Rebuttal Testimony and Exhibit
Jon Thurber

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. EL14-026

January 15, 2015

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**Exhibits**

## I. INTRODUCTION

**Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A. My name is Jon Thurber, 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 employed by Black Hills Utilities Holdings, Inc. ("Utility Holdings"), a wholly-owned subsidiary of Black Hills Corporation ("BHC"). I am Manager of Regulatory Affairs for Black Hills Power, Inc. ("Black Hills Power" or the "Company"). I am responsible for leading all aspects of the regulatory process for Black Hills Power.

**Q. FOR WHOM ARE YOU TESTIFYING ON BEHALF OF TODAY?**

A. I am testifying on behalf of Black Hills Power.

**Q. DID YOU FILE DIRECT TESTIMONY IN THIS DOCKET?**

A. Yes.

## II. PURPOSE OF REBUTTAL TESTIMONY

**Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

A. The purpose of my rebuttal testimony is to explain and support the portions of the Settlement Stipulation ("Settlement Agreement"), reached between Black Hills Power and the South Dakota Public Utilities Commission Staff ("Staff"), that pertain to the: (1) revenue requirement adjustments under South Dakota administrative rule 20:10:13:44; (2) decommissioning regulatory asset and amortization adjustment; (3) LIDAR adjustment, (4) employee additions/eliminations adjustment; (5) utility holdings allocation correction; (6) pension expense adjustment; and (7) new debt issuance. I also explain why the positions advanced by the Black Hills Industrial Intervenors' ("BHII") witness Mr. Lane Kollen on these subjects are not appropriate.

## III. REVENUE REQUIREMENT ADJUSTMENTS UNDER SOUTH DAKOTA ADMINISTRATIVE RULE 20:10:13:44

**Q. PLEASE EXPLAIN BLACK HILLS POWER'S APPROACH TO MEASURING ITS REVENUE REQUIREMENT IN THIS CASE.**

A. Black Hills Power utilized a twelve month test year based on historical data, ending September 30, 2013. Adjustments for known and measurable items were then made to the historical test year to determine the pro forma costs.

**Q. UNDER THE SETTLEMENT AGREEMENT, WERE ADDITIONAL ADJUSTMENTS MADE TO BLACK HILLS POWER'S REVENUE REQUIREMENT?**

A. Yes, the Settlement Agreement reflects a variety of adjustments that were made to the Company's filed revenue requirement.

**Q. ARE THE ADJUSTMENTS TO BLACK HILLS POWER'S REVENUE REQUIREMENT THAT ARE REFLECTED IN THE SETTLEMENT AGREEMENT CONSISTENT WITH THE REQUIREMENTS OF ARSD 20:10:13:44?**

A. Yes. The Company utilized an appropriate test year and made adjustments to its book costs that were based on changes in facilities, operations, and costs that were known with reasonable certainty and measurable with reasonable accuracy and either have been or will become effective within the 24 months following the last month of the test year.

Q. **PLEASE EXPLAIN THE BASIS FOR THE COMPANY'S BELIEF THAT THE ADJUSTMENTS ARE RELATED TO COSTS THAT ARE KNOWN WITH REASONABLE CERTAINTLY AND MEASURABLE WITH REASONABLE ACCURACT?**

A. The end of the historic test year in this filing was September 30, 2013. As such, there have been over fifteen months of changes in facilities, operations and costs that have occurred and would be appropriately adjusted for under the Rule. Furthermore, the vast majority of the adjustments relate to costs that the Company incurred during the 12 months following the historic test year.

Q. **REFERRING TO MR. KOLLEN'S DIRECT TESTIMONY, PAGE 7, LINE 16 THROUGH PAGE 8, LINE 21, DO YOU AGREE THAT THE COMMISSION SHOULD LIMIT ANY POST-TEST YEAR ADJUSTMENTS TO THE TWELVE MONTH PERIOD IMMEDIATELY FOLLOWING THE HISTORIC TEST YEAR ENDING SEPTEMBER 30, 2013?**

A. No, I do not. Mr. Kollen's interpretation of ARSD 20:10:13:44 ignores the plain language of the rule that specifically states that reasonably certain and reasonably accurate adjustments which will become effective within the twenty four months following the last month of the test period are permitted.

