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February 1, 2018

VIA Electronic Filing

Ms. M. Lynn Jarvis, Chief Clerk
North Carolina Utilities Commission
Dobb Building
430 North Salisbury Street
Raleigh, North Carolina 27603

**RE: Docket No. M-100, Sub 148
Dominion Energy North Carolina's Initial Comments**

Dear Ms. Jarvis:

On behalf of Virginia Electric and Power Company, d/b/a Dominion Energy North Carolina, enclosed for filing are Dominion Energy North Carolina's Initial Comments.

Please feel free to contact me with any questions. Thank you for your assistance in this matter.

Very truly yours,

/s/E. Brett Breitschwerdt

EBB:kma

Enclosure

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Feb 01 2018

**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)	INITIAL COMMENTS OF
)	DOMINION ENERGY
)	NORTH CAROLINA
)	

Virginia Electric and Power Company d/b/a Dominion Energy North Carolina (“Dominion Energy North Carolina” or “the Company”), by counsel, hereby submits its initial comments in response to the North Carolina Utilities Commission’s (“Commission”) *Order Ruling that Certain Components of Public Utility Rates are Provisional as of January 1, 2018, Initiating a Generic Proceeding, and Requesting Comments* (“the Order”), issued in this docket on January 3, 2018.

DOMINION ENERGY NORTH CAROLINA’S COMMENTS

The Order requests that Dominion Energy North Carolina, other North Carolina utilities (collectively, “the Utilities”), Public Staff-North Carolina Utilities Commission (“Public Staff”), and other interested parties comment on the changes to Federal tax law, enacted in the Tax Cuts and Jobs Act (“Federal Tax Cuts and Jobs Act” or the “Act”), which was signed into law on December 22, 2017. Among other modifications to the Internal Revenue Code (“IRC”), such as repealing the deduction for income attributable to domestic production activities and modifying the cost recovery rules for property, the Federal Tax Cuts and Jobs Act reduces the Federal corporate income tax rate from 35% to 21%, effective for taxable years beginning after December 31, 2017.

Through the Order, the Commission directed that, effective January 1, 2018, the Federal corporate income tax component of the Utilities' existing rates and charges be billed and collected on a provisional basis pending final disposition of this matter, with accompanying deferred accounting for any rate reduction. The Order further directed Dominion Energy North Carolina and the other Utilities to respond to two requests for information ("RFI") addressing: i) the Act's impact on the Utilities' annual cost-of-service, and ii) the Utilities' proposed accounting treatment for excess deferred federal income taxes ("EDFIT") arising from the Act. The Company's Initial Comments first respond to the Commission's RFIs and then briefly address the Company's plans to address the cost of service and EDFIT impacts of the Federal Tax Cuts and Jobs Act through future ratemaking proceedings.

I. Response to Commission RFIs

Commission RFI No. (1): Estimated Annual Cost-of-Service Effect of Tax Changes

The Order's RFI No. (1) requests the Utilities provide:

(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)

Response:

Attachment 1 presents the impact of the Federal Tax Cuts and Jobs Act on Dominion Energy North Carolina's base non-fuel cost of service, addressing: i) the reduction of the federal corporate income tax rate from 35% to 21%, and ii) the repeal of

the Section 199 Domestic Production Activities Deduction.¹ Column (1) of Attachment 1 presents the levels of operating revenues, expenses, and income approved in the *2016 Base Rate Case Order*.² Column (2) presents the computed impact on federal income tax expense from lowering the federal corporate income tax rate embedded in the retention factor from 35% to 21%. Column (3) shows the base non-fuel cost of service adjusted for this calculated impact. Column (4) presents the impact on federal income tax expense from repealing the Section 199 Domestic Production Activities Deduction. Removing this federal tax deduction increases income tax expense by \$0.7 million. Column (5) shows the net impact on operating expenses and income from these two tax changes. Overall, annual North Carolina jurisdictional income tax expense is expected to decrease by approximately \$10.8 million with a corresponding increase to operating income of the same amount beginning January 1, 2018.

