BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

AR 517

In the Matter of Housekeeping and Clarification Changes to OAR 860-022-0041.	STAFF COMMENTS

This rulemaking is used to make a few housekeeping and necessary clarification changes to OAR 860-022-0041.

Major changes are (1) to remove an iterative effect caused by calculating a tax effect on the amount either refunded or collected from customers; (2) allow a change in methodology if ownership of the utility changes; (3) removing a potential federal tax law normalization problem caused by drawing down current deferred taxes; (4) creating a placeholder due to a legislative proposal so all parties will have the ability to comment on any changes to treatment of the BETC tax credit; and (5) correcting the calculation of the "floor" for the three-factor Apportionment Method.

The first change is to address the iterative effect that takes place when taxes are refunded or collected by utilities to or from their customers and taxed as increased or decreased revenue again in the subsequent years. The tax effect of the collection or refund of taxes is called the iterative effect. This effect will continue each year and will cause the utilities to over-collect or over-refund the amount of taxes to be collected or refunded to customers. The section of the rule which relates to this change is 2(b) which states:

> ""Deferred taxes" for purposes of the utility means the total deferred tax expense of regulated operations, ~~**as reported in the deferred tax expense accounts as defined by the Federal Energy Regulatory Commission,**~~ that relate to the year being reported in the utility's results of operations report or tax returns**<u>, excluding deferred taxes related to the establishment of a regulatory receivable or payable account for any rate adjustment imposed under ORS 757.268, in the</u>**

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year the deferred tax is established but not thereafter, to eliminate the iterative tax effect of the rate adjustment;"

The new section 2(g) defines "Iterative tax effect." Section 4(d)(E), requires an adjustment to remove the effect in calculating the amount of tax paid each year:

"Elimination of the iterative tax effect to the extent such iterative tax effect has not been eliminated by subsection (4)(d)(A) of this rule"

The second change allows a change in methodology if ownership of the utility changes. As the rule was originally written, utilities had a one-time only election as to what kind of methodology they would use in calculation of their state income taxes. This change will allow the utilities to make a change in their election if their ownership changes. Staff believes this is reasonable, because an ownership change can significantly alter the approach that is most sensible for calculating state taxes for a particular utility. The section of the rule affected is 3(c)(C) as follows:

"If a utility's taxes collected in rates reflect non-Oregon state income taxes, the utility must make a one-time permanent election in its October 15, 2006, tax report filing**, or in the case of a utility ownership change pursuant to ORS 757.511, in the first tax report filing that includes a tax reporting period reflecting the new ownership,** to either:"

The third change removes a potential federal tax law normalization problem caused by drawing down current deferred taxes. To avoid this result, staff proposes to make an adjustment when the amount of federal and state "Taxes Paid" is less than the amount of deferred taxes related to depreciation of public utility property for Oregon regulated operations. The calculation would be required by revised subsection 4(d)

"The lowest of the amounts in subsections (4)(a), (4)(b) and (4)(c) of this rule, after making adjustments ~~for~~ **in paragraphs (4)(d)(A), (4)(d)(B), (4)(d)(C), (4)(d)(D), and (4)(d)(E), but no less than the deferred taxes related to depreciation of public utility property for regulated operations of the utility, except the deferred tax amount must be reduced by any tax refunds recognized in the reporting period and apportioned to the regulated operations of the utility: . . .**

The fourth proposal was included to create a placeholder due to a potential legislative change so all parties would have the ability to comment on any changes to treatment of the

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BETC tax credit. The current rule applies to BETC credits as they concern conservation and renewables only. The change to the rule opens it up to all BETC tax credits, no matter what the origin. Staff's understanding is that Section 19 of House Bill 3201, passed by the legislature in the recently-adjourned session, included language from HB 2211 requiring add back of all BETC credits. The portion of the rule that applies here is 4(d)(D):

> **<u>"An increase equal to the tax benefit of Oregon business energy tax credits, including those credits transferred pursuant to ORS 469.206 and ORS 469.208, of the unitary group, excluding those credits covered by subsection (4)(d)(A);"</u>**

The final change to the rule corrects the calculation of the "floor" for the three-factor Apportionment Method. The current rule, as adopted by Order 06-532, established a floor for the three-factor apportionment method to avoid a result whereby Oregon customers could receive more than 100 percent of the benefit from the tax losses of the utility's taxpaying group. Further, to avoid a possible normalization violation, the rule added back the current tax benefits of tax depreciation on public utility property (PUP) in calculating the amount of tax losses to be shared with Oregon customers. However, the rule mistakenly (in staff's view) added back all tax benefits from PUP depreciation, not just those benefits related to regulated utilities with losses, which is the amount necessary to consider for purposes of the floor/loss calculation to avoid a normalization violation. (Note that the starting point if the floor calculation is the stand-alone tax liability of Oregon regulated operations, which as defined in the rule already excludes all PUP tax benefits.) Thus, staff believes the current language for the floor calculation provides an improper result and does not reflect the Commission's intent in establishing a floor.

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Staff proposes a correction to the floor calculation that limits the offset to tax losses (of PUP depreciation tax benefits) to individual regulated entities in the taxpaying group with losses. This change is made to subsections 3(b)(A), 3(d)(A) and 3(d)(B)(i) of the rule, along with a definition of "income tax losses" in 2(d) that makes it clear it is referring to individual entities in the group.

DATED this 16th day of July 2007.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that on July 16, 2007, I served the foregoing upon all parties of record in this proceeding by delivering a copy by electronic mail and by mailing a copy by postage prepaid first class mail or by hand delivery/shuttle mail to the parties accepting paper service.

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