Direct Testimony and Exhibits
Richard Kinzley

Before the South Dakota Public Utilities Commission
of the State of South Dakota

In the Matter of the Petition for Declaratory
Ruling of Black Hills Power, Inc.

Docket No. EL 11- _____

April 28, 2011

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EXHIBITS

I. INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME, POSITION, AND BUSINESS ADDRESS.

A. My name is Richard Kinzley, and my business address is 625 Ninth St., Rapid City, South Dakota 57701. Since September 2008, I have been employed by Black Hills Corporation as the Vice President, Strategic Planning and Development. From 2000 to September 2008, I was the Director of Corporate Development. My responsibilities as the Director of Corporate Development included oversight of the financial modeling related to, and assisting in negotiating and integrating, various acquisitions and divestitures by Black Hills Corporation and its subsidiaries.

Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND EMPLOYMENT EXPERIENCE.

A. I graduated from the University of South Dakota in May 1988 with a Bachelor of Science in Business Administration degree. I am also a certified public accountant (non-active). I joined Black Hills Corporation in 1999, and have been involved in Black Hills Corporation's asset development and acquisition and divestiture activities over the past decade. Prior to that, I worked for nine years in public accounting with KPMG in Omaha, Nebraska and Ketel Thorstenson in Rapid City, South Dakota. My job responsibilities included auditing public and not-for-profit businesses, and preparation of tax returns for corporations and individuals. I also spent two years with Sodak Gaming in Rapid City, South Dakota as Director of Financial Reporting. My job responsibilities with Sodak Gaming included oversight of financial statement preparation, including SEC documents, and various financial analysis, including acquisition activities.

Q. WHAT ARE YOUR CURRENT DUTIES AT BLACK HILLS CORPORATION?

A. I lead Black Hills Corporation's strategic planning efforts and all acquisition and divestiture activities, and am involved in asset development activities of the Company.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to describe the option to purchase that is expected to be entered into with the developers regarding the Company's proposed BHP wind project (the "Project") and to describe the financial and resource modeling that has been completed to support the Project.

II. OPTION TO PURCHASE

Q. PLEASE DESCRIBE THE DEVELOPMENT OF THE PROJECT.

A. The Project has been developed over the past two years by a partnership between Renewable Solutions and PNE Wind USA, Inc. (collectively referred to as the "Developer"). The Developer has secured wind easements with two landowners for approximately 4,200 acres of developable land. The Developer has also secured the necessary transmission and access rights-of-way for the Project.

Q. PLEASE DESCRIBE THE EXPECTED OPTION TO PURCHASE AGREEMENT BETWEEN THE COMPANY AND THE DEVELOPER.

A. The Company and the Developer expect to enter into an Option and Asset Sale

Agreement ("Option to Purchase") in the very near future. Once fully negotiated and executed, a copy of the Option to Purchase will be filed with this docket. All references herein to the Option to Purchase shall be to the form of the Option to Purchase that is expected to be entered into. Under the Option to Purchase, the Company has the option to purchase from the Developer all of the necessary rights to the wind easements, transmission and access rights-of-way, the licenses, permits and approvals, and all other items necessary for the Company to fully develop the Project. From the Company's perspective, the price set forth in the Option to Purchase is a reasonable price. The bulk of the payment to the Developer will only be made if the Company excercises the Option to Purchase.

Q. EXPLAIN IN DETAIL WHAT STEPS THE DEVELOPER HAS TAKEN TO PREPARE THIS SITE FOR A WIND FACILITY?

A. In addition to securing necessary rights with affected landowners, the Developers have conducted various studies on the site and begun the permiting process. In summary, the Developer contacted, reviewed and analyzed necessary permits and approvals from the SD Department of Environment and Natural Resources, SD Department of Game, Fish and Parks, SD Department of Transportation, SD State Historic Preservation Office, SD Natural Heritage Program, Butte County Highway Department, Butte County, Federal Aviation Administration, Federal Energy Regulatory Commission, US Department of Commerce, US Department of Agriculture, Natural Resources Conservation Service, Environmental Protection Agency, US Fish and Wildlife Services and SD Ecological Services Field Office and US Army Corps of Engineers. Most final permits or approvals, cannot be obtained until the Company is closer to construction. The Company will pursue receipt of these permits and approvals at the appropriate time. A detailed list of these remaining activities is attached hereto as Exhibit RK-1.

