

HARDY MYERS
Attorney General



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DEPARTMENT OF JUSTICE
GENERAL COUNSEL DIVISION

July 25, 2006

Administrative Hearings Division
ALJ, Christina Smith
550 Capitol St NE Suite 215
PO Box 2148
Salem, OR 97308-2148

RE: AR 499 draft rules

Dear ALJ Smith,

Consistent with the schedule in this docket, Staff submits the attached draft rules. In addition, Staff is submitting a redline version and a word version of the rules. Staff has also included a list of issues that it plans to address, which may include proposed changes to the draft rule language, in its comments on July 31, 2006.

If you have any questions, please do not hesitate to contact me.

Sincerely,

Jason W. Jones
Assistant Attorney General
Regulated Utility & Business Section

cc: Service List

JWJ:jwj/GENQ8069.DOC

Annual Tax Reports and Automatic Adjustment Clauses Relating to Utility Taxes

(1) This rule applies to regulated investor-owned utilities that provided electric or natural gas service to an average of 50,000 or more customers in Oregon in 2003, or to any successors in interest of those utilities that continue to be regulated investor-owned utilities.

(2) As used in this rule:

(a) "Affiliated group" means the group of corporations of which the utility is a member and that files a consolidated federal income tax return.

(b) "Deferred taxes" for purposes of the utility means the total deferred tax expense of regulated operations as reported in the FERC deferred tax expense accounts that relate to the year being reported in the utility's results of operations report or tax returns.

(c) "FERC" means the Federal Energy Regulatory Commission.

(d) "Income" means taxable income as determined by the applicable taxing authority or regulatory taxable income when reporting or computing the stand-alone tax liability resulting from a utility's regulated operations.

(e) "Investment" means capital outlays for utility property used to provide regulated service to customers.

(f) "Local taxes collected" means the total amount collected from customers under the local tax line-item of customers' bills calculated on a separate city or county basis.

(g) "Pre-tax income" means the utility's net revenues before income taxes and interest expense, as determined by the Commission in a general rate proceeding.

(h) "Properly attributed" means the share of taxes paid that is apportioned to the Oregon regulated operations as calculated in section (3) of this rule.

(i) "Regulated operations of the utility" means those activities of a utility that are subject to rate regulation by the Commission.

(j) "Results of operations report" means the utility's annual results of operations report filed with the Commission.

(k) "Revenue" means retail revenues from ratepayers in Oregon as defined by FERC, excluding other operating revenues as defined by FERC and supplemental schedules not included in the utility's revenue requirement and adjusted for any rate adjustment imposed under this rule.

(l) "Revenue requirement" means the total revenue the Commission authorizes a utility an opportunity to recover in a general rate proceeding or other general rate revision, including an annual automatic adjustment clause under ORS 757.210.

(m) "Tax" means a federal, state or local tax or fee that is imposed on or measured by income and that is paid to a unit of government, but does not include a franchise fee or privilege tax.

(n) "Taxes authorized to be collected in rates" means the following for federal and state income taxes:

(A) The amount calculated by multiplying the following three values:

(i) The revenue the utility collects, using information from the utility's results of operations report;

(ii) The ratio of the net revenues from regulated operations of the utility to gross revenues from regulated operations of the utility, calculated using the pre-tax income and revenue the Commission authorized in establishing rates and revenue requirement; and

(iii) The effective tax rate used by the Commission in establishing rates for the time period covered by the tax report as set forth in the most recent general rate order or other order that establishes an effective tax rate, calculated as the ratio of total income tax expense in revenue requirement to pre-tax income.

(B) For purposes of paragraph (2)(m)(A), when the Commission has authorized a change during the tax year for gross revenues, net revenues or effective tax rate, the amount will be calculated using a weighted average of months in effect.

(o) "Taxes paid" means net amounts received by units of government from the utility or from the affiliated group and properly attributed to regulated operations of the utility, adjusted as follows:

(A) Increased by the amount of tax savings realized as a result of charitable contribution deductions allowed because of the charitable contributions made by the utility;

(B) Increased by the amount of tax credits on the tax return that are associated with investment by the utility in the regulated operations of the utility, which may include, but are not limited to, tax credits associated with renewable electricity production, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the Commission in the utility's most recent general ratemaking proceeding; and

(C) Adjusted by deferred taxes related to the regulated operations of the utility. The utility must initially use its results of operations report to establish the amount of deferred taxes. If the utility does not believe that the results of operations report sufficiently reflects the amount of the utility's deferred taxes for the applicable tax year, the utility may also use its tax returns for the tax year as a supplemental source for calculating the deferred taxes adjustment as a

separate submission. Deferred taxes do not include deferred tax items related to an adjustment under section (9) of this rule.

(p) "Taxpayer" means the utility or the affiliated group that files income tax returns with units of government.

(q) "Units of government" means federal, state and local taxing authorities.

