities in South Dakota that we have worked with are generally quite small; most do not have economic development staff. Often we are asked to help a community put together a loan package. We are able to help structure the deals with our knowledge of programs, resources, and experiences of other deal structures that we have worked on. We often work with a business owner that is interested in locating in a community and wants an idea of what is available and what might be expected of that particular city, along with its amenities, banks, resources, land, etc.

We have been successful in locating franchises in some of our communities by using our knowledge of the community demographics profile that is acceptable to a particular franchisor. Over the years in South Dakota we have successfully worked with several locations, the most recent examples being the motels in DeSmet and Sisseton.

Q. DO THE ECONOMIC DEVELOPMENT EFFORTS ALWAYS RESULT IN MORE JOBS?

A. Not always. In smaller communities it has been harder and harder to keep the local communities' basic services open – grocery stores, hardware stores, and gas/convenience stores, for example. We have had success keeping stores open by encouraging owners in other communities that are close to the communities where the closures are about to happen to own and operate more than one location. We have a grocery store owner in the Hayti/Lake Norden area that has five locations. This of course does not create any new jobs but it certainly keeps businesses open and saves some of the previous jobs. However, fewer people are needed when there's one owner.

Q. CAN YOU COST-JUSTIFY YOUR PROPOSED PROGRAM?

A. Yes. As Mr. Brause explained in his testimony, OTP serves a sparsely populated rural part of South Dakota that is not growing in population. The average population of the communities we serve is approximately 400, over one-half of the communities we serve have populations of fewer than 200, and we serve a number of towns with less than 100 people. Indeed, many of the small towns we serve are threatened by significant decline in their populations. And these declines are largely due to the lack of job opportunities in those communities. Our economic development efforts are aimed at increasing job opportunities within our communities in order to stem the tide of the migration out of our rural service territory.

As has been widely recognized, population decline can have serious and insidious financial impacts on communities. In short, when populations decline, the remaining (now fewer) citizens are each required to share a larger portion of the costs related to necessary infrastructure. With respect to electric service, the principle is fairly straight-forward. If we don't slow the out-migration, the cost of providing electric service to our remaining customers will increase.

As has been recognized by federal and state agencies that provide economic development assistance, it is not possible to calculate with precision the value of a job created or a job saved. To do so would require a granularity of data that cannot practicably be obtained. So evaluating the cost-effectiveness of any economic development program must by its nature rely on assumptions, averages and reasoned judgment. My testimony to this point has emphasized the economic and social benefits associated with economic development and the impact to the rural communities which are prevalent throughout our service territory. For purposes of further cost-justifying OTP's proposed economic development program, I have relied on a few assumptions, but I believe them to be reasonable. Even if one were to quibble with my assumptions, the analysis supports the reasonableness and cost-effectiveness of our proposed program.

One reasonable way to view the value of OTP's proposal is to consider the financial impact of out-migration from OTP's rural towns. I believe it to be a fair assumption that we must have approximately two jobs in our area to support a residential customer. Put another way, if we lose two jobs in a small town, it is my belief that we are likely to lose at least one residential customer, who must leave to find work elsewhere. And based on this assumption, I believe we can save one residential customer for every two jobs we create or retain through our economic development efforts. It can be fairly inferred, then, that our economic development efforts slowed customer attrition by about 33 residences in 2007. This slowing of out-migration has real economic value to OTP customers. Based upon a simple calculation using 2007 figures, our average yearly revenue per residential customer was $942, and the total annual revenues for 33 homes based on this average would have been about $31,086. If those customers are lost through out-migration, the loss of revenue is repeated in all future years, so the calculation of the impact of the loss must also account for the future losses. Using a simple ten-year projection with a discount rate of six per cent, the total value of the revenues from 33 residential customers would be more than $225,000. Our annual expenditure of $100,000 for economic development is cost-justified alone by the fact that those efforts mitigate this revenue erosion caused by out-migration.

