Direct Testimony
Erin E. Wentz

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

In the Matter of the Application of
Black Hills Power, Inc., a South Dakota Corporation

For Authority to Increase Rates
In South Dakota

Docket No. EL12-___

December 17, 2012

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EXHIBITS

None

I. INTRODUCTION & QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Erin E. Wentz, 625 Ninth Street, P.O. Box 1400, Rapid City, South Dakota 57701.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am currently employed as Manager, Electric Rates for Black Hills Utility Holdings.

Q. FOR WHOM ARE YOU TESTIFYING ON BEHALF TODAY?

A. I am testifying on behalf of Black Hills Power, Inc. ("Black Hills Power" or the "Company").

Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND BUSINESS BACKGROUND.

A. I am a graduate of the University of South Dakota in Vermillion, South Dakota, with both a Bachelor of Science in Business Administration degree and a Master of Professional Accountancy degree. My work experience includes working for a public accounting firm from 2002 through 2006. The accounting firm was Ketel Thorstenson, LLP, located in Rapid City, South Dakota. I began my career with Black Hills Corporation in December 2006 in the internal audit department. Shortly thereafter, I was promoted to Internal Audit Project Manager. In April 2011, I was offered, and accepted the position as Manager, Electric Rates.

Q. BRIEFLY DEFINE YOUR DUTIES AND RESPONSIBILITIES.

A. I am responsible for electric rates and regulatory matters for Black Hills Corporation's electric utility subsidiaries. I review financial information and verify the financial reporting for each subsidiary is accurate and in accordance with the rules and regulations of the Federal Energy Regulatory Commission ("FERC").

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

A. The purpose of my testimony is to present and explain the known and measurable adjustments made to the Revenue Requirement Model (the "Model"). The Model is presented in Volume 1 of Black Hills Power's Application as Statements A through R, and supporting Schedules and Work Papers. In my testimony, I will describe known and measurable annualized adjustments to certain utility costs that support the revenue requirement.

III. RATE BASE

Q. PLEASE DESCRIBE RATE BASE.

A. Rate base is the value established by a regulatory authority, upon which a utility is allowed to earn a specified rate of return as shown on Statement M. The Company is using a 12 month historical test year ended June 30, 2012, as a starting point. Rate base begins with the twelve month average amount of all fixed asset accounts for Black Hills Power as of June 30, 2012, as shown on Statement D, page 2, and is reduced by the twelve month average Accumulated Depreciation as shown on

Statement E, page 1. Known and measurable adjustments are made to rate base to reflect expected non-revenue producing capital additions from July 1, 2012 through April 1, 2013, as shown on Statement D, Page 2. A corresponding known and measurable adjustment is made to accumulated depreciation, thereby decreasing rate base. Rate base also includes a component of working capital as shown on Statement F. The final component of rate base is other rate base reductions, such as deferred federal income taxes as it relates to the timing difference of book depreciation and tax depreciation expense. These amounts can be found on Schedules M-1 and M-2.

Q. ARE YOU REQUESTING CONSTRUCTION WORK IN PROGRESS AS PART OF RATE BASE?

A. No. The only plant investment in rate base will be that which is used and useful prior to rates going into effect.

Q. IS THE COMPANY PROPOSING ADJUSTMENTS TO PLANT IN SERVICE?

A. Yes, there are other known and measurable adjustments for plant investments that will be used and useful prior to rates going into effect. A detailed list of those investments is shown on Schedule D-10.

Further, on Statement D, page 2, column (c), an adjustment was made to annualize plant moved into service during the test year. For example, if an asset was placed into service in December of 2011 for $1,000,000, the twelve month plant in service calculation shown on Schedule D-3, page 1, would only capture $500,000 as rate base. When the new rates go into effect, the customer will be using this asset and therefore the Company should receive recovery for the full cost of the asset. This adjustment is made for all assets placed in service during the test year and for assets placed in service during July and August 2012. This adjustment is consistent with previously filed rate cases.

