## Federal, State, and Local Apportionment Method Calculations
### Joint Approach

FEDERAL APPORTIONMNET METHOD CALCULATION

| | | Adjusted Federal Consolidated Tax |
|---|---|---|
| Step 1 | ***Federal Consolidated Tax Before Credits*** | 3,505 |
| | Less: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations | (4) |
| | Addback: Deferred Tax on Non-Oregon Regulated Entities | 1,500 |
| | Addback: Deferred Tax on PacifiCorp Non-Oregon Regulated Operations | 1,000 |
| | Addback: Imputed Tax Benefit of Charitable Contributions not Attributable to PacifiCorp Oregon Regulated Operations | 1 |
| | Addback: Imputed Tax Benefit of Depreciation on Disallowed Capital Costs | 3 |
| | ***Adjusted Federal Consolidated Tax Before Credits*** | **6,005** |

| | | PacifiCorp Oregon Regulated Operations | Consolidated Federal Taxpayer | Factor Gross | Factor Weighting | Factor Net |
|---|---|---|---|---|---|---|
| Step 2 | Total Gross Owned and Rented Property | 4,500 | 300,000 | 1.50% | X 0.3333 | 0.50% |
| | Total Wages and Salaries | 200 | 8,000 | 2.50% | X 0.3333 | 0.83% |
| | Total Sales and Other Receipts | 1,000 | 80,000 | 1.25% | X 0.3333 | 0.42% |
| | ***Apportionment Percentage - PacifiCorp Oregon Regulated Operations*** | | | | | **1.75%** |
| | Properly Attributed Current Federal Tax - Total PacifiCorp Regulated Operations | | | | | 6,005 |
| | ***Properly Attributed Federal Tax - PacifiCorp Oregon Regulated Operations*** | | | | | **105** |
| | Addback: Federal Deferred Tax for PacifiCorp Oregon Regulated Operations Only | | | | | 100 |
| | Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | | | | | 1 |
| | Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | | | | | 4 |
| | ***Properly Attributed Federal Tax*** | | | | | **210** |

STATE APPORTIONMENT METHOD CALCULATION

| | | Adjusted Oregon Unitary Tax |
|---|---|---|
| Step 1 | State Effective Tax Rate Used in Setting Rates | 4.84% |
| | Oregon Statutory Tax Rate | 6.60% |
| | ***Adjusted Oregon Statutory Tax Rate*** | **73.33%** |
| | Oregon Unitary Tax Before Credits | 125 |
| | ***Adjusted Oregon Unitary Tax Before Credits*** | **92** |
| | Less: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations | (5) |
| | Addback: Deferred Tax on Non-Oregon Regulated Entities | 1 |
| | Addback: Imputed Tax Benefit of Charitable Contributions not Attributable to PacifiCorp Oregon Regulated Operations | 1 |
| | Addback: Imputed Tax Benefit of Depreciation on Disallowed Capital Costs | 1 |
| | ***Adjusted Oregon Unitary Tax*** | **90** |

| | | PacifiCorp Oregon Regulated Operations | Unitary Taxpayer Oregon Only | Factor Gross | Factor Weighting | Factor Net |
|---|---|---|---|---|---|---|
| Step 2 | Total Gross Owned and Rented Property | 4,500 | 5,000 | 90.00% | X 0.3333 | 30.00% |
| | Total Wages and Salaries | 200 | 250 | 80.00% | X 0.3333 | 26.66% |
| | Total Sales and Other Receipts | 1,000 | 1,250 | 80.00% | X 0.3333 | 26.66% |
| | ***Oregon Apportionment Percentage*** | | | | | **83.32%** |
| | Properly Attributed Current State Tax - Total PacifiCorp Regulated Operations | | | | | 90 |
| | ***Properly Attributed Current State Tax*** | | | | | **75** |
| | Addback: Oregon Deferred Tax for PacifiCorp Oregon Regulated Operations Only | | | | | 25 |
| | Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | | | | | 1 |
| | Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | | | | | 5 |
| | ***Properly Attributed State Tax*** | | | | | **106** |

PacifiCorp

## LOCAL CALCULATION

| | Properly Attributed Local Tax |
|---|---|
| Multnomah County Gross Income - PacifiCorp Regulated Operations | 110 |
| Total Multnomah County Business Gross Income | 125 |
| ***Multnomah County Apportionment Percentage*** | 88.00% |
| Total Multnomah County Business Income Tax | 20 |
| ***Properly Attributed Local Tax*** | 18 |

## FEDERAL TAX CAP

**Step 1**

| | Properly Attributed Federal Tax Cap |
|---|---|
| PacifiCorp Total Regulated Operations Federal Standalone Tax Liability | 160 |
| Less: Imputed Negative Tax Liability from the Sum Total of All Loss Companies in the Federal Consolidated Group | (25) |
| ***Properly Attributed Federal Tax Cap for Total PacifiCorp Regulated Operations*** | 135 |

