

Barry A. Naum
Direct Dial (717) 795-2742
bnaum@spilmanlaw.com

March 9, 2018

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

VIA ELECTRONIC FILING

Re: Tax Cuts and Jobs Act of 2017; Docket No. M-2018-2641242

Dear Secretary Chiavetta:

Please find enclosed for filing with the Pennsylvania Public Utility Commission ("PUC" or "Commission") the Comments of Industrial Energy Users of Pennsylvania ("IECPA"), in the above-referenced matter.

This document was filed electronically with the Commission on this date. All parties are being served a copy of this document in accordance with the enclosed Certificate of Service.

Please contact me if you have any questions concerning this filing.

Sincerely,

SPILMAN THOMAS & BATTLE, PLLC

By 

Derrick Price Williamson
Barry A. Naum

BAN/sds

Enclosures

c: Erin Laudenslager (via E-mail)
James Mullins (via E-mail)
Certificate of Service

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Tax Cuts and Jobs Act of 2017

: Docket No. M-2018-2641242

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing document upon the following parties to this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by participant).

VIA FIRST-CLASS MAIL

Bureau of Investigation & Enforcement
Pennsylvania Public Utility Commission
400 North Street, 2nd Floor
P.O. Box 3265
Harrisburg, PA 17105-3265

Office of Small Business Advocate
Commerce Building, Suite 202
300 North Second Street
Harrisburg, PA 17101

Office of Consumer Advocate
5th Floor, Forum Place
555 Walnut Street
Harrisburg, PA 17101



Barry A. Naum

Dated: March 9, 2018

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Tax Cuts and Jobs Act of 2017

:

Docket No. M-2018-2641242

**COMMENTS OF
INDUSTRIAL ENERGY CONSUMERS OF PENNSYLVANIA**

TABLE OF CONTENTS

I. INTRODUCTION.....1

II. COMMENTS.....3

**A. The PUC Should Adjust Current Rates to Reflect the Reduced
Income Tax Expenses of Public Utilities3**

1. Federal Income Tax Expense.....3

2. Excess Deferred Tax Liabilities4

B. Refunds or Rate Reductions are the Only Reasonable Options6

**C. Negative Surcharges Should Have an Effective Date of
January 1, 20187**

III. CONCLUSION10

I. INTRODUCTION

In December 2017, Congress enacted the Tax Cuts and Jobs Act ("TCJA") legislation effectuating a comprehensive restructuring of federal tax law. The TCJA's changes, which include a reduction in the federal corporate income tax rate from 35% to 21%, significantly reduced the cost of service for Pennsylvania utilities. This reduction in cost of service is material and varies by utility. The TCJA's revisions to federal tax law should result in reduced rates for ratepayers as a result of utilities' lower federal income tax expenses (current and future) and excess Accumulated Deferred Income Tax balances (for both protected and unprotected assets). In short, the TCJA provides a once in a generation opportunity for the Pennsylvania Public Utility Commission ("PUC" or "Commission") to insure that ratepayers reap the benefits of these tax savings.

By Secretarial Letter issued on February 12, 2018, the Commission opened this docket to determine the effects of the TCJA on the tax liabilities of regulated utilities for 2018 and future years and the feasibility of reflecting such impacts in the rates charged to Pennsylvania ratepayers. To insure that ratepayers receive the full benefit of the federal tax change, the Commission will examine any reduced annual federal tax obligations, the effect on Accumulated Deferred Income Taxes of regulated utilities resulting from implementation of the TCJA, and the manner in which the reduced annual tax obligations will be addressed in rates. Recognizing the complexity involved in accounting for the various impacts on utilities' revenue requirements, the Commission solicited input from the utilities and other interested parties.

Specifically, the Commission requested that interested parties submit comments addressing: (1) whether the PUC should adjust current rates to reflect the reduced income tax expenses of public utilities; (2) if so, the appropriate negative surcharge or other methodologies that would permit immediate modifications to rates; and (3) the effective date of the surcharge or other methodology.

