

**STATE OF NORTH CAROLINA  
UTILITIES COMMISSION  
RALEIGH**

DOCKET NO. M-100, SUB 148

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
The Federal Tax Cuts and Jobs Act	)	REPLY COMMENTS OF THE
	)	PUBLIC STAFF

NOW COMES THE PUBLIC STAFF – North Carolina Utilities Commission, by and through its Executive Director, Christopher J. Ayers respectfully submits the following reply comments in this docket.

On January 3, 2018, the Commission issued an *Order Ruling That Certain Components of Certain Public Utility Rates Are Provisional as of January 1, 2018, Initiating a Generic Proceeding, and Requesting Comments* requesting that certain utilities, intervenors, and the Public Staff file initial comments in response to the matters set forth in that Order by February 1, 2018, and authorizing the filing of reply comments on or before February 15, 2018. The Order places public utilities subject to the Order (subject utilities) on notice that the Federal corporate income tax expense component of all existing rates and charges will be deemed to be collected on a provisional basis as of January 1, 2018. The Order also provides that it is appropriate to exclude water and wastewater companies with \$250,000 or less in annual operating revenues from the directives of the Order.

In the Order, the Commission specifically directs the subject utilities to provide the following information in their initial comments:

- (1) the estimated annual cost-of-service effect, on an item-by-item basis, of the changes to the levels of income tax expenses expected due to the enactment of the Federal Tax Cuts and Jobs Act. Please show the amount of each change and the related levels of tax expense before and after each change. Such information is to be presented on an NCUC jurisdictional basis (e.g., on a NC retail or NC intrastate basis, as appropriate); and
- (2) a complete detailed narrative explanation of how the Utility proposes to account for and treat excess deferred income taxes that were accrued in earlier years under Federal corporate income tax rates that were in excess of those set forth in the Federal Tax Cuts and Jobs Act.

The Public Staff and the following parties filed initial comments: Carolina Utility Customers Association, Inc. (CUCA), Toccoa Natural Gas Company (Toccoa), North Carolina Justice Center and the North Carolina Housing Coalition (NCJC et al.), Aqua North Carolina, Inc. (Aqua), Carolina Industrial Groups for Fair Utility Rates (CIGFUR), Public Service Company of North Carolina, Inc. (PSNC), Frontier Natural Gas Company (Frontier), the Attorney General's Office (AGO), Carolina Water Service, Inc. of North Carolina (CWSNC), Dominion Energy North Carolina (DENC), Piedmont Natural Gas Company, Inc. (Piedmont). Duke Energy Carolinas, LLC, (DEC) and Duke Energy Progress, LLC, (DEP) filed joint comments.

The following parties were granted permission to intervene, but did not file initial comments: North Carolina Sustainable Energy Association (NCSEA), and Cardinal Pipeline Company, LLC (Cardinal).

On February 9, 2018, Nucor Steel-Hertford (Nucor) filed a petition to intervene out-of-time.

On February 13, 2018, the AGO requested and extension of time to file reply comments. On February 15, 2018, the Commission granted the AGO's request and authorized an extension to Tuesday, February 20, 2018, for all parties to file reply comments.

On February 16, 2018, the Commission granted Nucor's petition to intervene out-of-time.

#### Initial Comments of Toccoa

In its initial comments Toccoa notes that, as a municipally-owned natural gas system, it is not subject to income and other tax obligations. Consequently, no tax allowances were included in the determination of Toccoa's revenue requirement when its rates were established, and no adjustment to its rates are required as a result of the Federal Tax Cut and Jobs Act (the Act).

For the reasons set forth in the comments of Toccoa, the Public Staff agrees that no adjustment should be made to Toccoa's rates in response to the tax reduction in the Act.

#### Initial Comments of the Other Public Utilities

DENC provides the estimated cost-of-service effect of the changes to the income tax expenses as a result of the Act as requested by the Commission. In addition to showing the effects of the reduction in the corporate income tax rate, DENC presents the impact on federal income tax expenses of the repeal of the

Section 199 Domestic Production Activities Deduction<sup>1</sup>. DENC also states that it proposes to address its base non-fuel rates and excess deferred income taxes (EDIT) in its next general rate case. DENC proposes to address changes in the rates for its riders (fuel, REPS, and DSM/EE) in the appropriate rider proceedings.

