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May 31, 2018

E-PORTAL FILING

Ms. Carlotta Stauffer, Clerk
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: Docket No. 20180051 – In re: Consideration of the tax impacts associated with Tax Cuts and Jobs Act of 2017 for Florida Public Utilities Company –Gas.

Attached for filing, please find the Florida Public Utilities Company – Natural Gas (FPUC) Petition for Approval of Tax Benefit Adjustment Amounts and Flow Through Mechanism, along with the direct testimony and exhibits of Michael Cassel, Michael Reno, and Matthew Dewey on behalf of FPUC-Gas.

Thank you for your assistance with this filing. As always, please don't hesitate to let me know if you have any questions whatsoever.

Kind regards,

Beth Keating
Gunster, Yoakley & Stewart, P.A.
215 South Monroe St., Suite 601
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MEK

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Consideration of the tax impacts associated with Tax Cuts and Jobs Act of 2017 for Florida Public Utilities Company - Gas.	DOCKET NO. 20180051-GU FILED: May 31, 2018

PETITION OF FLORIDA PUBLIC UTILITIES COMPANY FOR APPROVAL OF TAX BENEFIT ADJUSTMENT AMOUNTS AND FLOW-THROUGH MECHANISM

Florida Public Utilities Company ("FPUC," "FPUC-Gas" or "Company"), by and through its undersigned counsel, pursuant to Sections 366.04(1) and 366.06(1), Florida Statutes, and consistent with Order No. PSC-2018-0213-PCO-GU, issued in Docket No. 20180051-GU, and Order No. PSC-2018-0104-PCO-PU, issued in Docket No. 20180013-PU, hereby files this Petition asking the Florida Public Service Commission ("FPSC" or "Commission") for approval of FPUC's calculation of tax benefit amounts arising from the Tax Cuts and Jobs Act of 2017, along with the means of flowing that benefit through to FPUC's customers. FPUC also offers a flow-through mechanism, ("Proposal"), for consideration. With this Petition, FPUC is also submitting the Direct Testimony of witnesses Michael Cassel, Matthew Dewey, and Michael Reno on behalf of FPUC, consistent with Order No. PSC- 2018-0213-PCO-GU, issued in this proceeding on April 25, 2018.

In support of this request, the Company hereby states:

1) FPUC is a natural gas utility subject to the Commission's jurisdiction. Its principal business address is:

Florida Public Utilities Company
1750 S 14th Street, Suite 200
Fernandina Beach FL 32034

2) The name and mailing address of the persons authorized to receive notices are:

Beth Keating, Esq.
Gregory Munson, Esq.
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Mike Cassel
Director, Regulatory and Governmental Affairs
Florida Public Utilities Company
1750 S 14th Street, Suite 200
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3) The Company is unaware of any material facts in dispute at this time, but the proceeding may involve disputed issues of material fact. The Company's request set forth herein does not involve reversal or modification of a Commission decision or proposed agency action. The Commission is the affected agency located at 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399.

I. BACKGROUND

4) The Tax Cuts and Jobs Act of 2017[1] ("Act") was signed into law by President Trump on December 22, 2017, and applies to the taxable year beginning after December 31, 2017. Thereafter, the Commission established generic Docket No. 20180013-PU to address the Office of Public Counsel's ("OPC") Petition to Establish Generic Docket to Investigate and Adjust Rates for 2018 Tax Savings. By Order No. PSC-2018-0104-PCO-PU, the Commission asserted jurisdiction over the subject matter of responsive tax

[1] HR-1, Pub. L. No. 115-97, December 22, 2017, 131 Stat 2054.

adjustments effective on the date of the Commission's vote, February 6, 2018 ("Jurisdictional Date").

5) This docket was opened on February 23, 2018, to provide a vehicle for the Commission to consider the tax impacts associated with the passage of the Act on Florida Public Utilities Company - Gas. The Order Establishing Procedure for this proceeding, Order No. PSC-2018-0213-PCO-GU, was issued April 25, 2018. FPUC hereby submits this Petition and the testimonies of its witnesses consistent with the schedule established by the Prehearing Officer.

II. TAX ADJUSTMENT AMOUNTS

6) As explained in greater detail in the testimony of FPUC witness Cassel, the annual tax savings associated with the corporate income tax rate change from 35% to 21% is approximately $2,181,275.

7) As for deferred taxes, which are recorded on the Company's balance sheet as a regulatory liability, the amount on the Company's books was calculated at the prior 35% rate, but the actual taxes paid to the government will be paid at the 21% rate, resulting in a net benefit for customers. For protected deferred taxes, the estimated grossed-up balance for FPUC is approximately $21,799,999, which is recorded as a Deferred Regulatory Tax Liability. This estimated deferred balance will be amortized over 26 years using the Internal Revenue Service's ("IRS") prescribed methodology, which is approximately $838,462 annually.

8) The estimated grossed-up Deferred Regulatory Tax Liability balance related to the Unprotected Deferred Tax consists of two components: 1) the deferred taxes on the acquisition adjustment approved by Order No. PSC-12-0010-PAA-GU; and 2) the deferred taxes on the remaining unamortized balance, excluding the acquisition adjustment portion. In accordance with the amortization requirements of Order No. PSC-12-0010-PAA-GU, the balance of $6,518,569 that pertains to the acquisition adjustment must be deferred and amortized over the same period as the original deferred tax associated with the acquisition adjustment, which amounts to $298,560 annually. The second component of Unprotected Deferred Tax balance in the amount of $2,916,880 is addressed below.

9) There is also a direct impact to the Company's Gas Reliability Infrastructure Program ("GRIP") arising from the 2017 Tax Act. The first component consists of the tax savings on the GRIP surcharge from the Jurisdictional Date through the end of the calendar year. The second component is the impact to the GRIP surcharge for 2019 forward. The tax savings in 2018 will be $1,040,141. For 2019 and beyond, the savings will be approximately $1.2 million.

10) FPUC notes that the tax benefit amounts identified herein, as well as in the testimony of its witnesses, are not considered to be final amounts, but are instead approximates. As noted by Company witness Dewey, the staff of the US Securities and Exchange Commission ("SEC"), recognizing the complexity of reflecting the impacts of the Act, has issued guidance in Staff Accounting Bulletin 118 ("SAB 118"), which clarifies that the required analyses and accounting for income taxes can be completed

within up to one year if information is not yet available or complete. As further explained by witness Dewey, certain information pertaining to FPUC's calculation of the full tax benefits remains to be determined, including the portions of deferred taxes that can be normalized using the IRS' preferred normalization methodology known as "ARAM"; thus, the amounts are currently reflected as approximates and may be revised until December 22, 2018.

III. FLOW-BACK PROPOSAL

11) Except for the GRIP savings shown on Exhibit NGMC-2, FPUC proposes to retain the $2,181,275 annual amount of tax savings associated with the tax rate reduction, for purposes of addressing incremental, ongoing costs since the Company's last rate case in 2008. Currently, the Company is not over-earning and is projected to be earning at the bottom of its allowable range. As such, allowing the Company to retain the tax benefit will provide the Company with a better opportunity to earn within its range and may enable the Company to defer a rate case, thus ensuring extended rate stability.

