



Vinson & Elkins

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MARCH 23, 2018

**UNDERSTANDING THE FERC
MARCH 15TH ORDERS:**

FACTS, PROCESS AND TIMING

QUESTIONS?

Our panel will be answering questions throughout the presentation. Please submit your questions by utilizing the chat function via the webcast, or emailing Adele Pitzer at apitzer@velaw.com and your questions will be submitted to the panel for review.

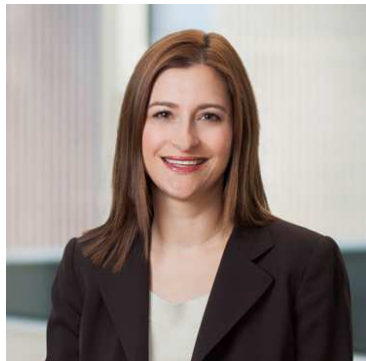
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PRESENTATION OUTLINE

- Capital Markets Perspective and Overview
- FERC's March 15th Issuances
 - PL17-1: Revised Policy Statement
 - RM18-11: Notice of Proposed Rulemaking
 - RM18-12: Notice of Inquiry
- What is a Cost-of-Service Rate?
- Oil Pipelines
- Natural Gas Pipelines
- Electric Transmission Companies
- Parting Thoughts and Conclusion

CAPITAL MARKETS PERSPECTIVE AND OVERVIEW

- March 15, 2018: FERC Announcement and Immediate Market Reaction (AMZ – 10%)
- March 15-21, 2018: Issuer Press Releases
 - Sample Releases to Date: AM/AMGP, CAPL, CELP, CNXM, GEL, MMLP, NBLX, SMLP, SUN, TRGP, ENLK/ENLC, OKE, PAA/PAGP, ETP/ETE, TEP/TEGP, ANDX, BPL, BWP, DCP, EEP, EPD, ENB, EQM, KMI, MMLP, MMP, MPLX, SEMG, SEP, TCP, TRP, WMB/WPZ
 - Most indicate no impact, negligible impact, or no material impact or no immediate impact, ultimate impact to be determined
- Why Disconnect?
 - FERC Regulated Pipelines have multiple contract structures
 - Not Impacted: negotiated rates, settlement rates, market-based rates, and discount rates not tied to the Cost-of-Service Rate
 - *May* be impacted: Cost-of-Service Rates and Index Rates; impact not immediate and to be determined on a case-by-case basis

CAPITAL MARKETS PERSPECTIVE AND OVERVIEW

- Key Takeaways
 - Impact on any particular pipeline or issuer (MLP or Corp.) is highly fact specific
 - Impact will be the result of rate proceedings to be determined in the future
 - Multiple variables in Cost-of-Service Rates in addition to tax costs
- Focus of today's presentation is impact on Cost-of-Service Rates and Index Rates, both of which include tax costs
 - Applicable to Liquids Pipelines, Gas Pipelines and Electric Utilities
 - Common Context: Impact of Lower Tax Rates Enacted in December 2017

March 15, 2018

Issuances Applicable to All Regulated Entities

MARCH 15TH FERC ISSUANCES

INCOME TAX ALLOWANCE – 2018 FERC

- Opinion No. 511-C (IS08-390)
 - Order on Remand in SFPP, L.P.’s proceeding following the D.C. Circuit *United Airlines* Order
- Revised Policy Statement (PL17-1)
 - Disallows master limited partnerships (MLPs) from recovering an income tax allowance in the Cost-of-Service
- Notice of Proposed Rulemaking (RM18-11)
 - Sets forth a process to determine whether jurisdictional Natural Gas Pipelines may be collecting unjust and unreasonable rates
- Notice of Inquiry (RM18-12)
 - Seeks comments on the effects of the Tax Cuts and Jobs Act on all FERC-jurisdictional rates, specifically asking about treatment of accumulated deferred income taxes

Cost-of-Service Rates

Understanding the Formula

COST-OF-SERVICE RATES

UNDERSTANDING THE FORMULA

BASIC FORMULA:

RATE (\$/unit) =

Total Cost of Service (\$)

divided by

Billing Determinants (unit)

COST-OF-SERVICE RATES

UNDERSTANDING THE FORMULA

TOTAL COST OF SERVICE:

- + Return on Rate Base
- + Operation & Maintenance Expenses
- + Administrative & General Expenses
- + Depreciation Expense
- + Non-Income Taxes
- + Income Tax Allowance
- Revenue Credits

TOTAL COST OF SERVICE

COST-OF-SERVICE RATES

UNDERSTANDING THE FORMULA

RETURN ON RATE BASE:

Overall Rate of Return X **Rate Base** = Return on Rate Base

RATE BASE:

Gross Plant – Accumulated Depreciation = *Net Plant*

Net Plant

- Accumulated Deferred Income Taxes

+ Working Capital

TOTAL RATE BASE

COST-OF-SERVICE RATES

UNDERSTANDING ADIT

ACCUMULATED DEFERRED INCOME TAXES: amount of income taxes collected by the pipeline but not yet needed to pay current income taxes

Accumulated Deferred Income Taxes (ADIT)					A-5
(000's omitted)					
Year	Commission Straight-line Depreciation Exp	IRS Accelerated Dep. (DDB) *	Difference Times Composite Tax Rate of 37.79% *	Accumulated Surplus	
1	25,163	50,326	9,509	9,509	
2	25,163	46,300	7,988	17,497	
3	25,163	42,596	6,588	24,085	

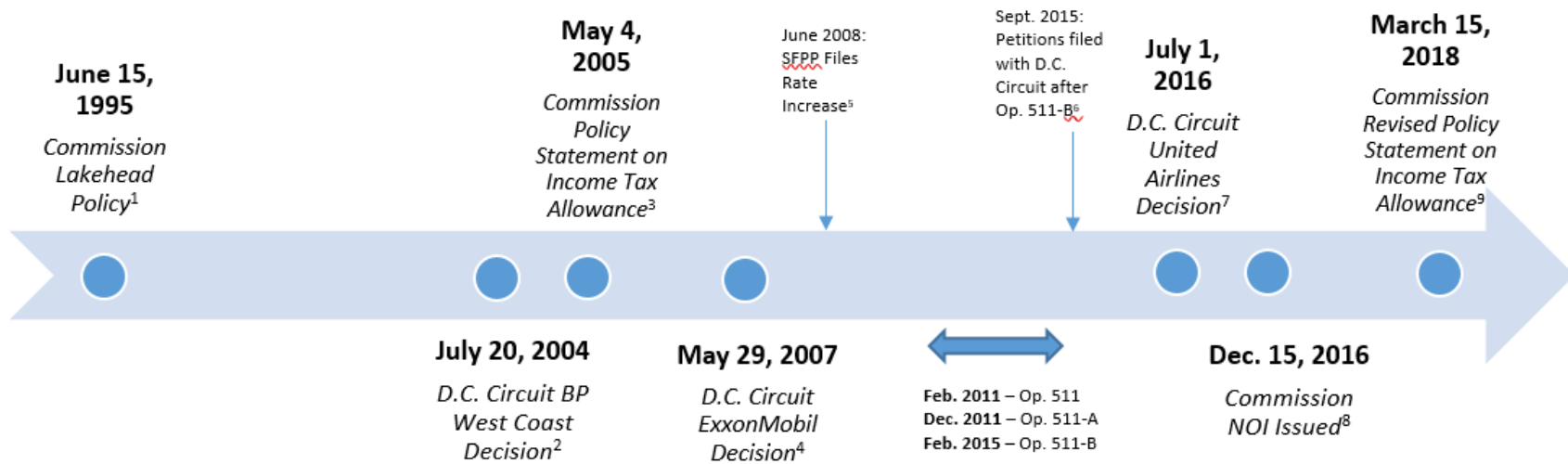
* Double Declining Balance is computed as twice the straight-line depreciation rate (2 * 4%) times net depreciable plant.
 ** See A-13 for computation of Composite Tax Rate.

Example from FERC's Cost-of-Service Manual. If this were computed through year 25, the economic life of the pipeline, the balance at year 25 would be 0. ADIT increases until reaching the *crossover* point and then starts to decline.

Revised Policy Statement

MLPs, Corporations, and the Income Tax Allowance

REVISED POLICY STATEMENT HISTORY



REVISED POLICY STATEMENT
WHAT DOES IT SAY?

The Commission revises its policy and will no longer permit a Master Limited Partnership pipeline to recover an Income Tax Allowance in its Cost of Service.

