STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on August 9, 2018

COMMISSIONERS PRESENT:

John B. Rhodes, Chair
Gregg C. Sayre
Diane X. Burman
James S. Alesi

CASE 17-M-0815 - Proceeding on Motion of the Commission on Changes in Law that May Affect Rates.

ORDER DETERMINING RATE TREATMENT OF TAX CHANGES

(Issued and Effective August 9, 2018)

BY THE COMMISSION:

INTRODUCTION

On December 29, 2017, the Commission issued an Order Instituting Proceeding[1] to address utility rate effects of the tax law changes required by the Tax Cuts and Jobs Act of 2017 (Tax Act), which was enacted on December 22, 2017. The Tax Act made significant changes to the federal income tax structure that materially impact the tax liabilities of New York's utilities, including a 40% reduction of the corporate income tax rate from 35% to 21%. The 2017 Order expressed the Commission's intent that ratepayers should receive the net benefits of the Tax Act's changes, and established a process to ensure that outcome. Through that process, information was gathered from the State's utilities, a technical conference was held, the

[1] Case 17-M-0815, Tax Act Impacts, Order Instituting Proceeding (issued December 29, 2017) (2017 Order).

Department of Public Service Staff filed a proposal[2] for implementing the Commission's intent, and comments were filed on Staff's proposal.

Having completed these steps, this order:

1) Preserves savings from the Tax Act for the benefit of ratepayers via deferral accounting until all net benefits are fully reflected in rates;
2) Requires sur-credits for Consolidated Edison Company of New York, Inc. (Con Edison) (steam), New York State Electric & Gas Corporation (NYSEG), Rochester Gas and Electric Corporation (RG&E), National Fuel Gas Distribution Corporation (NFGD), Corning Natural Gas Corporation (Corning), St. Lawrence Gas Company, Inc. (St. Lawrence), New York American Water, Inc. (NYAW), SUEZ Water New York (SUEZ New York), and SUEZ Water Westchester Inc. (SWW) on October 1, 2018;
3) Requires sur-credits for Con Edison (electric and gas), KeySpan Gas East Corporation d/b/a National Grid (KEDLI) and The Brooklyn Union Gas Company d/b/a National Grid NY (KEDNY) on January 1, 2019;
4) Allows for further consideration of the Tax Act savings to be addressed in the Qualifying New York Manufactures (QNYM) proceeding for the large water utilities;
5) Recognizes the tax benefits in completed and pending rate plans in 2018 and does not require sur-credits for Niagara Mohawk Power Corporation d/b/a National Grid (Niagara Mohawk), Central Hudson Gas & Electric Corporation (Central Hudson), Orange & Rockland Utilities, Inc. (O&R), SUEZ

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[2] Case 17-M-0815, supra, Staff Proposal to Address the Accounting and Ratemaking of the Tax Cuts and Jobs Act Of 2017 (filed March 29, 2018) (Staff Proposal).

Water Owego-Nichols, Inc. (SWON), Forest Park Water Company, Inc and Fishers Island Water Works Corp;

6) Exempts telecommunication, small water and small gas utilities from the refund due to minimal savings;
7) Addresses specific utility proposals and accounting details for the sur-credits; and,
8) Recognizes that the treatment of certain deferred tax savings for 2018 and the unprotected excess deferred income tax balances should be preserved to offset other deferred regulatory asset balances, be used to provide rate moderation of expected future rate increases, and to address cash flow-credit metric impacts.

BACKGROUND

The Tax Act's effects on New York utilities are significant and complicated. The most immediate change, and the one with the most significant impact, is the change from progressive federal corporate income tax rates of 15% to 35% to a flat rate of 21%, which Staff initially estimated would reduce the statewide federal income tax revenue requirement for the major electric, gas, steam and water utilities by $750 million, or a decrease of approximately 3.2% of revenues[3], on an annual basis, when the new corporate tax rate is fully effective. In addition, Staff estimated the deferred federal income tax allowance in rates and carried on utilities' books as of December 2017 exceeds the anticipated future tax liabilities by

[3] Updating from the companies' filed comments, the revised annual revenue requirement savings estimate is approximately $700 million, or a decrease of approximately 2.9% of revenues.

approximately $4.8 billion[4], due to the tax rate reduction to 21%.

