“The future of any company is only as good as its aspirations expressed through strategic plans.”

DAN LANDGUTH, CEO, Black Hills Corporation
As deregulation threatened to restructure the utility industry in the United States, Black Hills Corporation transitioned to new leadership and a new strategy. Having learned important lessons from its first round of diversification, the company consolidated and concentrated on its core strengths in power generation and customer service. It also prepared for a more competitive environment by cutting costs, changing its culture and embracing incentive-based regulation.
As the gothic towers ornamented with gargoyles on the campus of the University of Chicago, a group of economists in the late 1950s began to challenge the widely accepted idea of the administrative state that had come into existence in the early decades of the 20th century and which flourished under the administration of President Franklin Delano Roosevelt. Some of these academics argued that regulatory agencies were too often “captured” by the industries they were supposed to regulate and did not make decisions in the public interest. Others asserted that the inefficiencies of the regulatory process slowed the pace of innovation and kept prices artificially high. Still others questioned the widely accepted idea of “natural monopolies” in capital intensive, network industries like telecommunications and electrical power. Taken together, the academics made a compelling case for a new way of thinking about the government’s role in managing the economy.

By the 1970s, the long assault by academic economists and lawyers on the administrative state had begun to change people’s thinking in Washington as lawmakers looked at industries ranging from airlines to trucking to telecommunications and considered deregulation. As the movement took hold, rural states expressed some reservations. Regulatory pricing systems had often been used to subsidize service to small towns and rural areas where the lack of economies of scale made service more expensive. Eliminating these cross-subsidizing pricing structures threatened to make everything from air travel to telephone service much more expensive. Resistance by lawmakers representing rural states could not stem the tide.

By the early 1980s, the movement toward deregulation had developed enormous momentum. Congress had eliminated the Civil Aeronautics Board and made air travel more competitive. The trucking industry was deregulated. Government-sanctioned price-fixing for service fees in the securities industry had been eliminated, opening new horizons for discount stock brokers such as Charles Schwab and Ameritrade. Natural gas markets had been deregulated. The court-ordered break up of AT&T in 1984 introduced competition into the telephone equipment and long distance markets. Public policymakers were also talking about deregulating the electric utility industry.

Five years after President Carter signed PURPA, cogeneration plants and independent power producers had begun to multiply in some parts of the country. Policymakers initially envisioned that these independent power producers would supplement power generated by existing...
electric utilities. As the independents began to enter the market, however, these new power producers deployed smaller combined cycle gas turbine generating units that relied on jet aircraft engine technologies. The new technologies allowed smaller plants to produce power at costs that were competitive with large conventional steam plants.

Proponents of deregulation argued that the new technologies made traditional economies of scale obsolete and destroyed any argument for continuing the old monopoly system. They wanted to give choices to consumers. They talked about “retail wheeling” arrangements under which consumers would be able to buy power from various generators and have it delivered by a separate transmission company to their home or business. They pointed to the European Union where deregulation had successfully reduced prices for consumers and improved service.

Skeptics of deregulation responded, saying that some of the unique aspects of the electric business made it less suitable for competition. For one thing, electricity was difficult to store and satisfying demand generally depended on just-in-time production. Even if an independent generator could produce power competitively, the transmission infrastructure constituted a natural monopoly. Responding to the argument that Europe provided a good example for the potential benefits of deregulation or “restructuring” as some called it, skeptics pointed out that Europe’s electric utilities were traditionally government-owned with a single, integrated transmission system in each country. By contrast, across the broad geography of the continental United States there were many transmission systems, and not all of them were tied together, so power could not move easily from one market to another.

Utilities expressed some interest in deregulation if it provided a greater ability to adjust to changes in the economy. The Edison Electric Institute, for example, a leading representative of the shareholder-owned utility industry, suggested a need for regulatory reform in 1981 to allow power companies to include capital spent for construction work-in-progress in the rate base, anticipate inflation in rate setting, provide faster depreciation to recover capital during high periods of inflation, and permit the use of fuel adjustment clauses so that utilities could pass along the true costs of fuel to consumers. Utility companies also expressed concern about “stranded costs” for power plants and infrastructure that had already been built to fulfill a legal obligation to provide service to customers.

