

**BEFORE THE WASHINGTON  
UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,

Complainant,

v.

CASCADE NATURAL GAS  
CORPORATION,

Respondent.

DOCKETS UG-170929

PUBLIC COUNSEL'S COMMENTS  
ON CASCADE'S RESPONSE TO  
BENCH REQUEST 1

1. Public Counsel submits comments on Cascade's response to the Commission's Bench Request 1 pursuant to Order 05, Granting Staff's Motion Requesting Opportunity to Respond to Bench Request 1, dated March 9, 2018. Public Counsel witness Donna Ramas addresses the Tax Cut and Jobs Act (TCJA). Below are excerpts from Ms. Ramas's testimony, Exhibit DMR-1T and Exhibit DMR-42T.
  
2. The TCJA affects Cascade's request for revenue requirement as well as Cascade's Accumulated Deferred Federal Income Tax (ADFIT) balances. Cascade's requested revenue requirement will decrease as a result of the income tax rate reduction from 35 percent to 21 percent. Additionally, Cascade has over-collected from customers excess ADFIT because Cascade is currently collecting rates that include an imbedded income tax rate of 35 percent. This will result in an over-collection through at least the anticipated effective date for rates from this general rate case.<sup>1</sup> Public Counsel believes that the benefits from the tax legislation should be returned to customers, and this should be accomplished expeditiously and completely.

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<sup>1</sup> Public Counsel assumes that the new tax rate will be reflected in Cascade's rates going forward at the conclusion of this rate case.

## I. DONNA RAMAS'S RESPONSE TESTIMONY

3. Ms. Ramas addressed the TCJA in her Response Testimony, Exhibit DMR-1T. The following is an excerpt from her Response Testimony, Section II (TCJA Impacts):<sup>2</sup>

**Q: Are there any recent events that significantly impact the revenue requirements presented in Cascade's original filing dated August 31, 2017?**

A: Yes. On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act<sup>3</sup> into law. Among other changes, the TCJA reduced the federal income tax rate for corporations from the 35 percent rate used in Cascade's filing to 21 percent. The reduction to the federal income tax rate has a significant impact on the revenue requirements submitted by Cascade in its original filing. In the original and revised responses to Bench Request 1, Cascade indicates that the impact of reducing the federal income tax rate from 35 percent to 21 percent would revise their request from an increase in revenues of approximately \$5.9 million to an increase of approximately \$1.7 million. This impact, which is a reduction to the revenue increase of approximately \$4.2 million, only incorporates the impact of the reduction in the federal income tax (FIT) rate on income tax expense. It does not include the impacts on Cascade's Accumulated Deferred Federal Income Tax (ADFIT) balances, the resulting Excess Deferred Federal Income Tax (EDFIT) balance, or the flow-back of the EDFIT to ratepayers.

**Q: Should the impacts of the TCJA on Cascade's revenue requirements be reflected in this case?**

A: Absolutely. At a minimum, the federal income tax expense included in Cascade's revenue requirement and the resulting increase or decrease in

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<sup>2</sup> Response Testimony of Donna M. Ramas, Exh. DMR-1T at 4:7 – 5:20 (with footnotes included, but numbering is not as reflected in Exh. DMR-1T).

<sup>3</sup> The official title of the TCJA is an Act "To provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018", which is commonly referred to as the Tax Cuts and Jobs Act, abbreviated as TCJA.

current rates ultimately ordered by the Commission should be determined based on the actual federal income tax rate in effect during the period new rates from this case take effect. It would be unfair to ratepayers to set rates based on a 35 percent income tax rate when that rate is no longer in effect and the current tax rate is 21 percent.

**Q: Aside from the amount of federal income tax expense that is included in net operating income, does the TCJA impact other components of the revenue requirement equation?**

A: Yes. The TCJA changed numerous provisions of the federal tax law. The TCJA also impacts the Company's ADFIT balances and resulting EDFIT. Additional impacts of the TCJA will be discussed further in the final section of this testimony.