While the Tax Act income tax rate reduction will materially reduce major utilities' revenue requirements, the Tax Act also contains provisions that increase revenue requirements of utilities including the elimination of bonus depreciation effective September 27, 2017. Bonus depreciation was a tax incentive that allowed for the immediate deduction of a large percentage of capital investments, and provided a benefit to utilities by allowing the accelerated tax recovery of investments, thereby providing an interest-free cash flow benefit to utilities. Additionally, the Tax Act eliminated the water utility exemption from taxation of customer Contributions in Aid of Construction (CIAC), used to fund plant additions. The last material change impacting utilities, is the modification of the treatment of Net Operating Losses (NOLs). The Tax Act limits carryforwards of NOLs to 80% of taxable income. As evidenced from this summary, the effects of the Tax Act on utility revenue requirements are complicated. While the reduced corporate income tax rate is easily understood on the surface, since the change is from a progressive tax rate structure to a flat rate of 21% for all income levels, the impact on deferred taxes can be much more difficult to calculate. Furthermore, some small utilities might actually experience an increase in tax liability, if their pre-Tax Act tax rate was less than 21%. The change in the taxability of CIACs will increase water utilities' tax liabilities for contributed capital. Finally, the elimination of bonus depreciation will affect utilities' cash flows and require

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[4] Updating from the companies' filed comments, revises the excess deferred tax liability amount to approximately $5.0 billion.

utilities to provide additional capital to support new infrastructure investments.

STAFF PROPOSAL

In its Proposal, Staff was guided by the Commission's actions in response to the Tax Reform Act of 1986 (TRA-86)[5], which was the last major overhaul of the federal tax system and had a similar impact on ratemaking practices, and resulted in utilities deferring the effects of the tax changes until they could be addressed in subsequent rate cases. Because the changes in the Tax Act will materially reduce the costs of the large investor owned utilities, Staff similarly proposed the use of deferral accounting, with carrying charges accruing on accumulated balances, as an interim measure to preserve the net benefits for ratepayers, until the impacts of the tax law changes could be fully incorporated in each utility's next rate filing.[6]

Summary of Major Changes in the Tax Act

Corporate Tax Rate Reduction

One of the most significant changes coming from the Tax Act is the change from progressive tax rates with a top corporate tax rate of 35% to a flat 21% tax rate, effective January 1, 2018. This change will impact utilities' current tax expenses payable as well as deferred tax expenses which are

[5] See Case 29465, Tax Reform Act of 1986, Implementation, Statement of Policy on Accounting and Ratemaking Procedures to Implement Requirements of the Tax Reform Act of 1986 (issued July 7, 1987). (TRA-86 Order)

[6] Staff acknowledged that guidance from the Internal Revenue Service (IRS) through revised tax regulations has not yet been published, therefore the full ramifications of the tax law changes may not be known. There likely will be some additional deferrals that result, once the regulations are known.

recoverable in revenue requirements. Staff recommended that the utilities defer the now-excess revenue requirement amounts contained in rates, noting that utilities that use a non-calendar tax year will have to account for a blended tax rate until the start of their next fiscal year when the statutory rate of 21% becomes fully applicable.

Excess Accumulated Deferred Federal Income Taxes

The change in the corporate tax rate also impacts utilities accumulated deferred income tax balances. Deferred income taxes result from normalization accounting for tax and book timing differences. The majority of deferred tax balances on utilities' balance sheets are associated with accelerated tax depreciation of plant investment. The difference between the ratemaking tax expense and the actual current tax expense in any one year is added to a reserve known as accumulated deferred federal income tax reserve (ADFIT). The Tax Act's reduction of the highest corporate tax rate from 35% to 21% results in excess ADFIT, and represents amounts utilities collected from ratepayers to pay future taxes that, due to the reduction in corporate tax rates, will no longer be needed to satisfy future tax liabilities.

Regarding the excess ADFIT, Staff recommended that the excess amounts be reclassified as regulatory liabilities and passed back to ratepayers. Staff noted that a significant portion of the excess ADFIT is protected by Internal Revenue Service (IRS) regulations, which require an amortization over the remaining book life of the related plant assets. However, the Commission has discretion to determine the amortization of unprotected excess ADFIT amounts. Staff recommended that utilities recalculate their ADFIT under the new framework, identify protected and unprotected amounts, and establish regulatory liabilities for the excess amounts, until the reversal of the protected excess ADFIT is reflected in rates and the amortization of the unprotected excess amounts are addressed in a utility's next general rate change or in a sur-credit filing. The regulatory liabilities related to excess deferred taxes shall be recorded at the revenue requirement (grossed up for income tax effects) value of the accumulated excess deferred taxes.

