



Control Number: 47945



Item Number: 34

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# OPEN MEETING COVER SHEET

## COMMISSIONER MEMORANDUM

**MEETING DATE:** January 25, 2018

**DATE DELIVERED:** January 24, 2018

**AGENDA ITEM NO.:** 25

**CAPTION:** Project No. 47945 - Proceeding to Investigate and Address the Effects of the Tax Cuts and Jobs Act of 2017 on the Rates of Texas Investor-Owned Utility Companies

**ACTION REQUESTED:** Memo from Chairman Walker

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**Public Utility Commission of Texas**

TO: Chairman DeAnn T. Walker  
Commissioner Brandy Marty Marquez  
Commissioner Arthur C. D'Andrea

All Parties of Record (*via electronic transmission*)

FROM: Lisa Carter *LC*  
Commission Advising

RE: *Proceeding to Investigate and Address the Effects of the Tax Cuts and Jobs Act of 2017 on the Rates of Texas Investor-Owned Utility Companies, Project No. 47945, Accounting Order, January 25, 2018 Open Meeting, Item No. 25.*

DATE: January 24, 2018

Please find enclosed a memorandum regarding the above-referenced project, and an accounting order proposed by Chairman Walker. No other commissioner will file a memorandum in this docket.

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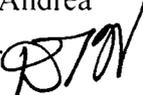


# *Public Utility Commission of Texas*

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## **Memorandum**

**TO:** Commissioner Brandy Marty Marquez  
Commissioner Arthur C. D'Andrea

**FROM:** Chairman DeAnn T. Walker 

**DATE:** January 24, 2018

**RE:** Open Meeting of January 25, 2018 – Agenda Item No. 25  
Project No. 47945 - *Proceeding to Investigate and Address the Effects of the Tax Cuts and Jobs Act of 2017 on the Rates of Texas Investor-Owned Utility Companies*

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After considering the various options for the Commission, I propose to take the following steps to address the federal legislation that passed related to federal income taxes.

I believe it is appropriate for the Commission to enter a deferred accounting order that requires the investor-owned electric, telecommunications, and water and sewer utilities for which the Commission has jurisdiction to establish rates, to begin recording a regulatory liability that reflects the following: (1) the difference between the revenues collected under existing rates and the revenues that would have been collected had the existing rates been set using the recently approved federal income tax rates; and, (2) the balance of excess accumulated deferred federal income taxes (ADFIT) that now exists because of the decrease in the federal income tax rate from 35% to 21%. The accounting order should also include a provision that requires each company to accrue, from the date of the order, carrying charges calculated at the company's weighted-average cost of capital on the balance of the regulatory liability, with the accrual of carrying charges continuing during the time period over which the liability is amortized through rates.<sup>1</sup>

I have attached a proposed order that I believe the Commission should adopt at the open meeting on January 25, 2018. This action will provide a mechanism to account for the difference in the tax liability created by the new legislation and the effect of that law on the accumulated balances of deferred tax liability carried on the utilities' books. The Commission can then determine the most effective manner to reflect the new, lower tax rates in rates. I believe the specific treatment of the deferred accounts should be addressed in future rate cases for each utility.

I also believe that the Commission Staff should review each electric utility on a case-by-case basis to determine the most appropriate action to take related to the reduction in the federal tax liability. However, I would like the Commission to consider some thoughts that I have on this

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<sup>1</sup> To the extent that a company can demonstrate that carrying charges on excess ADFIT balances are already reflected in rates as a result of such balances being used as an offset to the company's rate base, the calculation of carrying charges on those amounts of the excess ADFIT balance may not be required.

issue. In considering the matter, I have separated the various electric utilities into five categories for further analysis.

The first category consists of the three electric utilities that recently received rate orders: Oncor Electric Delivery Company, El Paso Electric Company, and Southwestern Electric Power Company. As the Commission is aware, the rate orders for each of these utilities includes language requiring the utility to create a regulatory liability account, and two of the orders also include a refund mechanism. Because the regulatory liability established for each of these utilities is not as comprehensive as the one that would be established by the attached proposed draft order, I propose modifying the regulatory liability requirements for the three utilities to conform to the attached proposed order.

I also believe it is important to achieve a reduction in the rates due to the new federal income tax liability. I have concerns with not adjusting the rates of these utilities at this time because of intergenerational ratepayer impacts due to the collection of the funds at this time and the refund of the amounts in the future. Further, I believe that the typical concerns with piecemeal ratemaking do not exist for these utilities due to the fact that the rates were very recently established.

