Agenda Date: 1/31/18
Agenda Item: 1B

STATE OF NEW JERSEY

Board of Public Utilities
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AUDITS

IN THE MATTER OF THE NEW JERSEY BOARD OF PUBLIC UTILITIES' CONSIDERATION OF THE TAX CUTS AND JOBS ACT OF 2017	)))	ORDER DOCKET NO. AX18010001

Parties of Record

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John Hildabrant, AQUA New Jersey, Inc.
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Stefanie A. Brand, Esq., Director, New Jersey Division of Rate Counsel

BY THE BOARD:

On December 22, 2017, the Tax Cuts and Jobs Act was signed into law by President Trump ("the 2017 Act"). The effective date of the 2017 Act is January 1, 2018.

BACKGROUND

The 2017 Act sets forth changes to the Federal Internal Revenue Tax Code ("Tax Code"). One significant change is the reduction in the maximum corporate tax rate from thirty-five percent (35%) to twenty-one percent (21%) taking effect on January 1, 2018. Based upon the New Jersey Board of Public Utilities' ("Board") review of the 2017 Act, it appears that these changes to the Tax Code will provide savings to New Jersey public utilities and will result in an over-collection of tax revenue by the public utilities that will not be paid in federal income taxes. To ensure that ratepayers receive the appropriate benefit from the reduction in taxes collected in rates that will no longer be paid, it is necessary for rates to be adjusted so that utility rates reflect the effective federal corporate tax rate. First, the new tax rate will have a direct impact on the grossing up of the revenue requirement established and approved by the Board in setting rates. In addition, the change in the tax rate may have an impact on other rate factors, including the accumulated deferred income tax.

DISCUSSION

The Board is charged with the authority to ensure that the regulated utilities' rates charged to ratepayers are just and reasonable. To ensure that rates are appropriately set, it is important to understand the implications of the new tax rate and the 2017 Act. When the Board sets rates in base rate cases and in certain annual/periodic clauses, utilities are permitted to gross up their revenue requirement based on the corporate tax rate. In developing the revenue requirement, other ratemaking elements are also affected by the corporate tax rate. In consideration of the reduction in tax rate and benefits from the 2017 Act, the rate revenue resulting from expenses relating to taxes reflected in rates but no longer owed as the result of the 2017 Act shall be passed onto the ratepayers. In reviewing the impacts of the 2017 Act, the Board **HEREBY ADVISES** that the Board will make any rate changes resulting from the 2017 Act effective January 1, 2018, to be consistent with the effective date of the 2017 Act.

To ensure that the ratepayers receive the appropriate reduction in tax expense, the Board **HEREBY DIRECTS** the utilities to defer with interest the effects of the 2017 Act on the books and records effective January 1, 2018, which is consistent with the effective date of the 2017 Act. The interest shall be calculated using the company's short term debt on the deferral related to the revenue requirement adjustment from the tax rate of 35% to the tax rate of 21%. Interest on the deferral related to the accumulated deferred income tax adjustment and other rate factors shall be at the company's overall allowed weighted average cost of capital. This will preserve the effect and ultimately pass the reduction in the revenue requirement to ratepayers for expenses relating to taxes reflected in rates but no longer owed. The deferral shall be the difference between a tax rate of 35% and 21% and its impact on both expense and on the flowback of excess accumulated deferred taxes. This will allow the Board to fully examine the full effect of the 2017 Act.

Therefore, the Board **HEREBY COMMENCES** a proceeding to examine the impact resulting from the 2017 Act on the utilities and the current rates under the Board's jurisdiction to determine the appropriate level and mechanism by which rates must be adjusted to reflect the benefits resulting from the 2017 Act as well as the interest rate calculation on the deferred account. Each affected public utility is **HEREBY DIRECTED** to submit to the Board no later than March 2, 2018, a Petition with a detailed calculation of the impact resulting from the 2017 Act on the revenue requirement by comparing the latest Board approved test year data and supporting data attached to settlements under the old and new tax laws, and on the revenue requirements collected through annual/periodic clauses comparing the annual data under the old and new tax laws. The affected utilities are **FURTHER DIRECTED** to base the calculation upon the following items:

1. The effects resulting from the 2017 Act shall be deferred upon the books and records of affected utilities as of January 1, 2018 with interest at the company's overall allowed weighted average cost of capital on the portion related to the accumulated deferred income taxes and at the company's short term debt on the portion related to the

adjustment for grossing up the revenue requirement at the new rate of 21% as opposed to the old tax rate of 35% so that the effects can be passed onto the ratepayers.

