AMERICAN WATER

NRRI Webinar:
New Tax Legislation and its Effect on Regulated Public Utilities

Brian Chin, Senior VP of Planning & Strategy Integration

February 9, 2018

Tax Reform Benefits Utility Customers

- For regulated utilities, benefits of prudent lower expenses are passed to customers.
- These expenses include taxes and interest utilities pay; when these costs decline, the benefits ultimately flow to customers.

System Improvements Can Be More Affordable

- **Additionally, a lower tax rate can mean utilities can invest more in infrastructure without increasing customers' bills as much.**

Analysts estimate every dollar of lower taxes equates to $8 of investment to make our water systems safer and more reliable with no changes to customer bills.

- **Utilities strive to provide safe and reliable service while being mindful of financial impact to our customers.**

Observations Across The Industry

- **The industry's assessments of tax reform are not complete**
  - General rate cases are historically a preferred venue by which stakeholders can consider tax reform impacts
    - More holistic review of multiple issues
    - Mitigates rate volatility for customers
    - Rate deferrals till next rate cases will ultimately benefit customers
  - More specific tax determinations are suboptimal venues
    - Tax changes are significantly complex; immediate rate adjustments now are likely to need recalibration later
    - For example: The SEC has given companies a full year to account for all financial statement impacts of tax reform

Selected Responses From Other Utilities & Investors

- **Improved rate base (positive) but decreased cash flow outlook (negative)**
- **Utility responses**
  - Issue debt or equity
  - Seek constructive regulatory solutions

- **Utility equities have been underperforming the S&P 500 YTD since investors understand utilities' customers ultimately capture the benefit of tax reform**
- **Moody's placed 24 utilities on credit outlook negative in January 2018**

AEP

- *Current Rating: Baa1, stable*
  - *No plans to issue equity*
  - *Capital Investment: $500 Million reduction*
  - *Credit Metrics: "slightly lower"; forecasts mid teens FFO/Debt vs upper teens previously*
  - *Long Term EPS Growth: Affirmed 5-7%*

WEC Energy Group

- *Current Rating: A3, negative credit watch*
  - *No plans to issue equity*
  - *Capital Investment: $2.1 Billion increase*
  - *Credit Metrics: FFO/Debt in range of 16-18% through 2022 (vs 16-19% previously)*
  - *Long Term EPS Growth: Affirmed 5-7%*

Dominion Energy

- *Current Rating: Baa2, negative credit watch*
  - *Equity offering: $500 Million*
  - *Capital Investment: $1 Billion reduction*
  - *Credit Metrics: Sees +/- 15% FFO/Debt levels by year end*
  - *Long Term EPS Growth: Updated 8+%*

Entergy

- *Current Rating: Baa2, negative credit watch*
  - *Equity offering: Finance requirements through debt and equity*
  - *Capital Investment: Affirmed $10.7 Billion*
  - *Credit Metrics: Sees certain credit metrics adversely affected, but expects to hold an investment grade rating*
  - *Long Term EPS Growth: Affirmed 5-7%*