**Q: How have you reflected the impacts of the TCJA in your exhibits?**

A: With respect to the revenue requirements and adjustments presented in Exhibits DMR-2 through DMR-6, I include federal income tax expense at the actual 21 percent federal income tax rate. I have not included additional impacts of the TCJA on revenue requirements beyond the reduction in the FIT rate on federal income tax expense in Exhibits DMR-2 through DMR-6.

4. The following is an excerpt from Ms. Ramas's Response Testimony, Section VI (Additional TCJA Impacts):<sup>4</sup>

**Q: Did Cascade provide information regarding all of the impacts of the TCJA on the various components of its revenue requirements?**

A: In its original and supplemental responses to Bench Request 1, Cascade provided impacts of the reduction to the FIT rate on the income tax expense for the adjusted 2016 test year in its filing. The response also provided the

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<sup>4</sup> Ramas, Exh. DMR-1T at 51:14 – 56:16 (with footnotes included, but numbering is not as reflected in Exh. DMR-1T).

excess deferred federal income tax (EDFIT) reserve balances resulting from the reduction to the income tax rate, broken out between plant related EDFIT that reverses under the Average Remaining Asset Method (ARAM) required under the IRS normalization rules and the non-protected portion that does not fall under the IRS normalization rules. While the plant related EDFIT that is protected under the IRS normalization rules will be amortized under the ARAM methodology over the remaining regulatory lives of the associated property, the Company has proposed that the non-protected EDFIT balance be amortized over 10 years. The information provided by the Company in the supplemental response to Bench Request 1 and attachment “BR-01(02) Supplemental.xlsx” identifies the estimated amortization of the protected EDFIT under the ARAM as approximately \$2.19 million in 2018, and the amortization of the non-protected EDFIT balance as \$1,017,702 annually. These amounts are on a total Cascade basis. The response indicates that the Washington Plant allocation factor is 77.24 percent, which would result in a \$1.7 million amortization of the protected portion ( $\$2.19\text{M} \times 77.24\%$ ) and \$786,073 amortization of the non-protected portion ( $\$1,017,702 \times 77.24\%$ ) on a Washington basis, or a combined amortization impact of approximately \$2.5 million.

**Q: Your recommended revenue requirement for Cascade is based on the current FIT rate of 21 percent. What federal income tax rate is currently factored into the rates Cascade is currently collecting?**

A: Current rates were established when the FIT rate was 35 percent. Thus, during the current period, Cascade is collecting revenues from customers that were established based on the 35 percent FIT.<sup>5</sup> Beginning January 1, 2018, Cascade’s actual income tax expense is based on the current FIT rate of 21 percent.

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<sup>5</sup> It is not clear what amount is factored into current base rates for income tax expense as Cascade’s most recent rate case, Docket UG-152286 was resolved through a Joint Settlement Agreement and the income tax expense was not specifically identified in the agreement.

**Q: Has the Company estimated the excess amount of income tax expense it will collect from customers in 2018, as a result of the reduced FIT rate not being reflected in current rates charged to its Washington ratepayers?**

A: The Company has assumed that new rates from this case will take effect August 1, 2018. As a result, the Company will be over-collecting income tax expense in rates for an eight-month period, from January 1, 2018, to July 31, 2018. In Cascade's supplemental response to Bench Request 1(C), Cascade estimated the tax benefit resulting from the difference in the 35 percent FIT rate factored into current rates and the actual current 21 percent FIT rate as \$1,394,552. The Company provided its calculation of the estimated tax benefit in attachment "BR-01(04) Supplemental.xlsx" provided with its supplemental response to Bench Request 1.

In calculating the \$1,394,552 estimated tax benefit over the period January 1, 2018 through July 31, 2018, the Company used the amount of income tax expense for its adjusted 2016 test year based on the 21 percent FIT rate, which it presented in "BR-01(01) Supplemental.xlsx." The Company's calculation is shown on Exhibit DMR-7, column (A). In response to Bench Request 1(C), Cascade indicated that it will not be able to provide the final actual income taxes for 2018 "until the 2018 tax return is complete late in 2019." The Company asserts in its response that its use of the income tax expense for its adjusted test year in calculating the impacts is a reasonable proxy for estimating the amount of tax benefit.

