



minnesota power

AN ALLETE COMPANY

Legislative Energy Commission Meeting

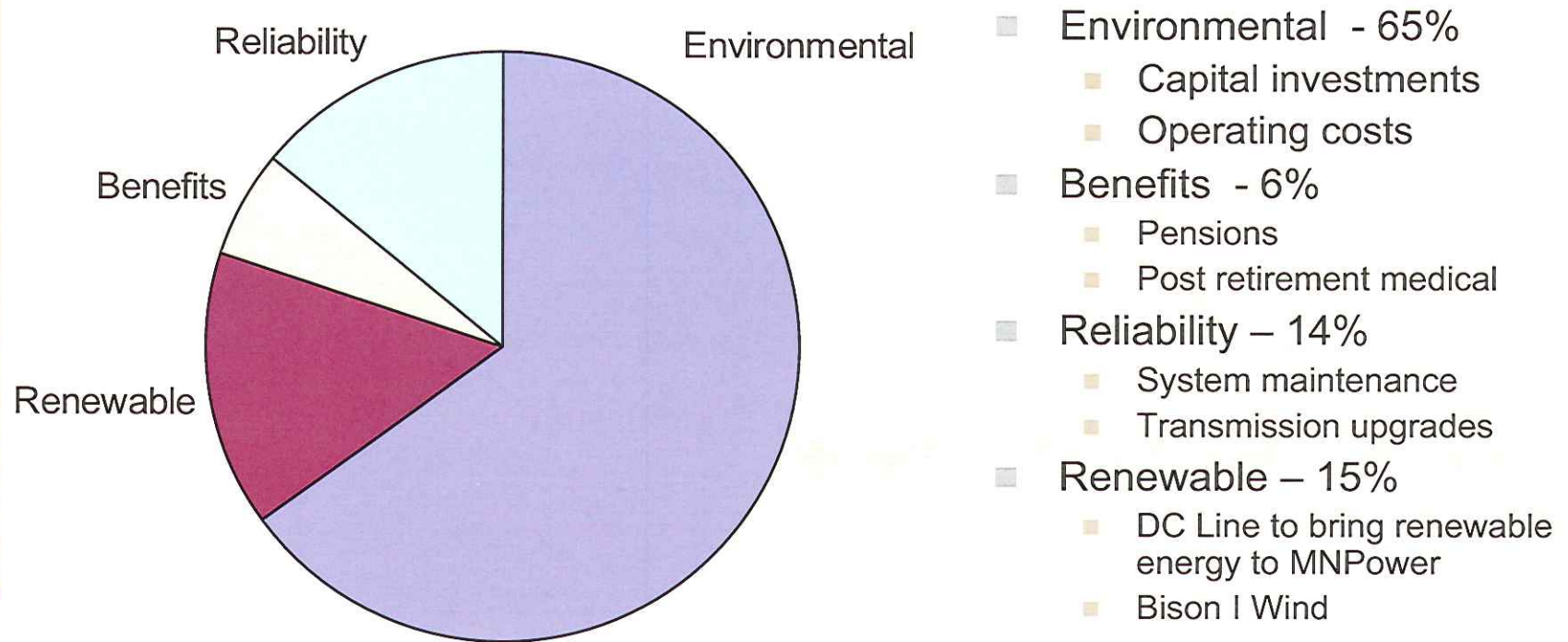
Margaret Hodnik
VP Regulatory and Legislative Affairs

July 22, 2010

Causes of Recent MP Rate Base Investment Leading to Rate Increases

- Federal Regional Haze Rule for NO_x/SO₂ (1999); 2013 implementation deadline
- MN Mercury Reduction Act (2005)
- Renewable Energy Standard (2007)
- Ongoing Maintenance
 - Generation, transmission, distribution system replacements/upgrades and related annual operating costs
 - Service reliability/quality maintenance

