HOUSE BUSINESS AND INDUSTRY COMMITTEE

February 11, 1981

SUMMARIES FOR

HOUSE BILL 407 -

Introduced by Rep. Cozzens, amends the tax increment laws for urban renewal to authorize tax increment financing for urban development as provided in 7-15-4233 and provides for adjustment in the base taxable value whenever changes by law, administrative rule or judicial decision revise the valuation of the urban renewal area.

HOUSE BILL 395 -

Introduced by Rep. Meyer, revises the statutory authority for the Public Service Commission to ascertain the value of property of a public utility by including a utility plant in service or under construction as "used and useful for the convenience of the public."

HOUSE BILL 431 -

Introduced by Rep. Meyer and others, authorizes the Public Service Commission to consider data projected for a future period in setting public utility rates.

HOUSE BUSINESS AND INDUSTRY COMMITTEE

Rep. Ray Jensen, V-Chairman, called the meeting to order February 11, 1981 at 8:00 a.m. in Room 129 Capitol Building, Helena. All members were present. Bills to be heard were HBs 395, 407, 431.

HOUSE BILL 407 -

REP. CHUCK COZZENS, House District #64, Yellowstone County, deals with the concept of tax increment financing which became part of the law in 1972 and is currently being used in several larger cities in Montana. Smaller towns are looking at it. Details are to be presented by proponents.

LARRY GALLAGHER, Community and Economic Development and Rehabilitation consultant, showed a large chart. Urban renewal law enacted in 1959 to take advantage of federal programs for urban renewal activities - assumes elected officials must declare that it is in the public interest that blighted conditions exist - declining or stagnant tax base are evidence. All levying agencies have a strong interest in the wellbeing of tax base property.

If there is no incentive, owners will not invest money in improving their properties. The date a plan is adopted, the tax base is frozen. Declining value would trigger the identification of the need to adopt tax increment taxation to encourage private development by increasing the value above, applying the difference between the base and the increased value - the difference is the tax increment. See EXHIBIT A attached. This is to encourage private investment by using new tax dollars developed by confidence being restored in the area. Subsection (5) "costs incurred in connection with the redevelopment activities allowed under 7-15-4233" was added by HB 407.

Cities have used that money in connection with rehabilitation. Federal moneys are becoming scarce. Cities feel that they ought to be allowed to use their tax increment dollars as the Legislature has already allowed them to use the tax increment dollars as they have been using the federal dollars. Since the last session the Legislature has not been tampering with the tax values, but other agencies - ruling, regulatory and jurisdictional processes - have eroded the base because of inaccurate assessment.

LES PRENTICE, Missoula Redevelopment Agency, Missoula, director said Missoula does have several projects under construction because of their efforts. Because some of the federal programs which are probably going to dry up, we now need to rely on their own tax increment funds. They do need these amendments to the tax increment law. There are several projects that would allow them to get involved in if this is done. The rollback issue in particular has affected us. There has been $463,000 of rollback in Missoula and that has seriously impaired their tax income. Cash flow from the tax increment fund has been eroding and seriously eroded their funding.

JOHN COFFEE, Chairman of the Missoula Redevelopment Agency private sector said changing Missoula needs a lot of help in tax base and jobs. Their economy is hurt very badly; but he thinks that things are on the mend and look pretty good. Hopefully, they need to increase the tax base thereby increasing tax increment. Can do many things with tax increment funding. They are concerned that we do notspend this funding to increase the tax base - need to put money into things that will make tax increment grow. This can be done if this bill is passed. We would like to set up a facade improvement program whereby the persons who cannot, but need to, mend the facade, we would step in and pick up a percentage of the interest on that loan thereby making the loan at less interest rate. This would enable the land owner to improve his building and thereby increase the tax base in the city.

Budget problems - they have gone through two attempted budgets and it is impossible to know what kind of money they are dealing with - nobody knows. The base year is affected. This won't be misused because they have the city council to go through and work projects are scrutinized each year. Recommends passage of the bill. See his further testimony on his Witness Sheet.

JOHN JEWELL, Councilman from Great Falls, said he supported the tax increment 10 years ago. They support HB 407 wholeheartedly in order to improve the tax base.

BRUCE A. MacKENZIE, D.A.Davidson & Co., Great Falls, MT, said bonding houses require this change. Any change in the actual tax base through a change in taxable valuation methods is taken into account. This increment is what goes to pay for any bonds. If this were to decrease, you decrease the amount of funds available to repay, especially when looking at large increments. The source of that repayment is gone. Some means of adjustment is necessary. Have to be assured that this increment is going to stay there.

JANET CORNISH, Butte-Silver Bow, Butte, representing the local government of the Butte-Silver Bow Redevelopment Agency, supports HB 407.

DONALD R. PEOPLES, Chief Executive of Butte-Silver Bow Urban Renewal, Butte, strongly endorses HB 407. See his testimony EXHIBIT B.

RICK GRIFFITH, Butte-Silver Bow Urban Revitalization Agency, Butte, said the Urban Renewal law that exists givesthem a viable program. They have problems with the way it exists now because they may not be able to get a percentage increment. Without HB 407, they cannot go ahead with projects which will result in a successful revitalization through involvment in financing programs. HB 407 will be a great improvement. EXHIBIT C.

RON MOLEN, Missoula Chamber of Commerce, Missoula, said the City of Missoula has watched a once strong area rapidly deteriorate because of no means of inducing people to go back in and finance that area. They now have 180,000 vacant square feet in the downtown area and immediate loss of jobs. They currently have two large projects because of federal urban renewal tax increment financing. Other projects are uncertain with the 34% rollback, and current interest rates, and drying up of federal funds. The cash flow needs to be maintained because one of the primary goals has been to develop private investment on a 6-1 basis. The primary means of doing this is through the bonding houses. This bill with amendments would bring back more jobs and strengthen the base of the taxes in that urban renewal district.

DONALD KERNS, Redevelopment Director, Helena, said nine structures have been improved costing $6 million, yet the City of Helena has a negative tax increment. He strongly urged that the committee pass HB 407 so that they can recognize some of the problems with this today.

ALICE FRYSLIE, President of the Helena Improvement Society, Helena, supports passage of HB 407. See her testimony on a Witness Sheet.

JAN BROWN, Downtown Helena, Inc. (which is an association of the retail merchants), supports this legislation.

CHARLIE HAIL, Vice President of the Helena School Board, would not oppose this legislation. They are very supportive of tax amendments.

DAVE GOSS, Billings area Chamber of Commerce, said the City of Billings supports amendments heartily. This is necessary because of budget cuts in Washington, D.C. The second amendment provides the ability to establish rollback.

CLARK PYFER, representing the Montana Chamber of Commerce and himself, is chairman of the Montana Chamber of Commerce and a private owner in downtown Helena; is an ower of tax increment financing. He is sold on this program. It is a partnership for private and public funds and it brings it back to the local level where, as a property owner and citizen, you understand how it is handled.

See the letters from Hiram Shaw, Butte; Stephen P. Olson, Senior Vice President of the First Northwestern Bank of Kalispell; Henry K. Good, President of the Uptown Kalispell Development Corporation; F. Charles Mercord, President of the First Federal Savings and Loan of Kalispell; Norma E. Happ, City of Kalispell, all addressed to Rep. Ken Nordtvedt in support of HB 407.

OPPONENTS: None

QUESTIONS -

Rep. Harper - when you are talking about shifting the original tax base - the city is losing money in one area - is there some sort of limitation? Mr. Gallagher said the increment is used to get bonding and it is necessary to have that in order to get money.

Rep. Robbins asked how many square feet are vacant in downtown Helena. Mr. Kerns said there are 100,000 vacant square feet in Helena downtown.

Rep. Schultz asked if all properties will pay their full taxes on the tax base. Mr. Gallagher said there would be a $90,000 increment. The tax is generated by applying the all-purpose levy on the difference.

Rep. Jensen asked what would cause this increasing increment to decline so it would be necessary to change the base? Mr. Gallagher said declining commercial property, not because of those activities, but because of tax assessing errors - discrepancies between commercial valuations allowing rollbacks. Commercial valuation of $5 million and 10% cut allowed through no direct devaluation of the property - somebody simply made a decision.

Are proposing that we be allowed to roll it back to that 10%.

Rep. Ellison said if you adjust this base upward, it looks like somebody is going to come out on the short end. - if you lower the tax base 10%... Mr. Gallagher said this would provide the ability to bond if these bases will not decline, but will improve substantially. If it does rollback other agencies will be affected.

Rep. Schultz asked where the city would get the funds. Mr. Gallagher said bonding could be done - as it is now they can't do this.

Rep. Cozzens closed expressing appreciation for the time and questions. Page 2 of Mr. Gallagher's testimony. Each city has the opportunity of making the judgment on use of those dollars - think control should be kept local. Urge careful consideration and support of this bill.

HOUSE BILL 395 -

REP. DARRYL MEYER, House District #42, Great Falls, sponsor, explained HB 395 is a new way for a company to construct new plants by adding a portion of the construction cost to their rate base. It helps keep the consumer rates lower.

JACK BURKE, Montana Power Company, Butte, as Executive Vice President of MPC has the responsibility for governmental affairs, and local government, and consumers. They support HB 395 very strongly. It would allow a utility to include in its rate base for establishing rates to customers a plant that is under construction but not yet on-line - to include the cost of that construction in their rate base while the plant is being built. The PSC does not allow this because statutes say only a utility plant that is "used and useful for the convenience of the public" can be included for establishing rates. See his testimony EXHIBIT D.

JAMES HUGHES, Mountain Bell, Helena, said a majority of their construction is done on an on-going basis. Their annual construction budget is running around $6 million per year and it is considered Work in Progress. Some of the same principles certainly apply to Mountain Bell. If you can take advantage of the cash flow involved as part of the rate base, that cash flow improvement does increase your cost of capital. The benefit to the consumer is that the company is not having to go out and borrow so much as you improve your cash flow situation because of the Work in Progress. Even if there were such a thing as zero growth and you were adding people to the system - more and more people will be using more - increased use causes a non-static condition. Urges support of this bill.

GENE PHILLIPS, Pacific Power and Light Company, agrees with the comments previously stated. Utility construction programs have increased to serve the needs of existing and anticipated new customers. Construction work in progress (CWIP) - utilities must borrow and as the need for capital increases, the financing pressure increases. Investors want to be satisfied that rate on their investments are satisfactory. This would improve interior cash flow - would improve interest costs - would result in gradual rate increases - would reduce cost of capital. Urged Do Pass.

WILLIAM C. GLYNN, Vice President, Treasurer and Chief Financial Officer of the Montana-Dakota Utilities Co., said Mr. Burke set forth what arguments there are. Consequences of not allowing construction costs that are not providing service as yet to be included in the rate base are more fully explained in his prepared testimony - EXHIBIT E. The need is real, geniune, and serious.

REP. FABREGA RETURNED TO THE COMMITTEE AS CHAIRMAN.

EUGENE W. MEYER, Kidder, Peabody & Co., Inc., 10 Hanover Square, N.Y., N.Y. 10005, Vice President of Management has been personally responsible for the pricing of $50 million of new utility financing bringing the impact of the financing markets into perspective. You have to show that you have the wherewithal to pay for that market. Have not been able to do financing except at very high financial costs. They pursue a tight money policy to try to reduce inflation. High interest rates go on and it is difficult to attract financing the amount of debt that has to be raised. When you delay the ultimate completion of a plant, you add to its costs.

Utilities have been warned that under no circumstances can they get financing unless CWIP is certain to be considered in the rate base. You cannot be assured that you will actually be able to complete that plant. Failure to complete a plant is not unheard of - some plants have not been completed after $2-3 million have been spent and the consumer pays for that write-off and gets no power for it.

With CWIP in the rate base the following happens to the utility. There is more cash flow - not all the cash flow has to come from outside. The cost of money is enormous - the less you have to attract outside, the less that plant will cost because it can be done at a lower cost because investors will not demand as high a cost of equity that is generating some funds internally. Won't have to worry about increased costs of building. Think you would assure an adequate supply. There is a difference between what you face when you finance an electric company and other utilities and a franchised industry. The industrial company has no franchise and will not build if it is unable to make money, but even if it is profitable and it decides to do so, it takes 6-9-12 months to make it meaninfgul. It takes 10 years for an electric company to get a project going. You are in great peril in Montana in attracting capital unless some changes are made. What capital you are able to scrape together will cost an arm and a leg. Those prices will find their way to a ratepayers bill.

LARRY GESKE, President of the Great Falls Gas Company, supports HB 395. Mr. Glynn brought up some points on the regulatory lag. Expenses can be 12-15 months out of sync in passing on costs. They are filing one gas rate on top of another and are not having an opportunity to earn a fair return. When the rates go into effect, you are recovering expenses 12-15 months behind. The Gas Company does not have heavy capital requirements today and when they get into coal gasification, will get into planned requirements for costs.

DENNIS LOPACH, Mountain Water Co., Missoula, is concerned about the problem of financing the additions to its plant. Asks for serious consideration of the bill. The PSC has never addressed the Work-in-Progress idea and has used the idea of a plant in operation.

OPPONENTS -

JAMES C. PAINE, Montana Consumer Counsel, Helena, representing all transportation and commercial and industrial customers. This will have a significant adverse impact on all ratepayers in the state. One of the main thrusts is that CWIP put in now would be cheaper in the long run. The analyses are flawed in one respect or another. They fail to take into consideration the on-going rate is thought to be too high. They do not present value analyses to the consumer. The consumers will be better off with not having to pay this interest rate.

Construction Work in Progress - would like the members of the committee to keep in mind that there is a significant difference between regulated utilities and private industries, and that is competition - it is there in the private sector and it is not in the utility. It keeps businesses efficient - they are forever looking for means to cut costs and that is not so in the regulated utilities. They are allowed to do this and if the rest of the bills pass, every one of those bills tears away at the incentives for the utilities to cut costs. The PSC is the replacement for competition. The primary role of the PSC is that they must afford the opportunity to the utility to earn a rate of return. If they pass this will be a guarantee of that return. Private sector businesses do not have that type of guarantee.

CWIP represents a switching of the investment from the investor to the customer. The utilities want their money up front - there is a class of customers that is discriminated by CWIP. This legislation would say that it is used and useful. Until you get that service we maintain you do not get that service - the business consumer that payson the inclusion of CWIP and then goes belly-up before that comes on line - this is a burden on those citizens who pay and die before they get to use it. It is hard to say that it is used and useful to them. This is purely an inflationary increase for the utilities.

Allowance for funds used during construction would allow the utility to be fully compensated for their cost. It allows the utility when it is put on line to recover their investment in the facility itself - they are fully compensated. Strongly urged not to pass this legislation.

GEORGE F. HESS, Montana Consumer Counsel, Minneapolis, Minn., said HB 395 would define something to be a matter of law which is not a matter of logic. It defies a used and useful purpose. Construction Work in Progress is not used nor usable in supplying service to companies today. There is no service out of Colstrip. They are under construction. The question involved here is not whether the company recovers its cost - it is a matter of when it recovers its cost. It is a matter of which generation shoulders the burden of those costs. If it is excluded from the rate base, the company is allowed to recover those costs from the customers who get to use the plant. It recovers a return on determined costs through the inclusion of the undepreciated portion of those costs as long as the plant is in service. They are not arguing to me that is a better reason for doing this - it is not cheaper - what's happening by including CWIP in the rate base is you are forcing the ratepayer to supply a portion of their capital. Any valid analysis should take into account the time value of money to consumers. Another argument for including CWIP is that AFUDC is not real earnings - that is nonsense. AFUDC is an allocation of a project's cost of construction of which a part can be added to the cost of construction such as if a utility had a $5 million labor bill, $1 of which could properly be considered construction cost, that would be allocated to expenses. The allocation of the cost of funds used for construction is proper. It improves cash earnings because it comes from higher returns. There is a question as to whether it is an advantage to a customer to give him the money in lieu of the promise of a lower rate. It is a misapplication of funds, assuming Montana customers allow CWIP, that they have paid for a service that is to go out-of-state.

