

BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

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FPSC - COMMISSION CLERK

In the Matter of:

DOCKET NO. 20180051-GU

CONSIDERATION OF THE TAX
IMPACTS ASSOCIATED WITH
TAX CUTS AND JOBS ACT OF
2017 FLORIDA PUBLIC
UTILITIES COMPANY - GAS.

DOCKET NO. 20180052-GU

CONSIDERATION OF THE TAX
IMPACTS ASSOCIATED WITH
TAX CUTS AND JOBS ACT OF
2017 FOR FLORIDA PUBLIC
UTILITIES COMPANY -
INDIANTOWN DIVISION.

DOCKET NO. 20180053-GU

CONSIDERATION OF THE TAX
IMPACTS ASSOCIATED WITH
TAX CUTS AND JOBS ACT OF
2017 FOR FLORIDA PUBLIC
UTILITIES COMPANY - FORT
MEADE DIVISION.

DOCKET NO. 20180054-GU

CONSIDERATION OF THE TAX
IMPACTS ASSOCIATED WITH
TAX CUTS AND JOBS ACT OF
2017 FOR FLORIDA DIVISION
OF CHESAPEAKE UTILITIES
CORPORATION.

VOLUME 2
PAGES 200 through 322

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PROCEEDINGS: HEARING

COMMISSIONERS
PARTICIPATING: COMMISSIONER JULIE I. BROWN
COMMISSIONER GARY F. CLARK
COMMISSIONER ANDREW G. FAY

DATE: Tuesday, November 27, 2018

TIME: Commenced: 10:06 a.m.
Concluded: 11:49 a.m.

PLACE: Betty Easley Conference Center
Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: ANDREA KOMARIDIS
Court Reporter

APPEARANCE: (As heretofore noted.)

PREMIER REPORTING
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EXHIBITS

DOCKET NO. 20180051-GU

NUMBER:	ID	ADMITTED
17 - Reedy Creek court case		221
18 - Quarterly earnings surveillance report for FPUC Indiantown Division, 2012 through 2018		221
19 - Quarterly earnings surveillance report for FPUC's Fort Meade Division, 2014 through 2018		221

EXHIBITS

DOCKET NO. 20180052-GU

NUMBER:	ID	ADMITTED
18 - Reedy Creek court case		221
19 - Quarterly earnings surveillance report for FPUC Indiantown Division, 2012 through 2018		221
20 - Quarterly earnings surveillance report for FPUC's Fort Meade Division, 2014 through 2018		221

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EXHIBITS

DOCKET NO. 20180053-GU

NUMBER:	ID	ADMITTED
17 - Reedy Creek court case		221
18 - Quarterly earnings surveillance report for FPUC Indiantown Division, 2012 through 2018		221
19 - Quarterly earnings surveillance report for FPUC's Fort Meade Division, 2014 through 2018		221

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NUMBER:	ID	ADMITTED
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20 - Quarterly earnings surveillance report for FPUC's Fort Meade Division, 2014 through 2018		221

1 P R O C E E D I N G S

2 (Transcript follows in sequence from
3 Volume 1.)

4 CONTINUED EXAMINATION

5 BY MS. PONDER:

6 Q And again, I have flagged -- if you could,
7 turn to that page. And is that your signature on this
8 surveillance report dated June 10, 2015?

9 A Yes, it is.

10 Q And again, on -- this contains the same
11 attestation that you read into the record with a little
12 bit of my assistance previously?

13 A Yes, it is.

14 Q And did Fort Meade -- Fort Meade did not file
15 any sworn revisions to any of its surveillance reports
16 for the years 2014 to 2017 --

17 A Not to my --

18 Q -- correct?

19 A -- knowledge.

20 Q Again, you would agree that Fort Meade -- the
21 Fort Meade Division does not manage the company in a
22 haphazard way.

23 A I would agree with that.

24 Q In fact, you -- the company applies a
25 principled and rigorous set of management practices,

1 including budgeting, forecasting, and strategic-planning
2 assumptions for O&M, capital, and funding needs,
3 priorities, and objectives, correct?

4 A I would agree with that as well.

5 Q Isn't it correct that Fort Meade has been
6 reporting earnings below its authorized range since the
7 company was purchased in 2014?

8 A That sounds correct, yes.

9 Q And is it your opinion that, because of the
10 reduction in income taxes, you should, today, raise your
11 customers' rates through the ECCR even though it was the
12 company's choice to be in its current under-earnings
13 posture?

14 A Again, I would suggest that we want to use
15 that as a mechanism to recover that tax detriment.

16 Q Also, for Fort Meade, the lower federal
17 corporate income tax rate has resulted in the company
18 now having EADIT, excess ADIT.

19 A That's correct, yes.

20 Q Okay. So, I'll refer to that as EADIT again.
21 And the company has calculated amounts of its EADIT,
22 correct?

23 A That's correct, yes.

24 Q On Pages 5 and 6, you address the company's
25 proposal to retain the estimated unprotected and

1 protected deferred tax balances. You testify that Fort
2 Meade proposes to retain both the estimated annual
3 unprotected EADIT liability amortization benefit of
4 \$4,588, and the estimated annual amount of protected
5 EADIT tax liability amortization of \$1,787, for a net
6 benefit of approximately \$6,375 annually; is that
7 correct?

8 A That is correct, yes.

9 Q On Page 6 of your testimony, you indicate the
10 annual retention of these funds, of the \$6,375, for the
11 estimated unprotected and protected tax balances will
12 not put Fort Meade into its authorized range, but it
13 still will meet the intended goal of the 2017 tax act by
14 allowing the company to continue to make capital
15 investments; is that correct?

16 A Yes, that's correct.

17 Q And you can't point to where, in your
18 testimony, you provide the -- an earnings range where
19 Fort Meade will be earning, should the Commission allow
20 the company to retain these funds, can you?

21 A I cannot.

22 Q And you can't point to any language within the
23 2017 tax act suggesting an intended goal of the act is
24 to allow a utility to keep tax savings so as to continue
25 making capital investments while potentially delaying

1 the need for a costly rate proceeding.

2 A I would agree that that's not expressly
3 written in that language.

4 Q On Page 7 of your testimony, you state that
5 there is a direct tax impact, the company's tax Gas
6 Reliability Infrastructure Program, or GRIP; is that
7 correct?

8 A That's correct.

9 Q Is it your testimony that the company proposes
10 to retain the tax-savings benefit related to the 2018
11 GRIP surcharge from the jurisdictional date until
12 December 31, 2018, which the company calculates to be
13 approximately \$2,376? Is that correct?

14 A That is correct, yes.

15 Q On Page 8, you state that: In retaining this
16 portion of the tax benefit, the company will be allowed
17 to earn closer to its jurisdictional range and recover
18 costs not currently recovered in base rates, correct?

19 A That's correct as well.

20 Q Again, you can't point to where in your
21 testimony you show where, in it's earnings range, Fort
22 Meade will be earning, should the Commission allow the
23 company to retain the \$6,375, right?

24 A That's correct, yes.

25 Q And again, specifically related to the GRIP

1 tax benefit of \$2,376, you can't point to where in your
2 testimony you provide a calculation addressing that
3 impact and where the earnings of the company would be,
4 should the Commission allow the retention of those
5 funds.

6 A That's correct.

7 Q And again, you acknowledged earlier that you
8 reviewed the Reedy Creek case. And do you still agree
9 that, except for the cost-of-capital components that you
10 would have to replace because of less-deferred taxes,
11 these funds are basically revenue-neutral for Fort
12 Meade?

13 A Again, I would agree with that component;
14 though, a different set of circumstances, again, for
15 this company.

16 Q Okay. That concludes my questions for Fort
17 Meade.

18 So, we're on to the 54 Chesapeake docket. And
19 again, I'll be referring to Chesapeake just as that.

20 You state in your testimony that the annual
21 tax savings for Chesapeake with the tax-rate change to
22 be approximately \$954,499; is that correct?

23 A Yes, that's correct.

24 Q On Page 4, you indicate that Chesapeake
25 proposes to retain this annual tax benefit to enable the

1 company to earn within or near its allowed range while
2 continuing to make additional investments?

3 A That's correct, yes.

4 Q And these tax savings represent money that the
5 ratepayers have already paid to Chesapeake; is that
6 correct?

7 A That's correct.

8 Q Again, it's the ratepayers' money that we're
9 talking about here with the tax savings.

10 A That's correct.

11 Q And would you agree that the authorized
12 earnings range for Chesapeake is 9.8 to 11.8?

13 A Yes, that's correct.

14 Q Again, you can't point into -- to your -- in
15 your testimony -- where in your testimony that you
16 include a calculation of where the authorized range the
17 company will be earning, should the Commission allow the
18 company to retain these tax savings of \$954,499,
19 correct?

20 A That's correct.

21 Q And this annual tax savings of \$954,499 is a
22 result -- direct result of the federal income tax
23 legislation, the 2017 tax act, and the rate change from
24 35 percent to 21 percent, correct?

25 A That's correct.

1 Q So, Chesapeake did not do anything to generate
2 these savings.

3 A That's correct.

4 Q They were not generated by company man- --
5 management; these savings were generated by the tax
6 legislation, specifically, correct?

7 A That's correct.

8 Q Chesapeake -- because of the tax -- 2017 tax
9 act, Chesapeake also now has excess accumulated deferred
10 income taxes, correct?

11 A That's correct.

12 Q And again, I'll be referring to these as
13 EADIT. And looking at your Exhibit CFMC-1 revised, you
14 indicate that the company shows a regulatory liability
15 for EADIT of \$8,475,577, of which 9- -- excuse me -- of
16 which \$9,537,104 is a protected liability, of
17 \$1,061,527, is an unprotected asset; is that correct?

18 A That's correct, yes.

19 Q You state in your testimony that Chesapeake
20 wants to retain the protected EADIT liability per-year
21 amortization of \$369,596 less the \$119,554 per-year
22 unprotected EADIT net amortization, which would result
23 in a net benefit amount to be retained by the company of
24 \$250,042; is that correct?

25 A That's correct, yes.

1 Q Also, on Page 6, you state the proposal of
2 re- -- retaining the benefit meets the intended goal of
3 the 2017 tax act by allowing the company to continue to
4 make it's cal- -- make capital investments; is that
5 correct?

6 A That's correct.

7 Q Again, you would agree that 2017 tax act does
8 not have any specific language suggesting that an
9 intended goal is to allow a utility to keep tax savings
10 so as to continue to make capital investments while
11 potentially delaying the need for a costly rate
12 proceeding.

13 A Again, I would agree that that's not
14 expressly -- expressly written in that language.

15 Q And as the case for Chesapeake, you
16 acknowledge that you've reviewed the Reedy Creek case
17 and that you still agree that, except for cost-of-
18 capital components that you would have to replace
19 because of less-deferred taxes, the funds here we're
20 speaking of are basically revenue-neutral for the
21 utility.

22 A Again, I would agree, noting that it's a
23 sep- -- separate set of circumstances in that case, from
24 that case.

25 MS. PONDER: Thank you.

1 **how that's the case?**

2 A Well, while -- I'm not exactly sure of the --
3 the tax structure, but those companies are earning in
4 a -- in a different posture. So, they end up in a tax
5 detriment as opposed to -- because of the way their
6 assets are on the books.

7 Q Okay. Thank you.

8 **And would you agree that, generally, regulated**
9 **public utility rates are set on a stand-alone basis?**

10 A Yes, I would.

11 Q And is it your contention that the tax
12 detriment associated with the operating losses at Fort
13 Meade and Indiantown are directly re- -- directly
14 related to the fact that Fort Meade and Indiantown are
15 part of the consolidated tax return filed by Chesapeake
16 Utility Corporation?

17 A Yes, I would agree with that.

18 Q And is it correct that your argument regarding
19 the tax detriment is that the tax losses for Fort Meade
20 and Indiantown are worth less to Chesapeake Utility
21 Corporation at a 21-percent tax rate rather than a
22 35-percent tax rate?

23 A If you could, repeat that question; make sure
24 I understand what you're asking.

25 Q Sure. Is it your argument that, as far as the

1 tax detriment goes, the tax losses for Fort Meade and
2 Indiantown are worth less to Chesapeake Utility
3 Corporation, the parent company, at a 21-percent tax
4 rate as opposed to a 35-percent?

5 A Yes, I would agree with that.

6 MS. DZIECHCIARZ: All right. Thank you.

7 Staff has no more questions.

8 COMMISSIONER BROWN: Thank you.

9 Commissioners, any questions?

10 Commissioner Clark.

11 COMMISSIONER CLARK: I'm going to try and ask
12 one. I get -- tax law, I guess, would be an
13 extremely weak area that -- of mine, but I'm trying
14 to understand, more importantly, the effect on
15 rates.

16 Can -- can you tell me, Mr. Cassel, what the
17 effect would be on rates if the Commission
18 basically denied your request and said no, that all
19 the savings need to be passed through? What would
20 happen to the rates in each of the individual four
21 companies?

22 THE WITNESS: Well, thank you. I -- I think
23 the important thing to remember in that is we -- at
24 this point, we are operating four utilities, four
25 separate tariffs. And the unintended consequence

1 of that would be us filing four individual rate
2 cases.

3 And we're on a path, as you've seen over the
4 last several years, to -- to bring those tariffs
5 together and do it in a more consolidated and a
6 more economical, more efficient, operationally,
7 way, so that, when we do file the rate case, that
8 we can do that once because, what would happen is,
9 we would have the impact of raising -- for Fort
10 Meade, for example, we would raise taxes.

11 We would go through the rate case, with the
12 additional rate-case expense and then, you know,
13 likely raise those rates and then have to turn back
14 around and do that again, several years later when
15 we consolidate.

16 COMMISSIONER CLARK: So, you're saying that if
17 the tax savings are allowed to be retained by the
18 utilities in these cases, you're basically avoiding
19 a rate increase.

20 THE WITNESS: What I would say is we're --
21 we're temporarily avoiding it. We're not looking
22 to avoid a rate case altogether; we're just trying
23 to appropriately time the rate cases with the
24 intention of bringing all four of those rate cases
25 together into one tariff.

1 We think that's the most efficient and
2 economical way to do that. So, it's not a -- not
3 an avoidance. It's just timing it appropriately
4 for our customers.

5 COMMISSIONER CLARK: If the Commission
6 required the savings to be passed through, how
7 would you handle that pass-through in the short
8 term?

9 THE WITNESS: Well, we would have to file rate
10 cases on each of those entities to do that.

11 COMMISSIONER CLARK: So, you would still have
12 to go through a complete rate case in order to pass
13 those savings back to the customer?

14 THE WITNESS: Yes, I believe so.

15 COMMISSIONER CLARK: Okay. Madam Chair.

16 COMMISSIONER BROWN: I have one question,
17 similar lines. I mean, some -- these utilities are
18 operating well below their authorized rate of
19 return.

20 Prior to the tax act going into effect, did
21 the companies have a plan of attack in addressing
22 it? One -- I -- I think you answered one of the
23 questions when you acquired one of the entities.

24 It was operating at -- below.

25 Did you have a path other than this short-term

1 remedy?

2 THE WITNESS: Yes, Commissioner, we did
3 absolutely have -- as -- as I referenced earlier,
4 we've been working, over the last several years,
5 through, if you'll recall Phase 1 and Phase 2,
6 what's now our swing-service docket.

7 These have been very definitive steps for the
8 utility to bring the common practices and best
9 practices, obviously, of those tariffs together and
10 get those programs more aligned with the intention
11 of filing a -- what would be four rate cases coming
12 together in one tariff and doing it one time and
13 ending with a consistent tariff, instead of filing
14 individually, several times over.

15 COMMISSIONER BROWN: You plan on doing that in
16 2019?

17 THE WITNESS: We're -- right now, given all
18 the circumstances that have gone on with the
19 hurricanes and we're -- and our resourcing, we're
20 planning 2020 to 2021 would be our intention.

21 COMMISSIONER BROWN: Okay.

22 THE WITNESS: And that was the plan prior to
23 this. This just gives us the opportunity to more
24 appropriately time -- knowing some of the other
25 things come down, you know, from a resource

1 perspective, this just allows us to smooth that
2 timing out somewhat.

3 COMMISSIONER BROWN: Right. And obviously,
4 the -- you -- you all were hit by the hurricane
5 significantly.

6 THE WITNESS: That's correct.

7 COMMISSIONER BROWN: And we'll deal with that
8 in another docket.

9 Thank you.

10 THE WITNESS: Thank you.

11 COMMISSIONER BROWN: Any other questions?

12 Redirect.

13 MS. KEATING: We have no redirect.

14 COMMISSIONER BROWN: So, we will be dealing
15 with exhibits here. I believe, when staff took up
16 some of the stipulated issues, they had asked for
17 certain exhibits to be entered into the record.
18 And as part of that, I do believe Mr. Cassel's
19 exhibits were entered into the record; is that
20 correct?

21 MS. DZIECHCIARZ: Yes.

22 COMMISSIONER BROWN: Okay. So, what I have
23 right now -- the only thing that re- -- remains
24 outstanding -- Ms. Keating? Yeah, they were --
25 they were entered in.

1 MS. KEATING: I just wanted to make sure, yes.

2 COMMISSIONER BROWN: They were. They were.

3 So, the only thing we're dealing with now are
4 Office of Public Counsel's additional exhibits that
5 were provided here.

6 Ms. Ponder?

7 MS. PONDER: Yes -- excuse me. So, we would
8 like to move into the record each of the --

9 COMMISSIONER BROWN: I have it. Would you
10 like me to list them?

11 MS. PONDER: Yes. Would you?

12 COMMISSIONER BROWN: You want -- you would
13 like all of those to be entered in --

14 MS. PONDER: Correct.

15 COMMISSIONER BROWN: There's one document, the
16 tax act, that you did not use --

17 MS. PONDER: Correct, the one I did not call.

18 COMMISSIONER BROWN: Okay. Ms. Keating, do
19 you have a problem with moving those in, just
20 for --

21 MS. KEATING: No, Commissioner.

22 COMMISSIONER BROWN: Okay. So, I will do this
23 very clearly, for the record here. In the 51
24 docket, we will go ahead and move into the record
25 Exhibits 17, 18, and 19.

1 For the 52 docket, we will go ahead and move
2 into the record Exhibits 18, 19, and 20.

3 In the 53 docket, we will go ahead and move in
4 17, 18, and 19.

5 And in the 54 docket, we will go ahead and
6 move into the record 18, 19, and 20.

7 MS. PONDER: Thank you.

8 COMMISSIONER BROWN: Thank you.

9 (Whereupon, Exhibit Nos. 17, 18, and 19 were
10 admitted into the record in Docket Nos. 20180051-GU
11 and 20180053-GU; and Exhibit Nos. 18, 19, and 20
12 were admitted into the record in Docket Nos.
13 20180052-GU and 20180054-GU.)

14 COMMISSIONER BROWN: Would you like to be
15 excused at this time?

16 THE WITNESS: If you're done, I would be glad
17 to.

18 COMMISSIONER BROWN: Yes. Thank you very much
19 for your testimony today.

20 All right. So, we have Office of Public
21 Counsel -- would you like to take a brief break
22 before you have your witness called?

23 MS. PONDER: Sure. That would be great.

24 Thank you.

25 COMMISSIONER BROWN: Okay. We'll take about a

1 five-minute break and reconvene at 11:20.

2 (Brief recess.)

