



A Division of MDU Resources Group, Inc.

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February 15, 2018

Executive Secretary
North Dakota Public Service Commission
State Capitol Building
Bismarck, ND 58505-0480

Re: Rate Impact and Accounting Treatment Investigation
Tax Cuts and Job Act of 2017

Montana-Dakota Utilities Co. – Initial Comments
Case No. PU-17-490

Montana-Dakota Utilities Co., a Division of MDU Resources Group, Inc. (Montana-Dakota), herewith provides its initial comments pursuant to the North Dakota Public Service Commission's Order Initiating Investigation dated January 10, 2018.

Montana-Dakota appreciates the opportunity to provide a summary of its review of the 2017 Tax Cuts and Jobs Act signed into law on December 22, 2017 (TCJA) and findings thus far. Montana-Dakota will also address next steps proposed to reflect the effects of the TCJA on its natural gas and electric rates and tracking mechanisms currently authorized in North Dakota.

The primary impacts of the TCJA to Montana-Dakota's utility operations are described below:

Reduction in Corporate Tax Rate from 35% to 21% –

In addition to simply calculating taxes based on a 21% rate versus a 35% rate effective January 1, 2018, under the TCJA Montana-Dakota was required to immediately remeasure utility-related deferred taxes¹ based on the 21% tax rate with a regulatory liability established representing the difference between the old

¹ For tax filings, utilities calculate income tax liability using accelerated depreciation as a deduction. For regulatory and financial reporting purposes, utilities must use straight-line depreciation to determine depreciation expense and to calculate income taxes. The difference in income taxes calculated using the two methods is deferred tax, which represents the utility's tax liability in future periods. The deferred taxes have historically been collected at the statutory tax rate in effect at the time the timing difference originated and would have been paid as taxes. Because of the significant reduction in the federal tax rate, the amount collected over the current statutory rate is referred to as "excess deferred taxes".

and new tax rate referred to as the excess deferred taxes. In accordance with the TCJA a determination of the excess deferred taxes was made on a company-wide basis in order to record the amount of excess deferred taxes in 2017.

The next step in the process involved determining how those excess deferred taxes would be returned to customers. Under the TCJA, the plant related excess deferred taxes are to be amortized over the average remaining life of the assets referred to as the Average Rate Assumption Method (ARAM). ARAM is used because the excess deferred taxes may not be returned any faster than over the remaining lives of the underlying assets. The determination is based on the year tax depreciation for the vintage account is less than book depreciation recorded for the vintage account or asset. Montana-Dakota recently identified the annual excess deferred taxes that will reverse in 2018 on a jurisdictional basis and is analyzing those results, the impact to rates and the expected amortization in future years. Of the total excess deferred taxes recorded as a regulatory liability, the plant related excess deferred taxes are the most significant.

Non-plant excess deferred taxes are not subject to ARAM. Montana-Dakota is proposing to flow those excess deferred taxes back over a 10-year period based on a review of the items contributing to the excess deferred tax balance.

Production Tax Credit (PTC) –

The TCJA did not change the existing law applicable to the PTC rate currently at 2.4 cents/Kwh.

Bonus Tax Depreciation –

The 40 percent bonus depreciation to be applicable in 2018 was eliminated under the TCJA.

Interest Expense Deductibility –

The deduction for net interest expense is limited to 30% of adjusted taxable income (taxable income without interest expense/income, net operating losses and depreciation after four years). This limitation does not apply to regulated public utilities.

Contribution in Aid of Construction (CIAC) –

Contributions received from customers, except for contributions made by a governmental entity pursuant to a master development plan that has been approved prior to enactment of the TCJA are now taxable.

Miscellaneous Expense Deductions-

The TCJA also resulted in changes to various expense deductions. As noted below most of the changes are not anticipated to have an effect at this time.

