



Agenda Date: 12/17/14
Agenda Item: 2A

STATE OF NEW JERSEY
Board of Public Utilities
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ENERGY

IN THE MATTER OF THE BOARD'S REVIEW OF THE)	ORDER OF CLARIFICATION
APPLICABILITY AND CALCULATION OF A)	MODIFYING THE BOARD'S
CONSOLIDATED TAX ADJUSTMENT)	CURRENT CONSOLIDATED
)	TAX ADJUSTMENT POLICY
)	
)	DOCKET NO. EO12121072

Party of Record:

Stefanie A. Brand, Esq., Director, New Jersey Division of Rate Counsel

BY THE BOARD¹:

An incorrect version of the Order in this matter was mistakenly used and sent with a Secretary's letter dated November 3, 2014. That letter indicated the only intended change to the October 22, 2014 Order was a correction to the docket number. As pointed out by Rate Counsel in its November 5, 2014, filing in the Appellate Division, in fact, the inaccurate version of the Order that accompanied the November 3, 2014 Secretary's letter included additional findings. However, the Board Order as originally issued on October 22, 2014, did not include these findings, or any other deviations contained in the version accompanying the November 3 Secretary's letter, nor were these changes ever approved by the Board.

To correct this error and alleviate any confusion, the Board is **HEREBY REISSUING** its Order as originally intended, with only the docket number corrected. Pursuant to R. 1:13-1, an order may be corrected for clerical mistakes arising from oversight or omission at any time, notwithstanding the pendency of an appeal.

The language of the October 22, 2014 Order follows:

By order dated January 23, 2013, the Board of Public Utilities ("Board") directed Board Staff ("Staff") to convene all interested parties to participate in a proceeding to review issues related to the consolidated tax saving adjustment ("CTA") to determine: 1) the continued use by the

¹ President Richard S. Mroz and Commissioner Upendra J. Chivukula have recused themselves due to a possible conflict of interest and did not participate in the deliberations on this matter.

Board of the CTA policy; 2) how to calculate the amount of savings that result from filing a consolidated return; 3) how these savings should be equitably shared between the regulated company and the ratepayers; and 4) if a rulemaking proceeding should be undertaken to establish utility-wide or statewide standards with respect to the implementation of a CTA policy.

To further the review of CTA policy, Staff requested information via Notices of Opportunity to Comment dated March 6, 2013, (attachment 1) and July 25, 2013 (attachment 2). Additionally, a request for information was sent to interested parties on November 1, 2013 (attachment 3). All non-confidential responses to these requests were posted on the Board's website.

Following its review of all information submitted pursuant to these requests, Staff proposed that the current CTA policy remain in effect except as amended by the following:

1. The time period for the calculation of the savings would look back five years from the beginning of the test year;
2. The savings allocation method would allow 75% of the calculated savings to be retained by the company and 25% of the calculated savings to be allocated to the ratepayers; and
3. Transmission assets of the electric distribution companies (EDCs) would not be included in the calculation of the CTA.

At the June 18, 2014 Board agenda meeting, Staff notified the Board of its intention to distribute the proposal to all interested parties. The notice containing Staff's proposal (attachment 4) was published in the New Jersey Register on July 7, 2014 at 46 N.J.R. 1657(a), distributed to interested parties and posted on the Board's website with a request that written comments on the proposed modification of CTA policy be submitted on or before Monday, August 18, 2014.

Positions of the Parties on Staff's June 18, 2014 Proposal

Rate Counsel:

Rate Counsel believes that Staff's proposal: effectively eliminates the CTA for most companies; would result in ratepayers paying "hypothetical" taxes that do not reflect the actual tax liability of the utilities, and thus would not lead to the setting of rates that are just and reasonable; that the distinctions made to achieve the proposed formula are arbitrary and capricious; and that there is no factual basis in the record to establish a look-back period of only five years or a "sharing" that gives the utility the overwhelming majority of the pie. Therefore, Rate Counsel asserts that Staff's proposal should be rejected.