(3) The amount of income taxes paid that is properly attributed to regulated operations of the utility is calculated as follows:

(a) The amount of federal income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures:

(A) The total amount of federal income taxes paid by the taxpayer; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in the denominator.

(b) The amount of state income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures:

(A) The total amount of Oregon income taxes that is paid by the taxpayer; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in Oregon in the denominator.

(c) The amount of local income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures for each local taxing authority in Oregon:

(A) The total amount of income taxes paid by the taxpayer to the local taxing authority;
and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in the local taxing authority in the numerator and amounts for the taxpayer in the local taxing authority in the denominator.

(4) By October 15 of each year, each utility must file a tax report with the Commission. The tax report must contain the following information for each of the three preceding fiscal years:

- (a) The amount of federal and state income taxes paid to units of government by the taxpayer;
- (b) The amount of the federal and state income taxes paid that is incurred as a result of income generated by the Oregon regulated operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility;
- (c) The amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility, as calculated in section (3) of this rule;
- (d) The amount of federal and state taxes income taxes authorized to be collected in rates for the Oregon regulated operations of the utility;
- (e) The amount of the difference between the amount in subsection (4)(d) of this rule and the lowest of the amounts in subsections (4)(a), (4)(b) and (4)(c), after making the adjustments defined in subsection (2)(o) of this rule;
- (f) The amount of local income taxes paid to units of government by the taxpayer, by local taxing authority;
- (g) The amount of local income taxes paid to units of government by the taxpayer that is incurred as a result of income generated by the regulated Oregon operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility, by local taxing authority;
- (h) The amount of local income taxes paid to units of government by the taxpayer that is properly attributed to Oregon regulated operations of the utility, as calculated in section (3) of this rule, by local taxing authority.
- (i) The amount of local income taxes collected from Oregon customers, by local taxing authority;
- (j) The amount of the difference between the amount in subsection (4)(i) of this rule and the lowest of the amounts in subsections (4)(f), (4)(g) and (4)(h) after making the adjustments defined in subsection (2)(o) of this rule, by local taxing authority; and
- (k) The proposed surcharge or surcredit rate adjustments for each customer rate schedule to charge or refund customers the amount of the differences in subsections (4)(e) and (4)(j) of this rule.

(5) In calculating the amount of taxes paid under section (4) of this rule:

(a) "Taxes paid" must be allocated to each tax year employed by the utility for reporting its tax liability in the following manner:

(A) For each tax liability shown on an initial or amended tax return for the

immediately preceding tax year, which return is filed on or before the date the tax report is due for such tax year, to the tax year for which such return is filed.

(B) For each tax liability or tax adjustment shown on an amended tax return or made as a result of a tax audit, that is filed, paid or received after the date the tax report is due for the applicable tax year, to the tax year in which the related tax liability or tax adjustment is recognized by the utility for accounting purposes.

(C) Taxes paid must include any interest paid to or interest received from units of government with respect to tax liabilities.

(b) When a utility's fiscal year or parent changes, and a partial year consolidated federal income tax return is filed during the year, taxes paid must be calculated in the manner defined by ORS 314.355 and OAR 150-314.355. For purposes of this rule, the taxes paid amount will reflect a weighted average of the months in effect related to each filing.

(6) The utility must explain the method used for calculating the amounts in this rule and provide copies of all workpapers and documents supporting the calculations. Each utility must obtain and provide any information requested by the Commission to implement and administer this rule.

(7) The Commission will establish an ongoing docket for each of the October 15th tax report filings. If a petitioner is granted intervention and becomes a party to the docket, they may have access to all such tax report filings at the time the tax report filings are filed with the Commission, subject to the terms of any protective order issued.

(a) Within 20 days following the October 15 tax report filings, an Administrative Law Judge will conduct a conference and adopt a schedule.

(b) Within 180 days of the tax report filings, the Commission will issue an order making the findings in section 8 of this rule.

(8) The Commission's order in subsection 7(b) of this rule will contain the following findings:

(a) Whether the taxes authorized to be collected in rates for any of the three preceding fiscal years differs by \$100,000 or more from the amount of taxes paid to units of government that are properly attributed to the Oregon regulated operations of the utility;

(b) For the preceding fiscal year, the difference between the amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of taxes authorized to be collected in rates;

(c) For the preceding fiscal year, the difference between the amount of local income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of local taxes collected in rates; and

(d) Any other finding or determination necessary to implement the automatic adjustment clause.

(9) Upon entry of an order finding a difference of \$100,000 or more in section (8) of this rule, the utility must file an amendment to its automatic adjustment clause tariff to be effective each June 1, unless otherwise authorized by the Commission. The amended tariff must implement a rate adjustment applying to taxes paid to units of government and collected from ratepayers for each fiscal year beginning on or after January 1, 2006.

