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CORPORATE PARTICIPANTS

Jerome E. Nichols *Black Hills Corporation - Director of IR & Corporate Communications*

Linden R. Evans *Black Hills Corporation - President, CEO & Director*

Richard W. Kinzley *Black Hills Corporation - Senior VP & CFO*

CONFERENCE CALL PARTICIPANTS

Andrew Marc Weisel *Scotia Howard Weil, Research Division - Analyst*

Christopher James Turnure *JP Morgan Chase & Co, Research Division - Analyst*

Julien Patrick Dumoulin-Smith *BofA Merrill Lynch, Research Division - Director and Head of the US Power, Utilities & Alternative Energy Equity Research*

Michael Weinstein *Crédit Suisse AG, Research Division - United States Utilities Analyst*

Vedula Murti

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Black Hills Corporation First Quarter 2019 Earnings Conference Call. My name is Brian, and I will be your coordinator for today. (Operator Instructions) As a reminder, this conference is being recorded for replay purposes.

I would now like to turn the presentation over to Mr. Jerome Nichols, Director of Investor Relations of Black Hills Corporation. Please proceed, sir.

Jerome E. Nichols - *Black Hills Corporation - Director of IR & Corporate Communications*

Thank you, Brian. Good morning, everyone. Welcome to Black Hills Corporation's First Quarter 2019 Earnings Conference Call. Leading our quarterly earnings discussion today are Linn Evans, President and Chief Executive Officer; and Rich Kinzley, Senior Vice President and Chief Financial Officer.

Before we begin today, we would like to note that Black Hills will be attending the American Gas Association Financial Forum starting May 21 in Fort Lauderdale, Florida. Our leadership will be making a presentation, and the materials and webcast information will be posted on our website at www.blackhillscorp.com under the Investor Relations heading.

During our earnings discussion today, some of the comments we make may contain forward-looking statements as defined by the Securities and Exchange Commission, and there are a number of uncertainties inherent in such comments. Although we believe that our expectations and beliefs are based on reasonable assumptions, actual results may differ materially. We direct you to our earnings release, Slide 2 of the investor presentation on our website, and our most recent Form 10-K and Form 10-Q filed with the Securities and Exchange Commission for a list of some of the factors that could cause future results to differ materially from our expectations.

I will now turn the call over to Linn Evans.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Thank you, Jerome. Good morning, everyone, and thank you for joining us. Starting on Slide 3. I will cover highlights of the quarter. Rich will then provide a financial update, and then I'll finish with the discussion around our strategy.

Moving to Slide 4. Before I speak to the substance of the presentation this morning, I'd like to note a couple of items. Our theme this year for our annual report was ready, and we incorporated that theme into our presentation this year.

You will see messaging and branding, and our customers are seeing advertising around ready that started earlier this year. Being ready for our customers requires initiative to enhance everything that we do, constant evolution and being easy to do business with.

In the same way, we are improving how we can be ready for you, our investors, through improving how we present our investor materials. Going forward, our earnings presentations will be more focused on the current quarter's results and current initiatives, while our investor presentation will include more strategy and more forward-looking information.

You will note these changes in this presentation, where we have excluded some of our forward-looking, long-term reference slides. These slides will be included in our investor decks for events such as the upcoming AGA that Jerome mentioned and discussed. This does not, in any way, signal changes in our strategy or operations, however.

Moving to Slide 5. We had an excellent quarter from operationally and financially. Our operations teams performed exceptionally well during difficult winter conditions. We delivered strong quarterly earnings growth and advanced key strategic initiatives.

We were ready for our customers' energy needs, delivering safe and reliable service when they needed it the most. Safety is our top priority in all we do, and I'm proud of how our team, our system -- and our systems performed during severe weather conditions in the first quarter, with our team sustaining 0 injuries during the response to our customers' needs.

Our team proactively delivered the energy to keep our customers and community safe during the record-breaking cold temperatures associated with the January polar vortex, the nearly 100 mile-per-hour winds produced by the bomb cyclone in Colorado, and then Winter Storm Ulmer and its resulting flooding in Iowa and in Nebraska.