**Step 2**

| | PacifiCorp Oregon Regulated Operations | PacifiCorp Total Regulated Operations | Factor | | |
|---|---|---|---|---|---|
| | | | Gross | Weighting | Net |
| Total Gross Owned and Rented Property | 4,500 | 16,000 | 28.13% | X 0.3333 | 9.38% |
| Total Wages and Salaries | 200 | 500 | 40.00% | X 0.3333 | 13.33% |
| Total Sales and Other Receipts | 1,000 | 3,000 | 33.33% | X 0.3333 | 11.11% |
| ***Apportionment Percentage - PacifiCorp Oregon Regulated Operations*** | | | | | 33.82% |
| Properly Attributed Current Federal Tax Cap - Total PacifiCorp Regulated Operations | | | | | 135 |
| ***Properly Attributed Federal Tax Cap - PacifiCorp Oregon Regulated Operations*** | | | | | 46 |
| Addback: Federal Deferred Tax for PacifiCorp Oregon Regulated Operations Only | | | | | 100 |
| Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | | | | | 1 |
| Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | | | | | 4 |
| ***Properly Attributed Federal Tax Cap*** | | | | | 151 |

## STATE TAX CAP

| | Properly Attributed State Tax Cap |
|---|---|
| PacifiCorp Total Regulated Operations Oregon Standalone Tax Liability | 75 |
| Less: Imputed Negative Tax Liability from the Sum Total of All Loss Companies in the Oregon Unitary Group | (5) |
| ***Properly Attributed State Tax Cap for Total PacifiCorp Regulated Operations*** | 70 |
| Addback: Oregon Deferred Tax for PacifiCorp Oregon Regulated Operations Only | 25 |
| Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | 1 |
| Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | 5 |
| ***Properly Attributed State Tax Cap*** | 101 |

## TOTAL

| | Apportionment Method | Tax Cap |
|---|---|---|
| *Total Properly Attributed Federal Tax* | 210 | 151 |
| *Total Properly Attributed State Tax* | 106 | 101 |
| ***Total Properly Attributed Federal and State Taxes Paid**** | 316 | 252 |

| | |
|---|---|
| ***Properly Attributed Local Taxes Paid*** | 18 |

*** Properly Attributed Federal and State Tax Paid is derived as the greater of the aggregate amounts calculated in the Federal and State Apportionment Method Calculations or the aggregate amounts calculated in the Federal and State Tax Caps.

PacifiCorp

## Federal, State, and Local Apportionment Method Calculations
### PacifiCorp Approach

*FEDERAL APPORTIONMENT METHOD CALCULATION*

| | | Adjusted Federal Consolidated Tax |
|---|---|---|
| Step 1 | ***Federal Consolidated Tax Before Credits*** | **3,500** |
| | Less: Current Tax on Non-Oregon Regulated Entities | (400) |
| | Less: Current Tax on PacifiCorp Non-Oregon Regulated Operations | (105) |
| | Less: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations | (4) |
| | Addback: Imputed Tax Benefit of Charitable Contributions not Attributable to PacifiCorp Oregon Regulated Operations | 1 |
| | Addback: Imputed Tax Benefit of Depreciation on Disallowed Capital Costs | 3 |
| | ***Adjusted Federal Consolidated Tax Before Credits*** | **2,995** |

| | PacifiCorp Oregon Regulated Operations | Modified Consolidated Federal Taxpayer | Factor | | |
|---|---|---|---|---|---|
| | | | Gross | Weighting | Net |
| Total Gross Owned and Rented Property | 4,500 | 150,000 | 3.00% | X 0.3333 | 1.00% |
| Total Wages and Salaries | 200 | 4,000 | 5.00% | X 0.3333 | 1.67% |
| Total Sales and Other Receipts | 1,000 | 40,000 | 2.50% | X 0.3333 | 0.83% |

| | | |
|---|---|---|
| Step 2 | ***Apportionment Percentage - PacifiCorp Oregon Regulated Operations*** | **3.50%** |
| | Adjusted Federal Consolidated Tax Before Credits | 2,995 |
| | ***Properly Attributed Federal Tax Before Adjustements - PacifiCorp Oregon Regulated Operations*** | **105** |
| | Federal Deferred Tax for PacifiCorp Oregon Regulated Operations Only | 100 |
| | Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | 1 |
| | Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | 4 |
| | ***Properly Attributed Federal Tax*** | **210** |

*STATE APPORTIONMENT METHOD CALCULATION*

| | | Adjusted Oregon Unitary Tax |
|---|---|---|
| Step 1 | State Effective Tax Rate Used in Setting Rates | 4.84% |
| | Oregon Statutory Tax Rate | 6.60% |
| | ***Adjusted Oregon Statutory Tax Rate*** | **73.33%** |
| | Oregon Unitary Tax Before Credits | 127 |
| | ***Adjusted Oregon Unitary Tax Before Credits*** | **93** |
| | Less: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations | (5) |
| | Addback: Imputed Tax Benefit of Charitable Contributions not Attributable to PacifiCorp Oregon Regulated Operations | 1 |
| | Addback: Imputed Tax Benefit of Depreciation on Disallowed Capital Costs | 1 |
| | ***Adjusted Oregon Unitary Tax*** | **90** |

| | PacifiCorp Oregon Regulated Operations | Unitary Taxpayer Oregon Only | Factor | | |
|---|---|---|---|---|---|
| | | | Gross | Weighting | Net |
| Total Gross Owned and Rented Property | 4,500 | 5,000 | 90.00% | X 0.3333 | 30.00% |
| Total Wages and Salaries | 200 | 250 | 80.00% | X 0.3333 | 26.66% |
| Total Sales and Other Receipts | 1,000 | 1,250 | 80.00% | X 0.3333 | 26.66% |

| | | |
|---|---|---|
| Step 2 | ***Oregon Apportionment Percentage*** | **83.32%** |
| | Adjusted Oregon Unitary Tax | 90 |
| | ***Properly Attributed State Tax Before Adjustments*** | **75** |
| | Addback: Oregon Deferred Tax for PacifiCorp Oregon Regulated Operations Only | 25 |
| | Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | 1 |
| | Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | 5 |
| | ***Properly Attributed State Tax*** | **106** |

