ORDER NO. 19-050

ENTERED Feb 19 2019

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1918

In the Matter of	
AVISTA CORPORATION, dba AVISTA UTILITIES,	ORDER
Application for Authorization to Defer Federal Income Tax Expenses for the Effects of Revisions of the Federal Income Tax Code Upon Cost of Service.	

DISPOSITION: STAFF'S RECOMMENDATION ADOPTED

At its public meeting on February 14, 2019, the Public Utility Commission of Oregon adopted Staff's recommendation in this matter. The Staff Report with the recommendation is attached as Appendix A.

BY THE COMMISSION:

Nolan Moser

Nolan Moser
Chief Administrative Law Judge

A party may request rehearing or reconsideration of this order under ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-001-0720. A copy of the request must also be served on each party to the proceedings as provided in OAR 860-001-0180(2). A party may appeal this order by filing a petition for review with the Circuit Court for Marion County in compliance with ORS 183.484.

ORDER NO. 19-050

ITEM NO. 3

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: February 14, 2019

REGULAR __X__ **CONSENT** ____ **EFFECTIVE DATE** ______ **March 1, 2019**

DATE: January 30, 2019

TO: Public Utility Commission

FROM: John Fox JF

THROUGH: Jason Eisdorfer and Marianne Gardner JE MG

SUBJECT: AVISTA UTILITIES: (Docket No. UM 1918) Application for Authorization to Defer Federal Income Tax Expenses for the Effects of Revisions of the Federal Income Tax Code upon Avista's Cost of Service.

STAFF RECOMMENDATION:

Approve Avista Utilities (Avista or Company) Application for Authorization to Defer Federal Income Tax Expenses for the Effects of Revisions of the Federal Income Tax Code upon Avista's Cost of Service, docketed as UM 1918, for the twelve-month period beginning December 31, 2017, calculated to be \$3.7 million (Oregon-allocated) for 2018.

DISCUSSION:

Issue

Whether the Commission should approve Avista's Application for Authorization to Defer Federal Income Tax Expenses for the Effects of Revisions of the Federal Income Tax Code upon Avista's Cost of Service (Application) for the 12-month period beginning December 31, 2017.

Applicable Rule or Law

Beginning with the date of the application, the Commission may approve the deferral of identifiable utility expenses or revenues, the recovery or refund of which the Commission finds should be deferred in order to minimize the frequency of rate changes for the fluctuation of rate levels or to match appropriately the costs borne by and benefits received by ratepayers. ORS 757.269(2)(e) and (4). Unless subject to an automatic adjustment clause under ORS 757.210(1), amounts deferred are allowed in rates to the extent authorized by the Commission in a proceeding under ORS 757.210 to change rates and upon review of the utility's earnings at the time of application to amortize the deferral. ORS 757.259(4); OAR 860-027-0300(9). The Commission's final determination on the amount of deferrals allowable in the rates of the utility is subject to a finding by the Commission that the amount was prudently incurred by the utility. ORS 757.259(5).

Analysis

Tax Act Deferral Background
On December 22, 2017, President Donald Trump signed H.R.1 – Tax Cuts and Job Act (Tax Act), with most provisions going into effect on January 1, 2018. The Tax Act amends sections of the 1986 code, most notably the reduction in the federal corporate income tax rate from 35 percent to 21 percent. The change in the corporate income tax rate also results in excess deferred income tax (EDIT) assets and liabilities that must be reversed.

On December 29, 2017, the Company filed a deferral application (Docket No. UM 1918) "for an order authorizing it to utilize deferred accounting for the impact to its federal income tax (FIT) expenses due to the revisions of the federal income tax code" with the intent of tracking the net impacts of the Tax Act to pass onto to customers. At the time the Application was filed, the impacts of the Tax Act were unknown.

On December 29, 2017, Staff also filed an application (UM 1923) to defer the changes in Avista's federal tax obligations resulting from H.R.1 — Tax Cuts and Jobs Act (Application). Staff filed similar applications for all six energy utilities to ensure ratepayers would benefit from the tax reduction beginning January 1, 2018. Avista responded on April 30, 2018, referring back to the contemporaneous docket and stating the Company did not believe the Commission need rule on Staff's separate application.