REVISED POLICY STATEMENT OVERVIEW

- What are Policy Statements?
 - *Issuances from the FERC providing guidance and regulatory certainty regarding statutes, orders, rules, and regulations that FERC administers.*
 - *Typically discuss the factors that FERC will use to evaluate future proceedings.*
- Why did FERC issue the Revised Policy Statement?
 - *Opinion No. 511-C. This Order on Remand held that the existing policy regarding income tax allowance in the Cost-of-Service for MLPs resulted in a double recovery of income tax costs to the pipeline.*
 - *The Policy Statement on Income Tax Allowances permitted MLPs and pass-through entities to collect an income tax allowance, so FERC issued a Revised Policy Statement to put regulated entities on notice that future reviews of income tax allowance will be different.*
- What do I do as a company in response to a Policy Statement?
 - *All going forward filings with FERC should be in compliance with the Policy Statement; FERC will likely review the filings and order the company to comply with the Policy Statement if not already incorporated.*

REVISED POLICY STATEMENT WHAT DOES THIS MEAN TO ME?

- I am a Pipeline (Natural Gas or Liquids) that is:
 - A pass-through pipeline owned by an MLP.
 - *Opinion 511-C involved review of a liquids pipeline held by an MLP – the Revised Policy Statement should apply.*
 - Incorporated.
 - *No double recovery when a corporate pipeline’s Cost-of-Service includes an income tax allowance.*
 - A pass-through entity owned in whole or part by a Corporation or other entities subject to federal income tax.
 - *The “innumerable partnership and other pass-through business forms that are not MLPs” are not addressed – these entities need to address the double-recovery concern in future FERC proceedings.*
 - A joint venture pipeline with one owner that is an MLP and one owner that is a Corporation.
 - *This is one of the “innumerable” forms that FERC will need to address in a subsequent proceeding.*

REVISED POLICY STATEMENT TIMING AND PROCESS

- When is the Revised Policy Statement effective?
 - *March 21, 2018*
- Can I file for Rehearing?
 - *No. A Policy Statement is not a final action that can be appealed.*
- What can I file?
 - *Request for Rehearing – FERC has held that rehearing is improper because a party cannot be aggrieved by the policy statement (however, they have substantively clarified such statements based on the requests in some instances).*
 - *Request for Clarification – FERC generally responds to these but has no obligation or specific timeframe to respond.*
- Can I appeal this to the Courts?
 - *No. A Policy Statement is not a final action that can be appealed.*
- Why?
 - *All FERC regulated entities will address impact of Policy Statement in future specific rate making proceedings that can be appealed.*

Notice of Inquiry

Effects of Tax Cuts and Jobs Act

NOTICE OF INQUIRY

CORPORATE INCOME TAX RATE DECREASE

- Tax Cuts and Jobs Act of 2017
 - What part of this impacts FERC rates?
 - *Federal corporate income tax rate decrease from a maximum 35% to a flat 21%.*
 - How are FERC rates impacted by the federal income tax decrease?
 - *Income Tax Allowance (for entities permitted to include it in the Cost-of-Service) will be decreased or removed.*
 - *ADIT - the current balance does not reflect the income tax liability that will occur in future years.*
 - Why is FERC considering these impacts on all of its regulated industries?
 - *FERC regulates Electric Transmission, Natural Gas Pipeline, and Liquid Pipeline rates to ensure they are “just and reasonable.”*
 - *FERC received letters asking them to act and reduce rates.*

NOTICE OF INQUIRY

CORPORATE INCOME TAX RATE DECREASE

- Tax Cuts and Jobs Act of 2017, continued . . .
 - How is the FERC Addressing the Rates in Each Industry?
 - *Natural Gas Pipelines – the Commission issued a Notice of Proposed Rulemaking regarding filing of cost information and options for the pipeline to choose.*
 - *Oil and Liquids Pipelines – no industry-wide initiative at this time.*
 - *Electric Transmission entities with stated rates or formula rates with fixed line items for the income tax rates were issued orders to show cause directing to propose revisions to the rates or show cause why they should not be required to do so; Electric Transmission entities with formula rates will make the adjustment in their next formula rate filing.*

