

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. EL25-

Exhibit____

**FINANCIAL SOUNDNESS, CAPITAL STRUCTURE
AND COST OF CAPITAL**

Direct Testimony and Schedules of

TODD R. WAHLUND

June 4, 2025

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ATTACHED SCHEDULES

Schedule 1	Qualification and Responsibilities of Todd R. Wahlund
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I. INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND CURRENT EMPLOYER.

A. My Name is Todd R. Wahlund. I currently am employed by Otter Tail Corporation. Otter Tail Power Company (“OTP” or the “Company”) is a wholly owned subsidiary of Otter Tail Corporation.

Q. PLEASE SUMMARIZE YOUR CURRENT RESPONSIBILITIES.

A. I am the Chief Financial Officer and Vice President of Finance for Otter Tail Corporation. I am responsible for the financial functions and performance for Otter Tail Corporation and its operating company subsidiaries, including OTP. I also direct the corporate services for treasury, accounting, tax, external reporting, investor relations, financial planning, information technology, internal audit, business risk management, and acquisition evaluations.

Q. HAVE YOU INCLUDED AN ATTACHMENT OF YOUR QUALIFICATIONS AND EXPERIENCE?

A. Yes. A summary of my qualifications and experience is included as Exhibit____(TRW-1), Schedule 1.

II. PURPOSE AND OVERVIEW OF DIRECT TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

A. The purpose of my Direct Testimony is to support OTP’s capital structure and overall rate of return (ROR). In connection therewith, I discuss several issues that are related to OTP’s proposed capital structure and ROR, including the Company’s prior and planned capital expenditures, credit ratings and unique financial characteristics. Finally, I sponsor the information provided in Volume 4A, Section D, Rate of Return/Cost of Capital Schedules D-1 through D-3.

Q. PLEASE PROVIDE A BRIEF OVERVIEW OF YOUR DIRECT TESTIMONY.

A. My Direct Testimony:

- Demonstrates the reasonableness of OTP’s 2024 Test Year capital structure, cost of long-term debt (LTD) and the overall ROR;
- Discusses the financial impacts and scope of OTP’s recent capital expenditures and its estimated future capital expenditures;

- Discusses how constructive regulatory policy, including OTP's regulatory capital structure and a reasonable return on equity (ROE), is important for OTP to maintain its senior unsecured credit ratings, support OTP's capital expenditures, and enable OTP to attract capital and provide service at a fair and reasonable cost;
- Explains the unique financial characteristics of OTP and how they affect the cost of equity for OTP; and
- Presents OTP's 2024 Test Year capital structure and overall ROR.

Q. PLEASE PROVIDE A BRIEF SUMMARY OF YOUR DIRECT TESTIMONY.

A. OTP's 2024 Test Year capital structure, costs of LTD and common equity, and ROR are reasonable and should be adopted for determining OTP's rates. Table 1, below, summarizes percentages and costs of LTD and common equity. These amounts also are shown in Exhibit____(TRW-1), Schedule 2.

Table 1
2024 Test Year Capital Structure and ROR

Component	Percentage	Cost	Weighted Cost
Long-Term Debt	46.46%	5.39%	2.50%
Common Equity	53.54%	10.80%	5.78%
Rate of Return	100.00%		8.29%

OTP has been engaged in an extensive customer-focused investment program, involving capital expenditures of approximately \$1.461 billion from 2018 through 2024, or an average of approximately \$209 million per year.¹ These investments are projected to continue, with OTP's capital expenditures projected to be approximately \$1.426 billion in 2025-2029 (an average of approximately \$285 million per year).² The Commission's decisions in this proceeding, including the Commission's decisions regarding OTP's capital structure and ROE, could significantly affect the costs of financing these expenditures and the costs to customers.

¹ See Table 2, below.

² Otter Tail Corporation 2024 10-K at 40.

- 1 Q. WHAT DO YOU RECOMMEND TO THE COMMISSION?
- 2 A. I recommend the Commission approve a capital structure for the 2024 Test Year
- 3 consisting of 53.54 percent equity and 46.46 percent LTD. I also recommend the
- 4 Commission approve an overall ROR of 8.29 percent and a ROE of 10.80 percent.
- 5
- 6 Q. HOW IS THE BALANCE OF YOUR DIRECT TESTIMONY ORGANIZED?
- 7 A. The balance of my Direct Testimony is organized as follows:
- 8 • Section III describes our historic and planned financing and investment
- 9 activities.
- 10 • Section IV discusses OTP's credit ratings.
- 11 • Section V discusses some of OTP's unique financial characteristics.
- 12 • Section VI describes OTP's proposed capital structure, including its
- 13 components, costs of capital and overall ROR.
- 14 • Section VII summarizes my conclusions.

