

**STATE OF NORTH DAKOTA  
PUBLIC SERVICE COMMISSION**

**Montana-Dakota Utilities Co., a Division of MDU  
Resources Group, Inc.  
Tax Reform Effects  
Rates**

**Case No. PU-18-89**

**ORDER ON SETTLEMENT**

**September 26, 2018**

**Preliminary Statement**

On March 9, 2018, Montana-Dakota Utilities, Co. (MDU) filed revised electric retail rates in response to the federal 2017 Tax Cuts and Jobs Act, Pub L. 115-97, H.R.1, 115<sup>th</sup> Congress, enacted December 22, 2017, (TCJA) and the Commission's January 10, 2018 Order in Case No. PU-17-490 .

On April 25, 2018, the Commission issued a Notice of Opportunity for Hearing, which provided until June 8, 2018 for receiving written comments and hearing requests. No response was received. The Notice identified the issue to be considered in this matter is whether the proposed rates are just and reasonable.

On August 10, 2018, MDU and Commission Advocacy Staff filed a Settlement Agreement that they state represents a settlement of all outstanding issues between the settling parties regarding MDU's application to update retail rates in response to the TCJA.

On August 30, 2018, the Commission discussed the matter with the parties during an informal hearing.

**Discussion**

The TRJA affects MDU's income tax expense and excess deferred income taxes (EDIT) in three ways:

1. Income Tax Reduction: The annual income tax expense reduction is estimated at \$7,232,919. This reflects the effect of the income tax rate change from 35% to 21% on taxable income.
2. Plant EDIT: The Internal Revenue Service (IRS) protects the method of return of plant Excess Deferred Income Tax (EDIT). The IRS specifies the manner and time period in which the EDIT for these assets must be reversed known as the Average Rate Assumption Method (ARAM). ARAM requires the return of EDIT over the remaining life of the asset that created the EDIT. The total protected EDIT balance

is estimated at \$61,506,000, however using ARAM the 2018 reversal attributable to MDU North Dakota electric operations is valued at \$1,213,000.

3. Non-plant EDIT: Non-plant EDIT relates to the remaining company assets attributable to electric operations that do not qualify for IRS ARAM treatment. The Commission may set the timing and manner of return of the Non-plant EDIT. This total non-protected EDIT balance is estimated at \$1,778,283.

The Settlement Agreement provides three mechanisms for passing TCJA savings to customers:

1. Rate Adjustment: A base rate reduction will be applied to the kWh energy charge to all customers on an equal percentage basis for an ongoing annual revenue reduction of \$8,436,006. This represents the entirety of the \$7.2M income tax reduction and 75% of the tax-effected 2018 annual Plant EDIT. The remaining 25 percent of the annual plant EDIT (approximately \$300,000) will be retained by MDU to offset ongoing infrastructure investment (e.g. replacement of underground cable installed prior to 1983).
2. Customer Refund: The amount of the customer refund will be 4.5% of revenue collected from the January 1, 2018 effective date of the TCJA through the date of final implementation of the rate adjustment. The exact refund and method of calculation will be filed within 30 days of Commission adoption of the settlement agreement.
3. Rider Rate Adjustments: The entire non-plant EDIT balance of \$1.7M will be tax effected (increases to \$2,352,379) and returned to customers through application to the under-collection balances of MDU's electric billing riders in the following order: First to zero out the Environmental Cost Recovery Rider (ECRR), then to the Generation Cost Recovery Rider (GCRR), and in the event of a remainder, to the Transmission Cost Recovery Rider (TCRR).