Rate Counsel acknowledges that some adjustment of the CTA calculation may be appropriate as the current methodology has at times led to very significant adjustments that the Board may wish to correct. The Board is not free to arbitrarily select inputs to the calculation to practically eliminate the CTA, as it believes is the case with the Straw Proposal. Rate Counsel submits some alternative criteria that may be used to calculate a modified CTA. These criteria have a rational basis in the law, and would result in a fair sharing of the benefits of consolidated taxes between ratepayers and shareholders, if adopted. (Rate Counsel Comment at 2)

Rate Counsel believes that it is well-established law in New Jersey that the savings associated with a utility's participation in a consolidated tax group must be shared with the utility's customers and that the CTA likewise represents sound ratemaking policy. (Id. at 4-5)

Rate Counsel believes that because New Jersey ratepayers will continue to pay what they describe as fictitious income tax expenses in rates while receiving little or no CTA benefit, the Straw Proposal fails to meet the Board's statutory obligation to set just and reasonable rates. (Id. at 6)

Rate Counsel states there are three electric utilities, three gas utilities, and one combined gas/electric utility in New Jersey. If all seven of those utilities currently had pending base rate cases, five of the seven – Public Service Electric and Gas Company, Atlantic City Electric Company, Jersey Central Power & Light Company, South Jersey Gas Company, and Elizabethtown Gas - would not be subject to a consolidated tax adjustment under the Straw Proposal. The State Supreme Court has ruled that the tax benefits flowing from the filing of a consolidated tax return have to be shared with ratepayers, as a utility is "entitled to an allowance for actual taxes and not for higher taxes that it would pay if it filed on a different basis." Given this precedent, Rate Counsel believes that a proposal resulting in no consolidated tax adjustment for five of the seven New Jersey gas and electric utilities cannot be viewed as "just and reasonable" and is not consistent with the Board's statutory mandate. (Id. at 7)

Regarding the specifics of Staff's proposal, Rate Counsel believes that the selection of a five year look back period is arbitrary since nothing is in the record to support Staff's proposal to use a five year time frame for the calculation of a CTA. Using a five year look back period, negative net income of one or two years can easily outweigh the positive income of the prior years, resulting in no consolidated tax adjustment. The five year look back period thus provides a distorted picture of the true economic activity of the utility and the holding company and results in the collection of millions of dollars each year from ratepayers for the payment of these hypothetical taxes. The five year look back period thus results in an inaccurate measurement of consolidated tax benefits and is unfair to ratepayers. (Id. at 10-11)

Rate Counsel recommends a twenty year look back period which it believes is consistent with federal tax laws which allow losses to be carried forward for 20 years and has a basis in tax law and in regulatory policy. (Id. at 11)

Rate Counsel believes that Staff's proposal to give only 25% of the calculated CTA to ratepayers is not a fair allocation of the tax benefit, because it ignores the fact that the CTA calculation already gives New Jersey ratepayers only an allocated share of the consolidated tax benefit. Ratepayers do not get the entire tax benefit, only a share based on the positive net income of the utility. There is nothing in the record in this proceeding to suggest that a further reduction in the ratepayers' share by 75% is reasonable. (Id. at 12-13) Rate Counsel further asserts that it is important to recognize that the Board is not recommending that 25% of the entire CTA benefit be allocated to ratepayers, but rather that ratepayers receive only 25% of the benefit that they would receive under the current methodology. (Id. at 14) Rate Counsel believes if the Board is determined to reduce ratepayers' share of the consolidated tax benefit, ratepayers should receive at least half of the calculated benefit. It is ratepayers who are paying millions of dollars in tax expense collected by the utility each year which is not going to the IRS but is being passed on to an unregulated affiliate. To allow a greater portion of the benefit to go to shareholders is inequitable and arbitrary and should not be adopted. At the very least, if a further sharing is to be considered, it should be an equal 50/50 allocation. (Id. at 15)