**Q. MR. KOLLEN INDICATES THAT ADJUSTMENTS ARE NOT PERMITTED UNLESS THE CORRESPONDING PROJECTED CHANGES IN REVENUE ARE INCLUDED IN THE REVENUE REQUIREMENT. PLEASE EXPLAIN WHY A RETAIL REVENUE ADJUSTMENT FOR SALES GROWTH WAS NOT INCLUDED IN THE SETTLEMENT AGREEMENT?**

A. It is my understanding that it has been Staff's practice to exclude all revenue producing plant from the plant annualization and post-test year addition adjustments. Revenue producing plant consists primarily of distribution investments. Staff followed this practice in this case. It would therefore be inappropriate for additional revenues to be reflected in the cost of service because the investment needed to serve the sales growth is not included as well. Commission policy has been to reflect any incremental revenue or cost savings associated with post-test year adjustments in the revenue requirement.

**Q. MR. KOLLEN CHARACTERIZES THE COMPANY'S ADJUSTMENTS AS OPPORTUNISTIC AND SELECTIVE. DO YOU AGREE WITH HIS CHARACTERIZATION OF THE ADJUSTMENTS THAT HAVE BEEN PROPOSED BY THE COMPANY?**

A. No, absolutely not. Contrary to his characterizations, the Company included pro forma cost increases and cost reductions that occurred after the historic test year in the adjustments it made. Some of the material cost reductions, at the total company level, included in the filing were:

- Schedule H-1 Neil Simpson I labor and benefit costs - $746,475;
- Schedule H-6 FAS106 Retiree Healthcare - $168,896;
- Schedule H-6 FAS87 Pension Expense - $508,454;
- Schedule H-11 Advertising Expense - $262,517;
- Schedule H-16 Ben French Severance Expense - $180,861;
- Schedule H-18 Ben French, Osage, Neil Simpson I O&M - $3,753,186;
- Schedule H-21 Customer Service Model Adjustment - $215,934; and
- Statement J Ben French, Osage, Neil Simpson I Depreciation Removal - $1,732,526.

In total, the Company removed over $7,500,000 worth of expenses from the historic test year on an annual basis in the original filing.

**Q. IN THE SETTLEMENT AGREEMENT, THE COMPANY AGREED TO UPDATE MANY ADJUSTMENTS IN THE ORIGINAL FILING THAT WERE BASED ON BUDGETS TO REFLECT RECENT ACTUAL COSTS. WERE THERE ANY MATERIAL REDUCTIONS IN EXPENSES AS A RESULT OF THESE UPDATES?**

A. Yes, a few of the material cost reductions, at the total company level, were as follows:

- Updated Schedule G-3 to reflect the actual debt issuance and cost – weighted average cost of debt was reduced from 6.45% to 6.08%, for over $1,000,000;
- Updated Schedule H-6 Pooled Medical Costs – approximately $400,000; and

- Updated Schedule H-8 Generation Dispatch and Scheduling Costs – over $300,000.

Clearly, the Company reflected both cost increases and reductions in the original filing and Settlement Agreement. Mr. Kollen's characterization of the Company as opportunistic and selective lacks merit.

**Q. SHOULD THE COMMISSION ACCEPT THE ADJUSTMENTS TO THE REVENUE REQUIREMENTS THAT ARE REFLECTED IN THE SETTLEMENT AGREEMENT?**

A. Yes, I believe the Commission should accept the adjustments as they were made in conformance with the requirements of ARSD 20:10:13:44.

## IV. <u>DECOMMISSIONING REGULATORY ASSET AND AMORTIZATION</u>

**Q. DID THE COMMISSION ISSUE AN ACCOUNTING ORDER TO ESTABLISH A REGULATORY ASSET FOR THE COSTS ASSOCIATED WITH DECOMMISSIONING THE NEIL SIMPSON I, OSAGE, AND BEN FRENCH POWER PLANTS?**

A. Yes. On January 9, 2014, in Docket EL13-036, the Commission issued an Order approving deferred accounting for the transfer of remaining plant balances and associated inventory for soon to be decommissioned plants to a regulatory asset.

