



Department
of Public Service

Case 17-M-0815 Tax Cuts and Jobs Act of 2017 Technical Conference on Utility Accounting and Ratemaking

February 9, 2018

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Overview Of Proceeding

- The Tax Cuts and Jobs Act of 2017 (Tax Act) signed into law December 22, 2017
- Commission Institutes Proceeding December 29, 2017
 - Tax Act makes significant changes to the federal tax structure
 - Effects of the Tax Act on utilities will be material
 - Commission's intent to protect ratepayers' interest
 - Expressed goal is to ensure preservation of net benefits for ratepayers

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Milestones

- Informal request for information from major electric, gas, steam, water utilities, and all telephone companies, to identify and quantify the impact of the Tax Act
- Technical conference – February 9, 2018
- Staff issues whitepaper – March 29, 2018
- Parties' comments due 90 days later – June 27, 2018
- Commission to issue decision

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Goals For Today

- Gain a common and comprehensive understanding of how the Tax Act impacts New York State utilities
- Discuss appropriate ratemaking and related accounting
- Discuss how best to quantify the net benefits
- Explore financial implications of the Tax Act and related ratemaking
- Explore if ratemaking for all utilities and/or all industries should be the same

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Tax Act – Specific Changes

- Federal Income Tax Rate Change
- Repeal of Alternative Minimum Tax
- Elimination of Bonus Depreciation
- Treatment of Net Operating Losses
- Interest Deduction Limitations
- Meals and Entertainment Deduction Limitations
- Other

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Tax Rate Change

- Corporate top marginal tax rate reduced from 35% to 21% effective January 1, 2018

Impacts

- Lower current tax expenses
- Lower deferred tax accruals
- Excess accumulated deferred tax balances

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Elimination of Bonus Depreciation

- Bonus depreciation eliminated for utilities effective September 27, 2017

Impacts

- Return to MACRS tax recovery
- Lower cash flow

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Treatment of Net Operating Losses (NOL)

- Deduction of NOL will be limited to 80% of taxable income for losses arising in taxable years beginning after December 31, 2017
- NOL carryback is repealed and losses may be carried forward indefinitely

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Interest Deduction Limitation

- Interest deduction limitation does not apply to utilities, but may affect holding companies
- Interest costs assigned to utility should still be deductible
- May have to revisit tax sharing allocations with respect to consolidated structures

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Transition Issues

- Blended tax rates for non-calendar year filers
- 2017 return to MACRS tax depreciation
- Existing deferred income taxes
 - Revaluation
 - Reclassification of excess funded as a regulatory liability

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Excess Deferred Income Taxes

- Revaluation of deferred tax assets/liabilities at year end 2017
 - Excess deferred taxes recorded as regulatory assets/liabilities (grossed up)
- Asset related excess (protected)
- Other timing differences (unprotected)
- Segregation of balances on books

Ratemaking Issues to be Considered

- Goal to Capture Net Benefits for Ratepayers
- Measuring the Impacts of the Tax Act Changes
 - Use of actual operating results vs projections used in revenue requirement determinations for current rates
- Preservation of Net Tax Benefit
 - Deferred accounting should be employed to preserve the net benefits until rates are adjusted

Ratemaking Issues to be Considered (Cont'd)

- How to Preserve and/or Return Net Benefits
 - Deferred accounting until next rate case
 - Implement a sur-credit
 - Rate case re-opener
 - Use to offset other existing deferred regulatory assets (i.e. cleaning up balance sheet)
 - Other options

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Ratemaking Issues to be Considered (Cont'd)

- Considerations on Preservation/Returning Net Benefits
 - Utility cash flow/credit metrics implications
 - Reasonable timeframe to return benefits to ratepayers
 - Protected/Unprotected benefits
- Change in Law Provisions in Rate Plans
 - Reliance on generic proceeding outcome vs provisions in rate plans

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Ratemaking Issues to be Considered (Cont'd)

- Carrying charge rate to be applied to deferred balance
 - Pre-tax overall weighted average cost of capital
 - Other customer capital rate
 - Rate allowed in current rate plan
- Other Items Impacted by Tax Act Changes
 - Change in value of a basis point
 - Rate plan revenue adjustments and incentives
 - Earnings calculation used in earning sharing mechanism
 - FERC transmission rates
 - FERC interstate pipeline rates

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Ratemaking Issues to be Considered (Cont'd)

- Implementation of Tax Act Changes in Rates
 - Some companies currently have pending rate cases that will reflect tax law changes when new rates are implemented (NiMo, Central Hudson, Orange & Rockland, Suez Water Owego-Nichols)
 - Explore reasonable trigger point before a company is required to file an updated rate case or alternative mechanism to reflect Tax Act changes in customer bills
 - By a certain date
 - Based on the balance of accumulated deferrals (at what point does the regulatory liability become too large)
 - Other

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Financial Implications of Tax Law Changes

- Rating Agencies View of Tax Reform
 - Due primarily to reduced future cash flows, largely viewed as credit negative for utility industry
 - Moody's - negatively changes outlooks on 25 regulated utilities
 - S&P – impact on most issuers mild enough to offset effect and preserve ratings; trickier path for companies skirting edge of financial profile requirements
 - Anticipate most companies will actively manage their cash flow to debt ratios by issuing more equity or through regulatory relief, including stronger capital structures

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Financial Implications of Tax Law Changes (Cont'd)

- Looking at the Impact
 - Is impact material enough and durable enough to warrant stronger capitalization ratios
 - Is there a need to modify dividend policies or capital programs
 - Cost/benefit of how the impact is addressed
- Stabilization / Enhanced Cash Flow
 - Should other options be considered
 - Delaying and/or extending time frame of return of excess deferred FIT to ratepayers
 - New investments that benefit customers
 - Accelerated recovery of regulatory assets or capital programs

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Discussion

- Other Concerns
 - Needed system changes and/or updates to tax or accounting software
 - Other
- Utility and/or Industry Specific Considerations
 - Should the Commission give consideration to whether a utility has rates based on cost of service (energy & water) vs market based rates (telephone)
 - Should consideration be given to the size of a utility (small water companies)
- Other Comments and/or Questions

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Next Steps

- Staff Issues Whitepaper with Recommendations
- Parties Have 90 Day Comment Period
- Commission Decision

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