

SETTLEMENT AGREEMENT

This Settlement Agreement (“Agreement”) is entered into as of October 10, 2006, by and between the South Dakota Public Utilities Commission (“SD PUC”), on the one hand, and on the other, NorthWestern Corporation and its subsidiaries NorthWestern Energy Marketing, LLC and The Clark Fork and Blackfoot, LLC (“NorthWestern”) and Babcock & Brown Infrastructure Limited and its subsidiaries BBI US Holdings Pty Ltd., BBI US Holdings II Corp., and BBI Glacier Corp. (“BBIL”) (together, NorthWestern and BBIL, the “Applicants”). The SD PUC and the Applicants are each a “Party” and together are the “Parties.”

WITNESSETH:

WHEREAS, on June 7, 2006, the Applicants filed with the Federal Energy Regulatory Commission (“FERC”) in Docket No. EC06-127-000 an “Application” requesting authorization under Section 203 of the Federal Power Act (“FPA”), 16 U.S.C. § 824(b) for the merger of a BBIL subsidiary with and into NorthWestern, which will result in the NorthWestern Companies becoming indirect, wholly-owned subsidiaries of BBIL (the “Merger”);

WHEREAS, on June 28, 2006, the SD PUC filed with the FERC in Docket No. EC06-127-000 a “Notice of Intervention and Request for Full 60 Day Time Period for Filing of Protest;”

WHEREAS, on July 13, 2006, the Applicants filed with the FERC in Docket No. EC06-127-000 a “Joint Answer and Supplement” to various interventions and protests (“Joint Answer”);

WHEREAS, on August 14, 2006, the Applicants and SD PUC filed a “Joint Motion to Facilitate Settlement Discussions by Permitting a Conditional, Limited Extension of Time to File a Protest;”

WHEREAS, the Applicants and SD PUC each desire to resolve all issues concerning the Merger in FERC Docket No. EC06-127-000; and

WHEREAS, the Applicants and SD PUC have provided each other with good and valuable consideration in exchange for this Agreement;

NOW THEREFORE, in consideration of the premises and the mutual promises herein made, and in consideration of the covenants herein contained, the Applicants and SD PUC, intending to be legally bound hereby, agree as follows.

1. In the FERC Application and Joint Answer, Applicants have made various commitments, including (but not necessarily limited to) the following:

- (i) a five-year hold harmless commitment regarding wholesale transmission rate increases as a result of merger costs net of merger savings; (*see* Application at 18; *id.*, Exhibit M at 1)
- (ii) a commitment regarding the pricing of affiliate transactions for non-power goods and services; (*see* Application at 18-19; *id.*, Exhibit M at 2)
- (iii) certain cross-subsidization commitments; (*see* Application at 19-20; *id.* Exhibit M)
- (iv) commitments regarding ring fencing and encumbrance of utility assets to finance non-utility assets or operations; (*see* Application’s Exhibit M at 2-4 & Joint Answer at 4)
- (v) the commitment regarding not passing on any acquisition premium through either wholesale or retail rates; (*see* Joint Answer at 5 and 15)
- (vi) the commitment by NorthWestern to continue reporting after the merger under U.S. Generally Accepted Accounting Principles, as well as the accounting rules and orders of the FERC and SD PUC; (*see* Joint Answer at 6)
- (vii) the commitment to honor employee, retirement and other Benefit Plan obligations as set forth in the terms of the Agreement and Plan of Merger; (*see* Application’s Exhibit I (Agreement and Plan of Merger) § 5.11; Joint Answer at 7) and
- (viii) the commitment to make appropriate capital expenditures (*see* Joint Answer at 9-10).

Although these commitments were made in part for the benefit of South Dakota retail and wholesale customers, the Applicants incorporate these commitments in this Agreement and, as such, make these commitments to the SDPUC. To the extent that the language of the ring fencing commitments referenced in Application’s Exhibit M at 2-4 explicitly extend to, are for the benefit of, or subject actions to the approval of the “Commission” (*i.e.* FERC) and/or the Montana PSC, such commitments and the rights, powers and benefits thereof are hereby extended to the SD PUC.

2. If in any future gas or electric rate case before the SD PUC (and to the extent possible before FERC which will affect South Dakota wholesale ratepayers), NorthWestern seeks to include in its rate base an asset owned by NorthWestern or any affiliated entity as of the effective date of the Merger, NorthWestern will:

- (i) value such assets for rate base purposes at their original cost less depreciation pursuant to S.D. Codified Laws § 49-34A-19, unless otherwise authorized by the SD PUC, and original cost shall be measured at the original cost of first acquisition or construction by NorthWestern, any affiliated entity or any of their respective

predecessors in interest, including by any affiliate or predecessor in interest of NorthWestern such as pre-bankruptcy NorthWestern or Montana Power Company; and

(ii) not seek approval to use BBIL's acquisition cost to value such assets unless BBIL is the original owner.

With respect to assets acquired or developed by NorthWestern after the effective date of the Merger, the valuation of such assets for rate base purposes and rate recovery in any South Dakota rate proceeding shall be governed by South Dakota law.

