Phase One

Working Group One, Issue 7

Is there inconsistent application of the requirement to pay the **Income Tax Component of Contribution (ITCC)** charges across the Utilities? If yes, how should the Commission address this inconsistency?

### ITCC and inconsistent treatment of liability to reduce costs associated with interconnection facilities & upgrades

Utility generator interconnection agreements can require interconnection customers to provide security for the estimated amount of the potential utility income tax liability related to generator interconnection facilities. This is based on the value of grid upgrades which are paid for by the customer, constructed by the utility on their behalf, and which the customer is then required to legally transfer to utility ownership. In theory, this could be construed as a gift to the utility which would be considered income and subject to income tax. In practice, the IRS has not taxed utilities for the value of these facilities, and has established “Safe Harbor” provisions to avoid liability.

Decision (D.) 94-06-038 established three options to assure payment to the purchasing utility for any future taxes: 1) pay the ITCC; 2) provide the utility a letter of credit for the value of the ITCC; or 3) execute an indemnity agreement and provide a guarantee for the value of the ITCC.

Despite D.94-06-038, Southern California Edison (SCE) is reported to have requested interconnection applicants to pay the ITCC upfront on projects interconnecting to SCE’s distribution system, despite stating elsewhere that it is allowing all three options.[[1]](#footnote-1)

In contrast, while the Pacific Gas & Electric Company (PG&E) reserves the right to require—on a nondiscriminatory basis—an Interconnection Customer to provide such security, PG&E has sought and received a waiver from requiring this for projects in its territory, let alone requiring up-front payment of the potential ITCC liability in full.[[2]](#footnote-2) However, anecdotal reports indicate that this has not been consistently applied to all applicants.

This proceeding should address inconsistency with D.94-06-038, inconsistency of treatment of interconnection customers within a utility service area, and encourage consistency in line with best practices between utilities.

ITCC charges, when applied, add roughly 30% to the cost of upgrades associated with an interconnection request. As SCE territory’s average total in-front-of-the-meter upgrade costs are approximately $150,000 per MW[[3]](#footnote-3), these charges represent the second largest contributor to interconnection costs, despite the de minimis risk of actual liability being imposed.

Posting of security represents a real cost to the developer, depriving it of capital necessary to develop the project. The more general question that needs to be addressed is whether it is good policy to require a developer to set aside substantial sums every year, over the term of an agreement, to protect the utility from a risk that most likely will never arise. Given the limited risk to the utility and real cost to developer, and subsequent advice or rulings from IRS and FERC, the ITCC security requirement warrants reconsideration.

While requiring the interconnection customer to post ITCC security protects the utility from theoretical tax liability, this policy may not be cost effective for ratepayers or best advance energy policy, particularly the objective to encourage the development of new renewable generation.

The IRS safe harbor notices provide the generator explicit and easy-to-comply-with rules to avoid a taxable event for transactions under interconnection agreements. We are aware of no contribution under an interconnection agreement that has caused a transmission owner to incur an income tax liability. The risk of any utility or ratepayer ITCC exposure, while admittedly greater than zero, is negligible; the corresponding cost to the developer of maintaining the security for the theoretically maximum amount of tax exposure exacts real costs and necessarily impedes project development.

1. For example, Southern California Edison Company, Energy Resource Recovery Account

   (ERRA) Review Of Operations, 2014, Chapters VIII-XVI, A.15-04-002 (Apr. 1, 2015), at

   28, available at: http://www3.sce.com/sscc/law/dis/dbattach5e.nsf/0/25FCD51A45ACEC1988257E1B005DD90D/$FILE/A1504002%202015%20ERRA%20Review%20-%20SCE-2%20Ch.%20VIII-XVI\_PUBLIC.pdf [↑](#footnote-ref-1)
2. Docket No. ER11-3944-000. On June 29, 2011, Pacific Gas and Electric Company (PG&E) submitted a request for waiver of the provision in the appendices or attachments of certain generator interconnection agreements that requires interconnection customers to provide security for the estimated amount of the potential income tax liability on generator interconnection facilities. The income tax at issue is commonly referred to as the income tax component of contribution (ITCC). PG&E’s requested waiver would, on a prospective basis waive the provisions requiring customers to post ITCC under each generator interconnection agreement**1** and authorize PG&E to refund all ITCC security amounts (with interest) to certain customers. In this order, we grant PG&E’s waiver request.

   CAISO supported PG&E’s request for waiver.

   PG&E currently does not require the Interconnection Customer to provide Income Tax Component of Contribution (“ITCC”) security to cover the potential tax liability on the Interconnection Facilities; however, PG&E reserves the right to require, on a non-discriminatory basis, the Interconnection Customer to provide such security, in a form reasonably acceptable to PG&E as indicated in Section 5.17 of the LGIA (or Section 11 of the SGIA), in an amount up to the cost consequences of any current tax liability. Upon request, and within sixty (60) Calendar Days’ notice, the Interconnection Customer shall provide PG&E such ITCC security in the form requested by PG&E.  [↑](#footnote-ref-2)
3. This figure is from the Clean Coalition data request and reflects interconnections prior to 2013. Confidential quarterly interconnection cost reports from the IOUs were subsequently initiated and available to Commission staff. [↑](#footnote-ref-3)