It seems that requiring involuntary payments from ratepayers is counter to what should be done - they put the risk on the entrepreneurs instead of on the ratepayer.

BILL OPITZ, Director of the Public Service Commission, endorses what the Consumer Counsel and George Hess have said. He can show with figures that if the consumer's cost of his money exceeds the rate that is capitalized under AFUDC, the consumer is better off waiting until that plant is on-line to pay for that plant. That takes into account the time value of money. People have raised the issue of how come we are paying for all the power that is being shipped out-of-state. The inter state rates are sufficiently high that the Montana consumer is not paying for that power going to the West Coast. You are asking Montana citizens to subsidize electricity. See EXHIBIT F.

CWIP is not allowed in the rate base under the conditions that are proposed in HB 395 and when they set rates they would not be included, but in this case they would be. What could be any more inflationary - the same kilowatt is today costing you 3¢ and the next day you are going to pay 4¢? Need to know the figures. How much more would it cost over the six preceding years to save that $1 million. Montana Power is one of the few utilities in the nation who are actually selling above book value. They are doing a study at the PSC on this. Their earnings have increased and at the same time they have issued 14% more common equity shares.

REP. JOE QUILICI, House District #84, Butte, is chairman of the Consumer Counsel Committee. You and I are going to pick up the tab for these increases in return - Montana ratepayers. If you start picking it up for #3 and #4 for CWIP - what if you move out of the state - you are picking it up for someone else. What about senior citizens who might die and they have been paying the tab for this and getting no return.

Northern Tier is thinking of coming through the State of Montana, but Northern Tier isnn't here and we are, and if this goes through, you will be picking up the tab before it ever gets here. It is going to be the Montana ratepayers. Hoped the committee takes a real hard look at this before they pass it out of committee.

ED SHEEHY, Retired Federal Employees, Helena, opposes HB 395. There are 1200 retired federal employees living in Montana. It is very difficult for someone who pays out of his own pocket to appear here as an opponent, but the members pressured him to come here today. He feels the Legislature is not the place for this matter to be settled. We have the elected PSC and this is the forum for rate cases. He believes they should do the job for which they were elected.

HELEN WALLER, Chairman of the Northern Plains Resource Council, opposes HB 395. See her testimony EXHIBIT G.

PHYLLIS A. BOCK, Mountanan's Power to the People (MPP), Helena, opposes HB 395, because it will increase rates. She would label this a utility relief bill and asked that it Do Not Pass. See further testimony on her Witness Sheet.

JIM JENSEN, LISCA, opposes HB 395, said this bill would require payment for a service that many citizens cannot afford and will never use. It is the same as saying that people should pay their rent 10 years in advance even before moving into their apartment - no one on this committee would encourage that logic. It just doesn't make good sense. They should not have to pay for something they do not use.

TOM SCHNEIDER, Montana PSC, is from the southeastern part of the state. Others have given a very good description of the effects of this bill. He urged very earnestly to kill this bill.

QUESTIONS -

Rep. Andreason asked if a prevalued analysis of the expenditures of the consumers of the rates to determine what they would be spending had been done. Rep. Meyer said No, they have several present values analyses. Mr. Opitz said they have done a present value analysis of what the consumer would pay. The GAO report concerned just the issue of CWIP assuming a uniform unit of input for five years and they went through the analysis and capitalized in one and not the other, and with zero interest rate, it was $130,000 higher overall. When you used a discount rate of 6%, the two figures came within $30,000 of each other and $10,000 the other way. It would be 10% now and at that cost of money to the consumer he is better off paying as the plant comes on-line. EXHIBIT F explains this.

It will encourage management to get that plant on line in a timely manner. Colstrip is a cost plus basis with Bechtel and what is the incentive to get that plant on-line.

Rep. Kessler asked if this piece of legislation passes, what assurances do we have that they will have the added incentives? Mr. Burke said the allegations against Bechtel were shown to be not ture - we need the power that that plant will produce. Construction is ahead of schedule. The labor productivity is 20% better than expected. It is not a cost-plus contract. Bechtel is the architect. Due to high productivity they are running at about 80% of labor projected. Their object is to keep electricity at the lowest cost to consumers. MPC ranks about 213. This bill would keep our cost of capital at a lower rate.

Rep. Meyer asked about a breakdown of the $3.24 return on their quarterly report to shareholders. Mr. Burke said out of the $3.24, $1.20 was from utility operation and the balance from other non-utility portions of the company - 64¢ is AFUDC. Increase in utility earning was not the cause of the increase of the total earnings that Opitz reported. The utility earnings are not increasing to the degree that is necessary to raise the capital.

Rep. Harper asked about prohibiting CWIP to out-of-state usage. Mr. Opitz said it is a concept that has been kicked around for years. A copy of a speech made by a California man in 1975 concerning CWIP said the Federal Energy Regulatory Commission was examining a rule-making decision to explore whether CWIP should be put into the rate base.

Rep. Harper asked to what extent can we expect out-of-state ratepayers to help pay the cost of plants? Can the PSC just set the rate and they can pay it? Mr. Opitz said interstate rates are set by the Federal Energy Regulatory Board, and they haven't been putting CWIP into the rate base.

Rep. Harper said MPC is to disclose the building of a new plant in eastern Montana. The power is going to go out-of-state - aren't we in fact being asked to build a plant for out-of-state users without a real guarantee that they will be included? Mr. Burke said Colstrip is not all owned by MPC. Under no circumstances would they engage in any more building of generating capacity unless CWIP is included.

Rep. Manning said plants that Montana Power build and the portion they own is built for Montana consumers. In the utility business, the plant is built in anticipation of need. Hopefully, when it comes on-line, it is already being used. So power has been imported. Whatever excess power is on the market, those revenues we get from out-of-state sales in the utility regulation, those revenues reduce the cost to Montana consumers. Try to get the most for that excess in order to reduce the cost.

Rep. Vincent asked if it is thought fair or reasonable for this committee to consider it on its merits without considering 3-4 other pieces of legislation. Mr. Burke - yes - you have to act on each piece as it comes along. It signals that investment would be safe. All other address other methods of regulation which would improve the regulatory procedures. There is a bill in the Senate to grant the PSC immediate authority to grant immediate increases. Would you think it alright to work backwards? This bill would simply say if you made the ordinary application for rate increase, it would be automatically allowed that day. Mr. Burke said it would require the PSC to act. He thinks that bill is important in the improvement in the regulatory process. This bill is important standing by itself. If this bill passes and that one does not, it would make that much difference.

Rep. Pavlovich asked the purpose of the chart, EXHIBIT H. The explanation of the chart is set forth in EXHIBIT D-1. The top part of that chart shows what is added to a plant by virtue of the AFUDC. It shows over the 40 years the rate that the ratepayer must pay, and an overall cost of capital on that amount. The dark part of the chart is the construction cost that is built into the capitalization of the cost of the plant.

Rep. Wallin said Mr. Sheehy thought the PSC should handle the rate cases. Why doesn't your group handle this case instead of making it a bill? Mr. Opitz said the utilities have made the bill. In 1977 a statute was enacted that said if we don't have our rate cases out within 9 months, they would go into effect. We do handle these applications. There are many things that the Commission can do looking at all factors besides looking at CWIP to see that the utility has the opportunities to receive a fair return on its investment. CWIP use has been turned down to utilities because it is not used or useful. The law does not allow it. This bill would mandate that into the consideration.

Rep. Ellison asked if Montana has been a net importer or a net exporter of electricity? Mr. Burke said over the last years, it has probably exported slightly more power than it has imported. In the next 5 years we will be importing more power than we will export. Colstrip 3 will come on-line in 1984, and 4 will come on-line in 1985 and they expect those plants will be loaded.

Rep. Ellison asked Mr. Opitz to answer the above question and he said he didn't have the figure either. Depending on the water year - we will normalize for water. If it is a good water year, we will export. Would say not a large exporter.

Rep. Vincent asked beyond Project 89 what does the company have planned relative to building new facilities? Mr. Burke said there is a report filed with the DNRC that lays it out. In the immediate future, to his knowledge, what we are announcing today at Fort Benton is the main project. We are soliciting on application a preliminary permit to build a Canyon Ferry dam to build a run-of-the-river dam. That plant would probably be coming on-line in the 1986-87 time frame. Resource 89 decision which will be announced at the end of this month is scheduled to come on-line in 1989. Throughout this period there will be additions to existing plants. You are then outside of the 10-year time frame.

Rep. Fabrega said a utility has a monopoly and is mandated to provide service. The question is whether that mandate allows them to ask for this kind of financing. The mandate gives them a return which allows them a chance to build. He doesn't think that is the proper way to go. Montana has had the sad case where inadequate service was being provided even tho there was another utility willing to serve properly. The State of Montana took a very substantial direction in the area of the Major Facility Siting Act in which the Board of Natural Resources determines the need for an additional plant.

Rep. Andreason asked Mr. Eugene Meyer regarding his testimony that if this legislation passes, this would signal investors that Montana was a good investment place. What other states have included this? Mr. Meyer said the following states: Arizona, Connecticut, Florida, Illinois, Kansas, Kentucky, Maryland, Nevada, New Jersey, New Mexico, New York, North Carolina, Ohio, South Carolina, Texas, Utah, Vermont, West Virginia, and Wisconsin.

Rep. Meyer closed; said things were coming off the shelf - retailer will pass a cost along to the customer. Capital - lots of competition and it is going to cost more money and he alluded to who is going to pay and when. Do we want to pay or should our children pay? CWIP is one way we can keep one of our largest employers in business - you know what has happened to railraods, Chrysler, New York, etc. We will pay much for services that we need. He is willing to pay a little bit more now than to pay the higher costs later.

HOUSE BILL 431 -

HB 431 is rescheduled for the 40th day, February 20, but testimony will be allowed at this time. Rep. Fabrega said the hearing will be opened and continued at the later date.

REP. DARRYL MEYER, House District #42, Great Falls, chief sponsor said HB 431 is an act requiring the Public Service Commission to consider data projected for a future period in setting public utility rates.

LARRY D. GESKE, President of the Great Falls Gas Company, Great Falls, supports HB 431 because of the problems they encounter with regulatory lag in setting rates. See his testimony EXHIBIT I.

(There were no other proponents that couldn't be present February 20.)

OPPONENTS -

GEORGE F. HESS, on behalf of the Montana Consumer Counsel, opposes HB 431, saying the fundamental reason for having laws is for the protection of the public from possible abuse of monopoly power in the sale of human necessities. See his testimony EXHIBIT J.

Other opponents are listed on the Visitors' Register.

Rep. Schultz asked about the members of the Consumer Counsel Committee. Mr. Paine told him there are four members. It is a bi-partisan committee having two members from the house and two members from the Senate. They are Reps. Quilici and Dr. Lory, and Senators Boylan and Kolstad.

The meeting adjourned at 11:00 a.m.

REP. W. J. FABREGA, Chairman

Josephine Lahti, Secretary

VISITORS' REGISTER

HOUSE B & I COMMITTEE

BILL 407 Date 2/11/81

SPONSOR Cozzens.

NAME	RESIDENCE	REPRESENTING	SUP-PORT	OP-POSE
Larry Gallagher	330 Fuller Ave Helena.	Missoula Redevelopment Agcy	✓	
[illegible]	[illegible]			
[illegible]	[illegible]	[illegible]		
[illegible]	[illegible]	[illegible]		
Ron Molen	105 Broadview Pl Msla	Msla Chamber of Commerce	✓	
David C. Mitchell	1117 Jackson Msla	Missoula Redev. Agency	✓	
Bruce A. MacKenzie	P.O. Box 456	D.A. Davidson & Co	X	
Charlie Hail	2009 [illegible] Helena	Self	X	
[illegible]	Helena	[illegible]	X	
Rick Griffith	Butte	Butte-Silver Bow	✓	
Donald Keene	Helena	City of Helena	✓	
[illegible] Cornish	Butte	Butte-Silver Bow	✓	
[illegible]				
Jon Brown	Helena	Downtown Helena	✓	

IF YOU CARE TO WRITE COMMENTS, ASK SECRETARY FOR LONGER FORM.

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Form CS-33
1-81

LAWRENCE GALLAGHER Consultant 303 North Ewing Street ● Helena, Montana 59601 ● Telephone 406/442-8539

Exhibit A

MEMORANDUM

TO: House Bill #407 Supporters

FROM: Lawrence Gallagher, Consultant

DATE: February 2, 1981

SUBJECT: Reasons to Amend Tax Increment Sections 7-15-4288 and 7-15-4293. (Hearing scheduled for February 11, 1981, 8:00 AM, Room 129, House Business and Industry.)

The First Amendment Proposed

The first amendment proposed is to amend Section 7-15-4288. Costs which may be paid by tax increment financing, to include: "(5) Costs incurred in connection with the redevelopment activities allowed under 7-15-4233."

What does 7-15-4233 allow?

7-15-4233. Powers which may be exercised by urban renewal agency or authorized department. (1) In the event the local governing body makes such determination, such body may authorize the urban renewal agency or department or other officers of the municipality to exercise any of the following urban renewal project powers:

(a) to formulate and coordinate a workable program as specified in 7-15-4209;

(b) to prepare urban renewal plans;

(c) to prepare recommended modifications to an urban renewal project plan;

(d) to undertake and carry out urban renewal projects as required by the local governing body;

(e) to make and execute contracts as specified in 7-15-4251, 7-15-4254, 7-15-4255, and 7-15-4281, with the exception of contracts for the purchase or sale of real or personal property;

(f) to disseminate blight clearance and urban renewal information;

(g) to exercise the powers prescribed by 7-15-4255, except the power to agree to conditions for federal financial assistance and imposed pursuant to federal law relating to salaries and wages shall be reserved to the local governing body;

(h) to enter any building or property in any urban renewal area in order to make surveys and appraisals in the manner specified in 7-15-4257;

(i) to improve, clear, or prepare for redevelopment any real or personal property in an urban renewal area;

(j) to insure real or personal property as provided in 7-15-4258;

(k) to effectuate the plans provided for in 7-15-4254;

(l) to prepare plans for the relocation of families displaced from an urban renewal area and to coordinate public and private agencies in such relocation;

(m) to prepare plans for carrying out a program of voluntary or compulsory repair and rehabilitation of buildings and improvements;

(n) to conduct appraisals, title searches, surveys, studies, and other preliminary plans and work necessary to prepare for the undertaking or urban renewal projects;

(o) to negotiate for the acquisition of land;

(p) to study the closing, vacating, planning, or replanning of streets, roads, sidewalks, ways, or other places and to make recommendations with respect thereto;

(q) to organize, coordinate, and direct the administration of the provisions of this part and part 43;

(r) to perform such duties as the local governing body may direct so as to make the necessary arrangements for the exercise of the powers and performance of the duties and responsibilities entrusted to the local governing body.

(2) Any powers granted in this part or part 43 that are not included in subsection (1) as powers of the urban renewal agency or a department or other officers of a municipality in lieu thereof may only be exercised by the local governing body or other officers, boards, and commissions as provided under existing law.

