THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF SOUTH DAKOTA

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IN THE MATTER OF THE APPLICATION OF OTTER TAIL CORPORATION D/B/A OTTER TAIL POWER COMPANY FOR AUTHORITY TO INCREASE ITS ELECTRIC RATES

EL08-030

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Transcript of Proceedings
June 23, 2009

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BEFORE THE PUBLIC UTILITIES COMMISSION,
DUSTY JOHNSON, CHAIRMAN
STEVE KOLBECK, VICE CHAIRMAN
GARY HANSON, COMMISSIONER

COMMISSION STAFF
Rolayne Ailts Wiest
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Jon Thurber
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APPEARANCES

BRUCE GERHARDSON, appearing on behalf of Otter Tail Power

Reported By Cheri McComsey Wittler, RPR, CRR

TRANSCRIPT OF PROCEEDINGS, held in the above-entitled matter, at the State Capitol Building, 500 East Capitol Avenue, Pierre, South Dakota, on the 23rd day of June, 2009, commencing at 2 o'clock p.m.

CHAIRMAN JOHNSON: We'll come out of recess for the June 23 Public Utilities Commission meeting. There's only one item left on our agenda, electric item number 1, which is Docket EL08-030. This is the Otter Tail Corporation rate case.

There has been a Joint Motion for Approval of the Settlement Stipulation filed. So at this time I think it's probably appropriate -- actually since we've got a court reporter and folks listening on the internet maybe before we go any further, why don't we have you introduce the team that's here with Otter Tail, and then we can go ahead and hear any comments that you might have to support the settlement stipulation.

MR. GERHARDSON: Thank you, Chair Johnson, Commissioners. With me today --

CHAIRMAN JOHNSON: I'm sorry. Let me interrupt. I should double-check and make sure we have the folks on the internet we need to have on. Do we have Bob Towers and Dave Peterson on the line?

MR. TOWERS: Yes, we have Bob Towers.

MR. PETERSON: And Dave Peterson here too.

CHAIRMAN JOHNSON: How are we coming across, gentlemen?

MR. PETERSON: A little bit faint.

CHAIRMAN JOHNSON: A little bit faint. Well, we'll work on that then. How are we coming across now?

MR. PETERSON: Much better.

CHAIRMAN JOHNSON: Much better. Good. My apologies. Go ahead and proceed.

MR. GERHARDSON: Thank you, Chair Johnson, Commissioners. I'm Bruce Gerhardson, associated general counsel with Otter Tail Power Company. And we do have several members of Otter Tail Power's staff here.

And why don't I begin with Mr. Tom Brause, our vice president of administration. Bernadeen Brutlag, who is the manager of our regulatory services. Peter Beithon, manager of regulatory economics, is sitting next to Bernadeen. Ron Spangler, our rate case manager, is back in this room. Kyle Semm (phonetic), our senior rates analyst, is in the row there too. Dave Prazak is up at the counter here. He's the supervisor of pricing. Jason Grenier is a pricing analyst with us.

And just entering the room now is Jennifer Whittingham Flodine (phonetic) on cue. She's our rate case coordinator.

Now these folks are here really as subject matter experts in the case that any of you have questions on issues that are within their area of expertise. So I would encourage questions anywhere during the course of my presentation or afterwards, whatever is your preference. The reason for them being here is to answer those questions.

Our president, Chuck McFarland, did wish to be here. He had two things that are of interest both to Otter Tail and the State of South Dakota that he felt he needed to participate in that both occurred today. One is a MISO RECB, the cost allocation, as you may be aware that he was participating in some discussions on that subject. And also some allocations on carbon dioxide as it may occur in some federal legislation that's been proposed. So those were very important issues that he felt he could not be away from --

CHAIRMAN JOHNSON: If people throughout the region are going to refer to the Otter Tail problem, it probably makes sense to have Otter Tail well represented there, huh?

MR. GERHARDSON: Thank you. And I will say I think that generally speaking momentum is going well for resolution of the Otter Tail problem. We want to keep that momentum up.

My presentation really has -- you know, it takes an obvious course. We're going to summarize our filing and what our request was. Next I'll describe briefly the contents of our filing, the thoroughness of our filing. And then finally I'll turn to the settlement that we're asking along with staff that you approve today.

We filed our request on October 31, 2008, requested an overall revenue increase of 15.3 percent or $3.9 million. We based our requests on an historic test year. 2007 was the historic test year.

And to put that in perspective I guess the last time Otter Tail had a rate increase in the State of South Dakota was 1987. So about 21 years had passed between our last rate case and our filing.

The requested 15.3 percent represents over that period about a .7 percent increase per year given the span of time that's occurred.

The reasons for the requested increase, some of which are intuitive, some of which are because of things that occurred recently. One is since 1987, of course, we've seen an increase over time in operating costs, most notably, materials, labor, pension, both active and post retirement medical expenses. Some of those items as you know have risen in costs dramatically.

Also since 1987 we've seen dramatic increases in some instances in fuel and purchase power costs. Not all of which was being recovered in Otter Tail's case through our fuel clause.

We also made during that period of time significant investments in wind generation and some other infrastructure. I think I should note we added a combustion turbine at Solway, Minnesota, a diesel generator at Otter Tail's system operations center in Fergus Falls.

We've made several transmission investments over that period of time, several production improvements including improvements at the Big Stone plant here in South Dakota and our Coyote plant in North Dakota and our Hoot Lake plant in Minnesota.

And, as I mentioned, we made some significant investments in wind recently, two sites in North Dakota. One at Langdon, North Dakota, one at Ashtabula, North Dakota.

And we have been very proud of the cost containment that we've been able to achieve over this 21-year period. It's allowed us to stay out of the arena for a very long time.

During that time we have maintained excellent -- by all measures excellent reliability, excellent customer service measures, and excellent safety standards. And so we are very proud of that fact.

Now I want to turn back to the wind investment and the revenue requirement that is part of this increase request relating to the wind.

To give you a sense of the amount of the increase that is associated with wind, about half of our original request, about 50 percent of the 15.3 percent or when I turn to the settlement, about 60 percent of the settlement is related to revenue requirements associated with the wind investment.

The one thing that the increase requested and the increase upon which we've settled doesn't reflect really is the benefit that the wind gives our customers when put on our system. And that comes because the energy that comes from the wind generation is represented in our fuel clause adjustment at zero cost. That is, there are kilowatt hours that are now in our fuel clause adjustment that show up without any cost. Of course, there's cost in the base rate increase.

The result is a significant offset to customer bills in the form of a reduction to what the fuel clause adjustment would have been without the wind investment. So when we talk in terms of 15 percent requested and 11.7 percent upon which we are settled, it would be incorrect to mistakenly think that it's all cost. The wind is providing that benefit of zero cost energy in the fuel clause too.

Now I want to turn just briefly to the components of our filing. I believe we've made a very thorough filing. And one thing I should point out is it has been a long time since our company made a filing in South Dakota. So we do appreciate the courtesies and the assistance in many ways that the staff here had as we made our filing and as they made data requests so that we could support our filing.

We believe it was thorough and comprehensive. We provided the standard statements that are required by the rules. We supported it with a tremendous number of working papers. We had direct testimony by nine witnesses. And with that we made our filing.

We provided public notice according to Commission rules. And about notice, we had about 11,700 customers in the State of South Dakota. And since providing notice in November we've had 15 contacts that are logged into our customer service -- our CIS system, customer information system, indicating that of the 11,700 customers we had 15 contacts total over that time period requesting information about the filing.

It isn't necessarily Complaints. It may be just information about the increase.

Now I should also point out that there are also some contacts that could have been made to customer service personnel that have not yet been logged in the system but we made an inquiry and found out about 15 contacts have been made since that time.

After making our filing we provided a significant number of responses to the discovery requests of staff over the last several months. And we began to work with staff after they had completed their discovery in the month of March on the possibility of reaching a settlement on the issues that had been presented.

In the course of those discussions Otter Tail agreed to make adjustments to rate base and operating costs that reduced the revenue requirement and the revenue deficiency in the case from the 15.3 to 11.7 percent adjustment.

We also made several adjustments to the rate design that we were proposing in the case. The result is a revenue requirement, as I mentioned, of 11.7 percent or an increase of $2.97 million. We also changed in the course of our discussions the approach that we had to whole margins, both what we call asset-based wholesale margins and nonasset-based wholesale margins.

For the record, asset-based margins are those margins that are derived from our owned generation. Nonasset-based margins are those where we have made a purchase in the market and a sale in the market.

The margins from asset-based sales in the settlement are treated such that both the company and our customers have a shared stake in the success of our plant operations. That provides an incentive for the company to be successful in maintaining and operating those plants. The more they operate, the better our customers do, the better we have an opportunity to do in the wholesale market.

Our customers will benefit in reduced fuel adjustment clause on their bill if we're successful in maintaining and operating those plants. 85 percent of the margins will be reflected as a credit -- pardon me. 85 percent of our margins based on our historical performance of asset-based margins are reflected as a credit to the base rate revenue requirement. And then changes to that amount will be reflected in fuel -- in the fuel clause on a going-forward basis. So the variability will be reflected in the fuel clause.

And then the 15 percent of the asset-based wholesale margins will be retained by the company as an incentive to steward the generation resources wisely.

And this approach, as I mentioned, provides a strong incentive for Otter Tail to optimize its plant operations.

On nonasset-based sales, again those sales that are not associated with generation that we own, Otter Tail in its filing proposed sharing 15 percent of the margins with customers through a credit to the fuel clause adjustment on a going-forward basis.

Through settlement discussions we arrived at a settlement of 25 percent of the margins will be reflected as a credit to the fuel clause adjustment. That percentage is intended to cover the fully allocated costs of those operations. The traders that transact both asset-based and nonasset-based are the same personnel, and this is a way to create a sharing mechanism to cover the costs of that.

Now turning to rate design, again I'd like to acknowledge the work of staff in this area. Otter Tail proposed some significant changes to its rate design. A few items really that are most notable, we had declining block rate structures throughout our rates. Otter Tail had proposed the elimination of declining block rates. And declining block rates again for the record are those rates where they -- the rate goes down as consumption increases.

The settlement that we reached with respect to declining block rates reflects staff's recommendation to take a much more moderate approach to the elimination of these declining block rate structures. This is really I think both in staff's eyes and in Otter Tail's eyes as more of a first step to a gradual elimination of the declining block structures.