The Industrial Energy Consumers of Pennsylvania ("IECPA")¹ offers these Comments in response to the Commission's inquiry. IECPA is an association of energy-intensive industrial consumers of electricity and natural gas taking service from a variety of regulated utilities in Pennsylvania, including Columbia Gas of Pennsylvania, Inc., Metropolitan Edison Company, PECO Energy Company, Pennsylvania Electric Company, Peoples Natural Gas Company LLC, PPL Electric Utilities Corporation, UGI Utilities, Inc. – Gas Division, and West Penn Power Company.

¹ For purposes of this proceeding, IECPA members include: Air Products & Chemicals, Inc.; AK Steel Corporation; Arconic, Inc.; ArcelorMittal USA LLC; Benton Foundry, Inc.; Carpenter Technology Corporation; East Penn Manufacturing Company; Knouse Foods Cooperative, Inc.; Praxair, Inc.; and Proctor & Gamble Paper Products Company.

II. COMMENTS

A. The PUC Should Adjust Current Rates to Reflect the Reduced Income Tax Expenses of Public Utilities.

1. Federal Income Tax Expense

As noted in the February 12 Secretarial Letter, the PUC is charged with the statutory obligation of safeguarding the interests of Pennsylvania retail utility customers in paying rates for utilities' prudent costs, including taxes paid, that are just and reasonable. *See* Secretarial Letter, p. 1. In the process of establishing just and reasonable rates, a revenue gross-up factor is applied to revenues collected for the purpose of taxes in order to account for the effect that taxes have on a utility's ability to earn a fair return on equity. This revenue gross-up factor is based on the tax rates applicable to the utilities' services at the time of the test year in their last base rate case and is applied to all tax-related revenues received by the utilities going forward. Now that the federal tax rate has been reduced by 40%, the revenue gross-up factor must also be adjusted downward. If the gross-up factor remains the same, utilities will be collecting more revenues for tax expense than they will ever remit to the taxing authorities. The new tax rate went into effect on January 1, 2018; therefore, utilities are over-collecting right now. It is undeniable that utility rates will remain excessive until the Commission acts. Customers should be protected from paying rates that, as of January 1, 2018, provide utilities with income tax collections pursuant to rates that cannot be just and reasonable.

Unless the Commission directs otherwise, utility rates may go unadjusted for an extended period of time. This would be unfair to ratepayers and arguably contrary to law. The Commission should swiftly correct this inequity by ordering utilities to institute regulatory accounting treatment for any impacts of the new law, including current and deferred tax impacts. Prior to an adjustment

in rates, utilities should record the tax savings in regulatory deferral accounts as a regulatory liability, and these over-collections should be returned to customers over a relatively short period.

2. Excess Deferred Tax Liabilities

It is common that, over time, utilities collect more income tax from customers than they are required to remit in any particular year. The disparity between taxes collected and taxes payable results in an Accumulated Deferred Income Tax ("ADIT") balance. Due to modified accelerated cost recovery system depreciation and other bonus depreciation, ADIT balances can grow quite large. Typically, utilities use their ADIT balances as a source of zero-cost capital. Utilities may argue that ratepayers "benefit" from this scenario because the zero-cost capital serves to decrease their required overall rates of return. Another way of looking at it, however, is that ratepayers are simply providing utilities with an interest-free loan. While the debate over the merits of each argument is interesting, they are not dispositive in this proceeding.

Up until the enactment of the TCJA, utilities have assumed that their ADIT balances needed to be sufficient to cover future tax expenses based on a 35% rate. Now, as a result of the TCJA, the utilities likely have a significant surplus of tax-related revenues that *greatly* exceeds their actual current and future tax liabilities, which will be assessed at a 21% rate. In some instances, this excess ADIT balance may represent a *massive* benefit for ratepayers that should be credited to them. To put this into perspective, when the TCJA took effect, large utilities across the nation saw their respective excess ADIT balances explode to **over one billion dollars**.² This

