MONTANA-DAKOTA UTILITIES CO.

A Division of MDU Resources Group, Inc.

Before the Public Utilities Commission of South Dakota

Docket No. NG05-__

Direct Testimony
of
Rita A. Mulkern

Q. Would you please state your name and business address?

A. Yes. My name is Rita A. Mulkern and my business address is 400 North Fourth Street, Bismarck, North Dakota 58501.

Q. What is your position with Montana-Dakota Utilities Co.?

A. I am the Regulatory Analysis Manager of Montana-Dakota Utilities Co. (Montana-Dakota), a Division of MDU Resources Group, Inc.

A. Would you please describe your duties as Regulatory Analysis Manager?

A. I am responsible for the preparation of cost of service studies, fuel cost adjustments, purchased gas cost adjustments and gas tracking adjustments in each of the jurisdictions in which Montana-Dakota operates.

Q. Would you please describe your education and professional background?

A. I graduated from North Dakota State University in 1981 with a Bachelor of Arts degree with majors in Economics and Business Administration and a minor in Statistics. I joined Montana-Dakota in July 1981 as a Regulatory Statistician, became Cost of Service Supervisor in 1986 and assumed my current position in 1999.

Q. Have you testified in other proceedings before regulatory bodies?

A. Yes, I have presented testimony before the Public Service Commissions of Montana, North Dakota, and Wyoming and the Minnesota and South Dakota Public Utilities Commissions.

Q. Are you familiar with the books and records of Montana-Dakota and the manner in which they are kept?

A. Yes. Montana-Dakota's books and records are kept in accordance with the Federal Energy Regulatory Commission (FERC) Uniform System of Accounts.

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to present the per books cost of service for the twelve months ended December 31, 2004, the pro forma cost of service reflecting known and measurable adjustments that will occur by December 2005 and the calculation of the revenue deficiency.

Q. What statements, schedules and exhibits are you sponsoring?

A. I am sponsoring Statements D through F, Statements H through M, Statements P through R and Exhibit No.___(RAM-1) and Exhibit No.___(RAM-2).

Q. What were the results of East River gas operations for the twelve months ended December 31, 2004?

A. Statement M, pages 1 and 2 show the per books income statement and rate base for total Company and East River gas operations. As shown on page 1, East River gas operations had a return on rate base of negative 7.097 percent for the twelve months ended December 31, 2004.

The details for each line item, i.e. sales revenue, other revenue, etc., are included in the applicable statement. Pages 3 and 4 list the pro forma adjustments to operating revenues, expenses and rate base. All adjustments were calculated on either an East River specific basis or on a total Company basis and allocated to East River, as indicated on the statement or schedule detailing each adjustment.

Q. How was the per books cost of service allocated to East River?

A. The Company utilizes a jurisdictional accounting system that directly assigns and/or allocates every item of revenue, expense and rate base to the jurisdictions as part of the regular accounting process on a monthly basis. The allocation methods and procedures are the same as have previously been used in Commission proceedings and are based on the principle of assigning and/or allocating costs to the cost causer.

Q. What criteria were used to determine the pro forma adjustments?

A. The pro forma adjustments to operating revenue, expenses and rate base were based on known and measurable changes occurring by December 31, 2005 and are listed on pages 3 and 4 of Statement M. All of these adjustments are reasonably certain to occur and can be measured with reasonable accuracy, thus meeting the criteria of known and measurable.

Q. What adjustments were made to operating revenues?

A. The adjustments to operating revenues are contained in Statement I. Adjustment No. 1 restates the per books consumption at current rates, using the estimated annual gas cost for 2005, exclusive of the surcharge adjustment, and eliminates the unbilled revenue, increasing revenue by $106,148.

Adjustment No. 2 increases revenues by $367,041 to reflect the effect of normal weather on sales volumes.

Adjustment No. 3 is an increase to revenues of $159,583 to reflect the annualization of firm customers to the December 2004 level.

Adjustment No. 4 includes the late payment revenue of $3,868.

Q. What adjustments were made to operation and maintenance (O&M) expenses?

A. The adjustments to operation and maintenance expenses are contained in Statement H. Pages 1 and 2 of Schedule H-1 summarize O&M expenses, with details provided on pages 3 through 19.