PacifiCorp

## LOCAL CALCULATION

| | Properly Attributed Local Tax |
|---|---|
| Multnomah County Gross Income - PacifiCorp Regulated Operations | 110 |
| Total Multnomah County Business Gross Income | 125 |
| ***Multnomah County Apportionment Percentage*** | **88.00%** |
| Total Multnomah County Business Income Tax | 20 |
| ***Properly Attributed Local Tax*** | **18** |

## FEDERAL TAX CAP

**Step 1**

| | Properly Attributed Federal Tax Cap |
|---|---|
| PacifiCorp Total Regulated Operations Federal Standalone Tax Liability | 160 |
| Less: Imputed Negative Tax Liability from the Sum Total of All Loss Companies in the Federal Consolidated Group | (25) |
| ***Properly Attributed Federal Tax Cap for Total PacifiCorp Regulated Operations*** | **135** |

**Step 2**

| | PacifiCorp Oregon Regulated Operations | PacifiCorp Total Regulated Operations | Factor | | |
|---|---|---|---|---|---|
| | | | Gross | Weighting | Net |
| Total Gross Owned and Rented Property | 4,500 | 16,000 | 28.13% | X 0.3333 | 9.38% |
| Total Wages and Salaries | 200 | 500 | 40.00% | X 0.3333 | 13.33% |
| Total Sales and Other Receipts | 1,000 | 3,000 | 33.33% | X 0.3333 | 11.11% |
| ***Apportionment Percentage - PacifiCorp Oregon Regulated Operations*** | | | | | **33.82%** |

| | |
|---|---|
| Properly Attributed Current Federal Tax Cap - Total PacifiCorp Regulated Operations | 135 |
| ***Properly Attributed Federal Tax Cap Before Adjustments - PacifiCorp Oregon Regulated Operations*** | 46 |
| Federal Deferred Tax for PacifiCorp Oregon Regulated Operations Only | 100 |
| Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | 1 |
| Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | 4 |
| ***Properly Attributed Federal Tax Cap*** | **151** |

## STATE TAX CAP

| | Properly Attributed State Tax Cap |
|---|---|
| PacifiCorp Total Regulated Operations Oregon Standalone Tax Liability | 75 |
| Less: Imputed Negative Tax Liability from the Sum Total of All Loss Companies in the Oregon Unitary Group | (5) |
| ***Properly Attributed State Tax Cap Before Adjustments - PacifiCorp Oregon Regulated Operations*** | 70 |
| Oregon Deferred Tax for PacifiCorp Oregon Regulated Operations Only | 25 |
| Addback: Imputed Tax Benefit of Charitable Contributions Attributable to PacifiCorp Oregon Regulated Operations Only | 1 |
| Addback: Tax Credits Attributable to PacifiCorp Oregon Regulated Operations Only | 5 |
| ***Properly Attributed State Tax Cap*** | **101** |

| | Apportionment Method | Tax Cap |
|---|---|---|
| *Total Properly Attributed Federal Tax* | 210 | 151 |
| *Total Properly Attributed State Tax* | 106 | 101 |
| ***Total Properly Attributed Federal and State Taxes Paid**** | **316** | **252** |

| | |
|---|---|
| ***Properly Attributed Local Taxes Paid*** | **18** |

*** Properly Attributed Federal and State Tax Paid is derived as the greater of the aggregate amounts calculated in the Federal and State Apportionment Method Calculations or the aggregate amounts calculated in the Federal and State Tax Caps.

PacifiCorp

## ATTRIBUTION PROBLEMS ADDRESSED BY THE PROPOSED ATTRIBUTION FLOOR

1. **Applying the same tax-loss to a utility multiple times.**

Without the floor, if NW Natural has an affiliate with a tax loss, the rule would reduce the utility's taxes paid by an amount greater than the total affiliate tax loss on the consolidated return.

| | Tax Liability | Temporary Rule Attribution | 3-Factor Allocation | Interim Order Attribution |
|---|---|---|---|---|
| Utility | 50 | 40 | 25% | 10 |
| Affiliate | -10 | 0 | 75% | 30 |
| Total | 40 | | | |

2. **Reallocating the utility's taxes paid to another entity, even when each member of the consolidated group has a positive tax liability.**

Without the floor, if NW Natural acquired a taxpaying affiliate, it could be penalized by having its actual taxes incurred attributed instead to the affiliate, even when there was no tax-loss entity and no benefit derived from the consolidated return.

| | Tax Liability | Temporary Rule Attribution | 3-Factor Allocation | Interim Order Attribution |
|---|---|---|---|---|
| Utility | 50 | 50 | 25% | 25 |
| Affiliate | 50 | 50 | 75% | 75 |
| Total | 100 | | | |

## THE FLOOR RATE LANGUAGE

(3)(c) The amount of income taxes paid that is properly attributed to the Oregon regulated utility operations under subsections (3)(a) and (3)(b) shall not be less than the amount of the stand-alone federal and state income tax liabilities of the utility, reduced by the imputed negative tax associated with the sum of all federal and state income tax losses of entities in the utility's affiliated and unitary groups, respectively, and then multiplied by the average of the ratios for the utility's gross plant, wages and salaries, and sales, using amounts applicable to the Oregon regulated operations of the utility as set forth in the utility's Results of Operations Report in the numerator and amounts for the utility in the denominator.