12) Similarly, FPUC also proposes to amortize the estimated Protected Deferred Tax Liability over 26 years or $838,462 per year, and the second component of the Unprotected Deferred Tax Asset that is not associated with the acquisition adjustment over 10 years at $291,688 per year. The Company further requests that it be allowed to retain this benefit. In light of the Company's earnings posture, as noted above, this amount will provide the Company with further opportunity to earn within its range, while also enabling the Company to extend service at present rates for a longer period.

13) As for the 2018 tax benefit associated with GRIP discussed above, the Company proposes to flow this savings back to customers through the calculation of the 2019 GRIP surcharge. Going forward from 2019, the new tax rate would be incorporated in the calculation of the GRIP surcharge passing an estimated full $1.2 million benefit on to FPUC's customers.

14) If the Commission accepts FPUC's proposal to utilize the retain a portion of the benefits of the Tax Act, while flowing a significant portion of the benefits back to customer through the GRIP surcharge calculation, FPUC's customers would see not only a beneficial impact to the GRIP surcharge, but extended rate stability. The Company would likewise benefit from an improved earnings posture and a healthier fiscal outlook, which ultimately inures to the benefit of FPUC's shareholders and customers alike.

IV. REQUEST FOR RELIEF

15) FPUC asks that the Commission determine that the tax benefits arising from the 2017 Tax Act tax rate reduction, excluding the GRIP 2018 savings based on Exhibit NGMC-2, as well as the estimated Deferred Tax portion of the Protected and the estimated Unprotected Deferred Tax regulatory asset that is not associated with the acquisition adjustment, be retained by the Company, as described herein.

16) FPUC further proposes to pass the tax benefits directly associated with the GRIP program through the calculation of future GRIP surcharges, as described herein.

17) FPUC asks that it be allowed to update the estimated tax benefits to be consistent with any adjustments to those estimates through December 22, 2018.

RESPECTFULLY SUBMITTED this 31st day of May, 2018.

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Attorneys for Florida Public Utilities Company (Gas Division)

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing Petition for Approval of Tax Benefit Adjustment Amounts and Flow Through Mechanism, along with the direct testimony and exhibits of Michael Cassel, Michael Reno, and Matthew Dewey on behalf of FPUC-Natural Gas in the referenced docket have been served by Electronic Mail this 31st day of May, 2018, upon the following:

Suzanne Brownless Florida Public Service Commission 2540 Shumard Oak Boulevard Tallahassee, FL 32399-0850 sbrownle@psc.state.fl.us	J.R. Kelly/E. Sayler/Virginia Ponder Office of Public Counsel c/o The Florida Legislature 111 W. Madison Street, Room 812 Tallahassee, FL 32399-1400 kelly.jr@leg.state.fl.us Sayler.Erik@leg.state.fl.us Ponder.Virginia@leg.state.fl.us

By: ______________________

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Before the Florida Public Service Commission

Docket No. 20180051-GU

In re: Consideration of the tax impacts associated with Tax Cuts and Jobs Act of 2017 for Florida Public Utilities Company

Prepared Direct Testimony of Michael Cassel

Date of Filing: May 31, 2018

Q. Please state your name and business address.

A. My name is Michael Cassel. My business address is 1750 South 14th Street, Suite 200, Fernandina Beach, FL 32034.

Q. By whom are you employed and what is your position?

A. I am employed by Florida Public Utilities Company ("FPUC") as the Director of Regulatory and Governmental Affairs.

Q. Please describe your educational background and professional experience.

A. I received a Bachelor of Science Degree in Accounting from Delaware State University in Dover, Delaware in 1996. I was hired by Chesapeake Utilities Corporation ("CUC") as a Senior Regulatory Analyst in March 2008. As a Senior Regulatory Analyst, I was primarily involved in the areas of gas cost recovery, rate of return analysis, and budgeting for CUC's Delaware and Maryland natural gas distribution companies. In 2010, I moved to Florida in the role of Senior Tax Accountant for CUC's Florida business units. Since that time, I have held various management roles including Manager of the Back Office in 2011, Director of Business

Management in 2012. I am currently the Director of Regulatory and Governmental Affairs for CUC's Florida business units. In this role, my responsibilities include directing the regulatory and governmental affairs for the Company in Florida including regulatory analysis, and reporting and filings before the Florida Public Service Commission ("FPSC") for FPUC, FPUC-Indiantown, FPUC-Fort Meade, Central Florida Gas, and Peninsula Pipeline Company. Prior to joining Chesapeake, I was employed by J.P. Morgan Chase & Company, Inc. from 2006 to 2008 as a Financial Manager in their card finance group. My primary responsibility in this position was the development of client specific financial models and profit loss statements. I was also employed by Computer Sciences Corporation as a Senior Finance Manager from 1999 to 2006. In this position, I was responsible for the financial operation of the company's chemical, oil and natural resources business. This included forecasting, financial close and reporting responsibility, as well as representing Computer Sciences Corporation's financial interests in contract/service negotiations with existing and potential clients. From 1996 to 1999, I was employed by J.P. Morgan, Inc., where I had various accounting/finance responsibilities for the firm's private banking clientele.

Q. Have you ever testified before the FPSC?

A. Yes. I've provided written, pre-filed testimony in a variety of the Company's annual proceedings, including the Fuel and Purchased Power Cost Recovery Clause for our electric division, Docket No. 20160001-EI, and the Gas Reliability Infrastructure Program ("GRIP") Cost Recovery Factors proceeding, Docket No. 20160199-GU for FPUC and our sister company, the Florida Division of Chesapeake Utilities Corporation,. Most recently, I provided written, pre-filed testimony in FPUC's electric Limited Proceeding, Docket No. 20170150-EI.

Q. What is the purpose of your testimony?

A. I will explain and support FPUC's natural gas proposal for disposition of tax benefits related to the Federal Tax Cuts and Jobs Act of 2017 ("2017 Tax Act").

Q. Are you sponsoring any exhibits in this case?

A. Yes. I am sponsoring Exhibits NGMC-1 and NGMC-2, which provide a summary of FPUC's natural gas proposed treatments of the impacts resulting from the 2017 Tax Act.

I. FPUC's PROPOSAL

Q. **Is FPUC subject to a settlement that includes provisions addressing the 2017 Tax Act?**

A. No, FPUC is not subject to any settlement including provisions addressing the 2017 Tax Act. As such, by Order No. PSC-2018-0104-PCO-PU, the Commission asserted jurisdiction over the subject matter of responsive tax adjustments effective on the date of the Commission's vote, February 6, 2018 ("Jurisdictional Date").

Q. **Could you please identify the components of the 2017 Tax Act being addressed by FPUC in this proposal?**

A. The components of the 2017 Tax Act being addressed by FPUC are: 1) the federal rate change from 35% to 21%; 2) the Unprotected Deferred Tax Liability and Tax Asset; and 3) the Protected Deferred Tax Liability.

Q. **What is the impact of the federal income tax rate change from 35% to 21% resulting from the 2017 Tax Act?**

A. For FPUC, the annual tax savings amount associated with the tax rate change, based on the 2018 proforma surveillance report, is estimated to be approximately $2,181,275.