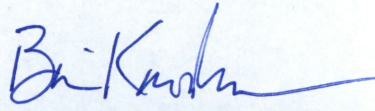
Having considered this matter, the Commission finds MDU's retention of 25% of tax-effected 2018 plant Edit is not acceptable. Implementing the Settlement Agreement will result in just and reasonable rates if 100% of tax-effected 2018 plant EDIT is returned to customers. Therefore, the Commission issues the following:

### **Order**

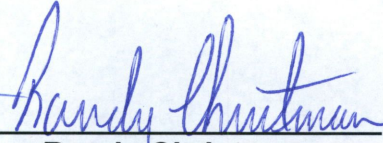
1. The Settlement Agreement, attached to and made a part of this Order, is APPROVED except for MDU's retention of 25% of tax-effected 2018 plant EDIT.
2. MDU shall adjust base rates to return 100% of the tax-effected 2018 plant EDIT

3. MDU shall file within 30 days, for Commission approval, compliance rate schedules and a refund plan consistent with the Settlement Agreement and this Order.

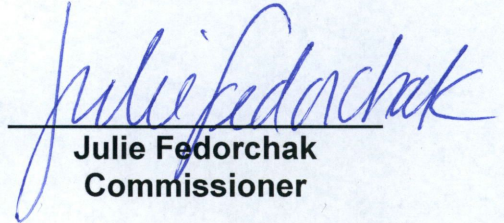
**PUBLIC SERVICE COMMISSION**



**Brian Kroshus**  
Commissioner



**Randy Christmann**  
Chairman



**Julie Fedorchak**  
Commissioner

**STATE OF NORTH DAKOTA  
PUBLIC SERVICE COMMISSION**

<b>Montana-Dakota Utilities Co.</b>	)	
<b>Application to Reduce Rates to</b>	)	<b>Case No. PU-18-89</b>
<b>Reflect the Effects of Tax Cuts and</b>	)	
<b>Jobs Act of 2017</b>	)	

**SETTLEMENT AGREEMENT**

This Settlement Agreement is entered into by and between Montana-Dakota Utilities Co., a Division of MDU Resources Group, Inc. ("Montana-Dakota" or "Company"), and the Advocacy Staff of the North Dakota Public Service Commission ("Advocacy Staff"), (collectively the "Settling Parties"). The Settling Parties agree this Settlement Agreement, if approved by the Public Service Commission ("Commission"), would resolve all outstanding issues in this case between the Settling Parties in a manner consistent with the public interest and will result in just and reasonable rates for the Company's electric service in North Dakota.

**PROCEDURAL HISTORY**

1. On January 10, 2018, the North Dakota Public Service Commission issued an Order Initiating Investigation to determine the effect of the Tax Cuts and Jobs Act of 2017 (Tax Reform) on Montana-Dakota and other jurisdictional utilities in Case No. PU-17-490.
2. On February 15, 2018, Montana-Dakota filed its initial comments regarding the effects of Tax Reform on its natural gas and electric rates in Case No. PU-17-490
3. On March 9, 2018, Montana-Dakota filed an Application to decrease its rates for electric service in North Dakota by an annual revenue amount of \$7,231,099,

representing a 3.9 percent decrease from current rates in response to Tax Reform and the Commission's January 10, 2018 Order issued in Case No. PU-17-490. Filed with the Application were revised tariffs and supporting statements. The Application was designated as Case No. PU-18-89 by the Commission.

4. On March 29, 2018 the Commission suspended the rates filed on March 9 and on April 25, 2018, the Commission issued a Notice of Opportunity for Hearing. Comments and requests for hearing were to be submitted by June 8, 2018. No comments or requests for a hearing were submitted to the Commission.

5. This Settlement Agreement is supported by the administrative record. Accordingly, the Settling Parties jointly recommend the Commission issue an Order approving this Settlement Agreement in its entirety, without conditions or modifications.

#### **TERMS OF SETTLEMENT AGREEMENT**

1. Change in Retail Rates. The Settling Parties agree to, and recommend the Commission approve, a decrease in Montana-Dakota's electric service rates for retail customers in North Dakota to yield an annual revenue decrease of \$8,436,006 effective upon a final Order in this proceeding. Supporting schedules are provided in Exhibit 1. This amount represents an overall decrease in retail rates, including base retail sales and the fuel and purchase power adjustment, of 4.5 percent. The change in electric retail rates reflects a recalculation of the revenue requirement, authorized in August 2017 in Case No. PU-16-666, to reflect the change in the tax rate from 35 percent to 21 percent of \$7,232,919 plus 75 percent of the plant related excess deferred income taxes of \$1,212,633 as adjusted for taxes or \$1,203,087. The remaining 25 percent of the 2018 plant related excess deferred income taxes will serve to support distribution infrastructure

projects such as underground cable systems installed before 1983 that are subject to a significantly higher failure rate than systems installed after 1983 and an LED change out for street lighting systems currently installed in approximately 100 North Dakota communities.