As explained in the Company's response to RFI No. 2 below, the Company reduced the balance of accumulated deferred federal income taxes ("ADFIT") in its financial records to reflect an estimated amount of EDFIT for the Virginia Electric and Power Company system effective December 31, 2017. However, such estimate and the portion allocable to the North Carolina retail operations will be further refined throughout the coming year as a more detailed analysis is completed and needed guidance from the Internal Revenue Service ("IRS") is forthcoming.

¹ Sec. 13305 of the Federal Tax Cuts and Jobs Act repeals the Section 199 Domestic Production Activities Deduction. As of the date of this filing, the Virginia state domestic production activities deduction has not been eliminated. However, the Virginia General Assembly is expected to take action to address Virginia's conformity with the IRC as amended by the Federal Tax Cuts and Jobs Act during the 2018 legislative session.

² See *Order Approving Rate Increase and Cost Deferrals and Revising PJM Regulatory Conditions*, Docket No. E-22, Sub 532 (Dec. 22, 2016) ("*2016 Base Rate Case Order*").

In addition to the Company's base non-fuel rate cost of service addressed in Attachment 1, the Federal Tax Cut and Jobs Act impacts the Company's Rider EDIT, as approved in the *2016 Base Rate Case Order*.³ Rider EDIT is a decrement rider that refunds to customers over a two-year period, commencing on November 1, 2016 through October 31, 2018, a regulatory liability for excess deferred income taxes associated with recent reductions in the North Carolina corporate income tax rate. The regulatory liability approved by the Commission was calculated using a tax gross-up factor that included a 35% federal income tax rate in effect prior to the enactment of the Act. Beginning January 1, 2018, the federal corporate income tax component of the tax gross-up factor will be reduced from 35% to 21% pursuant to the Act. Attachment 2 presents the reduction in the regulatory liability and the associated reduction to the Rider EDIT credit of \$1.4 million for the period January 1, 2018 through October 31, 2018 due to the change in the tax gross-up factor.

Commission RFI No. (2): Narrative Explanation of Proposed Accounting for Excess Deferred Federal Income Tax

The Order's RFI No. (2) requests the Utilities provide:

(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

Response:

In accordance with Generally Accepted Accounting Principles, the Company recorded in its financial records a reduction in the balance of ADFIT effective December 31, 2017, to reflect an estimate of the impact of the Federal Tax Cuts and Jobs Act. The

³ See *2016 Base Rate Case Order*, at 9-10, 148.

reductions in ADFIT associated with the Company's regulated operations and recognized for ratemaking purposes were reclassified to regulatory liability accounts. The predominant amounts of EDFIT established as a regulatory liability are associated with utility property depreciation and related book-tax timing differences, which are subject to the IRC's normalization rules pursuant to new IRC Section 1561(d), which contains similar provisions to the rules promulgated in Section 203(e) of the Tax Reform Act of 1986. *See* 26 U.S. Code § 1561(d). Per Section 13001 of the Federal Tax Cuts and Jobs Act, the Company is required to use the average rate assumption method ("ARAM") for purposes of amortizing EDFIT over the remaining regulatory lives of the property that gave rise to the original reserve for deferred taxes. Amortizing such EDFIT using a methodology other than ARAM would violate the normalization rules and would result in the loss of the use of accelerated depreciation by the Company and a cash penalty equal to the amount by which the excess deferred tax reserve is reduced more rapidly than permitted under the Act. Accordingly, the Company will begin amortizing the estimated plant-related EDFIT for financial accounting purposes effective January 1, 2018 subject to adjustment pending additional guidance from the IRS.

II. Planned Ratemaking in Response to Federal Tax Cuts and Jobs Act

First, as directed by the Order, Dominion Energy North Carolina is now treating the Federal corporate income tax component of its existing approved rates and charges as provisional rates that are subject to deferral accounting. This includes the Company's currently-approved and effective base rates (fuel and non-fuel), as well as: i) annual riders for fuel and fuel-related costs, the Company's demand-side management programs and energy efficiency program costs ("DSM/EE"), and Renewable Energy and Energy

Efficiency Portfolio Standard (“REPS”) compliance costs, and ii) Rider EDIT, as discussed above.