Because of our focus on safety and reliability and our investments in upgrading our infrastructure systems, we reduced, and in many cases, we avoided outages during these severe winter conditions. Our proactive approach to customers and communities helped affected communities begin to recover more quickly during widespread flooding in both Iowa and Nebraska, which was a difficult time of loss for many.

April 18 was National Line Mechanic Appreciation Day, and we could not be more proud of our resilient employees who maintain and enhance our extensive energy systems on a daily basis. These committed men and women often brave the worst of weather conditions head on to deliver the essential energy our customers depend upon. In fact, our line mechanic team currently has a perfect safety record in 2019 with 0 injuries year-to-date. I personally thank them for their commitment to safety and delivering valued service to our customers.

We delivered excellent earnings growth during the quarter. Returns in our customer-focused capital investments and colder-than-normal weather were primary drivers. We increased our 2019 guidance primarily due to the benefit of weather in the first quarter.

Strategically, we continued to refine our capital investment plan. We identified an additional $246 million of customer investment opportunities and added those investments to our 5-year capital forecast, providing further confidence in our long-term growth expectations. We also continued to advance regulatory proceedings. We submitted new filings and made progress on key capital projects despite severe winter weather.

Slide 6 lists our specific accomplishments for the quarter, starting with our Electric Utilities. In December, we announced our Renewable Ready program in South Dakota and Wyoming to provide our larger government, commercial and our industrial customers a cost-effective option to purchase utility-scale renewable energy. We are in the midst of the regulatory approval process for these voluntary tariffs, and we're also seeking approval to construct the $57 million 40-megawatt Corriedale Wind Energy Project to support this program. I'm pleased to report we continue to receive strong interest from potential customers for this program.

In South Dakota, construction continued on our 175-mile transmission line, extending from Rapid City, South Dakota to Stegall, Nebraska. The project remains on budget and on track to place the third and final 94-mile segment in service this fall. Two segments that span 81 miles were previously placed in service in both July and November of last year.

In September last year, we requested a new tariff to support the growth of blockchain in Wyoming. The tariff will help recruit blockchain companies to call Wyoming their home, delivering additional energy demand to our system. Following a hearing earlier this week on April 30, the Wyoming commission has approved the tariff.

Moving to the natural gas utilities on the right-hand side of Slide 6. On February 1, we filed a rate review in Colorado to consolidate the rates, tariffs and services of our 2 gas utilities in that state. Our Colorado gas rate review filing also seeks a new rider mechanism to recover integrity investments. We received approval for the legal consolidation last October and completed the consolidation last December. We have a hearing on the consolidated rate review application scheduled in June.

In March, we filed applications for the legal consolidation of our 2 natural gas utilities in Nebraska and our 4 natural gas utilities in Wyoming. Similar to the process in Colorado, we plan to file combined rate reviews following approval and completion of the pending consolidation requests.

At our power generation segment, we commenced construction in March on the $71 million 60-megawatt Busch Ranch II wind farm near Pueblo, Colorado. When placed in service this fall, the wind farm will deliver all of its renewable energy to Colorado Electric, a Black Hills utility affiliate, under a 25-year purchase -- power purchase agreement. This will fulfill the requirement of Colorado Electric to deliver 30% of its energy as renewable energy to customers by the year 2020.

On April 29, our Board declared a quarterly dividend of $0.505 per share, which represents an annualized rate of $2.02 in 2019, and is our 49th consecutive annual dividend increase, one of the longest track records in the utility industry and a record we are extremely proud of. Finally, we issued approximately 280,000 shares under our At-the-Market equity offering during the first quarter for net proceeds of approximately $20 million. To recap, we had a great quarter serving our customers, delivering for you, the shareholders, and making progress on our long-term customer-focused utility growth strategy.

Now I'll turn it over to Rich for our financial update. Rich?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

All right. Thanks, Linn, and good morning, everyone. I'm fighting quite a chest cold, so I have to step away from the microphone for a moment. Please bear with me but, hopefully, I can get through this clean.