(a) The utility must establish a balancing account and automatic adjustment clause tariff to recover or refund the difference determined by the Commission in subsection (8)(b) of this rule through a surcharge or surcredit rate adjustment.

(b) A utility that is assessed a local income tax must establish a separate balancing account and automatic adjustment clause tariff for each local taxing authority assessing such tax. The utility must apply a surcharge or surcredit on the bills of customers within the local taxing authority assessing the tax. The amount of the surcharge or surcredit must be calculated to recover or refund the difference determined by the Commission in subsection (8)(c) of this rule.

(c) Any rate adjustment must be calculated to amortize the difference determined by the Commission in subsections (8)(b) and (8)(c) of this rule over a period authorized by the Commission.

(d) Any rate adjustment must be allocated by customer rate schedule according to equal percentage of margin for natural gas utilities and equal cents per kilowatt-hour for electric utilities, unless otherwise authorized by the Commission.

(e) Each balancing account must accrue interest at the Commission-authorized rate for deferred accounts. For purposes of calculating interest, the amount of the difference calculated in this section of the rule will be deemed to be added to the balancing account on January 1 of the year following the tax year.

(f) The automatic adjustment clause must not operate in a manner that allocates to customers any portion of the benefits of deferred taxes resulting from accelerated depreciation or other tax treatment of utility investment or regulated affiliate investment required to ensure compliance with the normalization method of accounting or any other requirements of federal tax law.

(g) By October 15, 2006, each utility must seek a Private Letter Ruling from the Internal Revenue Service on whether the utility's compliance with Senate Bill 408, this rule, or any other relevant guidance or authorities would cause the utility to fail to comply with federal normalization requirements or other requirements of federal tax law. While a utility's request for a Private Letter Ruling is pending, or a related Revenue Ruling is pending, no rate adjustment will be implemented, but interest will accrue according to subsection (9)(e) of this rule on the amount of any rate adjustment determined by the Commission pursuant to subsections (8)(b) and (8)(c) of this rule.

(10) No later than 30 days following the Commission's findings in section (8) of this rule, any person may file to terminate the automatic adjustment clause on the basis that it would result in a material adverse effect on customers. In the event of a filing under this section, the applicable rate adjustment will not be implemented until the Commission makes its determination. If the Commission decides against termination, interest will accrue according to subsection (9)(e) of this rule on the final amount of the rate adjustment. The person filing the claim will bear the burden of proof to substantiate the claim.

(11) At any time, a utility may file a claim that a rate adjustment under the automatic adjustment clause violates ORS 756.040 or other applicable law. In making a determination regarding a potential violation of ORS 756.040, the Commission will perform an earnings review using the utility's results of operations report for the applicable tax year. The utility filing the claim will bear the burden of proof to substantiate the claim.

(12) The Commission may disclose, or any intervenor in a utility tax report proceeding may obtain and disclose, the amount by which the amount of taxes that units of government received from the utility or from the affiliated group differs from the amount of costs for taxes collected, directly or indirectly, as part of rates paid by customers, including whether the difference is positive or negative. The Commission will not disclose or authorize disclosure of any information that is exempt from disclosure under the Public Records Law (ORS 192.410-192.505).

Stat. Auth.: ORS Ch. 183, 756, 757 & 759

Stats. Implemented: ORS 756.040, 756.060, 757.267 & 757.268

[Hist.: PUC 5-2005(Temp), f. & cert. ef. 9-15-05 thru 3-13-06]

AR 499 permanent rule final draft.doc

Annual Tax Reports and Automatic Adjustment Clauses Relating to Utility Taxes

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(2) As used in this rule:

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(b) "Deferred taxes" for purposes of the utility means the total deferred tax expense of regulated operations as reported in the FERC deferred tax expense accounts that relate to the year being reported in the utility's results of operations report or tax returns.

(c) "FERC" means the Federal Energy Regulatory Commission.

(~~d~~e) "Income" means taxable income as determined by the applicable taxing authority or regulatory taxable income when reporting or computing the stand-alone tax liability resulting from a utility's regulated operations.

(~~e~~d) "Investment" means capital outlays for utility property used to provide regulated service to customers.

(~~f~~e) "~~Local taxes collected in rates~~" means the total amount collected from customers under the local tax line-item of customers' bills calculated on a separate city or county basis.

(~~g~~f) "Pre-tax income" means the utility's net revenues before income taxes and interest expense, as determined by the Commission in a general rate proceeding.

(~~h~~g) "Properly attributed" means the share of taxes paid that is apportioned to the Oregon regulated operations as calculated in section (3) of this rule.

(~~i~~h) "Regulated operations of the utility" means those activities of a utility that are subject to rate regulation by the Commission.

(~~j~~i) "Results of operations report" means the utility's annual results of operations report filed with the Commission.

(~~k~~j) "Revenue" means retail revenues from ratepayers in Oregon as defined by FERC, excluding other operating revenues as defined by FERC and supplemental schedules not included in the utility's revenue requirement and adjusted for any rate adjustment imposed under this rule.