15 **III. OTP CAPITAL EXPENDITURES**

- 16 Q. PLEASE SUMMARIZE OTP'S CAPITAL EXPENDITURES SINCE ITS LAST
- 17 SOUTH DAKOTA RATE CASE.
- 18 A. OTP's last South Dakota rate case (Docket No. EL 18-021) was filed on
- 19 April 20, 2018 based on a 2017 Test Year. Since 2017, OTP's capital expenditures
- 20 have totaled approximately \$1.461 billion, as shown on Table 2 below.

21 **Table 2**

22 **OTP Capital Expenditures 2018-2024³**

23

Year	OTP Capital Expenditures (\$ millions, OTP Total)
2018	\$87
2019	\$187
2020	\$357
2021	\$140
2022	\$148
2023	\$241
2024	\$301
Total	\$1,461
Average	\$209

³ Otter Tail Corporation 2018 Form 10-K at 51; Otter Tail Corporation 2020 Form 10-K at 30; Otter Tail Corporation 2022 Form 10-K at 34; Otter Tail Corporation 2024 Form 10-K at 40.

1 Q. HOW DO THESE PRIOR EXPENDITURES COMPARE TO OTP'S NET PLANT IN
2 SERVICE?

3 A. OTP's net electric plant in service was approximately \$1.451 billion as of
4 December 31, 2017.⁴ OTP's \$1.461 billion capital expenditures during 2018-2024
5 represent approximately 101 percent of its net electric plant at the beginning of
6 that period. The result, after plant retirements, was a net increase in OTP's net
7 electric plant in service of approximately \$1.063 billion, to approximately \$2.514
8 billion as of December 31, 2024.⁵ OTP witness Mr. Matthew J. Olsen also provides
9 further information regarding these expenditures.
10

11 Q. PLEASE SUMMARIZE OTP'S ANTICIPATED CAPITAL EXPENDITURES.

12 A. We anticipate an additional \$1.426 billion of capital expenditures in 2025-2029
13 (an average of approximately \$285 million per year).⁶ Mr. Olsen further explains
14 OTP's capital expenditure plans in his direct testimony.
15

16 Q. HOW HAS OTP FINANCED ITS RECENT CAPITAL EXPENDITURES?

17 A. OTP has obtained long term funding for its \$1.461 billion of capital expenditures
18 during 2018-2024 through a combination of approximately \$625 million of LTD
19 issued by OTP (including approximately \$170 million for replacement of matured
20 notes), \$148.7 million of earnings retained by OTP and \$355.0 million of equity
21 infusions from Otter Tail Corporation. The sum of those retained earnings plus
22 equity infusions reflects the net level of reinvestment of OTP earnings.
23

24 Q. HAVE YOU SUMMARIZED THOSE RETAINED EARNINGS AND EQUITY
25 INFUSIONS?

26 A. Yes. Table 3 below identifies the net reinvestment in OTP (the sum of OTP retained
27 earnings plus Otter Tail Corporation equity infusions) for the years 2018-2024.
28 During that time, practically all of OTP's net income has been reinvested in utility
29 operations, either as retained earnings or added infusions of equity from Otter Tail
30 Corporation.
31

⁴ Otter Tail Corporation 2017 Form 10-K/A at 109.

⁵ Otter Tail Corporation 2024 Form 10-K at 66.

⁶ Otter Tail Corporation 2024 10-K at 40.

Table 3
Net Reinvestment of OTP Earnings
(\$ millions)

	OTP Net Income	Retained Earnings	Otter Tail Corp Equity Infusions	Net Reinvestment [Retained Earnings + Otter Tail Corp Equity Infusions]	Effective Rate of Reinvestment
2018	\$54.4	\$11.9	\$25.0	\$36.9	67.8%
2019	\$59.0	\$14.5	\$35.0	\$49.5	83.9%
2020	\$66.8	\$22.3	\$150.0	\$172.3	257.9%
2021	\$72.5	\$20.6	\$0.0	\$20.6	28.4%
2022	\$80.0	\$25.0	\$50.0	\$75.0	93.8%
2023	\$84.4	\$26.0	\$40.0	\$66.0	78.2%
2024	\$91.0	\$28.4	\$55.0	\$83.4	91.6%
Total	\$508.1	\$148.7	\$355.0	\$503.7	99.1%
Average	\$72.0	\$21.2	\$50.7	\$72.0	100.0%

These retained earnings and equity infusions have provided essential funding and have allowed OTP to maintain an appropriate balance of debt and equity and a balanced capital structure for OTP.