I'll start on Slide 8. As Linn noted, we delivered solid first quarter financial performance. Returns on investments made to benefit customers at our gas utilities and favorable weather year-over-year at our natural gas and electric utilities were the big drivers of the strong Q1 financial results.

Our quarterly EPS, as adjusted, increased 6% year-over-year, despite dilution from 11% increased share count related to the equity unit conversion back last November of 2018. As a result of our strong first quarter, we increased our 2019 EPS guidance by $0.05 on each end of the range to $3.40 to $3.60 per share. We also reaffirmed our 2020 EPS guidance range of $3.50 to $3.80 per share. The assumptions related to our earnings guidance are detailed on Slides 43 and 44 in the appendix.

On Slide 9, we reconciled GAAP earnings to earnings as adjusted, a non-GAAP measure. We do this to isolate special items and communicate earnings that better represent ongoing performance. This slide displays the last 5 quarters and trailing 12 months as of March 31, 2019, and 2018.

In Q1 2019, we had no special items. We did experience special items in 2018, not reflective of our ongoing performance, all of which were income tax related. The first item reflected the impact of the Tax Cuts and Jobs Act throughout the year. The second and larger item related to tax benefits of legal restructurings completed in 2018.

As part of an effort to simplify our legal structure in Q1 and Q4 last year, we restructured certain entities acquired as part of the SourceGas acquisition. The restructurings increased goodwill that is amortizable for tax purposes, resulting in a $49 million deferred tax benefit in the first quarter and a $23 million deferred tax benefit in the fourth quarter. These items are not indicative of our ongoing performance and then accordingly, we reflect them on an as-adjusted basis.

Our first quarter 2019, as adjusted, EPS was $1.73 compared to $1.63 for the first quarter last year. As Linn and I already noted, the earnings uplift this year was primarily driven by returns on customer investments and a colder winter heating season. We estimate that winter weather last year, as compared to normal, positively impacted Q1 2018 EPS by $0.05. This year, we estimate that colder weather compared to normal positively impacted Q1 2019 EPS by $0.12.

Also, we expect to enjoy a lower effective tax rate this year compared to last year, excluding the 2018 special items I just mentioned. I will discuss this further on the next slide.

Slide 10 is a slide we added to our investor materials last year to improve transparency related to year-over-year comparisons. The waterfall chart illustrates the primary drivers of our positive results from Q1 2018 to Q1 2019. All amounts on this chart are net of income taxes. I'll add more detail by segment on the next slide. But overall, our utilities delivered strong gross margins, with an increase of over 7% in Q1 2019 compared to Q1 2018. Total operating expenses were approximately 5% higher compared to Q1 last year, driven primarily by higher outside services, employee costs, bad debt expense and depreciation.

We also experienced favorability in our effective income tax rate in Q1 2019 compared to the prior year. Our effective tax rate this year is expected to be approximately 14% compared to approximately 18% last year when excluding the prior year special items. Forecasted federal renewable energy production tax credits and state investment tax credits related to the Busch Ranch II wind farm, that as Linn mentioned, will we placed in service this fall as well as excess deferred tax amortization related to tax reform, drive the reduction in the 2019 effective tax rate.

Under generally accepted accounting principles related to interim tax accounting, we are required to recognize a large portion of our annual forecasted 2019 tax credits and excess deferred federal income tax amortization in Q1, given we anticipate earning nearly half our annual income in the first quarter.

Slide 11 is a new slide we've added to our presentation, combining the operating income results for all our operating segments onto one slide. I'll make a few high-level comments here, and you can find additional details on Q1 year-over-year changes in gross margin and operating expenses in our earnings release.

Operating income grew year-over-year due to strong performance at the Electric and Gas Utilities. At our Electric Utilities, operating income for Q1 2019 improved by $2.5 million compared to Q1 2018, an increase of over 6%. Gross margins increased by $4.8 million, primarily from lower purchase power capacity charges, higher off-system power marketing and favorable weather. Partially offsetting the increase in gross margins were higher operating expenses, which increased $2.3 million over Q1 last year, primarily due to higher outside services and employee costs.