Therefore, I would request that the three utilities work with the Commission Staff to address a limited, specific reduction to the recently established rates for the amounts collected related to federal income taxes. I believe that if the utilities are open to such a settlement, then the proceeding could be a simple reduction in the expense for federal income taxes with new rate schedules established for the various rate classes. If the utilities are not open to such a settlement, then I believe the Commission Staff should consider whether it is appropriate to file rate proceedings for each of the three utilities in order to ensure that the rates charged to the ratepayers are just and reasonable.

The second category for consideration is Southwestern Public Service Company, which has a pending rate proceeding. I anticipate that the parties will address the appropriate federal tax expense to include in rates in that proceeding. Therefore, I do not believe that the Commission needs to take any further action other than the deferred accounting order related to this utility at this time.

The third category relates to the two utilities that plan to file rate proceedings in May of 2018: Texas-New Mexico Power Company and Entergy Texas. Because both of these companies plan to file rate cases in the very near future, I believe it is best to implement the deferred accounting order and allow them to file rate cases in May as currently planned.

The fourth category includes the five transmission-only utilities: Cross Texas Transmission, Electric Transmission Texas, Lone Star Transmission, Sharyland Utilities, and Wind Energy Transmission Texas. I believe that the Commission should direct Commission Staff to review the impacts of the federal tax rate change on each of these utilities to determine whether rate cases are necessary. I would also request that each of the utilities consider voluntarily working with the Commission Staff to address this single issue. Therefore, in addition to the deferred

accounting order, I believe that these utilities should be addressed on a case-by-case basis by the Commission Staff to ensure that the rates charged to the ratepayers are just and reasonable.

This leaves for the fifth category the two remaining investor-owned electric utilities: AEP Texas and CenterPoint Energy Houston Electric. After reviewing preliminary information that I have received from the Commission Staff, I do not believe that the Commission Staff should initiate a proceeding related to the rates of AEP Texas, but instead should continue to monitor the earnings related to that utility. However, I believe that the Commission should consider initiating a rate proceeding for CenterPoint Energy Houston Electric at this time.

In Project No. 46910, *Year-End 2016 PUC Earnings Reports for Electric Utilities*, the Commission Staff addressed the earnings of CenterPoint Energy Houston Electric and did not recommend requiring a base rate case at that time. As discussed at the open meeting on October 26, 2017, I had concerns with the subsidization between the distribution and transmission rates for this company. However, I also had concerns with requiring a rate proceeding at that time due to the impacts of Hurricane Harvey on the expense of the utility.

It is my understanding that CenterPoint Energy Houston Electric intends to file in the near future a distribution cost recovery factor (DCRF) proceeding; therefore, the effects of the federal income tax legislation can be addressed in that proceeding for the distribution assets and rates. However, a DCRF proceeding will not address the impacts of the federal income tax legislation on the transmission rates charged by the utility. In my opinion, this will further skew the subsidization issues that affect the transmission rates charged by CenterPoint Energy Houston Electric. Although I continue to have concerns about the impacts of Hurricane Harvey on a test year, I believe that there are too many factors that show there is a need for a rate review at this time. Therefore, I recommend that the Commission require CenterPoint Energy Houston Electric to file a comprehensive rate proceeding within the next 120 days.

As to the telecommunication utilities, I believe that the Commission Staff should address each such utility through the process to be adopted in the current rulemaking to implement Senate Bill 586 from the last legislative session - Project No. 47669, *Rulemaking to Revise 16 Tex. Admin. Code § 26.404 Small and Rural Incumbent Local Exchange Company Universal Service Plan Pursuant to S.B. 586*. I do not believe any action for the telecommunication utilities should be taken at this time except for the deferred accounting order under consideration.

As to the water and sewer utilities, in addition to the deferred accounting order, I believe that the Commission should direct Commission Staff to review the impacts of the federal tax rate change on each of these utilities to determine whether rate cases are necessary. Thus, such utilities should be addressed on a case-by-case basis by the Commission Staff to ensure that the rates charged to the ratepayers are just and reasonable. The focus at this time should be on the class A and larger class B utilities. After that review is complete, then the Commission Staff should look at a sample of the class C and smaller class B utilities and report back to the Commission whether there is a need to further address these utilities.

I look forward to discussing these issues with you at the open meeting.