Similarly, by stemming the tide of this out-migration, OTP avoids the stranding of utility facilities that would no longer be needed for unoccupied homes and businesses, the value of avoiding this waste could be added to the value of the lost revenues to further justify our economic development efforts.

I recognize that there are those who might want to undercut this analysis by attacking my assumptions as imprecise. As I mentioned, I am not aware of anyone working in economic development who believes such a degree of precision is required to justify their efforts. And no such precision should be required to justify OTP's efforts. While the benefit may not be able to be calculated to the dollar, the benefit of our economic development efforts are real and they justify the reasonable expenditures proposed for inclusion in our Test Year.

Q. HOW ELSE DO YOUR COMMUNITIES BENEFIT FROM YOUR ECONOMIC DEVELOPMENT EFFORTS?

A. By creating opportunities and slowing out-migration from our rural communities we also helped these communities stabilize their tax base and maintain the number of students they have in their schools. Our efforts also helped to ensure that community members have access to health care services and that their children have the same educational opportunities as those who live in larger communities. Our efforts helped our communities utilize their infrastructure and utility resources more effectively. While these impacts might be difficult to quantify, they are indeed real to the inhabitants of these small towns. For many of our communities, the issues associated with out-migration and lack of opportunity have been among their greatest concerns for the past few decades. Because our customers are so significantly impacted by these issues, we have emphasized these concerns in our mission statement. As Mr. Brause explained, our mission includes a commitment to improve the quality of life in the communities we serve. The economic development program costs included in our Test Year will help fulfill this mission.

VI. CONCLUSION

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

OTTERTAIL CORPORATION

Corporate Cost Allocation Manual

Last Update: February 2008

I. INTRODUCTION

The corporate entity ("Corporate") of Otter Tail Corporation provides services to the operating companies that comprise the Corporation. One of three things can occur with costs from Corporate services: 1) allocated to Otter Tail Power Company; 2) allocated to Varistar Inc., or 3) not allocated and remain at Corporate. The purpose of this manual is to detail how costs are being allocated to Otter Tail Power Company.

Otter Tail Power Company (the largest operating company of Otter Tail Corporation) serves retail electric customers in three jurisdictions including Minnesota, North and South Dakota and is governed by the rules and regulations in each jurisdiction. As a regulated utility, Otter Tail Power is allowed to recover prudent and reasonable costs for services it receives from Corporate, and reflects the cost of these services in its revenue requirements for setting rates.

The services provided by Corporate include financial reporting, tax planning and reporting, treasury and cash management, financial planning, internal audit, human resource and labor expertise, benefit plans, corporate communications, safety and risk management, shareholder services and investor relations, sourcing, aviation and executive management services (CEO, COO, CFO and General Counsel). These services are distinct from and do not duplicate similar services in Otter Tail Power Company. See Section V below for additional information of Corporate services. To support these services, there are specific corporate costs associated with administration and information technology ("IT") that also need to be allocated.

The remainder of this document is devoted to explaining the services being provided and the methodology and allocation factors used to allocate Corporate service costs to Otter Tail Power Company.

II. METHODOLOGY

Corporate identifies costs in three categories: 1) directly assignable costs, 2) indirect costs that are allocated on a department or functional allocation factor, and 3) general costs that are allocated using a general allocation factor.

Directly assignable costs are those costs where the purpose behind the costs can be attributed to a specific operating company. For example, consulting fees to help with a project related to an individual operating company would be directly assigned to that operating company.

Indirect costs have an identifiable cost causation related to another activity or factor. For example, costs for an employee in the Risk Management department of Corporate to attend a seminar on safety would be allocated using a functional allocation factor such as number of employees.

General costs are those costs that cannot be directly assigned or where cost-causation cannot be identified. Examples would include postage, local telephone and communication service costs, time spent preparing the annual report and other SEC filings, preparing to meet with rating agencies, working with and tracking shareholder matters. These types of costs will be allocated on a general allocation factor discussed below.