NW Natural
8/21 public comment hearing

# Avista Presentation

## AR 499 – Adoption of Permanent Rules to Implement SB 408 Relating to Utility Taxes

**Kelly Norwood**
**August 21, 2006**

Avista
8/21 public comment hearing

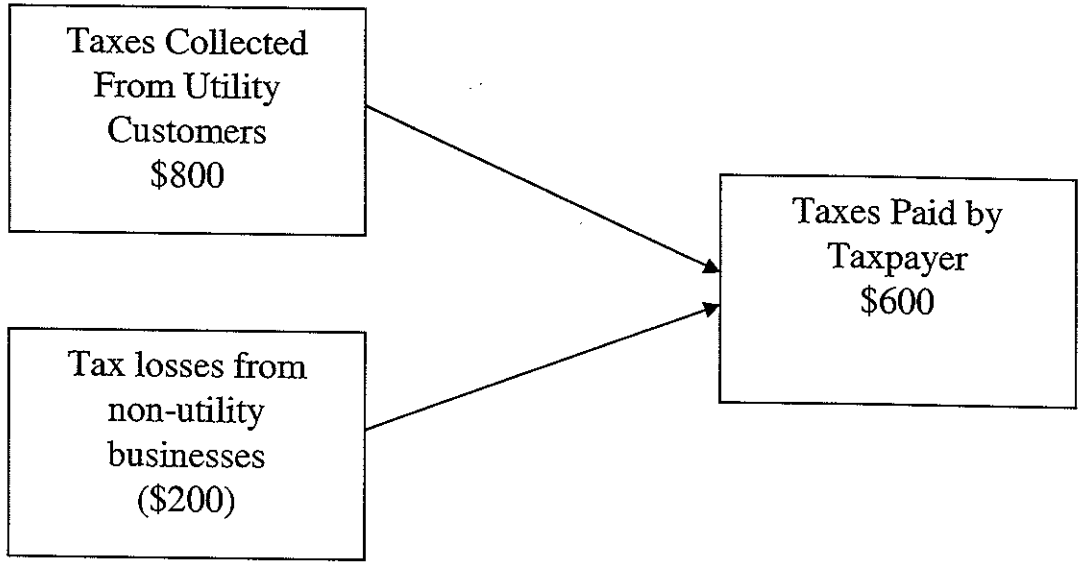
# OBJECTIVE IN IMPLEMENTING SB 408

Develop and implement permanent rules related to SB 408 that capture the letter and intent of the law, and that is workable in the long-term.

What follows is a discussion of the impact of the three-factor apportionment method, and how it might be further modified to accomplished its intended purpose.

## THE "PROBLEM"

The "problem" that SB 408 is attempting to fix is the circumstance where tax losses in non-utility businesses reduce the total taxes paid by the parent corporation to an amount less than that collected from regulated utility customers.



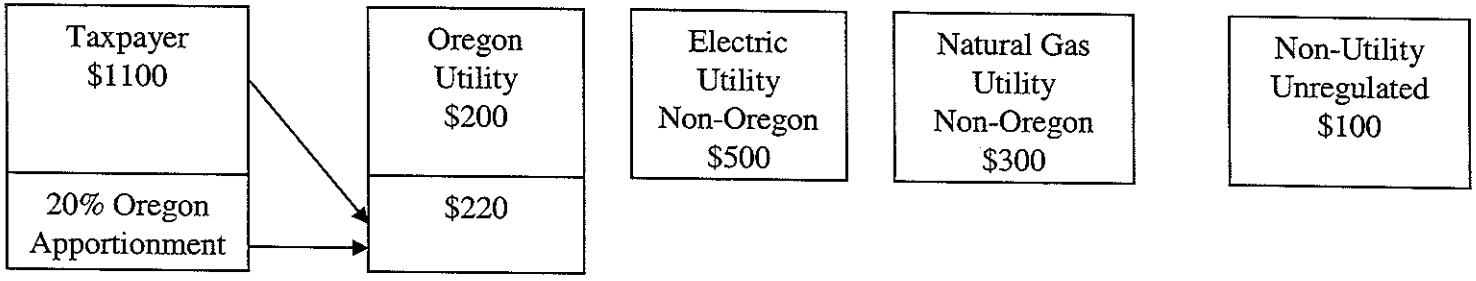
## MOST RECENT PROPOSAL TO FIX THE PROBLEM

The most recent apportionment proposal to fix the problem would likely violate Internal Revenue Service (IRS) rules related to the normalization of tax benefits from accelerated depreciation, unless modified as proposed later in this presentation. The violation would occur when all, or a portion, of the benefits from accelerated depreciation are flowed through to customers through the automatic rate adjustment.

The most recent proposal also creates an additional problem of redistributing tax benefits from regulated operations in other state jurisdictions to Oregon customers, as shown in the next slide.