**Q. PLEASE EXPLAIN THE DECOMMISSIONING ADJUSTMENT INCLUDED IN THE COMPANY'S FILED POSITION.**

A. Black Hills Power proposed to amortize the costs associated with the retirement and decommissioning of the Neil Simpson I, Ben French, and Osage facilities over five years as reflected on Schedule J-2. The unamortized balance of the regulatory asset included in the test year would then be reduced by the accumulated amortization for a full year. The costs associated with the retirement of the units included the unrecovered plant and obsolete inventory. The estimated costs associated with decommissioning the units were provided in Response to SDPUC Request No. 3-23.

**Q. WHY DID BLACK HILLS POWER REQUEST RECOVERY OVER A FIVE YEAR PERIOD?**

A. The time period provided a balance between the amount of time required to minimize rate impact to customers and matched the expense as best as possible with the customers who have utilized the assets being retired. The proposed amortization period achieved an annual amortization expense that is approximately equivalent to the annual amount that it would cost to continue to operate these facilities.

**Q. PLEASE DESCRIBE THE DECOMMISSIONING ADJUSTMENT INCLUDED IN THE SETTLEMENT AGREEMENT.**

A. The Settlement Agreement makes the following adjustments to the Company's filed position:

- The obsolete inventory balance was updated to reflect the thirteen month average balance to correlate with the amount removed from working capital.
- The contingencies were removed from the estimated decommissioning costs. The Settlement Agreement grants Black Hills Power the opportunity to seek

recovery, in a future Black Hills Power rate case, of all costs for decommissioning not otherwise recovered from customers.

- An adjustment was made to reflect the accumulated deferred income taxes associated with the decommissioning adjustment. Please refer to the rebuttal testimony of Mr. Robert Hollibaugh for details.
- The amortization period was modified from five to ten years.
- The regulatory asset included in rate base is reduced by one and one-half years of amortization expense to reflect the average unamortized balance over the first three years of the amortization period in rate base.

**Q. ARE THERE ANY ADDITIONAL REVENUES ADDED TO THE TEST YEAR AS A RESULT OF THIS ADJUSTMENT?**

A. There are no additional revenues as a result of retiring and decommissioning the facilities. The salvage value credit was reflected in the lump sum decommissioning bid and resulted in a lower cost to customers.

**Q. MR. KOLLEN STATES THAT DECOMMISSIONING COSTS SHOULD NOT BE INCLUDED IN THE SETTLEMENT AGREEMENT BECAUSE THE COSTS WILL NOT HAVE BEEN INCURRED IN THE TWELVE MONTH PERIOD FOLLOWING THE HISTORIC TEST YEAR. DO YOU AGREE?**

A. No, I disagree with Mr. Kollen for a variety of reasons. First, as I discussed above, I disagree with Mr. Kollen's interpretation of ARSD 20:10:13:44. In particular, the Rule does not limit adjustments to known and measurable costs that were incurred in the twelve months following the historic test year. Second, the vast majority of the decommissioning costs that are reflected in the Settlement Agreement are supported by a fixed price contract that was provided by the Company in response to SDPUC Request No. 3-25. Black Hills Power selected the fixed price contract through a competitive bidding process as the lowest cost proposal that met the technical specification of the request for proposal. Third, the remaining costs that are included in the Settlement Agreement are supported by the Company's engineering cost estimate that was provided in response to SDPUC Request No. 3-23. As a result, the decommissioning costs that are reflected in the Settlement Agreement are known with reasonable certainty and measurable with reasonable accuracy.

**Q. HAS THE COMMISSION ACCEPTED ENGINEERING ESTIMATES FOR DECOMMISSIONING COSTS IN A RECENT APPROVED RATE CASE SETTLEMENT?**

A. Yes. In Docket EL12-046, Northern States Power Company used a decommissioning cost study as the estimate to determine the appropriate decommissioning accrual for its nuclear facilities in advance of incurring the costs. After removing the contingencies, Staff accepted Northern States Power Company's study as the basis for the decommissioning accrual and included the adjustment as part of the rate case settlement ultimately approved by the Commission. Here, the Staff and the Company used the Northern States Power

Company rate case settlement as a guide for the decommissioning adjustment included in this Settlement Agreement.

