

MINUTES

MONTANA HOUSE OF REPRESENTATIVES 54th LEGISLATURE - REGULAR SESSION

COMMITTEE ON STATE ADMINISTRATION

Call to Order: By **CHAIRMAN RICHARD SIMPKINS**, on March 1, 1995,
at 9:00 A.M.

ROLL CALL

Members Present:

Rep. Richard D. Simpkins, Chairman (R)
Rep. Matt Denny, Vice Chairman (Majority) (R)
Rep. Dore Schwinden, Vice Chairman (Minority) (D)
Rep. Matt Brainard (R)
Rep. Patrick G. Galvin (D)
Rep. Dick Green (R)
Rep. Antoinette R. Hagener (D)
Rep. Harriet Hayne (R)
Rep. Sam Kitzenberg (R)
Rep. Bonnie Martinez (R)
Rep. Gay Ann Masolo (R)
Rep. William Rehbein, Jr. (R)
Rep. George Heavy Runner (D)
Rep. Susan L. Smith (R)
Rep. Carolyn M. Squires (D)
Rep. Jay Stovall (R)
Rep. Lila V. Taylor (R)
Rep. Joe Tropila (D)

Members Excused: NONE

Members Absent: NONE

Staff Present: Sheri Heffelfinger, Legislative Council
Christen Vincent, Committee Secretary

Please Note: These are summary minutes. Testimony and
discussion are paraphrased and condensed.

Committee Business Summary:

Hearing: SB 284, SB 105
Executive Action: None

{Tape: 1; Side: A.}

HEARING ON SB 105Opening Statement by Sponsor:

SEN. LOREN JENKINS, SD 45, opened stating this bill would put a little more faith in the administrative code committee in rulemaking authority. Many of those people that are veterans realize when they go home the implementation cost of the laws they pass in the legislature are not quite in context with the bills passed as law. He stated this causes problems. The administrative code committee reviews the rules during the interim and adapts or accepts that they are the new legislative intent.

He stated this bill states one half of the administrative code committee notify the preceding officer that the members object to a notice of rule making. He stated the committee shall notify the agency in writing that the committee had proposed change in the codes and will address these issues in the next committee meeting. Following the notice by the agency, the proposal may not be adopted until publication of the last issue of the register that is published before the expiration of the six month period unless prior to that time the committee meets and does not make the same objection. A copy of the committee's notification to the agency must be included in the committee's record.

He said the committee will have to meet and is funded to meet at least once every six months. Page 3 and 4 explain what may accompany after the next legislative session. All or some of the rule may be objected to. This would not be effective until May 1 following the regular session after notice by the Secretary of State. If they object to a portion of the rule they will bring it up to the committee and agency. If there still is an objection they won't enforce the rule until the legislature has time to review the rule in the next session. If the legislature doesn't review the rule will go back to the committee and if the committee modifies or withdraws the rule before a rule is adopted then the rule can be adopted if they meet together and work out the problems.

This bill gives the code committee the authority to stop objectionable rules, but doesn't give the authority to wipe them out. This would give them the authority to hold the rule until the legislature can look at it.

Proponents' Testimony:

Lance Clark, Montana Association of Realtors, stated they concurred with the sponsor that the Code Committee needs to have more teeth in determining whether laws have gone beyond the legislative intent of law. He urged a do pass on the bill.

Don Allen, Montana Wood Products Association, stated it was his experience that often after the rules come out they don't follow

the intent of the law. This would give the Committee the ability to delay action until the rules could be looked at by the next legislature. About 65% of the rules follow the intent of the law. As they move to streamline government this bill would allow additional authority in different departments. He thought the bill was a good idea. The amendments from the Senate improve the bill and require half of the committee to object before the committee could delay the action if they felt it was necessary. He urged a do pass.

Opponents' Testimony:

Laurie Ekanger, Governor's Office, stated there was another bill similar to this one that they were also opposed to. This allows four members of the legislature to walk in and stop legislative action for two years until a new legislature looks it over. There are concerns about the constitutionality of the bill. This allows a few members of the legislature to stop the implementation of the laws the full legislature had passed. She urged a do not pass.

Informational Testimony: None

Questions From Committee Members and Responses:

REP. PAT GALVIN stated in the title of the bill it says the rule may be objected to by "a" member but other parts say it must take half of the committee to object to the rule. He asked for clarification.

SEN. JENKINS stated there were amendments from the Senate. The original bill said "a" member but they felt it was too much authority to give to the committee and the bill would be better if half of the committee would have to object to the rule or a portion of the bill in order to hold the enforcing of it.

REP. LILA TAYLOR asked for the make up of the Code Committee.

Sheri Heffelfinger stated the Code Committee is a bipartisan committed appointed by the legislature made up of four members of the House and four members of the Senate.

REP. TAYLOR asked how the chairman was elected to the committee.

Ms. Heffelfinger stated the chairman is elected by the members of the committee.

REP. MATT DENNY asked what powers the Code Committee would have if they felt something was inappropriate.

Ms. Heffelfinger stated they would be able to object to the rule and hold it but they would not be able to stop the rule from going through. She submitted **EXHIBIT 1**.

REP. GEORGE HEAVY RUNNER asked for some expansion on the question of unconstitutionality of the bill.

Ms. Ekanger stated there is a grey area in the Constitution about the separation of power and this would give too much power to a few members of the legislature.

REP. SUSAN SMITH asked if this would give the authority to a few people to represent a whole.

Ms. Ekanger stated the legislature would give the authority to the Code Committee. She stated the committee is bipartisan, however.

REP. JAY STOVALL asked what power the Governor has.

Ms. Ekanger stated if the director works for the Governor he would have power. If the person was independent of the Governor he would be able to protest to the committee.

CHAIRMAN SIMPKINS asked if the legislature designated the authority to the committee, would this be a different situation.

Ms. Ekanger stated that was correct.

CHAIRMAN SIMPKINS stated this bill wouldn't stop the rule, it would postpone the rule. He asked if this was already the process.

Ms. Ekanger stated this process already exists. She stated the concerns about the bill was that four members of the legislature would be able to postpone a rule until the next session. In the next session there would be a new legislature that may have a different view of the bill.

CHAIRMAN SIMPKINS asked if it would be more favorable for them to amend the bill to say "five" members of the board must object to the rule.

Ms. Ekanger stated she didn't know.

CHAIRMAN SIMPKINS asked the sponsor if he had any objection to amending the bill in such a way.

SEN. JENKINS stated he would have a problem with amending the bill in such a way.

CHAIRMAN SIMPKINS stated this doesn't say they can stop the rules.

SEN. JENKINS stated he was correct. They didn't think they should have the authority to kill a rule only postpone a rule.

REP. CAROLYN SQUIRES asked if they would be handicapping and slowing down the process and could they get in trouble for not complying with the rules if these four people were to object.

SEN. JENKINS stated the Code Committee would have to meet in six months. They would be able to determine if this process was abused or correctly followed. The committee would not only be able to object to a rule as a whole but also to a portion of a rule.

REP. SQUIRES asked if he felt this could tentatively stop the whole process.

SEN. JENKINS stated if they do the job they are supposed to they would only be looking at the legislative intent of the rules.

{Tape: 1; Side: B.}

Closing by Sponsor:

SEN. JENKINS stated they needed to stop thinking that the legislature and administration were separate. The committee would be able to hold those rules that were not the intent of the legislature until the next legislature could look at them. This "puts the teeth back in the Code Committee." There is a safeguard to this bill that half of the committee must object to the rule before they could delay. He stated this bill was necessary to pass.

HEARING ON SB 284

Opening Statement by Sponsor:

SEN. FRED VAN VALKENBURG, SD 32, stated this bill was considered to be complex but it is actually simple and straight forward. It comes down to whether or not they should use market competition as the cost of coal or apply complex returns. This affects what the charge for utilities is. This had been studied at length. They don't want the market to be a monopoly, they want to set price. There is no retroactive cost for this. He referred to testimony submitted by Joe Presley, EXHIBIT 2

Proponents' Testimony:

REP. BILL RYAN, HD 44 submitted letters written to him. EXHIBIT 3 He stated when something is not allowed in the rate case they turn around and knock it. He urged a do pass recommendation from the committee.

CHAIR TURNED OVER TO VICE CHAIRMAN MATT DENNY.

Jack Haffey, Montana Power Company, submitted written testimony. EXHIBIT 4

Diana Tikner, Western Energy Co., submitted written testimony.
EXHIBIT 5

{Tape: 2; Side: A.}

John Alkey, stated they are not taking about a monopoly in this bill. If they file a case next year the price will reflect the increasing price. He urged a do pass.

John Vacio, submitted written testimony. **EXHIBIT 6**

Pat Campbell worried about his job. He stated the more potential a company has to grow the better. He urged the committee to support the bill.

Kelly Wiedrich, IVOE Local 400, stated he was concerned about the jobs. He submitted written testimony. **EXHIBIT 7**

Jim Shaffer, Colstrip Miner, submitted written testimony.
EXHIBIT 8

Opponents' Testimony:

Nancy McCaffree, PSC, submitted written testimony. **EXHIBIT 9**

Bob Nelson, Consumer Council, stated this was created to represent the consumers. The PSC return was not spur of the moment. It was applied to the facts. He read the court decision.

{Tape: 2; Side: B.}

The committee did not recognize the need. Montana Power has done a good job at lowering costs. He didn't think they should allow them to raise rates. This is subject to reversal. They have appealed the decision but it hasn't been overturned. Simple assertion is easy to make things more difficult to prove. He urged the committee to do not pass this bill.

Nick Golder, NPRC, submitted written testimony. **EXHIBIT 10**

Tom Schneider, Northern Plains Resource Council, stated this is dangerous to blindly accept contract prices. The partners and financial community are in disagreement over this. They are saying the same thing has been alluded to for a long time. It represents opening a can of worms for the legislature to set strict regulatory limits.

Debbie Smith, Sierra Club, stated in the sponsor's opening statements he had said legitimate costs for Montana Power had been denied. She asked if they are legitimate. By saying market pricing is simple is not the case. She asked if the companies are going to treat their employees well. She stated this undermines their analysis.

Jim Jensen, MEIC, stated this bill is the most severe threat they have had in regulating utilities in Montana. He stated this couldn't be reviewed in the legislative session. He urged the committee to reject the bill.

J.V. Bennett, MontPIRG, submitted written testimony. EXHIBIT 11

Informational Testimony: None

Questions From Committee Members and Responses:

REP. SAM KITZENBERG asked what the difference was between Montana and Wyoming.

SEN. VAN VALKENBURG stated the difference was in coal. This has a greater BTU value. There is also a difference in the state's taxation of the coal. Montana Legislation reduced this to a 15% rate. He stated there is no simple single answer to the question.

REP. KITZENBERG stated jobs are a big issue. He asked what plans the opponents have to replace the jobs.

Mr. Golder stated whoever buys will get rid of the top heavy management.

Mr. Vacio stated a lot of people have benefited from this as well and they have a good relationship.

{Tape: 3; Side: A.}

REP. BILL REHBEIN asked if Montana Power will solve these problems whether or not this bill is passed.

Mr. Haffey stated Montana Power will solve these whether the Legislature adopts this bill or not. The mine won't necessarily be sold. Cost incurred will have a slight rate increase. He didn't think it is possible they could have gotten coal cheaper.

REP. REHBEIN asked where they got their information.

Mr. Golder stated they were deeply involved in what had gone on in their management. They see their management practiced that would have put him out of business if he would have used them. He would hate to be silent and let these things go on.

REP. REHBEIN stated he would like to see actual figures.

Mr. Golder stated he didn't have actual figures.

REP. SQUIRES asked someone to reply on the ratio of employees.

Ms. Tickner stated the ratio is four-to-one and that is with salary hourly payments.

REP. SQUIRES asked if there are any guarantees.

Mr. Haffey stated this is not something that has been studied thoroughly and it isn't a threat. It would be fairness to policy to adopt this bill. One option is to sell the assets. This will solve it one way or another. There is no threat that would happen.

REP. SMITH asked if Montana Power were to sell Western Energy if a new company would replace it or would ROE be used.

SEN. VAN VALKENBURG stated as long as the agreement met with present cost methods this would be allowed.

REP. JAY STOVALL asked if this bill were to pass would they have the right to set rules.

Dan Obrick, SD 1, stated this would give explicit direction but it is hard to speculate.

REP. STOVALL asked if it should be left up to the PSC.

Mr. Obrick stated they would have to look and compare.

REP. STOVALL asked if this was a fair way of doing this.

Mr. Obrick stated there are other factors that need to be taken into consideration.

REP. STOVALL asked if this was simpler than the Rate of Return.

Mr. Obrick stated there are other outlines and other things that are taken into consideration.

REP. DICK GREEN asked for a comment about there being no other marketplace.

Mr. Haffey stated this would turn the direction to some other mine. There are many options and he believed the case is robust for the coal market.

REP. BRAINARD asked if 80% of this would go to Montana Power.

Ms. Tickner stated only 75% would go to them.

REP. BRAINARD asked how many this would be.

Ms. Tickner stated it would be 13.

REP. Brainard asked if these were all long term agreements.

Ms. Tickner stated there are some long term, and some short term. There is a variety.

REP. BRAINARD asked if there were any long term that went to Montana Power.

Ms. Tickner stated there were.

REP. BRAINARD asked how much it would be per ton.

Ms. Tickner stated it would be consistent with the others.

REP. BRAINARD asked if Western Energy were sold would it be an option to sell to Montana Power.

REP. TAYLOR asked if Western Energy sold would the price be different.

Ms. McCaffree stated there would be options, but she couldn't say for sure.

REP. HEAVY RUNNER asked if this issue was rarely brought before a court and is it unfair?

Mr. Haffey stated that wasn't what he was saying. The courts say Montana law allows it.

REP. HEAVY RUNNER asked since they had failed with this going through the courts if they would turn to outside help.

Mr. Haffey stated the courts simply interpret the law and that is why they had turned to the legislature.

REP. BONNIE MARTINEZ asked if there were other ways and methods to do this.

Ms. McCaffree stated there are other ways to do this.

{Tape: 3; Side: B.}

CHAIRMAN SIMPKINS asked how many shares they had with Western Energy.

Mr. Haffey stated if they own Montana Power, they own Western Energy.

CHAIRMAN SIMPKINS asked if there was an ample supply.

Mr. Haffey stated they have some surplus and have capacity means.

CHAIRMAN SIMPKINS asked if there were 100 megawatts of power that they were unable to use.

Mr. Haffey stated the power from unit 4 is not part of the rate base and is separately managed. They have 30% ownership with that.

CHAIRMAN SIMPKINS asked if they could see them having to sell out of state.

