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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Consideration of the tax impacts associated with Tax Cuts and Jobs Act of 2017 Florida Public Utilities Company - Gas.
______________________________________/

DOCKET NO. 20180051-GU

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CITIZENS' POST HEARING BRIEF

The Citizens of the State of Florida, through the Office of Public Counsel ("Citizens" or "OPC"), pursuant to the Order Establishing Procedure in this docket, Order PSC-2018-0213-PCO-GU issued April 25, 2018, Order PSC-2018-0274-PCO-GU issued May 31, 2018, and Order PSC-2018-0412-PCO-GU issued August 20, 2018, submit this Post-Hearing Brief.

STATEMENT OF BASIC POSITION

Florida Public Utilities Company – Gas ("FPUC"), in its May 31, 2018 petition, seeks a determination by the Florida Public Service Commission ("Commission" or "PSC") related to the tax benefits arising from the Tax Cuts and Jobs Act of 2017 ("TCJA"). FPUC has identified, as a result of the TCJA, a regulatory liability for excess accumulated deferred income taxes ("ADIT") in the amount of $25,581,776. (TR 228) This represents money that belongs to FPUC's customers (both residential and commercial) and it should be returned to the customers who previously paid according to the higher income tax rate. However, FPUC proposes to retain the net annual amortization of the protected and unprotected excess ADIT estimated by FPUC to be approximately $537,174 annually. (TR 234) The Commission should reject this proposal as being unjust, unfair and unreasonable, and should apply this amount for the benefit of customers in the form of a rate reduction. (TR 260)

FPUC has also identified a base rate savings of $1,141,134 as a result of the TCJA. (TR 98, 234) This represents money that FPUC's ratepayers are currently paying at the higher income tax rate, which FPUC is not entitled to continue collecting. Again, FPUC is requesting to keep this money for which it has no valid claim. OPC Witness Smith disagreed with FPUC's proposal to retain this amount and contends the 2018 base rate income tax savings should be applied for the benefit of customers through a permanent base rate reduction. (TR 241)

FPUC Witness Cassel indicated the impact of the TCJA on the Company's Gas Reliability Infrastructure Program ("GRIP") results (i) in a 2018 tax savings of $1,040,141 and (ii) in an annual tax savings, for the period 2019 and beyond, of approximately $1.2 million. (TR 101) FPUC proposed to flow back the 2018 tax savings benefit to its customers by incorporating it as an over-recovery in its 2019 GRIP projection. (TR 101, 236) Additionally, FPUC proposed to apply the new 21 percent federal income tax rate into its 2019 GRIP surcharge projections and future projections, which will reduce the annual GRIP revenue amount by the annual tax savings of approximately $1.2 million. (TR 101, 236) OPC does not take issue with the Company's proposals to flow through the GRIP-related TCJA savings directly to its customers. (TR 241)

FPUC's revised filing on August 27, 2018, contained a reclassification of excess ADIT related to cost-of-removal from protected to unprotected. (TR 237) Witness Smith did not disagree with this classification; however, due to the uncertainty in this area and the fact that different utilities have taken different positions as to the classification, he testified that it may be appropriate for FPUC to seek a private letter ruling ("PLR") from the Internal Revenue Service ("IRS") regarding its classification of the excess ADIT relating to cost of removal/negative net salvage as "unprotected". (TR 237, 238) Notwithstanding, because of the cost involved in seeking such a ruling, Witness Smith acknowledged that guidance provided by PLRs to other Florida

utilities may be sufficiently clear so as to prevent FPUC and its affiliates from having to incur the costs to obtain their own specific PLR. (TR 240)

Since all other issues are subject to stipulations, this brief will address only issues 4B, 5B and 21.

ISSUES

ISSUE 4B: What is the appropriate disposition of the protected excess deferred income taxes?

OPC: The Company should not be allowed to retain the benefit of the protected excess ADIT. The protected excess ADIT should be reversed using an Average Rate Assumption Method ("ARAM") if the utility has the available information to calculate the ARAM, or via another appropriate method that complies with normalization requirements, if the Company does not have the information to compute the ARAM.