Rate Counsel further believes that if transmission assets are excluded from the Board's consolidated tax calculation, ratepayers will never receive tax benefits accrued through the use of ratepayer funds. Ratepayers are entitled to share in the benefits of the consolidated tax filing. If transmission assets are removed from the calculation, then regulated rates are subsidizing unregulated and unprofitable ventures with no benefit to New Jersey ratepayers. Rate Counsel recommends that the Board continue to include transmission assets in the consolidated tax adjustment. (Id. at 16)

Finally, Rate Counsel believes that if the Board wishes to make "material changes" to its current CTA policy, it must institute an agency rulemaking pursuant to the provisions of the Administrative Procedure Act pursuant to Metromedia, Inc. v. Div. of Taxation, 97 N.J. 313, 331-32 (1984). Ibid

New Jersey Large Energy Users Coalition ("NJLEUC"):

NJLEUC asserts that what distinguishes New Jersey from other jurisdictions that have eliminated use of the CTA is a long, clear and consistent series of appellate court precedents that authorize the Board to utilize a CTA in rate cases involving utilities that are parties to consolidated tax agreements. Therefore, for more than 30 years, the Board has properly responded to the clear and consistent legal authority and appellate precedents and implemented a CTA in each base rate case brought by the State's utilities. (NJLEUC Comment at 1)

NJLEUC believes that the CTA methodology that Staff proposes would result in a negligible, if not zero, CTA for many utilities that file consolidated tax returns. (Id. at 3)

NJLEUC opposes the five year look back proposal because it would establish an unduly limited and arbitrary time period that has no basis in the record, tax law or utility regulatory policy. This limited period would not fully reflect the tax contribution of utility ratepayers and the benefits ratepayers should receive for the resulting rates to be considered just and reasonable. NJLEUC urges the Board to instead adopt a time period for CTAs that is consistent with the pertinent provision of the Internal Revenue Code, 26 U.S.C. 172. This provision permits consolidated tax groups to carry forward losses incurred prior to 1998 for a period of 15 years, and losses incurred after 1997 to be carried forward for 20 years. If the carried losses are not offset against gains during the 20 year period, the losses expire and would no longer be eligible to be used as part of a CTA. (Id. at 4-5)

NJLEUC opposes the proposed sharing arrangement in Staff's proposal as inadequate to fairly compensate ratepayers. NJLEUC is not aware of a record developed in any proceeding that would support a formula for the utilities and ratepayers to share CTA-related savings that departs from the current Rockland CTA methodology which already incorporates a "sharing approach" based upon a "rate base" method that essentially treats the tax benefits derived by the holding company as cost-free capital contributed by ratepayers, with the carrying costs associated with the "loan" credited to ratepayers. (Id. at 5)

NJLEUC opposes the proposed removal of transmission-related utility assets from the calculation of the CTA. The fact that the Board does not have regulatory jurisdiction over utility transmission assets should have no bearing whatsoever on the tax ramifications associated with consolidated tax arrangements between aggregated groups containing both regulated and non-regulated entities. (Id. at 6)

NJLEUC raises as an additional issue the need for the Board to implement a rulemaking proceeding to properly address the CTA on a generic basis. NJLEUC believes that this proceeding is not adjudicative in nature and the decisions to be made regarding the future contours of CTAs in utility rate proceedings are broad and will apply to all of the State's utilities. Because the policies to be adopted in this proceeding would represent broad policy guidelines that would determine the nature and method of calculation of CTAs and would be generally applied on a prospective basis in future rate proceedings, NJLEUC suggests respectfully that the criteria and process to be adopted should be the subject of a rulemaking proceeding. (Id. at 7)

Jersey Central Power & Light ("JCP&L")

JCP&L believes that the Board's current CTA methodology is fundamentally flawed, violates federal tax laws, and its continued application would result in confiscatory rates for JCP&L, and likely for other utilities as well. As such, JCP&L agrees that Staff's proposal, which would lessen the magnitude of the CTA for JCP&L (and likely for other utilities), is clearly a positive development. (JCP&L comment at 2)