Q. HAS THE IMPORTANCE OF OTP'S BALANCED CAPITAL STRUCTURE AND OTTER TAIL CORPORATION EQUITY INFUSIONS BEEN RECOGNIZED BY RATING AGENCIES?

A. Yes. Fitch Ratings (Fitch) has stated:

Fitch expects OTP to remain FCF [Free Cash Flow] negative through the forecast, with future funding needs met by a balanced mix of debt and equity, and parent OTTR will downstream additional equity as needed to support the balanced capital structure.⁷

Fitch's credit rating for OTP also assumes that its "large capex program" will be supported by a "balanced capital structure."⁸

Q. DID FITCH IDENTIFY ANY RISKS ASSOCIATED WITH FAILURE TO MAINTAIN A BALANCED CAPITAL STRUCTURE?

A. Yes. Fitch identified the following factors that could, individually or collectively, lead to negative rating action or downgrade:

- Adverse future regulatory outcomes.

⁷ Fitch Ratings, Otter Tail Corporation; Otter Tail Power Company at 3 (Sept. 12, 2024).

⁸ Fitch Ratings, Otter Tail Corporation; Otter Tail Power Company at 7 (Sept. 12, 2024).

- Failure to maintain a balanced equity component in its capital structure.
- Sustained FFO leverage above 4.5x.⁹

Q. WILL THE ROE AND CAPITAL STRUCTURE APPROVED BY THE COMMISSION IMPACT OTP'S CAPITAL EXPENDITURES AND COST?

A. Yes. The ROE and capital structure authorized in this proceeding will have a substantial impact on OTP's ability to carry out its capital expenditures and the ongoing cost of doing so in three important ways.

First, the ROE and capital structure will have a direct impact on OTP's level of authorized earnings, which will, in turn, directly affect its ability to fund capital expenditures with internally generated retained earnings. As shown above, internally generated retained earnings have been a significant source of funding for OTP's capital expenditures, and the Company expects retained earnings to continue to be a significant source of funding for its future capital expenditure plans.

Second, the authorized ROE and capital structure will have a significant effect on rating agencies' and investors' perceptions of OTP, the effect of which is likely to be heightened by the scale of the Company's planned capital expenditures. These perceptions will have a substantial impact on both the availability and the cost of the capital needed to complete OTP's capital expenditure plans.

Finally, ROE and capital structure both impact cash from operations relative to total debt, which is a key financial metric that ultimately influences the cost of debt capital and therefore customers' rates.

IV. OTP CREDIT RATINGS

Q. ARE CREDIT RATINGS IMPORTANT TO OTP AND ITS CUSTOMERS?

A. Yes. Credit ratings are very important to OTP and its customers. That is because investors in the debt placements use credit ratings, along with their own analysis, to decide whether to purchase OTP debt and at what price, which in turn, drives the interest rate on that debt. Credit ratings therefore impact the cost of debt OTP incurs to fund its substantial capital expenditures.

⁹ Fitch Ratings, Otter Tail Corporation; Otter Tail Power Company at 4 (Sept. 12, 2024). "FFO" stands for Funds from Operations.

1 Q. WHAT ARE OTP'S CURRENT CREDIT RATINGS?

2 A. OTP's current senior unsecured credit ratings are set out in Table 4 below:

3
4 **Table 4**
5 **OTP Credit Ratings¹⁰**

	Moody's	Fitch	S&P
Corporate Credit / Long-Term Issuer Default Rating	A3	BBB+	BBB+
Senior Unsecured Debt	N/A	A-	N/A
Outlook	Negative	Stable	Stable

6
7 Q. WHAT FACTORS DO AGENCIES CONSIDER WHEN ESTABLISHING CREDIT
8 RATINGS FOR A UTILITY?

9 A. Credit rating agencies look at a utility's business risk and its financial risk (based
10 on credit metrics that typically measure the relationship between cash flow and
11 debt and ultimately project whether the utility will be able to satisfy its debt
12 obligations) in making rating determinations. To maintain a given credit rating,
13 the credit metrics a utility must meet increase (become more stringent) as the
14 utility's business risk rating decreases (indicating higher business risk). Capital
15 expenditure levels are significant to rating agencies' evaluation of a utility's credit
16 ratings.