It will by moderating -- the approach that we were proposing through our settlement we will reduce the disproportionate rate impacts of those customers who are consuming more energy. We will retain defining block structures for our residential customers, our farm service customers, and our general service -- general service under 20 kilowatt customers.

Now while it's only three rates, that does make up the vast majority of our customers. Of the 11,700 customers we have in South Dakota those three rates make up about 10,000 of those customers. So those customers will be -- the rates that those customers are taking service under will have benefited from the moderation that staff recommended in the reduction of declining block rates.

Now our original request and this settlement proposal are both consistent with the federal and state policy initiatives of which I think you're all aware, such as those in the Energy Policy Act, that would support commissions approving rate structures that encourage conservation. Generally thought, that to have rates go down as consumption increases is counterproductive in conservation.

The second rate design change that I would like to mention is the addition of the fuel clause adjustment to all Otter Tail rates. You may recall that we had part of our revenue deficiency was on account of the fact that our fuel clause did not recover all of the costs of fuel, the variability that occurred in fuel since our last rate case.

We had a few rates that did not include a fuel clause adjustment. Those rates then have since 1987 been paying 1987 fuel and purchase power costs, which would be different from most, say, residential customers who have a fuel adjustment clause. They've been seeing the increases as those have occurred.

Now on account of that there are some rates that will see a larger increase and it's because they're in a sense being caught up in the fuel and purchase power costs that are necessary to serve them.

The next rate design change that I would like to mention is our seasonal rate, a change that we made to our seasonal rates.

We did have rates in our existing rates that had seasonal differences; that is, during summer and winter seasons you pay a different amount, per kilowatt hour. Our proposal is that virtually all rates will have a seasonal component. And the seasonal differential really is related to the fact that there are seasonal differences in the amount we pay for market energy.

And so we're attempting to send price signals about the consumption patterns that people may have that would reflect our marginal costs in each of the seasons.

And then the final thing I'd like to mention about our rate design changes is we did make changes to the substantial customer charge. The settlement that we're asking you to approve today does increase the existing residential customer charge from -- there were two separate charges depending upon the zone in which you took your rate -- took your service. One was at $5.80. The other was at $6.55. That is now increasing to $7 for all customers. So we're seeing an increase of either 45 cents or 1.20, depending upon which zone you're in.

There are other rate design changes that I'm not mentioning in this presentation, but I think those four are some of the more significant that I thought were worth mentioning.

Now our proposal, we are requesting that final rates be implemented July 1. As you may recall, we had interim rates implemented beginning May 1. Upon receiving approval, we would send notification of the implementation of final rates to all residential customers -- actually all of our customers. And there are several customers who are on rates who would be discontinued under our settlement proposal. There are a total of 72 customers who would no longer be able to take service under the rates that they have.

There are four customers taking service under what's called the commercial demand control rate. That was an experimental rate. And then there are 68 customers under what's called the electronic climate control rate. That was a rate that was closed in 1987, meaning no customers have been able to sign up for that rate since that time, and these are customers who continue to take service under that rate.

Otter Tail has proposed that we make personal contacts to those customers that are on those rates that are seeing an impact of $500 or more per year. And that personal contact would be either in the form of a phone call or a face-to-face meeting. The remainder would see a letter about the discontinuance of those rates. Those customers would then begin to take service under other available rates.

The customers that would be receiving an in-person or a phone contact, it's approximately 20 customers.

So with that background, Otter Tail requests that you approve the settlement that we have reached with staff. The settlement provides Otter Tail with an annual level of revenues that's fair, just, and reasonable. The rates allow Otter Tail a reasonable opportunity to earn a return that's adequate to enable Otter Tail to continue providing service to our South Dakota customers that is safe, reliable, and will continue with a high degree of customer service.

Now, again, I mentioned that if you have questions, we have several experts, subject matter experts, in the room, and I'd be happy to attempt to answer any questions you may have.

CHAIRMAN JOHNSON: Thank you very much, Otter Tail.

Staff, comments.

MS. SEMMLER: This is Kara Semmler from staff. We too have some subject matter experts that could help answer any question, but we support the resolution and ask that the Commission adopt it.

MR. KNADLE: Excuse me, Chairman. This is Bob Knadle of Commission staff.

I just wanted to point out a couple of things before we get into discussion and any issues the Commission would want us to address. There is one confidential item. If we want to get into some discussions on the capital structure and return on equity, we will need to go into a closed session on that. And there's a couple other items that may or may not be confidential, but if it does come up in the discussion, I will point those out.

And there's one other clarification, I guess, on the nonasset-based margin share and the 25 percent. If the company doesn't make any margins in the year, there will be no sharing. There's only sharing if the margins are positive. So if they lose money on these sales, that's not going to get past through the fuel adjustment clause. That's out of their own pocket, so to speak.

And then on the asset-based margins, you know, there's so much included on the rate case and whether there's going to be increase or decrease, that will be reflected in the fuel adjustment clause. I just wanted to clarify those two points.

Staff has a pretty detailed memo that will support the settlement stipulation. I'm not going to go into detail on that, but if the Commission wants to ask a specific question here or -- staff we're more than willing to address those.

We also have three consultants on-line that will deal with addressed issues, you know, that they addressed in the settlement stipulation also.

Thank you.

CHAIRMAN JOHNSON: Thank you, Mr. Knadle, Ms. Semmler.

My thought, and it's just a suggestion to try to bring some structure to our questions, is perhaps we would use the staff memo as almost a template of order to deal with things. So, for instance, we would take adjustments to rate base first and then go to operating and comment and go into rate design.

If there's a suggestion that works better for my colleagues, certainly I'm all ears.

Okay. With that then, let's go ahead and discuss any adjustments that were made to rate base. Anybody have any questions?

I'll kick it off. With regard to plant additions, I'm looking -- the pages aren't numbered, but I think it's page 3. You talk about number 2, eliminate the hoop link unit 3 super feeder tube's adjustment because the project is not complete.

And I understand the Used and Useful Doctrine, but when would this be complete? I mean, might there be some value in having some sort of adjustment on this front?

Kind of walk me through staff and the Applicant's reasoning on number 2 there.

MR. KNADLE: This is Bob Knadle with Commission staff.

The standards the Commission uses or staff uses and the Commission has adopted is the known and measurable. At the time that staff and the company entered into settlement discussions, you know, this was not completed yet. We didn't have the actual cost. What we did have is an estimated in-service date and estimated cost.

And what has been reflected in the plan addition is what has been completed and placed into service so we know the actual cost. And there also could be, you know, offsets regarding to savings related to these plan additions that are not known and measurable at this time.

CHAIRMAN JOHNSON: So is this not a good candidate for a CWHIP type treatment?

MR. KNADLE: There has been a couple statutes passed in the not too distant future that commissions cost recovery and environmental cost recovery, what the company could file under one of those two statutes. It would be a lot cleaner than trying to do it in a rate case.

What we'd end up doing is -- you know, what Commission has approved in the past and staff has always based their rate cases on is the historical test year adjusted for known and measurable changes. We start to get into the equipment area looking at our forecasted test year, which is a lot, you know, harder to, you know, justify and prove on everybody's parts, my opinion.

CHAIRMAN JOHNSON: And I suppose it's a matter of degree. I'm very supportive of a historic test year. It all depends on what -- you know, known and measurable can mean different things to different people. I've always talked to -- when the IOUs wanted to go to a forecast test year, I said, well, you know, the Commission's willing to take a reasonable view of what known and measurable is. And there can be plenty of adjustments. Just because you don't get to adjust every line item, doesn't mean you don't get to adjust a lot of them.

And I guess I'm hearing from you that this falls on the too speculative side for staff to feel comfortable trying to work this in at this time. Is that right?

MR. KNADLE: That would be correct. And basically by using historical test you're adjusting for known and measurable changes. As you can see, Otter Tail hasn't filed a rate case since 1987. There's a number of other electrical utilities that hasn't filed for quite some time. And that would indicate to me that, you know, the way we're processing these rate cases doesn't harm the company.

CHAIRMAN JOHNSON: Okay. So then on number 4, modify the adjustment, this deals with deferred income taxes. This was just an adjustment to better reflect actual?

MR. KNADLE: What the North Dakota investment tax credit did was is the company included some adjustments related the difference between book and tax depreciation for the years 2007 and 2008. We have picked up plan additions in 2009.

For example, the Ashtabula plan I believe went in service the end of '08 or early 2009. So by picking up that plan adjustment out that period of time it's appropriate to pick up the 2009 investment tax credit, the difference between books and tax as a reduction in the rate base.

CHAIRMAN JOHNSON: Then moving on to working capital, you know, number 2 notes modifying lead days to reflect statutory rather than actual payment dates. Why was that done? Why does that make sense?

MR. KNADLE: What it is is a time value of money. And, you know, in the statute there are statutory payment days when they're required to make these payments to the Government authority. And if the company volunteers to make this payment earlier than they have to, you know, the rate payer shouldn't have to be able to pay for that in time value of money. They don't have to do that. They won't get fined if they pay at the last day. So it's a voluntary payment on the part of the company which they don't have to do.

CHAIRMAN JOHNSON: Does basing it on a statutory date also -- I'm trying to work through this. Does that eliminate potential gaming where you can sort of manipulate during the historic test year when you're making payments that would differ from your normal standard operating procedure and nontest year? Does this eliminate that potential for gaming?

MR. KNADLE: As far as when you run it through the working capital calculation by doing it either way, it's not going to make that much difference. I mean, in dollar amount it won't. So I don't think the company -- it wouldn't be worth their while to try to game it, what you're talking about. Put it that way.

CHAIRMAN JOHNSON: Okay. Other questions on any rate base adjustments that were made? Let's go ahead and go to the operating income adjustments that were made.

Any questions?

With regard to the rate case expense, rather, on some exhibit I think it was listed as -- well, here on the memo it mentions a settlement increases these costs about $75,000 for the additional costs expected to be incurred by staff.

I saw in some exhibit that staff's estimates were estimated at $100,000. So why the differing numbers? Was $25,000 already worked in initially in Otter Tail's calculations?

MR. KNADLE: Yeah. What Otter Tail included in their adjustment was $25,000 for the staff to process the case. The statutory limit is 100,000. In the previous rate case for Black Hills Power & Light I believe it came in just shy of $100,000. I expect when all the bills come in in this case we're either going to meet or exceed $100,000 to process the case.

CHAIRMAN JOHNSON: You talk about the known and measurable fine line. This would be another instance where not everything's come in, but I presume in this case we're talking about relatively smaller dollars because they're a lot closer to billable than, you know, the hoop link improvements, that this does make more sense to work in at this time.