The reader should be made aware that each city has an opportunity to review the annual work program and budget for urban renewal activities and therefore can limit the powers to be exercised. Should a city decide not to use the powers to rehabilitate properties or to enter into a compulsory code enforcement program, it simply can decide not to do so whenever it adopts its annual work program. Section 7-15-4206. (18) "Urban renewal plan" means a plan, as it exists from time to time, for one or more urban renewal areas or for an urban renewal project, which plan:

(a) shall conform to the comprehensive plan or parts thereof for the municipality as a whole; and

(b) shall be sufficiently complete to indicate, on a yearly basis or otherwise:

(i) such land acquisition, demolition, and removal of structures; redevelopment; improvements; and rehabilitation as may be proposed to be carried out in the urban renewal area;

It is clear that local government has the discretion whether or not to use the powers authorized by the urban renewal law and if this amendment is approved to use tax increment dollars for those activities.

Why do we need the amendment?

The urban renewal law (7-15-4281) provided financial authority to municipalities to: "borrow money and apply for and accept advances, loans, grants, contributions, and any other form of financial assistance from the federal government; from the state, a county, or any other public body; or from any sources, public or private, for the purposes of this part and enter into and carry out contracts in connection therewith;"

The section goes on to authorize appropriations, the levy of taxes and assessments, expenditures, investments, adoption of annual budgets; to enter into agreements with agencies or departments vested with urban renewal project powers.

Additionally, municipalities have the power to issue urban renewal bonds, refunding bonds, and/or general obligation bonds, (in accordance with procedures set forth) to finance urban renewal activities..." to finance the exercise of any and all powers conferred upon the municipality by this part (43) and part 42 which are necessary and proper to complete the project in accordance with the approved plan and any modification thereof duly adopted by the local governing body."

If municipalities can use all of these various funding mechanisms to pay the costs of urban renewal activities, why can't they use their own tax increment dollars for approved urban renewal activities?

Cities are being forced to do without federal categorical funds and the old federal programs which were used to finance urban renewal activities no longer exist. Thus, it is important if urban renewal is to suceed that we be allowed to use <u>our own</u> tax increment dollars as we are authorized to use federal and other funding sources.

<u>The Second Amendment Proposed</u>

The second amendment proposed is to amend Section 7-15-4293 to include <u>administrative</u> or <u>judicial</u> change in the method of appraising property, the tax rate applied to it, or the tax exemption status of property, or <u>the taxable valuation of property if the change in taxable valuation is based on conditions existing at the time the base year was established</u>.

Why? Cities which have adopted tax increment financed urban renewal projects (Billings, Helena, Great Falls, Butte, Kalispell, Missoula) have been unable to budget from one year to the next because of rulings by courts, tax appeal boards, or the State Department of Revenue. These non-statutory decisions have resulted in substantial changes to the taxable valuation of commercial properties reducing the vlaue of certain properties in tax increment districts to such an extent that despite substantial new private investment there is no tax increment or the anticipated overall increment is not adequate to cover debt service on bonds anticipated to be sold.

This amendment would allow a municipality to adjust its base year accordingly if, for example, a blanket, statewide, 34% rollback of commercial property values was mandated by a court or the State Tax Appeals Board or the State Department of Revenue.

NAME John Atlee BILL No. 407

ADDRESS 320 Ravenwood - Missoula DATE 3/11/81

WHOM DO YOU REPRESENT Missoula Redevelopment Agency

SUPPORT Yes OPPOSE AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

We support the bill as it concerns the [illegible] that can be funded by Tax Increment funds. In Missoula we are interested in spending our Tax Increment funds in such a manner as to increase the Tax base & at the same time increase the Increment. Under the present law this can be done, but only in certain ways. In light of the possible cut backs in Federal programs that assist Urban Redevelopment, we strongly believe that a community's Tax Increment must be used to help fill this void.

FORM CS-34
1-81

Exhibit B

Ken Nordtvedt
Chairman, House Taxation Committee
Rm. 102
State Capitol
Capitol Station
Helena, Montana

Mr Nordtvedt and Members of the House of Representatives Taxation Committee:

My name is Don Peoples and I am the Chief Executive of Butte-Silver Bow. Butte-Silver Bow established its Urban Renewal District in 1979 and completed its Urban Renewal Plan including a tax increment provision in October of 1980. We are very pleased with this method of financing projects within the district as it is dependent on revenues generated within our area. We hope to realize the first increment funds during the next fiscal year.

The local government of Butte-Silver Bow heartily supports House Bill 408. The expansion of allowable activities for which tax increments may be used will provide us with local sources of funding for all of our revitalization activities. This is especially important in light of dwindling Federal aid programs to cities and the growing additude in many communities that the Federal Government should have less to do with local development projects. HB 408 would allow our Urban Revitalization Agency to engage in facade improvement programs, economic development and energy conservation activities which are all crucial to Butte-Silver Bow's redevelopment success.

We are especially interested in the provision included in HB 408 which will adjust our frozen tax base to allow for individual tax appeals. Property owners within our Urban Renewal District have, in 40 cases (1980), appealed their property taxes up to an allowable 34%. This is very detrimental to our tax increment program and could result in a negative increment in 1981. HB 408 would adjust the 34% roll back to our base year of 1980 and the increment can then be figured on a relative basis.

We therefore strongly endorse HB 408 and would be happy to provide any additional data which may aid your decision making process.

Thank you for this opportunity to express our concerns.

Exhibit C

BUTTE-SILVER BOW URBAN REVITALIZATION AGENCY

Courthouse
Butte, Montana 59701
(406) ~~723-4714 or 723-4713~~ -
723-8262 ext. 354

February 3, 1981

Ken Nordtvedt, Chairman
House Committee of Taxation
Room 102
State Capitol
Capitol Station
Helena, Montana 59601

Mr. Nordtvedt and Members of the Committee:

My name is Rick Griffith and I am the Chairman of the Butte-Silver Bow Urban Revitalization Board. Our agency was established in 1979 to rehabilitate and renovate Butte's Urban Renewal Area which consists of our entire central business district and the surrounding neighborhoods. The Montana Urban Renewal Law gives us a framework in which to operate our agency and the tax increment financing provision can provide us with a viable funding source for urban renewal projects.

However, we are rather concerned as to whether we will receive a positive increment in the first year since our frozen tax base was established in 1980. Despite the fact that 17 new businesses have come to our renewal area in the last year and a number of other establishments have either expanded within the area or moved from other sections of our community we are anticipating some problems. This is due to the administrative tax roll backs granted to property owners within our central business district. HB 407, introduced by Representative Cozzens of Billings would certainly help us alleviate this problem. We understand that taxes do present a hardship to building owners in economically depressed areas but we must realize some increase in our tax base is necessary to reverse an overall downward trend. HB 407 will allow communities to adjust their frozen or base year to reflect administrative roll backs in property taxes. In this manner property owners may continue to get some tax relief but their community can also benefit to some extent when any improvements are made which result in an increased taxable value.

The Butte-Silver Bow Revitalization Agency also favors the other provision in Mr. Cozzens bill. Expanding the number of costs which may be covered by tax increment funds will give our Agency the ability to conduct activities which are so crucial to the success of our district. Economic development and a revolving loan fund for store front rehabilitation are two areas of primary concern for our agency. Under existing statutes these activities can not be paid for with tax increment funds. HB 407 will permit us to go forward with these and other projects which will result in a successful revitalization effort.

Thank you for your consideration.

Rick Griffith, Chairman

NAME A[illegible] BILL No. [illegible]

ADDRESS [illegible] DATE [illegible]

WHOM DO YOU REPRESENT [illegible]

SUPPORT X OPPOSE AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

As president of the [illegible] I [illegible] [illegible] operation of Helena Citizens [illegible] establishing [illegible] programs which [illegible] improve [illegible] better place [illegible] [illegible] the M.T.S. [illegible] [illegible] for [illegible] [illegible]

[illegible]

FORM CS-34
1-81

NAME Charlie Heil BILL No. 407

ADDRESS 2009 Oro Fino Gulch Helena DATE 2-11-81

WHOM DO YOU REPRESENT Self

SUPPORT X OPPOSE AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

NAME [illegible] BILL No. [illegible]

ADDRESS [illegible] DATE [illegible]

WHOM DO YOU REPRESENT [illegible]

SUPPORT X OPPOSE AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

2412 Gladstone Avenue
Butte, Montana 59701
January 31, 1981

Honorable Ken Nordtvedt
Chairman
House Taxation Committee
State Legislature
Helena, Montana 59601

Dear Mr. Chairman:

This letter is in reference to HB 407, introduced by Legislator Chuck Cozzens concerning the uses of tax increment financing for urban renewal.

I am a member of the Butte-Silver Bow Urban Revitalization Agency, created by the Butte-Silver Bow Council of Commissioners in 1979.

The Council has, in approving the Agency's Urban Renewal Plan, also authorized the use of tax increment financing as a means of supporting local urban renewal projects.

In determining, however, what the best local uses of these funds would be, we find that we are limited by State Law in making our own determinations. I would, therefore, urge the Committee to give strong consideration to adopting that provision of HB 407 which extends the uses to which tax increment financing can be applied to include all uses authorized under urban renewal law.

This is particularly of concern to our Agency since we are suffering economic decline in our community and must rely heavily on this method of financing to carry out our local projects.

Some examples of the additional uses to which we would put these funds include:

* Parking facilities development
* Historic preservation
* Economic development
* Tourism development

We would also want to be able to consider a building rehabilitation revolving loan program, for both commercial and residential rehabilitation loans. This program would guarantee and reduce the interest on bank loans to property owners, thus enabling the private sector to participate in multiplying the funds available for this effort.

I would also urge the committee to give favorable consideration to the provisions of HB 407 allowing for administrative property tax rollbacks to be adjusted to the base year of the tax increment program. This would enable the community to at least recover a percentage of the tax increments which is so important to our ability to finance local projects.

HB 407 is of vital importance to our agency in Butte and to the ability of the community to see the projects that we have been working towards achieving for two years actually begin to work.

Your consideration would be very much appreciated.

Respectfully submitted,

Hiram Shaw

Hiram Shaw

FIRST NORTHWESTERN BANK
Kalispell, Montana 59901
406/755 5082

BANCO ®

January 29, 1981

Mr. Ken Nordvedt, Chairman
House Tax Committee
State Capitol
Helena, Montana 59601

Dear Mr. Nordvedt:

Presently we are working with the City of Kalispell Community Development Department in a very successful commercial rehabilitation loan subsidy program. The leveraging project, with a public/private partnership agreement is a very important tool in our community's revitalization programs. House Bill #407, with proper planning, involvement of the private sector and authorization from the local governing body, can greatly assist Montana Cities in their community development efforts.

I strongly endorse House Bill #407.

Sincerely,

Stephen P. Olson
Senior Vice President

ms

UPTOWN KALISPELL

KALISPELL DEVELOPMENT CORPORATION • 12 Third Street East • Kalispell, Montana 59901 • Telephone 406-257-7491

January 29, 1981

Mr. Ken Nordtvedt, Chairman
House Tax Committee
State Capitol
Helena, Montana 59601

Dear Mr. Nordtvedt:

The Kalispell Development Corporation endorses House Bill #407. The amendment to the Tax Increment Financing Law will further revitalization of our approved Kalispell Downtown Redevelopment Plan adopted by City Ordinance. The Kalispell Development Corporation was started with initial funding from the membership and other interested community leaders. At the present time we have a successful community development program underway simply because we are involving the private sector in development of land made possible through a HUD Small Cities Grant. Friday of last week, the Mayor dedicated a 42 unit housing project for the elderly and handicapped. This land assemblage was made possible through the City of Kalispell's HUD Small Cities Grant; and the development is now under management from a private developer. This improved project has greatly added to our housing needs and has established a better tax base.

Two lending institutions, First Federal Savings and Loan Association of Kalispell and the First Northwestern National Bank of Kalispell, are working with the Community Development Department in leveraging loans in both the residential and commercial areas; again, positive proof that the public and private sectors definitely can work toward community revitalization. Through Montana's Tax Increment Law, we feel that we have set up the necessary guidelines through the City of Kalispell that would encourage private development and revitalization. We urge the adoption of House Bill #407.

Sincerely,

KALISPELL DEVELOPMENT CORPORATION

Henry K. Good

Henry K. Good,
President

HKG:sm

FIRST FEDERAL SAVINGS AND LOAN OF KALISPELL 202 MAIN STREET • KALISPELL, MONTANA 59901 • (406) 755-7101
P. O. BOX 27

January 29, 1981

Mr. Ken Nordvedt
House Tax Committee
State Capitol
Helena, Montana 59601

Dear Mr. Nordvedt:

First Federal Savings & Loan of Kalispell has, for the past 2 years, entered into a contractual agreement with the City of Kalispell to provide financing for rehabilitation of residential properties. We are proud to say that, as of this date, this program has proven successful - both from the standpoint of the city's community development program and our financial institution. The city, with their HUD Small Cities Grant, is leveraging monies with our savings and loan institutions funds to make low interest loans available for residential units within the city's approved redevelopment area. This public/private financial sector agreement is proving worthwhile and shows that revitalization projects, with the cooperation of local lending institutions and local government, can attain use of a workable program.

I strongly endorse the passage of House Bill 407 because it would provide additional mechanisms for community revitalization through private investment participation with programs that are endorsed with local government approval.

Sincerely,

F. Charles Mercord
President

FCM:jh

P.O. BOX 1035 ZIP CODE 59901

Mayor
Norma E. Happ

THE CITY OF KALISPELL, MONTANA

"IN THE HEART OF THE NATION'S PLAYGROUND"

January 29, 1981

Mr. Ken Nordtvedt
House Tax Committee
State Capitol
Helena, Montana 59601

Dear Mr. Nordtvedt:

May I add my strong support to passage of House Bill #407. The City of Kalispell, by Ordinance, has adopted the Kalispell Downtown Redevelopment Plan. To date we have had a very successful partnership with local lending institutions in our rehabilitation programs; and "The Elm's" housing project was made possible by working with the private sector in utilizing HUD's Small Cities Grant for the intended purpose of Community Development. With a well planned development program, Tax Increment Financing with the proposed amendments, would help Montana Cities to prepare and complete programs with local government approval. May I again urge the passage of this legislation.

Sincerely,

CITY OF KALISPELL

Norma E. Happ,
Mayor

NEH:dkp



VISITORS' REGISTER

HOUSE B & I COMMITTEE

BILL H. B. 395 Date

SPONSOR

NAME	RESIDENCE	REPRESENTING	SUP-PORT	OP-POSE
[illegible]	406 Fuller Helena	Mont. Power Utilities	X	
[illegible]	[illegible]	Northern Plains Resource Council		X
Helen Waller	Circle, MT	" " " "		X
Bill Opitz	Helena	PSC		X
Ed Sheehy	Helena	Retired Federal Employees		X
[illegible]	"	MT.'S POWER TO THE PEOPLE		✓
Toni Kelley	Mt Yellowstone Trail	NPRC		✓
Jim Jensen	Helena	LISCA		X
Tom Schneider	Helena	Montana PSC		X
[illegible] Burke	Butte	Montana Power	X	
[illegible] Meyer	Newark, NY	[illegible]	X	
James Hughes	Helena	Mountain Bell	X	
[illegible]	Helena	HERO		X
[illegible]		[illegible]		X

IF YOU CARE TO WRITE COMMENTS, ASK SECRETARY FOR LONGER FORM.

