

Company: San Diego Gas & Electric Company (U 902 M)  
Proceeding: 2019 General Rate Case  
Application: A.17-10-\_\_\_\_\_  
Exhibit: SDG&E-35

**SDG&E**

**DIRECT TESTIMONY OF RAGAN G. REEVES**

**(TAXES)**

**October 6, 2017**

**BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA**



## TABLE OF CONTENTS

I.	INTRODUCTION .....	1
A.	Summary of Proposals .....	1
B.	Organization of Testimony .....	1
II.	PAYROLL TAXES .....	1
A.	Introduction.....	1
B.	Discussion.....	1
1.	Federal Insurance Contributions Act .....	2
2.	Federal Unemployment Tax Act.....	2
3.	California State Unemployment Insurance.....	2
4.	Methodology Used to Estimate Tax Expense .....	2
C.	Summary of Estimated Payroll Taxes.....	3
D.	Results.....	3
III.	AD VALOREM TAXES .....	3
A.	Introduction.....	3
B.	Discussion.....	4
C.	Summary of Estimated Ad Valorem Tax Expenses .....	6
D.	Results.....	9
IV.	INCOME TAXES .....	9
A.	Introduction.....	9
B.	Discussion of Income Tax Expense.....	9
1.	Methodology .....	9
2.	Schedule M Items and Other Specific Tax Deductions .....	11
C.	Discussion of Deferred Taxes.....	14
1.	Bonus Depreciation.....	14
2.	Contributions-in-Aid-of-Construction .....	16
D.	Summary Tables .....	16
E.	Results.....	22
F.	Tax Memorandum Account .....	23
1.	Background.....	23
2.	Clarification of the Scope and Intent of the TMA from PG&E's 2017 GRC Decision .....	24
3.	2016 TMA Balances .....	26
4.	Proposal for 2019 GRC Cycle .....	28

V.	FRANCHISE FEES .....	29
A.	Introduction.....	29
B.	Discussion.....	29
C.	Summary of Estimated Franchise Fees.....	30
D.	Results.....	31
VI.	CONCLUSION.....	31
VII.	WITNESS QUALIFICATIONS.....	32

## LIST OF APPENDICES

Appendix A: Glossary of Terms.....	RGR-A-1
Appendix B: 2016 Tax Memorandum Account Tracking Schedule .....	RGR-B-1

## **SUMMARY**

- My testimony presents San Diego Gas & Electric Company's (SDG&E) estimated tax expense for Test Year (TY) 2019, and explains how those estimates were derived. The tax expenses discussed in my testimony include income taxes, payroll taxes, ad valorem taxes, and franchise fees.
- My testimony estimates a Test Year 2019 income tax expense of \$152.1 million, payroll tax expense of \$18.4 million, ad valorem tax expense of \$102.1 million, and franchise fees of \$70.8 million.
- The Protecting Americans from Tax Hikes Act of 2015 (the PATH Act) was enacted on December 18, 2015 (Pub. L. No. 114-113). The PATH Act extended bonus depreciation through 2019. The bonus depreciation rate is 50% through 2017 but is reduced to 40% for 2018 and to 30% for 2019.

**SDG&E DIRECT TESTIMONY OF RAGAN G. REEVES**  
**(TAXES)**

**I. INTRODUCTION**

**A. Summary of Proposals**

My testimony presents San Diego Gas & Electric Company's (SDG&E's) estimated tax expense for Test Year (TY) 2019, and explains how those estimates were derived.<sup>1</sup> My testimony also presents the 2016 results of the Tax Memorandum Account (TMA).

**B. Organization of Testimony**

SDG&E incurs three categories of taxes: (1) payroll taxes, (2) ad valorem (*i.e.*, property) taxes, and (3) income taxes. In addition, SDG&E incurs franchise fees, which it includes in its tax expense estimates. I will discuss each of these tax expense categories in turn.<sup>2</sup> A summary table for each category of tax expense is presented at the end of each section.

To the extent that the California Public Utilities Commission (CPUC or Commission) adopts levels of operations and maintenance (O&M) expense or capital that are different from what has been proposed by SDG&E in this Application, taxes would be re-calculated to reflect the impact of those changes.

**II. PAYROLL TAXES**

**A. Introduction**

The purpose of this section is to provide an estimate of SDG&E's 2019 payroll tax expenses, and to describe the methodology used to develop SDG&E's estimate.

**B. Discussion**

Payroll taxes were estimated by applying a tax rate on TY 2019 O&M and capital labor covered under this filing up to a maximum wage base. Payroll taxes are paid by both the employee and the employer. The following discussion relates to the employer's payroll tax liability.

---

<sup>1</sup> A late reduction in SDG&E's proposed TY 2019 revenue requirement is reflected in the Summary of Earnings testimony of Khai Nguyen (Exhibit SDG&E-42). Due to the timing of the TY 2019 revenue requirement change, SDG&E has updated only certain witness testimonies to reflect this reduction prior to filing its application. SDG&E's Tax testimony proposal has not yet been updated to reflect this reduction. The tax revenue requirement reduction will be provided and updated in the testimony and workpapers at SDG&E's earliest opportunity.

<sup>2</sup> The TMA discussion is included within the income taxes section of my testimony.

## 1                   **1.       Federal Insurance Contributions Act**

2               Federal Insurance Contributions Act (FICA) taxes, also referred to as social security  
3 taxes, are composed of two pieces: (1) the Old-Age, Survivors, and Disability Insurance  
4 (OASDI), and (2) the Hospital Insurance (HI or Medicare). For 2016, the OASDI tax rate was  
5 6.2% of wages up to a maximum wage base of \$118,500. The Medicare tax rate was 1.45% of  
6 wages with no maximum wage base. Based on rate schedules contained in the 2017 Annual  
7 Report published by the Social Security Administration (2017 Annual Report), the employer's  
8 portion of the OASDI and Medicare tax rates have been at current levels since 1990 and are not  
9 expected to change through 2019 based on currently enacted law.<sup>3</sup> The OASDI wage base is  
10 \$127,200 for 2017 and is projected to increase to \$130,500 for 2018 and \$135,600 for 2019  
11 based on data reported in the 2017 Annual Report.<sup>4</sup>

## 12                   **2.       Federal Unemployment Tax Act**

13               The 2016 Federal Unemployment Tax Act (FUTA) tax rate was 2.4% on wages up to  
14 \$7,000. Based on currently enacted law, the FUTA tax rate is expected to increase to 2.7% for  
15 2017, and then is expected to decrease to 0.6% for 2018 and 2019. The FUTA wage base is not  
16 expected to change through 2019.

## 17                   **3.       California State Unemployment Insurance**

18               The California State Unemployment Insurance (SUI) is composed of two pieces: (1) the  
19 Unemployment Insurance (UI), and (2) the California Employment Training Tax (CET). The  
20 2016 UI tax rate was 3.1% on wages up to \$7,000. The CET tax rate was an additional 0.1% on  
21 wages up to \$7,000. Based on currently enacted law, the UI tax rate is expected to decrease to  
22 3.0% for 2017 – 2019. The CET tax rate and wage bases for SDG&E are not expected to change  
23 through 2019.

## 24                   **4.       Methodology Used to Estimate Tax Expense**

25               Payroll taxes are a function of taxable wages and applicable tax rates. The computation  
26 of the estimated payroll taxes begins with the 2016 taxable wages stratified into salary  
27 increments. The annual wage base in effect for the year for each type of payroll tax was applied  
28 to total wages to ensure that wages up to, but not exceeding, the wage base cap were subject to

---

<sup>3</sup> See Table VI.G1, Payroll Tax Contribution Rates for the OASDI and HI Programs, 2017 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds.

<sup>4</sup> See Table V.C1, 2017 Annual Report.

the tax. Thus, wages up to the salary increment where the annual wage is closest to the wage base cap are subject to the tax. Wages above the wage base cap for any particular type of payroll tax were derived from multiplying the number of employees in each stratum above the cap by the wage base cap. The resulting taxable wages for each tax type were totaled and the applicable statutory tax rate was then applied to the total taxable wages. The Medicare portion of the FICA tax is computed without respect to a wage base since all wages are subject to that tax. A companywide composite tax rate was computed based on total forecasted payroll taxes using the above methodology divided by total forecasted wages. The composite payroll tax rate for each year was applied to labor dollars applicable to this filing to determine the employer's payroll tax expense.

### C. Summary of Estimated Payroll Taxes

Table SDG&E-RGR-1 below summarizes the amount of payroll taxes on all non-capitalized wages applicable to this filing.

**Table SDG&E-RGR-1**  
**Summary of Estimated Payroll Taxes**  
**(\$ in Thousands)**

	<i>Line No.</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
<b>Electric Distribution</b>	1	9,005	10,409	10,857	11,518
<b>Gas Distribution</b>	2	4,176	5,258	5,577	5,942
<b>Electric Generation</b>	3	0	958	963	978

### D. Results

The increase in payroll taxes from 2016 to 2019 reflects the impacts of staffing level changes presented by other witnesses in their direct testimonies, the impact of labor cost escalation on those changes, and the increase in the composite payroll tax rate resulting from the OASDI wage base increase as discussed above.

## III. AD VALOREM TAXES

### A. Introduction

The purpose of this section is to provide an estimate of SDG&E's ad valorem taxes that will be incurred during TY 2019, and to describe the methodology used to develop the estimate.

## **B. Discussion**

Ad valorem taxes are a function of the assessed value of property and a tax rate applied to that value. Property owned and used by public utilities as of January 1 (the lien date) each year is re-assessed to its full market value by the California State Board of Equalization (SBE). By definition, ad valorem taxes are based on the value of the property being taxed. Appraisers have developed various generally accepted indicators of value that are correlated to yield an estimation of the market value of the property being assessed. The primary indicator of value for regulated public utility property is the Historical Cost Less Depreciation (HCLD) indicator, and a secondary indicator is the Capitalized Earnings Ability (CEA).