Q. **How does FPUC propose that this amount be addressed?**

A. At present, the Company is not over-earning and is projected to be earning at the bottom of its range for the foreseeable future. As such, the Company should be allowed to retain the annual tax benefit excluding the portion related to the Gas Reliability Infrastructure Program ("GRIP"), for purposes of addressing ongoing, incremental costs that have been incurred since the Company's last base rate increase. This amount is $1,141,134. This will enable the Company to earn within, or near, its allowed range until its next base rate proceeding while continuing to make additional investments in infrastructure. The Company does believe that the tax savings associated with GRIP investments should be returned to customers as discussed in more detail on page seven of my testimony.

Q. What are the different components to the Unprotected Deferred Tax balance and the proposed treatment?

A. FPUC has a regulatory liability and asset recorded on its balance sheet for the Unprotected Deferred Tax at a rate of 35% consistent with the applicable law prior to the 2017 Tax Act. At the implementation of the new tax rate, the Company is only required to pay those taxes out at 21%.

Exhibit NGMC-1 demonstrates the impact of these calculations. There are two distinct components of the Unprotected Deferred Tax balance.

The first component is a deferred tax liability associated with the acquisition adjustment. This grossed up balance is $6,518,569 million and the Company requests that this be included with the net acquisition adjustment and amortized at $298,560 per year based on the remaining amortization months of the acquisition adjustment.

The second component is a net Unprotected Deferred Tax Asset and has an estimated balance of $2,916,880. The Company requests this Deferred Tax Asset be amortized over 10 years at $291,688 per year. This annual amortization detriment could be netted against the annual Protected benefit, as discussed below, and the Company requests that the net of these amounts be retained by the Company.

Q. What is FPUC's proposed resolution for the Protected Deferred Tax savings?

A. FPUC has a regulatory liability recorded on its balance sheet for the Protected Deferred Tax at a rate of 35% consistent with the applicable law prior to the 2017 Tax Act. As a result of the 2017 Tax Act, the Company will only be required to pay those taxes out at 21%. The benefit in the Protected Deferred Tax is recorded on FPUC's balance sheet as a grossed-up Deferred Regulatory Tax Liability currently estimated to be $21,799,999. This deferred balance will be amortized using the Internal Revenue Service ("IRS") prescribed methodology and is estimated to flow back over 26 years at approximately $838,462 per year. Exhibit NGMC-1 provides the calculation of this amount. 2018 Final amounts will not be available until late 2018, as further explained by FPUC's witness Matthew Dewey. FPUC proposes retaining the estimated annual amount of $838,462 less the Unprotected Deferred Tax Amortization, as discussed above, of $291,688 for a net benefit of $546,774. This meets the intended goal of the 2017 Tax Act by allowing the Company to continue making capital investments while potentially delaying the need for a costly rate proceeding.

Q. Is there a direct tax impact to the Company's Gas Reliability Infrastructure Program ("GRIP")?

A. Yes. There are two components of the tax rate change that impact GRIP. The first component is the amount of tax savings on the 2018

GRIP surcharge from the jurisdictional date. The second component is the change in the ongoing GRIP surcharge from 2019 and beyond.

Q. How does FPUC propose treating the tax impact of these two components relative to the GRIP?

A. For the first component, FPUC calculates the 2018 tax savings that will accumulate between the Jurisdictional Date and the date GRIP rates will be changed on customer bills (1/1/2019) to be $1,040,141. Exhibit NGMC-2 demonstrates this calculation. The Company proposes flowing this benefit back to customers by incorporating it as an over-recovery in the 2019 GRIP projection. This will have the effect of lowering customer GRIP surcharges by the amount of the benefit.

The second component is the GRIP surcharge rates for periods 2019 and beyond. The Company proposes, incorporating the new, lower federal tax rate into the 2019 GRIP surcharge projections and future projections, which will reduce the annual GRIP revenue amount by the annual tax savings. This is currently estimated to be approximately $1.2 million.

These two requests will, if approved, directly pass the benefit of the lower tax rate on GRIP related revenues created by the 2017 Tax Act back to FPUC's customers.

Q. Is FPUC's proposal the best approach for your customers?

A. Yes. FPUC's proposal provides a fair and reasonable balancing of the benefits of the 2017 Tax Act. It returns many of the benefits directly to FPUC's customers and does so in a manner that will reduce customer confusion and promote bill stability by applying those tax benefits to offset other beneficial system investments that otherwise would potentially subject our customers to rate increases. FPUC's proposal eliminates the inherent confusion of mixed price signals that exist when individual components of customer bills change in opposite directions. FPUC's proposal also allows FPUC to retain a fair portion of the tax benefit arising from the 2017 Tax Act in a manner that not only allows the Company to earn close to or within its jurisdictional range, but also allows the Company to recover costs not currently recovered in base rates such that the Company may be able to maintain base rates at their current levels for longer than would otherwise be possible given the Company's current earnings posture.

Q. Does FPUC believe this treatment is the most appropriate treatment for the Company?

A. Yes. Adjusting the rates for just one component, such as taxes, of a customer's bill is akin to single-issue rate-making and is inconsistent with fundamental regulatory principles. Additionally, this type of rate-making principle assumes that the Company is currently earning its authorized Return On Equity ("ROE") and that nothing has changed since the last rate proceeding. However, FPUC is currently under-earning relative to its authorized ROE so a reduction to its rates based on the authorized ROE would push the utility's earned ROE even lower on a pro-forma basis, which is again inconsistent with the objectives and goals of rate-making and produces an unreasonable result for FPUC.

Q. Will the impacts of the 2017 Tax Act put FPUC into an over-earnings position?

A. No. FPUC's proposed treatment of the impacts of the 2017 Tax Act benefits will not put the Company into an over-earning position.

II. SUMMARY

Q. Please summarize your testimony.

A. FPUC's proposal, as outlined above, not only meets the intended goal of the 2017 Tax Act by encouraging investment in infrastructure, but it does so in the most efficient, timely and responsible manner possible. FPUC's proposal also allows FPUC to retain a fair portion of the tax benefit arising from the 2017 Tax Act in a manner that allows the Company to earn at or within its jurisdictional range, ensuring that FPUC's customers receive the dual benefits of direct savings and a financially strong service provider able to ensure continued system improvements for safe and reliable service consistent with fundamental regulatory principles.

Q. Does this conclude your testimony?

A. Yes.

FLORIDA PUBLIC UTILITIES COMPANY
Computation of Gas Tax Savings
Projected 2018 Test Year

DOCKET NO.: 20180051-GU
EXHBIT NO.: NGMC-1
Page 1 of 1

	FN	FC Allocated	Total FN	ANNUAL	
ANNUAL TAX SAVINGS FROM RATE CHANGE:					
NOI BEFORE TAX CHANGE	$ 10,640,348		$ 10,640,348		
NOI AFTER TAX CHANGE	$ 12,268,779		$ 12,268,779		
NET INCOME EFFECT OF TAX CHANGE	$ 1,628,431		$ 1,628,431		
GROSS UP	$ 552,844		$ 552,844		
PRETAX - GROSSED UP SAVINGS (EXPENSE)	$ 2,181,275	$ -	$ 2,181,275	$ 2,181,275	
REGULATORY TAX LIABILITY:					
ESTIMATED PROTECTED GROSSED UP REG TAX LIABILITY	$ 21,601,595	$ 198,404	$ 21,799,999	$ 838,462	26 YEARS
ESTIMATED UNPROTECTED ACQ ADJUSTMENT PRETAX GROSSED UP REG TAX LIABILITY	$ 6,518,569		$ 6,518,569	$ 298,560	LIFE OF ACQ. ADJ.
ESTIMATED UNPROTECTED GROSSED UP REG TAX LIABILITY	$ (2,558,387)	$ (358,493)	$ (2,916,880)	$ (291,688)	10 YEARS
NET ESTIMATED REGULATORY LIABILITY	$ 25,561,777	$ (160,088)	$ 25,401,689	$ 845,334	
TOTAL				$ 3,026,609	

