

Before the South Dakota Public Utilities Commission  
State of South Dakota

In the Matter of the Application of Otter Tail Power Company  
For Authority to Increase Rates for Electric Utility  
Service in South Dakota

Docket No. EL18-021

Exhibit \_\_\_\_

**POLICY**

Rebuttal Testimony of

**BRUCE G. GERHARDSON**

March 15, 2019

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**ATTACHED SCHEDULES**

Schedule 1 – Staff Response to SD-OTP-111

Schedule 2 – Staff Response to SD-OTP-118

1 **I. INTRODUCTION AND SUMMARY**

2 Q. PLEASE STATE YOUR NAME AND OCCUPATION.

3 A. My name is Bruce Gerhardson. I am employed by Otter Tail Power Company (OTP) as  
4 Vice President of Regulatory Affairs. I am also an attorney licensed to practice law in  
5 the State of South Dakota.

6

7 Q. DID YOU PREPARE DIRECT TESTIMONY IN THIS PROCEEDING?

8 A. Yes. I filed Direct Testimony on behalf of OTP describing OTP and why OTP is  
9 requesting a rate increase. I provided a summary showing the very high levels of  
10 customer satisfaction OTP has achieved, and I described some of our recent capital  
11 expenditures, including the very large recent projects that OTP successfully completed  
12 under budget. I also discussed some of the significant sources of OTP's revenue  
13 deficiency and introduced OTP's other witnesses.

14

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

16 A. I address the appropriate legal framework and practical effects of the Return on Equity  
17 (ROE) recommended by consultant witness Mr. Basil L. Copeland Jr. on behalf of South  
18 Dakota Public Utilities Commission (Commission) Staff (Staff). I also introduce the  
19 Rebuttal Testimony provided by other OTP witnesses.

20

21 Q. HAVE OTP AND STAFF REACHED A SETTLEMENT STIPULATION IN THIS  
22 CASE?

23 A. Yes. On February 15, 2019, OTP and Staff entered into a Settlement Stipulation  
24 covering all issues except for OTP's authorized ROE. As noted in the accompanying  
25 Joint Motion for Approval of Settlement Stipulation, OTP agrees that the terms of the  
26 Settlement Stipulation are just and reasonable and consistent with South Dakota law. The  
27 Commission considered and approved the Settlement Stipulation on March 1, 2019.

1 Q. WHY IS ROE NOT PART OF THE SETTLEMENT STIPULATION?

2 A. We were unable to reach an agreement with Staff that would reflect OTP’s cost of equity  
3 capital, and the unique aspects of our performance in, and commitments to, South  
4 Dakota. These unique aspects include: (1) demonstrated substantial cost savings for  
5 South Dakota customers; (2) a combination of consistently very high quality service and  
6 very low rates; (3) our extremely large investments in South Dakota, notwithstanding the  
7 fact that South Dakota represents less than 10 percent of our retail customers; (4) the long  
8 period of time since our last rate case; and (5) our commitment to not file another rate  
9 case until 2022. Having achieved this level of performance and having made this kind of  
10 investment commitment in South Dakota, we feel it is vital that the authorized ROE be  
11 fair and reasonable. Through this case we have demonstrated that our recommended 10.3  
12 percent ROE is fair and reasonable and consistent with South Dakota law, and we have  
13 demonstrated that Mr. Copeland’s recommended ROE of 8.25 percent is simply not fair,  
14 not reasonable nor is it consistent with South Dakota law.

15 For additional perspective, about six months ago, the North Dakota Public  
16 Utilities Commission approved a settlement reached in our 2018 North Dakota rate case  
17 at an authorized ROE of 9.77 percent.<sup>1</sup> Also, the national average approved ROE in 2018  
18 was 9.68 percent for vertically integrated electric utilities. With those touchpoints, and  
19 given the other evidentiary support in this case, including OTP’s demonstrated superior  
20 performance and OTP’s enormous past and future investments in beneficial infrastructure  
21 in South Dakota, I must strongly oppose the out-of-touch ROE recommendations of Mr.  
22 Copeland.

23  
24 Q. PLEASE INTRODUCE THE WITNESSES OFFERING REBUTTAL TESTIMONY  
25 AND PROVIDE A BRIEF SUMMARY OF THEIR TESTIMONY.