3 COMMISSIONER BROWN: All right. We will go
4 back on the record at this time.

5 Ms. Ponder, your one and only witness.

6 MS. PONDER: Yes, thank you.

7 COMMISSIONER BROWN: Confirm that he is sworn
8 in, please.

9 EXAMINATION

10 BY MS. PONDER:

11 Q Good morning.

12 A Morning.

13 Q Mr. Smith, you were sworn in earlier today; is
14 that correct?

15 A That's correct.

16 Q Okay. Can you please state your name and
17 address for the record, please.

18 A My name is Ralph C. Smith. My address is
19 Larkin & Associates, PLLC, 15728 Farmington Road,
20 Lavonia, MI 48154.

21 Q And did you cause to be prefiled -- to be
22 prefiled testimonies in the 51, 52, 53, and 54 dockets?

23 A Yes, I did.

24 Q Do you have any corrections to these
25 testimonies?

1 A No, I do not.

2 **Q And if I were to ask you the same questions**
3 **today, would your answers be the same?**

4 A Yes, they would.

5 MS. PONDER: I would like to move the prefiled
6 testimonies into the record as though read for the
7 51, 52, 53, and 54 dockets.

8 COMMISSIONER BROWN: Seeing no objection, we
9 will go ahead and enter into the record as though
10 read Mr. Smith's prefiled testimony in the 51, 52,
11 53, and 54 dockets.

12 (Whereupon, the prefiled direct testimony of
13 Witness Smith was entered into the record of
14 Docket No. 20180051-GU as though read.)

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DIRECT TESTIMONY**OF****RALPH SMITH**

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

20180051-GU

1 **I. INTRODUCTION**2 **Q. WHAT ARE YOUR NAME, OCCUPATION, AND BUSINESS ADDRESS?**

3 A. My name is Ralph Smith. I am a Certified Public Accountant licensed in the State of
4 Michigan and a senior regulatory consultant at the firm Larkin & Associates, PLLC,
5 Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan,
6 48154.

7

8 **Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES, PLLC.**

9 A. Larkin & Associates, PLLC, ("Larkin") is a Certified Public Accounting and Regulatory
10 Consulting Firm. The firm performs independent regulatory consulting primarily for
11 public service/utility commission staffs and consumer interest groups (public counsels,
12 public advocates, consumer counsels, attorneys general, etc.). Larkin has extensive
13 experience in the utility regulatory field as expert witnesses in over 600 regulatory
14 proceedings, including numerous electric, water and wastewater, gas and telephone utility
15 cases.

16

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC**
2 **SERVICE COMMISSION?**

3 A. Yes, I have testified before the Florida Public Service Commission ("FPSC" or
4 "Commission") previously. I have also testified before several other state regulatory
5 commissions.

6

7 **Q. HAVE YOU PREPARED AN EXHIBIT DESCRIBING YOUR QUALIFICATIONS**
8 **AND EXPERIENCE?**

9 A. Yes. I have attached Exhibit RCS-1, which is a summary of my regulatory experience and
10 qualifications.

11

12 **Q. ON WHOSE BEHALF ARE YOU APPEARING?**

13 A. Larkin & Associates, PLLC, was retained by the Florida Office of Public Counsel ("OPC")
14 to review the impacts on public utility revenue requirements due to the Tax Cuts and Jobs
15 Act of 2017 ("TCJA" or "2017 Tax Act"). My testimony addresses the impacts of the
16 TCJA on Florida Public Utilities Company ("FPUC-Gas" or "Company") on behalf of the
17 OPC. Accordingly, I am appearing on behalf of the Citizens of the State of Florida.

18

19 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

20 A. I am presenting OPC's recommendations regarding certain aspects of the TCJA impacts on
21 the Company. I address TCJA impacts on Florida Division of Chesapeake Utilities
22 Corporation d/b/a Central Florida Gas ("Chesapeake"), Indiantown and Fort Meade, the
23 Company's affiliated gas distribution utility operations in separately filed testimony
24 (collectively, the four affiliated gas distribution utilities are referred to as the
25 "Companies"). In this testimony, I address TCJA impacts on FPUC-Gas.

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Q. WHAT INFORMATION DID YOU REVIEW IN PREPARATION OF YOUR TESTIMONY?

A. I reviewed each Company's respective filing, including the direct testimony and exhibits, and the affiliated gas Companies' direct testimony and exhibits. This review includes the revised and supplemental direct testimony and exhibits filed by the Companies on August 27, 2018. I also reviewed the Companies' responses to OPC's formal and informal discovery and other materials pertaining to the TCJA and its impacts on the Companies. In addition, I reviewed Rule 25-14.011, Florida Administrative Code ("F.A.C."), concerning procedures for processing requests for rulings to be filed with the Internal Revenue Service ("IRS").

Q. PLEASE DESCRIBE HOW THE REMAINDER OF YOUR TESTIMONY IS ORGANIZED.

A. After this introduction (Section I), I address the TCJA impacts related to each of the following issues:

- In Section II, I address the amount and recommended treatment of Protected and Unprotected Excess Accumulated Deferred Income Taxes ("EADIT").
- In Section III, I address the amount and recommended treatment of 2018 income tax savings in base rates related to the reduction in the federal income tax rate to 21 percent.
- In Section IV, I address TCJA savings related to the Company's Gas Reliability Infrastructure Program ("GRIP").
- In Section V, I address whether a Private Letter Ruling ("PLR") should be required for the Companies, and issues related to a PLR request.

1

2 **II. QUANTIFICATION, CLASSIFICATION AND APPLICATION OF**
3 **EXCESS ACCUMULATED DEFERRED INCOME TAXES**

4 **Q. WHAT ARE ACCUMULATED DEFERRED INCOME TAXES ("ADIT")?**

5 A. ADIT is a source of cost-free capital to reflect that the utility collects money from
6 ratepayers for Deferred Income Tax Expense and holds onto that money prior to eventually
7 paying the income taxes to the government. ADIT results from differences between book
8 and tax accounting. ADIT is referred to as Accumulated Deferred Income Taxes to
9 recognize that these balances typically build up (or accumulate) over time, e.g., as tax
10 deductions exceed corresponding book expense. One primary source of ADIT results from
11 claiming accelerated tax deductions. The tax depreciation deductions on public utility
12 property typically occur on an accelerated basis (i.e., method differences) and over a
13 shorter period (i.e., life differences) than book depreciation accruals relating to the original
14 cost of the public utility property. These types of differences between book and tax
15 depreciation are referred to as "method/life" differences. Unlike many other types of book-
16 tax differences, the tax depreciation "method/life" differences are subject to normalization
17 requirements under Sections 167 and 168 of the Internal Revenue Codes.

18

19 **Q. WHAT ARE "EXCESS" ACCUMULATED DEFERRED INCOME TAXES**
20 **("EXCESS ADIT" OR "EADIT")?**

21 A. Regulated public utilities will be required to identify the portions of their ADIT balances
22 that represent "excess" ADIT based on recalculations using the difference between the old
23 federal income tax ("FIT") rate (typically 35%) under which the ADIT was originally
24 accumulated and the new federal corporate income tax rate of 21% provided for in the
25 TCJA. Basically, the utility's ADIT must be revalued at the new FIT rate (as if it had

1 always been applicable) and the amounts that have been accumulated using the federal
2 income tax rates that are higher than the current 21% flat rate will represent "excess" ADIT.

3
4 **Q. WHAT AMOUNT OF EADIT DOES FPUC-GAS SHOW AS OF MARCH 31, 2018?**

5 A. In its May 31, 2018 filing, FPUC-Gas shows EADIT of \$24,716,879, of which \$21,799,999
6 is protected and \$2,916,880 is unprotected. In its August 27, 2018 filing, the Company
7 shows on its Exhibit NGMD-1 revised a regulatory liability for EADIT of \$25,581,776
8 (Dewey testimony page 5, line 11 indicates \$25,401,688), of which \$21,767,953 is a
9 regulatory liability for Protected EADIT and \$3,793,823 is a regulatory liability for
10 Unprotected EADIT. The Company continues to describe the amounts of EADIT liability
11 as estimated, and indicates that its measurement and accounting for the impact of the tax
12 law change will be completed on or before December 22, 2018, citing Securities and
13 Exchange ("SEC") Staff Accounting Bulletin 118. The Company indicates that per SEC
14 Staff Accounting Bulletin 118 guidance, if information is not yet available or complete, a
15 one-year period in which to complete the required analysis and accounting is permitted.

16 The amounts listed above include the "gross up" amount. The EADIT resulting
17 from the tax rate change is increased or "grossed up" for the current income tax rate. The
18 "grossed up" amount of the EADIT regulatory liability (or asset) will then be amortized
19 and subject to income taxes at the current rate; therefore, the net income impact equals the
20 amortized tax benefit.

21
22 **Q. WHAT ITEMS CHANGED BETWEEN THE VERSION OF THE COMPANY
23 EXHIBIT FILED ON MAY 31, 2018 AND THE EXHIBIT NGMD-1 REVISED?**

24 A. Company witness Dewey addresses the changes at pages 3-5 of his August 27, 2018
25 testimony. The lines on Exhibit NGMD-1 Revised that were changed by the Company

1 included "Depreciation," "Cost of Removal," and "Repairs Deduction." The changes relate
2 to periods in which ADIT was accumulated prior to the Company's tax software being
3 implemented in 2015. After the pre-software implementation ADIT amounts were
4 identified, the EADIT related to "Cost of Removal" was moved from the "Protected"
5 category into the category labeled as "Unprotected Plant." The result of these revisions
6 was to increase the Protected EADIT liability and to decrease the Unprotected EADIT
7 liability.

8
9 **Q. HOW DO IRS NORMALIZATION REQUIREMENTS AFFECT THE**
10 **CATEGORIZATION OF ADIT AND EXCESS ADIT?**

11 A. IRS normalization requirements will apply to the portion of the property-related ADIT that
12 relates to the use of accelerated tax depreciation (including bonus tax depreciation). This
13 will result in two general categories of excess ADIT: (1) "protected" (i.e., it is related to
14 the use of accelerated tax depreciation and is subject to the normalization requirements)
15 and (2) "unprotected" property and non-property related excess ADIT, which is not subject
16 to normalization requirements and for which the amortization or application is up to the
17 discretion of the Commission.

18
19 **Q. HOW DOES THE CATEGORIZATION OF "PROTECTED" OR**
20 **"UNPROTECTED" AFFECT THE AMORTIZATION OF THE EADIT?**

21 A. The 2017 Tax Act provides that the Average Rate Assumption Method ("ARAM") must
22 be used for the protected portion of the EADIT. The flow back of the "protected" excess
23 ADIT, therefore, must follow the prescribed method to comply with normalization
24 requirements. In contrast, the flow back of the unprotected portion of the excess ADIT
25 will be up to the discretion of the Commission. Unprotected ADIT is not subject to

1 normalization requirements. The unprotected ADIT will be revalued at the lower 21% tax
2 rate, creating balances of excess unprotected ADIT that can be flowed back to customers
3 over amortization periods to be determined by the Commission, or applied in some other
4 manner to be determined by the Commission (e.g., such as for the recovery of regulatory
5 assets).

6
7 **Q. HOW DOES FPUC-GAS CLASSIFY THE EXCESS ADIT BETWEEN THE**
8 **“PROTECTED” AND “UNPROTECTED” CATEGORIES?**

9 A. FPUC-Gas filed an update on August 27, 2018 in which it reclassifies EADIT related to
10 the cost of removal from “protected” (as per FPUC-Gas’s original May 31, 2018 filing)
11 into “unprotected.” As a result of the reclassification, the Company now shows the
12 following on its Exhibit NGMD-1 Revised for FPUC-Gas:

- 13 • A total regulatory liability for EADIT of \$25,561,776,
- 14 • A regulatory liability for Protected EADIT of \$21,767,953,
- 15 • A regulatory liability for "Unprotected Plant" EADIT of \$6,520,702, and
- 16 • A regulatory asset for "Unprotected Non-Plant" EADIT of \$2,726,878.
- 17 • A net regulatory liability for "Unprotected" EADIT of \$3,793,824.

18
19 Additionally, on Exhibit NGMD-2 Revised, the Company shows the following for
20 EADIT regulatory liability or asset amounts for the Common Division:

- 21 • A net regulatory asset for Unprotected EADIT of \$354,178¹ consisting of:
 - 22 ○ A regulatory liability for Protected EADIT of \$416,016
 - 23 ○ A regulatory asset for Unprotected EADIT of \$770,194.

¹ The result is an estimated regulatory asset of \$354,178 of which \$160,088 is allocated to Florida division. Dewey testimony, page 3.

1 The allocated Common Division amounts to FPUC-Gas are shown on Company
2 Exhibit NGMC-1 Revised as follows:

- 3 • A net regulatory asset for Unprotected EADIT of \$160,088 consisting of:
 - 4 ○ A regulatory liability for Protected EADIT of \$188,039
 - 5 ○ A regulatory asset for Unprotected EADIT of \$348,121.

6
7 **Q. DO YOU AGREE WITH FPUC-GAS'S CLASSIFICATION OF THE EADIT**
8 **BETWEEN THE "PROTECTED" AND "UNPROTECTED" CATEGORIES?**

9 A. I have no disagreement with the Company's updated classification of EADIT. However, I
10 note that the guidance provided in the TCJA and in previous IRS rulings presents some
11 degree of uncertainty as to the classification of the EADIT related to at least one of the
12 large book-tax differences, specifically to the EADIT relating to cost of removal/negative
13 net salvage.

14
15 **Q. WHAT DOES THE COMPANY PROPOSE FOR THE AMORTIZATION OF THE**
16 **EADIT?**

17 A. As described by Company witness Cassel in his August 27, 2018 Revised Direct Testimony
18 at pages 5 and 6 and as shown on his Exhibit NGMC-2 Revised, the Company proposes
19 the following:

- 20 • That the \$6,518,569 EADIT liability associated with the acquisition adjustment
21 should be amortized at \$298,560 per year² based on the remaining amortization
22 months of the acquisition adjustment.

² This Company-proposed amortization equates to an amortization period of approximately 21.83 years (\$6,518,569/\$298,560 = 21.83).

- 1 • That the Unprotected EADIT net asset of \$3,072,874 should be amortized over 10
2 years at \$307,287 per year.
- 3 • That the Protected EADIT liability which is currently estimated by the Company
4 to be \$21,955,992 should be amortized using the IRS prescribed methodology,
5 which is estimated by the Company to flow back over 26 years at approximately
6 \$844,461 per year.

7 The Company proposes to retain the estimated annual amount of Protected EADIT liability
8 amortization of \$844,461 and the \$307,287 per year Unprotected EADIT net asset
9 amortization for a net benefit amount to be retained by the Company of \$537,174 instead
10 of refunding these monies to its customers.

11

12 **Q. WHAT IS THE APPROPRIATE DISPOSITION OF THE PROTECTED EADIT?**

13 A. The protected EADIT should be reversed using an ARAM if the utility has the available
14 information to calculate the ARAM, or via another appropriate method that complies with
15 normalization requirements, if the Company does not have the information to compute the
16 ARAM.

17

18 **Q. ARE YOU CONTESTING THE AMOUNTS ASSOCIATED WITH THE**
19 **COMPANY'S PROPOSED EADIT AMORTIZATIONS?**

20 A. No. The Company has indicated that its EADIT amounts are estimates and are subject to
21 correction by December 22, 2018. I have accepted the Company's revised amounts as
22 reasonable estimates, subject to the later true up.

23

24 **Q. HOW SHOULD THE AMORTIZATION OF THE EADIT RELATED TO THE**
25 **ACQUISITION ADJUSTMENT BE APPLIED?**

1 A. The Company had indicated that the \$6,518,569 EADIT liability associated with the
2 acquisition adjustment will be amortized at \$298,560 per year based on the remaining
3 amortization months of the acquisition adjustment. It should be confirmed that the
4 \$298,560 EADIT acquisition adjustment related amortization is already flowing back at
5 that rate in the Company's current base rates. If that cannot be confirmed, an adjustment
6 may need to be made.

7

8 **Q. WHAT IS THE ESTIMATED AMOUNT OF THE DEFERRED TAX PORTION OF**
9 **THE PROTECTED EADIT REGULATORY LIABILITY THAT IS NOT**
10 **ASSOCIATED WITH THE ACQUISITION ADJUSTMENT THAT FPUC-GAS IS**
11 **REQUESTING TO RETAIN?**

12 A. The estimated amount of the deferred tax portion of the protected regulatory asset that
13 FPUC-Gas is requesting to be retained is approximately \$838,462 per year over 26 years.

14

15 **Q. WHAT IS THE ESTIMATED AMOUNT OF THE DEFERRED TAX PORTION OF**
16 **THE UNPROTECTED REGULATORY ASSET THAT IS NOT ASSOCIATED**
17 **WITH THE ACQUISITION ADJUSTMENT THAT FPUC-GAS IS REQUESTING**
18 **TO RETAIN?**

19 A. The estimated amount of the deferred tax portion of the unprotected regulatory asset that
20 is not associated with the acquisition adjustment is approximately \$291,688 per year over
21 10 years.

22

23 **Q. WHAT IS THE TAX BENEFIT ARISING FROM THE EADIT THAT FPUC-GAS**
24 **REQUESTS TO BE RETAINED?**

1 A. The net gross-up tax benefit arising from the EADIT amortization that FPUC-Gas proposes
2 to retain is approximately \$537,174 annually.

3

4 **Q. SHOULD FPUC-GAS UPDATE THE ESTIMATED TAX BENEFIT TO BE**
5 **CONSISTENT WITH ANY ADJUSTMENTS TO THOSE ESTIMATES**
6 **THROUGH DECEMBER 22, 2018? IF SO, HOW SHOULD IT BE HANDLED?**

7 A. Yes. Adjustments or corrections to the amounts should be addressed in a true-up filing.

8

9 **Q. ARE YOU CONTESTING THE COMPANY'S PROPOSAL TO RETAIN THE NET**
10 **BENEFIT OF THE EADIT AMORTIZATION?**

11 A. Yes, I am. The estimated annual amount of Protected EADIT liability amortization of
12 \$844,461 net of the \$307,287 per year Unprotected EADIT net asset amortization produces
13 an estimated net benefit amount of \$537,174, which should be returned to customers via a
14 base rate reduction. This net EADIT amortization amount can be trued-up if needed by
15 December 22, 2018. This contrasts with the Company's proposal to retain the full net
16 benefit amount of \$537,174.

17

18 **III. 2018 INCOME TAX SAVINGS IN BASE RATES RELATED TO THE**
19 **REDUCTION IN THE FEDERAL INCOME TAX RATE TO 21**
20 **PERCENT.**

21 **Q. HOW MUCH 2018 INCOME TAX SAVINGS FROM BASE RATES HAS THE**
22 **COMPANY IDENTIFIED?**

23 A. Company witness Cassel's August 27, 2018 Revised Direct Testimony at page 4 identifies
24 the amount of base rate savings as \$1,141,134.

25

1 **Q. WHAT TREATMENT HAS THE COMPANY PROPOSED FOR THE 2018 BASE**
2 **RATE INCOME TAX SAVINGS?**

3 A. Mr. Cassel has indicated that, because the Company is not over-earning, the Company
4 wants to retain the full amount of the annual TCJA base rate savings.
5

6 **Q. IS THE FACT THAT FPUC-GAS IS NOT OVER-EARNING A REASON TO**
7 **ALLOW THE COMPANY TO RETAIN THE TCJA BASE RATE SAVINGS?**

8 A. No, it is not. The fact that a particular utility, such as FPUC-Gas, may not be earning its
9 most recent authorized rate of return is not a convincing reason to disregard any regulatory
10 liabilities related to the accumulation of TCJA-based savings. The federal tax reform was
11 an extraordinary, one-time event that was beyond the control of utility management. The
12 utilities have sought single-issue ratemaking for events beyond the utilities' control for
13 other types of costs, typically ones that fluctuate or increase between utility rate cases, to
14 the detriment of consumers.
15

16 **Q. SHOULD THE 2018 INCOME TAX SAVINGS BE RETAINED BY THE**
17 **COMPANY?**

18 A. No, they should not. The 2018 base rate income tax savings should be applied for the
19 benefit of customers through a base rate reduction. According to the Florida Supreme
20 Court in Reedy Creek Co. v. Fla. Public Serv. Comm., 418 So. 2d. 249, 254(1982), "A
21 change in a tax law should no [sic] result in a 'windfall' to a utility, but in a refund to the
22 customer who paid the revenue that translated into the tax saving." The Commission
23 should account for lower federal tax rates in 2018 and beyond and require that such TCJA
24 savings, including the 2018 base rate savings, be applied for the benefit of the utility's
25 ratepayers through a permanent base rate reduction.