Mr. Nelson stated the primary long term safe service will sell out of state and is committed through long term contracts to supply Montana Power and other utilities was well.

REP. DENNY asked if Montana Power transported costs if they believed the PSC would discount the transfer cost.

SEN. VAN VALKENBURG stated that was right.

REP. TAYLOR asked who the interveners were.

SEN. ECK stated they can vary all over.

REP. TAYLOR asked if they all have input.

SEN. ECK stated they do if it deals with the issue.

REP. DORE SCHWINDEN asked what the general assessment of other states was.

Mr. Schneider stated it varies across the United States and it is not unique.

Closing by Sponsor:

SEN. VAN VALKENBURG closed and thanked the committee for their time.

HOUSE STATE ADMINISTRATION COMMITTEE

March 1, 1995

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ADJOURNMENT

Adjournment: 12:00 p.m.


RICHARD SIMPKINS, Chairman


CHRISTEN VINCENT, Secretary

RS/cdv

HOUSE OF REPRESENTATIVES

State Administration

Johna
6-9 McCaffrey
Barnett

ROLL CALL

DATE 3-1-95

NAME	PRESENT	ABSENT	EXCUSED
Rep. Dick Simpkin, Chairman	✓		
Rep. Matt Denny, Vice Chairman, Majority	✓		
Rep. Dore Schwinden, Vice Chair, Minority	✓		
Rep. Matt Brainard	✓		
Rep. Pat Galvin	✓		
Rep. Dick Green	✓		
Rep. Toni Hagener	✓		
Rep. Harriet Hayne	✓		
Rep. George Heavy Runner	✓		
Rep. Sam Kitzenberg	✓		
Rep. Bonnie Martinez	✓		
Rep. Gay Ann Masolo	✓		
Rep. Bill Rehbein	✓		
Rep. Susan Smith	✓		
Rep. Jay Stovall	✓		
Rep. Carolyn Squires	✓		
Rep. Lila Taylor	✓		
Rep. Joe Tropila	✓		

ADMINISTRATIVE CODE COMMITTEE'S POWERS

Legal Memorandum



Montana Legislative Council

Prepared by
MONTANA LEGISLATIVE COUNCIL
Room 138
State Capitol
Helena, Montana 59620
(406) 444-3064

EXHIBIT 1
DATE 3-1-95
HB. _____

ADMINISTRATIVE CODE
COMMITTEE'S POWERS

Prepared for the Administrative
Code Committee

By John MacMaster
Staff Attorney

Montana Legislative Council
October 1986

This legal memo was prepared at the request of Representative Gary Spaeth, Chairman of the Administrative Code Committee. It sets forth the various powers of the Committee under the Montana Administrative Procedure Act (MAPA). The Committee may:

(1) Review the incidence and conduct of administrative proceedings under MAPA; 2-4-402 (3)(e), MCA.

(2) Review all proposed rules, though Department of Revenue proposals may only be reviewed for procedural compliance with MAPA; 2-4-402 (1) and (2), MCA.

(3) Require an agency proposing a rule to hold a hearing on the rule; 2-4-402 (3)(c), MCA.

(4) Submit oral and written testimony at an agency's rulemaking hearing; 2-4-402 (3)(b), MCA.

(5) Require an agency to publish the full or partial text of rule material adopted and incorporated by reference to the material; 2-4-307 (4), MCA.

(6) Obtain an agency's rulemaking records for the purpose of reviewing compliance with 2-4-305; MCA; 2-4-402 (3) (a), MCA.

(7) Require an agency to prepare an economic impact statement regarding a rule proposal. As an alternative, the Committee may by contract prepare its own statement. Notice of the statement and of where a copy can be obtained is published in the Montana Administrative Register; 2-4-405, MCA.

(8) Petition an agency for the adoption, amendment, or repeal of a rule; 2-4-315, MCA.

(9) Make a written recommendation to an agency for the adoption, amendment, or repeal of a rule; 2-4-402 (3) (b), MCA.

(10) Make a written objection to an agency regarding a proposed or adopted rule. The agency must respond in writing. If the Committee does not then withdraw or substantially modify its objection the Committee may require publication of the objection next to the rule in both the Montana Administrative Register and the Administrative Rules of Montana; 2-4-406, MCA.

(11) Poll the Legislature to determine whether a proposed rule is consistent with the Legislature's intent; 2-4-403, MCA. See also 2-4-404, MCA.

(12) Make a recommendation to the Legislature regarding an agency's grant of rulemaking authority. For example, the Committee could recommend that the statute granting rulemaking authority be amended or repealed; 2-4-314, MCA.

(13) Petition an agency for a declaratory ruling on the applicability of an agency rule. The ruling is subject to judicial review, including review at the Committee's request; 2-4-501, MCA.

(14) Seek judicial review of an emergency rule; 2-4-303, MCA.

(15) Institute, intervene in, or otherwise participate in proceedings involving MAPA (including an action to change or repeal a rule) in the state and federal courts and administrative agencies; 2-4-402 (3) (d), MCA.

(16) Require an agency to give the Committee copies of documents filed in a proceeding involving the interpretation of MAPA or an agency rule; 2-4-410, MCA.

(17) Require an agency to review its rules biennially to determine if rules should be adopted, amended, or repealed; 2-4-314 (1), MCA. That section requires each agency to do this. The Committee can use various powers set forth in this legal memo, paragraph (16) for example, to force an agency to carry out the review.

In addition to the above powers under MAPA, the Committee may remind an agency that the Legislature

holds the power of the purse and may not look favorably upon an agency in the next regular session if the agency exceeds its rulemaking authority or plays fast and loose with either that authority or the legislative intent behind a statute. The Committee may also, under its inherent powers as a legislative committee, draft and introduce legislation relating to MAPA; an agency's grant of rulemaking authority; adoption, amendment, or repeal of a rule; or other matters relating to rulemaking.

MACC-6302/JM/JM1

ADMINISTRATIVE RULES -- MAPA REQUIREMENTS

Outline for a Mini-Seminar

(August 1990)

Prefatory remarks: The Administrative Code Committee, its staff, and their functions. Rules are not reviewed by the Legislative Council. They are reviewed by Legislative Council attorneys assigned as staff attorneys to the ACC for rule review purposes.

Background reading

- Read and study, and periodically reread, Title 2, Ch. 4, parts 1 through 4 of the MCA, and the annos to those parts.
- Chapters 2 and 3 of the Legislative Council's Bill Drafting Manual can be consulted on grammar, punctuation, capitalization, and other matters of style and English usage. Photocopies of these chapters can be distributed to those working with rules.
- "Review of Administrative Rules", dated August 1990, an ACC staff memo outlining how the ACC's staff should review rule notices.
- Memo from David Niss to "Lawyers" regarding "Updated Procedure and Format Memo for Review of Administrative Rules", dated May 7, 1984. Read and periodically reread. Use as a reference source.
- Attorney General's Model Rules, including the Appendix of Sample Forms, see Title 1 of the ARM.

Definition of administrative rule

See 2-4-102(10) and (11).

EXHIBIT _____

DATE _____

HB _____

Legislative delegation of rulemaking authority

- The Legislature has the authority to delegate to the Executive Branch agencies the authority to adopt, as law, administrative rules.
- Some reasons why a delegation of rulemaking authority may be necessary or desirable:
 - Lack of expertise in the Legislature;
 - The field of law involved is too complex, too broad, or too narrow and obscure;
 - The administrative agency that will administer a statute and implement it by rules has an abundance of expertise or much more expertise than the Legislature, and it is better that the agency adopt rules than that the Legislature attempt to completely cover the area by statute;
 - Necessity for on-going compliance with federal law that the state must follow, or has to follow to get federal funds;
 - The field of law does not easily lend itself to regulation completely by statute;
 - The field of law is a fast-moving one and the law must be constantly updated and the Legislature does not meet often enough to itself do the updating;
 - The legislative process results in a bill granting rulemaking authority because the Legislature does not have the time, or the inclination, to completely flesh out a concept, or a compromise results in a vague or incomplete law that must be fleshed out by rule.

MAPA does not grant authority for substantive rules

- See 2-4-301. Section 2-4-201 is authority only for the types of rules mentioned in that section. It does not grant authority for

substantive rules. See 2-4-102(11) for definition of substantive rules.

Key sections for rulemakers

- Persons formulating, writing, and filing rule proposal and adoption notices should pay particular attention to 2-4-302, 2-4-303, 2-4-305 through 2-4-307, and the annotations to those sections.

Statutory authority for rules

- Under 2-4-305(3), each new rule or amendment of a rule must cite the MCA section that is authority for the rule. You cannot adopt rules unless an MCA section clearly grants authority to adopt rules and the rules implement a particular MCA section or sections.
- The cited authority must grant authority to implement, by rule, the MCA section(s) the rule cites as implemented. That is, the authority section must say "shall (or may) adopt rules to implement this part (chapter) (title) (sections___through___)". Or the authority section may state specific subjects that may be implemented by rule.

Implementation of MCA sections

- Each new rule or amendment of a rule must cite the section(s) of the MCA that the rule implements. You cannot have a rule unless it (properly and in fact) implements one or more MCA sections.
- "Implement" a section means to flesh it out, explain it, further or fulfill its purpose, make it work or work better, interpret it, carry it into effect, etc. The whole purpose of administrative rules is to do one or more of the above. A rule that is not in some such way connected to

at least one MCA section is invalid. You cannot have a rule that has nothing to do with implementing statutory law.

Consistency with MCA: conflicts

- Each rule must be consistent with, and not in conflict with, the MCA section(s) it implements and all other statutory and constitutional law, including applicable federal law. See 2-4-305(6) (a). A rule can never override a provision of a statute or constitution.
- A rule cannot add to what a statute already contains a provision or additional requirement not envisioned by the Legislature. See the 2-4-305 annotations casenotes from the following cases: McPhail v. Mont. Bd. of Psychologists, Bd. of Barbers v. Big Sky College of Barber-Styling, Michels v. Dept. of Social and Rehabilitation Services, Bell v. St.

Statements of reasonable necessity for rules

- Section 2-4-302(1) requires a rule proposal notice to include a rationale for the intended action. Under 2-4-305(6) (b), the proposal notice must contain a statement explaining why a new rule or a rule amendment is reasonably necessary to effectuate the purpose of the statute the rule implements.
- Reasonable necessity and rationale are similar, but the former includes the latter and is a stiffer test to meet. If you adequately show reasonable necessity you have an adequate rationale.
- The rule must be necessary to implement the statute and the necessity must be reasonable. State as explicitly and clearly as you can why the rule is needed. Do not be afraid to be lengthy. Do not merely state what the rule provides or does or covers. Start by

asking yourself who wanted the rule and exactly why they wanted it and you will usually be able to formulate the reason for the rule, but the reason must be a reasonable one and a good one and constitute necessity for the rule.

-- You can state the reasonable necessity for each rule, have a number of statements, each covering two or more rules, or have one or more statements covering all the rules in general.

-- Examples of reasonable necessity:

- The rule is mandated by the Legislature (the MCA section that grants authority to adopt rules says the agency "shall" adopt rules). A provision that the agency "may" adopt rules is not reasonable necessity for rules.
- The rule is needed to conform our law to federal law or to receive federal funds.
- The rule is needed to make our law uniform with that of other states.
- Rules regulating mirrors on school buses are necessary because investigation shows that three recent school bus accidents were caused by faulty mirrors, improperly placed mirrors, not enough mirrors, or other problems with mirrors.
- Rules are necessary to provide a procedure by which the public can apply for or receive something from the state government and to ensure due process.
- A rule is being amended to delete a conflict with a statute.
- Fees are changed to make them commensurate with costs, as required by statute.
- The rule changes are needed to conform the rules to recent legislative enactments.
- A majority of those affected by the rules agree that experience and studies by experts show the rules are necessary to

protect the public safety and welfare.

- Standards contained in the rules are being updated because they are obsolete or are no longer state-of-the art.
- The rules are needed to ensure fair competition and reduce unfair trade practices that have frequently occurred.
- Documented instances of incompetent or substandard work show that rules are necessary to reduce such occurrences.

Subsections (1) and (2) of 2-4-305

- The requirements of these self-explanatory provisions are often overlooked. Be sure you comply with these provisions.

Adoptions by reference

- Covered in 2-4-307 and the Model Rules. Review that section and the Model Rules when you intend to adopt rules or standards by referring to them in the adopting rule and stating that they are adopted and incorporated by reference.
- The rule cannot say that it adopts all future amendments to the rules or standards that are incorporated by reference. If you wish to adopt future amendments you must do so specifically in a new rule amendment proposal notice that refers to the amendments adopted or to the amended version of the rules or standards that are incorporated by a reference to them.

Time periods

- An adoption notice must be published in the MAR no less than 30 days nor more than six months after the publication date of the proposal notice. See 2-4-302(2) (c) and (3), 2-4-305(7), and 2-4-306(4).

- You must give a least 20 days notice of a hearing and the notice period begins on the date of publication of the notice in the MAR.
- You must allow at least 28 days from the date of publication of a proposal notice in the MAR for interested persons to submit written material.

M5006 0214JMDA

**SUMMARY OUTLINE: ADMINISTRATIVE RULE
BACKGROUND INFORMATION RELATED TO SB 105**

Prepared by Sheri S. Heffelfinger
Researcher, Montana Legislative Council
March 1, 1995

Administrative Code Committee

- Established in 1975 (Title 5, chapter 14, part 1, MCA)
- 8-member, bipartisan committee (four members of House, four members of Senate; chairman selected by members)
- Purpose:
 - oversight and review of executive agency rules to ensure compliance with MAPA
 - forum for complaints

General MAPA requirements

- All proposed and adopted rules must be printed in Montana Administrative Register, published twice monthly
- Interested persons must be given opportunity to comment on proposed rules
- Rule not effective unless:
 - rule is within scope of authority granted by Legislature
 - rule is consistent with statute and intent and "reasonably necessary"
 - rule was adopted in compliance with process outlined in MAPA for reasonable notice, hearing, and submission of comments on rules

Administrative Code Committee's Review of Agency Rules

- Committee reviews:
 - whether rule complies with MAPA
 - rule's clarity and economic impact
 - complaints about proposed or adopted rules
- Review process includes:
 - staff attorney's analysis and one-on-one consultation with agency
 - if conflict exists, matter brought to the ACC at next meeting
 - ACC takes action (see potential actions/powers outlined below)
 - staff attorney continues to followup to ensure agency compliance

(OVER)



WESTMORELAND RESOURCES, INC.