Bonus Depreciation

Bonus tax depreciation for utilities was eliminated effective September 27, 2017, and utilities will now have to return to modified accelerated cost recovery system (MACRS) tax depreciation for the full value of new investments. Staff indicated that an effect of eliminating bonus depreciation is that prospective levels of deferred taxes from new investments would be lower than the previously assumed levels used to establish the various utility revenue requirements. As a result, utilities will have to finance more of the planned plant investments than anticipated due to the loss of the free cash flow provided by bonus depreciation and will have higher actual rate bases.

Staff stated that the change will result in a revenue requirement deficiency and recommended that the utilities include this offset when calculating the total net benefit impact of the Tax Act.

Net Operating Losses

For ratemaking purposes, the tax impact of NOLs are generally deferred and the balance of the deferred FIT included in rate base. Regarding NOLs, Staff noted that utilities will now realize the benefits of NOLs at the lower 21% tax rate, with the ratemaking treatment to be applied to the 14% excess (35% minus 21%), similar to that applied to other unprotected deferred tax balances. Staff recommended that utilities calculate the offsetting impact of this, and include in the calculation of the Tax Act net benefits.

Contributions in Aid of Construction

TRA-86 made CIACs taxable for utilities, however for water companies this required tax was repealed in 1996. The Tax Act requires CIACs to water utilities to once again be taxable as income. The TRA-86 Order adopted the utility-financing method[7] for electric, gas and telephone companies, and the present-value method[8] for major water companies (Class A).

In its proposal, Staff recommended a departure from the TRA-86 Order for major water companies, proposing instead that major water companies should now use the utility-financing method, like the other industries. In the alternative, if a major water company could show that the utility-financing method would have a significant adverse effect on its finances or customers, when compared to the present value method, the company could use the present value method. For smaller water companies (Classes B, C and D), Staff recommended the present-value method be used, while also allowing for the possibility of using the gross-up method,[9] but only in situations where utility financing sources are not available.

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[7] Under the utility financing method, the utility essentially finances the tax cost over the life of the asset.

[8] Under the present-value method, the amount paid by the developers is the utility's tax on the CIAC minus the present value of the future tax depreciation benefits.

[9] Under the gross-up method, developers pay the taxes associated with CIAC at the time the assets are transferred to the utility.

Ratemaking Approaches and Refund Mechanisms

It was the Commission's intent by instituting this proceeding that the net benefits accruing from the Tax Act would be preserved for ratepayers. These net benefits include the revenue requirement impacts of the change in the corporate federal income tax rate from 35% to 21%, the excess accumulated deferred income taxes related to the change in the corporate federal income tax rate, and the offsetting impacts of the elimination of bonus depreciation.[10] Staff recommended deferral accounting, with interest,[11] be used to preserve all benefits for ratepayers, until the tax changes can be incorporated into each utility's next rate filing. While deferral accounting will capture and preserve the benefits for ratepayers, Staff recognized in consideration of the material levels of annual benefits, that the deferrals should not, linger indefinitely. Staff proposed two options for returning the tax benefits to ratepayers: instituting a sur-credit (refund) which would serve as an offset on customer bills, or reopening existing rate plans for utilities that do not file a rate case in 2018 to adjust rates to reflect the Tax Act's effects.

Staff stated that the sur-credit would reflect the immediate and ongoing tax changes, return any accumulated savings and reduce prospective charges. The advantages of this method are that it can be implemented quickly with minimal effort, and allows the utilities' existing rate plans to operate and continue as intended without reopening them. The possible drawbacks include the potential of credit downgrades in certain

[10] There are other changes stemming from the Tax Act, but Staff indicated it did not anticipate those changes to produce material savings.

[11] Staff recommended utilities use the interest rate for deferrals in their existing rate plans. If no rate exists, a utility's pre-tax rate of return should be used.

situations, largely because of the negative impacts on cash flow, which in turn could lead to a higher cost of capital, and increase rates for some extended period of time.

The advantage of Staff's second option is that rates would be adjusted to reflect the new tax requirements after a comprehensive review by the Commission, allowing for the pass-back of savings to be tailored to each utility's specific circumstances. Staff identifies the disadvantage of this approach as requiring more time to work through the individual rate change filings, resulting in delay of ratepayer benefits, while also leading to disruptions of rate plans, which is not aligned with the goal of minimizing the reopening of existing rate plans.

