Date of Hearing: June 20, 2018

ASSEMBLY COMMITTEE ON UTILITIES AND ENERGY
Chris Holden, Chair
SB 1028 (Hill) – As Amended April 25, 2018

SENATE VOTE: 38-0

SUBJECT: Public utilities: rates: federal tax law changes

SUMMARY: This bill would require the California Public Utilities Commission (CPUC) to evaluate the effects of federal House Resolution 1 (corporate tax cuts) on the expenses and tax liabilities incurred by public utilities for payment of federal taxes and if the CPUC determines that the projected expenses and tax liabilities for federal tax are affected, it would require the commission to adjust the rates of the utility. Specifically, **this bill**:

1) Requires the CPUC to evaluate the full effect of the enactment of federal House Resolution 1 (H.R. 1; Public Law 115-97) upon the expenses and tax liabilities incurred by public utilities for payment of federal taxes.

2) Requires the CPUC to adjust the rates of the utility to reflect the changes in projected expenses and tax liabilities in light of the changes in federal law.

3) Applies the provisions of this bill to only those public utilities over which the CPUC exercises its authority to fix rates and only to the extent the revenue requirements of the utility are based upon the tax rates in effect at the time rates were fixed for the utility by the CPUC.

EXISTING LAW:

1) Defines a "public utility" to includes every common carrier, pipeline corporation, gas corporation, electrical corporation, telephone corporation, water corporation, sewer system corporation, and heat corporation, where the service is performed for, or the commodity is delivered to, the public or any portion thereof. (Public Utilities Code § 216)

2) Requires that all charges demanded or received by any public utility for any product, commodity or service be just and reasonable, and that every unjust or unreasonable charge is unlawful. (Public Utilities Code § 451)

3) Provides the CPUC with general, broad authority to regulate every public utility in the state. (Public Utilities Code § 701)

4) Authorizes the CPUC to require a public utility to correct any rates, practices, equipment or behavior that is unjust, unreasonable, unsafe, improper, inadequate, or insufficient. (Public Utilities Code § 761)

FISCAL EFFECT: According to Senate Appropriations Committee, the CPUC would incur costs occur regardless of the passage of this measure. According to the CPUC, the evaluations and rate adjustment included in this bill would result in a total fiscal impact of $787,183 for the following positions and contract services:

- $287,183 including Benefits and Operating Expenses and Equipment for one Public Utilities Regulatory Analyst V to assess annual federal tax liability, accelerated depreciation, and other financial impacts in all private electric and natural gas utility General Rate Cases and applications regulated by the Commission.

- $70,000 annually for a Business Services Officer III to administer contracts, issuing Request for Proposals, and coordinating administrative contract functions.

- Ongoing contracting costs of $500,000 per year for specialized federal tax law and financial cost analyses of federal corporate tax rate changes and of accelerated depreciation for businesses, and other financial impacts on all electric and natural gas utility General Rate Case and applications regulated by the Commission. These services will provide ongoing tax code expertise. Staying up to date on federal tax changes involves deep knowledge of the tax code and Internal Revenue Service rulings such as "private letters" which may impact regulated electric and natural gas utilities. For example, in the PG&E Transmission Owner Federal Energy Regulatory Commission rate case number 18, the estimated federal tax law change is a windfall of about $130 million out of about $1.8 billion that was not anticipated when this rate case began. Thus, the magnitude of funds that need to be returned to California ratepayers could be substantial.

BACKGROUND:

CPUC General Rate Cases (GRC) – The CPUC determines the amount a utility can charge, invest in and profit through an extensive general rate case which occurs every 3-5 years depending on the utility. The GRC is the CPUC's main opportunity to review utility operations, investments, and associated costs. The utilities tax burden is one factor in how much a utility can charge customers in rates. As the case with other expenses, income taxes are recoverable by the utility in their rates. Since utilities are allowed to charge customers for a set amount any change in taxes becomes either profit or loss for the utility. Generally any difference in the amount a utility is allowed to charge versus the amount it expends is recorded in a memorandum account. These accounts are corrected during the next GRC cycle.