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Form CS-33
1-81

STATEMENT OF INTENT

The primary purpose of House Bill 395 is the removal of the legal obstacle which has prevented the Public Service Commission's consideration of the merits of the construction work in progress (CWIP) concept. House Bill 395 also is intended to require that the CWIP concept be implemented because of evidence that it can provide significantly lower aggregate utility costs in the long run. depending on interest

There is convincing evidence that the savings to consumers and ratepayers under the CWIP concept are real and significant and that the allowance of CWIP in rate base will lower the rate base of major plant investments made by the utilities of Montana, lower the cost of capital to those utilities, and thus, lower the long-term cost of utility service to existing, as well as, future consumers.

The construction of certain types of utility facilities should be encouraged and the character of others should be recognized for special treatment. Facilities which are not production in nature, such as pollution control facilities, and production facilities which utilize alternative or renewable resources should be encouraged and CWIP treatment can provide an additional incentive for their development and lower costs for their construction.

Facilities which are pollution control related or which utilize alternative or renewable resource technology are appropriately given CWIP treatment because their construction accrues to the general public welfare and CWIP treatment should be accorded in all cases as an incentive and as a means of obtaining lower construction and capital costs.

To carry out these purposes and to assure a fair and proper consideration of the merits of the issue before the Commission on a case-by-case basis, it is appropriate to amend HB 395. The amendment creates three classes of utility construction work in progress that are to be included in utility rate base: pollution control facilities; renewable and alternative energy facilities; and facilities the inclusion of which in rate base is demonstrated to produce lower aggregate costs.

The amendment is intended to require the Commission to follow, in part, the Federal Energy Regulatory Commission's policy by including all pollution control related plant under construction in utility rate base (18 CFR Section 2.16). The Federal Commission has followed this practice since 1976. The federal policy allowing CWIP treatment provides a sound basis for similar treatment by this state's commission.

The amendment also mandates that utility facilities which are alternative or renewable resource in character be accorded CWIP treatment during construction. CWIP treatment for these facilities is justified as a matter of sound policy. The long-term benefits of increased renewable and alternative energy production accrue to the benefit of the general public and should be encouraged by the additional incentive of CWIP treatment.

Finally, ~~as to all~~ other types of utility plant under construction, ~~the~~ this Bill ~~amendment~~ requires CWIP treatment in instances where the utility demonstrates, under such reasonable standards as the Commission may adopt, that the aggregate cost to the consumer of inclusion in rate base is less, over the entire life of the plant, including the remaining period of construction, than the aggregate cost under traditional ratemaking methodology. It is contemplated that the Commission would adopt rules which would establish reasonable criteria that the utilities could follow in presenting evidence which demonstrates the degree of savings produced by CWIP treatment and that such rules would be so drafted as to allow ~~a~~ fair~~, case-by-case~~ consideration of the merits of the CWIP concept.

Exhibit D

COMMITTEE HEARING ON HOUSE BILL 395

Testimony of John J. Burke, The Montana Power Company

My name is John J. Burke. I am Executive Vice President of The Montana Power Company with special responsibility for consumer, government and public affairs. I am testifying in favor of House Bill 395, which is an act to include utility plants in service or under construction within the meaning of "property used and useful for the convenience of the public" or, specifically, to include construction work in progress (CWIP) in utility rate base.

This legislation should be enacted. It provides important benefits for utility consumers because it will result in lower utility rates over the long term than otherwise would be required and because it will help assure reliable service to those consumers.

It is urgently needed to maintain and protect the financial integrity of Montana's public utilities as they enter a period of record-high construction programs and serious problems of raising the capital they must secure to carry out their utility responsibility of supplying their consumers with the best possible service at the lowest possible rates.

Present Regulatory Treatment

Under present regulatory treatment, Montana utilities are not allowed to include construction work in progress in rate base but, instead, record their financing costs incurred to construct a facility as Allowance for Funds Used During Construction (AFUDC). AFUDC, while it provides no cash flow for the utility, is added to the direct costs of construction so that, when the facility is completed, AFUDC goes into rate base along with those direct costs of plant additions. This, of course, increases the cost and rate base of the facility and adds to the revenue required to support the facility when it goes into service. Those revenue requirements then must be borne by the consumer.

Benefits of CWIP in Rate Base Compared with AFUDC

As an example of the benefit to consumers of allowing CWIP in rate base, compared with the capitalization of AFUDC, I show you two tables and graphs which represent the construction cost and revenue requirements of a $450,000,000 plant investment which has a 10-year construction period and a 30-year service life.

You will see that, with CWIP in rate base and no AFUDC taken on the plant, the revenue requirements increase modestly during the construction period and reach their peak in the 10th, or final year of construction of the plant. They then taper off each year thereafter as the plant is depreciated.

With no CWIP in rate base but with AFUDC capitalized at a rate of 10% annually, consumers are not required to support the plant until the 11th year when it goes into service but, in that year, the revenue requirements immediately jump to between $145,700,000 and $163,400,000, depending on the rate of return allowed. Thus, in one year, the revenue requirements under AFUDC are between 1-1/2 and 1-3/4 times the revenue requirements under CWIP, imposing a serious burden on the consumers and ratepayers.

As the graphs demonstrate, the revenue requirements under AFUDC also taper off as the plant is depreciated but they continue to be higher in every one of the 30 years of service life. At the end of 30 years, the consumers will have been called upon to pay out from $544 million to $814 million more in revenue than if CWIP had been used.

<u>Capitalization of AFUDC Increases Plant Cost by 50%</u>

The reason for the increased revenue requirements under AFUDC is that the capitalization of AFUDC and its addition to direct costs of construction increase the overall plant investment cost by more than 50 percent.

With CWIP in rate base, the total plant investment is $450,000,000. With the capitalization of AFUDC, that cost rises to $692,755,000. The comparison is shown in the table and chart entitled: "$450,000,000 Plant Investment - CWIP vs. AFUDC."

<u>AFUDC Provides No Cash Flow, Erodes Quality of Earnings</u>

AFUDC, because it is a noncash item but merely a recording of the utility's financing costs incurred to construct a facility, does not contribute to the utility's cash flow. In addition, its existence as a component of earnings tends to lower the quality of those earnings in the view of investors, making it more difficult for the utility to raise capital at the lowest possible rates and under the best terms and conditions. It is for those reasons that investors may demand a higher rate of return for a utility with substantial amounts of AFUDC reported in earnings but with no opportunity to earn on construction work in progress.

In the past, AFUDC has not been a major factor for The Montana Power Company because construction programs were more modest and interest rates were much lower than they are today. However, with inflation, soaring interest rates and record construction expenditures required to provide needed facilities, AFUDC is becoming a serious problem. Between 1972 and 1980, AFUDC ranged from 2 percent to 7 percent of utility construction expenditures. In the next five years, however, AFUDC interest is anticipated to total $150.6 million or 13.6 percent of a total utility construction program that will be in excess of one billion dollars.

Raising Capital Is a National Problem

The Montana Power Company's outlook for the next five years is one that is shared by the investor-owned utility industry throughout the Nation.

Nationally, the utility industry expects to spend $160 billion in the 1981-1985 period to construct new plant and facilities. This record construction program is about 75 percent of the industry's total net electric plant at the end of 1980. But funds to finance that construction are jeopardized because AFUDC has grown from 12.9 percent of net income in 1969 to 40.1 percent in 1979 and it is estimated that recorded AFUDC in 1980 will be approximately 50 percent of net income.

With record construction requirements and all-time high interest rates, utilities are facing ever-increasing difficulty in marketing their securities, especially as investors recognize that the huge amounts of AFUDC being reported do not represent cash income. This has led to the downgrading of bond ratings with a resulting increase in the cost of capital to the utilities. At least one utility, Arkansas Power & Light Company, recently was forced to pay an interest rate of 16.1 percent --- one of the highest ever borne by a utility --- to sell bonds. In a chaotic market which had caused other utilities to postpone offerings, Arkansas was forced to go ahead because it was running out of cash and had no options remaining.

Allowance of CWIP in Rate Base Is Growing

Since the early 1970's when many utilities began facing cash shortages and began having difficulty raising new capital to finance their construction programs, regulators throughout the Nation have been approving the inclusion of CWIP in rate base in increasing numbers.

The 1979 annual report of the National Association of Regulatory Utility Commissioners (NARUC) shows that 39 of 51 federal and state commissions that regulate electric, gas and telephone utilities now allow CWIP in some form in rate base.

Importance of CWIP to Utility Consumers

Inclusion of Construction Work in Progress in utility rate base is vitally important to consumers because:

1st - The reduction in rate base resulting from the replacement of AFUDC by CWIP saves the consumer millions of dollars by reducing the revenue requirements supporting new plant investment.

2nd - Without CWIP in rate base, the utility must pay interest and dividends on funds used during construction, increasing the total cost of the plant investment so that, when the facility goes into service, consumers, as we have seen, then must pay for both the direct additions to the facility and the long-term interest on funds used during construction.

3rd - Inclusion of CWIP in rate base avoids the enormous revenue impact on consumers which occurs when AFUDC is capitalized and the consumers then are called upon to begin paying costs associated with the facility when it goes into service at the end of the construction period.

4th - Allowance of CWIP in rate base improves the quality of earnings, increases cash flow and enhances the utility's financial standing among investors, thus lowering the risk which goes to the heart of pricing utility securities. This benefits the consumer by lowering the cost of capital and the revenue requirements to service that capital.

Electric rates should reflect the true cost of providing utility service on a "pay as you go" basis and should be structured to produce the lowest cost of service to the consumer, as well as providing investors with a fair return for risking their capital to provide funds for the utility. Utilities must continue to improve their financial integrity in terms of cash flow and quality of earnings if they are to raise capital to assure reliable service at the lowest possible rates for their consumers. Allowance of construction work in progress in rate base enhances both cash flow and quality of earnings with significant benefits to the utility consumer over the long term.

For these reasons, I urge this Committee to vote that House Bill 395 "Do Pass" so that it can become law and provide its benefits to the utility consumers of Montana.

Thank you.

-0-

DEFINITIONS

CWIP - Construction Work in Progress

CWIP is self-explanatory in that it represents the funds that are expended for the construction of a utility plant or facility.

When CWIP is included in rate base, the revenues of existing customers (who are expected to be future customers as well, i. e. customers when the facility is placed in service) are used to support the plant under construction as it is being built and these revenues continue to support the plant after it is placed in service.

When CWIP is not allowed in rate base, the revenues of the existing customers are not required to support the plant until construction has been completed and the plant goes into service.

AFUDC - Allowance for Funds Used During Construction

AFUDC is the recording of a utility's financing costs incurred to construct a facility and, as such, is added to the cost of construction. When the facility is completed, AFUDC goes into the rate base along with direct costs and the utility depreciates AFUDC over the useful life of the facility and earns a rate of return on the undepreciated balance of AFUDC.

During the construction period, the utility reports AFUDC as current income but, as a practical matter, the AFUDC portion is not received as cash in the current period. Cash flows from AFUDC do not occur until after construction is completed and the facility goes into service. Therefore, AFUDC, while it is reported as current income, actually is a noncash item and only represents possible future cash flows.

"Used and Useful" Utility Plant

Over the years, utility regulators usually have applied a "used and useful" criterion to determine how much plant and equipment may be allowed in rate base, normally permitting capital invested in CWIP in rate base only after the facilities under construction became operational.

Since the early 1970's, many electric utilities began facing cash shortages and began having difficulty raising new capital to finance large construction projects. As a means of alleviating this situation, utilities began requesting that CWIP be allowed in rate base, and regulatory commissions have approved these requests in increasing numbers.

In 1974, a Federal Circuit Court of Appeals ruled in favor of allowing CWIP in rate base under the "used and useful" test, pointing out that "funds are not necessarily 'used and useful' only when they are currently invested in completed plants." (Goodman v. Public Service Commission of D.C., 497 F. 2nd 661 /D.C. Cir. 1974/)

WHY CWIP SHOULD BE INCLUDED IN UTILITY RATE BASE

Inclusion of Construction Work in Progress (CWIP) in utility rate base is important for these basic reasons:

1. Electric rates should reflect the cost of providing electricity on a "pay as you go" basis and should be structured to produce the lowest cost to the consumer.

2. A utility must continue to improve its financial strength in terms of cash flow and quality of earnings if it is to raise capital to provide reliable service at the lowest possible rates.

3. A utility's investors are entitled to a fair return for risking their capital to provide funds for the utility.

4. Inflation and regulation have changed the basic nature of investment in utility securities, increasing the importance of CWIP in rate base.

5. The alternative to CWIP, use of Allowance for Funds Used During Construction (AFUDC), is unsound because it is a noncash accounting entry, it does not provide any cash flow to the utility and it lowers the quality of the utility's earnings.

6. Use of AFUDC increases the cost of plant investment and accelerates the rise in the embedded cost of a utility's outstanding capital.

Benefits of CWIP to the Consumer

1. The reduction in rate base resulting from the replacement of AFUDC by CWIP saves consumers millions of dollars. As an example, inclusion of CWIP in the rate base of a $450,000,000 plant investment reduces the revenue requirements of that plant by at least $543,615,000 over the 40-year construction and service life of the plant.

2. Without CWIP in rate base, the utility must pay interest and dividends on funds used during construction, increasing the total cost of the plant so that, when the plant goes into service, consumers then must pay for both the plant and the long-term interest on funds used during construction.

3. CWIP improves the quality of earnings, cash flow and a utility's financial standing among investors, thus lowering the risk which goes to the heart of pricing the utility's securities and benefiting the consumer by lowering the cost of capital and revenue requirements to service that capital.

4. Use of CWIP avoids the enormous impact on consumers which occurs when AFUDC is used and consumers are called upon to begin paying costs associated with the plant when it goes into service. Inclusion of capitalized AFUDC in a $450,000,000 plant investment increases revenue requirements by $122,000,000 to $140,000,000 in the plant's first year of service life.

5. Conversely, use of CWIP in rate base produces a much smaller initial rate increase during construction and, when the plant goes into service, its costs are reduced over its service life and the impact of rate increases on the consumer is much smaller.

Benefits of CWIP to the Utility

1. Use of CWIP in rate base improves cash flow, providing dollars for construction and reducing the amounts of money the utility otherwise would have to borrow.

2. Future capital costs are reduced because the investment quality of the utility's securities is enhanced, providing a more receptive market and enabling the utility to borrow funds at lower rates and under better terms and conditions.

3. CWIP enables the utility to build the needed facilities required by its consumers, thus reducing the risk of being forced to delay construction of facilities that are necessary to provide reliable service to its consumers now and in the future.

4. Use of CWIP facilitates the financing of pollution control equipment, thereby enhancing the quality of the environment, a factor that has led the U. S. Environmental Agency (EPA) to support CWIP and the Federal Energy Regulatory Commission (FERC) to allow it in rate base, for that purpose.

Summary

CWIP in rate base enables utility consumers to pay a lower long-term total bill than would be required under the AFUDC concept and minimizes the impact of increased revenue requirements in each year of a facility's service life.

CWIP facilitates the construction of generating facilities and other plant necessary to supply existing and future consumers.

CWIP reduces the amount of capital required by a utility and improves its ability to maintain and improve the quality of service.

CWIP improves the quality of a utility's earnings, providing it with a better environment among investors and enabling it to obtain capital funds from the marketplace at lower rates and under better terms and conditions.

