

**THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS**

In the Matter of a General Investigation)
Regarding the Effect of Federal Income Tax)
Reform on the Revenue Requirements of) Docket No. 18-GIMX-248-GIV
Kansas Public Utilities and Request to Issue)
an Accounting Authority Order Requiring)
Certain Regulated Public Utilities to Defer)
Effects of Tax Reform to a Deferred)
Revenue Account.)

**STAFF'S MOTION TO OPEN GENERAL INVESTIGATION AND ISSUE
ACCOUNTING AUTHORITY ORDER REGARDING FEDERAL TAX REFORM**

The Staff of the Kansas Corporation Commission (Staff and Commission, respectively), hereby submits a Report and Recommendation (R&R) dated December 13, 2017, attached hereto and made a part hereof by reference, and moves for the Commission to issue an Order:

(1) Opening a general investigation for the purposes of examining the financial impact of anticipated federal income tax reform on regulated electric, natural gas, water, and telecommunications public utilities (identified in Staff's R&R) operating in Kansas;

(2) Requiring, through the use of an Accounting Authority Order (AAO), certain regulated public utilities (identified in Staff's R&R) that are taxed at the corporate level to track and accumulate in a deferred revenue account, with interest compounded monthly at the most current Commission-approved customer deposit interest rate, the reduction in their regulated cost of service that would occur in the event that a new lower federal income tax rate is signed into law. These deferrals should take effect at the same time as the new federal corporate tax rate change and the calculations should be performed using the cost of service data that was used to set the utilities' last Commission-approved revenue requirement (including any line-item surcharges that contain a provision for regulated income tax expense) or Kansas Universal Service Fund (KUSF) determination; and

(3) Confirming that the Commission's intention regarding the AAO is to preserve any potential tax benefits so that they may be evaluated in the context of a comprehensive evaluation of the reasonableness of the utilities' rates or KUSF distributions as well as notifying affected public utilities that this portion of their rates or KUSF distributions should be considered interim subject to refund until the Commission has an opportunity to review the reasonableness of the utilities' rates or KUSF distributions on a comprehensive and case-by-case basis. Lastly, the Commission should confirm that it intends to capture the reduction in Accumulated Deferred Income Tax (ADIT) balances that will occur in the event that a lower corporate federal income tax rate takes effect, over time, in a manner that comports with Internal Revenue Service (IRS) Tax Normalization Rules.

In support of its Motion, Staff states the following:

Background

1. The Tax Cuts and Jobs Act (TCJA) is a Congressional bill that amends the Internal Revenue Code (IRC) to reduce federal tax rates and modify policies, credits, and deductions for individuals and businesses.¹ It was first introduced in the U.S. House of Representatives on November 2, 2017, and passed by the House on November 16, 2017 (the House Bill).² On December 2, 2017, the U.S. Senate passed its version of the bill (the Senate Amendment).³ While both versions of the TCJA have similar framework overall, there are some key differences that will need to be resolved prior to sending a final bill to the President.⁴ As such, the TCJA is currently in reconciliation conference meetings.⁵ For corporations, the TCJA, among other changes, reduces the corporate tax rate from 35% to 20%.⁶

2. The lowering of the federal corporate tax rates could result in substantial reductions in the regulated cost of service for many utilities operating in Kansas.⁷ This is because the Commission, in determining rates, generally authorizes recovery of all federal taxes from ratepayers. Failure to recognize the reduction in federal taxes owed if the TCJA becomes law could result in a financial windfall to the utilities in terms of rates, or KUSF support, if applicable.

3. In 1986, in Docket No. 155,094-U, the Commission was faced with the issue of federal tax reform due to the Tax Reform Act of 1986.⁸ Similar to the TCJA, the Tax Reform Act of 1986 phased-in a reduction in corporate tax rates from 46% down to 40%, and finally 34%.⁹

¹Report and Recommendation, p. 2 (Dec. 13, 2017) (R&R).

²Id.