MR. KNADLE: Yeah. I would guess we're 99 percent sure we're going to hit the $100,000. That would be my opinion.

CHAIRMAN JOHNSON: Well, that's pretty good. 99 percent. So I was a little surprised that staff had pushed and received a concession to amortize the costs out over five years. I know it's been 21 years but, you know, we all follow the industry enough to realize that rate cases are likely coming more often in the future in this country than they've happened in the past 20 years. Is there the potential when you take a five-year look toward amortization that you could get almost pancaked rate case costs if you had a rate case within the next five years?

MR. KNADLE: In this adjustment here there's no true-up mechanism. As in the last case that was filed 1987, we allowed a certain amount of expense for rate case. We could amortize it over, you know, 3, 4, 5 years. The company has stayed out for over 20 years.

I mean, different methods you could do it. You could do a tracking method on it and then, you know, you'd get the actual cost and then you would determine if they undercollected it or overcollected it and reflected it in the next rate case.

We have opted not to do that in case. We expect the company is going to come in and file. If Big Stone II comes on-line, they will be filing for that for sure. It is anticipated they're looking at additional wind, and if they end up purchasing that as a purchase power agreement or if they own part of that plant, they'll come in for a rate case.

So, you know, my expectation is, you know, they're going to be in for a rate case, you know, around that five-year range or four.

MR. JACOBSON: You could also think of it as an incentive not to come in, which would be to rate stability.

CHAIRMAN JOHNSON: Sure. In this instance the mechanism we would be using for recovery, I mean, all of the risk falls on the Applicant. If they came in before five years, some of those rate case costs would just never be recovered on this rate case.

MR. JACOBSON: That's correct. But if they stay out for a long time, just like Bob said, they gain.

CHAIRMAN JOHNSON: You stay out for 21 years you -- yeah. That makes sense. You can collect on that rate case those costs for 21 years so. Other costs on operating income adjustments?

COMMISSIONER KOLBECK: On the economic development section of that they've got the $100,000 allowance for that. But they didn't include it in their -- or they increased their actual test year by 62,000, but then in the end it resulted in a reducing of actual expense by 81. Would you explain how that --

MR. KNADLE: This is Bob Knadle again. What the company did is requested 100,000 for economic development, no sharing, but what was actually in the test year was approximately $38,000. And that was related to one employee that is economic development employee they share between Minnesota and South Dakota so South Dakota got allocated a percentage of that. What the settlement does is basically take that 38,000 and shares it 50/50 between rate payers and the company.

COMMISSIONER KOLBECK: How did that result in a reducing operating expense loans by 81, though?

MR. KNADLE: What that would do is it would be a reduction from the company -- what we're looking at is a difference between what the company requested and what the settlement was. So it's a reduction -- they wanted 100,000. We ended up basically putting 19,000 in. So it would be a reduction of 82.

Does that make sense?

COMMISSIONER KOLBECK: It does.

MR. KNADLE: Sorry. We could have made that more clear, I guess, in other memo. Sorry about that.

MR. JACOBSON: I would also clarify in the other economic development programs that we've approved there's a reporting requirement or recurring approval process, and in this case that does not exist.

Taking into consideration it's a lower dollar amount, they may well use up, you know, a significant portion of their allowance just to make those reports and come before us for approval so.

CHAIRMAN JOHNSON: I can piggyback on that, Commissioner. So I know this is a bit of a briar patch I'm throwing us into but, I mean, are we just exacerbating the issue? I mean, we've had recent conversations almost as I'm talking. So I don't know if it's a discussion, but does this asymmetry with regard to our treatment of economic development, is that bothersome?

If they stay out for another 20 years, are we now today signing onto a mechanism that we know, in fact, is going to be quite different than we've got from other IOUs? And does this disparate treatment bother anybody else, and should it bother me?

MR. KNADLE: What we're looking at, roughly speaking, they have less than 12,000 customers here and the other companies what the Commission has approved is essentially $100,000. That would be 50,000 for the rate payer, 50,000 for the company.

And, you know, staff couldn't justify, you know, raising the economic development funds to that level for that few of customers. It's a lot bigger hit on that small customer base.

And so by having an employee that would, you know, dedicate part of his time to these different towns we thought that would be beneficial without doing any long study and, you know, have the company doing reporting requirements and that type of thing.

So basing on that, you know, I think this is, you know, the proper way to do it. And they still would get some economic development benefit for the different towns that they serve.

MR. JACOBSON: Always add that we can always send out a data request to find out what is going on and take appropriate action. We have the authority to take any action that we consider in the future.

CHAIRMAN JOHNSON: Yeah. And my concern doesn't have necessarily to do with what they're doing day to day. I mean, I don't know that I need to be looking over their shoulder. My question is a bigger picture one, which is I'm trying to decide in my own mind to what extent is investment and economic development an appropriate use of rate payer dollars. And, you know, you all kind of split the baby here, and that's probably a pretty good fault position. It just is odd to have us treat different IOUs differently.

Now, Mr. Knadle, your point about different size is a compelling one. I suppose a counterargument to that is doesn't Otter Tail Power service territory, couldn't that benefit more? Couldn't the return on your economic development investment potentially be higher than it would for an area that is already growing and would likely grow regardless of what economic development programs were put in place at the utility level?

Mr. Gerhardson, any comments from the Applicant on this topic of conversation?

MR. GERHARDSON: Yes. Thank you, Chair Johnson.

Otter Tail has had active development operations in the State of South Dakota. We've worked with the dairy industry several years ago up until today, and we continue to work -- as was mentioned I think by Mr. Knadle, we do have staff who are devoted exclusively to economic development. We also have our area personnel who are sort of more hands on on the ground.

We've had success. I think your comments were accurate. We have a different kind of service territory than some of the other utilities. In our other states we did actually have quite a bit of discussion on economic development to retain jobs as much as to grow jobs. And in fact probably I would say that's a much more important component for us and our service territory is retention of jobs.

From a cost justification standpoint, we see even on our electric system increased costs to other customers when jobs are lost and populations declined. There's more investment in a community, let's say, than there would need to be for a smaller population. So it needs to be spread out over fewer customers. So that's the benefit that we see.

We are comfortable with the settlement. We are -- we would be concerned, I will say, if we get into the reporting requirement with this small of a revenue requirement being -- creating a lot of reporting.

So, Chair Johnson, I'm not exactly sure which issue I'm addressing here. I'm addressing several at once probably.

But we're comfortable with the settlement. We think it is a fair resolution given the comprehensive settlement that we're entering into. This was not a large dollar item for either staff or for Otter Tail in the end, and we think this hits a spot we can live with.

CHAIRMAN JOHNSON: Well, and, of course, it's not lost on this Commissioner that -- I mean, everybody wants to talk about energy as economic development, but the biggest impact energy can have on economic development is keep rates low and to make an environment that, you know -- bills low generally equals a pretty robust economic environment in any case.

So I interrupted Commissioner Kolbeck. So I've got other questions on operating income, but I'll pause and see if you've got anything else in that arena.

COMMISSIONER KOLBECK: Tree trimming. You know, the settlement normalizes these expenses, but the -- did not adjust the test year for tree trimming expenses. Does that mean that the company will not be increasing expenses on tree trimming?

MR. KNADLE: No. What it means is the company didn't make an adjustment for tree trimming expense. The staff proposed adjustment. The company accepted it. They do have like a five-year tree trimming cycle, and the expense varies from year to year. So what they're trying to do is normalize the expense. And that's kind of what that accomplishes.

Then it generally -- the past rate cases what we do is we use this method for the next rate case. We'll just keep doing the same method. For example, storm repair expense and tree trimming expense are both based on a five-year average, so to speak.

So the next time they file a rate case staff would utilize the same five years so that way we're not picking and choosing the same way the company could pick and choose when they file a rate case and the expense is high. It just normalizes that expense. So it's fair to the company and the rate payers.

COMMISSIONER KOLBECK: So the tree trimming is still a very important aspect of --

MR. KNADLE: Yeah. Really important. The NERC standards there's fines and penalties and, yeah, safety and reliability is, you know --

COMMISSIONER KOLBECK: All right. Thanks.

CHAIRMAN JOHNSON: Just an add on question. I understand the interest in normalizing expenses. I think that's the right approach. But given we've had these new NERC standards as well as regional standards as well we're trying to normalize expenses but is there a new normal?

I mean, is looking back to the last few years going to really be indicative of the future? So maybe that's an opportunity for the Applicant to explain if these new reliability standards do change fundamentally the way they do business with regard to tree trimming.

MR. GERHARDSON: Chair Johnson, Commissioners, there are a number of things in the area of NERC that are increasing our expenses. There's just no question.

I think tree trimming is certainly one of them. We've had an active tree trimming program. We're conscious of tree trimming. It is a major component of our effective reliability -- of providing a reliable service.

I don't -- I think we're accepting of the adjustment because I think reason -- there are different reasonable ways to come to what is normal over a period.

We would probably get into the discussion that you've just had on known and measurable changes and what is too speculative, I think. Although we do see an increase in a lot of our operational costs to comply with increased NERC reliability standards. I expect those costs will increase over the next few years as our attention is more and more devoted to those standards, tree trimming and otherwise.

COMMISSIONER KOLBECK: I just wondered if you could explain the sale of steam to the ethanol plant. Do you expect that to increase? You're going to be -- it says you proposed an adjustment to it. As of January there will be a new change.

Are you going to be selling more steam? Are you going to have more byproduct off of Big Stone II?

MR. GERHARDSON: I may have to turn to one of our experts, as I am not familiar with this item as maybe Mr. Beithon.

MR. BEITHON: Commissioner, Pete Beithon. I'm the manager of regulatory economics.

I don't anticipate that we'll see a change in the amount of steam we sell. I think there were some adjustments in how that was billed, and now we're billing them more. And this adjustment reflects that increased revenue, and we expect that revenue stream to stay pretty stable at this point.

COMMISSIONER KOLBECK: Okay. Because I know of their -- at Big Stone I know that Jeff had mentioned there is not an abundance of steam. I mean, you don't have a lot of extra product, I should say, coming out of that plant. So that was just my concern.

MR. BEITHON: Right. Right.

COMMISSIONER KOLBECK: Thank you.

CHAIRMAN JOHNSON: Going to NSF check. In past rate cases we have allowed charges -- you know, higher, in fact, up to I think the statutory maximum. I mean, is $15 a pretty good -- I mean, trying to drive toward cost causer, is $15 a pretty good indicator toward actual cost?