3. Applicants will not seek to recover from South Dakota ratepayers the costs incurred by NorthWestern or BBIL in undertaking and consummating the Merger.

4. Applicants will use their reasonable best efforts to have a majority of NorthWestern's board of directors be citizens of the United States and at least one member will be independent in that he or she will not be employed by nor otherwise affiliated with NorthWestern or any other Applicant but shall have substantial utility experience or qualify as a financial expert as defined by the NASDAQ Stock Market Inc. Marketplace rules. NorthWestern shall maintain an Audit Committee and a Governance Committee with the independent director serving as the chairperson of each such committee. Until the later of June 30, 2010 or three years after the effective date of the Merger, at least one member of the board will be a bona fide South Dakota resident.

5. Applicants shall fully perform their obligations under the Agreement and Plan of Merger. This commitment shall include, but not be limited to, performance of all obligations to NorthWestern's retirees and maintenance of personnel and operations in South Dakota as set forth in the Agreement and Plan of Merger.

6. NorthWestern shall use its reasonable best efforts to obtain and maintain electric power supply and natural gas delivery resources (including capacity, energy, fuel, transmission and distribution) to serve its South Dakota wholesale and retail customers with an adequate and reliable source of electricity and natural gas service, stable and reasonably priced at the lowest long-term total cost, including an allowance for a just and reasonable return under the applicable federal and state regulatory standards. For short-term transactions, NorthWestern shall serve its South Dakota wholesale and retail customers at the lowest reasonable cost for the transaction, including a reasonable return under applicable federal and state regulatory standards. Neither NorthWestern nor any other Applicant shall take any action or fail to act in a way that would prevent NorthWestern from meeting these obligations. NorthWestern shall maintain these resources to serve such customers. NorthWestern agrees not to sell or otherwise transfer its regulated generation assets in South Dakota rate base and used to serve South Dakota customers, or the capacity and energy from them to the extent that they are necessary or prudent to meet its obligations to South Dakota retail and wholesale customers, without the approval of the SD PUC which will not be unreasonably withheld or delayed.

7. After the Merger, NorthWestern shall make the necessary financial commitments to upgrade, replace and maintain its systems as required to provide a level of reliability,

including outage frequency and duration, and customer service as it had prior to the Merger and as necessary to conform to industry standards, South Dakota law and SD PUC orders and regulations; provided, however, that such costs shall be eligible for recovery in retail or wholesale rates to the same extent as other costs and expenses under applicable rate-making principles.

8. NorthWestern shall not sell, lease, pledge, mortgage, secure or otherwise transfer any of its SD PUC regulated assets to (or for the benefit of) BBIL or any other of its affiliated companies except for the payment of duly authorized dividends in accordance with South Dakota law.

9. NorthWestern will continue to abide by the “Financial Measures” and “Affiliate and Inter-Corporate Transaction” covenants set forth in Sections 4.(b)(iii) through (xi) of the Stipulation and Settlement Agreement dated July 8, 2004, between NorthWestern and the Montana Public Service Commission and other Montana agencies (“Montana Settlement”), except that the term “Parent Company” shall mean NorthWestern. NorthWestern incorporates these covenants into this Agreement to and for the benefit of the SD PUC and South Dakota ratepayers.

10. Without the approval of the SD PUC, NorthWestern will not borrow money secured by South Dakota regulated utility assets to upstream funds to either BBIL or its affiliates. Any portion of any financing by BBIL or its affiliates, other than NorthWestern, that is devoted to any purpose other than providing funds to NorthWestern for its public utility operations shall be non-recourse to NorthWestern.

11. Any loans made by BBIL or any other affiliated entity to NorthWestern shall be commercially reasonable and shall not have less favorable interest rates and other terms than those that would be available to NorthWestern in the market as a stand alone entity. Any service or good provided by an affiliate to NorthWestern shall be commercially reasonable and shall conform and be subject to the standards for such transactions set forth in the Settlement Agreement between NorthWestern Public Service and SD PUC Staff dated October 19, 1999, and approved in Docket NG99-002.

12. NorthWestern will provide to the SD PUC the report and recommendations from the independent Transmission and Distribution Infrastructure Audit (“Audit”) that was performed by NorthWestern pursuant to the Montana Settlement. NorthWestern further agrees to appear before the SD PUC to present the results of the Audit, discuss how the results and recommendations of the Audit are pertinent to South Dakota operations, what steps have been taken by South Dakota’s operations management to implement the recommendations of the Audit in South Dakota, what progress has been made to date in carrying out the Audit recommendations in South Dakota and what NorthWestern’s plans are going forward to fully achieve the recommended actions relative to South Dakota operations. Following such report, if the SD PUC determines that additional evaluation of NorthWestern’s South Dakota infrastructure or its maintenance and replacement programs is necessary, NorthWestern shall retain an outside expert to perform a reasonable (in terms of scope and cost) independent evaluation of its infrastructure and its maintenance and replacement procedures. NorthWestern’s

cost of performing such additional outside evaluation shall be eligible for recovery in retail rates in the same manner and in accordance with the same rate-making principles applicable to its other costs and expenses.