³Id.

⁴Id.

⁵Id.

⁶Id.

⁷Id. at 3.

⁸Id.

⁹Id.

The Commission, concerned that utilities would experience a financial windfall as a result of the tax reductions, but also recognizing that other cost of service components could offset the reductions, decided that it would review company-specific information and data on a case-by-case basis.¹⁰ However, to ensure that income tax savings were not lost to ratepayers, the Commission created a mechanism to capture the ratepayer benefits of the corporate tax reduction accruing during the review period.¹¹ The mechanism was stated as follows:

“Effective April 1, 1987, each utility...shall accrue monthly in an appropriate deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, a percentage of its revenues representing the difference in its cost of service, as determined by the Commission in its most recent rate order, and such cost of service had the federal income tax component been based on the blended rate of 38% rather than 46%. The blended rate of 38% for 1987 is derived by using the statutory rate of 46% for April, May and June and the statutory rate of 34% for July through December.

At such time as the Commission’s review is complete, if it is determined that a rate decrease is proper and would have been proper as of April 1, 1987, for those utilities...any excessive collections in the deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, with appropriate adjustments, shall be refundable to ratepayers along with interest calculated at the rate being used for interest paid on customer deposits. Any balance remaining in the account will be credited to the utility’s operating revenue.”¹²

Staff’s Request

4. Similar to the 155,095-U Docket, Staff requests that the Commission open a general investigation and order utilities to use deferral accounting to capture the effect of the reduction in the regulated cost of service for future evaluation on a case-by-case basis. In doing so, as of the effective date of the legislation, each affected utility that is taxable at the corporate level should accrue monthly, in a deferred revenue account, the portion of its revenue representing the

¹⁰Id. See Order Opening General Investigation, Docket No. 155,094-U (Mar. 18, 1987), attached to Staff’s R&R as Attachment A.

¹¹Id.

¹²Id.

difference between: (1) the cost of service as approved by the Commission in its most recent rate case¹³ or KUSF determination proceeding; and (2) the cost of service that would have resulted had the provision for federal income taxes been based on 20% (or the corporate income tax rate ultimately approved) rather than 35%.

5. For regulated telecommunications utilities that are not taxable at the corporate level, but instead pass through their taxable income to owners of the corporation, Staff is not recommending these utilities be required to utilize deferred accounting at this time.¹⁴

6. Staff also notes in its R&R that if the corporate tax rate is lowered, there will also be a significant reduction to the ADIT Liabilities and Assets on the regulated books of utilities operating in Kansas.¹⁵ This occurs because the deferred taxes on the books of regulated utilities will now be payable at the lower corporate tax rate, as opposed to the higher rate that was assumed when rates were set. This will amount to hundreds of millions of dollars of excess ADIT on the books of regulated utilities operating in Kansas. Staff's research of this issue indicates that Accounting Standards Codification (ASC) 980, Accounting for Regulated Operations, will require that regulated utilities account for the reduction in ADIT balances as a Regulatory Liability if it is probable that regulators will require a reduction in future revenue through rates in order to reflect the amortization or turnaround of this excess ADIT. Therefore, Staff also requests that the Commission confirm that it intends to capture excess ADIT for the benefit of ratepayers using a

¹³In this case, "rate case" should also include any line-item surcharge that contains a provision for regulated income taxes in the revenue requirement. Examples would be the Gas System Reliability Surcharge utilized by many natural gas utilities and the Asbury and Riverton Cost Recovery Rider utilized by the Empire District Electric Company.

¹⁴As explained in Staff's R&R, the effects on federal tax reform on the taxable liability of the owners of these companies will not be as easily identifiable as an entity that is taxed at the corporate level. While Staff will evaluate the financial impact of federal tax reform on these utilities, and will request the Commission open company-specific investigations in the event that Staff believes federal tax reform has had a material impact on the tax liabilities of the owners of these utilities, at this time Staff does not recommend any particular Commission action that would apply to those utilities.

