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ORIGINAL
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February 19, 1990

Mr. Steve Tribble
Division of Records and Reporting
Florida Public Service Commission
101 East Gaines Street
Tallahassee, FL 32301

Docket No. 891278-PU

Dear Mr. Tribble:

Enclosed for filing please find the original and fifteen (15) copies of Florida Power & Light Company's Posthearing Comments in the above referenced docket.

Respectfully submitted,

Matthew M. Childs, P.A.

MMC/eg

cc: All Parties of Record

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

IN RE: Revision of Rule 25-14.003, F.A.C., Corporate Income tax Expense) Adjustment Rule: Midpoint and Additional Changes	DOCKET NO. 891278-PU FILED: February 19, 1990

POSTHEARING COMMENTS OF FLORIDA POWER & LIGHT COMPANY

Florida Power & Light Company ("FPL"), hereby submits these Posthearing Comments on the proposed amendment to Rule 25-14.003, F.A.C.

INTRODUCTION:

The current "Tax Savings Rule", 25-14.003, F.A.C., has operated for a number of years in connection with the change to the Federal or State corporate income tax rates. As originally envisioned, the Tax Savings Rule was intended to be a calculation of either a tax savings or tax deficiency amount pursuant to a Commission prescribed form. The amount of any tax savings refund or tax deficiency collection was intended to target the midpoint of each utility's last authorized cost of capital. Although actual results of a utility's operations could produce a different result, the amount of the tax savings refund or deficiency collection would not produce resultant

earnings results different than the midpoint of the utility's last authorized rate of return midpoint.

Despite any practical difficulties in actually applying the Tax Savings Rule by the Commission, the intent of the Rule was to achieve evenhanded results, whether income tax rates increased or decreased and to achieve these results outside the controversy and detailed review required in connection with a general base rate proceeding. One extremely important facet of the existing Rule was the implicit but conscious recognition that retrospective adjustment of revenue recovery would be confined to the factor that changed - the federal or state corporate income tax rates.

The prohibition against the one-sided adjustment for factors other than a change in the corporate income tax rate is very important. Not only does this preserve the balance in the rate setting context, it restricts the prohibited retrospective adjustment to rates. It is with this context that FPL offers these comments on the proposed revision to the Tax Savings Rule.

1. <u>The Proposed Use of Zero as the Cost of Investment Tax Credits is Unfair and Would Violate the Internal Revenue Code.</u>

The proposed amendment to Rule 25-14.003 (1)(f) is improper. The very fact that it is being proposed reflects that the "rule" is for Investment Tax Credits ("ITC") to be assigned their appropriate cost in the capital structure. The

mathematical effect of retaining ITC in the capital structure but assigning it zero cost is to artificially and improperly reduce the cost of capital but, only for purposes of applying the Tax Savings Rule. The further mathematical effect of this artificial adjustment is to increase the probability that a tax savings refund will be made when the corporate income tax rate is reduced and to increase the amount of the refund. On the other hand, if the corporate income tax rates were to be increased, then assigning zero cost to ITC would decrease the probability that a tax deficiency collection would be made and decrease the amount of the tax deficiency. Of course, in both instances the results would be completely different from that determined to be appropriate when the utility's rates were set.

Although staff acknowledges that this result - the lack of symmetry was unintended, it is the obvious consequence of the proposal to assign ITC zero cost. Though "unintended" the consequence is arbitrary and unfair.

In addition to being arbitrary and improper as a matter of ratemaking policy, the assignment of zero cost to ITC would not be consistent with Section 46(f)(2) of the Internal Revenue Code and, as a consequence probably would result in the complete loss of ITC. Were this to happen, then each of the affected utilities would lose ITC and the utility and its customers would be faced with the extreme financial burden of replacing the substantial amount of ITC capital with other capital. Mr. Gower

pointed out that the treatment proposed for ITC was inconsistent with the requirements of Section 46(f)(2).

For these reasons, the proposal to assign ITC zero cost under the Tax Savings Rule should be eliminated. However, if the Commission considers it advisable to pursue this revision, FPL urges that an appropriate ruling request to the Internal Revenue Service be pursued first. Although the result would still be arbitrary and unfair, at least the risk of violating the Internal Revenue Code would be eliminated and the substantial adverse consequences of doing so would be eliminated.