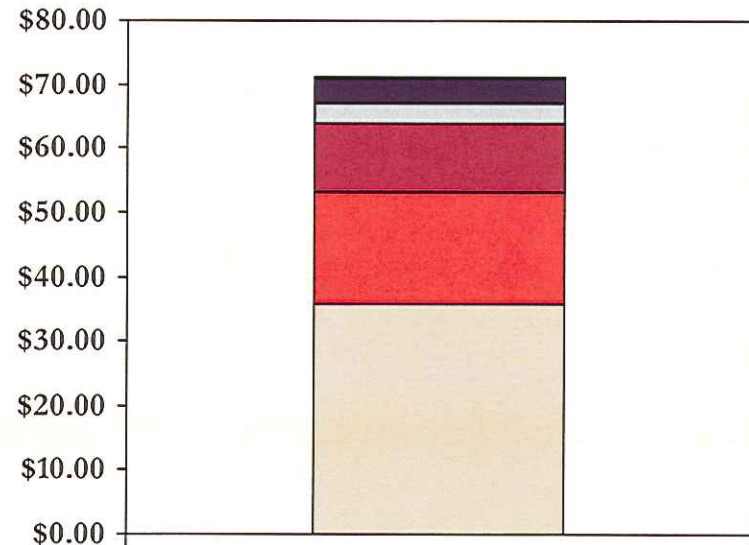
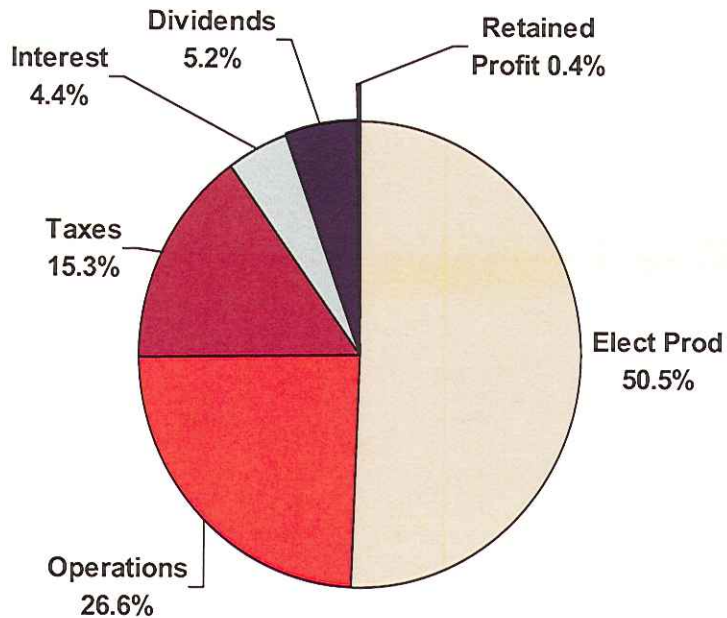
Key Rate Drivers Since 2008



Includes 2010 Rate Case, Renewable Rider and Transmission Rider

Cost Components of Average MP Residential Electric Bill

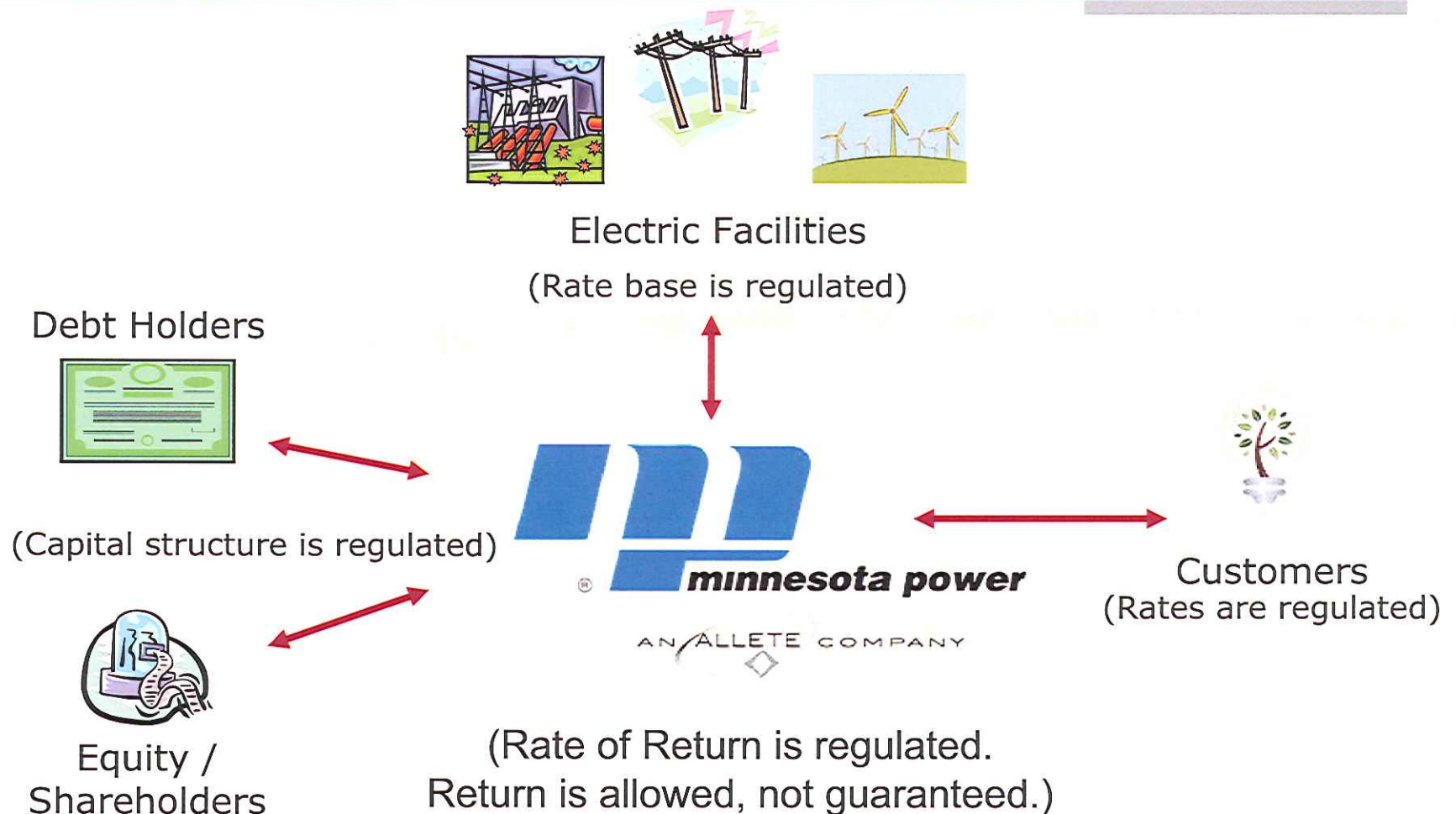
Average Electric Bill was \$71.05 at 12/31/09
 \$65.00 for electricity plus \$6.05 in taxes