¹⁵R&R at 5.

methodology that is consistent with the tax normalization requirements specified in the tax legislation or IRS Tax Normalization Rules, as applicable. This will ensure that these significant reductions in ADIT are preserved as a Regulatory Liability until the Commission has an opportunity to be flowing these excess ADIT balances back to ratepayers over time.

Jurisdiction and Authority

7. The Commission has full power, authority and jurisdiction to supervise and control the public utilities doing business in Kansas, and is empowered to do all things necessary and convenient for the exercise of such power, authority and jurisdiction. Specifically, the Commission is given this power, authority and jurisdiction under K.S.A. 66-101 for electric public utilities, K.S.A. 66-1,201 for natural gas public utilities, K.S.A. 66-1,188 for local exchange carriers, and K.S.A. 66-1,231 for miscellaneous public utilities. All Commission grants of power, authority, and jurisdiction are to be liberally construed, and all incidental powers necessary to carry into effect the provisions of the Public Utility Act are expressly granted to and conferred upon the Commission.¹⁶

8. The Commission has jurisdiction over utility rates pursuant to K.S.A. 66-117, K.S.A. 66-101b (Electric), K.S.A. 66-1,202 (Natural Gas), K.S.A. 66-1,189 (Telecommunications), and K.S.A. 66-1,232 (Miscellaneous). Furthermore, the Commission has jurisdiction over KUSF distributions pursuant to K.S.A. 66-2008.

WHEREFORE, for the reasons set forth above, Staff respectfully requests that the Commission issue an Order adopting Staff's recommendations, as contained in the attached R&R.¹⁷

¹⁶See K.S.A. 66-101g (Electric); K.S.A. 66-1,207 (Natural Gas); K.S.A. 66-1,194 (Telecommunications); K.S.A. 66-1,237 (Miscellaneous).

¹⁷The specific recommendations are also itemized on page 1 of this Motion, as items (1)-(3). Staff would also note that should the tax reform legislation fail to pass, Staff will recommend the Commission close this docket.

Respectfully Submitted,



Michael Neeley, S. Ct. #25027
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STATE OF KANSAS)
)
COUNTY OF SHAWNEE) ss.
)

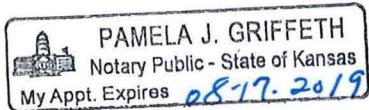
VERIFICATION

Michael Neeley, being duly sworn upon his oath deposes and states that he is Litigation Counsel for the State Corporation Commission of the State of Kansas, that he has read and is familiar with the foregoing *Staff's Motion to Open General Investigation and Issue Accounting Authority Order Regarding Federal Tax Reform* and that the statements contained therein are true and correct to the best of his knowledge, information and belief.



Michael Neeley # 25027
Kansas Corporation Commission of the
State of Kansas

Subscribed and sworn to before me this 14th day of December, 2017.



Pamela J. Griffeth
Notary Public

My Appointment Expires: August 17, 2019

REPORT AND RECOMMENDATION UTILITIES DIVISION

TO: Chairman Pat Apple
Commissioner Shari Feist Albrecht
Commissioner Jay Scott Emler

FROM: Andria Jackson, Managing Auditor
Justin Grady, Chief of Accounting and Financial Analysis
Jeff McClanahan, Director of Utilities

DATE: December 13, 2017

SUBJECT: Recommendation to Initiate a General Investigation Regarding the Effect of Federal Income Tax Reform on the Revenue Requirements of Kansas Public Utilities and Issue an Accounting Authority Order.

EXECUTIVE SUMMARY:

For the first time in 30 years, there is a strong push to enact sweeping federal income tax reform. Currently, both the U.S. House of Representatives and the U.S. Senate have passed tax reform legislation. While each version of the bill varies to some degree, both call for a significant reduction in the corporate income tax rate from 35% to 20% and reductions in the taxation of business income of pass-through entities that is taxed at the personal level. With tax reform currently in reconciliation conference meetings and the administration pushing to sign comprehensive tax reform legislation before the end of the year, Staff recommends the Commission open a general investigation to analyze the potential impacts of federal tax reform on Kansas public utilities.