² See Jeffrey Tomich, *Tax overhaul has consumers, utilities jockeying for billions*, E&E News, (Jan. 8, 2018) <https://www.eenews.net/stories/1060070317>; see also Comments of DTE Electric Company and DTE Gas Company, *In the matter, on the Commission's own motion, to consider changes in the rates of all Michigan rate regulated electric, steam, and natural gas utilities to reflect the effects of the pending federal Tax Cuts and Jobs Act: Alpena Power Company, Consumers Energy Company, Detroit Thermal, LLC, DTE Electric Company, DTE Gas Company, Indiana Michigan Power Company, Northern States Power Company, Upper Peninsula Power Company, Upper Michigan Energy Resources Corporation, Wisconsin Electric Power Company, Presque Isle Electric & Gas Co-op, Michigan Gas Utilities Corporation, and SEMCO Energy Gas Company ("Michigan TCJA Investigation")*, Michigan Public

money was collected by utilities from ratepayers to fund a regulatory liability *that does not now exist* at the same level as it did prior to the TCJA. This difference therefore belongs to the ratepayers, and utilities should write-down their excess ADIT balances and recompense ratepayers accordingly.

The proper debate is not *whether* ratepayers should reap the benefits of the revenues they initially paid to the utilities, but *how and over what period of time*. In terms of timing, the Internal Revenue Service's normalization rules may guide when the utilities begin to flow the benefits arising out of excess ADIT balances to ratepayers. Generally, under the average rate assumption method ("ARAM"), utilities should amortize their excess ADIT balances over the remaining lives of the utility property that gave rise to the original ADIT balance.

It is important to distinguish that utilities need to separate their excess ADIT balances into two categories: the "protected" ADIT balance and the "non-protected" ADIT balance. The excess ADIT balance that resulted from utilities collecting taxes at the 35% rate prior to the TCJA's effective date are protected by the normalization rules and ARAM. In simplified terms, under ARAM, these excess deferred taxes cannot be flowed through to ratepayers more quickly than if the TCJA was never enacted. Therefore, the protected ADIT asset balance must be spread over the remaining regulatory life of the property that generated the deferred taxes in the first instance. Although the greatest benefit to ratepayers would be found in having the excess balances amortized over the shortest period of time possible, IECPA understands that utilities should comply with the normalization guidelines in order to continue to use accelerated depreciation for tax purposes in future periods with respect to protected assets.

Service Commission Case No. U-18494 (filed Jan. 19, 2018); *see also* Comments of Consumers Energy Company, *Michigan TCJA Investigation*, Michigan Public Service Commission Case No. U-18494 (filed Jan. 19, 2018).

Apart from the "protected" ADIT balances, there also is an element of excess ADIT balances largely related to costs capitalized as a component of regulated plant investment on the utilities' books. Some of these costs relate to non-direct construction factors and certain regulatory assets for pensions and benefits. These "non-protected" excess ADIT balances or assets are *not* subject to ARAM restrictions. Although not all utilities carry such balances, the Commission has complete discretion to order those that do to rapidly amortize their balances. There are no compelling reasons why the Commission should not require utilities to flow these funds back to ratepayers immediately. Importantly, both elements of excess ADIT balance amortizations must be grossed up to convert the tax amortization from an operating income credit to a revenue requirement credit.

B. Refunds or Rate Reductions are the Only Reasonable Options.

There are several ways that utilities may propose to return the rate-related benefits of the TCJA to ratepayers: (1) issue customer refunds; (2) lower rates; (3) use the money as a source of zero-cost financing for capital projects; (4) direct the funds to offset future rate increases; or (5) apply some combination of these applications. The only just and reasonable options are customer refunds and reduced rates. The other options simply benefit utilities and shareholders to the detriment of customers. If the utilities wish to amend their capital structure or increase rates, they should pursue a traditional rate case or other PUC-approved process.

More importantly, these revenues were collected specifically for the purpose of funding the utilities' current and future tax liability costs. They were not collected for any other purpose, and to allow the utilities to retain these revenues to achieve other utility objectives would constitute unreasonable and unjust ratemaking outside of the context of proper cost causation. Refunds or rate reductions are both equitable and require minimal effort to implement, and would fairly acknowledge that the savings resulting from the TCJA *belong to the ratepayers*.