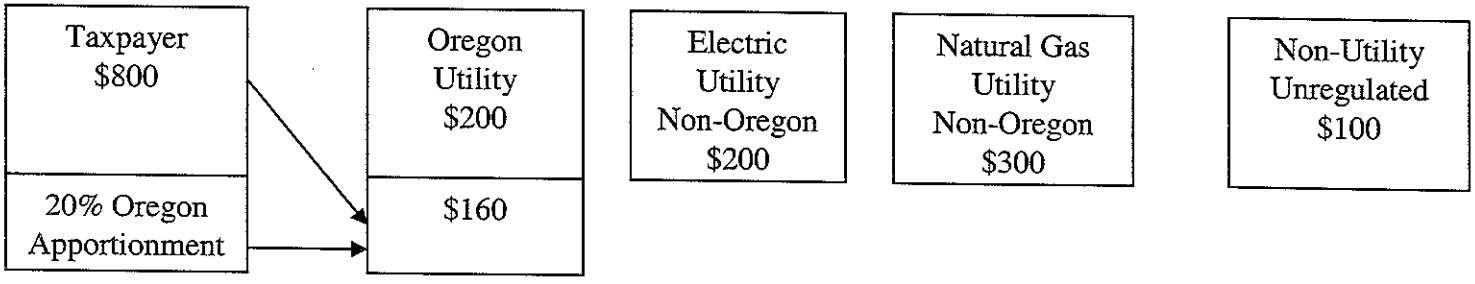
# REDISTRIBUTION OF TAX BENEFITS FROM NON-OREGON REGULATED OPERATIONS

## Example 1




In Example 1, customers would pay the Oregon stand-alone "lesser of" amount of $200, rather than the apportioned amount of $220.

## Example 2

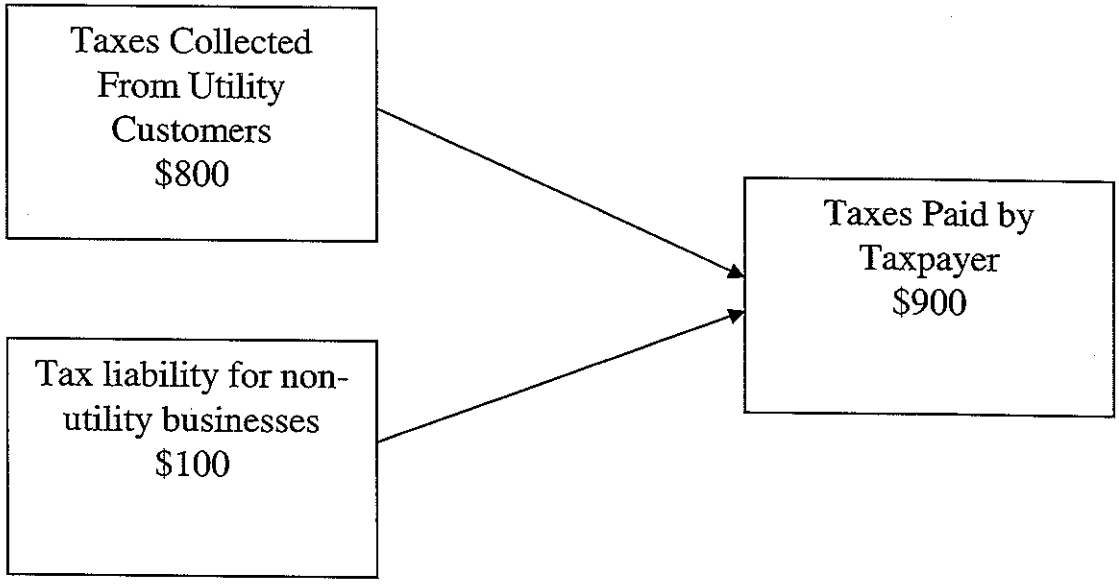



In Example 2, customers would pay the "lesser of" apportioned amount of $160, instead of the $200 stand-alone amount, and would receive a benefit from the non-Oregon regulated utility operations.

# THE FIX

**Step 1**

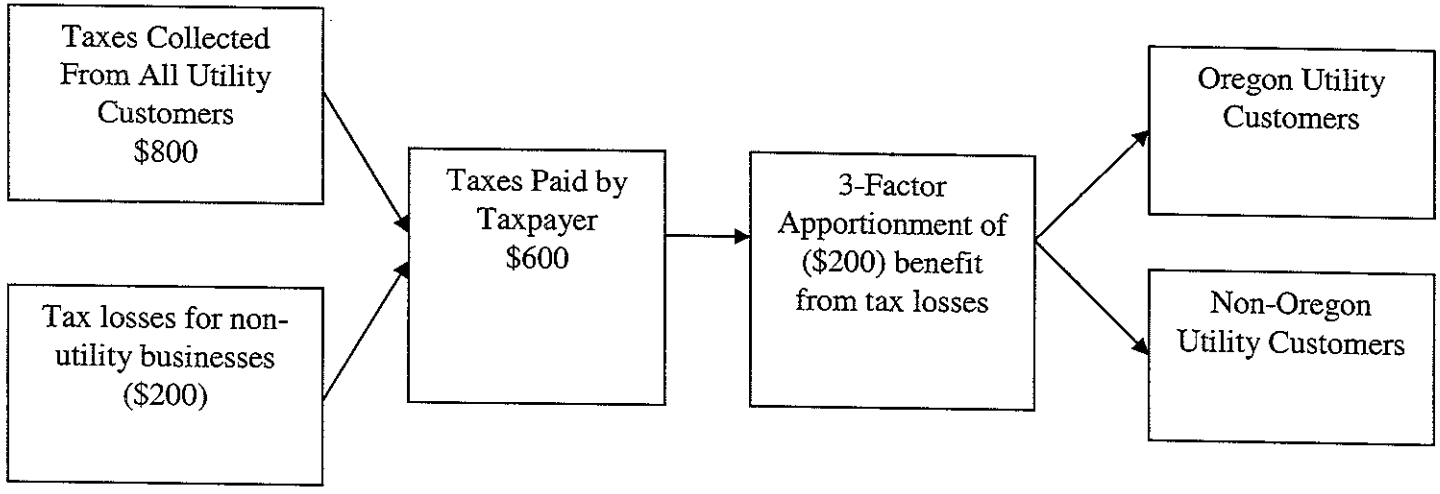
If there is not a tax loss for the non-utility businesses, there is no need for an apportionment.