At our Gas Utilities, operating income for Q1 2019 improved $7.9 million compared to Q1 2018, an increase of over 8%. Gross margins increased $16.1 million, primarily from returns on investments for customers and colder weather. Customer growth in our service territories and increased transport and transmission volumes also contributed to the gross margin increase.

Partially offsetting the gross margin increase were higher operating expenses, which increased by $7 million, primarily from higher outside services and higher employee costs. Depreciation increased $1.2 million from higher rate-based plant in service.

On the bottom of Slide 11, you see our Power Generation and Coal Mining segments delivered consistent year-over-year Q1 results. Both businesses continue to operate efficiently and provide excellent returns.

Slide 12 shows our financial position through the lens of capital structure, credit ratings and financial flexibility. Our credit ratings remain at BBB+ at both Fitch and S&P and Baa2 at Moody's, with a stable outlook from all 3 agencies. We remain committed to maintaining our strong investment-grade credit ratings.

At March 31, our net debt to capitalization ratio was 57.7%, a decrease of 120 basis points from year-end. This reduction was driven by the increase in our retained earnings due to our solid first quarter earnings and $20 million of new equity issued under our At-the-Market equity offering program, as well as by strong first quarter cash flows that allowed us to reduce our short-term debt from year-end.

Given we increased our 2019 capital spending forecast by $107 million since our last public CapEx disclosures, we expect debt to total capitalization to increase slightly as 2019 progresses. You'll note in our updated guidance assumptions on Slide 43 and 44 in the appendix that we expect to use the ATM to issue a total of $80 million to $100 million in new equity this year, and $40 million to $80 million next year to help fund the increased CapEx program, which Linn is going to speak to shortly.

While debt to total capitalization will likely remain in the 58% to 59% range into 2020, we continue to target a debt to total cap in the mid-50s over the long term.

Slide 13 illustrates our dividend track record. We've grown the dividend at a faster rate the past few years, demonstrating our confidence in our future earnings growth potential. As we've stated in the past, our intent is to not reduce the amount of the annual dividend increase, and we maintain our stated dividend payout ratio range of 50% to 60% of EPS.

I'll turn it back to Linn now for his strategic overview.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Thank you, Rich. Now moving on to Slide 15. As discussed during previous calls, we grouped our strategic goals into 4 major categories: Profitable Growth, Valued Service, Better Every Day and Great Workplace. Our overall objective is to be best-in-class in everything that we do, and our ready branding and messaging complements this customer-focused strategy.

We will drive future earnings growth through our customer-focused investment program to better serve our customers' needs. Based on our capital forecast, we expect to deliver long-term earnings per share growth above the utility average. In addition, we fully expect incremental growth opportunities from generation and other larger projects. We're also focused on continuing to grow our dividend. We have increased our annual dividend for 49 consecutive years, one of the longest track records in the industry.

Slide 16 helps us illustrate how we think about strategic execution. We are aligning our people, processes, our technology and our analytics around our customers' needs. In addition to our investment for customers to deliver safe and reliable service, we are transforming our customer experience, working hard to know our customers well and make it easier to do business with us. We are driving growth through higher penetration, adding renewable energy and creating innovative tariffs to recruit new businesses.

In particular, we are enabling the growth of data centers in our territories, which fit the unique attributes of our service territory. And we are investing in the safety and reliability of our electric and natural gas infrastructure systems, using a disciplined programmatic integrity program.

Slide 17 illustrates the strategic diversity of our business culture. We have a mix of complementary gas and electric utilities across stable and growing Midwest states. The quarterly operating income chart on the left illustrates the seasonality of our earnings between electric and gas utilities. Our balanced mix reduces total company risk.

Slide 18 illustrates our large electric and natural gas infrastructure systems. These systems span across 8 states and provide more diverse opportunities for investment, more interconnections for reliability and growth, and greater overall efficiency of operations for our customers.

Slide 19. Our systems require significant long-term investment to meet our customers' needs. Forecasted capital investment is focused largely on safety, reliability and supporting our customers' growth. This capital forecast far exceeds forecasted depreciation, which translates to future earnings growth.