The movement toward deregulation of electricity picked up speed in the early 1990s. The Energy Policy Act of 1992 restructured the power generation market, exempting independent power producers who were engaged exclusively in...
the sale of wholesale power from the restrictions of the Public Utility Holding Company Act. With this legislation, the first act of a three-part deregulation drama opened that would eventually turn the electric utility industry upside down and transform the opportunities open to Black Hills Corporation.

**RAISED WITH CRAFTSMAN’S WORK ETHIC**

The man charged with leading Black Hills Corporation as it faced the prospect of deregulation had grown up in a company town. Dan Landguth’s father had worked for the Homestake Mining Company most of his career, retiring in the late 1950s as the head of the foundry. With his two brothers, Dan had been raised in Lead and graduated from high school there in 1964. From his parents, he received a strong work ethic, a belief in the value of education, and a craftsman’s commitment to workmanship.

Enrolling at the South Dakota School of Mines and Technology, Landguth studied math, science and engineering. After graduation in 1968, he started work as a management trainee for Pacific Gas & Electric (PG&E) in northern California. After a year in California, he and his wife, Barbara, wanted to move closer to home. “I was going to look for a job in Colorado,” Landguth remembers, but on a family trip to South Dakota he interviewed with Everett Pompy, the head of personnel at Black Hills Power and Light. During the interview, Neil Simpson stopped by and was clearly impressed. Afterwards, Landguth thought the interview might pay off at some distant date. Instead, he got a call from Pompy soon after the interview. “Neil and I are going to create a position for you,” Pompy said.

In California, Landguth had worked with PG&E’s large customers to help them forecast their demand for power. His job had combined his engineering background with elements of customer service and marketing. Black Hills Power and Light did not have an engineer who was focused this way on major customers. Simpson and Pompy thought Landguth could help.

From his first job as a power use engineer, Landguth rose quickly through the ranks. Bob Asheim put him in charge of the Ben French station in the 1970s at a time when the company was installing pollution control equipment and building the first combustion turbines at the plant. On 24-hour on-call duty, Landguth learned the rhythms of the daily life of the company’s energy production operations. Promoted to vice president of administration in 1980, Landguth worked closely with Owen on operations and strategy. In 1985 he became senior vice president and chief operating officer of Black Hills Power and Light. Larry Owen sent him to the American Management Association to take courses and to develop a strategic vision. After Landguth became CEO in 1991, that vision drove the company’s development.

When Congress passed the Clean Air Act of 1990, Black Hills Corporation had little to worry about. Wyoming was already a step ahead of the federal government. Air-quality standards promulgated by the Wyoming Department of Environmental Quality were already among the toughest in the nation.

Black Hills Corporation had installed state-of-the-art desulfurization equipment at the Wyodak plant in the mid-1980s. In 1990, the company completed a $5 million project to reduce the amount of particulate and nitrogen oxide emissions. The company added a more efficient air heater, new burners and an economizer. The air heater improved the efficiency of the plant by lowering the gas outlet temperature. The new burners allowed the coal to burn at a lower temperature, forming fewer nitrogen oxides. The economizer collected more of the usable energy before the gas went out the stack.

In addition to the changes at Wyodak, the company also upgraded its environmental equipment at the Ben French Station in Rapid City and the Kirk Plant in Lead. The Osage Plant in Wyoming also received a renewed National Pollutant Discharge Elimination System permit in 1991. Overall, these efforts contributed significantly to the company’s commitment to meet the both the region’s power needs and the air quality standards of the state and the nation.
REFOCUSING ON POWER GENERATION

As Landguth and the executive team at Black Hills Corporation developed the company’s new strategic plan, their concerns included the company’s ability to continue growing and delivering returns to shareholders. “I thought it was important that we make a complete assessment,” Landguth said. The team looked at the organization’s strengths in terms of assets and people. What looked back at them were coal and expertise in power generation.

Having managed the utility operation during the earlier era in the company’s diversification efforts, Landguth was particularly sensitive to return on investment. He wanted to make sure that money that wasn’t invested in the utility would be invested wisely. He also wanted to avoid the regulatory issues that the company had encountered when it went into trucking, so he and his team focused on investment opportunities outside of Black Hills Power’s existing service territory.

