Attachment A

Agenda Date: 7/16/03
Agenda Item: 2A

STATE OF NEW JERSEY
Board of Public Utilities
Two Gateway Center
Newark, NJ 07102
www.bpu.state.nj.us

ENERGY

IN THE MATTER OF THE VERIFIED PETITION OF ROCKLAND ELECTRIC COMPANY FOR THE RECOVERY OF ITS DEFERRED BALANCES AND THE ESTABLISHMENT OF NON-DELIVERY RATES EFFECTIVE AUGUST 1, 2003)	FINAL DECISION AND ORDER DOCKET NO. ER02080614
IN THE MATTER OF THE VERIFIED PETITION OF ROCKLAND ELECTRIC COMPANY FOR APPROVAL OF CHANGES IN ELECTRIC RATES, ITS TARIFF FOR ELECTRIC SERVICE, ITS DEPRECIATION RATES, AND FOR OTHER RELIEF)	DOCKET NO. ER02100724

(SERVICE LIST ATTACHED)

BY THE BOARD:

This Final Decision and Order memorializes and provides the reasoning for the action taken by the Board of Public Utilities ("BPU" or "Board") in the above captioned matters, by a vote of five Commissioners at its July 16, 2003 public agenda meeting, which action was summarized in the Board's Summary Order dated July 31, 2003. This Final Decision and Order supersedes the Board's July 31, 2003 Summary Order.

treatment of these items because they are not sufficiently "known and measurable" at this time, the Board is extremely sensitive to and concerned about issues relating to system reliability and, thus, **HEREBY AUTHORIZES** RECO to file a Phase II proceeding on or before September 1, 2004 to address the Upper Saddle River and the Darlington projects and the associated flow-through impacts that the record reflects and the ALJ properly found were not completed in the test year. The Board **HEREBY ORDERS** that RECO shall be permitted to include in this Phase II filing a request for recovery of the costs of completed reliability enhancements, which enhancements it had sought in this case, but which the record reflects and the ALJ appropriately concluded, had not actually been performed. The Board **FURTHER ORDERS** that the Phase II proceeding include consideration of whether the Upper Saddle River and Darlington projects provide plant additions necessary for transmission (in which case, they could possibly be subject to FERC regulation) or distribution (in which case, they could be subject to Board scrutiny). RECO shall have the burden of proof with respect to the classification of these facilities, including the appropriateness of including any transmission related investment or expense in distribution rates versus the FERC transmission rate.

b. Consolidated Tax Adjustment

As discussed supra, Staff proposed a consolidated tax savings adjustment reducing RECO's rate base by $1.329 million. (SRB at 13). The supplemented record reflects that, since 1999, RECO has been included in the consolidated federal income tax filings of CEI, along with CEI's other subsidiaries. (S-22). Moreover, even before CEI acquired RECO's parent company, O&R, RECO was included in O&R's consolidated tax returns. (S-19). As a result of filing on a consolidated basis, CEI pays less federal income taxes than it would if each of its subsidiaries filed separately, thus receiving significant tax savings.

Staff asserted that, if tax savings have been achieved by CEI by offsetting the tax losses of the Company's affiliates with positive taxable income from RECO, these savings should be shared with ratepayers. The tax savings are appropriately shared with RECO's customers because, were it not for the positive taxable income collected from ratepayers by RECO and the other regulated utilities within the group, CEI's tax savings would be significantly reduced. (SIB at 64).

It is well-settled law and Board policy that consolidated tax savings are to be shared with customers. I/M/O the Petition of Atlantic City Electric Company for Approval of Amendments to its Tariff to Provide for an Increase in Rates and Charges for Electric Service, Phase II, Docket No. ER90091090J (Order dated October 20, 1992) ("1992 Atlantic Electric Order"); I/M/O the Petition of Jersey Central Power and Light Company For Approval of Increased Base Tariff Rates and Charges for Electric Service and Other Tariff Revisions, Docket No. ER91121820J (Order dated June 15, 1993) ("1993 JCP&L Order"). The New Jersey courts have confirmed that the BPU has "the power and the function to take into consideration the tax savings flowing from the filing of a consolidated return and determining what proportion of the consolidated tax is reasonably attributable to [the utility]." Lambertville Water Company v. New Jersey Bd.

of Public Utility Com'rs, 153 N.J. Super. 24, 28 (App. Div. 1977), reversed on other grounds, 79 N.J. 449 (1979), (citing FPC v. United Gas Pipe Line Co., 386 U.S. 237, 87 S.Ct. 1003, 18 L.Ed.2d 18 (1967)).