Allocation factors are updated annually with the most recent calendar year's data and remain unchanged for 12 months. Current year factors are applied to corporate billings to the utility in first month following availability of final, audited financial information required for some factors.

III. ALLOCATION FACTORS

Indirect Allocation Factors:

A. IT Factor: This factor is based on the previous year ending December 31 ratio of corporate labor assigned to Otter Tail Power where the numerator is the total Corporate labor (not including bonuses) assigned to Otter Tail Power and the denominator is the total of all Corporate labor (not including bonuses). See Appendix A.

B. HR Factor: This factor is based on the average of the previous year ending December 31 ratio of employees, and the previous year ending December 31 ratio of benefit expenses. For the employee ratio the numerator is both full and part-time employees in electric operations and the denominator is the total number of full and part-time employees for all of Otter Tail Corporation. For the benefit ratio, the numerator is total benefit costs (including benefit costs cleared through the payroll loading rate) from electric operations, and the denominator is consolidated benefit costs for all of Otter Tail Corporation (including benefit costs cleared through the payroll loading rate) excluding benefit costs for Corporate employees. The specific consolidated corporate accounts that will be used to calculate this ratio (including Otter Tail Power benefit costs cleared through payroll loading) are accounts C5030, C5230, C6030, C6530, C7030. See Appendix A.

C. RM Factor: This risk-management factor is the average of the previous year ending December 31 ratio of employees, and the previous year ratio of insurance premiums paid. For the employee ratio the numerator is both full and part-time employees in electric operations and the denominator is the total number of full and part-time employees for all of Otter Tail Corporation. For the insurance premium ratio, the numerator is the total premiums paid by Otter Tail Power and the denominator is the sum of insurance premiums paid by all operating companies. See Appendix A.

D. Internal Audit Factor: This factor is based on the previous year ending December 31 ratio where the numerator is the total hours spent auditing electric operations and the denominator is the sum of hours auditing electric and non-electric operations. Non-electric operations do not include hours spent auditing Corporate-related matters. See Appendix A

General Allocation Factor:

This factor is based on a three-factor formula that is comprised of the average ratio of Total Assets, Total Revenues and Total Labor Dollars for the most recent calendar year. The specific consolidated corporate accounts that will be used to calculate the Total Labor Dollars ratio are C5010, C5020, C5030, C5210, C5220, C5230, C6010, C6015, C6020, C6030, C6510, C6520, C6530, C7010, C7020 and C7030. Appendix A shows the computation of this factor based on prior-year audited numbers and shows the source for the information to calculate each ratio.

IV. CLARIFICATION ON CERTAIN COSTS

There are certain costs that need to be discussed in further detail to gain an understanding of exactly how they are being allocated, or in some instances, not being allocated. This section will list each of these costs individually and provide background and instruction on how each is handled for allocation purposes.

A. Labor: Each employee at Corporate tracks their time on a daily basis. Attached as Appendix B are samples of time-sheets for typical corporate employees. Percentages are used instead of hours to track time between Corporate, Utility, and Non-utility activities. The time designated Utility is directly assigned to Otter Tail Power. The percentage of time being recorded in the Corporate column is allocated based on the employee's position and will use one of the allocation factors discussed above in Section III.

B. Bonuses and Benefits: Cash bonuses are allocated based on each employee's labor ratio from the previous year. An employee's labor ratio reflects both directly assigned and allocated labor. Bonuses are accrued and allocated during the current year, and a true-up is made in the following year after the exact bonus amount is determined and the employee's actual labor ratio from the previous year is available. Benefit costs are allocated on each employee's labor ratio from the most recent 30-day pay period.

C. Contributions, Employee Stock Purchase Plan and Deferred Compensation Expense: The costs associated with these three items are not allocated to Otter Tail Power. Each operating company makes their own contributions and those contributions made from a corporation perspective are typically not allocated. Costs for the stock purchase plan and deferred compensation plan are kept at Corporate and not allocated.

