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UTILITIES COMMISSION

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Attorney for the Commission Staff

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE INVESTIGATION)	
INTO THE IMPACT OF FEDERAL TAX CODE)	CASE NO. GNR-U-18-01
REVISIONS ON UTILITY COSTS AND)	
RATEMAKING.)	COMMENTS OF THE
)	COMMISSION STAFF TO
)	TETON WATER'S TAX
)	REPORT

The Staff of the Idaho Public Utilities Commission comments as follows on Teton Water and Sewer Company's tax report filed in response to Order No. 33965.

BACKGROUND

On December 22, 2017, the President signed the Tax Cuts and Jobs Act of 2017 (the "Tax Act") into law with the effective date of January 1, 2018. The Tax Act reduced the federal corporate tax rate from 35% to 21%, which significantly decreases tax expenses for many utilities. The Tax Act also reduced the first level of income tax for many other filers from 15% to 12%. Commission-regulated utilities include tax expenses in their revenue requirements. The Commission then uses the revenue requirement to set fair, just, and reasonable rates. The Commission initiated this case to investigate whether to adjust utilities' rates and charges to reflect that the Tax Act has decreased the utilities' income tax expenses and revenue requirement. *See* Order No 33965. The Commission directed certain rate-regulated utilities to

file a report by March 30, 2018, that advises the Commission on how the Tax Act affects them.
Id.

UTILITY REPORT

Teton Water & Sewer Company (Teton Water or the Company) is a public utility that is part of this investigation. It provides domestic water services to 291 customers in the Teton Springs Golf and Casting Club Unit Development in Teton County, Eastern Idaho.

On February 2, 2018, the Company filed a report and provided a financial statement to show how the Tax Act affected its tax expense. The Company's report stated that Teton Water is a Limited Liability Company. Accordingly, for tax purposes, the Company's net income passes to the Company's owner and is taxed at the personal rate. The Company is, therefore, not affected by the Tax Act's decrease to the federal corporate tax rate. Instead, the Tax Act affects the personal tax rate bracket of the Company's owner.

Since the Company provides both water utility service and sewer service, and the Commission only regulates water utilities and not sewer companies, the Company filed a Profit and Loss financial statement covering the water utility side of its business for the operating financial period from January through December 2017. *See Attachment A.* The statement shows the Company generated \$158,776 of total income, and incurred \$115,953 in operating expenses and \$24,626 in other expenses. The Company's net income was \$18,197.

The Company identifies scenarios showing the impact of the Tax Act. At the Pre-Tax Act Personal tax rate of 25% (2016/2017), the tax expense would be \$4,549, at the Post-Tax Act Personal tax rate of 22% (2018), the tax expense will amount to \$4,003. The revenue requirement tax rate, when set at 15%, would cause a tax expense of \$2,730. The Company stated the Tax Act will not materially affect the Company's tax expense, and therefore rates should not decrease.

STAFF ANALYSIS

Staff thoroughly reviewed the Company's Profit and Loss financial statement and tax circumstances in the light of the Tax Act. In summary, upon reviewing the Company's filing, Staff determined the Tax Act will lower the Company's tax expenses by \$468 per year. Because the amount is so small, Staff recommends that the Commission not direct the Company to spread that benefit to customers through a water-rate decrease. Rather, Staff recommends that the

Commission order the Company to increase its annual contribution to the Emergency Reserve Fund, established in Case No. TTS-W-08-01 (Order No. 30718), by \$468. Staff's analysis and recommendations are further explained below.

The Company's filing reflects a net income of \$18,197. However, Staff disagrees with the classification for ratemaking purposes, and believes a different balance is more appropriate for some accounts on the Company's Profit and Loss financial statement. Staff also identifies the tax-impact scenarios differently. Attachment B illustrates the Staff's position and adjustments proposed for the Company's filing.

In the "Other Expenses" section of the Profit and Loss financial statement, the Company reported Interest Expense on Long-Term Debt of \$17,691. While the Company may have paid these expenses, the Company does not have debt approval from the Commission under Idaho Code §61-901 et. seq. Even if the Company had debt authority, the cost would be recovered in the Company's overall rate of return and not as an operating expense. The overall rate of return used to establish rates was based on a higher return on equity component and rate. Therefore, for ratemaking purposes, interest expenses should not be included. The effect of removing these expenses is illustrated on Attachment B, Column B.

