

Prefiled Direct Testimony and Exhibits  
Kendall G. Kiewer

Before the South Dakota Public Utilities Commission  
of the State of South Dakota

In the Matter of the Application of  
NorthWestern Corporation, d/b/a NorthWestern Energy

For Authority to Increase Electric Utility Rates  
in South Dakota

Docket No. EL14-\_\_\_\_\_

December 19, 2014

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## EXHIBITS

Workpapers for Statements D & E Normalizing Adjustments	Exhibit__(KGK-1)
Economic Development Test Year Expenditures	Exhibit__(KGK-2)
Jurisdictional Allocation of Shared Administrative Costs	Exhibit__(KGK-3)
Electric and Gas Allocation of Shared Administrative Costs	Exhibit__(KGK-4)

1 **Witness Information**

2 **Q. Please state your name and business address.**

3 **A.** My name is Kendall G. Kliewer. My business address is 3010 W. 69<sup>th</sup> Street,  
4 Sioux Falls, South Dakota, 57108.

5  
6 **Q. By whom are you employed and in what capacity?**

7 **A.** I am the Vice President and Controller of NorthWestern Corporation d/b/a  
8 NorthWestern Energy (“NorthWestern” or “the Company”).

9  
10 **Q. Please summarize your educational and employment experiences.**

11 **A.** I have been with NorthWestern since November 2002. My primary  
12 responsibilities include, among other duties, overseeing compliance with  
13 financial reporting requirements established by the Securities and Exchange  
14 Commission (“SEC”) and other regulatory agencies, technical research with  
15 regard thereto, reviewing NorthWestern’s financial statements, and implementing  
16 and overseeing accounting policies and procedures. Previously, I was a Senior  
17 Manager at KPMG, LLP in Lincoln, Nebraska. During my tenure at KPMG, I  
18 coordinated financial statement audits, consulted with clients on appropriate  
19 accounting practices and SEC reporting requirements, assisted clients with the  
20 preparation and review of various SEC filings, and planned and supervised  
21 audits. I have a Bachelor of Science degree in Business Administration from the  
22 University of Nebraska and am a Certified Public Accountant.

1 **Q. Have you previously testified before the South Dakota Public Utilities**  
2 **Commission (“Commission”)?**

3 **A.** Yes, I provided testimony in Docket No. NG11-003 and Docket No. NG06-013.

4

5 **Purpose of Testimony**

6 **Q. What is the purpose of your testimony in this proceeding?**

7 **A.** My testimony:

- 8 1. Discusses the Statements and Schedules included in the filing;
- 9 2. Presents a detailed explanation of various adjustments to the income  
10 statement and rate base;
- 11 3. Discusses NorthWestern’s method of allocating shared administrative  
12 costs; and
- 13 4. Discusses stock-based compensation.

14

15 **Overview of Revenue Requirement, Statements and Schedules**

16 **Q. What was your role in preparing the revenue requirement in this filing?**

17 **A.** I supervised the preparation of the information based on the books and records  
18 of the Company as well as the pro forma information contained in this filing,  
19 including the Statements and supporting Schedules. NorthWestern used a  
20 revenue requirement model consistent with the model used in Docket No.  
21 NG11-003. Statement M details the revenue requirement.

22

1 **Q. What test year is used in this filing?**

2 **A.** NorthWestern is using a 12-month test year based on historical data, ending  
3 September 30, 2014, as adjusted with known and measurable changes. The  
4 financial statements are in compliance with Federal Energy Regulatory  
5 Commission (“FERC”) rules and regulations.