Florida Public Utilities Company
Gas Reliability Infrastructure Program (GRIP)
Calculation of the Projected Revenue Requirements
January 1, 2018 through December 31, 2018

DOCKET NO.: **20180051-GU**
EXHIBIT NO.: **NGMC-2**

Item	GRIP CALCULATION WITH NEW TAX EXPANSION FACTOR Year End Total/Balance	GRIP CALCULATION WITH 2017 TAX RATE IN EXPANSION FACTOR Year End Total/Balance	DIFFERENCE
Qualified Investment			
Qualified Investment - Mains - Current Year 1070 Activity	$5,412,000	$5,412,000	$0
Qualified Investment - Mains - Closed 1070 Activity to Plant	($5,141,400)	($5,141,400)	$0
Qualified Investment - Services - Current Year 1070 Activity	$1,188,000	$1,188,000	$0
Qualified Investment - Services - Closed 1070 Activity to Plant	($1,188,000)	($1,188,000)	$0
Qualified Investment - Mains - Current 1010 Activity	$5,141,400	$5,141,400	$0
Qualified Investment - Services - Current 1010 Activity	$1,188,000	$1,188,000	$0
Total Qualified Investment - Mains 1070	$1,268,943	$1,268,943	$0
Total Qualified Investment - Service 1070	$138,427	$138,427	$0
Total Qualified Investment - Mains 1010	$69,736,070	$69,736,070	$0
Total Qualified Investment - Service 1010	$21,655,147	$21,655,147	$0
Total Qualified Investment	$92,798,587	$92,798,587	$0
Less: Accumulated Depreciation	($7,932,305)	($7,932,305)	$0
Net Book Value	$84,866,282	$84,866,282	$0
Average Net Qualified Investment			
Depreciation Rates			
Approved Depreciation Rate-Mains	2.60%	2.60%	0.00%
Approved Depreciation Rate-Services	2.70%	2.70%	0.00%
Return on Average Net Qualified Investment			
Equity - Cost of Capital, inclusive of Income Tax Gross-up	6.470%	7.674%	-1.20%
Debt - Cost of Capital	1.410%	1.410%	0.00%
Equity Component - inclusive of Income Tax Gross-up	$5,352,891	$6,502,894	($1,150,003)
Debt Component	$1,166,550	$1,166,550	$0
Return Requirement	$6,519,441	$7,669,444	($1,150,003)
Investment Expenses			
Depreciation Expense - Mains	$1,740,730	$1,740,730	$0
Depreciation Expense - Services	$567,314	$567,314	$0
Property Taxes	$1,611,487	$1,611,487	$0
General Public Notice Expense & Customer Notice Expense	$52,000	$52,000	$0
Total Expense	$3,971,531	$3,971,531	$0
Total Revenue Requirements	$10,490,971	$11,640,975	($1,150,003)
Annual Revenue Requirement for Bare Steel Replacement Investment	$747,727	$747,727	$0
Net Annual Revenue Requirements	$9,743,244	$10,893,248	($1,150,003)
Less January 1 to February 6 Amount Revenue Requirement			$ 109,862
Net Effect on GRIP of Lower Expansion Factor			($1,040,141)

Before the Florida Public Service Commission

Docket No. 20180051-GU

In re: Consideration of the tax impacts associated with Tax Cuts and Jobs Act of 2017 for Florida Public Utilities Company

Prepared Direct Testimony of Matthew Dewey

Date of Filing: May 31, 2018

Q. Please state your name and business address.

A. My name is Matthew Dewey. My business address is 909 Silver Lake Blvd, Dover, DE 19904.

Q. By whom are you employed and what is your position?

A. I am employed by Chesapeake Utilities Corporation ("CUC") as an Accounting Director. CUC is the corporate parent of Florida Public Utilities Company.

Q. Please describe your educational background and professional experience.

A. I have a Bachelor of Science degree in Accounting from Goldey-Beacom College and have been employed with Chesapeake Utilities Corporation in various accounting positions since 1987.

Q. Have you ever testified before the Florida Public Service Commission ("FPSC")?

A. Yes, I have pre-filed written testimony for the Florida Division of Chesapeake Utilities Corporation, which does business as Central Florida Gas Company, in its 2009 base rate case, Docket No. 20090125-GU.

Q. What is the purpose of your testimony?

A. I will explain how the tax impacts associated with the Federal Tax Cuts and Jobs Acts of 2017 (the "2017 Tax Act") were calculated. I will also explain the methodology used to make these calculations, and how these tax impacts affected FPUC's balance sheet.

Q. Were these calculations of the Deferred Regulatory Liabilities related to the 2017 Tax act calculations performed by you, or under your direct supervision?

A. These calculations were performed under my direct supervision.

Q. Are you sponsoring any exhibits in this case?

A. Yes. I am sponsoring exhibit NGMD-1 and exhibit NGMD-2. The exhibit NGMD-1 shows the Company's calculations to support the estimated regulatory liabilities of $25,561,777 as of March 31, 2018. This amount resulted from implementing the reduction in the federal tax rate from 35% to 21% per the 2017 Tax 7Act. The worksheet lists the estimated Accumulated Deferred Income Tax ("ADIT") account balances as of December 31, 2017 at the blended tax rate, which includes the federal tax rate at 35%. The worksheet also calculates the Company's estimated ADIT account balances as of December 31, 2017, at the blended tax rate, which adjusts for the reduced federal tax rate of 21% per the 2017 Tax Act. The worksheet shows the classification of each estimated excess, or deficient, deferred income taxes into one of the following classifications: Protected, Unprotected plant and Unprotected. This classification is required since protected excess deferred income taxes are required to be flowed back based on IRS normalization guidelines. To record the regulatory liability, we are required to add back the income tax gross-up to get to an applicable revenue amount. The worksheet also calculates the gross-up to record the estimated regulatory liability for Protected, Unprotected plant and Unprotected. In February 2018 and March 2018, estimated deferred tax assets were allocated from the parent, Chesapeake Utilities Corporation, to all Chesapeake subsidiaries and divisions, including FPUC-Natural Gas, at the blended tax rate. I do not expect these adjustments to re-occur. The net difference between the 35% and 21% was reported with a net effect of zero to the balance sheet. My exhibit NGMD-2 supports the same calculation described above for the Florida Corporate general ledger. The result is an estimated regulatory asset of $354,178 of which $160,088 or 45.2% is allocated to FPUC- Natural Gas.

Q. Could you clarify the meaning of a "gross-up" as it pertains to deferred taxes?

A. Yes. The deferred tax impact as a result of the tax rate change is increased, or "grossed up" for the current tax rate. This balance will then be amortized and subject to income taxes at the current rate so that the net income impact equals the amortized tax benefit or detriment.