13. The Parties also acknowledge that NorthWestern's corporate headquarters is currently located in Sioux Falls, South Dakota, and NorthWestern's upper management personnel are currently located in both South Dakota and Montana. Given the events of the past several years, including NorthWestern's bankruptcy, the SD PUC believes that re-establishing and maintaining stability at NorthWestern is an essential public interest objective. Accordingly, until the later of June 30, 2010 or three years following the effective date of the Merger, NorthWestern shall maintain its corporate headquarters in Sioux Falls at comparable executive and support staffing levels.

14. NorthWestern will maintain fully staffed operational capability in South Dakota to manage utility facilities and operations in South Dakota. This operational capability in South Dakota shall include adequate personnel (together with the use of contractors) to perform the necessary operation and maintenance functions with locally based personnel and professional level operations management who are fully capable of performing all operations level systems planning, budgeting, management, operation and maintenance functions, without having to rely on personnel from the parent company or from operations personnel located outside South Dakota except in the case of weather or other emergency.

15. This Agreement is not intended to modify the terms or conditions of any outstanding order of the SD PUC regarding NorthWestern or any outstanding agreement or stipulation between the SD PUC and NorthWestern, and all such outstanding orders, agreements and stipulations shall remain in effect and unchanged by this Agreement. The omission of any particular matter within the regulatory authority of the SD PUC from the terms of this Agreement is not intended to have any effect whatsoever upon such omitted matter nor imply any result or consequence with respect to such matter, and no inference shall be drawn from its omission.

16. Within five days after the effective date of this Agreement, Applicants shall file a notice with FERC of the parties resolution of their issues concerning the Merger in Docket No. EC06-127-000. It shall be the responsibility of Applicants to comply with all Federal Power Act or FERC requirements as to the filing of the Settlement Agreement.

17. Provided all conditions in this Agreement are met, the SD PUC will not object to FERC's approval of the Merger as it is described in the Application and will not re-file a Protest or Comment in the proceeding unless the Application is amended materially.

18. This Agreement will be required to be a public record of the SD PUC approved at a public meeting of the SD PUC.

19. After the effective date of this Agreement, in the event of a material change in circumstances, including a change in applicable law, or in the event that any Applicant or the SD PUC believes that a provision of this Agreement is causing, or is probable of causing in the

foreseeable future, an unjust, unreasonable, imprudent or unlawful result, such Party may petition the SD PUC for relief from such provision or for modification or termination of this Agreement, which the SD PUC will act on in accordance with applicable legal and regulatory standards subject to the right of appeal under South Dakota law.

20. This Agreement and each of its provisions is binding upon (i) Applicants, their affiliates, parents, subsidiaries, officers, directors, shareholders, agents, representatives, attorneys, successors and assigns, specifically including, without limitation, any purchaser or other transferee, directly or indirectly (whether by purchase, merger, consolidation or otherwise), of all or a material portion of NorthWestern's public utility assets and (ii) the SD PUC, any successor agency, and their officers, directors, agents, representatives, and attorneys.

21. Except as set forth in paragraph 19, the terms of this Agreement may only be amended or modified by a writing that has been executed by all of the Parties intending to be bound thereby.

22. This Agreement (and any amendments hereto) may be executed in two or more counterparts, each of which shall be deemed an original but all of which together shall constitute but one and the same instrument. Executed signature pages may be removed from partially executed counterparts and attached to one or more other counterparts to produce fully executed counterparts. This Agreement may be executed by facsimile copy, and each signature shall be and constitute an original signature, again as if all Parties had executed a single original document. This Agreement shall be originally executed as many times as required to provide a fully executed duplicate original of such document to each Party requesting it.

23. This Agreement shall be construed and interpreted in accordance with the laws of the State of South Dakota with respect to matters within the state jurisdiction and with respect to matters within the federal jurisdiction, federal law.

24. Each of the parties hereto represents and warrants that the person(s) whose name(s) appears below as the signatory(ies) for such Party has authority to execute this agreement on behalf of such Party and that all necessary action has been taken by the Party's governing body to authorize such execution, including in the case of the SD PUC the approval by commission vote in accordance with South Dakota law.

WHEREFORE, the Parties have each indicated their agreement hereto by the signatures of their authorized representatives below.

NORTHWESTERN CORPORATION and its subsidiaries
NORTHWESTERN ENERGY MARKETING, LLC and
THE CLARK FORK AND BLACKFOOT, LLC

By: _____
Michael Hanson
Chief Executive Officer

BABCOCK & BROWN INFRASTRUCTURE LIMITED and its subsidiaries
BBI US HOLDINGS PTY LTD., BBI US HOLDINGS II CORP., and
BBI GLACIER CORP.

By: _____
Steven Boulton
Chief Executive Officer

SOUTH DAKOTA PUBLIC UTILITIES
COMMISSION

By: _____
Patty Van Gerpen
Executive Director

By: _____
John J. Smith
General Counsel