The joint preliminary comments filed by DEP and DEC provide an overview of the key provisions in the Act that will impact utilities. The Companies claim that the Act could result in a cash flow shortfall and, therefore, compel the Companies to rely on third-party capital. The Companies provide the estimated cost of service effect of the Act. DEP and DEC acknowledge that both Companies have pending rate cases before the Commission and suggest the Commission should use the reduction in the Federal income tax expenses to offset a portion of the rate increases requested in the respective rate cases. DEC proposes addressing the impacts of the Act in its pending rate case. DEP proposes handling the impact of the Act in a future rate case since the record is closed in its pending rate case. Both DEP and DEC propose to address changes in the rates for their riders (fuel, REPS, and DSM/EE) in the appropriate rider proceedings.

Piedmont makes very similar arguments to those made by DEP and DEC in their joint comments. Piedmont provides an overview of the tax changes from the Act that will impact regulated natural gas utilities, and also claims that immediate flow-through of tax reductions could force it to rely on third-party capital. Piedmont provides its cost of service effect of the Act, proposes to change its base

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<sup>1</sup> The Section 199 Domestic Production Activities Deduction is also commonly referred to as the manufacturing deduction.

rates in its next general rate case, which it intends to file in the next 12 to 24 months, and proposes to implement the tax change in its IMR mechanism.

PSNC provides the cost of service effect of the Act and discusses how it would propose to adjust its rates. PSNC also proposes to address the EDIT resulting from the Act in its next general rate case.

Frontier states in its comments that its initial rates were not based on cost of service and that it has never undergone a general rate case proceeding. Frontier also points out that it was not subject to the flow back of reductions to the State corporate income tax rate in Docket No. M-100, Sub 138.

CWSNC provides calculations for changes in its annual cost of service due to the Act, and states that it will not be able to calculate the exact amount of its EDIT for “at least 60 days” from the date of its filing of initial comments (February 1, 2018). CWSNC also advocates addressing tax changes in a general rate case. CWSNC also points out that Contributions in Aid of Construction (CIAC) are now taxable revenues for water and wastewater utilities.

Aqua requests that changes due to the Act be handled in its next general rate case. On February 5, 2018, Aqua filed notice that it intends to file a general rate case in Docket No. W-218, Sub 497.

Entities other than public utilities intervened in the docket and provided initial comments. CUCA, CIGFUR, NCJC et al., and the AGO all propose that the savings from reductions in the corporate income tax rate resulting from the Act should be passed along to ratepayers as soon as practicable. In addition, CIGFUR

recommends that all subject utilities begin filing quarterly reports, no later than April 30, 2018, on the status of their deferral accounts established by the Order. NCJC et al. recommend that some of the reductions from the tax savings be used to reduce residential customer bills, and that the Commission possibly direct portions of the savings to energy efficiency programs and reductions in the fixed portion of residential rates, as opposed to the volumetric charge.

Based on its review of the Act and the initial comments of the other parties, the Public Staff respectfully submits the following reply comments in this docket:

1. The Public Staff recommends that the Commission seek to resolve issues raised in this docket in any pending general rate cases for the utilities subject to the provisions of this docket (the subject utilities). Currently, DEC has a pending rate case in Docket No. E-7, Sub 1146. The Public Staff recommends that the issues raised in this docket be addressed in that general rate case.

2. The Public Staff does not oppose Aqua's request to resolve the issues raised in this docket related to the income tax changes resulting from the Act in the general rate proceeding it intends to file, provided Aqua files a general rate case on or before April 1, 2018.

3. The Commission has dealt with similar issues in two prior Commission proceedings in Dockets Nos. M-100, Sub 113, and M-100, Sub 138. In Docket No. M-100, Sub 113, the Commission addressed tax reductions from the Federal Tax Reform Act of 1986 (TRA86). Among other things, TRA86 reduced the top corporate tax rate from 46% to 34%. In Docket No. M-100, Sub 148, the

Commission addressed the tax reductions from the State House Bill 998 (S.L. 2013-316), which, among other things, changed the net income tax imposed on C Corporations and amended the gross receipts and franchise taxes.