17
18 Q. HAS OTP'S CAPITAL EXPENDITURE LEVEL BEEN RECOGNIZED AS A
19 CREDIT RATING FACTOR?

20 A. Yes. Fitch and Moody's identify OTP's planned capital expenditures as factors
21 influencing their credit ratings, with Fitch noting those capital expenditures need
22 to be supported by a balanced capital structure.¹¹

23
24 Q. HOW HAVE THE CREDIT RATINGS AGENCIES VIEWED OTP'S HEIGHTENED
25 CAPITAL EXPENDITURE LEVEL?

26 A. Both Moody's and S&P have recognized that there will be a tightening of metrics
27 during a period of heightened capital expenditure levels. Moody's revised the
28 rating outlook of OTP to negative from stable based on an expectation that the

¹⁰ Otter Tail Corporation 2024 Form 10-K at 42.

¹¹ Fitch Ratings, Otter Tail Corporation; Otter Tail Power Company at 2-4 (Sept. 12, 2024); Moody's Ratings, Otter Tail Power Company: Update Following Negative Outlook at 1 (Aug. 1, 2024).

1 Company's financial profile will be pressured by a combination of higher capital
2 expenditure and incremental leverage that will outpace cash flow growth.¹²

3 S&P has maintained a stable outlook for OTP based on a forecast that its
4 adjusted stand-alone funds from operations (FFO) to debt ratio will range from
5 about 16 to 19 percent. S&P, however, also notes that it could lower the rating if
6 OTP's financial measures weaken to an FFO to total debt ratio that is consistently
7 below 15 percent,¹³ meaning there is little room in OTP's financial metrics before
8 possible downgrade. Therefore, it is important to continue supporting OTP's
9 financial integrity during this heightened period of capital expenditure.

10
11 Q. DOES OTP'S AUTHORIZED CAPITAL STRUCTURE AFFECT FINANCIAL RISK?

12 A. Yes. Financial risk is measured through credit metrics. Those metrics generally
13 assess the utility's liabilities and its ability to satisfy those liabilities. The
14 authorized capital structure affects both aspects of the financial risk equation.

15 Ratings agencies predicate OTP's ratings and outlook on the assumption
16 that the Company will finance its future capital expenditures through a balanced
17 capital structure. For example, Fitch has stated that it expects "future funding
18 needs [to be] met by a balanced mix of debt and equity" and that OTP will maintain
19 a "balanced capital structure."¹⁴ Moving away from financing future capital
20 expenditures through a balance of debt and equity would put additional pressure
21 on credit metrics, both by reducing the amount of internally generated earnings
22 available to fund capital expenditures, and by increasing OTP's debt burden.

23
24 Q. IS THE 2024 TEST YEAR CAPITAL STRUCTURE ALIGNED WITH THE RATING
25 AGENCIES' EXPECTATIONS REGARDING THE FINANCING OF OTP'S
26 CAPITAL EXPENDITURES?

27 A. Yes. As discussed in more detail below, the 2024 Test Year capital structure
28 reflects OTP's actual 2024 capital structure, which was implemented consistent
29 with balanced funding between debt and equity. Deviation from this actual capital
30 structure would put pressure on credit metrics, and also could be perceived as an
31 unsupportive regulatory outcome and therefore affect business risk.

32

¹² Moody's Ratings, Otter Tail Power Company: Update Following Negative Outlook at 2 (Aug. 1, 2024).

¹³ S&P Global Ratings, Tear Sheet: Otter Tail Power Co. at 2 (Sept. 23, 2024).

¹⁴ Fitch Ratings, Otter Tail Corporation; Otter Tail Power Company at 3 (Sept. 12, 2024).

1 Q. IS THIS A PARTICULARLY POOR TIME TO INCREASE PRESSURE ON CREDIT
2 METRICS?

3 A. Yes. I explained above that Moody's revised its outlook for OTP to negative,
4 reflecting an expectation that the Company's cash flow from operations before
5 changes in working capital (CFO pre-WC) to debt ratio will be weaker in the future.
6 Placing additional pressure on credit metrics (through, for example, use of a
7 hypothetical capital structure) could cause credit metrics to deteriorate to the point
8 where Moody's would actually downgrade OTP's credit rating, as opposed to just
9 maintaining or revising its outlook. Also, as noted above, there is very little
10 downside room in S&P's metrics before crossing the threshold for potential
11 downgrade. A downgrade, in turn, very likely would increase the cost of future
12 debt issuances, ultimately increasing the cost of service to customers.
13

14 Q. CAN YOU QUANTIFY THE COST OF A CREDIT DOWNGRADE?

15 A. Yes. Generally, a one notch change to OTP's Moody's credit rating would be
16 expected to increase the cost of long-term debt by anywhere between 12.5 and 40
17 basis points. With \$515 million of projected long-term debt issuances over the
18 2026-2029 period, a downgrade would likely increase annual interest expense in a
19 range of approximately \$0.6 million to \$2.1 million (OTP Total), or \$19.3 million
20 to \$61.8 million (OTP Total) over the lifetime of a 30-year issuance.