Q. PLEASE EXPLAIN COLUMN E, TRANSFER TRANSMISSION PLANT IN SERVICE ON STATEMENT D, PAGE 2.

A. Most of Black Hills Power's transmission assets are segregated from the retail utility assets since they are regulated by FERC. However, Black Hills Power is obligated to pay for its transmission service under the Joint Open Access Transmission Tariff. The transmission assets are directly assigned to the FERC jurisdiction in Statement N and Schedule N-1.

A. WORKING CAPITAL

Q. HOW WAS WORKING CAPITAL CALCULATED AND INCLUDED IN RATE BASE?

A. Working Capital, as shown on Statement F, is comprised of four components. The first is cash working capital as determined from a lead/lag study. The others are fuel stock, materials and supplies, and prepaid expenses using a 12 month average on balances as of June 30, 2012, with known and measurable adjustments. The final adjusted balance of $18,045,403, as shown on Statement F, is included as part of rate base.

Q. PLEASE DESCRIBE HOW THE CASH WORKING CAPITAL AMOUNT WAS DETERMINED.

A. The Company prepared a per books and an as adjusted cash working capital ("CWC") amount for this rate case. The per books CWC is located on Schedule F-3 page 1 and the as adjusted CWC is on Schedule F-3 page 2. The as adjusted CWC amount is used as a component of rate base. The per books and as adjusted CWC amounts were determined by preparing a Lead/Lag Study.

Q. HOW DOES A LEAD/LAG STUDY MEASURE THE AMOUNT OF CASH REQUIRED FOR OPERATING EXPENSE?

A. A lead/lad study measures the difference between: (1) the time a service is rendered and billed until the time revenues for that service are received ("lag") and (2) the time that services, materials, etc. are obtained/used and the time payments for those services are made ("lead"). The applicable lead period for each major category of expense is compared to the revenue lag period. The difference between those periods, expressed in days, multiplied by the average daily operating expense, yields the amount of cash working capital requirement.

Q. HOW WAS THE EXPENSE LEAD DAYS CALCULATED ON SCHEDULE F-3?

A. The expense lead days are the actual days between when a service is received and when payment is made for those services. To determine the expense lead days for each expense category, the Company reviewed a sample of invoices paid from that category and determined the average number of days it took to pay each of those invoices. The expense per day is calculated by taking the total expense per category divided by the number of days in the year. Finally, that expense per day for each category is multiplied by the expense lead days for that category to determine the expense dollar days for each category. Line 41 of Schedule F-3 contains the combined total of the expense dollar days and the combined total of the expense per day for all the expense categories. The total in column (d) was then divided by the total in column (b), resulting in the expense lead days of 48.87 which is shown on line 44 of Schedule F-3, page 2.

Q. CAN YOU DESCRIBE HOW THE REVENUE LAG DAYS WERE CALCULATED?

A. The midpoint of service for each revenue month during the test year was first determined by dividing the total days of the year by 12 and then by 2. Then the amount of lag days between when the meter is read and when the customer is billed was determined by using the Company’s billing system and calculating that amount on a monthly basis. The monthly results are then averaged to arrive at an annual average. Next, the average number of days between billing and receipt of payment was determined. This was done by using the Company’s billing system and calculating that amount on a monthly basis and then averaging the monthly results to arrive at an annual average. Finally, the sum of the results discussed above were added together to determine the total revenue lag days of 37.96.

Q. WHAT WAS THE RESULT OF THE LEAD/LAG STUDY?

A. The result of the lead/lag study demonstrates that, in aggregate, customers have supplied funds to the utility to pay for expenses prior to the utility paying for the same expenses. As a result, a rate base reduction of $(5,627,732) was included as a component of rate base.

Q. EXPLAIN THE KNOWN AND MEASURABLE ADJUSTMENT MADE TO MATERIALS AND SUPPLIES.

A. A known and measurable adjustment has been made to materials and supplies for a $750,000 spare transformer rebuild that will be received in 2013. This spare transformer is for Neil Simpson II power plant. In case of a transformer failure, the spare transformer will allow more timely restoration of service.