2. Non-Plant Related Excess Deferred Income Taxes. The Settling Parties agree to offset the deferred balances being collected from customers under the Environmental Cost Recovery Rider Rate 57 and the Generation Resource Recovery Rider Rate 56 with the total amount of non-plant excess deferred income taxes of \$1,778,283 as adjusted for income taxes equating to a revenue reduction of \$2,352,379. The Environmental Cost Recovery Rider deferred balance existing as of the date of the Order issued in this case will be eliminated entirely with the remaining dollars credited to the Generation Resource Recovery Rider. Based on balances as of June 30, 2018, the Environmental Rider Rate 57 balance and resulting rates will go to zero. The Generation Resource Recovery Rider will be reduced as shown below. In the event the Generation Resource Recovery Rider deferred balance is also fully offset at the time of Commission approval of this agreement any additional dollars will be applied to the Transmission Cost Adjustment Rate 59 deferred balance.

**Generation & Environmental Rider Balances  
as of June 30, 2018**

	Total	Amount of Reduction
Generation	\$823,651	\$(666,967)
Environmental	1,685,412	(1,685,412)
	\$2,509,063	(\$2,352,379)

3. Revenue Allocation. The Settling Parties agree the decrease in retail rates

described in paragraph 1 will be allocated to the classes on an equal percentage basis in order to maintain the class revenue allocation authorized in Case No. PU-16-666 as shown in Exhibit 2. The Settling Parties further agree that the revenue decrease allocated to each rate class shall be applied to the energy component of each rate with the exception of Irrigation Service Rate 25 that will also reflect a decrease in the summer demand component.

4. Impact to Residential Customers. A Residential customer using 980 Kwh per month on average will see a decrease in their bills of \$5.49 or 5 percent reflecting the change in retail rates and the reduction in the deferred rider balances based on the estimates provided in Paragraph 2.

5. The parties agree that upon execution of this Settlement Agreement there are no outstanding issues related to Tax Reform or Case No. PU-17-490 with respect to Montana-Dakota's electric operations in North Dakota.

#### **OTHER TERMS AND CONDITIONS**

A. Basis of Settlement. It is agreed this Settlement Agreement is a negotiated settlement agreement subject to approval by the Commission. This Settlement Agreement does not establish any principle or precedent, nor adopt or recommend any specific type or amount of expense or rate base for this or any future proceeding, nor any principle or precedent regarding rate design methodology.

B. Effect of the Settlement Negotiations. It is understood and agreed that all offers of settlement and discussions related to this Settlement Agreement are privileged and may not be used in any manner in connection with proceedings in this case or otherwise, except as provided by law. In the event the Commission does not approve

this Settlement Agreement, it shall not constitute part of the record in this proceeding and no part thereof may be used by any party for any purpose in this case or otherwise.

C. Rate Refund. Upon issuance of a Commission Order for new electric rates, the Company will determine the final amount to be refunded to customers subject to Advocacy Staff review and agreement. The amount to be refunded will be determined by applying the 4.5 percent percentage decrease in retail rates (including the fuel and purchase power adjustment) to the revenues collected for service provided beginning January 1, 2018 through the period ending with the implementation of new rates. The Settling Parties agree the Company shall issue a bill credit to customers, upon determination of the amount to be refunded, including interest at the three-month Treasury Bill rate as published by the Federal Reserve Board. A refund plan will be submitted within 30 days of an entry of an Order in this case.