D. Stock Option Expense: Under FAS 123(R) companies are required to record the value of stock options over the period in which the options vest. These expenses are allocated to Otter Tail Power based on the number of options granted to employees in this company.

E. Restricted Stock and Restricted Stock Units: Under FAS 123(R) companies are required to record the value of restricted stock and restricted stock units over the period in which the shares vest. Restricted stock and restricted stock unit expense on shares granted to Otter Tail Power employees are directly assigned to Otter Tail Power. No portion of restricted stock or restricted stock units granted to Corporate employees and the Board of Directors is allocated to Otter Tail Power Company.

F. Executive Stock Incentive Plan: Under FAS 123(R) companies are required to record the value of incentive stock, awarded based on the performance of the company's stock price, over the time period used to evaluate performance. Otter Tail Corporation provides incentive stock to the corporate officers as part of their overall compensation package. The costs associated with this plan are not allocated.

G. Bank Charges: Corporate serves as the "Bank" for all operating companies and therefore incurs the various fees associated with all the accounts maintained by the operating companies. Each operating company is directly charged for their respective fees and the fees associated with Corporate's accounts are allocated using the General Allocation Factor.

H. External Audit Fees: Otter Tail Corporation currently retains an independent registered public accounting firm to audit its financial reports and records. Each year this firm provides to Otter Tail Corporation a Client Service Plan that outlines the number of hours it has assigned to audit electric and non-electric operations. Fees from the firm are allocated based on the ratio of assigned hours for electric versus total audit hours on consolidated operations.

I. Meetings: Costs associated with periodic meetings that involve personnel from across the operating companies such as quarterly leadership meetings, quarterly accounting and HR meetings are allocated based on the number of people attending from each company, versus the total number of people in attendance.

J. Travel and meals: With the exception of travel-related expense related to operations of Otter Tail Power's jointly owned generation plants, travel expense is not allocated.

K. Aviation Services: Corporate provides air service for the operating companies of Otter Tail Corporation. There are two aircrafts available for use. One is owned by Otter Tail Power Company (the King Air), the other is owned by Varistar Corporation (the Citation). To help recover the variable costs associated with flying these two aircraft, corporate charges $650/hr for the King Air and $920/hr for the Citation.[1]

[1] The aviation charge rates may be changed during the year to reflect changes in variable costs (i.e., aviation fuel).

Because the King Air is owned by Otter Tail Power, at the end of each quarter the costs associated with the King Air that have not been recovered through the hourly rate are charged to Otter Tail Power. For example, the costs not cleared for the quarter total $9,000. Otter Tail Power has recorded depreciation expense for the quarter of $1,000 which is added to the $9,000 of un-cleared costs for a total of $10,000. The $10,000 is multiplied by the non-utility usage factor (the percentage of hours flown for operating companies other than Otter Tail Power) and for our example we'll say it's 52%. Otter Tail Power will then be charged $3,800 ($9,000 less $5,200 ($10,000 x 52%)) to reflect the utility-portion of costs not cleared on the King Air.

V. DESCRIPTION AND ALLOCATION OF SERVICES PROVIDED

Further detail is discussed below on the services provided by Corporate. Each service shown below is directly related to an individual cost center at Corporate. For each service a description is provided along with the primary allocation factor that is used to allocate associated costs. Again, costs that can be directly assigned to the various operating companies are directly assigned. Indirect costs are allocated using one of the factors discussed in Section III.

A. Corporate Overheads

Description: Represents charges for succession planning and developing leadership at the operating companies, bank charges, building lease and depreciation expense.

Allocation Factor: Costs associated with succession planning and developing leaders at the various operating companies are not allocated but kept at Corporate. All other costs not directly assigned are allocated on the General Allocation Factor.

B. Executive Management Services

Description: Represents charges for Otter Tail Corporation's executive management team comprised of the four Officers, and Contributions.

