Tax Cuts and Jobs Act of 2017
FERC Form 501-G

On July 18, 2018, the Federal Energy Regulatory Commission (Commission) issued a Final Rule on its proposed rulemaking in Docket No. RM-18-11 to address the impacts of the federal Tax Cuts and Jobs Act of 2017. The Final Rule requires interstate natural gas pipelines to file a one-time report (Form 501-G), which is designed to collect financial information to allow the Commission to evaluate the impact of the Tax Cuts and Jobs Act on pipelines' cost of service.

Pipelines filing the one-time report will have four options: take no action other than filing the one-time report; file a statement explaining why a rate adjustment is not needed; file a Natural Gas Act limited Section 4 filing to reduce rates; or make a commitment to file a general Section 4 rate case in the near future. Form 501-G uses data as of the end of 2017. Additionally, for pipelines whose capital structure was not less than 65% equity on December 31, 2017, the form uses an imputed capital structure at 57% equity, which is not consistent with Kern River's authorized capital structure.

Kern River supports the Commission's efforts to design a process to analyze each pipeline's individual situation. Kern River's Form 501-G filing is due by October 11, 2018, and will reflect conditions unique to Kern River.

Adjustments to reflect the uniqueness of Kern River's levelized rate design, namely 100% equity capital structure and use of average rate base, must be made. Additionally, data from 2017 includes prior period adjustments made for the implementation of the Alternate Period Two settlement and is appropriately removed from Kern River's 2017 return. Making these adjustments presents a more accurate view of the impact of tax reform on Kern River under current conditions.

As illustrated in the table below, no rate adjustment is appropriate for Kern River. Using Kern River's actual 2017 data, as reported in the FERC Form 2 and FERC Form 501-G (16.9% ROE), applying the effect of the new 21% corporate income tax rate (+4.2% ROE), making adjustments to reflect Kern River's unique levelized rate design (-8.0% ROE) and removing prior period adjustments (0.8% ROE), Kern River's ROE is 12.3%. Importantly, this 12.3% ROE does not reflect the large contract turn-back that occurred in 2018, after the date of the data reflected in FERC Form 501-G.

2017 ROE per FERC Form 501-G	16.9%
Impact of Tax Reform @ 21% Rate	4.2%
Hypothetical 2017 ROE per FERC Form 501-G	21.1%
Impact of Levelized Rate Design	-8.0%
Impact of Alternate Period Two	-0.8%
Hypothetical 2017 ROE	12.3%

Kern River's customers will benefit from tax reform through deferral of a rate case, as a reduction in tax costs will partially offset the loss of revenue from long-term demand-based transportation contracts. Currently, a total of 30% of Kern River's capacity is not under long-term contracts, leaving Kern River at risk for recovering its cost of service under month-to-month and other short-term contracts until the next rate case.

Recognizing market conditions might cause significant turn-back in 2018, Kern River developed several options to reduce rates. Ultimately, one option (Alternate Period Two) was implemented and provided a reduction of 9.3-24.8% below standard Period Two rates. Regardless, effective May 1, 2018, shippers turned back approximately 495,000 Dth/day of long-term firm capacity, bringing the total capacity uncontracted to approximately 648,000 Dth/day or 30% of Kern River's design capacity.

Subsequent to receiving the turn-back, Kern River offered the capacity on a continuous basis, and then during spring 2018 sold approximately 287,000 Dth/day of fixed-rate contracts through an open season process with only 20% of the capacity being sold for more than one year. Absent an opportunity to sell the remaining capacity under fixed-rate contracts at acceptable terms, Kern River proceeded to sell the capacity under month-to-month volumetric negotiated index-based contracts.

In summary, the turned-back capacity available May 1, 2018, has been sold under short-term contracts and approximately 381,000 Dth/day (18% of Kern River's design capacity) is month-to-month and subject to market volatility and rates that change daily. Kern River's rates are designed based on terms of 10 or 15 years and Kern River has historically contracted its capacity under long-term contracts. Therefore, on August 15, 2018, Kern River posted an open season to sell all capacity available for 12-month service beginning May 1, 2019, (496,960 Dth/day) for a term of five years or longer. Information regarding the open season can be found on Kern River's website at http://services.kernrivergas.com. Kern River urges all shippers to analyze the open season posting and seriously consider bidding on the capacity.

If Kern River re-contracts the capacity through the ongoing open season, Kern River may choose to submit a limited Section 4 filing to reduce rates. To provide timely information, Kern River will post a draft of its 501-G filing by Thursday, October 4, 2018, a week in advance of the required date to file it with the Commission.

Should you have any questions regarding this information please contact Preston Miller at 801-937-6346, Mac McGuire at 801-937-6410, John Dushinske at 801-937-6087 or Laura Demman at 402-398-7278.