**Q. MR. KOLLEN STATES THAT THE ACCUMULATED DEFERRED INCOME TAX ADJUSTMENT ASSOCIATED WITH THE DECOMMISSIONING REGULATORY ASSET IS INCORRECTLY CALCULATED. DOES THE COMPANY AGREE WITH MR. KOLLEN's POSITION?**

A. No. The Company believes Mr. Kollen's treatment of accumulated deferred income tax is incorrect. Mr. Robert Hollibaugh addresses the accumulated deferred income tax calculation in his rebuttal testimony.

**Q. ARE THERE ANY OTHER STATEMENTS THAT MR. KOLLEN MADE PERTAINING TO DECOMMISSIONING THAT YOU WOULD LIKE TO ADDRESS?**

A. Yes. Mr. Kollen indicates in his direct testimony on page 20, lines 6 – 8, that the Settlement Agreement reflects a ten year amortization of the decommissioning regulatory asset. Then, on page 42, line 23, through page 43, line 1-3, of Mr. Kollen's direct testimony, he states that the Settlement Agreement reflects a five year amortization of the decommissioning regulatory asset. Although I do not know if this inconsistency reflects an oversight in drafting or a misunderstanding of the terms of the Settlement Agreement, to the extent that Mr. Kollen incorporates a five year amortization in his numbers, his assumption is inconsistent with the terms of the Settlement Agreement.

**Q. DID THE COMPANY REQUEST AN ORDER FROM THE COMMISSION TO DEFER ANY COSTS ASSOCIATED WITH THE DECOMMISSIONING OF THE RETIRED STEAM PLANTS?**

A. No. The Company and Staff filed the Settlement Agreement on December 9, 2014, that established the amortization of decommissioning costs. The Settlement Agreement also grants Black Hills Power the opportunity to seek recovery, in a future Black Hills Power rate case, of all costs for decommissioning not otherwise recovered from customers. Since the Settlement Agreement was filed prior to the end of 2014 and is being considered in this rate proceeding, it was not necessary to request an accounting authority order allowing Black Hills Power to use deferred accounting for costs associated with the decommissioning of the retired steam plants.

**Q. DO YOU BELIEVE THE COMMISSION SHOULD ACCEPT THE TREATMENT OF THE DECOMMISSIONING ADJUSTMENT?**

A. Yes, I believe the treatment of the decommissioning adjustment that is reflected in the Settlement Agreement is appropriate and in conformance with past practices.

## V. LIDAR ADJUSTMENT

**Q. PLEASE EXPLAIN THE COMPANY'S FILED LIDAR ADJUSTMENT.**

A. For purposes of background, at the time that Black Hills Power filed the pending rate case, it planned to perform LIDAR (Light Detection and Ranging) imaging of all of its 69 kV and 230 kV facilities in 2014. The need for and scope of the LIDAR surveying project is discussed in the direct testimony of Mike Fredrich.

The Company's filed position reflected the estimated cost of the LIDAR surveying project on its 69 kV transmission system. The project cost of $798,000 was shared with the joint owners of the 69 kV system, and Black Hills Power's share was amortized over five years to correspond with the expected frequency of the survey. The Company requested the unamortized amount be included in rate base.

**Q. DOES THE SETTLEMENT AGREEMENT REFLECT AN ADJUSTMENT FOR THE LIDAR PROJECT?**

A. Yes. The LIDAR project cost was updated to reflect the least cost, competitive bid contract, and the current allocation to the joint owners of the 69 kV systems in South Dakota and Wyoming. Black Hills Power's share of the costs was amortized over five years, and one-half of the unamortized balance was reflected in rate base. The accumulated deferred income taxes associated with one-half of the unamortized regulatory asset was reflected in the Settlement Agreement. The accumulated deferred income tax adjustment is covered in more detail in the rebuttal testimony of Mr. Robert Hollibaugh.