P.O. Box 7087, Billings, Montana 59103 [406] 248-7803

February 27, 1995

FEDERAL EXPRESS

Honorable Dick Simpkins
Montana House of Representatives
State Capitol
Capitol Station
Helena, Montana 59620

Dear Representative Simpkins:

Re: Senate Bill No. 284--Montana Power Bill

Because of a previous commitment, I will not be able to attend the House State Administration Committee Hearing on Senate Bill No. 284. I am enclosing written testimony that I would have given had I been able to attend this hearing. I hope you will consider this testimony in your deliberations on Senate Bill No. 284.

Besides my testimony, I am enclosing a copy of Judge Sullivan's decision dated December 29, 1994, upholding the Public Service Commission decision to disallow approximately \$7 million of Montana Power Company's \$35 million annual coal costs from its mining subsidiary Western Energy Company (WECO). I particularly call your attention to Findings of Fact Nos. 13 and 14.

Sincerely,

Joe Presley
President

Enclosures

EXHIBIT two
DATE March 1, 1995
HB SB 284



International Brotherhood of Electrical Workers A.F.L.-C.I.O.



LOCAL UNION 44 • 19C

Butte, Montana 59702

Post-it™ Fax Note

7671

Date	3-1-95	# of pages	2
To	Bill Ryan HQ	From	Alia
Co./Dept	State Capital	Co.	2744 IBEW
Phone #		Phone #	406-723-3203
Fax #	406-444-1634	Fax #	406-723-3220

Date: February 6, 1995

House Business & Industry
 TO: The Honorable Gary Devlin, Chairman of The Senate Taxation Committee
 Capitol Station
 Helena, Mt. 59620

FROM: Stan I. Dupree, Business Mgr. & Financial Secretary, Local 44 of the
 International Brotherhood of Electrical Workers.

RE: S.B. 284

Dear Mr. Chairman:

I offer this testimony on behalf of the 860 people that are members of Local 44, about 446 which are Montana Power Company Employees. I ask you to support SB. 284. This seems to be a fair proposal considering the facts surrounding this. The Supreme Court upheld the ruling of The Montana Public Service Commission when they did not allow 7 million dollars of coal purchases to be included into the rate base. Although the Supreme Court did agree with Mont. Power Co. that it is not fair but it was legal. I feel that your support of this legislation will accomplish a number things, such as:

It will remove the political pressure from the PSC.

It will allow the PSC to retain a certain amount of control on the price of coal and how much will be allowed into the rate base, if MPC is forced into a sale of the mine the PSC will have lost control over this issue.

It will save MPC from putting the Western Energy Coal Mine on the auctioning block and running the risk of an out of state company getting the bid and possibly laying off Montana workers to bring in their own workforce.

It will allow MPC to claim the coal used to generate electricity into its rate base which is only fair.

I have been informed that the cost to the average consumer will be approximately .75 cents per month.

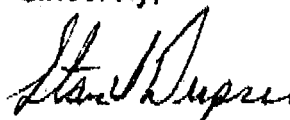
The monopolistic rein that major utilities have had in the past is no longer existent. Competition is alive and on the rise, and all utilities coast to coast are downsizing, streamlining and out of necessity, becoming more competitive every day. I am sure that MPC is not trying to do away with the PSC or take away any of the PSCs jurisdiction,

EXHIBIT *these*DATE *March 1, 1995*

they are trying to prove that coal costs, are in fact an overhead cost that must be recovered, as all costs of doing business are. MPC does have an option, they can sell the coal mine which would make the price of coal being included into the rate base automatic, or at least being perceived as the cost of doing business. The real issue at hand is the mine is owned by Western Energy which is a subsidiary of the MPC and the PSC did not condone the idea of the MPC selling coal to itself. If sale of the mine is the MPCs only way of getting the 7 million dollars into the rate base then you can rest assured the sale will probably happen.

You are probably aware that MPC has historically been one of Montanas largest and most benevolent employers and that they still are. To force the MPC into a sale they would rather not make and a sale that actually would benefit no one would be a travesty of the most naive kind. I urge you to support the intelligent legislation of Senate Bill 284. I am

Sincerely,



Stan I. Dupree
Bus. Mgr./ Fin. Sec.
Local 44, IBEW.

TESTIMONY
OF
JACK HAFLEY

THE MONTANA POWER COMPANY

IN SUPPORT OF SENATE BILL NO. 284

EXHIBIT four
DATE March 1, 1975
HB SB 284

Mr. Chairman and members of the committee, my name is Jack Haffey. I am Vice-President of Administration and Regulatory Affairs for the Montana Power Company, and I am here today to testify in support of Senate Bill No. 284.

Senator Van Valkenburg has explained the bill to you, in his opening statement. I would like to take just a few minutes to give you the reasons Montana Power supports the bill and strongly encourages you to pass it.

It is important that I briefly tell you about the history of our coal involvement, then I will (1) address the policy nature of the bill, (2) explain the need for fairness in utility regulation, (3) tell you why we strongly believe the Commission method of determining reasonableness of coal costs is unfair, (4) encourage you to adopt the market place standard to determine reasonableness, and (5) mention the other options Montana Power must consider if this bill does not pass.

First, a couple comments on Montana Power's history in the coal business.

- In 1959, Montana Power purchased the Colstrip townsite and 60 to 70 million tons of coal reserves owned by the Northern Pacific Railway Company for \$1.5 million.
- During the first half of the 1960s, Montana Power continued to purchase additional coal reserves until, by the mid-1960s, it owned about 850 million tons of coal reserves.
- We acquired these reserves for two reasons. One reason was that we believed it would be difficult to develop hydro sites in the future, and expected that steam electric generation, such as coal-fired units,

would be needed to enable us to serve our customers in the future.

The second reason was that we believed there would be a commercial market for coal, because other utilities would also need to turn to coal as a fuel for electric generation.

- In 1966, Western Energy was incorporated to manage the coal assets, for commercial sales to other utilities and to make coal available to our utility for its electric generation needs in the future.
- It was obvious that our utility would never need 850 million tons of coal, and actual use by MPC has confirmed this, so the commercial sales mission of Western was clear from the very beginning.
- The Western Energy coal properties are not and have never been included in rates charged to our electric utility customers.
- The J.E. Corette Plant began production in 1968, and Colstrip Units #1 and #2 began in the mid-1970s. However, there were no coal cost disallowances until 1980.
- Colstrip Units #3 & #4 began production in the mid-1980s.

With that brief history let me address the Policy Matter.

- Utility regulation is an important and complicated responsibility of state government, and the legislature created the PSC for this purpose.

- Only rarely, should a utility regulatory issue be brought to the legislature.
- For 15 years, our electric utility has had part of the expense of its coal purchases from its affiliate, Western Energy, disallowed for inclusion in rates by the Commission. The method the Commission has used is called the rate of return or profitability method.
- When an electric utility purchases something it needs, like coal, from an affiliate, the Commission should give special scrutiny to that transaction, to ensure that the utility does not pay too much. We do not argue with that. But the Commission, for 15 years, has used a method we consider unfair, as it has decided how much of our Electric Utility's coal costs to disallow, without addressing the issue of whether the price of the coal is reasonable.
- We have tried to persuade the Commission to use a relevant standard -- the market price of the coal -- to determine reasonableness of coal costs, but have been unsuccessful.
- We have taken our concerns to the courts (as MDU has), but the courts have repeatedly told us that state law gives the Commission the latitude to use the rate of return method. The Supreme Court, even though it stated its preference for the market price method, cannot substitute its judgment for that of the PSC.
- We even tried to settle the matter by swallowing hard and accepting some level of disallowance for the long term -- but were unsuccessful.

- The disallowance, in 1994, went to a level of \$7 million, out of a total coal invoice of \$35 million, or 20% of the coal bill from Western Energy to us.
- While the invoice to us from Western Energy remained fairly constant at \$35 million, the disallowances from 1984 to 1994 went from \$700,000 to about \$2.6 million, to \$7 million.
- Finally, we decided we must place this policy question in front of the legislature. We have exhausted our other options, the magnitude of the disallowance is simply and totally unacceptable, and the method used to calculate it is unfair.

So, we have come to you -- after 15 years of trying other means to obtain a fair result.

Just a word about fairness in the context of utility regulation.

- In Montana and other states, it is universally understood that the regulation of utilities by the state must balance the interest of consumers and utilities. The United States Supreme Court has addressed and confirmed this notion of balance.
- The Commission's approach to this coal cost reasonableness issue does not produce this required balance.

What is it about the rate of return or profitability method that is unfair -- that does not produce this balance?

- First, a rate of return or profitability concept applies, properly, to a certain type of utility regulation that is

called cost of service regulation. It calls for the regulator to allow the utility to include in its rates its reasonable cost of providing electricity, plus the opportunity to earn a certain rate of return on its assets.

- For utilities that are expected to be around for the long term and to continuously add to and improve their plant and equipment to provide reliable service, the one-year (or test year) rate of return approach works.
- To the contrary, a coal mine has a different profitability profile than a utility -- it exists to go out of business -- to continue until the coal is all mined.
 - Therefore it has high initial investments that then depreciate until the coal is all mined. It does not continually add equipment.
 - As a result, its profitability tends to increase over time as its asset base declines.
 - It is not unexpected to see high rates of return in later years based upon this reason.
- To apply the utility concept of acceptable rate of return in any one year (a test year) to a coal mine or coal company produces unacceptable results -- because it makes the coal profitability look excessive, when over the life of the mine it is in fact quite reasonable.
- Second, from 1984 to 1994, our electric utility has had all its coal plants on line....so our coal tonnage purchases from Western have been about the same year

after year.

- And, during this period the invoice to us from Western has been approximately \$35,000,000 every year.
- But, in 1984 the amount the Commission disallowed was \$700,000 out of \$35,000,000, or about 2%. In the late 1980s and early 1990s the disallowed amount was about \$2.7 million, or about 8% of \$35,000,000. In 1994, the amount disallowed was about \$7,000,000 out of \$35,000,000, or about 20%.
- Implicit in this track record is the idea that if Western Energy is not so profitable in a particular year, then our Electric Utility's coal costs are reasonable. But when Western Energy is more profitable, our Electric Utility's coal costs are unreasonable.

This result is absurd. There is no rational relationship between Western Energy's profitability and the reasonableness of our utility's coal costs. The coal is either reasonably priced or it is not. The profitability of the seller has nothing to do with it.

- Furthermore, the profitability method used by the Commission actually can produce a result, in a given year, that would imply that if Western's profitability is low enough the Commission could order us to pay more for coal than our coal contracts require. This result dramatically shows the irrationality of the method.
- Not only is the rate of return method unfair and irrelevant, but it can also be applied unfairly. In the last rate case, the Commission did not consider or

include the reclamation cost obligations of Western Energy in its disallowance determination, even though this liability is clear. Consideration of this obligation would have significantly reduced the \$7 million.

So, we firmly believe this method does not strike that balance that fair utility regulation requires -- it is not a proper standard to use to determine reasonableness of utility fuel purchases from an affiliate -- and its varying, even irrational results prove it.

What, then, is the appropriate standard to determine whether the costs of coal purchased from an affiliate are reasonable, for inclusion in electric utility rates?

We believe the market place and market price set the proper standard. Look to see what the utility might have been able to get the coal for from another supplier. This standard works, is relevant and rational.

- The original decision to locate steam plants at Colstrip to use Western Energy coal was a true matter of choice.
- Colstrip Units #1 and #2 are owned, equally, by Puget Sound Power & Light and Montana Power. Puget was obliged, in the 1970 - 71 time period, as was Montana Power, to find the best buy -- the lowest total cost of getting electricity to its customers. It had choices. Its decision to invest in plants to be built at Colstrip and burn Western Energy's coal was made because it made economic sense to Puget.

- Puget, WWP, PP&L and PGE (the 70% owners of Units #3 & #4) later also had choices as to location, and chose the Colstrip site and Western Energy coal for the construction of Units #3 & #4. So, the original decisions were ones made in the face of other options. Western had to offer a competitive price in the context of the total cost of delivering electricity (by these utilities) or risk not getting the market.
- Our Electric Utility has played no role in establishing the contract price for the coal to Units #1 and #2, or the price for coal to Units #3 and #4.
- For Units #1 & #2, Puget (a 50% owner in the plants) negotiated the coal price with Western Energy and our Electric Utility pays this price determined by Puget and Western Energy (whose interests oppose each other).

In fact, the price re-opener provision in that contract recently resulted in arbitration. Meaning Puget and Western Energy could not agree.

Our Electric Utility is bound by the arbitration decision, yet will have no input to the arbitration whatsoever.

- For Units #3 & #4, Puget and the other owners went to arbitration from the beginning. Arbitration determined that contract price. Once again, MPC's Electric Utility was not involved.
- So, our Electric Utility plays no role in

price determination. There is simply no opportunity for a sweetheart deal.

- Even though MPC and the other owners pay the same prices for coal, part of MPC's coal expense has been disallowed and none of the other utilities have had any of these coal expenses disallowed.
- Our Electric Utility represents only 20% of the market for Western Energy. We are obviously not dominant.
- Even if we were involved in price establishment, which we are not, we could not dictate the price.
- In summary here, a market choice existed at the start -- even in locating plants at Colstrip, we have no say in the contract price, and we are not a dominant part of Western Energy's market.
- The price standard -- what could we have purchased the coal for from somebody else -- is clearly the fairest standard to use as policy to determine reasonableness of purchases by an Electric Utility from an affiliate -- and that is what we ask from the legislature as state policy.

Would such a standard cause a rate increase to our electric customers?

Not by itself.

- We would be required to prove, in a rate case, using market information, that our prices for coal are reasonable, compared to the relevant market.
- The Montana Consumer Counsel would also present market information.
- The Commission would then weigh the market evidence and decide what, if any, disallowance was appropriate.
- The point here is that the standard would be rational and relevant, the policy would be fair, and the Commission would have to focus on whether the price paid for the coal was reasonable or not, rather than on the ancillary issue of profitability of the coal company.

Just an ironic footnote: Even as we have had these disallowances over the years, our steam plants, including our full coal costs, have been consistently among the lowest cost coal steam plants in the nation.

What about other options to solve this challenge?

- We hope the legislature passes this bill. It is the right thing to do in terms of fairness in utility regulation.
- It is important to mention that the Commission, the Consumer Counsel and some others disagree with our view of fairness here.

That is clearly their right. We agree to disagree. It is not a matter of personalities or a personal

matter of any sort.