In the Ordinary Income/Expense section of the Profit and Loss statement, the Company reported \$1,180 of income associated with the Water On/Water Off Service Fees account. The Company assessed these fees based on its tariff for voluntarily turning customers' water service on and off. These revenues are naturally unpredictable. Staff thus recommends that, for ratemaking purposes, this revenue should be shown as a three-year average. That average results in \$1,423 for Water On/Off Service Fees, as illustrated on Attachment C. The netted increase of \$243 is illustrated on Attachment B, Column C.

The Company's Profit and Loss Statement states that Water Connection Fees were \$11,204. These are one-time hookup fees assessed to new customers and are unpredictable. In addition, the Company reported that, as of March 22, 2018, it had no connections planned and no contact from realtors, builders, or property owners. Staff recommends these be removed for ratemaking purposes, as reflected on Attachment B, Column D. Hookup fees are now taxable under the Tax Act, so Teton Water should revise its hookup fee tariff to reflect the tax gross up. Staff will work with the Company to properly amend this tariff provision.

Lastly, Staff disagrees with the analytical tax scenarios presented on the Company's Profit and Loss financial statement of a Pre-Tax Act rate of 25% and Post-Tax Act rate of 23%.

Teton Water is a Limited Liability Company, which has been organized in the State of Idaho on November 21, 2012. *See* Order No. 32685 (Case No. TTS-W-12-01). For tax purposes, the Company follows the Internal Revenue Service (IRS) rule for “Owner of Single-Member LLC.” As a single-member LLC, the Company has elected not to be treated as a corporation, which renders the LLC a “disregarded entity,” and the LLC’s activities are reflected on the owner’s federal tax return. Because personal tax returns are proprietary, Staff assumes that a utility company’s income is the first income the owner receives and uses the IRS schedule appropriate to a single payer. Therefore, Staff recommends the Commission use the IRS tax schedule for an individual to establish tax rates for this Company. *See* Attachment D. Using this table, Staff calculated that the Company’s tax for 2017 to be \$3,273. *See* Attachment B, line 6. Using the similar table from the 2017 Tax Act, Staff calculated the Company’s tax expense to be \$2,805, as shown on line 7. This results in a reduction of \$468, as shown on line 8.

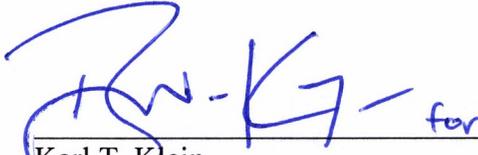
Staff does not believe this small change warrants reducing customer rates. As noted above, the Company has an Emergency Reserve Fund that was established in its last rate case, Case No. TTS-W-08-01. Staff thus recommends the Commission order the Company to increase its contribution to that Emergency Reserve Fund by \$468 annually, to a total contribution of \$7,435 annually.

STAFF RECOMMENDATIONS

Based on Staff’s review of the Company’s Profit and Loss Statement and the tax rates included in the Tax Cuts and Jobs Act of 2017, Staff recommends that the Commission recognize the tax savings for Teton Water to be \$468 annually. Staff further recommends that the Commission order the Company to contribute \$468 annually from tax savings to its surcharge account for the Emergency Reserve Fund.

Respectfully submitted this 5th

day of April 2018.