B. OTHER RATE BASE REDUCTIONS

Q. WHAT OTHER REDUCTIONS TO RATE BASE WERE MADE?

A. Deferred federal income taxes related primarily to accelerated depreciation, advances for construction, and pension related costs are included as reductions to rate base, as shown on Schedules M-1 and M-2.

Q. ARE THESE OTHER REDUCTIONS TO RATE BASE CONSISTENT WITH THE COMPANY'S LAST RATE CASE?

A. Yes, the Company used a consistent approach and accounts to reduce rate base.

Q. WHAT OTHER ADJUSTMENTS DID YOU MAKE TO REDUCE RATE BASE?

A. As shown on Statement M, the Company also made an adjustment to reduce rate base for additional accumulated depreciation on existing assets. The adjustment increases accumulated depreciation to reflect one half of the annual depreciation expense for depreciation on existing assets.

<u>IV. ADJUSTMENTS TO THE OPERATING EXPENSES</u>

Q. PLEASE DEFINE OPERATING EXPENSES.

A. Total operating expenses are costs incurred by the Company in order to supply electricity to the customers of Black Hills Power. In the development of the revenue requirement, these operating costs are passed on to customers dollar for dollar; that is, without Black Hills Power earning any net income on those expenses. Expenses are reflected in the following statements:

1) Statement H provides the operating and maintenance expenses by FERC account.
2) Statement J is the calculation of depreciation expense.
3) Statement K shows the calculation of federal income tax expense.
4) Statement L calculates taxes other than federal income taxes - such as federal payroll taxes and property taxes.

All these Statements are summarized on Statement M to show the per books and the pro forma rate of return.

Q. PLEASE EXPLAIN THE ADJUSTMENTS FOR THE EXPENSES ON STATEMENT H.

A. Several adjustments were made to the expense as shown on Statement H, columns (b) – (q). Statement H starts with the per books information for the twelve months ending June 30, 2012, by FERC account number. Each adjustment has a column on this page and a Schedule supporting the determination of the adjustment.

Delivered Energy Cost Expenses were eliminated as shown in column (q), as the Company is not proposing to change the base rate of the energy cost adjustment. The corresponding revenue was also eliminated as shown on Statement I, page 1. The removal of the expense and revenue is further discussed in Mr. Kilpatrick's direct testimony.

Adjustment (b): The adjustment of $(119,723) on Schedule H-1 represents costs associated with one replacement, one addition related to the Strategic Workforce Planning Initiative, as well as one additional employee needed for Company operations. The replaced employee vacated January 2012, and the expense adjustment reflects an annualization assuming the employee was employed for the entire test year. Further, there were Black Hills Power employees who transferred to Black Hills Utility Holdings. This adjustment reflects a decrease of payroll dollars associated with the transfer of these employees. Finally, the adjustment reflects wage increases for Black Hills Power employees. The wage increase amounts are calculated using contracted union wage increases and expected non-union wage increases.

Adjustment (c): Schedule H-4 contains the corporate costs charged to Black Hills Power from Black Hills Service Company for the twelve months ending June 30, 2012. The known and measurable adjustment represents an increase of $1,119,825 to operating expenses. These expenses are a combination of direct and indirect charges without any additional fees. All costs are charged to Black Hills Power as the costs are incurred by Black Hills Service Company. The allocation methods for indirect charges are described in the Cost Allocation Manual, which is included in direct testimony of Mr. Berzina, Exhibit JB-3.

Adjustment (d): Schedule H-5 contains the corporate costs charged to Black Hills Power from Black Hills Utility Holdings for the twelve months ending June 30, 2012. The known and measurable adjustment represents an increase of $2,508,618 to operating expenses. These expenses are a combination of direct and indirect charges without any additional fees. All costs are charged to Black Hills Power as the costs are incurred by Black Hills Utility Holdings. The allocation methods for indirect charges are described in the Cost Allocation Manual, which is included in direct testimony of Mr. Berzina, Exhibit JB-4.