**Q. MR. KOLLEN HAS SUGGESTED THAT LIDAR COSTS ARE NOT PROPERLY INCLUDED. DO YOU DISAGREE WITH MR. KOLLEN'S POSITION ON THE LIDAR ADJUSTMENT?**

A. Yes. The Company has provided evidence to support the inclusion of these costs as a known and measurable adjustment. The request for proposal selected as part of the competitive bid process for the LIDAR project and the revised pricing was provided as a Supplemental Response to SDPUC Request No. 4-34 on October 15,

2014. The supporting work papers for the allocation of LIDAR costs to Black Hills Power was provided as a Supplemental Response to SDPUC Request No. 4-36, on October 15, 2014. The calculation included the actual allocation of the joint owners of South Dakota 69 kV system using the April 1, 2014, allocation. The Company provided Staff with a revised allocation of LIDAR costs to Black Hills Power on October 21, 2014, to remove the costs associated with the joint owners of the Wyoming 69 kV using the April 1, 2014, allocation. The email and supporting work papers were provided to Staff on October 21, 2014, and were provided in discovery in the Second Supplemental Response to SDPUC Request 4-36 on January 5, 2015.

**Q. WHY DOES THE LIDAR ADJUSTMENT INCLUDED IN THE SETTLEMENT AGREEMENT REFLECT A KNOWN AND MEASURABLE ADJUSTMENT?**

A. The project costs are based on a fixed price contract that was competitively bid to achieve the lowest cost for customers. The actual cost was approximately half of the original budget. The allocations to the joint owners of the 69 kV system in South Dakota and Wyoming were based on the current allocations in effect. The LIDAR surveying work and data acquisition was completed in the fourth quarter of 2014.

**Q. DO COSTS NEED TO BE INCURRED BY OCTOBER 1, 2014, TO BE CONSIDERED KNOWN AND MEASURABLE?**

A. No, the fixed price contract with costs incurred within 24 months of the last month of the test period qualify as an appropriate adjustment under ARSD 20:10:13:44. There are no anticipated reductions to test year costs or additional revenues expected as a result of this project.

**Q. DO YOU BELIEVE IT IS APPROPRIATE TO REFLECT A TEN YEAR AMORTIZATION PERIOD?**

A. No, a five year amortization period corresponds with the expected frequency of the LIDAR survey. A ten year amortization is arbitrary, and the annual amortization allocated to South Dakota of $64,107 based on a 5 year amortization is not of the magnitude that would justify a ten year amortization for rate mitigation purposes.

**Q. DID THE COMPANY REQUEST AN ORDER FROM THE COMMISSION TO DEFER ANY COSTS ASSOCIATED WITH THE LIDAR PROJECT?**

A. No. The Company and Staff filed the Settlement Agreement on December 9, 2014, that established the amortization of LIDAR costs for the Commission to consider. Since the Settlement Agreement was filed prior to the end of 2014 and is being considered in this rate proceeding, it was not necessary to request an accounting authority order allowing Black Hills Power to use deferred accounting for costs associated with the LIDAR project.

**Q. DO YOU SUPPORT THE TREATMENT OF THE LIDAR ADJUSTMENT THAT IS REFLECTED IN THE SETTLEMENT AGREEMENT?**

A. Yes, I do.

## VI. EMPLOYEE ADDITION/ELIMINATION ADJUSTMENT

**Q. PLEASE EXPLAIN THE COMPANY'S FILED EMPLOYEE ADDITION AND ELIMINATION ADJUSTMENT.**

A. Black Hills Power planned to hire nineteen unfilled and new positions as of January 28, 2014, payroll which are necessary to provide electric service to customers. In addition, the Company reflected the elimination of two employees after the January 28, 2014, payroll. The adjustment reflects the net employees' salary and benefit costs.

**Q. DID THE SETTLEMENT AGREEMENT REFLECT THE ADJUSTMENT AS FILED?**

A. No. Through Staff's audit, costs were only included for positions actually hired at the time of settlement negotiations. Adjustments were also made to reflect the 2015 known and measurable wage annualization and to include only the portion of labor costs charged to expense accounts.

**Q. DOES MR. KOLLEN AGREE WITH THIS ADJUSTMENT?**

A. No, he does not. Mr. Kollen's recommendation is to remove all costs associated with employee additions and eliminations.