# THE FIX

**Step 2**

If the net tax losses from the non-utility businesses cause the taxpayer to pay less in taxes than that collected from utility customers, the tax benefits from the non-utility businesses would be apportioned to utility customers using the three-factor apportionment methodology proposed by the Commission in the July 14, 2006 Interim Order.



## THE RESULT

Does not violate the normalization of tax benefits from accelerated depreciation

Does not redistribute tax benefits from other regulated jurisdictions to Oregon

Accomplishes what was intended by SB 408

Easy to administer and audit

## ALTERNATIVE METHOD FOR FEDERAL TAXES

An alternative proposal to solve the normalization violation problem is to start with the consolidated federal income tax liability before tax credits, then add back the tax effect of charitable contributions for the taxpayer, and make an adjustment for all deferred taxes. By adjusting for all deferred taxes up front, a normalization violation is avoided. Then the three-factor apportionment ratio of property, payroll, and sales would be used to apportion the resulting consolidated amount of federal income tax to determine the amount properly attributed to Oregon regulated operations.

Although this alternative method solves the normalization violation problem, it does not solve the problem of the redistribution of tax benefits from non-Oregon regulated operations to Oregon customers.

# OREGON STATE INCOME TAXES

The state income tax to be paid to Oregon is already determined by an Oregon Department of Revenue (DOR) four-factor formula applied to federal taxable income for the taxpayer, and then applying the statutory state income tax rate.

This predetermined amount of Oregon state income tax simply needs to be apportioned to: 1) Oregon regulated operations, and 2) other non-utility businesses that have situs amounts of property, payroll, and/or sales in Oregon.

In apportioning the state income tax to Oregon regulation operations, the entities that were included in the DOR state apportionment factor numerators are the same entities that would be included in the AR 499 apportionment factor denominator, and the Oregon regulated apportionment factor amounts would be included in the numerator.

The amount of state income tax apportioned to Oregon regulated operations under the AR 499 rules is the Oregon stand-alone amount, as well as the properly attributed amount.

No "lesser of" calculation between stand-alone and properly attributed needs to be made.

## OTHER ISSUES

Local income taxes is not an issue for Avista, since it does not operate in Multnomah County.

The property, payroll, and sales used for ratemaking purposes should be used in determining the apportionment factor, instead of situs amounts.

Avista's proposed apportionment methodology resolves the problem of double counting losses. If Avista's method is not adopted, the amount of the federal income tax benefit from a loss should be capped.

Avista agrees with a December 31, 2006 filing date for a Private Letter Ruling (PLR) with the IRS.

Avista has addressed other issues in its filed written comments and reply comments.

# Alternative Method for Federal Taxes

| | | Oregon Regulated | Non-Oregon Regulated | Non-Utility | Total Taxpayer |
|---|---|---|---|---|---|
| | | (a) | (b) | (c) | (d) |
| | **Assumptions:** | | | | |
| 1 | Property/Payroll/Sales Apportionment Factor | 30% | 65% | 5% | 100% |
| 2 | Tax Depreciation | $2,000 | $8,000 | $100 | $10,100 |
| 3 | Book Depreciation | $1,000 | $4,000 | $100 | $5,100 |
| 4 | Excess Tax Depreciation | $1,000 | $4,000 | $0 | $5,000 |
| 5 | FIT Rate | 35% | 35% | 35% | |
| 6 | Deferred FIT | $350 | $1,400 | $0 | $1,750 |
| 7 | Total Tax Liability | | | | $8,000 |
| 8 | Total Tax Liability Prior to Tax Credits | | | | $8,200 |
| 9 | Tax Benefit from Charitable Contributions | | | | $100 |

| | | |
|---|---|---|
| | **Calculation:** | |
| 10 | Total Tax Liability Prior to Tax Credits | $8,200 |
| 11 | Adjust for All Deferred Taxes | $1,750 |
| 12 | Adjust for Tax Benefit from Charitable Contributions | $100 |
| 13 | Adjusted Tax Liability | $10,050 |
| 14 | Oregon Apportionment Factor | 30% |
| 15 | Oregon Properly Attributed Taxes Paid | $3,015 |

Avista
8/21 public comment hearing

**AR 499 Public Comment Hearing**
**August 21, 2006**

**ICNU Proposed Language Regarding a "Floor" on the Properly Attributed Amount**

The amount of federal income taxes paid properly attributed to regulated operations of the utility shall not be greater than the § 3(12)(a) amount for federal taxes paid, less an amount equal to the sum of all federal income tax losses of each entity within the federal consolidated tax group that, if filing federal taxes alone, would not have produced a positive federal tax liability.

