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August 13, 2026

**VIA E-PORTAL**

Mr. Adam Teitzman
Commission Clerk
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

**Re: Docket No. 20260026-GU – Application for Rate Increase by Florida City Gas.**

Dear Mr. Teitzman:

Attached for filing, please find the Rebuttal Testimony of Michael Reno for Florida City Gas.

Thank you for your assistance with this filing. As always, please don't hesitate to let me know if you have any questions whatsoever.

Sincerely,

Beth Keating

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

Docket No. 20260026-GU: Petition for rate increase by Florida City Gas

Prepared Rebuttal Testimony of Michael Reno

Date of Filing: August 13, 2026

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## I. Introduction

**Q. Please state your name, occupation and business address.**

A. My name is Michael Reno. I am a managing director in Ernst & Young LLP's National Energy Practice. My business address is 11011 New York Avenue, NW, Washington, District of Columbia, 20005-4213.

**Q. Have you previously testified or presented testimony before the Florida Public Service Commission?**

A. Yes, I filed direct and rebuttal testimony on behalf of Florida Public Utilities Company (all gas divisions) and the Florida Division of Chesapeake Utilities Corporation, in Docket No. 20220067-GU.

**Q. On whose behalf are you appearing in this proceeding?**

A. I am testifying on behalf of Florida City Gas ("FCG").

**Q. Please describe your educational background and professional experience.**

A. I graduated from Kansas State University in 1987 with a Bachelor of Science degree in Business Administration, with an emphasis in accounting, and a Master's of Science in 1988, with an emphasis in accounting. After completion of my Master's of Science in Accounting, I joined Deloitte Tax LLP, formerly Deloitte Haskins & Sells. In 2012, I joined Ernst & Young LLP as an executive director in the National Energy Practice. I am a Certified Public Accountant, licensed in the District of Columbia and in the Commonwealth of Virginia. I have practiced public accounting for over 32 years. In my practice, I provide tax services to regulated water, electric and gas utilities. I regularly assist clients with tax planning, support and explain tax reporting positions, and perform tax return reviews. My experience includes providing advice on accounting for income taxes and performing tax provision reviews. I also regularly consult with companies regarding tax accounting and its impact on the rate setting process as well as compliance with the normalization rules. Additionally, I am a frequent speaker at industry seminars and conferences on the topic of tax accounting for rate-regulated utilities. I have spoken at the Edison Electric Institute tax committee meetings and the American Gas Association tax committee meetings in addition to other industry meetings.

**Q. What are the purposes of your prepared rebuttal testimony in this proceeding?**

A. The purpose of my testimony is to rebut various conclusions contained in the direct testimony of OPC's Witness Lane Kollen pertaining to his adjustment to include a "Parent Debt Adjustment", change the interest synchronization adjustment, and his proposal to include a regulatory liability in place of the historic deferred tax liability that was extinguished upon Chesapeake Utilities Corporation's purchase of FCG.

**Q. How will you refer to these entities in your testimony?**

A. When referring to Florida City Gas, I will refer to it as "FCG" or "the Company." When referring to Chesapeake Utilities Corporation, the parent company, I will refer to it as "CUC."

**Q. Are you providing any exhibits with your rebuttal testimony?**

A. No.

## II. Purpose and Summary of Testimony

**Q. What is the purpose of your rebuttal testimony?**

A. I will explain why Mr. Kollen's recommendation for an adjustment for parent company debt is unnecessary and why his recommendation for the establishment of a regulatory liability in lieu of the pre-acquisition ADIT is inappropriate.

## III. Parent Debt Adjustment

**Q. Please describe Mr. Kollen's parent debt adjustment recommendation.**

A. In Section IV of his direct testimony, Mr. Kollen argues that if the Commission adopts the Company's allocation of CUC's consolidated capital structure to FCG for the WACC (Weighted Average Cost of Capital), then the Commission must also apply the parent debt adjustment under Florida Administrative Code 25-14.004. He argues that the Company cannot "have it both ways" by using the CUC financing for the WACC but treating FCG as if it has no equity investment from CUC for purposes of the parent debt adjustment. The adjustment Mr. Kollen proposes would result in an approximately $1.8 million reduction to income tax expense.