Q. WHAT KIND OF DILIGENCE HAS THE COMPANY DONE WITH REGARD TO THE RIGHTS OBTAINED BY THE DEVELOPER?

A. The Company engaged CH2M Hill to perform a review of the work done by the Developer's consultant, Westwood Professional Services. CH2M Hill recommended additional consultation with the US Fish and Wildlife Service and Butte County but indicated they anticipated no major hurdles. The site is at an advanced stage in the development process to allow for an accelerated construction schedule. In addition, the Company is working with an external law firm to review and analyze the landowner agreements and title work on the property.

Q. DOES THE COMPANY HAVE PLANS TO EXPAND ON THIS SITE IN THE FUTURE?

A. The site does have an expansion capability of up to approximately 30 megawatts in addition to the 20 megawatts that the Company plans to initially build. The Developers have secured the right to expand with the necessary landowners and will assign that future development right to the Company in the Option to Purchase. Therefore, the property could have value beyond the initial development. The Company's future expansion plans will depend largely on future resource planning taking into account customer need, federal and state policy initiatives and cost to build other generation (natural gas, coal, etc.). The expansion possibilities of the site position the Company to accommodate and adapt to the ever changing energy policy environment.

III. MODELING

Q. PLEASE INTRODUCE THE MODELS THAT WERE CREATED TO EVALUATE THE PROJECT?

A. The Company used an economic evaluation model to evaluate the Project. This model and its components are summarized as follows:

Forecasted Gross Revenue Requirement. As part of the Economic Evaluation Model described below, the Company prepared a forecasted gross revenue requirement for the years 2013 to 2037. The year 2013 was selected because the Project would be in service in late 2012 and presumably in rates in 2013. The Forecasted Gross Revenue Requirement is attached as Exhibit RK-2.

Net Revenue Requirement Analysis. The Net Revenue Requirements Analysis determined the potential rate impact to the Company's customers. The Net Revenue Requirements Analysis is attached as Exhibit RK-3.

Economic Evaluation Model. This term refers generally to the use of the various components used to evaluate the economic impact to the Company by adding this proposed Project. Attached as Exhibit RK-4 is the document showing assumptions used in running the Economic Evaluation Model.

Q. PLEASE EXPLAIN THE ECONOMIC EVALUATION MODEL RESULTS.

A. As noted above, the Economic Evaluation Model evaluates the economic impact of adding the proposed Project to the Company's present resource mix.

The Production Cost Model – Without Project determined the cost to serve customers in future years. In 2013, this amount was calculated to be $110,906,000. This number was compared to the cost to serve customers in 2013 if the proposed Project is added to the Company's resource mix and is in service for 2013. The cost to serve customers in 2013 with the proposed Project's energy, as shown in the Production Cost Model – Wind, is calculated as $108,749,000. This results in $2,157,000 less cost to serve customers in 2013 ("Displaced Resource Savings") under the presently projected resource mix for the reason that the Project displaces the costs associated with other generating resources or creates opportunities for additional energy sales.

Pursuant to the Forecasted Gross Revenue Requirment, the Company's revenue requirement for 2013 for the Project were projected to be $4,700,000. This amount includes Project landowner expenses, operating expenses, regulatory depreciation, implied regulatory interest, the provision for federal income tax, reduction for Production Tax Credits, and a return on the capital invested in the Project.

The Displaced Resource Savings of $2,157,000 was then used to reduce the Project's 2013 revenue requirement of $4,700,000 with the difference of $2,543,000 representing the net revenue requirement for the Project in 2013. This number is then used as a percentage of the 2013 forecasted total revenue requirement of the Company of $165,000,000, with the result being the percentage increase in rates in 2013 as a result of adding the Project to the Company's resource mix.

