

SESSION OF 2020

**SUPPLEMENTAL NOTE ON SUBSTITUTE FOR SENATE
BILL NO. 126**

As Amended by Senate Committee of the Whole

Brief*

Sub. for SB 126 would create and amend law relating to the tracking and collection of state and federal income tax by certain public utilities.

Income Tax Exemption

The bill would exempt the following utilities from Kansas income tax for tax years ending on or after December 31, 2021:

- Every electric and natural gas public utility, as defined in law, that is subject to rate regulation by the KCC; and
- Any utility that is a cooperative, as defined in law, or owned by one or more cooperatives.

Additionally, such utilities would not be permitted to be included in a consolidated or unitary combined return, or to collect income tax as a component of retail rates.

Tracking Changes to Income Tax Collection

The bill would require a public utility, as defined in KSA 66-104, that includes expenses related to income taxes as a component of its retail rates to track and defer into a

*Supplemental notes are prepared by the Legislative Research Department and do not express legislative intent. The supplemental note and fiscal note for this bill may be accessed on the Internet at <http://www.kslegislature.org>

regulatory asset or liability, as appropriate, an overcollection or undercollection of income tax expenses if the income tax rates assessed on a utility are adjusted as a result of any changes in state or federal law.

Application for New Rates

The bill would require a utility to file an application for new retail rates reflecting adjusted income tax rates with the KCC within 60 days of enactment of such a change in state or federal law if the adjustment results in an overcollection or undercollection of income tax expenses that is equal to or exceeds 0.25 percent of a utility's KCC approved base revenue level from the utility's most recent rate proceeding. The utility would then be required to refund or collect the tracked amounts from their retail customers in a manner approved by the KCC.

KCC Order

The KCC would be required to issue an order addressing an application for adjusted retail rates due to a change in income tax expenses within 120 days. Such an order would be required to:

- If requested by the utility, give due consideration to the common interests of the utility and its customers, including but not limited to:
 - The use of a two-year implementation of current period rate changes to maintain the credit quality of the utility by ensuring that any such change in rates would not cause the utility's credit metrics that are traditionally considered by credit rating agencies to deteriorate to a level that could impair the utility's current credit rating.

If a retail rate change to address adjusted income tax expense is implemented over a period of time, the utility would be required to track and defer any overcollection or undercollection of income tax expenses as a regulatory liability or asset, as appropriate, that would accrue interest at the utility's weighted cost of capital, as determined by the KCC in the utility's most recent general rate proceeding, and refund or collect the balance in the next full general rate proceeding.

In the event a utility has a full general rate case pending or has notified the KCC of its intention to file such an application, at the time any adjusted income tax rates become effective, the bill would allow the KCC to issue an order finding that such adjusted income tax rates should not be reflected in retail rates until a utility's new retail rates become effective following its general rate proceeding. The bill would require the utility to demonstrate the public interest would be promoted by excluding adjusted income tax rates from its retail rates.

Full Rate Proceeding Clarification

The bill would make clear that a filing resulting from adjusted income tax rates could not require the utility to file a full general rate case, or require the utility to update any component of retail rates other than the income tax expense component. The bill would provide that rate updates resulting from changes in income tax expenses would not be considered a violation of any existing rate moratorium agreement.

Excess Accumulated Deferred Income Tax Balances

The bill would require excess accumulated deferred income tax balances resulting from income taxes adjusted due to changes in state or federal law remain unamortized on the utility's books of account until new retail rates from its

next full general rate proceeding after the adjusted income tax rates take effect, at which time such balances would be required to be amortized and reflected in retail rates.

If requested by the utility, excess accumulated deferred income tax balances resulting from changes in state law effective January 2021 would be amortized into retail rates over a period of not less than 30 years by order of the KCC.

Excess accumulated deferred income tax balances resulting from any other changes in state or federal law would be amortized into retail rates by order of the KCC in a manner consistent with requirements of state and federal tax law and relevant regulations, and in a manner that will not impair the utility's credit rating.

Municipal and Cooperative Utilities

The bill would clarify that provisions related to adjustments for state or federal income tax expenses would not apply to municipal electric or natural gas utilities, or to a cooperative.