**Q. Do you agree with Mr. Kollen's recommendation?**

A. No. As explained in Noah Russell's direct testimony in Section X, the interest synchronization calculation on MFR Schedule G-3 page 2 already captures the tax benefits of the allocable parent company debt. Applying an additional parent debt adjustment would double-count the same tax benefit.

<u>The Interest Synchronization Calculation Already Reflects the Parent Debt Tax Benefit.</u>

The purpose of Rule 25-14.004 is to capture the income tax benefit associated with parent company debt used to finance a subsidiary's equity investment. As Witness

Russell explained in his direct testimony, FCG has no third-party debt of its own; the debt needed to purchase FCG was obtained at the CUC level. An allocated portion of the parent company debt is included in FCG's capital structure, and the related tax benefit of interest expense associated with the allocable parent company debt is calculated on MFR G-3 page 2 and deducted from income in calculating income tax expense on MFR G-2 page 30. This mechanism achieves the same result that Rule 25-14.004 is designed to achieve, without applying the adjustment twice.

<u>This Methodology Has Precedent and Was Approved in Prior FPUC Rate Cases.</u>

The methodology described above was approved by the Commission in FPUC's 2022 gas rate case (Order No. PSC-2023-0103-FOF-GU in Docket 20220067-GU) and in FPUC's 2024 electric rate case (Order No. PSC-2025-0287-AS-EI in Docket 20240099-EI). Both dockets involve the same intercompany financing structure that Mr. Kollen challenges here.

<u>Mr. Kollen's Argument ignores an important fact in this rate case</u>

Mr. Kollen argues that using CUC's consolidated capital structure for the WACC necessarily triggers a separate parent debt adjustment. This ignores the fact that FCG does not have an interest expense deduction recorded in its tax return because it does not hold third party debt. The Company's methodology adjusts for this fact through its interest synchronization calculation. The WACC allocation reflects CUC's consolidated financing sources, and the interest synchronization calculation captures the associated tax benefits. There is no gap that requires an additional adjustment under Rule 25-14.004.

The Company's methodology already captures the tax benefit of the allocable parent company debt through the interest synchronization calculation, consistent with prior Commission-approved practice for CUC's Florida regulated affiliates.

**IV. <u>Section 338(h)(10) ADIT Treatment</u>**

**Q. Please describe Mr. Kollen's Section 338(h)(10) ADIT recommendation.**

A. In Section III of his direct testimony, Mr. Kollen argues that the joint CUC-FPL Section 338(h)(10) election eliminated the pre-acquisition FCG accumulated deferred income tax ("ADIT") balance of $38.814 million, which he characterizes as customer-paid deferred taxes representing a zero-cost of capital rate in the regulatory capital structure. He recommends that the Commission direct the Company to establish a regulatory liability equivalent to the lost ADIT and include it at zero cost in the WACC. His Table 6 shows this adjustment, reducing the WACC from 6.69% to 6.32%. In addition, Mr. Kollen states that a normalization violation can be avoided by simply substituting a regulatory liability in place of the ADIT that no longer exists.

**Q. What is the practical effect of Mr. Kollen's recommendation?**

**A.** Mr. Kollen's proposal would require the Commission to treat FCG as though approximately $38.814 million of deferred tax liability still exists through the establishment of a regulatory liability, even though that tax liability was eliminated as part of the transaction. His proposal therefore creates a hypothetical source of zero-cost capital that is not reflected on FCG's books, does not represent an actual tax obligation (it was an obligation of the prior owner), and it does not correspond to deferred taxes that FCG will be required to pay in the future

**Q. Do you agree with Mr. Kollen's recommendation?**

A. No. The IRS has consistently stated that you cannot include an ADIT where one does exist in reality. The tax associated with those temporary differences was recognized and resolved through the transaction. Because those deferred taxes are no longer deferred and were extinguished at the time of the transaction, there is no remaining deferred tax balance available to include as zero-cost capital in rates.

As Mr. Kollen has stated, Section 338(h)(10) election results in the elimination of the pre-acquisition FCG ADIT as a result of the prior owner paying that tax.

Therefore, it is inappropriate to include such ADIT in the calculation of rates or to establish this as an ongoing tax obligation (or regulatory liability as discussed below). CUC did not get, nor will it get in the future, any tax benefit associated with the legacy FCG ADIT balance in question. Further, CUC will not be required to pay any taxes associated with this balance in the future.