A summary of the above calculation for 2013 follows:

Production cost with wind	$108,749,000
Production cost w/out Project	$110,906,000
Displaced Resource Savings	($2,157,000)
Gross Revenue Requirement for Project	$4,700,000
Net Revenue Requirement for Project	$2,543,000

The net revenue requirement for the Project of $2,543,000 is divided by $165 million (the total projected Company revenue requirement), which equals 1.5%, which is the expected approximate impact to customer rates in 2013.

Q. WHAT IS THE FUTURE IMPACT TO CUSTOMER RATES WHEN THE PROJECT IS ADDED TO THE COMPANY'S RESOURCE MIX?

A. As demonstrated above, customer rates will increase by approximately 1.5% in 2013 as a result of this Project.

Q. WHAT MAJOR ASSUMPTIONS WERE MADE IN DETERMINING THE POTENTIAL IMPACT ON CUSTOMER RATES?

A. The major assumptions for each model listed above are set forth in the attached Exhibit RK-5. The Company relied on the Ventyx Fall Reference Case for its natural gas and carbon tax forecast.

Q. HOW WOULD YOU CHARACTERIZE THE APPROACH TAKEN IN THE MODELING?

A. The model is conservative in its determination of rate impact to customers. The upside to customers is that the Project presents reasonable opportunities to additionally lower customer costs, through items such as renewable energy credits sales and mitigation of increased emissions costs,which benefit customers. No benefits from these opportunities have been included in our financial models.

Q. WHAT EFFECT DID THE PRODUCTION TAX CREDIT HAVE ON THE IMPACT TO CUSTOMER RATES?

A. The Production Tax Credit has a significant impact on minimizing the impact of the proposed Project on customer rates. The Production Tax Credit was discussed in the testimony of Kyle D. White. The expected Production Tax Credit for the proposed Project totals about $1,453,000 for 2013, which amount reduces the revenue requirement of the Project for 2013. As noted in the testimony of Kyle D. White, the Production Tax Credit benefit continues until 2022.

Q. WHAT OTHER ITEMS FAVORABLY IMPACTED CUSTOMER RATES?

A. In addition to the favorable impact of the Production Tax Credit, several other items included in our models favorably impacted customer rates. While these are difficult to quantify in dollars and cents, some of these items (all of which reduce customer rate impacts) include:

1) Bonus depreciation for federal tax purposes – this provision, like the Production Tax Credit, is also currently only available for projects placed in

service through 2012.

2) Low pricing of wind turbines and other major components of the Project - market conditions are currently very competitive for these components and associated services and are notably lower than in recent years.

3) Purchasing the Project from the Developers at an attractive cost.

4) An expected favorable cost for regulation service for the Project.

And, of course, there is certainly a benefit to the Company and its customers by diversifying the Company's resource mix by adding wind. There is no certainty that the federal tax incentives expiring in 2012, including the Production Tax Credit and bonus depreciation, will be extended.

Q. WHAT IS THE LONG TERM IMPACT TO CUSTOMERS OF THE PROJECT?

A. Initial minimal rate impacts, as described previously in this testimony, are mitigated by the fact that this Project will have significant depreciation expense in early years due to the utilitization of bonus depreciation, which reduces rate impacts in future rate proceedings. Further, the Project will effectively be fully depreciated in twenty years, and at that time the customers will receive the benefit of an inexpensive generating resource with only minor operating costs. Another long-term positive impact is the fact that the Project brings diversification to the Company's resource mix.

Q. DID THE COMPANY PREPARE A COST-BENEFIT ANALYSIS REGARDING THE ADDITION OF THE WIND PROJECT?

A. Yes, as modeled in Exhibit RK-5. As detailed in this testimony, based on the conservative assumptions used in the models, there is an expected cost to customers associated with this Project. However, I believe that the cost is reasonable for the benefits acquired, and I believe the cost over the life of the Project will be less than modeled.

Q. DID THE COMPANY PREPARE A COST-BENEFIT ANALYSIS USING POTENTIAL CARBON TAXES?

A. Yes, a Carbon Tax Model was run and is attached as Exhibit RK-6. The results showed that a carbon tax, beginning in 2014, would result in the Project creating a net benefit to system costs in 14 of the 25 years analyzed. The aggregate net revenue requirement for 2013-2037 in the carbon scenario with the Project would result in net customer savings of approximately $2,834,000.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.