The document that Landguth and his team developed was entitled “Focus 2000.” It sought to align the company’s assets with power generation and incorporated seven key strategies: 1) cost containment and increased productivity; 2) increased investment in the electric utility through the construction of a new power plant; 3) increased coal sales to the electric utility to fuel the new power plant; 4) increased income from oil and gas; 5) above utility industry average increases in dividend growth; 6) development of a highly motivated workforce; and 7) dedication to customer service. With these core elements of the plan, Landguth and his team began to deploy capital and people to achieve these new goals.

BUYING BACK WYODAK

The first step along the path to a renewed emphasis on power generation was to own the plant at Wyodak outright, rather than to lease it from investors. In 1990, the company and PacifiCorp struck a deal to buy the Wyodak plant from the group of investors that had owned it since 1978. Black Hills Power’s share of this deal was 20 percent or just over $42 million. The deal would put the assets of the plant into the rate base and increase Black Hills Power’s earnings potential.

The purchase price for Wyodak included more than just the book value of the plant. It also included an amount that accountants call “goodwill” or the market value of the plant over and above its depreciated cost of construction. The PUC had never allowed goodwill into the rate base before, but Black Hills Power believed it could make a compelling case to the state’s regulators. Appearing before the commission,
Black Hills Power argued that ratepayers would benefit from the full value of the purchase because the adjustment cost was still less than building a new plant or purchasing power. In addition, if the regulators didn’t allow the full purchase price into the rate base, shareholders would unfairly lose the earnings potential of this portion of the purchase price.

After deliberating, the PUC agreed with the company. On December 17, 1990 the commission declared it was prudent to include the full purchase price in the rate base. “It was the first time that we were able to demonstrate benefits to customers from ownership,” said Kyle White, who was manager of rates and regulation in these years. As part of the regulatory deal, however, the PUC declared that Black Hills Power would not be allowed to file a rate increase until January 1, 1992. Without the ability to seek rate relief, Black Hills Power assumed a new challenge – to find ways to constantly increase efficiency to keep pace with the effects of inflation elsewhere in the business.

RENEWED FOCUS ON COST CONTAINMENT

In the aftermath of the PUC decision, Landguth accelerated the processes of consolidation and cost containment in 1991. He reduced the size of the executive staff, eliminating two officer positions. He cancelled projects. In February 1991 he announced a 5 percent reduction in force that eliminated another 15 administrative staff positions in general services, human resources and information services. The following year, the work force was reduced by another 2.5 percent. The company also set a goal of reducing operating and maintenance costs to 3 percent below 1990 levels. Meanwhile, increasing demand in the company’s service territory created a need for more capacity.

This 50th anniversary logo celebrated the incorporation of Black Hills Power and Light Company in 1941. Over the course of a half century, the company’s total assets had grown from less than $5 million to nearly $295 million.

As inflation climbed, the price of electricity for residential customers remained essentially flat.
PLANNING NEIL SIMPSON II
Landguth was convinced the key to Black Hills Corporation’s immediate future was increasing sales of Wyodak coal to a new power plant, and preferably to a plant with an arms-length relationship with Black Hills Power, so that coal sales could be at market prices. To sell the potential capacity of this new plant, Landguth, Tom Ohlmacher, and the company’s general counsel, David Morrill, went on the road. Visiting all of the regional power companies, including Montana-Dakota Utilities, Idaho Power, Pacific Corporation, Montana Power, and the Public Service Company of Colorado, they were looking for potential partners as they pitched the idea of building another 330 MW plant at Wyodak.

Many of the potential partners were skeptical. They thought the costs of the plant and the price of fuel would be too high. They said the company would never be able to get the plant permitted because the opposition to coal-fired power plants was too strong. Black Hills Corporation offered its engineering studies and talked about its supply of Wyodak coal.

At a meeting in Salt Lake City, Ohlmacher remembers, they sat down with several Pacific executives, including Tom Lockhart who had spent a number of years working for Black Hills Corporation. By this time, Pacific had merged with Utah Power to create a huge utility company renamed PacifiCorp. “It was a final heart to heart,” Ohlmacher said. “Black Hills Corporation was asking ‘Are you going to be part of this or not?’” PacifiCorp couldn’t make the economics of construction work out. New transmission lines would have to be built to reach potential customers. They saw deregulation looming on the horizon and were hesitant to take on the financing.

