

March 3, 2022

VIA ELECTRONIC FILING

Rosemary Chiavetta
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
P.O. Box 3265
Harrisburg, PA 17105-3265

**Re: Peoples Gas Company LLC's Petition for Approval to Distribute to Customers the Net Savings Associated with its Excess Accumulated Deferred Income Taxes for the January 1, 2018, to December 31, 2021, Period.
Docket No. P-2022**

Dear Secretary Chiavetta:

Enclosed for filing, please find the Petition of Peoples Gas Company LLC ("Peoples Gas" or "Company") for Approval to Distribute to Customers the Net Savings Associated with its Excess Accumulated Deferred Income Taxes ("EADIT") for the January 1, 2018, to December 31, 2021, Period.

By way of background, on November 18, 2021, the Pennsylvania Public Utility Commission ("Commission") entered an Opinion and Order ("TCJA Order") at Docket No. P-2021-3025898, which, among other things, directed Peoples Gas to file a Petition to distribute the amortized amount of the Company's EADIT with 60 days, *i.e.*, by January 17, 2021.

By Letter-Petition on December 17, 2021, Peoples Gas requested a 45-day extension to file the EADIT Petition, *i.e.*, until March 3, 2022.

By Secretarial Letter on January 6, 2022, the Commission granted Peoples Gas' request for a 45-day extension. Pursuant to the TCJA Order and the January 6, 2022, Secretarial Letter at Docket No. P-2021-3025989, Peoples Gas hereby files the above-captioned Petition.

Copies will be provided as indicated on the Certificate of Service.

Rosemary Chiavetta
March 3, 2022
Page 2

Respectfully submitted,

Michael W. Hassell

Michael W. Hassell

MWH/dmc
Enclosures

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been served upon the following persons, in the manner indicated, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

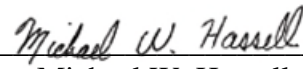
VIA E-MAIL

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Date: March 3, 2022



Michael W. Hassell

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Petition of Peoples Gas Company LLC For Approval :
To Distribute The Net Savings Associated With : P-2022-
Excess Accumulated Deferred Income Taxes :

**PEOPLES GAS COMPANY LLC’S PETITION FOR APPROVAL TO DISTRIBUTE TO
CUSTOMERS THE NET SAVINGS ASSOCIATED WITH ITS EXCESS
ACCUMULATED DEFERRED INCOME TAXES FOR THE JANUARY 1, 2018, TO
DECEMBER 31, 2021, PERIOD.**

I. INTRODUCTION

Pursuant to the Pennsylvania Public Utility Commission’s (“Commission”) Opinion and Order dated November 18, 2021, at Docket No. P-2021-3025898 (“November 18 Order”), Peoples Gas Company LLC (“Peoples Gas” or “Company”) hereby files this Petition for Approval to Distribute to Customers the Net Savings Associated with Its Excess Accumulated Deferred Income Taxes (“EADIT”) for the January 1, 2018, to December 31, 2021, Period (“Petition”).

As explained further in the instant Petition, Peoples Gas is proposing to distribute the amortized amount of EADIT-related savings to customers beginning July 1, 2022. The distribution of the EADIT-related savings would result in those tax savings flowing back to Peoples Gas’s customers by December 31, 2022.

In support of this Petition, Peoples Gas states as follows:

I. RELEVANT BACKGROUND AND PROCEDURAL HISTORY

1. By Secretarial Letter dated February 12, 2018, at Docket No. M-2018-2641242, the Commission directed Peoples Gas and other major jurisdictional utilities to file current base rates

and riders as temporary rates, pursuant to Section 1310(d) of the Public Utility Code. 66 Pa. C.S. § 1310(d). The Commission initiated that proceeding to determine the effects of the Tax Cuts and Jobs Act of 2017 (“TCJA”) on the tax liabilities of Commission-regulated public utilities for 2018 and future years. The TCJA, *inter alia*, reduced the corporate Federal Income Tax rate from 35% to 21% effective January 1, 2018.

2. The February 12, 2018, Secretarial Letter also directed Peoples Gas and the other major jurisdictional utilities to file certain data concerning the effects of the TCJA on each utility. On March 9, 2018, Peoples Gas filed the required information and completed Attachment C of the Secretarial Letter, including a calculation of a negative surcharge to be applied to customer bills in accordance with a prescribed formula. That filing by Peoples Gas indicated a negative surcharge of -2.6676%.

3. By order entered May 17, 2018, at Docket No. R-2018-3000502 (“Peoples Gas Compliance Order”), the Commission approved temporary rates for Peoples Gas, pursuant to Section 1310(d), 66 Pa. C.S. § 1310(d), in the form of a negative surcharge of -2.6676% for a trial period of six months. The Peoples Gas Compliance Order further directed that if the temporary rates become permanent due to no further action, these rates will remain in effect until Peoples Gas files and the Commission approves new base rates pursuant to Section 1308(d), 66 Pa. C.S. § 1308(d), that include the effects of the TCJA tax rate changes.