**Q. MR. KOLLEN ARGUES THAT THE COMMISSION SHOULD NOT ALLOW BUDGETED EMPLOYEE ADDITIONS IN RATES BECAUSE THEY DO NOT REFLECT ACTUAL EXPERIENCE. ARE MR. KOLLEN'S CONCERNS REGARDING BUDGETED EMPLOYEE**

**ADDITIONS AND ACTUAL EXPERIENCE ADDRESSED IN THE SETTLEMENT AGREEMENT?**

A. Yes. Staff only allowed positions that have been hired. The Company has not recovered costs associated with budgeted employees in rates, so Mr. Kollen's comparison of actual to budget headcounts are invalid.

## VII. UTILITY HOLDINGS ALLOCATION CORRECTION

**Q. DOES THE COMPANY AGREE WITH MR. KOLLEN THAT THE STAFF REVENUE REQUIREMENT MODEL INCLUDES AN ERROR IN ALLOCATION TO SOUTH DAKOTA FOR TRANSMISSION LOAD DISPATCH COSTS?**

A. Yes, the Company agrees that no costs associated with transmission load dispatch, FERC Account 561, should be allocated to South Dakota.

**Q. DOES BLACK HILLS POWER BELIEVE THAT THE SETTLEMENT AGREEMENT SHOULD BE MODIFIED TO CORRECT THIS ERROR?**

A. No, it does not. Black Hills Power supports the Settlement Agreement and the resulting revenue requirement that has been presented to the Commission. If Staff and Black Hills Power litigated this proceeding, the Company and Staff would likely advocate different positions than what is reflected in Staff's revenue requirement model. Related thereto, on page 2 of the Settlement Stipulation, under Purpose, it states, "The Parties acknowledge that they may have differing views that justify the end result, which they deem to be just and reasonable, and, in light of such differences, the Parties agree that the resolution of any single issue, whether express or implied by the Stipulation, should not be viewed as precedent setting."

Notwithstanding the differences of opinion regarding the costs that comprise the revenue requirement, the Company and Staff ultimately agreed that the total revenue deficiency is $6,890,746. The revenue deficiency is material to the Company. The Company agreed to a two year rate moratorium, which can only be negotiated as part of a Settlement Agreement. The Company used the annual revenues authorized in this Settlement Agreement to determine if it could manage its business through a rate freeze. Black Hills Power agreed to significant concessions in order to reach a comprehensive resolution of all issues in this rate proceeding and as a result believes that the revenue deficiency should be maintained as presented to the Commission.

**Q. WOULD THE COMPANY HAVE ACCEPTED THE ALLOCATION CORRECTION DURING SETTLEMENT NEGOTIATIONS?**

A. Yes, it would have. However, the Company would also have had the opportunity to negotiate differently on other adjustments or request other adjustments to achieve the revenues necessary to recover its costs and earn a fair rate of return on investments.

**Q. DO YOU HAVE ANY EXAMPLES OF COSTS THAT HAVE INCREASED THAT WERE NOT REFLECTED IN THE SETTLEMENT AGREEMENT?**

A. Yes. After the Company reached a Settlement Agreement with Staff, it became aware that the production operations and maintenance ("O&M") costs associated with the Wyodak power plant ("Wyodak") were abnormally low during the historic test year and were not reflective of current production O&M costs. The total company Wyodak production O&M cost was $3,390,425 during the historic test year, and these costs were included in the Settlement Agreement. When compared to the costs incurred from October 2013 through September 2014, the total company Wyodak production O&M cost increased $459,738 for a total cost of 3,850,163. Please see Exhibit JTR-1 for details.

**Q. PLEASE DESCRIBE THE PRODUCTION O&M COSTS ASSOCIATED WITH WYODAK?**

A. Wyodak is operated by the majority owner, PacifiCorp, who invoices Black Hills Power on a monthly basis for the operating costs of the plant. The O&M costs are the routine costs of operating a power plant. Labor costs represent approximately 50% of the O&M costs, and the remainder of the costs is primarily associated with materials and outside services. Materials include production materials such as lime for environmental compliance and consumable items such as filters, piping, motors, and generators. Wyodak uses contractors for many services, such as ash hauling, security, janitorial, plant maintenance, and inspections.