21 **V. OTP TEST YEAR CAPITAL STRUCTURE AND RATE OF**
22 **RETURN**

23 Q. PLEASE SUMMARIZE OTP'S RECOMMENDED CAPITAL STRUCTURE, COSTS
24 OF DEBT, AND ROR FOR THE 2024 TEST YEAR.

25 A. OTP recommends an overall ROR of 8.29 percent, which is based on the
26 percentages and costs of LTD and common equity summarized in Table 5 below
27 (which is a duplicate of Table 1 and provided here for convenience) and shown on
28 attached Exhibit____(TRW-1), Schedule 2.
29
30
31

Table 5
Recommended 2024 Test Year Capital Structure and ROR

Component	Percentage	Cost	Weighted Cost
Long-Term Debt	46.46%	5.39%	2.50%
Common Equity	53.54%	10.80%	5.78%
Rate of Return	100.00%		8.29%

1 OTP witness Ms. Ann E. Bulkley explains the cost of common equity and proposed
2 ROE in her Direct Testimony.

3
4 Q. HOW DO THE PROPOSED ROR, CAPITAL STRUCTURE AND CAPITAL COSTS
5 COMPARE TO THOSE IN OTP'S LAST SOUTH DAKOTA RATE CASE?

6 A. The proposed 8.29 percent ROR is 120 basis points higher than the 7.09 percent
7 ROR approved by the Commission in OTP's last South Dakota Rate Case.¹⁵ The
8 proposed ROR reflects an increase in the cost of LTD (from 5.22 percent to 5.39
9 percent) and an increase in ROE (from 8.75 percent to 10.80 percent). The
10 proposed 53.54 percent equity ratio is an increase from the 52.92 percent equity
11 ratio approved in that case.¹⁶

12
13 Q. DOES OTP'S CAPITAL STRUCTURE BENEFIT CUSTOMERS?

14 A. Yes. Having a financially strong company benefits customers and OTP's capital
15 structure, including its equity ratio, has a significant effect on its financial strength.
16 The debt to total capitalization ratio is an important credit metric for rating
17 agencies determining OTP's credit ratings. OTP's capital structure also assists OTP
18 in financing its investments and operations at a reasonable cost and ensures OTP's
19 ability to access capital markets in a variety of economic conditions. OTP's capital
20 structure has contributed to its ability to simultaneously finance its significant
21 capital expenditures and maintain its credit ratings. Finally, we expect its capital
22 structure and equity ratio will also facilitate OTP's completion of its future capital
23 expenditure plan. All these factors benefit OTP customers.

24 **A. Capital Structure**

25 Q. IS OTP'S CAPITAL STRUCTURE AN ACTUAL, MARKET-BASED CAPITAL
26 STRUCTURE?

27 A. Yes. OTP is a legally separate, wholly owned subsidiary of Otter Tail Corporation.
28 OTP has its own separate capital structure, its own short-term credit facility, and
29 issues long-term debt securities in private placements to institutional investors.
30 OTP's capital structure is subject to capital market scrutiny from credit rating
31 agencies and institutional investors.

32

¹⁵ *In the Matter of the Application of Otter Tail Power Company for Authority to Increase its Electric Rates*, Docket No. EL 18-021, Final Decision and Order; Notice of Entry at 11 (May 30, 2019).

¹⁶ *See In the Matter of the Application of Otter Tail Power Company for Authority to Increase its Electric Rates*, Docket No. EL 18-021, May 24, 2019 Exhibits Reflecting May 14, 2019 Decision, Exhibit 8.

1 Q. DO CREDIT RATING AGENCIES EVALUATE OTP SEPARATELY FROM OTTER
2 TAIL CORPORATION?

3 A. Yes. OTP has separate Issuer Default Ratings from Fitch, S&P, and Moody's.
4 Ultimately, because OTP is a separate legal entity with a separate credit facility and
5 separately issued LTD: (1) banks and investors recognize the importance of OTP's
6 separate capital structure; and (2) OTP's capital structure is subject to capital
7 market scrutiny from those banks and institutional investors.