Sensing Black Hills Corporation’s eagerness to move forward, PacifiCorp thought they might have some bargaining power and made an offer to become part owners of the Wyodak Mine. Landguth rejected this overture saying “Black Hills is not interested in selling an interest in the mine. The mine forms one of our core businesses, and we want to continue to do business.” After Landguth rejected this overture, Pacific walked away. According to Ohlmacher, “They said to us, ‘If you can build those coal plants for that, you should just start building them.’”

Soon after the meeting in Salt Lake City, Black Hills Corporation decided to go forward on its own. In 1991 the company announced that it would build an 80 MW coal-fired power plant at Wyodak with completion scheduled for January 1, 1997. Landguth explained to shareholders that the company needed the
generating capacity, given the growth of demand in the region. After considering the alternatives, a mine-mouth operation at Wyodak offered the least cost option. In addition, given the depressed state of the construction industry in 1991, the company believed it could keep construction costs low. Landguth also emphasized that the plant would be environmentally sound. The company also estimated that it would consume 400,000 tons of coal annually. As planners developed cost studies, the total price to build the new plant, dubbed Neil Simpson II, was approximately $125 million.

Black Hills Power, the company’s regulated utility, hoped to ease the financing of the new plant by asking the South Dakota PUC to approve gradual rate increases while the facility was under construction. With this strategy, interest charges during construction wouldn’t have to be added to the rate base and in the long run, said Ev Hoyt, “our customers would end up with a cheaper plant.” But South Dakota statutes didn’t allow the PUC to base rates on plants under construction. Working with other utilities in 1992, the company was able to convince legislators that a change in the law would benefit utility customers by phasing in rate increases prior to the completion of a generating plant. The Legislature agreed and revised the law. In the fall of 1992, Black Hills Power filed its rate stability plan with the PUC, but the plan to build the new plant was soon challenged by an unexpected competitor.

A CHALLENGE RISES FROM ROSEBUD

Rosebud Energy Corporation, a Montana-based independent power producer, managed a 35 MW plant near Colstrip, Montana. They informed Black Hills Power that they wanted to build a qualifying facility burning waste coke at Edgemont and to sell their electricity to Black Hills Power under the rules of PURPA. With the power from their plant, Rosebud contended, Black Hills Power would not need to build a new plant at Wyodak.

Black Hills Power expressed interest in the project but not as a substitute for Neil Simpson II. Neil Simpson II was too far along in the planning process and was needed for both interconnection reliability and resource planning. The company invited Rosebud to be part of the planning process for the next power plant and base its argument for “avoided cost” on that unit. Rosebud, however, wasn’t interested in waiting. Instead, they told the PUC that the company had been imprudent in its planning and decision to build Neil Simpson II. They wanted the regulators to kill the project.

The PUC focused on who could produce power most efficiently. Black Hills Power argued that...
Rosebud could not build a more cost effective plant. They also made a compelling argument to the commission that having another plant at Wyodak would provide critical backup for customers if one plant had to be shut down for one reason or another.

Strategically, it was critical that Black Hills Corporation make a more compelling case than Rosebud. The company saw the entry of an independent power producer in its market as "a threat to our ability to survive as a company," said White. "If we couldn't grow earnings, we weren't going to be long-lived."

**A BOLD MOVE SEALS THE PLANT**

Working with Black and Veatch, a leading engineering and design firm based in Kansas City, company engineers pored over the designs for the new plant looking for ways to reduce the construction costs. As Landguth looked over the plans and the cost projections he became increasingly confident. In a meeting one day with Morrill he announced, "Let's guarantee the price. If it costs more than that, we're going to take the inflation risk. We're going to take the construction risk. We're going to take the risk of equipment that may sit on a dock someplace and is not shipped. We're going to take the labor risk. The shareholder will assume all of these risks and not the customer."

Morrill had handled the negotiations with Pacific over the construction of the Wyodak plant in the 1970s when inflation was rampant and the costs of construction skyrocketed. No doubt he thought Landguth was unhinged. When Landguth presented the idea to the company’s board of directors, they were very hesitant. But Landguth made the case for the opportunities that lay ahead. He had worked in power plants.
He knew his team. “I had a tremendous amount of respect for the people that operated our power plants that they could get it up and operating on time and under budget,” he said.

