PACIFIC GAS AND ELECTRIC COMPANY
San Bruno Explosion and Fire OII
Investigation 12-01-007
Data Response

PG&E Data Request No.:	CPSD_002-05		
PG&E File Name:	SanBrunoExplosion-FireOII_DR_CPSD_002-Q05Rev01		
Request Date:	March 12, 2012	Requester DR No.:	002
Date Sent:	May 4, 2012	Requesting Party:	Consumer Protection and Safety Division
PG&E Witness:		Requester:	Gina Adams

QUESTION 5

Identify how much was collected from ratepayers for federal and state taxes for each year from 1995 to present. Identify the amount of federal and state taxes actually paid to the IRS and/or FTB on behalf of PG&E Utility.

The scope and time periods contained in the request have been revised as discussed below based on a conversation with Bruce Smith and Shilpa Ramaiya of PG&E and Gina Adams of CPSD on Thursday March 15, 2012.

Question modified to request information only from 2005 to present.

REVISED ANSWER 5

PG&E previously provided a response to this data request is and is now revising the response with respect to Table 2 showing the amount of Federal and State taxes collected from ratepayers.

First, in the original data response, PG&E erroneously included both current and deferred taxes collected from customers in Table 2, when the data response stated that, to make a proper comparison, only current taxes were being included.

Second, the response indicated the PG&E would supplement the data in Table 2 in certain years for GTS rate cases when additional ratemaking data was received. PG&E determined information was available for 2004, and has added that information to Table 2. Table 1 below shows taxes paid with the filed tax returns. Taxes paid for a given year are subject to future adjustments based on claims and/or assessments.

TABLE 1

Taxes Paid with Filed Returns

Year	Federal Tax Liability	California State Tax Liability
2005	$1,138,541,523	$278,434,000
2006	$677,766,096	$186,483,364
2007	$364,451,347	$108,173,400
2008	$3,820,322	$86,112,092
2009	$0	$89,820,095
2010	$0	$120,425,390
2011	Not Available – Tax Returns Have Not Been Completed	

Table 2 below shows current Federal and State taxes included in the adopted revenue requirement based on Commission adopted results of operations (RO) supporting settlements for the 2003, 2007, and 2011 GRCs and the fully litigated 2004 GT&S rate case. The table also includes Federal and state income taxes included in the adopted revenue requirement based on the adopted RO supporting the settlement in PG&E's 2011 GT&S rate case. There are no adopted RO analyses, and thus no adopted amount of tax expense, in other years.

TABLE 2

Taxes Included in Adopted Revenue Requirement

Test Year	GRC – Federal	GRC – California	GTS – Federal	GTS – California
2003	$278,963,000	$83,006,000	N/A	N/A
2004	N/A	N/A	$21,602,000	$9,121,000
2005	N/A	N/A	N/A	N/A
2006	N/A	N/A	N/A	N/A
2007	$379,591,000	$100,535,000	N/A	N/A
2008	N/A	N/A	N/A	N/A
2009	N/A	N/A	N/A	N/A
2010	N/A	N/A	N/A	N/A
2011	$472,458,000	$113,135,000	$46,280,000	$10,896,000

N/A indicates that adopted results of operations were not available for that year and case.

There are many caveats that should be made with regard to the data set forth above, and any attempt to compare those numbers to the Federal and State income taxes that are actually paid:

- Only Current Taxes Are Shown. The data shows only amounts included in rates as current taxes. The amounts included in rates as deferred taxes are recognized by regulators as being collected for taxes that will be paid in the future. Ratepayers receive the benefit from this accelerated inclusion in rates of taxes (i.e., of taxes t will be paid in the future) as a rate base reduction, until the deferred taxes are paid. We have not attempted to evaluate the ratepayer savings from deferred taxes (which are now quite significant), nor have we included deferred taxes collected currently from customers in the figures shown above.

- Attrition Years. Taxes are not explicitly included in any forecast ratemaking computation (RO) for the attrition years. Instead, PG&E historically has received only a small percentage increase in revenue requirements. These small percentage increases would not normally allow PG&E on an RO basis to recover both its increases in capital costs during attrition years (because of greater rate base, depreciation, and property taxes) and inflationary increases in its costs of material and labor. Thus, if an income tax computation were made for attrition years using an RO forecast accounting for growth in capital costs and inflation, current income tax expenses considered to be included in attrition year rates would almost certainly be substantially lower than in the test year.

- <u>Other Rate Mechanisms Including Taxes</u>. In addition to the GRC and GT&S rate cases, PG&E reflects income taxes in a variety of other mechanisms. For example there is a tax component included in transmission ownership rates established in FERC rate cases. There is a tax component indirectly associated with the rate reduction bonds that were recovered through 2006. There is a tax component associated with the bankruptcy regulatory asset that will be recovered through 2014. Finally, there are many tax components associated with special dedicated rate balancing and memorandum accounts (e.g., for advanced metering, power plants before they are included in rate cases; the Diablo Canyon steam generator replacement project; and several other projects). In many cases involving special memorandum and balancing accounts, collection of the projected taxes, along with other revenue requirements, has been deferred, reducing current taxes.