ICNU
8/21 public comment hearing

## City of Portland Comments to Proposed Changes to AR 499 Draft Rules
## 21 August 2006

### A. Properly Attributed Issues

#### 1. Tax Normalization Requirements.

Non-Oregon deferred taxes: Allocating benefits related to regulated operations to Oregon customers could trigger a normalization violation. (13f requires an adjustment for deferred taxes of Oregon operations.)

**COP Comment**

Internal Revenue Code Section 168[i] requires that the taxpayer ( i.e. the regulated utility) use in computing its tax expense for ratemaking purposes the same method of depreciation that the taxpayer use for income tax purposes. This "normalization rule" only applies to depreciation expense and only to the "Public Utility Property" of the taxpayer. The normalization rule only applies to depreciation on the specific properties over which the Commission has ratemaking jurisdiction.

Under the Treasury Regulations[ii] the Commission is considered to have jurisdiction over a specific property of the regulated utility only if the depreciation expense with respect to the property is included in cost of service as determined by the regulatory body for ratemaking purposes or for reflecting operating results in its regulated books of account.

ORS 757.268(8) authorizes the Commission to include in rates "(a) Deferred taxes resulting from accelerated depreciation or other tax treatment of **utility investment** (emphasis supplied); and (b) Tax requirements and benefits that are **required** (emphasis supplied) to be included in order to ensure compliance with the normalization requirements of federal tax law.

The purpose of SB 408 was to match as closely as possible "real world" taxes actually paid to governments with the "regulatory taxes" collected in utility rates while not violating the normalization requirements of federal tax law.

The Commission should do no more in implementing SB 408 than meet the minimum requirements of the normalization rules of federal tax law required in relation to the utility investment and accordingly the COP suggests an additional alternative to those proposed:

> "h) After apportioning the actual federal taxes paid by the utility, or its affiliated group (as defined in IRC § 1563) if applicable, adjust for those deferred taxes related to the excess of tax depreciation on Public Utility Property (as defined in IRC §168(9)(B)) over depreciation that would have been allowed the utility under ( IRC 167(a)(l) straight line method) , solely on those properties over which the Commission has ratemaking jurisdiction and only to the extent required by IRC § 168 and the regulations there under.

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[i] IRC §168(9)(A)

[iii][ii] Treas.Reg.§ 1.167(l)–3

COP
8/21 public comment hearing

## A. Properly Attributed Issues

### 2. Add backs to Taxes Paid.

Tax credits and benefits unrelated to Oregon regulated operations (e.g., Production Tax Credits and charitable contributions), unless adjusted, would be allocated to Oregon customers. (13f requires an adjustment for Oregon items)

**COP Comment**

The single alternative proposed to use "taxes before credits" is over broad in increasing "Taxes paid" and simply does not reflect the narrow statutory language of ORS 757.268(13)(f). The actual "real world" taxes paid with the tax returns filed with governments by the utility or its affiliated group if applicable, must be apportioned to the regulated operations of the utility (using the three factor formula proposed by the Commission) before adjustments are made for the tax benefits of charitable contributions made by the utility or tax credits on property investments by the utility not "taken in to account" in the utility's last rate making hearing in order to clearly reflect the Statute. The COP suggests an additional alternative to those proposed:

> "b)After apportionment of taxes paid to the regulated operations of the utility, add back the tax benefit of charitable contributions made by the utility (to Oregon charities), and the tax credits on utility expenditures for public utility property under the jurisdiction of the Commission but not "taken into account" in the utilities last general ratemaking process. "Taken into account" shall relate to the character or nature or foreseeable of a class or type of expenditure category and not to the specificity of a particular item or amount"

### 3. Situs versus allocated amounts.

Use of situs amounts in the three-factor calculation for Taxes Paid creates a mismatch with how Taxes Collected is calculated.

**COP Comment**

For state corporate income taxes the statutory rate varies (e.g. California 8.84%, Washington 0%) and accordingly the Unitary (UDITPA) overall effective rate is used by the Commission in computing regulated tax expense and in computing the net-to–gross multiplier for rate making. For UDITPA purposes the income of the unitary group, including the utility under the jurisdiction of the Commission, is based on a formula that uses the actual situs of property. Oregon corporate income taxes actual paid in the "real world" is reduced by income apportioned to other states because the situs of utility property is in that other state.

The draft rule properly accounts for the UDITPA apportionment of income by using the same method of apportionment in computing "taxes paid" by the regulated operation of the utility.

The alternative proposed to use the same basis for property as used in setting utility rates has the potential to unfairly burden ratepayers with hypothetical taxes that were never actual paid because the property situs used in the UDITPA three property formula apportioned the income to a state without an income tax but the utility still got a credit for "taxes paid" in its Oregon calculation.

The COP suggests the Commission stay with the draft rule in the interim order without change.

### 4. State Taxes Paid: Unitary Group.

Basing calculation of state income taxes paid on all companies of the affiliated group in the state requires unwarranted complexity and is inconsistent with the unitary taxpaying group that includes the utility.