Additionally, Staff requests the Commission issue an Accounting Authority Order (AAO) in this general investigation docket requiring all taxable, regulated electric, natural gas, water¹, and telecommunication public utilities² to track and accumulate, in a deferred revenue account, the portion of its revenue that results from the use of a 35% federal corporate tax rate for its last

¹ Staff's definition of electric, natural gas, and water utilities excludes any public utility not rate regulated by the Commission pursuant to K.S.A. 66-104 *et.seq.*

² Staff's definition of telecommunications public utilities only includes local exchange carriers as defined by K.S.A. 66-1,187(h) that currently receive KUSF support.

Commission-approved revenue determination (or Kansas Universal Service Fund (KUSF) distribution) instead of the new lower federal corporate tax rate. These deferrals should commence as of the effective date of the new federal corporate tax rate as applicable to the utility and should accrue interest at the Commission-approved rate used to compensate customers for customer deposits held by the utility.³

The AAO should also state that it is the intention of this Commission to capture, for the benefit of ratepayers, over the time period that is consistent with Tax Normalization Rules, the excess deferred taxes that will result if a lower federal corporate tax rate is established. The combined effects of these statements in the AAO will be to put taxable regulated utilities operating in Kansas on notice that the portion of their current rates and KUSF distributions that are impacted by federal tax reform should be considered interim and subject to refund, with interest, until the Commission has an opportunity to evaluate the reasonableness of those rates or KUSF distributions with new lower federal tax rates.

This general investigation will allow Staff and the Commission to evaluate the effects of new lower federal tax rates for all taxable regulated public utilities operating in Kansas on an individual, case-by-case basis. The AAO will ensure that these tax benefits that should accrue to ratepayers and contributors to the KUSF are not lost to regulatory lag while this review takes place. Ultimately, the goal of the general investigation will be to quantify the economic impacts of the new lower tax rates on Kansas utilities and pass the cost savings on to Kansas utility consumers and contributors to the KUSF as rapidly as possible. If ultimately the tax reform legislation does not become law, Staff will recommend the Commission close the docket.

BACKGROUND:

The Tax Cuts and Jobs Act is a Congressional bill that amends the Internal Revenue Code to reduce tax rates and modify policies, credits, and deductions for individuals and businesses. The bill was introduced in the House of Representatives on November 2, 2017, and was passed on November 16, 2017 (the House Bill).⁴ On December 2, 2017, the Senate passed its version of the bill (the Senate Amendment).⁵ While both versions of the bill have similar framework overall, there are some key differences that will need to be resolved prior to sending a final bill to the President.⁶ As such, the bill is currently in reconciliation conference meetings. For corporations, the bill, amongst other changes, reduces the corporate tax rate from 35% to a 20% rate.⁷

³ Interest on the deferred revenue account should compound monthly, and reflect the most recent Commission-approved customer deposit interest rate.

⁴ H.R. 1, 115th Cong., 1st Sess. (2017). The U.S. House bill can be found here: https://waysandmeans.house.gov/uploadedfiles/bill_text.pdf.

⁵ S. Amdt. 1855, 115th Cong., 1st Sess. (2017). The version of tax reform that passed the U.S. Senate can be found here: <https://www.finance.senate.gov/imo/media/doc/12.2.17%20HR%201.PDF>.

⁶ For a summary of the key differences between the House Bill and the Senate Amendment, see: <https://www.jct.gov/publications.html?func=startdown&id=5048>.

⁷ Under the House proposal, the 20% federal income tax rate becomes effective January 1, 2018, and under the Senate proposal, the rate would become effective January 1, 2019. There are also key differences in the two bills regarding renewable energy tax credits and their ability to be utilized to offset taxable income.