6  
7 **Q. What Statements are included in this filing and who sponsors them?**

8 **A.** The following is a list of Statements provided, along with the respective sponsor:

9 **A.** Balance Sheet (Kendall G. Kliewer)

10 **B.** Income Statement (Kendall G. Kliewer)

11 **C.** Statement of Retained Earnings (Kendall G. Kliewer)

12 **D.** Utility Plant in Service (Kendall G. Kliewer)

13 **E.** Accumulated Depreciation (Kendall G. Kliewer)

14 **F.** Working Capital (Kendall G. Kliewer)

15 **G.** Cost of Capital (Brian B. Bird)

16 **H.** Operation and Maintenance Expense (Kendall G. Kliewer)

17 **I.** Operating Revenues (Kendall G. Kliewer)

18 **J.** Depreciation Expense (Kendall G. Kliewer)

19 **K.** Income Taxes (Kendall G. Kliewer)

20 **L.** Taxes other than Income (Kendall G. Kliewer)

21 **M.** Overall Revenue Requirement (Kendall G. Kliewer)

22 **N.** Allocated Cost of Service by Jurisdiction (Jeffrey J. Decker)

23 **O.** Allocated Cost of Service by SD Customer Class (Jeffrey J. Decker)

24 **P.** Energy Cost Adjustment Factors (Jeffrey J. Decker)

1           **Q. Description of Utility Operations (Kendall G. Kliewer)**

2           **R. Affiliate Transactions (Kendall G. Kliewer)**

3  
4   **Q. What Schedules are included in this filing?**

5   **A.** Schedules with supporting information have been included for Statements D, E,  
6   F, G, H, J, K, L, M, N and O. These Schedules detail any adjustments made to  
7   the test year data.

8  
9   **Q. Please describe rate base.**

10   **A.** NorthWestern's rate base is based on a 13-month average of all asset accounts  
11   as of September 30, 2014. This is shown on Schedule D-3. This plant balance  
12   is reduced by accumulated depreciation, as shown on Statement E. Rate base  
13   also includes materials, supplies, fuel stock, and prepayments. Statement F  
14   calculates the cash working capital reduction to rate base. Statement K details  
15   the accumulated deferred federal income taxes reduction to rate base. Schedule  
16   F-3 details other reductions to rate base for cash received for customer deposits,  
17   uncollectible account reserves, and insurance reserves.

18  
19   **Q. Has Construction Work in Progress ("CWIP") been included in rate base?**

20   **A.** No, CWIP is not included in rate base. Rate base includes only plant investment  
21   that is anticipated to be used and useful prior to the time rates go into effect in  
22   this docket.

1 **Q. Please explain the nature of adjustments to the 13-month average test year**  
2 **rate base.**

3 **A.** NorthWestern has made adjustments to rate base in Statements D, E, F, and K.  
4 The most significant pro forma adjustments to the test year relate to investments  
5 that are anticipated to be used and useful prior to implementation of the new  
6 rates proposed in this docket. Additional rate base is added to reflect expected  
7 capital additions from October 1, 2014 through the expected completion of this  
8 filing (September 30, 2015). This is shown on Schedule D-10. Additional  
9 depreciation expense is included in Statement J, as well as a corresponding  
10 increase in accumulated depreciation, shown in Statement E.

11

12 **Normalization Adjustments to Rate Base**

13 **Q. Please describe the proposed major adjustments for plant additions as well**  
14 **as other rate base adjustments.**

15 **A.** The rate base normalizations are as follows:

16

17 **Adjustment #1 – Normalize investments during test year to reflect a full**  
18 **year**

19 An adjustment was made to the test year rate base to reflect major investments  
20 (\$250,000 or greater) as if they were in service for the entire year. This  
21 increased rate base by \$10,443,105. Related adjustments were also made to  
22 accumulated depreciation and depreciation expense for \$291,573 for these  
23 assets. Exhibit\_\_(KGK-1) details these adjustments.

24

1           **Adjustment #2 – New depreciation rates**

2           An adjustment was made to reflect the new depreciation rates as a result of the  
3           Foster Associates, Inc. 2014 technical update to the 2012 depreciation study.  
4           The technical update supports electric depreciation rates, and common rates are  
5           supported by the 2012 study. The amount of this adjustment increases  
6           depreciation expense and accumulated depreciation by \$650,130. Statement J  
7           details this adjustment and Ron White addresses this in detail in his prefiled  
8           direct testimony.