Definitions

The bill would define "overcollection or undercollection of income tax expense" as the portion of utility revenue representing the difference between the cost of service as approved by the KCC in the utility's most recent base rate proceeding and the cost of service that would have resulted had the provision for state or federal income taxes been based upon the adjusted corporate income tax rate. The bill would specify that "overcollection or undercollection of income tax expense" would not include the effects of accumulated deferred income taxes or excess accumulated deferred income taxes.

Technical Changes

The bill also would make technical changes.

Background

The bill was introduced by the Senate Committee on Assessment and Taxation. The bill was referred to the Senate Committee on Utilities on February 8, 2019.

In the March 20, 2019, Senate Committee hearing, a representative of the Kansas Industrial Consumers Group (KICG) provided proponent testimony, stating reduction in utility income tax collection would directly reduce utility rates because tax expenses are passed on to consumers. Written-only proponent testimony was provided by representatives of Renew Kansas Association and the Kansas Grain and Feed Association.

Opponent testimony was provided by representatives of Black Hills Energy, Evergy, Kansas Gas Service, and Liberty Utilities. Opponents stated the bill could negatively impact certain deferred tax benefits that have accrued for utility customers, resulting in increased rates, multiple rate cases in a single year, and implementation of rate reductions at an unreasonable pace. Written-only opponent testimony was submitted by Atmos Energy Corporation.

Neutral testimony was provided by a representative of the KCC, outlining concerns with various provisions of the bill identified by KCC staff.

In the January 28, 2020, Senate Committee hearing, representatives of the Citizens' Utility Ratepayer Board (CURB), KICG, and the Wichita Regional Chamber of Commerce provided proponent testimony. The representatives stated generally the bill would offer an opportunity to lower electric rates for residential and industrial consumers. Written-only proponent testimony was provided

by Americans for Prosperity Kansas and by a representative of Renew Kansas Association and the Kansas Grain and Feed Association.

Opponent testimony was provided by representatives of Black Hills Energy, Evergy, Kansas Gas Service, Liberty Utilities, and Sunflower Electric Power Corporation. Opponents generally stated they are not opposed to the concept of the bill, but are concerned it would not achieve the desired result of lowering electric rates and have a negative impact on utility credit ratings.

Neutral testimony was provided by a representative of the KCC. The representative's testimony was substantially similar to testimony provided at the March 20, 2019, Senate Committee hearing.

The Senate Committee adopted a substitute bill that included the following changes:

- Allow provisions of the bill to apply in situations where income tax is undercollected;
- Establish what circumstances must exist before a utility must file an application for new rates;
- Clarify that a utility would not need to file a full general rate case when overcollection or undercollection of income tax occurs;
- Clarify that an application for adjusted rates would not constitute a violation of any existing rate moratorium agreement if it only updates income tax expense components of a utility's base rates;
- Establish requirements for an order issued by the KCC in response to an application for adjusted rates resulting from a change in state and federal income tax law;

- Clarify that provisions related to adjustments for state or federal income tax expenses would not apply to municipal electric or natural gas utilities, or a cooperative; and
- Clarify that provisions related to the income tax exemption would not apply to cooperative utilities or to a utility owned by one or more cooperative, subject to rate regulation by the KCC.

The Senate Committee of the Whole amended the bill to:

- Increase the amount of time a utility would have to file an application for new retail rates;
- Clarify how the rate of interest on a recorded income tax expense that is implemented over time is calculated;
- Clarify procedure when a utility has a pending rate case before the KCC, or has notified the KCC of such an intent at the time any adjusted income tax rates become effective;
- Clarify language regarding amortization of excess accumulated deferred income tax balances;
- Clarify provisions related to exemption from Kansas income tax;
- Clarify the definition of “overcollection and undercollection of income tax expense”; and
- Make several technical and conforming changes.

According to the fiscal note prepared by the Division of the Budget on the bill as introduced, the KCC indicates enactment of the bill would have no effect on agency expenditures. Additionally, the Department of Revenue was unable to determine the fiscal effect enactment of the bill

would have, if any, on the agency or state revenues. A fiscal note was not immediately available on the substitute bill, as recommended by the Senate Committee. Any fiscal effect associated with enactment of the bill is not reflected in *The FY 2020 Governor's Budget Report*.