4. The Peoples Gas Compliance Order provided that the TCJA temporary surcharge will be effective July 1, 2018 on a prospective basis. However, the Commission also recognized that the tax savings from TCJA commenced on January 1, 2018. In lieu of addressing this portion of the tax savings in the May 17, 2018 order, the Commission directed Peoples Gas to establish a “deferred regulatory liability” account to record on its books the tax savings associated with the

TCJA for the January 1, 2018, through June 30, 2018, time period (the “Stub Period”). The Peoples Gas Compliance Order also directed that: the account shall accrue interest at the residential mortgage lending rate specified by the Secretary of Banking in accordance with the Loan Interest and Protection Law (41. P.S. §§ 101, et seq.); the rate treatment of this amount plus accrued interest shall be addressed in Peoples Gas’ next base rate case; in that future proceeding, Peoples Gas and parties can address the appropriate negative surcharge, amortization or other disposition of this deferred regulatory liability, including any legal issues; and if Peoples Gas has not filed, within three (3) years of May 17, 2018 (i.e., by May 17, 2021), a Section 1308(d), 66 Pa. C.S. § 1308(d), general base rate case, Peoples Gas must file a petition to propose how to distribute the funds in the deferred regulatory liability account related to the Stub Period.

5. Peoples Gas did not file a Section 1308(d) general base rate case between May 17, 2018, and May 17, 2021.

6. On further review of the negative surcharge calculations contained in the March 9, 2018, filing, Peoples Gas determined that those calculations did not fully reflect the tax reductions intended by the Commission and did not correctly calculate the negative surcharge. In accordance with the procedure set forth in the Peoples Gas Compliance Order, Peoples Gas then filed on June 4, 2018, a petition for reconsideration to allow Commission staff to review and address the newly discovered computation errors.

7. The petition for reconsideration stated a corrected negative surcharge of -6.6820%, which was approved by the Commission by Reconsideration Order entered on June 14, 2018. The petition for reconsideration did not request modification and the Reconsideration Order did not modify any of the procedures approved in the Peoples Gas Compliance Order, related to the

establishment of the deferred regulatory liability account and the distribution of funds in that account.

8. On July 5, 2018, Peoples Gas filed REPLACEMENT PAGE to Supplement No. 50 to Peoples Gas' Tariff Gas- PA PUC No. 8 with an effective date of July 1, 2018. Supplement No. 50 was filed in compliance with the Peoples Gas Compliance Order and June 14, 2018, orders and included the rate schedule headed Rider TCJA – TCJA Temporary Surcharge. By Secretarial Letter issued July 9, 2018, this tariff filing was accepted and made effective as of July 1, 2018.

9. On May 17, 2021, Peoples Gas filed a Petition to Establish a Mechanism to Distribute the Tax Savings Associated with Tax Cuts and Jobs Act of 2017 for the Period between January 1, 2018, and June 30, 2018 (“TCJA Petition”) at Docket No. P-2021-302598. The TCJA Petition was filed in accordance with the directives of the Peoples Gas Compliance Order.

10. Through the TCJA Petition, Peoples Gas estimated that it had a total refund obligation of \$3,723,470. This amount included \$3,087,632 representing the tax savings associated with the TCJA for the Stub Period, plus \$635,838 of projected interest accrued as the residential mortgage lending rate specified by the Secretary of Banking in accordance with the Loan Interest and Protection Law (41. P.S. §§ 101, et seq.) through June 2022, the midpoint of the proposed refund period.

11. Also through the TCJA Petition, Peoples Gas proposed to distribute its refund obligation over the calendar year 2022 through an adjustment to the TCJA Temporary Surcharge as part of the annual TCJA Temporary Surcharge filing to be made on December 1, 2021.

12. In response to a Data Request from the Commission’s Bureau of Technical Utility Services, Peoples Gas recalculated its interest calculation to be consistent with the interest methodologies used by other utilities in their filings to distribute Stub Period tax savings. This

recalculation resulted in a return of interest of \$697,836 in addition to the tax savings of \$3,087,632 for a total return of \$3,785,568.

13. On November 18, 2021, the Commission issued its Order ruling on the TCJA Petition. Through the November 18 Order, the Commission approved Peoples Gas's TCJA Petition with the modification to the calculation of interest owed, as noted above.