However, JCP&L believes that the Staff proposal does not address the fundamental legal and policy flaws inherent in the application of any CTA. Moreover, the proposal addresses some, but not all, of the inherent flaws in the current calculation methodology. Therefore, while JCP&L appreciates Staff's efforts, the Company nonetheless urges the Board to: (1) completely eliminate the imposition of a CTA (either immediately or through a "phase-out period" as discussed below); or (2) in the alternative, build upon Staff's Straw Proposal with additional modifications that address the other flaws in the current CTA calculation methodology. (Id. at 3)

JCP&L's fundamental position continues to be that the Board should completely eliminate the imposition of a CTA in utility rate-setting. It is important to emphasize that there is no legal mandate in New Jersey that requires the Board to implement a CTA during base rate cases or otherwise in the rate-setting process. Title 48 contains nothing that requires a CTA. Similarly, the Board's regulations make no mention of a CTA, let alone require one. While there have been court decisions that affirmed the Board's ability to reflect some impact from a consolidated tax filing in an individual rate case, none of those decisions requires the Board to do so in every case. (Id. at 3 - 4) JCP&L believes that the argument that the Board "must" implement a CTA as a matter of law is clearly erroneous and should not deter the Board from completely eliminating a CTA, as a matter of policy, in the instant proceeding. (Id. at 5)

JCP&L believes that, should the Board determine that it would be more appropriate to eliminate the CTA more gradually, it should consider a five-year phase out. Under this approach, the Board would immediately implement the revised CTA calculation methodology proposed by Staff in any currently pending base rate cases or in any base rate cases that conclude within five years of the date of the final Order in this matter. With respect to any base rate cases that conclude more than five years from the date of the final Order in this case, there would be no CTA applied. (Id. at 6)

JCP&L believes that, should the Board determine to modify the CTA methodology (either in lieu of eliminating a CTA immediately or during a five-year phase out period), the Board should amplify Staff's Straw Proposal by adding the following: ruling that any element of the methodology that is inconsistent with federal tax laws will be eliminated; excluding the impact of all net operating loss carryforwards of unregulated affiliates; eliminating entities that are no

longer part of the consolidated tax group from the calculation; and eliminating tax losses of other regulated utility group members from the calculation. (Id. at 7-8)

Atlantic City Electric Company ("ACE")

ACE believes that the CTA should be eliminated in its entirety and that the imposition of a CTA is inconsistent with encouraging investment and job growth in New Jersey, and runs contrary to sound regulatory practice. Thus, ACE recommends that the Staff Proposal be modified to include a provision requiring the CTA to "sunset" at a specific date. ACE respectfully suggests that a five year sunset period would be reasonable. (ACE Comment at 2) Additionally, ACE believes that the final order in this matter is a vehicle for the Board to provide clarity regarding the mechanics of the CTA calculation, and to consider other specific and targeted CTA refinements. Ibid.

ACE requests that the Board should require that any CTA calculation reflect Internal Revenue Service audit changes, as well as any tax law changes for the applicable tax years. Additionally, the Board should state that the CTA "benefit" will be reduced by the alternative minimum tax paid. Finally, the Board should confirm that net plant book value should be used as the basis in determining the total value of all assets and the value of transmission assets will be eliminated from the CTA calculation for electric distribution companies. In addition, ACE believes that the Board must spell out any modifications to the CTA in sufficient detail to avoid the creation of new areas of controversy. Ibid.

Elizabethtown Gas ("Elizabethtown")

While Elizabethtown continues to believe that the Board should completely eliminate the CTA when establishing base rates for the State's distribution utilities, Elizabethtown nonetheless recognizes that the revised CTA policy will likely reduce the impact of the CTA on individual utilities and thus represents a positive step toward creating a fairer and more equitable ratemaking environment in comparison to the current CTA Policy. (Elizabethtown Comments at 2)

Elizabethtown believes that there is no merit in claims that the Board is somehow required to adopt a CTA. While New Jersey's courts have held that the Board has the authority to include a CTA in determining just and reasonable rates, the courts have never held that the Board is required to do so. On the contrary, Elizabethtown asserts that continuing to utilize a CTA in setting base rates is only lawful to the extent that it permits the Board to establish just and reasonable rates. Ibid.