Federal House Resolution 1 – Under the recent House Resolution 1 utilities are expected to receive lower taxes. Among other provisions, H.R. 1 significantly lowers corporate taxes from 35% to 21% and changes the rules for deducting equipment costs, but also exempts utilities from any limitations of deducting interest on loans, debt or credit. This means that utilities will be freer than other corporations to borrow money for infrastructure upgrades and could likely increase the demand for utility bonds. These changes in federal law under H.R. 1 lower the overall tax burden to the utilities.

What the CPUC is already doing – Prior to this bill the CPUC had directed all electric, gas and water utilities to track the savings from the federal tax law change in memorandum accounts.

Memorandum accounts are used by the CPUC regularly to track actual costs of a program. Under most circumstances the savings would be credited back to ratepayers in a future general rate case. The CPUC is also requesting the tax savings information from telephone carriers that are subject to general rate cases. The CPUC claims to be working on the most appropriate procedural mechanism to return the tax savings to ratepayers.

Other states – As a result of the corporate tax savings under H.R. 1 many states have already taken proactive measures to ensure customers benefit from utility savings. Kentucky, Michigan, Connecticut, Louisiana, Minnesota, Missouri, Montana, Oklahoma, South Dakota and West Virginia have started proceedings related to the passage of the federal tax cuts. In Oklahoma the Corporations Commission's administrative law judges have recommended that utilities pass the savings along to their customers. South Dakota's Public Utility Commission has determined that investor owned power and natural gas utilities should share the savings from the tax bill with customers. The Michigan Public Service Commission ordered utilities to study the tax cuts' impact and how they will pass the savings along to customers. In Montana the Public Service Commission ordered utilities to calculate the change in their tax liabilities and come up with proposals for applying their savings.[1] The attorneys general from 12 states signed a letter sent to FERC in January which called for an investigation into the "justness and reasonableness" of utility rates now that the tax cuts approved by Congress last month reduce the corporate income tax rate from 35% to 21%. The states include: New York, California, Connecticut, Illinois, Kentucky, Maryland, Massachusetts, Nevada, North Carolina, Rhode Island, Texas and Virginia. Public consumer advocacy offices and state regulatory agencies from Connecticut, Florida, Maine, Nevada, New Hampshire, Rhode Island and Vermont also are involved.

COMMENTS:

1) Author's Statement. According to the author's office, SB 1028 ensures any recent federal tax savings privately owned utilities receive are passed back to ratepayers. This bill applies only to utilities with near-exclusive rights to sell and operate within a given service area, and who have their rates set by the CPUC. Ratepayers pay the federal taxes of these utilities, and should receive the benefits of reductions in those taxes. States across the country have already called on their utilities to pass any savings on to ratepayers; SB 1028 would ensure the same is true for California. SB 1028 provides clear direction to the CPUC that any change to these utilities' taxes shall be adjusted for in rates.

2) Ratepayer Savings. Since ratepayers have already paid for the corporate taxes previously forecasted by the utilities, any tax savings would result in a profit for the utility. This bill would provide ratepayers with savings, to the extent they are warranted, due to the recently adopted adjustments in the federal corporate tax changes. These savings could come in many forms, depending on what mechanisms the CPUC uses to adjust rates. Some possibilities could be: rebates to ratepayers, using these savings to pay for future expenses or deductions in rates or requested expenses moving forward. With each utility being uniquely affected by the taxes, not all ratepayers may experience rate changes.

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[1] https://www.rtoinsider.com/tax-cut-and-jobs-act-opsi-utilities-83740/

3) Related Legislation. ACA 22 (McCarty, Ting, 2018) imposes a 10 percent surcharge on any qualified taxpayer's net income over $1 million. The surcharge will be deposited into the Middle Class Fiscal Relief Fund, with specified appropriations. A "qualified taxpayer" is defined as corporations subject to certain taxation, which appears to include utilities. The bill is pending referral in the Assembly.

REGISTERED SUPPORT / OPPOSITION:

Support

Office of Ratepayer Advocates
The City Of Lakewood
The Utility Reform Network

Opposition

None on file.

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