26 A. The following individuals will be presenting Rebuttal Testimony in this proceeding:

- 27 • **Kevin G. Moug** explains that setting the ROE for OTP in this case will send signals  
28 to the capital markets in regard to investing in South Dakota utilities and impact the  
29 overall view of the South Dakota regulatory environment. Mr. Moug also explains

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<sup>1</sup> N.D. Pub. Serv. Comm’n Case No. PU-17-398, ORDER ON SETTLEMENT (Sept. 26, 2018); Copeland Direct at 3.

1 the negative effects that an unreasonably low ROE would have on OTP's cost of  
2 capital and generally on potential investment in South Dakota utilities and utility  
3 investment in South Dakota.

- 4 • **Robert B. Hevert** responds to the Direct Testimony of Mr. Copeland regarding the  
5 appropriate ROE for OTP and explains the wide gaps between Mr. Copeland's  
6 analysis and recommended ROE and the actual cost of equity and ROE  
7 determinations of every other regulatory commission decision since at least 1980.<sup>2</sup>  
8 Mr. Hevert also explains the flaws that cause Mr. Copeland's analysis and ROE  
9 recommendation to fail the requirement for a return comparable to returns available  
10 from investments in other comparable utilities.

## 11 **II. COMPARISON OF MR. COPELAND'S ANALYSIS AND ROE** 12 **RECOMMENDATION TO APPROPRIATE STANDARDS**

13 Q. WHAT IS MR. COPELAND'S RECOMMENDATION AS TO OTP'S COST OF  
14 EQUITY AND AN APPROPRIATE ROE FOR OTP?

15 A. Mr. Copeland contends OTP's cost of equity is presently about 7.00 percent.<sup>3</sup> He  
16 recommends a range for OTP's ROE of 8.00 percent to 8.50 percent and that the  
17 Commission approve a ROE of 8.25 percent.<sup>4</sup>

18  
19 Q. HOW DO THESE RECOMMENDATIONS COMPARE TO ROES DETERMINED BY  
20 OTHER REGULATORY AGENCIES?

21 A. As explained by Mr. Hevert, Mr. Copeland's estimated cost of equity, his recommended  
22 ROE range and his specific ROE recommendation are all far below the lowest ROE  
23 determined by any regulatory agency since at least 1980.

24

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<sup>2</sup> Hevert Rebuttal at Section II.

<sup>3</sup> Copeland Direct, p. 3.

<sup>4</sup> Copeland Direct, p. 3.

1 Q. DID THE CRITERIA HE APPLIED MEET THE REQUIREMENTS OF SOUTH  
2 DAKOTA LAW?

3 A. No.

4  
5 Q. DOES SOUTH DAKOTA LAW SET THE STANDARD FOR DETERMINING A  
6 UTILITY’S RETURN ON ITS INVESTMENT?

7 A. Yes. SDCL 49-34A-8 requires that OTP “earn a fair and reasonable return upon the  
8 value of its property.”

9  
10 Q. WHAT IS A FAIR AND REASONABLE RETURN?

11 A. The South Dakota Supreme Court has adopted the standard for a fair and reasonable  
12 return.<sup>5</sup> That standard is based on the United States Supreme Court *Bluefield*<sup>6</sup> and *Hope*<sup>7</sup>  
13 cases. The *Bluefield* and *Hope* cases require the return be set at a level that inspires  
14 “confidence in the financial soundness of the utility”<sup>8</sup> and be “commensurate with  
15 returns” earned by comparable companies.<sup>9</sup> The authorized return must also allow the  
16 utility to maintain its credit profile and attract capital.<sup>10</sup>

17  
18 Q. IS MR. COPELAND’S ANALYSIS AND RECOMMENDED ROE CONSISTENT  
19 WITH THE FAIR AND REASONABLE STANDARD?

20 A. No. Mr. Copeland’s analysis and recommendation are based on a standard that is  
21 inconsistent with the standards of South Dakota law. Mr. Copeland contends the  
22 Commission should use “the lowest reasonable estimate of the cost of equity as the  
23 allowed rate of return.”<sup>11</sup> Mr. Copeland may believe that utility commissions should take  
24 that approach, but they do not, as Mr. Copeland also readily acknowledges in Staff’s  
25 response to OTP-SD-111, which is included as Exhibit \_\_\_(BGG-2), Schedule 1.

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<sup>5</sup> Northwestern Public Service Co. v. Cities of Chamberlain, etc., 265 N.W.2d 867, 873-74 (S.D. 1978).