8
9 Q. PLEASE DESCRIBE THE SCRUTINY OF CREDIT RATING AGENCIES AND
10 INSTITUTIONAL INVESTORS.

11 A. Fitch, S&P, and Moody's publish Issuer Default Ratings for OTP. Institutional
12 investors in our debt placements rely heavily on these credit ratings in their due
13 diligence evaluation of the Company for the purpose of deciding whether, and at
14 what price (and resulting interest rate), to purchase debt issued by OTP.

15
16 Q. HOW DOES OTP'S PROPOSED EQUITY RATIO COMPARE TO THE EQUITY
17 RATIOS OF THE COMPANIES IN MS. BULKLEY'S COMPARABLE GROUP?

18 A. Ms. Bulkley's Direct Testimony shows that OTP's 53.54 percent equity ratio is
19 within the range of the equity ratios for the operating subsidiaries of companies in
20 her comparable group. Ms. Bulkley notes the equity ratio range for the operating
21 subsidiaries of the companies in her comparable group is 45.33 percent to 58.67
22 percent. OTP's proposed 53.54 percent equity ratio is within that range.

23
24 Q. HOW DOES OTP'S PROPOSED EQUITY RATIO RELATE TO ITS CAPITAL
25 EXPENDITURE PLAN?

26 A. OTP has been engaged in a substantial capital expenditure program that began in
27 2007 and is projected to continue through 2029, as discussed above. OTP's equity
28 ratio is needed to support this program and maintain strong senior unsecured
29 credit ratings, as I explained earlier in my Direct Testimony.

30
31 Q. HOW HAS OTP FINANCED THIS CAPITAL EXPENDITURE PLAN?

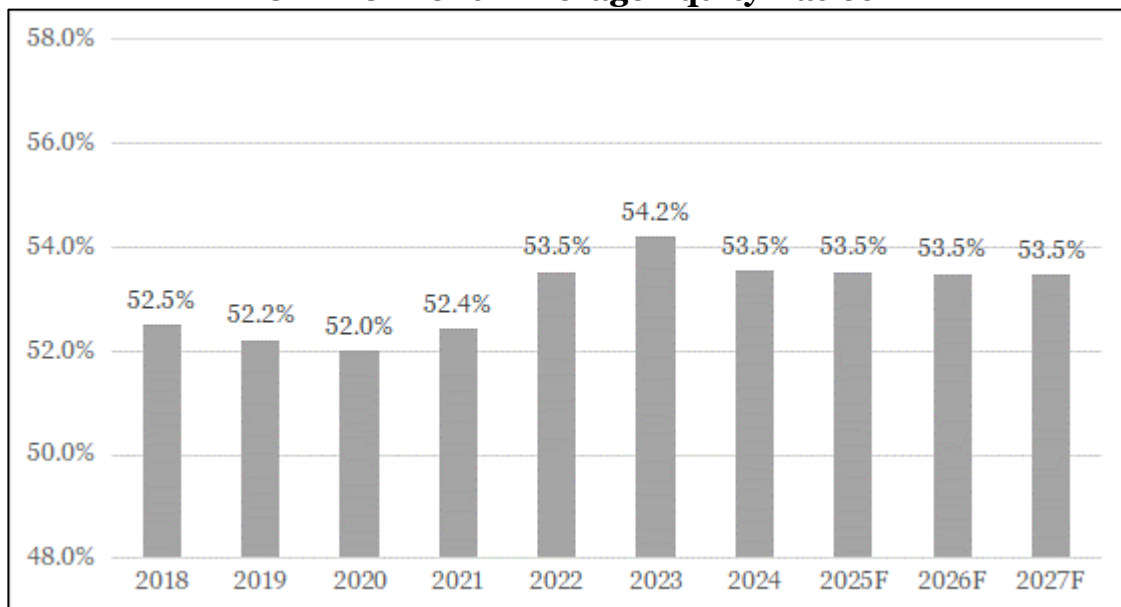
32 A. OTP has sought to maintain a balanced capital structure as it has undertaken these
33 investments, relying on a combination of retained earnings, equity infusions from
34 Otter Tail Corporation and LTD issuances. Table 3 above shows historical retained
35 earnings and equity infusions. Between 2018 and 2024, OTP issued approximately
36 \$625 million of LTD (with \$170 million replacing maturing notes).