(~~lk~~) "Revenue requirement" means the total revenue the Commission authorizes a utility an opportunity to recover in a general rate proceeding or other general rate revision, including an annual automatic adjustment clause under ORS 757.210.

(~~ml~~) "Tax" means a federal, state or local tax or fee that is imposed on or measured by income and that is paid to a unit of government, but does not include a franchise fee or privilege tax.

(~~nm~~) "Taxes authorized to be collected in rates" means the following for federal and state income taxes:

(A) The amount is ~~calculated as the product determined by~~ multiplying the following three values:

(i) The revenue the utility collects, using information from the utility's results of operations report;

(ii) The ratio of the net revenues from regulated operations of the utility to gross revenues from regulated operations of the utility, calculated using the pre-tax income and revenue the Commission authorized in establishing rates and revenue requirement; and

(iii) The effective tax rate used by the Commission in establishing rates for the time period covered by the tax report as set forth in the most recent general rate order or other order that establishes an effective tax rate, calculated as the ratio of total income tax expense in revenue requirement to pre-tax income.

(B) For purposes of ~~section-paragraph~~ (2)(m)(A), when the Commission has authorized a change during the tax year for gross revenues, net revenues or effective tax rate, the amount will be calculated using a weighted average of months in effect.

(~~on~~) "Taxes paid" means net amounts received by units of government from the utility or from the affiliated group and properly attributed to regulated operations of the utility, adjusted as follows:

(A) Increased by the amount of tax savings realized as a result of charitable contribution deductions allowed because of the charitable contributions made by the utility;

(B) Increased by the amount of tax credits on the tax return that are associated with investment by the utility in the regulated operations of the utility, which may include, but are not limited to, tax credits associated with renewable electricity production, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the Commission in the utility's most recent general ratemaking proceeding; and

(C) Adjusted by deferred taxes related to the regulated operations of the utility. The utility must initially use its results of operations report to establish the amount of deferred taxes. If the utility does not believe that the results of operations report sufficiently reflects the amount

of the utility's deferred taxes for the applicable tax year, the utility may also use its tax returns for the tax year as a supplemental source for calculating the deferred taxes adjustment as a separate submission. Deferred taxes do not include deferred tax items related to an adjustment under section (9) of this rule.

(pe) "Taxpayer" means the utility or the affiliated group ~~that, whichever~~ files income tax returns with units of government.

(qp) "Units of government" means federal, state and local taxing authorities.

(3) The amount of income taxes paid that is properly attributed to regulated operations of the utility ~~will be~~ is calculated as follows:

(a) The amount of federal income taxes paid to units of government that is properly attributed to the regulated operations of a utility ~~will be~~ is the product of the following two figures:

(A) The total amount of federal income taxes paid by the taxpayer; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in the denominator.

(b) The amount of state income taxes paid to units of government that is properly attributed to the regulated operations of a utility ~~will be~~ is the product of the following two figures:

(A) The total amount of Oregon income taxes that is paid by the taxpayer; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in Oregon in the denominator.

(c) The amount of local income taxes paid to units of government that is properly attributed to the regulated operations of a utility ~~will be~~ is the product of the following two figures for each local taxing authority in Oregon:

(A) The total amount of income taxes paid by the taxpayer to the local taxing authority; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in the local taxing authority in the numerator and amounts for the taxpayer in the local taxing authority in the denominator.

(4) By October 15 of each year, each utility ~~will~~must file a tax report with the Commission. The tax report ~~will~~must contain the following information for each of the three preceding fiscal years:

(a) The amount of federal and state income taxes paid to units of government by the taxpayer;

(b) The amount of the federal and state income taxes paid that is incurred as a result of income generated by the Oregon regulated operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility;

(c) The amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility, as calculated in section (3) of this rule;

(d) The amount of federal and state taxes income taxes authorized to be collected in rates for the Oregon regulated operations of the utility;

(e) The amount of the difference between the amount in subsection (4)(d) of this rule and the lowest of the amounts in subsections (4)(a), (4)(b) and (4)(c), after making the adjustments defined in subsection (2)(on) of this rule;

(f) The amount of local income taxes paid to units of government by the taxpayer, by local taxing authority;

(g) The amount of local income taxes paid to units of government by the taxpayer that is incurred as a result of income generated by the regulated Oregon operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility, by local taxing authority;

(h) The amount of local income taxes paid to units of government by the taxpayer that is properly attributed to Oregon regulated operations of the utility, as calculated in section (3) of this rule, by local taxing authority.

(i) The amount of local income taxes collected from Oregon customers, by local taxing authority;

(j) The amount of the difference between the amount in subsections (4)(i) of this rule and the lowest of the amounts in subsections (4)(f), (4)(g) and (4)(h) after making the adjustments defined in subsection (2)(on) of this rule, by local taxing authority; and

(k) ~~The~~ the proposed surcharge or surcredit rate adjustments for each customer rate schedule to charge or refund customers the amount of the differences in subsections (4)(e) and (4)(j) of this rule.