In the Board's 1993 JCP&L Order, supra, the Board clearly explained that:

> The Board believes that it is appropriate to reflect a consolidated tax savings adjustment where, as here, there has been a tax savings as a result of the filing of a consolidated tax return. Income from utility operations provides the ability to produce tax savings for the entire GPU system because utility income is offset by the annual losses of the other subsidiaries. Therefore, the ratepayers who produce the income that provides the tax benefits should share in those benefits. The Appellate Division has repeatedly affirmed the Board's policy of requiring utility rates to reflect consolidated tax savings and the IRS has acknowledged that consolidated tax adjustments can be made and there are no regulations which prohibit such an adjustment. The issue, in this case, is not whether such an adjustment should be made, but rather, what methodology should be used to make such an adjustment. In this area, the courts have held that the Board has power and discretion to choose any approach which rationally determines a subsidiary utility's effective tax rate. Toms River Water Company v. New Jersey Public Utilities Commissioners, 158 NJ Super 57 (1978).
>
> Based on our review of the record in this case, the Board **REJECTS** the ALJ's recommendation to accept the income tax expense adjustment proposed by Petitioner and, instead **ADOPTS** the position of Staff that the rate base adjustment is a more appropriate methodology for the reflection of consolidated tax savings. The rate base approach properly compensates ratepayers for the time value of money that is essentially lent cost-free to the holding companies in the form of tax advantages used currently and is consistent with our recent Atlantic Electric decision (Docket No. ER9009190J). Moreover, in order to maintain consistency with the methodology applied in the Atlantic decision, we modify the Staff calculation and find that a rate base adjustment which reflects consolidated tax savings from 1990 forward, including one-half of the 1990 savings, is appropriate in this case.
>
> [1993 JCP&L Order at pages 7-8].

In this proceeding, RECO argued that: (1) it has had negative taxable income due to its deferred BGS balances; and (2) it has not contributed any income to offset losses from unregulated affiliates on a consolidated basis. (Cross-Motion, at 12). Although the ALJ was persuaded by these arguments, for the reasons discussed herein, the Board **HEREBY REJECTS** the ALJ's determination on this issue.

The Board **FINDS** that RECO's arguments were incorrectly based upon data from only the two most recent years. The 1991-2001 time period utilized by Staff is consistent with both the 1992 Atlantic Electric Order, and the 1993 JCP&L Order, supra, and appropriately compensates ratepayers for the value of money that has essentially been lent cost-free to the parent holding companies in the form of currently used tax advantages. In the 1993 JCP&L case, the Board determined that it was appropriate to utilize data from 1990 forward, including one-half the1990 savings. In the 1992 Atlantic Electric case, the Board explained that there may have been a period of time in the mind.-to-late 1980's where investors might have reasonably expected that the Board would not make consolidated tax adjustments because of certain IRS private letter rulings and they may have devised investment strategies based on that expectation. However, the Board further found that, "it is clear that at some point during the 1988-1991 timeframe, investors should reasonably have expected that prospective consolidated tax adjustments would or at least could be made." Therefore, the Board utilized data from 1991 forward, including one-half of the 1990 savings. In this case, Staff used a similar starting point, but began with 1991, in order to start with a full year period.

The Board agrees with Staff that RECO's argument that it would be improper to consider data from the period prior to the date of the merger between O&R and Con-Ed (i.e. July 1999) is not valid. RECO's positive net income during the years 1991-1999 clearly produced tax savings for its parent company in those years, and RECO's customers should not be denied their share of these savings simply because of a subsequent merger of its parent with Con-Ed.

The Board continues to believe that if a utility is part of a conglomerate which profits by consequential tax benefits from the utility's contributions, the utility customers are entitled to have a computation of their fair share of those benefits reflected in their utility rates. This ensures that the Company receives the use of the actual tax dollars saved, while ratepayers are not put in the position of providing the utility with a return on these dollars. Accordingly, the Board **HEREBY ADOPTS** the position of Staff that the $1.329 million rate base adjustment, calculated in accordance with well-settled Board policy, appropriately reflects consolidated tax savings achieved by RECO through offsetting tax losses of affiliates with RECO's positive taxable income. Further, the Board **ORDERS** RECO to submit a consolidated tax adjustment in every future base rate case filing. The future consolidated tax adjustments are to be made utilizing the methodology that Staff utilized to calculate its $1.329 million adjustment as shown on Exhibit 4 of this order.

3. Pro Forma Operating Income

With the exception of certain specific issues discussed in this section, the Board **HEREBY ADOPTS** and incorporates by reference as if completely set forth herein, the ALJ's Initial Decision with respect to RECO's pro forma operating income.

g) Rate Design

The ALJ having made no finding on rate design, the Board **HEREBY ADOPTS** the recommendation of Staff and the Company, and **HEREBY DIRECTS** that the $7.217 million base rate reduction be implemented on an across the board basis, with the exception of a non-contested reduction in the differential in the winter tail block rate for Service Classification No. 5.