Elizabethtown states that continued use of a CTA in setting base rates is at cross-purposes with the goal of increasing investment, and that the continuation of a CTA is nothing more than the product of reliance on precedent rather than logic and common sense. The unreasonableness of the continued application of a CTA is demonstrated by the fact that a comprehensive CTA is not currently used in ratemaking by the Federal Energy Regulatory Commission or by regulatory authorities in 47 of 50 states. Ibid.

Assuming that the Board adopts Staff's proposal, other modifications to the calculation of CTAs, analogous to the exclusion of transmission assets for EDCs, may be appropriate for other utilities. Different corporate structures and business models may justify adjustments in the determination of individual utility CTAs within the context of the five year look back and 75%-

25% sharing formula reflected in the revised CTA Policy. Accordingly, Elizabethtown requests clarification that as part of its revised CTA Policy, the Board will allow utilities to make a record concerning their individual circumstances and the way in which those circumstances may affect the application of the revised CTA Policy in individual utility rate proceedings. Ibid.

United Water

The United Water companies continue to believe that utilization of a CTA, as commonly referred to, is inappropriate in the establishment of utility rates and supports the comments made by the New Jersey Utilities Association. However, United Water believes that, if a CTA is to be applied, it is appropriate to have a defined methodology which produces consistent results across electric, gas, and water and wastewater utilities. The proposed modifications meet these needs to a greater degree than before and represent a step in the right direction. (United Water Comment at 1)

United Water also believes that a change in the proposed look back period and/or allocation percentage would likely produce results which are inconsistent between the various utilities and, if such changes are considered, previous recommendations should be considered and adopted thereby establishing an upper boundary of the CTA rate base adjustment for water and wastewater companies.

New Jersey National Gas ("NJNG")

NJNG concurs with the comments of the NJUA that the utilities do not support a CTA in rate-setting proceedings. If the Board does determine to continue with a CTA, a further modification to Staff's proposal is appropriate. Specifically, NJNG believes that non-regulated Renewable Energy investments made in New Jersey should be excluded from the CTA calculation. (NJNG Comment at 1-2)

Associated Construction Contractors of New Jersey ("ACCNJ")

ACCNJ supports the elimination of the CTA and supports proposals to significantly alter its application. ACCNJ believes that the CTA is a barrier to investments across all areas of critical utility infrastructure and that New Jersey should not remain an outlier as the vast majority of states do not utilize the CTA. (ACCNJ Comment at 1-2)

New Jersey Utilities Association ("NJUA")

NJUA views the proposal as a step in the right direction and as recognition by Staff that the current policy is flawed. Nevertheless, the NJUA, on behalf of its participating member companies, continues to hold that application of any CTA in rate setting proceedings is improper. As demonstrated by its white paper submitted with the comments, the NJUA asserts that the CTA is not applied in the vast majority of regulatory jurisdictions and, in recent years, has been explicitly rejected by a number of regulatory commissions where application of a CTA had previously been considered. Most notably, the CTA may negatively impact investment in utility infrastructure. (NJUA Comment at 1-2)

NJUA claims that the Board not only has a rational basis upon which to base its rejection of a CTA, but it has the legal authority to do so. While it has been argued that an adjustment must be made as a "well-settled" matter of law, NJUA claims that there exists no statute or regulation

directing the Board to apply the CTA. Accordingly, a reading of the relevant case law does not reveal a New Jersey court-imposed mandate regarding the application of a CTA. The leading cases concerning the application of a CTA were decided a number of years ago under a tax regime that is different from that which utility companies are subject to today. Notably, the most recent of those cases in which a CTA was upheld was decided 35 years ago. While the cases cited have upheld the Board's authority to provide for the application of a utility's tax savings resulting from a consolidated tax filing, not one included a mandate or established a standard related to such an application. Rather, the courts deferred to the Board's discretion in regard to ratemaking, rather than imposing a duty to impose any particular methodology. (Id. at 2)