(5) In calculating the amount of taxes paid under section (4) of this rule:

(a) "Taxes paid" ~~shall~~must be allocated to each tax year employed by the utility for

reporting its tax liability in the following manner:

(A) For each tax liability shown on an initial or amended tax return for the immediately preceding tax year, which return is filed on or before the date the tax report is due for such tax year, to the tax year for which such return is filed.

(B) For each tax liability or tax adjustment shown on an amended tax return or made as a result of a tax audit, that is filed, paid or received after the date the tax report is due for the applicable tax year, to the tax year in which the related tax liability or tax adjustment is recognized by the utility for accounting purposes.

(C) Taxes paid ~~shall must include~~ be inclusive of any interest paid to or interest received from units of government with respect to tax liabilities.

(b) When a utility's fiscal year or parent changes, and a partial year consolidated federal income tax return is filed during the year, taxes paid ~~will must~~ be calculated in the manner defined by ORS 314.355 and OAR 150-314.355. For purposes of this rule, the taxes paid amount will reflect a weighted average of the months in effect related to each filing.

(6) The utility must explain the method used for calculating the amounts in this rule and provide copies of all workpapers and documents supporting the calculations. Each utility must obtain and provide any information requested by the Commission to implement and administer this rule.

(7) The Commission will establish an ongoing-rolling docket for each of the October 15th tax report filings. If a party-petitioner is granted intervention and becomes a party to the docket, they ~~will~~ may have access to all such tax report filings at the time ~~they~~ the tax report filings are filed with the Commission, subject to the terms of any protective order issued ~~that may be in~~ place.

(a) Within 20 days following the October 15 tax report filings, an Administrative Law Judge will conduct a conference and adopt a schedule.

(b) Within 180 days of the tax report filings, the Commission will issue an order making the findings in section 8 of this rule.

(8) The Commission's order in subsection 7(b) of this rule will contain the following findings:

(a) Whether the taxes authorized to be collected in rates for any of the three preceding fiscal years differs by \$100,000 or more from the amount of taxes paid to units of government that are properly attributed to the Oregon regulated operations of the utility;

(b) For the preceding fiscal year, the difference between the amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of taxes authorized to be collected in rates;

(c) For the preceding fiscal year, the difference between the amount of local income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of local taxes collected in rates; and

(d) Any other finding or determination necessary to implement the automatic adjustment clause.

(9) Upon entry of an order finding a difference of \$100,000 or more in section (8) of this rule, the utility must file an amendment to its automatic adjustment clause tariff to be effective each June 1, unless otherwise authorized by the Commission. The amended tariff ~~will~~must implement a rate adjustment applying to taxes paid to units of government and collected from ratepayers for each fiscal year beginning on or after January 1, 2006.

(a) The utility ~~will~~must establish a balancing account and automatic adjustment clause tariff to recover or refund the difference determined by the Commission in subsection (8)(b) of this rule through a surcharge or surcredit rate adjustment.

(b) A utility that is assessed a local income tax ~~shall~~must establish a separate balancing account and automatic adjustment clause tariff for each local taxing authority assessing such tax. The utility ~~will~~must apply a surcharge or surcredit on the bills of customers within the local taxing authority assessing the tax. The amount of the surcharge or surcredit ~~will~~must be calculated to recover or refund the difference determined by the Commission in subsection (8)(c) of this rule.

(c) Any rate adjustment ~~will~~must be calculated to amortize the difference determined by the Commission in subsections (8)(b) and (8)(c) of this rule over a period authorized by the Commission.

(d) Any rate adjustment ~~will~~must be allocated by customer rate schedule according to equal percentage of margin for natural gas utilities and equal cents per kilowatt-hour for electric utilities, unless otherwise authorized by the Commission.

(e) Each balancing account ~~will~~must accrue interest at the Commission-authorized rate for deferred accounts. For purposes of calculating interest, the amount of the difference calculated in this section of the rule will be deemed to be added to the balancing account on January 1 of the year following the tax year.

(f) The automatic adjustment clause ~~shall~~must not operate in a manner that allocates to customers any portion of the benefits of deferred taxes resulting from accelerated depreciation or other tax treatment of utility investment or regulated affiliate investment required to ensure compliance with the normalization method of accounting or any other requirements of federal tax law.

(g) By October 15, 2006, each utility ~~will~~must seek a Private Letter Ruling from the Internal Revenue Service on whether the utility's compliance with Senate Bill 408, this rule, or any other relevant guidance or authorities would cause the utility to fail to comply with federal normalization requirements or other requirements of federal tax law. While a utility's request for

a Private Letter Ruling is pending, or a related Revenue Ruling is pending, no rate adjustment will be implemented, but interest will accrue according to subsection (9)(e) of this rule on the amount of any rate adjustment determined by the Commission pursuant to subsections (8)(b) and (8)(c) of this rule.

