BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF NEW YORK

CASE 17-M-0815-Proceeding on Motion of the Commission on Changes in Law that May Affect Rates.

COMMENTS OF THE MUNICIPAL COALITION

(Towns of Clarkstown, Haverstraw, Orangetown, Ramapo and Stony Point and the Rockland County Solid Waste Management Authority)

June 27, 2018

Joel R. Dichter
Dichter Law LLC
118 North Bedford Road
Suite 300
Mount Kisco, NY
11549
(212) 593-4202
(212) 994-5394(fax)
dichter@dichterlaw.com
Attorneys for the Municipal Coalition

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 17-M-0815-Proceeding on Motion of the Commission on Changes in Law that May Affect Rates

Comments of the Municipal Coalition

1. Introduction:

These comments are submitted on behalf of the Towns of Clarkstown, Haverstraw, Orangetown, Ramapo and Stony Point and the Rockland County Solid Waste Management Authority (collectively referred to as the "Municipal Coalition"). The Municipal Coalition routinely intervenes in Orange & Rockland Utilities, Inc. and Suez Water New York rate proceedings before the Commission.

The Federal Tax Cuts and Jobs Act of 2017 ("TCJA"), signed into law on December 22, 2017, reduced the federal corporate income tax rate from 35 percent to 21 percent effective for tax years beginning after December 31, 2017. Since utility rates include an allowance for federal income taxes, both current and deferred, rates set prior to December 31, 2017 that included an allowance for federal income taxes at 35 percent are now significantly excessive to compensate the utility for its tax expense.

Also, the TCJA no longer allows public utilities to claim a bonus depreciation tax deduction on their tax return. Immediately prior to the TCJA, utilities were allowed to expense for tax purposes 50 percent of the cost of eligible investments. That particular tax deduction is no longer available to public utilities under the TCJA.

Finally, for originating tax/book timing differences, utilities have been collecting from ratepayers and deferring on their books deferred taxes at a 35 percent tax rate, based on the assumption that when the timing differences reverse taxes will be owed to the U.S. Treasury at a

35 percent rate. That is no longer the case, however. Because the tax rate has now been reduced from 35 percent to 21 percent, taxes deferred and accumulated in the deferred tax reserve account are now excessive. They are excessive because any taxes owed in the future when tax/book timing differences reverse will be paid to the U. S. Treasury at the new 21 percent tax rate, rather than the old 35 percent tax rate that was in effect with the tax payments were initially paid by ratepayers. That is, taxes deferred using a 35 percent tax rate will be paid back at a 21 percent rate. Thus, the 14 percent difference represents the excess in the deferred tax reserve or "EDIT".

Other changes in the TCJA may result in minor changes in the determination of taxable income for public utilities. But, the reduction in the corporate income tax rate, the elimination of the bonus depreciation deduction, and the EDIT are the three most significant changes affecting public utilities resulting from the TCJA.

Accordingly, the Commission commenced their proceeding to preserve the funds arising from the reduction in the corporate tax rate. These comments address the methodology for doing so and the timeframe over which funds emanating from the tax reduction that are due ratepayers should be returned.

2. EDIT Classifications:

Not all EDITs are classified and treated the same. Essentially, EDITs can be classified into three categories: 1) property-related protected; 2) property-related non-protected; and 3) non-property, non-protected.

Under the TCJA, normalization requirements apply to accelerated federal tax method and life depreciation tax/book timing differences. For these EDITs, the normalization provision requires that the related EDITs be used to reduce revenue requirements and revenue no sooner than would occur as the book/tax differences reverses. The TCJA requires, in most instances, the EDITs to be returned to ratepayers using the so-called Average Rate Assumption Method

("ARAM") whereby the utility identifies the deferred tax reversal pattern and reverses the EDIT beginning when book depreciation exceeds tax depreciation and the deferred tax turnaround occurs. The EDITs for which the ARAM method is required is what were previously referred to herein as property-related "protected" EDITs, because EDITs in this category are protected by or subject to the ARAM flow-back method.

The property-related, non-protected category of EDITs relate to other property-related tax/book timing differences for which deferred taxes were previously provided but which do not reflect tax method or life depreciation differences. The principal timing difference included in this category usually is the "repair allowance" under which utilities are able to claim a tax-deductible expense allowance for repairs that are otherwise treated as capital costs for financial reporting purposes. Unlike with protected property-related EDITs, the non-protected property-related EDITs are not subject to normalization and the ARAM flow-back method. Rather, the TCJA leaves it to the discretion of the regulatory state commissions, including this Commssion, to choose a reasonable period of time over which to return EDITs to ratepayers.

The third category of EDITs relate to deferred taxes collected for tax/book timing differences that are not related to property. Typical examples in this category include pensions, OPEBs, and regulatory assets. EDITs in this category also are unprotected in that the TCJA did not impose a normalization requirement. Thus, this Commission may direct the return of the EDIT to ratepayers without reference to the ARAM.

3. <u>Non-Protected EDITs are properly amortized over a short amortization period:</u>

As previously stated, amortization under ARAM is required for property-related protected EDITs. In fact, failing to use the ARAM likely will result in the Company being unable to claim accelerated depreciation tax deductions. In contrast, there are no "applicable IRS regulations" relating to unprotected EDITs. The IRS has no preference on how rapidly regulators require unprotected EDITs be returned to utility customers.