Confident that they had the least cost option for ratepayers, the company made a dramatic announcement in 1992. They informed the South Dakota PUC and the Wyoming Public Service Commission that Black Hills Power would build Neil Simpson II for $113.6 million (with financing costs this number was later revised to $124.9 million). With this construction cost, Black Hills Power would be able to deliver electricity from the plant at 4 to 4.5 cents per kilowatt hour. The company believed that Rosebud would not be able to match this low rate. With this commitment, the company essentially agreed to take all the risk for any construction cost overruns. There were a couple of escape clauses, however. In particular, the company said that all bets were off if it was forced to buy power from a qualified facility like Rosebud.

Black Hills Power’s guaranteed price was a good deal for customers and the South Dakota PUC recognized it. On May 26, 1993, the commission denied Rosebud’s request and concluded that Black Hills Power had acted in good faith in planning Neil Simpson II. They permitted the company to move forward with construction. The commission also held that it had no authority to determine a utility’s need for additional capacity or the timing of that need. That risk belonged to the utility and its shareholders. The commission’s review of the company’s planning and construction would take place only when the utility sought to put that additional capacity into the rate base. In other words, the regulators told management: if you want to build it, go ahead, but the risk is yours.

**STOCK ISSUED TO FINANCE THE PLANT**


To help finance the construction, Black Hills Corporation issued new stock for the first time in many years. Altogether, 525,000 shares were issued in 1993 through the company’s

**ENERGY POLICY ACT 1992**

The Energy Policy Act of 1992 sought to reduce American dependence on foreign oil and improve air quality. The Act continued the development of a competitive market for wholesale electricity generation. It created a new class of power producers known as “exempt wholesale generators” (EWG’s). It also mandated that the FERC establish rules that would allow these wholesale generators to transmit power over existing lines. The Act encouraged state regulators and utilities to look for alternatives to the construction of new power plants, including conservation and purchasing power from independent producers.
Dividend Reinvestment Program, netting the company more than $13.3 million in new equity capital. Dale Clement, then chief financial officer, projected that Black Hills Corporation would issue $87 million in bonds to fund construction, increasing the company’s debt ratio significantly from 34 percent in December 1993 to 45 to 48 percent by 1996.

With the company’s commitment to bring the project in at $124.9 million, the pressures were intense. Landguth tapped Tom Ohlmacher, the company’s director of power generation, to run the project. Ohlmacher worked closely with Black and Veatch who handled the construction management. Meanwhile, the company moved deliberately into new markets to find customers for the surplus power that Neil Simpson II would generate.

**NEW WHOLESALE POWER BEGINS**

In 1994, Black Hills Corporation created Black Hills Generation and sought approval from federal regulators for the new business to begin generating and selling wholesale electric power and energy. The new business filed for and obtained exempt wholesale generator status under the terms of the Public Utility Holding Company Act. The company also announced plans to create another new subsidiary – Wygen – to build an additional 80 MW plant at Wyodak to produce power for wholesale markets.

As a Wyoming-based subsidiary of Wyodak Resources Development, Wygen may have seemed somewhat risky to observers. With excess capacity in the overall market for power, some observers were skeptical that the company would be able to build a plant and then sell the power profitably. Landguth reassured investors that the plant would only be built if the company could secure sufficient long-term contracts for the plant’s output to make the project financially successful. To avoid raising regulatory issues over transfer pricing, he also affirmed to state policymakers that Wygen would not sell electricity to its sister company, Black Hills Power.

The first success of this strategy came when the company bid for and won a contract to supply Montana-Dakota Utilities (MDU) with power to meet the needs of its Sheridan, Wyoming service territory. The ten-year agreement, scheduled to begin in January 1997, provided a solid base to the wholesale initiative with expected revenues of $90 million over the contract period. MDU and Black Hills Power also agreed to share in the construction of a new combustion turbine generator to meet peak needs for power. The MDU contract, along with the company’s contract with the city of Gillette, gave Black Hills Corporation a strong foothold in the growing wholesale power business.
COMPANY OFFERS TO FREEZE RATES

The MDU contract also changed the economics of the Neil Simpson II plant and gave Black Hills Power the opportunity to offer customers a better deal. Around the time that construction began on Neil Simpson II, the company withdrew its application to the South Dakota PUC for a rate stability plan. Landguth told shareholders that lower capital costs, coal cost concessions, and cost containment meant a lower overall rate increase would be needed when the plant began operating. Customers also benefitted after the company struck its wholesale agreement with MDU. Putting a percentage of Neil Simpson II’s production into the competitive market removed some of the cost that would be added to the rate base and thus lowered the overall amount the company would need to increase rates.