- lobbying expenses in regard to legislation before local governing bodies are no longer deductible – no anticipated effect on Montana-Dakota.
- limits in the nonrecognition of gain for like-kind exchanges to real property that is not held primarily for sale – no anticipated effect on Montana-Dakota.
- eliminates the entertainment expense deduction and places a 50% limit on employer expenses associated with providing food and beverages to employees through an eating facility meeting (the de minimis fringe requirement) – effect is expected to be immaterial as the Company's policies are consistent with the new rules.
- eliminates the deduction for qualified transportation fringe to employees except for ensuring employee safety – no anticipated effect on Montana-Dakota.
- research and development expenses must be capitalized and amortized over 5 years – the Company is currently researching this item.
- disallows a deduction for any settlement, payout or attorney fees related to sexual harassment or sexual abuse if payments are subject to a nondisclosure agreement – no anticipated effect on Montana-Dakota.
- denies a deduction for any amounts paid or incurred to, or at the direction of, a government or governmental entity in relation to the violation of any law or investigation into the potential violation of any law with an exception for restitution identified in a court order or settlement agreement – no anticipated effect on Montana-Dakota.
- repeals performance based compensation exceptions to the \$1 million annual limitation, with certain transition relief provisions – transition relief provisions that would be applicable to Montana-Dakota are under review.

Montana-Dakota currently recovers its revenue requirements through several mechanisms. Each of those mechanisms and the impact of the TCJA will be discussed in turn.

Natural Gas Utility

Base Retail Rates

Montana-Dakota's natural gas distribution revenue requirement is currently recovered through base retail rates established in a general rate case proceeding. As the Commission is aware, the Company submitted an application requesting authority to increase its natural gas distribution rates on July 21, 2017 in Case No.

PU-17-295 that is currently pending before the Commission. As the TCJA was only placed into law on December 22, 2017, the pending rate application does not yet incorporate its effects. The TCJA will reduce the Company's request in the pending application, including the amount required to be recovered under the interim rates implemented on September 19, 2017. The Commission recently authorized Montana-Dakota's request for a Continuation of the Hearing originally scheduled to begin on February 28, 2018 to reflect the effects of the TCJA and to allow all parties the time necessary to investigate the changes. Because this change in hearing dates will lengthen the time interim rates will be in effect, Montana-Dakota submitted a request to reduce the interim natural gas rates in Case No. PU-17-295 based on the change in the current tax rate only on February 14, 2018 resulting in a decrease in required revenues under interim of approximately \$1.9 million.

The full effect of the TCJA on distribution rates will be provided as part of the Company's rebuttal testimony expected to be filed by March 15, 2018. This will allow Commission Advocacy Staff and other intervenors the opportunity to review and respond to Montana-Dakota's updates reflecting the TCJA. The overcollection of rates associated with the TCJA from January 1, 2018 through the date new interim rates are implemented will be refunded to customers as part of the interim refund process upon a final order.

Gas Cost Tracking Adjustment

Montana-Dakota recovers all gas costs through its Cost of Gas rate that is subject to change on a monthly basis. The only identified change to the Cost of Gas mechanism is a required change to the tax effected authorized overall rate of return on rate base that is used to determine the return on prepaid demand, commodity and storage balances recovered through the Cost of Gas rate. This change was incorporated in the Cost of Gas rate to be effective March 1, 2018 (filed on February 8, 2018 in Case No. PU-18-008). Any differences associated with Cost of Gas rates charged in January and February 2018 will be reflected in the deferred account and returned to customers through that process.

Electric Utility

Base Retail Rates

Montana-Dakota's currently effective electric rates were authorized in Case No. PU-16-666 for service rendered on and after August 7, 2017. Montana-Dakota is currently reviewing the authorized rates to determine the full effect of the TCJA. Montana-Dakota estimates a reduction in base retail rates resulting from the

corporate tax rate change and the flow back to customers for the excess deferred taxes based on the cost of service authorized in Case No. PU-16-666 of approximately \$8-10 million. Montana-Dakota expects to have results available to submit to the Commission by March 1, 2018 including proposed rate changes. Because of potential volatility in the annual amount to be returned to customers associated with the application of the ARAM, a mechanism to track those changes between rate cases may be appropriate and will be discussed further in the Company's March 1 filing.

Montana-Dakota will also provide a proposed plan for rate refunds that will be applicable from January 1, 2018 through the date new electric rates are authorized by the Commission.