To the extent utility rates continue to reflect a 35% tax rate after January 1, 2018, any excess revenues collected are subject to refund as they are not protected by normalization or ARAM. Once again, the Commission retains discretion over the treatment of these "current" tax balances. That being the case, IECPA recommends that the Commission order utilities to immediately convert these balances into a one-time credit for retail customers. If, however, the Commission determines that a one-time credit is not feasible, then utilities should be required to amortize applicable balances over a relatively short period (preferably less than 12 months).

In any event, the Commission will have to ensure that the credit(s) flow back to customers in proportion to how the excess revenues were generated. Utilities must return these short-term savings to customers as soon as possible in order to protect the customers that actually paid the excess taxes and insure that they are the ones that receive the overpayment credits. Ideally, the PUC will require refunds or negative surcharges that accurately compensate each individual customer. At a minimum, however, refunds need to be determined on a customer-class specific basis to ensure that restitution aligns with each customer class's actual overpayment of Commission-approved cost-based rates. It would be inappropriate, and in violation of the cost of service principles, to impose a *uniform* negative surcharge across all customer classes.

C. Negative Surcharges Should Have an Effective Date of January 1, 2018.

As explained above, all utilities currently recover an income tax allowance that assumes a corporate tax rate of 35%. The TCJA reduced that rate to 21% on January 1, 2018. Therefore, the tax expenses that are currently built into rates no longer reflect actual costs. Furthermore, most utilities maintain ADIT balances that are now significantly overfunded. The Commission's fundamental responsibility is to fix just and reasonable rates. Under the circumstances, it would not be just and reasonable for the Commission to approve revenue relief or rate increases based on tax-related projections that have become inaccurate by operation of law. The Commission should

make it clear that it expects utilities with open rate cases to update their filings to reflect the new tax law. Therefore, for those utilities that have a pending rate case, the Commission should require immediate reductions to their cost projections.

Similarly, the Commission should initiate show-cause proceedings for all utilities not currently engaged in a rate case. Utilities should be required to submit testimony and exhibits indicating the revenue impact of the TCJA and include a proposal regarding how customers will benefit from any cost of service reductions. It is important that intervention is available in these cases so that all interested parties may contest (and offer their own) evidence and proposals.

To increase administrative efficiency, however, the Commission should encourage utilities to voluntarily reduce their rates. This would not be unprecedented, as utilities in several states have already acknowledged the effect of the TCJA and have preemptively reduced their rates. For example, the following utilities took unilateral action that benefited ratepayers and reduced regulatory workload:

- Days after President Trump signed the TCJA into law, Commonwealth Edison Company filed an expedited plan with the Illinois Commerce Commission so that it could take *immediate* action to pass along the savings that the company would receive due to the reduced tax rate.³
- Baltimore Gas & Electric Company announced that it would begin to pass along \$82 million in annual tax savings starting February 2018.⁴

³ See *Commonwealth Edison Company Verified Petition for Special Admission to File and put into Effect on Less Than 45 Days Notice, Tariffs Accelerating Bill Credits Attributable to Federal Tax Reform*, Illinois Commerce Commission Docket No. 18-0034, Order (issued Jan. 18, 2018); see also News Release, Commonwealth Edison Company, *ComEd Filing to Provide Savings to Customers from Corporate Tax Decrease* (Jan. 5, 2018) <https://www.comed.com/News/Pages/NewsReleases/2018-01-05.aspx>.

⁴ See News Release, Baltimore Gas and Electric Company, *BGE Plan to Pass Federal Tax Reduction Savings to Customers Accepted by Maryland Public Service Commission* (Jan. 31, 2018), <https://www.bge.com/News/Pages/Press%20Releases/BGE-Plan-to-Pass-Federal-Tax-Reduction-Savings-to-Customers-Accepted-by-Maryland-Public-Service-Commission.aspx>; see also Maryland Public Service Commission Case Nos. 9056, 9064, and 9221.