The company submitted its application for a 9.96 percent rate increase in 1994. It was the first increase Black Hills Power had requested in 12 years. In announcing the application, the company noted that the consumer price index had risen 25.8 percent in the same period, while electric rates had been flat. Even so, industrial customers resisted the rate increase. Their resistance melted when Black Hills Power offered an innovative approach to ratemaking.

Back in the 1970s the company had fought for and won the right to pass on increases in fuel and purchase power costs to customers without going through a formal rate hearing. By the 1990s these fuel and purchased power costs were hitting industrial customers such as Homestake Mining, Dachota Cement and sawmill operator Pope and Talbot particularly hard because all had a high load factor and carried a disproportionate share of the capital cost of the company’s power generating infrastructure. These industrial customers also expressed concern that Black Hills Power was creating more generation capacity than it needed with Neil Simpson II and they did not believe that customers should carry the burden of this excess capacity. Black Hills Power knew that these industrial users would resist a full rate increase when Neil Simpson II came on line. Kyle White, who managed rates, wanted to soften their resistance. He suggested that Black Hills Corporation take capacity out of the equation.

In addition to softening the resistance from industrial customers, removing the fuel cost adjustments from the rate structure would help to transform the culture of the company and prepare it for deregulation. “We were essentially market takers,” White said. Whatever price the company paid for fuel, it could pass on to power customers. Exposing the company’s profits to the ups and downs of the markets would make Black Hills Power employees more attuned to opportunities to improve efficiency and increase sales. Management also saw opportunities in the wholesale power market. By removing fuel cost adjustments, the company hoped for greater freedom from regulators to pursue these new competitive opportunities.

The commission’s ruling in Black Hills Power’s rate case reflected a compromise based on this new strategy. Black Hills Power was allowed to implement a 6.76 percent overall increase in its electric rates with the agreement that the company would freeze rates until January 1, 2000. The company also agreed to eliminate its fuel and purchased power cost adjustment clauses. Shareholders would take the risk for increases in fuel and purchased power costs. In exchange, and unlike most utilities, Black Hills Corporation shareholders would get to keep 100 percent of the profits from the sale of excess energy to off-
Dan Landguth and Virginia Simpson stand at the center of a crowd of well-wishers at the ribbon cutting for the new Neil Simpson II power plant.
system customers. This new structure provided incentives to shareholders for capital investment and gave management increased opportunities to reward employees for greater sales efforts and continuous process improvements.

**EMPLOYEES PUSH TO COMPLETE PLANT**

As Neil Simpson II neared completion in 1995, the intensity of the work increased. For many people, it became a seven-day a week effort for months. The plant had to be run through a series of environmental compliance tests. The regulations were new and untested because no new coal-fired plant had been built in the United States for a number of years. Mark Lux and Tom Stalcup sat at the controls and ran the plant in manual to meet the test. The plant passed.

The project came in under budget and ahead of schedule, saving the company millions of dollars. “It was a long struggle,” said Lux, “You get to the point where you wonder if you’re going to be able to survive, both personally and mentally. But when you get done with it, it’s the highlight of your career. The first time you synchronize that generator to the power grid is amazing.”

**ERA ENDS WITH KIRK PLANT CLOSING**

With cheaper power available from Neil Simpson II, Black Hills Corporation marked the end of an earlier era in the company’s history by closing the 31 MW Kirk Plant in Lead in September 1995 and transferring most of its 17 employees to the Neil Simpson power plant operations near Gillette.

The closure underscored many of the technological issues facing the industry in the 1990s. As Lux, plant supervisor at Kirk at the time of the closing, pointed out, “The old stokers were very reliable. Not long before the closing, we set a record of availability of 13 and a half months on Unit 4. That was a pretty solid record and still stands today.” An outstanding maintenance crew, “some of the best I’ve seen in my 20-plus years experience in the industry,” said Lux, also kept the old machinery running well.