HCLD is the primary indicator of value for closely rate-regulated property because it approximates rate base. HCLD is equal to the estimated cost of property, which is subject to assessment by the SBE, less the accumulated depreciation taken on the property. Historical cost consists of the original cost of plant balances on the January 1 lien date, plus construction work-in-progress and materials and supplies on hand to operate the plant. Adjustments are made to add the value of possessory interests held by the utility on government-owned property and to deduct non-taxable licensed motor vehicles, software, leasehold improvements, business inventories, and other property not subject to ad valorem taxes. Finally, the HCLD indicator is adjusted by deducting the accumulated deferred federal income taxes on taxable property.

The CEA, or the income approach to value, is designed to recognize the concept that the value of business property is closely related to its ability to generate income. The CEA indicator is used when the property being appraised is purchased in anticipation of receiving income (*i.e.*, rental property), and the actual future income stream can be reliably forecast, or a hypothetical income stream can be estimated by comparison to other similar properties. The CEA is the preferred approach for the appraisal of properties when reliable sales data are not available or the cost approach does not yield reliable results. The CEA is a secondary indicator of value for public utility property because the income of public utility property is limited by regulation, and comparison to the income stream from similar properties is limited.

SDG&E has filed its property statements with the SBE for the 2016 and 2017 lien dates. The property statements form the basis of the appraisals to set the value of SDG&E's property for the 2016-2017 and 2017-2018 fiscal years. The SBE reports the value of property subject to ad valorem tax annually on the "Notice of Unitary Appraised Value," which SDG&E has



1 received for the 2016 and 2017 lien dates. In correlating the value indicators calculated by the  
2 SBE from information contained in the property statement, the SBE applied a weighting of 75%  
3 to the HCLD indicator and 25% to the CEA indicator to derive the total appraised value of  
4 SDG&E's unitary property.<sup>5</sup> Added to the value of SDG&E's unitary property is the value of  
5 SDG&E's non-unitary property.<sup>6</sup> In estimating ad valorem taxes for ratemaking purposes,  
6 adjustments were made to exclude taxes resulting from: (a) the assessment of non-utility  
7 property since it is not included as an operating expense, and (b) Construction Work in Progress  
8 (CWIP), which is capitalized rather than directly charged to ad valorem tax expense. Also  
9 excluded is the value of electric transmission property, since such property is excluded from this  
10 proceeding.

11 The SBE has followed the same assessment methodology for several years; consequently,  
12 SDG&E followed this methodology to estimate the assessed value for unitary property and the  
13 resulting ad valorem tax expense estimate for TY 2019.

14 The tax rate used to estimate California ad valorem taxes is the basic statewide tax rate of  
15 1% established under Proposition 13, plus an additional rate component of 0.4986%, which is a  
16 composite rate derived from dividing taxes paid to local jurisdictions by the total assessed value  
17 of property in all voter approved local assessment districts as allowed under Proposition 13. The  
18 escalation in the rates from 2016 to 2019 represents the average historical rate of increase in  
19 local tax rates over the most recent five-year period.

20 The estimated ad valorem taxes for SDG&E's Desert Star Energy Center, which is  
21 located in Nevada, are added to California ad valorem taxes as an "Other Adjustment" on the  
22 Electric Generation summary table, Table SDG&E-RGR-2-3 below.

23 The estimated ad valorem tax expense for TY 2019 is comprised of the second  
24 installment payment from fiscal year 2018-2019 plus the first installment payment for fiscal year  
25 2019-2020.

---

<sup>5</sup> Unitary property is property owned or used by the utility that the SBE has determined is used in the utility's operating business. The weight given to the CEA and HCLD indicators by the SBE can be derived mathematically by correlating the value indicators to the final value.

<sup>6</sup> Non-unitary property is property owned by the utility that the SBE has determined is not used in the utility's operating business.

**C. Summary of Estimated Ad Valorem Tax Expenses**

The following tables, Table SDG&E-RGR-2-1, Table SDG&E-RGR-2-2, and Table SDG&E-RGR-2-3, summarize SDG&E's estimated ad valorem tax expenses for Electric Distribution, Gas Distribution, and Electric Generation, respectively.

**Table SDG&E-RGR-2-1**  
**San Diego Gas & Electric Company**  
**Summary of Estimated Ad Valorem Tax Expenses**  
**Electric Distribution**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
1	Taxable Plant in Service	7,396,329	7,819,195	8,451,362	9,231,016
2	Taxable Reserve for Depreciation	(2,769,061)	(2,934,016)	(3,105,914)	(3,279,766)
3	Taxable Net Plant	4,627,268	4,885,179	5,345,448	5,951,250
4	Taxable Reserve for Def. Inc. Tax	(573,978)	(597,349)	(649,032)	(693,111)
5	Adjustment for Income Approach	(148,350)	(156,935)	(171,889)	(192,448)
6	Assessed Value - Non-Unitary	13,277	14,045	15,383	17,223
7	Net Assessable Value	3,918,217	4,144,940	4,539,910	5,082,915
8	Ad Valorem Tax Rate	1.4986482%	1.5385850%	1.5785218%	1.6184586%
9	Ad Valorem Tax - Fiscal Year	58,720	63,773	71,663	82,265
10	Other Adjustments	34	34	34	34
<u>Fiscal Year</u>					
11	Total Operating Ad Valorem Tax	58,754	63,807	71,697	82,299
12	Capitalized Ad Valorem Tax	(2,516)	(3,403)	(4,309)	(4,746)
13	Net Operating Ad Valorem Tax	56,238	60,404	67,388	77,553
<u>Calendar Year (Note 1)</u>					
14	Total Operating Ad Valorem Tax	53,891	60,983	67,454	76,700
15	Capitalized Ad Valorem Tax	(4,064)	(2,608)	(3,603)	(4,420)
16	Net Operating Ad Valorem Tax	49,827	58,375	63,852	72,280

(Note 1) - Calendar year total operating ad valorem tax = ½ of the current fiscal year total ad valorem tax plus ½ of the prior fiscal year total ad valorem tax.

**Table SDG&E-RGR-2-2**  
**San Diego Gas & Electric Company**  
**Summary of Estimated Ad Valorem Tax Expenses**  
**Gas Distribution**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
1	Taxable Plant in Service	1,927,644	2,033,578	2,257,227	2,450,089
2	Taxable Reserve for Depreciation	(978,555)	(1,016,097)	(1,053,902)	(1,092,432)
3	Taxable Net Plant	949,089	1,017,481	1,203,325	1,357,657
4	Taxable Reserve for Def. Inc. Tax	(105,175)	(119,410)	(146,801)	(165,691)
5	Adjustment for Income Approach	(30,887)	(32,869)	(38,669)	(43,626)
6	Assessed Value - Non-Unitary	2,764	2,942	3,461	3,904
7	Net Assessable Value	815,791	868,144	1,021,317	1,152,244
8	Ad Valorem Tax Rate	1.4986482%	1.5385850%	1.5785218%	1.6184586%
9	Ad Valorem Tax - Fiscal Year	12,226	13,357	16,122	18,649
10	Other Adjustments	6	6	6	6
<u>Fiscal Year</u>					
11	Total Operating Ad Valorem Tax	12,232	13,363	16,128	18,655
12	Capitalized Ad Valorem Tax	(729)	(883)	(1,436)	(1,921)
13	Net Operating Ad Valorem Tax	11,503	12,481	14,692	16,733
<u>Calendar Year (Note 1)</u>					
14	Total Operating Ad Valorem Tax	10,998	12,737	14,685	17,331
15	Capitalized Ad Valorem Tax	(809)	(743)	(902)	(1,850)
16	Net Operating Ad Valorem Tax	10,189	11,994	13,784	15,481

(Note 1) - Calendar year total operating ad valorem tax = ½ of the current fiscal year total ad valorem tax plus ½ of the prior fiscal year total ad valorem tax.

1

**Table SDG&E-RGR-2-3**  
**San Diego Gas & Electric Company**  
**Summary of Estimated Ad Valorem Tax Expenses**  
**Electric Generation**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
1	Taxable Plant in Service	1,151,035	1,173,641	1,212,399	1,544,541
2	Taxable Reserve for Depreciation	(349,532)	(388,459)	(429,189)	(464,887)
3	Taxable Net Plant	801,503	785,182	783,210	1,079,654
4	Taxable Reserve for Def. Inc. Tax	(69,110)	(74,604)	(81,995)	(132,454)
5	Adjustment for Income Approach	(26,806)	(26,007)	(25,664)	(34,668)
6	Assessed Value - Non-Unitary	2,399	2,328	2,297	3,103
7	Net Assessable Value	707,987	686,898	677,847	915,636
8	Ad Valorem Tax Rate	1.4986482%	1.5385850%	1.5785218%	1.6184586%
9	Ad Valorem Tax - Fiscal Year	10,610	10,569	10,700	14,819
10	Other Adjustments	1,743	1,743	1,743	1,743
<u>Fiscal Year</u>					
11	Total Operating Ad Valorem Tax	12,353	12,312	12,443	16,562
12	Capitalized Ad Valorem Tax	(220)	(194)	(164)	(175)
13	Net Operating Ad Valorem Tax	12,133	12,118	12,279	16,387
<u>Calendar Year (Note 1)</u>					
14	Total Operating Ad Valorem Tax	11,285	12,270	12,315	14,441
15	Capitalized Ad Valorem Tax	(847)	(172)	(91)	(112)
16	Net Operating Ad Valorem Tax	10,438	12,099	12,224	14,328

2

3

4

(Note 1) - Calendar year total operating ad valorem tax = ½ of the current fiscal year total ad valorem tax plus ½ of the prior fiscal year total ad valorem tax.