**Q: Does your adjusted test year income tax expense differ from the amount calculated by Cascade?**

A: Yes. Each of my recommended revisions to Cascade's proposed adjustments and each of the adjustments recommended in this testimony impact the adjusted test year income tax expense. As shown on Exhibit DMR-4, in the final column on page 2, my adjusted test year income tax expense, based on the current FIT rate of 21 percent, is \$4,543,207, which

is \$957,217 greater than Cascade's adjusted test year amount of \$3,585,990. As shown on Exhibit DMR-7, column (B), if the amount of adjusted test year income tax expense is revised to reflect Public Counsel's adjusted amount in the Company's calculation of the estimated tax benefit for the period January 1, 2018, to July 31, 2018, the estimated tax benefit increases from the \$1,394,522 calculated by Cascade to \$1,766,803.

**Q: What has Cascade proposed with regard to the excess federal income taxes currently being collected in rates?**

A: The Company proposed in its supplemental response to Bench Request 1(D) that the impacts of the TCJA on the 2018 results of operations for the period January 1, 2018, through the anticipated rate effective date from this proceeding (estimated as August 1, 2018) be treated as a period cost and included in the 2018 results of operations. Cascade proposes that these results would be incorporated into Cascade's existing earnings sharing mechanism. The Company proposes that 100 percent of the earnings in 2018 above its authorized rate of return be flowed-back to customers through the earnings sharing mechanism established in the Settlement Agreement in Docket UG-152286. The Company would remove the 50 percent sharing of over-earnings between shareholders and ratepayers to instead reflect a 100 percent return of the excess earnings to customers for 2018 under its proposal. Cascade proposes to use some of the over-collected tax to "mitigate the impacts of regulatory lag."<sup>6</sup> Cascade further states that it anticipates that it will not earn its authorized return in 2018; thus, the over-collected federal income taxes would not be returned to Washington ratepayers under Cascade's proposal.

Public Counsel believes all of the over-collected federal income taxes resulting from the TCJA should be flowed-back to ratepayers. Ratepayers are currently paying a higher amount for income taxes in rates

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<sup>6</sup> Cascade Supplemental Response to Bench Request 1(D) (Jan. 29, 2018).  
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than the amount of income tax expense Cascade is actually incurring. It is Public Counsel's position that 100 percent of the over-collection should be returned to ratepayers through either a separate mechanism or through a deferral to be returned to ratepayers at a future time.

**Q: Are you taking a position at this time regarding whether the treatment proposed by Cascade in its supplemental response to Bench Request 1 should be adopted?**

A: As previously indicated, I do agree that the revenue requirements resulting from this case should be calculated based on the 21 percent FIT rate currently in effect. With regard to the treatment of the excessive income taxes currently being collected in rates, and the appropriate treatment of the flow-back of the EDFIT, I am not taking a position at this time, except to recommend that 100 percent of the amount of income taxes being over-collected from ratepayers should be return to ratepayers and a regulatory liability should be established if amortization of EDFIT is not included in rates in this case.

The Company's supplemental response to Bench Request 1 was submitted January 29, 2018, which is less than three weeks before this testimony is being filed. The amounts presented by Cascade in its response have not been fully vetted and include some assumptions. Cascade's response also included several proposals regarding the treatment of the excess taxes currently being collected and the amortization of the EDFIT balances. The Company has not filed supplemental testimony thoroughly explaining its proposals.

Public Counsel will review the positions taken by the various parties in this proceeding, as well as Cascade's rebuttal testimony, and may cross examine witnesses at hearings on the impacts of the TCJA. However, if the Commission does not include the amortization of the EDFIT in the revenue requirements resulting from this case, I do recommend that the amortization

be deferred as a regulatory liability and addressed in Cascade's next rate case.