But the plant was not efficient. With the Wyodak Mine located nearly 100 miles from the plant, trucking costs for fuel added substantially to the overall cost of generating power. Newer generating facilities at Wyodak that employed pulverized coal burning equipment produced more power per ton of coal. The company had set a target to reduce costs to $30 per megawatt hour at all of its power plants. With its higher costs, the Kirk Plant couldn’t hit that target. Closing the Kirk Plant, Landguth told employees, would save the company nearly $1.2 million in 1996 operating expenses. It was time to move on.
WORK CULTURE CHANGES

Employees who transferred from the Kirk Plant to Gillette experienced a dramatic change in the work culture. Although the Kirk Plant had been sold to Black Hills Power and Light by Homestake in 1954, the Homestake culture still deeply affected the life of the plant nearly 40 years later. Lead was a company town dominated by the relationship of Homestake to the community and the union to the company.

“The Kirk Power Plant, in those days, was a very strong union environment,” said Lux. Gillette and Wyodak were totally different.

In the late 1980s, employees at Wyodak had voted to affiliate with the United Mine Workers. The union had failed to negotiate a contract and was decertified. Management stepped in to address a number of issues. According to Jim Mattern, who served as director of Human Resources during these years, these issues focused less on wages, working conditions and rules. Instead, employees seemed more concerned about communication, leadership and coordination.

Black Hills Corporation executives listened to Wyodak employees in order to understand their frustrations. Then they reorganized to create five new operations and maintenance supervisor positions to improve the flow of information and ideas. “We started dealing with the issues,” said Mattern. “We said there’s going to be continuity, communications, and consistency.” Management’s efforts to resolve these concerns seemed to help.

The culture at Neil Simpson II was also different because of the changes in technology. The employees who came from the 60-year old Kirk Plant “were used to running stoker-fired units,” said Lux. The new plant was a state-of-the-art facility. “At Neil Simpson II,” said Lux, “98 percent of the controls were electronic. Operators who were used to turning pistol grips on a boiler turbine generator panel were now playing with a keyboard and starting everything up with a mouse.” As they adjusted to the challenges of the new facility, the Kirk employees also had to get to know employees at Neil Simpson that had been working at this site for years.

As employees from Kirk adjusted to life at Neil Simpson II, many of them also confronted larger workplace issues that Landguth raised with employees throughout the company. The economy was changing. Companies needed to be able to move quickly. Employees could no longer expect to stay in one job or with one company all their lives. If they wanted security, they needed to constantly expand themselves by making sure they [were] properly trained on new technology.” That message was not always welcomed by employees who had spent most of their careers working for the company. “I was very loyal,” said Don Dubej who had worked his way up to management as a line services manager in the late 1980s. “But I

Women increasingly filled non-traditional jobs at Wyodak and Black Hills Power in the 1990s.
wondered, 'Has he lost interest in me and others? Are they not really concerned about our well-being and welfare beyond six or seven years?'” For employees of Black Hills Corporation, just as for employees of many businesses around the country, these were tough questions.

Landguth understood that the new economic environment could make employees like Dubej uneasy. He took time to visit the company’s power plants and offices to talk to employees. Often he traveled with Jim Mattern. “We’d be at a power plant, and might be there from six in the morning until midnight to get all the crews,” Mattern said. “He was adamant that ‘we meet on their schedule, not on our schedule.’”

In these meetings, Landguth and other employees confronted a bald fact. The old days of rate-of-return regulation were coming to an end. In the old culture, customer service was paramount because customers who complained went to the PUC and those complaints affected the company’s working relationship with regulators. Regulators controlled a company’s income. Under the new regulatory regime, with rates frozen and income growth dependent on increasing efficiencies, unhappy customers increased costs.

With the commercial launch of the Netscape browser in 1995, millions of people soon discovered the advantages and opportunities of the World Wide Web. Companies raced to position themselves in cyberspace even as they struggled to understand how customers, suppliers and competitors would use this new technology.

Black Hills Corporation posted its first home page in October 1996. Like many early websites, it offered cyber surfers a variety of experiences. They could take an on-line tour of the Neil Simpson II Power Plant, visit the Wyodak Coal Mine or learn about Western Production Company’s oil and gas operations. A “Just For Kids” section featured tours and downloadable coloring book pages, as well as safety tips. Customers could find out how to properly install electric service in a new home or conserve energy and save money.