- <u>Bonus Depreciation</u>. Bonus depreciation has been enacted (or extended) numerous times over the last decade.[1] Bonus depreciation has had the effect of deferring PG&E's payment of taxes that have been included in rates as a current tax expense. This had a very substantial effect of reducing PG&E's tax payments to the Federal Government in 2006 thru 2010. The net result of this Federal tax deferral is that ratepayers receive the benefit of the deferral as a rate base reduction in the next rate case (and in between rate cases PG&E increases capital spending above the levels that otherwise might have occurred). In 2011, the Commission adopted a special memorandum account mechanism to track the capital savings derived from bonus depreciation enacted in December 2010, and assure that those savings were used by PG&E to make additional capital expenditures (Commission Resolution L-411A, dated June 23, 2011).

- <u>Regulatory Treatment of Comparisons Between Taxes Paid and Ratemaking Taxes</u>. Even without the specific caveats noted above there are significant reasons why tax payments may differ from amounts included in rates. This matter was studied extensively in the early 1980s and the issues were resolved by this Commission

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1 On February 7, 2008, the Economic Stimulus Act of 2008 provided 50 percent bonus depreciation for qualified property placed in service after December 31, 2007 and before January 1, 2009 (P.L. 110-185 Sec 103). On February 17, 2009, the American Recovery and Reinvestment Act of 2009 extended 50 percent bonus depreciation for qualified property placed in service before January 1, 2010 (P.L. 111-5 Sec 1201. On September 27, 2010, the Small Business Job Act of 2010 extended 50 percent bonus depreciation for qualified property for property placed in service before January 1, 2011 (P.L. 111-240, Sec. 2022(a)(1)). On December 17, 2010, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended bonus depreciation through December 31, 2012. It provided for 100% bonus depreciation for property placed in service after September 8, 2010 and before January 1, 2012 and 50 percent bonus depreciation for qualified property placed in service after December 31, 2011 and before January 1, 2012 (P.L. 111-312 Sec 401).

and by the Federal Energy Regulatory Commission. The policies adopted then have been followed by Federal and State regulators ever since. The California rulemaking that resolved these matters was OII 24, which resulted in D.04-05-036.[2] The purpose of OII 24 was to thoroughly analyze numerous circumstances that can give rise to differences between taxes actually paid by the utility and those included in rates. OII 24 was not a casual proceeding. It was ordered in 1978 and not completed until six years later. It involved the participation of numerous parties, including two elements of Commission staff, and the combined cities. The hearings alone lasted 22 days.

In each instance, the differences that had been identified between ratemaking taxes and "real world" taxes were explained and justified, thereby resulting in the Commission's continued use of the traditional methodology of using a results of operation forecast methodology for purposes of computing income tax expense.

In OII 24 the Commission described part of this issue generally as "What differences exist between estimates of revenue and expenses used for ratemaking purposes to calculate income tax and the revenue and expense recorded on the tax return:"[3]

> Under the Rate Case Plan general rate case decisions for major utilities are based on a future test period, relying on estimates of operating results made prior to the test-period. It is highly improbable the recorded amounts experienced in the calendar year will be exactly equal to the amounts adopted in the decision for operating revenue, operating expenses, income taxes, other taxes, and rate base. This is also true for the estimate of tax deductions used to calculate the adopted income taxes included in the adopted results. Thus, it occurs that the difference between income taxes adopted and income taxes paid results partly from these differences between test-year estimates and recorded results.
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> Staff and Industry agree that such differences are inherent in the use of future test periods for ratemaking. They warn that differences in income taxes between estimated and actual cannot be isolated from other factors in determining whether an adjustment should be made to the test-year estimate. Any review of differences would have to include the effects of differences of all estimates for revenues, operating expenses, income taxes and return on investment. Any prospective adjustment based on past over-or underestimates would have to take into consideration the overall effect of the differences for all

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2 D.04-05-036, 15 CPUC2d 42.

3 D.84-05-036, 15 CPUC2d at 52.

components of the test-year. Under these circumstances parties recommend no change in the present ratemaking procedure.[4]

The Commission agreed with the parties: "Since income taxes are derived residually, we agree that individual factors should not be isolated for purposes of comparing estimated and recorded results."[5] The Commission reached the same conclusion in its analysis of various specific items that gave rise to differences to tax payments and taxes included in rates. Apart from the specific caveats noted above, these items also explain differences between amounts included in rates and tax payments to the government.

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4 D.84-05-036, 15 CPUC 2d at 52.

5 D.84-05-036, 15 CPUC 2d at 53. In Columbia Gas, the FERC, with a wealth of experience, current and historical, made a similar observation about comparisons between ratemaking taxes and taxes actually paid:

> There are, however, vast differences between our assessment of the profit the company is due and the calculation of the amount by which the company is considered to have been enriched by the Internal Revenue Service. Some of these differences stem from the differences in the revenue that is used in calculating the company's profit. The most obvious difference is that we base our determination of the company's profit on projections of revenue. The Internal Revenue Service uses, of course, the revenues the company either actually receives or accrues the right to receive during the tax year. There are even greater differences in the expenses that are recognized.
>
> Because these differences are so vast, the Commission has found that the taxes the company pays to the Internal Revenue Service are not a reliable guide, even as a starting point, for determining a company's tax allowance. Instead, the Commission has always made its own assessment of the tax cost the company incurs in providing service. Columbia Gas Transmission Co., 23 FERC 61396, 61851; aff'd City of Charlottesville v. FERC, 774 F.2d 1205 (D.C. Cir. 1985) (emphasis added).