Adjustment (e): Schedule H-6 represents the costs to provide retiree healthcare, the pension plan expense, pooled medical, as well as, the employer portion of the 401(k) Plan. The pro forma costs are compared to the test year expense and the difference represents an increase to operating expenses of $510,780.

Adjustment (f): Schedule H-7 provides the calculation to normalize bad debt expense using a three year historical period. The average net write-offs during those three years was then divided by the average billed revenues to determine the average uncollectable expense for the Company. This average rate was then applied to the projected new revenue amount to determine what the expected bad debt expense would be. This was compared to the actual test year amount and an increase to operating expenses of $114,741 was then included as an adjustment.

Adjustment (g): Schedule H-8 provides for Black Hills Power's costs related to generation dispatch and scheduling. These costs are in accordance with the Generation Dispatch and Energy Management Agreement ("GDEMA") between Black Hills Power, Inc. and Cheyenne Light dated June 14, 2012 that has been approved by the Federal Energy Regulatory Commission. This agreement allocates costs to the parties contracting for services based on total capacity of each company. Based on the current Generation Dispatch and Scheduling pro forma costs, the expense adjustment is a removal of $(52,601).

Adjustment (h): Schedule H-9 is an adjustment for purchased power costs for an increase of $2,034,740. Happy Jack Wind Power Purchase Agreement ("PPA"), Silver Sage Wind PPA, and Colstrip Contract (energy only) rates are adjusted to reflect the contractual rates that will be in effect for 2013. The rate for purchasing power from Cheyenne Light, in accordance with the GDEMA, was based on the most current information available related to market price. Finally, because the Ben French power plant has suspended operations, Black Hills Power will need to purchase additional power on the market in order to meet customer needs. The purchased power MWh increase is reflected in the adjustment as well as the most current information on market price. The removal of Ben French coal is adjusted under Adjustment (m), or Schedule H-14.

Adjustment (i): Schedule H-10 provides an adjustment for removal of generation plant overhaul expenses related to the Ben French power plant and the Neil Simpson I power plant. Both of these plants will be permanently retired in March 2014 to comply with environmental standards. Therefore, total expenses related to these generation plants overhaul of $(323,892) was removed from the test year. This adjustment also calculates the accrual reversal amortization calculation. Similar to how the accrual was established, which was over a seven year period, the amount on line 13 is amortized over this same time frame. The annual adjustment calculation results in an additional $(104,108) removal from the test year.

Adjustment (j): Schedule H-11 represents the removal of costs associated with unallowable advertising as well as elimination of preliminary charges. The total expenses that were eliminated from the test year was $(729,412).

Adjustment (k): The adjustments in Schedule H-12 relate to Power Marketing activities of Black Hills Power. Adjustments made represent costs for energy sold by Power Marketing for marketing purposes which are not used to serve Black Hills Power’s load and thus, not included in cost of service expense. The total expenses that were eliminated from the test year was $(33,205,684).

Adjustment (l): Schedule H-13 is a detailed listing of rate case expenses that are expected to be incurred in this rate case proceeding. The costs will be amortized into expenses over a three year period with the un-expensed amount included in rate base.

Adjustment (m): Schedule H-14 adjusts for the removal of operating and maintenance expenses related to the Ben French power plant operations. As shown on line 19, there were some employees that relocated from the Ben French Power Plant to the Neil Simpson Power plant. This is further discussed in Mr. Lux's direct testimony. The net adjustment of $(1,330,993) is a reduction to operation and maintenance expense.

Adjustment (n): Schedule H-15 provides for the pro forma adjustment for the price of coal. This adjustment was required due to plant outages and was based on normalizing coal average use by plant. The normalized coal usage was used to determine the projected coal costs for 2013. The coal price is based on Statement R pricing for 2013. Further, this adjustment removes coal costs and transport costs related to Ben French power plant, due to suspended operations. The net adjustment of $(3,049,322) is shown on Statement H. The testimony of Mr. White addresses the Statement R – Affiliate Transaction coal pricing in further detail.

Adjustment (o): Schedule H-16 represents the removal of costs associated with severance expense during the test year. The total expenses eliminated were $(287,953).