<sup>6</sup> Bluefield Water Works & Improvement Co. v. Public Service Comm’n, 262 U.S. 679 (1923).

<sup>7</sup> Federal Power Comm’n v. Hope Natural Gas Co., 320 U.S. 591 (1944).

<sup>8</sup> Northwestern Public Service Co., 265 N.W.2d at 873 (quoting Bluefield, 262 U.S. at 693).

<sup>9</sup> Northwestern Public Service Co., 265 N.W.2d at 873-74 (quoting Hope, 320 U.S. at 603).

<sup>10</sup> Northwestern Public Service Co., 265 N.W.2d at 873-74.

<sup>11</sup> Copeland Direct, p. 24.

1           As discussed by Mr. Hevert, Mr. Copeland’s calculated cost of equity (7.00  
2 percent) and recommended ROE (8.25 percent) are significantly lower than any ROE  
3 authorized going back to at least 1980. The large gaps between Mr. Copeland’s analysis  
4 of cost of capital and recommended ROE and the decisions of every other regulatory  
5 commission (including the Commission) do not provide for a comparable return, as  
6 required under decisions of the South Dakota Supreme Court and United States Supreme  
7 Court. Ultimately, the result of Mr. Copeland’s approach is that returns available in  
8 every other jurisdiction are significantly higher than Mr. Copeland’s recommendation.

9           Decisions by regulatory commissions are very significant to investors who track  
10 allowed ROEs. Those investors will easily recognize that higher returns are available  
11 from every other jurisdiction. Investors have no incentive to accept a ROE that is  
12 significantly below the returns available to any other utility serving in any other  
13 jurisdiction, and those investors can make an investment in a utility doing business in  
14 those jurisdictions as readily as making an investment in OTP. Finally, selecting the  
15 lowest possible ROE also does not “assure confidence in the financial soundness of the  
16 utility,” which is a requirement of South Dakota law.<sup>12</sup>

17  
18 Q. DOES THE FACT OTP HAS MORE CUSTOMERS IN MINNESOTA AND NORTH  
19 DAKOTA JUSTIFY MR. COPELAND’S APPROACH?

20 A. No. OTP is entitled to earn a fair and reasonable return on its property dedicated to  
21 serving South Dakota.<sup>13</sup> This requirement is not made less applicable by the smaller  
22 number of customers in South Dakota.<sup>14</sup> Further, as I will explain in more detail below,  
23 OTP’s investments in South Dakota are far larger than the role South Dakota plays in our  
24 integrated system, which *increases* the importance of the Commission establishing a  
25 reasonable ROE in this case.

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<sup>12</sup> Northwestern Public Service Co., 265 N.W.2d at 873 (quoting Bluefield, 262 U.S. at 693).

<sup>13</sup> SDCL 49-34A-8.

<sup>14</sup> Copeland Direct, p. 41.

1 Q. DOES MR. COPELAND ADOPT OTHER INAPPROPRIATE CRITERIA AS THE  
2 BASIS FOR HIS ANALYSIS AND RECOMMENDATION?

3 A. Yes. Mr. Copeland also contends that the Commission should set the ROE at a level that  
4 would “redress past wrongs” and reflect “a ‘refund’ of the excess returns.”<sup>15</sup> These are  
5 standards of retribution that have no basis in South Dakota law and no relationship to a  
6 “fair and reasonable return.” Adopting these standards, or an analysis and  
7 recommendation that are based on these standards, would make South Dakota an outlier  
8 from virtually every other jurisdiction and obviously not lead to a return comparable to  
9 returns available from other utilities providing service in any other jurisdiction. Investors  
10 are under no obligation to accept inadequate returns and will simply invest elsewhere.

11

12 Q. DOES MR. COPELAND’S RECOMMENDATION TO REDRESS PAST WRONGS  
13 AND REFUNDS FIT OTP’S FACTS?

14 A. No. Mr. Copeland’s recommendation is contrary to actual facts relating to OTP. OTP  
15 has consistently *not* achieved its authorized return in South Dakota, as shown in Table 1  
16 below. This includes years immediately following a rate case, which reflects the  
17 regulatory lag inherent in South Dakota ratemaking due to the use of historical test years  
18 and the delay in implementation of interim rates.

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<sup>15</sup> Copeland Direct, p. 41.