Adjustment No. 5, shown on page 3, adjusts the cost of gas to reflect the pro forma dk sales and an annual 2005 gas cost level, which was derived by calculating cost of gas based on annual demand charges and 2005 commodity cost of gas. The distribution loss factor of 1.00 percent represents the current loss factor.

Adjustment No. 6, relating to labor expense, was developed by applying the percentage change in total Company labor costs to the per books East River labor expense. The pro forma labor costs were based on 2005 payroll adjusted to reflect a three year average (2003-2005) level of bonuses. The adjustment is a decrease because in 2004 Montana-Dakota switched from recording bonuses when paid to recording bonuses on an accrual basis, thus matching the recording of bonuses in the year they are earned. As a result, bonuses for both 2003 (paid) and 2004 (accrued) were recorded in 2004 and the decrease in the labor adjustment reflects the elimination of the dual bonuses.

Adjustment No. 7 to benefits is an increase of $144,614. Benefits expense consists of medical/dental insurance, pension expense, the Supplemental Income Security Plan (SISP), 401K, post-retirement, workers compensation and other benefits. Each of these items, excluding the other benefits, was adjusted individually by using the 2005 budgeted amounts and applying the percentage increase to each type of benefit.

Adjustment No. 8 reflects insurance expense at current levels for 2005 and is an increase of $4,833.

Adjustment No. 9 to software maintenance expense is an increase of $2,569 in 2005 due to additional annual maintenance costs associated with a license agreement and software upgrades.

Adjustment No. 10 reflects an $8,042 increase in communication expense. Communication expense consists of telephone, cell phone, network and circuit charges. The increase expected in 2005 is due to an increase in network charges as a result of the increase in the number of connections, as well as higher band-width needs and an overall increase in long-distance usage.

Adjustment No. 11 reflects an increase in Office Supplies of $1,441 due to an overall increase in paper costs.

Adjustment No. 12 adjusts Company consumption and is the expense for electric and natural gas consumption in Company buildings.

The electric component is projected to remain flat. The natural gas component is expected to increase $1,516 based on the increase in from per books revenues to normalized revenues.

Adjustment No. 13 is to uncollectible accounts and is based on the five year average of net write-offs to pro forma sales and transportation revenues, which results in an increase in uncollectible accounts of $5,992.

Advertising is shown on page 12. Pursuant to past Commission policy, general promotional advertising expense has been eliminated.

Q. Would you explain why you are including institutional advertising expenses?

A. Montana-Dakota is seeking to include institutional advertising that we believe benefits customers and serves the public interest. As a corporate citizen, Montana-Dakota needs to be active in the communities that it serves. Montana-Dakota's motto is "In the community to serve" and one of the ways of being a strong community member is to advertise our company and what we do for the communities. Our communities expect nothing less and advertising in the local newspapers, on television, in school yearbooks, programs, etc., is a necessary part of being active in the community. This advertising benefits the community and the customers in that community, thus serving the public interest.

Q. Would you please continue with your explanation of adjustments to operation and maintenance expenses?

A. Adjustment No. 15 to rate case expense reflects the expenses to be incurred in this case, amortized over a three-year period. The adjustment is an increase of $3,470.

Adjustment No. 16 shows the East River portion of expenses associated with the cost of performing a depreciation study for gas and common property, amortized over a five year period. This adjustment shows an increase of $906.

Adjustment No. 17 is for employee training. Employee training is expected to increase due to the expansion of the existing training modules and the implementation of a new training program in 2005. Montana-Dakota has been experiencing a steady increase in the number of employees retiring in the past three years. In 2004 and into the next four years, the Company expects to continue to see a loss of employees in managerial roles through retirements. The Company has recognized that additional training is required to prepare all employees for changes in the future.

Adjustment No. 18 is an adjustment to rent for $1,828. The increase in rent is due to the construction of a new office for MDU Resources as part of a new corporate campus and the adjustment reflects the allocation of the cost of new building, through rent expense, to East River.

The items adjusted individually above represent approximately 82 percent of total East River gas O&M, as shown on page 18 and 19. The remaining items, which make up approximately 18 percent of other O&M, are assumed to remain flat.

Q. What adjustments were made to depreciation expense?

A. The adjustment to depreciation expense is contained in Statement J. Adjustment No. 19 restates annual depreciation expense to the average pro forma level of plant in service, using the same depreciation rates as used in the Company's Black Hills area.