4. The Public Staff recommends that the Commission direct the subject utilities to reduce their rates to reflect any and all cost savings resulting from the reduction in the federal income tax expense component of the cost of providing utility service as soon as practicable. The rates for riders should also be reduced in each subject utility's respective annual rider filings to reflect the reduction in the federal income tax expense.

5. The Public Staff recommends that the Commission direct the subject utilities to refund the amount collected in the deferred account established by the Commission in this Docket that represents the difference in between revenues billed under the prior Federal income tax rate and the Federal income tax rate resulting from the Act starting January 1, 2018.

6. As in Docket No. M-100, Sub 113, the excess amount of the accumulated deferred income tax balances (EDIT) that are due to the decrease in the corporate income tax in the Act should be flowed back to the ratepayers. The treatment of EDIT in those dockets should provide a framework for the treatment of EDIT created by the Act.

7. The Act provides that certain EDIT should be flowed back to the ratepayers subject to certain limitations. The EDIT subject to these limitations is generally referred to as the "protected EDIT." The EDIT that is not subject to

limitations in the timing of flow back is generally referred to as the “unprotected EDIT.”

8. The protected EDIT should be flowed back as soon as practicable in accordance with Federal tax normalization rules. Compliance with Federal tax normalization rules slows the return of the protected EDIT to ratepayers as compared to what regulators might otherwise desire. The Public Staff does not recommend delaying the return of the protected EDIT or in any way further slowing the return of the protected EDIT to ratepayers, other than the delay required under Federal law.

9. The flow back of the unprotected EDIT should be addressed in the next general rate case filed by the subject utilities, except for those with currently pending general rate cases, as noted above.

10. Arguments raised by the subject utilities related to cost of capital and cash flow should not be addressed in this docket. Absent compelling evidence of financial harm to the utilities, the ratepayers should receive the benefit of the tax reductions from the Act as soon as possible. Cost of capital is appropriately addressed in a general rate case. If a subject utility believes its cost of capital has changed and earnings are insufficient to achieve the new cost of capital, it should file for a general rate case to address this issue.

11. The Act changes the taxable treatment of CIAC for water and wastewater companies. This could have a significant impact on water and wastewater companies in that contributed plant is a significant portion of the plant



additions by these companies. The Public Staff recommends that the Commission open a new docket to address the implications of the inclusion of CIAC in taxable income for water and wastewater companies. The Public Staff further recommends that the treatment of CIAC should follow the precedent established in Docket No. M-100, Sub 113, and that water and wastewater companies should seek to collect the income tax on CIAC from the contributor using the full gross-up method. Individual companies seeking to use the present value method could do so with prior approval of the Commission. In opening a new docket, the Commission may provide notice of this change to all water and wastewater companies, not just the utilities subject to this docket, and direct those companies to seek to collect the income tax on CIAC from contributors of plant for new contributions contracted for on or after the date of the opening of that new docket.

12. Frontier asserts that its rates are not based on cost of service, and therefore, it should not be subject to this docket. Frontier has been collecting funds from its ratepayers in order to pay Frontier's Federal income tax obligations. The Act reduces the Federal tax obligations of Frontier and its ratepayers should benefit from the reduction in the federal corporate income tax resulting from the Act. Accordingly, the Public Staff recommends that Frontier be subject to the provisions of this docket.

13. To implement the above recommendations, the Public Staff requests that the Commission direct the subject utilities to file with the Commission and the Public Staff rate reductions to address the changes raised in paragraphs 4 and 7 above by March 30, 2018. The subject utilities should also file workpapers with the

Commission and the Public Staff to support the rate reduction calculations. Once rates are established, the subject utilities should continue to file quarterly reports on the status of their EDIT deferred account, and the deferral account established under this Docket that represents the difference between revenues billed under the prior Federal income tax rate and the Federal income tax rate resulting from the Act starting January 1, 2018.

The Public Staff respectfully requests that the Commission consider the foregoing comments in its deliberations in this docket.

This the 20<sup>th</sup> day of February, 2018.

PUBLIC STAFF  
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**CERTIFICATE OF SERVICE**

I certify that a copy of these Comments has been served on all parties of record or their attorneys, or both, by United States mail, first class or better; by hand delivery; or by means of facsimile or electronic delivery upon agreement of the receiving party.

This the 20<sup>th</sup> day of February, 2018.

Electronically submitted  
s/ Heather D. Fennell