**Q. WERE THE ACTUAL PRODUCTION O&M COSTS ASSOCIATED WITH THE WYODAK POWER PLANT ABNORMALLY HIGH FROM OCTOBER 2013 THROUGH SEPTEMBER 2014?**

A. No, please see the table below for Wyodak's production O&M costs from October 2010 through September 2014.

| | 10/1/10 - 9/30/11 | 10/1/11 - 9/30/12 | 10/1/12 - 9/30/13 | 10/1/13 - 9/30/14 | 4 Year Average |
|---|---|---|---|---|---|
| Wyodak O&M | 3,566,605 | 3,560,008 | 3,390,425 | 3,850,163 | 3,591,800 |

Clearly, the historic test year was less than every other year during the four year period by at least $160,000, and adjusting the test year to the four year average would result in a total company adjustment of over $200,000. In addition, expenses associated with major maintenance outages were normalized during this time period through major maintenance accrual accounting.

**Q. WOULD IT BE APPROPRIATE TO ADJUST THE HISTORIC TEST YEAR WYODAK O&M COSTS TO THE FOUR YEAR AVERAGE FROM OCTOBER 2010 THROUGH SEPTEMBER 2014?**

A. No, the historic costs have not been adjusted for inflation, wage increases, and benefit changes. Known and measurable adjustments for labor and inflation would need to be reflected in the historic annual amounts in order for a normalization to reflect current costs. Applying three percent annual inflation to the October 2010 through September 2011 Wyodak production O&M expense yields a similar expense as the October 2013 through September 2014 Wyodak production O&M expense. The October 2013 through September 2014 Wyodak production O&M costs are conservative because they do not reflect the annualization of known and measurable wage and benefit changes for 2014 and 2015.

**Q. HOW WOULD THE COMPANY PROPOSE TO RESOLVE THE UTILITY HOLDINGS COMPANY TRANSMISSION ALLOCATION ERROR IN STAFF'S MODEL?**

A. The Company recommends making no adjustment to the Settlement Agreement. Staff's revenue requirement model reflects many concessions made by Staff and Black Hills Power. However, if the Commission modifies the Settlement Agreement to correct the transmission allocation error, the Company respectfully requests that the Commission also modify the Settlement Agreement to include an adjustment to reflect South Dakota's allocated share of Wyodak's production O&M costs from October 2013 through September 2014, as reflected on Exhibit JTR-1.

## VIII. <u>PENSION EXPENSE</u>

**Q. DID BLACK HILLS POWER PROPOSE AN ADJUSTMENT TO THE TEST YEAR LEVEL OF PENSION EXPENSE?**

A. Yes. The Company proposed to reduce test year total company pension expense by approximately $508,000, as reflected on Schedule H-6. The Company's adjustment is based on a 5 year average of actual pension costs from 2010 – 2014.

**Q. WHY DID THE COMPANY USE A 5 YEAR AVERAGE AS THE BASIS FOR THE ADJUSTMENT?**

A. As provided in response to SDPUC Request No. 1-1, the table below summarizes the actual pension expense from 2010 to 2014:

| Year | FAS 87 Cost | Year by Year Variation |
|---|---|---|
| 2010 | $2,925,853 | |
| 2011 | 1,819,156 | -37.82% |
| 2012 | 3,251,072 | 78.71% |
| 2013 | 2,709,322 | -16.66% |
| 2014 | 976,122 | -63.97% |
| Average | $2,336,305 | |

In particular, the annual total company pension expense has ranged between $976,122 and $3,251,072 from 2010 through 2014, and the annual percent change has ranged between a 64% decrease and a 79% increase. The Company proposed normalizing pension expenses as a result of the volatility in expense experienced from year to year.

**Q. DOES THE SETTLEMENT AGREEMENT REFLECT A 5 YEAR NORMALIZATION OF PENSION EXPENSE?**

A. Yes. As provided in the Settlement Stipulation, the Commission Staff and Black Hills Power agree this normalization period shall be used in future rate cases over the next five years unless there is an extraordinary event that makes a five-year normalization period unreasonable.