9  
10           **Adjustment #3 – Post test year investments in service at time of rate**  
11           **increase**

12           An adjustment was made to reflect plant investments that are expected to be  
13           used and useful prior to the rates going into effect, as detailed on Statement D-  
14           10. The major additions are the Big Stone Air Quality Control System (“AQCS”)  
15           project and the Yankton East Substation project, which Dennis Wagner and  
16           Michael Cashell address in their prefiled direct testimonies. NorthWestern  
17           requests the opportunity to true up this list prior to finalizing this docket.  
18           Adjustments for these investments are included in Statements D, E, and J.

19  
20           **Adjustment #4 – Rate Case Expense**

21           An adjustment was made to rate base to reflect the three-year amortization of  
22           the expense to file this rate case. Schedule H-9 shows this calculation.

23  
24   **Q.   Do you expect any post-test year major retirements that impact rate base?**



1 **A.** Yes. Schedule D-10 shows the removal of the annual depreciation expense of  
2 \$205,134 for the Big Stone assets expected to be retired once the AQCS has  
3 been placed into service.  
4

5 **Q. How was working capital calculated and included in rate base?**

6 **A.** Statement F details the working capital calculation.  
7

8 **Q. What is indicated by the negative cash working capital?**

9 **A.** When cash working capital is negative, working capital is being provided by  
10 customers. Accordingly, the negative cash working capital is included as a  
11 decrease to rate base and reduces the annual revenue requirement.  
12

13 **Q. What are deferred income taxes?**

14 **A.** Deferred taxes are differences between the book and tax treatment for certain  
15 transactions. Accelerated tax depreciation generally exceeds book depreciation  
16 during the early years of an asset's service life, creating an accumulated  
17 deferred income tax liability.  
18

19 **Q. Why are deferred income taxes a reduction to rate base?**

20 **A.** Since deferred income taxes are typically liabilities for taxes due in future  
21 periods, they represent a source of funds. Accordingly, the average  
22 accumulated deferred income tax liability balance is deducted from rate base to  
23 recognize such funds are available for NorthWestern to use between the time

1 they are collected in rates from customers and the time they are eventually  
2 remitted to the government.

3  
4 **Normalization Adjustments to the Operating Revenues and Expenses**

5 **Q. Please describe normalizing adjustments made to the test year operating**  
6 **revenues and expenses.**

7 **A.** These adjustments are described below:

8  
9 **Adjustment #1 – Option L Revenue**

10 In 1997, NorthWestern began offering an Extended Service Rider termed  
11 “Option L” which involved long-term service agreements with large industrial  
12 customers and discounts for service depending on the length of the agreement.  
13 Docket No. EL97-014 states this lost margin cannot be collected from other  
14 customers. The customers served under Option L received discounts totaling  
15 \$339,137 during the test year. A normalizing adjustment was made to test year  
16 revenue to ensure other customers are not paying for this revenue shortfall.  
17 Schedule H-10 shows the details of this calculation. Jeff Decker explains  
18 NorthWestern’s request to eliminate Option L in his prefiled direct testimony.

19  
20 **Adjustment #2 – Non-sufficient Funds (“NSF”) Revenue**

21 This adjustment reflects additional revenue NorthWestern expects to receive by  
22 changing the return fee for NSF checks from \$15 to \$30. This adjustment uses  
23 the total NSF occurrences in the test year for electric and combination

1 customers, which adds \$18,705 to revenue. Schedule H-10 shows the  
2 calculation.

3  
4 **Adjustment #3 – Tampering Fee Revenue**

5 Consistent with prior ratemaking treatment in Docket No. NG11-003, this  
6 adjustment was made to reflect the revenue received from the ability to bill  
7 customers for meter tampering. NorthWestern estimates this occurs five times  
8 per year and costs approximately \$100 per occurrence. NorthWestern’s general  
9 terms and conditions will be updated to reflect the Company’s ability to add this  
10 charge to a customer’s bill. This adjustment is detailed in Schedule H-10.