14. Further, the TCJA Order explained that Peoples Gas did not include tax savings associated with the Company's EADIT for the Stub Period, and that the Commission had approved the distribution of TCJA-related tax savings for the period prior to July 1, 2018, which included the flowback of EADIT, for other utilities. The Commission also stated that the "Commission's intent to flow back taxes to customers on a current basis is clear.... Thus, it is clear that the Commission intended for all tax savings to be flowed back to customers on a timely basis." As such, the Commission required Peoples Gas to file a Petition within 60 days of the TCJA Order to distribute the tax savings associated with its EADIT.

15. On December 17, 2021, Peoples Gas filed a Letter-Petition for Extension of Time for filing the petition to distribute the tax savings associated with the Company's EADIT ("Letter-Petition"). The Letter Petition requested a 45-day extension to file a Petition to distribute the Company's EADIT savings, explaining that the Company required more time to file a Petition to distribute its EADIT savings because of the need to examine tax normalization concerns stemming from an October 22, 2021, Internal Revenue Service Private Letter Ruling at No. PLR-101961-21 in response to an inquiry from another public utility, as well as possible conflicts with upcoming holidays and the end of year closing of Peoples Gas's books.

16. On January 6, 2022, the Commission issued a Secretarial Letter granting the Company's extension of time request. As such, Peoples Gas is required to file this Petition to distribute its EADIT savings on or before March 3, 2022.

II. PROPOSAL TO DISTRIBUTE THE AMORTIZED AMOUNT OF EADIT

17. Peoples Gas's TCJA Petition met the requirements of the calculation directed by the Commission in the Peoples Gas Compliance Order, however, as noted by the TCJA Order, the calculation excluded the additional savings related to the Company's EADIT for the Stub Period.

18. Peoples Gas has undertaken a detailed review of its annual TCJA surcharge calculations, along with reviewing other utilities' calculations. As a result of this review, the Company has determined that, in addition to refunding EADIT for the Stub Period and the rate base offset, the Company must correct its treatment of accumulated deferred income taxes since the inception of the Company's TCJA Rider. The rate base offset used in the TCJA calculation needs to be cumulative in order to conform to tax normalization requirements, as explained in the IRS guidance set forth in PLR-101169-21, a copy of which is attached as Appendix A.

19. Accordingly, Peoples Gas proposes to refund the amortization of EADIT-related tax savings and rate base offset, including a gross up and accrued interest, upon Commission approval through December 31, 2022, through the Company's existing TCJA rider. The calculation of the total additional amount to be returned, \$939,925, is attached hereto as Exhibit No. 1. Page 1 of the exhibit calculates the proposed change in the TCJA rate from the existing negative surcharge rate of 8.5353% to proposed negative surcharge rate of 11.4253%. Page 2 of the exhibit provides a detail of the components of the refund and page 3 provides the detailed calculations of the refund.

20. Currently, the TCJA surcharge for 2022 provides for a negative surcharge of 8.5353%, which applies as a credit for service on Peoples Gas's customer's bills. The amount refunded through this petition will be an additional \$939,925. Assuming timely approval of this change to allow for a July 1, 2022, implementation of the new TCJA tariff supplement, a new negative surcharge of 11.4253% would be implemented effective July 1, 2022, through December 31, 2022.

21. Peoples Gas will calculate its TCJA surcharge going forward from January 1, 2022, to include the amortization of the Company's EADIT and a rate base offset in accordance with IRS normalization rules.

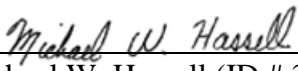
22. In order to implement the distribution of the amortization of EADIT and a cumulative rate base offset in a timely manner, Peoples Gas respectfully requests Commission approval of the instant Petition no later than June 1, 2022.

III. CONCLUSION

WHEREFORE, for the reasons set forth above, Peoples Gas Company LLC respectfully requests that the Pennsylvania Public Utility Commission grant this Petition for Approval to Distribute to Customers the Net Tax Savings Associated with Its Excess Accumulated Deferred Income Taxes for the January 1, 2018 to December 31, 2021 period and thereby authorize Peoples Gas Company LLC to file and place into effect an interim revision to its TCJA Temporary Surcharge so to affect the distribution of an additional \$939,925 of net tax savings associated with the Company's Excess Accumulated Deferred Income Taxes, as set forth above and calculated in Exhibit 1 to this Petition.