MR. GERHARDSON: My recollection, and I'll look at Ron to see if I'm correct on this, I believe this was based on some cost studies as to what this cost us to process this.

MR. SPANGLER: You are correct. It was very close. I don't remember.

MR. GERHARDSON: And so Ron even figured the $15 was fair in our instance. So that is the increase that we proposed.

CHAIRMAN JOHNSON: Okay. Other questions on operational?

COMMISSIONER HANSON: Mr. Chairman, if I could, forgive me if -- I'm attempting to follow this on the computer as opposed to having paper. I had a number of questions.

But just trying to ascertain the effect on the direct or depreciation assignment versus allocation. Can you explain that a little bit and how South Dakota's being compared to other states and how it's affecting us.

MR. GERHARDSON: I'm going to ask that Ms. Brutlag respond to your question.

MS. BRUTLAG: I'm Bernadeen Brutlag, manager of regulatory services. The history goes back that there was a difference in rates in depreciation rates and depreciation components 20 years ago for about four years between mainly North Dakota and Minnesota. But South Dakota also about that same time had a rate case and had a different set yet.

In order to preserve the differences for each of the customers in each state, we directly assigned the depreciation reserve and depreciation expense rather than allocate it the way we allocate plant.

And we attempted to preserve that over these 20 years. Quite frankly, what happened is Minnesota and North Dakota were the two main drivers of that, but it's very difficult to maintain that -- to isolate that difference from what really occurs between when loads change among the states. And, quite honestly, we couldn't track it any longer. We don't know what that difference is.

In the case of South Dakota by eliminating that direct assignment it actually benefited. It reduced our revenue requirements overall for South Dakota because of what was on the books.

COMMISSIONER HANSON: That surprises me. I recognize how once you get into depreciation schedules you don't want to change it after you get going with it. But -- and I would assume that it would be extremely challenging to try to allocate who gets what and how much. But I'm surprised that South Dakota benefited when you changed that.

MS. BRUTLAG: Well, maybe I should point out that our overall depreciation systemwide didn't change. I mean, this was just an allocation or a direct assignment among the states.

And, you know, I'll have to be honest with you. It's probably the luck of the draw that South Dakota came out better when we went to an allocated process, back to an allocated process.

COMMISSIONER HANSON: Do you imagine that that's still the case, that we are still benefiting from that change?

MS. BRUTLAG: You will benefit now on because the direct assignment's gone, at least if you approve that. And we will now allocate our total depreciation expense and cumulative depreciation in the exact same manner that we allocate the plant that has produced that, that we're depreciating. So there's a match there.

And to me that's a better rate-making theory going forward. So it's equitable to all jurisdictions, we believe.

COMMISSIONER HANSON: Thank you. Thank you, Mr. Chairman.

CHAIRMAN JOHNSON: So KPA and utility management increases, I'm on the next page here, and in the filing itself I think there was some discussion of operation goals or operational goals versus, you know, sort of shareholder goals, stockholder goals. Walking -- give me some examples of each of those so that we've got a good idea here of how this applies and how it doesn't.

MR. GERHARDSON: Well, I think I can give a couple of examples. Mr. Brause may have to chime in and correct me if I'm incorrect. But I think maybe a good example of a shareholder benefit, KPA or KPI, the goal that we have and that we track and we measure is plant availability. That is, how often are our plants available?

And, in fact, we measure what's called equivalent availability. That is not only how often they're available, but to what degree. Are they available at 100 percent, 90 percent, 70 percent.

Obviously, by tracking that what we can do is because our power plants are lower cost than market is the more often they run and the better they run, the lower the cost the customers to refuel and the purchase power costs that are showing up in the FCA. So that's one real distinct I think customer benefit.

Maybe on the other side would be a shareholder benefit. That might be just your standard there are shareholder benefits if we perform financially well. Earnings per share might be something that we track that would generally benefit our shareholders as opposed to customers. Although there may be a crossover where our shareholders can benefit some from just performing well as a utility, certainly even in the equivalent availability.

Our customers also benefit if we're doing well for our shareholders in that we can raise capital more effectively. So there's some crossover, but generally I think the thought and the discussion is along those lines.

CHAIRMAN JOHNSON: Well, that was a little bit what I was driving at. There is some interrelativeness. I mean, if a double A costs X and an A minus costs Y, the benefits there aren't always easy to assign perfectly.

But I think I like where this settlement goes. Just trying to say, well, here are the more direct benefits. Not saying there aren't some indirect benefits to these particular operational goals. But just trying to draw a line somewhere. I think that makes sense.

So under payroll increases and in the middle of the paragraph staff memo says, The settlement modifies these adjustments by eliminating the 2009 wage increases for, and it has a list of employment classes. I mean, what's left out?

I mean, it seems like there's quite a number of classes listed there. I mean, who -- I mean, which wage increases were not eliminated?

MR. JACOBSON: Commissioner, the -- the Coyote union group was the one which was known and measurable, and that was included.

CHAIRMAN JOHNSON: And for all the rest of these negotiations or management decisions that have not yet been made to determine what compensation was going to be, and so those adjustments weren't made?

MR. JACOBSON: That's correct.

CHAIRMAN JOHNSON: Okay.

MR. KNADLE: Excuse me. That's just for 2009. They did have increases for 2008 that were known and measurable. Just wanted to clarify that.

CHAIRMAN JOHNSON: Good clarification.

I've got one more question on these operation changes, and it relates to the nonasset-based wholesale margins and specifically having to do with the fully allocated cost study.

And I guess I need some more information about what this looks like. I'm not familiar with this study. I mean, how often would it be done? Presumably annually. To whom is it submitted? What is the process for approval? Is this all occurring on the staff side?

And a question for staff first, and then we'll have the Applicant respond.

MR. KNADLE: Staff requested a fully allocated cost study through some data responses. At that time the company hadn't performed one yet. And in the process we were going through the data requests and that, and towards the settlement the company did provide, you know, a fully allocated cost study based on I believe it was December 2008, a time study of how their employees worked for asset-based and nonasset-based.

And then they developed, you know, a rate basically, you know, approximately 25 to 30 percent of the fully allocated cost study.

And I believe the company's going to continue to do this study and it will update it from time to time by going-forward basis and then staff would have a chance to analyze that in more detail when they file another rate case.

And on a side note, this is similar to, you know, what is being considered in North Dakota for the nonasset-based sales. I mean, they're in settlement negotiations. I have talked to the North Dakota Commission. It's ballpark with what happened in Minnesota. So, I mean, this is going to be a process that we may have to revise from time to time. It's kind of our first shot at it.

But I believe, you know, it's -- what this -- what these costs are going to cover is this is an unregulated business. And all the costs that can be directly assigned, the cost revenues are directly assigned, not including the cost of service.

Essentially what we're talking about here is employees that are sitting there doing asset-based sales and nonasset-based sales are the same people. Okay.

And so what you have to do is, you know, try to figure out a method that's fair to both the company and the rate payers to determine what portion of their time is spent on, you know, which -- nonasset-based or asset-based sales.

That is going to change over time, I imagine depending on what the market is. And there may be times they don't do that much asset-based sales. It fluctuates just as the asset-based sales does.

But I believe, you know, this is a fair way to start with the sharing mechanism.

CHAIRMAN JOHNSON: So just I guess when I read the cost study I was envisioning that this would be an analysis of the energy purchased and the energy sold. I mean these are paper transactions. Not paper anymore.

But it sounds like you're talking more about a labor study, which I would presume would be relatively small dollars. Isn't the more important numbers probably the large numbers that are of energy that's been purchased and sold, and does the study take into account that or is there any verification how that -- or they put that 25 through the fuel adjustments?

MR. KNADLE: That's going to get through the fuel adjustment only if it's positive based on the margin.

CHAIRMAN JOHNSON: But then we don't get any review of that outside of the regular review of the fuel clause that takes place, and we have 10 days to review; is that right?

MR. KNADLE: Yeah. They're going to provide that adjustment on an annual basis because at that point in time we'd have a chance to look at what work papers they supply us.

CHAIRMAN JOHNSON: But this cost study would have to do with labor allocations.

MR. KNADLE: Yeah. Incremental cost, how the personnel spends it's time. It will change over time, I expect. I don't know how much it's going to fluctuate. Maybe the company would have more information they wanted to add to the discussion.

CHAIRMAN JOHNSON: But this would be a potential item where if we see a relatively high level of consistency from year to year that maybe with the next rate case it would be a set allocation as opposed to a cost study-based number.

MR. KNADLE: That's a possibility. We'd have to look at it that point in time.

CHAIRMAN JOHNSON: Yeah. Sure.

MR. JACOBSON: Commissioner, if I could, one thing that happened, you know, we're aware of back in the California crisis of 2001 we saw energy purchasing sales for our companies explode. And rather than have a fixed amount based on the test year activity for this percentage mechanism in place, it will follow those big gyrations in sales and work out much better.

CHAIRMAN JOHNSON: Oh, I agree with the mechanism to capture some of those costs. And I compliment staff on managing to negotiate a 25 percent share. I think that makes sense. I do think there probably is great annual volatility.

To me it just seemed odd because I wouldn't expect a lot of annual volatility in the labor costs. And so a cost study on that component would surprise me. That being said, I completely agree there should be an annual adjustment for the actual margins of the sale of electricity.

Other questions on operating expense adjustments?

Mr. Rislov.

MR. RISLOV: I just wondered if it's appropriate for me to jump in or you wanted the three Commissioners to go first. Because I have several. And I want to get everybody involved if I possibly can. I hate to think of them wasting their time and their trips to Pierre.

I just want to make sure on rate case expense there is no true-up. Whatever happens, happens. When they come in and file the next rate case, you know, if they collect 40 or 60, whether it be two years, three years, five years, they collect 100, what's past is past. Its a clean slate. You go forward with the rate case expense on the next case.

MR. KNADLE: It's a clean slate.

MR. RISLOV: Okay. That makes it very simple.

Industry and association dues. TLB-1, Schedule II. And actually if a Commissioner wants to jump in and ask a question now, I think it would be a perfectly appropriate time.

CHAIRMAN JOHNSON: Well, I asked Mr. Rislov a question on Friday so I showed my poker hand to him. So if it's the question I'm thinking, it's not a particularly large one so maybe I'm missing something, Mr. Rislov.