VI. EFFECTS OF ALL RATE CHANGES

In addition to reflecting the base rate reduction, the interim recovery of the deferred BGS balance, the revised SBC, the unchanged ECA, as well the expiration of the Temporary Credit implemented as part of the year-four rate reduction mandated by the EDECA, all as provided herein, the Company will implement an increase in its BGS charges effective August 1, 2003 to reflect the results of the statewide auction previously approved by the Board by Order in Docket No. EX01110754 dated February 6, 2003. The Company estimates that for its customers taking "fixed price" BGS service, the effect of all rate changes will be to increase its annual revenue by $19.929 million before application of the 6% New Jersey Sales and Use Tax, and $21.125 million with the tax included, or by approximately 16%. For the average residential customer (SC-1) using 880 kwh per month, the increase is estimated to be about 15.4% (from $85.21 per month to $98.36 per month).

DATED: **4/20/04**

BOARD OF PUBLIC UTILITIES
BY:

SIGNED

JEANNE M. FOX
PRESIDENT

SIGNED

FREDERICK F. BUTLER
COMMISSIONER

SIGNED

CAROL J. MURPHY
COMMISSIONER

SIGNED

CONNIE O. HUGHES
COMMISSIONER

SIGNED

JACK ALTER
COMMISSIONER

ATTEST:

SIGNED
KRISTI IZZO
SECRETARY

ROCKLAND ELECTRIC COMPANY

Source Data

Exhibit 4

Taxable Income /(Loss)	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	Cumulative	
R Orange and Rockland	38,274,936	38,159,031	65,568,063	66,445,393	32,633,033	44,314,738	42,257,257	28,895,310	252,979,653	37,722,810	47,952,636	693,202,862	23.19%
R Rockland Electric Co	12,444,076	6,492,735	1,423,777	1,037,462	4,907,614	4,877,033	8,428,537	16,019,406	15,239,148	(9,922,708)	(13,766,456)	47,180,624	1.58%
R Pike County Light & Power	375,474	39,132	39,800	105,135	421,425	32,270	133,512	191,456	349,559	(825,632)	(463,042)	399,089	0.01%
R Con Edison Company of New York Inc.									809,046,200	564,853,517	874,709,351	2,248,609,069	75.22%
Regulated Subtotal	49,094,486	44,690,898	67,031,640	67,587,990	37,962,072	49,224,041	50,819,306	45,106,172	1,077,614,560	591,827,987	908,432,491	2,989,391,644	100.00%
Clove Dev. Corp	(1,678,732)	563,643	621,049	497,760	557,101	669,370	850,563	825,587	1,087,581	4,799,920	906,450	9,700,272	
O&R Energy Dev	63,178	54,500	(601)	(31,458)	46,575	9,595	8,091	21,939	10,890	9,043		191,752	
O&R Develop	64,177	(695,530)	(673,352)	(478,130)	(515,705)	(453,552)	(382,720)	(1,336,380)	(749)	(594,515)	(1,276,449)	(6,342,905)	
ORIC	372,657	(61,573)	0	0	0	0	0	0	0	0	0	311,084	
Saddle River Holding	(120,743)	(23,006)	36,884	(568,182)	(321,519)	(307,786)	(285,193)	(1,118,794)	(1,548,480)	110,167	20,267	(4,126,385)	
Wickham Group	(286,922)	(214,840)	0	0	0	0	0	0	0	0	0	(503,762)	
Atlantic Morris Broadcasting	(1,100,352)	(1,092,275)	(903,756)	(406,261)	(26,943)	0	0	0	0	0	0	(3,529,587)	
Palisades Management Services	5,938	0	0	0	0	0	0	0	0	0	0	5,938	
Norstar Holding Inc.	4,028,233	2,281,764	1,314,041	782,598	(2,003,458)	(5,150,084)	(15,444,112)	(2,163,572)	(226,646)	0	0	(16,581,236)	
Norstar Management ORE					(785,730)	405,299	115,732	(2,759)	5,078	(67,258)	27,758	(301,880)	
Millbrook Holding	(15,706)	(48,753)	(37,326)	(37,510)	(34,812)	(57,786)	(52,274)	(51,996)	(9,311)	(10,960)	(1,490,756)	(1,847,190)	
Palisades Energy Service			0	0	0	0	(704,547)	(880,845)	(492,058)	(113,544)	0	(2,190,994)	
Compass Resources Inc			0	0	0	0	(19,692)	(2,233)	(3,246)	(4,868)	0	(30,039)	
Enserve Holding							(8,651)	(336,084)	(65,492)	(68,096)	(64,406)	(544,729)	
Con Edison Inc									(196,514)	(38,500,203)	(21,225,940)	(59,922,657)	
Con Edison Energy									1,257,160	5,272,163	6,374,729	12,904,051	
Con Edison Development									(14,124,846)	(46,367,171)	(56,261,951)	(116,753,969)	
Con Edison Solutions Inc.									(10,569,320)	(20,068,340)	1,898,014	(28,739,646)	
Con Edison Communications									(909,131)	(7,641,191)	(19,343,960)	(27,894,283)	
Unregulated Subtotal	1,329,728	763,930	356,939	(241,183)	(3,064,491)	(4,884,944)	(15,922,803)	(5,047,157)	(25,785,084)	(103,244,854)	(90,436,245)	(246,196,164)	
Total Taxable Income (Loss)	50,424,214	45,454,828	67,388,579	67,346,807	34,877,581	44,339,097	34,896,503	40,059,015	1,051,829,476	488,583,133	817,996,247	2,743,195,480	
Total Tax Per Return	17,261,616	15,531,409	23,660,421	23,663,910	12,259,406	15,518,684	12,213,776	14,020,655	368,140,314	171,004,096	286,298,685	286,298,685	

