

2011 HOUSE ENERGY AND NATURAL RESOURCES

HB 1221

2011 HOUSE STANDING COMMITTEE MINUTES

House Energy and Natural Resources Committee
Pioneer Room, State Capitol

HB1221
01/20/11
13188

Conference Committee

Committee Clerk Signature



Relating to advance determination of prudence and to provide an effective date.

Minutes:

Rep. Porter: We will open the hearing on HB 1121.

Rep. Keiser: Let me give you a history on the concept of prudence. If you have never seen an application that needs to be created and brought forward to the Public Service Commission to consider the placement and implication of the energy transmitting facility you can see one all of the requirements that must be addressed. Not only the legal but every aspect of the placement of the facility needs to be addressed. This could take up to ten years or more to bring a project to life, much less actually building a facility. In 1995 this committee had legislation brought forward and said this is a huge expense that we are accruing all the way into a developing a proposal and plan of action. If it does take four or five years and these expenses get accrued, we had two options. The options were to accrue that expense and then expense it after that plan was built. That delayed it for a long time all the cost associated with bringing a plant to life. The legislature said the problem with that is as they accrue these expenses there is interest on those expenses and it compounds the overall cost of using that approach. It was suggested and we made the change to allow the Public Service Commission to take a proposal, review it and to have an advance determination of prudence, so that they could expense some of those expenses in your rates because it is a regulated industry. They were able to accelerate the recovery of the cost as they got into these projects. It made sense and it saved the rate payers money because they don't have to pay for those costs or the interest on those costs over the period of time. We must look at this section of the code and make some refinements to it. What will happen if a plant doesn't materialize? What happens to those costs then? We need to have that clarified as a policy standpoint.

Rep. Porter: Support of HB 1221.

Dan Kuntz: Attorney for the MDU Resources, in support of HB 1221. Hb amends a law enacted in 2005 that allows regulated public utilities to obtain an advanced determination of prudence from the Public Service Commission on generation and transmission projects (see attachment 1)

Rep. Porter: Any questions for Mr. Kuntz?

Loran Laugtug: I am representing Ottertail Power Company. WE are here in support of HB 1221, a bill to modify Section 49-05-16 of the North Dakota Century Code. (see attachment 2)

Rep. Porter: Any questions?

Rep. Hanson: Is Ottertail sell electricity in Minnesota, South Dakota, and North Dakota?

Loran Laugtug: Yes we sell about half our power to Minnesota and the other half in North and South Dakota, about 41% of the cost to North Dakota.

Rep. Hanson: Did you pass the cost on to all three states? We pass the cost on proportionally depending on how many customers are in each state. North Dakota's cost was just over 40%.

Rep. Porter: Further questions?

Rep. Kelsh: What is the anticipated growth in electrical demand going ahead five years.

Loran Laugtug: Today we would tell you less than 1%. It depends on what the economy does. Agriculture has kept much of our service territory alive.

Rep. Porter: Further questions?

Rep Nelson: You said you can't make final comments to a large project and reach financial close without fair expression of approval for each of the utilities you are subject to. How do the other states give you that clear approval?

Loran Laugtug: Each state is different in North Dakota is the advanced determination of the prudence. IN Minnesota we have a proceeding for a certificate of need for two transmission lines. In South Dakota we had not gone to get advance determination.

Rep. Keiser: What would we need to change in our law so that you would always want to build your plant in North Dakota?

Loran Laugtug: Big Stone was chosen because that was a site where we had always planned to build a unit there. Coyote has been discussed as a potential site in the future. I don't think there is anything that could change anything at EPA.

Rep. Porter: Further questions? further testimony.

Kathy Aos: I am here for XL Energy and in support of HB 1221. We also support the testimony that was given.

Rep. Porter: Further testimony in support.

Bob Graveline: Utility shareholder of North Dakota. We also support and encourage a do pass on HB 1221.

Rep. Porter: Further testimony in support. Is there any opposition?

Ilona Jeffcoat-Sacco: The original plan was to have the cost of Big Stone as part of that rate case. That could be incorporated into those rate case expenses and recovered without any number of years. I think it is a good thing to put some number in there, so that there is some guidance, we want to keep the cost of this expense close to the people using the electricity when the expense was added. (see attachment 3)

Rep. Nelson: It is in the bill that the cost amortization period would be five years. If it was written in the code what would the PSC use for a period of time?

Rep. Porter: Any further testimony? We will close the hearing on HB 1221.

Rep. Keiser: I move the adoption of the amendment on HB 1221.

Rep. Anderson: Second

Rep. Keiser: I move the amended HB 1221 to a do pass.

Rep. DeKrey: Seconded

Rep. Porter: Is there any discussion?

Rep. Hanson: I oppose the bill, because 100 % of my customers are Ottertail power and they are paying the cost of Big Stone.

Yes 14 No 1 Absent 0 Carrier Rep. Nelson

2011 HOUSE STANDING COMMITTEE MINUTES

House Energy and Natural Resources Committee
Pioneer Room, State Capitol

HB 1221
01/28/2011
13650

Conference Committee

Committee Clerk Signature	
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Relating to advance determination of prudence and to provide an effective date.

Minutes:

Rep. Porter: We will open the hearing HB 1221. When Michael was drafting that the English was incorrect. We have a new amendment passed out, we have a motion and a second on HB 1221 on the new language amendment.

Rep. Keiser: I move to adopt the new amendment.

Rep. DeKrey: Second.

Rep. Porter: Is there any discussion? All those in favor Voice vote taken. Motion carried.

Rep. Keiser: I move a do pass as amended.