Q. What adjustments were made to taxes other than income?

A. The adjustments to taxes other than income are contained in Statement L. Adjustment No. 20 restates ad valorem taxes to the pro forma level of plant in service based on the 2004 ratio of ad valorem taxes to plant. This adjustment is an increase of $1,237.

Adjustment No. 21 to payroll taxes is an increase of $980 based on the ratio of payroll taxes to labor expense for 2004 applied to pro forma labor expense.

Adjustment No. 22 restates the South Dakota Gross Receipts Tax to the pro forma level of revenue and is an increase of $2,282.

Q. What adjustments were made to income taxes?

A. The adjustments to income taxes are contained in Statement K. Adjustment No. 23, shown on page 7, is to interest expense, which is deductible for tax purposes. Interest expense is calculated on the pro forma rate base using the weighted cost of debt and debt ratio from Statement G. The resulting interest expense is a decrease of $70,068 from the per books level.

Adjustment No. 24 calculates the tax depreciation and deferred taxes on the pro forma plant additions and is shown on page 8.

Adjustment No. 25 calculates the current income tax expense on all of the pro forma adjustments to operating revenues and expenses as shown on page 9.

Adjustment No. 26 eliminates the closing/filing and reserve adjustments in the current income tax accrual and in the deferred taxes. This adjustment adjusts current and deferred income taxes to the calculated amount for East River and conforms to past Commission practices.

Q. What adjustments were made to rate base?

A. The pro forma rate base reflects known and measurable adjustments that will occur through December 31, 2005, with the resulting rate base stated on an average basis. The pro forma adjustments to rate base are summarized on Statement M, page 4. Adjustment A is the known and measurable plant additions that will be in service by December 31, 2005. These additions are shown on Statement D, Schedule D-2, pages 3 and 4.

Adjustment B, shown in Statement E, increases the average reserve for depreciation on the per books plant by $517,227 to restate the reserve to the average pro forma level in order to match the average pro forma plant levels.

The working capital adjustments are included in Statement F. Adjustment C is an increase of $3,119 to restate materials and supplies to a thirteen-month average balance.

Adjustment D restates the prepaid insurance expense to a thirteen-month average balance for 2005 using the pro forma insurance expense and is an increase of $9,222.

Adjustment E, shown on Statement K, page 15, is the increase to deferred taxes to extend the average accumulated deferred tax balance to match the pro forma plant and accumulated reserve.

Adjustment F, shown on Statement K, page 15, is the decrease to accumulated investment tax credits (ITCs) to extend the average ITC balances to match the pro forma plant and accumulated reserve.

Adjustment G restates customer advances for construction to reflect a thirteen-month average balance and is an increase of $1,009 as shown on Statement F, Schedule F-1, page 4.

These are all of the pro forma adjustments to revenue, expense and rate base.

Q. What does Exhibit No.____(RAM-1) show?

A. Exhibit No.____(RAM-1), which is identical to Statement M, pages 5 through 7, shows the calculation of the revenue deficiency of $1,786,862 based on the pro forma operating income and rate base and using the overall rate of return of 9.921 percent from Statement G, page 2.

Q. Is the Company requesting an increase of $1,786,862 annually?

A. No, as stated by Mr. Imsdahl and Ms. Aberle, the Company is requesting an increase of $849,745. Exhibit No.___(RAM-2) shows the effect of the $849,745 increase on the East River system. As shown on the Exhibit, Montana-Dakota's return will be 0.68 percent, and the resulting return on equity will be a negative 6.12 percent.

Q. Does this complete your direct testimony?

A. Yes, it does.

MONTANA-DAKOTA UTILITIES CO.
INCOME STATEMENT
GAS UTILITY - EAST RIVER
TWELVE MONTHS ENDED DECEMBER 31, 2004
PRO FORMA

	Per Books	Pro Forma Adjustments	Pro Forma
Operating Revenues			
Sales	$6,006,140	$632,772	$6,638,912
Other	58,074	3,868	61,942
Total Revenues	6,064,214	636,640	6,700,854
Operating Expenses			
Operation and Maintenance			
Cost of Gas	4,741,019	581,700	5,322,719
Other O&M	1,543,156	106,690	1,649,846
Total O&M	6,284,175	688,390	6,972,565
Depreciation	524,264	(89,200)	435,064
Taxes Other Than Income	194,961	4,499	199,460
Current Income Taxes	(578,226)	89,492	(488,734)
Deferred Income Taxes	137,346	(48,109)	89,237
Total Expenses	6,562,520	645,072	7,207,592
Operating Income	($498,306)	($8,432)	($506,738)
Average Rate Base	$7,020,910	($439,114)	$6,581,796
Rate of Return	-7.097%		-7.699%