This quarter, as I said before, we added $246 million to our 5-year forecasts. We added $107 million in 2019, $58 million for 2020, and the rest is in the outer years. Most of the increase relates to safety and integrity needs. We now plan to invest $777 million in 2019, with that being $2.8 billion over the 5-year period. Both of these are all-time high capital forecast for us.

We've also refined our programmatic capital forecast for 2019. Expect this to be our final forecast update for this year. On a going-forward basis, we expect to update our capital forecast in the fall, and we'll disclose that forecast with third quarter earnings.

As noted on prior calls, our capital forecast includes opportunities we are relatively certain to occur, and we add capital, especially in the outer years, as we gain more clarity and more comfort around specific projects. With the continued buildout of our programmatic infrastructure replacement plans, combined with growth and larger project opportunities, we fully expect our actual out-year capital expenditures to be greater than those in the current forecast for 2020 and beyond.

Please see our appendix slide in this presentation for more detail of our capital investment forecast. You'll note on Slides 30 and Slide 32 that we have adjusted the annual base investment for both Electric and Gas Utilities compared to our prior investor presentation.

Moving on to Slide 20. This slide illustrates the breakdown of our 5-year capital forecasts. Note that over 90% of our forecasted investment is in our utilities, and those utility -- and of those utility investments, over 70% are recovered in a timely and efficient manner.

Slide 21 shows the time line around our multistate jurisdiction simplification efforts. We strongly believe consolidation of the multiple entities within each state will provide us long-lasting benefits for all stakeholders, including our regulators. And this would happen through streamlined and fewer regulatory proceedings and filings. We have 3 states in which we own multiple gas distribution utilities: Those are Colorado, Nebraska and Wyoming, all of which are now officially underway for simplification.

In Colorado, we filed a consolidated rate review, and are working through the regulatory process. We expect a decision by year-end. In Wyoming and Nebraska, we will file consolidated rate reviews following approval of the applications for legal consolidation and the completion of the consolidation in each state. We plan to file a consolidated rate review in Wyoming later in 2019 and during 2020 in Nebraska.

Slide 22 illustrates our focus on operational excellence. Our safety performance continue to be excellent, and our reliability from 2017 through the first quarter of 2019 was simply outstanding. Our safety performance is on track for 2019, and we continue to report much better performance than the utility industry. Also, we received an ENERGY STAR Award from the EPA for our outstanding efforts to improve residential energy efficiency.

Slide 23 illustrates the results of executing our customer-focused strategy and delivering strong, long-term total shareholder returns.

And then Slide 24 shows our 2019 scorecard. To hold ourselves accountable to you, our investors, we publish our major initiative scorecard each year. The scorecard includes a number of key objectives, including executing on our capital program, completing construction of 3 major projects that include the Natural Bridge Pipeline, the Busch Ranch II wind farm and the Rapid City to Stegall transmission line. During this quarter, we checked off filing on the Nebraska legal consolidation.

That concludes my remarks. We're happy to entertain questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Michael Weinstein with Crédit Suisse.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

So my first question has to do with the increase in the safety and integrity spending. This is a bit surprising given the roll forward was pretty recent. Is this being driven by the drive to consolidate and file rate cases at the utilities over the next year or 2 to gas utilities? And can we expect this kind of significant programmatic increase again in a more frequent basis going forward?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Michael, this is Linn. As I said in my comments, we intend to try to do this one time a year, so we're not doing anymore this year. We continue to refine our programmatic capital opportunities. We've got a group of engineers that have been doing that for some time. They continue to understand our system, dissect our system. And most of what we've added this time was due to the fact that we are starting to understand better the project scope and the timing of some of those investments that we've been looking at for a while.