Adjustment (p): The Ben French Power plant suspended operations September 1, 2012. This power plant was used as part of Black Hills Power required spinning reserve. Due to suspension of operations, the Company will need to purchase spinning reserves from the market, and will be unable to sell spinning reserve as it has done in the past. Therefore, total spinning reserve sales included in the test year was removed of $174,357.

V. ADDITIONAL CHANGES TO THE OPERATING EXPENSES

Q. WHAT ADDITIONAL ADJUSTMENTS DID YOU MAKE TO THE OPERATING EXPENSES?

A. The depreciation expense was adjusted, as shown on Statement J, to account for the capital additions that will be placed in service on or before the effective date of this rate case. Depreciation rates established in the depreciation study completed in January 2009 were used to calculate the additional depreciation expense.

Q. HOW IS THE DEPRECIATION ADJUSTMENT CALCULATED ON STATEMENT J?

A. The depreciation adjustment is calculated by using the existing depreciation rates, as determined by the last depreciation study, multiplied by the average adjusted plant in service. The adjusted depreciation expense is then compared to the per books amount for the test year and the difference is recorded on Statement M as the adjusted depreciation expense and an increase in accumulated depreciation.

Q. PLEASE EXPLAIN THE REMAINING CHANGES TO THE REVENUE REQUIREMENT MODEL.

A. On Statement L, payroll taxes were adjusted based on the known and measurable adjustments described on Schedule H-1. The net payroll change was multiplied by the federal and state payroll tax rates to determine an adjustment decrease of $(9,578) to payroll taxes as shown on Schedule L-1.

Q. PLEASE EXPLAIN THE ADJUSTMENT FOR THE SOUTH DAKOTA PUC TAX.

A. This adjustment is based on the additional revenue requirement for South Dakota multiplied by the gross receipts tax resulting in an additional cost shown on Statement L.

Q. HOW IS THE ADJUSTMENT FOR PROPERTY TAXES CALCULATED ON STATEMENT L?

A. The additional property tax is calculated based on the 12 month average of assets in FERC account 106, then adding subsequent additions and multiplying by the blended property tax rate. The blended property tax ratio was developed based on projected tax levies for a normalized twelve month operating period. The total property tax adjustment is $469,541 as shown on Schedule L-1.

Q. HOW IS THE FEDERAL INCOME TAX CALCULATED?

A. Federal income taxes are calculated based on the adjusted rate base amount on Statement M and Statement G page 1, debt and equity ratios. The adjusted operating income before tax amount found on Statement M, column (e), line 14 is then reduced by the adjusted interest expense as calculated on Statement K, page 3 line 5. This resulting amount is then multiplied by the 35 percent federal income tax rate.

Q. WHAT IS THE SOURCE OF THE PER BOOKS REVENUE ON STATEMENT I, PAGE 3?

A. The per books revenue is from the billing system for the customers of Black Hills Power for the test year ended June 30, 2012. Billing determinates and adjustments to retail revenue is further discussed in Ms. Kirsch's direct testimony.

Q. PLEASE DESCRIBE THE ADJUSTMENT TO OTHER NON-FIRM REVENUE ON STATEMENT I, PAGE 1.

A. The other non-firm revenue adjustment represents the removal of revenue associated with Power Marketing. The removal of expenses associated with Power Marketing are removed on Schedule H-12. The reason for the adjustment is the revenue and associated costs are included in the Energy Cost Adjustment ("ECA") on an annual basis.

Q. PLEASE DESCRIBE THE ADJUSTMENT TO CONTRACT SALES REVENUE ON STATEMENT I, PAGE 1.

A. The contract sales adjustment as shown on Statement I, page 2, is the adjustment for the MEAN (Municipal Energy Agency of Nebraska) contract sale price per MWh. The total contract sales adjustment is an increase of $1,571,695 in revenue. The remainder of the adjustment relates to the removal of energy cost revenue calculated on Statement I, page 5.