Q. DOES THE 2024 TEST YEAR REFLECT OTP'S ACTUAL 2024 EQUITY RATIO?
A. Yes. The 2024 Test Year capital structure reflects OTP's actual, average common equity over the 13-months ending December 31, 2024.

Q. HAS OTP'S EQUITY RATIO INCREASED OVER TIME AS ITS CAPITAL EXPENDITURE PLAN HAS PROGRESSED?

A. Yes. Given the scope of OTP's capital expenditure plan, the Company determined it is prudent to strengthen its balance sheet to support its investment plans and help maintain strong senior unsecured credit ratings. Thus, OTP's equity ratio has increased over time through a mixture of retained earnings and equity infusions from Otter Tail Corporation, as shown in Table 3, above. I project OTP's equity ratio will remain at 2024 levels going forward, as shown in the figure below.

Figure 1
OTP 13-Month Average Equity Ratios



Q. DO CUSTOMERS BENEFIT FROM THE STRENGTHENING OF OTP'S BALANCE SHEET?

A. Yes. Strengthening OTP's balance sheet has allowed us to maintain credit metrics and strong senior unsecured credit ratings during a period of prolonged capital expenditures, ultimately reducing the cost of these customer-benefiting investments. These benefits will remain in place for the duration of the debt placed in support of the capital expenditure program.

1 Q. ARE THERE OTHER REASONS FOR OTP TO HAVE STRENGTHENED ITS
2 BALANCE SHEET?

3 A. Yes. OTP must be able to access capital at a reasonable cost to finance both
4 investments and operations. Further, this access must occur in a variety of
5 economic conditions. Recent events, including the COVID-19 pandemic, Winter
6 Storms Uri and Elliott, and bank failures in 2023 all severely impacted investors'
7 willingness to provide capital, and the price at which utilities can obtain that
8 capital. Different structural changes like sustained higher energy prices, greater
9 sales volatility, supply chain challenges, and inflation also affect the conditions
10 under which OTP is able to access the financial markets. Finally, general conditions
11 of economic uncertainty (including interest rate volatility) increase the importance
12 of maintaining a strong balance sheet, thereby allowing us to strategically execute
13 financing plans at a reasonable cost, to the benefit of customers. By strengthening
14 OTP's balance sheet, we were able to better meet those changes and continue to
15 maintain access to capital at reasonable costs.

16 **B. Long-Term Debt**

17 Q. PLEASE DESCRIBE OTP'S LTD ISSUANCES.

18 A. As discussed above, OTP issues LTD securities in private placements to
19 institutional investors.
20

21 Q. WHAT ARE THE AMOUNT AND COST OF OTP'S LTD FOR THE 2024 TEST
22 YEAR?

23 A. The 13-month average of OTP's LTD for the 2024 Test Year is \$835.5 million. The
24 cost of LTD for the 2024 Test Year is 5.39 percent, as shown on Exhibit____(TRW-
25 1), Schedule 3.
26

27 Q. HOW DO THE COST AND AMOUNT OF LTD COMPARE TO OTP'S LAST SOUTH
28 DAKOTA RATE CASE?

29 A. As shown in the table below, the overall cost of LTD has increased by
30 approximately 17 basis points, while the amount of debt capital has increased by
31 \$323.5 million.
32

Table 6
OTP LTD (2018 South Dakota and Current Rate Cases)

	2018 South Dakota Rate Case¹⁷	Current Rate Case	Difference
Amount	\$512.0	\$835.5	\$323.5
Cost	5.22%	5.39%	0.17%

Q. PLEASE SUMMARIZE OTP'S LTD PLACEMENTS SINCE ITS LAST SOUTH DAKOTA RATE CASE.

A. Since January 1, 2019, OTP has placed a total of \$625 million of new LTD, and has retired \$170 million of LTD. The average cost of LTD placed since January 1, 2019, is 4.30 percent.