Karl T. Klein
Deputy Attorney General

Technical Staff: Joe Terry
Johan Kalala-Kasanda

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Cash Basis

Teton Water & Sewer Co.
Profit & Loss
January through December 2017

Ordinary Income/Expense	
Income	
600.000 · Water Income	
600.461 · Water Metered Sales Residential	102,872.84
600.462 · Water Metered Sales Commercial	7,648.00
600.463 · Water Metered Sales Multi-Family	35,872.00
600.475 · Water On / Water Off Service Fe	1,180.00
600.476 · Water Connection Fees	11,203.56
Total 600.000 · Water Income	<u>158,776.40</u>
Total Income	<u>158,776.40</u>
Gross Profit	158,776.40
Expense	
700.000 · Water Expense	
700.615 · Water - Purchased Power	11,133.41
700.616 · Water - Fuel for Power Product	267.92
700.618 · Water - Chemicals	6,635.60
700.621 · Water- Material & Supplies-O&M	18,416.01
700.627 · Water- Materials & Supplies-G&A	492.45
700.631 · Water - Contract Srvce-Profsnl	
001 · Regulatory Expense - IPUC	0.00
700.631 · Water - Contract Srvce-Profsnl - Other	15,686.40
Total 700.631 · Water - Contract Srvce-Profsnl	<u>15,686.40</u>
700.635 · Water - Contract Srvce-Testing	693.00
700.636 · Water - Contract Srvce - Other	52,760.42
700.641 · Water - Rents	699.60
700.656 · Water - Insurance Expenses	3,476.00
Total 700.000 · Water Expense	<u>110,260.81</u>
720.000 · WS - Unallocated Expenses	
720.610 · Unallocated - Bank Fees	2,771.34
720.620 · Unallocated - Operating Expense	20.24
720.630 · Unallocated - Postage	259.07
720.640 · Unallocated - Telephone	2,641.45
Total 720.000 · WS - Unallocated	<u>5,692.10</u>
Total Expense	<u>115,952.91</u>
Net Ordinary Income	42,823.49
Other Expense	
800.403 · Water-Depreciation Expense	144.00
800.408 · Taxes & Fees	
800.010 · Water - Regulatory Fees (IPUC)	329.00
800.011 · Water - Property Taxes	5,294.20
800.013 · Water - Other Taxes - DEQ	1,168.00
Total 800.408 · Taxes & Fees	<u>6,791.20</u>
900.000 · Interest Expense	
900.100 · Interest Exp on Long-Term Debt	17,691.13
Total 900.000 · Interest Expense	<u>17,691.13</u>
Total Other Expense	<u>24,626.33</u>
Net Income	<u>18,197.17</u>
Pre-Tax Act Personal Tax Rate (2016/2017) - 25%	\$ 4,549.29
Post-Tax Act Personal Tax Rate (2018) - 22%	\$ 4,003.38
Revenue Requirement Tax Rate - 15%	\$ 2,729.58

Teton Water Company
Tax Calculations and Adjustment
Calendar Year 2017

Attachment B
Case No. GNR-U-18-01
Staff Comments to
Teton Water's Tax Report
04/05/18

Line No.	Column	A	B	C	D	E
1	Income	\$ 158,776				\$ 147,816
2	Operating Expenses	(115,953)				(115,953)
3	Net Ordinary Income	42,823				31,863
4	Other Expenses	(24,626)	\$ 17,691			(6,935)
5	Net Income	18,197				24,928

6	Taxes 2017	\$ 3,273
7	Taxes 2018	\$ 2,805
8	Difference: Decrease in Tax Expense	\$ 468

Teton Water Company

<u>Year</u>	<u>Water on/off service fees</u>
2017	\$ 1,180
2016	1,416
2015	1,672
	<u>\$ 4,268</u>

3 Year Average	\$ 1,423
Filed amount	1,180
Adjustment	\$ 243

IRS TAX TABLE: Single taxable income tax brackets and rates

<u>Bracket - 2017</u>	<u>Rate - 2017</u>	<u>Tax Owed - 2017</u>	<u>Rate - 2018</u>	<u>Tax Owed - 2018</u>
0 - \$9,325	10%	10% of Taxable Income	10%	10% of taxable income
\$9,325 - \$37,950	15%	\$932.50 Plus 15% of the excess over \$9,325	12%	\$952.50 Plus 12% of the excess over \$9,525
\$37,950 - \$91,900	25%	\$5,226.25 Plus 25% of the excess over \$37,950	22%	\$4,453.50 plus 22% of the excess over \$38,700

Source: IRS.gov

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 5th DAY OF APRIL 2018, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF TO TETON WATER'S TAX REPORT**, IN CASE NO. GNR-U-18-01, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

JON PINARDI MANAGING PAR
TETON WATER & SEWER
COMPANY LLC
PO BOX 786
DRIGGS ID 83422



SECRETARY