Allocation Factor: Contributions are not allocated and all other costs not directly assigned are allocated on the General Allocation Factor including labor classified as Corporate.

C. Board of Directors

Description: Represents charges for board of director fees, restricted stock, travel and other expenses associated with attending Board meetings.

Allocation Factor: Fees are allocated on the General Allocation Factor. Otter Tail Power is not allocated any costs associated with restricted stock granted to directors or travel related expenses.

D. Corporate Development

Description: Represents charges for the Platform Leaders and their staff that have oversight responsibilities with the non-electric operating companies, identifying and researching acquisition candidates, due diligence on acquisition targets, and integrating recently acquired companies into Otter Tail Corporation.

Allocation Factor: All costs are currently being directly assigned to Varistar Corporation but if Otter Tail Power uses these services for an acquisition, the associated costs would be directly billed to Otter Tail Power.

E. Administrative Services

Description: Represents charges for providing administrative support to all the other services, office supplies, cell phones and office equipment leases.

Allocation Factor: All costs not directly assigned are allocated on the General Allocation Factor including labor classified as Corporate.

F. Information Technology

Description: Represents charges for supporting corporate computers, networks, land-based phones and T1 lines, internet, software and other various pieces of hardware. In addition, consulting services are provided as requested to the various operating companies.

Allocation Factor: License and maintenance fees comprise a large portion of the non-labor costs. As much as possible, these costs are directly assigned based on the number of user licenses utilizing the software by operating company. All costs not directly assigned are allocated on the IT Factor including labor classified as Corporate.

G. Corporate Accounting

Description: Represents charges for maintaining financial records, statements and systems, SEC filings, tax accounting and filings, cash management and consulting with various operating companies on an as-needed basis.

Allocation Factor: External audit fees are allocated as discussed in Section IV. Costs not directly assigned are allocated on the General Allocation Factor including labor classified as Corporate.

H. Internal Audit

Description: Represents charges for reviewing internal controls and conducting operation audits at the various companies within Otter Tail Corporation.

Allocation Factor: Costs not directly assigned are allocated on the Internal Audit Factor including labor classified as Corporate.

I. Financial Planning and Sourcing

Description: Represents charges for supporting financial analysis and budgeting at the operating company and corporate level, communicating with both debt and equity analysts, maintaining Otter Tail Corporation's capital structure, monitoring and accessing capital markets and other services as identified by the Chief Financial Officer. Charges also represent services related to sourcing, procurement, vendor relationships, and developing strategies to leverage the consolidated buying power of Otter Tail Corporation as a whole.

Allocation Factor: Sourcing-related costs are directly assigned in most instances. Costs not directly assigned are allocated on the General Allocation Factor including labor classified as Corporate.

J. Corporate Communications

Description: Represents charges for corporate communications including press releases, advertising and branding and annual report preparation. Another service provided is coordinating and tracking contributions made on behalf of Corporate.

Allocation Factor: Costs not directly assigned are allocated on the General Allocation Factor including labor classified as Corporate.

K. Shareholder Services

Description: Represents charges for maintaining shareholder records, communicating with investors at various fairs, coordinating transfer agents and planning the annual shareholder meeting.

Allocation Factor: Costs not directly assigned are allocated on the General Allocation Factor including labor classified as Corporate.

L. Human Resources

Description: Represents charges for establishing and maintaining policies related to employment and benefits of corporate employees and executive compensation, searches for candidates for upper-level management positions on behalf of operating companies, organizes and facilitates leadership training, organizes and aids in the administration of company benefit programs.

Allocation Factor: Costs not directly assigned are allocated on the HR Factor including labor classified as Corporate.

M. Legal Affairs

Description: Represents charges for legal services related to employment law, litigation, contracts, rates and regulation, environmental matters, real estate and other various legal matters.