Q. The total estimated regulatory liability balance of $25,401,689 as noted above related to the federal rate change from 35% to 21% per the 2017 Tax Act, is described as an estimated, why?

A. The staff of the US Securities and Exchange Commission ("SEC") has recognized the complexity of reflecting the impacts of the 2017 Tax Act, and on December 22, 2017 issued guidance in Staff Accounting Bulletin 118 ("SAB 118"), which clarifies accounting for income taxes under ASC 740 if information is not yet available or complete and provides for up to a one year period in which to complete the required analyses and accounting. Therefore, we will complete our measurement and accounting for the impact of the tax law changes on or before December 22, 2018.

Q. Does the Company know of any expected changes which could adjust the regulatory liability?

A. Not at this time. However, once the 2017 federal and state tax returns are filed, the Company will be adjusting entries based on the differences between the tax returns as filed and the 2017 tax provision. These adjustments could affect the ADIT balances as of December 31, 2017.

Q. Does this conclude your testimony?

A. Yes.

FLORIDA PUBLIC UTILITIES

Computation of Regulatory Liability (FN)

Docket No.: 20180051-GU

Exhibit No.: NGMD-1

					BEFORE	AFTER									
FL	5.50%			Fed	35.00%	21.00%					21.00%				
				Blended	38.58%	25.35%					25.35%				
Seg 3	FERC		Code	Name	Beginning Balance	Rate Change	Protected	UnProtected Plant	UnProtected NonPlant	OTP Adj	12/31/2017 Balance	Allocation from Parent UnProtected NonPlant	3/31/18 NetAdjust to LT Bonus	Q1 Entries	03/31/2018 Balance
2500	282	UNNP	2500	ADIT Property LT	$ 258,328	$ (88,598)			$ (88,598)		$ 169,730				$ 169,730
25AA	283	[illegible]	25AA	Acquisition Adjustment	$ (14,189,179)	$ 4,866,438		$ 4,866,438	$ -	$ (53)	$ (9,322,794)			$ 106,749	$ (9,216,045)
25AF	282	[illegible]	25AF	AFUDC	$ -	$ -		$ -	$ -		$ -			$ -	$ -
25AM	283	UNNP	25AM	Customer Based Intangibles	$ 2,105,813	$ (722,227)			$ (722,227)		$ 1,383,586			$ 35,113	$ 1,418,699
25AM	283	UNNP	25AM.01	Amortization Schedules Prior Acquisitions	$ (147,060)	$ 50,437			$ 50,437		$ (96,623)			$ 1,226	$ (95,397)
25BD	283	UNNP	25BD	Bad Debts	$ 51,440	$ (17,642)			$ (17,642)		$ 33,798			$ 7,856	$ 41,654
25BN	283	UNNP	25BN.01	Short Term Bonus	$ -	$ -			$ -		$ -	$ 182,315	$ 72,484	$ -	$ 254,799
25CN	283	UNNP	25CN	Conservation	$ 297,076	$ (101,888)			$ (101,888)	$ (45)	$ 195,143			$ 60,523	$ 255,666
25DP	282	P	25DP.01	Depreciation	$ (46,549,599)	$ 15,965,034	$ 15,965,034		$ -	$ 618	$ (30,583,947)			$ (149,987)	$ (30,733,934)
25DP	282	P	25DP.02	Contribution in Aid of Construction	$ 1,350,259	$ (463,096)	$ (463,096)		$ -		$ 887,163			$ 82,766	$ 969,929
25DP	282	P	25DP.03	Cost of Removal	$ (1,785,297)	$ 612,300	$ 612,300		$ -		$ (1,172,997)			$ (104,876)	$ (1,277,873)
25DP	282	P	25DP.04	Asset Gain/Loss	$ (36,252)	$ 12,433	$ 12,433		$ -		$ (23,819)			$ 533	$ (23,286)
25DP	[illegible]	P	25DP.05	Adjustment for Repairs Depreciation	$ -	$ -	$ -		$ -		$ -			$ -	$ -
25EN	[illegible]	[illegible]	25EN	Environmental	$ 2,572,576	$ (882,312)			$ (882,312)	$ (8)	$ 1,690,256			$ 17,027	$ 1,707,283
25GP	[illegible]	[illegible]	25GP	Grip Over Recoveries	$ -	$ -			$ -		$ -			$ -	$ -
25ID	[illegible]	[illegible]	25ID	Reserve for Insurance Deductibles	$ (89,296)	$ 30,626			$ 30,626		$ (58,670)			$ (476)	$ (59,146)
25IT	[illegible]	[illegible]	25IT	Investment Tax Credit	$ -	$ -			$ -		$ -			$ -	$ -
25MC	[illegible]	[illegible]	25MC	Merger Cost Amortization	$ -	$ -			$ -		$ -			$ -	$ -
25PC	[illegible]	[illegible]	25PC	Piping and Conservation	$ 410,586	$ (140,818)			$ (140,818)	$ (9)	$ 269,759			$ 9,130	$ 278,889
25PG	[illegible]	[illegible]	25PG	Purchased Gas Cots	$ -	$ -			$ -		$ -			$ -	$ -
25PN	[illegible]	[illegible]	25PN	Pension	$ (233,083)	$ 79,940			$ 79,940	$ 6	$ (153,137)			$ 26,462	$ (126,675)
25PR	[illegible]	[illegible]	25PR	Post Retirement Benefits	$ 2	$ (1)			$ (1)	$ 1	$ 2			$ -	$ 2
25PR	[illegible]	[illegible]	25PR.02	Post Retirement Benefits (Non-Current)	$ 251,877	$ (86,386)			$ (86,386)		$ 165,491			$ 135	$ 165,626
25RC	[illegible]	[illegible]	25RC	Rate Case	$ -	$ -			$ -		$ -			$ -	$ -
25RE	[illegible]	[illegible]	25RE	Repairs Deduction	$ (654,523)	$ 125,786		$ 125,786	$ -	$ 21	$ (528,716)			$ 5,957	$ (522,759)
25RG	[illegible]	[illegible]	25RG	ADIT Reg Asset	$ (98,878)	$ 33,912			$ 33,912	$ (33,920)	$ (98,886)			$ -	$ (98,886)
25RP	[illegible]	[illegible]	25RP	Property Taxes	$ -	$ -			$ -		$ -			$ -	$ -
25RT	[illegible]	[illegible]	25RT	Rabbi Trust					$ -		$ -	$ 135,072			$ 135,072
25SD	[illegible]	[illegible]	25SD	ADIT State Decoupling	$ 1,177,120	$ 260,609			$ 260,609		$ 1,437,729			$ -	$ 1,437,729
25SI	[illegible]	[illegible]	25SI.01	Self Insurance (Current)	$ (885)	$ 303			$ 303		$ (582)			$ -	$ (582)
25SR	[illegible]	[illegible]	25SR.01	SERP (Current)					$ -		$ -	$ 303,293			$ 303,293
25SV	[illegible]	[illegible]	25SV	ADIT Outside Services	$ -	$ -			$ -		$ -			$ -	$ -
25WR	[illegible]	[illegible]	25WR	Storm Reserve	$ 258,161	$ (88,541)			$ (88,541)	$ 1	$ 169,621			$ 380	$ 170,001
25SL	[illegible]	[illegible]	S_NOL_SYS	S_NOL_SYS	$ (56,291)	$ (12,124)			$ (12,124)	$ 6,202	$ (62,213)			$ -	$ (62,213)
25SL2	[illegible]	[illegible]	S_NOL_SYS - 2014 - FL	S_NOL_SYS - 2014 - FL	$ 50,089	$ 10,788			$ 10,788		$ 60,877			$ -	$ 60,877
			Total		$ (55,057,016)	$ 19,444,973	$ 16,126,671	$ 4,992,224	$ (1,673,922)	$ (27,186)	$ (35,639,229)	$ 620,680	$ 72,484	$ 98,518	$ (34,847,547)
					$ (1)	$ (1)									
				Protected Gross-up			$ 5,474,924				$ 5,474,924				$ 5,474,924
				UnProtected Plant Gross-up				$ 1,694,835			$ 1,694,835				$ 1,694,835
				UnProtected NonPlant Gross-up					$ (568,288)		$ (568,288)	$ (109,994)	$ (12,845)		$ (691,127)
				Unrecorded adjustment to correct grossup calulation at year end							$ -				$ -
25TX			25TX	Tax Reform 2017 Reg Asset Gross Up			$ 5,474,924	$ 1,694,835	$ (568,288)		$ 6,601,471	$ (109,994)	$ (12,845)	$ -	$ 6,478,632
			Total with Gross-up				$ 21,601,595	$ 6,687,059	$ (2,242,210)		$ (29,037,758)	$ 510,686	$ 59,639	$ 98,518	$ (28,368,915)
							a	b	c						