Like line 17 I saw the Minnesota Electric Association's on there. I don't see a South Dakota counterpart. Do those costs flow through a different cost area? And if so, what other types of association dues flow through that other cost area? Is that what you were driving at, Mr. Rislov?

MR. RISLOV: Yes. We see nothing about any South Dakota association. Maybe they're free, I don't know, or whatever. Just a question. What comprises this list, and what would qualify one not to be on this list?

MR. GERHARDSON: I'm going to ask, Mr. Beithon, are you prepared to speak to that or Mr. Spangler? And one moment. I don't know that I have a copy of that so I'm going to see if I can look at one.

CHAIRMAN JOHNSON: We see the South Dakota Board of Technical Professions is on line 32, but it appears to be the only South Dakota-specific dues.

MR. KNADLE: Just for clarification, talk about the South Dakota Investor-Owned Utilities Association, would that be correct, as a counterpart?

MR. GERHARDSON: Can I hear that one more time? South Dakota Utility Investors? Is that what you --

MR. KNADLE: I think it's the South Dakota Investor-Owned Utilities Association.

CHAIRMAN JOHNSON: But I don't think that's the same of the group. I think it's South Dakota Electric Utilities.

MR. RISLOV: Well, there's two groups. Nettie Myers heads the one group. At least she's the person we see and Steve Willard is with the other group. So whatever their name would happen to be.

MR. GERHARDSON: My assumption is that -- and I was trying to get to -- my assumption is that this -- and you guys will correct me if I'm wrong, that this would be those things that appear above the line, that those --

MR. RISLOV: You had already removed the others.

MR. GERHARDSON: We will have already removed those that we did not feel are appropriate for recovery from rate payers. So my assumption is that those dues are paid by us, but that they are not -- they do not comprise any component of our revenue requirement. They are below the line.

MR. RISLOV: Okay.

MR. GERHARDSON: So there are memberships to which we would pay dues that would not be reflected in our revenue requirement or our rates, therefore.

MR. RISLOV: And I understand looking at Minnesota Electric Association, Incorporated actually wouldn't be a counterpart. That would be a group of utilities who are working together to solve common problems. Not that Steve Willard's group doesn't do the same, but that's more of a legislative lobbying function rather than I'll call it engineering functions or operations functions; is that correct?

MR. GERHARDSON: That sounds correct. I am not particularly familiar, but I see nodding.

MR. BRAUSE: That's correct.

MR. RISLOV: Yeah. Where the annual meetings of this group may be in Redwood Falls rather than in

Honolulu.

MR. GERHARDSON: That's correct.

MR. RISLOV: Okay. And because perhaps I've testified on this issue in the past and actually I think I've almost copied Mr. Tower's word for word from earlier testimony, I'm not sure, but there's been some change in FAS 106. And I would consider it looks like it's a fairly big change.

And just for my edification as we follow this through in the future, I'm really curious about what has happened in here and what the thought processes were and what affect this process has.

MR. GERHARDSON: Again on FAS 106 I'll turn to Mr. Beithon or Ms. Brutlag.

MR. BEITHON: Commissioners, Mr. Rislov, when FAS 106 came into existence Otter Tail didn't request special treatment. I think South Dakota was allowing special treatment for us at that point. We have in essence eaten the transition obligation up until this point.

All we're asking for is to switch over to 106 at this point to be consistent with the rest of our jurisdictions and also to take care of the remaining few years in the transition obligation.

MR. RISLOV: If I could interrupt, it might be easier this way, but when did you start amortizing the transition obligation roughly? I don't need an exact date.

MR. BEITHON: '93 about.

MR. RISLOV: So we're about 16 years into the amortization, which it's a 20-year period; right?

MR. BEITHON: Right.

MR. RISLOV: We've got about four years left.

MR. BEITHON: About four years left.

MR. RISLOV: And I see below, right below that, we talk about, you know, I assume the next FAS 112 postemployment, FAS 106 postemployment, FAS 187 pension, I assume that's the current portion of the pension costs rather than the amortization; is that correct?

This is on staff's memo, if you have that. And maybe I could just ask the question and make it simpler. But I was --

MR. BEITHON: I believe you're correct.

MR. RISLOV: And maybe I shouldn't have been surprised but the thought was, and this goes back 20 years, that eventually the PAYGO obligation would become very large as people retired and we were seeing, you know, a large group of retirees. And I may be misstating this, but I know there was concern that it may become a very large annual expense in the future.

MR. BEITHON: I believe you're correct. I'm trying to recall what all went into this discussion. But -- and even in my testimony. But I believe by doing what we're doing here the South Dakota rate payer's slightly better off.

MR. RISLOV: Well, but I guess what I was saying is it surprised me because I assumed the current obligation plus you'd be looking at the one year amortization of the transition obligation within the current obligation.

Those would comprise this amount; is that correct?

MR. BEITHON: I believe you're correct.

MR. RISLOV: You would compare that with PAYGO? You did a comparison of what PAYGO would have cost you this year?

MR. BEITHON: Correct.

MR. RISLOV: As in that matter, is this correct -- okay. PAYGO would have still been, as I see, $30,000 less than the combination of these two?

And maybe the question I should ask is what's the current obligation under FAS 106 without the amortization compared to what the obligation would have been with PAYGO? If that makes any sense.

Mr. Beithon, I think if I could be provided that later. I don't think that will make much difference. If we're 16 years in the transition obligation, you're going to eat it, which I think is an excellent choice on your part.

You know, I would be curious to know what that number is. Because, you know, some of the -- some of the estimates back in the late '80s may or may not reflect what's actually happening now, and I'm just curious about where this has gone. Because undoubtedly this issue's going to come up again another rate case. So I guess it's more curiosity point. Don't waste much time looking it up now.

MR. BEITHON: I'd be happy to provide that information for you.

CHAIRMAN JOHNSON: Let's just check with our reporter real quick.

(Discussion off the record)

CHAIRMAN JOHNSON: We'll take a short 10-minute break, if you don't mind me interrupting your own questioning.

Have you got one or two before we finish up?

MR. RISLOV: Yeah. It will give me a chance to catch my second wind.

CHAIRMAN JOHNSON: Great. We will be off the internet and recess for 10 minutes.

(A short recess is taken)

CHAIRMAN JOHNSON: Mr. Rislov was in the middle of some lines of questioning dealing with operative adjustments.

Mr. Rislov.

MR. RISLOV: I think I have one more that's on payroll increases. And I believe I heard Mr. Knadle say they annualized 2009 to an extent and 2008 and included adjustments for 2009 and 2008.

I guess I want to ask him if you didn't annualize the payroll increases that occurred in the test year?

MR. KNADLE: Yes, we did.

MR. RISLOV: So you actually adjusted for three years, not just two? At least in part for three years.

MR. KNADLE: Yeah. The test year is 2007. The annualized increases during the test year increased in 2008 and partially 2009.

MR. RISLOV: Okay. Thank you.

CHAIRMAN JOHNSON: Other questions on operating, adjustments to operating?

Okay. We can always come back. If there are no further adjustments on operating, the next section of the memo was cost of capital and rate of return.

Now, of course, I won't mention the recommended return on equity, but I did want to ask if there was a draft testimony for staff's cost of capital consultant and, if so, if there was a range given for a reasonable return on equity and, if so, what that range was.

UNIDENTIFIED SPEAKER: Bob, how do we want to handle this is that --

(Discussion off the record)

MR. TOWERS: Bob Towers. I'll turn it over to Basil Copeland. But I can say I've just recently reread that draft testimony, and the range was 9 to 10 percent. 9 percent.

CHAIRMAN JOHNSON: Okay. Perfect. 9 to 10 percent. That's what I was looking for. Great. Other questions on cost of capital and rate of return?

Okay. With that, we'll proceed to rate design issues. Questions on rate design issues.

COMMISSIONER HANSON: I noticed the -- I take a little bit of exception with the position that the staff has taken on this. I personally favor blocked rates, but I favor them in the opposite direction. I think that if we're going to have efficiency with them, we need them to be increasing as opposed to decreasing. I appreciate the challenge that you had and you don't want to have rate shock, so to speak.

Could you explain how long it might take before we can get to a flat rate under the present system?

And then a second question for Otter Tail Power, is there any desire on the part of OTP to go to a step -- to a block rate that's increasing?

MR. THURBER: This is Jon Thurber, staff. When we looked at their flat rates the high usage customers were receiving an increase too high above the average annual increase, what we came across for the class revenue study.

We had a little bit of an issue in terms of how with a flat rate the fixed costs would be spread across all rates and not just certain levels of usage. So the large customers would be paying a greater share of the fixed portion of the costs.

In terms of how quickly we can move towards a flat rate, we focused -- along with, you know, looking at the costs, also looking at the bill impacts of these changes. And if Otter Tail does, you know, bring Big Stone II online and add wind, you know, we can continue to move towards that. We just, you know, are a little more reluctant to have the high usage customers receive a 25 percent or so increase.

COMMISSIONER HANSON: The 25 percent on their overall rate or just on that portion of the block?

MR. THURBER: Well, it would be 25 percent of the rate during the summer. You know, it depends on their usage levels. But overall because of the summer/winter differential and the conversion to a flat rate, those high usage customers were really going to be bearing the brunt of the burden of the increase.

COMMISSIONER HANSON: I guess on a fairness doctrine you then assume that it was not fair to have that burden on the larger users as opposed to spreading it out on the smaller users. But speaking somewhat on a philosophical level, doesn't it make sense to have a heavier burden on larger users because they're the ones -- the causers of the additional infrastructure, improvements and such?

And perhaps Otter Tail might want to tackle that one, unless Mr. Thurber has --

MR. THURBER: At the same time, the high usage customers will be contributing more towards the overall system as well. It is a little -- like you stated, Commissioner, it is a philosophical concern.

But, you know, we're looking at the overall costs for the customers.

COMMISSIONER HANSON: I don't see a right or wrong here. I'm just curious as to what was going through your process there. Thank you.

MR. GERHARDSON: Chair Johnson, Commissioner

Hanson, Commissioners, you know, from the company's perspective, you know, the way I can describe the history of this, when we -- we filed a case in Minnesota before we filed this one. In that case we filed a moderated version. We did not eliminate an entirely declining block of rates in our initial filing.

Commission and staff in that case wanted us to go further, and in that case they chose to eliminate all of the declining block rates in their decision.

We followed suit in this filing and in North Dakota. We've seen moderation. Now the rationale for moderation is not to -- to not get to a flat rate structure. The rationale for moderation I think is whether -- you know, is a judgment call as to whether customers can change abruptly their behavioral patterns.