Rep. DeKrey: Second.

Rep. Porter: Is there any discussion? Do pass motion carried.

Yes 12 No 0 Absent 3 Carrier Rep. Nelson

January 20, 2011

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1221

Page 1, line 10, overstrike "proposing" and insert immediately thereafter "intending"

Page 2, line 14, overstrike "annual"

Page 2, line 15, after the period insert "The public utility shall provide periodic reports as directed by the Commission to include a description of the status of the resource addition and any changes in material circumstances affecting the resource addition."

Re-number accordingly

Date: 1-20-2011
Roll Call Vote #: 1

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1221

House House Energy and Natural Resources Committee

Legislative Council Amendment Number _____

Action Taken: Do Pass Do Not Pass Amended Adopt Amendment
 Rerefer to Appropriations Reconsider

Motion Made By Rep Keiser Seconded By Rep. Anderson

Representatives	Yes	No	Representatives	Yes	No
Chairman Porter			Rep. Hanson		
Vice Chairman Damschen			Rep. Hunskor		
Rep. Brabandt			Rep. Kelsh		
Rep. Clark			Rep. Nelson		
Rep. DeKrey					
Rep. Hofstad					
Rep. Kasper					
Rep. Keiser					
Rep. Kreun					
Rep. Nathe					
Rep. Anderson					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

If the vote is on an amendment, briefly indicate intent:

voice vote taken motion carried.

Date: 1-20-11
Roll Call Vote #: 2

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1221

House House Energy and Natural Resources Committee

Legislative Council Amendment Number _____

Action Taken: Do Pass Do Not Pass Amended Adopt Amendment
 Rerefer to Appropriations Reconsider

Motion Made By Rep Keiser Seconded By Rep DeKrey

Representatives	Yes	No	Representatives	Yes	No
Chairman Porter	✓		Rep. Hanson	✓	
Vice Chairman Damschen	✓		Rep. Hunskor	✓	
Rep. Brabandt	✓		Rep. Kelsh	✓	
Rep. Clark	✓		Rep. Nelson		✓
Rep. DeKrey	✓				
Rep. Hofstad	✓				
Rep. Kasper	✓				
Rep. Keiser	✓				
Rep. Kreun	✓				
Rep. Nathe	✓				
Rep. Anderson	✓				

Total (Yes) 14 No 1

Absent 0

Floor Assignment Rep Nelson

If the vote is on an amendment, briefly indicate intent:

January 21, 2011

VK
1/21/11

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1221

Page 1, line 10, overstrike "proposing"

Page 1, line 13, after "customers" insert "that intends to make"

Page 1, line 15, overstrike "proposal" and insert immediately thereafter "resource addition"

Page 2, line 14, overstrike "annual"

Page 2, line 15, after the period insert "The public utility shall provide periodic reports, as directed by the commission, which must include a description of the status of the resource addition and any changes in material circumstances affecting the resource addition."

Renumber accordingly

Date: 1-28-2011
Roll Call Vote #: 1

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1221

House House Energy and Natural Resources Committee

Legislative Council Amendment Number _____

Action Taken: Do Pass Do Not Pass Amended Adopt Amendment
 Rerefer to Appropriations Reconsider

Motion Made By Rep. Keiser Seconded By Rep. DeKrey

Representatives	Yes	No	Representatives	Yes	No
Chairman Porter			Rep. Hanson		
Vice Chairman Damschen			Rep. Hunskor		
Rep. Brabandt			Rep. Kelsh		
Rep. Clark			Rep. Nelson		
Rep. DeKrey					
Rep. Hofstad					
Rep. Kasper					
Rep. Keiser					
Rep. Kreun					
Rep. Nathe					
Rep. Anderson					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

If the vote is on an amendment, briefly indicate intent:

voice vote taken motion carried

Date: 1-28-2011
Roll Call Vote #: 2

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1221

House House Energy and Natural Resources Committee

Legislative Council Amendment Number _____

Action Taken: Do Pass Do Not Pass Amended Adopt Amendment

Rerefer to Appropriations Reconsider

Motion Made By Rep DeKrey Seconded By Rep. Hofstad

Representatives	Yes	No	Representatives	Yes	No
Chairman Porter	✓		Rep. Hanson	✓	
Vice Chairman Damschen	✓		Rep. Hunskor	✓	
Rep. Brabandt	✓		Rep. Kelsh		
Rep. Clark	✓		Rep. Nelson	✓	
Rep. DeKrey	✓				
Rep. Hofstad	✓				
Rep. Kasper					
Rep. Keiser	✓				
Rep. Kreun					
Rep. Nathe	✓				
Rep. Anderson	✓				

Total (Yes) 12 No 0

Absent 3

Floor Assignment Rep Nelson

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1221: Energy and Natural Resources Committee (Rep. Porter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (14 YEAS, 1 NAYS, 0 ABSENT AND NOT VOTING). HB 1221 was placed on the Sixth order on the calendar.

Page 1, line 10, overstrike "proposing"

Page 1, line 13, after "customers" insert "that intends to make"

Page 1, line 15, overstrike "proposal" and insert immediately thereafter "resource addition"

Page 2, line 14, overstrike "annual"

Page 2, line 15, after the period insert "The public utility shall provide periodic reports, as directed by the commission, which must include a description of the status of the resource addition and any changes in material circumstances affecting the resource addition."

Renumber accordingly

2011 SENATE INDUSTRY, BUSINESS AND LABOR

HB 1221

2011 SENATE STANDING COMMITTEE MINUTES

Senate Industry, Business and Labor Committee
Roosevelt Park Room, State Capitol

HB 1221
March 16, 2011
15419

Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to advance determination of prudence.

