Agenda Date: December 28, 2018
Item Number: A1

Docket: UG-171219
Company: Pacific Power & Light Company

Staff: David Panco, Regulatory Analyst
Chris McGuire, Assistant Director – Energy Regulation

Recommendation

Issue an order in Docket UG-171219 approving Pacific Power & Light Company's petition as amended on November 20, 2018, authorizing Pacific Power & Light Company to: (1) pass back to customers the benefits of lower federal income tax rate, and (2) defer excess deferred income taxes (EDIT). Take no action on the addition of Schedule 197, Federal Tax Act Adjustment, to the company's tariff WN U-75, allowing the revisions to become effective January 1, 2019, by operation of law.

Background

On December 22, 2017, the Tax Cuts and Jobs Act (TCJA) was signed into law, with the provisions of the law becoming effective January 1, 2018. Most significantly, the TCJA reduced the federal corporate tax rate from 35 percent to 21 percent. The effect of this change in federal tax rate not only reduced annual tax expense utilities pay to the IRS, it also required utilities to re-value the deferred federal income tax liability companies carried on their books. This re-valuation reduces the deferred federal income tax liability but also creates an excess deferred income tax liability (EDIT) that represents past over-collection of deferred tax expense. The EDIT liability is owed back to customers.

From a regulatory perspective, the TCJA created two general requirements: (1) utilities must pass the benefit of the lower tax expense on to ratepayers, and (2) utilities must identify the EDIT liability and return those dollars to ratepayers in a manner consistent with federal normalization rules and commission policy.

On December 28, 2017, Pacific Power & Light Company (Pacific Power or company) filed a petition requesting an order authorizing the company to defer the expected impacts of the TCJA. The petition would allow Pacific Power to defer for later return to customers both (1) the interim over-collection of taxes during the period January 1, 2018, to the date the 21 percent tax rate is embedded in base rates, and (2) EDIT.

On November 20, 2018, Pacific Power amended its petition to propose a mechanism for beginning to pass the benefits of the lower tax rate on to customers. The company would pass the interim over-collection back to customers through proposed tariff Schedule 197. Proposed Schedule 197 is provided as Exhibit 6 to Pacific Power's amended petition. The company proposes to continue deferring EDIT.

Discussion

Current Tax Expense

Pacific Power relies upon its most recent 2017 Commission Basis Report (CBR)[1] as the basis for calculating the revenue impacts of the TCJA. That report was modified to include plant additions for 2018, and then adjusted to reflect the changed federal tax rate and other identified effects of the TJCA. Staff agrees that this is reasonable as the test period from the company's last full general rate case was calendar year 2013, and using the 2017 CBR as a basis reflects the results of the multi-year rate plan resulting from its 2015 limited-issue rate filing.

Given that Pacific Power does not intend to file a general rate case until 2020 (wherein it would embed the 21 percent tax rate in base rates), the company proposes to use a rolling deferral and amortization process to return the benefit of the new tax rate to customers until base rates are reset. This would be implemented through proposed Schedule 197, Federal Tax Act Adjustment. Schedule 197 would return approximately $8.3 million to customers in the first year (calendar year 2019), representing a reduction of 2.3 percent to base revenues. The typical residential customer using 1,200 kWh per month will see a billing decrease of $2.89 per month.

Staff views Pacific Power's proposed Schedule 197 as a reasonable way to return the benefits of the lower tax rate to customers outside of a general rate case. The company has calculated the over-collection fairly and proposes to return all over-collections to customers in a timely manner.

Excess Deferred Income Taxes (EDIT)

In this petition Pacific Power proposes to continue deferring EDIT. Pacific Power has stated its intention to file a general rate case in 2020 with an effective date of January 1, 2021. The company proposes use of the EDIT regulatory liability to offset the impact of upcoming changes in depreciation expense.[2] The company estimates Washington customers' share of EDIT balances accrued by the end of 2020 to be approximately $36 million.

Staff supports Pacific Power's proposal to continue deferring EDIT. In general, staff is supportive of utilities attempting to mitigate intergenerational inequity by using regulatory liabilities to offset the rate impact of shortening the depreciable lives of major generation assets. However, staff believes resolution of intergenerational inequity is best done in the context of a general rate case where increasing depreciation expense can be offset by the regulatory liability.

Conclusion

Staff has reviewed the company's proposed filing and finds it is a fair and reasonable resolution of current net operating impacts of the reduction in income tax rates. Outstanding EDIT balances can be most comprehensively addressed in the company's next general rate case.

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[1] UE-180364

[2] UE-171219, Amended Petition, Heading preceding ¶8 and ¶8