Allocation Factor: All costs associated with legal services are directly assigned. All lawyers other than the General Counsel are directly assigned to one operating company, or a group of operating companies. Three lawyers are currently assigned to Otter Tail Power and two lawyers are assigned to non-electric companies.

N. Risk Management

Description: Represents charges for assisting operating companies with assessment and management of risks, identifying and implementing loss control strategies to minimize the frequency and financial consequences of accidental losses, assisting operating companies in post loss claim management, overseeing Otter Tail Corporation's consolidated insurance program, and identifying and documenting the environmental conditions during the process of acquiring a new company.

Allocation Factor: Costs not directly assigned are allocated on the RM Factor including labor classified as Corporate.

VI. CONCLUSION

As circumstances arise, such as adding a new service that will be provided by Corporate, appropriate changes will be made to the manual. Appendix A will be updated annually in February when the prior-year audited records are available.

Appendix A

Computation of Allocation Factors for 2008

General Allocation Factor

REVENUES	2007	
Electric Retail Revenue	276,894	
Electric Wholes Revenue	20,345	
Other Operating Revenues	20,625	
Non-Asset Based Power Pool Sales	62,214	
Total Electric Revenues	380,078	
Total Consolidated Revenues continuing operations	1,295,806	
Ratio	**29%**	**29%**
Revenue Ratio		
TOTAL ASSETS		
Assets - Electric Operations	813,565	
Consolidated Assets	1,454,754	
Asset Ratio	**56%**	**56%**
TOTAL LABOR DOLLARS		
Labor Dollars - Electric Operations	61,773	
Consolidated Labor Dollars	258,497	
Labor Dollars - Ratio	**24%**	**24%**
2008 General Allocation Factor		**36%**

IT Factor

	2007	Factor
Labor Allocated to OTP	1,960	
Total Corporate Labor	5,309	
2008 IT Factor		**37%**

HR Factor

Benefit Costs	Electric Operations	Consolidated Operations	Factor
Benefits Costs - Cost of Goods Sold	0	7,662	
Benefits Costs - Overhead (Indirect)	0	9,846	
Benefits Costs - Sales	0	537	
Benefits Costs - R&D	0	0	
Benefits Costs - A&G	736	4,568	
Benefits Loaded Through Labor	24,522	24,522	
Subtotal	25,258	47,135	
Benefit Ratio		**54%**	
Employee Ratio		**17%**	
2008 HR Factor			**35%**

Appendix A

Computation of Allocation Factors for 2008

RM Factor

	2007	Factor
Employee Ratio		
Employees - Electric Operations	714	
Consolidated Temp & Full-Time Employees	4,300	
Employee Ratio	**17%**	
Insurance Premium Ratio		
Insurance Premiums Paid by OTP	2,125	
Sum of all Insurance Premiums Paid	10,386	
Insurance Ratio	**20%**	
2008 RM Factor		**19%**

Internal Audit Factor

	2007	Factor
Electric Auditing Hours	2,712	
Non-Electric Hours	3,808	
2008 Internal Audit Factor		**42%**

Reset Time Sheet

OTTER TAIL CORPORATE TIME SHEET

FOR WAGE HOUR EXEMPT EMPLOYEES

OTTERTAIL CORPORATION

Pay Period Starting Date 2/16/2007

Employee: 1 **Department:** Financial Planning & Sourcing

Employee ID: xxxx **Manager:** xxxxx

Paid Time Off Reporting

Day	Date	Pay Code	Hrs not worked
Fri	2/16		
Sat	2/17		
Sun	2/18		
Mon	2/19		
Tue	2/20		
Wed	2/21		
Thu	2/22		
Fri	2/23		
Sat	2/24		
Sun	2/25		
Mon	2/26		
Tue	2/27		
Wed	2/28		
		Totals	0

Time Allocation (Allocate PTO, HOL, FLT, etc. 100% to Corp)