1  
2

Table 1  
Summary of Actual Overall Returns

<u>Year</u>	<u>Authorized Return*</u>	<u>Actual Return</u>	<u>Excess / (Shortfall)</u>
2011	8.29%	6.79%	(1.50%)
2012	7.91%	7.82%	(0.09%)
2013	7.76%	7.03%	(0.73%)
2014**	7.67%	8.23%	0.56%
2015**	7.88%	7.49%	(0.39%)
2016	7.83%	6.67%	(1.16%)
2017	7.74%	5.74%	(2.00%)

Notes

\* Filed annually with TCRR compliance filings; reflects annual updates to equity ratio and debt costs and use of 9.25 percent ROE in Environmental Cost Recovery Rider (ECRR) and Transmission Cost Recovery Rider (TCRR).

\*\* Results exclude effects of CWIP, consistent with South Dakota law but include revenues on CWIP due to revenues from the ECRR and TCRR. When CWIP effects are included, OTP would not have achieved its authorized returns.

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Clearly, OTP has not had any “excess returns” that need to be refunded, but Mr. Copeland’s analysis is based on the premise that there were.

Q. DOES SOUTH DAKOTA LAW SUPPORT A STANDARD TO SELECT THE LOWEST POSSIBLE ROE AND OR AN ROE TO REDRESS PAST WRONGS OR REFUND EXCESS RETURNS?

A. No. South Dakota law requires the Commission to establish a fair and reasonable return, which requires balancing and consideration of both customer and investor interests. Mr. Copeland presents an argument as to what he thinks the law should require. But that decision has been made by the legislature, and Mr. Copeland’s approach does not meet the standard the legislature has chosen.

Q. HOW DOES MR. COPELAND’S RECOMMENDATION COMPARE TO THE ROES OF OTHER UTILITIES IN SOUTH DAKOTA?

A. As shown in Exhibit\_\_\_(BGG-2), Schedule 2, Staff has declined to provide information regarding other utilities authorized ROEs. Based on publicly-available information, OTP estimates that the authorized ROEs for other electric utilities in South Dakota are at least

1 9.25 percent.<sup>16</sup> Given all factors, there is no justification for OTP to have an authorized  
2 ROE that is lower than other South Dakota utilities, much less 100 basis points lower.  
3

4 Q. WHAT ARE THOSE FACTORS?

5 A. As I will explain below, OTP has provided consistently high-quality service, with  
6 demonstrated cost savings, consistently low rates, high customer satisfaction and very  
7 infrequent rate cases (our last case being in 2010). OTP has also made, and is continuing  
8 to make, extensive investments in South Dakota. These factors demonstrate that OTP is a  
9 very high-performing utility, all of which justifies a ROE that is higher than the ROEs for  
10 other South Dakota utilities.  
11

12 Q. WOULD MR. COPELAND'S ANALYSIS AND RECOMMENDATION MEET THE  
13 APPROPRIATE STANDARDS FOR DETERMINING AN ROE IF MR. COPELAND  
14 ALWAYS USED THE SAME METHOD OF ANALYSIS?

15 A. No. Use of a mechanically rigid approach does not equate with reasonableness nor does  
16 it meet the standards for determining the ROE under applicable law. South Dakota  
17 statutes require a return that is "fair and reasonable." Under both South Dakota Supreme  
18 Court and United States Supreme Court decisions, the question of whether that standard  
19 has been met is based on whether the result is reasonable, not the method used to reach  
20 the result.

21 The United States Supreme Court has explained that: "Under the statutory  
22 standard of 'just and reasonable,' it is the result reached not the method employed which  
23 is controlling."<sup>17</sup> The South Dakota Supreme Court has also focused on the importance  
24 of results, not methods used in assessing reasonableness:

25 [T]he Public Utilities Commission need not follow any single formula in  
26 arriving at the rates fixed so long as the method followed and the order  
27 entered when applied to the facts and viewed as a whole do not produce  
28 and unjust or arbitrary result.<sup>18</sup>

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<sup>16</sup> These ROEs were established as part of settlements and Staff has declined to provide information as to how those settled amounts were reached or the actual ROEs. Our calculations, therefore, are the best information available.

<sup>17</sup> Hope, 320 U.S. at 602.

<sup>18</sup> Northwestern Public Service Co., 265 N.W.2d at 872.

