DECISION MEMORANDUM

TO:COMMISSIONER NELSON

COMMISSIONER SMITH

COMMISSIONER HANSEN

MYRNA WALTERS

TONYA CLARK

DON HOWELL

STEPHANIE MILLER

DAVE SCHUNKE

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WORKING FILE

FROM:SCOTT WOODBURY

DATE:AUGUST 30, 1996

RE:PL———(HR 3448)

REPEAL OF TAX ON CONTRIBUTIONS IN AID OF CONSTRUCTION (WATER UTILITIES)

Under the Tax Reform Act of 1986, contributions in aid of construction (CIAC) are treated as taxable income.  The Tax Reform Act was applicable to all utilities.  The Commission in Case No. U-1500-176 addressed how income taxes payable on CIAC should be treated for ratemaking purposes.  On June 6, 1988, the Commission issued Order No. 21933 (attached), which required the regulated utilities to adopt certain methods, depending upon the type of utility, for treating income taxes related to contributions.  Regarding water utilities, the Commission stated:

IT IS HEREBY ORDERED that water companies with fewer customers than Boise Water Corporation . . . shall use a full gross-up method whereby the person making the contribution in aid of construction pays the full tax obligation of the utility on the contribution, unless they exercise the option in the following paragraph.

IT IS FURTHER ORDERED that any utility may adopt the method used by Pacific Power & Light Company whereby the additional expense for the tax on the contributions in aid of construction is charged to the stockholders and has no impact upon the customers.  All tax impacts of contribution are excluded from results of operation and no additional costs are passed on to the customers.

IT IS FURTHER ORDERED that Boise Water Corporation may continue using the method approved in Order No. 20955, subject to review by the Commission. [Boise Water Corporation enters into escrow agreements with developers who have requested water main extensions and special facilities for residential development].

In addition to this Order, individual water utilities may have received specific Commission authorization with respect to CIAC.

President Clinton recently signed into law a minimum wage bill which included as a rider a repeal of the tax on contributions in aid of construction for water utilities.  The Act is effective for amounts received after June 12, 1996.  Staff has reviewed HR 3448 (attached), the version which passed Congress August 1, 1996, and was presented to the President for signing, and makes the following observations regarding implementation: It is Staff’s desire that all water utilities account for otherwise qualified CIAC in a manner that will not be taxable.  The following is a list of requirements for payments from customers to be considered nontaxable CIAC for IRS purposes.

1.  It must be a contribution.

2.  It cannot be included in rate base for ratemaking purposes.

3.  It does not include amounts paid as service charges for starting or stopping service.

4.  The property must be an intregal part of the gathering, treatment or commercial distribution of water, which would be 20-year property (now 25 year property for Water Utility Property).

5.  The original Act (restored by Senate Bill) states CIAC does not include connection fees.

Staff is obtaining a copy of the Public Law signed by the President.  It is Staff’s intention to advise all water utilities of the change in law and instruct them as to what changes in accounting and operations are required.  As a matter of administrative housekeeping, Staff would suggest that the Commission issue a general Order in this matter to all water utilities.

Commission Decision

◆re: Staff advice and instruction letter to water utilities.

◆re: general Order re: Repeal of tax on contribution in aid of construction for regulated water utilities.

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