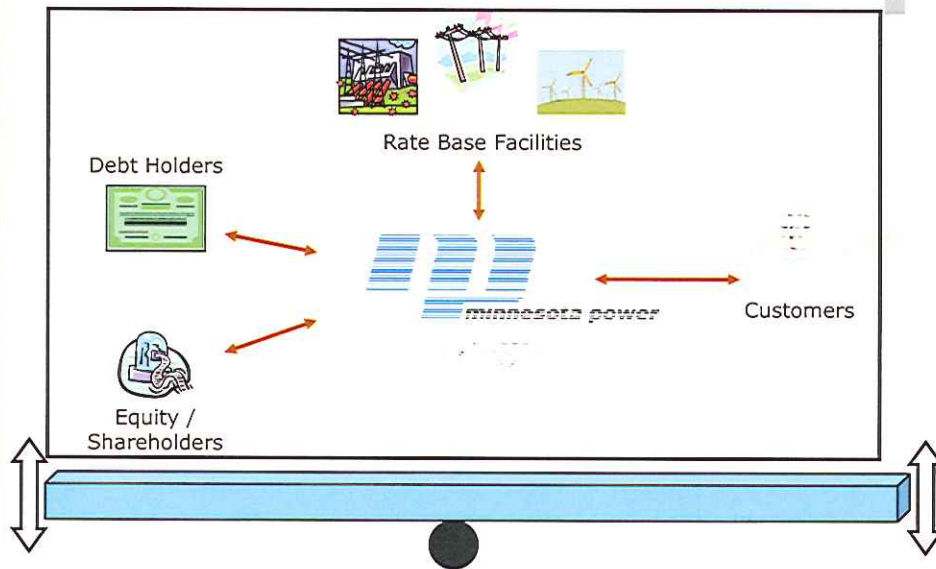
■ Ret Profit	\$0.25
■ Dividends	\$3.71
□ Interest	\$3.12
■ Taxes	\$10.86
■ Operations	\$17.23
□ Elec Prod	\$35.88

Cost amounts from Minnesota Power's jurisdictional report for 2009
 Dividends based upon ALLETE's dividend payout ratio
 Taxes include Income Taxes, Property Taxes and taxes on customer bill – excludes payroll and other taxes

How the Regulatory Model Works



Regulatory Model -- balance is essential



Each part of model is regulated--

- Regulators control how much debt and equity utilities hold
- Facilities, resources acquired with regulatory approval
- Rates can only be changed with regulatory approval
- Electric service quality and reliability highly regulated
- ...And markets determine the cost of debt rates and utility stock prices

- Model needs balance for all stakeholders
- Unilateral, single factor changes can result in negative, unintended consequences to the regulatory equation
- Out of balance there is no incentive to invest or customer rates can become noncompetitive
- Changes can be considered, yet, ensuring balance with any change is critical to customers, investors, utilities

Regulatory Processes

Rate base regulation, while a focal point, is not sole utility review:

- Certificate of Need
- Resource Planning
- Rate Cases
- Riders to promote policy objectives
 - Project approval
 - Cost recovery approval
- Other filings/forms of current recovery such as:
 - Depreciation filings
 - Service quality/reliability
 - Fuel clause related proceedings, etc.
 - Various compliance filings

Resource Planning

■ Keys:

- Customer requirements
- Unique MP customer base (industrials)
- Goal to evaluate supply and demand on non-discriminatory basis to make best choices
- Assess cost/risk/flexibility of alternatives
- Minimize cost/rate impact and meet all other societal requirements
- Strive to treat supply/demand options on par after meeting base conservation requirements
- Conservation issues:
 - How sustainable is conserved energy as “supply”? Can go away with technologies (flat screen TVs, etc.). Program evolution necessary.
 - Monitor policy economic outcomes/evaluate sustainability