The lowering of the federal corporate tax rates would result in substantial reductions in the regulated cost of service for many utilities operating in Kansas. In addition, some regulated telecommunications companies that receive distributions from the KUSF are pass-through tax entities, such as S-Corps and LLCs. These entities do not pay corporate taxes at the utility level, but instead pass through their taxable income to their owners, which is then taxable at the individual taxpayer level.⁸ Both the House Bill and the Senate Amendment contain significant reductions in the taxability of pass-through, business income taxed at the personal level.

The last time Congress passed a sweeping tax reform act was the Tax Reform Act of 1986 (the Act) which was signed into law on October 22, 1986. In response, the Commission initiated Docket No. 155,094-U (155,094-U Docket) as a general investigation to analyze the impacts of the tax reform.⁹ The Act resulted in a phased-in reduction in corporate tax rates from 46% to 40% to 34%, which was anticipated to provide substantial cost savings to many Kansas utilities and to have additional impacts on the revenue requirements of the utilities. The Commission was concerned that utilities could experience a financial windfall as a result of the tax reductions but also realized that, despite the tax reductions, other costs of service components could offset the reductions. Therefore, the Commission ordered the review of company-specific information and data on a case-by-case basis. In an attempt to ensure that income tax savings were not lost to ratepayers, the Commission created a mechanism to capture the ratepayer benefits of the corporate tax reduction accruing during the review period. The mechanism was stated as follows:

“Effective April 1, 1987, each utility...shall accrue monthly in an appropriate deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, a percentage of its revenues representing the difference in its cost of service, as determined by the Commission in its most recent rate order, and such cost of service had the federal income tax component been based on the blended rate of 38% rather than 46%. The blended rate of 38% for 1987 is derived by using the statutory rate of 46% for April, May and June and the statutory rate of 34% for July through December.

At such time as the Commission’s review is complete, if it is determined that a rate decrease is proper and would have been proper as of April 1, 1987, for those utilities... any excessive collections in the deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, with appropriate adjustments, shall be refundable to ratepayers along with interest calculated at the rate being used for interest paid on customer deposits. Any balance remaining in the account will be credited to the utility’s operating revenue.”¹⁰

Because the company reviews were on a case-by-case basis, the outcomes of Staff’s reviews varied between each company. Staff proposes the Commission take a similar approach in response to the current tax reform.

⁸ Staff’s approach to calculate income taxes in KUSF proceedings involving pass-through entities involves a determination of which tax calculation (C-Corp or S-Corp) results in the lowest amount of income tax payable. The calculation that produces the lowest tax liability on the regulated operations is utilized for purposes of setting the KUSF distribution amount.

⁹ See Attachment A for the 155,094-U Docket Order.

¹⁰ Order Opening General Investigation, Docket No. 155,094-U, ¶¶ 5-6 (Mar. 18, 1987).

ANALYSIS:

As noted above, the Tax Cuts and Jobs Act has not yet been signed by the President. However, the House Bill and Senate Amendment are currently in reconciliation conference meetings and it is widely anticipated that tax reform will be signed by the President before the first of the year. Because the ultimate timing of the passage of federal income tax reform is uncertain, as is the effective date of any legislation that may be passed, Staff requests the Commission open this general investigation and notify taxable utilities operating in Kansas that the portion of their regulated revenue stream that reflects higher corporate tax rates should be considered interim and subject to refund (with interest) until lower federal tax rates are factored into utilities' permanent rates or KUSF distributions.

Similar to the 155,094-U Docket, Staff requests the Commission order utilities to use deferral accounting to capture the effect of the reduction in the regulated cost of service for future evaluation on a case-by-case basis. In doing so, as of the effective date of the legislation, each utility (as defined above) that is taxable at the corporate level should accrue monthly, in a deferred revenue account, the portion of its revenue representing the difference between:

1. the cost of service as approved by the Commission in its most recent rate case¹¹ or KUSF determination proceeding; and
2. the cost of service that would have resulted had the provision for federal income taxes been based on 20% (or the corporate income tax rate ultimately approved) rather than 35%.