**Q: Cascade indicates in its supplemental response to Bench Request 1(C) that the amortization of EDFIT has minimal impacts on rates or the outcome of this rate case. Is the impact of the EDFIT amortization minimal?**

A: No. As indicated above, using the Washington Plant allocation factor of 77.24 percent, the amounts presented by the Company would result in a \$1.7 million amortization of the protected portion of the EDFIT (\$2.19M x 77.24%) in 2018 and \$786,073 annual amortization of the non-protected portion (\$1,017,702 x 77.24%) on a Washington basis, or a combined amortization impact of approximately \$2.5 million. It is not clear why the Company contends that the amortization of the EDFIT "has minimal impacts on rates or the outcome of this rate case...." The Commission could consider including this annual amortization in rates in this case with the amortization period associated with the non-protected EDFIT beginning with the rate effective date from this case. The amount could then be subject to review in the next rate case, allowing more time to review the impacts, with a true-up in the next rate case. However, if the Commission opts to require Cascade to defer the impacts as a regulatory liability to the next rate case, then this case would not be impacted by the EDFIT amortization.

## II. DONNA RAMAS'S CROSS ANSWERING TESTIMONY

5. Ms. Ramas addressed the TCJA in her Cross-Answering Testimony, Exhibit DMR-42T, which is being filed along with these comments on Bench Request 1. The following is an excerpt from Ms. Ramas's Cross-Answering Testimony, Section V (Bench Request 1 – TCJA):<sup>7</sup>

**Q: Did you address the impacts of the TCJA in your response testimony?**

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<sup>7</sup> Ramas, Exh. DMR-42T at 14:3 – 18:5 (with footnotes included, but numbering is not as reflected in Exh. DMR-42T).



A: Yes. As indicated in my direct testimony, Public Counsel's recommended revenue requirement was based the 21 percent federal income tax rate resulting from the TCJA. Additional impacts of the TCJA beyond the impact of the reduction in the federal income tax rate on test year income tax expense were addressed at pages 51 through 56 of my response testimony.<sup>8</sup> Page 55 of the testimony, lines 6 through 11, stated:

With regard to the treatment of the excessive income taxes currently being collected in rates, and the appropriate treatment of the flow-back of the EDFIT, I am not taking a position at this time, except to recommend that 100 percent of the amount of income taxes being over-collected from ratepayers should be returned to ratepayers and a regulatory liability should be established if amortization of EDFIT is not included in rates in this case.

Additionally, in addressing the Company's proposal that the impacts of the TCJA being realized from the January 1, 2018, effective date through the date of new rates resulting from this case be treated as period costs that are included in the 2018 results of operations and incorporated in the existing earnings sharing mechanism, I stated as follow:

Public Counsel believes that all of the over-collected federal income taxes resulting from the TCJA should be flowed-back to ratepayers. Ratepayers are currently paying a higher amount for income taxes in rates than the amount of income tax expense Cascade is actually incurring. It is Public Counsel's position that 100 percent of the over-collection should be returned to ratepayers through either a separate mechanism or through a deferral to be returned to ratepayers at a future time.<sup>9</sup>

My testimony also indicated that the amounts presented by Cascade in its January 29, 2018 supplemental response to Bench Request 1 had not been fully vetted. The response included assumptions and several proposals regarding treatment of the excess taxes being collected, the amortization of

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<sup>8</sup> Ramas, Exh. DMR-1T at 51:14 – 56:16.

<sup>9</sup> *Id.* at 54:20 – 55:2.

the EDFIT balances, and that the Company had not filed supplemental testimony thoroughly explaining its proposals.<sup>10</sup>

**Q: On March 9, 2018, the Commission issued Order 05 in this docket granting Staff's motion requesting the opportunity to respond to Bench Request 1. Do you wish to supplement the information contained in your response testimony regarding the Company's response to Bench Request 1?**

A: Yes. I recommend that the Commission include the flow-back of the EDFIT in the revenue requirements resulting from this case. Since the EDFIT balances are known, and Cascade was able to use its Powertax System to determine the amount of reduction to the plant-related EDFIT (i.e., flow-back of plant-related EDFIT) that will occur during 2018 under the Average Remaining Asset Method (ARAM) required under the IRS normalization rules, there is no need to exclude the flow-back from the revenue requirements resulting from this case.

In its First Supplemental Response to Bench Request 1, the Company provided the 2018 reduction in the plant related Excess Deferred Income Tax (EDIT) balance using the ARAM for both the portion of the EDFIT protected under the IRS normalization rules and the non-protected portion of the plant-related EDFIT. The Commission has the option of amortizing the non-protected, plant-related EDFIT balances over a period of its choosing and is not required to use the ARAM for that portion.