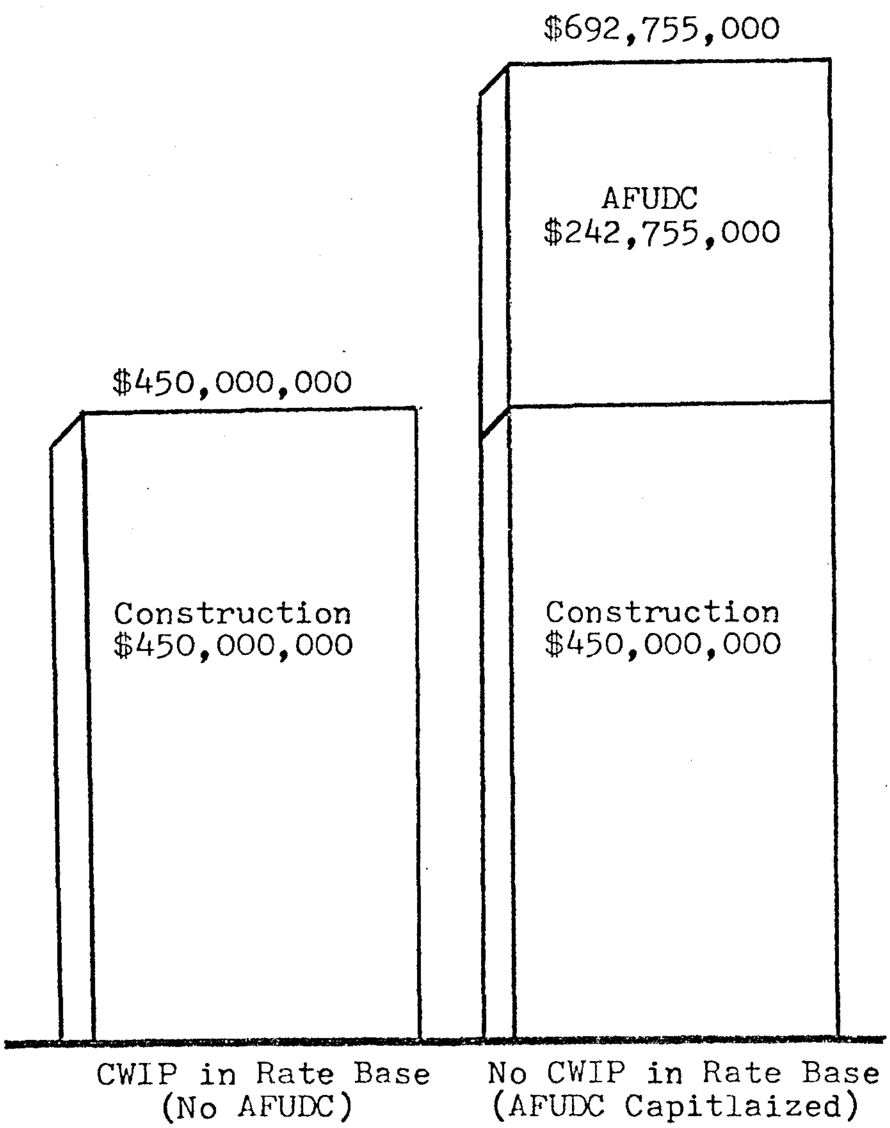
By improving the overall economic health of a utility, CWIP benefits both the utility's consumers and investors.

-0-

$450,000,000 PLANT INVESTMENT - CWIP VS. AFUDC

Construction Schedule	Plant Additions	AFUDC (1)	Additions + AFUDC Cumulative
Year 1	$ 5,850,000	$ 585,000	$ 6,435,000
2	9,000,000	1,544,000	16,979,000
3	14,850,000	3,183,000	35,012,000
4	21,150,000	5,616,000	61,778,000
5	45,000,000	10,678,000	117,456,000
6	75,150,000	19,261,000	211,867,000
7	138,150,000	35,002,000	385,019,000
8	86,850,000	47,187,000	519,056,000
9	48,150,000	56,721,000	623,927,000
10	5,850,000	62,978,000	692,755,000
	$450,000,000	$242,755,000	

(1) - AFUDC capitalized at 10% annually, compounded.



ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION (AFUDC)

Allowance for funds used during construction (AFUDC) is the recording of a utility's financing costs incurred during construction of a facility (see "Definitions"). AFUDC is added to the total cost of the plant investment, increasing the cost and rate base once the plant is in service. It is reported as current income in the utility income statement, either as "other income" or as a reduction of interest expense, but it is not received as cash in the current period.

Because it is a noncash item, AFUDC does not contribute to internal cash generation or cash flow, and its existence as a component of earnings tends to lower the quality of those earnings in the view of the financial community and investors. The latter disadvantage is becoming more and more crucial as utilities seek to borrow funds to undertake record construction programs required to provide reliable service for their consumers.

In the past, AFUDC has not been a material factor for The Montana Power Company, but, with inflation and soaring interest rates coupled with record plant investment, it will become a serious problem in the future just as it is becoming a more serious problem for the entire electric utility industry.

Following are the ratios of AFUDC to utility construction for the 1972-1980 period and the current forecasts to 1985 as they relate to Montana Power:

Utility Construction

	Direct Costs	AFUDC (a)	Total with AFUDC	AFUDC as % of Total
1972	$ 23,009,000	$ 506,000	$ 23,515,000	2.15%
1973	44,291,000	1,193,000	45,484,000	2.62
1974	70,480,000	3,830,000	74,310,000	5.15
1975	93,049,000	7,084,000	100,133,000	7.07
1976	62,107,000	3,827,000	65,934,000	5.80
1977	46,001,000	1,411,000	47,412,000	2.98
1978	52,725,000	2,562,000	55,287,000	4.63
1979	54,803,000	3,926,000	58,729,000	6.68
1980(b)	102,987,000	7,513,000	110,500,000	6.80
1981 Est.	196,700,000	18,100,000	214,800,000	8.43
1982 "	212,300,000	35,200,000	247,500,000	14.22
1983 "	186,700,000	49,500,000	236,200,000	21.00
1984 "	166,300,000	25,000,000	191,300,000	13.07
1985 "	193,600,000	22,800,000	216,400,000	10.54

(a) - Divided between allowance for funds used during construction (AFUDC) and allowance for borrowed funds used during construction (ABFUDC) since 1977.

(b) - Preliminary.

NOTE: AFUDC is taken on all projects which require $100,000 or more of direct investment and have a construction period of at least 60 days.

AFUDC RATE - THE MONTANA POWER COMPANY

The AFUDC rate used by the Company in each year is dictated by the cost of capital so that, in the recent period, the soaring cost of debt and the record high levels of interest rates have a severe effect on the rate used. Montana Power's historical and estimated AFUDC rates are as follows:

1972 -	7.00%	
1973 -	7.00%	
1974 -	7.00%	
1975 -	7.00%	
1976 -	7.00%	
1977 -	8.50%	
1978 -	8.50%	
1979 -	12.00%	
1980 -	13.00%	
1981 -	12.00%	Preliminary
1982 -	12.00%	"
1983 -	12.00%	"
1984 -	12.00%	"
1985 -	12.00%	"

REGULATORY ALLOWANCE OF CWIP AND AFUDC IN RATE BASE

The 1979 annual report of the National Association of Regulatory Utility Commissioners (NARUC) shows that 39 of 51 federal and state regulatory commissions which regulate electric, gas and telephone utilities allow CWIP in rate base in some form.

CWIP is allowed in some cases without restriction; in others, it is allowed on a discretionary basis or for specific facilities and under specific conditions.

Survey responses of 51 commissioners, including the Federal Energy Regulatory Commission (FERC) and 50 state commissions shows the following breakdown insofar as inclusion in rate base is concerned:

CWIP only allowed in rate base	8
AFUDC only allowed in rate base	12
Both CWIP and AFUDC allowed in rate base	31
	51

-0-

CWIP VS. AFUDC FOR $450,000,000 PLANT INVESTMENT

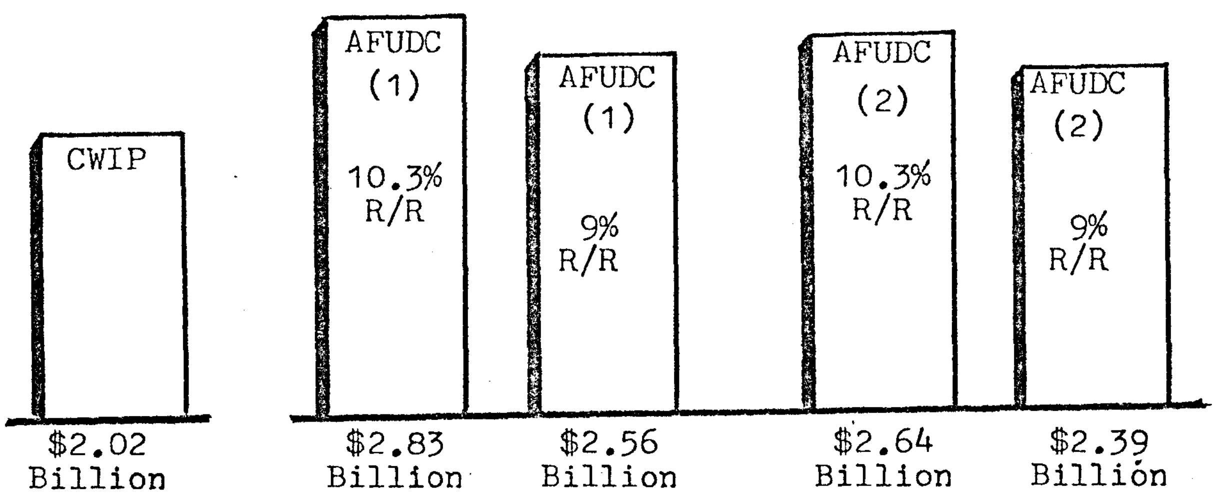
Comparison of 40-Year Revenue Requirements

Opponents of CWIP in rate base will argue that the use of AFUDC in lieu of CWIP will provide a lower revenue impact, but that argument is not valid, as indicated by the tables and graphs which compare the two concepts for a $450,000,000 plant investment which has a 10-year construction period and a 30-year service life.

The argument also may be used that AFUDC interest should not be compounded although, unless interest is compounded, the utility can not recover the costs associated with constructing and financing the plant investment because it has, during the construction period, a continuing cost of investment and borrowed money.

However, as the following bar charts demonstrate, allowance of CWIP in rate base for the $450,000,000 plant results in a lower revenue requirement over the 40-year construction and service life of the facility than the use of AFUDC on any basis of comparison:

Revenue Requirements



(1) - AFUDC at 10% annually, compounded.
(2) - AFUDC at 10% annually, interest not compounded.

NAME JAMES R. HUGHES BILL No. HB 395

ADDRESS 2020 WINNE HELENA DATE 2-11-81

WHOM DO YOU REPRESENT MOUNTAIN BELL

SUPPORT X OPPOSE AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

NAME [illegible] BILL No. [illegible]

ADDRESS [illegible] DATE [illegible]

WHOM DO YOU REPRESENT [illegible]

SUPPORT ✓ OPPOSE ______ AMEND ______

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

Exhibit E 395

PRICING ELECTRIC & GAS SERVICE

TO REFLECT CURRENT COSTS

WILLIAM C. GLYNN

VICE PRESIDENT, TREASURER AND CHIEF FINANCIAL OFFICER

MONTANA-DAKOTA UTILITIES CO.

BEFORE

THE HOUSE BUSINESS & INDUSTRY COMMITTEE

STATE OF MONTANA

FEBRUARY 11, 1981

In order to survive, business must price its product so that it at least recovers its costs. In non-regulated industries the businessman is permitted to timely adjust his prices to reflect current economic conditions because his pricing is subject to the forces of the free market. In regulated industries, like the public utility industry, where all the forces of the free market are not present, the United States Congress and State Legislatures like this body have established regulatory agencies which are intended to be a substitute for the free market forces that are not otherwise present.

Montana-Dakota Utilities Co. is not here today in pursuit of legislation that would change the intent of that initial legislative act, nor is it seeking decontrol of the prices charged its customers for gas and/or electric service in Montana. Rather it is before you today to seek legislation that will give the regulator the tools it needs to respond to the problems facing the utility industry. The expression of the legislative intent that is contained in the bill before you is critical if the utility industry is to survive in Montana. While the difficulties of the utility industry are many and varied, these difficulties can be summarized into one statement of need: <u>Our product, natural gas and electric service, must be priced so as to reflect current costs, and mechanisms must be put in place that will enable the utility to recover these costs currently through the regulatory process</u>.

Our business like our lives is becoming increasingly more complex and largely as a function of someone else's actions. It is these in increased complexities, including the effects of actions by others, that has made it difficult for the industry and the regulator to adjust prices on a timely basis so that the price of our product to our customer does in fact reflect current costs. Legislation and legislative intent that was satisfactory historically is no longer adequate given these increased complexities. For example, up until the past few years the cost of our basic product, natural gas, was very stable and therefore predictable. Inflation was also at manageable levels. In recent years however, and because of an action by the United States Congress, natural gas prices have and will continue to escalate rapidly. There is no need to dwell on what inflation has done to all of us and to the cost of the goods and services a utility must buy in order to supply service to its customers. In large part then, the cost increases we incur to provide the service rendered are not directly controllable by the Company or the utility industry. Rather, they are the consequences of congressional action and inflation.

What we as a company and our regulators perceived to be "current costs" in years gone by are no longer current costs. For example, several years ago experienced historical costs were in fact indicative of "current costs." Thus the very common method of using historical costs as indicators of "current costs" for purposes of setting rates charged utility customers was reasonable. As was illustrated earlier, this is no longer the case. The complexity of issues now facing the utility and its regulator has also increased due in part to the passage of federal legislation that requires the industry and the regulator to reexamine historical ratemaking policies and standards and implement new policies as appropriate. These matters are complex and require a great deal of time for study by both the industry and the regulator. It is therefore the combination of increased business and regulatory complexity in a rising cost environment that has caused our prices to be <u>not reflective</u> of current costs. For example, the prices being charged for natural gas today in Montana by Montana-Dakota Utilities Co. are reflective of plant invested as of June 1978 and operating cost levels experienced in 1979.

This very basic problem of not having our prices reflect current costs, but in fact costs experienced 2-3 years ago, has caused Montana-Dakota Utilities Co. to lose money (not meet expenses) in each of the last four years as a result of supplying natural gas service to Montana customers. For example, those pretax losses were $3.1 million in 1977, $4.0 million in 1978, and $2.8 million in 1979. While 1980 information is not yet final we do know that we lost money in 1980 as well. These losses were experienced at the same time the regulator was finding through the public hearing and review process that the company was entitled by law to earn approximately $5 million a year in pretax income. With these kinds of losses being experienced, it is readily apparent that the problem is serious. Serious to the point that action must be taken to change the results that have been experienced by our company. <u>No business can long continue to sustain losses</u>.

The legislative proposals brought before you will give both the utility and the regulator more tools to deal with the complex questions that must be addressed such as the equity of pricing among customers and pricing structures that will cause the customers to use the product more wisely. Our request of you is simple, your action perhaps will be more difficult. We ask that you give the regulatory agency the tools it needs in the form of legislative action as contained in bills that have come before this legislature this past week and again here today. This type of action will cause the utility and the regulator to be able to price the product to the customers based upon current costs and at the same time cause more time to be spent on other issues facing our industry and the state of Montana.

Montana-Dakota Utilities Co. finds itself in a position of severe financial stress brought about primarily by the large, continuing and growing losses it has experienced in its natural gas operations in Montana over the past four years. The company is presently unable to sell mortgage bonds to raise the money it needs to maintain its present level of service in Montana and to extend service to new customers. The impact of this critical situation will begin to be felt by the Montana customer in 1981.

The body of laws within which the Montana regulator operates and the policies and regulatory precedence that have evolved from such laws are no longer responsive to the economic conditions in which we find ourselves, nor do they permit the timely response that is absolutely essential if the public utility industry in Montana is to survive. If the energy delivery systems in Montana can no longer meet the requirements of its citizens, the economic future of the state is bleak.