Corp	Utility: Regulated	Utility: Not Regulated	Utility: BSP II - OTP	Utility: BSP	Utility: BSP II	Utility: Coyote	Not Electric	Total	Company/Project
0%	0%	0%	0%	0%	0%	0%	0%	0%	

Pay Code	Total Hours
EXC - Excused Absence Paid	0
FLT - Floating Holiday	0
FNL - Funeral/Maternity	0
HOL - Holiday	0
JUR - Jury Duty	0
LST - Unpaid Absence	0
PTO - Paid Time Off	0
SCK - Accrued Sick Leave	0
STD - Short Term Disability	0
VAC - Accrued Vacation	0
Total	**0**

Allocation		Accounting	% of Time
Corp	OTP	060-7100-499	0%
	Non-electric	060-7100-299	0%
Utility	Regulated	060-7100-460	0%
	Not Regulated	060-7100-402	0%
	BSP II - OTP	060-7100-494	0%
	BSP	060-7100-497	0%
	BSP II	060-7100-496	0%
	Coyote	060-7100-498	0%
Non-electric		060-7100-200	0%
Total			0%

Allocation Factor	General	Ratio
OTP		38%
Non-electric		62%

Error Legend
Monthly Allocation does not equal 100%

Employee signature Date
This is a true and accurate report of my time.

Manager signature Date

Timesheet Version: 2007 Exempt timesheet v2.0

Appendix B

Reset Time Sheet

OTTER TAIL CORPORATE TIME SHEET
FOR NON WAGE HOUR EXEMPT EMPLOYEES

OTTER TAIL CORPORATION

Pay Period Start Date	1/1/2007		
Employee:	1	Department:	Corporate Accounting
Employee ID:	xxxx	Manager:	xxxxxxxx

Paid Time Off Reporting | **Time Allocation (Allocate PTO, HOL, FLT, etc. 100% to Corp)**

Carry Forward Hours - Paid in Prior Period

Day	Date	Pay Code	Hrs worked	Hrs not worked	Addn'l Reg Hrs	OT Hrs worked	Corp	Utility: Regulated	Utility: NOT Regulated	Utility: BSP II - OTP	Utility: BSP	Utility: BSP II	Utility: Coyote	Not Electric	Total	Company/Project
Mon	1/1															
Tue	1/2															
Wed	1/3															
Thu	1/4															
Fri	1/5															
Sat	1/6															
		Week 1 Subtotal	0	0	0	0										
Sun	1/7															
Mon	1/8															
Tue	1/9															
Wed	1/10															
Thu	1/11															
Fri	1/12															
Sat	1/13															
		Week 2 Subtotal	0	0	0	0										
Sun	1/14															
Mon	1/15															
		Week 3 Subtotal	0	0	0	0										
		Pay Period Total	0	0	0	0	-	-	-	-	-	-	-	-	-	

Pay Code				
EXC - Excused Absence Paid				
FLT - Floating Holiday				
FNL - Funeral/Maternity				
HOL - Holiday				
JUR - Jury Duty				
LST - Unpaid Absence				
PTO - Paid Time Off				
SCK - Accrued Sick Leave				
STD - Short Term Disability				
VAC - Accrued Vacation				
OVT - Overtime				
STE - Straight Time Extra				
REG - Regular Work Time				
Total	0	0	0	0

Allocation		Accounting	% of Time
Corp	OTP	050-7100-499	-
	Non-electric	050-7100-299	-
Utility	Regulated	050-7100-450	-
	Not Regulated	050-7100-402	-
	BSP II - OTP	050-7100-494	-
	BSP	050-7100-497	-
	BSP II	050-7100-496	-
	Coyote	050-7100-498	-
Non-electric		050-7100-200	-
	Total		0%

Allocation Factor	General	Ratio
OTP		38%
Non-electric		62%

Error Legend

Monthly time allocation does not equal 100%

Employee signature ____________________ Date
This is a true and accurate report of my time.

Manager signature ____________________ Date

Timesheet Version: 2007 Non-exempt timesheet v2.0