NorthWestern Energy
Delivering a Bright Future

January 29, 2018

Patricia Van Gerpen, Executive Director
South Dakota Public Utilities Commission
500 E. Capitol
Pierre, SD 57501

RE: GE17-003 – In the Matter of Staff's Request to Investigate the Tax Cuts and Jobs Act on South Dakota Utilities

Dear Ms. Van Gerpen:

As a result of the Tax Cuts and Jobs Act (TCJA) 2017, NorthWestern Energy (NorthWestern) expects its earnings to increase in 2018 due to the reduction in statutory tax rates. We expect this lower statutory rate will result in lower future revenue requirements. During the December 29, 2017 South Dakota Public Utilities Commission (Commission) hearing in Docket GE17-003, several options for implementation of this lower tax rate were discussed. The option that best fits NorthWestern's situation at this time would be to use these tax benefits as a means to moderate the impact of future rate increases. NorthWestern is making a significant investment in advanced metering infrastructure (AMI) technology starting in 2018 to improve our ability to manage outages and provide energy usage information to our customers. That investment, along with other modernization investments, will put upward pressure on customers' rates. NorthWestern's desire is to keep rates stable for our customers. Therefore, rather than reducing rates as a result of the TCJA only to increase them shortly thereafter due to an increase in our revenue requirement, our proposal would moderate the volatility of customer rate changes.

NorthWestern acknowledges that customers could benefit from tax reform immediately, and our preferred approach delays that benefit until we file a future rate case. Therefore, NorthWestern also proposes to provide interest on the accrued tax benefits (equal to our current rate of return) to ensure customers capture the time value of money of those tax benefits. Effective January 1, 2018, the tax benefits would be accrued in a regulatory liability until our next natural gas and electric rate cases are filed. This liability would be amortized, over a mutually agreed upon period, as a reduction to the increase in revenue requirement approved in our next rate cases. Our proposal ensures that customers capture the full tax benefits without the volatility of a short-term rate decrease followed by a larger increase. As a result of our investment in AMI and other modernization efforts in the near future, NorthWestern believes it is likely we will file general rate cases (electric and natural gas) by 2020.

Additionally, NorthWestern joined the Southwest Power Pool (SPP) as a transmission-owning member effective October 1, 2015, and thus receives a revenue requirement from SPP for certain qualifying transmission facilities. NorthWestern flows this revenue requirement back to customers through its Delivered Cost of Energy Adjustment Clause. The revenue requirement is updated annually and determined by a formula rate using actual historical costs. The next formula rate will be filed March 1, 2018 to be effective April 1, 2018 and will use 2017 historical data. Thus, the revenue requirement will not be impacted by the tax reduction until April 1, 2019. We expect our revenue requirement to decrease due to the reduction in tax rates. Therefore, beginning April 1, 2019, our customers will receive a smaller credit through the Delivered Cost of Energy Adjustment Clause as a result of the TCJA.

NorthWestern is working to quantify the benefit of TCJA and will include those calculations in a filing to the Commission by March 31, 2018. NorthWestern cautions that the benefit is not as simple as taking the difference of 35% and 21% multiplied by our expected South Dakota electric and natural gas earnings. The income taxes we are currently accruing are significantly less than 35%, as a result of various deductions the IRS has historically provided to utilities. Many of those deductions remained in the TCJA, while others did not. As the Commission may have noted in our earnings guidance for 2018, NorthWestern's expected tax rate was in the range of 8%-12%. Nonetheless, NorthWestern will see a tax reduction benefit and that benefit will be applied to our expected South Dakota electric and natural gas earnings for 2018 to preserve the benefit for our customers. Again, NorthWestern will provide that information in its filing to the Commission due March 31, 2018. NorthWestern appreciates the opportunity to discuss our proposal further with the Commission and its staff as we work together to keep customers' rates stable.

Sincerely,

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