NJUA believes that at a time when the State is focused on increasing investment for infrastructure resilience, the CTA reduces investment in rate base, and negatively impacts a utility's ability to attract investment. Additionally, application of a CTA may result in adjustments that appear to have little or no relationship to the actual current and future tax situation of the utility, potentially resulting in unintended consequences and negative impacts on utility credit quality and cost of capital. Ibid.

While NJUA believes that Staff's proposal certainly appears, under most circumstances, to be less onerous than the current policy, the fact remains that New Jersey is one of a very limited number of regulatory jurisdictions (3 of 53) that currently applies a comprehensive CTA. In addition, application of a CTA runs counter to traditional rate making principles and stifles investment in the State's infrastructure. (Id. at 3)

Aqua New Jersey ("AQNJ")

AQNJ supports the elimination of the CTA and notes that New Jersey is one of the few remaining states that utilizes a CTA adjustment. However, the company believes that if the Board continues to utilize a modified CTA, such a policy should be implemented to produce consistent results for all utilities operating in the state. AQNJ believes that the current proposal is a step in the right direction as it appears to be less onerous and punitive in nature and that the modified CTA should be limited by a defined cap. (AQNJ Comment at 1-2)

New Jersey American Water ("NJAWC")

Although NJAWC continues to recommend elimination of the CTA in order to bring New Jersey's regulatory policy on this issue in line with the vast majority of other jurisdictions in the United States, NJAWC endorses the comments of the NJUA, and agrees that Staff's proposal is a step in the right direction. (NJAWC Comment at 1-2)

NJAWC reiterates that the Board should not use a CTA in the rate setting process. The CTA is a disincentive for American Water to invest discretionary capital in New Jersey, driving utility discretionary capital away from the State of New Jersey at a time when the state is actively seeking to increase investment in critical infrastructure. The CTA harms New Jersey's reputation of treating businesses fairly, promoting investment, and supporting reliable utility systems at a time when New Jersey utilities are trying to compete for and attract capital for critical infrastructure improvements. Removing this disincentive for investors in affected utilities will make New Jersey a better place to invest in utility infrastructure. It would provide clarity and greater assurance to investors that utility rates are set based on the cost of utility service – not the structure of the corporate parent, or whether it operates in multiple state jurisdictions. (Id. at 2)

NJAWC believes that Staff's proposal provides substantial CTA mitigation to those electric utilities which have substantial "transmission" operations subject to the jurisdiction of the Federal Energy Regulatory Commission ("FERC") by excluding the financial results of the transmission operations from the electric utilities' CTA calculations. That particular adjustment to the Board's current methodology provides no mitigation to other utilities. NJAWC accepts Staff's proposal to limit the CTA calculation to the previous five years, but notes that while this change does help mitigate some of the more onerous impacts of the current adjustment, this time period is no less arbitrary than that used by the current methodology, and could have unintended consequences on utilities due to factors not currently anticipated by Staff. On balance, however, NJAWC supports this shorter time period in preference to any longer time period. NJAWC supports the final change proposed, to apportion the impact of the CTA at a ratio of 75/25 between shareholders and ratepayers, as this proposed change provides substantive mitigation to the non-electric companies. If the proposed ratio is not adopted by the Board, the substantive mitigation contemplated by Staff in making this proposal would be largely lost, providing little to no relief for the non-electrics. (Id. at 2-3)

Utility and Transportation Contractors Association of New Jersey ("UTCA")

UTCA believes that the CTA is a barrier to investment and is not utilized in the vast majority of states. UTCA also believes that the current CTA approach in New Jersey has resulted in unintended consequences and negative impacts on utility credit quality and cost of capital, which has led to less infrastructure investment. UTCA supports Staff's proposal and believes that it would significantly scale back the application of the CTA on New Jersey utilities. However, UTCA believes that New Jersey should join the overwhelming majority of other states and eliminate the CTA completely. (UTCA Comments at 1-2)