1 Here, Mr. Copeland's analysis and recommendations in this case are extreme outliers,  
2 completely unlike any ROE determination by any other regulatory commission since at  
3 least 1980 and produce an unjust and arbitrary result. When the requirement is that the  
4 return be comparable to the return available from investing in similar utilities, mechanical  
5 consistency does not save a result that so obviously fails to meet the standard of  
6 comparability.

7  
8 Q. DOES THE FACT THAT MR. COPELAND PURPORTS TO FOLLOW THE SAME  
9 METHODOLOGY USED IN DOCKET NO. EL11-019 SATISFY THE SOUTH  
10 DAKOTA LEGAL STANDARD?

11 A. No. As noted above, results are more important than methodology. Even if Mr.  
12 Copeland has followed the methodology used in Docket No. EL11-019, his results and  
13 recommendations are neither fair nor reasonable and therefore violate South Dakota legal  
14 requirements.

15 **III. OTHER FACTORS THE COMMISSION SHOULD CONSIDER**

16 Q. PLEASE SUMMARIZE OTP'S CONCERNS WITH MR. COPELAND'S ANALYSIS  
17 AND RECOMMENDATIONS.

18 A. As explained in the Rebuttal Testimonies of Mr. Moug and Mr. Hevert, Mr. Copeland's  
19 7.00 percent estimated cost of equity, his recommended ROE range of 8.00 percent to  
20 8.50 percent, and his recommended 8.25 percent ROE are all far below: (1) the  
21 Commission-approved 9.25 percent ROE for other vertically integrated electric utilities  
22 in South Dakota; (2) the lowest ROEs authorized since 1980; and (3) the average 2018  
23 ROE for vertically integrated electric utilities of 9.68 percent. OTP is also concerned  
24 about the overall signal an unreasonable ROE would send when OTP is performing so  
25 exceptionally and has made such substantial commitments to make enormous  
26 investments in infrastructure in South Dakota.

1 Q. ARE THERE FACTORS OTHER THAN COST DATA THAT THE COMMISSION  
2 SHOULD CONSIDER WHEN SETTING THE ROE FOR OTP?

3 A. Yes. As I will explain, there are a number of other factors the Commission should  
4 consider. These include: (1) demonstrated substantial cost savings OTP has achieved for  
5 South Dakota customers; (2) OTP's combination of consistently very high quality service  
6 and very low rates; (3) the long period of time since our last rate case; (4) our  
7 commitment to not file another rate case for four years; and (5) our extremely large  
8 investments in South Dakota, notwithstanding the fact that South Dakota represents less  
9 than 10 percent of our retail customers.

10 Ultimately, OTP's performance and commitment to South Dakota merits a ROE  
11 that is *above* average and above ROEs approved for other utilities, not the "lowest  
12 reasonable estimate of the cost of equity as the allowed rate of return."<sup>19</sup> It certainly does  
13 not merit taking retribution against OTP.<sup>20</sup>

14

15 Q. DID MR. COPELAND CONSIDER OTP'S VERY HIGH LEVELS OF CUSTOMER  
16 SATISFACTION IN HIS ROE RECOMMENDATION?

17 A. No. Mr. Copeland did not consider the fact OTP's customers are highly satisfied with  
18 OTP's service. I explained OTP's performance, as reflected in the American Customer  
19 Satisfaction Index, transaction surveys and J.D. Power's study of electric utility  
20 residential customer satisfaction, in my Direct Testimony.<sup>21</sup> Customer satisfaction is a  
21 critical element of our mission and I am proud of how my coworkers have succeeded in  
22 meeting and often exceeding our customers' expectations.

23

24 Q. DID MR. COPELAND CONSIDER HOW OTP'S RATES COMPARE TO OTHER  
25 UTILITIES IN HIS ROE RECOMMENDATION?

26 A. No. Mr. Copeland also did not consider the facts related to OTP's overall average rates.  
27 As I explained in my Direct Testimony, OTP's overall average rates are substantially

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<sup>19</sup> Copeland Direct, p. 24.

<sup>20</sup> Copeland Direct, p. 41.

<sup>21</sup> Gerhardson Direct, p. 16-19.

1 lower than regional and national averages and consistently the second-lowest of any  
2 electric utility in South Dakota, despite the challenges OTP faces as a very small utility  
3 serving customers in a very large, sparsely populated service territory.<sup>22</sup> Mr. Copeland  
4 also did not acknowledge the fact Otter Tail Corporation (OTP's parent company) was  
5 recognized as the 4<sup>th</sup> lowest price provider among all utility parent companies  
6 nationwide, with a blended rate for all customers of 8.16 cents/kWh.<sup>23</sup> OTP has achieved  
7 very high-quality service at very low rates despite being a very small investor-owned  
8 utility serving an expansive rural service area.