And, of course, the larger users may be larger users because of purchases they made in heating equipment or other things over periods of time so they may not have the kinds of abilities to adjust consumption patterns down as quickly as we might think. So we see some benefit in moderating in certain instances the imposition of a rate change.

Now I think our general philosophy is we were moving towards and we would expect to take another step and maybe a full step to a flat rate in the next rate filing. In fact, my gauge would be personally I think we could probably get there. But these considerations will continue.

Now with respect to inclining block rate structures, I would say we see a conservation benefit whenever you do that. Whenever you add costs incrementally as you increase consumption you will then encourage the decrease in consumption. But these same considerations will have to be taken into account. And that is how much flexibility do our customers have?

So while I don't know that there's ever been a policy stated by the company as to our position on inclining block rates, I think right now we're shooting to get to a flat rate structure.

COMMISSIONER HANSON: I appreciate those comments and the challenge that it poses and the desire not to create a rate shock as you're going through the process. Also appreciate the -- on a different subject, the urban/rural customer charge differential and doing away with that. I think that was a good move on your part.

Thank you, Mr. Chairman. I may have some other questions on this portion, but I'll let others finish up.

CHAIRMAN JOHNSON: Mr. Gerhardson, you sort of talked generally about, you know, heating and cooling equipment, but to be specific there may be some people who went all electric in Otter Tail's service territory that made that investment with believing that their rates would have some predictability to them and an adjustment too far isn't fair to them.

I mean, am I right on the specific example?

MR. GERHARDSON: Well, I think you're right. And, you know, it's a judgment call as to when you implement. We have to implement it at some point in time, a change. The question is how far can you go. And reasonable minds may differ as to impacting certain customers who have made decisions based upon that.

But you're absolutely right. Those are absolutely the kinds of considerations that are going into moderating some of these proposals.

CHAIRMAN JOHNSON: And, of course, there can be some conservation benefits to an inclining block rate. You know, one has to ask is that the best way to introduce efficiency?

Because what you give up is it can have a detrimental effect toward manufacturers and large energy users in an area. Maybe cause people to make different location and relocation decisions based on what their energy bill would be. Am I looking at that issue right as well?

MR. GERHARDSON: Absolutely. Those are all sort of economic considerations that are going into the decision-making on rate design. There are several factors that are in play at one time that go into what is the rate design that any company should have and when they're going to make a change structurally how quickly can they make it? I think the settlement hits a sweet spot for us in South Dakota for the time.

CHAIRMAN JOHNSON: I'm not sure I understood the interest of Otter Tail Power to have a facility charge along with a customer charge as opposed to just a larger customer charge. I mean, give me firmer understanding of why Otter Tail wanted two items.

In fact, I think in some of these classes there continue to be two line items. What's the benefit of having those two lines rather than just one line? To me general terms like facilities charge and customer charge don't provide additional transparency. Where am I mistaken?

I mean, I have a hard time telling you what's in one versus what's in the other.

MR. GERHARDSON: I think maybe I'd ask Mr. Prazak to chime in. I think our effort was intended to be a greater specificity as to what is going into a rate. That is, facilities charges are related to facilities.

That is the service drop and the equipment if I understand correctly. Customer charge are those things that are more sort of office things, billing, equipment.

Mr. Prazak, maybe you can correct probably what I've erred in here.

MR. PRAZAK: Dave Prazak, Otter Tail Power. Mr. Gerhardson's correct. We want to make a differentiation between some of those back office type costs versus facilities. And in Otter Tail's case we have customers that have non-electric heating, and they have smaller demands so their portion of a transformer is much smaller than a customer with an electric heating system. In fact, it could be four, five times greater.

So the price signal that we're sending to those customers that require more facilities is to again cost causation paid for those facilities.

CHAIRMAN JOHNSON: Are you talking about on the residential side?

MR. PRAZAK: Yeah. That's the example I'm using.

CHAIRMAN JOHNSON: But I just -- I found on the residential side there was just a single -- I mean, there was the residential, and there was residential demand control. I didn't see a residential electric only rate. Did I miss something?

MR. PRAZAK: No. You didn't miss anything. Customers that do have electric heating 100 percent, they can still take service on the residential rate. It might be a little bit more expensive. They decided not to be controlled. So in those cases that can happen where they have those different facility sizes.

CHAIRMAN JOHNSON: But I didn't see where the facilities charge would vary from residential customer to residential customer. I mean, if that's the rate you're in, that's the facility charges you pay. So I don't think I understand the marginal differences you're talking about.

MR. PRAZAK: Okay. If you dig down deeper into the rate design part we have in our testimony, we would have a chart that would show different levels of customers. And we did choose just to stick with one flat charge for all, but we did separate them.

CHAIRMAN JOHNSON: But to me I don't know what you gain by having two line items. You know, if it's going to be a flat charge and not really particularly directly related to the cost of that particular customer's facilities, I mean, I guess I would agree with staff I'm glad the settlement has just that one line item. But with the other classes that continue to have two line items, both customer and facilities charge, does that really add to people's understanding of what they're paying for? I mean, obviously you think so. So help me get there.

MR. GERHARDSON: If I may just chime in, I think that -- I think in theory what we've been trying to do is head to the granularity that we talked about, to separate those charges. Because they may change from rate case to rate case.

We're not going to change them in between, absent extraordinary circumstances. But we could see that the ability to do the back office stuff goes up at a higher rate than facilities or facilities go up at a higher rate.

I think that the general goal is to reflect costs in the best level of granularity. I think reasonable minds certainly can differ as to whether customers are going to understand that level of specificity. I think we were willing very quickly to move towards a single line item that would combine those two charges.

For instance, on residential that didn't seem to be much bang for the buck on that so it was better just to combine those two. I think for the larger, sophisticated customers we may see some benefit, certainly in the instance where the facility charge varies. And I do think there are several of our rates, and Dave correct me if I'm wrong, that is the case. The customer charge would remain fixed. They're only going to get one bill. But the transformer size may vary, and it may vary the amount of that facilities charge.

In that way there is a cost reflected in the type of service that they have elected. This is not a volumetric kind of charge that varies depending on the amount they use month-by-month. It's really when they're deciding as to what facilities to install to provide service. They may have that reflected in their bills on a going-forward basis.

So some thought is that cost causation and reflecting the costs that are caused by an individual customer on their bills helps them to make decisions more accurately, I guess.

CHAIRMAN JOHNSON: See, and I think I'm fine with that because again treating residential customers differently than the larger, more sophisticated customers I think is fine. But it's interesting. We just had a resolution passed by -- a regional farmers union group said to Northwestern, your bills are too confusing, there are too many line items. I wonder if some people don't feel like this is just one more way to be nickeled and dimed on their monthly bills.

Now we know that's not the case. We know all of these costs are supported. Most people don't understand the interplay between what you do and how you're regulated.

I just wonder to me, though, transparency helps when people can -- with greater understanding allows them to improve their lives. Because we're not talking about volumetric charges, because we're talking about fixed charges, I'm not sure I see that link between greater -- and I wouldn't even call this much greater granularity.

I know you've got two line items. I'm just not sure that it is very easily understandable to the common person what that means, what those two items how they exactly differ. Now granted with the larger customer you'll explain and they'll get it. But they still don't have much of an ability to change any of that.

With that being said, let's give it a shot. It was eliminated for the smaller customers. I think that was the right thing to do.

So talk to me a little bit about the classes that were eliminated. In your filing as well as in staff's memo there is some good space spent describing the fact that -- it's tough to get around rate shock when you start talking about increases of this size.

I know we're only talking about 72 customers, but from a cost benefit analysis does it make sense to get rid of these rate classes? Was it causing detriment or was it an administrative burden to administer a class that maybe only had four customers or 70 customers? Your thoughts.

MR. GERHARDSON: Well, Chair Johnson, Commissioners, you are actually hitting on one of the difficulties with the -- the vast majority of these, there's 68 under one of the rates, there's four under the experimental rate.

And I think what I'd do is I think Mr. Spangler's most familiar with the operational challenges of the rate that includes the 68. There are what I would say are technical and administrative difficulties in ensuring that the folks that are taking service under those rates are having the rates applied correctly.

And, Mr. Spangler, I guess I'd ask that you address that.

MR. SPANGLER: Chair Johnson and Commissioners, my name is Ron Spangler. Mr. Gerhardson is correct. The electric climate control rate, there's basically three different discounts those customers can qualify for.

One is based on the connected cooling, heating, and cooking kW that they have installed at their locations. One of the administrative difficulties that we have is the connected kW that somebody has today could change tomorrow by a piece of equipment failing. They could add new equipment and those types of things. We have -- even though there's not a tremendous amount of customers on these -- in these rates, it's difficult for us to be able to go in and inspect those locations from time to time.

We have the ability to do that, but it's just been something that's been very difficult for us to do.

We did do some analysis on these customers, and some of the 68 on the electric climate control rate there are some of those customers that would benefit. Depending upon what their kW was over the last 12 months, we would switch them to either the under 20 kW or the over 20 kW and greater rates. Some of those customers on the lower end actually would benefit by moving to one of the general service rates.

And as Mr. Gerhardson did mention earlier today, we do have an effort that we are ready to do to contact in both writing and personal contacts with those customers on the change if you were to approve that today.

CHAIRMAN JOHNSON: So is it largely because of the administrative burden you described that these rates were essentially consolidated -- I mean, eliminated is a better word.

MR. SPANGLER: And to be quite frank, the rate schedule is very, very difficult for customers and in some cases my own and myself I've been at the company for about 13 years and it took me a very long time to understand the rate itself. So it's -- it's very, very difficult for both customers and employees to understand in some respects.

So I think both the administrative difficulties that we have, and the understandability is probably one of the other reasons.

CHAIRMAN JOHNSON: So to shift to these rate classes where a fuel adjustment clause is being implemented, I guess my big question on that is, you know, why in the world wasn't there a fuel adjustment clause put in in 1987? I mean, that -- that seems to be an odd rate treatment given what I know about how the Commission has treated rate cases back far before 1987.

Any insight? Does Otter Tail have any insight?

MR. GERHARDSON: You know, if I may, Chair Johnson, this predates pretty much all of us in 1987, the last rate case. We did examine that and actually -- oh, it doesn't predate all of us.

And it was universal across our three states, this phenomenon that these rates were all without fuel clause in all of our states.