In response to Public Counsel Data Request 124, provided as Exhibit DMR-46, the Company provided a breakdown of the protected and non-protected portion of the plant-related Excess Deferred Income Taxes as of December 31, 2017. Since the vast majority of the balance is protected under the normalization rules, I do not oppose utilizing the ARAM in amortizing the entire plant-related EDIT balance. The Commission also has

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<sup>10</sup> *Id.* at 55:12-18.

discretion regarding the amortization period to apply to the non-plant related EDIT balances. The Company has proposed a 10-year amortization period for the non-plant related EDIT balances. While the Commission may shorten the amortization period if it so chooses, I do not oppose the Company's proposed 10-year amortization period. Presented below is the impact on the Company's revenue requirements if the amortization of the Excess Deferred Income Taxes are included in the revenue requirements in this case. This is based on the Company's calculated annual reduction to the plant-related EDIT under the ARAM method for both the protected and non-protected plant-related EDIT balances, as well as a 10-year amortization of the non-plant related EDIT balances. As shown below, the result would be an additional \$2,546,360 reduction to current rates.

<u>Description</u>	<u>Amount</u>
2018 Reduction in Plant Related EDIT	1,699,492
Amortization of Non-Plant EDIT	789,473
Total Annual Amortization of EDIT	2,488,965
WA Allocation Factor	77.24%
Annual Amortization, WA basis	1,922,477
Revenue Conversion Factor	0.75499
Revenue Requirement Impact	<u>2,546,360</u>

There are no compelling reasons that I am currently aware of for not including the above amortizations of the Excess Deferred Income Taxes in the determination of revenue requirements in this case. In fact, in its Second Supplemental Response to Bench Request 1 provided on March 15, 2018, Cascade agrees that the reversal and amortization of the Excess Deferred Federal Income Taxes should be included in this case as a pro forma adjustment that reduces income tax expense. In a spreadsheet provided with its Second Supplemental Response to Bench Request 1, the Company included the pro forma adjustment to income tax expense, reducing the

income tax expense by the \$1,922,477 shown in the above table.<sup>11</sup> The Commission could increase this impact by shortening the amortization period for the non-plant related and the non-protected plant related EDIT balances at its discretion.

**Q: Is it still Public Counsel's position that the excess income taxes being recovered in rates from January 1, 2018, to the rate effective date of new rates from this case be returned to ratepayers?**

A: Yes, it is. There are three options of which I am aware for achieving this: (1) The amount could be returned to ratepayers through a separate mechanism, (2) the amount could be deferred and returned to ratepayers at a future time, or (3) the amount could be amortized and included as a reduction to revenue requirements as part of this proceeding.

### III. CONCLUSION

6. The TCJA has a significant effect on utility rates by reducing a major cost component of regulatory ratemaking. The benefits of this cost reduction comes in multiple forms: reduction of Cascade's tax liability and returning EDFIT to customers. Reduction of the tax rate is currently known, and to correct the tax rate embedded in rates is straightforward. Thus, the benefit of the lower tax rate should be immediately implemented with new rates.
7. Return of EDFIT is more complicated, but the issue is coming more into focus. As Ms. Ramas testifies, there are several ways the Commission can address EDFIT to benefit ratepayers, including deferring excess amounts collected from ratepayers starting on January 1, 2018 for future ratemaking treatment.
8. Public Counsel believes the Commission's Bench Request 1 is an important step in

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<sup>11</sup> The spreadsheet provided with the Second Supplemental Response to Bench Request 1 also identified the revenue requirement impact of the pro forma adjustment as \$2,546,351: The \$2,546,351 is within \$9 of the \$2,546,360 revenue requirement impact presented in the above table, with the difference attributable to rounding.

determining the appropriate rate impact. That rate impact should be decided in Cascade's pending general rate case, and EDFIT should be returned to customers via a rider mechanism that will return the excess ADFIT in its entirety to customers.

9. Public Counsel appreciates the opportunity to offer these comments.

DATED this 23rd day of March 2018.

ROBERT W. FERGUSON  
Attorney General



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