Minutes:

Testimony Attached

Chairman Klein opened the committee hearing on HB 1221, relating to advance determination of prudence.

Daniel S. Kuntz, Montana Dakota Utilities Co. Testimony attached. In support of HB 1221.

Chairman Klein: Of course you site Big Stone 2, and that certainly was in the news a lot last election cycle, how would and so by passing this, are we looking to. I am concerned about the rate payers. Certainly everybody is, that is what we do out here. But, we also want our industry to continue to grow and provide the energy that we need. In a more simple term do you want to talk about the change in the amortization and capitalization as it would relate to how this bill will now make it easier?

Dan Kuntz: I don't know if it makes it easier, but I can clarify what this bill does. It was a little different than how Big Stone 2 was eventually treated and how it deals with the question that came up when Big Stone 2 was discontinued. The Big Stone 2 is a perfect example of advanced determination of prudence process. Ottertail and MDU came in for that advanced determination of prudence to build that particular plant or be partners in that plant that was going to be built in Big Stone, South Dakota. It was a huge investment for both of our companies. It would've been a major investment had we been completed but, based upon all the information that we had at the time that we started on that endeavor, it was the least cost project available to us and certainly appeared prudent. We started on that process getting permits, getting right of ways, doing the planning, the engineering studies and so forth and in the meantime a number of things happened. We had obviously the market demand declined as a result in the change of economy, we had an election at the federal level that were considerable concerns about environmental regulations, there were conditions opposed upon Ottertail by the Minnesota Public Utility Commission, as a result of those factors over a period of about 3 or 4 years, the decision was made. The other thing that happened is some of the partners because of those circumstances decided to withdraw from the partnership so at that point we no longer had an enough partners where we could build an economically sized project. In order to make the project efficient it

had to be somewhere close to that 600 megawatt size and by the time we lost some of our partners we were down below the level that we could support a project that size and with all the uncertainty regarding coal and environmental regulations we weren't able to attract new partners to come in and continue the project. So the decision was made and approved by the Public Service Commission that we should discontinue. But as you can imagine, over a course of three or four years a considerable amount of money had been spent on the planning and engineering and permit gathering and that sort of thing. Under the advanced determination and prudence law we are allowed to recover those expenses which under accounting rules for utilities at least have to be capitalized for that project. We can't expense those planning, engineering, and stuff as they occur. They have to be capitalized so that they then become part of the cost of the project when it finalized. They are not included in our rates up to that time, or any of that planning. So the commission determined and of course the Advance Determination of Prudence law that those expenditures had been prudent when they were incurred and we're entitled to recover them over a period of time. The question came up under the current law though, as to whether we were allowed to earn a return on those what had been capitalized expenses up until the time that they were amortized over the three or five year period. The current law was somewhat ambiguous in terms of whether that we were entitled to earn a return on those monies. A compromise was reached where we were allowed a return on that money from the period of time that the project was discontinued which was September-November time frame in the fall anyway up until the time the commission's order became effective the following summer. So we were allowed a return on those monies during that 9 month period but are not allowed a return after the commission's order became effective. This bill clarifies that not only would we not be allowed to earn a return once the commission's order became effective, we would not be able to allow a return on those expenses even once the project was discontinued period. At that point, forward you were allowed to amortize those expenses but you, the guilty bearers the cost if you will of not being able to recover any return until that amortization period is complete. That is probably the biggest substantive difference in the bill.

Chairman Klein: So you wouldn't have been able to collect those 9 months of return? **Dan Kuntz:** That's correct.

Senator Andrist: If this law had been in place you've been able to collect less? **Dan Kuntz:** That's correct, we would've been able to collect less than what we did under the settlement that we had with the commission. **Senator Andrist:** So help me understand how the bill will help you in the future? **Dan Kuntz:** How it helps us in the future is to assure that the advance determination of prudence process stays in place. As Chairman Klein pointed out there was considerable controversy, the bill caught some heat after the Big Stone 2 project and unfortunately one of its first projects of significant magnitude was a major project that was discontinued. Hopefully that doesn't happen very often, but that is one of the possibilities. The importance of keeping this statute in place was something important to the utilities. They're willing to give up that ambiguity in the statute in term of when they are able to recover those dollars in order to maintain the integrity of the advance determination of prudence process.

Senator Nodland: Prior to this bill, a utility would not be able to apply for a rate change until after they had built a large project? **Dan Kuntz:** You could apply for a rate change

prior to the completion of the project, but you could not necessarily include the cost of the project in that rate request change. The only way you could do that is a separate concept which is called construction work in progress. You could come to the commission and say we'd like to get the costs for example of the Big Stone 2 projects included in rates earlier than waiting until it's done. And that is something I think the utilities would've probably looked at the Big Stone 2 just because of that long lag time that has taken in the capitalization of those costs and in between. But that's something that the commission would then have to discession to review and determine yes or no whether they are going to allow the construction work in progress actually in regulations and at what point. This is a little different concept. Most projects don't take 5-7 years to complete like a coal generation project does, but they are still major investments for our Board of Directors, and our investors as well as our lenders. Even a gas processing plant is 18-24 months of planning, and probably \$100 million dollars, \$ 50 M into a project. Our Board of Directors, lenders are going to want to know is the Commission comfortable with this project and are they going to allow you to recover it in rates when you're done. **Senator Andrist:** Would this bill have helped you also had Big Stone become a reality or does it just help you in those cases where the project becomes unfeasible? **Dan Kuntz:** It definitely helps us with respect to Big Stone 2, even if we would've been able to complete it. Because of that particular project, and I forget the numbers but, but it was like \$300 million dollars would've been our share and MDU and we're a pretty small utility in relative to utilities nation-wide. That was a major commitment for our company to partner up on an investment of that size. I don't know that our directors would've been comfortable investing in a project with that size without having the blessing of the Public Service Commission. I certainly know our lenders would've asked questions if we wouldn't have had the PSC blessing to move forward with that project was prudent. It definitely helped us in terms of going forward to Big Stone 2, now in hindsight of course, we weren't able to complete Big Stone 2, but I think certainly with respect to future projects it's going to be helpful. I think even the commission is finding it useful that there involved in that decision making process or at least the opportunity to review that decision making process on the front-end of these projects and they are comfortable with the choices that were making in the selection whether we're building wind versus gas, or gas versus coal or that we're building instead of buying, there involved in that process on the front end. We then have more comfort putting those dollars out knowing that when the project complete we're not going to get second guessed that we should've done something different.