Montana-Dakota Utilities Co. began its business in Glendive in 1924 and is proud to have served the people of Montana with utility service these past 56 years. We desire to continue to provide that service into the future, but as you can appreciate, we cannot do that if we do not change the course we are currently on.

Thank you for your careful consideration of the facts presented in this statement and of the proposed legislation before you.

NAME ______________________ BILL No. __________

ADDRESS ______________________ DATE __________

WHOM DO YOU REPRESENT ______________________

SUPPORT __________ OPPOSE __________ AMEND __________

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

NAME Dennis Loosch BILL No. 395 431

ADDRESS Arcade Bldg DATE 2/11/81

WHOM DO YOU REPRESENT Mountain Water Co

SUPPORT X OPPOSE AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

#122

NAME James C. Paine BILL No. 395 & 431

ADDRESS 34 W. 6th Ave DATE 2-11-81

WHOM DO YOU REPRESENT Montana Common

SUPPORT OPPOSE X AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

REGARDING: HOUSE BILL 395 - Charging rates for construction work in progress

Some perspective can be gained from looking at the Washington Public Power Supply System (WPPSS). WPPSS is building five nuclear generating units. Of these, the first is scheduled to commence operation in the Fall of 1983 - Its original completion date was scheduled for September, 1977!

BPA and other utility consumers are paying right now for the first three plants (which are still being built). These CWIP rate charges were responsible for the unprecedented 88% BPA rate hike in December, 1979. BPA's rates are expected to rise an additional 400% by December, 1986, including a 50% rate hike scheduled for this coming July. These massive rate hikes are for plant that is not yet in service.

The total cost of WPPSS plants 1-5 is currently $46.5 BILLION (and rising) This price tag has increased 81% in the past two years! Right now the WPPSS price tag amounts to $1,000 per year for the next 30 years for the average family of four in Washington.

Source: Joel Connelly, reporter for the SEATTLE POST-INTELLIGENCER

NAME George F Hess BILL No. 395 & 431

ADDRESS 3601 Park Center Blvd Minneapolis Minn 55416 DATE

WHOM DO YOU REPRESENT Montana Consumer Council

SUPPORT OPPOSE X AMEND

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

NAME Bill Opitz BILL No. HB 395 & 431

ADDRESS 2 Wood Ct Helena DATE Feb 11, 1981

WHOM DO YOU REPRESENT PSC

SUPPORT ______ OPPOSE X AMEND ______

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

NAME ED SHEEHY BILL No. 395 & 431

ADDRESS 1731 5th Helena DATE 2-11-81

WHOM DO YOU REPRESENT Retired Federal Employees

SUPPORT ______ OPPOSE X AMEND ______

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

Exhibit F

PV of No CWIP in Rate Base - AFUDC Capitalized
10% Disc. Rate

6	168,118	x	.56447	=	94,898
7	157,190	x	.51316	=	80,664
8	146,260	x	.46651	=	68,232
9	135,330	x	.42410	=	57,393
10	124,402	x	.38554	=	47,962
11	113,473	x	.35049	=	39,771
12	102,544	x	.31863	=	32,674
13	91,614	x	.28966	=	26,537
14	80,684	x	.26333	=	21,247
15	69,757	x	.23939	=	16,699
					$486,077

CWIP in Rate Base - No AFUDC Capitalized (10%)

yr.					
1	14,000	x	.90909	=	12,727
2	28,000	x	.82645	=	23,141
3	42,000	x	.75131	=	31,555
4	56,000	x	.68301	=	38,249
5	70,000	x	.62092	=	43,464
6	116,500	x	.56,447	=	65,761
7	109,500	x	.51316	=	56,191
8	102,500	x	.46651	=	47,817
9	95,500	x	.42410	=	40,502
10	88,500	x	.38554	=	34,120
11	81,500	x	.35049	=	28,565
12	74,500	x	.31863	=	23,738
13	67,500	x	.28966	=	19,552
14	60,500	x	.26333	=	15,931
15	53,500	x	.23939	=	12,807
					494,120

points to the answer. Conservation of energy, says Yergin, simply lacks glamour. The measures needed for a broad energy-conservation program are neither new nor dramatic, but merely plain, common-sense applications of things we already know. Scattered in countless nooks and crannies of the economy—a quad saved here by caulking windows, another saved there by not building 20 power plants—they are not easily packaged into the kind of narrowly focused "hard-hitting program" that sells in Washington. Moreover, unlike the expensive new programs now being pushed for various synthetic fuels, there is no lobby behind these conservation approaches. Who, for instance, has heard of a pro-co-generation lobby or an anti-conversion-loss lobby?

So the root cause of our present floundering is clearly political rather than technological. Pushed and pulled in a variety of directions, neither Congress nor the Administration has focused on what their own experts are telling them is the best way out of the maze. Here are some suggestions for how—at a fraction of the cost of starting up alternative energy sources—Washington could begin exploiting the one source that's under its nose:

- Conduct a massive advertising-and-education campaign to give the public the *specifics* of how it can voluntarily contribute to a national energy-conservation effort. If this doesn't suffice, impose measures to compel public participation—such as higher gasoline taxes, lower oil-import quotas, etc.
- Accelerate the move toward a national retrofitting program for homes and factories. This would involve much stronger programs than now exist for providing energy-efficient building codes and appliance efficiency standards, and for encouraging the upgrading of buildings with government loans and tax write-offs.
- Revise state and federal regulations that inhibit such things as co-generation and trucking efficiency.
- Conduct a massive research effort to find ways of reducing the huge conversion-loss drain by substituting modern technologies for obsolete ones.

John Gibbons, director of Congress's Office of Technology Assessment, and head of the NAS study on energy conservation, sums up the opinion of almost everyone who has examined its potential: "We're now at a true watershed in the energy debate. Up to now we've been taking the same approach to the problem America has always followed when faced with a shortage in any part of its economy: produce more. Our dilemma has been that, for the first time in our history, we've discovered we can't get more production by turning up the old spigots. But now we've found a new spigot with a very large supply, and as soon as we begin turning it on we'll be on our way out of the dilemma."

REPRINTED FROM THE JUNE 1980 ISSUE OF READER'S DIGEST

A Reader's Digest REPRINT

The Energy Crisis: There Is an Easy Answer

While the nation wrestles with finding ways to produce more energy, we're ignoring the real solution—a massive drive by individuals and government to plug the myriad holes in our energy-wasteful economic machine. The experts are convinced it can be done. What on earth are we waiting for?

BY JAMES NATHAN MILLER

A MOMENTOUS QUESTION is now beginning to surface in Washington, one that could profoundly alter America's future: Is it possible that the country already possesses an easily available source of energy large enough to give it all the fuel it will need in the foreseeable future, while at the same time freeing it from its present crippling dependence on foreign oil producers? There's growing evidence that the answer is yes.

A mass of studies has been pouring out of universities and research institutions—Princeton, the University of California, Harvard, Cornell, the National Academy of Sciences, the Ford Foundation and many others—all pointing to the same source: the energy the United States is now allowing to leak through a million holes in its economic machine. Last year, in a widely praised report, the Harvard Business School said that reclaiming this waste will give us "the cheapest, safest, most productive energy alternative readily available in large amounts, the equivalent of the elimination of all imported oil—and then some."

Early this year a massive analysis of the energy crisis by the National Academy of Sciences (NAS) zeroed in on the same source. By eliminating the machine's unnecessary leakage, NAS reported, America would be able to cut its energy consumption by 25 percent while *doubling* its economic output over the next 30 years.

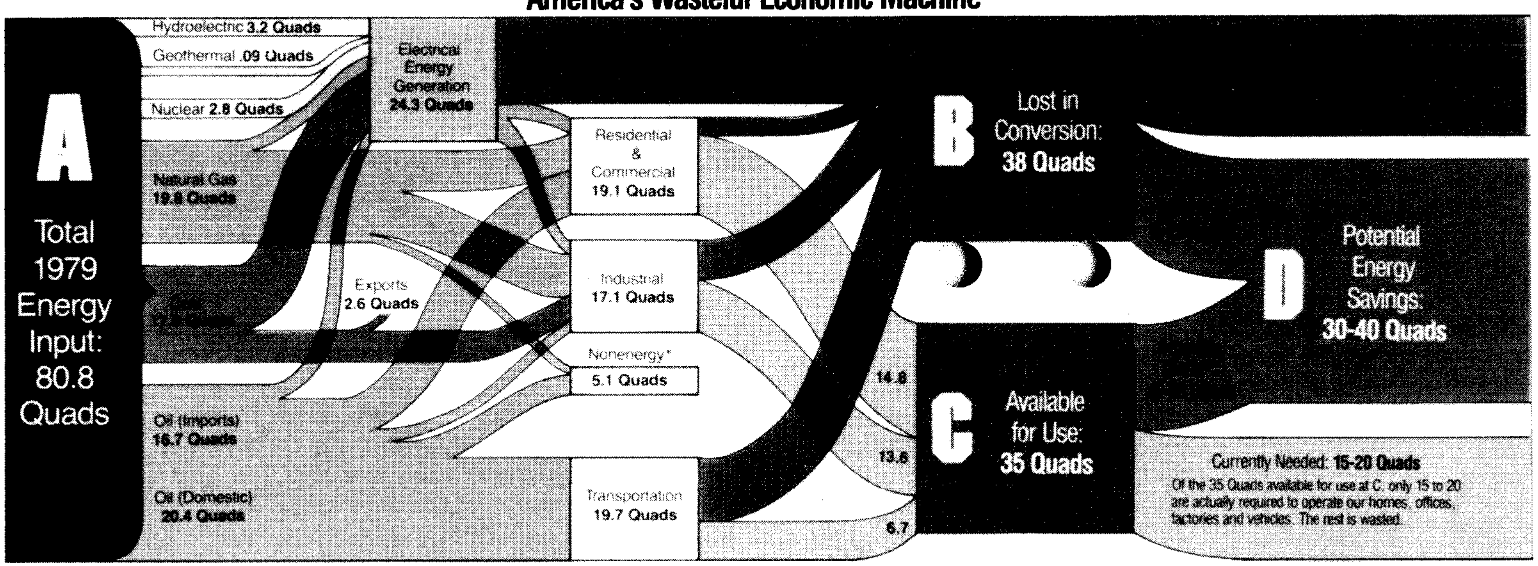
If such claims are valid, the implications are staggering: stated very simply, all the country has to do to solve its most serious domestic and international problem is to use its existing fuels more efficiently. To understand the basis of the startling new optimism, begin with the chart below. The critical figure to keep in mind as you study this chart is the number 80.8, shown under "A." That's how many quads of energy the United States fed into its economic system last year.*

The chart shows, first, how these 80.8 quads—most of them from our three main fuels: oil, coal and natural gas—were divided up among the four main users. It then shows how the fuels emerged from the machine in two streams: at "B" in the form of useless heat, and at "C" in the form of usable heat, light and motion.

Ever since the 1973 Arab oil embargo, the national debate on the energy crisis has focused futilely on "A"—specifically, on how to increase the machine's input by finding new fuels to substitute for oil. But now, by focusing on the output end of the machine—at "B" and "C"—the experts say they've finally found the bonanza they've been seeking.

*A quad—the unit of measurement economists use when they're talking global supply and demand—is a quadrillion (1,000,000,000,000,000) British thermal units (Btu's) of energy. Twenty Three Mile Island-sized nuclear plants generate just one quad of electricity a year. It takes 170 supertankers to haul one quad of oil. The nations of the world supply all their energy needs on about 250 quads a year.

America's Wasteful Economic Machine



Source: The Center for Strategic and International Studies, Georgetown University

*Plastics, fertilizers, etc.

**Estimates differ widely as to the specific amounts of energy that can be recovered from B and C. The overall figure given at D for potential energy savings is based on the National Academy of Sciences forecast for the year 2010.

Part of it would be obtained from "B," by reducing a monstrous leak in the machine that up to now everyone has considered irreducible: the 50-percent drain caused by the system's so-called "conversion losses." The other source of recoverable waste is shown at "C": the energy we squander through inefficiencies in our homes, cars and factories.

Detailed engineering studies indicate that the energy potentially recoverable from these two sources adds up to the hard-to-believe total of between *30 and 40* quads a year. That's almost half our total current energy consumption. It's also *twice* what we now import in oil, and equal to all the coal and natural gas we currently use.

Are these breathtakingly hopeful estimates truly realistic? Or are they—like so many other claims in the energy debate—based on dreams of wildly expensive, far-off technological "breakthroughs"? To judge for yourself, take a closer look at the three major areas of energy use:

Residential & Commercial

THE SQUARE labeled Residential & Commercial represents our homes and offices. Between them they consumed 19.1 quads of energy last year. Researchers have shown that about half of this energy was wasted because of simple, correctable inefficiencies.

The biggest leakage is through crevices around uncaulked and loose-fitting windows and doors, as well as through hidden air passages.* Together, these deficiencies make the average house a vast network of large and minuscule drafts of heated air moving to the outside. The next biggest heat loss is the imperceptible migration of heat through inadequately insulated walls and attics. Nationally, the researchers have found that up to three-quarters of U.S. homes are inadequately insulated, and between 10 percent and 20 percent have no insulation at all.

How inefficient does this make them? Two years ago in Arkansas, a power company persuaded local contractors to build 800 houses to

*Called hot-air bypasses, these leaks occur inside walls, up staircases, and around chimneys and electrical wall outlets.

the highest possible standards of insulation and weatherstripping, then compared their energy consumption with similar houses in the same area that had been built conventionally only three years before. The tightly built houses had heating and cooling bills *72 percent* lower than those of the conventional structures.

Office buildings are even worse; per square foot of floor space, they consume 40-percent more heating energy than do homes. Many offices seem specifically designed to waste energy. A large number have permanently sealed windows, requiring 24-hour-a-day air conditioning throughout the summer (year-round in the Sun Belt states). Office-lighting levels are often far too bright, and lighting systems are often controlled by one switch in the manager's office—which is why you frequently see 20- or 30-story buildings ablaze with light as the night cleaning crews move from office to office.

Furnaces, water heaters and other appliances are similarly inefficient. Most furnaces vent 20 to 30 percent of their heat up the chimney, though a simple flue damper could prevent as much as 40 percent of the loss. The air conditioner, refrigerator and dishwasher in the average American home consume about twice the electricity they actually need to do the job. Almost all electrically heated houses depend on the grossly wasteful method called resistance heating (in which metal coils get hot from their resistance to the electricity passing through them) rather than the far more effective "heat pump" principle, which generates two to three times as much heat from the same amount of electricity.

All this adds up to a correctable loss of around ten quads a year caused by the way our buildings are built and operated. How did we get into such a mess? There's a perfectly logical—and even economically sound—reason. When most of America's houses and offices were built, heating oil cost 10 to 15 cents a gallon. It's now at a dollar and climbing fast. In those days the average single-family dwelling could be kept comfortable for $150 to $200 a year. Today's figure is over $1000. In fact, in those days the term "energy cost" didn't even exist. Labor and materials were the costs economists and businessmen worried about. Thus, with good reason, builders invested a minimum of effort in making their structures energy-efficient. And today we're paying the price.

How do we get out of the mess? First, we must adopt new building codes requiring all new construction to incorporate the best energy-saving technology. (The Department of Energy is drafting such a code.) Second—and even more important—we must conduct a national "retrofitting" campaign, using government loans and tax incentives to get owners to upgrade existing structures. (Sweden and the Netherlands have each committed $200 million a year to massive retrofitting programs designed to make all their houses energy-efficient by 1992.)