Source Data Calculations

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	Cumulative
Tax Rate	34%	34%	35%	35%	35%	35%	35%	35%	35%	35%	35%	
Taxable Income X Tax Rate	17,144,233	15,454,842	23,586,003	23,571,382	12,207,153	15,518,684	12,213,776	14,020,655	368,140,316	171,004,097	286,298,686	
Unspecified Adjustment	(117,385)	(76,767)	(94,418)	(92,528)	(52,253)	(0)	0	0	2	1	1	(433,347)
sum where cumulative is positive	47,857,527	45,247,468	67,652,088	68,054,292	38,565,748	49,903,006	51,677,960	45,953,678	1,079,970,191	601,909,113	915,713,670	3,012,504,741
sum where cumulative is negative	2,566,687	207,360	(263,509)	(707,485)	(3,688,167)	(5,563,909)	(16,781,457)	(5,894,663)	(28,140,715)	(113,325,980)	(97,717,423)	(269,309,261)

Source: Source Data = S-21

Con Edison, Norstar Management, & Norstar Holding Data = S-18, Attachment RECO-S-SREV-147-1 (tax liability / .35)

ROCKLAND ELECTRIC COMPANY

Consolidated Tax Savings Adjustment

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	Cumulative	
RECO Taxable Inc/(Loss)	12,444,076	6,492,735	1,423,777	1,037,462	4,907,614	4,677,033	8,428,537	16,019,406	15,239,148	(9,922,708)	(13,766,456)	47,180,624	1 57%
Total Positive-Affiliate Taxable Income (1)	47,857,527	45,247,468	67,652,088	68,054,292	38,565,748	49,903,006	51,677,960	45,953,678	1,079,970,191	601,909,113	915,713,670	3,012,504,741	100 00%
Total Negative-Affiliate Taxable (Loss) (2)	2,566,687	207,360	(263,509)	(707,485)	(3,688,167)	(5,563,909)	(16,781,457)	(5,894,663)	(28,140,715)	(113,325,980)	(97,717,423)		
Statuatory Tax Rate	34%	34%	35%	35%	35%	35%	35%	35%	35%	35%	35%		
Consolidated Tax Savings	872,674	70,502	(92,228)	(247,620)	(1,290,858)	(1,947,368)	(5,873,510)	(2,063,132)	(9,849,250)	(39,664,093)	(34,201,098)		
Alternative Minimum Tax	0	0	0	0	0	0	0	0	0	0	0		
Total Net Savings	872,674	70,502	(92,228)	(247,620)	(1,290,858)	(1,947,368)	(5,873,510)	(2,063,132)	(9,849,250)	(39,664,093)	(34,201,098)	(94,285,982)	
Elimination Adjustments												9,397,240	
Total Net Savings After Eliminations												(84,888,742)	
RECO's % of Positive Affil Tax Inc												1 57%	
Tax Benefit - RECO												(1,329,493)	

	Cumulative
RECO's Adjustment for Dissolved Corps..	
Total Net Savings	(94,285,982)
Elimination Adjustments	9,397,240
Other Misc Tax adjustments	179,816
Total Net Savings after Eliminations	(84,708,926)
RECO's Rounded % of Pos Affil Tax Inc.	1.55%
Tax Benefit - RECO Per (S-18, Attachment RECO-S-SREV-147-1)	(1,312,988)

(1) Sum of taxable income / (loss) during the year from affiliates with postive cumlative taxable income for the 1991 - 1999 period
(2) Sum of taxable income / (loss) during the year from affiliates with negative cumlative taxable income for the 1991 - 1999 period.