Senator Andrist: I presume you're looking for this kind of legislation in the other states where you serve too. Is that right? **Dan Kuntz:** We haven't specifically sponsored it but there are processes in the other states. I can't tell you precisely what they are. For example, if you're building a project like in South Dakota, when we had Big Stone 2, we served North Dakota, South Dakota, and Montana with our electric generation plus a little bit in Wyoming. For example, in South Dakota, we first had to get a Certificate of Public Convenience and Necessity, because the project was being built there. That's very comparable to the advance determination of prudence because the commission is not going to issue a certificate in South Dakota unless you can prove that there is a need for a project. In Minnesota, where a number of our other partners were involved, and therefore we had to get involved in that particular process because there was transmission involved, there was a Certificate of Need Process associated there, so the Minnesota commission had extensive review in determining whether this project the transmission and the

generation were prudent, so each of the commissions have a little different process. I am not exactly sure what it is in all the other states, it's particularly important for Montana Dakota, North Dakota because about 2/3 of our electric load is in North Dakota. So if we can't get approval from our major regulatory jurisdiction, a major project like this would almost be a non starter for us.

Senator Andrist: Have you been successful in being granted recovery in the other states?

Dan Kuntz: That issue is before the Montana Commission right now, and a rate request. I've not been involved in that case, but, it's my understanding that there in settlement discussions right now with the staff and as far as I know, I haven't heard that's been a real major issue of those expenses in that case. I haven't been involved specifically in handling that case.

Senator Schneider: If there are other states that allow regulators to make an advance determination of prudence and you just answered that, but could you provide the committee with something resembling a survey of what and how many states do this without spending a lot of time? **Dan Kuntz:** I can check and see if we've got some resources, but off the top of my head I don't know, don't have that survey because I am just concerned about the states we work in. I know there are other states that have it that vary for example. Virtually all the states have a Certificate of Public Convenience and Necessity Project where if you're building in that particular state you have to get a certificate of public convenience and necessity, which is kind of parallel to Advance Determination of Prudence Process that we're talking about here for projects that might be outside the state.

Senator Murphy: Are you saying that a bill can keep you from being second guessed? If it can, I want one. **Dan Kuntz:** It protects us from being second guessed on the particular prudence of that project because of the fact circumstances have changed. New commissioners are elected, markets change, that is one of the risks that we have as a utility on one hand our returns, the upside is regulated and we're limited to how much we can make on our successful projects, on the other hand we have protection if you will, that even on the unsuccessful projects that we could show that we acted prudently we're entitled to include those costs in our rates. That is kind of a quick pro faux for being regulated. If you can show that you acted prudently even though it wasn't successful, you are entitled to include those costs in your rates. But then your return is capped as well too on your good ones.

Chairman Klein: In regards to Senator Murphy's question, being no one believes they are being second guessed, because we certainly go into these projects with a tremendous amount of information and the cost of what you just explained, and I think everyone was pretty much on board, some years ago when we were moving forward and Big Stone was going to be great provider of a lot of energy. We were all excited about that, so certainly everyone talks about hindsight in this case and it wasn't even 20/20. **Dan Kuntz:** It was just kind of perfect storm of circumstances, change in market, change in regulations, change in administration, it was just unfortunate because it was we believed an excellent project, a least cost project would been a clean coal plant built on an existing site, we would've been able to share infrastructures with the existing Big Stone 2 plant, we would've been able to share some new environmental upgrades on the existing plant. Now we're going to have do this on our own, but circumstances change.

Senator Klein: Dan you stopped as a side note Big Stone 2 is gone forever? **Dan Kuntz:** Well for certainly for the foreseeable future. **Senator Klein:** Is there still a need for energy in America? **Dan Kuntz:** Well there certainly is going to be a need for energy in America right now because the economy there is plenty of electricity in the market, but I think that situation. We're buying electricity on the market now. We still have a need for generation. We're about a little over 100 megawatts short of what our needs are to meet our system. Well right now, energy is pretty cheap in the market, we can buy it out of the market pretty cheap but that won't be long term. **Senator Klein:** And prudence at looking at nuclear has changed over the weekend also. **Dan Kuntz:** In response to your question Mr. Chairman about Big Stone 2, is it still has future? Right now I think any coal project is going to be faced with some difficulties. The uncertainty around environmental regulations I think once those uncertainties are answered if new technologies are developed, hopefully there will be a future for new coal generation projects. But for right now it would be difficult to attract investors in a major coal project.

Kathy Aas: On behalf of EXCEL energy we also are in support of HB1221. Nothing new to offer.

Robert Graveline: Utility Shareholders of North Dakota and we to support HB 1221 and we think it ought to be passed.