Discussion and Findings

As noted above, the Board opened this proceeding to review the use of the CTA based on its assessment that the current policy, that has its origins in the 1992 Atlantic City Electric base rate case, is producing results that appear to be out of step with current economic developments and tax laws. The current proceeding was intended to explore possible changes to the CTA policy that would more appropriately address the current economic climate while balancing the needs of the utilities and ratepayers and has included multiple requests for information and comments which were ultimately filed by a number of parties including the utilities, Rate Counsel, NJLEUC and other interested groups. The proposed modifications run the gamut from maintaining the status quo to complete elimination of the CTA.

Several commenters raised the issue of the manner by which the Board should make any modifications to the CTA policy. The Board has flexibility to determine how to proceed in matters presented to it, and may use its discretion to choose the most appropriate manner, including by contested case, rulemaking or informal process, based on the issues raised and the potential effects of the resolution. See, In re: Request for Solid Waste Util. Customer Lists, 106 N.J. 508 (1987); In re the Petitions of MP Real Estate LP, Studebaker Submetering, Inc. and the New Jersey Apartment Association for Permission to Check-Meter Water Service, BPU Docket Nos. WO00040254, WO00060360, WO00070510 (June 24, 2004). In determining how to proceed, the Board is mindful that the CTA policy was initially implemented by Board order, with subsequent modifications made in subsequent Board orders. We also note that the interested parties have had four opportunities through the instant matter to submit responses to

detailed information requests by Staff and descriptions of their positions on the CTA, limited only by generous response deadlines. The Board conducted a lengthy and transparent process – including making proposed changes accessible for review and comment -- with the active involvement of a wide range of interested parties. Therefore, the Board believes that any further modifications to the CTA policy should be made in the same manner as past modifications and therefore **FINDS** that the implementation of any modification to its current CTA policy should be done by Board order as the calculation of the CTA will be company specific².

Under the Board's longtime policy, when a regulated utility is part of a holding company structure and is included in the consolidated federal income tax filing of its parent company and, as a result, the parent company and the regulated utility (as well as other subsidiaries) pay less federal income taxes than each would pay if it filed separately, these consolidated tax savings are shared with the regulated utility's customers. This policy was implemented to ensure that when ratepayers pay the tax expense of the utility, they receive some credit for those payments if, as a result of the consolidated tax filing, less taxes are ultimately paid.

The methodology utilized to calculate the CTA in the most recent fully litigated rate case has been used by the Board for approximately twenty years.³ The method used is the so-called "rate base" method which allows the parent company to keep certain tax savings, while requiring the jurisdictional entity to reflect the savings by reducing the rate base upon which the utility's return is determined. The Board determined that this was an appropriate way for the regulated entity to share the benefits resulting from filing a consolidated tax return. The Board reiterates its belief that the rate base methodology remains an appropriate way to share CTA savings. However, the Board believes that to more accurately balance the allocation of the savings, that amount of the calculated CTA savings should be adjusted by utilizing a specific percentage sharing method to be used before any credit is applied.

The current CTA method involves a look-back to 1991 to calculate the required base rate adjustment; however, since that time, both federal income tax laws and the corporate structures of many of the utility companies have changed. It has become clear that the review period has been extended not because of any regulatory rationale but merely by the passage of time. The Board can find no rational basis for the unending extension of the review period, and believes that the implementation of a shorter, fixed review period is necessary to return the impact of the CTA to that which was originally intended. This shorter look-back will mean that the tax adjustment will more closely reflect the current economic state of the utility at the time the CTA is applied.