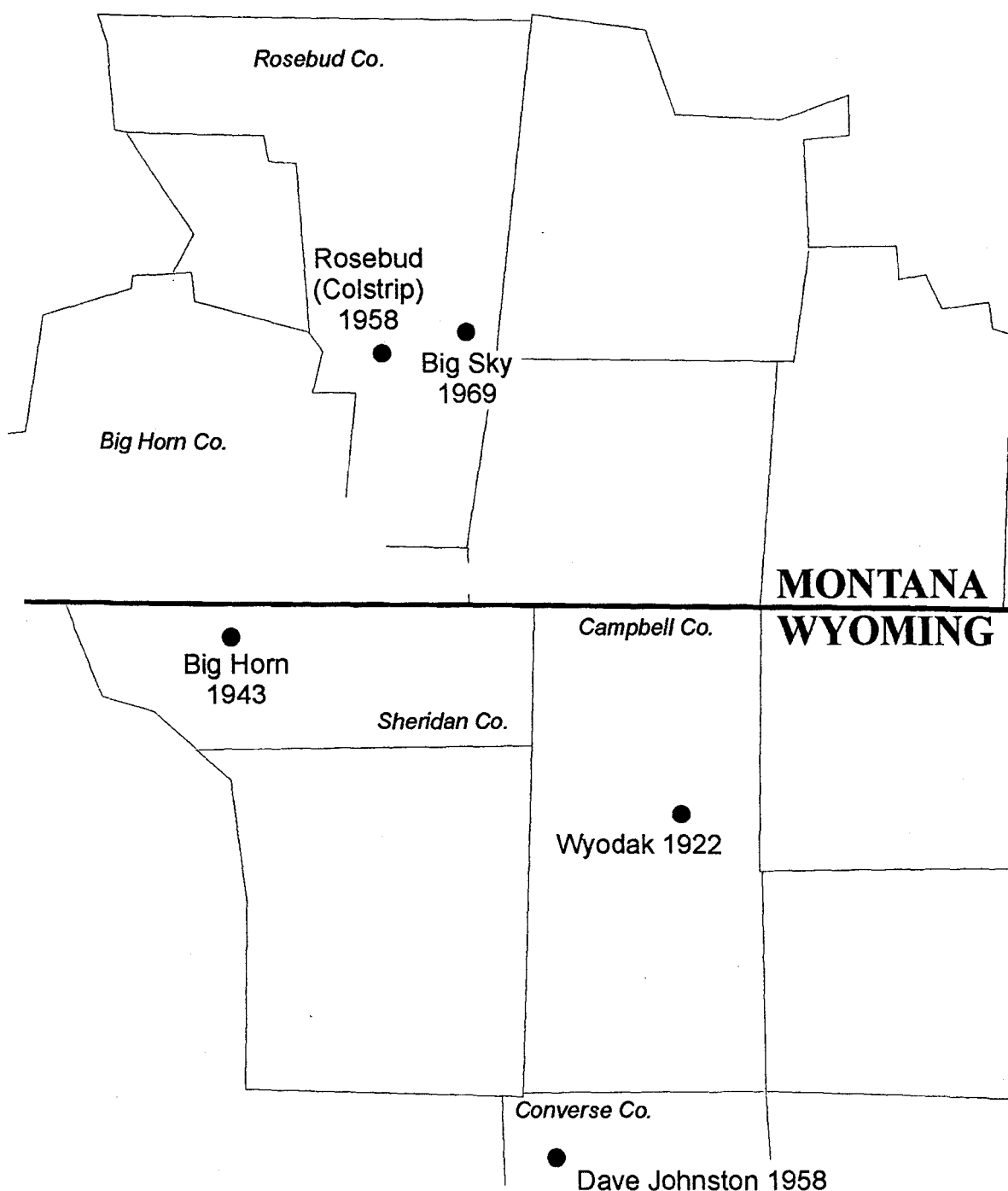
- We feel our electric and gas utilities have had good relationships with the Commission, Consumer Counsel and other participants in utility matters over the last many years. I think, and trust, that you will hear them confirm that they view our behavior as a utility in Montana to be very responsible and participative in environmental and social stewardship matters, among other areas.
- We, as a corporation, are absolutely obliged to solve this corporate financial health problem.
 - If this bill would not pass, we would be obliged to consider other solutions, including whether disposal of the Western Energy coal assets, sale of the assets, would be advisable in order to get the full value out of that business, and to eliminate these cost disallowances.
 - We cannot accept disallowances of about \$5 to \$7 million/year over the life of these plants, and these contracts. It would amount to about \$40-\$60 million of disallowances, in current dollars.
 - We would not take this step without considerable thought and analysis, but it would have to be considered.
 - Even the thought of this option creates uncertainty and anxiety for employees. To deny it as an option would be wrong, ---- but it has not been thoroughly studied by the corporation as of this time.

- We encourage you to pass this bill, and we will be happy to answer any questions you might have, at the appropriate time.

Thank you.

jdH\Speech.coal

PRODUCING MINES IN POWDER RIVER BASIN 1970

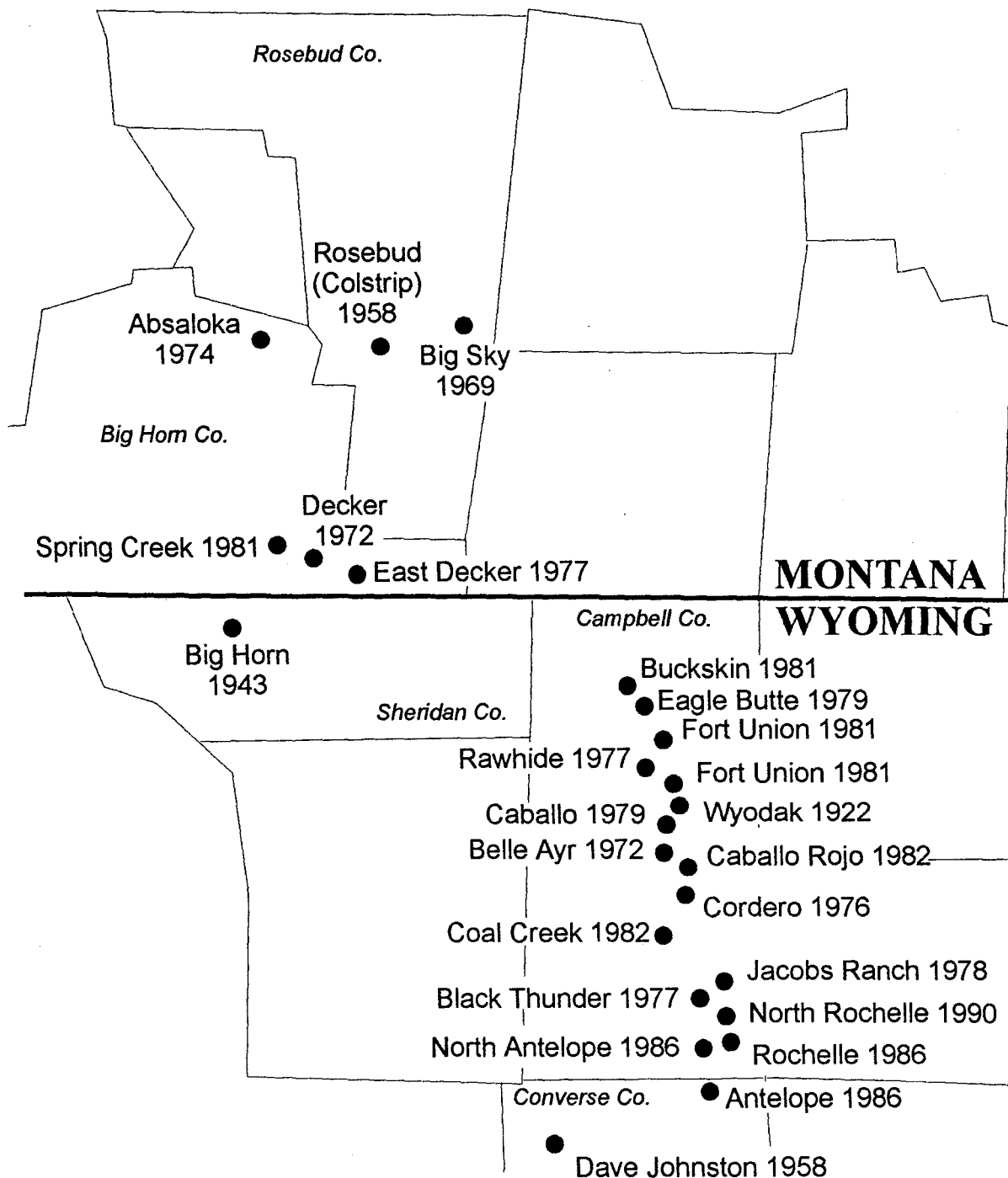


Note: Years indicate mine start up years.

Sources: BXG, Inc, *Western Coal Series Powder River Basin 1995-2005*, June 1994
1992 *Keystone Industry Manual*

EXHIBIT five
DATE March 1, 1995
HB SB 284

PRODUCING MINES IN POWDER RIVER BASIN 1993



Note: Years indicate mine start up years.

Sources: BXG, Inc, *Western Coal Series Powder River Basin 1995-2005*, June 1994
1992 *Keystone Industry Manual*

HISTORICAL PRB COAL PRODUCTION

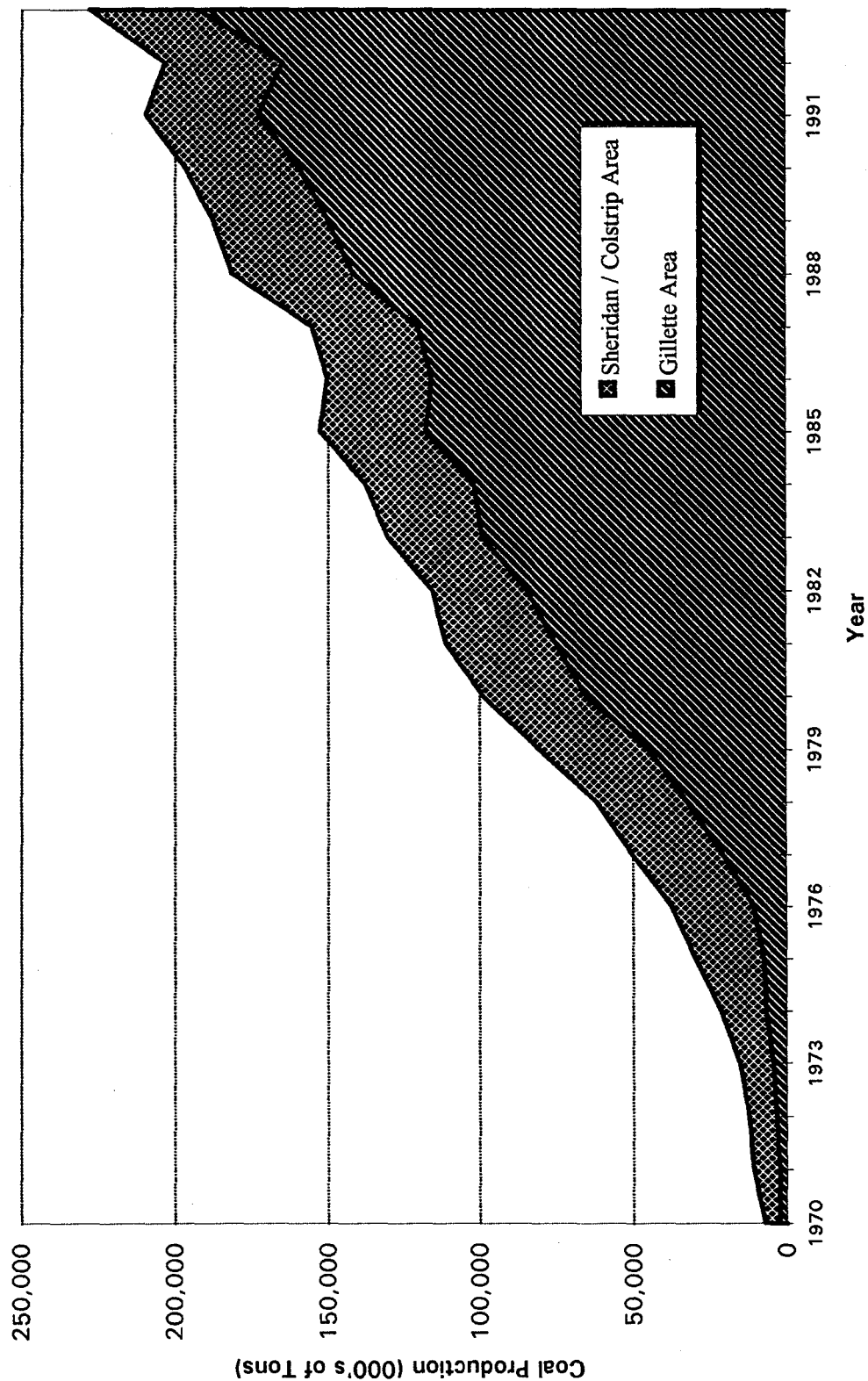


Exhibit 6
3-1-95

MONTANA SECOND JUDICIAL DISTRICT COURT, SILVER BOW COUNTY

MONTANA POWER COMPANY, a
Montana corporation,

Plaintiff,

vs.

MONTANA PUBLIC SERVICE COMMISSION,
head of the Department of Public
Service Regulation,

Defendant,

and

MONTANA CONSUMER COUNSEL,

Intervenor.

45-25
FILED

DEC 29 1994

BY L. MALONEY, CLERK
DEPUTY CLERK

No. 94-C-255

51-4

**FINDINGS OF FACT, CONCLUSIONS OF LAW,
ORDER, AND JUDGMENT**

On November 17, 1994, the Court heard oral argument on Montana Power Company's (MPC) Complaint filed pursuant to Section 69-3-402, M.C.A. MPC's Complaint challenges that portion of the Montana Public Service Commission's (PSC) decision in Order No. 5709e in which the PSC disallowed as operating costs approximately \$7 million of the \$35 million which MPC spends each year to purchase

ORIGINAL

*Talked w/ Frank Buckley
w/ M.T. Consumer Council. The 11.5%
returned after the*

coal from Western Energy Company (WECO). Attorneys Patrick Fleming and Marjorie Thomas argued for Plaintiff Montana Power Company. Attorney Denise Peterson argued for the Defendant Montana Public Service Commission. Attorney Mary Wright argued for Intervenor Montana Consumer Counsel (MCC). After considering the arguments of counsel and after reviewing the briefs and relevant portions of the record, the Court makes the following Findings of Fact and Conclusions of Law:

FINDINGS OF FACT

1. On June 21, 1993 Montana Power Company (MPC) filed an application with the Montana Public Service Commission (PSC) for authority to increase its electric utility rates by more than \$36 million to produce total annual revenues of \$443 million. MPC is a major electric and gas utility serving a large service territory in the State of Montana. The proceeding on the rate increase application was designated PSC Docket No. 93.6.24.