For purposes of the Company’s base non-fuel rates and Rider EDIT, the Company intends to address the cost of service impacts and disposition of deferred amounts due to the Federal Tax Cuts and Jobs Act through the Commission’s general ratemaking procedure set forth in N.C.G.S. §§ 62-130 and 62-133. This approach ensures that the Company has sufficient time to comprehensively evaluate the direct and indirect impacts of this complex new Act in determining the Company’s updated cost of service. The differences between rates in effect at January 1, 2018, including provisional components, and revenues that would have been billed incorporating the IRC as now amended by the Federal Tax Cuts and Jobs Act, will be held in a deferred account as previously discussed herein. The Company believes this approach to be reasonable and fair to customers and the Company, as the Company is now collecting these amounts on a provisional basis. Through the Company’s next general rate case, Dominion Energy North Carolina will comprehensively address all impacts from the Federal Tax Cuts and Jobs Act as part of its updated cost of service filed in that proceeding. In sum, North Carolina’s general ratemaking procedures provide the most reasonable and appropriate mechanism to assess the ongoing justness and reasonableness of the Company’s rates, and to affect future rate changes in a manner that ensures both customers and the utility are treated fairly based upon a comprehensive review of increases or decreases in the Company’s total cost of service.

For the Company’s rates and charges with approved deferral accounting and experience modification factors (*i.e.*, fuel factor, DSM/EE and REPS riders), the

Company proposes to defer any differences between rates in effect at January 1, 2018, including any provisional components, and revenues that would have been billed incorporating the IRC as now amended by the Federal Tax Cuts and Jobs Act, through the ordinary deferral accounting process. Any such differences will be addressed in future annual rider proceedings where applicable.

Respectfully submitted, this 1st day of February, 2018.

By: /s/ E. Brett Breitschwerdt

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Dominion Energy North Carolina
Docket No. M-100, Sub 148
Estimated Annual Cost of Service Impact Due to Enactment of Federal Tax Cuts and Jobs Act
February 1, 2018
(Thousands of Dollars)

Attachment 1

Line No.	Item	(1) NC Jurisdictional Cost of Service Approved Rates Docket E-22, Sub 532	(2) Federal Income Tax (FIT) Rate Reduction from 35% to 21%	(3) NC Jurisdictional Cost of Service After FIT Rate Reduction (1) + (2)	(4) Eliminate Sec. 199 Deduction	(5) NC Jurisdictional Cost of Service After Eliminating Sec. 199 Deduction (3) + (4)
1	<u>TOTAL OPERATING REVENUE</u>	375,722		375,722		375,722
2	<u>OPERATING REVENUE DEDUCTIONS</u>					
3	Operation & Maintenance Expense	189,675		189,675		189,675
4	Depreciation & Amortization	60,047		60,047		60,047
5	Income Taxes	33,820	(11,476)	22,344	717	23,061
6	Taxes Other Than Income Taxes	15,233		15,233		15,233
7	(Gain)/Loss on Disposition of Property	309		309		309
8	<u>TOTAL OPERATING REVENUE DEDUCTIONS</u>	299,084	(11,476)	287,608	717	288,325
9	<u>OPERATING INCOME</u>	76,638	11,476	88,114	(717)	87,397
10	LESS: Interest Expense On Customer Deposits	19		19		19
11	Interest On Tax Deficiencies	1		1		1
12	<u>ADJUSTED OPERATING INCOME</u>	76,618	11,476	88,094	(717)	87,377

Notes:

Column 1 - Page 106, 2016 Rate Case Order

Column 2 - Reflects the change in income taxes associated with net income provided on rate base

Column 4 - Fernald Exhibit 1, Schedule 3-1(p) Revised, Column (a), Line 9. As of the date of this filing, the VA state domestic production activities deduction has not been eliminated. However, the VA legislature is expected to take action to address VA's conformity with the IRC during the 2018 legislative session.