11  
12 **Adjustment #4 – Connect/Reconnect Fee Revenue**

13 As shown on Schedule H-10, NorthWestern is proposing to increase the fee to  
14 customers for connections and reconnections. The current charge of \$15.00 will  
15 be increased to \$150.00 for connections after business hours, which will  
16 increase revenue by \$4,995. Reconnections after hours after failure to pay will  
17 go from \$69 to \$150, increasing revenue by \$23,895. Connections that occur  
18 during normal business hours will increase from \$10 to \$20, resulting in  
19 \$135,400 of additional revenue. Reconnections during normal business hours  
20 after disconnection for failure to pay will go from \$49 to \$60, resulting in an  
21 increase of \$10,373 to revenue. Jeff Decker’s prefiled direct testimony includes  
22 Exhibit\_\_ (JJD-1) - Confidential and additional information regarding this  
23 adjustment.

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**Adjustment #5 – Capacity Costs**

The test year includes capacity costs for 15 MW contracted from Basin Electric Power Cooperative (“Basin”). NorthWestern entered into an agreement with Basin to supply firm capacity of 19 MW in 2015. NorthWestern also entered into an agreement with Missouri River Energy Services (“MRES”) for capacity of 30 MW, 30 MW, and 35 MW for 2016, 2017, and 2018 respectively. A normalizing adjustment was made to increase NorthWestern’s capacity costs by the four-year average (2015-2018) of the contracted capacity with Basin/MRES. This resulted in the inclusion of an additional \$444,000 of capacity costs. The adjustments are detailed on Schedule H-2.

**Adjustments #6, #7, #8 – Labor Expense, Payroll Taxes and 401K**

**Contribution**

Consistent with prior ratemaking treatment, actual base year labor allocated or directly charged to South Dakota operations was increased 3% annually for 2015 and 2016, or \$688,834. Our contract covering bargaining unit employees provides for 3% pay increases in 2015 and 2016. We expect non-union wage increases to be similar and have therefore adjusted them by 3% as well. Payroll taxes have also been increased accordingly for both years as shown on Statement L. NorthWestern’s 401K expense, which is comprised of a 4% company match for those who contribute at least 4%, and a non-elective company contribution of at least 5% for all participants, has also been increased as shown on Schedule H-3.

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**Adjustment #9 – Advertising Expense**

Consistent with prior ratemaking treatment, this adjustment was made to reflect the removal of promotional and institutional advertising expenses of \$172,967 originally recorded as an operating expense. This is reflected on Schedule H-3.

**Adjustment #10 – Economic Development**

NorthWestern is able to support its communities in fostering economic growth by providing financial support to local or area economic development organizations. The adjustment for economic development in Schedule H-3 reflects a 50/50 split between electric utility customers and shareholders. This is consistent with previous Commission decisions regarding economic development expenses for NorthWestern’s South Dakota natural gas customers (Docket No. NG11-003). While financial support for these groups has a role, it is important to note that NorthWestern provides additional support through employee participation on local economic development boards, regional economic development organizations, and state-led initiatives. NorthWestern does not track individual employee hours spent on economic development activities as it is our culture to support customers, communities and the states we serve while meeting daily operations and customer care activities. It is also important to note that employee involvement in local and state economic development partnerships is not limited to normal working hours. NorthWestern employees dedicate many hours outside the normal work day in participating on economic development boards that provide benefits to customers and their communities as well.

1 Exhibit\_\_(KGK-2) provides detail of the test year expenditures and Schedule H-3  
2 includes a normalizing entry of \$50,593, which removes 50% of the economic  
3 development costs allocated to South Dakota electric customers. Upon  
4 Commission approval of NorthWestern’s proposed treatment of economic  
5 development-related expenses as part of this rate case filing, NorthWestern will  
6 provide an annual report and budget to the Commission for its review and  
7 approval by March 30 of each year, beginning on March 30, 2016.