We've also, importantly, been able to confirm the availability of things like materials and contractors. That was an emphasis of this particular quarter as well. And then we got some additional customer growth that we've identified. So that's the bulk of what we've added this particular quarter. Going forward, we think we'll be doing this mostly in the third quarter during that earnings call, unless and until we start to identify maybe larger projects as we go forward.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

Are you still on track, I guess, to announce approximately 1 to 2 major projects a year that are not included in the capital forecast?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

That's what we currently think, Michael. Yes. We've got a number of projects that we have in the pipeline, if you will. And as we gain confidence in those, especially with regulators and the need and the necessity of those, then we start to bring those forward as we gain that confidence.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

As you're nearing the target mid-50s debt ratio, mid-50% debt ratio, you're getting pretty close to that now. How are you viewing M&A as a growth path going forward at this point?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Our approach and perspective on M&A hasn't changed over the last several quarters. We see the premiums being paid is awfully high. Right now we'd probably better off our shareholders put $1 in the ground, $1 in a year and earn on that than we would be to pay $2 and only earn one of those is kind of how we see it. We'll see what happens over time with respect to that. And we think we're pretty good at it, but it's not something that we're focused on, and it's not part of our strategic plan right now.

Operator

And our next question will come from the line of Julien Dumoulin-Smith with Bank of America.

Julien Patrick Dumoulin-Smith - *BofA Merrill Lynch, Research Division - Director and Head of the US Power, Utilities & Alternative Energy Equity Research*

Hey. Nicely done on the capital upgrades here.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Thank you, Julien.

Julien Patrick Dumoulin-Smith - *BofA Merrill Lynch, Research Division - Director and Head of the US Power, Utilities & Alternative Energy Equity Research*

If I can go back a little bit to Michael's question a little bit. Can you comment a little bit more on the timing? It seems perhaps unique amongst peers to accelerate CapEx especially into 2019. I know that the absolute numbers are going up. Was there also a shift in time line on when these dollars and when projects are being spent, too? I know, obviously, things are a little bit fungible, but sort of curious if it's not only an increase but an acceleration of other projects that you've previously contemplated, too?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Good question, Julien. Not so much an acceleration. No. There was some acceleration, I would argue, or at least firmed up some that we were hopeful to spend in '19 and '20 because we were not sure about materials and contractors. So that helped us firm up this year's and next year's capital more than what it was last quarter.

Julien Patrick Dumoulin-Smith - *BofA Merrill Lynch, Research Division - Director and Head of the US Power, Utilities & Alternative Energy Equity Research*

Got it. All right. Excellent. And then can you comment a little bit more on Nebraska specifically, I suppose both in terms of incremental opportunities out there? Then also talk about just the sort of the process. Obviously, you filed this two-part effort. Can you talk about just what we should expect in terms of when the tariffs get collapsed? And how that kind of reconciles the process of the rate case as well as well as capital opportunities and any future opportunities that come out of that as you think about that process, the capital spend process there?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Sure. Well, Nebraska is one of the states that we acquired with the SourceGas transaction. So we continue to learn and evaluate what we acquired with SourceGas. Now it's 3 years later, we have a pretty good handle on it, but we continue to learn and continue to understand, especially as new -- as we anticipate new PHMSA, for example, regulations be passed down, and how we might need to comply with those, and what that investment requirement might be.

With respect to the consolidation, our intervention period, if I recall correctly, ended last Monday. And so that's one check -- or milestone behind us with respect to the consolidation. We don't expect approval until late 2019 with respect to a consolidation in November but that is under -- excuse me, in Nebraska, but that's currently underway.

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

And then just to add to a bit to that. Then once approved and consolidated, we would then file the consolidated rate review, which would play out through 2020. So the impact of that certainly won't come until later next year.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Yes. We expect to be completely wrapped up with both the consolidation and rate review by late next year.

Julien Patrick Dumoulin-Smith - *BofA Merrill Lynch, Research Division - Director and Head of the US Power, Utilities & Alternative Energy Equity Research*