For regulated telecommunications utilities that are not taxable at the corporate level, but instead pass through their taxable income to owners of the corporation, Staff is not recommending these utilities be required to utilize deferral accounting at this time. The effects of federal tax reform on the taxable liability of the owners of these companies will not be as easily identifiable as an entity that is taxed at the corporate level. While Staff will evaluate the financial impact of federal tax reform on these utilities, and will request the Commission to open company-specific investigations in the event that Staff believes federal tax reform has had a material impact on the tax liabilities of the owners of these utilities, at this time Staff does not recommend any particular Commission action that would apply to those utilities.

Although the Commission generally examines a utility's revenue requirement from its overall cost of service, this situation warrants a different approach as a significant reduction in income tax expense should not become a windfall for utilities but should rather be captured and flowed back to ratepayers. Just as the Commission has allowed ratemaking for single issues without the examination of other components of cost of service in certain extraordinary circumstances, such as the costs of fuel, energy efficiency expenses, environmental expenditures, cyber security expenditures, etc., Staff contends that this circumstance calls for a mechanism to isolate the financial impact of the lower corporate tax rates in order to preserve these lower cost of service

¹¹ In this case, "rate case" should also include any line-item surcharge that contains a provision for regulated income taxes in the revenue requirement. Examples would be the Gas System Reliability Surcharge utilized by many natural gas utilities and the Asbury Environmental and Riverton Cost Recovery Rider utilized by Empire District Electric Company.

benefits for ratepayers. However, in the event that a utility believes that other costs of service have more than offset the decrease in its income tax expenses, it will have the ability to file such information and supporting data with the Commission to be reviewed and evaluated on a case-by-case basis.

The intent behind the use of this deferred accounting mechanism is to ensure that a utility is neither positively nor negatively affected by the passage of federal income tax reform. As income taxes are simply a pass-through in the cost of service for regulated utilities, a sudden and dramatic reduction in the level of this expense should not inure to the benefit of shareholders. Because the revenue that would be deferred as a result of Staff's recommendation will also be accompanied by an offsetting reduction to income tax expense, the utility's profitability levels should not be materially impacted as a result of the deferral accounting Staff recommends.

In addition to the reduction in annual book tax expense (and corresponding reduction in annual revenue requirement) that is anticipated if the corporate tax rate is lowered, there will also be a significant reduction on the Accumulated Deferred Income Tax (ADIT) Liabilities and Assets on the regulated books of utilities operating in Kansas. This occurs because the deferred taxes on the books of regulated utilities will now be payable at the lower corporate tax rate, as opposed to the higher rate that was assumed when rates were set. This will amount to hundreds of millions of dollars of excess ADIT on the books of regulated utilities operating in Kansas. Staff's research of this issue indicates that Accounting Standards Codification (ASC) 980, Accounting for Regulated Operations, will require that regulated utilities account for the reduction in ADIT balances as a Regulatory Liability, if it is probable that regulators will require a reduction in future revenue through rates in order to reflect the amortization or turnaround of this excess ADIT. Staff recommends that the Commission confirm that it intends to capture these excess deferred income taxes for the benefit of ratepayers using a methodology that is consistent with the tax normalization requirements specified in the tax legislation or Internal Revenue Service (IRS) Tax Normalization Rules, as applicable. This will ensure that these significant reductions in ADIT are preserved as a Regulatory Liability until the Commission has an opportunity to begin flowing these excess ADIT balances back to ratepayers over time.