9  
10 Q. DID MR. COPELAND CONSIDER THE SIGNIFICANT CUSTOMER SAVINGS OTP  
11 HAS DELIVERED ON RECENT CAPITAL PROJECTS?

12 A. No. Mr. Copeland's analysis and recommendation do not reflect the significant savings  
13 for South Dakota customers resulting from OTP's under-budget completion of the Big  
14 Stone Air Quality Control System (AQCS) Project. As I explained in my Direct  
15 Testimony, OTP's performance reduced 2017 Test Year revenue deficiency by  
16 approximately \$0.9 million (OTP SD) and customers will see a total of \$17.2 million  
17 (OTP SD) in savings over the life of the project, with a net present value of \$7.8 million  
18 (OTP SD).<sup>24</sup> Mr. Copeland also did not recognize that the under-budget completion of  
19 the Big Stone AQCS reduced return to shareholders by \$0.3 million (OTP SD) in the  
20 2017 Test Year, by \$5.4 million (OTP SD) over the life of the project, with a net present  
21 value of \$2.7 million (OTP SD).<sup>25</sup>

22  
23 Q. HAS OTP ACHIEVED SAVINGS ON OTHER LARGE CAPITAL PROJECTS?

24 A. Yes. OTP has now completed its two largest transmission projects, the Big Stone Area  
25 Transmission-Brookings Project (BSAT-Brookings) and Big Stone Area Transmission-  
26 Ellendale (BSAT-Ellendale). Both projects are located in South Dakota (with a portion  
27 of BSAT-Ellendale being located in North Dakota). Collectively, OTP's budgeted

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<sup>22</sup> Gerhardson Direct, p. 14-16.

<sup>23</sup> Gerhardson Direct, p. 16.

<sup>24</sup> Tommerdahl Direct, p. 5-6.

<sup>25</sup> Tommerdahl Direct, p. 6.

1 investment in BSAT-Brookings and BSAT-Ellendale was \$317 million (OTP Total). The  
2 projects were completed at a cost of \$187 million (OTP Total), or over 40 percent under  
3 budget. These under-budget projects will save money for all customers taking service  
4 from all utilities in the MISO region, and it will do so for the entire duration of these  
5 long-lived projects. This is another example of OTP being an excellent performer that  
6 works diligently to deliver electricity as economically possible.

7  
8 Q. DID MR. COPELAND CONSIDER THE FREQUENCY OF OTP RATE CASES IN  
9 SOUTH DAKOTA?

10 A. No. OTP has filed fewer rate cases than the other South Dakota utilities. OTP's last rate  
11 case was filed eight years before the current case. OTP filed its last South Dakota rate  
12 case on August 20, 2010 in Docket No. EL10-011. Since that time:

- 13 • Xcel Energy has filed *three* rate cases (Docket Nos. EL11-019, EL12-046,  
14 and EL14-058);
- 15 • Black Hills Power has filed *two* rate cases (Docket Nos. EL12-061 and  
16 EL14-026);
- 17 • MidAmerican has filed *two* rate cases (Docket Nos. EL14-072 and NG14-  
18 005)
- 19 • NorthWestern has filed *two* rate cases (Docket Nos. EL14-106 and NG11-  
20 003)
- 21 • Montana-Dakota Utilities (MDU) has filed *three* rate cases (Docket Nos.  
22 EL15-024, NG15-005 and NG12-008).

23 Our infrequent rate case filings speak to our control of costs on behalf of our customers.  
24

25 Q. DID MR. COPELAND CONSIDER THE SCALE OF OTP'S RECENT  
26 INVESTMENTS IN SOUTH DAKOTA?

27 A. No. Mr. Copeland did not consider either the investments made by OTP or the benefits  
28 to South Dakota that result from those investments.