Renewable Resource Cost Adjustment

Montana-Dakota recovers the cost of its wind generating resources, Diamond Willow, Cedar Hills and Thunder Spirit I through its Renewable Resource Cost Adjustment Rate 55. The current charges under Rate 55 were effective August 7, 2017 as authorized in Case No. PU-16-666. Montana-Dakota reviewed the charges applicable under Rate 55 again in November 2017 and found that no change was necessary. Montana-Dakota's preliminary findings in regard to the effects of the TCJA indicate the revenues to be collected under the Renewable Resource Cost Adjustment will be reduced by approximately \$1 million. Montana-Dakota will submit updated charges under the Renewable Resource Cost Adjustment by February 23, 2018. Any overcharges occurring between January 1, 2018 and the date the new rates are implemented will be returned to customers through the deferred account.

Generation Resource Recovery Rider

Montana-Dakota recovers the cost of its Lewis & Clark II generating resource through its Generation Resource Recovery Rider Rate 56. The current charges under Rate 56 were effective August 7, 2017 as authorized in Case No. PU-16-666. Montana-Dakota submitted proposed changes to the Rate 56 charges on November 27, 2017 in Case No. PU-17-469. Montana-Dakota's preliminary findings in regard to the effects of the TCJA indicate the revenues to be collected under the Generation Resource Recovery Rider will be reduced by approximately \$300,000. Montana-Dakota will submit updated charges under the Generation Resource Recovery Rider by February 23, 2018. Any overcharges occurring between January 1, 2018 and the date the new rates are implemented will be returned to customers through the deferred account.

Transmission Cost Adjustment

Montana-Dakota recovers the cost of MISO and Southwest Power Pool (SPP) transmission expenses and passes back transmission related credits through its Transmission Cost Adjustment Rate 59. The current charges under Rate 59 were effective August 7, 2017 as authorized in Case No. PU-16-666. Montana-Dakota submitted proposed changes to the Rate 59 charges on November 21, 2017 in Case No. PU-17-468. The Company anticipates changes will be required to reflect reductions in the MISO charges reflecting the TCJA to be offset by a lower Transmission Facility Credit from SPP. Montana-Dakota and other MISO Transmission Owners with projected rates submitted a filing to FERC on February 1 requesting FERC waive certain provisions of the MISO tariff in order for the Transmission Owners with projected rates to revise rates to reflect the reduction in the corporate tax rate. Under the MISO tariff, rates are to be changed only on an annual basis with any changes reflected in subsequent true-ups. If the waiver is granted, MISO expects to implement new rates reflecting the reduction in the tax rate by April 1 for March service. MISO will then rebill January and February service so that any tax benefits will be reflected in rates effective January 1, 2018.

Environmental Cost Recovery Rider

Effective August 7, 2017, as authorized in Case No. PU-16-666, the Environmental Cost Recovery Rider reflects the recovery of the deferred balance existing as of December 31, 2016 applicable to assets that were moved into retail rates. Montana-Dakota is recovering that deferred balance over a 2-year period beginning with rates established in the electric rate case. The TCJA has no impact on the deferred balance recovery rates. Recoveries will continue to be reviewed to determine the end date of the charges under the Environmental Cost Recovery Rider.

Fuel and Purchased Power Adjustment

Any changes associated with coal, fuel, reagents or MISO purchases because of the TCJA will flow through the Fuel and Purchased Power Adjustment that is changed on a monthly basis.

Montana-Dakota appreciates the Commission's consideration of options for finding a fair and equitable basis for reflecting the TCJA in customer rates and the time necessary to determine the changes given the timing of TCJA enactment and the work necessary to determine year end results that formed the basis for the proposals to be submitted.

In summary, Montana-Dakota proposes to capture the effects of the TCJA in its natural gas rates through the pending docket, will submit changes to the Renewable and Generation Rider by February 23, 2018 and file new electric rates by March 1, 2018.

If you have any questions regarding these comments, please contact me, at (701) 222-7856 or tamie.aberle@mdu.com.

Sincerely,

A handwritten signature in dark ink that reads "Tamie A. Aberle". The signature is written in a cursive style with a large initial "T".

Tamie A. Aberle
Director of Regulatory Affairs

Attachments

cc: Karl Liepitz
Garret Senger