Got it. Excellent. And then just to clarify in brief, you alluded to a new tariff, I believe, in Wyoming around some blockchain opportunities. If you can, is that incremental -- when you think about incremental sales, I mean, obviously, that's shifting customers from one tariff to another. Also probably speaks a little bit as the leading indicator of growth. Is there something that's pivoting here in terms of your expectations in that state, just even in the last few months? Curious on what you could see as a result of this tariff, specifically. And also potentially other capital needs that would come behind it, too, whether voluntary renewables or just low incremental low growth.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Yes, the blockchain load would represent incremental growth to us or new load. It would not be changing from one tariff to another tariff. It would be new loads for us. And Wyoming, in general, as a state has worked very hard to be a home state, if you will, for blockchain. My recollection, they passed about 7 different statutes, pieces of legislation in 2017 that allowed Wyoming to be, in Wyoming's words, on par with countries like Singapore, et cetera, with respect to being advantageous to register your cryptocurrencies and your blockchain mining kind of activities within the state of Wyoming. And so we see this is a great opportunity for us to partner with the state, local economic development with the tariffs that we have put in place.

There was strong interest in blockchain, as you probably all might remember, a couple of years ago that seems to have tempered some with some of the cryptocurrency prices dropping, but we want to make sure we are ready for that. And we are getting phone calls, and we are speaking to future potential customers with respect to blockchain in Wyoming.

Operator

And our next question will come from the line of Chris Turnure with JPMorgan.

Christopher James Turnure - *JP Morgan Chase & Co, Research Division - Analyst*

I wanted to get an update on Colorado legislation. I think today is the last day of the session. There's a bunch of different bills out there. Kind of which ones do you see as the most relevant? And kind of what might those mean for your customer base kind of customer bills versus other utilities in the state?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Thanks for the question. Yes, we're watching those very closely. It's very early, as you just said. We have some house bills that have been passed. Probably the one that we're watching the closest is the CO_2 reduction bill that would stairstep in a CO_2 reduction of up to 90% by the year 2050 relative to the year 2005, and we understand that will be across the entire Colorado economy. So obviously, we're watching that very closely. It's very early. We've had some introductory discussions internal to Black Hills, and so we're, frankly, still analyzing that and look forward to see what's ultimately passed before we start digging into it much, much deeper. But it would probably -- based on what we're seeing so far, certainly, have an impact upon customers, likely requiring us to add more renewable storage and things of that nature in the future. So much more to come. It's very early for us.

Christopher James Turnure - *JP Morgan Chase & Co, Research Division - Analyst*

Okay. Great. And then another kind of relatively high-level question. You have a lot of different utilities in a lot of different states. How are you thinking about kind of earned ROE trends over the next 3 years in your base plan?

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

We don't see a big change in earned ROEs. We feel like we're treated fairly now, I would say, in all of our states. We just came out of a rate case in Arkansas, for example. Finished that last December, and we were pleased. We'd always like better, but we were certainly pleased. So we don't see a reduction in ROEs coming, but we're going to keep an eye on that, of course.

Christopher James Turnure - *JP Morgan Chase & Co, Research Division - Analyst*

Okay. So even as you kind of evolve through this set of rate cases and make a lot of investments, we shouldn't assume that regulatory lag widens or changes or that your actual earned ROE trends lower.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

No. We manage that as best as we possibly can under circumstances, yes.

Operator

And our next question will come from the line of Andrew Weisel with Scotia Howard Weil.

Andrew Marc Weisel - *Scotia Howard Weil, Research Division - Analyst*

Question on financing. So regarding the incremental CapEx. If I compare that to the increase in your equity needs, it looks like you're financing it with about 50% equity this year and about 40% next year. You've been clear about expecting to continuously raise the CapEx. So my question is, should we assume something like a 50% equity ratio on all incremental dollars? Or would there be a point where that might change?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

This is Rich. I would suggest that would change as we move forward this year with the outsized CapEx spend. And then next year's a pretty strong capital year, too, as you can see on our schedules. We did kind of finance pretty close to 50% of the incremental capital we just added with incremental ATM, as you pointed out. But again, as we move beyond 2020, I would expect our FFO to debt -- excuse me, FFO to debt -- debt to total capitalization to continue to improve. And so at that point, our cash flows would be covering the dividend and the CapEx pretty well, and we wouldn't need as much equity, unless we continue to add significantly to the capital schedule. But smaller additions wouldn't require 50% equity financing, I would suggest.