2. Montana Consumer Counsel (MCC) intervened in PSC Docket No. 93.6.24 on behalf of MPC's ratepayers. Pursuant to Procedural Order No. 5709a, MPC and MCC (jointly, Parties) prefled testimony and exhibits sponsored by witnesses. The PSC convened a public hearing beginning on January 18, 1994 in which it heard testimony and admitted prefled testimony, specified data responses (discovery) and exhibits. The PSC issued Final Order No. 5709d on April 28, 1994. Parties filed motions for reconsideration on numerous issues. In Order No. 5709e, issued June 15, 1994, the PSC affirmed its Final Order, with some minor modifications.

3. Under the authority of Sections 2-4-701, et seq. (Montana Administrative Procedures Act or MAPA) and 69-3-401, et seq. (Review of PSC actions) M.C.A., MPC filed its Complaint in this Cause on June 17, 1994. MPC's single issue for review is the PSC's disallowance of \$7 million of coal expense for ratemaking purposes.

4. On July 6, 1994 the PSC filed its Answer and various motions, including requests for recaptioning the pleading as a petition for judicial review, joining the MCC as a necessary party under Rule 19, Mont. R. Civ. P., and setting a briefing schedule and oral argument. MCC filed a motion to be joined as a necessary party or alternatively, as an intervening party, pursuant to Rule 24, Mont. R. Civ. P., with an Answer on July 8, 1994. The PSC submitted the Administrative Record on August 22, 1994.

5. MPC filed a Motion for Summary Judgment and a Motion for Injunctive Relief on September 21, 1994. On September 28, the PSC and MCC filed motions opposing summary judgment and injunctive relief and requested a schedule for briefing and oral argument.

6. By Order filed October 17, 1994 this Court granted MCC's request for intervenor party status, denied MPC's Motion for Summary Judgment, dismissed without prejudice MPC's request for an injunction, denied the PSC's request for recaption of the pleading as judicial review under MAPA, and set a schedule for briefing and oral argument. Granting MPC's request for review under Title 69, Chapter 4, M.C.A., this Court designated MPC's Brief on its Motion for Summary

Judgment as its Brief in support of its position as Plaintiff on its Complaint, for the Court's review of the PSC decision on the coal issue in Order Nos. 5709d and 5709e.

7. This Court heard oral argument on November 17, 1994. The Court has considered the transcript of the proceeding in Docket No. 93.6.24, the exhibits and discovery admitted in this matter, the arguments in briefs and oral presentations, and applicable statutory and case law. In its review of the record and the law, the Court finds that Plaintiff MPC has failed to sustain its burden of proof under Section 69-3-402, M.C.A., to present clear and convincing evidence of manifest error. MPC has not overcome the statutory presumption in Section 69-3-110(2), M.C.A., that the decision on coal expense in Order Nos. 5709d and 5709e was lawful and reasonable. Mountain States Telephone & Telegraph v. Public Service Commission, 135 Mont. 171, 178, 338 P.2d 1044 (1959). The Court's reasoning is as follows:

8. As part of its cost of service, MPC had sought to recover from its ratepayers \$35 million in coal expense on a contract with its subsidiary WECO. On this issue, MPC presented the testimony of Mr. Robert P. Gannon, President and Chief Operating Officer of MPC's Utility Division, Mr. Jerrold P. Pederson, Vice President and Chief Financial Officer of MPC and its subsidiaries, including Entech and WECO, and Drs. John Landon and Mark Berkman, from National Economic Research Associates (NERA), who testified jointly.

9. Drs. Landon and Berkman recommended the use of the market price method to determine annual coal expense of \$35 million to be allowed into rates. Mr. Gannon had stated that the Landon/Berkman testimony would show that coal

companies' profits are unrelated to a reasonable price of coal. The PSC found that their testimony was not credible on market price analysis. They had not done a careful reading of the authority they had relied on, Dr. William F. Shepherd. After prefiling testimony and vehemently denying MCC's position in Response Testimony, Dr. Berkman attempted to correct his testimony after reviewing Dr. Shepherd's treatise. On cross-examination he admitted that MCC's witness, Dr. Wilson, accurately characterized Dr. Shepherd's position in support of rate of return method as an appropriate indicator of market power. The Court finds that the PSC's rejection of the Landon/Berkman joint testimony was based on substantial evidence in the record. Trans., pp. 582-583.

10. MCC sponsored the testimony of Dr. John W. Wilson and Mr. C. David Kirby from J. W. Wilson & Associates on the coal expense issue. To reflect the subsidiary nature of the transaction, Dr. Wilson recommended that the PSC use the rate of return method to adjust the amount of coal expense recovered in rates. Dr. Wilson proposed that the PSC allow into rates an amount reflecting rate of return to WECO of 11.5 percent on its utility coal sales to MPC. Mr. Kirby recommended that the PSC disallow \$7,027,675 of coal expense for ratemaking purposes using the rate of return method.

11. The Court finds that the PSC must apply intense scrutiny to utility-subsidiary transactions, regardless of the claim that the subsidiary supplies the utility as a result of an arm's length transaction negotiated by a generating partner. Montana-Dakota Utilities Co. v. Montana Department of Public Service Regulation,

231 Mont. 118, 752 P.2d 155 (1988). The PSC would not have been obligated to use a market price method even if there had been an arm's length transaction, so long as a rate of return method was supported by substantial evidence.

12. The Court nevertheless finds that MPC failed to demonstrate an arm's length agreement or a competitive marketplace when the contract was negotiated in the early 1970's when MPC purchased said coal rights. MPC arranged for construction of the generating plants at Colstrip knowing that it had the coal resource. The boilers for these plants were specifically designed to burn coal from the coal mines at Colstrip. There was no evidence that the plants could burn coal from other producers or that there was an alternative supply of coal that could be used in these boilers. The Court finds that MPC's early decisions to site their generating facilities at its coal source and to design the facilities specifically to burn WECO coal give WECO a market advantage that precludes a finding of an arm's length agreement or a competitive marketplace for coal supplies to the Colstrip.

13. Testimony and exhibits establish the history on the relationship between MPC and WECO. MPC acquired the Colstrip coal leases from the Northern Pacific Railroad in 1959 as a contingency to meet future generation needs. Exh. MCC-4, pp. 6-7. MPC planned to use Colstrip coal in its Corette plant in 1964, two years before beginning construction. Not until after WECO's creation in 1966 did MPC's reports indicate that the coal resource might supply other than MPC's generating needs. MPC did not acquire the leases contemplating a non-utility operation. Exh. MCC-4, pp. 7-8.

14. Puget Sound Power and Light (Puget), a co-owner of Colstrip units, was

not responsible for the decisions to locate power plants and negotiate for purchase of coal for the generating units at Colstrip. Puget became a joint venture partner only after MPC had determined the plant's location and source of coal. Exh. MCC-4, pp. 6-10. MPC developed plans and ordered equipment for Colstrip I by 1970, began construction in 1971, and entered into an agreement in 1972 with Puget to develop the plant as a joint venture, backdating documents so that Puget would share in all project costs. Exh. MCC-4, p. 9.

15. In December 1991, Entech's board of directors approved a plan to reorganize the corporate structure of WECO, reducing WECO's assets and stockholders' equity and transferring most of WECO's non-Colstrip business operations to Entech, a wholly owned subsidiary of MPC. The transferred assets earned very low rates of return. Trans., p. 660. WECO now is more nearly a pure Colstrip coal mining operation. Exh. MCC-6, Exprg. testimony, Kirby, pp. 4-5. WECO's financial statements now present an accurate picture of its profits from coal mining. Exh. MCC-6, pp. 4-7. WECO had increased earnings of \$6.5 million over a previous case, reflecting WECO's booked results without non-Colstrip operations and accounting for 40 percent of the increase in the PSC's adjustment. Trans., p. 660. While profitability increased, the number of tons ordered and test period fuel expense remained at the same level as in MPC's 1984 application to include Colstrip 3. Exh. MPC-25, p. 5. As MPC admitted in its Brief, WECO now earns 87 percent profit on its investment. Exh. MCC-6, p. 8, Trans., p. 661.

16. In the reorganization, WECO dividended \$146 million to Entech. As of

December 31, 1992, WECO had a liability on its books of over \$80 million for accrued reclamation costs related to coal mined through 1992. The record shows in Data Response MCC 1-105, supplied by Mr. Pederson, that WECO had enough resources to pay its reclamation costs without the \$80 million needed for a stand-alone WECO. Mr. Pederson failed to include the income earned on the transferred assets. Therefore, the court rejects MPC's argument that the captive coal method is overstated as a result of WECO being able to dividend \$80 million of reclamation costs because of its huge coal mining profits.

17. This decision follows precedent in administrative, district court and Montana Supreme Court decisions in affirming the PSC's right to choose the rate of return method to determine the appropriate level of coal purchase expense to recover from the ratepayer. In 1981, the Supreme Court remanded the PSC's decision to disallow a portion of coal purchase cost recovery based on the rate of return method. The Court, at that time stating it preferred a marketplace cost of coal approach, nevertheless recognized that the PSC had the right to choose the method, so long as the decision was supported by sufficient evidence. Montana-Dakota Utilities Co. [MDU] v. Bollinger, 193 Mont. 508, 632 P.2d 1086 (1981).

18. In 1983 and 1988 the Supreme Court maintained this posture and again held that the PSC had the right to choose the rate of return method to determine an appropriate coal purchase expense on a subsidiary transaction. In two cases involving MPC and MDU, the Supreme Court affirmed the PSC's orders disallowing part of the rate increase request based on the rate of return method for the utilities' coal

purchases from subsidiary coal-producing companies. Montana Power Company v. Department of Public Service Regulation, 204 Mont. 224, 665 P.2d 1121 (1983) and Montana-Dakota Utilities Co. v. Montana Department of Public Service Regulation, 231 Mont. 118, 752 P.2d 155 (1988).

19. Under the standard of review of findings of fact in a PSC decision under Sections 69-3-401 et seq., M.C.A., the Court is limited in reviewing a PSC decision because of the technical nature of rate hearings and the agency expertise required to weigh and balance expert opinion to render decisions. The Court may not substitute its judgment for that of the PSC when the PSC has been presented evidence presented by experts. State Department of Public Service Regulation v. Montana Irrigators, Inc., 209 Mont. 375, 381, 680 P.2d 963 (1984). This decision was unanimously rendered by the five member Commission. In rate cases, the PSC is the judge of the fact and the court only determines questions of law. Montana Dakota Utilities Co. v. Montana Public Service Commission, 243 Mont. 492, 795 P.2d 473 (1990).

20. MPC has the burden to present clear and convincing proof showing manifest error before overcoming the presumption that the order was lawful and reasonable. Mountain States T & T, 135 Mont. at 178. On the allegation that the order was unreasonable, MPC has failed to meet its burden to demonstrate manifest error in the disallowance of \$7 million of the \$35 million coal purchase cost.

21. In restructuring, WECO declared dividends to its parent Entech (a wholly owned subsidiary of MPC), resulting in a reduction of \$146 million in retained

earnings. WECO transferred to Entech the far less profitable investment in non-Colstrip business, thus presenting a more accurate picture of what the coal-produced profits of the coal company amounted to. Exh. MCC-6, pp. 4-7. WECO is highly profitable at an 87 percent rate of return. WECO also enjoyed a \$6.5 million increase in earnings over the preceding rate case, but costs and tons ordered remained at the level of the 1984 proceeding. Exh. MPC-25, p. 5.

22. The PSC's use of the rate of return method resulted in a higher disallowance than in previous MPC rate proceedings. When the actual rate of return for the coal-producing subsidiary became apparent, the PSC recognized that the disallowance in the past proceedings should have been greater. Order No. 5709d, Paragraph 212, Kirby, Response, pp. 3, 5, 7 and 8; Gannon, Direct, p. 11; Pederson, Direct, p. 2. The method used, when applied to the facts in this proceeding, did not produce an unjust or arbitrary result. Montana Power Company, 204 Mont. at 228-29.

23. The PSC's use of an 11.5 percent rate of return for WECO was reasonable since firms in the fuel industries, of which 15 were in the coal industry, were generally in the 9-12 percent range. The PSC did not use the "California approach," i.e., treat the subsidiary as part of MPC and use the rate of return on equity of 11 percent allowed MPC in Docket No. 93.6.24. The PSC used 11.5 percent rate of return from PSC Docket No. 90.6.39 on the portion of WECO's sales to MPC, reasoning that this level would still be reasonable in light of the declining cost of capital since that case.

24. Plaintiff MPC has not raised any issue with the findings of fact. Rather, MPC faults the PSC for believing MCC's expert opinion on the underlying facts over that of MPC's witnesses. In determining whether the order is lawful, the applicable standard of review is whether the PSC's interpretation of the law is correct. Steer, Inc. v. Department of Revenue, 245 Mont. 470, 474, 803 P.2d 601 (1990) and Mountain Water v. Montana Public Service Commission, 254 Mont. 76, 79, 835 P.2d 4 (1992). Weighing and balancing expert opinion is under the purview of the PSC. The PSC correctly interpreted Montana case law in using the rate of return method, accepting MCC's expert opinions and rejecting MPC's testimony for sound reasons.

25. The Court finds no evidence that the overall rates in Order Nos. 5709d and 5709e were set so low as to be confiscatory and deprive the utility of its property without due process of law. MDU v. PSC, 243 Mont. at 496. The rate order has met the standard of the United States Supreme Court: it is not the theory but the rate order as a whole that determines whether it is confiscatory. Duquesne Light Co. v. Barash, 488 U.S. 299, 103 L.Ed.2d 646, 109 S.Ct. 609 (1989).

CONCLUSIONS OF LAW

1. The Findings of Fact are incorporated as Conclusions of Law.
2. In determining whether the order is lawful, the applicable standard of review is whether the PSC's interpretation of the law is correct. Steer, Inc. v. Department of Revenue, 245 Mont. 470, 474, 803 P.2d 601 (1990) and Mountain Water v. Montana Public Service Commission, 254 Mont. 76, 79, 835 P.2d 4 (1992).

3. The PSC has the right to choose the method to determine the level of

coal expenses MPC can recover from its ratepayers, so long as the decision is supported by sufficient evidence and does not produce an unjust or arbitrary result. A competitive marketplace, which the Commission found not to be present in this case, would even so not mandate use of a market price method to determine the allowable coal expense. Montana-Dakota Utilities Co. [MDU] v. Bollinger, 193 Mont. 508, 632 P.2d 1086 (1981); Montana Power Company v. Department of Public Service Regulation, 204 Mont. 224, 665 P.2d 1121 (1983); and Montana-Dakota Utilities Co. v. Montana Department of Public Service Regulation, 231 Mont. 118, 752 P.2d 155 (1988).