2. Provide the tariff rates reflecting the new tax rate at 21% to be effective on April 1, 2018. These rates will be on an interim basis until a final review is complete. In addition, provide the detailed workpapers showing how each rate was developed using the last approved rate design on an inter- and intra-class basis. This April 1, 2018 rate change is intended to stop the continued over-collection of revenues at the old corporate tax rate.
3. The calculation of the effects from the 2017 Act including the deferral related to the accumulated deferred income taxes and other factors, and the associated calculation of interest as set forth above and the deferral related to the adjustment for grossing up the revenue requirement at the new rate of 21% and the associated calculation of the interest as set forth above. Also, the rate mechanism related to refunding the deferrals to ratepayers.
4. The calculation of the deferred account on the portion related to the adjustment for grossing up the revenue requirement shall be computed by comparing income tax expense during the base period defined as the last Board approved rate case or clause orders for the utility to the tax expense results from the provisions of the 2017 Act. The calculation of the deferred account on the accumulated deferred income tax balances and other rate impacts should be based on December 31, 2017 financial results.
5. All work papers and supporting documentation regarding the calculations shall be submitted with the calculations. All documentations shall also be provided in a PDF as well as an excel spreadsheet, with formulas so the Board, its Staff, the Division of Rate Counsel and any other stakeholder intervening or participating in this proceeding may examine the formulas for each line item in the spreadsheets. The calculation shall not be limited to a base rate revenue requirement comparison but shall include a comparison calculation of all rate clauses and other cost recovery mechanisms currently set to reflect the old tax law and recover the federal tax rate of 35% and compared to a revenue requirement using the new tax law and rate of 21% deferring the difference. The calculation shall be shown from the regulated utilities perspective.
6. The utilities shall also identify the proposed treatment of changes, if any, from the 2017 Act to the following areas and provide the underlying calculations:
    a. Tax rate reduction;
    b. Expense and Interest deductions;
    c. Contribution/advances in aid for construction;
    d. Depreciation;
    e. Excess accumulated deferred taxes;
    f. Investment tax credits;
    g. Alternative minimum tax; and
    h. Other elements of the rate affected by the changes in the 2017 Act.
7. As part of the submittal, the affected utilities shall provide rate and tariff design proposals to reflect the revenue requirement changes and any clause changes including proof of revenues, and a bill impact analysis supported by the appropriate back-up data, calculations and rationale for the proposed revenue allocation. The rate design and allocation of the dollar amount adjustment shall be consistent with the inter- and intra-class rate design approved when current rates were established and approved by the Board.

In an effort to develop a full understanding of the effects of the 2017 Act, and the calculations provided by the affected utilities, and for a timely completion of this proceeding, the Board

HEREBY SETS FORTH the following procedural schedule which includes a period of time for discovery and comments by interested stakeholders:

- Motions to Intervene: 02/20/18
- Filing of Petitions with Calculation: 03/02/18
- First Round of Discovery: 03/23/18
- Responses: 04/09/18
- Technical Conference: 04/16/18
- Follow-up Discovery: 04/20/18
- Responses: 05/03/18
- All Comments: 05/17/18
- Reply Comments: 05/24/18
- Settlement Conference: 05/29/18
- Settlement Conference: 05/31/18

The parties are free to examine the amounts of the deferrals and rate adjustment mechanism and the appropriateness of applying the allowed overall weighted average cost of capital on the portion of the deferral related to the accumulated deferred income taxes and short term debt on the portion related to the revenue requirement not being adjusted as of January 1, 2018.

The decision to defer adjustment to rates between January 1, 2018 and March 31, 2018, to defer the adjustment to rates related to the Accumulated Deferred Income Tax and to change rates effective April 1, 2018, is an appropriate manner in which to address the changes from the 2017 Act. The immediate change to rates will stop the continued over-collection of tax revenue while interested stakeholders have the opportunity to examine the calculations of the deferrals so that an accurate additional adjustment to rates can be determined in time for a July 1, 2018 effective date or as soon thereafter as the Board deems appropriate. This approach will ensure that ratepayers receive a timely and equitable treatment of the benefits associated with the 2017 Act. It also minimizes the amount that utilities must maintain as deferred during the pendency of this proceeding. As noted above, the deferral mechanism with the appropriate carrying cost interest allows for additional rate changes.