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IV. TCJA SAVINGS RELATED TO THE COMPANY'S GAS RELIABILITY INFRASTRUCTURE PROGRAM ("GRIP").

Q. HAS THE COMPANY IDENTIFIED TCJA SAVINGS RELATED TO ITS GAS RELIABILITY INFRASTRUCTURE PROGRAM ("GRIP")?

A. Yes. Mr. Cassel's August 27, 2018 Revised Direct Testimony at page 7 addresses the impacts of the TCJA on the Company's GRIP. He indicates the Company expects 2018 tax savings of \$1,040,141, as shown on his Exhibit NGMC-2, would accumulate between the Jurisdictional Date and the date that GRIP rates will be charged on customer bills (January 1, 2019). The Company proposes to flow this benefit back to customers by incorporating it as an over-recovery in its 2019 GRIP projection, which would have the effect of lowering customer GRIP surcharges by the amount of the benefit.

At page 7, he also addresses the GRIP impact for periods 2019 and beyond. He indicates the Company would apply the new, lower 21 percent federal income tax rate into its 2019 GRIP surcharge projections and future projections, which he estimates will reduce the annual GRIP revenue amount by the annual tax savings of approximately \$1.2 million.

Q. DO YOU AGREE WITH THE COMPANY'S PROPOSALS FOR THE GRIP-RELATED TCJA SAVINGS?

A. Yes, I do. The Company proposes to flow through the GRIP-related TCJA savings to customers through its GRIP surcharge filings. The two pieces of GRIP-related TCJA savings would pass the benefit of the new, lower federal income tax rate directly to FPUC-Gas' customers.

1 Q. SHOULD THE TAX BENEFITS DIRECTLY ASSOCIATED WITH THE GRIP
2 PROGRAM BE PASSED ON TO CUSTOMERS THROUGH FUTURE GRIP
3 SURCHARGES?

4 A. Yes. The tax benefits associated with the GRIP should be passed on to customers as
5 reductions to GRIP surcharges.

6

7 Q. DO YOU AGREE THAT THE GRIP RELATED TCJA-SAVINGS SHOULD BE
8 FLOWED THROUGH TO CUSTOMERS IN THE GRIP SURCHARGE FILINGS?

9 A. Yes.

10

11 V. WHETHER A PRIVATE LETTER RULING ("PLR") SHOULD BE
12 REQUIRED FOR THE COMPANIES, AND ISSUES RELATED TO A
13 PLR REQUEST.

14 Q. DID THE COMPANY'S AUGUST 27, 2018 REVISED FILING CONTAIN A
15 RECLASSIFICATION OF EADIT RELATED TO COST-OF-REMOVAL FROM
16 "PROTECTED" TO "UNPROTECTED"?

17 A. Yes. One of the items revised in the Company's August 27, 2018 filing was the
18 classification of EADIT related to the cost of removal. In the Company's original May 31,
19 2018 application, EADIT related to cost of removal was classified as "protected." In the
20 Company's August 27, 2018 filing, an updated amount of EADIT related to cost of removal
21 is now classified as "unprotected."

22

23 Q. DO YOU HAVE AN OPINION AS TO WHETHER THE EADIT RELATED TO
24 COST OF REMOVAL/NEGATIVE NET SALVAGE IS "PROTECTED" OR
25 "UNPROTECTED"?

1 A. Yes, I do. Based on currently available guidance, it is my opinion that the EADIT related
2 to cost of removal/negative net salvage is "unprotected." This is because the tax deduction
3 for cost of removal is not addressed under §167 or §168 of the Internal Revenue Code
4 ("IRC" or "Code"), which are the sections pertaining to the use of accelerated tax
5 depreciation and the sections which contain the normalization requirements pertaining to
6 the continued use of accelerated tax depreciation. Deductions provided for under other
7 sections of the Code are not subject to the normalization requirements associated with the
8 utility's ability to continue to use accelerated depreciation for federal income tax purposes.

9

10 **Q. IS THERE SOME UNCERTAINTY IN THIS AREA?**

11 A. Yes, there is. The comparison of utility book and tax depreciation for purposes of tracking
12 the method/life and other differences can be very complex. Utility book depreciation rates
13 typically include a component for negative net salvage (as well as for the recovery of
14 original cost over the estimated useful life of the assets). The normalization process
15 involves comparing book and tax depreciation; however, the calculations can be very
16 complex. Such calculations are typically done by larger utilities using specialized
17 software, such as PowerPlan and PowerTax, and the proper application can require
18 significant additional analytical work by the utility and the vendor. Since the comparison
19 of book and tax depreciation involves complex calculations and utility book depreciation
20 typically includes an element for negative net salvage, some jurisdictions (e.g., New York)
21 and some Florida utilities (e.g., Duke Energy Florida ("DEF")) have raised concerns about
22 the cost of removal/negative net salvage component of book depreciation and the risks
23 presented for potential normalization violations. For example, DEF appears to be taking a
24 different position than Tampa Electric Company ("TECO") and Peoples' Gas System

1 (“PGS”) concerning the treatment of cost of removal/negative net salvage and has proposed
2 to treat that item as "protected," pending receipt of additional guidance.

3
4 **Q. SHOULD FPUC-GAS SEEK A PLR FROM THE IRS REGARDING ITS**
5 **CLASSIFICATION OF THE EXCESS ADIT RELATING TO COST OF**
6 **REMOVAL/NEGATIVE NET SALVAGE AS “UNPROTECTED”?**

7 A. Possibly, yes; however, a Commission decision concerning whether to require FPUC to
8 seek a PLR does not appear to be as urgent an issue as it is with respect to some of the
9 other, larger Florida regulated public utilities. Due to FPUC-Gas’s relatively small size
10 compared to some of the other Florida regulated utilities, I would recommend that the
11 larger Florida utilities (e.g., such as TECO and PGS) first seek PLRs concerning the
12 classification of EADIT related to cost of removal/negative net salvage as “unprotected”.
13 It may be that the guidance provided by the PLRs issued to the larger utilities will be
14 sufficiently clear that FPUC-Gas and its affiliates might not need to obtain their own PLR.
15 Although obtaining a PLR related to the utility’s own specific fact situation provides more
16 definitive assurance, it might not be necessary for FPUC-Gas and its Florida utility
17 affiliates (Chesapeake, Indiantown, and Fort Meade) to seek their own specific PLRs.

18
19 **Q. IF FPUC-GAS SEEKS A PLR AND THE IRS RULES THEREIN (OR IN**
20 **ANOTHER PLR) THAT THE EADIT RELATING TO COST OF**
21 **REMOVAL/NEGATIVE NET SALVAGE IS TO BE TREATED AS**
22 **“PROTECTED,” WHAT PROCESS SHOULD BE FOLLOWED FOR THE**
23 **RECLASSIFICATION?**

1 A. Pending clarification of the appropriate classification of EADIT for cost of
2 removal/negative net salvage, FPUC-Gas should amortize the related EADIT using the
3 ARAM if the classification ruled by the IRS indicates this is “protected.”
4

5 **Q. HAS THE COMPANY ESTIMATED THE COST OF OBTAINING A PLR?**

6 A. Yes. At page 4 of his August 27, 2018 Supplemental Direct Testimony, Mr. Cassel
7 estimates the cost of seeking a PLR to be \$20,000 to \$50,000 and indicates the Company
8 could obtain a more firm estimate of the cost if needed. At page 5 of that testimony, he
9 proposes deferred accounting treatment for the PLR cost and amortization over four years
10 if incurred.
11

12 **Q. WHAT MECHANISM SHOULD BE UTILIZED TO AVOID THE NEGATIVE**
13 **IMPACT TO FPUC-GAS OF THE COST OF SEEKING A PLR?**

14 A. As I suggested earlier, awaiting IRS rulings from the larger Florida utilities on their
15 respective PLRs before requiring FPUC-Gas to seek a PLR will potentially avoid the need
16 for FPUC-Gas to seek its own PLR. If the PLRs for the larger Florida utilities are clear
17 and consistent in their rulings, having FPUC-Gas and its affiliates request their own PLR
18 may be unnecessary. Thus, the cost for having FPUC-Gas and its Florida affiliates request
19 a PLR does not need to be incurred at this time.
20

21 **Q. IN HIS AUGUST 27, 2018 SUPPLEMENTAL DIRECT TESTIMONY, AT PAGE 4,**
22 **MR. CASSEL PROPOSES THAT, IF A PLR REQUEST IS REQUIRED, FPUC**
23 **SHOULD BE ALLOWED TO FILE A PLR REQUEST JOINTLY WITH THE**
24 **OTHER AFFILIATED CUC ENTITIES IN FLORIDA. WOULD THAT BE A**
25 **REASONABLE ACCOMMODATION?**

1 A. Yes, it would. If the Commission determines in this proceeding, or subsequently, that a
2 PLR request should be made by FPUC-Gas on a TCJA related issue, then a combined PLR
3 request by the Companies may be appropriate, particularly if the facts and circumstances
4 are identical or similar with respect to the PLR request.

5

6 **VI. FINDINGS AND RECOMMENDATIONS**

7 **Q. ARE YOU RECOMMENDING ANY ADJUSTMENTS TO THE COMPANY'S**
8 **QUANTIFICATIONS OF THE TCJA IMPACTS AT THIS TIME?**

9 A. No, I am not. The Companies' quantifications do not appear to be unreasonable for the
10 purposes of estimating the one-time annual revenue requirement reduction and EADIT
11 related to the TCJA.

12

13 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSALS TO FLOW GRIP-**
14 **RELATED TCJA SAVINGS THROUGH ITS GRIP SURCHARGE FILINGS?**

15 A. Yes.

16

17 **Q. ARE YOU RECOMMENDING ANY DIFFERENT REGULATORY**
18 **TREATMENTS FOR THE BASE RATE TCJA SAVINGS?**

19 A. Yes, I am. The regulatory liability for the base rate TCJA savings should be applied for
20 the benefit of customers as a permanent base rate reduction. This contrasts with the
21 Company's proposal to retain such savings. Additionally, the net annual amortization of
22 the Protected and Unprotected EADIT that is not associated with the acquisition
23 adjustment, estimated by the Company to be approximately \$537,174 annually, should be
24 applied for the benefit of customers as a rate reduction, rather than being retained by the
25 Company.

1

2 **Q. DOES THIS COMPLETE YOUR PREFILED TESTIMONY?**

3 **A. Yes, it does.**

1 (Whereupon, the prefilled revised direct
2 testimony of Witness Smith was entered into the
3 record of Docket No. 20180052-GU as though read.)

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DIRECT TESTIMONY**OF****RALPH SMITH**

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

20180052-GU

1 **I. INTRODUCTION**2 **Q. WHAT ARE YOUR NAME, OCCUPATION, AND BUSINESS ADDRESS?**

3 A. My name is Ralph Smith. I am a Certified Public Accountant licensed in the State of
4 Michigan and a senior regulatory consultant at the firm Larkin & Associates, PLLC,
5 Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan,
6 48154.

7

8 **Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES, PLLC.**

9 A. Larkin & Associates, PLLC, ("Larkin") is a Certified Public Accounting and Regulatory
10 Consulting Firm. The firm performs independent regulatory consulting primarily for
11 public service/utility commission staffs and consumer interest groups (public counsels,
12 public advocates, consumer counsels, attorneys general, etc.). Larkin has extensive
13 experience in the utility regulatory field as expert witnesses in over 600 regulatory
14 proceedings, including numerous electric, water and wastewater, gas and telephone utility
15 cases.

16

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC**
2 **SERVICE COMMISSION?**

3 A. Yes, I have testified before the Florida Public Service Commission (“FPSC” or
4 “Commission”) previously. I have also testified before several other state regulatory
5 commissions.

6

7 **Q. HAVE YOU PREPARED AN EXHIBIT DESCRIBING YOUR QUALIFICATIONS**
8 **AND EXPERIENCE?**

9 A. Yes. I have attached Exhibit RCS-1, which is a summary of my regulatory experience and
10 qualifications.

11

12 **Q. ON WHOSE BEHALF ARE YOU APPEARING?**

13 A. Larkin & Associates, PLLC, was retained by the Florida Office of Public Counsel (“OPC”)
14 to review the impacts on public utility revenue requirements due to the Tax Cuts and Jobs
15 Act of 2017 (“TCJA” or “2017 Tax Act”). My testimony addresses the impacts of the
16 TCJA on Florida Public Utilities Company - Indiantown Division (“Indiantown” or
17 “FPUC-Indiantown”) on behalf of the OPC. Accordingly, I am appearing on behalf of the
18 Citizens of the State of Florida.

19

20 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

21 A. I am presenting OPC's recommendations regarding certain aspects of the TCJA impacts on
22 the Company. I address TCJA impacts on Florida Public Utilities Company (“FPUC-
23 Gas”), Chesapeake Utilities Corporation Florida Division (“Chesapeake”), and Fort
24 Meade, the Company’s affiliated gas distribution utility operations in separately filed

1 testimony (collectively, the four affiliated gas distribution utilities are referred to as the
2 “Companies”). In this testimony, I address TCJA impacts on Indiantown.

3

4 **Q. WHAT INFORMATION DID YOU REVIEW IN PREPARATION OF YOUR**
5 **TESTIMONY?**

6 A. I reviewed each Company’s respective filing including the direct testimony and exhibits,
7 and the affiliated gas Companies’ direct testimony and exhibits. This review included the
8 revised and supplemental direct testimony and exhibits filed by the Companies on August
9 27, 2018. I also reviewed the Companies’ responses to OPC’s formal and informal
10 discovery and other materials pertaining to the TCJA and its impacts on the Companies.
11 In addition, I reviewed Rule 25-14.011, Florida Administrative Code (“F.A.C.”),
12 concerning procedures for processing requests for rulings to be filed with the Internal
13 Revenue Service (“IRS”).

14

15 **Q. PLEASE DESCRIBE HOW THE REMAINDER OF YOUR TESTIMONY IS**
16 **ORGANIZED.**

17 A. After this introduction (Section I), I address the TCJA impacts related to each of the
18 following issues:

- 19
- 20 • In Section II, I address the amount and recommended treatment of Protected and
Unprotected Excess Accumulated Deferred Income Taxes ("EADIT").
 - 21 • In Section III, I address the amount and recommended treatment of 2018 income
22 tax savings in base rates related to the reduction in the federal income tax rate to 21
23 percent.
 - 24 • In Section IV, I address whether a Private Letter Ruling ("PLR") should be required
25 for the Companies, and issues related to a PLR request.

- In Section V, I summarize my findings and recommendations.

II. QUANTIFICATION, CLASSIFICATION, AND APPLICATION OF EXCESS ACCUMULATED DEFERRED INCOME TAXES

Q. WHAT ARE ACCUMULATED DEFERRED INCOME TAXES ("ADIT")?

A. ADIT is a source of cost-free capital to reflect that the utility collects money from ratepayers for Deferred Income Tax Expense and holds onto that money prior to eventually paying the income taxes to the government. ADIT results from differences between book and tax accounting. ADIT is referred to as Accumulated Deferred Income Taxes to recognize that these balances typically build up (or accumulate) over time, e.g., as tax deductions exceed corresponding book expense. One primary source of ADIT results from claiming accelerated tax deductions. The tax depreciation deductions on public utility property typically occur on an accelerated basis (i.e., method differences) and over a shorter period (i.e., life differences) than book depreciation accruals relating to the original cost of the public utility property. These types of differences between book and tax depreciation are referred to as “method/life” differences. Unlike many other types of book-tax differences, the tax depreciation “method/life” differences are subject to normalization requirements under Sections 167 and 168 of the Internal Revenue Codes.

Q. WHAT IS "EXCESS" ACCUMULATED DEFERRED INCOME TAXES ("EXCESS ADIT" OR "EADIT")?

A. Regulated public utilities will be required to identify the portions of their ADIT balances that represent "excess" ADIT based on recalculations using the difference between the old federal income tax (“FIT”) rate (typically 35%) under which the ADIT was originally accumulated and the new federal corporate income tax rate of 21% provided for in the TCJA. Basically, the utility’s ADIT must be revalued at the new FIT rate (as if it had

1 always been applicable) and the amounts that have been accumulated using federal income
2 tax rates that were higher than the current 21% flat rate will represent "excess" ADIT.

3

4 **Q. WHAT AMOUNT OF EADIT DOES INDIANTOWN SHOW AS OF MARCH 31,**
5 **2018?**

6 A. In its June 1, 2018 filing, on Company Exhibit FIMC-1, Indiantown shows a net EADIT
7 liability of \$214,786, of which \$188,337 is protected and \$26,449 is unprotected.¹ In its
8 August 27, 2018 filing, on Exhibit FIMC-1 Revised, the Company shows a net regulatory
9 liability for EADIT of \$214,785, of which \$221,269 is a regulatory liability for Protected
10 EADIT and \$9,484 is a regulatory asset for Unprotected EADIT. The Company continues
11 to describe the amounts of EADIT liability as estimated, and indicates that its measurement
12 and accounting for the impact of the tax law change will be complete on or before
13 December 22, 2018, citing Securities and Exchange ("SEC") Staff Accounting Bulletin
14 118. The Company indicates that per SEC Staff Accounting Bulletin 118 guidance, if
15 information is not yet available or complete, a one-year period in which to complete the
16 required analysis and accounting is permitted.

17 The amounts listed above include the "gross up" amount. The EADIT resulting
18 from the tax rate change is increased or "grossed up" for the current income tax rate. The
19 "grossed up" amount of the EADIT regulatory liability (or asset) will then be amortized
20 and subject to income taxes at the current rate; therefore, the net income impact equals the
21 amortized tax benefit.

22

23 **Q. WHAT ITEMS CHANGED BETWEEN THE VERSION OF THE COMPANY**
24 **EXHIBIT FILED ON JUNE 1, 2018 AND THE EXHIBIT FIMD-1 REVISED?**

¹ Amounts do not add exactly due to rounding.

1 A. Company witness Dewey addresses the changes at pages 3-4 of his August 27, 2018
2 testimony. The lines on Exhibit FIMD-1 Revised that were changed by the Company
3 included "Depreciation," "Cost of Removal," and "Repairs Deduction." The changes relate
4 to periods in which ADIT was accumulated prior to the Company's tax software being
5 implemented in 2015. After the pre-software implementation ADIT amounts were
6 identified, the EADIT related to "Cost of Removal" was moved from the "Protected"
7 category into the category labeled as "Unprotected Plant." The result of these revisions
8 was to increase the Protected EADIT liability and to decrease the Unprotected EADIT
9 liability.

10

11 **Q. HOW DO IRS NORMALIZATION REQUIREMENTS AFFECT THE**
12 **CATEGORIZATION OF ADIT AND EXCESS ADIT?**

13 A. IRS normalization requirements will apply to the portion of the property-related ADIT that
14 relates to the use of accelerated tax depreciation (including bonus tax depreciation). This
15 will result in two general categories of excess ADIT: (1) "protected" (i.e., is related to the
16 use of accelerated tax depreciation and is subject to the normalization requirements) and
17 (2) "unprotected" property and non-property related excess ADIT, which is not subject to
18 normalization requirements and for which the amortization or application is up to the
19 discretion of the Commission.