- Potomac Electric Power Company and Delmarva Power and Light Company have requested to begin providing a credit to lower customer bills beginning in the *first quarter* of 2018.⁵
- The five largest utilities in Oklahoma are lowering rates retroactively from January 9, 2018, and refunding ratepayer money, *with interest*.⁶

Without the benefit of first reviewing the Comments of Pennsylvania's utilities, IECPA hopes that they are as eager to issue refunds or reduce rates. In any event, a contested case may still be necessary to determine how utilities deal with their excess ADIT balances. This is a complex issue and stakeholders should be afforded the due process attendant to a fully litigated proceeding. Calculating the cost of service reduction related to annual tax expense, however, is a simple math problem that is unlikely to prompt controversy. To the extent possible, the Commission should immediately order corresponding rate reductions or refunds, without the need for a contested case when it comes to straightforward issues.

⁵ See Potomac Electric Power Company's presentation from the Technical Conference on the Tax Cuts and Jobs Act Impact held on February 21, 2018, *In the Matter of the Application of Potomac Electric Power Company for Authority to Increase Existing Retail Rates and Charges for Electric Distribution Service*, District of Columbia Public Service Commission Formal Case No. 1150, and *In the Matter of: Impact of the Tax Cuts and Jobs Act of 2017 on the Existing Distribution Service Rates and Charges for Potomac Electric Power Company and Washington Gas Light Company*, District of Columbia Public Service Commission Formal Case No. 1151 (filed Feb. 21, 2018); see also Delmarva Power and Light Company – Revised Tariff Pages, *In the Matter of the Impact of the Federal Tax Cuts and Jobs Act of 2017 on Maryland Utility Rates*, MD PSC Case No. 9473 (filed Feb. 9, 2018).

⁶ See Jessi Mitchell, *OCC Orders Major Utilities To Transfer New Savings to Ratepayers*, News 9 (Jan. 9, 2018) <http://www.newson6.com/story/37229441/occ-orders-major-utilities-to-transfer-new-tax-savings-to-ratepayers>; see also Corporation Commission of Oklahoma Case Nos. PUD 201700568 (Centerpoint Energy Resources Corporation d/b/a Centerpoint Energy Oklahoma Gas), PUD 201700569 (Oklahoma Gas and Electric Company), PUD 201700570 (Arkansas Oklahoma Gas Corporation), PUD 201700570 (Oklahoma Natural Gas Company, a Division of One Gas, Inc.), and PUD 201700572 (Public Service Company of Oklahoma).

III. CONCLUSION

Because the TCJA materially reduced the cost of service for Pennsylvania utilities, and the reductions were not the result of management efficiency or improvements in service, the savings realized through the tax cut should immediately be deferred in regulatory liability accounts. Thereafter, the Commission must insure that customers receive full credit for these cost of service reductions. The benefits should come in the form of direct refunds or reduced rates, both apportioned on a volumetric basis. For those utilities currently involved in a rate case, their cost of service projections should be immediately reduced. All other utilities should be required to demonstrate how and when ratepayers will benefit from their reduced costs of service. Interested parties should have an opportunity to assess and, as necessary, challenge these proposals in contested proceedings.

Respectfully submitted,

By 

Derrick Price Williamson (I.D. No. 69274)
Barry A. Naum (I.D. No. 204869)
SPILMAN, THOMAS & BATTLE, PLLC
1100 Bent Creek Boulevard, Suite 101
Mechanicsburg, PA 17050
Phone: (717) 795-2740
Fax: (717) 795-2743
dwilliamson@spilmanlaw.com
bnaum@spilmanlaw.com

Bryan A. Brandenburg
CLARK HILL PLLC
212 East Cesar Chavez Avenue
Lansing, MI 48906
Phone: (517) 318-3011
Fax: (517) 318-3077
bbrandenburg@clarkhill.com

Counsel to Industrial Energy Consumers of Pennsylvania

Dated: March 9, 2018