

AVISTA CORP.
RESPONSE TO REQUEST FOR INFORMATION

JURISDICTION:	WASHINGTON	DATE PREPARED:	1/11/2018
CASE NO.:	UE-170485 & UG-170486	WITNESS:	Mark Thies
REQUESTER:	UTC Staff	RESPONDER:	Liz Andrews/Don Falkner
TYPE:	Bench Request	DEPT:	State & Federal Regulation
REQUEST NO.:	Bench Request No. 1	TELEPHONE:	(509) 495-8601
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REQUEST:

Please provide the following:

- A. Accumulated Deferred Federal Income Tax (ADFIT) balance as of December 31, 2017.
- B. The amount of excess deferred income tax reserve as described in IRC Sec 168(i)(9)(A)(ii) as of December 31, 2017, to comply with the TCJA.
- C. The amount of excess deferred income tax expense the Company is currently collecting as of January 1, 2018, until the anticipated effective date of this general rate case.
- D. A proposed amortization schedule for parts B and C of this bench request along with a supporting rationale for each schedule. Please identify and describe the amortization assumption, e.g., composite, average rate, or other alternative method.
- E. For the current proceeding, provide an updated revenue requirement based on the Company's rebuttal position that accounts for the anticipated impacts of the TCJA.
- F. In the event that all impacts of the TCJA are not fully known to the Company by the due date set forth in this bench request, a projected date by which the Company intends to file an accounting petition to address the impacts.
- G. Supporting workpapers in electronic format with all formulas and links intact. See WAC 480-07-510(3)(e).

RESPONSE:

A.-G. For the reasons outlined below, the Company at this time is not able to quantify all of the impacts of the Tax Cuts and Jobs Act (TCJA). Nevertheless, all of the benefits associated with the costs paid by customers related to the TCJA will be returned to customers as discussed in this response.

The Company is in the process of evaluating the impacts of the new legislation (H.R.1 — Tax Cuts and Jobs Act) signed into law December 22, 2017, with most provisions going into effect on January 1, 2018. The Act contains provisions that impact regulated utilities' federal tax obligations, including a reduction to the corporate income tax rate. The Company is preparing to comply with the financial accounting requirements of Accounting Standards Codification (ASC)-740 which requires recognition of the effect of tax law changes to be recognized in the period of enactment, in this case, December 2017. The Accumulated Deferred Federal Income Tax (ADFIT) balance as of December 31, 2017 is not finalized at this time as the Company is still closing and additional time is necessary to comply with ASC-740 as of December 2017.

Due to the lengthy and complex nature of the TCJA, it is not possible at this time to identify all specific changes in Avista's federal tax obligations that may be impacted by the passage of the TCJA law. The Company is working with its tax consultants to ensure the impacts of the tax code revisions are appropriately calculated.

There are numerous provisions, with the primary provision being the reduction in the federal corporate tax rate from 35% to 21%. However, this is only one aspect of the expected impact of the tax code reform and should not be considered in isolation. For example, the change in the federal corporate income tax rates results in excess deferred income tax assets and liabilities which must be revalued, as well as other possible expenses that may no longer be deductible, and impacts on future cash flows which will impact financing levels.¹

Avista's current retail rates (and its proposed rebuttal revenue requirement position in this general rate case proceeding) assume a federal corporate tax rate of 35 percent. The revised corporate tax rate in the TCJA for 2018 and going forward is 21 percent, which will reduce current and deferred income tax expense customers currently assume in cost of service. It will also have an impact on the Company's ADFIT balance currently included in rate base (i.e., as ADFIT balances decline, rate base balances increase).

As it relates to our regulated operations, the Company is in the process of determining the overall tax benefit of the TCJA in the following areas:

1. The current and deferred income tax expense and conversion factor (or gross up to cover tax expenses) will change as a result of lowering the tax rate from 35% of taxable income to 21% of taxable income - The TCJA benefit to Washington customers, when known, ultimately will offset a portion of the increase in base rates proposed by the Company on rebuttal in this general rate case proceeding.
2. Deferred tax amounts are required to be revalued at the lower corporate rate (21%). The revaluation for both plant and non-plant amounts associated with regulated utility operations results in a balance sheet reclassification from deferred tax to deferred regulatory assets or liabilities. (Amount of excess deferred federal income tax reserve as described in IRC Sec 168(i)(9)(A)(ii) as of December 31, 2017.) – This will impact plant and non-plant related regulatory balances, both increasing and decreasing the overall TCJA benefit for customers. This is under evaluation and Washington's jurisdictional electric and natural gas benefit of these items are currently not available. As a part of this item, amortization of deferred tax amounts that represent the difference between the historical 35% rate and the revised 21% rate need to be determined. For plant-related excess deferred income tax expense, the Company anticipates this would be amortized in accordance with the TCJA's average rate assumption method (ARAM). (The Company estimates the ARAM for Avista results in an amortization period of approximately 36 years.) For non-plant related excess deferred income tax expense, further review is necessary to determine the appropriate amortization schedule. The overall benefit to be returned to Washington electric and natural gas customers as a result of this item has not been finalized at this time. This is an important aspect of the new law, for if the ARAM methodology for deferred taxes is not properly implemented, Avista will lose the benefit of Accelerated Tax Depreciation.
3. Lastly, it also has an impact on pro formed net plant, including the overall impact on accumulated deferred federal income tax balances of reflecting the TCJA (possibly increasing overall net rate base, and increasing annual revenue requirement).
4. The following are some of the complications that prevent a certain determination of the tax impact at this time:

¹ Because we have not yet been able to calculate all of the benefits related to the TCJA, the Company cannot yet publically release any "partial" information without triggering certain filings with the Securities and Exchange Commission.