**COP Comment**

In Order No 06-400 the Commission stated "To comply with the language of SB 408 , particularly the definitions set forth in the law, the various unitary groups that include entities in the federal consolidated return must be aggregated to determine the amount of taxes paid by the affiliated group in Oregon"

The COP agrees with the Commission. Utility arguments that the requirement is an unwarranted complexity are false. The aggregation calculation is simple addition. The aggregation calculation is necessary to keep a utility for "gaming the System" by juggling what are claimed to be the unitary groups in the overall federal consolidated return. The alternative suggested is also a "back door" attempt to get stand-along treatment for a utility member of a consolidated group by claiming it is non- unitary with the rest of the affiliated group in the federal return.

**5. State Taxes Paid: Multi-state tax rate.**

Three-factor calculation for state tax using only Oregon income tax creates a mismatch between how Taxes Paid and Taxes Collected are calculated for multi-state utilities for which Commission recognizes non-Oregon state taxes in setting rates.

**COP Comment**

The COP proposal in item 3 above relating to situs versus ratemaking of property located in other states also resolves this issue. Restated; the Uniform Division of Income for Tax Purposes Act ( UDITPA) method is used to determine the unitary effective tax liability when a utilities actual tax liability is not solely dependant on its Oregon operations for ratemaking purposes. Accordingly in order to provide comparability between actual "Taxes paid" and regulated tax expense used in ratemaking the same UDITPA method must be used. Thus the actual taxes paid to state governments would be allocated to the regulated operations based on the three factor formula. Any other method (such as the "option") departs from the effort to match as closely as possible taxes paid with those included in rates.

**6. Local Taxes Paid Apportionment.**

Three-factor calculation for local taxes is inconsistent with the gross income allocation method Multnomah County uses to apportion Oregon net income to the county.

**COP Comment**

The Multnomah County Income Tax Return, line 1, begins with the net income of the unitary group, including the utility, from the groups Oregon Form 20. The county then uses a one factor apportionment factor (gross income) to apportion the net income to Multnomah County for applying the 1.45% tax. The COP agrees with the suggestion alternative; except the COP believes that the amount of "taxes paid" would need an adjustment in order to comply with the normalization requirements of the federal tax law. Otherwise the entire benefit of any accelerated depreciation included in the Oregon net income apportioned on the Multnomah County return would have "flowed through" to ratepayers in the taxes paid calculation.

**7. Definition of "Sales" Factor.**
In the three-factor formula, Sales may not include all income underlying taxes paid (e.g., dividend income)
**COP Comment**
The COP strongly disagrees and believes that the UDITPA method for allocation and apportionment of income from whatever source derived should be followed by the Commission. Accounting for the source of various types of income (e.g. dividends) included in the sales factor in the three factor formula is an area of state tax law that is well settled after decades of litigation. The Commission in Order No. 06-400 stated its intention to adopt the widely established methodology of UDITPA and that methodology clearly covers the allocation or apportionment of all forms of income, dividends, rents, investment gains, etc. The Commission definition need only adopt the methodology used by Oregon for income tax apportionment purposes and need not create new rules.

**8. Floor for Properly Attributed Amount.**
As losses reduce the taxes paid starting point, the three-factor method apportions those losses to all entities, including the losers. Thus, utility's properly attributed amount could be lower than stand-alone by more than 100% of the combined losses.
**COP Comment**
Good! If the affiliated group of corporations of which the utility is a member pay no "real world" tax because of tax planning or other circumstances then if after the required normalization deferred tax add back and other statutory add backs the utility pays no taxes then the ratepayers should be refunded the taxes that were included in their rates but never paid under the automatic adjustment clause. The three factor formula doesn't apportion losses it apportions the "taxes paid" by the utilities affiliated group. If there are none then there are none to be apportioned. Why should the utility ratepayers "share" in taxes that aren't paid?
The COP sees no statutory basis for the proposed alternative of creating a misnamed "floor" to create "taxes" that never were paid to a government.

**9. "Double Whammy."**
SB 408 adjustment exacerbates higher/lower earnings.
**COP Comment**
Any utility is free to start a rate case and request lower rates if it feels its earning are to high and they have been exacerbated by SB 408. The rate setting system exists for that purpose. Any "automatic adjustment with artificial limiters not statutorily supported is strongly opposed by the COP.

## B. Other Issues
### 10-12. The 12(a) cap
If "With and Without" method were used for the cap, section (12) would not be meaningful because (12)(a) would always be lower than (12)(b). With and without" calculation does not reflect all impacts on the affiliated group related to the utility. A stand-alone calculation of taxable income is not consistent with how state income tax payments are determined
**COP Comment**

The language of ORS 757.268(12) effectively provides a flow through of tax benefits attributable to any non-regulated businesses of a utility (e.g. discontinued operations, foreign operations, energy service businesses, tax advantaged investments) to the utilities ratepayers by choosing the lesser of the taxes generated by only the regulated operations of the utility or the utility in total ( regulated and non-regulated) as "taxes paid" in the automatic adjustment calculation.
The COP doesn't view a need for anything other than a straight forward application of the 12(a) and 12(b) "lesser of" measurements to a utility or apportioned in the case of an affiliated group.

**13. Private Letter Rulings.**
The proposed date of October 15 for filing the Private Letter Ruling does not provide sufficient process time for the companies, OPUC, and other participants to prepare and review drafts
**COP Comment**
The Commission in its rules must state that the purpose of the PLR is to get approval for the minimum level of depreciation adjustment necessary to comply with the normalization requirements of federal tax law.