Respectfully submitted,

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Date: March 3, 2022

Attorneys for Peoples Gas Company LLC

Exhibit 1

Peoples Gas Company LLC
 TCJA EADIT Petition
 Rate Calculation

Line No.		Existing Rate Calculation	Adjustment	Revised Rate Calculation
1	Earnings Excess (See December 1, 2021 Filing)	\$ 3,641,824		
2	Complement of Tax Rate	0.711079		
3	Revenue Excess (Line 1 / Line 2)	\$ 5,121,546	\$ 939,925	
4	Less: Projected July 2018 - December 2021 over(under) difference	\$ 3,355,066		
5	Subtotal	\$ 1,766,480	\$ 939,925	
6	Jan - June 2018 Stub Period Refund	\$ 3,785,468	\$ -	
7	Total over(under)	\$ 5,551,948	\$ 939,925	
8	Commission Allowed Revenues	\$ 65,046,689 (1)	\$ 32,523,345 (2)	
9	Percent Increase (Decrease)	-8.5353%	-2.8900%	-11.4253%
		<i>Rate effective January 1, 2022</i>	<i>see Exhibit 1, page 2</i>	<i>Proposed Rate effective July 1, 2022</i>

Notes

(1) - estimated annual revenues

(2) - estimated revenues for the period of July 1, 2022 through December 31, 2022

Peoples Gas Company LLC
TCJA EADIT Petition
Summary of Adjustments

Exhibit No. 1
Page 2 of 3

Line No.	Item	Amount	Support	Description
1	EADIT	\$ (1,389,927)	see page 3, column (1)	EADIT Amortization - Jan. 1, 2018 to Dec. 31, 2021
2	Less: EADIT Rate Base Offset	837,852	see page 3, column (7)	Cumulative Impact of Deferred Taxes
3	Gross Up	(224,314)	see page 3, column (8)	Adjustment to refund revenue
4	Plus: Interest	(163,536)	see page 3, column (14)	Regulatory Interest
5	Amount to be refunded	<u>\$ (939,925)</u>		

Appendix A

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **202142002**
Release Date: 10/22/2021
Index Number: 167.22-01

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B6
PLR-101961-21

Date:
July 26, 2021

Legend

Taxpayer =
Corporation =
State A =
State B =
Commission A =
Commission B =
Order =
Date 1 =
Date 2 =
Date 3 =
Date 4 =
Date 5 =
Date 6 =
Date 7 =
Date 8 =
Year 1 =
Year 2 =
Year 3 =

Dear :

This letter responds to a request for a private letter ruling dated January 7, 2021, submitted by Taxpayer. Taxpayer requests rulings with respect to the application of § 168(i)(9) of the Internal Revenue Code, former § 167(l), and section 13001(d) of the Tax Cuts and Jobs Act, Pub. L. 115-97(the "TCJA") (together, the Normalization Rules), regarding the proper accounting and ratemaking treatment of excess deferred income

taxes (“EDIT”). The relevant facts as represented in Taxpayer’s submission are set forth below.

FACTS

Taxpayer is an electric and natural gas utility headquartered in State A.

Taxpayer is a wholly owned member of Corporation and Subsidiaries consolidated group. Corporation is an energy services holding company incorporated in State B. Taxpayer is included in the consolidated federal income tax return of Corporation. Taxpayer employs a calendar year reporting period and uses an accrual method of accounting. Corporation elected to be treated as a corporation for federal tax purposes. Corporation and Subsidiaries are not presently under audit by the Internal Revenue Service.

Taxpayer is engaged in the production, transmission, and distribution of electricity and the distribution of natural gas in State A. It is subject to the regulatory authority of Commission A and Commission B as to the terms and conditions of service and the rates it is permitted to charge for its service. Its rates are established or approved based on its costs of service, including a return on its capital investment (rate base).

Taxpayer’s rates are established by Commission A on a “cost of service, rate-of-return” basis. Thus, Taxpayer is permitted an opportunity to recover its prudently incurred costs and earn an appropriate return on its rate base, which reflects its net invested capital. The convention employed in State A with respect to rate base is that a utility’s accumulated deferred income tax balance (“ADIT”) offsets gross rate base (rate base computed before reduction by ADIT). Included in Taxpayer’s ADIT balance are a significant amount of deferred taxes attributable to accelerated depreciation claimed with respect to public utility property. Thus, Taxpayer’s ADIT is, to a substantial extent, subject to the normalization rules contained in § 168(i)(9) and former § 167(l). Commission A uses an historical test period consisting of a 12-month period for purposes of determining Taxpayer’s costs and rate base. Results of this test period are adjusted by “pro forma adjustments” to remove materially distortive items and to give effect to known and measurable changes that are not offset by other factors.

As part of this process of setting rates, Taxpayer computes its depreciation expense and its income tax expense, including both current and deferred components of income tax expense, for inclusion in its cost of service. Taxpayer also reduces its gross rate base by its ADIT balance to determine the rate base on which it is permitted to earn a return. Taxpayer’s accounting treatment for depreciation expense, income tax expense, ADIT, and rate base has been consistent with the Normalization Rules.

On December 22, 2017, the TCJA was signed into law. Among other changes, the TCJA reduced the federal corporate income tax rate from 35 percent to 21 percent for tax years beginning after December 31, 2017, Taxpayer’s calendar Year 1 tax year.