FLORIDA PUBLIC UTILITIES
Computation of Regulatory Liability (FN)

Docket No.: 20180051-GU
Exhibit No.: NGMD-1

Seg 3	FERC	Code	Name	BEFORE				AFTER						
FL	5.50%		Fed	35.00%	21.00%					21.00%				
			Blended	38.58%	25.35%					25.35%				
Seg 3	FERC	Code	Name	Beginning Balance	Rate Change	Protected	UnProtected Plant	UnProtected NonPlant	OTP Adj	12/31/2017 Balance	Allocation from Parent UnProtected NonPlant	3/31/18 NetAdjust to LT Bonus	Q1 Entries	03/31/2018 Balance
		Excess Deferred Tax Liability before gross up												
			Excess Deferred Tax Liability - Protected			$ (16,126,671)								$ (16,126,671)
			Excess Deferred Tax Liability - Unprotected Plant			$ (4,992,224)								$ (4,992,224)
			Excess Deferred Tax Liability - Unprotected Non Plant			$ 1,673,922					$ (620,680)	$ (72,484)		$ 980,758
			Excess Deferred Tax Liability - Total			$ (19,444,973)								$ (20,138,137)
								FN ADIT	G/L	$ (29,037,782)				$ (28,368,939)
								Adjust G/L 25TX		$ 24				$ 24
		25TX	Tax Reform 2017 Reg Asset Gross Up							$ 6,601,471				$ 6,478,632
		25TX	G/L							$ 6,601,471				$ 6,478,632
								Adjust G/L 25TX		$ 0 d				$ 0
		280R-254P	Reg Liability - Protected						a	$ (21,601,595)				$ (21,601,595)
		280R-254N	Reg Liability -UnProtected						d-b-c	$ (4,444,849)	$ 433,987	$ 50,681		$ (3,960,181)
										$ (26,046,444)				$ (25,561,776)
			Reg Liability -UnProtected Plant							$ (6,687,059)				$ (6,687,059)
			Reg Liability -UnProtected Non Plant							$ 2,242,210	$ 433,987	$ 50,681		$ 2,726,878
										$ (4,444,849)				$ (3,960,181)

FLORIDA PUBLIC UTILITIES COMPANY
Computation of Regulatory Liability Common Division (FC)

Docket No.: 20180051-GU
Exhibit No.: NGMD-2

			BEFORE		AFTER		
FL	5.50%	Fed	35.00%	21.00%	21.00%		
		Blended	38.58%	25.35%	25.35%	Allocation from Parent	3/31/18

Seg 3	FERC		Code	Name	Beginning Balance	Rate Change	Protected	UnProtected Plant	UnProtected NonPlant	OTP Adj	12/31/2017 Balance	UnProtected NonPlant	NetAdjust to LT Bonus	Q1 Entries	03/31/2018 Balance
2500	282	UNNP	2500	ADIT Property LT	$ 2,791	$ (957)			$ (957)		$ 1,834			$ -	$ 1,834
25BN	283	UNNP	25BN.01	Short Term Bonus	$ 646,396	$ (221,693)			$ (221,693)	$ 43	$ 424,746			$ 14,462	$ 439,208
25BN	283	UNNP	25BN.02	Long Term Bonus	$ 12,907	$ (4,427)			$ (4,427)		$ 8,480			$ -	$ 8,480
25DP	282	P	25DP.01	Depreciation	$ (937,944)	$ 321,685	$ 321,685		$ -		$ (616,259)			$ (43,664)	$ (659,923)
25DP	282	P	25DP.04	Asset Gain/Loss	$ (17,530)	$ 6,012	$ 6,012		$ -		$ (11,518)			$ (2,334)	$ (13,852)
25DP	282	P	25DP.05	Adjustment for Repairs Depreciation	$ -	$ -	$ -		$ -		$ -			$ -	$ -
25EN	283	UNNP	25EN	Environmental	$ -	$ -			$ -		$ -	$ -		$ -	$ -
25ID	283	UNNP	25ID	Reserve for Insurance Deductibles	$ (1,421)	$ 487			$ 487	$ (1)	$ (935)			$ (1)	$ (936)
25PN	283	UNNP	25PN	Pension	$ 1,281,408	$ (439,482)			$ (439,482)	$ 15	$ 841,941			$ (5,222)	$ 836,719
25PR	283	UNNP	25PR	Post Retirement Benefits	$ (3,007)	$ 1,031			$ 1,031	$ (3,550)	$ (5,526)			$ -	$ (5,526)
25PR	283	UNNP	25PR.02	Post Retirement Benefits (Non-Current)	$ (7,376)	$ 2,530			$ 2,530		$ (4,846)			$ -	$ (4,846)
25RC	283	UNNP	25RC	Rate Case	$ -	$ -			$ -		$ -			$ -	$ -
25RD	283	UNNP	25RD	Loss on Reacquired Debt	$ (397,679)	$ 136,391			$ 136,391	$ 33,873	$ (227,415)			$ 7,208	$ (220,207)
25RE	282	UNPP	25RE	Repairs Deduction	$ 55,515	$ (19,040)		$ (19,040)	$ -	$ 5	$ 36,480			$ (420)	$ 36,060
25RT	283	UNNP	25RT	Rabbi Trust					$ -		$ -				$ -
25SD	283	UNNP	25SD	ADIT State Decoupling					$ -		$ -			$ -	$ -
25SD	283	UNNP	25SD	ADIT State Decoupling	$ -	$ -			$ -		$ -			$ -	$ -
25SI	283	UNNP	25SI.01	Self Insurance (Current)	$ -	$ -			$ -		$ -			$ -	$ -
25SI	283	UNNP	25SI.02	Self Insurance (Non-Current)	$ -	$ -			$ -		$ -			$ -	$ -
25SL	283	UNNP	25SL	ADIT State NOL	$ -	$ -			$ -		$ -			$ -	$ -
25VA	283	UNNP	25VA	Vacation	$ 144,792	$ (49,659)			$ (49,659)	$ 12	$ 95,145			$ (1,613)	$ 93,532
NOL_	283	UNNP	NOL_SYS	NOL_SYS	$ -	$ -			$ -		$ -			$ -	$ -
25SL	283	UNNP	S_NOL_SYS	S_NOL_SYS	$ (253,510)	$ (54,602)			$ (54,602)	$ (3,104)	$ (311,216)			$ -	$ (311,216)
25SL	283	UNNP	S_NOL_SYS - 20	S_NOL_SYS - 2014 - FL	$ 256,614	$ 55,271			$ 55,271		$ 311,885			$ -	$ 311,885
			Total		$ 781,956	$ (266,453)	$ 327,697	$ (19,040)	$ (575,110)	$ 27,293	$ 542,796	$ -	$ -	$ (31,584)	$ 511,212
					$ -	$ -									
				Protected Gross-up			$ 111,251				$ 111,251				$ 111,251
				UnProtected Plant Gross-up				$ (6,464)			$ (6,464)				$ (6,464)
				UnProtected NonPlant Gross-up					$ (195,247)		$ (195,247)	$ -			$ (195,247)
				Unrecorded adjustment to correct grossup calulation at year end					$ 2,735		$ 2,735				$ 2,735
25TX			25TX	Tax Reform 2017 Reg Asset Gross Up			$ 111,251	$ (6,464)	$ (192,512)		$ (87,724)	$ -	$ -		$ (87,724)
			Total with Gross-up				$ 438,948	$ (25,504)	$ (767,622)		$ 455,072	$ -	$ -	$ (31,584)	$ 423,488
							a	b	c						