Our view is the same as yours, that the impact that's occurring now possibly wasn't anticipated that there would be sort of a jump for these customers because they hadn't been seeing the incremental costs in the fuel clause. So whatever the rationale was, it may have been that this consequence was not discussed at great length.

We think that's a good reason to add the fuel clause now, so that that doesn't occur a second time. I don't know if I've explained or answered your question. I guess maybe I'd turn to Mr. Beithon and say do you have some sense of what was going on then?

MR. BEITHON: I think part of what happened was we -- though anticipated going 20 years, the last time we filed we've been filing every few years. We were able to adjust those rates at that point and not have the fuel clause almost because our rates wasn't creating much difficulty.

Other thing is I don't think that at the time of our last rate cases energy was as big of an issue. We didn't see the energy prices rising as quickly. We were more worried I think about capacity at that point in time. So just plain didn't anticipate in that last case that we were going to have an issue with this.

CHAIRMAN JOHNSON: Well, and certainly in the '80s for most utilities in the area they were in an excess capacity situation and if you think you're only going to be out for four to eight years, probably not an issue you worry about as much if you're going to be out for 21 or 22.

Other questions on rate design issues?

MR. RISLOV: I would have a couple if you three Commissioners are done.

I should note that in the fuel clause what makes that really odd is that they're all interruptible rates so the fuel clause would have been the appropriate application in this case because demand clause would have been de minimus under an interruptible rate.

So, yes, I was here at the time it. No, I don't recall. I'm going to blame Minnesota.

CHAIRMAN JOHNSON: A fine default position.

MR. RISLOV: You know, and maybe -- I'd like to talk about the rate design philosophy too because you did make a change and you did say you want to go to flat rates. And Commissioner Hanson has talked about declining block rates but I'm going to make an observation and you comment on it.

I think -- there's a lot of problems with inclining block rates making revenue requirements and a number of other procedural problems.

But I foretell that we'll be looking at smart grid type applications and marginal cost rates, and inclining block rates will really not be part of the equation in the future. Would you comment on that?

I mean, do you see any -- does that strike you as possibly true?

MR. GERHARDSON: That strikes me as possibly true. And if I may, Commissioners, and Mr. Rislov, I mean, that is in a way one reason it would be difficult for us to take a firm position on inclining block rates.

We do think that there are technological advances occurring. There are other discussions about the best way to achieve conservation. Inclining block rates certainly may be a component of that. They are used in other states in other contexts. For us right now again probably the more important goal is is to do what we're doing in phasing out what we've got as declining block.

MR. RISLOV: And I'll have to admit. In the past I have liked the multiple blocks on declining block rates because it's been my belief that tends to follow cost and Commissioner Hanson again brought up marginal cost, concerns about adding new plant -- if I could put words in his mouth liberally.

I guess my question would be this: Because you have flattened the rate blocks, are you concerned that you may be looking at a situation where you may be causing some of the larger users to fuel switch, which may not be an efficient outcome building fixed costs into these rates once you get past the 4 or 5,000 kilowatt hour per month level?

MR. GERHARDSON: Commissioners and Mr. Rislov, I think that as we look at rate design, and we have made some significant changes in several aspects of our rate design not only in this state and others, we have considered what that might do to consumption and whether it would alter consumption for any range of our customers. Those are hard things to predict and study in some ways.

My sense is they are considerations of ours. We don't feel that the settlement or even our proposal would have had the kind of dramatic effect that caused this grave concern. I think that's what I can say.

Would it have some? In a way it is intended to have conservation. But you're right. Fuel switching would not achieve a conservation goal either.

MR. RISLOV: Well, and my concern is that if we drive people to say fuel oil or propane and you're adding wind facilities at this point, it may be more appropriate to provide incentives for people to use electricity rather than other fuels. That's got to be a consideration I would think as you flatten these blocks to the extent fixed costs are built into what used to be the tail block of those rates.

MR. GERHARDSON: Absolutely a consideration and a concern. And we agree with you wholeheartedly that fuel switching of the type you're talking about wouldn't achieve a conservation goal.

MR. RISLOV: Have you done any work in determining whether or not -- okay. We can talk about a 1,000-kilowatt-hour user, a 3,000 or a 5,000 but, you know, obviously when one's talking about adding facilities we're talking about peak load. And most of these rates are -- when we look at moving forward, whether it be within MISO or even within the utilities trying to avoid adding additional facilities to serve the peak load, do you have any sense of whether flattening these blocks will, in fact -- you know, and placing those costs on larger users if that will have an effect on peak load reduction or I guess a better load factor than by maintaining the declining block rates as they were?

MR. GERHARDSON: I would have to say that I'd have to defer to Mr. Prazak on that. I am not aware of any studies we've done to reflect that. I can't -- I'm trying to think through sort of how the dots would have to connect.

MR. RISLOV: Well, I guess my concern is as Commissioner Hanson expressed, you know, to the extent you don't have to be building generation transmission there's a benefit on the marginal cost basis.

And I guess I'm asking this for my own education. I mean, if there's anything pointing toward flattening these blocks as to eliminating the peak load, you know, within the system, you know, if there's a connection or percentage that can be applied to it.

MR. PRAZAK: Dave Prazak. Mr. Rislov, I think you bring up a good point, and that's one of the reasons that we've actually added some new rates to our arsenal, I guess.

And one specifically is our time of day rate, which actually shows on peak costs, shoulder peak costs, and off peak costs. And that gives a lot of price transparency to those customers who may want to take advantage of those and decide to move load and take advantage of the off peak rates or shoulder rates and avoid some of those on peak rates.

MR. RISLOV: But in general, you know, as far as customer's concerned within what I call the more generic rates, there is really no hard data showing that two blocks, for instance, will work better than three or even a flat rate necessarily will work better than two or three; is that correct?

MR. PRAZAK: Well, all I can say is in our experience so far we're seeing customers in Minnesota who are on flat rates move more towards the time of day to take advantage of those different cost differentials.

MR. RISLOV: Okay. So even though you can't necessarily separate it within the -- you know, I'll call it the combined rate, you are seeing them picking options that would look more like a marginal cost understanding on their part where they can lower their -- okay.

MR. PRAZAK: Yes.

MR. RISLOV: Okay. I understand what you're getting at. Good point. Thank you.

CHAIRMAN JOHNSON: We're through staff memo. I've got sort of three assorted questions, and we can sort of open it up to assorted questions.

But my first dealt with the -- the filed notification that would go to residential customers. On the back page of that you've got some information on residential demand control. If there are only 5,600 folks on the residential demand control, does it make sense -- I fear that could be confusing to folks just on the normal residential rates, that the front page deal with them and the back page essentially deal with something they don't know anything about and --

Any thoughts on whether or not this is the right thing to send out?

MR. GERHARDSON: I'm going to have Mr. Spangler address your question.

MR. SPANGLER: Chair Johnson, Commissioners, this is Ron Spangler again. Pardon me.

When we developed the customer notice we were looking at the South Dakota rules that require notification. And it talked about different levels of comparisons with present rates to new rates. And when you look at the -- the classes that we have, our residential class makes up both the residential and the residential demand control rates.

And from my perspective when we were developing the notice I wrapped both the residential and the residential demand control in the same residential class as required by the rule.

Now if you look at the second notification that we've developed, I believe it does have both the residential and residential demand control on that notice. That notice wasn't specifically going to go to either residential or residential demand control customers, but depending upon how you wanted to work this, we can make it so that the residential demand control was not on the residential notice.

But I guess I would have to defer to the attorneys to tell us whether we could do that within the rules or not.

CHAIRMAN JOHNSON: Staff, would that raise any concerns? I hesitate to give people a whole bunch of information on a class that doesn't pertain to them.

MR. JACOBSON: You mean, in other words, have a separate notification for regular residential and -- no. That's fine, if it administratively can work for the company. That would be preferable.

CHAIRMAN JOHNSON: Well, and perhaps Mr. Spangler and the Applicant -- I'll just make my preference known. My preference would be to have separate. But if in discussions with staff and internal attorneys you determine you don't think you can under the law, that it will hinder the rule, that's fine. Proceed. But my preference would be to have separate notices.

MR. GERHARDSON: Chair John, maybe if I could -- you know, I haven't asked Ms. Semmler about this, but I don't see any reason if the Commission's order wanted to reflect that that was the preference of the Commission, I think we could treat it as a rule variance to the extent this is the rule.

Mr. Spangler and I didn't talk about this at any length. I certainly think it's within the spirit of the rule.

MS. SEMMLER: I agree. Yeah. I don't see a problem with our Administrative Rules and compliance if it's two separate.

CHAIRMAN JOHNSON: Yes, Mr. Spangler.

MR. SPANGLER: I just wanted to make one more comment. Mr. Beithon reminded me the residential demand control there's only just under 500 customers in South Dakota on that. I think we heard 5,600. That might be a system wide number.

CHAIRMAN JOHNSON: But if that system -- okay. Yeah. I suppose 10 percent would make sense. But I had presumed -- and I'm looking specifically at -- oh, you know what I bet I did. Took bills and converted that to meters. And I didn't divide by 12. Got you. Perfect.

Well, frankly then that probably makes it even more of interest to me to try to have the separate notices if we're going to confuse, you know, the 11,000 by information for the 500.

MR. SPANGLER: I do want to make one more if I could, Chair Johnson. I do want to talk to our technical people when it comes to stuffing the bills whether we make sure that we can get it based on rate and the residential revenue classes.

I believe we can, but that might be one reason why we might have to do something just slightly different.

CHAIRMAN JOHNSON: Well, if the Commission, you know, approved the settlement, let's have that my preference would be to have the Order be silent on this whole issue. You all know the preference of at least one Commissioner. And if you technically can do it, then please do.

MR. SPANGLER: Okay.

CHAIRMAN JOHNSON: Make sense? Okay.

What is the -- for residential what is the average monthly kilowatt hours used? Ballpark.

MR. PRAZAK: This is Dave Prazak. I think it's around 750.

MR. SPANGLER: I think it was -- this is Ron Spangler. It was 894 or something like that.

MR. PRAZAK: That's correct.

CHAIRMAN JOHNSON: Okay. And then I think last for me is -- I mean, I looked in the record. Am I right in that we only had one person write in with concerns about this proceeding?

MS. SEMMLER: That is correct, Chairman.

Deb Gregg in our Consumer Affairs Office keeps track of phone calls as well, and she didn't receive any phone calls.

