Q. Please state your name and business address.

A. My name is James A. Rizzo. My business address is 6363 Main Street, Williamsville, New York 14221-5887.

Q. By whom are you employed and in what capacity?

A. I am employed by National Fuel Gas Distribution Corporation ("Distribution" or the "Company") as Assistant Vice President in the Tax Department.

Q. Have you previously provided testimony in this case?

A. Yes. I provided Direct Testimony, Exhibits and workpapers regarding the Company's Property Taxes and Income Taxes.

Q. What is the purpose of your Rebuttal Testimony?

A. The purpose of the testimony is to respond to the testimony of Staff witness Richard Davi concerning Property Taxes and Income Taxes and discuss discrepancies noted in the Staff Accounting Panel's calculation of Income Taxes in Staff Exhibit_(SAP-1), Schedule 3 of 10.

PROPERTY TAXES

Q. Do you agree with witness Davi's testimony regarding the use of a zero percent growth rate for projecting property taxes in the rate year?

A. No. I do not agree with this arbitrary approach, which was based upon an analysis of the three-year average changes in property taxes.

Q. Why is using an approach that is based on a three-year average inappropriate?

A. The use of the three-year average is inappropriate because it is not a valid proxy for real property tax expense going forward. Witness Davi's testimony indicates that the three-year average produces a negative growth rate of 0.29 percent, an amount which he recognizes is unsustainable. However, witness Davi then decides to arbitrarily propose a growth rate of zero percent. I agree that the negative growth rate experienced in the three-year period is not a proper yardstick for measuring future property tax expense in this rate case, but neither is a zero percent growth factor sustainable, or appropriate.

Q. Please explain.

A. In recent years, the Company has received increasing functional obsolescence awards which led to lower assessed values and property taxes. However, the amount of the awards has levelled off over the past few years and is expected to decline in the future as a result of the Company's Leak Prone Pipe Program (discussed later), and other pipeline projects. As the functional obsolescence awards decline, additional capital expenditures will lead to increased property tax expense given that the property tax increase associated with the Company's plant additions will no longer be offset by increasing functional obsolescence awards.

Q. Why is it inappropriate to apply a zero percent growth rate to project the future property taxes to be paid?

A. As explained in my Direct Testimony, actual property taxes paid in the historic test year were adjusted by the Company's inflation factor plus an estimated change in the overall assessments. The use of inflation for forecasting property tax expense provides a reasonable, sustainable estimate for the rate year therefore, as provided in my Direct Testimony, I propose that an inflation factor be applied to property taxes due to an inevitable increase in tax expense.

Q. In addition to an inflation factor, are there other adjustments that should be made to property taxes in the Rate Year?

A. Yes. In addition to tax rates, changes in assessments affect property taxes. The Company has reflected an estimate of change in overall assessment value in its projection.

Q. Please explain.

A. As part of the Company's overall capital expenditures program, the Company has implemented programs that will directly result in an increase in property taxes in the future.

Q. What Company programs would increase property taxes in the future?

A. The Company's Leak Prone Pipe (LPP) Replacement Program (as noted in the Direct Testimony of Kevin D. House) would have an obvious impact on future property tax expenses. As older gas pipelines are replaced with newer and more appropriately-sized pipe, the Company's functional obsolescence award will necessarily decrease. This will result in increased assessed values and increased property taxes. Also, the replacement pipelines will have a higher assessed value (and higher property taxes) as a result of having less accumulated depreciation than the older pipelines.

The Gas Network Enhancement Pilot Program (as noted in the Direct Testimony of the Energy Services Panel) will also lead to increased property taxes as new pipelines are added to the Company's gas network.

ACCUMULATED DEFERRED INCOME TAXES

Q. What is the "proration" methodology as it relates to the calculation of accumulated deferred income taxes (ADIT) in this rate filing?

A. The proration methodology is a specific method promulgated by the IRS for calculating ADIT for any rate filing that includes a future test period. For purposes of proration, a future test period is any period after the date on which new rates are scheduled to go into effect. In the current rate filing, the future test year (or future "rate year") is the 12-months ending March 2018, with new rates scheduled to go into effect on or about April 1, 2017.