EDITs are ratepayer funds that have been collected and held by the utility in order to pay taxes at some point in the future but, because of the reduction in the corporate tax rate, are no longer needed to pay taxes. Thus, at this point in time, ratepayers have become involuntary investors in the public utility. But, unlike other investors, ratepayers are not entitled to dividend payments. The only "compensation" that ratepayers receive on their "investment" is the rate base deduction for the un-refunded EDITs – "paid" at the Company's rate of return. But, with personal credit card interest rates being much higher than the Company's cost of capital, EDIT's are a particularly poor investment vehicle for most ratepayers. Nor are they a voluntary investment on the ratepayers' part. Neither this Commission nor the Public Utility should be conscripting investment capital from ratepayers through EDITs. Rather, this Commission should require public utilities to return EDITs to New York ratepayers rapidly. The appropriate matching is achieved in the ratemaking process when rates are set based on the cost of service. A short amortization for EDITs, will bring rates more closely aligned with costs sooner rather than later.

One agreement for a longer period may be to promote stabilization of rates. But rate stability is not a valid concern in this instance. Ratepayers do not need to be protected from a refund they are due. Nor is it reasonable to string out the EDIT refund for up to 50 plus years to protect customers from unstable rates. There is no consumer protection issue here. Ratepayers can be informed that the refund is limited in time to the amortization period approved by the New York PSC and after that time the refund obligation will be satisfied.

Refunds must be provided sooner rather than later so that those customers that receive the refund more closely match customers that contributed to O&R's EDITs. If one waits the remaining average life of the depreciating assets to fully refund the EDITs, many of the customers that contributed to the EDITS in prior years will no longer be customers of the public utility and will not receive a refund. Avoiding inter-generational inequities requires that EDITs be refunded promptly. The EDITs are ratepayer funds that are no longer needed to pay future tax expenses. As such, it is important that those funds be returned to their rightful owners – the customers – as quickly as possible.

4. Recommended Amortization Period:

As a general rule, the Municipal Coalition recommends that this Commission require the return of unprotected EDITs to customers over a three year period. This is an amortization period frequently adopted by the Commission for deferral costs. The utility expects prompt recovery from ratepayers when it is the Company's costs that are unrecovered. Ratepayers should expect no less when customers are due a refund. A three-year period is also a reasonable anticipation of how long rates are set in the typical rate case settlement. In certain instances, the Commission may wish to adjust the return of the consumer funds to no more than five years to meet the particular facts of specific rate plans. If there is any concern that rates will remain in effect longer than three or five years, then the EDIT amortization credit can be implemented through a negative rate rider that expires at the end of three or five years.

5. Public Utilities supporting a rapid amortization period:

In the neighboring State of New Jersey, New Jersey Natural Gas Company agreed to an immediate refund of all of its unprotected EDITs. Moreover, O&R's affiliate electric utility in New Jersey, Rockland Electric Company, has agreed to refund its unprotected EDITs to New Jersey customers over three years and to refund the 2018 over-collections immediately. Here, in New York, Natural Fuel Gas Distribution has petitioned the Commission to return funds over five years. Similarly, Corning National Gas Company has proposed a five-year refund period for unprotected tax items consistent with prior ratemaking practices. In contrast, in the pending O&R electric case in New York, O&R has proposed returning non-protected funds to ratepayers over 46 years. See the Pre-filed Rebuttal Testimony of David E. Peterson of Chesapeake Regulatory Consultants, on which this filing is derived, recommending a three year in lieu of the 46 years in the O&R electric and gas cases (Cases 18-E-0067 and 18-G-0068) for the reasons stated herein. There is no valid basis to refund non-protected EDITs over the average remaining life of the utilities assets. To do so would put New York rate- payers at a disadvantage

via its neighbors, force ratepayers to invest in the utility and result in an inter-generational mismatch of cost and benefits.

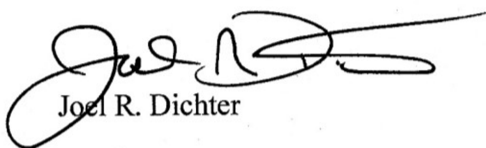
6. <u>2018 Deferrals:</u>

The same reasons for recommending a three amortization for non-protected EDITs apply no less to the 2018 deferred TCJA balance. The one-time 2018 deferred TCJA balances should also be returned to ratepayers over a period of time no greater than three years.

7. <u>Conclusion:</u>

There is simply no valid reason for a general rule that would delay giving customers back their money, arising from the decrease in the corporate tax rate, over an amortization period of any longer than three years. A three year amortization period for the refund of excess deferred taxes will prevent inter-generational inequities, not force customers to become investors in the utility, and is consistent with both the proposals of a number of local utilities and this Commission's typical amortization period for deferrals.

Respectfully Submitted,



Joel R. Dichter

DICHTER LAW LLC
118 North Bedford Road
Suite 300
Mount Kisco, NY
11549
Tel: (212) 593-4202
Fax: (212) 994 5394
Email: Dichter@dichterlaw.com

Attorneys for the Municipal Coalition