As a result of the tax reduction, the deferred taxes Taxpayer had accumulated at a 35 percent rate were reduced to those that would have been accumulated at a 21 percent rate had the 21 percent rate been in effect for all prior years. Because Taxpayer had a net deferred tax liability (“DTL”) on December 31, 2017, the tax rate reduction resulted in EDIT, because Taxpayer now expects to pay income taxes to the Department of the Treasury at the reduced 21 percent rate, as the timing differences that gave rise to its DTL reverse. In general, Taxpayer had collected the EDIT from customers through its traditional ratemaking methodology and not on a precise dollar-for-dollar basis. The 14-percentage point reduction in the tax rate is available to reduce the tax expense that Taxpayer included in setting customer rates. It is the timing of this reduction of the EDIT that is the issue of this ruling request.

Taxpayer maintains records that include the vintage records necessary to apply the average rate assumption method (“ARAM”). The total balance of Taxpayer’s EDIT is unknown. The annual amount of EDIT reversal under ARAM will vary each year, and this variance is unknown at this time. In general, this variability is caused by future events, including the time at which a vintage begins to reverse or when a vintage fully reverses. Taxpayer provides deferred taxes on plant-related timing differences whether or not those timing differences are protected by the Normalization Rules or unprotected by the Normalization Rules. Taxpayer and Commission A intend to apply ARAM to all plant-related timing differences. There is no dispute over this intent to apply ARAM. Throughout Taxpayer’s general rate case (“GRC”), these balances are commonly referred to as “protected plus” or “PP” to acknowledge the fact that ARAM is being applied not only to all protected EDIT, but also unprotected plant-related EDIT.

Taxpayer has been accounting for EDIT balances in ratemaking on a consistent method since the Tax Reform Act of 1986, Pub. L. No: 99-514 (“TRA 1986”). That method has been as follows:

Taxpayer closes its books on a monthly basis. Each resulting monthly income statement and balance sheet contains its share of book depreciation, rate base, income tax expense, and ADIT (including EDIT). Taxpayer includes the ARAM reversal of EDIT in its monthly calculation of tax expense. Its EDIT balance is included in its ADIT to ensure that rate base is reduced by the proper amount of deferred taxes. This treatment ensures that book depreciation, income tax expense, ADIT, and rate base are computed consistently.

Taxpayer’s rates are set periodically in a GRC using an historical test period. In a GRC, the accounting activity recorded in each month during the historical test year is the basis for setting customer rates, plus or minus any pro-forma adjustments. Once customer rates are established, they remain constant until the next GRC. At that next GRC, customer rates will be reset based on a new, different historical test year – different income and expenses (including income tax expense and book depreciation expense), different rate base, and different

ADIT. The assumption underlying the use of an historical test year is that the costs and benefits in the historical period, plus or minus any pro-forma adjustments, will be representative of future periods during which customers will pay the rates. The process is intended to ensure that customer rates will be fair, just, reasonable, and sufficient. This is so even though the actual income and incurred costs, including EDIT reversals, for the period for which the rates are set will be different than those used to set the rates during the GRC.

In its Year 2 GRC, Taxpayer used calendar year Year 1 as the historical test year. This was its first GRC following the TCJA. In its monthly accounting activity throughout Year 1, Taxpayer recorded its EDIT reversal using ARAM. Those accounting entries had the effect of reducing Taxpayer's deferred tax expense and reduced Taxpayer's EDIT balance. No other entries were made with respect to EDIT. These entries were identical to those Taxpayer made since the tax rate reduction provided by the TRA 1986 to account for the EDIT created by the TRA 1986 tax rate reduction and used to set rates since that time.

In filing its Year 2 GRC, Taxpayer included the EDIT reversals that it recorded in calendar year Year 1, consistent with the use of Year 1 as the historical test period. In addition, its ADIT balance, including the EDIT, reflected these reversals. The accounting that occurred in calendar year Year 1 formed the basis for the amounts that Taxpayer proposed in setting rates for Year 2. In other words, the Year 1 book accounting provides the basis for ratemaking in the Year 2 GRC, which was originally intended to be effective for new rates beginning in mid-Year 3.

In response to Taxpayer's Year 2 GRC filing, Commission A issued Order on Date 1. Commission A did not follow Taxpayer's requested historical treatment. Instead, Commission A ordered the approach that raises the normalization issues that are the subject of this request.

Order requires Taxpayer to separately track EDIT on a tariff rate schedule independent of its rates set in its general rate order. In one requirement, Commission A requires the schedule to be updated annually for the reversal of the EDIT for the current year as if rates were set each year. Furthermore, in another requirement, Commission A requires Taxpayer to true-up for the difference between the EDIT amounts set in the schedule and the actual amount passed back due to volumetric variances. Commission A has ordered that the schedule must produce an annual adjustment to Taxpayer's rates for ARAM amortization of EDIT without any corresponding adjustment to Taxpayer's rates for annual changes in depreciation expense, income tax expense, rate base, or ADIT (including EDIT).