ARGUMENT:

FPUC Witness Cassel identified three impacts of the TCJA that FPUC's proposal addressed: (1) the federal tax rate change from 35% to 21%; (2) the Unprotected Deferred Tax Liability and Tax Asset; and (3) the Protected Deferred Tax Liability. (TR 98) Witness Cassel testified that, as a result of the TCJA, FPUC recorded a regulatory liability on its balance sheet for the Protected Deferred Tax at a rate of 35%, which it is now only required to pay at a rate of 21% in taxes. (TR 100) The benefit in the Protected Deferred Tax is recorded on FPUC's balance sheet as a grossed-up (for tax purposes) Deferred Regulatory Tax liability. (TR 100)

As OPC Witness Smith testified, these accumulated deferred income taxes (ADIT) result from differences between book and tax accounting, and represent balances that typically build up (or accumulate) over time, e.g. as tax deductions exceed corresponding book expense. (TR 227) Witness Smith explained that one primary source of ADIT results from claiming accelerated tax deductions. He further explained that the tax deductions on public utility property typically occur

on an accelerated basis (method differences) and over shorter periods of time (life differences) than book depreciation accruals relating to the original cost of the public utility property. (TR 227) He noted that these types of method/life differences are subject to normalization requirements under Sections 167 and 168 of the Internal Revenue Code. (TR 227) The term "protected" ADIT applies to the portion of the property-related ADIT that is subject to normalization requirements and accelerated tax depreciation (including bonus tax depreciation). (TR 229)

Further, Witness Smith explained that the "excess" ADIT (EADIT) is the portion of the ADIT balances that are "excess" based on recalculating the difference between the old federal income tax rate (FIT) of 35% under which the ADIT was originally accumulated and the new FIT rate of 21% under the TCJA. (TR 227) In other words, the utility's ADIT must be revaluated at the new FIT (as if it had always been applicable), and the amounts that have been accumulated using the FIT rates that are higher than the current 21% flat rate will represent "excess" ADIT. (TR 228) It is the protected EADIT that is subject to normalization and the Average Rate Assumption Method (ARAM). (TR 229) As of its August 27, 2018 filing, FPUC had an estimated regulatory liability for the Protected EADIT of $21,767,953. (TR 228) FPUC proposed that this amount should be amortized using the IRS prescribed methodology for a flow back period of 26 years at approximately $844,461 per year. (TR 232, HE2) Witness Cassel testified that FPUC wants to keep the estimated annual amortization of the protected EADIT of $844,461 instead of returning it to FPUC's customers. (TR 100, 183) However, Witness Cassel acknowledged that the EADIT amounts are included in the total tax savings of $2,181,275 and that these are monies FPUC's ratepayers have already paid to FPUC. (TR 182, 183) He further acknowledged it is the normal practice of utilities to pass through to its customers as an expense the payment of income taxes. (TR 188) Nonetheless, Witness Cassel asserted that retention of these EADIT amounts by

FPUC meets the intended goal of the TCJA by allowing the Company to continue making capital investments while potentially delaying the need for a costly rate proceeding. (TR 100) Yet, under cross-examination, Witness Cassel affirmed that the TCJA did not contain any language, express or otherwise, that suggests an intended goal of the act was to allow a utility to keep tax savings so as to continue making capital investments while potentially delaying the need for a rate proceeding. (TR 184)

In contrast to the Company's proposal to retain the benefits of protected EADIT, OPC recommends that these tax savings be flowed back to customers. Witness Smith testified that the annual amortization of the protected EADIT not related to the acquisition adjustment, should be applied for the benefit of the customers as a rate reduction. (TR 233, 241) To do otherwise would be unjust, unfair and unreasonable. The bottom line is the tax savings represent money that was previously paid by FPUC's customers, it belongs to those customers, and it should be returned to them.

ISSUE 5B: What is the appropriate disposition of the unprotected excess deferred taxes?

OPC: The Company should not be allowed to retain the benefit of the unprotected excess ADIT. The Unprotected excess ADIT net asset of $3,072,874 should be amortized over 10 years at $307,287 per year.