20

21 **Q. HOW DOES THE CATEGORIZATION OF “PROTECTED” OR**
22 **“UNPROTECTED” AFFECT THE AMORTIZATION OF THE EADIT?**

23 A. The 2017 Tax Act provides that the Average Rate Assumption Method (“ARAM”) must
24 be used for the protected portion of the EADIT. The flow back of the “protected” excess
25 ADIT, therefore, must follow the prescribed method to comply with normalization

1 requirements. In contrast, the flow back of the unprotected portion of the excess ADIT
2 will be up to the discretion of the Commission. Unprotected ADIT is not subject to
3 normalization requirements. The unprotected ADIT will be revalued at the lower 21% tax
4 rate, creating balances of excess unprotected ADIT that can be flowed back to customers
5 over amortization periods to be determined by the Commission, or applied in some other
6 manner to be determined by the Commission (e.g., such as for the recovery of regulatory
7 assets).

8

9 **Q. HOW DOES INDIANTOWN CLASSIFY THE EXCESS ADIT BETWEEN THE**
10 **“PROTECTED” AND “UNPROTECTED” CATEGORIES?**

11 A. Indiantown filed an update on August 27, 2018 in which it reclassifies EADIT related to
12 the cost of removal from “protected” (as per Indiantown’s original June 1, 2018 filing) into
13 “unprotected.” As a result of the reclassification, the Company now shows the following
14 on its Exhibit FIMD-1 Revised for Indiantown:

- 15 • A net regulatory liability for EADIT of \$216,202,
- 16 • A regulatory liability for Protected EADIT of \$219,605,
- 17 • A regulatory asset for "Unprotected Plant" EADIT of \$31,584,
- 18 • A regulatory liability for "Unprotected Non-Plant" EADIT of \$26,181, and
- 19 • A net regulatory asset for "Unprotected" EADIT of \$3,403.

20

21 Additionally, on Exhibit FIMD-2 Revised, the Company shows the following for
22 EADIT regulatory liability or asset amounts for the Common Division before being
23 allocated to Indiantown:

- 24 • A net regulatory asset for Unprotected EADIT of \$354,178 consisting of:
 - 25 ○ A regulatory liability for Protected EADIT of \$416,016

1 ○ A regulatory asset for Unprotected EADIT of \$770,194.

2 The allocated Common Division amounts to Indiantown are shown on Company
3 Exhibit FIMC-1 Revised as follows:

4 • A net regulatory asset for Unprotected EADIT of \$1,417 consisting of:

5 ○ A regulatory liability for Protected EADIT of \$1,664

6 ○ A regulatory asset for Unprotected EADIT of \$3,081.

7

8 **Q. DO YOU AGREE WITH THE COMPANY'S CLASSIFICATION OF THE EADIT**
9 **BETWEEN THE "PROTECTED" AND "UNPROTECTED" CATEGORIES?**

10 A. I have no disagreement with the Company's updated classification of EADIT. However, I
11 note that the guidance provided in the TCJA and in previous IRS rulings presents some
12 degree of uncertainty as to the classification of the EADIT related to at least one of the
13 large book-tax differences, specifically to the EADIT relating to cost of removal/negative
14 net salvage.

15

16 **Q. WHAT DOES THE COMPANY PROPOSE FOR THE AMORTIZATION OF THE**
17 **EADIT?**

18 A. As described by Company witness Cassel in his August 27, 2018 Revised Direct Testimony
19 at pages 5 and 6 and as shown on his Exhibit FIMC-1 Revised, the Company proposes the
20 following:

21 • That the Unprotected EADIT net asset of \$6,484 should be amortized over 10 years
22 at \$648 per year.

23 • That the Protected EADIT liability which is currently estimated by the Company
24 to be \$221,269 should be amortized using the IRS prescribed methodology, which

1 is estimated by the Company to flow back over 26 years at approximately \$8,510
2 per year.

3 The Company proposes to retain the estimated annual amount of Protected EADIT liability
4 amortization of \$8,510 and the \$648 per year Unprotected EADIT net asset amortization
5 for a net benefit amount to be retained by the Company of \$7,862 instead of refunding
6 these monies to its customers.

7

8 **Q. WHAT IS THE APPROPRIATE DISPOSITION OF THE PROTECTED EADIT?**

9 A. The protected EADIT should be reversed using an ARAM if the utility has the available
10 information to calculate the ARAM, or via another appropriate method that complies with
11 normalization requirements, if the Company does not have the information to compute the
12 ARAM.

13

14 **Q. ARE YOU CONTESTING THE AMOUNTS ASSOCIATED WITH THE
15 COMPANY'S PROPOSED EADIT AMORTIZATIONS?**

16 A. No. The Company has indicated that its EADIT amounts are estimates and are subject to
17 correction by December 22, 2018. I have accepted the Company's revised amounts as
18 reasonable estimates, subject to the later true up.

19

20 **Q. WHAT IS THE TAX BENEFIT ARISING FROM THE EADIT THAT THE
21 COMPANY REQUESTS TO BE RETAINED?**

22 A. The net gross-up tax benefit arising from the EADIT amortization that the Company
23 proposes to retain is approximately \$7,862 annually.

24

1 **Q. SHOULD INDIANTOWN UPDATE THE ESTIMATED TAX BENEFIT TO BE**
2 **CONSISTENT WITH ANY ADJUSTMENTS TO THOSE ESTIMATES**
3 **THROUGH DECEMBER 22, 2018? IF SO, HOW SHOULD IT BE HANDLED?**

4 A. Yes. Adjustments or corrections to the amounts should be addressed in a true-up filing.

5

6 **Q. ARE YOU CONTESTING THE COMPANY'S PROPOSAL TO RETAIN THE NET**
7 **BENEFIT OF THE EADIT AMORTIZATION?**

8 A. Yes, I am. The estimated annual amount of Protected EADIT liability amortization of
9 \$8,510 net of the \$648 per year Unprotected EADIT net asset amortization produces an
10 estimated net benefit amount of \$7,862, which should be returned to customers via a base
11 rate reduction. This net EADIT amortization amount can be trued-up if needed by
12 December 22, 2018. This contrasts with the Company's proposal to retain the full net
13 benefit amount of \$7,862.

14

15 **III. 2018 INCOME TAX SAVINGS IN BASE RATES RELATED TO THE**
16 **REDUCTION IN THE FEDERAL INCOME TAX RATE TO 21**
17 **PERCENT**

18 **Q. HOW MUCH 2018 INCOME TAX SAVINGS FROM BASE RATES HAS THE**
19 **COMPANY IDENTIFIED?**

20 A. Company witness Cassel's August 27, 2018 Revised Direct Testimony at page 4 identifies
21 the amount of annual net tax detriment, based on its 2018 pro forma surveillance report, as
22 \$54,096.

23 **Q. WHY IS THIS AMOUNT AN ANNUAL TAX DETRIMENT?**

24 A. As shown on Company Exhibit FIMC-1 Revised, the Company projects to have negative
25 net operating income for 2018. Because of the lower federal income tax expense, the
26 amount of negative net income projected by the Company for 2018 would be larger at the

1 new 21% FIT rate than at the previous FIT rate. The larger amount of projected 2018 net
2 operating loss (i.e., negative net income) of \$40,385 is “grossed-up” by \$13,711 on
3 Company Exhibit FIMC-1 Revised to derive the Company’s estimated net detriment
4 amount of \$54,096.

5

6 **Q. WHAT TREATMENT HAS THE COMPANY PROPOSED FOR THE 2018 BASE**
7 **RATE INCOME TAX DETRIMENT?**

8 A. Mr. Cassel has indicated that, because the Company is not over-earning, the Company
9 wants to recover the full amount of its calculated annual TCJA tax detriment through the
10 Energy Conservation Cost Recovery ("ECCR") clause.

11

12 **Q. IN YOUR OPINION, IS THE FACT THAT INDIANTOWN IS NOT OVER-**
13 **EARNING A REASON TO ALLOW THE COMPANY TO RECOVER THE 2018**
14 **BASE RATE INCOME TAX DETRIMENT?**

15 A. No, it is not.

16

17 **Q. SHOULD THE AMOUNT OF THE 2018 INCOME TAX DETRIMENT BE**
18 **CHARGED TO CUSTOMERS BY THE COMPANY THROUGH THE ECCR?**

19 A. No, they should not. The estimated amount of 2018 income tax detriment does not have
20 anything to do with the ECCR and, therefore, should not be charged to ratepayers through
21 the ECCR. The federal tax reform was an extraordinary, one-time event that was beyond
22 the control of utility management. The utilities have sought single-issue ratemaking for
23 events beyond the utilities’ control for other types of costs, typically ones that fluctuate or
24 increase between utility rate cases, to the detriment of consumers.

25

1 **Q. HOW LONG HAS INDIANTOWN BEEN EARNING BELOW ITS AUTHORIZED**
2 **EARNINGS RANGE?**

3 A. Indiantown has been earning below its authorized range since 2013.
4

5 **Q. WHAT IS THE APPROPRIATE REMEDY THE UTILITY CAN SEEK IF IT IS**
6 **EARNING BELOW ITS AUTHORIZED RANGE?**

7 A. If the Company believes its base rates are insufficient to earn a fair rate of return, it has the
8 ability to file a base rate case to address the situation. The fact that a particular utility, such
9 as Indiantown, may not be earning its most recent authorized rate of return is not a
10 convincing reason to charge an estimated amount of TCJA-based tax detriment to
11 customers through the ECCR. Instead, the Company has the opportunity to request a base
12 rate increase.
13

14 **Q. SHOULD THE 2018 INCOME TAX SAVINGS BE RETAINED BY THE**
15 **COMPANY?**

16 A. No, they should not. The 2018 base rate income tax savings should be applied for the
17 benefit of customers through a base rate reduction. According to the Florida Supreme
18 Court in Reedy Creek Co. v. Fla. Public Serv. Comm., 418 So. 2d. 249, 254(1982), “A
19 change in a tax law should no [sic] result in a ‘windfall’ to a utility, but in a refund to the
20 customer who paid the revenue that translated into the tax saving.” The Commission
21 should account for lower federal tax rates in 2018 and beyond and require that such TCJA
22 savings, including the 2018 base rate savings, be applied for the benefit of the utility's
23 ratepayers through a permanent base rate reduction.
24

1 **IV. WHETHER A PRIVATE LETTER RULING ("PLR") SHOULD BE**
2 **REQUIRED FOR THE COMPANIES, AND ISSUES RELATED TO A**
3 **PLR REQUEST**

4 **Q. DID THE COMPANY'S AUGUST 27, 2018 REVISED FILING CONTAIN A**
5 **RECLASSIFICATION OF EADIT RELATED TO COST-OF-REMOVAL FROM**
6 **"PROTECTED" TO "UNPROTECTED"?**

7 A. Yes. One of the items revised in the Company's August 27, 2018 filing was the
8 classification of EADIT related to the cost of removal. In the Company's original June 1,
9 2018 application, EADIT related to cost of removal was classified as "protected." In the
10 Company's August 27, 2018 filing, an updated amount of EADIT related to cost of removal
11 is now classified as "unprotected."

12
13 **Q. DO YOU HAVE AN OPINION AS TO WHETHER THE EADIT RELATED TO**
14 **COST OF REMOVAL/NEGATIVE NET SALVAGE IS "PROTECTED" OR**
15 **"UNPROTECTED"?**

16 A. Yes, I do. Based on currently available guidance, it is my opinion that the EADIT related
17 to cost of removal/negative net salvage is "unprotected." This is because the tax deduction
18 for cost of removal is not addressed under §167 or §168 of the Internal Revenue Code
19 ("IRC" or "Code"), which are the sections pertaining to the use of accelerated tax
20 depreciation and the sections which contain the normalization requirements pertaining to
21 the continued use of accelerated tax depreciation. Deductions provided for under other
22 sections of the Code are not subject to the normalization requirements associated with the
23 utility's ability to continue to use accelerated depreciation for federal income tax purposes.

24
25 **Q. IS THERE SOME UNCERTAINTY IN THIS AREA?**

1 A. Yes, there is. The comparison of utility book and tax depreciation for purposes of tracking
2 the method/life and other differences can be very complex. Utility book depreciation rates
3 typically include a component for negative net salvage (as well as for the recovery of
4 original cost over the estimated useful life of the assets). The normalization process
5 involves comparing book and tax depreciation; however, the calculations can be very
6 complex. Such calculations are typically done by larger utilities using specialized
7 software, such as PowerPlan and PowerTax, and the proper application can require
8 significant additional analytical work by the utility and the vendor. Since the comparison
9 of book and tax depreciation involves complex calculations and utility book depreciation
10 typically includes an element for negative net salvage, some jurisdictions (e.g., New York)
11 and some Florida utilities (e.g., Duke Energy Florida (“DEF”)) have raised concerns about
12 the cost of removal/negative net salvage component of book depreciation and the risks
13 presented for potential normalization violations. For example, DEF appears to be taking a
14 different position than Tampa Electric Company (“TECO”) and Peoples’ Gas System
15 (“PGS”) concerning the treatment of cost of removal/negative net salvage and has proposed
16 to treat that item as "protected," pending receipt of additional guidance.

17

18 **Q. SHOULD THE COMPANIES SEEK A PLR FROM THE IRS REGARDING ITS**
19 **CLASSIFICATION OF THE EXCESS ADIT RELATING TO COST OF**
20 **REMOVAL/NEGATIVE NET SALVAGE AS “UNPROTECTED”?**

21 A. Possibly, yes; however, a Commission decision concerning whether to require the
22 Companies to seek a PLR does not appear to be as urgent an issue as it is with respect to
23 some of the other, larger Florida regulated public utilities. Due to the Companies' small
24 size compared to some of the other Florida regulated utilities, I would recommend that the
25 larger Florida utilities (e.g., such as TECO and PGS) first seek PLRs concerning the

1 classification of EADIT related to cost of removal/negative net salvage as “unprotected”.
2 It may be that the guidance provided by the PLRs issued to the larger utilities will be
3 sufficiently clear that Indiantown and its affiliates might not need to obtain their own PLR.
4 Although obtaining a PLR related to the utility’s own specific fact situation provides more
5 definitive assurance, it might not be necessary for Indiantown and its Florida utility
6 affiliates (FPUC-Gas, Chesapeake, and Fort Meade) to seek their own specific PLRs.

7

8 **Q. IF INDIANTOWN, ALONG WITH ITS FLORIDA UTILITY AFFILIATES,**
9 **SEEKS A PLR AND THE IRS RULES THEREIN (OR IN ANOTHER PLR) THAT**
10 **THE EADIT RELATING TO COST OF REMOVAL/NEGATIVE NET SALVAGE**
11 **IS TO BE TREATED AS “PROTECTED,” WHAT PROCESS SHOULD BE**
12 **FOLLOWED FOR THE RECLASSIFICATION?**

13 A. Pending clarification of the appropriate classification of EADIT for cost of
14 removal/negative net salvage, Indiantown should amortize the related EADIT using the
15 ARAM if the classification ruled by the IRS indicates this is “protected.”

16

17 **Q. HAS THE COMPANY ESTIMATED THE COST OF OBTAINING A PLR?**

18 A. Yes. At page 4 of his August 27, 2018 Supplemental Direct Testimony, Mr. Cassel
19 estimates the cost of seeking a PLR to be \$20,000 to \$50,000 and indicates the Companies
20 could obtain a more firm estimate of the cost if needed. At page 5 of that testimony, he
21 proposes deferred accounting treatment for the PLR cost and amortization over four years
22 if it is incurred.

23

24 **Q. WHAT MECHANISM SHOULD BE UTILIZED TO AVOID THE NEGATIVE**
25 **IMPACT TO THE COMPANIES OF THE COST OF SEEKING A PLR?**

1 A. As I suggested earlier, awaiting IRS rulings from the larger Florida utilities on their
2 respective PLRs before requiring the Companies to seek a PLR will potentially avoid the
3 need for Indiantown and its Florida public utility affiliates to seek their own PLR. If the
4 PLRs for the larger Florida utilities are clear and consistent in their rulings, having
5 Indiantown and its affiliates request their own PLR may be unnecessary. Thus, the cost
6 for having Indiantown and its Florida affiliates request a PLR does not need to be incurred
7 at this time.

8

9 **Q. IN HIS AUGUST 27, 2018 SUPPLEMENTAL DIRECT TESTIMONY, AT PAGE 4,**
10 **MR. CASSEL PROPOSES THAT, IF A PLR REQUEST IS REQUIRED,**
11 **INDIANTOWN SHOULD BE ALLOWED TO FILE A PLR REQUEST JOINTLY**
12 **WITH THE OTHER AFFILIATED CUC ENTITIES IN FLORIDA. WOULD**
13 **THAT BE A REASONABLE ACCOMMODATION?**

14 A. Yes, it would. If the Commission determines in this proceeding, or subsequently, that a
15 PLR request should be made by Indiantown on a TCJA related issue, then a combined PLR
16 request by the Companies may be appropriate, particularly if the facts and circumstances
17 are identical or similar with respect to the PLR request.

18

19 **V. FINDINGS AND RECOMMENDATIONS**

20 **Q. ARE YOU RECOMMENDING ANY ADJUSTMENTS TO THE COMPANY'S**
21 **QUANTIFICATIONS OF THE TCJA IMPACTS AT THIS TIME?**

22 A. No, I am not. The Companies' quantifications do not appear to be unreasonable for the
23 purposes of estimating the one-time annual revenue requirement reduction and EADIT
24 related to the TCJA.

25

1 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSALS TO FLOW AN**
2 **ESTIMATED AMOUNT OF TCJA DETRIMENT THROUGH ITS ECCR**
3 **SURCHARGE FILING?**

4 A. No.

5

6 **Q. ARE YOU RECOMMENDING ANY DIFFERENT REGULATORY**
7 **TREATMENTS FOR THE BASE RATE TCJA SAVINGS?**

8 A. Yes, I am. The expense increase calculated by the Company for the base rate TCJA savings
9 should be addressed in a base rate case. This contrasts with the Company's proposal to
10 charge the amount to customers via its ECCR filing. Additionally, the net annual
11 amortization of the Protected and Unprotected EADIT, estimated by the Company to be
12 approximately \$7,862 annually, should be applied for the benefit of customers as a rate
13 reduction or refund, rather than being retained by the Company.

14

15 **Q. DOES THIS COMPLETE YOUR PREFILED TESTIMONY?**

16 A. Yes, it does.

1 (Whereupon, the prefilled revised direct
2 testimony of Witness Smith was entered into the
3 record of Docket No. 20180053-GU as though read.)

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20180053-GU
Attachment A
DIRECT TESTIMONY

OF

RALPH SMITH

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

20180053-GU

1 **I. INTRODUCTION**

2 **Q. WHAT ARE YOUR NAME, OCCUPATION, AND BUSINESS ADDRESS?**

3 A. My name is Ralph Smith. I am a Certified Public Accountant licensed in the State of
4 Michigan and a senior regulatory consultant at the firm Larkin & Associates, PLLC,
5 Certified Public Accountants, with offices at 15728 Farmington Road, Livonia,
6 Michigan, 48154.

7

8 **Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES, PLLC.**

9 A. Larkin & Associates, PLLC, ("Larkin") is a Certified Public Accounting and
10 Regulatory Consulting Firm. The firm performs independent regulatory consulting
11 primarily for public service/utility commission staffs and consumer interest groups
12 (public counsels, public advocates, consumer counsels, attorneys general, etc.). Larkin
13 has extensive experience in the utility regulatory field as expert witnesses in over 600
14 regulatory proceedings, including numerous electric, water and wastewater, gas and
15 telephone utility cases.

