

Draft Resolution W-4867
PG&E Talking Points
1/12/11

- **The Draft Resolution Is Misguided.** The draft resolution appears to be founded on an erroneous premise: that the New Tax Law’s bonus depreciation provision is intended to provide cash to consumers, who will in turn increase personal spending. In fact, the bonus depreciation provision is just one part of the New Tax Law’s comprehensive set of tax changes and is intended to encourage very large businesses such as utilities to make investments in new capital equipment in 2011 and 2012, with all “bonus depreciation” tax incentives expiring for property placed in service after December 31, 2013.

- **Overview Of The New Tax Law.** The New Tax Law contained numerous provisions intended to provide tax breaks to all segments of the economy:
 - Middle-income earners benefit from a payroll-tax holiday
 - Lower-income earners benefit from continued expanded availability of child credit and other breaks
 - Higher-income earners benefit from lowered estate tax rate
 - Small businesses benefit from increased “Section 179 expensing” and other tax breaks¹
 - Bonus depreciation is primarily useful to very large businesses spending more than \$2 million on new capital equipment in 2011 and, to a lesser extent, in 2012.² Small businesses are less likely to benefit from bonus depreciation because they can already write off 100% of equipment costs up to \$500,000 (previously, \$250,000).³

- **Ratepayers Would Receive Minimal, If Any, Benefits If The “Cost Savings” Of Bonus Depreciation Were Refunded In Rates.** Based on current estimates, the average PG&E customer would receive no refund in 2011⁴ and a very modest (if any) refund in 2012 if PG&E were to “quantify” the tax benefits of the New Tax Law and return them via rates.
 - Tax savings realized through the New Tax Law cannot be flowed through to customers as reduction in tax expense but only as an offset to financing costs (i.e., return on rate base). Any such offsets to financing costs from a 2011 tax return deferral would only begin after PG&E’s 2011 tax payments (September 15, 2011), reducing any customer benefit.
 - In addition, any savings associated with the New Tax Law would have to be reduced by the Manufacturer’s Deduction, lost CIAC-related revenues,⁵

¹ Wall Street Journal, “Congress Passes Tax Deal” (12/17/10) -

<http://online.wsj.com/article/SB10001424052748703395204576023772342189318.html>

² Section 179.org, “Section 179 FAQ’s” - http://www.section179.org/section_179_faqs.html

³ Wall Street Journal, “‘Small-Business’ Bill Holds Plenty for Big Firms” (7/28/10) -

<http://online.wsj.com/article/SB10001424052748703940904575395520866814284.html>

⁴ Largely because of a counteradjustment to Working Cash.

⁵ Prior to the New Tax Law, utilities such as PG&E would ask customers to make an Income Tax Component of Contribution (ITCC) payment to cover the tax liability incurred on Contributions in Aid of Construction (CIAC), with such ITCC amounts recorded as a form of Miscellaneous

and potentially other amounts as well, further reducing (if not completely eliminating) any rate refund.

In addition, there are a myriad other ways that utility costs could increase as a result of the New Tax Law (see, e.g., SCE comments on draft resolution, p. 6, citing elimination of the Section 199 deduction).

- **The Primary Purpose Of Bonus Depreciation Is To Encourage Large Firms Such As PG&E To Invest In Capital Equipment.** The bonus depreciation provision of the New Tax Law is akin to the Federal Government offering a 10% to 20% off “sale” on the cost of capital investments. For example, in 2011, PG&E would be able to replace 100 power poles for the same cost that it would be able to replace 80 power poles without the New Tax Law.

Such additional capital spending would create jobs, both for the manufacturers of the capital equipment as well as the labor to install the equipment, which in turn will spur the economy, which is the purpose of the New Tax Law. It will also result in additional dollars to the state in the form of payroll and other taxes.

- **Making Rates Subject To Refund Defeats The Purpose Of The New Tax Law’s Bonus Depreciation Provision.** Generally, the New Tax Law provides a 100% federal income tax deduction for capital investments placed in service by the end of 2011 and a 50% deduction for investments placed in service by the end of 2012.⁶ PG&E must start planning now: determining which capital projects should be pursued, submitting orders for the necessary equipment, hiring the associated contractors, and overseeing the work so that the equipment is placed in service before these deadlines.

By making such investments subject to refund, the draft Resolution defeats the purpose of the New Tax Law by discouraging California utilities from starting this planning process. Given the very small to non-existent rate refund that customers would receive, as compared to the significant cost savings that the New Tax Law would provide for new capital investments in 2011 and 2012, utility customers would be worse off in the long-run if the Commission were to order utilities to return the “cost savings” to customers via refunds rather than encourage utilities to accelerate investment in capital infrastructure. Such an outcome is neither beneficial to customers nor in the general public interest.

Revenues, which in turn reduces PG&E’s overall revenue requirement. Because the New Tax Law effectively eliminates PG&E’s federal tax liability (and leaves only the state tax liability on CIAC) for the statutory period, customers would pay less in ITCC, thereby reducing PG&E’s Miscellaneous Revenues and increasing the RRQ.

⁶ The 100% deduction may extend to 2012 for certain projects and costs, and the 50% deduction may extend to 2013 for certain projects and costs.