1           **D.     Results**

2           The changes from 2016 to 2019 are the result of changes in plant and depreciation  
3 balances presented by other witnesses in their direct testimonies, and the expected escalation in  
4 the tax rate for local assessments as discussed above.

5           **IV.    INCOME TAXES**

6           **A.     Introduction**

7           The purpose of this section is to provide an estimate of SDG&E's income tax expense for  
8 TY 2019, and to describe the assumptions and methodology used to calculate income tax  
9 expense. This section also presents the 2016 results of the TMA as of the date of this  
10 Application.<sup>7</sup>

11          **B.     Discussion of Income Tax Expense**

12               **1.     Methodology**

13          SDG&E's operating income is subject to federal income tax and the California  
14 Corporation Franchise Tax (CCFT). Income tax expense is a function of cost-of-service amounts  
15 and capital expenditures adopted by the CPUC, as adjusted to comply with income tax rules.  
16 Accordingly, the calculation of ratemaking income taxes is dependent upon federal and state tax  
17 laws, prior CPUC decisions with general applicability to all utilities, and decisions with specific  
18 reference to SDG&E.

19          Consistent with CPUC Decision (D.) 84-05-036 issued in Order Instituting Investigation  
20 (OII) 24, the income tax estimates contained in this section are based on SDG&E's stand-alone  
21 taxes, not on an allocation of tax expense from Sempra Energy, the parent company of SDG&E.<sup>8</sup>

22          Another issue considered by the CPUC in OII 24 was whether expenses not borne by  
23 customers should be included as income tax deductions in computing estimated TY income tax  
24 expense. The CPUC stated that it had consistently calculated income taxes for ratemaking  
25 purposes based on the cost of service developed from authorized expenses.<sup>9</sup> The CPUC also  
26 found that if they were to include expenses not subject to rate recovery as a deduction in

---

<sup>7</sup> The incurred amounts for 2016 are subject to change until the 2016 federal and California income tax returns are filed. Those tax returns have not been filed as of the date of this Application. In addition, the incurred amounts for 2016 do not yet reflect any adjustments from the completion of audits, because any audit adjustments for the 2016 tax year will not be known until future years.

<sup>8</sup> 1984 Cal. PUC LEXIS 1325 at \*57-58 (Finding of Fact 12); 15 CPUC 2d 42.

<sup>9</sup> *Id.* at \*15.

1 calculating taxable income, stockholders would be penalized by a reduction in their net income  
2 equal to the full amount of the expenditures, because they would have no offsetting tax  
3 deduction.<sup>10</sup> The Commission concluded that their method of excluding expenses not borne by  
4 customers in the calculation of TY income tax expense is reasonable and should continue.<sup>11</sup> As  
5 such, SDG&E follows this conclusion of law from OII 24 in this GRC proceeding.

6 The estimates contained in this section were calculated using current federal and state tax  
7 laws enacted through the date of this testimony. SDG&E has not attempted to forecast any  
8 future changes in tax law in the income tax calculation. SDG&E has utilized current federal and  
9 state statutory tax rates of 35% and 8.84%, respectively, in developing its estimate of federal and  
10 state income tax expense.

11 State income tax expense has been computed by reducing operating income by operating  
12 expenses, including property taxes, payroll taxes, and making certain permanent and flow  
13 through tax adjustments for differences in the book and state tax return treatment of items of  
14 income and expense (Schedule M adjustments) as explained in more detail later in this section.  
15 Consistent with the CPUC policy discussed in D.93848,<sup>12</sup> a flow through accounting  
16 methodology was utilized in estimating state tax expense.<sup>13</sup>

17 Federal income tax expense has been computed by reducing operating income by  
18 operating expenses, including property taxes, payroll taxes, prior year state taxes, and making tax  
19 adjustments for differences in the book and federal tax treatment of certain items of income and  
20 expense (Schedule M adjustments), also explained in more detail later in this section.

21 Where required, SDG&E has followed the normalization rules contained in Internal  
22 Revenue Code Section (IRC) § 168, and Treasury Regulations Section (Treas. Reg.) § 1.167(l)-1  
23 in computing federal income tax expense.<sup>14</sup> Accordingly, federal tax depreciation on post-1980  
24 vintage year assets has been “normalized” by using a book life and method to calculate tax  
25 depreciation. Consistent with CPUC policy, where normalization is not required by the IRC,  
26 SDG&E has employed flow-through accounting. For example, tax depreciation on pre-1981

---

<sup>10</sup> *Id.* at \*16-18.

<sup>11</sup> *Id.* at \*62 (Conclusion of Law 2).

<sup>12</sup> 1981 Cal. PUC LEXIS 1240; 7 CPUC 2d 332.

<sup>13</sup> Flow-through accounting treats temporary differences between recognition of expenses for book purposes and their tax return treatment as current adjustments to the revenue requirement.

<sup>14</sup> Normalized tax accounting follows the financial accounting treatment for items of income and expense in the revenue requirement calculation.

1 vintage assets has been flowed through as an adjustment to federal tax expense as required by  
2 D.93848.<sup>15</sup>

3 Tax expense based on income has been reduced by the amortization of deferred  
4 Investment Tax Credits (ITC) generated in prior years in accordance with SDG&E's prior  
5 election under applicable law<sup>16</sup> to ratably flow through the ITC benefit as a reduction to  
6 ratemaking tax expense at a rate not to exceed the book life of the property that generated the  
7 ITC. This application conforms to the treatment of deferred ITC amortization mandated by  
8 D.88-01-061<sup>17</sup> and is the same treatment employed by SDG&E in prior rate cases.

9 SDG&E's federal income tax expense has been reduced by the amortization of remaining  
10 excess deferred federal income taxes resulting from a reduction in the federal income tax rate  
11 from a high of 41% to the current 35% beginning in 1993, utilizing the Average Rate  
12 Assumption Method (ARAM) as required by Internal Revenue Service (IRS) normalization rules  
13 and mandated by D.88-01-061.<sup>18</sup>

14 The Tax Reform Act of 1986 (TRA 86) adopted rules regarding capitalization of  
15 construction period interest for long-lived assets that have an extended construction period.  
16 These rules were codified in IRC § 263A. For book and ratemaking purposes, construction  
17 period interest is capitalized through an allowance for funds used during construction (AFUDC).  
18 While similar in concept, there are specific differences between the book and tax treatment of  
19 construction period interest. As in prior rate cases, for tax purposes SDG&E follows the rules in  
20 IRC § 263A in this filing with respect to the treatment of construction period interest.

21 As prescribed by the CPUC in D.84-05-036, SDG&E used the statutory federal tax rate  
22 of 35% and the statutory state tax rate of 8.84% in its development of the net-to-gross multiplier  
23 used to gross-up tax expense to a revenue requirement.<sup>19</sup>

## 24 **2. Schedule M Items and Other Specific Tax Deductions**

25 SDG&E makes several adjustments to book income in the form of Schedule M  
26 adjustments to arrive at taxable income. In addition, there are other types of deductions

---

<sup>15</sup> 1981 Cal. PUC LEXIS 1240; 7 CPUC 2d 332.

<sup>16</sup> SDG&E's election under former IRC § 46(f)(2).

<sup>17</sup> 1988 Cal. PUC LEXIS 102; 27 CPUC 2d 310.

<sup>18</sup> *Id.* at \*95-96.

<sup>19</sup> 1984 Cal. PUC LEXIS 1325 at \*62-63 (Conclusion of Law 9).

1 permitted under the IRC that have been incorporated into the computation of SDG&E's tax  
2 expense, as discussed below.

3 Fixed Charges – Operating. This adjustment represents the interest expense accrued on  
4 debt used to finance rate base. The deduction is computed using rate base and the authorized  
5 weighted-average cost of long-term debt. The CCFT interest deduction is based on rate base net  
6 of deferred ITC (as ITC is not available for CCFT purposes).

7 Fiscal Year/Calendar Year Property Tax Adjustment. An adjustment is made to add back  
8 book calendar-year property tax expense and deduct fiscal-year property tax expense as allowed  
9 by federal and state tax law. Consistent with CPUC policy, this deduction is flowed through in  
10 the calculation of income tax expense.

11 Prior Year CCFT. Federal law allows a deduction for state income taxes paid. In  
12 California, this is the CCFT deduction. For ratemaking purposes, D.89-11-058<sup>20</sup> specifies that  
13 the allowable deduction is the prior years' CPUC-adopted CCFT, not the current year CCFT.  
14 Since there is, as yet, no CPUC-adopted CCFT, SDG&E has used the prior year's CCFT  
15 estimate in calculating federal tax expense for TY 2019.

16 Internally-Developed Software. For financial accounting purposes, software  
17 expenditures are capitalized and amortized to expense over various lives. For tax purposes, a  
18 current-year deduction is allowed under IRC § 174 for internally developed software  
19 expenditures.<sup>21</sup> SDG&E has deducted internally developed software expenditures as a flow-  
20 through deduction pursuant to D.84-05-036.<sup>22</sup> IRC § 167(f)<sup>23</sup> requires capitalization of un-  
21 modified, or "canned" software. SDG&E applies normalized tax accounting treatment to  
22 expenditures for canned software pursuant to D.84-05-036.