- i. Financial closing for year-end 2017 is still in progress, and not is completed, nor audited;
- ii. All the year-end accounting is being done at the Company's system level, not service and jurisdictional levels (going to those additional levels of detail requires additional time to complete);
- iii. Not properly capturing deferred tax turnaround using the prescribed Average Rate Adjustment Mechanism in regulated customer rates would subject the Company to a normalization violation which would eliminate our ability to take advantage of accelerated tax depreciation;
- iv. The non-excess deferred tax balance will be growing at a slower pace than previously projected due to new deferred taxes accumulating at the lower 21% rate versus 35%; which will create upward rate pressure;
- v. The excess deferred taxes will reverse over time, which will also reduce deferred tax balances, creating additional upward rate pressure;
- vi. Utilities have been exempted from the 100% capital expensing regulations, as well as the limitations on the deductibility of interest expense, however, previously anticipated Bonus Depreciation for 2018 and 2019 has been eliminated; and
- vii. With the very limited amount of time since the legislation has been signed into law, we are not aware if the IRS has begun addressing directive treasury regulations associated with implementing the various aspects of the new tax legislation in H.R. 1, and the Company cannot anticipate what changes those might hold for implementation.

This overall evaluation is an extensive task. In the meantime, the Company proposed a regulatory deferred accounting process to capture the benefits of the TCJA until such time as the benefits are reflected in base rates. To that end, on December 29, 2017, the Company filed with the WUTC separate electric and natural gas "Petition[s] for an Order Authorizing Deferral of Federal Income Tax Expenses for the Effects of Revisions of the Federal Income Tax Code Upon Avista's Cost of Service." In each Petition, the Company requests 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 caused by enactment of the tax reform. Since the federal income tax code changes are effective beginning January 1, 2018, Avista would defer the impact of the changes to federal income tax expenses beginning in January 2018 until all benefits have been captured through the deferral and refunded to customers through a special tariff. Avista fully expects that all the financial impacts of changes to the federal tax code will be addressed in a manner that properly captures those impacts and are properly incorporated in customers' rates so that customers receive the benefits associated with all costs paid by customers.

As it relates to the revenue requirement requested by the Company in this rate case proceeding, the Company is in the process of determining the overall impact of the TCJA on its request for rate relief. It presently believes that it can complete its analyses before the end of March 2018. The Company proposes that by March 30, 2018², in this Docket (UE-170485/UG-170486), it will file a report with the Commission providing the requested information in items A. - G. of this Bench Request, including its estimated overall benefit to customers of the TCJA along with all supporting workpapers. This will provide an opportunity

² March 30, 2018 is consistent with that proposed by the Idaho Public Utilities Commission (IPUC) Staff in its Staff Memo to the IPUC on January 5, 2018. IPUC Staff's memo proposes that "By Friday, March 30, 2018, [each utility will] file a report to identify and quantify all tax changes individually. Each utility's report must include proposed rebate tariff schedules that show the revenue requirement impacts from the Act, with the differences between the law in effect on December 31, 2017 and the law in effect on and after January 1, 2018."

for the Commission and interested parties to audit this information, and if satisfied, to allow such tax benefit to be passed through to customers by May 1, 2018 – at the same time as new rates are effective in this proceeding. This would avoid the need to increase rates as a result of this case, only to lower them shortly thereafter once the benefits of tax reform have been calculated. In short, it would be preferable to synchronize these rate adjustments if possible.

To that end, the Company would file a separate rebate tariff, effective May 1, 2018, the overall benefit to customers of the TCJA, as well as include the return of the January – April 2018 deferred balance owed customers. This separate rebate tariff would remain in place until such time as any deferred balances have been returned to customers and the impact of the TCJA are reflected in base rates. This electric and natural gas rebate tariff will subsequently be revised effective May 1, 2019 and May 1, 2020 to reflect the benefits of the TCJA associated with years 2 and 3 of the rate plan. By proceeding in this manner, the benefits reflected through this separate rebate tariff will serve to offset a portion of the new rates implemented on May 1, 2018 (and the subsequent changes effective May 1, 2019 and May 1, 2020). Otherwise customers may face the prospect of multiple rate changes, both up and down, only contributing to customer's confusion.³

Apart from any tax benefits that will accrue to customers, it is important at this time for the Commission to continue with the resolution of all issues in this current general rate case proceeding, in order to establish current levels of expense for cost recovery for Avista effective May 1, 2018, including updated levels of utility plant, power supply costs, and other utility expenses/revenues. Decisions on these issues must be made, irrespective of the final resolution of the tax changes. The separate rebate tariff, as proposed by Avista, the amount of which to be determined by March 30, 2018, would capture the TCJA benefits for customers, also effective May 1, 2018. This would ensure customers were to receive the benefit of the TCJA, while establishing new base rates for Avista.

Company witness Mr. Mark Thies will be available at the hearing to respond to questions and concerns.

³ At the time of the Company's filed report on March 30, 2018, the Company will describe how it proposes to spread the tax benefit to customers and over what time period for each portion of the tax benefit and deferred balance.