4. The PSC must apply intense scrutiny to all utility-subsidary transactions. Montana-Dakota Utilities Co. v. Montana Department of Public Service Regulation, 231 Mont. 118, 752 P.2d 155 (1988).

5. The Court may not substitute its judgment for that of the PSC when the PSC has weighed evidence presented by experts. State Department of Public Service Regulation v. Montana Irrigators, Inc., 209 Mont. 375, 381, 680 P.2d 963 (1984).

6. Plaintiff MPC has failed to sustain its burden of proof under Section 69-3-402, M.C.A., to present clear and convincing evidence of manifest error in disallowing \$7 million of coal purchase expense from its subsidiary, WECO, based on the rate of return method. MPC has not overcome the statutory presumption in Section 69-3-110(2), M.C.A., that the decision on coal expense in Order Nos. 5709d and 5709e was lawful and reasonable. Mountain States Telephone & Telegraph v. Public Service Commission, 135 Mont. 171, 178, 338 P.2d 1044 (1959).

7. Order Nos. 5709d and 5709e comply with the constitutional requirement to set reasonable rates which are not confiscatory and do not deprive MPC of its property without due process of law. There is no evidence that the overall impact of the rate order as a whole is confiscatory. Duquesne Light Co. v. Barash, 488 U.S. 299, 103 L. Ed. 2d 646, 109 S. Ct. 609 (1989); MDU v. PSC, 243 Mont. at 496.

If this Court were to rule in favor of the Montana Power Company on this issue, it would be reversing itself on its previous ruling in Montana Power Company v. Department of Public Service, 204 Mont. 224 (1983). There, this Court ruled against MPC on the same basic issue; the PSC's right to choose the method of determining the reasonableness of the price paid by MPC for Western Energy coal.

In affirming this court's ruling, the Supreme Court ruled that:

"... substantial evidence existed to support the Public Service Commission's decision to disallow part of requested increase upon assessing reasonableness of price paid by power company to its wholly owned subsidiary for coal by 'rate of return' method, requiring examination of reasonableness of return being earned by subsidiary on its sales to parent, rather than by 'market price' method, requiring examination of price charged in marketplace for similar sales in comparison to those being charged by subsidiary to parent, notwithstanding that under power company's presentation of market price method, competitive marketplace was established."

Nothing basically has changed from the 1983 case to the instant case, other than the amount of the disallowance, nor will this Court's ruling be changed.

ORDER AND JUDGMENT

WHEREFORE, THIS COURT AFFIRMS Public Service Commission's decision in Order Nos. 5709d and 5709e, PSC Docket No. 93.6.24, which denies Montana

Power Company recovery from ratepayers of approximately \$7 million out of \$35 million in coal purchase expense paid to its subsidiary Western Energy Company, based on the rate of return method of determining the appropriate level of coal purchase expense from a utility's subsidiary.

Let Judgment enter accordingly.

DATED this 21st day of December, 1994.



Mark P. Sullivan
District Court Judge

MPSPSC.2

DEPARTMENT OF REVENUE



TED SCHWINDEN, GOVERNOR

MITCHELL BUILDING

STATE OF MONTANA

HELENA, MONTANA 59620

April 27, 1988

CERTIFIED RETURN RECEIPT REQUESTED

David S. Smith, Treasurer
Western Energy Company
16 East Granite
Butte, MT 59701

RE: Assessment of additional Coal Gross Proceeds for the
1983 thru 1986 production years.

Dear Mr. Smith:

This letter with the attached schedules constitutes notice of the above referenced assessment. This assessment is issued in accordance with Section 15-8-601, Montana Code Annotated. The additional taxable value results primarily from the inclusion of additional revenue as described below.

1) The value of the coal sold to Colstrip 1 & 2 partners (Montana Power Co and Puget Sound Power & Light) was imputed for 1983 since the coal sold in the non arm's-length transactions was priced lower than the market price established by similar agreements with Northern States Power and Wisconsin Power and Light. The values for Montana Power Co and Puget were imputed by using six month weighted averages from NSP and WP&L sales. Values were not imputed for 1984-1986 since the price per ton for sales to related parties were at or above prices charged to unrelated parties.

2) Oiling revenue was included thru the third quarter of 1983. After that it has been excluded. Section 15-35-107(1)(b) M.C.A. which became effective October 1, 1983 allows an adjustment to value for coal that has been processed.

3) Additional sales revenue has been included which was received from customers for work done at the mine and for a coal operations study. These relate to the coal sales and should be included as part of the total coal sales revenue.

4) Information regarding the contract commitment revenue was requested, however, none was provided. Consequently, there is no alternative but to include it in the value of the coal f.o.b. the mine. This does not include deferred revenue for Corette sales. This revenue will be taxed in the appropriate tax period.

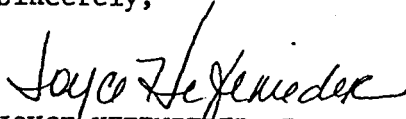
David S. Smith, Treasurer
April 27, 1988
Page 2

Additional adjustments resulted from a total recomputation of contract sales price based on the adjusted coal sales revenue for the tax period. This includes the royalty exemption as a deduction for contract sales price. Any minor differences which occur in the detail are due to rounding.

You are advised that according to Section 15-8-601, a request can be made for an assessment review conference within 30 days of the date of this notice. If a request for conference is not received within 30 days, the assessment becomes final and will be certified to the County Assessor.

Please direct any questions you may have concerning this assessment to one of the undersigned.

Sincerely,



JOYCE HEFENIEDER, Revenue Agent
Natural Resource & Corporation Tax Division

Reviewed and Approved by:

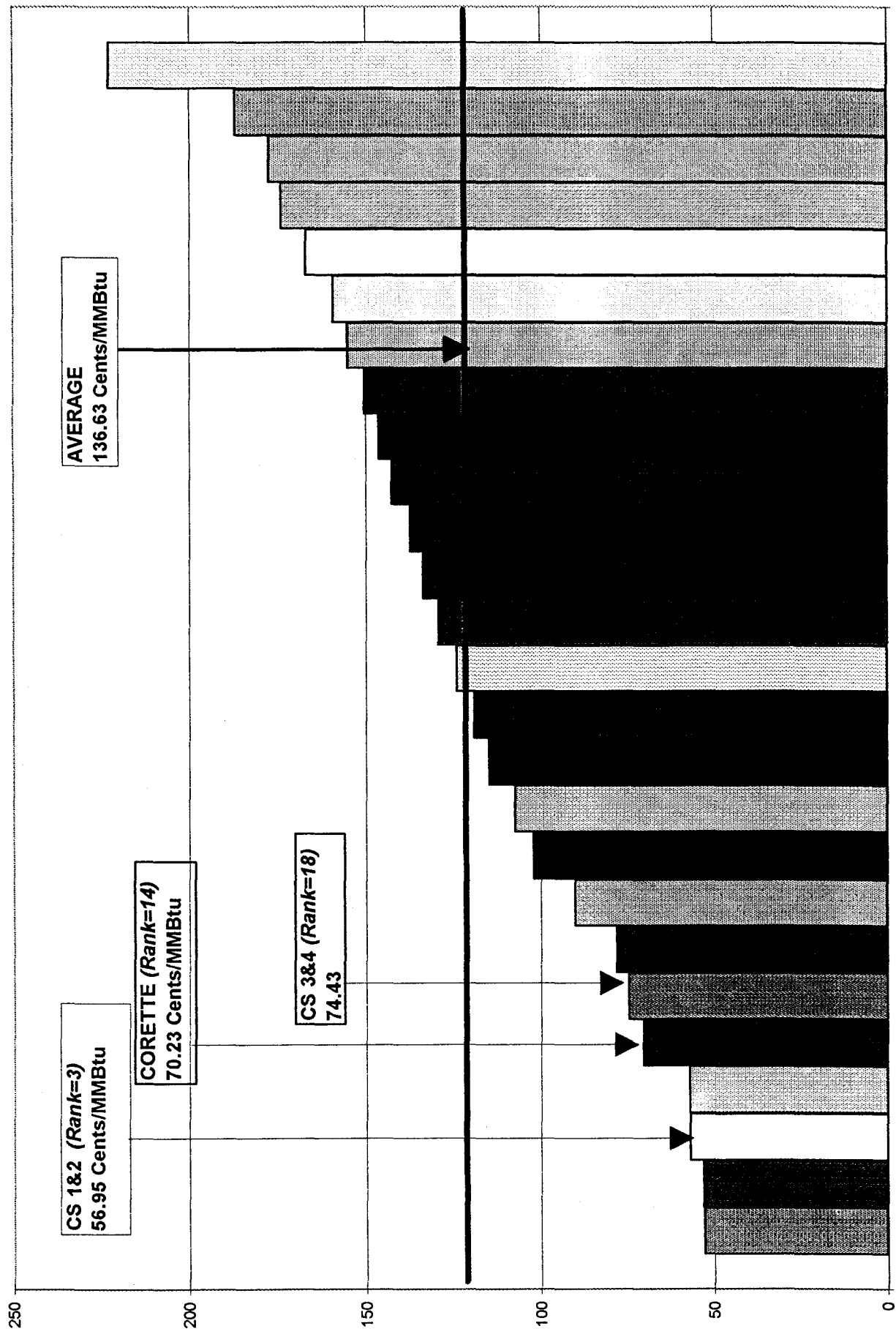


RICHARD J. MARBLE, Chief
Solid Minerals Bureau
Natural Resource and Corporation Tax Division

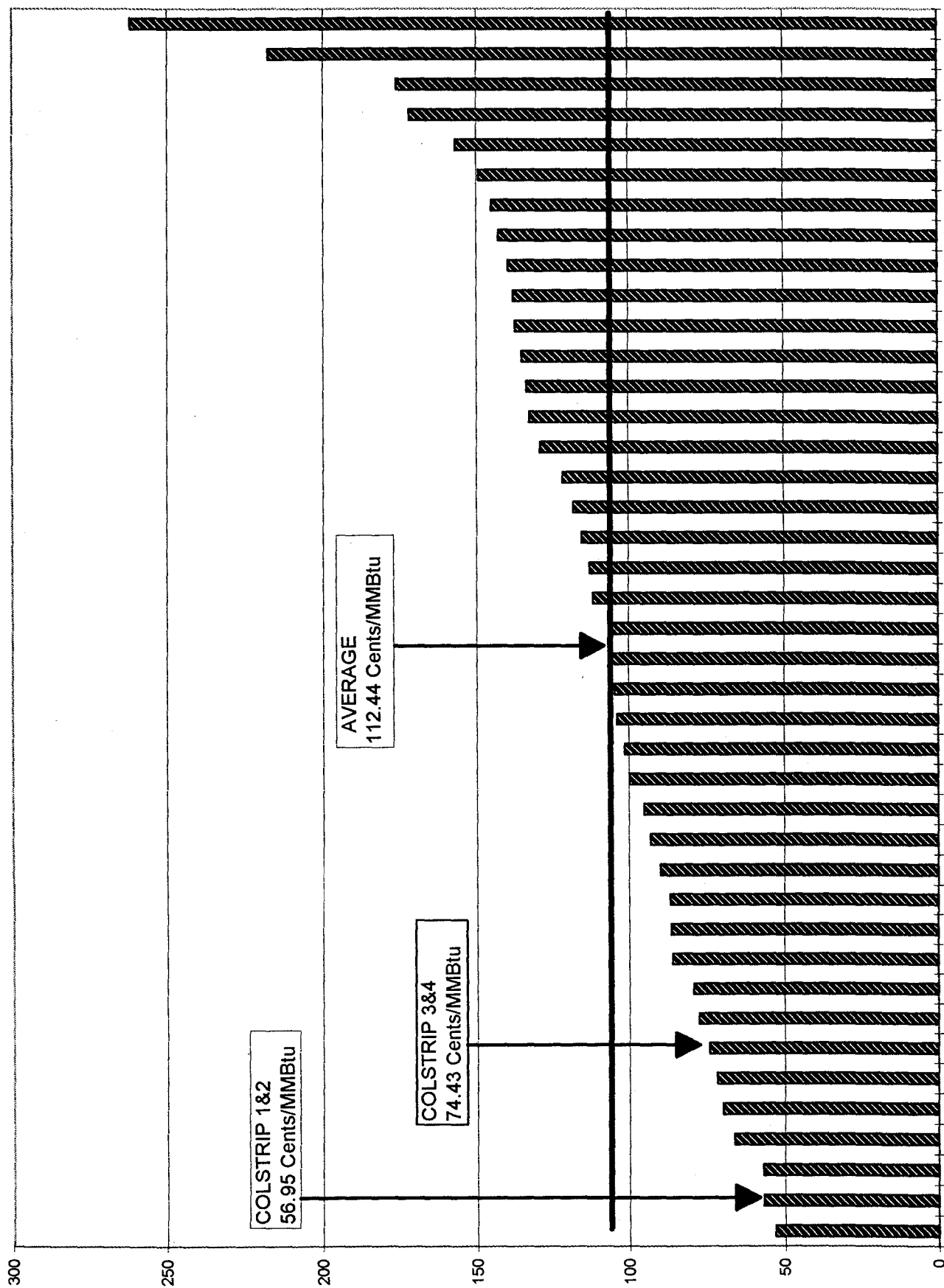
Attachments

JH/rjm/tm

1994 CENTS/MMBtu FUEL COSTS FOR 428 COAL FIRED PLANTS



1994 CENTS/MMBtu FUEL COSTS FOR 40 MINE MOUTH COAL FIRED PLANTS



Kelly Wiedrich
Business Agent
IUOE Local 400
530 South 27th Street
Billings, MT 59101
Office 406-252-7966
Home 406-652-6372

February 27, 1995

House of Representatives
Capital Station, Box 201701
Helena, MT 59620-1701

Honorable Representative,

I appreciate how busy your schedule is this year and would like to thank you, in advance, for allowing me a little of your time to try and explain the position the miners, employed at the Rosebud Mine, have taken on SB 284.

Ten members of Local 400 who work as miners for Western Energy Company (WECO) took time off of work Monday and Tuesday, February 6th and 7th, without pay, to gather information on SB 284 and voice their concerns. Monday evening we met with PSC member Bob Anderson, PSC Chairwoman Nancy McCaffree, Representative Bill Ryan, and Representative William Menahan. These are the points we stressed with them and other members of the PSC, House, and Senate.