23 Federal Tax Depreciation. Federal tax depreciation on post-1980 vintage property is  
24 governed by the normalization rules described earlier. Differences between book and tax  
25 depreciation resulting from the different lives and methods used to compute book and tax  
26 depreciation are normalized. Federal tax return depreciation on pre-1981 vintage property is

---

<sup>20</sup> 1989 Cal. PUC LEXIS 815 at \*34 (Conclusion of Law 1); 33 CPUC 2d 495.

<sup>21</sup> The 2019 tax deduction for internally-developed software is a function of the forecasted spend on internally-developed software in TY 2019. Spend data is forecasted by capital witnesses in the rate base module and the tax module pulls in the forecasted spend data from the rate base module.

<sup>22</sup> 1984 Cal. PUC LEXIS 1325.

<sup>23</sup> IRC § 167(f) required capitalization of un-modified software purchased after August 10, 1993.



1 flowed through as a deduction in the computation of federal taxable income, as is depreciation  
2 attributable to differences in the basis used to depreciate property for book and tax purposes.

3 State Tax Depreciation. California did not adopt the federal accelerated depreciation  
4 lives and methods or the normalization requirements enacted by the Economic Recovery Tax Act  
5 of 1981 (ERTA) and the TRA 86. Accordingly, there is no requirement to normalize state tax  
6 depreciation; therefore, SDG&E flows through state tax depreciation in excess of the amount  
7 deducted for book purposes. SDG&E's state tax depreciation is calculated using the Asset  
8 Depreciation Range Method (ADR) prescribed by the IRS prior to 1981, which utilizes double  
9 declining balance depreciation switching to a straight-line method when book depreciation  
10 exceeds the double declining balance method.

11 Federal Cost of Removal. SDG&E follows the guidance in IRS Revenue Ruling 2000-  
12 7,<sup>24</sup> which provides a current deduction for actual costs to remove assets retired from service.  
13 However, under the normalization rules, costs to remove assets that have been depreciated using  
14 the Accelerated Cost Recovery System (ACRS) or Modified Accelerated Cost Recovery System  
15 (MACRS) cannot be flowed through. Accordingly, federal removal costs are deducted only on  
16 pre-1981 vintage assets retired from service. This treatment is consistent with D.93848.

17 State Cost of Removal. California did not adopt the federal ACRS or MACRS  
18 depreciation systems, choosing instead to remain on the ADR system. Accordingly, SDG&E  
19 flows through removal costs for CCFT purposes irrespective of the vintage of the underlying  
20 assets per D.84-05-036.<sup>25</sup>

21 Repairs Deduction. The Schedule M adjustment for the repairs deduction represents the  
22 difference between expenditures that are permitted to be deducted as repairs for tax purposes and  
23 those same expenditures that are required to be capitalized for financial reporting purposes.  
24 SDG&E has flowed through the tax benefits associated with its projected repairs deduction to  
25 ratepayers for TY 2019 for both federal and California purposes in accordance with D.93848.

26 Section 199 Deduction. The American Jobs Creation Act of 2004 added Section 199 to  
27 the IRC. Under IRC § 199, manufacturers may deduct the lower of: (1) a fixed percentage of  
28 their qualified production activities income, or (2) 50% of the wages of employees involved in  
29 the qualified production activity. The fixed percentage is 9% of qualified income for tax years

---

<sup>24</sup> 2000-1 C.B. 712.

<sup>25</sup> 1984 Cal. PUC LEXIS 1325 at \*59 (Finding of Fact 23).

1 after 2009. For public utilities, income derived from the generation of electricity qualifies for  
2 deduction under Section 199. Accordingly, SDG&E has calculated a Section 199 deduction for  
3 its qualified production of electricity in its calculation of income tax expense. The deduction is  
4 limited to the lesser of 9% of income from the production of electricity or 50% of wages paid to  
5 employees engaged in the production of electricity. If the company has no taxable income in a  
6 particular year, the Section 199 deduction is unavailable for that year.

7 Tax Credits. SDG&E has reflected an offset to tax expense for allowable federal and  
8 state tax credits allowed under current law. SDG&E has also reflected a “credit addback” where  
9 required in computing taxable income. As a general rule, a taxpayer cannot claim both a  
10 deduction and a credit for the same item of expense. Therefore, SDG&E has added the amount  
11 of credits claimed back to taxable income to reverse the corresponding tax deductions.

## 12 **C. Discussion of Deferred Taxes**

13 The accumulated deferred federal income tax (ADFIT) resulting from the difference  
14 between normalized tax depreciation computed using a book life and book method and the  
15 comparable tax depreciation computed using ACRS or MACRS has been included as an  
16 adjustment to rate base in this GRC (see the testimony of R. Craig Gentes, Exhibit SDG&E-33,  
17 for a discussion of rate base). SDG&E’s treatment of deferred taxes is in accordance with IRC §  
18 168(i)(9), Treas. Reg. § 1.167(l)-1, and numerous related IRS rulings that taken together  
19 constitute the “tax normalization” requirements.

20 All current law has been followed in the development of deferred federal income taxes.  
21 Accumulated deferred taxes for TY 2019 were developed on a monthly basis and prorated in  
22 accordance with the normalization requirements in Treas. Reg. § 1.167(l)-1(h)(6)(ii).<sup>26</sup>

### 23 **1. Bonus Depreciation**

24 On December 18, 2015, President Obama signed into law The Protecting Americans from  
25 Tax Hikes Act of 2015 (the PATH Act).<sup>27</sup> One of the provisions of the PATH Act was an

---

<sup>26</sup> The method prescribed by Treas. Reg. § 1.167(l)-1(h)(6)(ii) is to be used when rates are set on a projected future period. Tax expense must be computed using a rate and method consistent with the rate and method used for book depreciation. The deferred tax reserve that reduces rate base must be computed using the average of the beginning-of-year balance plus a prorated end-of-year balance. The prorated end-of-year balance was computed assuming that additions to the deferred tax balances are credited ratably at the end of each month throughout the year.

<sup>27</sup> Pub. L. No. 114-113, H.R. 2029.

1 extension of the bonus depreciation rules, which has deferred tax implications for SDG&E's TY  
2 2019 forecasts.

3 The bonus depreciation rules allow taxpayers to immediately expense a specified  
4 percentage of qualifying property placed into service in a particular year, rather than requiring  
5 the taxpayer to depreciate the full amount of the property over multiple years. Unlike previous  
6 extensions that generally extended bonus depreciation for only one year, the PATH Act extended  
7 bonus depreciation to eligible property placed into service between January 1, 2015 and  
8 December 31, 2019,<sup>28</sup> and for costs, incurred before January 1, 2020 attributable to eligible long  
9 production period property (LPPP)<sup>29</sup> that is placed into service before January 1, 2021.<sup>30</sup> The  
10 bonus depreciation rules expire generally on December 31, 2019 (and expire on December 31,  
11 2020 for eligible LPPP).

12 The bonus depreciation percentage for eligible property placed in service in 2015-2017 is  
13 50%.<sup>31</sup> The percentage decreases to 40% for 2018 and decreases further to 30% for 2019.<sup>32</sup>  
14 Special rules allow qualifying LPPP to receive a one-year extension on the bonus depreciation  
15 phase-out rates. Therefore, for qualifying LPPP, the 50% bonus depreciation rate applies to  
16 property placed in service in 2018, the 40% rate applies to property placed in service in 2019,  
17 and the 30% rate applies to property placed in service in 2020.<sup>33</sup>

18 The bonus depreciation rules contained in the PATH Act apply to the same types of  
19 property eligible for bonus depreciation under prior law. Property eligible for bonus depreciation  
20 is generally limited to business property with a tax recovery period of 20 years or less and only if  
21 the original use of the property commences with the taxpayer.

22 For ratemaking purposes, bonus depreciation allowed by the PATH Act is subject to the  
23 tax normalization rules contained in IRC § 168 and Treasury Regulations under former IRC §  
24 167. The ratemaking effect of the PATH Act is to increase federal tax return depreciation for  
25 2015 through 2019 above the regular tax depreciation provided by the federal MACRS  
26 depreciation system. The extra bonus tax depreciation allowed by the PATH Act creates

---

<sup>28</sup> IRC § 168(k).

<sup>29</sup> LPPP is defined as property with a MACRS tax depreciation life of at least 10 years, a cost exceeding \$1 million, and a construction period of one year or more. IRC § 168(k)(2)(B)(i).

<sup>30</sup> IRC § 168(k)(2)(B).

<sup>31</sup> IRC § 168(k)(1)(A).

<sup>32</sup> IRC § 168(k)(6).

<sup>33</sup> *Id.*

1 additional deferred taxes equal to the extra bonus depreciation multiplied by the 35% federal  
2 income tax rate. The impact of the PATH Act's extension of bonus depreciation on SDG&E's  
3 2015 and 2016 tax years was reflected in D.16-06-054 (SDG&E's 2016 GRC Decision);<sup>34</sup>  
4 therefore, the additional deferred taxes created by the PATH Act's extension of bonus  
5 depreciation for 2015 through 2019 are reflected in the accumulated deferred tax balances for  
6 purposes of calculating rate base for TY 2019.

7 Except in the case of certain qualified self-constructed assets placed in service in 2005,  
8 bonus depreciation has not been calculated on property placed in service between January 1,  
9 2005 and December 31, 2007, when bonus depreciation was not allowed. The residual impact of  
10 bonus depreciation taken on qualified property placed in service in prior periods is reflected in  
11 the accumulated deferred income tax balances for 2016-2019.