Sandy Tabor: Lignite Energy Council. Also supportive of HB 1221.

Illona A. Jeffcoat-Sacco: Public Service Commission. Neutral on HB 1221. See written testimony. There is a think-tank organization that assists regulatory commissions that I believe can provide a fairly good survey of Advance Prudence in other states because we've had it in some lectures and I will check with that person when I get upstairs and try to produce something. **Chairman Klein:** That it would helpful and could you bring it to the clerk. Senator Schneider would like to know that too.

Chairman Klein: So Illona, what we've done here, you are almost sounding positive because now you appreciate the utilities have heard some of the commissions' concerns. They haven't heard all of them? **Illona Jeffcoat-Sacco:** No I don't think they've heard all of them and I am not going to enumerate them all either. **Chairman Klein:** What you're saying however, is that there were issues in this particular section that they have addressed and you are certainly confident and comfortable that it's helpful to the commission. **Illona Jeffcoat-Sacco:** That is exactly correct. We did want to be sure that we did say that, not just sit here and not say a word. We wanted you to know, they did address several of the concerns the commission had. **Chairman Klein:** A concern that I heard certainly was the due diligence and the commission providing for a hindsight issue. Does this put the commission in to holding it to a higher standard now that we're going to be looking to you is it not? **Illona Jeffcoat-Sacco:** I don't think so. The question of prudence is the question is this right investment. Example cited. The prudence question is should we buy it, should we invest. The commission has to make that decision when the utility wants rate recovery under traditional rate making. The difference is that the companies coming in early when their making that investment decision and asking the commission to agree that it is the right investment decision. So those parties are operating under the facts at that earlier point and

time and there is more of this possibility of hindsight is 20/20 if you wait until the rate making time to determine if the utility made the right decision. I think its equal for both parties. Any interveners, or rate payers, the commission and the company and I don't see it causing any problems. It is just a different mindset and we have to get used to that. **Chairman Klein:** Example cited relating to hindsight. We should've waited. **Illona Jeffcoat Sacco:** Yes, and that is exactly what the possibility is in a rate proceedings or a different group of commissioners elected, or a different economic environment, when a utility has to wait for that blessing on the investment decisions until a rate case. Then a commission can look back. **Chairman Klein:** In most cases, MDU they asked for recovery of their investment which seemed reasonable. Everything seemed to indicate that this was a great idea, we moved forward and then they got everyone pulling out with a lot of money invested, is it not then someone's responsibility, the rate payers, how do we tell the consumers that then? **Illona Jeffcoat Sacco:** Telling the consumers is very hard, but the obligation of the rate payer to pay for that cost of that investment decision whether it works out or not, if it's prudent, the obligation of the rate payer to pay for it is the same with or without this law. It is not because of this law that we're paying for the Big Stone costs, it's just that this law makes it a little more obvious. Newsworthy perhaps and also now one of the changes provides that it will be paid closer to the time when it was expended. In theory, you waited for a rate change; you might not pay those costs for 10 years, which is not really fair.

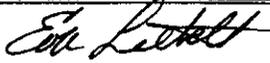
Closed Hearing on HB 1221.

2011 SENATE STANDING COMMITTEE MINUTES

Senate Industry, Business and Labor Committee
Roosevelt Park Room, State Capitol

HB 1221
March 16, 2011
Job Number 15529

Conference Committee

Committee Clerk Signature	
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Explanation or reason for introduction of bill/resolution:

Relating to advance determination of prudence

Minutes:

Discussion and Vote

Chairman Klein: Said to go to 1221. He said it was talking about the determination of prudence. If this bill went away the IOU's would be just fine because they can still recover. This is consumer issue and consumer driven. He visited with Bob and he explained it.

Senator Nodland: Said a couple of questions he thought he had answered but can't understand why they would ask for a rate increase after you have spent your money and done your project. He said especially with large projects and that was the issue with Big Stone. It makes sense to come in and show your proposal and put everything in for the PSC to look at and they decide if it is good or not and what rate you can increase. This regulatory issue is a lot different.

Senator Andrist: Said it was his understanding that the prudence thing is already in law and this just cleans it up and makes it more comfortable with the language. He said he thought the public service commission said the same thing, this is better language.

Senator Murphy: Said he hopes that is true otherwise it would be worthless.

Chairman Klein: Said the issue isn't clean up but clarification and they are going to rely more on the public service commission granting them that prudence authority up front. He said they have allowed them to spread those costs after the public service commission said this is prudent and after it fell through. He said this bill will help the consumer rather than helping the big utility companies.

Senator Laffen: Said that he thought there was another piece in this that was the crux of the bill. At the end it states if they do one of these projects and it is stopped they don't get a return on their investment. That was a bone of contention in the Big Stone project the utility came back after they invested all that money and said we are stopping the project but we want rate payers to also pay for the return of that investment and they got it. It clarifies that they wouldn't ask for that again. They are willing to concede that so they can keep this prudence in this piece of law.

Senator Murphy: Said so the PSC didn't approve this project?

Chairman Klein: Said they did that is why they were able to go back to the PSC and say we went through all this prudence and you agreed.

Senator Murphy: Said that the advanced determination of prudence law allow the utility the option to have the commission review the prudence so you can't be second guessed but they did anyway.

Chairman Klein: Said they did but they did allow them to get a return of investment of the amount of money they loosed and that won't happen anymore.

Senator Nodland: Moved a do pass.

Senator Andrist: Seconded the motion.