RECOMMENDATION:

Staff recommends the Commission take the following specific actions:

1. Open a general investigation for the purposes of examining the financial impact of anticipated federal income tax reform on regulated electric, natural gas, water, and telecommunication public utilities (as clarified in footnotes 1 and 2 above) operating in Kansas.
2. Issue an AAO requiring all regulated public utilities (as defined above) that are taxed at the corporate level to track and accumulate in a deferred revenue account, with interest compounded monthly at the most current Commission-approved customer deposits interest rate, the reduction in their regulated cost of service that would occur in the event that a new lower federal income tax rate is signed into law. These deferrals should take effect at the same time as the new federal corporate tax rate change, and the calculations should be performed using the cost of service data that were used to set the utilities' last

Commission-approved revenue requirement (including any line-item surcharges that contain a provision for regulated income tax expense) or KUSF determination.

3. Confirm that the Commission's intention in these AAO rulings is to preserve these tax benefits so that they may be evaluated in the context of a comprehensive evaluation of the reasonableness of the utilities' rates or KUSF distributions, as well as notifying these public utilities that this portion of their rates or KUSF distributions should be considered interim subject to refund until the Commission has an opportunity to review the reasonableness of the utilities' rates or KUSF distributions on a comprehensive and case-by-case basis. Lastly, the Commission should confirm that it intends to capture the reduction in ADIT balances that will occur in the event that a lower corporate federal income tax rate takes effect, over time, in a manner that comports with IRS Tax Normalization Rules.

THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Attachment A

Before Commissioners: Michael Lennen, Chairman
Margalee Wright
Keith R. Henley

In the Matter of the Effects of the Federal Tax Reform Act of 1986 on the Revenue Requirements of Kansas Public Utilities.) DOCKET NO. 155,094-U)

ORDER

The above-captioned matter comes before the State Corporation Commission of the State of Kansas on its own motion. Having reviewed its files and records and being duly advised in the premises, the Commission finds and concludes as follows:

1. On September 27, 1986, the Congress of the United States passed one of the most sweeping tax reform acts in history. The Tax Reform Act of 1986 (the Act) was signed into law by the President on October 22, 1986.

2. As a result of this enactment, corporations in higher tax brackets will realize a phased-in reduction in corporate tax rates from 46% to 40% to 34%. The lowering of tax rates under the Act could result in substantial cost savings to many utilities in Kansas. The Act also brought about other major changes in federal income tax law, a number of which will have additional impacts on the revenue requirements of Kansas public utilities. Staff believes the utilities listed on Schedule A will be the most significantly affected, but staff will not necessarily limit its review to these utilities.

3. Due to the potentially significant impact on revenue requirements of the Act, the Commission believes it is necessary and desirable to reflect those impacts in the rates of regulated utilities and hereby opens this formal docket to address those consequences. Although the Commission generally examines a utility's revenue requirements as determined from its overall cost of service, the instant situation warrants a different approach. Significant reductions in income tax expense should not become a

windfall for utilities but should rather be flowed through to ratepayers. Although there may well be offsetting increases in other components of cost of service, we cannot presume so. Just as we have allowed changes in the cost of purchased gas and the cost of energy to be flowed through monthly to ratepayers by the PGA and ECA clauses without examination of other components of cost of service, so too do we think it appropriate in principle to isolate the impacts of the Act. However, utilities that believe that other costs of service have more than offset the decrease in their income tax expenses have the discretion to file such information and supporting data with the Commission. Thereupon the Commission will review such information and data on a case-by-case basis. This in no manner limits Commission staff from conducting an investigation on any component of cost of service whether or not raised in the utility's discretionary filing.

4. The Commission consequently intends to review the Act's impacts on the revenue requirements of Kansas public utilities from the standpoint of the income tax component of cost of service only and will endeavor to complete its review by the end of 1987 for tax savings relating to 1987. Commission staff has already requested, by letter dated October 10, 1986, a report from the utilities most likely to be significantly affected by the Act. Although a number of these reports have been received, staff suggests most are inadequate and have not presented a sufficient analysis of the impact of the Tax Reform Act on operations. Staff suggests more detailed review is therefore necessary. Since this review process will take time, it is necessary to create a mechanism whereby the Commission can conduct its review of revenue requirements without sacrificing the ability to capture for ratepayers any benefits of the corporate tax reduction accruing during the period in which the review is being conducted.