(10) No later than 30 days following the Commission's findings in section (8) of this rule, any person may file to terminate the automatic adjustment clause on the basis that it would result in a material adverse effect on customers. In the event of a filing under this section, the applicable rate adjustment will not be implemented until the Commission makes its determination. If the Commission decides against termination, interest will accrue according to subsection (9)(e) of this rule on the final amount of the rate adjustment. The person filing the claim will bear the burden of proof to substantiate the claim.

(11) At any time, a utility may file a claim that a rate adjustment under the automatic adjustment clause violates ORS 756.040 or other applicable law. In making a determination regarding a potential violation of ORS 756.040, the Commission will perform an earnings review using the utility's results of operations report for the applicable tax year. The utility filing the claim will bear the burden of proof to substantiate the claim.

(12) The Commission may disclose, or any intervenor in a utility tax report proceeding may obtain and disclose, the amount by which the amount of taxes that units of government received from the utility or from the affiliated group differs from the amount of costs for taxes collected, directly or indirectly, as part of rates paid by customers, including whether the difference is positive or negative. The Commission will not disclose or authorize disclosure of any information that is exempt from disclosure under the Public Records Law (ORS 192.410-192.505).

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[Hist.: PUC 5-2005(Temp), f. & cert. ef. 9-15-05 thru 3-13-06]

AR 499 permanent rule ~~706~~-final draft.doc

In its comments on July 31, staff plans to address, and may file proposed changes to rule language, on several issues, including:

1. Whether the calculation of properly attributed federal and state income taxes should be based on factors (e.g., property and payroll) solely in Oregon or in all jurisdictions in which the utility has regulated operations.
2. Whether the calculation of properly attributed state income taxes should be based on all companies within the affiliated group in the state or only those companies in the utility's unitary group.
3. How the calculation of properly attributed local income taxes should be performed.
4. How the calculation of the "with and without" 12(a) cap should be performed.
5. How deferred taxes for non-Oregon regulated operations within the affiliated group should be treated, in order to ensure compliance with normalization requirements of federal tax law.

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(a) "Affiliated group" means the group of corporations of which the utility is a member and that files a consolidated federal income tax return.

(b) "Deferred taxes" for purposes of the utility means the total deferred tax expense of regulated operations as reported in the FERC deferred tax expense accounts that relate to the year being reported in the utility's results of operations report or tax returns.

(c) "FERC" means the Federal Energy Regulatory Commission.

(d) "Income" means taxable income as determined by the applicable taxing authority or regulatory taxable income when reporting or computing the stand-alone tax liability resulting from a utility's regulated operations.

(e) "Investment" means capital outlays for utility property used to provide regulated service to customers.

(f) "Local taxes collected" means the total amount collected from customers under the local tax line-item of customers' bills calculated on a separate city or county basis.

(g) "Pre-tax income" means the utility's net revenues before income taxes and interest expense, as determined by the Commission in a general rate proceeding.

(h) "Properly attributed" means the share of taxes paid that is apportioned to the Oregon regulated operations as calculated in section (3) of this rule.

(i) "Regulated operations of the utility" means those activities of a utility that are subject to rate regulation by the Commission.

(j) "Results of operations report" means the utility's annual results of operations report filed with the Commission.

(k) "Revenue" means retail revenues from ratepayers in Oregon as defined by FERC, excluding other operating revenues as defined by FERC and supplemental schedules not included in the utility's revenue requirement and adjusted for any rate adjustment imposed under this rule.

(l) "Revenue requirement" means the total revenue the Commission authorizes a utility an opportunity to recover in a general rate proceeding or other general rate revision, including an annual automatic adjustment clause under ORS 757.210.

(m) "Tax" means a federal, state or local tax or fee that is imposed on or measured by income and that is paid to a unit of government, but does not include a franchise fee or privilege tax.

(n) "Taxes authorized to be collected in rates" means the following for federal and state income taxes:

(A) The amount calculated by multiplying the following three values:

(i) The revenue the utility collects, using information from the utility's results of operations report;

(ii) The ratio of the net revenues from regulated operations of the utility to gross revenues from regulated operations of the utility, calculated using the pre-tax income and revenue the Commission authorized in establishing rates and revenue requirement; and

(iii) The effective tax rate used by the Commission in establishing rates for the time period covered by the tax report as set forth in the most recent general rate order or other order that establishes an effective tax rate, calculated as the ratio of total income tax expense in revenue requirement to pre-tax income.

(B) For purposes of paragraph (2)(m)(A), when the Commission has authorized a change during the tax year for gross revenues, net revenues or effective tax rate, the amount will be calculated using a weighted average of months in effect.