D. Applicability and Scope. This Settlement Agreement shall be binding on the Settling Parties, and their successors, assigns, agents, and representatives. Consistent with the Commission's settlement guidelines, this Settlement Agreement does not set policy or overturn precedent. This Settlement Agreement shall not in any respect constitute an agreement, admission or determination by any of the Settling Parties as to the merits of any specific allegation or contention made by the Settling Parties in this proceeding.

E. Effective Date. This Settlement Agreement shall be effective on the date of the Commission Order approving the Settlement Agreement. The revised rates and tariffs agreed to by this Settlement Agreement shall be effective on the dates specified herein.

F. Modification. If the Commission's Order modifies or conditions approval of

this Settlement Agreement, it shall be deemed terminated if any Settling Party files a letter with the Commission within three (3) business days of notice of such Order stating that a condition or modification to the Settlement Agreement is unacceptable to such party.

### CONCLUSION

The Settling Parties agree the terms of this Settlement Agreement are a result of negotiations between the Settling Parties, are in the public interest and will result in reasonable electric rates. For these reasons, the Settling Parties urge the Commission to approve the Settlement Agreement.

Dated this 9<sup>th</sup> day of August, 2018.

**MONTANA-DAKOTA UTILITIES CO.**

By: Garret Senger

Its: Garret Senger  
EVP - Regulatory Affairs,  
Customer Service & Administration

Dated this 8<sup>th</sup> day of August, 2018.

**NORTH DAKOTA PUBLIC SERVICE  
ADVOCACY STAFF**

By: John M. Schuh

John M. Schuh  
Advocacy Staff Counsel

**MONTANA-DAKOTA UTILITIES CO.  
INCOME STATEMENT  
ELECTRIC UTILITY - NORTH DAKOTA  
PROJECTED 2017 - BASE RETAIL RATES**

**ADJUSTED FOR TCJA VS. AUTHORIZED**

	<u>TCJA Adjusted</u>	<u>PU-16-666 Authorized</u>	<u>Change</u>
Operating Revenues			
Retail Sales (Base Only) 1/	\$178,407,642	\$186,843,648	(\$8,436,006)
Other	3,671,067	3,671,067	0
Total Revenues	<u>\$182,078,709</u>	<u>\$190,514,715</u>	<u>(\$8,436,006)</u>
Operating Expenses			
Operation and Maintenance			
Fuel & Purchased Power	\$54,243,161	\$54,243,161	\$0
Other O&M	53,324,432	53,324,432	0
Total O&M	<u>\$107,567,593</u>	<u>\$107,567,593</u>	<u>\$0</u>
Depreciation and Amortization	24,736,626	24,736,626	0
Taxes Other Than Income	5,934,298	5,934,298	0
Income Taxes	6,734,973	15,170,979	(8,436,006)
Total Expenses	<u>\$144,973,490</u>	<u>\$153,409,496</u>	<u>(\$8,436,006)</u>
Operating Income	<u>\$37,105,219</u>	<u>\$37,105,219</u>	<u>\$0</u>
Rate Base	<u>\$503,873,151</u>	<u>\$503,873,151</u>	<u>\$0</u>
Rate of Return	<u>7.364%</u>	<u>7.364%</u>	<u>0.000%</u>
Return on Equity	<u>9.650%</u>	<u>9.650%</u>	<u>0.000%</u>

1/ Revenue calculated prior to rate design.