Q. PLEASE EXPLAIN THE ADJUSTMENT FOR THE REMOVAL OF ENERGY COST REVENUE ON STATEMENT I, PAGE 5.

A. Revenue associated with the energy cost adjustment was removed from retail revenue on Statement I page 1 as well as cost adjustment revenue related to contract sales for MEAN and MDU. This relates to the matching principle as delivered energy costs were also eliminated in Statement H, column (q), as the Company is not proposing a change to the base rate of the energy cost adjustment. This adjustment is further described in Mr. Kilpatrick's direct testimony.

Q. PLEASE DESCRIBE THE ADJUSTMENT TO CITY OF GILLETTE REVENUE.

A. The City of Gillette revenue was removed as it relates to replacement energy. The associated costs are included in Power Marketing adjustment at Schedule H-12.

Q. PLEASE EXPLAIN THE MISCELLANEOUS SERVICE REVENUE ADJUSTMENT.

A. The miscellaneous service revenue adjustment reflects the proposed change in rates for reconnect revenues for SD customers. The proposed tariff changes are further discussed in Ms. Rahn's direct testimony.

Q. PLEASE EXPLAIN THE ADJUSTMENT TO RENT FROM ELECTRIC PROPERTY AND OTHER.

A. The total adjustment of $(2,926,782) relates to two different components. The Reserve Capacity Agreement expired in 2012; therefore the revenue associated with the contract of $(2,728,900) was removed from the test year as this contract will no longer continue. Further, there was removal of $(197,882) related to pole attachment revenue as shown on Statement I, page 2, due to a decrease in pole attachment rates as the formula for charging pole attachment rates has been changed by the Federal Communications Commission.

Q. HOW ARE THE ADJUSTED SALES FOR RESALE HANDLED ON STATEMENT I, PAGE 1?

A. The remaining revenue in the sales for resale on line 12 are considered revenue credits.

Q. WHAT IS THE REQUESTED AMOUNT OF THE SOUTH DAKOTA INCREASE IN ELECTRIC BASE RATES?

A. Black Hills Power is seeking to increase its electric base rates to recover $13,745,826 million in additional annual revenues, or an increase of 9.94%. This increase is calculated based on Black Hills Power's pro forma revenue requirement using a test year of the twelve months ending June 30, 2012. This revenue requirement is based on the jurisdictional allocation prepared on Schedule N-1.

Q. EXPLAIN HOW STATEMENT N AND SCHEDULE N-1 WAS PREPARED.

A. Statement N was prepared based on Black Hills Power's per book financial statements as filed in the application. Schedule N-1 is the same as Statement N, except that the amounts in the total column on Schedule N-1 are from the adjusted amounts for the rate base and cost to serve customers. The allocation factors used in Statement N and Schedule N-1 are consistent to ensure the adjusted amounts are allocated based on the similar methodologies. The jurisdictional allocation factors as well as steps allocating rate base and expenses to jurisdictions are further described in Ms. Kirsch's direct testimony.

Q. HOW WILL THE SOUTH DAKOTA REVENUE REQUIREMENT BE APPLIED TO RATE CLASSES?

A. Using the adjusted rate base and cost of service, functions are then created using FERC functional classifications (Production, Transmission, Distribution, Customer Service and General). Within each functional classification, an allocation percentage was used to allocate rate base and costs based on the main driver of the rate base or expense. This methodology conforms to the general rate making principle of cost causation.

Q. EXPLAIN HOW STATEMENT O AND SCHEDULE O-1 WAS PREPARED.

A. Statement O was prepared based on the per book amounts in the financial statements for only the South Dakota portion of the revenue requirement model that was developed in Statement N. Schedule O-1 reflects the as adjusted amounts. The total South Dakota amount is allocated to the South Dakota customers based on the allocation factors developed. The allocation factors and the class cost of service study are further discussed in Ms. Kirsch's direct testimony.

VI. CONCLUSION

Q. DOES THE MODEL RESULT IN A JUST AND REASONABLE REVENUE REQUIREMENT?

A. Yes. The Model uses the per books financial statements for the test year ending June 30, 2012, which contains known and measurable adjustments. The effect is a straight-forward application supporting the requested increase in base rates.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.