2. <u>There Should Be No Revision To The Rule, Directly Or Indirectly, So As To Exclude So - Called "Nonrecurring" Expenses Or To Apply The "O & M Benchmark".</u>

FPL adopts the comments on both of these potential revisions which were contained in the testimony of Mr. Gower. In any event, FPL respectfully submits that these two potential proposals are not before the Commission in this rulemaking proceeding.

On page 10 of the September 25, 1989, Memorandum from the Commission Staff in Docket No. 861190-PU, involving a proposed amendment of Rule 25-14.003, F.A.C., the Commission Staff addressed whether the Tax Savings Rule should be clarified to indicate that both the tax change calculation and the earnings levels will be tested and varified. Thereafter, in the Staff "DISCUSSION" was a comment to the effect that elements included

in the tax savings calculation must be "recurring, and must occur within the year in question." This observation is completely inconsistent with the Tax Savings Rule as it currently exists. Moreover, there is no notice or discussion of this potential construction of even the proposed revisions to the Tax Savings Rule which would support the addition of this qualification to any tax savings refund or tax deficiency collection proceeding. In addition, it appears that a further revision to the Tax Savings Rule is sought to be accomplished through the revision of the reporting form. Although FPL is not aware of any formal revision to the reporting form approved by the Commission, Attachment D to the same September 25, 1989, Staff Memorandum previously referred to contains a footnote requesting a calculation of the O & M Benchmark. As previously noted, FPL does adopt the subsidy comments of Mr. Gower on this proposal. However, FPL would point out that this proposed reporting form has not been noticed or included as part of the revision to the Tax Savings Rule. Under the Florida Administrative Procedure Act, Section 120.52(16), F.S. the effect of this revision is to propose or adopt a rule. FPL does not believe that it is appropriate as a matter of administrative practice to propose subsidy revisions to Commission rules and procedures which are not noticed. Moreover, FPL submits that this particular proposed revision is inappropriate and should not be adopted.

3. Suggested Rule Improvements

The suggested changes to the rule as discussed by Mr. Gower during the hearing are included in Tampa Electric Company's Post-Hearing Statement as Exhibit 1. The suggested changes he proposes would require rate increases or decreases (rate adjustment) at the time tax rates are changed rather than a retroactive refund or collection. The rate adjustment, if any, would be determined in the same manner as refunds or collections under the current rule, except for the redefinition of midpoint on page 2 of 7 of the suggested rule. The rate adjustment would then be included in base rates permanently after a twelve month period.

Mr. Gower explained that the suggestion would change the rule so that rates and charges to customers could be changed where appropriate, at a date conincident with the change in tax rates, rather than waiting for a year or longer to settle the issue. That would avoid the rather excessive cost of continual annual hearings to apply the rule. He noted it would be necessary to use an historic period to change rate but that this procedure was possible. He pointed out that to avoid the annual filings under the rule between rate cases, those changes to reflect tax rate changes having previously been identified could be rolled into base rates. This revision would get rid of regulatory lag and associated administrative costs, which are

now attendant on the annual filings to calculate the refunds, which have been seen over the last several years. TR.34

Mr. Gower also suggested that the definition of "Midpoint" be the weighted average cost of capital calculated using the average capital structure for the period of time covered by the tax rate change report and based on the midpoint of the return on equity approved by the Commission in the utility's last rate case, the current embedded cost of fixed rate capital, the actual cost of variable cost debt, and the required cost of other sources of capital which were utilized in the utility's last rate case. This suggested change would simplify the rule by not introducing issues as to capital costs and would not introduce additional adjustments that would not be Commission policy in a full revenue requirement proceeding.

The remainder of the suggested changes result from the proposed rate adjustment to reflect tax rate changes. These include: 1) The reporting requirements which would be changed to apply to the most recent reasonable available twelve month period, as approved by the Commission, prior to the effective date of the tax rate change and reflect a proforma adjustment for the tax rate change, as well as specific adjustments to reflect current Commission policy; and 2) the definition of "Associated Revenues" would be changed to specify the tax rate to be used in calculating the revenue expansion factor shall reflect the newly effective tax rate.

WHEREFORE, Florida Power & Light Company hereby submits its Posthearing Comments this 19th day of February, 1990.

Respectfully submitted,

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Attorneys for Florida Power
& Light Company

By: _____
Matthew M. Childs, P. A.

CERTIFICATE OF SERVICE
DOCKET NO. 891278-PU

I HEREBY CERTIFY that a true and correct copy of Florida Power & Light Company's PostHearing Comments in the above referenced docket have been furnished by U. S. Mail and Hand Delivery to the following individuals on the 19th day of February, 1990.

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