(o) "Taxes paid" means net amounts received by units of government from the utility or from the affiliated group and properly attributed to regulated operations of the utility, adjusted as follows:

(A) Increased by the amount of tax savings realized as a result of charitable contribution deductions allowed because of the charitable contributions made by the utility;

(B) Increased by the amount of tax credits on the tax return that are associated with investment by the utility in the regulated operations of the utility, which may include, but are not limited to, tax credits associated with renewable electricity production, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the Commission in the utility's most recent general ratemaking proceeding; and

(C) Adjusted by deferred taxes related to the regulated operations of the utility. The utility must initially use its results of operations report to establish the amount of deferred taxes. If the utility does not believe that the results of operations report sufficiently reflects the amount of the utility's deferred taxes for the applicable tax year, the utility may also use its tax returns for the tax year as a supplemental source for calculating the deferred taxes adjustment as a

separate submission. Deferred taxes do not include deferred tax items related to an adjustment under section (9) of this rule.

(p) "Taxpayer" means the utility or the affiliated group that files income tax returns with units of government.

(q) "Units of government" means federal, state and local taxing authorities.

(3) The amount of income taxes paid that is properly attributed to regulated operations of the utility is calculated as follows:

(a) The amount of federal income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures:

(A) The total amount of federal income taxes paid by the taxpayer; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in the denominator.

(b) The amount of state income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures:

(A) The total amount of Oregon income taxes that is paid by the taxpayer; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in Oregon in the denominator.

(c) The amount of local income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures for each local taxing authority in Oregon:

(A) The total amount of income taxes paid by the taxpayer to the local taxing authority; and

(B) The average of the ratios calculated for the utility's property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in the local taxing authority in the numerator and amounts for the taxpayer in the local taxing authority in the denominator.

(4) By October 15 of each year, each utility must file a tax report with the Commission. The tax report must contain the following information for each of the three preceding fiscal years:

- (a) The amount of federal and state income taxes paid to units of government by the taxpayer;
- (b) The amount of the federal and state income taxes paid that is incurred as a result of income generated by the Oregon regulated operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility;
- (c) The amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility, as calculated in section (3) of this rule;
- (d) The amount of federal and state taxes income taxes authorized to be collected in rates for the Oregon regulated operations of the utility;
- (e) The amount of the difference between the amount in subsection (4)(d) of this rule and the lowest of the amounts in subsections (4)(a), (4)(b) and (4)(c), after making the adjustments defined in subsection (2)(o) of this rule;
- (f) The amount of local income taxes paid to units of government by the taxpayer, by local taxing authority;
- (g) The amount of local income taxes paid to units of government by the taxpayer that is incurred as a result of income generated by the regulated Oregon operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility, by local taxing authority;
- (h) The amount of local income taxes paid to units of government by the taxpayer that is properly attributed to Oregon regulated operations of the utility, as calculated in section (3) of this rule, by local taxing authority.
- (i) The amount of local income taxes collected from Oregon customers, by local taxing authority;
- (j) The amount of the difference between the amount in subsection (4)(i) of this rule and the lowest of the amounts in subsections (4)(f), (4)(g) and (4)(h) after making the adjustments defined in subsection (2)(o) of this rule, by local taxing authority; and
- (k) The proposed surcharge or surcredit rate adjustments for each customer rate schedule to charge or refund customers the amount of the differences in subsections (4)(e) and (4)(j) of this rule.

(5) In calculating the amount of taxes paid under section (4) of this rule:

(a) "Taxes paid" must be allocated to each tax year employed by the utility for reporting its tax liability in the following manner:

(A) For each tax liability shown on an initial or amended tax return for the

immediately preceding tax year, which return is filed on or before the date the tax report is due for such tax year, to the tax year for which such return is filed.

(B) For each tax liability or tax adjustment shown on an amended tax return or made as a result of a tax audit, that is filed, paid or received after the date the tax report is due for the applicable tax year, to the tax year in which the related tax liability or tax adjustment is recognized by the utility for accounting purposes.

(C) Taxes paid must include any interest paid to or interest received from units of government with respect to tax liabilities.

(b) When a utility's fiscal year or parent changes, and a partial year consolidated federal income tax return is filed during the year, taxes paid must be calculated in the manner defined by ORS 314.355 and OAR 150-314.355. For purposes of this rule, the taxes paid amount will reflect a weighted average of the months in effect related to each filing.

(6) The utility must explain the method used for calculating the amounts in this rule and provide copies of all workpapers and documents supporting the calculations. Each utility must obtain and provide any information requested by the Commission to implement and administer this rule.

(7) The Commission will establish an ongoing docket for each of the October 15th tax report filings. If a petitioner is granted intervention and becomes a party to the docket, they may have access to all such tax report filings at the time the tax report filings are filed with the Commission, subject to the terms of any protective order issued.