8  
9 **Adjustment #11 – Field Inventory**

10 As part of our InService implementation, which is described in detail in Bobbi  
11 Schroepel’s prefiled direct testimony, a field inventory of the South Dakota  
12 distribution system was completed in the fall of 2013. Costs for this inventory  
13 totaled approximately \$900,000 and were charged to FERC Account 588. For  
14 purposes of this filing, a three-year average was used as the test period level of  
15 expense, resulting in a decrease to operating expense of \$560,232. Details of  
16 this are shown on Schedule H-5.

17  
18 **Adjustment #12 – SPP Expense**

19 An adjustment has been made to add \$650,000 of expected costs for the  
20 transition into the Southwest Power Pool (“SPP”). This is in addition to the  
21 \$92,500 already included in FERC Account 566 for SPP-related costs in the test  
22 year. Bleau LaFave addresses this topic in his prefiled direct testimony.

1        **Adjustment #13 – Bad Debt Expense**

2        An adjustment was made to normalize bad debt expense using a three-year  
3        historical period. The average bad debt expense during the three-year period  
4        was divided by revenue to determine the bad debt expense percentage for  
5        NorthWestern. The amount for 2013 was normalized to remove all expense  
6        related to Northern Beef Packers LP. Once calculated, the percentage was  
7        applied to the adjusted revenue amount to determine the test period bad debt  
8        expense. The resulting decrease to bad debt expense is adjusted in Statement  
9        H and detailed on Schedule H-7.

10  
11       **Adjustment #14 – Spousal Travel on Company Aircraft**

12       Consistent with prior ratemaking treatment in Docket No. NG11-003, an  
13       adjustment was made to remove \$1,124 of expenses related to spouses riding  
14       on NorthWestern's airplane to attend the National Lineman's Rodeo. This  
15       adjustment is detailed in Schedule H-8.

16  
17       **Adjustment #15 – Rate Case Expense**

18       Consistent with prior ratemaking treatment, an adjustment was made for the  
19       expenses related to filing this rate case. This is detailed in Schedule H-9.

20  
21       **Adjustment #16 – Government Lobbying-Related Costs**

22       Consistent with prior ratemaking treatment, this adjustment was made to reflect  
23       the removal of \$35,656 of government lobbying-related costs originally recorded

1 as a utility operating expense. This removes all lobbying expenses from the test  
2 year. Schedule H-11 details this adjustment.

3  
4 **Adjustment #17 – Depreciation Expense**

5 As part of this rate filing, NorthWestern has completed Statement J which  
6 reflects depreciation rates for its electric utility assets, as determined by a  
7 depreciation study completed by Foster Associates, Inc. The implementation of  
8 the new rates for electric utility assets results in an increase to test year  
9 depreciation expense of \$650,130. Additionally, depreciation expense was  
10 adjusted for the impact of normalizing the investments made during the test year  
11 to record a full year of depreciation expense. This adjustment increased  
12 depreciation expense by \$291,573. Lastly, an adjustment was made to add a  
13 full year of depreciation expense for the assets expected to be placed in service  
14 before the new rates go into effect. This is detailed on Schedule D-10 and totals  
15 \$2,453,839. The combined normalizing adjustment for depreciation expense is  
16 an increase of \$3,395,540.

17  
18 **Adjustment #18 – Interest Synchronization**

19 Consistent with prior ratemaking treatment, this adjustment reflects the change in  
20 federal income taxes by using the interest synchronization method of computing  
21 the interest deduction for income tax purposes. Under this method, interest in  
22 the income tax calculation was set equal to the implied interest in the proposed  
23 cost of capital included in this filing. See Schedule H-12 for details.



1           **Adjustment #19 – Gross Receipts Tax**

2           Consistent with prior ratemaking treatment, this adjustment reflects the change in  
3           gross receipts tax related to the increase in revenue. This adjustment is detailed  
4           on Schedule L-1.