**Q. Do you agree Mr. Kollen's recommendation of inclusion of regulatory liability as a replacement for the extinguished ADIT?**

A. No. The inclusion of a regulatory liability in lieu of the extinguished ADIT would result in an indirect violation of the normalization rules. Replacing extinguished ADIT with a regulatory liability would recreate the same ratemaking effect through a different accounting label. The elimination of the deferred tax liability does not authorize regulators to recreate the ratemaking effect of that liability through another mechanism. Customers would receive a future benefit for which CUC and FCG do not have a corresponding income tax benefit. Mr. Kollen's proposal would create a liability that does not represent an actual deferred tax obligation and for which FCG has no obligation to pay in the future. The inclusion of the proposed regulatory liability would have a detrimental effect on customers in the future as a result of the normalization violation penalties.

**Q. What is an indirect violation of the normalization rules?**

A. The general premise is that you cannot do indirectly that which is prohibited to do directly. Section 168(i)(9)(A) of the Internal Revenue Code sets out the direct normalization rules (use the same method, maintain the deferred tax reserve). Section 168(i)(9)(B) then extends those rules to cover indirect circumventions by capturing any "procedure or adjustment" that produces results inconsistent with subparagraph (A), even if the taxpayer has not explicitly flowed through the tax benefit. The phrase "one way in which the requirements of subparagraph (A) are not met" makes clear that a violation can occur not only through a direct deviation from the method/period requirements, but also through any ratemaking procedure or adjustment that achieves the same effect indirectly. Under the regulations, Treas. Reg. §1.167(l)-1(h) provides the computational rules for the deferred tax reserve account. While this regulation does not use the exact phrase "shall not be accomplished indirectly," it operates functionally the same way: the IRS examines whether the result of the ratemaking methodology is consistent with normalization, regardless of the mechanism used. If the methodology produces numbers that do not reflect the proper deferral, it is a violation, whether "direct" or "indirect." Section 1.46-6(b)(4) makes clear that cost of service or rate base is considered to have been reduced by reason of all or a portion of a credit if such reduction is done in an indirect manner. Section 1.46-6(b)(4)(iii) provides that a type of indirect reduction is any ratemaking decision intended to achieve an effect similar to a direct reduction to cost of service or rate base. In determining whether a ratemaking decision is intended to achieve this effect, consideration is given to all the relevant facts and circumstances, including the record of the proceeding, the regulatory body's orders, and the anticipated effect of the ratemaking decision on the cost of service or rate base. In IRS Chief Council Advice, CCA 200641005, the IRS states "Moreover, it is a violation of §203(e) of the Act for taxpayers to adopt any accounting treatment that, directly or indirectly, circumvents the rule set forth in the previous sentence".

**Q. What are the consequences of a normalization violation?**

A. If the utility fails to use the normalization method of accounting, the utility may not claim accelerated depreciation on any of its public utility property. Congress intentionally made the consequences of a normalization violation severe to both the utility and the ratepayers to deter regulators from attempting to flow through the benefit of accelerated depreciation to ratepayers. If a utility commits a normalization violation, the utility must revert to the same method of depreciation it uses to prepare its regulated books of account from the date of the violation until the utility remedies the violation. The effect of reverting to book depreciation is that the income tax expense in a utility's rates will equal the utility's actual income tax. Therefore, no amount of income tax is treated as ratepayer-funded capital and there is no zero-cost capital included for deferred tax liabilities. Simply stated, the WACC would be higher and detrimental to customers.

**Q. What should the Commission conclude regarding Mr. Kollen's proposed regulatory liability?**

A. The Commission should reject it. Mr. Kollen's proposal asks the Commission to provide customers with the benefit of approximately $38.814 million of deferred taxes that no longer exist. The deferred tax liability was extinguished at the time of the transaction. Neither the actual post-acquisition tax position nor sound normalization principles support including a hypothetical deferred tax balance in FCG's regulatory capital structure. Recharacterizing the amount as a regulatory liability does not cure that defect. It seeks to circumvent accounting and regulatory practices and regulations to accomplish the establishment of an extinguished liability, resulting in a normalization violation.

**Q. Does this conclude your rebuttal testimony?**

A. Yes.

Docket No. 20260026-GU

## CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Rebuttal Testimony of Michael Reno has been furnished by Electronic Mail and/or Electronic Data Room access to the following parties of record this 13th day of August, 2026:

| | |
|---|---|
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