Roll Call Vote: Yes-7 No-0

Senator Andrist to carry the bill

REPORT OF STANDING COMMITTEE

HB 1221, as engrossed: Industry, Business and Labor Committee (Sen. Klein, Chairman) recommends **DO PASS** (7 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1221 was placed on the Fourteenth order on the calendar.

2011 TESTIMONY

HB 1221

Prepared by Daniel S. Kuntz for
Montana-Dakota Utilities Co.

Testimony on HB 1221

HB 1221 amends a law enacted in 2005 that allows regulated public utilities to obtain an advanced determination of prudence from the Public Service Commission on generation and transmission projects. The amendments are intended to clarify the current law based upon experience in using the law since it was enacted.

By way of background, the rates of a regulated utility are considered reasonable if they are at a level that allows the utility to: (1) recover its prudently incurred expenses; and (2) earn a reasonable rate of return on its prudently invested capital. Accordingly, every expense and every investment made by a public utility can be reviewed by the Public Service Commission to determine whether the expense or investment was prudent when the expense was incurred or the investment made. Typically, that review doesn't occur until a utility proposes to increase its rates based upon additional expenses or investments it has incurred or obligated itself to since its last increase request. The problem with that process, particularly for major investments or contractual commitments, is the review occurs after the commitment has been made. Conducting the review after the investment is made places utilities and their lenders at considerable financial risk that a project, which the utility deemed prudent based upon the information available to it when it made the investment, is later determined imprudent by the commission based upon hindsight.

The Advanced Determination of Prudence law allows the utility the option to have the Commission review the prudence of an investment before the investment is made or committed to rather than after. By conducting the prudence review before the

investment, the utility and its lenders have assurance that the investment won't be second guessed and the utility denied rate recovery based on after-the-fact arguments the investment shouldn't have been made or a different investment should have been made. For example, a utility may determine, based on current information, that a new coal generation plant is a prudent investment to meet its generation needs. Such a project, however, takes years to plan, obtain the necessary permits, and build. Without an advanced determination of prudence by the Commission, the utility runs the risk that if circumstances change, such as decreased customer demand, or new environmental regulations, or election of a new commission, the commission will determine, with the wisdom of hindsight, that the utility should have invested in some other form of generation and therefore deny rate recovery for some or all of the investment in the coal generation plant. An advanced determination of prudence removes this unnecessary risk by allowing the utility to request that the Commission conduct its prudence review before the investment is made rather than after.

With that background, HB 1221 provides amendments to the advanced determination of prudence law to clarify and improve the law.

On lines 7-10 of page 1, the bill adds a definition of "resource addition." The current law references "resource addition" but the term is not specifically defined. The new definition includes facility purchases and demand response systems that are not specifically mentioned in the current law.

On lines 5 through 10 of page 2, the bill deletes the reference to reasonableness as part of the prudence determination. Although the reasonableness of a project is an inherent part of a prudence determination, it is not a separate determination. Deletion

of the reference to reasonableness also clarifies that the Commission retains its authority to review the reasonableness of the final expenditures on the project in a rate proceeding even if it issues an advance determination of prudence for the overall project.

On lines 18 through 24 of page 2, the bill clarifies the process for the Commission to reconsider or modify an advanced determination of prudence order including the payment of expenses for such reconsideration.

The changes to subsection 6 of 49-05-16 beginning on line 25 of page 2 deal with rate recovery for projects that have been determined prudent but are subsequently discontinued. These amendments address issues that arose following the discontinuance of the Big Stone II project. The amendments confirm that the utility is entitled to amortize and recover the capitalized cost of the project over a period of up to five years; however, the utility is not entitled to earn a return on the unamortized balance after the project is discontinued.

Finally, there were some additional changes that were intended to be included in the bill that were inadvertently omitted in drafting. First, the word "proposing" on line 10 of page 1 of the bill should be changed to "intending" to clarify that the law only applies to projects the utility intends to pursue. Second, it was intended that a sentence be added to subsection 3 of the statute (page 2 of the bill) to confirm that the Commission can require reports on the status of the project and changes in material circumstances. Therefore, we are proposing an amendment to the bill to add these provisions.

Montana-Dakota Utilities Co. supports the passage of HB1221 with the proposed amendments and urges the Committee's favorable consideration.

Testimony of Loren Laugtug
Otter Tail Power Company
Before the House Energy & Natural Resources Committee
January 20, 2011

Mr. Chairman and members of the Committee, for the record my name is Loren Laugtug and I am before you today on behalf of Otter Tail Power Company.

On behalf of my company, I would like to submit the following comments regarding my company's support for HB 1221, a bill to modify Section 49-05-16 of the North Dakota Century Code.

Let me begin by providing committee members with some important historical context on how major asset additions were accomplished by public utilities in an earlier era, and then contrast this with how these additions are done, or not done, in modern times.

In the 1960s and 1970s, the electrification of America caused the demand for electricity to grow at a rate of about 7% per year nationwide. This growth required utilities to undertake massive planning efforts to develop new, baseload electric generating plants and new, high-voltage transmission projects to route higher volumes of electricity to our customers. For Otter Tail Power, this led to the development of Big Stone Plant in South Dakota in 1975, a partnership with Montana-Dakota Utilities and Northwestern Energy, and in 1981 to the Coyote Generating Station near Beulah, a partnership with Montana-Dakota, Northwestern Energy and the Northern Municipal Power Agency.