**MONTANA-DAKOTA UTILITIES CO.  
REVENUE INCREASE CALCULATION  
ELECTRIC UTILITY - NORTH DAKOTA**

**CALCULATION OF REVENUE REQUIREMENT INCREASE**

<u>Authorized - PU-16-666</u>	<u>Projected 2017</u>
Net Pro Forma Rate Base	\$503,873,151
Overall Rate of Return	7.364%
Calculated Return on Rate Base	<u>\$37,105,219</u>
 Total Pro Forma Operating Expenses	 \$150,201,851
Total Pro Forma Revenue Requirement 1/ (less) Total Pro Forma Revenue Estimates	\$187,307,070 <u>182,029,218</u>
Unadjusted Revenue Increase Estimate	\$5,277,852
 Gross Up Factor 2/	 1.607756
Authorized Revenue Increase	<u><u>\$8,485,497</u></u>
 <b><u>Reflecting TCJA for 21% Tax Rate</u></b>	
Total Pro Forma Operating Expenses (Above)	\$150,201,851
Less: Reduction in Income Tax Expense (Page 3)	<u>5,240,439</u>
Total Pro Forma Operating Expenses	\$144,961,412
Total Pro Forma Revenue Requirement 1/ (less) Total Pro Forma Revenue Estimates	\$182,066,631 <u>182,029,218</u>
Unadjusted Revenue Increase Estimate	\$37,413
 Gross Up Factor 2/	 1.322837
Adjusted Revenue Increase	<u><u>\$49,491</u></u>
 <b>Change in Revenue Increase</b>	 <b>\$8,436,006</b>

1/ Calculated Return on Rate Base plus Pro Forma Expenses.

2/ Calculated as 1 divided by the inverse of the tax rate.

**MONTANA-DAKOTA UTILITIES CO.  
PRO FORMA INCOME STATEMENT  
ELECTRIC UTILITY - NORTH DAKOTA**

**CALCULATION OF OPERATING INCOME - PRIOR  
TO REVENUE INCREASE**

	<b>Montana-Dakota Authorized Op. Income</b>
<b><u>Authorized - PU-16-666</u></b>	
<b>Revenue:</b>	
Retail Sales Revenue	\$178,358,151
Other Revenue	3,671,067
Total Operating Revenue	<u>\$182,029,218</u>
<b>Operating Expenses:</b>	
Fuel & Purchased Power	\$54,243,161
Other O&M	53,324,432
Total Operating Expenses	<u>\$107,567,593</u>
Depreciation	24,736,626
Taxes Other Than Income	5,934,298
Current Income Taxes 1/	\$12,220,782
Deferred Income Taxes (So. Georgia)	(257,448)
Total Income Tax	<u>\$11,963,334</u>
Total Expenses	<u>150,201,851</u>
Net Operating Income	<u><u>\$31,827,367</u></u>
<b><u>Calculation of Income Tax (TCJA - 21% Tax Rate)</u></b>	
Pre-Tax Operating Income	\$43,790,701
Perms - AFUDC / Other	399,300
Interest Expense	(11,861,174)
Utility Operating Income - Pre-Tax	<u>\$32,328,827</u>
Income Tax Expense 2/	\$7,889,818
Excess DITs Plant (ARAM Method)-75%	(909,475)
Deferred Income Taxes (So. Georgia)	(257,448)
Total Income Tax	<u>\$6,722,895</u>
Net Operating Income (21% Rate)	<u><u>\$37,067,806</u></u>
<b>Reduction in Income Tax Expense</b>	<b>\$5,240,439</b>

1/ Calculated at 37.8015 percent effective rate.

2/ Calculated at 24.4049 percent effective rate.

MONTANA-DAKOTA UTILITIES CO.  
ELECTRIC UTILITY - NORTH DAKOTA

Allocation of Revenues - PU-16-666  
Reflecting TCJA

Customer Class	Authorized PU-16-666 Billing Determinants and Revenues				TCJA Change	
	Customers	Kwh	KW	Total Authorized Retail Revenues	\$	%
Residential Service	80,003	770,939,000		\$74,145,045	-\$3,345,621	-4.5%
Small General Service	11,867	117,869,000	17,553	12,930,742	-583,394	-4.5%
General Service	5,329	1,166,724,000	3,429,484	94,698,625	-4,283,499	-4.5%
Municipal Lighting	561	19,846,000		1,577,936	-71,230	-4.5%
Municipal Pumping	323	39,062,000	126,924	2,761,439	-124,802	-4.5%
Outdoor Lighting Service	2,604	7,437,000		725,862	-32,797	-4.5%
<b>Total North Dakota Electric</b>	<b>100,687</b>	<b>2,121,877,000</b>	<b>3,573,961</b>	<b>\$186,839,649</b>	<b>(\$8,441,343)</b>	<b>-4.5%</b>