16

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC**
2 **SERVICE COMMISSION?**

3 A. Yes, I have testified before the Florida Public Service Commission (“FPSC” or
4 “Commission”) previously. I have also testified before several other state regulatory
5 commissions.

6

7 **Q. HAVE YOU PREPARED AN EXHIBIT DESCRIBING YOUR**
8 **QUALIFICATIONS AND EXPERIENCE?**

9 A. Yes. I have attached Exhibit RCS-1, which is a summary of my regulatory experience
10 and qualifications.

11

12 **Q. ON WHOSE BEHALF ARE YOU APPEARING?**

13 A. Larkin & Associates, PLLC, was retained by the Florida Office of Public Counsel
14 (“OPC”) to review the impacts on public utility revenue requirements associated with
15 the Tax Cuts and Jobs Act of 2017 (“TCJA” or “2017 Tax Act”). My testimony
16 addresses the impacts of the TCJA on Florida Public Utilities Company - Ft. Meade
17 Division (“Ft. Meade” or “Company”) on behalf of the OPC. Accordingly, I am
18 appearing on behalf of the Citizens of the State of Florida.

19

20 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

21 A. I am presenting OPC's recommendations regarding certain aspects of the TCJA impacts
22 on the Company. I address TCJA impacts on Florida Public Utilities Company
23 (“FPUC-Gas”), Chesapeake Utilities Corporation Florida Division (“Chesapeake”),
24 and Indiantown, the Company’s affiliated gas distribution utility operations in
25 separately filed testimony (collectively, the four affiliated gas distribution utilities are

1 referred to as the “Companies”). In this testimony, I address TCJA impacts on Ft.
2 Meade.

3
4 **Q. WHAT INFORMATION DID YOU REVIEW IN PREPARATION OF YOUR**
5 **TESTIMONY?**

6 A. I reviewed each Company’s respective filing, including the direct testimony and
7 exhibits, and the affiliated gas Companies’ direct testimony and exhibits. This review
8 included the revised and supplemental direct testimony and exhibits filed by the
9 Companies on August 27, 2018. I also reviewed the Companies’ responses to OPC’s
10 formal and informal discovery and other materials pertaining to the TCJA and its
11 impacts on the Companies. In addition, I reviewed Rule 25-14.011, Florida
12 Administrative Code (“F.A.C.”), concerning procedures for processing requests for
13 rulings to be filed with the Internal Revenue Service (“IRS”).

14
15 **Q. PLEASE DESCRIBE HOW THE REMAINDER OF YOUR TESTIMONY IS**
16 **ORGANIZED.**

17 A. After this introduction (Section I), I address the TCJA impacts related to each of the
18 following issues:

- 19
- 20 • In Section II, I address the amount and recommended treatment of Protected
and Unprotected Excess Accumulated Deferred Income Taxes ("EADIT").
 - 21 • In Section III, I address the amount and recommended treatment of 2018
22 income tax savings in base rates related to the reduction in the federal income
23 tax rate to 21 percent.
- 24

- 1 • In Section IV, I address TCJA savings related to the Company’s Gas Reliability
- 2 Infrastructure Program (“GRIP”).
- 3 • In Section V, I address whether a Private Letter Ruling (“PLR”) should be
- 4 required for the Companies, and issues related to a PLR request.
- 5 • In Section VI, I summarize my findings and recommendations.

6

7 **II. QUANTIFICATION, CLASSIFICATION, AND APPLICATION OF**

8 **EXCESS ACCUMULATED DEFERRED INCOME TAXES**

9 **Q. WHAT ARE ACCUMULATED DEFERRED INCOME TAXES (“ADIT”)?**

10 A. ADIT is a source of cost-free capital to reflect that the utility collects money from

11 ratepayers for Deferred Income Tax Expense and holds onto that money prior to

12 eventually paying the income taxes to the government. ADIT results from differences

13 between book and tax accounting. ADIT is referred to as Accumulated Deferred

14 Income Taxes to recognize that these balances typically build up (or accumulate) over

15 time, e.g., as tax deductions exceed corresponding book expense. One primary source

16 of ADIT results from claiming accelerated tax deductions. The tax depreciation

17 deductions on public utility property typically occur on an accelerated basis (i.e.,

18 method differences) and over a shorter period (i.e., life differences) than book

19 depreciation accruals relating to the original cost of the public utility property. These

20 types of differences between book and tax depreciation are referred to as “method/life”

21 differences. Unlike many other types of book-tax differences, the tax depreciation

22 “method/life” differences are subject to normalization requirements under Sections 167

23 and 168 of the Internal Revenue Codes.

24

1 **Q. WHAT IS "EXCESS" ACCUMULATED DEFERRED INCOME TAXES**
2 **("EXCESS ADIT" OR "EADIT")?**

3 A. Regulated public utilities will be required to identify the portions of their ADIT
4 balances that represent "excess" ADIT based on recalculations using the difference
5 between the old federal income tax ("FIT") rate (typically 35%) under which the ADIT
6 was originally accumulated and the new federal corporate income tax rate of 21%
7 provided for in the TCJA. Basically, the utility's ADIT must be revalued at the new
8 FIT rate (as if it had always been applicable) and the amounts that have been
9 accumulated using federal income tax rates that were higher than the current 21% flat
10 rate will represent "excess" ADIT.

11

12 **Q. WHAT AMOUNT OF EADIT DOES THE COMPANY SHOW AS OF MARCH**
13 **31, 2018?**

14 A. In its June 1, 2018 filing, on Company Exhibit FTMC-1, Ft. Meade shows a net EADIT
15 liability of \$92,333, of which \$54,209 is protected and \$38,124 is unprotected. In its
16 August 27, 2018 filing, on Exhibit FTMC-1 Revised, the Company shows a net
17 regulatory liability for EADIT of \$92,332, of which \$46,451 is a regulatory liability for
18 Protected EADIT and \$45,881 is a regulatory liability for Unprotected EADIT. The
19 Company continues to describe the amounts of EADIT liability as estimated, and
20 indicates that its measurement and accounting for the impact of the tax law change will
21 be complete on or before December 22, 2018, citing Securities and Exchange ("SEC")
22 Staff Accounting Bulletin 118. The Company indicates that per SEC Staff Accounting
23 Bulletin 118 guidance, if information is not yet available or complete, a one-year period
24 in which to complete the required analysis and accounting is permitted.

1 The amounts listed above include the "gross up" amount. The EADIT resulting
2 from the tax rate change is increased or "grossed up" for the current income tax rate.
3 The "grossed up" amount of the EADIT regulatory liability (or asset) will then be
4 amortized and subject to income taxes at the current rate; therefore, the net income
5 impact equals the amortized tax benefit.

6
7 **Q. WHAT ITEMS CHANGED BETWEEN THE VERSION OF THE COMPANY**
8 **EXHIBIT FILED ON JUNE 1, 2018 AND THE REVISED EXHIBIT FTMD-1?**

9 A. Company witness Dewey addresses the changes at pages 3-4 of his August 27, 2018
10 testimony. The lines on Exhibit FTMD-1 Revised that were changed by the Company
11 included "Depreciation," "Cost of Removal," and "Repairs Deduction." The changes
12 relate to periods in which ADIT was accumulated prior to the Company's tax software
13 being implemented in 2015. After the pre-software implementation amounts were
14 identified, the EADIT related to "Cost of Removal" was moved from the "Protected"
15 category into the category labeled as "Unprotected Plant." The result of these revisions
16 was to increase the Protected EADIT liability and to decrease the Unprotected EADIT
17 liability.

18
19 **Q. HOW DO IRS NORMALIZATION REQUIREMENTS AFFECT THE**
20 **CATEGORIZATION OF ADIT AND EXCESS ADIT?**

21 A. IRS normalization requirements will apply to the portion of the property-related ADIT
22 that relates to the use of accelerated tax depreciation (including bonus tax depreciation).
23 This will result in two general categories of excess ADIT: (1) "protected" (i.e., is related
24 to the use of accelerated tax depreciation and is subject to the normalization
25 requirements) and (2) "unprotected" property and non-property related excess ADIT,

1 which is not subject to normalization requirements and for which the amortization or
2 application is up to the discretion of the Commission.

3
4 **Q. HOW DOES THE CATEGORIZATION OF “PROTECTED” OR**
5 **“UNPROTECTED” AFFECT THE AMORTIZATION OF THE EADIT?**

6 **A.** The 2017 Tax Act provides that the Average Rate Assumption Method (“ARAM”)
7 must be used for the protected portion of the EADIT. The flow back of the “protected”
8 excess ADIT, therefore, must follow the prescribed method to comply with
9 normalization requirements. In contrast, the flow back of the unprotected portion of
10 the excess ADIT will be up to the discretion of the Commission. Unprotected ADIT is
11 not subject to normalization requirements. The unprotected ADIT will be revalued at
12 the lower 21% tax rate, creating balances of excess unprotected ADIT that can be
13 flowed back to customers over amortization periods to be determined by the
14 Commission, or applied in some other manner to be determined by the Commission
15 (e.g., such as for the recovery of regulatory assets).

16
17 **Q. HOW DOES FT. MEADE CLASSIFY THE EXCESS ADIT BETWEEN THE**
18 **“PROTECTED” AND “UNPROTECTED” CATEGORIES?**

19 **A.** Ft. Meade filed an update on August 27, 2018 in which it reclassifies EADIT related to
20 the cost of removal from “protected” (as per Ft Meade’s original June 1, 2018 filing)
21 and into “unprotected.” As a result of the reclassification, the Company now shows
22 the following on its Exhibit FTMD-1 Revised for Ft. Meade:

- 23 • A net regulatory liability for EADIT of \$93,040,
- 24 • A regulatory liability for Protected EADIT of \$45,619,

- 1 • A regulatory liability for "Unprotected Plant" EADIT of \$7,776,
- 2 • A regulatory liability for "Unprotected Non-Plant" EADIT of \$39,645, and
- 3 • A net regulatory liability for "Unprotected" EADIT of \$47,421.

4

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Additionally, on Exhibit FTMD-2 Revised, the Company shows the following for EADIT regulatory liability or asset amounts for the Common Division before being allocated to Ft. Meade:

8

9

10

- A net regulatory asset for Unprotected EADIT of \$354,178 consisting of:
 - A regulatory liability for Protected EADIT of \$416,016
 - A regulatory asset for Unprotected EADIT of \$770,194.

11

12

The allocated Common Division amounts to Ft. Meade are shown on Company Exhibit FTMC-1 Revised as follows:

13

14

15

16

- A net regulatory asset for Unprotected EADIT of \$708 consisting of:
 - A regulatory liability for Protected EADIT of \$832
 - A regulatory asset for Unprotected EADIT of \$1,540.

17

Q. DO YOU AGREE WITH THE COMPANY'S CLASSIFICATION OF THE EADIT BETWEEN THE "PROTECTED" AND "UNPROTECTED" CATEGORIES?

18

19

20

A. I have no disagreement with the Company's updated classification of EADIT. However, it should be noted that the guidance provided in the TCJA and in previous IRS rulings presents some degree of uncertainty as to the classification of the EADIT related to at least one of the large book-tax differences, specifically to the EADIT relating to cost of removal/negative net salvage.

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Q. WHAT DOES THE COMPANY PROPOSE FOR THE AMORTIZATION OF THE EADIT?

A. As described by Company witness Cassel in his August 27, 2018 Revised Direct Testimony at pages 5 and 6 and as shown on his Exhibit FTMC-1 Revised, the Company proposes the following:

- That the Unprotected EADIT net liability of \$45,881 should be amortized over 10 years at \$4,588 per year.
- That the Protected EADIT liability which is currently estimated by the Company to be \$46,451 should be amortized using the IRS prescribed methodology, which is estimated by the Company to flow back over 26 years at approximately \$1,787 per year.

The Company proposes to retain the estimated annual amount of Protected EADIT liability amortization of \$1,787 and the \$4,588 per year Unprotected EADIT liability amortization for a net benefit amount to be retained by the Company of \$6,375 instead of refunding these monies to its customers.

Q. WHAT IS THE APPROPRIATE DISPOSITION OF THE PROTECTED EADIT?

A. The protected EADIT should be reversed using an ARAM if the utility has the available information to calculate the ARAM, or via another appropriate method that complies with normalization requirements, if the Company does not have the information to compute the ARAM.

1 **Q. ARE YOU CONTESTING THE AMOUNTS ASSOCIATED WITH THE**
2 **COMPANY'S PROPOSED EADIT AMORTIZATIONS?**

3 A. No. The Company has indicated that its EADIT amounts are estimates and are subject
4 to correction by December 22, 2018. I have accepted the Company's revised amounts
5 as reasonable estimates, subject to the later true up.

6

7 **Q. WHAT IS THE TAX BENEFIT ARISING FROM THE EADIT THAT THE**
8 **COMPANY REQUESTS TO BE RETAINED?**

9 A. The net gross-up tax benefit arising from the EADIT amortization that the Company
10 proposes to retain is approximately \$6,375 annually.

11

12 **Q. SHOULD FT. MEADE UPDATE THE ESTIMATED TAX BENEFIT TO BE**
13 **CONSISTENT WITH ANY ADJUSTMENTS TO THOSE ESTIMATES**
14 **THROUGH DECEMBER 22, 2018? IF SO, HOW SHOULD IT BE HANDLED?**

15 A. Yes. Adjustments or corrections to the amounts should be addressed in a true-up filing.

16

17 **Q. ARE YOU CONTESTING THE COMPANY'S PROPOSAL TO RETAIN THE**
18 **NET BENEFIT OF THE EADIT AMORTIZATION?**

19 A. Yes, I am. The estimated annual amount of Protected EADIT liability amortization of
20 \$1,787 and the \$4,588 per year Unprotected EADIT liability amortization produces an
21 estimated net benefit amount of \$6,375, which should be returned to customers via a
22 base rate reduction. This net EADIT amortization amount can be trued-up if needed
23 by December 22, 2018. This contrasts with the Company's proposal to retain the full
24 net benefit amount of \$6,375.

25

1 **Q. IN YOUR OPINION, IS THE FACT THAT FT. MEADE IS NOT OVER-**
2 **EARNING A REASON TO ALLOW THE COMPANY TO RECOVER THE**
3 **2018 BASE RATE INCOME TAX DETRIMENT?**

4 A. No, it is not.

5
6 **Q. SHOULD THE AMOUNT OF 2018 INCOME TAX DETRIMENT BE**
7 **CHARGED TO CUSTOMERS BY THE COMPANY THROUGH THE ECCR?**

8 A. No, they should not. The estimated amount of 2018 income tax detriment does not
9 have anything to do with the ECCR and, therefore, should not be charged to ratepayers
10 through the ECCR. The federal tax reform was an extraordinary, one-time event that
11 was beyond the control of utility management. The utilities have sought single-issue
12 ratemaking for events beyond the utilities' control for other types of costs, typically
13 ones that fluctuate or increase between utility rate cases, to the detriment of consumers.

14
15 **Q. HOW LONG HAS FT. MEADE BEEN EARNING BELOW ITS AUTHORIZED**
16 **EARNINGS RANGE?**

17 A. Ft. Meade has been earning below its authorized range since the Company was
18 purchased in 2014.

19
20 **Q. WHAT IS THE APPROPRIATE REMEDY THE UTILITY CAN SEEK IF IT IS**
21 **EARNING BELOW ITS AUTHORIZED RANGE?**

22 A. If the Company believes its base rates are insufficient to earn a fair rate of return, it has
23 the ability to file a base rate case to address the situation. The fact that a particular
24 utility, such as Ft. Meade, may not be earning its most recent authorized rate of return
25 is not a convincing reason to charge an estimated amount of TCJA-based tax detriment

1 to customers through the ECCR. Instead, the Company has the opportunity to request
2 a base rate increase.

3
4 **Q. SHOULD THE 2018 INCOME TAX SAVINGS BE RETAINED BY THE**
5 **COMPANY?**

6 A. No, they should not. The 2018 base rate income tax savings should be applied for the
7 benefit of customers through a base rate reduction. According to the Florida Supreme
8 Court in Reedy Creek Co. v. Fla. Public Serv. Comm., 418 So. 2d. 249, 254(1982), “A
9 change in a tax law should no [sic] result in a ‘windfall’ to a utility, but in a refund to
10 the customer who paid the revenue that translated into the tax saving.” The
11 Commission should account for lower federal tax rates in 2018 and beyond and require
12 that such TCJA savings, including the 2018 base rate savings, be applied for the benefit
13 of the utility's ratepayers through a permanent base rate reduction.

14
15 **IV. TCJA SAVINGS RELATED TO THE COMPANY'S GAS**
16 **RELIABILITY INFRASTRUCTURE PROGRAM (“GRIP”)**

17 **Q. HAS THE COMPANY IDENTIFIED TCJA SAVINGS RELATED TO ITS**
18 **GRIP?**

19 A. Yes. Mr. Cassel's August 27, 2018, Revised Direct Testimony at page 7 addresses the
20 impacts of the TCJA on the Company's GRIP. He indicates the Company expects 2018
21 tax savings of \$2,376 as shown on his Exhibit FTMC-2, would accumulate between
22 the Jurisdictional Date and the date that GRIP rates will be charged on customer bills
23 (January 1, 2019). The Company proposes retaining that benefit.

24 At page 7, he also addresses the GRIP impact for period 2019 and beyond. He
25 indicates the Company would apply the new, lower 21 percent federal income tax rate

1 into its 2019 GRIP surcharges projections and future projections, which he estimates
2 will reduce the annual GRIP revenue amount by the annual tax savings of
3 approximately two thousand dollars.

4 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSAL TO RETAIN THE**
5 **GRIP RELATED TCJA SAVINGS ON THE 2018 GRIP SURCHARGE FROM**
6 **THE JURISDICTIONAL DATE UNTIL DECEMBER 31, 2018?**

7 A. No. The tax benefits associated with the 2018 GRIP surcharge from the jurisdictional
8 date until December 31, 2018, should be passed on to customers as reductions to GRIP
9 surcharges.

10 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSAL TO PASS ON THE**
11 **GRIP RELATED TCJA SAVINGS ON THE ONGOING GRIP SURCHARGE**
12 **FROM 2019 AND BEYOND?**

13 A. Yes. The tax benefits associated with the GRIP should be passed on to customers as
14 reductions to GRIP surcharges

15 **Q. SHOULD THE TAX BENEFITS DIRECTLY ASSOCIATED WITH THE GRIP**
16 **PROGRAM BE PASSED ON TO CUSTOMERS THROUGH FUTURE GRIP**
17 **SURCHARGES?**

18 A. Yes. The tax benefits associated with the GRIP should be passed on to customers as
19 reductions to GRIP surcharges.

20 **Q. DO YOU AGREE THAT THE GRIP RELATED TCJA-SAVINGS SHOULD BE**
21 **FLOWED THOUGH TO CUSTOMERS IN THE GRIP SURCHARGE FILINGS?**

22 A. Yes.

1 **V. WHETHER A PRIVATE LETTER RULING (“PLR”) SHOULD BE**
2 **REQUIRED FOR THE COMPANIES, AND ISSUES RELATED TO A**
3 **PLR REQUEST**

4 **Q. DID THE COMPANY'S AUGUST 27, 2018 REVISED FILING CONTAIN A**
5 **RECLASSIFICATION OF EADIT RELATED TO COST-OF-REMOVAL**
6 **FROM "PROTECTED" TO "UNPROTECTED"?**

7 A. Yes. One of the items that was revised in the Company's August 27, 2018 filing was
8 the classification of EADIT related to the cost of removal. In the Company's original
9 June 1, 2018 application, EADIT related to cost of removal was classified as
10 "protected." In the Company's August 27, 2018 filing, an updated amount of EADIT
11 related to cost of removal has now been classified as "unprotected."