NOTICE OF INQUIRY

CORPORATE INCOME TAX RATE DECREASE

- Tax Cuts and Jobs Act of 2017, continued . . .
 - Why are the Oil Pipelines treated differently?
 - *The majority of oil pipeline rates are set by the oil pipeline rate index approved by the FERC.*
 - *The next index adjustment will be set looking at industry-wide oil pipeline cost change on a per barrel-mile basis over the prior five-year period (2015-2019) and this decrease will be reflected in the index.*
 - *The next index adjustment proceeding is scheduled for 2020 and the rates set pursuant to this adjustment will be effective as of July 1, 2021.*
 - *Reductions in tax costs will be considered in addition to demonstrated increases in other cost components.*

NOTICE OF INQUIRY

UNRESOLVED

- Request for Comments
 - Excess ADIT (the portion calculated at 35% that will only be owed at 21%)
 - *How can FERC ensure that rate base continues to be treated in a manner similar to that prior to the Tax Cuts and Jobs Act (i.e., how to preserve rate base neutrality) until excess ADIT is fully settled?*
 - *Should regulated entities make adjustments so that rate base is appropriately adjusted by excess ADIT? If so, how?*
 - *Should interest be included from January 1, 2018 until any adjustments to rate base are implemented?*
 - *How quickly should excess non-plant based ADIT flow back to customers?*
 - Assets Sold or Retired after December 31, 2017
 - *Should FERC address excess ADIT that is removed from the books after December 31, 2017 as a result of a sale or retirement of an asset? If so, how?*
 - Amortization of Excess ADIT
 - *How should entities adjust income tax allowance such that the allowance would be decreased or increased by the amortization of excess ADIT? Where should the amortization be recorded?*

NOTICE OF INQUIRY UNRESOLVED

- Request for Comments, continued . . .
 - Supporting Worksheets
 - *Should FERC require entities to submit a one-time worksheet to show computation of excess ADIT and corresponding flow-back?*
 - Treatment of ADIT for MLPs
 - *What is the effect of the elimination of the income tax allowance for MLPs (or any other pass-through entities disallowed an income tax allowance) on ADIT? Should it be eliminated altogether from cost of service or should previously accumulated sums be returned to ratepayers?*
 - Bonus Depreciation
 - *What is the effect of the bonus depreciation change? Should, and if so how, FERC take action to address bonus depreciation-related issues?*
 - Catch All
 - *Should FERC take action to address bonus depreciation-related issues? If so, how?*
 - *Any other effects of the Tax Cuts and Jobs Act FERC should address?*

NOTICE OF INQUIRY TIMING AND PROCESS

- When is the Notice of Inquiry effective?
 - *March 21, 2018*
- Can I file for Rehearing?
 - *No. A Notice of Inquiry is not a final action that can be appealed.*
- What can I file?
 - *Comments in response to the questions set forth in the NOI.*
 - *Comments are due May 21, 2018 (60 days after the March 21, 2018 publication in the Federal Register).*
- Can I appeal this to the Courts?
 - *No. A Notice of Inquiry is not a final action that can be appealed.*
- What will the Commission do after May 21, 2018?
 - *Consider all the comments received and may do one of the following (or a combination): (A) Issue a Notice of Proposed Rulemaking, (B) Issue a Policy Statement, or (C) Do Nothing.*
 - *DEADLINE = ?????? (there is no deadline or requirement to act)*

Notice of Proposed Rulemaking

FERC Form No. 501-G and Natural Gas Pipeline Options

NOTICE OF PROPOSED RULEMAKING OVERVIEW

- What is a Notice of Proposed Rulemaking (NOPR)?
 - *A proposal from FERC to establish new regulations.*
- What does this NOPR propose?
 - *Requires all Natural Gas Pipelines to make a one-time filing of a new form (Form 501-G) providing financial information to evaluate the impacts of the Tax Cuts and Jobs Act and the Revised Policy Statement.*
- Why did FERC only issue the NOPR for Natural Gas Pipelines?
 - *FERC has an existing industry-wide mechanism to adjust oil pipeline rates but no such similar “indexing” rates exist for Natural Gas Pipelines.*
 - *FERC can review rates by initiating an NGA Section 5 proceeding.*
 - *FERC does not have a mechanism to require Natural Gas Pipelines to provide the information requested in this NOPR without a new regulation.*

NOTICE OF PROPOSED RULEMAKING

WHAT DOES THIS MEAN TO ME?