Order includes Taxpayer's depreciation expense, tax expense, ADIT (including EDIT), and rate base for the test year in the computation of the primary cost of service and base rate. Order then requires an adjustment to cost of service by removing the test year ARAM amortization of EDIT and substituting for that amount, as a reduction in

cost of service, the estimated EDIT amortization for the year following the test year plus the next year which includes part of the rate year (in total, a 24-month period). No other similar adjustments are made for depreciation expense, income tax expense, ADIT (including EDIT), or rate base, which were, instead, based on the historical test period (again, not including pro forma adjustments which are not a topic of this PLR).

Order was applied to Taxpayer as follows: The test year was calendar year Year 1. The original rate year was to be Date 2 through Date 3, but the start of that rate period was initially delayed due to Coronavirus to an effective date of Date 4. After some further delays, the rates became effective Date 5, for gas operations and Date 6, for electric operations. Taxpayer's originally proposed ARAM EDIT amortization was based on the test year (calendar year Year 1). The Order adjustment was based on an estimate of ARAM EDIT amortization for the two-year period Date 7 through Date 8, the total two-year amount to be passed back in one year.

Taxpayer has proposed corrective action if the Service concludes that the EDIT treatment in Order is not consistent with a normalization method of accounting. If that determination is made, Taxpayer will need to reestablish a normalization method of accounting. In that event, Commission A has agreed to immediately open a proceeding upon Taxpayer's receipt of a PLR from the Service and revisit its order to comply with the Normalization Rules. This agreement was a condition of Taxpayer dismissing its judicial appeal of Order.

Taxpayer has taken additional action to ensure a quick and complete correction if Order is found inconsistent with the Normalization Rules. Taxpayer filed an accounting petition with Commission A on Date 5 in which it requested that Commission A allow Taxpayer to track the difference between Taxpayer's approach and the approach required in Order. The difference between the two approaches will be recorded to Taxpayer's balance sheet as a monthly entry. Two accounts will be used – a tracking account and a contra account (collectively, the "PLR Tracker Accounts"). The two accounts will net to zero and thereby have no impact on Taxpayer's financial results, as doing otherwise would not be in compliance with Commission A's order. However, the accounts will provide contemporaneous documentation of the variance between the two approaches.

For gas customers, rates consistent with Order went into effect on Date 5. For electric customers, new rates went into effect on Date 6. For both gas and electric customers, the accounting petition will provide Commission A with the ability to correct any normalization infraction that the IRS identifies in its ruling.

Taxpayer anticipates that any correction will involve two elements. The first element is a new tariff rate that will comply with the Service's ruling, which will be a new base tariff. That rate would continue in effect until Taxpayer's next rate-setting event, which is expected to be a GRC. The second element is a temporary tariff rate to bring the EDIT balance back into alignment with a normalization method of accounting. This

second component would have the effect of reversing the amounts that were tracked in the PLR Tracker Accounts. The recovery of these balances would likely occur over a relatively short period.

RULINGS REQUESTED

Taxpayer requests rulings whether the accounting for EDIT as required by Order of Commission A is consistent with the Normalization Rules of § 168(i)(9), former § 167(l), and section 13004(d) of the TCJA. Specifically:

- (1) Whether the Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA permit Taxpayer to adjust its EDIT ARAM amortization based on the test year to the EDIT ARAM amortization based on one or more subsequent years without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense;
- (2) Whether the Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA permit Taxpayer to adjust its EDIT ARAM amortization annually without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense;
- (3) Whether the Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA permit Taxpayer to provide a true-up to EDIT ARAM amortization in the year following the rate year based on volume variances between the test year and the rate year without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense;
- (4) Additionally, Taxpayer asks that if we determine that any of the requirements described of Order are not consistent with the Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA, Taxpayer requests that we provide in the ruling that Taxpayer will not be considered to be in violation of the normalization rules if it follows the corrective actions described in its letter.

LAW AND ANALYSIS

Former section 167(l) of the Code generally provided that public utilities were entitled to use accelerated methods for depreciation if they used a “normalization method of accounting.” A normalization method of accounting was defined in former § 167(l)(3)(G) in a manner consistent with that found in § 168(i)(9)(A). Section 1.167(l)-1(a)(1) provides that the normalization requirements for public utility property pertain only to the deferral of federal income tax liability resulting from the use of an accelerated method of depreciation for computing the allowance for depreciation under § 167 and the use of straight-line depreciation for computing tax expense and depreciation expense for purposes of establishing cost of services and for reflecting operating results

in regulated books of account. These regulations do not pertain to other book-tax timing differences with respect to state income taxes, F.I.C.A. taxes, construction costs, or any other taxes and items.