ARGUMENT:

As stated above in Issue 4B, OPC Witness Smith explained the EADIT is the portion of the ADIT balances that are "excess" based on recalculating the difference between the old FIT rate of 35% under which the ADIT was originally accumulated and the new FIT rate of 21% under the TCJA. (TR 227) He testified the "unprotected" property and non-property related EADIT is not subject to normalization requirements and that the amortization or application of these funds is up

to the discretion of the Commission. (TR 229) Witness Smith stated the unprotected ADIT will be revaluated at the lower 21% tax rate, creating balances of excess unprotected ADIT that can be flowed back to customers over amortization periods to be determined by the Commission (e.g., such as for the recovery of regulatory assets).

FPUC Witness Cassel testified that there are two components of the Unprotected Deferred Tax balance. (TR 99) The first component is a deferred tax liability associated with the acquisition adjustment with a grossed up balance of $6,518,569 and a remaining amortization of $298,560 per year. Id. The second component is a net unprotected deferred tax asset with an estimated balance of $3,072,874. Id. Witness Cassel further testified that FPUC requests the unprotected EADIT be amortized over 10 years at $307,287 per year. Id. He also suggested this annual amortization detriment should be netted against the annual protected benefit discussed above, and that FPUC should be allowed to retain the net of these amounts. (TR 99-100)

OPC Witness Smith agreed that the estimated annual Protected EADIT liability amortization of $844,461 less the estimated annual Unprotected EADIT amortization of $307,287 produces an estimate net benefit annual amount of $537,174. (TR 234) However, he testified that this net benefit amount of $537,174 should be returned to customers via a base rate reduction. (TR 234)

For the reasons articulated in Issue 4B, the Company should not be allowed to retain the customer's tax benefits. According to the Florida Supreme Court in Reedy Creek Co. v. Fla. Public Serv. Comm., 418 So. 2d. 249, 254 (1982), "a change in a tax law should no [sic] result in a 'windfall' to a utility, but in a refund to the customer who paid the revenue that translated into the

tax savings." (TR 235, HE 17)[1] By definition, the excess tax monies in FPUC's possession are a windfall.

In the recent cases before the Commission that address the tax savings, the electric and gas utilities have agreed to refund the monies to their customers or to apply them in a manner that directly benefits their customers (e.g., pay off storm costs in lieu of utilizing a storm surcharge). (TR 318) Currently, FPUC is earning a positive return, and Witness Cassel testified that FPUC would continue to earn within its authorized range without the customer's tax savings being retained by the Company. (TR 98) Although he contended that retaining the tax savings would not put FPUC in an over-earning position, Witness Cassel could not point to any calculations or evidence that was offered by FPUC to demonstrate where FPUC's projected earnings level would be if these customer tax saving were retained. (TR 103, 182) As stated above, Witness Cassel acknowledged that the EADITs are monies FPUC's ratepayers have already paid to the company (TR 182-183), and that it is a practice of utilities to pass through to customers as an expense the payment of income taxes. (TR 188) Witness Cassel further affirmed that, except for cost-of-capital components that would have to be replaced because of a lower amount of deferred taxes, the tax savings are basically revenue-neutral for the Company. (TR 188)

FPUC's proposal to keep the customer's tax savings associated with unprotected excess ADIT is both unfair and unreasonable. The tax savings represent money that belongs to the customers, and thus, should be flowed back to them. As recommended by Witness Smith, the $547,174 net amount of the Protected and Unprotected EADIT not related to the acquisition adjustment should be applied for the benefit of the customers as a rate reduction. (TR 241) To do otherwise would be unjust, unfair and unreasonable to FPUC's customers.

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[1] The term "windfall" is defined as "an unexpected, unearned, or sudden gain or advantage." *Merriam-Webster* https://www.merriam-webster.com/dictionary/windfall (last visited December 14, 2018).

ISSUE 21: Should FPUC be allowed to retain the tax benefits arising from the TCJA rate reduction, excluding the 2018 GRIP savings, as well as the estimated Deferred Tax portion of the Protected and estimated Unprotected Deferred Tax regulatory asset that are not associated with the acquisition adjustment?

OPC: No, FPUC should not be allowed to retain the tax benefits arising from the TCJA rate reduction.