FLORIDA PUBLIC UTILITIES COMPANY
Computation of Regulatory Liability Common Division (FC)

Docket No.: 20180051-GU
Exhibit No.: NGMD-2

Seg 3	FERC	Code	Name	Beginning Balance	Rate Change	Protected	UnProtected Plant	UnProtected NonPlant	OTP Adj	12/31/2017 Balance	UnProtected NonPlant	NetAdjust to LT Bonus	Q1 Entries	03/31/2018 Balance
				BEFORE					AFTER					
FL	5.50%		Fed	35.00%	21.00%					21.00%				
											Allocation from Parent	3/31/18		
			Blended	38.58%	25.35%					25.35%				
		Excess Deferred Tax Liability before gross up												
			Excess Deferred Tax Liability - Protected			$ (327,697)								$ (327,697)
			Excess Deferred Tax Liability - Unprotected Plant			$ 19,040								$ 19,040
			Excess Deferred Tax Liability - Unprotected Non Plant			$ 575,110					$ -	$ -		$ 575,110
			Excess Deferred Tax Liability - Total			$ 266,453								$ 266,453

[redacted]

Seg 3	FERC	Code	Name	Beginning Balance	Rate Change	Protected	UnProtected Plant	UnProtected NonPlant	OTP Adj	12/31/2017 Balance	UnProtected NonPlant	NetAdjust to LT Bonus	Q1 Entries	03/31/2018 Balance
								FN ADIT	G/L	$ 455,012				$ 423,428
								Adjust G/L 25TX		$ 59				$ 59
		25TX	Tax Reform 2017 Reg Asset Gross Up							$ (87,724)				$ (87,724)
		25TX	G/L							$ (87,725)				$ (87,725)
								Adjust G/L 25TX		$ 1				$ 1
										d				
		280R-254P	Reg Liability - Protected						a	$ (438,948)				$ (438,948)
		280R-254N	Reg Liability -UnProtected						d-b-c	$ 793,126				$ 793,126
										$ 354,178				$ 354,178
			Reg Liability -UnProtected Plant							$ 25,504				$ 25,504
			Reg Liability -UnProtected Non Plant							$ 767,622	$ -	$ -		$ 767,622
										$ 793,126				$ 793,126

BEFORE THE

FLORIDA PUBLIC SERVICE COMMISSION

Docket No. 20180051-GU

In re: Consideration of the tax impacts associated with Tax Cuts and Jobs Act of 2017 for Florida Public Utilities Company

Direct Testimony

of

Michael J. Reno,

Ernst & Young, LLP

On Behalf of

FLORIDA PUBLIC UTILITIES COMPANY

Natural Gas Division

I. **Introduction**

Q. **Please state your name, business address and by whom you are employed, and in what capacity.**

A. My name is Michael Reno. My business address is 1101 New York Avenue, NW, Washington, District of Columbia, 20005-4213. I am an executive director in Ernst & Young LLP's National Energy Practice.

Q. **On whose behalf are you testifying in this proceeding?**

A. I am testifying on behalf of Florida Public Utilities Company ("FPUC").

Q. **What is your educational and professional background?**

A. I graduated from Kansas State University with a Bachelor of Science degree in Business Administration, with an emphasis in accounting, in 1987, and a Masters of Science, with an emphasis in accounting, in 1988. After completion of my Masters of Science in Accounting, I joined Deloitte Tax LLP, formerly Deloitte Haskins & Sells. In 2012, I joined Ernst & Young LLP as an executive director in the National Energy Practice. I am a Certified Public Accountant, licensed in the District of Columbia and in the Commonwealth of Virginia. I have practiced public accounting for over 29 years. In my practice, I provide tax services to regulated water, electric and gas utilities. I regularly assist clients with tax planning, supporting and explaining tax reporting positions, and tax return reviews. My experience includes providing advice on accounting for income taxes and performing tax provision reviews. I also regularly consult with companies regarding tax accounting and its impact on the rate setting process as well as compliance with the normalization rules. Additionally, I am a frequent speaker at industry seminars and conferences on the topic of tax accounting for rate-regulated utilities. I have spoken at the Edison Electric Institute tax committee meetings and the American Gas Association tax committee meetings in addition to other industry meetings.

Q. Have you testified in any regulatory proceedings?

A. Yes, I have provided expert testimony on multiple occasions over the last 10 years on tax, tax accounting and regulatory tax matters before the New Jersey Board of Public Utilities, the California Public Utilities Commission, the Connecticut Public Utilities Regulatory Authority and the Federal Energy Regulatory Commission.

II. Purpose of Testimony

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to explain how the 2017 tax law changes, commonly known as the "the Tax Cuts and Jobs Act" (the TCJA), impact FPUC's revenue requirement.

III. Overview of the TCJA

Q. Can you describe what specifically is meant by the term TCJA?

A. The TCJA was signed into law by President Trump on December 22, 2017 and is the first major overhaul of federal income tax in more than

30 years. The stated purpose of the TCJA is to deliver historic tax relief for workers, families and job creators, and revitalize the US economy.

Q. How broad are the changes to the tax law?

A. All taxpayer groups, including corporations, pass-through entities and individuals, are affected, although the effects of the law change will vary widely based on each taxpayer's situation. Key domestic business provisions of the TCJA include: (i) permanently reducing the 35% corporate income tax rate to 21%, (ii) repeal of the corporate alternative minimum tax (AMT), (iii) change in the taxability of contributions to the capital of a corporation, (iv) interest expense limitation, (v) immediate expensing of qualified property, (vi) limiting net operating loss (NOL) usage to 80%, and (vii) repeal of domestic production activities deduction.