## 12 **2. Contributions-in-Aid-of-Construction**

13 Contributions-in-aid-of-construction (CIAC) are non-refundable contributions collected  
14 from utility customers in the form of money – or its equivalent – toward the construction of  
15 plant, such as customer-requested relocations. CIAC became taxable under the TRA 86. The  
16 CPUC proposed the Maryland Method or Method 5 as acceptable alternatives for the ratemaking  
17 treatment of CIAC in D.87-09-026.<sup>35</sup> SDG&E elected the Maryland Method to account for the  
18 tax impacts of CIAC and the related income tax component of CIAC (ITCC) as required by the  
19 TRA 86. Under the Maryland Method, the utility shareholders bear the impact of any shortfall  
20 between the tax liability and the tax gross-up ITCC collected from the contributor. The  
21 shareholders recover the shortfall through the tax depreciation benefits on the constructed  
22 property. Accordingly, there is no impact on rate base under the Maryland Method. In  
23 accordance with D.87-09-026, SDG&E has not reflected any impact on rate base for the tax paid  
24 on CIAC income and the related ITCC received subsequent to February 10, 1987, the date that  
25 CIAC became taxable under the TRA 86.

## 26 **D. Summary Tables**

27 The following summary tables reflect the federal and state income taxes applicable to this  
28 filing. The "Electric Distribution" tables, Table SDG&E-RGR-3-1 and Table SDG&E-RGR-4-  
29 1, include electric distribution and electric generation for 2016.

---

<sup>34</sup> See D.16-06-054 at 213.

<sup>35</sup> 1987 Cal. PUC LEXIS 195; 25 CPUC 2d 299.

**Table SDG&E-RGR-3-1**  
**Electric Distribution**  
**Calculation of Federal & State Income Taxes**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
1	Total Operating Revenue	1,307,232	1,279,115	1,327,476	1,530,300
2	O&M Expenses	(496,259)	(496,091)	(517,692)	(615,934)
3	Taxes Other than Income Taxes	(69,270)	(68,785)	(74,709)	(83,799)
4	Book Income Before Depr. & Income Taxes	741,703	714,240	735,076	830,568
5	State Tax Adjustments	(537,554)	(479,170)	(548,026)	(605,423)
6	Taxable Income	204,149	235,070	187,051	225,144
7	CCFT Rate	8.84%	8.84%	8.84%	8.84%
8	<b>California Corporate Franchise Tax</b>	18,047	20,780	16,535	19,903
9	Book Income Before Depr. & Income Taxes (Line 4, above)	741,703	714,240	735,076	830,568
10	Federal Tax Adjustments	(559,948)	(468,328)	(543,922)	(634,613)
11	Taxable Income	181,755	245,912	191,154	195,954
12	Federal Income Tax Rate	35%	35%	35%	35%
13	Federal Income Tax Before Credits	63,614	86,069	66,904	68,584
14	Investment Tax Credit Amortization	(2,086)	(2,319)	(1,509)	(795)
15	Average Rate Assumption Method (ARAM)	(124)	(155)	(145)	(135)
16	Other	(720)	(121)	(24)	0
17	<b>Total Federal Income Tax</b>	60,685	83,474	65,227	67,655

**Table SDG&E-RGR-3-2**  
**Gas Distribution**  
**Calculation of Federal & State Income Taxes**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
1	Total Operating Revenue	292,458	348,900	377,156	432,617
2	O&M Expenses	(156,888)	(188,971)	(199,044)	(217,734)
3	Taxes Other than Income Taxes	(14,365)	(17,252)	(19,360)	(21,423)
4	Book Income Before Depr. & Income Taxes	121,206	142,677	158,752	193,459
5	State Tax Adjustments	(99,624)	(113,966)	(123,364)	(124,643)
6	Taxable Income	21,582	28,712	35,389	68,816
7	CCFT Rate	8.84%	8.84%	8.84%	8.84%
8	<b>California Corporate Franchise Tax</b>	1,908	2,538	3,128	6,083
9	Book Income Before Depr. & Income Taxes (Line 4, above)	121,206	142,677	158,752	193,459
10	Federal Tax Adjustments	(89,144)	(94,880)	(105,701)	(118,833)
11	Taxable Income	32,062	47,797	53,051	74,625
12	Federal Income Tax Rate	35%	35%	35%	35%
13	Federal Income Tax Before Credits	11,222	16,729	18,568	26,119
14	Investment Tax Credit Amortization	(513)	(513)	(513)	(209)
15	Average Rate Assumption Method (ARAM)	0	0	0	0
16	Other	(51)	(17)	(3)	0
17	<b>Total Federal Income Tax</b>	10,658	16,199	18,052	25,910

**Table SDG&E-RGR-3-3**  
**Electric Generation**  
**Calculation of Federal & State Income Taxes**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
1	Total Operating Revenue	-	209,675	204,923	280,112
2	O&M Expenses	-	(70,895)	(70,714)	(99,407)
3	Taxes Other than Income Taxes	-	(13,057)	(13,186)	(15,306)
4	Book Income Before Depr. & Income Taxes	-	125,723	121,022	165,399
5	State Tax Adjustments	-	(52,837)	(65,789)	(84,484)
6	Taxable Income	-	72,887	55,233	80,915
7	CCFT Rate	8.84%	8.84%	8.84%	8.84%
8	<b>California Corporate Franchise Tax</b>	-	6,443	4,883	7,153
9	Book Income Before Depr. & Income Taxes (Line 4, above)	-	125,723	121,022	165,399
10	Federal Tax Adjustments	-	(64,135)	(67,738)	(92,745)
11	Taxable Income	-	61,589	53,284	72,654
12	Federal Income Tax Rate	35%	35%	35%	35%
13	Federal Income Tax Before Credits	-	21,556	18,649	25,429
14	Investment Tax Credit Amortization	-	-	-	-
15	Average Rate Assumption Method (ARAM)	-	-	-	-
16	Other	-	-	-	-
17	<b>Total Federal Income Tax</b>	-	21,556	18,649	25,429

**Table SDG&E-RGR-4-1**  
**Electric Distribution**  
**Summary of Income Tax Adjustments**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
<b><u>Federal Tax Adjustments:</u></b>					
1	Tax Depreciation	(272,634)	(250,629)	(272,109)	(332,465)
2	Fixed Charges – Operating	(90,885)	(81,041)	(81,512)	(92,334)
3	Repairs	(81,226)	(76,656)	(118,007)	(154,393)
4	Software Development	(60,759)	(37,300)	(42,699)	(28,334)
5	Cost of Removal	(6,072)	(5,279)	(5,279)	(5,279)
6	Ad Valorem Tax - Fiscal/Calendar	(8,107)	(2,029)	(3,536)	(5,273)
7	Section 199 Deduction	-	-	-	-
8	Credit Addback & Other	35	-	-	-
9	Prior Year Calif. Corp. Franchise Tax	(40,300)	(15,394)	(20,780)	(16,535)
10	Total Federal Tax Adj. (Deduction)	<u>(559,948)</u>	<u>(468,328)</u>	<u>(543,922)</u>	<u>(634,613)</u>
<b><u>State Tax Adjustments:</u></b>					
11	Tax Depreciation	(252,870)	(241,916)	(261,893)	(284,670)
12	Fixed Charges – Operating	(90,551)	(80,760)	(81,284)	(92,123)
13	Repairs	(81,226)	(76,656)	(118,007)	(154,393)
14	Software Development	(60,759)	(37,300)	(42,699)	(28,334)
15	Cost of Removal	(44,318)	(40,630)	(40,630)	(40,630)
16	Ad Valorem Tax - Fiscal/Calendar	(8,107)	(2,029)	(3,536)	(5,273)
17	Credit Addback & Other	278	121	24	-
18	Total State Tax Adj. (Deduction)	<u>(537,554)</u>	<u>(479,170)</u>	<u>(548,026)</u>	<u>(605,423)</u>



**Table SDG&E-RGR-4-2**  
**Gas Distribution**  
**Summary of Income Tax Adjustments**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
<b><u>Federal Tax Adjustments:</u></b>					
1	Tax Depreciation	(40,473)	(45,900)	(52,785)	(67,664)
2	Fixed Charges – Operating	(14,852)	(17,248)	(17,905)	(21,148)
3	Repairs	(14,403)	(13,678)	(13,678)	(13,678)
4	Software Development	(9,797)	(15,382)	(17,608)	(11,684)
5	Cost of Removal	(295)	(279)	(279)	(279)
6	Ad Valorem Tax - Fiscal/Calendar	(1,314)	(486)	(908)	(1,252)
7	Section 199 Deduction	-	-	-	-
8	Credit Addback & Other	6	-	-	-
9	Prior Year Calif. Corp. Franchise Tax	(8,016)	(1,908)	(2,538)	(3,128)
10	Total Federal Tax Adj. (Deduction)	(89,144)	(94,880)	(105,701)	(118,833)
<b><u>State Tax Adjustments:</u></b>					
11	Tax Depreciation	(57,181)	(65,062)	(71,129)	(74,737)
12	Fixed Charges – Operating	(14,823)	(17,230)	(17,899)	(21,147)
13	Repairs	(14,403)	(13,678)	(13,678)	(13,678)
14	Software Development	(9,797)	(15,382)	(17,608)	(11,684)
15	Cost of Removal	(2,151)	(2,144)	(2,144)	(2,144)
16	Ad Valorem Tax - Fiscal/Calendar	(1,314)	(486)	(908)	(1,252)
17	Credit Addback & Other	45	17	3	-
18	Total State Tax Adj. (Deduction)	(99,624)	(113,966)	(123,364)	(124,643)