29

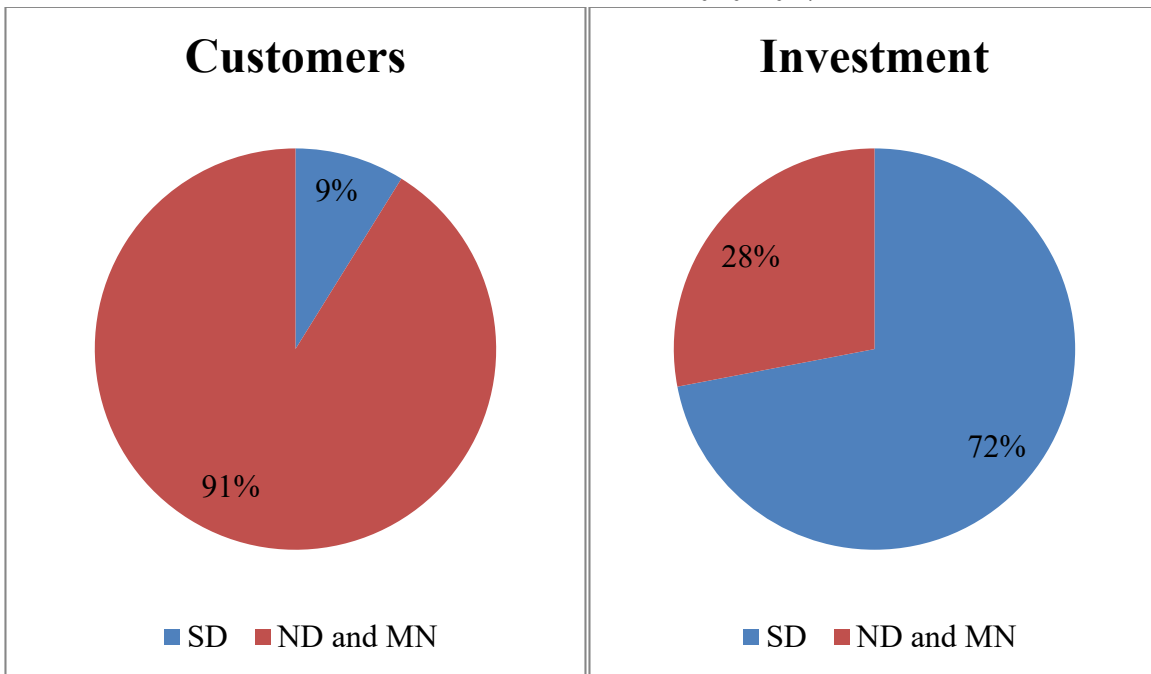
1 Q. PLEASE BRIEFLY DESCRIBE THOSE INVESTMENTS.

2 A. Since OTP's last South Dakota rate case (2009 Test Year), net plant in service has  
3 increased 46 percent or \$376 million (OTP Total). The vast majority (72 percent) of this  
4 growth is attributable to two South Dakota projects: the Big Stone AQCS Project (\$197  
5 million (OTP Total)) and BSAT-Brookings (\$72 million (OTP Total)).  
6

7 Q. HOW DOES OTP'S PROPORTION OF INVESTMENT IN SOUTH DAKOTA  
8 COMPARE TO OTP'S PROPORTION OF CUSTOMERS IN THE STATE?

9 A. OTP's investment in South Dakota far exceeds its proportion of customers in the state.  
10 The charts below compare OTP's system-wide customer counts and the proportion of our  
11 recent and near-term investments in our three states. The share of our investments in  
12 South Dakota has surpassed the state's share of our retail customers by about 800  
13 percent.

14 Figure 1  
15 Comparison of Customer Counts and Investment  
16 Investment Period 2010-2017



17

1 Q. ARE THERE ECONOMIC BENEFITS TO SOUTH DAKOTA FROM THESE  
2 INVESTMENTS THAT ARE BEYOND THE DELIVERY OF ELECTRIC SERVICE?

3 A. Yes. Every governor in the country is trying to attract large beneficial infrastructure  
4 projects to their state. These large projects bring significant employment and other  
5 economic benefits to the state. Further, the South Dakota legislature has recognized that  
6 “energy development in South Dakota and the Northern Great Plains significantly affects  
7 the welfare of the population, the environmental quality, the location and growth of  
8 industry, and the use of the natural resources of the state.”<sup>26</sup>

9 During peak construction of the Big Stone AQCS project, approximately 500  
10 people were working on site; during the tie-in outages, it increased to 650 people working  
11 on site.<sup>27</sup> Overall, there were over 2.3 million work-hours spent on the project.

