

111 FERC ¶ 61,351
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeem G. Kelly.

Tax Deduction for Manufacturing Activities
Under the American Jobs Creation Act of 2004

Docket No. EL05-109-000

GUIDANCE ORDER ON TAX DEDUCTION FOR MANUFACTURING ACTIVITIES
UNDER AMERICAN JOBS CREATION ACT OF 2004

(Issued June 2, 2005)

1. This order provides guidance on the Commission's ratemaking policy with respect to the Tax Deduction for Manufacturing Activities (TDMA) in section 102 of the American Jobs Creation Act of 2004 (the Act).¹ The Act provides for a deduction for income attributable to certain domestic production activities, including income from the sale of electricity and natural gas produced in the United States.² The TDMA will have ratemaking implications for public utilities that make jurisdictional sales of electricity at cost-based stated rates or cost-based formula rates, which are discussed further below, but not for jurisdictional natural gas pipelines.

Background

2. On October 22, 2004, the President signed the Act into law. The TDMA provides for a deduction of up to 9 percent³ of the income attributable to qualified production activities. Income from qualified production activities includes income from the lease, rental, sale, exchange or other disposition of electricity, natural gas or potable water

¹ Pub. L. No. 108-357, 118 Stat. 1418 (2004) (adding additional section 199 to the Internal Revenue Code, 26 U.S.C. § 1 *et seq.* (2000)).

² Act, section 102, § 199(c)(4)(A)(i)(III) (2004).

³ The TDMA will be phased in so that the allowable deduction equals 3 percent from 2005-2006, 6 percent for 2007-2009, and 9 percent from 2010 onwards. Act, section 102, § 199 (a)(2) (2004).

produced in the United States. However, the TDMA does not apply to income attributable to the transmission and distribution of electricity, natural gas and water. When fully implemented, the TDMA will be the equivalent of reducing the effective federal corporate income tax rate on production activities from 35 percent to 32 percent.⁴

Discussion

3. The TDMA is a special deduction that reduces the amount of income tax due from energy sales. The TDMA will have ratemaking implications only for public utilities that make jurisdictional sales of electricity at stated cost-based rates and cost-based formula rates. Income taxes are a cost that is included in the determination of virtually all cost-based rates. Accordingly, we expect these public utilities to appropriately reflect the TDMA amounts in any future filings to change their cost-based stated rates and cost-based formula rates.

4. Additionally, some public utilities utilize cost-based formula rates that are designed to automatically track changes in costs. The Commission is concerned that certain of the formulas established to develop rates may not be structured in a way that will provide an adequate mechanism for tracking the TDMA amount. Accordingly, we direct these public utilities to separately identify the TDMA amounts in any future filings to change their cost-based formula rates.

5. Moreover, since the TDMA only affects rates for jurisdictional entities to the extent that the TDMA amounts are reflected in the cost of service, the TDMA will not have any ratemaking implications for jurisdictional entities to the extent that they engage in the sale of electricity at market-based rates.

6. The TDMA also does not have any ratemaking implications for jurisdictional pipelines. The TDMA applies only to income attributable to qualified production activities, and jurisdictional pipelines do not engage in production activities.

⁴ For individuals, the reduction in the effective tax rate varies depending on the individual's tax bracket, but, in any case, the amount of the allowable TDMA cannot exceed 50 percent of the individual's W-2 wages of the employer for the taxable year. Act, section 102, § 199(b)(1) (2004).

The Commission orders:

Public utilities with cost-based stated rates or cost-based formula rates for electric energy sales should appropriately reflect the TDMA amounts in any future filing to change a stated cost-based rate or formula rate.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.