**PUC PROJECT NO. 47945**

**PROCEEDING TO INVESTIGATE AND ADDRESS THE EFFECTS OF THE TAX CUTS AND JOBS ACT OF 2017 ON THE RATES OF TEXAS INVESTOR-OWNED UTILITY COMPANIES** §  
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§  
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**PUBLIC UTILITY COMMISSION**  
  
**OF TEXAS**

**DRAFT PROPOSED ORDER  
RELATED TO CHANGES IN FEDERAL INCOME TAX RATES**

This Order addresses the change in the federal income tax rates on electric, telecommunications, and water and sewer investor-owned utilities in the State of Texas. Late last year, an act was passed that, in part, amends the Internal Revenue Code<sup>1</sup> by, among other things, reducing the federal income tax rate to be imposed on C corporations from 35% to 21%, effective January 1, 2018, as well as reducing the federal income tax rate on certain other entities.<sup>2</sup>

Through this Order, the Commission takes the first steps to reflect this lower tax rate in the utility bills of Texas customers. The Commission directs the Commission Staff to review each investor-owned utility in Texas, with input from interested stakeholders, on a case-by-case basis to determine the appropriate mechanism to adjust its rates to reflect the changes under the newly enacted federal tax law.

Until a rate change may be approved to adjust charges to Texas customers, the Commission issues this accounting order under its statutory authority to preserve any changes in the federal income tax expense charged by utilities until rates can be changed.<sup>3</sup> The Commission requires each electric, telecommunication, and water and sewer investor-owned utility, except as later stated in this Order, to record as a regulatory liability the following: (1) the difference between the revenues collected under existing rates and the revenues that would have been collected had the existing rates been set using the recently approved federal income tax rates; and, (2) the balance of excess accumulated deferred federal income taxes (ADFIT) that now exists because of the

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<sup>1</sup> Internal Revenue Code, 26 U.S.C.A. § 61 (West 2011 and Supp. 2014).

<sup>2</sup> Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, Pub. L. No. 115-97, 113 Stat. 2054 (Dec. 22, 2017).

<sup>3</sup> Public Utility Regulatory Act, Tex. Util. Code Ann. § 14.151 (West 2016 & Supp. 2017); Tex. Water Code Ann. § 13.131(a) (West 2008 & Supp. 2017).

decrease in the federal income tax rate from 35% to 21%. In addition, each utility must accrue, from the date of this Order, carrying charges calculated at the company's weighted-average cost of capital on the balance of the difference in revenues collected and the balance of excess ADFIT as calculated above, with the accrual of carrying charges continuing during the time period over which the liability is amortized through rates. However, to the extent that a company can demonstrate that carrying charges on excess ADFIT balances are already reflected in rates as a result of such balances being used as an offset to the company's rate base, the calculation of carrying charges on those amounts of the excess ADFIT balance may not be required.

The requirement in the Order to create a regulatory liability does not apply to Oncor Electric Delivery Company LLC, El Paso Electric Company, or Southwestern Electric Power Company, except as provided in this paragraph. These three utilities have previously been ordered by the Commission to establish a regulatory liability tracking the difference in the amount of federal income tax collected in current rates, and the amount of federal income tax calculated under the new federal income tax rates. Accordingly, these three utilities shall record the balance of excess ADFIT as a regulatory liability.

In addition, in reviewing the rates of water and sewer utilities, the Commission Staff should first focus on class A and the larger class B utilities. The Commission Staff should then take a sample of the class C and smaller class B utilities to determine the effect of the new tax law, and report the findings back to the Commission.

In accordance with the discussion in the Order, the Commission orders the following:

1. Each investor-owned electric, telecommunications, and water and sewer utility in the State of Texas, for which the Commission has jurisdiction, shall, starting the date this Order is signed, record as a regulatory liability the following: (1) the difference between the revenues collected under existing rates and the revenues that would have been collected had the existing rates been set using the recently approved federal income tax rates; and, (2) the balance of excess accumulated deferred federal income taxes (ADFIT) that now exists because of the decrease in the federal income tax rate from 35% to 21%. In addition, each utility must accrue carrying charges calculated at the company's weighted-average cost of capital on the balance of the difference in revenues collected and the balance of excess ADFIT as calculated above, with the accrual of carrying charges continuing during

the time period over which the liability is amortized through rates. To the extent that a company can demonstrate that carrying charges on excess ADFIT balances are already reflected in rates as a result of such balances being used as an offset to the company's rate base, the calculation of carrying charges on those amounts of the excess ADFIT balance may not be required.

2. The Commission Staff shall investigate each investor-owned utility in Texas, with input from interested stakeholders, on a case-by-case basis, as discussed in this Order, to determine the appropriate mechanism to adjust its rates to reflect the changes under the newly enacted federal tax law.
3. The Commission Staff shall report its findings regarding class C and smaller class B water and sewer utilities within six months of the signing of this Order.

Signed at Austin, Texas the \_\_\_\_\_ day of January 2018.

**PUBLIC UTILITY COMMISSION OF TEXAS**

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**DEANN T. WALKER, CHAIRMAN**

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**BRANDY MARTY MARQUEZ, COMMISSIONER**

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**ARTHUR C. D'ANDREA, COMMISSIONER**