5. The utilities listed on the attachment to this order shall take the following steps to insure that the maximum potential income tax savings resulting from the Act are not lost to

ratepayers. Effective April 1, 1987, each utility listed in Schedule A shall accrue monthly in an appropriate deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, a percentage of its revenues representing the difference in its cost of service, as determined by the Commission in its most recent rate order, and such cost of service had the federal income tax component been based on the blended rate of 38% rather than 46%. The blended rate of 38% for 1987 is derived by using the statutory rate of 46% for April, May and June and the statutory rate of 34% for July through December.

6. At such time as the Commission's review is complete, if it is determined that a rate decrease is proper and would have been proper as of April 1, 1987, for those utilities listed at Schedule A, any excessive collections in the deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, with appropriate adjustments, shall be refundable to ratepayers along with interest calculated at the rate being used for interest paid on customer deposits. Any balance remaining in the account will be credited to the utility's operating revenue. All other affected utilities not listed at Schedule A, do not have to accrue estimated tax savings in a separate deferred account, but these utilities also will be subject to refund with interest regarding potential tax savings.

IT IS, THEREFORE, BY THE COMMISSION ORDERED THAT:

1. The Commission will review the effects of the Federal Tax Reform Act of 1986 on the revenue requirements of certain Kansas public utilities from the standpoint of the income tax component of cost of service.

2. A mechanism is hereby created to allow the Commission time to conduct its review without sacrificing benefits which may accrue to ratepayers due to reduction of federal corporate tax rates and other major changes in federal income tax law.

3. Effective April 1, 1987, each utility listed in Schedule A will accrue in a deferred revenue subaccount, or other

appropriate tracking mechanism approved by the Commission, an amount calculated using the percentage of revenues which represents the difference between its cost of service as determined in its most recent rate order and its cost of service had the Federal income tax component been based on the blended rate of 38% instead of 46%.

4. At such time as the Commission's review is complete, if it is determined that a rate decrease is proper and would have been proper as of April 1, 1987, any excessive collections in the deferred revenue subaccount, or other appropriate tracking mechanism approved by the Commission, with appropriate adjustments, of those utilities listed in Schedule A shall be refundable to ratepayers along with interest calculated at the rate being used for interest paid on customer deposits. Any balance remaining in the account will be credited to the utility's operating revenue. All other affected utilities will be subject to refund with interest for tax savings.

5. The Commission retains jurisdiction of the subject matter and parties for the purpose of entering such further order or orders as from time to time it may deem proper.

Lennen, Chmn.; Wright, Com.; Henley, Com.

Date: March 18, 1987

Judith McConnell

Judith McConnell
Executive Director

SEAL

DL/sls

MAJOR UTILITIES TO ACCRUE TAX SAVINGS IN A DEFERRED ACCOUNT

TELECOMMUNICATIONS:

Southwestern Bell Telephone Co. of Kansas
Continental Telephone Company of Kansas
United Telephone Company of Kansas
AT&T Communications of the Southwest-Kansas

GAS & ELECTRIC:

Arkla Inc.
Centel Corporation
Empire District Electric Company
Getty Gas Gathering, Inc.
Greeley Gas Company
Kansas City Power and Light Company
Peoples Natural Gas
Union Gas System, Inc.
Anadarko Production Co.
Kansas Gas Supply
Kansas Public Service Company, Inc.

CERTIFICATE OF SERVICE

18-GIMX-248-GIV

I, the undersigned, certify that a true and correct copy of the above and foregoing Staff's Motion to Open General Investigation and Issue Accounting Authority Order Regarding Federal Tax Reform was placed in the United States mail, postage prepaid, or hand-delivered this 14th day of December, 2017, to the following:

DEAN MATTHEWS, FIELD OPERATOR
AMARILLO NATURAL GAS COMPANY
2915 I-40 WEST
AMARILLO, TX 79109
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