In those happy days, public utilities could simply plan their large generation and transmission projects, construct them as cost-effectively as they could, and then seek cost-recovery from utility commissions in each of the states where they served. As long as the utility could demonstrate that the resource addition was necessary for providing adequate electric service to its customers, and that it had been done as efficiently as possible, utility commissions, generally speaking, authorized cost-recovery in electric rates. The key point to understand here is that utilities were able to presume what we call 'prudence' prior to acquiring capital and commencing construction. It was rare that utility commissions second-guessed resource additions as long as they were within the mainstream of what utilities were building nationwide, i.e., coal, nuclear or oil. Bond-sellers and shareholders didn't concern themselves with the potential for non-recovery of investments due to regulatory uncertainty, or evolving federal laws, or impending environmental regulations.

Today, public utilities live in a very different environment. My company experienced this first-hand when we sought to build the Big Stone II generating plant in South Dakota, beginning in 2005. In order to achieve the economies of scale necessary to build a modern coal plant, we partnered with Montana-Dakota Utilities and five other regional utilities in proposing the 630 megawatt (MW) Big Stone II coal plant. If constructed, it would have been the cleanest and most efficient coal plant in the U.S. While all new generation projects are expensive, we believed Big Stone II was a risk worth taking in order to provide our customers with the lowest long-term electric costs.

As you might expect, the list of water and air permits, environmental impact statements and regulatory authorizations from multiple state and federal agencies is extensive in modern times. But all of these permissions must be in place before it's possible to begin preparing for what is known as "financial close". Bankers and bond-sellers want to know that all the "i's" have been dotted and all the "t's" have been crossed before a consortium of them are ready to provide construction financing. It's important that the members of this committee understand this so that you can appreciate the value of what state statutes currently authorize with "advance determination of prudence", found in NDCC 49-05-16. This is an opportunity for the public utilities engaged in a large 'resource addition' to make their case with the North Dakota Public Service Commission (ND PSC) and ask for a determination of 'prudence' in advance of construction of that project. In this proceeding, a utility must demonstrate to the commission that a project is a necessary and useful investment to be constructed on behalf of its ratepayers. In the case of Big Stone II, the estimated total cost was about \$1.5 billion dollars. In the modern era, Otter Tail could not make final commitments to such a large project and reach financial close without a clear expression of approval from each of the utility commissions we are subject to.

So Otter Tail Power Company and Montana-Dakota Utilities, the two public utilities in the Big Stone II project, filed with the ND PSC for Advance Determination of Prudence in November of 2006. The ND PSC provided its determination of prudence for our participation in Big Stone II in August of 2008. By September of 2009, however, economic, financial and regulatory circumstances surrounding the new plant's development had changed sufficiently to warrant Otter Tail's withdrawal from the project. The following are the changes that we felt were most significant as we made this difficult decision:

1. Significant changes to September 2009 energy price forecasts were expected to result in changes to Otter Tail Power Company's resource plan and resource adequacy requirements. The economy was heading into a recession and overall electric demand was dropping.
2. Unprecedented, difficult financial market conditions and cost-recovery risks made the acquisition of large amount of capital required for Big Stone II unreasonably costly. Lehman Brothers declared bankruptcy in September 2009 and banks generally were in a state of near-panic.
3. The Big Stone II project had lost two partner utilities in September 2007, and we had not, so far, been able to acquire new partners in their place. The risk that Otter Tail could be required to either increase its share of the 630 MW plant, or participate in a smaller and less economic project, raised the potential cost per MW to a level that we felt was unacceptable.
4. Finally, the legislative and regulatory uncertainty surrounding federal energy and climate change policy, including the Environmental Protection Agency's 2009 indication that it intended to regulate CO₂ under the existing Clean Air Act, increased the risks associated with such policies and regulations. The Obama Administration had placed a climate change bill near the top of its legislative agenda in January, and the Waxman-Markey bill had passed the U.S. House in late June that year. Only Senate approval stood in the way of "80% by 2050" from becoming federal law.

● Otter Tail's strategy at this point was to minimize potential losses for its customers and its shareholders, and to ask the ND PSC for a determination that it had once again been 'prudent' for Otter Tail to withdraw from the Big Stone II project. This request was approved by the PSC in June of 2010. In the settlement between Otter Tail Power Company and the ND PSC, the commission agreed that a) the company would be allowed to recover its North Dakota share of sunk costs from its North Dakota customers, b) that this would occur over a period of three years, and c) that the company would forego "carrying costs" from the date the commission order was issued, even though the company was ordinarily entitled to this under standard accounting practices promulgated by the Federal Energy Regulatory Commission (FERC).

● HB 1221 which you have before you today would continue to allow public utilities to seek advance determinations of prudence from the ND PSC for significant 'resource additions'. This is extremely important as utilities face the daunting challenge of replacing, refurbishing or augmenting our existing generation and transmission assets. A constructive regulatory environment that provides appropriate recovery mechanisms on prudent investments is essential to financial investors. Utilities must incur costs to fully evaluate and develop projects to provide service to their customers. Some projects will occur, others may not. Investors want to know that there are mechanisms in place to provide recovery of cancelled projects as long as management has acted with due diligence and prudence. The concession being made by utilities in HB 1221 is that project cancellation would preclude a utility from charging customers for "carrying costs" that are incurred after the date a utility announces it is withdrawing from a project. I believe this is consistent with the policy laid out by the Empower North Dakota Commission in its recent energy policy document:

Policy: Encourage state and federal policies that ensure the state business climate is predictable and stable.

- Avoid laws and regulations that place new barriers on investment and development.
- Enact and preserve state laws and regulations that facilitate investment and avoid uncertainty. (P. 7, "Comprehensive State Energy Policy")

● Mr. Chair and members of the committee, Otter Tail Power requests a "Do Pass" on House Bill 1221. Thank you.