1) In the Chet Blaylock and Nancy McCaffree editorials to the Billings Gazette they state that the \$7 million that was disallowed is only on the 20 percent of WECO's coal that is sold to MPC. This statement is misleading for the following reasons. 70% of all the coal mined at the Rosebud Mine in 1994 was burnt at the Colstrip power plants, units 1-4. Because one long term, out of state, coal contract for over 1.2 million tons per year expired December 31, 1994 and another long term, out of state contract, for about 1 million tons per year is scheduled to run out at the end of October 1995 the percentage of coal sold to the Colstrip units will be closer to 80%. The inference of the editorial's is that the disallowance on the 20% of the 70% will have no bearing on the remaining 50% of the coal sold to the other partners in Colstrip units 1-4. The fact that the MT PSC has determined that WECO is overcharging for their 20% of the 70% total will be used by the partners to try and drive down WECO's price to them. Therefore the PSC decision has the potential to affect 100% of the 70%. These percentages do not include the coal burned at the Billings Corette Plant or the Rosebud Power Plant located just north of Colstrip.

1.

EXHIBIT Seven
DATE March 1, 1995
HB SB 284

2) These editorials also state that MPC built the Corette plant and Colstrip Units 1-4 to burn only coal mined by them. This is a very broad and misleading statement. Every coal power plant ever built was designed to burn coal of general specifications. As long as the specific coal burned or blend of specific coals burned is within the plus and minus parameters of the boiler design they can burn other coals. To prove this you need only contact the many utilities that are continually buying different coals or coal blends for test burns at their facilities. In addition to this there are some inexpensive adjustments and modifications that can be made to a power plants boilers and other components which can broaden the range further. The Colstrip Units partners ran a successful test burn of coal provided by the Big Sky Mine last year. I believe the coal mined at the Absaloka Mine at Sarpy Creek would also fit the parameters of the Colstrip Units burn system. This contradicts statements made which claim that market price comparisons cannot be made because no one mines coal that can be burned in the Colstrip Units.

3) I have heard nothing which acknowledges that WECO does have a transportation cost in delivering coal to the Colstrip units. They maintain and operate 4 1/2 miles of conveyor system.

4) I was told that the method the PSC uses does not take into consideration the future costs WECO will be forced to incur for reclamation. The majority of those expenses will be incurred at the closing of the mine.

5) The present system using the rate of return method does not provide any incentive to WECO to improve production or efficiency. The present system forces MPC to plan their whole corporate strategy around rate of return and not around increasing profits through increased production and efficiency. The present system is not conducive to Labor Management cooperation in pursuing increased production or efficiency.

Although I can provide no guarantees, I believe a market price principle could be used by WECO to increase profits to their stockholders by increased production and efficiency without driving up the costs to the consumer. Under this scenario I also believe that WECO could pass on a percentage of the savings to the consumer. And it is also conceivable that such reductions in the mine mouth price of Rosebud Mine coal could be used to get back into the national coal market.

I believe that the present system used by the PSC is a contributing factor to the Rosebud Mine losing almost all of their out of state customers. Big Sky Mine and Absaloka Mine, which survive in a market price world, have each made large gains in the last year selling coal comparable to the Rosebud Mine coal. Rosebud Mine is already scheduled to lay off as many as 100 employees due to their loss of the out of state market. I have been informed that the Rosebud Mine is expected to lose the majority of their remaining out of state coal sale contracts in the near future. WECO, in a market price scenario, should have a competitive edge since they mine more coal than the smaller, growing, comparable mines.

6) The implied suggestion that WECO could be sold and the PSC would not have the same control over the purchasing company has not been answered to my satisfaction. I believe there is a very serious chance that this is currently a viable option for MPC. If this were to happen the members of this Union, citizens of this state, would lose the protection afforded them under our bargaining agreement with WECO. Their jobs, Union affiliation, wages, working conditions, pension, and health insurance benefits would all be open to negotiation. It is conceivable that a purchasing company would rehire a high percentage of the miners now working there but it is also very conceivable that a certain percentage would have to move out of the Colstrip area or even Montana to find similar employment. It is also conceivable that a percentage of the currently employed WECO miners would opt to move on rather than work under the conditions offered by the purchasing company.

There are a number of variations to this scenario floating around.

What guarantees are there that MPC won't decide that there are better investment opportunities selling Wyoming coal or investing in other markets? Dennis Washington and others have shown interest, in the past, in purchasing WECO.

7) SB 284 does not take any authority away from the PSC in their positions as advocates for the consumer other than requiring them to use a market price principle.

8) Enclosed is a comparison sheet of the productivity of the Rosebud Mine compared to the other Montana coal mines. As you can see, productivity at the Rosebud Mine has been stagnant compared to the improvements made at the other Montana mines. As stated earlier, there is no incentive for WECO to improve these numbers.

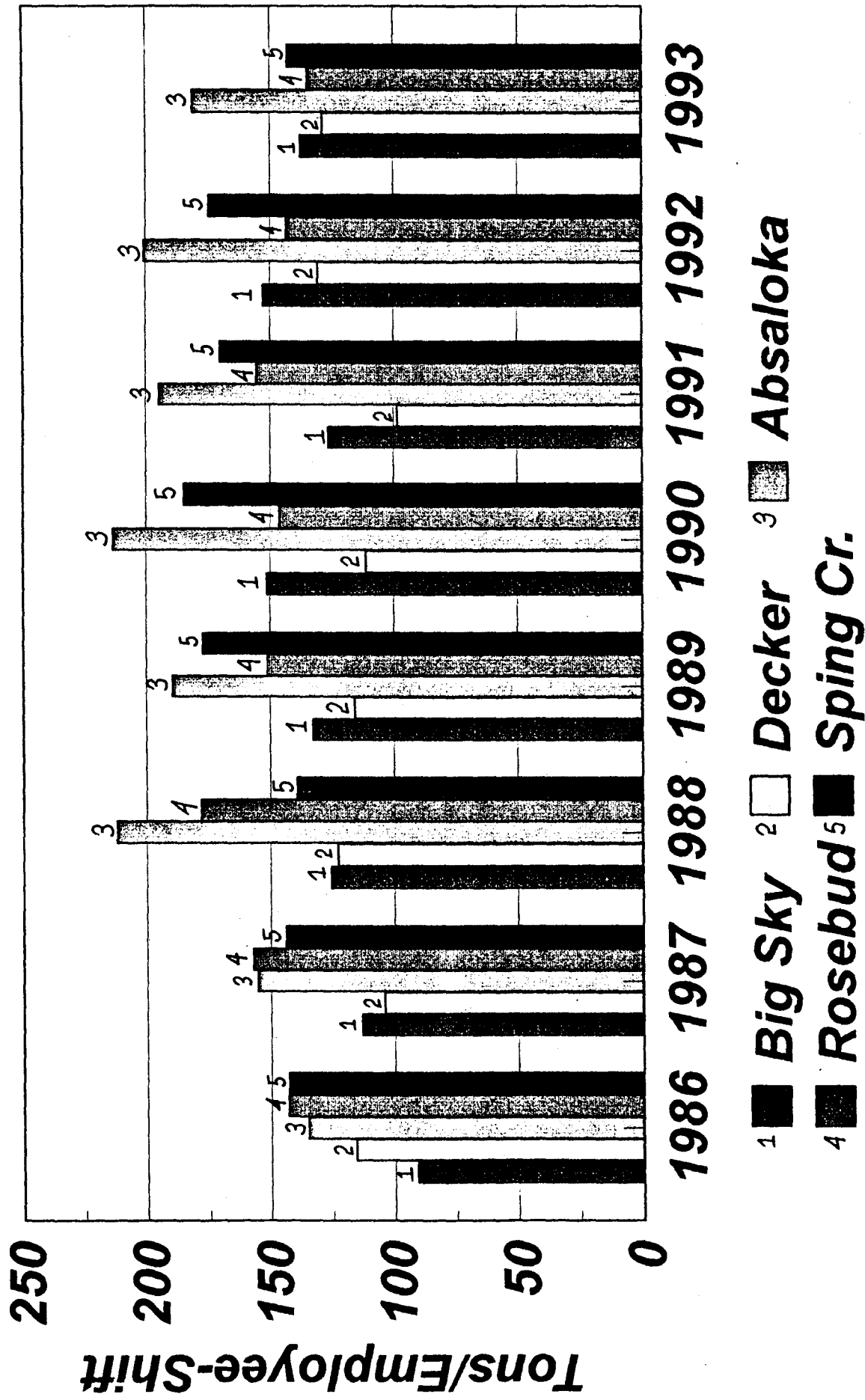
Honorable Representative please consider the possible future impacts of not changing the present system to one which treats WECO like all other coal mines in the state of Montana. Please ratify SB 284.

Sincerely yours,


Kelly Wiedrich

WESTERN ENERGY COMPANY

PRODUCTIVITY



Good morning Chairman & committee members

I am Jim Shaffer, I work for Western Energy Company as a mechanic.

In January of this year Western Energy sent a memo to the crew shacks ~~in~~ throughout the mine telling the workforce that MPC may sell Western energy because of a coal price disallowance by the PSC. This came to light after a rate case hearing.

In January I came to Helena to hear another bill in committee. While I was in Helena I took the time to stop in at the PSC office to visit with someone about this disallowance thing that I didn't fully understand. I talked to Nancy McCaffrey to some length. She explained to me how much of portion of overall Weco coal sales^{is} effected - 20%. She told me ~~the~~ about the rate of return method used with MPC for profitability. She told me that the Montana Consumers Counsel felt that MPC's subsidiary coal supplier should be held at a rate of return method at ~~10.5%~~ 10.5%. She said that the PSC allowed 11.5% profit the same as allowed for MPC. She said that in open market that Western Energy was getting an 87% profit on their coal^{sales}. She also told me that the PSC was a mediator between MPC & the MCC (Montana Consumer Counsel). Nancy gave me the phone # to the MCC. The next day when I got home I called the MCC & talked to Mr. Robert Nelson. In talking to Mr. Nelson

did with Nancy McCaffree at the PSC, ~~at~~ with the exception of when we talked about the sale of Weco, Mr. Nelson told me that if MPC was to sell Weco that in some way that I didn't understand that the MCC ^{profits of} would somehow take a portion of that sale.

Now in my conversations with ~~these~~ PSC & the MCC I didn't feel right. Because Weco is a subsidiary of MPC the PSC is going to intervene into 20% of Weco's business. The PSC said that Weco makes 87% profit! Now when I heard debate in the Senate I found out that in the mine plan it is estimated ~~that a~~ 15% to 18% profit, ^{over the life of the mine.} I also found out in debate that the PSC did not allow for reclamation costs which is a large overhead cost to Weco.

In my conversation with Nancy McCaffree at the PSC we talked about the scenario of if another company operating the same mine site as Weco, would the PSC be able to regulate the ~~allow~~ allowable coal costs? She said yes. This does not sound right to me. How could the PSC scrutinize a totally independent mine operator? Wouldn't the PSC have to allow costs of ~~market~~ market coal costs?

Western Energy should be allowed to do business as would any other mine operator. The PSC should allow for market coal costs in MPC's consumer rates.

Should MPC ~~decide~~ ^{would bid the} to Sell Western Energy the new operator ~~would set~~ coal price to be accepted by MPC. A market price, the coal costs would be allowed in rates to the consumer. This would be a rate increase

to scrutinize an independent operator. Since this is very possible and probable, would it make sense to allow Weco to operate on a market value and save the employees of Weco the turmoil of a new operator of this mine site. Who would know who the new operator will be and ~~what~~ how would they do business.

The Turn over of operators at this mine site could and probably would be devastating. There are no guarantees of who would be rehired to continue to work at this mine site. The workers would face reapplying for jobs, possible loss of wages, loss of accrued vacation time, possible loss of deferred savings, loss of participation in stock purchases in MPC, ESOP. (Employee Stock Option Plan). Changes of medical coverages i.e. preexisting conditions to a new plan, loss of accrued retirement benefits. Basically we would have to start over in a new job.

I feel Western Energy is a very good employer. They provide me and my family with good wages and benefits and a sense of direction for me to continue my career in the coal mining industry. With Western Energy I have good incentive to work hard and professionally in fair trade for wages and benefits.

I feel Western Energy should be allowed to participate fairly in the coal mining industry. MPC should be allowed compensation for coal costs at market values and have to consider selling off a competitive mining subsidiary.

Regrettably I feel a rate increase is inevitable one way or another. Please don't throw away break something that works & works good for who knows what else.

Testimony by: Nancy McCaffree, Chair
Public Service Commission

Before: House Committee on State
Administration
S.B. 284

Date: 1 March 1995

Mr. Chairman and members of the Committee, I appreciate the opportunity to appear before you today.

Before casting your vote, It is important that you understand why the Commission disagrees with Montana Power.

The Commission regulates Montana Power to ensure its has reasonable profits and adequate revenues. The Commission, balancing MPC's interests and that of the ratepayers, allowed MPC a fair rate of return on its investment and allowed MPC its reasonable expenses, including a reasonable expense of \$27 million for coal purchased from its affiliate, WECO. The Commission is concerned that MPC remain strong and healthy so that it can provide good service at reasonable rates. MPC is doing well. Two bond agencies upgraded MPC since the last rate increase. The Commission has allowed MPC reasonable expenses and a fair rate of return on MPC's investment.

Understandably, Montana Power wants to increase its revenues. One attempt has been to try to get more money for the coal WECO sells to MPC. For 15 years the PSC, supported by the courts, has said that MPC should receive a reasonable expense for this coal. MPC has argued in rate cases to recover a market price for coal from the ratepayers. However, because MPC's affiliate had

EXHIBIT 9
DATE 3-1-95
HB

no competitive market, the PSC used a "rate of return method" proposed by the Montana Consumer Counsel. Under the "rate of return" method, the PSC uses profit levels or returns on investment for coal companies like WECO to determine what is a reasonable expense to recover from ratepayers.

The "market" price they are asking for is really not what they want. What they want is their "contract" price. The "market" approach can be valid. Under current law the Commission has the authority to consider the market and routinely does so. The trick is determining a true market price in a case in which:

- ...the coal mine is owned by the utility;
- ...the coal mine was originally acquired to provide service to utility customers;
- ...the power plant was sited at the company's mine and designed to burn the company's coal;
- ...the market for coal may not have been competitive when the contract was signed; and
- ...the contract negotiation may not have been "at arms length"

In any rate case, the burden of proof lies with the company. The Commission makes a decision after exhaustive written testimony, discovery,

cross examination, written briefs and analysis. The issues are complex. The PSC listened to Montana Power's "market" arguments and saw that their witnesses did not support a market approach to the coal issue with believable testimony.

MPC has said that voting for this bill is not voting for a rate increase. The difference between MPC and the Montana Consumer Counsel position on coal in the current docket is \$5.6 million. We will not know the final effect of this legislation until parties have had a chance to address it in their testimony. However, if MPC's assumptions underlying the bill are correct (ie that the present value of the difference between the rate of return and market-price method is about \$50 million) it is fair to say you are being asked to vote for a rate increase. That is your right, but you should be informed about what you are doing.