Subsequent to the filing of these applications, Avista, Staff, other utilities and stakeholders participated in a workshop to understand the Tax Act implications, and began working through methodologies to calculate benefits to ratepayers and for passing such benefits on to customers. Since that time, Staff has continued to work with each utility informally to address the deferral and amortization of Tax Act benefits.

On April 12, 2018, the Company supplemented its Application, estimating 2018 benefits of \$3.9 million comprised of the following; current and deferred income tax expense and conversion factor \$3.151 million, plant-related excess deferred income tax \$0.553 million, and non-plant related excess deferred income tax \$0.194 million.

On May 25, 2018, the Company agreed, pursuant to the filing of an all-party stipulation in UM 1897, to waive, and not seek to apply, an earnings test to the Tax Act benefits.[1]

On July 12, 2018, the Company supplemented its Application, showing no change in the estimated 2018 benefits of $3.9 million and reporting an interim deferral amount recorded on the Company's books of $2.5 million through June 30, 2018.

On October 10, 2018, the Company supplemented its Application, revising the estimated 2018 benefits upward to $4.0 million due to an upward revision of the non-plant related excess deferred income tax from $0.194 million to $0.284 million. The Company also reported an interim deferral amount recorded on the Company's books of $2.4 million through September 30, 2018.

On January 23, 2019, the Company supplemented its Application, reporting actual deferred permanent and temporary tax benefits for 2018 of $3.7 million dollars. This amount is inclusive of interest on the deferred tax benefit of $158 thousand and increased amortization of plant related excess deferred income taxes from $439 thousand to $496 thousand after filing of the Company's final corporate income tax return for 2017.

Taxes in Current Rates
The income tax expense currently included in Avista's base rates was approved in its last general rate case (Docket No. UG 325) and does not reflect any of the provisions of the Tax Act. Therefore, the Tax Act benefits are not currently reflected in Avista's base rates.

Staff Findings and Discussion
The purpose of this proceeding is to identify the amount of tax benefits to be deferred, for the benefit of Avista's ratepayers. Full consideration of the tax benefits includes the following computational elements:

- The decrease in the annual revenue requirement due to changes in how taxable income from operations is determined, the effect of reducing the statutory federal rate from 35 percent to 21 percent, and changes in allowable tax credits, etc.
- Changes to the value of accumulated deferred income taxes included in the Company's rate base.
- Revaluation of deferred tax obligations at the new lower statutory rate resulting in excess deferred income taxes (EDIT).

[1] See *In the Matter of HYDRO ONE LIMITED, Application for Authorization to Exercise Substantial Influence over the Policies and Actions of AVISTA CORPORATION*, Docket No. UM 1897, All-party Stipulation filed May 25, 2018, commitment 42b.

- Federal law provides that the return to ratepayers of EDIT related to utility plant must generally comply with the Average Rate Assumption Method (ARAM). Failure to adhere to the ARAM methodology would terminate the Company's ability to use accelerated depreciation methods for tax purposes. These amounts are generally referred to as "protected" EDIT.
- EDIT unrelated to utility plant and plant related EDIT not subject to the ARAM methodology may be returned to customers using any reasonable amortization method. These amounts are generally referred to as "unprotected" EDIT.

The Company's methodology for estimating the decrease in annual revenue requirement is to restate the UG 325 revenue requirement model using the new 21 percent tax rate. In response to Staff's inquiry requesting 2018 forecast results with and without tax reform the Company responded in part,

> As a multi service-multi jurisdiction utility, a 2018 Forecasted Results of Operations, with or without the effects of the TCJA, isolated for Oregon, is not available.[2]

In response to Staff's inquiry regarding possible use of 2017 Results of Operations as a proxy for 2018, the Company responded in part,

> The Company did not believe use of 2017 Results of Operations would be more representative of expected 2018 Results of Operations, as base rates changed effective November 1, 2017, and therefore would be stale with regards to expected calendar 2018 results.[3]

Staff supports the Company's approach given that Company's current base rates became effective November 1, 2017, and were based on a test year ending September 30, 2018. This is a 9 month overlap with the calendar year 2018 deferral period.