What would such a program cost the country? Depending on how elaborate it was, the national price tag would be between $25 billion

and $100 billion. But study after study has shown that homeowners—who would spend an average of $1500 on improvements—would save far more through lower fuel bills. A relatively modest program, says the NAS, would cost $29 billion and save $64 billion. How long would it take? About 30 years. How many quads would it save? Without such a program, estimates the NAS, by the year 2010 home-and-office energy consumption (including energy lost in the conversion to electricity) would rise from its present 29 quads annually to 41 quads; with the program, it would drop to 22 quads. That would be a saving of 19 quads—*20-percent more energy than is contained in present U.S. oil imports.*

Industrial

Now LOOK at the user box marked Industrial. It tells precisely the same story. Examples of waste in a typical factory range from squandered steam in boilers to energy-wasting motors powering conveyors and low-efficiency lights in the parking lot. Now—because ten-cent energy has become $1 energy—factory managers are being forced to worry about fuel bills. And they're finding the same kind of opportunities that homeowners have found:

- General Motors says that in a single year, 1977, it was able to knock $165 million from its anticipated $991-million energy bill through aggressive energy management.
- A Pepsi-Cola canning plant in Watertown, Wis., has reduced its natural-gas consumption 40 percent by burning old wood pallets, paper boxes and other material it used to throw away. Its new incinerator eliminates previous garbage-disposal costs, heats the plant, provides all the hot water needed for its two canning lines, and is expected to pay for itself in three years.

Until a couple of years ago, economists believed that the size of the nation's energy input was directly coupled to the size of its output of goods and services, and that it was impossible to cut the former without cutting the latter. Events have proved them flatly wrong. From 1973 to 1978, industry reduced its energy use by ten percent—about a quad's worth—while it turned out 12-percent *more* goods and services.

Transportation

THE SQUARE marked Transportation shows another big leak in the system, one caused by America's world-famous love affair with the automobile. Private cars consume ten quads of energy a year, *60 per cent* of our total oil imports. Can we do anything to lower this figure? It looks as if we can, and sooner than anticipated. Consider:

Today's national 110-million-car "fleet" averages 14 miles to the gallon. Federal law says that by 1985 manufacturers must produce cars averaging twice that mileage, 27.5 m.p.g. Doubling the fleet's efficiency—whether it happens by 1995 (as most experts have predicted) or sooner (as current buying trends indicate)—will save five quads a year.

But that's only the beginning. A 50-cent-a-gallon tax on gasoline (with some form of rebate to the poor), along with the price increases already forecast, could save a quad. A quad could be recovered if Americans would improve their driving habits and keep their car engines tuned and tires properly inflated. Another way a quad could be saved would be through a gas-rationing plan aimed at cutting driving by ten percent (three miles a day for the average driver). Critics say, however, that the possibilities for fraud and bureaucratic foul-ups would probably sink such a plan.

The trucking industry is another ripe target. Present government regulations force a large number of trucks to take roundabout routes on long-distance deliveries and to return from them empty; abolishing these rules would produce a huge energy saving. So would modification of present railroad-rate regulations that discourage long-distance "piggybacking" of loaded trailers on railroad flatcars.

In all, it's a fair guess that between eight and ten quads of energy loss in the transportation system could be eliminated simply by making cars, drivers and driving laws more energy-efficient.

Recovering "Conversion Losses." Now look at "B" on the chart. This is where over half of America's energy is funneled off to something called "conversion losses." In a purely engineering sense, these losses cannot be considered "waste"; they result from fundamental laws of physics, which decree that when you convert one form of energy (coal, say) into another (electricity, say), part of the original energy will inevitably be lost to such factors as friction and heat absorption in the turbines and boilers that make the conversion. Even with the best engineering, these losses are enormous. The typical generating plant can convert only about one-third of the energy in its fuel into electricity delivered to users. The rest—an appalling 17.2 quads last year—disappears up the plant's cooling towers or into our rivers in the form of (polluting) waste heat. Cars are worse; even with the most efficient drivers, they deliver less than 15 percent of the energy in the gas tank to the wheels.

For one solution to the problem, observe the Atlantic Gelatin Division of the General Foods Corp. in Woburn, Mass. Like thousands of other manufacturers, Atlantic needs both steam and electricity in its manufacturing process. Until recently it had its own boiler for steam generation, but bought its electricity from Boston Edison.

Then the oil embargo hit, and within two years Atlantic's annual electricity bill shot from $250,000 to $1 million. So in 1975 the company hooked up an electric generator to its boiler and began producing its own electricity, piping the "waste" steam into its production lines. It's now paying about a third as much as before for its electricity—an arrangement that's expected to pay for the cost of the generator in 3½ years.

This process, called "co-generation," can produce electricity and steam about twice as efficiently as two separate boilers. It's been widely practiced in Europe for years, not

only in factories but by municipalities and big housing complexes as well. (In Germany and Sweden, builders of new power plants are *required* to find uses for waste heat.) But in the United States it's hardly used at all; in fact, public-utility laws discourage it. One estimate is that if the laws were changed (as several states are now doing) and industry decided to go heavily into co-generation, within five years it could save six quads a year of this now-wasted energy—and cancel the need for *120* generating plants the size of Three Mile Island.

But co-generation is only one way to escape conversion losses. At Cornell University, researchers studied the economics of a proposed upstate New York power plant that's planned principally to meet the area's growing need for home heating. The study indicated that the houses could be heated far more efficiently by turning to a new energy source—and not building the plant at all. What new source? For 30 percent of the plant's dollar cost—and using less than five percent of the energy it would consume—the same amount of "heat" could be supplied by retrofitting existing homes and ensuring that all new housing is built to top insulation standards.

Could such a far-out concept actually work? It already *is* working. Two years ago, Oregon's Pacific Power and Light Company made its customers a remarkable offer: the company would retrofit all electrically heated houses. The company would give owners interest-free loans that didn't have to be paid off unless an individual owner sold his house. Ten thousand customers signed up, and PPL has so far spent $8.5 million ($1400 per home) on the upgrading job. According to the company's initial calculations, the houses have reduced their electric-heat consumption by 45 percent, which has given PPL 33 million extra kilowatt-hours to sell to other customers. Moreover, its $8.5-million investment is only *25 percent* of what it would have had to spend to get the equivalent amount of electricity by building a new power plant.

A New Spigot. What does it all add up to? If the National Academy of Sciences is correct—if, that is, the country can cut its energy use by one-fourth while doubling its production—it means that there are *at least* 30 to 40 quads of recoverable waste in the system, and perhaps considerably more. The implication of such figures is clear and startling: the government's current energy program is on the wrong track. Instead of committing hundreds of billions of dollars to the crash development of unproven and controversial sources of new energy, Congress and the Administration should focus on this enormous, proven, cheap source, which we can start tapping immediately. This would buy us precious extra time for prudent development of the new fuels and technologies we will need during the next century.

If the best and quickest solution is so easily within our grasp, why has Washington been ignoring it—or at best giving it lip service? Daniel Yergin, co-director of the Harvard Business School's Energy Project,

Exhibit 9 1

TESTIMONY BEFORE THE HOUSE BUSINESS AND INDUSTRY COMMITTEE
Helen Waller, Chairman, Northern Plains Resource Council
February 11, 1981

Opposing House Bill 395

Mr. Chairman, my name is Helen Waller and I am testifying today on behalf of the Northern Plains Resource Council of which I am chairman.

NPRC opposes House Bill 395. Construction work in progress represents a serious threat to the consumers' pocket-books by promoting inefficiency, poor planning and bad forecasting. It insulates managers of regulated energy industries not only from their mistakes, but from the realities of the energy market place as it exists today. Under this rate policy, a utility reaps only profits, regardless of the quality of their management and planning. It is a no-lose situation for the utility, and a no-win situation for the consumer.

In the long run the users of energy pay an additional high cost when construction work is placed in the rate base: That is the cost of buying the most expensive energy around, whether it be electricity from new thermal plants or synthetic natural gas, without having the option of shopping around for the best buy. These products - thermal electricity and synthetic natural gas - are already behind in the market place when diredtly competing with the alternatives.

For example:

According to a major study done for the Bonneville Power Administration by Skidmore, Owings, and Merrill, increasing energy supplies by conservation or end-use efficiency measures is 6 to 10 times less expensive than building new electric plants. This is not "freeze-in-the-dark" mentality - it is using the energy surplus currently being wasted; such as industrial waste heat (or cogeneration), weatherization of residential and commercial structures, and the list goes on.

In a recently released analysis of the electric energy situation of the Pacific Northwest done under contract for the Dept. of Energy by the Natural Resources

Defense Council, utility projections of the Northwest's electricity demand in 1995 could be cut back more than 40% leaving the region with an energy surplus even if only 3 of the 7 coal and nuclear units now being built are completed. This is based on BPA's strong economic and population growth trends which significantly exceed the estimates of the U.S. Census Bureau. The program incorporates conservation (or end-use efficiency) measures, industrial waste heat (cogeneration) and wind.

Residential and commercial-sized micro-hydro electric generators can be installed and generate reliable electricity between 20-30 mills per kilowatt hour - half to three-quarters the cost of electricity from new thermal plants.

Wind electric generation, passive and active solar construction are competitive on the pay-back, based on the marginal cost of new thermally generated electricity.

These are submitted as examples, but are not an exhaustive list of the alternatives available.

The fact is that the huge central station generating plant is fast becoming a technological dinosaur. Schemes such as CWIP prolong and agonize the transition that a free energy market would accelerate. It does not make sense to allow the purchase of a cadillac on someone else's dime when an omni would do the job just fine.

One additional comment I would like to add regarding construction work in progress. Let me preface it with the statement that NPRC did not support the recent attempt to place a public power initiative on the ballot for a variety of reasons which are not relevant to this discussion. But, the question must be asked of this committee: If the public, the consumer, is going to finance the capitalization of the utility industry and venture the capital for new plants, then why shouldn't they become the owners of those plants? A CWIP rate structure is the best arguement that could be ventured for public management of the utility industry.

NAME Phyllis A. Bock BILL No. HB 395

ADDRESS HELENA DATE 2/11/81

WHOM DO YOU REPRESENT MT'S POWER TO THE PEOPLE (MPP)

SUPPORT ______ OPPOSE ✓ AMEND ______

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

I oppose this bill personally and MPP opposes this bill because it will increase utility rates - all our rates whether we're on the Mt. Power or M.D.U. systems and for what? To sell the excess powers to out-of-staters, who won't pay their fair share of the cost of building the new plant. This argument especially applies to Colstrip 3 and 4. We'll be subsidizing those out of state people who use and need additional power. I would label this a "utility relief bill" to the detriment of the ratepayers and would ask a "do not pass" on this bill.

FORM CS-34
1-81

NAME Jim Jensen BILL No. 395 / 431

ADDRESS Helena - Power Block DATE 2-11-81

WHOM DO YOU REPRESENT Low Income Senior Citizens Assn.

SUPPORT ______ OPPOSE X ______ AMEND ______

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

FORM CS-34
1-81

NAME Tom Schneider BILL No. 395/431

ADDRESS 1227 11th Ave DATE 2/11

WHOM DO YOU REPRESENT Mt. PSC

SUPPORT ______ OPPOSE X AMEND ______

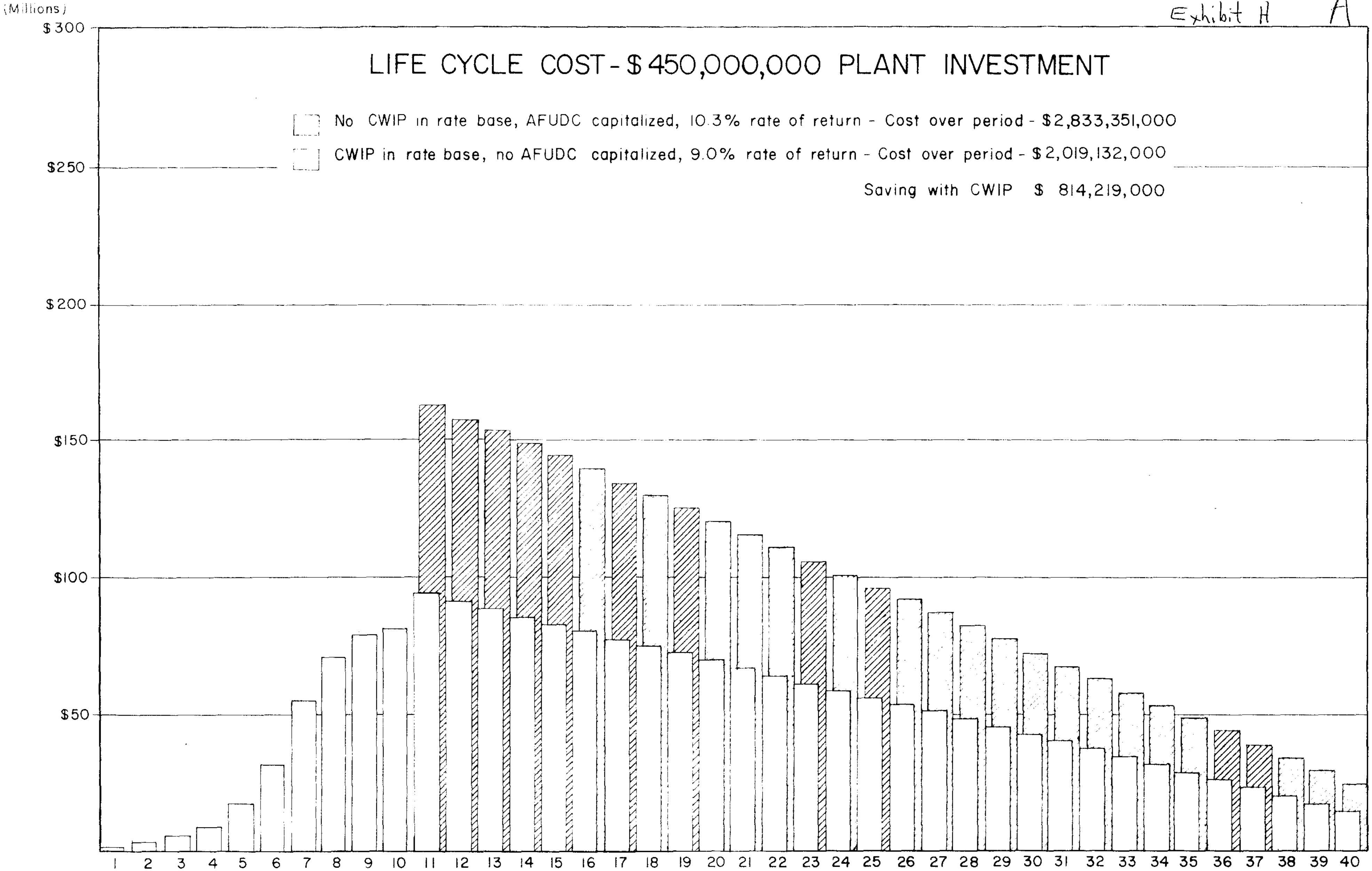
PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:

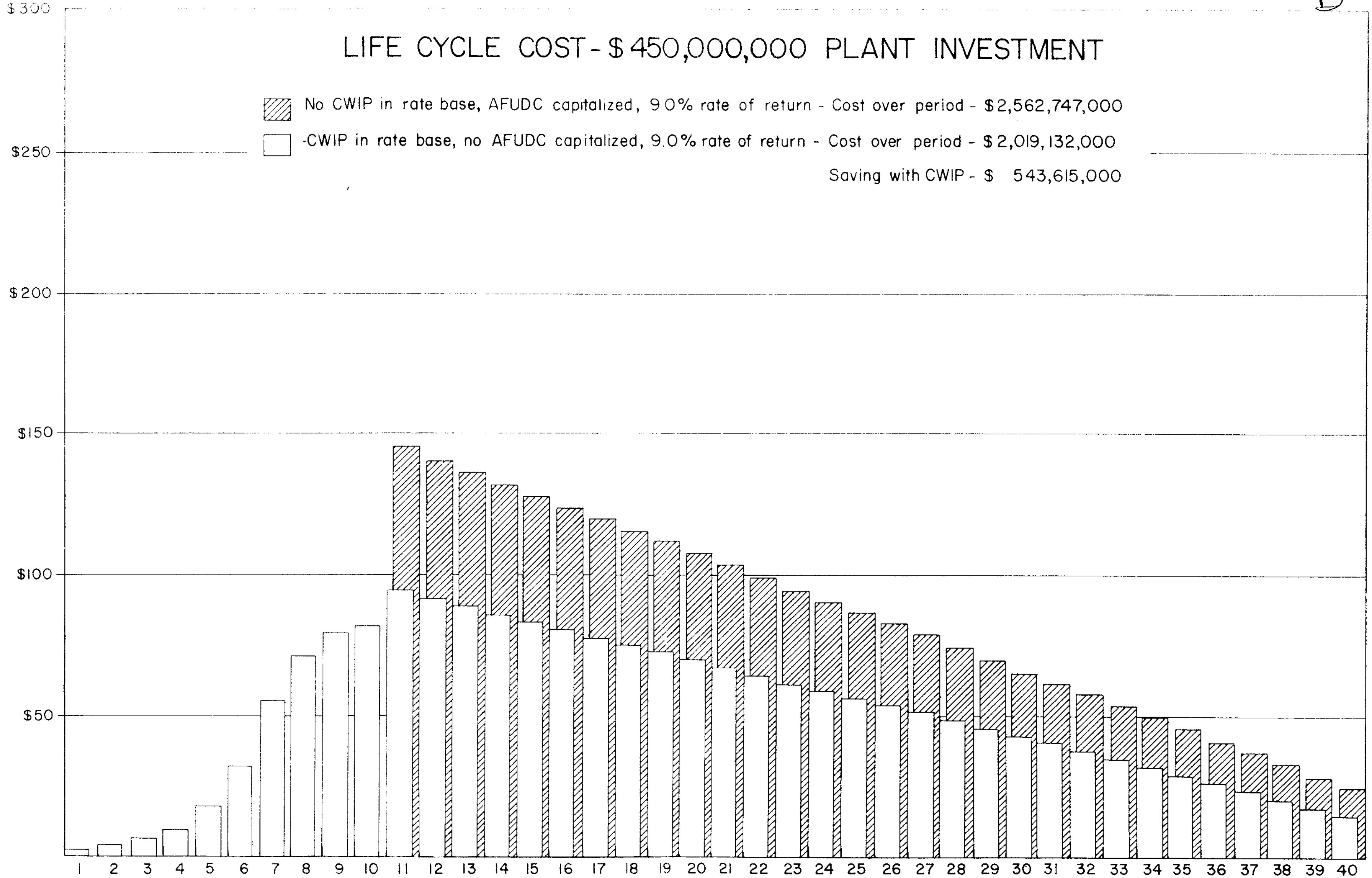
FORM CS-34
1-81

Exhibit H "A"

LIFE CYCLE COST - $450,000,000 PLANT INVESTMENT



B



LIFE CYCLE COST - $ 450,000,000 PLANT INVESTMENT
No CWIP in rate base, AFUDC capitalized, 9.0% rate of return - Cost over period - $2,562,747,000
CWIP in rate base, no AFUDC capitalized, 9.0% rate of return - Cost over period - $ 2,019,132,000
Saving with CWIP - $ 543,615,000
$300
$250
$200
$150
$100
$50
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36 37 38 39 40

VISITORS' REGISTER

HOUSE ______________________ COMMITTEE

BILL HB 431 Date ______________

SPONSOR ______________________

NAME	RESIDENCE	REPRESENTING	SUPPORT	OPPOSE
Phyllis A. Bock	Helena	MT.S POWER TO THE PEOPLE		✓
Jim Jensen	Helena	LISCA		X
Tom Schneider	Helena	Mt. PSC		X
Ann Wilsnack	Helena	AERO		X

IF YOU CARE TO WRITE COMMENTS, ASK SECRETARY FOR LONGER FORM.

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Form CS-33
1-81

Exhibit I

TESTIMONY OF LARRY D. GESKE

PRESIDENT OF GREAT FALLS GAS COMPANY

SUPPORTING HOUSE BILL 431

February 11, 1981

Great Falls Gas Company supports HB431, which has the potential of reducing regulatory lag under current PSC procedures.

Only Non-Current Expense Are Allowed By PSC

Since the PSC requires a utility to use historical data for its test year for rate making purposes, by the time the utility prepares the voluminous data required in PSC filing standards and the material is printed, actual filing takes place five to six (5-6) months after the close of the test year. Even though the Commission allows a twelve (12) month reach forward period past the test year to allow adjustments that are known and certain, criteria for the filing must be firm prior to data preparation, and known and certain items for the reach forward period must be tied down immediately (one or two months) after the test year (See attached Exhibit A). Other expense increases a utility actually experiences after the initial filing criteria is established during the reach forward period are generally not included in the PSC's final determination. As a result of this procedure, many utility expenses have been actually incurred twelve to fifteen (12-15) months prior to the Commission's final order, but are not included in their final order.

PSC Uses Unrealistic Sales Volumes

The Commission also insists that only sales volumes (normalized for weather) for the actual test year are used. Since the Commission and utilities are both working to maximize conservation, gas utilities are experiencing a declining market (Great Falls 5%/Year). When the PSC makes a determination of a utility's dollar increase in revenue requirement and they determine the increase in rates allowed, they divide the dollar increase by the test year sales volumes, which are unrealistically high compared to actual volume sales that will be experienced when the rates go into effect. The end result is that even the dollar increase the Commission allowed in the final order will not be realized by the utility in actual collections.

What Is The Result Of Unrealistic Utility Regulation?

The result of the PSC not recognizing current legitimate utility expenses at the time rates go into effect is that utilities are not provided a fair opportunity to earn the Commission's allowed rate of return.

In order to stay even halfway current with increased expense levels, a utility has no choice but to file one rate increase application on top of another. This has drastically increased Great Falls Gas Company management's time required in preparing filings, answering data requests and preparing to testify along with increased attorney fees. More filings require more PSC and Consumer Counsel staff to analyze this increased workload. Great Falls Gas management spends about a third of its time in rate work, which should be spent on improving utility services to its customers. Poor utility earnings over a long period will also reduce the amount of service a utility can provide to its customers.

Solution To Regulation Problems

The problem of using non-current utility sales and expense in setting rates by the PSC can be solved in at least two ways: one is to allow a utility to include legitimate expense increases in its test year up to the time the final rate order is issued; or two would be to shorten the time period allowed for the Commission to make a final determination on a filing from nine (9) months to three (3) months. Since the Commission is required to allow all parties to a utility filing to be given certain notices and an opportunity to be heard, it would appear that allowing more current expense and sales volumes to be used is the more practical alternative.

Forward Test Year

The Commission must allow reasonable estimates of a utility's sales volumes and expense levels to be included, at least up to the time a final PSC order is effective, so that new rates put into effect are at a level to recover expenses at that point in time.

EXHIB A

MONTANA PUBLIC SERVICE COMMISSION'S -

TIMETABLE FOR GREAT FALLS GAS CO.'S CURRENT FILING

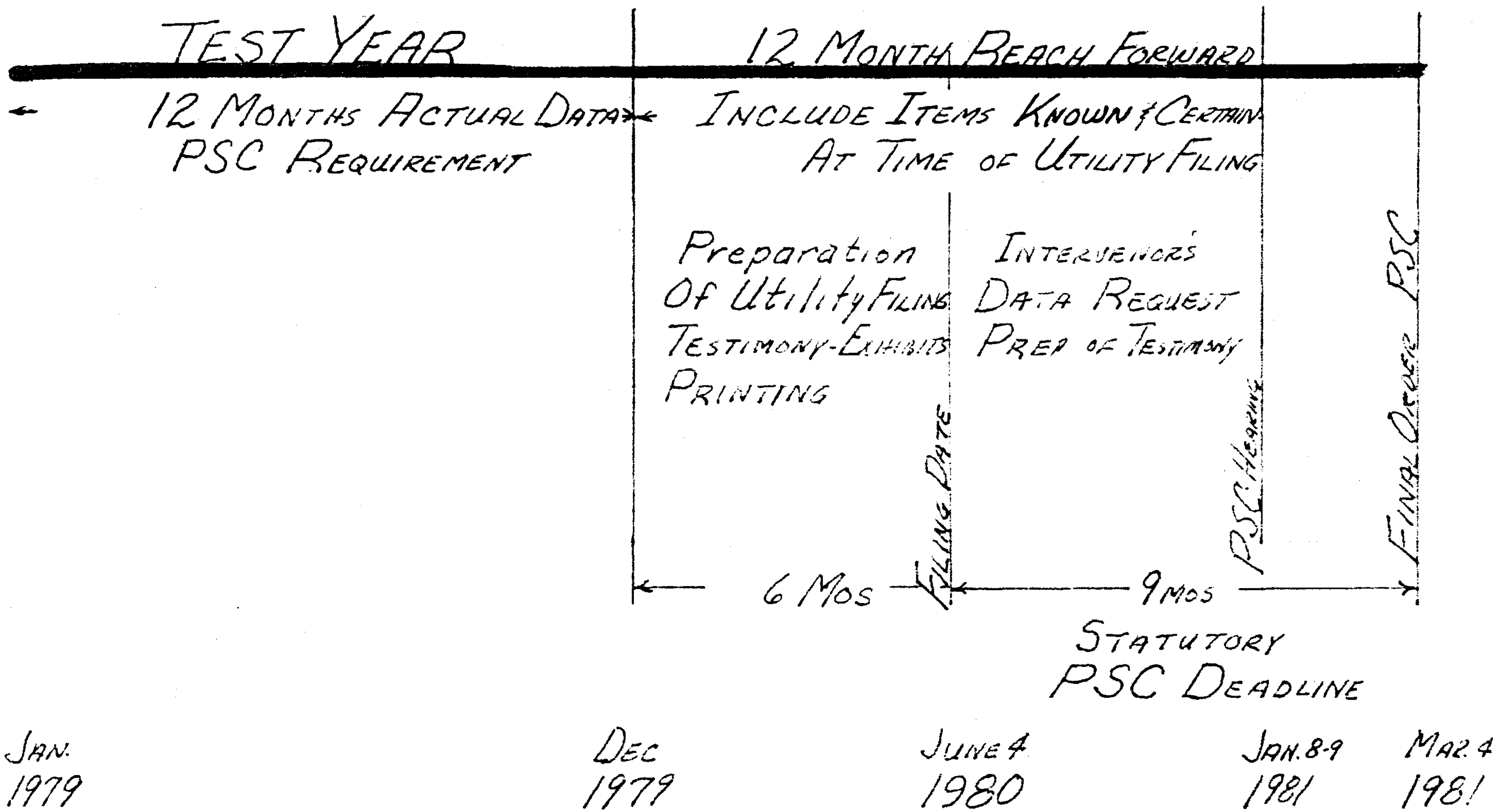


Exhibit J

COMMENTS OF GEORGE F. HESS ON BEHALF OF
MONTANA CONSUMER COUNSEL
CONCERNING HOUSE BILL NO. 431

I want to start by stating my understanding of the fundamental reason for having any laws dealing with the rates that may be charged for public utility services. The sole reason for such laws is the protection of the public interest against the possible abuse of monopoly power in the sale of human necessities. Any public utility law not designed to further that objective is neither necessary nor desirable.

This legislature created the Public Service Commission and it charged that body with the responsibility of devoting their full time and energies to the protection of the public interest. As things now stand, the Commission has wide latitude in deciding how best to achieve that goal. House Bill No. 431, by mandating the use of projections in the ratemaking process, would fetter the Commission's options as to how best to balance the interests of the utility's consumers and its stockholders. Under the present law, the commission is free to use projections if it thought that such a procedure were regulated to adequately protect the utility's stockholders and it has chosen not to do so. What possible public purpose could be served in requiring the

Commission to follow a procedure which it has carefully considered and consistantly rejected in recent years? There are at least three reasons I believe why the Montana Public Service Commission has not used projections recently.

First, it is impossible for staff and intervenors to make a meaningful check of forecast figures. Projections are usually based on budgets that require thousands and thousands of man-hours involving many people ranging from the field managers who budget in their own areas of responsibility up through the officers who have final approval. Aside from the sheer volume of material that would have to be reviewed, the reasonableness of budget estimates is particularly difficult to evaluate because of the judgements involved in their preparation. Budgets are prepared by managers and department heads drawing on their knowledge of conditions in their own areas of responsibility. It follows, that the only way one could make a reliable test of the soundness of the basic opinions entering into the budget is to become thoroughly familiar with the conditions which bear on future revenues and costs in each operational area. I doubt that any commission staff or intervenor has the manpower and resources available to make that kind of check.

An example may illustrate my point. Several years ago the Commission hired outside consultants in a Montana-Dakota Utilities Company case. The consultants made a projection that future revenue requirements were less than what was indicated by the use of an adjusted historical test year. The company argued that their projections were not valid because only the utility's personnel had sufficient knowledge of the operations to make an accurate projection.

Second, the use of projections tends to shift the burden of proof from the utility to the commission staff and the intervenors. Where an historical test year is used the utility has the burden of demonstrating what adjustments should be made for known and measurable changes. But where a budget is the accepted starting point, the staff and the intervenors must shoulder the almost impossible burden of attacking a forecast which relies heavily on opinions and estimates of the utility's own personnel. About all that one could do within the time allowed for the investigation of the proposed rates is to review the budget procedures and to compare the forecast with recent actual figures to determine whether the variations between the budget and the actual can be explained by known changes. If that is the only check to be made, it would seem to me that the better course to follow would be for the regulatory agency to start with actual figures and adjust them for whatever known changes the utility can quantify through convincing proof.

The third objection to the use of forecasts for rate making is that it lessens management's incentive to exercise strict cost controls. When the company knows that within reason, any budgeted amount will be allowed for rate making purposes, and, therefore, almost certain to be recovered from the ratepayers, there is little reason to expend great effort in finding ways to cut costs and to increase labor productivity. On the other hand, the use of a past test year without speculative adjustments for future inflation puts pressure on the utility's management to find ways of cutting costs to overcome or to at least mitigate the possible erosion of earnings from inflation.

The thought that projections must be used to achieve a reasonable regulatory result might be based on a misunderstanding of the Commission's use of an historical test year adjusted for known and measurable changes. The utilities, I am sure, will complain that historical data are stale and are of no relevance to future costs. Such complaints are not well placed.

The utility has the choice of selecting the test year. So the responsibility of presenting reasonably current results rests with the utility. In addition, the utility is free to make unlimited adjustments to test year data for known and measurable changes which have occurred within a reasonable period of time after the close of the test year.

Thus, to characterize the adjusted data as stale is not accurate. Finally, all elements entering into the rate determination are constantly changing - the level of sales, the revenues, expenses and rate base are not static. The use of an adjusted historical test year provides a reasonable measure of the relative relationships between revenues, expenses and rate base which can be anticipated in the foreseeable future.

But whether the adjusted historical test year continues to be an effective ratemaking tool is not really the issue here, House Bill No. 431 would require the use of projections rather than leaving the Commission free to choose the regulatory procedures best suited to protect the public interest.