Just a little aside: a long-time commissioner friend once told me, "if neither side is happy - that means we're doing a good job. Thank you for your time. The Commissioners and professional staff will be happy to answer questions.

Northern Plains Resource Council

Testimony on SB 284

Mr. Chairman, for the record my name is Nick Golder, I own a ranch near Colstrip, MT. I am a neighbor to Western Energy and have watched this process for many years. I am testifying as a member of the Northern Plains Resource Council.

This legislature is trying to get rid of wasteful government, yet, SB 284 proposes a method that will enable Montana Power/Western Energy Companies to continue wasteful business practices.

Western Energy, at Colstrip, currently has a ratio of 1 to 3 management to labor. 1 to 8 or 10 or 12 is generally considered healthy. If you add the Butte management to the Colstrip Western Energy figures, it will make this ratio look even worse.

Currently, maintenance at Western Energy is falling far behind. This spells real trouble for a business that is absolutely dependent on the equipment that produces the coal they sell.

Western Energy has just spent about 7 million dollars on a new computer system even though maintenance is far behind. I understand that it will take about a year to have the computer system up and running. There is a lot of question among knowledgeable people that this 7 million dollar investment will really pay for itself.

SB 284 would give Western Energy about 7 million dollars this year. This will pay for the new computer system that may or may not be needed. Is that what you intent to do with this bill, allow Western Energy to continue with their poor management practices and badly skewed priorities?

EXHIBIT Ten
DATE March 1, 1984
SB 284

MontPIRG

Montana Public Interest Research Group

360 Corbin Hall - Missoula, MT - (406) 243-2908

Testimony Against Senate Bill 284, March 1, 1995

Chairman Simpkins and members of the House State Administration Committee:

For the record, my name is J.V. Bennett, for the Montana Public Interest Research Group, or MontPIRG.

MontPIRG is a non-profit, non-partisan research and advocacy organization working for good government, consumer rights and sound environmental protection. MontPIRG represents over 4000 members in Montana, with 2200 student members, and is funded with membership donations.

As an organization advocating consumer interests and good government, MontPIRG rises in opposition to Senate Bill 284, which would limit the public Service Commission's ability to fairly regulate monopoly utilities.

Despite the abuses by monopolies in the early part of this century, we as a society have continued to allow some monopolies, like the Montana Power Company, as public utilities in order to efficiently provide vital services. At the same time we have recognized some sort of public oversight is required in the absence of competition on an open market. For this reason Montana instituted the Public Service Commission.

The Public Service Commission was instituted to have the expertise to gather and evaluate the information necessary to determine fair utility rates. The process is designed to insure the utility a fair profit and consumers a fair rate, in this case for electricity.

The Montana Power Company is asking the Legislature to skew the process by limiting the factors the Public Service Commission may consider in determining rates. By not allowing the Public Service Commission to consider the unique conditions of the Montana Power Company's relationship with its coal supplier, the Legislature would significantly increase the electricity rates to Montana consumers and business.

EXHIBIT 11
DATE 3-1-95
HB

Because the Montana Power Company buys its coal from a subsidiary under unique conditions which could not be met by another coal supplier, this bill's requirement for "market comparison" would not provide an accurate basis for determining rates. The result would be an unfair increase in electrical rates to customers who lack the option of switching to another supplier.

According to Montana Power it could pass on an additional \$50 million to rate payers if this market comparison methodology were used. This is \$50 million that will come out of the pockets of Montana families and business.

MontPIRG urges this committee to table Senate Bill 284. It's bad for consumers, bad for business and bad as a governmental policy. Bad for just about everybody, except Montana Power.

Exhibit 12
3-1-95

**TESTIMONY OF JOE PRESLEY
PRESIDENT OF WESTMORELAND RESOURCES, INC.
BEFORE THE HOUSE STATE ADMINISTRATION COMMITTEE
IN OPPOSITION TO SENATE BILL 284**

Hearing date March 1, 1995

MEMBERS OF THE HOUSE STATE ADMINISTRATION COMMITTEE, MY NAME IS JOE PRESLEY, PRESIDENT OF WESTMORELAND RESOURCES, INC. (WRI). WRI OPPOSES SENATE BILL NO. 284. WRI MINES COAL AT ITS ABSALOKA MINE, 25 MILES WEST OF COLSTRIP. WRI IS A CUSTOMER OF MONTANA POWER CO. (MPC) AND COMPETES WITH THEIR CAPTIVE COAL MINING SUBSIDIARY, WESTERN ENERGY (WECO), IN THE OUT OF STATE COAL MARKET. CURRENT MARKET PRICES FOR COAL SIMILAR TO WECO'S ARE IN THE RANGE OF \$5.00 TO \$7.00 PER TON AT THE MINE MOUTH OR FOB MINE. MPC IS PAYING WECO \$11 TO \$12 PER TON AT THE MINE MOUTH FOR SIMILAR COAL FOR THE COLSTRIP PLANTS.

IN THE LAST PUBLIC SERVICE COMMISSION (PSC) RATE CASE , THE PSC DECIDED THAT MPC WAS ENTITLED TO A GUARANTEED AFTER TAX RATE OF RETURN OF 11.5% ON INVESTED CAPITAL IN WECO. MOST MONTANA COMPANIES, INCLUDING WRI, WOULD LIKE TO HAVE A GUARANTEED AFTER TAX RATE OF RETURN OF 11.5% ON INVESTED CAPITAL. OBVIOUSLY, MPC IS NOT SATISFIED WITH THIS RETURN, AND THEY ARE ASKING THE LEGISLATURE TO GIVE THEIR STOCKHOLDERS A BETTER DEAL.

SUB-SECTION 2 OF SENATE BILL 284 IS DRAFTED TO ALLOW MPC TO CHARGE THE RATE PAYERS NOT ONLY THE FOB MINE COST OF COAL FROM ANOTHER MINE BUT ALSO THE RAIL TRANSPORTATION TO GET THE OTHER COAL TO THE COLSTRIP PLANTS. OF COURSE, THERE IS NO RAIL FREIGHT FROM WECO'S MINE TO THE POWER PLANTS. IN DETERMINING WHETHER MPC'S COAL COSTS ARE REASONABLE, SUB-SECTION 2 WOULD REQUIRE THE COMMISSION TO COMPARE THE UTILITY'S (MPC'S) COAL COSTS TO THE COSTS (EMPHASIS ADDED) THAT THE UTILITY

(MPC) WOULD HAVE INCURRED IF THE COAL HAD BEEN PURCHASED FROM A DIFFERENT SUPPLIER UNDER SIMILAR TERMS. USING COSTS OF COAL FROM ANOTHER MINE WOULD, IN MY OPINION, ALLOW MPC TO SAY THAT COSTS INCLUDES NOT ONLY THE FOB MINE COST BUT ALSO FREIGHT TO GET THE COAL TO COLSTRIP. THUS MPC WANTS TO PASS ON TO THE THEIR RATE PAYERS A PHANTOM TRANSPORTATION COST THAT THEY DO NOT INCUR.

MOREOVER, THEY DO NOT EVEN HAVE UNIT TRAIN UNLOADING FACILITIES TO UNLOAD UNIT TRAINS FROM ANOTHER MINE . SUB-SECTION 2 OF SB 284 REQUIRES THE PSC TO COMPARE THE COST FROM ANOTHER MINE TO WHAT MPC IS PAYING WECO. IF THERE IS NO WAY TO GET THE COAL TO THE POWER PLANTS FROM ANOTHER MINE, WHAT RELEVANCE DOES THIS SUB-SECTION HAVE? MPC CLEARLY WANTED TO KEEP OUT COMPETITION WHEN THEY LOCATED THEIR POWER PLANTS NEXT TO THEIR COAL RESERVES AND DID NOT PROVIDE FOR UNIT TRAIN UNLOADING CAPABILITIES FROM A COMPETING MINE.

MPC REPRESENTATIVES TOLD THE SENATE BUSINESS AND INDUSTRY COMMITTEE (AND THIS COMMITTEE?) THAT MPC ACQUIRED THE COAL RESERVES FROM THE NORTHERN PACIFIC RR FOR NON-UTILITY BUSINESS. IN OTHER WORDS THE RESERVES WERE NOT INTENDED FOR MPC USE. THIS FLIES IN THE FACE OF JUDGE SULLIVAN'S DECISION IN UPHOLDING THE PSC. A COPY OF JUDGE SULLIVAN'S DECISION IS ATTACHED TO MY TESTIMONY. HE CONCLUDED IN HIS FINDING OF FACT NO. 13 THAT:

"TESTIMONY AND EXHIBITS ESTABLISH THE HISTORY OF THE RELATIONSHIP BETWEEN MPC AND WECO. MPC ACQUIRED THE COLSTRIP COAL LEASES FROM THE NORTHERN PACIFIC RAILROAD IN 1959 AS A CONTINGENCY TO MEET FUTURE GENERATION NEEDS. EXH. MCC-4, PP 6-7. MPC PLANNED TO USE COLSTRIP COAL IN ITS CORETT PLANT IN 1964, TWO YEARS BEFORE BEGINNING CONSTRUCTION. NOT UNTIL AFTER WECO'S CREATION IN 1966 DID MPC'S REPORTS

INDICATE THAT THE COAL RESOURCES MIGHT SUPPLY OTHER THAN MPC'S GENERATING NEEDS. MPC DID NOT ACQUIRE THE LEASES CONTEMPLATING A NON-UTILITY OPERATION. EXH. MCC-4, PP 7-8.

MPC REPRESENTATIVES ERRONEOUSLY TOLD THE SENATE COMMITTEE (AND THIS COMMITTEE?) THAT PUGET SOUND POWER AND LIGHT (PUGET) PARTICIPATED IN THE DECISION TO LOCATE THE POWER PLANTS AND NEGOTIATE FOR PURCHASE OF COAL FOR THE GENERATING UNITS AT COLSTRIP. JUDGE SULLIVAN'S FINDING OF FACT NO. 14 STATES AS FOLLOWS:

"PUGET SOUND POWER AND LIGHT (PUGET), A CO-OWNER OF COLSTRIP UNITS, WAS NOT RESPONSIBLE FOR THE DECISIONS TO LOCATE POWER PLANTS AND NEGOTIATE FOR PURCHASE OF COAL FOR THE GENERATING UNITS AT COLSTRIP. PUGET BECAME A JOINT VENTURE PARTNER ONLY AFTER MPC HAD DETERMINED THE PLANT'S LOCATION AND SOURCE OF COAL. EXH. MCC-4, PP 6-10. MPC DEVELOPED PLANS AND ORDERED EQUIPMENT FOR COLSTRIP 1 BY 1970, BEGAN CONSTRUCTION IN 1971, AND ENTERED INTO AN AGREEMENT IN 1972 WITH PUGET TO DEVELOP THE PLANT AS A JOINT VENTURE, BACKDATING DOCUMENTS SO THAT PUGET WOULD SHARE IN ALL PROJECT COSTS, EXH. MCC-4, P.9"

MPC HAS INDICATED THAT IF SB 284 DOES NOT PASS, THEY MIGHT SELL WECO. IF THEY CAN LEGALLY SELL WECO, WHICH I QUESTION, AND GET MORE THAN WECO'S BOOK VALUE, WHO GETS THE GAIN—MPC'S STOCKHOLDERS OR THE RATE PAYERS WHO HAVE GUARANTEED MPC A 11.5% RATE OF RETURN ON THEIR INVESTED CAPITAL OVER THE YEARS? I BELIEVE THE COAL MINE IS AN INTEGRAL PART OF THE COLSTRIP UNITS AND MUST BE KEPT IN THE RATE BASE WITH THE POWER PLANTS. I URGE YOU TO REJECT SB 284.

NEVERTHELESS, IF THE LEGISLATURE WANTS TO CHANGE PUBLIC POLICY AND PASS SB 284, SUB-SECTION 2 NEEDS TO BE AMENDED TO READ AS FOLLOWS (CHANGES UNDERLINED):

(2) IN DETERMINING WHETHER THE COST INCURRED ARE REASONABLE, THE COMMISSION SHALL COMPARE THE COST INCURRED BY THE PUBLIC UTILITY TO THE MINE MOUTH COSTS THAT THE PUBLIC UTILITY WOULD HAVE INCURRED IF THE COAL OR OTHER BOILER FUEL HAD BEEN PURCHASED FROM A DIFFERENT SUPPLIER UNDER SIMILAR CONTRACT TERMS.

LEAVE TRANSPORTAION OUT OF THE LANGUAGE. MPC DOES NOT PAY TRANSPORTATION COSTS AND RATE PAYERS OF MPC SHOULD NOT BE FORCED TO PAY FOR COSTS THAT DO NOT EXIST.

SB 284

NAME

PAT CAMPBELL

REPRESENTING
MYSELF

FERIT AGIN 17
✓

HOUSE OF REPRESENTATIVES
VISITORS REGISTER

State Administration

COMMITTEE

DATE 3-1-95

BILL NO. SB 284

SPONSOR(S) _____

PLEASE PRINT

Jim Jensen

PLEASE PRINT

MEIC

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X

NAME AND ADDRESS	REPRESENTING	Support	Oppose
<u>Nancy McCaffree</u>	<u>PSC</u>		<input checked="" type="checkbox"/>
<u>Joe Novasio</u>	<u>Colstrip</u>	<input checked="" type="checkbox"/>	
<u>DIANNA TICKLER</u>	<u>WESTERN ENERGY CO</u>	<input checked="" type="checkbox"/>	
<u>Jim Shaffer</u>	<u>Colstrip miner</u>	<input checked="" type="checkbox"/>	
<u>Bob Nelson</u>	<u>Consumer Council</u>		<input checked="" type="checkbox"/>
<u>Nick Golder</u>	<u>NPRC</u>		<input checked="" type="checkbox"/>
<u>Kelly Wiedrich</u>	<u>IUDE Local 400</u>	<input checked="" type="checkbox"/>	
<u>Mary Wright</u>	<u>MT. Consumer Council</u>		<input checked="" type="checkbox"/>
<u>Susan Fischer</u>	<u>Entech</u>	<input checked="" type="checkbox"/>	
<u>Kim Tretheway</u>	<u>Entech</u>	<input checked="" type="checkbox"/>	
<u>Marce Couture</u>	<u>Entech</u>	<input checked="" type="checkbox"/>	
<u>Pamela Bognstad</u>	<u>Entech</u>	<input checked="" type="checkbox"/>	
<u>Tom Kiely</u>	<u>Entech</u>	<input checked="" type="checkbox"/>	

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.

HR:1993

wp:vissbcom/man

CS-14

J.V. Bennett

MontPIRG

Deborah Smith

Seneca Club

Tom Schmitt Self/No. 1 P/

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DATE 3-1-95

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