The website also provided links for information about the region. Tourists could click on the “Doorway to the Black Hills” page to be linked to the Rapid City Convention and Visitors Bureau. Businesses could find out about relocating to South Dakota and access information from the Governor’s Office of Economic Development.
If a competitive market should come to the Black Hills region, unhappy customers might simply go elsewhere.

Increasingly, the company’s performance was dependent on the commitment of employees to increasing shareholder value. As regulators adopted rules that provided financial incentives for improved productivity and service, union leaders and management changed the terms of their conversations. In negotiations in the 1990s they reached a series of agreements that provided rewards to employee groups if they achieved productivity goals. According to Hoyt, “We were able to say this is a win-win situation.” If the company could find ways to bring efficiencies to the bottom line, it would also be more able to increase compensation for front-line employees.

For many employees, however, the transition to the new paradigm was complicated by fear, giving up the comfort and known pattern of old ways of working to take risks and shoulder greater responsibilities. Landguth, Hoyt and others empathized with the worries of these employees because they, too, were casting anxious looks toward the horizon.

As the movement toward the deregulation of electricity grew in the United States and abroad, Black Hills Corporation took some comfort in state regulators’ resistance to the tides of sweeping change. Landguth told shareholders at the end of 1994 that South Dakota and Wyoming continued to give electric providers exclusive rights to franchised service territories. Within this regulatory system, the company had always faced competition from alternative fuels, self-generation and public power.

Landguth reassured shareholders that the company was well-positioned if deregulation did come. Wyodak coal and the company’s mine-mouth generation plants gave the company considerable competitive advantage in the power generation market. Coal could be mined and transferred by conveyor to Neil Simpson II, for example, for 50 cents per MMBTU, compared to natural gas prices that ranged from $1 to $12 per MMBTU in these years. Moreover, if national competition came, Black Hills Power sat in a particularly good position, poised at the junction of the Eastern and Western power grids.

Some employees and shareholders were not comforted by Landguth’s reassurances. “It caused a lot of stress on people,” Mattern said. “All that was in the news was deregulation, and if we weren’t doing it, what is wrong?”
The stress caused by the threat of deregulation had some benefits. Landguth’s team recognized that even if deregulation didn’t come to South Dakota or Wyoming, employees had to behave as if they were in a competitive market. “We were going to become even more customer-focused,” White said. “We were going to look for efficiencies and opportunities within the existing company. We no longer had the ability to go to our regulators and ask them to bail us out.”

While a number of other states moved forward with radical restructuring of the electric utility industry, South Dakota and Wyoming focused instead on performance-based management and market-based ratemaking as intermediate steps toward competition. These initiatives reinforced the idea that better performance could produce better results for shareholders and ratepayers.

By the end of the first act in the drama of electricity deregulation, the number of independent power producers in the United States had increased. Several states, including California and Montana, were deeply immersed in the process of redesigning the regulations, and subsequently the market, for electric service. But competition was still mostly academic.

Black Hills Corporation had begun to prepare for this brave new world. It had invested in power generating facilities to continue to provide reliable and relatively inexpensive power to its long-time customers in South Dakota and Wyoming. The number of customers in the company’s traditional service area continued to grow, up 7 percent between 1989 and 1994. Revenues from electric energy sales were up even more, 16 percent in the same period. While coal mining revenues fluctuated depending on the demand for fuel, Wyodak continued to play an important part in the company’s success, contributing nearly 41 percent of the company’s total operating income.

At the same time, the company was also building power generating capacity so it could satisfy demand from its own customers and enter the wholesale power market. By encouraging and cooperating with regulators to develop new rules, it had created incentives for employees and shareholders to take risks for the potential of greater returns. In the second act of this drama, energy markets in some states, especially in California, would be transformed.

LAUNCHING DAKSOFT

To diversify in the 1990s, Black Hills Corporation looked for strengths and market advantages within its own organization. By 1995, the company’s Information Services group had developed expertise in data processing, hardware, software, media and communications. Under Don Lewis, this group was organized as a separate business unit – DAKSOFT. Serving both internal and external customers, DAKSOFT developed software for external clients. The State of South Dakota’s Game, Fish and Parks Division, for example, commissioned DAKSOFT to develop a reservations management system for its campgrounds. The system was so successful that DAKSOFT began offering similar services to other states.