MONTANA-DAKOTA UTILITIES CO.
AVERAGE RATE BASE
GAS UTILITY - EAST RIVER
TWELVE MONTHS ENDED DECEMBER 31, 2004
PRO FORMA

	2004	Pro Forma Adjustments	Pro Forma
Gas Plant in Service	$13,091,890	$151,165	$13,243,055
Accumulated Reserve for Depreciation	5,428,612	517,227	5,945,839
Net Gas Plant in Service	7,663,278	(366,062)	7,297,216
CWIP in Service Pending Reclassification	45,943		45,943
Total Gas Plant in Service	7,709,221	(366,062)	7,343,159
Additions			
Materials and Supplies	$21,293	$3,119	$24,412
Prepayments	10,483	9,222	19,705
Total Additions	31,776	12,341	44,117
Total Before Deductions	$7,740,997	($353,721)	$7,387,276
Deductions			
Accumulated Deferred Income Taxes	$712,630	$86,472	$799,102
Accumulated Investment Tax Credits	3,057	(2,088)	969
Customer Advances	4,400	1,009	5,409
Total Deductions	720,087	85,393	805,480
Total Rate Base	$7,020,910	($439,114)	$6,581,796

MONTANA-DAKOTA UTILITIES CO.
PROJECTED OPERATING INCOME AND RATE OF RETURN
REFLECTING ADDITIONAL REVENUE REQUIREMENTS
GAS UTILITY - EAST RIVER

	Before Additional Revenue Requirements	**Additional Revenue Requirements**		Reflecting Additional Revenue Requirements
Operating Revenues				
Sales	$6,638,912	**$1,786,862**		$8,425,774
Other	61,942			61,942
Total Revenues	6,700,854	1,786,862		8,487,716
Operating Expenses				
Operation and Maintenance				
Cost of Gas	5,322,719			5,322,719
Other O&M	1,649,846			1,649,846
Total O&M	6,972,565			6,972,565
Depreciation	435,064			435,064
Taxes Other Than Income	199,460	2,680	1/	202,140
Current Income Taxes	(488,734)	624,464	1/	135,730
Deferred Income Taxes	89,237			89,237
Total Expenses	7,207,592	627,144		7,834,736
Operating Income	($506,738)	$1,159,718		$652,980
Rate Base	$6,581,796			$6,581,796
Rate of Return	**-7.699%**			**9.921%**

1/ Reflects taxes at 35% after deducting South Dakota Gross Receipts of .15%.

MONTANA-DAKOTA UTILITIES CO.
PROJECTED OPERATING INCOME AND RATE OF RETURN
REFLECTING ADDITIONAL REVENUE REQUIREMENTS
GAS UTILITY - EAST RIVER

	Before Additional Revenue Requirements	**Additional Revenue Requirements**		Reflecting Additional Revenue Requirements
Operating Revenues				
Sales	$6,638,912	**$849,745**		$7,488,657
Other	61,942			61,942
Total Revenues	6,700,854	849,745		7,550,599
Operating Expenses				
Operation and Maintenance				
Cost of Gas	5,322,719			5,322,719
Other O&M	1,649,846			1,649,846
Total O&M	6,972,565			6,972,565
Depreciation	435,064			435,064
Taxes Other Than Income	199,460	1,275	1/	200,735
Current Income Taxes	(488,734)	296,965	1/	(191,769)
Deferred Income Taxes	89,237			89,237
Total Expenses	7,207,592	298,240		7,505,832
Operating Income	($506,738)	$551,505		$44,767
Rate Base	$6,581,796			$6,581,796
Rate of Return	**-7.699%**			**0.68%**
Return on Equity				-6.12%

1/ Reflects taxes at 35% after deducting South Dakota Gross Receipts of .15%.