The proposed interim rate reduction and deferral outlined herein is in the best interests of the public and ratepayers and affected utilities and provides for due process. It allows for ratepayers to ultimately be compensated for the reduction in the tax rate. Any delay in reducing the tax rate would be unfair to ratepayers, however the final process makes ratepayers whole by requiring the deferral to include interest, alleviating concerns regarding the time value of compensation. Setting interim rate reductions will reduce the amount unnecessarily collected, the amount of potential refunds, and the amount deferred by utilities. The anticipated July 1, 2018 effective date for final rates resulting from this proceeding will be made in a timely fashion. Additionally, a company should not enjoy windfall profits during the review period set forth above. Use of the proposed deferred accounting with an interim rate reduction would provide no incentive to delay. Therefore, a deferred accounting approach with an interim rate reduction is the Board's best alternative. It also addresses the issue of timeliness through the calculation of interest and at the same time identifies the proceedings in which the rate adjustments should be made and sets forth a date by which all rate adjustments shall be made. It provides for due process and for the establishment of an accurate rate adjustment.

Now, therefore, the Board, **HEREBY ORDERS** the following:

1. The affected utilities are investor owned gas, electric, water and wastewater companies under the jurisdiction of the Board. In addition, affected utilities shall be those with 2017 revenues equal to or greater than $4.5 million. Each affected utility shall file a petition no later than March 2, 2018 including appropriate calculations as set forth above, proposed interim rates to be effective April 1, 2018, and tariff pages. Additionally, affected utilities shall file proposed final rates, effective July 1, 2018 incorporating all other effects of the 2017 Act.
2. The effects of the 2017 Act shall be deferred upon the books and records of affected utilities as of January 1, 2018 with interest at the company's approved overall weighted cost of capital on the portion related to the accumulated deferred income taxes and at the company's short term debt on the portion related to the adjustment for grossing up the revenue requirement at the new rate of 21% as opposed to the old tax rate of 35% so that the effects can be passed onto the ratepayers.
3. Each affected utility shall provide the tariff rates reflecting, the new tax rate at 21% to be effective on April 1, 2018. These rates will be on an interim basis until a final review is complete. In addition, the utility shall provide the detailed workpapers showing how each rate was developed using the last approved rate design on an inter- and intra-class basis. This April 1, 2018 rate change is intended to stop the continued over-collection of revenues at the old corporate tax rate.
4. Both portions of the effects of the 2017 Act being deferred should continue until the effective date of final rates anticipated to be effective July 1, 2018. Utilities shall submit, with its calculations of the effect of the 2017 Act, the mechanism by which the deferrals will be returned to ratepayers.
5. All documents required to be submitted to the Board, including the March 2, 2018 Petitions and calculations shall be filed with the Board's Secretary and shall also be submitted in electronic and reviewable form including Excel Spreadsheets with formulas to the Directors of the Board's Divisions of Energy, Water and Wastewater and Audits. Additionally, all documents filed with the Board shall also be provided concurrently to Rate Counsel both electronically (and in hard copy if requested).

The Board **HEREBY DIRECTS** that all entities seeking to intervene or participate in this matter file the appropriate application with the Board by February 20, 2018. All such motions to intervene or participate will be considered, in this proceeding as well as in consideration of the individual petitions filed by the utilities pursuant to this Order. As such, any party making such a motion **SHALL**, along with the motion, indicate in which utility's proceeding the party is seeking to intervene or participate.

The Board **HEREBY DIRECTS** that the schedule set forth above shall apply to each of the Petitions filed by the affected utilities pursuant to this Order on or before March 2, 2018.

The Board **HEREBY DIRECTS** that this Order be posted on the Board website and a copy of the Order be circulated to the service list electronically.

In the interest of economy, all parties are **HEREBY DIRECTED** to serve all documents electronically, while still providing hard copies to the Board for those documents which must be filed with the Board, and to any party upon request.

This Order shall be effective February 10, 2018.

DATED: 1\31\18

BOARD OF PUBLIC UTILITIES
BY:

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PRESIDENT

MARY-ANNA HOLDEN
COMMISSIONER

DIANNE SOLOMON
COMMISSIONER

UPENDRA J. CHIVUKULA
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RICHARD S. MROZ
COMMISSIONER

ATTEST:

CARMEN D. DIAZ
ASSISTANT BOARD SECRETARY

I HEREBY CERTIFY that the within
document is a true copy of the original
in the files of the Board of Public Utilities

**IN THE MATTER OF THE NEW JERSEY BOARD OF PUBLIC UTILITIES' CONSIDERATION OF THE TAX CUTS AND JOBS ACT OF 2017
DOCKET NO. AX18010001**

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