Q. What impact does the TCJA have on utilities?

A. The TCJA has many provisions that will impact the tax liability of utilities. The two most significant of those business provisions include the reduction in the corporate income tax rate and the disallowance of immediate expensing of property acquired.

Corporate taxpayers were previously subject to a top corporate rate of 35% under a graduated rate structure. Under the TCJA, corporate taxpayers are subject to a 21% corporate tax rate with no graduated rate structure, effective January 1, 2018.

Under prior law, utilities were allowed to claim bonus depreciation during the year in which qualified property was placed in service. The TCJA extended the bonus depreciation provisions and increased it to 100% expensing of qualified property. However, regulated utilities are no longer eligible to claim bonus depreciation. Under the TCJA, utilities engaged in a certain trade or business as described in clause (iv) of section 163(j)(7)(A) are precluded from immediate expensing while other taxpayers are eligible for immediately expensing certain qualified property. For purposes of the exception (i.e., the inability to claim immediate expensing), clause (iv) of section 163(j)(7)(A) defines the trade or business to include the furnishing or sale of – electrical energy, water, or sewage disposal services, gas or steam through a local distribution system, or transportation of gas or steam by pipeline. Consequently, utilities such as FPU will see some reduction in the savings associated with the reduction from 35% to 21% because of the elimination of this bonus depreciation.

Q. Does the TCJA have any provisions impacting how utility rates may be set?

A. Yes. The corporate income tax rate change has specific provisions requiring that a normalization method of accounting be applied to the rate change. The corporate taxpayer must normalize the excess tax reserves resulting from the reduction of the corporate income tax rates with respect to prior depreciation or recovery allowances taken on assets placed in service prior to when the corporate rate reduction takes effect.

Q. What is meant by the term "normalization" or "normalize"?

A. "Normalization" requirements apply to section 167 or 168 of the Internal Revenue Code. Compliance with the normalization rules involves: (1) setting up a deferred tax reserve for the difference between depreciation expense used by regulators to determine cost of service (normally the straight line method) and the accelerated method used for calculating tax expense on income tax returns and then (2) drawing down that reserve in later years as the accelerated depreciation benefits reverse. With respect to the TCJA and the change in tax rates, the law states a public utility is not in compliance with the normalization rules if the utility "reduces the excess tax reserve more rapidly or to a greater extent than such reserve would be reduced under the average rate assumption method."

Q. What is the term "excess tax reserve"?

A. The term tax reserve represents the amount of tax depreciation in excess of book depreciation multiplied by the tax rate, also known as the deferred tax liability. The excess tax reserve is the portion of such a reserve for deferred taxes (as of the day before the corporate rate reduction takes effect) that is greater than what the reserve for deferred taxes would be had the corporate rate reduction been in effect for all prior periods. The reserve for deferred taxes arising through the use of a normalization method of accounting represents a liability for federal income taxes payable at a future date. Accordingly, the reserve for deferred taxes is usually considered a form of interest-free financing in the ratemaking process. This treatment typically is achieved by treating the reserve as either a reduction to the rate base or, less frequently, as a zero-cost source of capital.

Q. How is compliance with the normalization requirements met?

A. There are two methods for normalization computation, (1) average rate assumption method (ARAM), and (2) Reverse South Georgia Method (RSGM).

ARAM is the required method and reduces the excess tax reserve over the remaining regulatory lives of the property that gave rise to the reserve for deferred taxes. Under this method, the excess tax reserve is reduced as the timing differences (i.e., differences between tax depreciation and regulatory depreciation with respect to the property) reverse over the remaining life of the asset. The reversal of timing differences generally occurs when the amount of the tax depreciation taken with respect to an asset is less than the amount of the regulatory depreciation taken with respect to the same asset. To ensure that the deferred tax reserve, including the excess tax reserve, is reduced to zero at the end of the regulatory life of the asset that generated the reserve, the amount of the timing difference which reverses during a taxable year is multiplied by the ratio of (1) the aggregate deferred taxes as of the beginning of the period in question to (2) the aggregate timing differences for the property as of the beginning of the period in question.

An alternative method, the RSGM, requires that the excess tax reserve on all public utility property in the plant account is computed based on the weighted average life or composite rate used to calculate depreciation for regulatory purposes. The excess tax reserve is then reduced ratably over the regulatory life of the property.

Q. Does the TCJA mandate a method for flowing back the excess reserve?

A. The TCJA specifically provides the method of flowing back the excess reserve solely as it relates to accelerated depreciation. It states that the excess amount in the reserve for deferred taxes is to be reversed using ARAM to be in compliance with the normalization rules. The alternative RSGM is available to certain taxpayers where the utilities books and records do not have sufficient vintage account data records to make the required computations under ARAM. In other words, the use of RSGM in lieu of ARAM is an alternative where the utility is unable to utilize ARAM with their existing books and records.

Q. Does TCJA mandate treatment of excess deferred taxes to deferred items other than section 167/168?

A. No. As mentioned above, normalization provisions only apply to the accelerated depreciation under section 167 and 168, which is commonly referred to as "protected" excess deferred tax reserves. The balance of the excess reserves outside of section 167 and 168 are "unprotected" and may be handled at the discretion of the utility and commission.

Q. What are the consequences of not complying with the normalization rules?

A. Failure to use a normalization method may result in the loss of accelerated depreciation deductions. If an excess tax reserve is reduced more rapidly or to a greater extent than such reserve would be reduced under ARAM or RSGM, if applicable, the taxpayer will not be treated as having used a normalization method with respect to the corporate rate reduction. If the taxpayer has not used a normalization method of accounting for the corporate rate reduction, the taxpayer's tax for the taxable year shall be increased by the amount by which it reduced its excess tax reserve more rapidly than permitted under a normalization method of accounting and the taxpayer will not be treated as using a normalization method of accounting for purposes of section 168(f)(2) and (i)(9)(C). The penalty for noncompliance includes an immediate tax for the amount improperly amortized as well as the inability to claim accelerated depreciation (including any eligible bonus depreciation) for the current and future years.

IV. <u>FPUC calculation of effects of TCJA</u>

Q. How has FPUC computed the excess deferred taxes?

A. FPUC computed excess deferred taxes in two categories, those related to plant and those related to non-plant. The plant related excess deferred taxes includes those that are associated with accelerated depreciation and subject to the normalization rules as well as other book/tax differences associated with plant. The non-plant related excess deferred taxes include all other book/tax differences that are not associated with plant. The normalization rules only require excess deferred income taxes associated with accelerated depreciation to be amortized under the average rate assumption method or reverse South Georgia method, if applicable. All other excess deferred income taxes are not subject to the normalization rules and may be amortized at the discretion of the utility and commission.

Q. Over what period are the excess deferred taxes to be amortized?

A. The excess deferred taxes related to plant are anticipated to be amortized utilizing the ARAM method, assuming the books and records allow for that calculation. The excess deferred taxes related to non-plant are anticipated to be amortized over a 10-year period.

Q. Does FPU's approach to amortization of excess deferred taxes comply with the normalization rules?

A. Yes.

Q. Does this conclude your testimony?

A. Yes.