Section 168(f)(2) provides that the depreciation deduction determined under § 168 shall not apply to any public utility property (within the meaning of § 168(i)(10)) if the taxpayer does not use a normalization method of accounting.

In order to use a normalization method of accounting, § 168(i)(9)(A) requires that a taxpayer, in computing its tax expense for establishing its cost of service for ratemaking purposes and reflecting operating results in its regulated books of account, use a method of depreciation with respect to public utility property that is the same as, and a depreciation period for such property that is not shorter than, the method and period used to compute its depreciation expense for such purposes. Under § 168(i)(9)(A)(ii), if the amount allowable as a deduction under § 168 differs from the amount that would be allowable as a deduction under § 167 using the method, period, first and last year convention, and salvage value used to compute regulated tax expense under § 168(i)(9)(A)(i), the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from such difference.

Section 168(i)(9)(B)(i) of the Code provides that one way the requirements of § 168(i)(9)(A) will not be satisfied is if the taxpayer, for ratemaking purposes, uses a procedure or adjustment which is inconsistent with such requirements. Under § 168(i)(9)(B)(ii), such inconsistent procedures and adjustments include the use of an estimate or projection of the taxpayer's tax expense, depreciation expense, or reserve for deferred taxes under § 168(i)(9)(A)(ii), unless such estimate or projection is also used, for ratemaking purposes, with respect to all three of these items and with respect to the rate base (hereinafter referred to as the "Consistency Rule").

Taxpayer's requests relate primarily to Taxpayer's compliance with the Consistency Rule. Taxpayer asks whether the Normalization Rules permit Taxpayer to adjust its EDIT ARAM amortization annually without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense. More specifically, Taxpayer also asks whether the Normalization Rules permit Taxpayer to adjust its EDIT ARAM amortization based on the test year to the EDIT ARAM amortization based on one or more subsequent years without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense. Lastly, Taxpayer asks whether the Normalization Rules permit Taxpayer to provide a true-up to EDIT ARAM amortization in the year following the rate year based on volume variances between the test year and the rate year without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense.

Therefore, the threshold question is whether the Consistency Rule applies to EDIT being accounted for under ARAM. Because these amounts were originally deferred pursuant to a normalization method of accounting, these amounts remain

subject to the Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA. Thus, if the EDIT being accounted for under ARAM is subject to Normalization Rules, the Consistency Rule must apply to the EDIT.

As described in § 168(i)(9)(B)(ii), the use of a procedure or adjustment that uses an estimate or projection of any of (1) the taxpayer's tax expense, (2) depreciation expense, or (3) reserve for deferred taxes under § 168(i)(9)(A)(ii), does not comply with the Consistency Rule unless such estimate or projection is also used, for ratemaking purposes, with respect to all three of these items and with respect to the rate base. Therefore, generally, the Normalization Rules do not permit Taxpayer to adjust its EDIT ARAM amortization without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense. More specifically, in regard to request (1), the Normalization Rules do not allow Taxpayers to make an adjustment to cost of service by removing the test year ARAM amortization of EDIT and substituting for that amount, as a reduction in cost of service, the estimated EDIT amortization for the year following the test year plus the next year which includes part of the rate year (in total, a 24-month period) while also making no similar adjustments for depreciation, expense, income tax expense, ADIT (including EDIT), or rate base, which were based on the historical test period. In regard to request (2), the Normalization Rules do not allow Taxpayer to adjust its EDIT ARAM amortization annually without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense.

Additionally, in response to request (3), providing a true-up to EDIT ARAM amortization in the year following the rate year based on volume variances between the test year and the rate year without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense likewise is not in compliance with the Consistency Rule. The true-up mechanism adjusts for volume differences only with respect to one item, EDIT amortization. This results in the use of estimated volumes in setting rates for all items other than EDIT reversal which uses actual volumes. This treatment is an inconsistent use of estimates or projects not allowed by section 168(i)(9)(B).

The Normalization Rules were enacted in response to Congressional concerns over the growing number of public utility commissions that were mandating investor-owned regulated utilities to not retain these tax benefits from accelerated depreciation, but, instead, to immediately flow-through all of these tax incentives to ratepayers in the form of lower income tax expense in regulated cost of service rates. Congress' response was to enact legislation that would preclude regulated investor-owned utilities from utilizing accelerated depreciation methods of tax purposes if the related tax benefits were immediately flowed-through to ratepayers in rates or were flowed-through to ratepayers faster than permitted under the Normalization Rules.