Q. Where is the proration methodology described by the IRS?

A. It is explained in Reg. 1.167(l)-1(h)(6)(ii). It is also discussed in recent IRS private letter rulings (PLRs), including PLR 201541010 and PLR 201531010.

Q. Why is use of the proration methodology important?

A. The Company must use the proration methodology in order to comply with the normalization requirements of the Internal Revenue

Code. Compliance with the normalization rules is necessary in order for a company to claim accelerated depreciation for tax filing purposes. Accelerated tax depreciation, versus straight-line depreciation, provides a cash-flow benefit for a company. Ratepayers benefit from this via a rate base reduction for the ADIT.

Q. Please explain the mechanics of the proration methodology.

A. The methodology is designed to account for the period of time the Company has received the ADIT, and provide the appropriate limit on the amount of ADIT that can be excluded from rate base as determined by the IRS. Under the proration methodology the pro-rata amount of any increase in ADIT during the future rate year is determined by multiplying the increase by a fraction, the numerator being the number of days remaining in the future period at the time of the increase (in our case, increases are projected on a monthly basis), and the denominator being the total number of days in the future period (in our case, 365). Using the required proration methodology, the Company calculated the final ADIT balance in its current rate filing as follows: The starting point is the projected ADIT balance at April 1, 2017, the beginning of the future rate year.

Next, the deferred tax increase projected for April 2017 is multiplied by 335/365 and added to the previous balance; then the deferred tax increase projected for May 2017 is multiplied by 304/365 and added to the balance; and so forth through March 2018, the end of the future rate year. Finally, consistent with the determination of rate base for the future rate year, the beginning and ending balances of ADIT for the future rate year are averaged to arrive at the final ADIT balance. Please refer to Exhibit ___ (JAR-3) Schedule 1, Page 2 of 2 for the calculation.

Q. Why must the proration methodology be used in this rate filing?

A. The use of the proration methodology is REQUIRED in a rate filing such as this one, which includes a future test period, to enable the Company to comply with the normalization requirements and claim accelerated depreciation for tax filing purposes. As noted earlier in this testimony, the Company receives a cash-flow benefit from accelerated tax depreciation (via a reduction in current income taxes payable) and ratepayers receive a benefit as a result of the reduction in rate base related to the ADIT. Although witness Davi's testimony indicates that he believes his methodology approximates the results of using proration, his method is, in fact, not consistent with the proration methodology. In verifying witness Davi's calculation, using Staff's proposed adjustments for capital expenditures and uncollectible expense, the ADIT balance using the proration methodology is calculated to be $247,738 as opposed to $250,021 calculated using witness Davi's approach. See Exhibit_(JAR-3) Schedule 2, Page 1 of 1. The use of witness Davi's estimation would result in a violation of the normalization requirements noted above and would prohibit the Company from claiming accelerated depreciation (including bonus depreciation), which would have adverse consequences for ratepayers. Therefore, it is essential that the proration methodology be followed properly in this case. The Company will update the ADIT calculation under the proration methodology through the Brief on Exceptions phase of this proceeding.

<u>NYS Tax Rate Change</u>

Q. Do you agree with Staff's proposal to pass back excess ADSIT to ratepayers over a three-year period?

A. Yes, provided that the Company would receive consistent deferral treatment if tax rates were to increase. As previously mentioned in DPS-39, the Company estimated the excess ADSIT amount for purposes of this rate case. The amount should be finalized after the year end closing of the accounting records. The Company is requesting deferral treatment for any difference between the estimated amount reflected in the final revenue requirement and the actual amount. Any under/over recovery would be recovered from or returned to ratepayers as appropriate in a future rate case. In addition, any future state tax rate increases would be deferred and recovered from ratepayers in a future rate case.

Q. Please explain any discrepancies in Staff Exhibit_(SAP-1), Schedule 3 of 10.

A. Staff Accounting Panel's proposed adjustments were not properly reflected in the current and deferred tax calculation included in Staff Exhibit_(SAP-1), Schedule 3 of 10. Specifically, Staff's proposed adjustments for depreciation expense and uncollectibles expense should be included in this calculation as these changes impact the calculation of federal and state taxable income.

Q. Does this conclude your Rebuttal Testimony?

A. Yes, at this time.