- What happens after the Form 501-G is filed?
 - WITH the Form 501-G, each Natural Gas Pipeline must select one of four options:
 1. File a limited NGA Section 4 filing reducing the pipeline rates for the tax rate reduction or pursuant the Revised Policy Statement (with no other changes to the Tariff or other Rate Components).
 2. Commit to file a general NGA Section 4 rate case “in the near future.”
 3. File a statement explaining why an adjustment to rates is not needed at this time.
 4. Take no action other than filing Form 501-G.
- What if I am a Hinshaw or Section 311 Pipeline?
 - *Hinshaw and Section 311 Pipelines performing interstate transportation services pursuant to FERC authorizations must file a new rate election for interstate service if their rates for intrastate service are reduced to reflect the Tax Cuts and Jobs Act.*

NOTICE OF PROPOSED RULEMAKING

TIMING AND PROCESS

- When is the Notice of Proposed Rulemaking effective?
 - *An unpublished NOPR posted in the Federal Register on March 23, 2018 noting that it is scheduled to be published on March 26, 2018.*
- Can I file for Rehearing?
 - *No. A NOPR is not a final action that can be appealed, but a Final Rule resulting from a NOPR is.*
- What can I file?
 - *Comments on the proposed rule set forth by the Commission.*
 - *Comments are due Wednesday, April 25, 2018 (if published on 3/26/18).*
- Can I appeal this to the Courts?
 - *No. A NOPR is not a final action that can be appealed, but an Order on Rehearing of a Final Rule can be appealed to the Courts.*
- What will the Commission do after FR Publication?
 - *Consider all the comments received and likely issue a Final Rule.*
 - *DEADLINE = ?????? (there is no deadline or requirement to act)*

NOTICE OF PROPOSED RULEMAKING

TIMING AND PROCESS

- Has the Commission expressed a timing for the Final Rule
 - *FERC Staff indicated in the Commission meeting that following issuance of a final rule they would expect to see filings of Form 501-G in the late summer, early fall of 2018*
- When will Pipelines be required to file the Form 501-G?
 - *FERC issued an Implementation Guide for Form 501-G*
 - *Grouped all Interstate Natural Gas Pipelines into four groups*
 - *The Filing Deadlines set forth in the Implementation Guide are:*
 - *Group I: 28 Days from the Final Rule Effective Date*
 - *Group II: 56 Days from the Final Rule Effective Date*
 - *Group III: 84 Days from the Final Rule Effective Date*
 - *Group IV: 112 Days from the Final Rule Effective Date*

Revenue Impacts

A Look at the Timing and Potential Impacts on Revenues for
Electric Transmission, Liquids Pipelines, Natural Gas Pipelines

LIQUIDS PIPELINE ENTITIES

SUMMARY – WHAT DOES THIS MEAN TO ME?

- Timing
 - Index-Rate Pipelines
 - *Reflect the data on Page 700 of FERC Form No. 6 in compliance with tax rate change and the Revised Policy Statement.*
 - *Year 2020 – FERC will review the index level looking at cost changes, as reflected on Page 700 of FERC Form No. 6 for the years 2015-2019, and establish a new index level.*
 - *Rate Changes with the next index level will first be effective on July 1, 2021.*
 - Cost-of-Service Rate Pipelines
 - *The pipeline can file on its own initiative to change the rate, or a rate proceeding may be initiated by complaint from a shipper.*
 - *Rate Changes will be effective as established by the proceeding (reparations may be awarded going back 2 years from the date of filing of the complaint).*
 - Market-Based Rates, Negotiated Rates, or Settlement Rates
 - *No changes expected to these rates.*

NATURAL GAS PIPELINE ENTITIES

SUMMARY – WHAT DOES THIS MEAN TO ME?

- Timing

****NOTE**** Pipelines may receive revenues from Cost-of-Service Rates, negotiated rates, discounted rates, and market-based rates, or a combination thereof. Therefore, it is impossible to determine what the overall revenue impact to any one pipeline entity will be without knowing the details of the type of contracts underlying the revenues received.

- Cost-of-Service Rates

- *A rate decrease would likely go into effect 30 days after the date of filing.*
- *A rate increase would likely be suspended for the full time allowed by law and go into effect subject to refunds 6 months after the date of filing.*

- Settlement Rates *subject to a Rate Moratorium per an approved Stipulation and Agreement*

- *No changes expected to these rates until after the Rate Moratorium.*

- Market-Based Rates, Negotiated Rates, or Discount Rates (that remain below the Cost-of-Service Rate and not tied to Cost-of-Service Rates)

- *No changes expected to these rates.*

ELECTRIC TRANSMISSION ENTITIES

SUMMARY – WHAT DOES THIS MEAN TO ME?