5  
6           **Adjustment #20 – Carrying Charges**

7           During the test year, the Company recorded interest income from customers  
8           calculated on under-collected tracker balances. An adjustment has been made  
9           to remove that income from the test year, as it is not guaranteed or known for  
10          any periods beyond the test year. Schedule H-13 details this adjustment.

11  
12       **Q. Did you include adjustments for demand-side management, ad valorem tax,**  
13       **Yankton Sioux Tribe discount, transmission expenses, or the cost of fuel**  
14       **and purchased power in this filing?**

15       **A.** No. Recovery of demand-side management costs, ad valorem tax, Yankton  
16       Sioux Tribe discount, transmission expenses, fuel and purchased power occurs  
17       through separate trackers.

18  
19       **Q. Does this filing include charitable donations, mergers and acquisitions**  
20       **expenses, or non-utility costs?**

21       **A.** No, it does not.

1 **Jurisdictional Allocations of Shared Costs**

2 **Q. Please briefly describe the methods used to allocate costs to South Dakota**  
3 **Electric Utility Operations.**

4 **A.** NorthWestern has three regulatory jurisdictions consisting of Montana, South  
5 Dakota, and Nebraska. In addition, NorthWestern has electric generation  
6 consisting of a 30% ownership interest in Colstrip Unit #4 (“CU4”) in Montana.

7  
8 NorthWestern’s administrative costs are allocated between jurisdictions and its  
9 ownership interest in CU4 using a three-factor formula, consisting of gross plant,  
10 margin, and labor. The three-factor formula is updated annually in October  
11 through an internal administrative allocation study. The 2014 jurisdictional  
12 allocation methodology is attached as Exhibit\_\_(KGK-3).

13  
14 In addition, NorthWestern uses a three-factor formula to allocate shared costs  
15 between South Dakota electric and gas operations and Nebraska gas operations  
16 consisting of plant, customers, and operation and maintenance labor expense for  
17 each of the electric and natural gas segments of its business. This formula is  
18 also updated annually in October through an internal administrative allocations  
19 study. The 2014 electric and natural gas allocation methodology is attached as  
20 Exhibit\_\_(KGK-4). These allocation methods were approved in NorthWestern’s  
21 most recent natural gas filing, Docket No. NG11-003.

22

1 In addition to the allocations described above, common plant and common  
2 depreciation are allocated between electric and natural gas using rate base  
3 percentage. The 2014 allocation percentage to electric was 76%.

#### 4 **Stock-Based Compensation**

6 **Q. Does this filing include stock-based compensation?**

7 **A.** Yes. South Dakota electric FERC Account 920 includes stock-based  
8 compensation costs of \$243,163.

10 **Q. How is stock-based compensation expense calculated?**

11 **A.** NorthWestern accounts for stock-based compensation in accordance with  
12 Statement of Financial Accounting Standards No. 123R, *Share-Based Payment*  
13 (“SFAS No. 123R”), which requires companies to recognize compensation  
14 expense for all equity-based compensation awards issued to employees. Under  
15 SFAS No. 123R, NorthWestern recognizes expense over the period during which  
16 an employee is required to provide service in exchange for the award. The  
17 expense is based on the fair value of the shares issued as of the grant date.

18  
19 **Q. Are stock-based compensation awards based on reasonable company  
20 goals that provide measurable benefits to utility customers?**

21 **A.** Yes. NorthWestern’s Long-Term Incentive Plan (“LTIP”) is a stock-based  
22 compensation program designed to motivate participants to achieve high levels  
23 of performance as well as reinforcing desired business behaviors and results.  
24 The goals of NorthWestern’s LTIP are to emphasize operational performance

1 and shareholder value creation, both of which benefit customers. The goals are  
2 the same for all employee levels covered by the LTIP, emphasizing a unified  
3 approach to long-term incentives at NorthWestern.

4

5 **Q. Does this complete your testimony?**

6 **A.** Yes, it does.