Staff notes that the plant-related (protected) excess deferred income tax of $496 thousand dollars is for 2018 only and this amount will change each year based on the ARAM methodology and would need to be updated for the deferral reauthorization in 2019.

The Company proposes to return the entire non-plant related (unprotected) excess deferred income tax of $235 thousand dollars in 2018. Accordingly, the deferred amount

[2] See Company response to Staff DR 1 (Staff_IR_001.docx).
[3] See Company response to Staff DR 1 (Staff_IR_002.docx).

for 2019 will not include an amortization of unprotected EDIT.

Staff has reviewed the Company models and finds that they are calculated in accordance with Oregon ratemaking principles including the conversion factor of 1.307 which is inclusive of all revenue sensitive costs in the UG 325 rate case and adjusted to reflect the new 21 percent tax rate.

Furthermore, the Company has been recording a monthly accounting entry of the deferred excess current/deferred income tax expense and deferred excess plant (protected) ADFIT. Throughout the various filings in this docket, the Company has stated its intent that "the amount of deferred tax benefits to be returned to customers will vary based on actual balances deferred during calendar 2018."[4]

Staff notes that the quarterly estimates provided have been very similar, ranging between $3.9 million and $4.1 million, respectively. Actual tax savings reported by the Company, excluding interest, are $418 thousand less than savings based on changing the UG 325 revenue requirement model. The variance is caused by lower than expected net operating income before taxes and higher than expected interest expense.

Staff finds the variances in actual 2018 operating results are reasonable and recommends the Commission approve a deferral of $3.7 million dollars, representing the 2018 Tax Act benefits as presented in Attachment A to this memorandum.

<u>Conclusion</u>

For the reasons stated above, Staff concludes that Company's calculations are a reasonable calculation of the amounts due to ratepayers from the Tax Act and recommends the Commission approve the Company's Application to Defer Tax Act Benefits.

PROPOSED COMMISSION MOTION:

Approve Avista's Application for Authorization to Defer Federal Income Tax Expenses for the Effects of Revisions of the Federal Income Tax Code upon Avista's Cost of Service, docketed as UM 1918, for the twelve-month period beginning December 31, 2017, calculated to be $3.7 million (Oregon-allocated) for 2018.

UM 1918

[4] See UM 1918 Supplemental Application filed January 23, 2019, page 3.

ATTACHMENT A

Avista Utilities
Summary of Ratepayer Benefits from Federal Tax Reform

Summary of Tax Cut and Jobs Act (TCJA) Benefits (Actual Results revenue requirement, in 000's)	**Before Tax Reform**	**After Tax Reform**	**Ratepayer Benefit**
Utility Operating Income (Excl. Tax Reform Deferral)	$ 16,521	$ 18,530	
Adjust to Ratemaking Taxable Income			
Long Term Interest Expense	(7,256)	(7,247)	
Income Taxes	4,827	2,817	
	14,092	14,101	
Composite Tax Rate	34.25%	19.98%	
Operational Tax Savings	4,827	2,817	2,010
Other Tax Savings			
Amortization of Protected EDIT (ARAM method)		(496)	496
Amortization of Unprotected EDIT		(235)	235
Interest on Deferred Tax Reform Benefit		(121)	121
Net Effect of Other Tax Act Changes		25	(25)
	4,827	1,991	2,836
Gross Up Factor	1.307	1.307	
2018 Tax Savings	$ 6,310	$ 2,602	$ 3,708

Summary of Excess Deferred Income Taxes (EDIT) (in 000's)	**Protected**	**Unprotected**	**Total**
Regulatory Liability - 2017 Financial Statements	$ 28,294	$ 235	$ 28,529
Unprotected EDIT returned in 1 year (above)		(235)	(235)
2018 Amortization of Protected EDIT (above)	(496)		(496)
ARAM EDIT to be amortized in future years *	$ 27,798	$ -	$ 27,798

* Oregon portion only - not including gross up for taxes