1

**Table SDG&E-RGR-4-3**  
**Electric Generation**  
**Summary of Income Tax Adjustments**  
**(\$ in Thousands)**

<i>Line No.</i>	<i>Description</i>	<i>2016 Recorded</i>	<i>2017 Estimated</i>	<i>2018 Estimated</i>	<i>2019 Test Year</i>
<b><u>Federal Tax Adjustments:</u></b>					
1	Tax Depreciation	-	(43,057)	(44,258)	(63,755)
2	Fixed Charges – Operating	-	(14,921)	(13,497)	(18,565)
3	Repairs	-	-	-	-
4	Software Development	-	-	-	-
5	Cost of Removal	-	-	-	-
6	Ad Valorem Tax - Fiscal/Calendar	-	(19)	(55)	(2,059)
7	Section 199 Deduction	-	(3,484)	(3,484)	(3,484)
8	Credit Addback & Other	-	-	-	-
9	Prior Year Calif. Corp. Franchise Tax	-	(2,653)	(6,443)	(4,883)
10	Total Federal Tax Adj. (Deduction)	-	(64,135)	(67,738)	(92,745)
<b><u>State Tax Adjustments:</u></b>					
11	Tax Depreciation	-	(37,896)	(52,237)	(63,860)
12	Fixed Charges – Operating	-	(14,921)	(13,497)	(18,565)
13	Repairs	-	-	-	-
14	Software Development	-	-	-	-
15	Cost of Removal	-	-	-	-
16	Ad Valorem Tax - Fiscal/Calendar	-	(19)	(55)	(2,059)
17	Credit Addback & Other	-	-	-	-
18	Total State Tax Adj. (Deduction)	-	(52,837)	(65,789)	(84,484)

2

## **E. Results**

3

4

5

6

7

The increase in federal and state income tax expense from 2016 to TY 2019 is primarily a function of increasing book income before taxes resulting from the return on a growing rate base (see the testimony of R. Craig Gentes, Exhibit SDG&E-33, for a discussion of rate base). Federal and state tax adjustments are also growing annually, partially offsetting the growth in book income before taxes from 2016 to TY 2019.

1           **F.      Tax Memorandum Account**

2                   **1.      Background**

3           In SDG&E's 2016 GRC Decision,<sup>36</sup> the Commission instructed SDG&E to establish a  
4 TMA for the 2016 GRC cycle (January 1, 2016 – December 31, 2018).<sup>37</sup> As stated by the  
5 Commission, the purpose of the TMA "is to increase the transparency of the utilities' incurred  
6 and forecasted income tax expenses to the Commission, so that the Commission can more  
7 closely examine the revenue impacts caused by the utilities' implementation of various tax laws,  
8 tax policies, tax accounting changes, or tax procedure changes."<sup>38</sup> The TMA "shall remain open  
9 and the balance in the account shall be reviewed in every subsequent GRC proceeding until a  
10 Commission decision closes the account."<sup>39</sup>

11           Pursuant to the Commission's directives, SDG&E filed Advice Letter No. 2928-E-  
12 A/2496-G-A on September 16, 2016 to establish the TMA. As further discussed in the testimony  
13 of SDG&E witness Norma Jasso (Exhibit SDG&E-41), the TMA is a two-way tracking account  
14 that separately tracks the revenue requirement impact of the differences between tax expenses  
15 forecasted and tax expenses incurred resulting from: (1) net revenue changes resulting from  
16 differences between forecasted federal and state tax adjustments and tax credits to incurred  
17 federal and state tax adjustments and tax credits; (2) mandatory tax law changes, tax accounting  
18 changes, tax procedural changes, and tax policy changes; (3) elective tax law changes, tax  
19 accounting changes, tax procedural changes, and tax policy changes; (4) the completion of audits  
20 by federal and state taxing authorities; and (5) the implementation of any IRS private letter ruling  
21 regarding compliance with IRS normalization regulations.

22           The Commission approved Advice Letter No. 2928-E-A/2496-G-A on December 5,  
23 2016. Consistent with D.16-06-054, SDG&E is tracking and will continue to track the items in  
24 the TMA in accordance with the provisions of Advice Letter No. 2928-E-A/2496-G-A until such  
25 time that the Commission closes the account.

---

<sup>36</sup> D.16-06-054.

<sup>37</sup> *Id.* at Ordering Paragraph 4.

<sup>38</sup> *Id.* at 196.

<sup>39</sup> *Id.*

1                   **2. Clarification of the Scope and Intent of the TMA from PG&E's 2017**  
2                   **GRC Decision**

3           In its final decision in Pacific Gas and Electric Company's (PG&E's) 2017 GRC, the  
4 CPUC instructed PG&E to establish a TMA "consistent with our identical orders in the SDG&E  
5 and SoCalGas Test Year 2016 proceeding."<sup>40</sup> The stated purpose, terms, and requirements of  
6 PG&E's TMA were identical to what the CPUC had ordered in SDG&E's 2016 GRC Decision.<sup>41</sup>

7           In comments to its proposed decision, PG&E raised several policy and practical concerns  
8 regarding the TMA, including the concern that, to the extent the TMA requires PG&E to true-up  
9 forecasted tax expenses for ratemaking purposes to the actual tax expenses incurred, the TMA is  
10 inconsistent with the CPUC's longstanding policy as stated in OII 24. The CPUC's policy as set  
11 forth in OII 24 is discussed below.

12                   **a. CPUC's Policy on True Up of Income Taxes**

13           The CPUC held in OII 24 that the impact of tax adjustments in excess of or below what  
14 was forecasted in the GRC generally should not be trued up.<sup>42</sup> In its decision, the CPUC  
15 explained the view expressed by both CPUC staff and Industry representatives that seeking a  
16 change from this general ratemaking policy for a particular, isolated tax item would not be  
17 appropriate:

18                   Staff and Industry agree . . . that differences in income taxes between  
19 estimated and actual cannot be isolated from other factors in determining  
20 whether an adjustment should be made to the test-year estimate. Any  
21 review of differences would have to include the effects of differences of  
22 all estimates for revenues, operating expenses, income taxes and return on  
23 investment. Any prospective adjustment based on past over- or  
24 underestimates would have to take into consideration the overall effect of  
25 the differences for all components of the test-year. Under these  
26 circumstances parties recommend no change in the present ratemaking  
27 procedure.<sup>43</sup>

28           The CPUC in OII 24 agreed with the recommendation of the parties that it generally was  
29 not appropriate and not good policy to true up forecasted income taxes to actual amounts:

---

<sup>40</sup> D.17-05-013 at 116.

<sup>41</sup> *Id.* at 116-117.

<sup>42</sup> *See* 1984 Cal. PUC LEXIS 1325 at \*33-34 ("such differences are inherent in the use of future test periods for ratemaking . . . Since income taxes are derived residually, we agree that individual factors should not be isolated for purposes of comparing estimated and recorded results.").

<sup>43</sup> *Id.* at \*33.

1 Since income taxes are derived residually, we agree that individual factors  
2 should not be isolated for purposes of comparing estimated and recorded  
3 results. Obviously, if the utility earnings are substantially less than  
4 authorized, then a comparison of estimated and actual income taxes is  
5 misleading. Moreover, an across-the-board comparison of estimated and  
6 recorded results is not useful for any purpose other than informational,  
7 because it is consistent with test-year ratemaking.<sup>44</sup>

8 **b. CPUC's Response to PG&E's Comments**

9 The CPUC addressed PG&E's comments and clarified that the intent of the TMA is not  
10 to adopt a true-up mechanism for taxes, and that the CPUC has not changed its longstanding  
11 policy on this issue:

12 PG&E's arguments rely on an incomplete reading of D.84-05-036 to  
13 oppose an outcome that is not, in fact, part of the APD. The Commission  
14 begins D.84-05-036 with an explanation that "[i]n the order that instituted  
15 this investigation we stated "the determination of reasonable allowable  
16 ratemaking expenses for federal and state income taxes is a matter of  
17 continuing concern to this Commission in its effort to establish reasonable  
18 utility rates." The Commission then addresses a number of specific  
19 questions with respect to taxes and appropriate ratemaking policies.  
20 PG&E cites D.84-05-036 and asserts that "[t]he Commission  
21 acknowledged that differences between estimated and recorded tax  
22 deductions and correspondingly estimated and recorded tax expense will  
23 occur in the ratemaking process and concluded that a true-up mechanism  
24 for taxes is not good policy." While the Commission does decline to  
25 "require utilities to submit adjustments reflecting reductions in taxes", it  
26 qualifies this result by stating "[w]e agree that changes in tax laws may be  
27 taken into account in ratemaking". The APD does not adopt any sort of  
28 "true-up mechanism"—rather, it adopts a mechanism that will provide the  
29 Commission with the information that it needs so that "changes in tax laws  
30 may be taken into account in ratemaking." PG&E appears concerned that  
31 the APD adopts what PG&E terms an "actual taxes" standard, stating "[i]n  
32 light of the widely recognized problems inherent in an actual taxes  
33 standard, it would be expected that a change in policy be preceded by a  
34 well-articulated explanation; however, the APD makes no reference to OII  
35 24, let alone an attempt to rationalize the APD's outcome against the  
36 instruction in OII 24." Again, the APD makes no such change in policy.<sup>45</sup>

---

<sup>44</sup> *Id.* at \*34.

<sup>45</sup> D.17-05-013 at 226-227 (citations omitted).