CHAIRMAN JOHNSON: Okay. So and frankly that's testament to Otter Tail Power being out for 21 years. That's a big deal. So I'm looking at the letter from Mr. Solem and some issues he raises. I think the Commission -- or the settlement stipulation addresses his resistance to a flat rate. I mean, we're sort of going to more of a -- a flatter but not flat rate.

And then he also brings up the energy adjustment clause, the fuel clause, and he says if their increases are approved, are they going to discontinue this extra charge? I think the proper answer to Mr. Solem, and correct me if I'm wrong, is, you know, that charge doesn't go away.

From a practical standpoint that's probably reset by this rate case toward a number approaching zero. In a perfect world that probably would start at zero, but that number will bounce around as it has on a month-to-month basis based on what you all purchase or generate electricity for.

Is that the right kind of answer?

MR. GERHARDSON: Chair Johnson, if I may respond, yes, that's exactly right. And it should -- I mean, if it isn't in the record, it should be reflected that the fuel clause can go positive or negative. So it can be actually a credit to a customer's bill. And there are actually several components of our settlement that reflect credits to the fuel clause for the margins that we talked about and some other things. So we'd want that to continue so the customers receive those credits. Otherwise, they have no mechanism for receiving those credits.

CHAIRMAN JOHNSON: Thank you. Other questions of the assorted nature?

COMMISSIONER KOLBECK: I just kind of have a general question. When we went into just the 50 people that were going to be notified and earlier you addressed that, but could you go into a little more specifically if the rate is approved today, you're going to call them tomorrow or how exactly is that going to be handled?

MR. GERHARDSON: We wouldn't -- pardon me, Chair Johnson, Commissioner Kolbeck, Commissioners, I mean, obviously it's a reasonable time. I don't know if I can say it will be done within 30 days of approval or not, but it's within a reasonable period of time so that our customer service personnel who have the most contact with them can contact them, some of which they would be very familiar with so it wouldn't take a lot of time.

Ron, do you have anything more on the time frame on that?

MR. SPANGLER: Chairman Johnson, Commissioners, this is Ron Spangler again.

We do have some of our energy management representatives from our marketing area that are able to move forward with notifying these customers as soon as possible. It might not be -- we may not be able to get to all of them before their next bill, but we could move probably relatively quickly on that.

COMMISSIONER KOLBECK: And I guess that's my concern is that we don't get any backlash, well, why didn't you tell me this a month ago? You know, how much money is it going to cost? And the largest of the gains of the other people I guess I'm concerned about. And how quickly we could get to them I think would help a lot.

And I don't really have a suggestion or anything like that. I just want to make it known that the sooner the better for them so they can get on to a different rate, save themselves some money, and continue on.

Thanks.

CHAIRMAN JOHNSON: I would -- I think that's a great point, Commissioner Kolbeck. We're not talking about a ton of people. So to the extent that it can be done, these people should be contacted before their next bill shows up, before the rates are put into effect anyway. It's a great point.

Any other assorted questions? Yes, Commissioner.

COMMISSIONER HANSON: Just a curiosity. Are there any -- let me ask it this way: How do renewable portfolio standards in other states affect this rate?

MR. GERHARDSON: Thank you for giving us an opportunity to respond to that, Commissioner Hanson.

One thing that I want to point out about Otter Tail's wind additions is they have always been demonstrated as cost-effective under our integrated resource planning.

That means we would have added those wind generation projects with or without renewable energy objectives or renewable energy standards in any state. We get the benefit, of course, of satisfying those standards incidentally through this process.

So I think it's very important to make that clear, that these have been demonstrated to be the most cost-effective ways. Or I should say a component of the least cost plan for meeting our energy and resources for our customers.

I don't know if that answers -- does that answer your question? We have not added any wind for the purpose of satisfying a renewable energy objective or renewable energy standard. I hope that answers your question.

COMMISSIONER HANSON: Well, of course my concern is is that the rate payers of South Dakota don't end up paying higher rates because another state required some type of a capacity to be built on their turbine.

And speaking that plainly, do you have anything further to add?

MR. GERHARDSON: Chair Johnson, Commissioner Hanson, Commissioner Kolbeck, absolutely. We're very conscious of that. I think you know that we are divided. About 50 percent of our load is in Minnesota. About 50 percent in the two Dakotas.

South Dakota -- your comment I think suggests that you may be of a mind similar to what we're hearing from staff and Commissioners at times in North Dakota.

We are -- as the only utility that I believe is split 50/50 we're very much aware of this. We are very conscious of it. We have, fortunately, had resource planning that has allowed us to meet all states' resource planning requirements that have those. And I think we're very conscious of it. We will remain very conscious of it. And I think these wind additions, you have nothing to worry about on those.

COMMISSIONER HANSON: Well, I'd be interested in hearing staff's reply to the question as well.

MR. KNADLE: I think the company -- these two wind additions that they just put in, as the company said, they are looking if it's economical. The IRP plan, North Dakota had approved it previously. And they are looking at adding additional wind.

And when staff reviews that if they do have an addition -- we're going to look at if it was built or purchased or part ownership was for Minnesota, we're going to look at that pretty seriously and decide whether at that point in time if it's an allowable expense or it should get assigned to Minnesota.

COMMISSIONER HANSON: Thank you. Appreciate that. Thank you, Mr. Chairman.

CHAIRMAN JOHNSON: Other assorted questions? Any --

COMMISSIONER HANSON: I'll ask another one. I wasn't going to ask it, but sometimes feel compelled anyway.

Is there anything within the rate design or this process that you went through that is going to deter you in any way from any sort of planned additions or any additional changes that you had been planning on?

MR. GERHARDSON: There's nothing in this process that would have any impact on our resource additions, to my knowledge. Our resource planning generally drives --

COMMISSIONER HANSON: Within the settlement, I should have said, as opposed to the process.

MR. GERHARDSON: Normally within the settlement. These will not impact our resource planning decisions going forward.

COMMISSIONER HANSON: Thank you. Thank you, Mr. Chair.

CHAIRMAN JOHNSON: Other questions, assorted questions, Commissioners or advisors? Any action?

MR. JACOBSON: Commissioner, I would just like to add one thing. When the Commission -- if and when it chooses to make its decision, we would request that the Order waive tariff -- the Administrative Rule 20:10:13:04, which deals with how the tariff is laid out. The rule specifies Sections 1 through 6 and et cetera. This deviates from that, their tariff.

Did that in order to administrative -- you know, relieve administrative burden to go along with tariffs in other states.

And there have been a couple of -- there are a couple of tariff sheets that require corrected sheet numbers up in the upper right-hand corner, nothing substantive. But the company will need to file final tariffs anyway to put the -- there's a line on the bottom of the sheet for the approval date, and they will need to resubmit those two. We just wanted to make you aware that those two things exist.

CHAIRMAN JOHNSON: Well, with that, and, of course, we can adjust if there are other suggestions, but I would move that the Commission adopt the settlement stipulation, waiving 20:10:13:04 regarding tariff layout, an effective date of July 1 for the new rates and terms and conditions and, of course, provided that the corrected sheets are filed properly.

Okay. We'll just pause and see from a style and form perspective if we've missed anything.

Hearing none, any discussion on the Motion?

I would just say if you had to have a -- I think the two most important numbers with regard to this Motion are 21 and 1 million. 21 being the number of years that Otter Tail Power was out. I think that shows some impressive cost containment on their part.

I think the other number is 1 million, which I think shows some impressive cost containment on staff's side as that is the amount that the revenue requirement was reduced by as a part of this process. There were some rather significant changes that were made, but the fact that the parties have come together, having compromised and I think having a settlement stipulation that is in the public interest I think is impressive. It hasn't been very easy to do, I'm sure.

A couple of other things of note, the 25 percent sharing of revenues for nonasset-based margins I think is impressive. Thanks again to staff for negotiating that up from 15 percent. I do think that's good news for rate payers. To the extent Otter Tail Power's able to do good things with those energy purchases and sales that is going to share in those benefits with rate payers.

And then I do think the rate design changes that were made are good news long term.

Other comments on the pending Motion?

COMMISSIONER HANSON: I think you more than sufficiently covered it. However, I would just like to say from a personal standpoint that there's a tremendous amount of work that goes into this, and sincerely appreciate all the work that staff went through to put this together and did not in any way through my comments pertaining to, oh, block rate or anything of that nature mean to imply that I thought otherwise.

So appreciate the work that you guys did. Gals, guys.

COMMISSIONER KOLBECK: I think the amount of staff work that was put into it is obvious when we had come home from different events late at night and there was still staff members here working. That's very commendable on their part.

And rate increases are a necessary evil, and it's definitely something that's very appreciated by myself and I'm sure my colleagues that the most amount of work has gone into this to have the best outcome.

Even though no one likes to raise rates, it's definitely better than the alternative. So thank you.

CHAIRMAN JOHNSON: I want to -- and I should have asked this before we went into Commission action, but did I hear the Applicant -- someone mention that wind generation accounted for up to 70 percent of the increase?

MR. GERHARDSON: Of the settlement, it's approximately 60 percent.

CHAIRMAN JOHNSON: 60 percent. Okay. Other comments?

Hearing none, we'll proceed to vote.

Hanson.

COMMISSIONER HANSON: Aye.

CHAIRMAN JOHNSON: Kolbeck.

COMMISSIONER KOLBECK: Aye.

CHAIRMAN JOHNSON: Johnson votes aye. Motion carries 3-0.

Unless there's any further business to come before the Commission, is there a Motion to adjourn?

COMMISSIONER KOLBECK: So moved.

CHAIRMAN JOHNSON: Motion's been made. We'll proceed to vote.

Hanson.

COMMISSIONER HANSON: Aye.

CHAIRMAN JOHNSON: Kolbeck.

COMMISSIONER KOLBECK: Aye.

CHAIRMAN JOHNSON: Johnson votes aye. Motion carries 3-0. Thanks.

(The proceeding concludes at 4:15 p.m.)

STATE OF SOUTH DAKOTA)
:SS CERTIFICATE
COUNTY OF SULLY)

I, CHERI MCCOMSEY WITTLER, a Registered Professional Reporter, Certified Realtime Reporter and Notary Public in and for the State of South Dakota:

DO HEREBY CERTIFY that as the duly-appointed shorthand reporter, I took in shorthand the proceedings had in the above-entitled matter on the 23rd day of June, 2009, and that the attached is a true and correct transcription of the proceedings so taken.

Dated at Pierre, South Dakota this 22nd day of July, 2009.

Cheri McComsey Wittler,
Notary Public and
Registered Professional Reporter
Certified Realtime Reporter

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