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Dominion Energy North Carolina
Docket No. M-100, Sub 148
Change in Rider EDIT Credit - Federal Tax Cuts and Jobs Act
February 1, 2018
(Thousands of Dollars)

Attachment 2
Page 1

Line No.	Description	(1) Rider EDIT Approved in Docket E-22 Sub 532 (35% FIT Rate)	(2) Rider EDIT w/ Federal Tax Reform (21% FIT Rate)
1	NC Retail EDIT Regulatory Liability as of 12/31/2017	\$ (7,407) [Note 1]	\$ (6,094) [Note 2]
2	Levelization Gross-up Factor	<u>93.99234%</u> [Note 3]	<u>93.99234%</u> [Note 3]
3	Levelized Rider EDIT Regulatory Liability [Line 1 / Line 2]	\$ (7,880)	\$ (6,484)
4	1 - Transactional Income Tax Rate	<u>61.1911%</u> [Note 4]	<u>74.3707%</u> [Note 5]
5	Net Operating Income Effect [Line 3 x Line 4]	\$ (4,822)	\$ (4,822)
6	Retention Factor	<u>60.81123%</u> [Note 6]	<u>73.90903%</u> [Note 7]
7	Levelized Rider EDIT Credit - 1/1/2018 - 10/31/2018 [Line 5 / Line 6]	<u>\$ (7,929)</u>	<u>\$ (6,524)</u>
8	Change in Rider EDIT Credit - Federal Tax Cuts and Jobs Act		<u>\$ 1,405</u> [Note 8]

References:

[Note 1]: NC Retail EDIT Regulatory liability per books as of 12/31/2017

[Note 2]: Page 2, Line 5

[Note 3]: EDIT regulatory liability to be amortized / Total levelized EDIT regulatory liability approved in Docket E-22, Sub 532

[Note 4]: 1 - Transactional income tax rate approved in Docket E-22, Sub 532

[Note 5]: 1 - Transactional income tax rate with 21% federal income tax component

[Note 6]: Retention factor approved in Docket E-22, Sub 532

[Note 7]: Retention factor with 21% federal income tax component

[Note 8]: Col. 2, Line 7 - Col. 1, Line 7; Difference in regulatory liability (line 1) deferred to regulatory asset account

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Dominion Energy North Carolina
Docket No. M-100, Sub 148
Change in Rider EDIT Credit - Federal Tax Cuts and Jobs Act
February 1, 2018
(Thousands of Dollars)

Attachment 2
Page 2

Line No.	Description		Amount
1	NC Retail EDIT Regulatory Liability as of 12/31/2017 - 35% FIT Rate in Tax Gross-up	[Note 1]	\$ (7,407)
2	Tax Gross-up Factor from Docket E-22, Sub 532	[Note 2]	<u>61.1911%</u>
3	Excess Deferred NC State Income Taxes	[Line 1 x Line 2]	\$ (4,532)
4	Tax Gross-up Factor with 21% FIT Rate	[Note 3]	<u>74.3707%</u>
5	NC Retail EDIT Regulatory Liability as of 12/31/2017 - 21% FIT Rate in Tax Gross-up	[Line 3 / Line 4]	<u><u>\$ (6,094)</u></u>

References:

[Note 1]: NC Retail EDIT Regulatory liability per books as of 12/31/2017

[Note 2]: 1 - Transactional income tax rate approved in Docket E-22, Sub 532

[Note 3]: 1 - Transactional income tax rate with 21% federal income tax component

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Dominion Energy North Carolina's Initial Comments, filed in Docket No. M-100, Sub 148 was served electronically or via U.S. mail, first-class postage prepaid, upon all parties of record.

This the 1st day of February, 2018.

/s/E. Brett Breitschwerdt

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