12
13 **Q. DO YOU HAVE AN OPINION AS TO WHETHER THE EADIT RELATED TO**
14 **COST OF REMOVAL/NEGATIVE NET SALVAGE IS "PROTECTED" OR**
15 **"UNPROTECTED"?**

16 A. Yes, I do. Based on currently available guidance, it is my opinion that the EADIT
17 related to cost of removal/negative net salvage is "unprotected." This is because the
18 tax deduction for cost of removal is not addressed under §167 or §168 of the Internal
19 Revenue Code ("IRC" or "Code"), which are the sections pertaining to the use of
20 accelerated tax depreciation and the sections which contain the normalization
21 requirements pertaining to the continued use of accelerated tax depreciation.
22 Deductions that are provided for under other sections of the Code are not subject to the
23 normalization requirements associated with the utility's ability to continue to use
24 accelerated depreciation for federal income tax purposes.

25
26 **Q. IS THERE SOME UNCERTAINTY IN THIS AREA?**

1 A. Yes, there is. The comparison of utility book and tax depreciation for purposes of
2 tracking the method/life and other differences can be very complex. Utility book
3 depreciation rates typically include a component for negative net salvage (as well as
4 for the recovery of original cost over the estimated useful life of the assets). The
5 normalization process involves comparing book and tax depreciation; however, the
6 calculations can be very complex. Such calculations are typically done by larger
7 utilities using specialized software, such as PowerPlan and PowerTax, and the proper
8 application can require significant additional analytical work by the utility and the
9 vendor. Since the comparison of book and tax depreciation involves complex
10 calculations and utility book depreciation typically includes an element for negative net
11 salvage, some jurisdictions (e.g., New York) and some Florida utilities (e.g., Duke
12 Energy Florida (“DEF”)) have raised concerns about the cost of removal/negative net
13 salvage component of book depreciation and the risks presented for potential
14 normalization violations. For example, DEF appears to be taking a different position
15 than Tampa Electric Company (“TECO”) and Peoples’ Gas System (“PGS”)
16 concerning the treatment of cost of removal/negative net salvage and has proposed to
17 treat that item as "protected," pending receipt of additional guidance.

18

19 **Q. SHOULD THE COMPANIES SEEK A PLR FROM THE IRS REGARDING ITS**
20 **CLASSIFICATION OF THE EXCESS ADIT RELATING TO COST OF**
21 **REMOVAL/NEGATIVE NET SALVAGE AS “UNPROTECTED”?**

22 A. Possibly, yes; however, a Commission decision concerning whether to require the
23 Companies to seek a PLR does not appear to be as urgent an issue as it is with respect
24 to some of the other, larger Florida regulated public utilities. Due to the Companies'
25 small size compared to some of the other Florida regulated utilities, I would

1 recommend that the larger Florida utilities (e.g., such as TECO and PGS) first seek
2 PLRs concerning the classification of EADIT related to cost of removal/negative net
3 salvage as “unprotected”. It may be that the guidance provided by the PLRs issued to
4 the larger utilities will be sufficiently clear that Ft. Meade and its affiliates might not
5 need to obtain their own PLR. Although obtaining a PLR related to the utility’s own
6 specific fact situation provides more definitive assurance, it might not be necessary for
7 Fort Meade and its Florida utility affiliates (FPUC-Gas, Chesapeake, and Indiantown)
8 to seek their own specific PLRs.

9
10 **Q. IF FT. MEADE, ALONG WITH ITS FLORIDA UTILITY AFFILIATES,**
11 **SEEKS A PLR AND THE IRS RULES THEREIN (OR IN ANOTHER PLR)**
12 **THAT THE EADIT RELATING TO COST OF REMOVAL/NEGATIVE NET**
13 **SALVAGE IS TO BE TREATED AS “PROTECTED,” WHAT PROCESS**
14 **SHOULD BE FOLLOWED FOR THE RECLASSIFICATION?**

15 A. Pending clarification of the appropriate classification of EADIT for cost of
16 removal/negative net salvage, Ft. Meade should amortize the related EADIT using the
17 ARAM if the classification ruled by the IRS indicates this is “protected.”

18
19 **Q. HAS THE COMPANY ESTIMATED THE COST OF OBTAINING A PLR?**

20 A. Yes. At page 4 of his August 27, 2018 Supplemental Direct Testimony, Mr. Cassel
21 estimates the cost of seeking a PLR to be \$20,000 to \$50,000 and indicates the
22 Companies could obtain a more firm estimate of the cost if needed. At page 5 of that
23 testimony, he proposes deferred accounting treatment for the PLR cost and
24 amortization over four years if it is incurred.

25

1 **Q. WHAT MECHANISM SHOULD BE UTILIZED TO AVOID THE NEGATIVE**
2 **IMPACT TO THE COMPANIES OF THE COST OF SEEKING A PRIVATE**
3 **LETTER RULING?**

4 A. As I suggested earlier, awaiting IRS rulings from the larger Florida utilities on their
5 respective PLRs before requiring the Companies to seek a PLR will potentially avoid
6 the need for Ft. Meade and its Florida public utility affiliates to seek their own PLR. If
7 the PLRs for the larger Florida utilities are clear and consistent in their rulings, having
8 Ft. Meade and its affiliates request their own PLR may be unnecessary. Thus, the cost
9 for having Ft. Meade and its Florida affiliates request a PLR does not need to be
10 incurred at this time.

11
12 **Q. IN HIS AUGUST 27, 2018 SUPPLEMENTAL DIRECT TESTIMONY, AT**
13 **PAGE 4, MR. CASSEL PROPOSES THAT, IF A PLR REQUEST IS**
14 **REQUIRED, FT. MEADE SHOULD BE ALLOWED TO FILE A PLR**
15 **REQUEST JOINTLY WITH THE OTHER AFFILIATED CUC ENTITIES IN**
16 **FLORIDA. WOULD THAT BE A REASONABLE ACCOMMODATION?**

17 A. Yes, it would. If the Commission determines in this proceeding, or subsequently, that
18 a PLR request should be made by Ft. Meade on a TCJA related issue, then a combined
19 PLR request by the Companies could be appropriate, particularly if the facts and
20 circumstances are identical or similar with respect to the PLR request.

21
22 **VI. FINDINGS AND RECOMMENDATIONS**

23 **Q. ARE YOU RECOMMENDING ANY ADJUSTMENTS TO THE COMPANY'S**
24 **QUANTIFICATIONS OF THE TCJA IMPACTS AT THIS TIME?**

1 A. No, I am not. The Companies' quantifications do not appear to be unreasonable for the
2 purposes of estimating the one-time annual revenue requirement reduction and EADIT
3 related to the TCJA.

4

5 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSAL TO RETAIN GRIP-**
6 **RELATED TCJA SAVINGS ON THE 2018 GRIP SURCHARGE FROM THE**
7 **JURISDICTIONAL DATE UNTIL DECEMBER 31, 2018?**

8 A. No, all GRIP related TCJA savings should be flowed through to customers via the
9 Company's GRIP surcharge filings.

10

11 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSAL TO FLOW GRIP**
12 **RELATED TCJA SAVINGS ON THE ONGOING GRIP SURCHARGE FROM**
13 **2019 AND BEYOND THROUGH ITS GRIP SURCHARGE FILINGS?**

14 A. Yes.

15

16 **DO YOU AGREE WITH THE COMPANY'S PROPOSALS TO FLOW AN**
17 **ESTIMATED AMOUNT OF TCJA DETRIMENT THROUGH ITS ECCR**
18 **SURCHARGE FILING?**

19 A. No.

20

21 **Q. ARE YOU RECOMMENDING ANY DIFFERENT REGULATORY**
22 **TREATMENTS FOR THE BASE RATE TCJA SAVINGS?**

23 A. Yes, I am. The expense increase calculated by the Company for the base rate TCJA
24 savings should be addressed in a base rate case. This contrasts with the Company's
25 proposal to charge the amount to customers via its ECCR filing. Additionally, the net

1 annual amortization of the Protected and Unprotected EADIT estimated by the
2 Company to be approximately \$6,375 annually, should be applied for the benefit of
3 customers as a rate reduction or refund, rather than being retained by the Company.

4

5 **Q. DOES THIS COMPLETE YOUR PREFILED TESTIMONY?**

6 A. Yes, it does.

7

1 (Whereupon, the prefiled direct testimony of
2 Witness Smith was entered into the record of Docket
3 No. 20180054-GU as though read.)

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DIRECT TESTIMONY**OF****RALPH SMITH**

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

20180054-GU

1 **I. INTRODUCTION**2 **Q. WHAT ARE YOUR NAME, OCCUPATION, AND BUSINESS ADDRESS?**

3 A. My name is Ralph Smith. I am a Certified Public Accountant licensed in the State
4 of Michigan and a senior regulatory consultant at the firm Larkin & Associates,
5 PLLC, Certified Public Accountants, with offices at 15728 Farmington Road,
6 Livonia, Michigan, 48154.

7

8 **Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES, PLLC.**

9 A. Larkin & Associates, PLLC, ("Larkin") is a Certified Public Accounting and
10 Regulatory Consulting Firm. The firm performs independent regulatory consulting
11 primarily for public service/utility commission staffs and consumer interest groups
12 (public counsels, public advocates, consumer counsels, attorneys general, etc.).
13 Larkin has extensive experience in the utility regulatory field as expert witnesses
14 in over 600 regulatory proceedings, including numerous electric, water and
15 wastewater, gas and telephone utility cases.

16

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC**
2 **SERVICE COMMISSION?**

3 A. Yes, I have testified before the Florida Public Service Commission (“FPSC” or
4 “Commission”) previously. I have also testified before several other state
5 regulatory commissions.

6

7 **Q. HAVE YOU PREPARED AN EXHIBIT DESCRIBING YOUR**
8 **QUALIFICATIONS AND EXPERIENCE?**

9 A. Yes. I have attached Exhibit RCS-1, which is a summary of my regulatory
10 experience and qualifications.

11

12 **Q. ON WHOSE BEHALF ARE YOU APPEARING?**

13 A. Larkin & Associates, PLLC, was retained by the Florida Office of Public Counsel
14 (“OPC”) to review the impacts on public utility revenue requirements due to the
15 Tax Cuts and Jobs Act of 2017 (“TCJA” or “2017 Tax Act”). My testimony
16 addresses the impacts of the TCJA on Florida Division of Chesapeake Utilities
17 Corporation d/b/a Central Florida Gas (“CFG” or “Chesapeake”) on behalf of the
18 OPC. Accordingly, I am appearing on behalf of the Citizens of the State of Florida.

19

20 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
21 **PROCEEDING?**

22 A. I am presenting OPC's recommendations regarding certain aspects of the TCJA
23 impacts on the Company. I address TCJA impacts on Florida Public Utilities
24 Company (“FPUC-Gas”), Indiantown, and Fort Meade, the Company’s affiliated
25 gas distribution utility operations in separately filed testimony (collectively, the

1 four affiliated gas distribution utilities are referred to as the “Companies”). In this
2 testimony, I address TCJA impacts on Chesapeake.

3

4 **Q. WHAT INFORMATION DID YOU REVIEW IN PREPARATION OF**
5 **YOUR TESTIMONY?**

6 A. I reviewed each Company’s respective filing including the direct testimony and
7 exhibits, and the affiliated gas Companies’ direct testimony and exhibits. This
8 review includes the revised and supplemental direct testimony and exhibits filed by
9 the Companies on August 27, 2018. I also reviewed the Companies’ responses to
10 OPC’s formal and informal discovery and other materials pertaining to the TCJA
11 and its impacts on the Companies. In addition, I reviewed Rule 25-14.011, Florida
12 Administrative Code (“F.A.C.”), concerning procedures for processing requests for
13 rulings to be filed with the Internal Revenue Service (“IRS”).

14

15 **Q. PLEASE DESCRIBE HOW THE REMAINDER OF YOUR TESTIMONY IS**
16 **ORGANIZED.**

17 A. After this introduction (Section I), I address the TCJA impacts related to each of
18 the following issues:

- 19 • In Section II, I address the amount and recommended treatment of Protected
20 and Unprotected Excess Accumulated Deferred Income Taxes (“EADIT”).
- 21 • In Section III, I address the amount and recommended treatment of 2018
22 income tax savings in base rates related to the reduction in the federal
23 income tax rate to 21 percent.
- 24 • In Section IV, I address TCJA savings related to the Company’s Gas
25 Reliability Infrastructure Program (“GRIP”).

- In Section V, I address whether a Private Letter Ruling ("PLR") should be required for the Companies, and issues related to a PLR request.

II. QUANTIFICATION, CLASSIFICATION, AND APPLICATION OF EXCESS ACCUMULATED DEFERRED INCOME TAXES

Q. WHAT ARE ACCUMULATED DEFERRED INCOME TAXES ("ADIT")?

A. ADIT is a source of cost-free capital to reflect that the utility collects money from ratepayers for Deferred Income Tax Expense and holds onto that money prior to eventually paying the income taxes to the government. ADIT results from differences between book and tax accounting. ADIT is referred to as Accumulated Deferred Income Taxes to recognize that these balances typically build up (or accumulate) over time, e.g., as tax deductions exceed corresponding book expense. One primary source of ADIT results from claiming accelerated tax deductions. The tax depreciation deductions on public utility property typically occur on an accelerated basis (i.e., method differences) and over a shorter period (i.e., life differences) than book depreciation accruals relating to the original cost of the public utility property. These types of differences between book and tax depreciation are referred to as "method/life" differences. Unlike many other types of book-tax differences, the tax depreciation "method/life" differences are subject to normalization requirements under Sections 167 and 168 of the Internal Revenue Codes.

Q. WHAT ARE "EXCESS" ACCUMULATED DEFERRED INCOME TAXES ("EXCESS ADIT" OR "EADIT")?

A. Regulated public utilities will be required to identify the portions of their ADIT balances that represent "excess" ADIT based on recalculations using the difference

1 between the old federal income tax ("FIT") rate (typically 35%) under which the
2 ADIT was originally accumulated and the new federal corporate income tax rate of
3 21% provided for in the TCJA. Basically, the utility's ADIT must be revalued at
4 the new FIT rate (as if it had always been applicable) and the amounts that have
5 been accumulated using the federal income tax rates that are higher than the current
6 21% flat rate will represent "excess" ADIT.

7

8 **Q. WHAT AMOUNT OF EADIT DOES CHESAPEAKE SHOW AS OF**
9 **MARCH 31, 2018?**

10 A. In its June 1, 2018 filing, Chesapeake shows an EADIT liability of \$8,413,950, of
11 which \$8,791,030 is a protected liability and \$377,080 is an unprotected asset. In
12 its August 27, 2018 filing, the Company shows on its Exhibit CFMD-1 revised a
13 regulatory liability for EADIT of \$8,475,577 (Dewey testimony page 5, line 9
14 indicates \$8,413,950), of which \$9,537,104 is a regulatory liability for Protected
15 EADIT and \$1,061,527 is a regulatory asset for Unprotected EADIT. The
16 Company continues to describe the amounts of EADIT liability as estimated, and
17 indicates that its measurement and accounting for the impact of the tax law change
18 will be completed on or before December 22, 2018, citing Securities and Exchange
19 ("SEC") Staff Accounting Bulletin 118. The Company indicates that per SEC Staff
20 Accounting Bulletin 118 guidance, if information is not yet available or complete,
21 a one-year period in which to complete the required analysis and accounting is
22 permitted.

23 The amounts listed above include the "gross up" amount. The EADIT
24 resulting from the tax rate change is increased or "grossed up" for the current
25 income tax rate. The "grossed up" amount of the EADIT regulatory liability (or

1 asset) will then be amortized and subject to income taxes at the current rate;
2 therefore, the net income impact equals the amortized tax benefit.

3

4 **Q. WHAT ITEMS CHANGED BETWEEN THE VERSION OF THE**
5 **COMPANY EXHIBIT FILED ON JUNE 1, 2018 AND THE EXHIBIT**
6 **CFMD-1 REVISED?**

7 A. Company witness Dewey addresses the changes at pages 3-4 of his August 27, 2018
8 testimony. The lines on Exhibit CFMD-1 Revised that were changed by the
9 Company included "Depreciation," "Cost of Removal," and "Repairs Deduction."
10 The changes relate to periods in which ADIT was accumulated prior to the
11 Company's tax software being implemented in 2015. After the pre-software
12 implementation ADIT amounts were identified, the EADIT related to "Cost of
13 Removal" was moved from the "Protected" category into the category labeled as
14 "Unprotected Plant." The result of these revisions was to increase the Protected
15 EADIT liability and to decrease the Unprotected EADIT liability.

16

17 **Q. HOW DO IRS NORMALIZATION REQUIREMENTS AFFECT THE**
18 **CATEGORIZATION OF ADIT AND EXCESS ADIT?**

19 A. IRS normalization requirements will apply to the portion of the property-related
20 ADIT that relates to the use of accelerated tax depreciation (including bonus tax
21 depreciation). This will result in two general categories of excess ADIT: (1)
22 "protected" (i.e., is related to the use of accelerated tax depreciation and is subject
23 to the normalization requirements) and (2) "unprotected" property and non-property
24 related excess ADIT, which is not subject to normalization requirements and for
25 which the amortization or application is up to the discretion of the Commission.

1

2 **Q. HOW DOES THE CATEGORIZATION OF “PROTECTED” OR**
3 **“UNPROTECTED” AFFECT THE AMORTIZATION OF THE EADIT?**

4 **A.** The 2017 Tax Act provides that the Average Rate Assumption Method (“ARAM”)
5 must be used for the protected portion of the EADIT. The flow back of the
6 “protected” excess ADIT, therefore, must follow the prescribed method to comply
7 with normalization requirements. In contrast, the flow back of the unprotected
8 portion of the excess ADIT will be up to the discretion of the Commission.
9 Unprotected ADIT is not subject to normalization requirements. The unprotected
10 ADIT will be revalued at the lower 21% tax rate, creating balances of excess
11 unprotected ADIT that can be flowed back to customers over amortization periods
12 to be determined by the Commission, or applied in some other manner to be
13 determined by the Commission (e.g., such as for the recovery of regulatory assets).

14

15 **Q. HOW DOES CFG CLASSIFY THE EXCESS ADIT BETWEEN THE**
16 **“PROTECTED” AND “UNPROTECTED” CATEGORIES?**

17 **A.** CFG filed an update on August 27, 2018 in which it reclassifies EADIT related to
18 the cost of removal from “protected” (as per CFG’s original June 1, 2018 filing)
19 into “unprotected.” As a result of the reclassification, the Company now shows the
20 following on its Exhibit CFMD-1 for Chesapeake:

21

- A total regulatory liability for EADIT of \$8,475,577,

22

- A regulatory liability for Protected EADIT of \$9,537,104,

23

- A regulatory asset for "Unprotected Plant" EADIT of \$741,165,

24

- A regulatory asset for "Unprotected Non-Plant" EADIT of \$320,362, and

25

- A net regulatory asset for "Unprotected" EADIT of \$1,061,527.

1
2 Additionally, on Exhibit CFMD-2 Revised, the Company shows the
3 following for EADIT regulatory liability or asset amounts for the Common
4 Division allocated to Chesapeake:

- 5 • A net regulatory asset for Unprotected EADIT of \$354,178¹ consisting of:
 - 6 ○ A regulatory liability for Protected EADIT of \$416,016
 - 7 ○ A regulatory asset for Unprotected EADIT of \$770,194.