Andrew Marc Weisel - *Scotia Howard Weil, Research Division - Analyst*

Okay. Great. Then just to clarify on the dividend. Rich, if I heard your comment right, you said you don't want to reduce the amount of the increase. Does that mean we should expect 12% -- sorry, $0.12 increases each year? That would obviously decelerate the percentage increase, but maybe that's how you get toward the midpoint of the target for the dividend payout ratio?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

Yes. I'm not going to speak to what our board is going to approve in the future but certainly in the last 2 years, we've done $0.12 increases in November with our third quarter earnings release. A pattern is kind of established there. And I think what you just described is probably reasonably accurate. We don't want to decrease it, the amount of the increase, and we certainly want to continue our track record of 49 years in a row of increasing it. So I would say what you characterized is probably reasonably accurate.

Operator

(Operator Instructions) Our next question will come from the line of Vedula Murti with Avon Capital.

Vedula Murti

I was -- I want to look at the Slide 10 here on the waterfall chart, and I think you gave a discussion about it. But I want to make sure I understand with regards to the tax item on the waterfall chart on Slide 10. It sounded like, from what you said, that various tax credits and other types of things for whatever reason all tend to congregate on an accounting basis in 1Q such that if we roll forward and we look at the waterfall charts through the rest of the year, this item will not be there. But if we think forward next year, then simply there will be -- whatever the difference is between this year and next year would then be reflected principally in 1Q again. Is that correct?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

Yes. This year's a little unusual, Vedula, in that we're adding Busch Ranch II at the end of the year, which on our forecast, we've got that coming in basically late third quarter. So you get 4 months of production tax credits. There is a state investment tax credit onetime that we get this year associated with that as well. And that's the biggest driver of that tax item. Also, the excess deferred income taxes that we set up back when we did tax reform at the end of 2017 are beginning to be amortized now. So that's a contributor there as well. In 2019, that's kind of a new item. We're starting to refund those amounts to customers. So reduced income taxes, but reduced revenue on that particular item. But those are not onetime in nature this year, but they are kind of new this year and, thus, create the outsized tax impact in the first quarter. Going forward, I wouldn't expect this to be as big, barring additional renewable projects added or something like that. But hopefully, that answers your question.

Vedula Murti

How would we -- how would you then maybe allocate between the items that you stated that comprise this line item if -- in terms of the return of the excess deferred income taxes? And that's a thing -- if that's an ongoing item, how much would that be of kind of like this item here versus production tax credits and state tax credits from having a new facility come online?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

Well, you can kind of glean some of this from our earnings release. The excess deferred tax item, just at the gas utilities was $2.4 million in the first quarter of revenue, so that would equate to a smaller amount on the tax side because you have to tax effect that. The production tax credits and the investment tax credit, we've not disclosed those specifically, but they are pretty big chunk of the $6.7 million I'd say, half or a little more.

And so there are a couple of other items in there. Again, when you -- GAAP requires us to look at our expected tax rate for the full year. And then based on how much money you've earned in any given quarter, which in the first quarter, we earned about half what we forecast for the year, not quite, but close, we have to recognize that amount of it in the first quarter. So that's why it kind of stands out here.

Vedula Murti

Then maybe one less thing on this item. How much of this would you suggest is nonrecurring as opposed to recurring going forward?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

Well, certainly, the investment tax credit that we are getting in Colorado, when we put the project in-service, will not recur. But the production tax credits will, and the excess deferred income tax amortization will be a recurring item, too. We set up about $300 million for that at the end of 2017, and that will amortize in over a long period of time.

Vedula Murti

I mean, so is it reasonable to think, like, maybe half of it is reoccurring and half not? Or how should we really think about that?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

It's more than that's recurring.

Vedula Murti

Excuse me?

Richard W. Kinzley - *Black Hills Corporation - Senior VP & CFO*

More than half of the benefits will recur.

Operator

With no further questions, I will return the call back to Linn Evans for closing remarks. Please go ahead, sir.

Linden R. Evans - *Black Hills Corporation - President, CEO & Director*

Thank you very much for joining us for our call today, and thank you for your interest in Black Hills, and have a great rest of your day. Thank you.

Operator

Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Good day.