**Q. IS MR. KOLLEN'S PROPOSED PENSION EXPENSE ADJUSTMENT REFLECTIVE OF NORMAL, ONGOING CONDITIONS?**

A. No, I do not believe the total company 2014 pension expense of $976,122 is reflective of normal, ongoing pension expense. The 2014 pension expense was abnormally low compared to the previous four years, and the Company expects future annual pension expense to be significantly higher than the 2014 expense.

**Q. MR. KOLLEN CHARACTERIZES THE COMPANY'S PENSION EXPENSE ADJUSTMENT AS "OPPORTUNISTIC." DO YOU AGREE?**

A. No, I do not agree with Mr. Kollen's characterization of this adjustment. If the Company in fact was being opportunistic, Black Hills Power would have proposed no adjustment to the test year. As previously mentioned, the Company's proposed adjustment reduced costs by approximately $508,000. In addition, the Staff and the Company agreed to normalize pension expense in future rate cases over the next five years unless there is an extraordinary event that makes a five-year normalization period unreasonable. This condition in the Settlement Stipulation displays a commitment to normalization rather than an opportunistic objective.

**Q. IS THERE ANY EVIDENCE THAT PENSION EXPENSE WILL INCREASE IN FUTURE YEARS?**

A. Yes. Black Hills Power's actual total company 2015 pension expense is $2,056,581. The actuarial calculation to support the expense was provided as a Supplemental Response to SDPUC 2-13. This information was not available at the time the Company and Staff reached a Settlement Agreement. If the Commission were to accept Mr. Kollen's adjustment to reflect the 2014 pension expense, the Company would be deficient in 2015 at the total company level by over $1,000,000.

The 2015 pension expense shows continued volatility in pension expense, as the 2015 expense was approximately 111% greater than the 2014 expense. The 2015 pension expense supports the reasonableness of the normalized pension expense included in the Settlement Agreement.

## IX. NEW DEBT ISSUANCE

**Q. PLEASE BRIEFLY DESCRIBE THE NEW DEBT ISSUANCE THAT WAS REFLECTED IN BLACK HILLS POWER'S ORIGINAL FILING.**

A. In its rate case Application, the Company reflected an issuance of new bonds to finance the anticipated costs related to the Cheyenne Prairie Generating Station and other capital expenditures. At the time the Application was filed, Black Hills Power anticipated adding approximately $50 million of long-term financing with an estimated all-in cost of debt of 5.67%.

**Q. HAS THE COMPANY ACTUALLY ISSUED THE NEW DEBT?**

A. Yes, the Company issued $85 million of 30 year First Mortgage Bonds with a coupon rate of 4.43% and an all-in cost of debt of 4.46%. The debt issuance was authorized by the Commission in Docket EL14-034.

**Q. WHY IS THE ALL IN DEBT COST DIFFERENT THAN THE COUPON RATE?**

A. The all-in debt cost includes the coupon interest rate and the debt issuance costs amortized over the life of the bonds. The debt issuance costs include the underwriting, legal, accounting, and other fees associated with issuing the bonds.

**Q. DOES THE SETTLEMENT AGREEMENT REFLECT THE ACTUAL COST OF THE NEW DEBT ISSUANCE IN THE WEIGHTED COST OF CAPITAL?**

A. Yes, the actual cost of the new debt is reflected in the Settlement Agreement.

**Q. MR. KOLLEN INDICATES THE ACTUAL DEBT COST IS 4.52% ON PAGE 50, LINES 1-2, OF HIS DIRECT TESTIMONY. IS THIS ACCURATE?**

A. No, it is not. Although Mr. Kollen references Black Hills Power's response to BHII Request No. 5 as support for the actual debt cost he assumed, the response does not support his assumption. Rather, the response states "Black Hills Power entered into an agreement to issue $85 million of 30 year First Mortgage Bonds with a coupon rate of 4.43." Additionally, Mr. Kollen failed to recognize that the Company provided the actual cost of debt in a supplemental response to SDPUC Request No. 2-57 on October 13, 2014.

**Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

A. Yes, it does.