8 The allocated Common Division amounts to Chesapeake are shown on
9 Company Exhibit CFMC-1 Revised as follows:

- 10 • A net regulatory asset for Unprotected EADIT of \$61,627 consisting of:
 - 11 ○ A regulatory liability for Protected EADIT of \$72,387
 - 12 ○ A regulatory asset for Unprotected EADIT of \$134,014.

13
14 These EADIT amounts are summarized in the following table:

	Chesapeake Florida Division	Common Allocated to Chesapeake	Total
Protected EADIT Liability	(9,537,104)	(416,016)	(9,953,120)
Unprotected EADIT Asset	1,061,527	770,194	1,831,721
Net EADIT Liability	<u>\$ (8,475,577)</u>	<u>\$ 354,178</u>	<u>\$ (8,121,399)</u>

15
16
17 **Q. DO YOU AGREE WITH CFG'S CLASSIFICATION OF THE EADIT**
18 **BETWEEN THE "PROTECTED" AND "UNPROTECTED"**
19 **CATEGORIES?**

20 **A.** I have no disagreement with the Company's updated classification of EADIT.
21 However, I note that the guidance provided in the TCJA and in previous IRS rulings

¹ The result is an estimated regulatory asset of \$354,178 of which \$61,627 is allocated to Florida division. Dewey testimony, page 3.

1 presents some degree of uncertainty as to the classification of the EADIT related to
2 at least one of the large book-tax differences, specifically to the EADIT relating to
3 cost of removal/negative net salvage.

4
5 **Q. WHAT DOES THE COMPANY PROPOSE FOR THE AMORTIZATION**
6 **OF THE EADIT?**

7 A. As described by Company witness Cassel in his August 27, 2018 Revised Direct
8 Testimony at pages 5 and 6 and as shown on his Exhibit NGMC-2 Revised, the
9 Company proposes the following:

- 10 • That the Unprotected EADIT net asset of \$1,195,541 should be amortized
11 over 10 years at \$119,554 per year.
- 12 • That the Protected EADIT liability which is currently estimated by the
13 Company to be \$9,609,491 should be amortized using the IRS prescribed
14 methodology, which is estimated by the Company to flow back over 26
15 years at approximately \$369,596 per year.

16 The Company proposes to retain the estimated annual amount of Protected EADIT
17 liability amortization of \$369,596 and the \$119,554 per year Unprotected EADIT
18 net asset amortization for a net benefit amount to be retained by the Company of
19 \$250,042 instead of refunding these monies to its customers.

20
21 **Q. WHAT IS THE APPROPRIATE DISPOSITION OF THE PROTECTED**
22 **EADIT?**

23 A. The protected EADIT should be reversed using an ARAM if the utility has the
24 available information to calculate the ARAM, or via another appropriate method

1 that complies with normalization requirements, if the Company does not have the
2 information to compute the ARAM.

3

4 **Q. ARE YOU CONTESTING THE AMOUNTS ASSOCIATED WITH THE**
5 **COMPANY'S PROPOSED EADIT AMORTIZATIONS?**

6 A. No. The Company has indicated that its EADIT amounts are estimates and are
7 subject to correction by December 22, 2018. I have accepted the Company's revised
8 amounts as reasonable estimates, subject to the later true up.

9

10 **Q. WHAT IS THE TAX BENEFIT ARISING FROM THE EADIT THAT CFG**
11 **REQUESTS TO BE RETAINED?**

12 A. The net gross-up tax benefit arising from the EADIT amortization that CFG
13 proposes to retain is approximately \$250,042 annually.

14

15 **Q. SHOULD CHESAPEAKE UPDATE THE ESTIMATED TAX BENEFIT TO**
16 **BE CONSISTENT WITH ANY ADJUSTMENTS TO THOSE ESTIMATES**
17 **THROUGH DECEMBER 22, 2018? IF SO, HOW SHOULD IT BE**
18 **HANDLED?**

19 A. Yes. Adjustments or corrections to the amounts should be addressed in a true-up
20 filing.

21

22 **Q. ARE YOU CONTESTING THE COMPANY'S PROPOSAL TO RETAIN**
23 **THE NET BENEFIT OF THE EADIT AMORTIZATION?**

24 A. Yes, I am. The estimated annual amount of Protected EADIT liability amortization
25 of \$369,596 net of the \$119,554 per year Unprotected EADIT net asset

1 amortization produces an estimated net benefit amount of \$250,042, which should
2 be returned to customers via a base rate reduction. This net EADIT amortization
3 amount can be trued-up if needed by December 22, 2018. This contrasts with the
4 Company's proposal to retain the full net benefit amount of \$250,042.

5
6 **III. 2018 INCOME TAX SAVINGS IN BASE RATES RELATED TO**
7 **THE REDUCTION IN THE FEDERAL INCOME TAX RATE TO**
8 **21 PERCENT**

9 **Q. HOW MUCH 2018 INCOME TAX SAVINGS FROM BASE RATES HAS**
10 **THE COMPANY IDENTIFIED?**

11 A. Company witness Cassel's August 27, 2018 Revised Direct Testimony at page 4
12 identifies the amount of base rate savings as \$630,137.

13
14 **Q. WHAT TREATMENT HAS THE COMPANY PROPOSED FOR THE 2018**
15 **BASE RATE INCOME TAX SAVINGS?**

16 A. Mr. Cassel has indicated that, because the Company is not over-earning, the
17 Company wants to retain the full amount of the annual TCJA base rate savings.

18
19 **Q. IS THE FACT THAT CHESAPEAKE IS NOT OVER-EARNING A**
20 **REASON TO ALLOW THE COMPANY TO RETAIN THE TCJA BASE**
21 **RATE SAVINGS?**

22 A. No, it is not. The fact that a particular utility, such as Chesapeake, may not be
23 earning its most recent authorized rate of return is not a convincing reason to
24 disregard any regulatory liabilities related to the accumulation of TCJA-based
25 savings. The federal tax reform was an extraordinary, one-time event that was
26 beyond the control of utility management. The utilities have sought single-issue

1 ratemaking for events beyond the utilities' control for other types of costs, typically
2 ones that fluctuate or increase between utility rate cases, to the detriment of
3 consumers.

4
5 **Q. SHOULD THE 2018 INCOME TAX SAVINGS BE RETAINED BY THE**
6 **COMPANY?**

7 A. No, they should not. The 2018 base rate income tax savings should be applied for
8 the benefit of customers through a base rate reduction. According to the Florida
9 Supreme Court in Reedy Creek Co. v. Fla. Public Serv. Comm., 418 So. 2d. 249,
10 254(1982), "A change in a tax law should no [sic] result in a 'windfall' to a utility,
11 but in a refund to the customer who paid the revenue that translated into the tax
12 saving." The Commission should account for lower federal tax rates in 2018 and
13 beyond and require that such TCJA savings, including the 2018 base rate savings,
14 be applied for the benefit of the utility's ratepayers through a permanent base rate
15 reduction.

16
17 **IV. TCJA SAVINGS RELATED TO THE COMPANY'S GAS**
18 **RELIABILITY INFRASTRUCTURE PROGRAM ("GRIP")**

19 **Q. HAS THE COMPANY IDENTIFIED TCJA SAVINGS RELATED TO ITS**
20 **GAS RELIABILITY INFRASTRUCTURE PROGRAM ("GRIP")?**

21 A. Yes. Mr. Cassel's August 27, 2018 Revised Direct Testimony at pages 6-7
22 addresses the impacts of the TCJA on the Company's GRIP. He indicates the
23 Company expects 2018 tax savings of \$324,362, as shown on his Exhibit CFMC-
24 2, would accumulate between the Jurisdictional Date and the date that GRIP rates
25 will be charged on customer bills (January 1, 2019). The Company proposes to
26 flow this benefit back to customers by incorporating it as an over-recovery in its

1 2019 GRIP projection, which would have the effect of lowering customer GRIP
2 surcharges by the amount of the benefit.

3 At page 7, he also addresses the GRIP impact for periods 2019 and beyond.
4 He indicates the Company would apply the new, lower 21 percent federal income
5 tax rate into its 2019 GRIP surcharge projections and future projections, which he
6 estimates will reduce the annual GRIP revenue amount by the annual tax savings
7 of approximately \$358,889.

8

9 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSALS FOR THE**
10 **GRIP-RELATED TCJA SAVINGS?**

11 A. Yes, I do. The Company proposes to flow through the GRIP-related TCJA savings
12 to customers through its GRIP surcharge filings. The two pieces of GRIP-related
13 TCJA savings would pass the benefit of the new, lower federal income tax rate
14 directly to CFG's customers.

15

16 **Q. SHOULD THE TAX BENEFITS DIRECTLY ASSOCIATED WITH THE**
17 **GRIP PROGRAM BE PASSED ON TO CUSTOMERS THROUGH**
18 **FUTURE GRIP SURCHARGES?**

19 A. Yes. The tax benefits associated with the GRIP should be passed on to customers
20 as reductions to GRIP surcharges.

21

22 **Q. DO YOU AGREE THAT THE GRIP RELATED TCJA-SAVINGS SHOULD**
23 **BE FLOWED THROUGH TO CUSTOMERS IN THE GRIP SURCHARGE**
24 **FILINGS?**

25 A. Yes.

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V. **WHETHER A PRIVATE LETTER RULING ("PLR") SHOULD BE REQUIRED FOR THE COMPANIES, AND ISSUES RELATED TO A PLR REQUEST**

Q. DID THE COMPANY'S AUGUST 27, 2018 REVISED FILING CONTAIN A RECLASSIFICATION OF EADIT RELATED TO COST-OF-REMOVAL FROM "PROTECTED" TO "UNPROTECTED"?

A. Yes. One of the items revised in the Company's August 27, 2018 filing was the classification of EADIT related to the cost of removal. In the Company's original June 1, 2018 application, EADIT related to cost of removal was classified as "protected." In the Company's August 27, 2018 filing, an updated amount of EADIT related to cost of removal is now classified as "unprotected."

Q. DO YOU HAVE AN OPINION AS TO WHETHER THE EADIT RELATED TO COST OF REMOVAL/NEGATIVE NET SALVAGE IS "PROTECTED" OR "UNPROTECTED"?

A. Yes, I do. Based on currently available guidance, it is my opinion that the EADIT related to cost of removal/negative net salvage is "unprotected." This is because the tax deduction for cost of removal is not addressed under §167 or §168 of the Internal Revenue Code ("IRC" or "Code"), which are the sections pertaining to the use of accelerated tax depreciation and the sections which contain the normalization requirements pertaining to the continued use of accelerated tax depreciation. Deductions provided for under other sections of the Code are not subject to the normalization requirements associated with the utility's ability to continue to use accelerated depreciation for federal income tax purposes.

1 **Q. IS THERE SOME UNCERTAINTY IN THIS AREA?**

2 A. Yes, there is. The comparison of utility book and tax depreciation for purposes of
3 tracking the method/life and other differences can be very complex. Utility book
4 depreciation rates typically include a component for negative net salvage (as well
5 as for the recovery of original cost over the estimated useful life of the assets). The
6 normalization process involves comparing book and tax depreciation; however, the
7 calculations can be very complex. Such calculations are typically done by larger
8 utilities using specialized software, such as PowerPlan and PowerTax, and the
9 proper application can require significant additional analytical work by the utility
10 and the vendor. Since the comparison of book and tax depreciation involves
11 complex calculations and utility book depreciation typically includes an element
12 for negative net salvage, some jurisdictions (e.g., New York) and some Florida
13 utilities (e.g., Duke Energy Florida (“DEF”)) have raised concerns about the cost
14 of removal/negative net salvage component of book depreciation and the risks
15 presented for potential normalization violations. For example, DEF appears to be
16 taking a different position than Tampa Electric Company (“TECO”) and Peoples’
17 Gas System (“PGS”) concerning the treatment of cost of removal/negative net
18 salvage and has proposed to treat that item as "protected," pending receipt of
19 additional guidance.

20
21 **Q. SHOULD CFG SEEK A PLR FROM THE IRS REGARDING ITS**
22 **CLASSIFICATION OF THE EXCESS ADIT RELATING TO COST OF**
23 **REMOVAL/NEGATIVE NET SALVAGE AS “UNPROTECTED”?**

24 A. Possibly, yes; however, a Commission decision concerning whether to require CFG
25 to seek a PLR does not appear to be as urgent an issue as it is with respect to some

1 of the other, larger Florida regulated public utilities. Due to Chesapeake's
2 relatively small size compared to some of the other Florida regulated utilities, I
3 would recommend that the larger Florida utilities (e.g., such as TECO and PGS)
4 first seek PLRs concerning the classification of EADIT related to cost of
5 removal/negative net salvage as "unprotected". It may be that the guidance
6 provided by the PLRs issued to the larger utilities will be sufficiently clear that
7 Chesapeake and its affiliates might not need to obtain their own PLR. Although
8 obtaining a PLR related to the utility's own specific fact situation provides more
9 definitive assurance, it might not be necessary for CFG and its Florida utility
10 affiliates (FPUC-Gas, Indiantown, and Fort Meade) to seek their own specific
11 PLRs.

12
13 **Q. IF CHESAPEAKE SEEKS A PLR AND THE IRS RULES THEREIN (OR IN**
14 **ANOTHER PLR) THAT THE EADIT RELATING TO COST OF**
15 **REMOVAL/NEGATIVE NET SALVAGE IS TO BE TREATED AS**
16 **"PROTECTED," WHAT PROCESS SHOULD BE FOLLOWED FOR THE**
17 **RECLASSIFICATION?**

18 A. Pending clarification of the appropriate classification of EADIT for cost of
19 removal/negative net salvage, Chesapeake should amortize the related EADIT
20 using the ARAM if the classification ruled by the IRS indicates this is "protected."
21

22 **Q. HAS THE COMPANY ESTIMATED THE COST OF OBTAINING A PLR?**

23 A. Yes. At page 4 of his August 27, 2018 Supplemental Direct Testimony, Mr. Cassel
24 estimates the cost of seeking a PLR to be \$20,000 to \$50,000 and indicates the
25 Company could obtain a more firm estimate of the cost if needed. At page 5 of that

1 testimony, he proposes deferred accounting treatment for the PLR cost and
2 amortization over four years if incurred.

3

4 **Q. WHAT MECHANISM SHOULD BE UTILIZED TO AVOID THE**
5 **NEGATIVE IMPACT TO CFG OF THE COST OF SEEKING A PLR?**

6 A. As I suggested earlier, awaiting IRS rulings from the larger Florida utilities on their
7 respective PLRs before requiring CFG to seek a PLR will potentially avoid the need
8 for CFG to seek its own PLR. If the PLRs for the larger Florida utilities are clear
9 and consistent in their rulings, having Chesapeake and its affiliates request their
10 own PLR may be unnecessary. Thus, the cost for having Chesapeake and its
11 Florida affiliates request a PLR does not need to be incurred at this time.

12

13 **Q. IN HIS AUGUST 27, 2018 SUPPLEMENTAL DIRECT TESTIMONY, AT**
14 **PAGE 4, MR. CASSEL PROPOSES THAT, IF A PLR REQUEST IS**
15 **REQUIRED, CHESAPEAKE SHOULD BE ALLOWED TO FILE A PLR**
16 **REQUEST JOINTLY WITH THE OTHER AFFILIATED CUC ENTITIES**
17 **IN FLORIDA. WOULD THAT BE A REASONABLE**
18 **ACCOMMODATION?**

19 A. Yes, it would. If the Commission determines in this proceeding, or subsequently,
20 that a PLR request should be made by Chesapeake on a TCJA related issue, then a
21 combined PLR request by the Companies may be appropriate, particularly if the
22 facts and circumstances are identical or similar with respect to the PLR request.

23

1 **VI. FINDINGS AND RECOMMENDATIONS**

2 **Q. ARE YOU RECOMMENDING ANY ADJUSTMENTS TO THE**
3 **COMPANY'S QUANTIFICATIONS OF THE TCJA IMPACTS AT THIS**
4 **TIME?**

5 A. No, I am not. The Companies' quantifications do not appear to be unreasonable for
6 the purposes of estimating the one-time annual revenue requirement reduction and
7 EADIT related to the TCJA.

8

9 **Q. DO YOU AGREE WITH THE COMPANY'S PROPOSALS TO FLOW**
10 **GRIP-RELATED TCJA SAVINGS THROUGH ITS GRIP SURCHARGE**
11 **FILINGS?**

12 A. Yes.

13

14 **Q. ARE YOU RECOMMENDING ANY DIFFERENT REGULATORY**
15 **TREATMENTS FOR THE BASE RATE TCJA SAVINGS?**

16 A. Yes, I am. The regulatory liability for the base rate TCJA savings should be applied
17 for the benefit of customers as a permanent base rate reduction. This contrasts with
18 the Company's proposal to retain such savings. Additionally, the net annual
19 amortization of the Protected and Unprotected EADIT that is not associated with
20 the acquisition adjustment, estimated by the Company to be approximately
21 \$250,042 annually, should be applied for the benefit of customers as a rate
22 reduction, rather than being retained by the Company.

23

24 **Q. DOES THIS COMPLETE YOUR PREFILED TESTIMONY?**

25 A. Yes, it does.

1 BY MS. PONDER:

2 Q And did you have prefiled exhibits attached to
3 your prefiled testimonies in these dockets?

4 A Yes, I had -- my qualifications were marked as
5 an exhibit, and I believe it was Exhibit 6 in all four
6 dockets.

7 Q And they were marked as RCS-1 to your
8 testimonies, correct?

9 A Correct.

10 Q And do you have any corrections to these
11 exhibits?

12 A No, I do not.

13 Q And again, they were the same in each docket,
14 yes.

15 COMMISSIONER BROWN: And they have already
16 been moved into the record.

17 MS. PONDER: Thank you.

18 BY MS. PONDER:

19 Q Would you please summarize your testimonies in
20 these dockets.

21 A Yes.

22 Good morning, Commissioners. I will be
23 referring to the Tax Cuts and Jobs Act of 2017 as the
24 TCJA or the 2017 tax act. I will be referring to one
25 impact of the tax act as excess accumulated deferred

1 income taxes. I will be referring to that as E-A-D-I-T,
2 or "EED-IT," or excess EDIT.

3 In the rate-setting process, income taxes are
4 a pass-through expense. In other words, the utilities'
5 income taxes related to providing gas utilities service
6 is borne by customers. When the rates for these
7 companies were last set, the federal income tax rate was
8 35 percent.

9 Under the 2017 tax act, the utilities' income
10 tax rate is now 21 percent, effective January 1st, 2018.
11 The difference between 35-percent federal income tax
12 rate and the 21-percent new federal income tax rate on
13 positive taxable income results in tax savings.

14 These tax savings are grossed up to a revenue-
15 requirement impact and represent monies that ratepayers
16 have paid to the utilities, monies that would not be
17 available to the utility but for the 2017 tax act.

18 The situation among these four utilities is
19 somewhat different. For the two larger utilities, FPUC
20 Gas in Docket 51, and Chesapeake in Docket 54 -- those
21 two utilities have positive taxable income and positive
22 earnings and have had those for many years.

23 For the two small utilities, Indiantown in
24 Docket 52, and Fort Meade, Docket 53 -- those have been
25 reporting and operating losses for several years. I

1 will now briefly address recommendations in each of the
2 four dockets in docket-number order.

3 For FPUC Gas, in Docket No. 51, the company
4 proposes to keep the annual base-rate savings of
5 approximately 2.18 million. Additionally, the company
6 seeks to retain the net annual amortization of the
7 protected and unprotected EADIT of approximately
8 \$537,000 per year. I recommend that the Commission
9 order the company to order the return or flow back these
10 benefits to the ratepayers.