ARGUMENT:

The estimated impact of the federal income tax rate change resulting from the 2017 Tax Act for FPUC is approximately $2,181,275. (TR 98, 180) FPUC Witness Cassel suggests the Company should be allowed to retain this amount instead of returning it to customers. (TR 98) However, Mr. Cassel admits FPUC is not currently under-earning and is projected to be earning within its authorized range - albeit at the lower end of the range for the foreseeable future. (TR 98, 102) Moreover, Mr. Cassel acknowledged that FPUC did not offer any evidence or provide any calculations indicating where FPUC would be earning relative to its authorized earnings range if the Commission were to allow the Company to keep the tax savings. (TR 182)

Witness Smith testified the 2018 base rate income tax savings should be applied for the benefit of customers through a base rate reduction. (TR 235) According to the Florida Supreme Court in Reedy Creek, "a change in a tax law should no [sic] result in a 'windfall' to a utility, but in a refund to the customer who paid the revenue that translated into the tax savings." (TR 235, HE 17)

Witness Cassel attempted to distinguish the Reedy Creek case from FPUC's position by offering that Reedy Creek utility was in an over-earnings position, and FPUC is not. (TR 113) He further claimed that, even if the entire tax benefit was retained by FPUC, it would not put the Company in an over-earnings posture, thus there would be no "windfall" to the utility. (TR 113) However, as stated above, by definition these excess monies are a windfall and FPUC failed to

provide any calculations or evidence to demonstrate what its projected earnings would be if the customer's tax savings were retained. (TR 182) Moreover, Witness Cassel mistakenly links the over-earning posture of the utility in Reedy Creek with the use of the term "windfall." The sentence plainly couples the idea of "windfall" with the idea that the customers who paid at the higher tax rate should benefit from the new lower tax rate.

Furthermore, Witness Cassel acknowledged that the tax savings represent monies that FPUC's ratepayers have already paid to the Company and affirmed that, except for cost-of-capital components that would have to be replaced because of the lower amount of deferred taxes, these funds (i.e. taxes) are basically revenue-neutral for FPUC. (TR 183, 188) Nonetheless, Witness Cassel suggests FPUC should be allowed to retain the tax proceeds "to recover costs not currently recovered in base rates such that [FPUC] may be able to maintain base rates at their current levels longer than would otherwise be possible given [FPUC's] current earnings posture." (TR 102:9-12). In spite of referencing no specific "costs" or changes in circumstances over the prior years, Witness Cassel seems to make a vague threat that FPUC will file a general rate case if not allowed to retain the tax proceeds. *See id.*

While the Company seductively asserts that it could avoid a "potential" rate case, a close examination of Witness Cassel's testimony demonstrates no rate case was avoided. In fact, he acknowledged that FPUC was earning within its authorized earnings range. (TR 98) Furthermore, none of the testimony or exhibits submitted by FPUC included any evidence indicating a rate case by the Company was pending. (HE 2-5)

During cross-examination, Witness Smith was questioned regarding the Commission's consideration of earnings in the 1979 tax act that resulted in the Supreme Court decision in Reedy Creek. He acknowledged the Commission in those 30 year old tax cases considered the utilities'

earnings in its disposition of tax benefits. (TR 315) However, he testified that, in current tax cases implementing the 2017 Tax Act, other electric and gas utilities have agreed to either refund the savings from the TCJA or apply the savings in some manner to reflect a benefit to their customers. (TR 317-318) He further testified that it varied from company to company as to exactly how it was applied, yet each company agreed that the savings needed to be returned to customers or applied in manner to benefit customers. (TR 318) In other words, the tax benefits resulting from the lowering of the tax rates should be flowed back to the customers who paid the taxes in rates and not result in some type of windfall to the utility.

Notwithstanding FPUC's proposal to keep the tax benefits, these tax savings should be flowed back to the customers. This money belongs to the Company's customers and should be returned to them. Thus, the base rate TCJA savings should be applied as a permanent base rate reduction. (TR 241)

ISSUE 24: Should this docket be closed?

OPC: No.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Citizens' Post-Hearing Brief has been furnished by electronic mail on this 28th day of December, 2018, to the following:

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