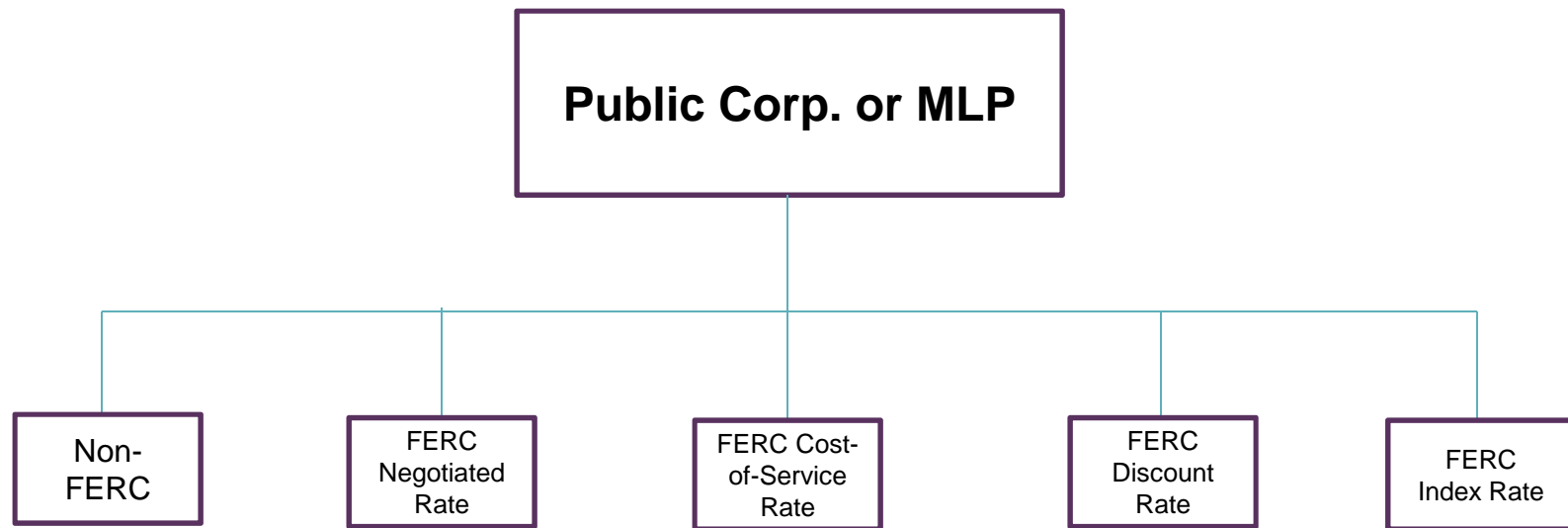
- Timing
 - Transmission formula rate utilities – adjust the input for tax changes and then rates reflecting changes will be effective
 - Numerous inputs so it is impossible to determine if the resulting rate will be an overall increase or an overall decrease.
 - Utilities subject to a show cause order – upon completion of those proceedings

Parting Thoughts & Conclusions

PARTING THOUGHTS & CONCLUSIONS

- While headlines focused on MLPs, FERC Issuances impact all classes of FERC regulated assets (liquids, gas, and electric utilities) held in corporations and pass-through entities.
- FERC regulated assets are contracted in a variety of ways (including negotiated and settlement rates), and most public corporations and MLPs have both asset and contract diversity.
- Impact on any particular asset using Cost-of-Service or Index-Rate contracts is highly fact specific and will be made in the context of individual rate filings.
- Analysis to be conducted and projections developed taking into account all variables before decisions made based on “assumed outcomes” (or headlines).

PARTING THOUGHTS & CONCLUSIONS



- Public corporations can and do own pass-through and tax paying subsidiaries.
- MLPs can and do own pass-through and tax paying subsidiaries.
- Both Public Corps. and MLPs hold a variety of FERC regulated and unregulated assets. The FERC regulated assets have a variety of contract structures, some of which will *not* be impacted and others of which *may* be impacted.
- Measuring outcome must be done taking into account all variables and is a complicated, fact specific inquiry.



THANK YOU

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