House Bill 1221

Presented by: Illona A. Jeffcoat-Sacco
General Counsel
Public Service Commission

Before: House Energy and Natural Resources Committee
Honorable Todd Porter, Chairman

Date: January 20, 2011

TESTIMONY

Mister Chairman and committee members, I am Illona Jeffcoat-Sacco, General Counsel with the Public Service Commission. The Commission asked me to testify today regarding House Bill 1221 and the proposed amendments.

While the Commission, the agency responsible for hearing these types of cases, is technically neutral on this bill, it does appreciate that the utilities have heard some of the Commission's concerns over this law as currently written. In addition, the proposed amendments further address our concerns and we ask the Committee to act favorably on these amendments. We do not have any technical concerns with the bill that would hamper our ability to administer the Advance Determination of Prudence Law.

Mister Chairman, this concludes my testimony. I will be happy to answer any questions you may have.

PROPOSED AMENDMENT TO HOUSE BILL NO. 1221

Page 1, line 10, overstrike "proposing" and insert immediately thereafter "intending"

Page 2, line 14, overstrike "annual"

Page 2, line 15, after the period insert "The public utility shall provide periodic reports as directed by the Commission to include a description of the status of the resource addition and any changes in material circumstances affecting the resource addition."

Re-number accordingly

Testimony on Engrossed HB 1221

HB 1221 amends a law enacted in 2005 that allows regulated public utilities to obtain an advanced determination of prudence from the Public Service Commission on generation and transmission projects. The amendments are intended to clarify the law based upon experience in using it since it was enacted.

By way of background, the rates of a regulated utility are considered reasonable if they are at a level that allows the utility to: (1) recover its prudently incurred expenses; and (2) earn a reasonable rate of return on its prudently invested capital. Accordingly, every expense and investment made by a public utility can be reviewed by the Public Service Commission to determine whether the investment or expense was prudent when it made or incurred. Typically, that review doesn't occur until a utility requests an increase in its rates based upon additional expenses and investments it has incurred or made since its last increase request. The problem with that process, particularly for a major investment, is the review occurs after the investment is made. Conducting the review after the fact places utilities and their lenders at considerable financial risk that a project, which the utility deemed prudent based upon the information available to it when it made the investment, is later determined imprudent by the Commission based upon hindsight.

The Advanced Determination of Prudence law allows the utility the option to have the Commission review the prudence of an investment before the investment is made.

By conducting the prudence review before the investment is made, the utility and its lenders have assurance the investment won't be second guessed and the utility denied rate recovery based on after-the-fact arguments the investment shouldn't have been made or a different investment should have been made. For example, a utility may determine, based on current information, that a new coal generation plant is a prudent investment to meet its generation needs. Such a project, however, takes years to plan, obtain the necessary permits, and build. Without an advanced determination of prudence by the Commission, the utility runs the risk that if circumstances change, such as decreased customer demand, or new environmental regulations, or election of a new commission, the commission will determine, with the wisdom of hindsight that the utility should have invested in some other form of generation. The utility could then be denied rate recovery for some or all of its investment in the coal generation plant. An advanced determination of prudence removes this unnecessary risk by allowing the utility to request the Commission to conduct its prudence review before the investment is made rather than after.

With that background, HB 1221 provides amendments to the existing Advanced Determination of Prudence law to clarify and improve the law.

On lines 7-10 of page 1, the bill adds a definition of "resource addition." The current law references "resource addition" but the term is not specifically defined. The new definition includes facility purchases and demand response systems that are not specifically mentioned in the current law.

Language on lines 13-14 of page 1 of the bill was added to clarify the law only applies to projects the utility actually intends to pursue.

On lines 5 through 10 of page 2, the bill deletes the reference to reasonableness as part of the prudence determination. Although the reasonableness of a project is an inherent part of a prudence determination, it is not a separate determination. Deletion of the reference to reasonableness clarifies that the Commission retains its authority to review the reasonableness of the final expenditures on the project in a rate proceeding even if it issues an advance determination of prudence for the overall project.

A sentence was added on lines 16-19 of page 2 of the bill to confirm the Commission can require reports on the status of the project and changes in material circumstances affecting the project.

On lines 18 through 24 of page 2, the bill clarifies the process for the Commission to reconsider or modify an advanced determination of prudence order including the payment of expenses for such reconsideration.

The changes to subsection 6 of 49-05-16 beginning on line 25 of page 2 deal with rate recovery for projects that have been determined prudent but are subsequently discontinued. These amendments address issues that arose following the discontinuance of the Big Stone II project. The amendments confirm that the utility is entitled to amortize and recover the capitalized cost of the project over a period of up to five years. The utility, however, is not entitled to earn a return on the unamortized balance after the project is discontinued.

Montana-Dakota Utilities Co. supports the passage of Engrossed HB1221 and urges the Committee's favorable consideration.

Engrossed House Bill 1221

Presented by: Illona A. Jeffcoat-Sacco
General Counsel
Public Service Commission

Before: Senate Industry, Business and Labor Committee
Honorable Jerry Klein, Chairman

Date: March 15, 2011

TESTIMONY

Mister Chairman and committee members, I am Illona A. Jeffcoat-Sacco, General Counsel with the Public Service Commission. The Commission asked me to testify today regarding Engrossed House Bill 1221.

While the Commission, the agency responsible for hearing these types of cases, is technically neutral on this bill, it does appreciate that the utilities have heard some of the Commission's concerns over this law as currently written. Further, we do not have any technical concerns with the bill that would hamper our ability to administer the Advance Determination of Prudence Law.

Mister Chairman, this concludes our testimony. I will be happy to answer any questions you may have.