(a) Within 20 days following the October 15 tax report filings, an Administrative Law Judge will conduct a conference and adopt a schedule.

(b) Within 180 days of the tax report filings, the Commission will issue an order making the findings in section 8 of this rule.

(8) The Commission's order in subsection 7(b) of this rule will contain the following findings:

(a) Whether the taxes authorized to be collected in rates for any of the three preceding fiscal years differs by \$100,000 or more from the amount of taxes paid to units of government that are properly attributed to the Oregon regulated operations of the utility;

(b) For the preceding fiscal year, the difference between the amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of taxes authorized to be collected in rates;

(c) For the preceding fiscal year, the difference between the amount of local income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of local taxes collected in rates; and

(d) Any other finding or determination necessary to implement the automatic adjustment clause.

(9) Upon entry of an order finding a difference of \$100,000 or more in section (8) of this rule, the utility must file an amendment to its automatic adjustment clause tariff to be effective each June 1, unless otherwise authorized by the Commission. The amended tariff must implement a rate adjustment applying to taxes paid to units of government and collected from ratepayers for each fiscal year beginning on or after January 1, 2006.

(a) The utility must establish a balancing account and automatic adjustment clause tariff to recover or refund the difference determined by the Commission in subsection (8)(b) of this rule through a surcharge or surcredit rate adjustment.

(b) A utility that is assessed a local income tax must establish a separate balancing account and automatic adjustment clause tariff for each local taxing authority assessing such tax. The utility must apply a surcharge or surcredit on the bills of customers within the local taxing authority assessing the tax. The amount of the surcharge or surcredit must be calculated to recover or refund the difference determined by the Commission in subsection (8)(c) of this rule.

(c) Any rate adjustment must be calculated to amortize the difference determined by the Commission in subsections (8)(b) and (8)(c) of this rule over a period authorized by the Commission.

(d) Any rate adjustment must be allocated by customer rate schedule according to equal percentage of margin for natural gas utilities and equal cents per kilowatt-hour for electric utilities, unless otherwise authorized by the Commission.

(e) Each balancing account must accrue interest at the Commission-authorized rate for deferred accounts. For purposes of calculating interest, the amount of the difference calculated in this section of the rule will be deemed to be added to the balancing account on January 1 of the year following the tax year.

(f) The automatic adjustment clause must not operate in a manner that allocates to customers any portion of the benefits of deferred taxes resulting from accelerated depreciation or other tax treatment of utility investment or regulated affiliate investment required to ensure compliance with the normalization method of accounting or any other requirements of federal tax law.

(g) By October 15, 2006, each utility must seek a Private Letter Ruling from the Internal Revenue Service on whether the utility's compliance with Senate Bill 408, this rule, or any other relevant guidance or authorities would cause the utility to fail to comply with federal normalization requirements or other requirements of federal tax law. While a utility's request for a Private Letter Ruling is pending, or a related Revenue Ruling is pending, no rate adjustment will be implemented, but interest will accrue according to subsection (9)(e) of this rule on the amount of any rate adjustment determined by the Commission pursuant to subsections (8)(b) and (8)(c) of this rule.

(10) No later than 30 days following the Commission's findings in section (8) of this rule, any person may file to terminate the automatic adjustment clause on the basis that it would result in a material adverse effect on customers. In the event of a filing under this section, the applicable rate adjustment will not be implemented until the Commission makes its determination. If the Commission decides against termination, interest will accrue according to subsection (9)(e) of this rule on the final amount of the rate adjustment. The person filing the claim will bear the burden of proof to substantiate the claim.

(11) At any time, a utility may file a claim that a rate adjustment under the automatic adjustment clause violates ORS 756.040 or other applicable law. In making a determination regarding a potential violation of ORS 756.040, the Commission will perform an earnings review using the utility's results of operations report for the applicable tax year. The utility filing the claim will bear the burden of proof to substantiate the claim.

(12) The Commission may disclose, or any intervenor in a utility tax report proceeding may obtain and disclose, the amount by which the amount of taxes that units of government received from the utility or from the affiliated group differs from the amount of costs for taxes collected, directly or indirectly, as part of rates paid by customers, including whether the difference is positive or negative. The Commission will not disclose or authorize disclosure of any information that is exempt from disclosure under the Public Records Law (ORS 192.410-192.505).

Stat. Auth.: ORS Ch. 183, 756, 757 & 759

Stats. Implemented: ORS 756.040, 756.060, 757.267 & 757.268

[Hist.: PUC 5-2005(Temp), f. & cert. ef. 9-15-05 thru 3-13-06]

AR 499 permanent rule final draft.doc

1 **CERTIFICATE OF SERVICE**

2 I certify that on July 25, 2006, I served the foregoing upon the parties in this proceeding
3 hereto by electronic mail and sending a true, exact and full copy by regular mail, postage prepaid
4 or by shuttle mail/hand deliver to the parties accepting paper service.

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