The Board has determined that, based upon the complete record, there is a sound policy argument for continuing the CTA and concurs with Staff's proposed modifications. We believe that these modifications will accomplish two things: customers will continue to share in the tax

² This is the same kind of procedure adopted by the Board in determining that no rulemaking was required to adopt standards for discount gas service agreements. See, In re: a Generic Proceeding to Consider Prospective Standards for Gas Distribution Utility Rate Discounts and Associated Contract Terms and Conditions, Docket No. GR10100761 (Order dated 8/18/2011)

³ In re: the Petition of Rockland Electric Company for Approval of Changes in Electric Rates, Its Tariff for Electric Service, Its Depreciation Rates, and for Other Relief, BPU Docket No. ER02100724, Order dated April 20, 2004, In re 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.

savings realized by the utility's parent; and a fixed review period will enable the regulated utilities to better plan the tax implications of their filings and investments.

The Board also believes that it is not appropriate to include in the calculations of CTA the transmission portion of an EDC's income since those earnings are not subject to the Board's jurisdiction.

These modifications give recognition to the fact that a fundamental tenet of utility regulation is that any methodology used by the regulator must result in an end result that is just and reasonable for both ratepayers and shareholders. Continuing application of the Board's existing CTA policy may not be the appropriate means of achieving that fundamental principle. We believe that the modifications proposed by Staff strike an appropriate balance between the interests of the regulated utilities and their customers.

Based on the complete record in this proceeding, the Board **HEREBY FINDS**:

1. New Jersey regulated utilities, as part of holding companies, are required to reduce rates as a result of a CTA applied during base rate cases to reflect certain tax savings realized by the holding company.
2. Utilities that are not structured as holding companies do not incur the CTA. The vast majority of states do not impose a CTA and neither does the FERC.
3. Changes in the Internal Revenue Code to incentivize wind, solar, renewables, manufacturing, and research and development have caused the CTA to increase to the point that continued use in its current form will discourage investment which is contrary to the State's policies for energy and economic growth.
4. The policy change is being made to encourage economic growth and improve the investment climate in the State.

Therefore, based on the entire record before us, the Board **FINDS** that it is appropriate to continue to include a Consolidated Tax Adjustment in utility base rate filings. The Board the Board also **FINDS** that the current CTA policy shall remain in effect with the following modifications:

1. The review period for the calculation shall be for five calendar years including any complete year that is included in the test year;
2. The calculated tax adjustment based on that review period shall be allocated so that the revenue requirement of the company is reduced by 25% of the adjustment; and
3. Transmission assets of the EDCs would not be included in the calculation of the CTA.

In an ongoing base rate base cases where the record remains open, affected utilities are **HEREBY DIRECTED** to file the calculation of the CTA as modified by this order within the case where it will be subject to review and comment. In pending rate cases where the record has been closed, the Board shall, following an initial decision by the Office of Administrative Law, reopen the record for the limited purpose of adding the calculation of the CTA as modified by this Order while providing all parties with the opportunity to comment.

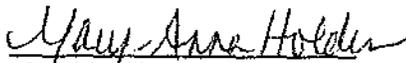
All other affected utilities are **HEREBY DIRECTED** to include a calculation of the CTA, as modified in this Order, as part of their next base rate case petitions. To separately account for FERC regulated transmission services the EDCs are **HEREBY DIRECTED** to utilize, when available, the taxable income related to those transmission services. When taxable income is not available for the relevant time period, the EDCs are **HEREBY DIRECTED** to use the relative rate base figures for FERC regulated transmission services and distribution services as a proxy figure for FERC transmission services taxable income.

DATED: 12/17/14

BOARD OF PUBLIC UTILITIES
BY:



JOSEPH L. FIORDALISO
COMMISSIONER



MARY-ANNA HOLDEN
COMMISSIONER



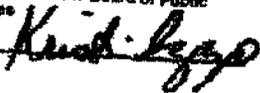
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ATTEST:



KRISTI IZZO
SECRETARY

I HEREBY CERTIFY that the within
document is a true copy of the original
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Utilities



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**In the Matter of the Board's Review of the Applicability and Calculation
of a Consolidated Tax Adjustment
Docket No. EO12121072**

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