Q. DOES THE 2024 TEST YEAR COST OF LTD REFLECT ANY 2025 DEBT OFFERINGS?

A. Yes. On March 27, 2025, OTP entered into a Note Purchase Agreement, whereby OTP agreed to issue \$100 million of senior unsecured notes consisting of \$50,000,000 in aggregate principal amount of its 5.49 percent Series 2025A Senior Unsecured Notes due March 27, 2035 (the Series 2025A Notes) and \$50,000,000 in aggregate principal amount of its 5.98 percent Series 2025B Senior Unsecured Notes due June 5, 2055 (the Series 2025B Notes, and with the Series 2025A Notes, the 2025 Notes). The Series 2025A Notes were issued on March 27, 2025, and the Series 2025B Notes are expected to be issued on June 5, 2025, subject to the satisfaction of certain customary conditions to closing.¹⁸

Q. WHY DID OTP INCLUDE THE COST OF THE 2025 NOTES IN THE COST OF LTD FOR THE 2024 TEST YEAR?

A. OTP has agreed to issue the 2025 Notes and therefore the associated costs are known and measurable. Further, OTP will use the capital raised during these debt offerings for investments it will make during the period rates from this case will be in effect. Therefore, it is reasonable to include the costs of the 2025 Notes in the calculation of the 2024 Test Year cost of LTD.

¹⁷ See *In the Matter of the Application of Otter Tail Power Company for Authority to Increase its Electric Rates*, Docket No. EL 18-021, May 24, 2019 Exhibits Reflecting May 14, 2019 Decision, Exhibit 8.

¹⁸ See Otter Tail Corporation Form 8-K (Mar. 27, 2025).

C. Common Equity

Q. WHAT IS THE AMOUNT OF COMMON EQUITY INCLUDED IN THE 2024 TEST YEAR?

A. The 2024 Test Year reflects common equity of \$1.006 billion, which is the actual 13-month average equity balance from December 2023 through December 2024. Exhibit____(TRW-1), Schedule 4 shows the 2024 Test Year equity balance by month.

Q. HOW DOES THE PROPOSED COMMON EQUITY LEVEL COMPARE TO OTP'S LAST SOUTH DAKOTA RATE CASE?

A. The \$1.006 billion common equity balance is \$430.5 million (approximately 75 percent) greater than the \$575.5 million balance in our last South Dakota rate case, as shown in Table 7 below:

Table 7
OTP Common Equity
(2018 South Dakota and Current Rate Cases)
(\$ millions)

	2018 South Dakota Rate Case¹⁹	Current Rate Case	Difference
Amount	\$575.5	\$1,006.0	\$430.5

Q. PLEASE DESCRIBE OTTER TAIL CORPORATION'S STOCK ISSUANCES SINCE 2004.

A. Since 2004, Otter Tail Corporation has utilized its At the Market Program (ATM), Employee Stock Purchase Plan (ESPP) and Dividend Reinvestment Plan (DRIP) for public issuance of its common stock. Otter Tail Corporation also had secondary offerings in 2004-2005 and in 2008. I have included detailed information showing the type of issuance (ESPP, DRIP, ATM, and Secondary) by year in Exhibit____(TRW-1), Schedule 5.

Q. ARE THERE COSTS ASSOCIATED WITH THESE ISSUANCES?

A. Yes. When a corporation issues common stock, the corporation incurs costs in the process of issuance, including underwriter discounts, audit, legal, printing and listing fees, and other expenses of issuance. When a corporation incurs these

¹⁹ See *In the Matter of the Application of Otter Tail Power Company for Authority to Increase its Electric Rates*, Docket No. EL 18-021, May 24, 2019 Exhibits Reflecting May 14, 2019 Decision, Exhibit 8.

1 issuance costs (also known as “flotation costs”), they reduce the net proceeds
2 received by the corporation issuing the stock (under generally accepted accounting
3 principles). Flotation costs are comparable to the issuance costs for LTD. I identify
4 the flotation costs associated with Otter Tail Corporation’s common stock
5 issuances in Exhibit____(TRW-1), Schedule 5. Ms. Bulkley has taken floatation
6 costs into account in making her ROE recommendation. OTP treated all of the
7 flotation costs as a reduction in proceeds, reflected on the balance sheet and not
8 expensed, which is the standard practice with all flotation costs.
9

10 Q. HAVE THESE COMMON STOCK ISSUANCES BY OTTER TAIL CORPORATION
11 BEEN RELATED TO OTP’S CAPITAL EXPENDITURES?

12 A. Yes. These Otter Tail Corporation common stock issuances are directly related to
13 OTP’s prior, current, and planned future capital expenditures.
14

15 Q. WERE THESE EQUITY ISSUANCES NECESSARY FOR OTTER TAIL
16 CORPORATION TO PROVIDE THE EQUITY INFUSIONS NEEDED BY OTP?

17 A. Yes. Otter Tail Corporation needed these equity issuances to fund the equity
18 infusions OTP needed to fund capital expenditures.
19

20 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

21 A. Yes, it does.