1 Accordingly, the CPUC clearly articulated in its decision in the PG&E 2017 GRC that  
2 the purpose and intent of the TMA is not to true up forecasted taxes to actual taxes, but rather to  
3 gain a better understanding of and visibility into “the revenue impacts caused by the utilities’  
4 implementation of various tax laws, tax policies, tax accounting changes, or tax procedure  
5 changes.”<sup>46</sup>

### 6 **3. 2016 TMA Balances**

7 Based on the foregoing and in accordance with D.16-06-054, SDG&E presents the 2016  
8 TMA balance. A schedule that shows the TMA balances for 2016 (TMA Schedule) is attached  
9 as Appendix B. In order to provide additional transparency to the CPUC, and consistent with the  
10 CPUC’s clarifications regarding the purpose and scope of the TMA as articulated in PG&E’s  
11 2017 GRC decision, the TMA Schedule separates the amount for each line item between: (a) the  
12 impact of differences between forecasted and incurred amounts related to changes in tax law, tax  
13 accounting, tax procedure, or tax policy, holding all other forecast items constant; and (b) the  
14 impact of differences not related to changes in tax law, tax accounting, tax procedure, or tax  
15 policy (*i.e.*, differences caused by differences in revenue, capital expenditures, the timing of  
16 when an asset is placed in service, etc.), holding all other forecast items constant. If the change  
17 in tax expense would decrease revenue, the amount is shown as a credit. If the change in tax  
18 expense would increase revenue, the amount is shown as a debit. Each line item in the TMA  
19 Schedule is discussed in turn, below.

#### 20 **a. Net Revenue Changes**

21 The definition and scope of the “Net Revenue Changes” tracking item ordered by the  
22 Commission is unclear to SDG&E. SDG&E has interpreted “Net Revenue Changes” to mean  
23 the revenue impact of differences between incurred and authorized 2016 amounts for all income  
24 tax adjustments and credits.<sup>47</sup> As shown in the TMA Schedule, none of these differences for  
25 2016 were caused by changes in tax law, tax accounting, tax procedure, or tax policy. Rather,

---

<sup>46</sup> D.16-06-054 at 196; *see also* D.17-05-013 at 116-117.

<sup>47</sup> During a telephone call on August 1, 2017, the Commission’s Energy Division provided clarifying guidance to SDG&E that the Energy Division would also like to see the differences between incurred and authorized net operating loss carryforwards as a separately stated item in the TMA. Pursuant to the Energy Division’s guidance, the TMA Schedule also includes the net operating loss carryforward amounts for 2016.

1 the differences between the incurred and authorized amounts were derived from residual factors  
2 outside of tax and thus represent the type of tax “true-up” discussed and rejected in OII 24.

3 **b. Completion of Audits**

4 There was no revenue impact for 2016 from completed federal or state audits.

5 **c. IRS Rulings on Normalization Issues**

6 There was no revenue impact from IRS Private Letter Rulings on normalization issues in  
7 2016.

8 **d. Mandatory Changes in Tax Law, Tax Accounting, Tax**  
9 **Procedures, or Tax Policy**

10 There was no revenue impact from mandatory changes in tax law, tax accounting, tax  
11 procedures, or tax policy in 2016.

12 **e. Elective Changes in Tax Law, Tax Accounting, Tax**  
13 **Procedures, or Tax Policy**

14 There was no revenue impact from elective changes in tax law, tax procedures or tax  
15 policy in 2016.<sup>48</sup>

16 SDG&E has not made any tax accounting method changes for 2016 as of the date of this  
17 Application; however, during 2016, SDG&E adopted Accounting Standard Update (ASU) 2016-  
18 09 – Improvements to Employee Share-based Payment Accounting, issued by Financial  
19 Accounting Standards Board (FASB) in March, 2016. The FASB issued this ASU to simplify  
20 several aspects of the accounting for employee share-based payment transactions. Under ASU  
21 2016-09, excess tax benefits and tax deficiencies, which represent the difference between the tax  
22 return deduction amounts and the compensation cost recognized for financial reporting purposes,  
23 are required to be recognized as income tax expense or benefit in the income statement instead of  
24 in additional paid-in-capital (APIC) on the balance sheet. This book accounting change does not  
25 impact or change the deduction or loss companies take on their tax returns relating to the share-  
26 based payments.

---

<sup>48</sup> The impact of the bonus depreciation extension under the PATH Act was incorporated in SDG&E’s 2016 GRC Decision; therefore, there is no 2016 impact to track for the PATH Act legislation since SDG&E’s 2016 GRC Decision reflects the 2016 50% bonus depreciation rate for the GRC period (*i.e.*, through 2018). SDG&E does expect to have a revenue impact related to the PATH Act legislation in its 2018 TMA, when the actual bonus depreciation rate drops from 50% to 40%. SDG&E will track any such revenue impact in its TMA for 2018.

1 ASU 2016-09 does not require any filing with or permission from the IRS or other taxing  
2 authority to implement; rather, it is purely a book accounting change under Generally Accepted  
3 Accounting Principles (GAAP). Therefore, the adoption of ASU 2016-09 is likely outside the  
4 definition of the items that the CPUC ordered SDG&E to track in its TMA. SDG&E believes,  
5 however, that including the revenue impact of this book accounting change is consistent with the  
6 CPUC's desire to increase transparency and visibility of accounting elections that potentially  
7 impact revenues; therefore, SDG&E has tracked the 2016 revenue impact of the book accounting  
8 change, as reflected in the TMA Schedule.

9 The book expense relating to the share-based payments, also called the Long Term  
10 Incentive Plan (LTIP), has not been included in the GRC revenue requirement approved by the  
11 CPUC since 2008, and thus the entire costs of the LTIP has been borne by the shareholders since  
12 2008. Accordingly, the majority of tax benefit recognized as tax expense on the income  
13 statement in 2016 from SDG&E's adoption of ASU 2016-09 was funded by shareholders. There  
14 was, however, a portion of the tax benefit recognized in 2016 related to stock options issued  
15 prior to 2008. Specifically, in its 2004 GRC, SDG&E was granted 50% recovery of the LTIP  
16 costs through rates, and the remaining 50% of the LTIP costs were determined to be shareholder-  
17 funded.<sup>49</sup> The revenue requirement impact of the ratepayer-funded portion of the tax benefit  
18 from the LTIP costs in SDG&E's 2004 GRC is reflected in the TMA Schedule.<sup>50</sup>

#### 19 **4. Proposal for 2019 GRC Cycle**

20 During SDG&E's 2019 GRC cycle, SDG&E will continue to notify the Commission of  
21 any tax-related law changes, accounting changes, policy changes, or procedural changes that  
22 materially affect (or may materially affect) revenues,<sup>51</sup> and will continue to report the revenue  
23 impact of any such changes to the Commission. SDG&E believes that continuing to notify the  
24 Commission of such changes and the corresponding revenue impact during the 2019 GRC cycle  
25 is consistent with the CPUC's policy goals of gaining better visibility into the utilities' elections  
26 of various tax options, as stated by the Commission in SDG&E's 2016 GRC Decision and as  
27 reiterated and clarified in PG&E's 2017 GRC Decision. Accordingly, SDG&E believes a TMA

---

<sup>49</sup> See D.04-12-015.

<sup>50</sup> As discussed earlier, SDG&E follows the CPUC's policy of excluding expenses not borne by customers in the calculation of income tax expense, as articulated by the CPUC in OII 24.

<sup>51</sup> Consistent with SDG&E's 2016 GRC Decision, "materially affect" for this purpose means a potential increase or decrease of \$3 million or more.



1 is no longer necessary and requests that the Commission eliminate the TMA for SDG&E's 2019  
2 GRC cycle.

3 If the Commission disagrees with SDG&E and believes that a TMA is necessary for the  
4 2019 GRC cycle, SDG&E proposes that the Commission reaffirm that the TMA is not intended  
5 to be a true-up mechanism for taxes (and thus is not intended to track the differences between  
6 forecasted and actual tax deductions that are caused by factors outside of tax and are unrelated to  
7 changes in tax law, tax accounting methods, tax procedures, or tax policy), but is intended to  
8 track the revenue impact of changes in tax law, tax accounting methods, tax procedures, and tax  
9 policy. Such a reaffirmation would be consistent with the Commission's long-standing policy of  
10 not trueing-up differences between forecasted and actual tax deductions, as articulated by the  
11 Commission in OII 24 and in D.17-05-013. Accordingly, the differences, positive or negative,  
12 between forecasted and actual tax expenses caused by derivative factors outside of tax and  
13 unrelated to changes in tax law, tax accounting methods, tax procedures, or tax policy would  
14 continue to flow to SDG&E's bottom line for each taxable year, consistent with the  
15 Commission's long-standing policy.<sup>52</sup> If the Commission is considering changing its long-  
16 standing policy on taxes and adopting an actual taxes standard, SDG&E believes that the  
17 Commission should first initiate an Order Instituting Rulemaking (OIR) or other regulatory  
18 proceeding with all the utilities under the Commission's jurisdiction to evaluate the potential  
19 impact of such a policy change.

## 20 **V. FRANCHISE FEES**

### 21 **A. Introduction**

22 The purpose of this section is to provide background and analysis for SDG&E's  
23 Franchise Fees as estimated for TY 2019.

### 24 **B. Discussion**

25 Franchise fees are payments made to counties and incorporated cities pursuant to local  
26 ordinances granting a franchise to the company to place utility property in the public rights of  
27 way. These facilities include poles, wires, conduits, and appurtenances for transmitting and  
28 distributing electricity, and pipes and appurtenances for transmitting and distributing gas.  
29 Franchise fees attributable to income from transmitting electricity are excluded from the

---

<sup>52</sup> See 1984 Cal. PUC LEXIS 1325 at \*33-34.

1 following franchise fee calculations. As of January 1, 2017, SDG&E had franchise fee  
2 agreements with 28 taxing jurisdictions.

3 The franchise fee requirements are based upon gross receipts representing the recovery of  
4 base margin. The franchise factors upon which the estimated 2017-2019 franchise fees were  
5 determined are based on a summary of 2016 electric and gas sales, transportation revenues, rate  
6 refunds, and uncollectibles. The factors were adjusted to forecasted 2019 levels based on  
7 historical trends in franchise payment data.