The underlying concept and purpose of the Normalization Rules is to prevent the flow-through of these accelerated depreciation-related tax benefits to ratepayers in regulated rates any faster than permitted by the Normalization Rules. Thus, the flow-

through of these tax benefits to ratepayers faster than permitted by the Normalization Rules would result in a normalization violation that would preclude the taxpayer from using any of the accelerated tax depreciation methods on public utility property and, instead, require the taxpayer to use the same depreciation method and period as those used to compute depreciation expense in its cost of service for ratemaking purposes. Conversely, a taxpayer that flows through these tax benefits to ratepayers slower than permitted by the Normalization Rules, or that never flows through any of the tax benefits from accelerated depreciation to ratepayers, would not be in violation of those rules.

By removing EDIT amortization for the test year and including the estimated EDIT amortization for the two following years, the EDIT amortization on the cost of service is higher than allowed under the ARAM limitation for the test year. This acceleration of the EDIT amortization occurs under the Order without any reduction to the EDIT balance which is taken into account in determining rate base. This provides customers not only with a lower cost of service through the acceleration of EDIT amortization but also a rate base which is artificially low because the EDIT credit balance included in rate base has not been reduced by the EDIT reversal that has been accelerated. This incorrectly provides customers with the double benefit of lower cost of service and lower rate base for the same EDIT.

Section 168(f)(2) provides that the depreciation deduction determined under § 168 shall not apply to any public utility property (within the meaning of § 168(i)(10)) if the taxpayer does not use a normalization method of accounting. However, in the legislative history to the enactment of the normalization requirements of the Investment Tax Credit (ITC), Congress stated that it hopes that sanctions will not have to be imposed and that disallowance of the tax benefit (there, the ITC) should be imposed only after a regulatory body has required or insisted upon such treatment by a utility. See Senate Report No. 92-437, 92nd Cong., 1st Sess. 40-41 (1971), 1972-2 C.B. 559, 581. See also, Rev. Proc. 2017-47, 2017-38 I.R.B. 233, September 18, 2017.

Commission A has, at all times, required that utilities under its jurisdiction use normalization methods of accounting. Further, Commission A has agreed to immediately open a proceeding upon receipt of Taxpayer's receipt of a PLR from the Service and revisit its order to comply with the Normalization Rules if the Service concludes that Order results in a rate calculation that is not consistent with the Normalization rules.

Taxpayer also intended at all times to comply with the Normalization Rules. Taxpayer has initiated the measures necessary to conform to the Normalization Rules. As noted, Taxpayer filed an accounting petition with Commission A in which it requested that Commission A allow Taxpayer to track the difference between Taxpayer's approach and the approach required in Order. The difference between the two approaches will be recorded to Taxpayer's balance sheet as a monthly entry identified as "the PLR Tracker Accounts." For both gas and electric customers, the accounting petition provides

Commission A with the ability to correct any normalization infraction that the IRS identifies in this ruling.

Taxpayer's failure to comply with the Normalization Rules was inadvertent. Because the Commission, as well as Taxpayer, at all times sought to comply, and because corrective actions will be taken at the earliest available opportunity, it is not appropriate to conclude that the failure to follow the Consistency Rule for the EDIT that is a part of ADIT and calculated according to ARAM constituted a normalization violation and apply the sanction of denial of accelerated depreciation to Taxpayer.

CONCLUSION

Accordingly, we rule as follows:

- (1) The Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA do not permit Taxpayer to adjust its EDIT ARAM amortization based on the test year to the EDIT ARAM amortization based on one or more subsequent years without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense;
- (2) The Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA do not permit Taxpayer to adjust its EDIT ARAM amortization annually without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense.
- (3) The Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA do not permit Taxpayer to provide a true-up to EDIT ARAM amortization in the year following the rate year based on volume variances between the test year and the rate year without making similar adjustments to rate base, ADIT, book depreciation expense, and tax expense.
- (4) While we have determined that the described requirements of Order are not consistent with the Normalization Rules of § 168(i)(9), former § 167(l), and section 13001(d) of the TCJA, Taxpayer will not be considered to be in violation of the normalization rules if it follows the corrective actions described in its letter.

Except as specifically set forth above, no opinion is expressed or implied concerning the federal income tax consequences of the above described facts under any other provision of the Code or regulations.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides it may not be used or cited as precedent.

This ruling is based upon information and representations submitted by Taxpayer and accompanied by penalty of perjury statements executed by an appropriate party.

While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative. We are also sending a copy of this letter ruling to the LB&I Policy Office.

Sincerely,

Patrick S. Kirwan
Chief, Branch 6
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

cc:

VERIFICATION

I, Andrew P. Wachter, on behalf of Peoples Gas Company LLC, hereby state that the facts set forth in the foregoing document are true and correct to the best of my knowledge, information and belief, and that I expect to be able to prove the same at a hearing held in this matter. I understand that the statements herein are made subject to the penalties of 18 Pa. C.S. § 4904 (relating to unsworn falsification to authorities).

Date: 03/03/2022



Andrew P. Wachter