11 For Indiantown, in Docket 52, the Indiantown
12 Division alleges an annual tax detriment resulting from
13 the TCJA of approximately \$54,000 per year and seeks the
14 Commission's approval to recover that amount through its
15 energy conservation cost recovery, ECCR clause. ECCR
16 has nothing to do with the base-rate tax impacts, which
17 are the focus of these TCJA dockets.

18 The Indiantown Division also seeks to retain
19 the net gross-up tax benefit from the EADIT, which is
20 approximately \$7,900 per year annually. I recommend
21 that the Commission deny Indiantown's request to charge
22 its customers through the ECCR clause to recover its
23 alleged tax detriment, and the Commission order
24 Indiantown to flow back the EADIT amortization of
25 approximately 7,900 per year to customers in the form of

1 a refund.

2 For Fort Meade -- Fort Meade seeks to recover
3 an annual tax detriment of approximately \$18,000 per
4 year through its ECCR. My recommendation is similar on
5 that to Indiantown.

6 Fort Meade also seeks the Commission approval
7 to retain the EADIT amortization of approximately \$6,400
8 per year. I recommend that the EADIT amortization be
9 refunded to customers.

10 Fort Meade also seeks to retain tax savings
11 related to its Gas Reliability Infrastructure Program,
12 a/k/a the GRIP. That's worth about \$2,400 per year. I
13 recommend that the GRIP be reduced to return these
14 federal income tax savings to customers.

15 Concerning Chesapeake, Docket 54, the company
16 seeks to retain annual savings of approximately 959 --
17 955,000, and retain the protected EADIT liability annual
18 amortization less the unprotected EADIT amortization,
19 for a net benefit of approximately \$250,000 per year.

20 Again, these tax savings are a direct result
21 of the federal income tax legislation. I recommend that
22 the comp- -- the Commission order the company to flow
23 back both the annual tax savings and the net benefit of
24 the EADIT amortization to the company's ratepayers.

25 That completes my summary.

1 MS. PONDER: Thank you.

2 I tender the witness for cross.

3 COMMISSIONER BROWN: Thank you.

4 Mr. Munson?

5 MR. MUNSON: Thank you, Commissioners.

6 EXAMINATION

7 BY MR. MUNSON:

8 Q Good morning, Mr. Smith. I have a few
9 questions for you, please. And I think -- let's just
10 start by confirming -- I think you said just now that
11 the Fort Meade tax detriment that the company -- and
12 I'm -- by the way, I'm going to go ahead and address all
13 four dockets at the same time, unless there's a concern
14 about that. And there may be a few cases where I note
15 exceptions, but otherwise I'm going to try to treat
16 those all at the same time.

17 But with regards to the Fort Meade -- with
18 regards to the Fort Meade, in the 0053 docket, I think
19 you said that the tax detriment that they are requesting
20 to retain was 17,900. Does that sound correct?

21 A \$17,929 is my understanding.

22 Q Okay. Very good.

23 And you agree with me that Fort Meade is
24 earning below its authorized earning range since 2014,
25 correct?

1 A Since 2014. So, for several years, yes.

2 Q Okay. And with Indiantown, you agree -- I
3 think you said in your summary just now and in your
4 testimony that the companies are requesting to retain
5 approximately \$54,000 per year. Does that sound
6 correct?

7 A Yes.

8 Q Okay. And you also agree that Indiantown has
9 been earning below its authorized range since 2013,
10 correct?

11 A Yes.

12 Q In your experience, Mr. Smith, what does it
13 cost a utility like Fort Meade or Indiantown to
14 participate in a base-rate case?

15 A Costs could be significant. In order to
16 implement these Tax Cuts and Jobs Act savings, though,
17 they wouldn't need a full rate case. They could simply
18 file a rate tariff, just like the other utilities, like
19 Tampa Electric has done.

20 Q Would you agree with me, the cost to
21 participate in a full base-rate case would be more than
22 \$55,000?

23 A It could be, yes.

24 Q So, in your direct testimony, you rely on the
25 Reedy Creek case that has been discussed. Do you

1 remember that portion of your testimony?

2 A Can you refer me to a specific page?

3 Q Sure. You have your testimony in front of
4 you?

5 A I do.

6 Q Okay. I'm -- I'm going to start with the 0051
7 docket, the FPUC Gas, that's on Page 12 of your direct,
8 Lines 18 to 25.

9 A Okay. Yes, I have it.

10 Q Okay. And you -- and do you see that portion
11 there? It discusses the Reedy Creek case, correct?

12 A Yes.

13 Q Okay. And so, you're familiar with that case?

14 A Yes.

15 Q Okay. And you recall, in fact, your Counsel
16 asked Witness Cassel -- Cassel questions about that
17 case. You saw that?

18 A Yes. I believe it was marked and some
19 questions were asked.

20 Q Okay. And you've read the entire case,
21 correct?

22 A At some point, yes.

23 Q Okay. So, you know that one of the issues in
24 that case raised by the Reedy Creek utility was whether
25 there was an agreement among the parties to refund the

1 revenues in that case, right?

2 A Based on my recollection, I believe that is
3 correct.

4 Q The other issue in the case was related to the
5 Commission's authority to modify its own orders due to
6 the doctrine of administrative finality. Does that
7 sound right as well?

8 A That sounds familiar.

9 Q Okay. So, really, in this case, the court in
10 Reedy Creek was deciding which of two amounts that Reedy
11 Creek should be required to refund, right?

12 A That's one way of looking at it, yes.

13 Q Okay. So, and -- and in particular, Reedy
14 Creek was going to be required to refund either 47,833
15 or 93,281, depending on the court's decision, right?

16 A I don't remember the exact amounts from that
17 decision, but there was a difference in amounts that was
18 addressed.

19 Q Okay. I guess the point is, is -- so, the
20 issue of whether a utility was going to be required to
21 refund any amount wasn't really before the Court in the
22 Reedy Creek case, was it?

23 A They were going to have to refund some amount
24 under each of those scenarios.

25 MR. MUNSON: Do you have the case in front of

1 you?

2 I'll tell you what. We'll go ahead -- I --
3 we --

4 COMMISSIONER BROWN: It was the first exhibit.
5 I don't know if you still have a copy. Do you --

6 MR. MUNSON: We --

7 COMMISSIONER BROWN: Could you hand him a --
8 we've already moved it into the record.

9 MR. MUNSON: Commissioner, just to speed
10 things along -- and I'm sorry to interrupt. We
11 actually -- I have a couple of other documents, and
12 it may be because I'm referring to particular
13 passages of that testimony that we want to hand out
14 all three.

15 COMMISSIONER BROWN: Sounds good.

16 MR. MUNSON: I don't feel the need, unless the
17 Commission feels otherwise, to mark any of these.
18 They're all either court cases or Commission
19 orders.

20 COMMISSIONER BROWN: Fair enough.

21 MR. MUNSON: Okay.

22 COMMISSIONER BROWN: As long as the witness
23 has a copy, for reference.

24 BY MR. MUNSON:

25 **Q Okay. And so, Mr. Smith, let me make sure**

1 you've got everything there. You should be looking at
2 the Reedy Creek Utilities case. Let's start with that,
3 please. And it's a slight -- the pagination is slightly
4 different, which is why I handed it out. It will be
5 quicker for me to refer you to the section I want to
6 focus on. But do you see that in front of you, the case
7 that was just handed out, Reedy Creek?

8 A Yes. It's one of the three documents.

9 Q Okay. Good.

10 And I'd like you to turn, if you would,
11 please, to the second page of my handout, which is
12 marked in the case as Page 252, with the asterisks.
13 It's really the second page. On the right-hand column
14 at the top, you see a paragraph that begins, "At the
15 workshop." Do you see that?

16 A Yes.

17 Q Okay. And in that paragraph -- I'm reading
18 down a little into the next sentence there. It says,
19 "Viewing the documents together with the testimony and
20 the record, it is clear that a utility would be required
21 to refund revenues if and only if it were earning excess
22 of its authorized rate of return." Do you see that?

23 A Yes.

24 Q And in fact, Reedy Creek in this case was in
25 an over-earnings position, wasn't it?

1 A It was.

2 Q Okay. Turning back, you may -- or you may
3 recall from reading this that the Reedy Creek case came
4 about as a result of the revenue act of 1978 that
5 lowered corporate taxes, correct?

6 A The revenue act of 1978 was the impetus, yes.

7 Q Okay. And the Commission opened a docket and
8 issued orders, just as they did in this case, to
9 determine what should happen to those savings, correct?

10 A Yes.

11 Q And specifically, you see on -- on the first
12 page of the Reedy Creek case, they reference two orders,
13 No. 8624 and 8624A. Do you see those?

14 A Yes.

15 Q Okay. And have you reviewed those orders in
16 be- -- this matter?

17 A Not recently.

18 Q Did you review them in -- in preparation of
19 your testimony?

20 A I think at one point, we did look at them,
21 yes.

22 Q Okay. But they're not referenced in your
23 direct testimony.

24 A They are not.

25 Q Okay. So, if you would, now -- the second of

1 the three documents I handed to you, you'll see as -- in
2 the upper-left-ish corner, it actually has an order
3 number there, 8624.

4 And if I could ask you to turn to that,
5 please.

6 A Okay. I have that document.

7 Q And if you will, turn to the second page. And
8 I'm going to refer to you to the first full sentence
9 that begins, "These accounting entries will be
10 required." Do you see that?

11 A Yes.

12 Q Okay. "These accounting entries will be
13 required during calendar year 1979 while our reviewing
14 and monitoring process is underway.

15 "As noted above, depending on the individual
16 circumstances of each utility, a refund may be
17 required." Do you see that?

18 A Yes.

19 Q So, in that case, in this order, the -- the
20 Public Service Commission was looking at the individual
21 circumstances of each utility to decide whether or not a
22 refund would be required, correct?

23 A Correct.

24 Q Okay. And those -- if you look at the next
25 sentence, they give an example. And it says, "If our

1 continuing surveillance program indicates a utility is
2 exceeding the ceiling of its last authorized rate of
3 return, such savings could be returned to the customers,
4 thereby lowering their overall rate of return." Do you
5 see that?

6 A Yes.

7 Q So, those individual circumstances included
8 whether or not the utility was over-earning, correct?

9 A That was the factor the Commission was looking
10 at here.

11 Q Okay. Let's now turn, please, to Order
12 No. 8624A, which is the last of the three documents I
13 gave you. And when you're -- and -- and I'm going to
14 direct your attention to the Paragraph No. 4 at the
15 bottom of that page.

16 And if you want -- if you need to take the
17 time to read Paragraph 4, or anything else, please do
18 so, but I want to direct your attention to the next-to-
19 last sentence on this page.

20 And I'll read this, "This jurisdictional
21 return shall, then, be compared with the rate of return
22 calculated by using the 13-month average capital
23 structure for the calendar year 1979, and the ceiling of
24 the last authorized rate of return on equity." Do you
25 see that?

1 A Yes.

2 Q Okay. So, essentially, what's going on there,
3 in 8624A -- the Public Service Commission is comparing
4 the utility's actual rate of return to the authorized
5 range of return on equity, correct?

6 A Yes.

7 Q Okay. And that -- that paragraph is entitled
8 "Measurement of Earnings for Refund Purposes," right?

9 A Yes.

10 Q Okay. I would like to next turn to
11 Paragraph 5. It's entitled "Disposition of Revenues."
12 And I'm going to just read to you the pertinent sentence
13 there, which begins with the second sentence in that
14 paragraph: If the utility's actual earned overall rate
15 of return exceeds the ceiling of the zone of
16 reasonableness, as determined in Paragraph 4, the
17 utility shall, after notice and hearing, refund to its
18 customers revenues equal to the lesser of the total
19 calculated differential contained in the reports or the
20 amount of revenue for 1979 that exceeds that which would
21 have been produced by the ceilings -- the ceiling of the
22 utility's rate of return as calculated in Paragraph 4.

23 Do you see that?

24 A Yes.

25 Q And so, based on that Paragraph 5, you would

1 **acknowledge, in fact, that the Commission only required**
2 **refunds of utilities that exceeded the ceiling of that**
3 **range of return in their equity, correct?**

4 A At that point in time, yes.

5 Q **And it, in fact, only required refunds of the**
6 **amounts that were actually in excess of that ceiling,**
7 **correct?**

8 A At that point in time, that's what this order
9 indicates.

10 MR. MUNSON: No further questions.

11 COMMISSIONER BROWN: Thank you.

12 Staff?

13 MS. DZIECHCIARZ: Staff has no questions.

14 Thank you.

15 COMMISSIONER BROWN: Commissioners, any
16 questions? Seeing -- yes, Commissioner Clark.

17 COMMISSIONER CLARK: Mr. Smith, if the
18 Commission approved the refund to the consumers,
19 what is the appropriate mechanism to get that
20 refund back to the consumers? Is it through the
21 base rate? Is it a refund? Is it a clause
22 adjustment? What would your suggestion be?

23 THE WITNESS: My suggestion would be that,
24 once the amounts are determined, that the company
25 file a tariff reflecting either the refund or the

1 reduction in this specific tariff.

2 COMMISSIONER CLARK: Would -- in your opinion,
3 would that require a revenue study, a rate study.

4 THE WITNESS: No, it would require
5 implementation and the Commission's decision made
6 in this docket, similar to what Tampa Electric did.
7 They filed the tariff -- revised tariff to reflect
8 the return of Tax Cuts and Jobs Acts savings to
9 their customers. It didn't require a full rate
10 case.

11 COMMISSIONER CLARK: Okay. Thank you.

12 COMMISSIONER BROWN: All right. OPC,
13 redirect.

14 FURTHER EXAMINATION

15 BY MS. PONDER:

16 **Q Mr. Smith, rate-case expense including a**
17 **limited proceeding is a one-time cost and it's**
18 **customary -- excuse me -- authorized over several**
19 **years -- amortized over sev- -- several years; is that**
20 **correct?**

21 A It's typical for rate-case expense to be
22 amortized over a period that would typically reflect the
23 rate-case filing interval.

24 **Q So, in your experience in a tariff filing, is**
25 **rate-case expense normally part of the recovery in the**

1 **tariff?**

2 A No, not for a tariff filing. I think if it
3 were a general rate case, rate-case expense would
4 typically be identified and then amortized or normalized
5 over some period of multiple years, but for simple
6 tariff filing, I wouldn't think that rate-case expense
7 would be included, and should be minimal.

8 Q You were asked a series of questions about
9 some orders from the Commission more than 30 years ago.
10 Do you recall that?

11 A Yes.

12 Q Did you participate in the Gulf, Peoples Gas,
13 Tampa Electric Company, and Duke Energy case -- tax
14 cases this year?

15 A I did.

16 Q And did all of those companies agree to return
17 a hundred percent of the tax savings?

18 MR. MUNSON: Object -- I'm going to object.
19 I'm sorry. I think this is well beyond the scope
20 of my cross.

21 COMMISSIONER BROWN: Objection overruled. I
22 believe that it goes right to the case that you
23 were addressing. So, I'll allow it.

24 THE WITNESS: Yes, each of those large
25 electric and gas utilities have agreed to apply the

1 savings from the tax cuts and jobs act in some
2 manner to reflect a benefit to their customers. It
3 varied from company to company exactly how it was
4 applied, but each company agreed that it needed to
5 be returned to customers or applied in a manner to
6 benefit customers.

7 BY MS. PONDER:

8 **Q And -- and which method do you believe is --**
9 **is correct?**

10 A I think they all reflect the individual
11 circumstances of those utilities. Gulf, it's my
12 understanding, did a one-time flow-back. Some of the
13 others -- it was applied against storm costs. And some
14 is resulting as partial offset to storm costs and a
15 refund or rate reduction. So, it depends on each
16 company's individual circumstances.

17 For purposes of FPUC Gas --

18 **Q In this spec- -- this specific case, what**
19 **would be the method that you believe is correct for the**
20 **companies?**

21 A For these companies, filing a -- a tariff to
22 reflect either the base-rate reduction or the -- a
23 refund to customers for their tax savings would be
24 appropriate and should result in minimal cost to
25 implement.

1 MS. PONDER: Thank you. That's all.

2 Thank you.

3 COMMISSIONER BROWN: All right. There are --
4 the exhibits associated with this witness have
5 already been entered into the record. And there
6 are no other exhibits that you -- we -- we have not
7 marked nor do we need to.

8 MR. MUNSON: That -- that's correct,
9 Commissioner.

10 I was wondering if I could ask one follow-up
11 question related to that, just one, on recross.

12 COMMISSIONER BROWN: You would like a question
13 to --

14 MR. MUNSON: To the witness.

15 COMMISSIONER BROWN: -- Public Counsel's --
16 well, if I allow that, then I will have to,
17 obviously, allow Public Counsel an opportunity.

18 And if Public Counsel does not have an
19 objection --

20 MS. PONDER: If we're allowed to redirect --

21 COMMISSIONER BROWN: You absolutely will be
22 allowed. I am in a generous mood.

23 MR. MUNSON: Thank you, Commissioner. I -- I
24 do appreciate that -- the exercise of that
25 discretion. I'll be very brief.

1 FURTHER EXAMINATION

2 BY MR. MUNSON:

3 Q Mr. Smith, you mentioned some other utilities
4 that were not -- that are not involved in this -- these
5 dockets, correct?

6 A Yes.

7 Q And are you aware -- you're aware of fact that
8 none of those utilities were under-earning in that case,
9 right?

10 A I don't recall their exact earnings situation.
11 I think they were all earning positive returns. I don't
12 recall exactly where they fell within their particular
13 band.

14 MR. MUNSON: Thank you.

15 COMMISSIONER BROWN: Any --

16 MS. PONDER: No, no further questions.

17 COMMISSIONER BROWN: I don't even know if it's
18 called redirect of redirect or -- all right. So,
19 that will conclude this witness.

20 You -- Mr. Smith, you can be excused.

21 We have no exhibits to address here.

22 So, I would look to staff. Are there any
23 other matters to address in these four dockets?

24 MS. DZIECHCIARZ: There are no other matters.

25 Post-hearing briefs for the remaining contested

1 issues are due December 28th, 2018.

2 COMMISSIONER BROWN: Okay. And then I just
3 want to remind the parties that those post-hearing
4 briefs are to only address the contested issues.
5 And everyone is well-aware of what those issues
6 are, correct?

7 MS. PONDER: Yes.

8 COMMISSIONER BROWN: Okay. Do any of the
9 parties have any additional matters?

10 MS. PONDER: OPC does not.

11 MS. KEATING: Commissioner, we do not. Thank
12 you.

13 COMMISSIONER BROWN: Staff, nothing --
14 anything --

15 MS. DZIECHCIARZ: We're good.

16 COMMISSIONER BROWN: -- else? All right. If
17 there -- hearing that there are no --
18 Commissioners, any concluding matters you'd like to
19 part with? All right. Seeing none, we are
20 officially adjourned.

21 Thank you and --

22 MS. KEATING: Thank you.

23 COMMISSIONER BROWN: Have a good day.

24 (Whereupon, proceedings concluded at 11:49
25 a.m.)

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CERTIFICATE OF REPORTER

STATE OF FLORIDA)
COUNTY OF LEON)

I, ANDREA KOMARIDIS, Court Reporter, do hereby
certify that the foregoing proceeding was heard at the
time and place herein stated.

IT IS FURTHER CERTIFIED that I
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I FURTHER CERTIFY that I am not a relative,
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financially interested in the action.

DATED THIS 6th day of December, 2018.



ANDREA KOMARIDIS
NOTARY PUBLIC
COMMISSION #GG060963
EXPIRES February 9, 2021