8 Franchises are calculated using two formulas: (1) the “Broughton Act” formula, and (2)  
9 the “Percent of Gross Receipts” formula. The Broughton Act formula, as prescribed by CPUC  
10 guidelines, is calculated based upon the summarized receipts within each city or county as  
11 allocated by electric pole line and gas pipeline mileage in their public rights of way, and the  
12 applicable franchise fee rate pursuant to the franchise fee ordinance. The Percent of Gross  
13 Receipts formula is calculated based upon the summarized receipts within each city or county,  
14 and the applicable franchise fee rate pursuant to the franchise fee ordinance.

15 The franchise agreement with each taxing authority specifies which of the above methods  
16 SDG&E will use to determine its franchise fee liability. The majority of agreements require that  
17 the franchise fee be calculated under both methods with SDG&E paying the higher of the two  
18 calculated fees. The remaining agreements specify that only the Broughton Act or Percent of  
19 Gross Receipts method be used.

20 The total payments to all taxing authorities were summed and divided by total receipts to  
21 arrive at system-wide franchise fee factors for electric and gas. The system-wide franchise fee  
22 factors for the most recent five years were then averaged to yield forecasted average franchise  
23 fee factors for TY 2019. The average electric franchise fee factor for TY 2019 is projected to be  
24 3.4468% based on the trend from actual 2012-2016 franchise fees. The average gas franchise fee  
25 factor for TY 2019 is projected to be 2.0799%, likewise based on the trend from actual 2012-  
26 2016 franchise fees.<sup>53</sup>

### 27 **C. Summary of Estimated Franchise Fees**

28 Table SDG&E-RGR-5-1 below provides the Franchise Fees as estimated for TY 2019.

---

<sup>53</sup> The forecast methodology used to estimate the franchise fee factor does not reflect ongoing or upcoming negotiations with local jurisdictions, the results of which may be implemented during this GRC cycle.

1

**Table SDG&E-RGR-5-1**  
**(\$ in Thousands)**

<b>Franchise Fees</b>	<b><i>Line No.</i></b>	<b><i>2016 Recorded</i></b>	<b><i>2017 Estimated</i></b>	<b><i>2018 Estimated</i></b>	<b><i>2019 Test Year</i></b>
<b>Electric Distribution</b>	1	44,643	43,632	45,248	52,230
<b>Gas Distribution</b>	2	6,088	7,195	7,783	8,936
<b>Electric Generation</b>	3	0	7,227	7,063	9,655

2

**D. Results**

3

As noted above, the change in franchise fee expense from 2016 to 2019 results from

4

changes in base margin as presented by other witnesses in their direct testimonies.

5

**VI. CONCLUSION**

6

This concludes my prepared direct testimony.

1 **VII. WITNESS QUALIFICATIONS**

2 My name is Ragan G. Reeves. I am employed by Sempra Energy, SDG&E's parent  
3 company, as a Principal Tax Counsel. My business address is 488 8<sup>th</sup> Avenue, HQ08N1, San  
4 Diego, California 92101-7123. I advise SDG&E and Sempra's other business units on the  
5 implications of federal and state tax law, including tax compliance issues, tax audit issues and  
6 strategies, and proposed acquisitions and restructurings.

7 Prior to joining Sempra Energy in 2005, I worked as a tax attorney for eight years at  
8 Miller & Chevalier, Chartered, in Washington, D.C., where my practice focused on tax credits,  
9 tax litigation, and tax controversy matters.

10 I received a Bachelor's of Business Administration in Accounting, a Masters in  
11 Professional Accounting, and a Juris Doctorate from the University of Texas at Austin. I am  
12 licensed to practice law in the District of Columbia and Texas, and I am a registered in-house  
13 counsel in California. I am also a licensed Certified Public Accountant in Texas.

14 I have previously testified before the CPUC.

## **APPENDIX A – GLOSSARY OF TERMS**

A.: Application

ACRS: Accelerated Cost Recovery System

ADFIT: accumulated deferred federal income tax

ADR: Asset Depreciation Range

AFUDC: allowance for funds used during construction

APIC: Additional Paid-In-Capital

ARAM: Average Rate Assumption Method

ASU: Accounting Standard Update

ATRA: American Taxpayer Relief Act of 2012

CEA: capitalized earnings ability

CCFT: California Corporation Franchise Tax

CET: California Employment Training

CIAC: contribution in aid of construction

CPUC: California Public Utilities Commission

CWIP: Construction Work in Progress

D.: Decision

ERTA: Economic Recovery Tax Act of 1981

FASB: Financial Accounting Standards Board

FICA: Federal Insurance Contributions Act

FTB: Franchise Tax Board

FUTA: Federal Unemployment Tax Act

GAAP: Generally Accepted Accounting Principles

HCLD: historical cost less depreciation

HI: Hospital Insurance (i.e., Medicare)

IRC: Internal Revenue Code

IRS: Internal Revenue Service

ITC: Investment Tax Credit

ITCC: Income Tax Component of CIAC

LTIP: Long Term Incentive Plan

LPPP: Long Production Period Property

MACRS: Modified Accelerated Cost Recovery System

O&M: Operations and Maintenance

OASDI: Old Age, Survivors, and Disability Insurance

OII: Order Instituting Investigation

OIR: Order Instituting Rulemaking

PATH Act: The Protecting Americans from Tax Hikes Act of 2015

PG&E: Pacific Gas and Electric Company

Regs: Treasury Regulations

SBE: California State Board of Equalization

SDG&E: San Diego Gas & Electric Company

SUI: State Unemployment Insurance

TMA: Tax Memorandum Account

TRA 86: Tax Reform Act of 1986

TY – Test Year

UI: Unemployment Insurance

**APPENDIX B  
TAX MEMORANDUM ACCOUNT TRACKING SCHEDULE**

<b>SDG&amp;E</b>																	
<b>Tax Memorandum Account Tracking Schedule</b>																	
<b>For the Tax Year Ended December 31, 2016</b>																	
(\$ amounts in thousands)																	
	<b>Incurred Amount <sup>1</sup></b>			<b>Amount Authorized in 2016 GRC</b>			<b>Difference</b>			<b>Difference NOT Related to Changes in Tax Law, Tax Accounting, Tax Procedure, or Tax Policy</b>			<b>Difference Related to Changes in Tax Law, Tax Accounting, Tax Procedure, or Tax Policy</b>				
	<b>Electric</b>	<b>Gas</b>	<b>Total</b>	<b>Electric</b>	<b>Gas</b>	<b>Total</b>	<b>Electric</b>	<b>Gas</b>	<b>Total</b>	<b>Electric</b>	<b>Gas</b>	<b>Total</b>	<b>Electric</b>	<b>Gas</b>	<b>Total</b>		
<b><u>1) Incurred vs Authorized Tax Adjustments and Credits</u></b>																	
Federal and State Tax Adjustments and Credits	(29,997)	(5,335)	(35,331)	(23,276)	(5,068)	(28,344)	(6,721)	(267)	(6,987)	(6,721)	(267)	(6,987)	0	0	0	[a]	
Federal Tax Impact of California Franchise Tax	2,397	865	3,262	695	462	1,157	1,702	403	2,106	1,702	403	2,106	0	0	0	[b]	
After-Tax Differences	(27,600)	(4,469)	(32,069)	(22,581)	(4,606)	(27,187)	(5,018)	137	(4,882)	(5,018)	137	(4,882)	0	0	0	[c] = [a] + [b]	
Gross-Up Rate Applied to Differences										1.68746	1.68746	1.68746	1.68746	1.68746	1.68746	[d]	
Subtotal										(8,469)	231	(8,238)	-	-	-	[e] = [c] * [d]	
Impact of Corollary Basis Adjustments										(62)	39	(24)	-	-	-	[f]	
Impact of Net Operating Loss ("NOL") Carryforwards	0	0	0	0	0	0	-	-	-	-	-	-	-	-	-	[g]	
Revenue Impact of Differences										(8,531)	269	(8,262)	0	0	0	[h] = [e] + [f] + [g]	
<b><u>2) Adjustments due to Completion of Audits</u></b>																	
None										0	0	0	0	0	0	[i]	
<b><u>3) Adjustments due to IRS Private Letter Rulings on</u></b>																	
None										0	0	0	0	0	0	[j]	
<b><u>4) Mandatory Changes in Tax Law, Tax Accounting, Tax Procedures, or Tax Policy</u></b>																	
None										0	0	0	0	0	0	[k]	
<b><u>5) Elective Changes in Tax Law, Tax Accounting, Tax Procedures, or Tax Policy</u></b>																	
Adoption of ASU 2016-09 -- Accounting for Employee Stock-Based Compensation:																	
Federal and State Tax Impact										-	-	-	(27)	(11)	(38)	[l]	
Gross-Up Rate										1.68746	1.68746	1.68746	1.68746	1.68746	1.68746	[m]	
Revenue Impact of Change										0	0	0	(45)	(19)	(64)	[n] = [l] * [m]	
<b>Total Revenue Impact of Differences/Changes</b>										(8,531)	269	(8,262)	(45)	(19)	(64)	[o] = [h] + [i] + [j] + [k] + [n]	
Interest (Payable)/Receivable										(1)	0	(1)	-	-	-	[p]	
<b>Ending Balance (Credit)/Debit</b>										<b>(8,532)</b>	<b>269</b>	<b>(8,263)</b>	<b>(45)</b>	<b>(19)</b>	<b>(64)</b>	<b>[q] = [o] + [p]</b>	
<sup>1</sup> Incurred amounts are subject to change until the income tax returns are filed and the federal and state audits are completed.																	