12

13 Q. DOES SOUTH DAKOTA RECOGNIZE THE IMPORTANCE OF THESE KINDS OF  
14 INVESTMENTS TO SOUTH DAKOTA?

15 A. Yes. The Governor’s Office of Economic Development (GOED) specifically works to  
16 retain and expand existing business and expand and diversify the state’s industry and  
17 economy.<sup>28</sup>

18

19 Q. DOES OTP PLAN TO MAKE ADDITIONAL SUBSTANTIAL INVESTMENTS IN  
20 SOUTH DAKOTA?

21 A. Yes. Approximately half, or \$430 million (OTP Total), of our forecasted capital  
22 spending in the 2018-2021 period is for three South Dakota Projects: BSAT-Ellendale;  
23 Lake Norden Area Transmission Project and the Astoria Generating Station.  
24 Additionally, there are routine projects to upgrade the distribution and local transmission  
25 systems that are not quantified for this amount. When combined with our investments in  
26 the Big Stone AQCS and BSAT-Brookings, OTP will have invested over \$600 million

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<sup>26</sup> SDCL 49-41B-1.

<sup>27</sup> Phinney Direct, p. 11.

<sup>28</sup> <http://www.sdreadytowork.com/GOEDMission.aspx>.



1 (OTP Total) in South Dakota in a 7-year period. The total cost of the projects (reflecting  
2 partners' shares) is over \$1,000,000,000 (one billion).

3  
4 Q. ARE SOUTH DAKOTA CUSTOMERS RESPONSIBLE FOR PAYING FOR ALL OF  
5 THIS INVESTMENT ON THEIR OWN?

6 A. No. We operate an integrated system and the costs are shared by all jurisdictions.  
7 Further, BSAT-Brookings and BSAT-Ellendale are wholesale transmission projects:  
8 those costs are recovered from utilities (and their customers) throughout MISO.  
9 Ultimately, OTP's South Dakota customers will only pay for roughly five percent of the  
10 amount invested in South Dakota.

11  
12 Q. WHAT IS THE SIGNIFICANCE OF THESE INVESTMENTS AND BENEFITS?

13 A. OTP believes that these investments and benefits should be given some consideration in  
14 the context of all of the other factors that we have demonstrated, including exemplary  
15 service, cost savings, low rates, and infrequent rate cases. Data provided by expert  
16 witnesses is an important factor, but it is by no means the only factor to be considered in  
17 setting a ROE. The Commission has the authority and the responsibility to consider all of  
18 these factors and to not simply engage in a mechanical exercise or simply accept the  
19 results of a mechanical exercise when setting the ROE for a South Dakota utility.

20  
21 Q. WILL ADOPTING MR. COPELAND'S RECOMMENDATION SEND THE WRONG  
22 SIGNALS TO UTILITIES?

23 A. Yes. The Commission has a role in signaling the behaviors that it desires from its  
24 utilities. For example, if the Commission wants utilities to make the kinds of beneficial  
25 investments we have made in our system, and make them in South Dakota, it should not  
26 adopt the hostility clearly present in Mr. Copeland's approach and recommendation. If  
27 Mr. Copeland's recommendation was adopted in this case, the lowest returns OTP would  
28 be authorized for its investments in South Dakota would be from the state in which the  
29 vast majority of those investments are located. Worse yet, the returns would be the  
30 lowest authorized returns in the country, and well below industry averages. I do not

1 know how I could explain such an occurrence other than as a signal that the Commission  
2 is not supportive of the investments. Further, adopting Mr. Copeland's recommendation  
3 would send a signal that the Commission does not value the superior results OTP has  
4 consistently delivered for customers. Ultimately, it would not be in the public interest to  
5 arrive at a low ROE in this case, such as that recommended by Mr. Copeland. Instead, for  
6 all the reasons identified in this testimony, the Commission should grant a ROE  
7 consistent with OTP's request.

#### 8 **IV. CONCLUSION**

9 Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY.

10 A. Mr. Copeland's estimated cost of equity, his recommended ROE range and his specific  
11 ROE recommendation are inconsistent with South Dakota law. They are also incredibly  
12 inappropriate given OTP's demonstrated substantial cost savings for South Dakota  
13 customers, consistently very high-quality service and very low rates, the long period of  
14 time since our last rate case, our commitment to not file another rate case for four years  
15 and our extremely large investments in South Dakota.

16  
17 Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

18 A. Yes.