Between these two refund options, Staff supported the sur-credit. Staff proposed that any utility that has not incorporated the Tax Act changes into its base rates be required to file tariff changes to implement a sur-credit, reflecting both immediate and ongoing effects of the Tax Act changes, to be effective October 1, 2018, unless a utility can demonstrate that the sur-credit would have a negative impact on ratepayers' interests. For any company that has a pending rate filing before the Commission as of October 1, 2018, Staff recommended the immediate and ongoing effects of the Tax Act changes be incorporated into the pending case and the associated revenue requirement(s). In either case, a proposed plan for pass back or amortization of all deferred benefits, including the pass back of the identified excess ADFIT balances would be required.[12]

[12] For the companies who have pending rate filings, Staff indicated that a comprehensive resolution that addresses all of the net benefits resulting from the Tax Act should be incorporated and be addressed in the pending rate case.

Measurement of the Net Benefit

To properly quantify the net revenue requirement benefits, a measurement methodology must be established to determine the income tax expense under both the new and old tax laws. Staff proposed two options to be considered. The first would use the rate year revenue requirement projections that were used to establish utilities' existing rates, and the second would use a utility's actual operating results for the rate year. Staff proposed that the impact of the Tax Act should be measured by the effect on the rate year revenue requirement projections used to set utilities' current rates, rather than the utilities' actual operating results. Staff believed that its preferred approach appropriately captures the differences in the rates customers are currently paying versus rates that would result if the change in tax law were known at the time rates were set, is consistent with provisions of multi-year rate plans and will not provide a benefit to utilities that are underearning nor an excessive benefit to ratepayers if a company is overearning.[13]

Carrying Charge Rate to be Applied to Deferred Net Benefits

Since it will take longer than a year or more to return the tax benefits to ratepayers, Staff proposed using the rate for existing deferrals in a utility's particular rate plan to calculate the carrying costs. If a utility's rate plan does not specify a carrying charge rate, Staff proposed the carrying costs be calculated using the utility's Commission-approved pre-tax rate of return. Staff indicated the use of the Commission-

[13] Under the actual operating results approach, used in 1986 when multi-year rate plans were not common, the difference between tax liabilities on actual earnings under the new and old tax laws was deferred. In effect this approach implicitly captured the tax impacts of all variances from forecasts.

approved pre-tax rate of return not only is supported by the longer-term duration of the pass back of benefits, but also is consistent with the rate base treatment of tax deferrals in ratemaking.

As to the balances on which to apply the carrying cost rate, Staff proposed to include the revenue requirement impact of the following items: the change in the corporate federal income tax rate; any required amortization of the excess accumulated deferred income taxes; and, the carrying cost impacts of the elimination of bonus depreciation and the tax rate reduction impact on use of MACRS.

Financial Considerations/Credit Ratings

Staff noted that the major rating agencies view the credit ramifications of the Tax Act as largely negative for utilities, because once the impacts are reflected in rates, the lower 21% statutory tax rate reduces the amount of cash collected from customers, while the loss of bonus depreciation and lower incremental deferred taxes reduce the amount of "tax equity" available to finance rate base. Because of this, Staff believed some utilities might want to deviate from Staff's proposal in favor of a different mechanism or approach for returning benefits to ratepayers. Under such circumstances, Staff encouraged utilities to include in their comments, detailed cash flow data to substantiate that the alternative approach is in customers' long-term interest.

Special Considerations

Staff acknowledged that the current state of the telecommunication industry justified special treatment for that industry. Because the two largest incumbent local exchange carriers (ILECs), Verizon New York Inc. and Frontier

Telecommunications of Rochester, Inc. are no longer rate regulated, are not receiving State Universal Service Fund (SUSF) support, and are not assured of recovering tax expenses through rates, Staff proposed they be exempted from the deferral and sur-credit requirements. Staff also recommended to exempt the other seven telephone companies (Frontier Communications affiliates and Windstream New York, Inc.) that have agreed not to request SUSF support. Of the remaining 30 ILECs, which also face competitive pressure and are eligible to request and receive SUSF support, Staff recommended that all but nine[14] that receive SUSF support[15] to maintain operations also be exempted. For these nine ILECs, Staff proposed the amount they receive from the SUSF be reduced to reflect the 21% federal tax rate, and that the ILECs reimburse the SUSF for payments made since the Tax Act went into effect.

For water utilities, Staff's analysis determined that only the larger (Classes A and B) utilities will experience material savings from the Tax Act, and recommended that these utilities follow the recommended deferral and sur-credit

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[14] The Staff Proposal recommended eight companies - Chazy and Westport Telephone Corporation (Chazy & Westport); Edwards Telephone Company, Inc. (Edwards); Germantown Telephone Company Inc. d/b/a GTel Teleconnections (Germantown); Newport Telephone Company, Inc. (Newport); Oriskany Falls Telephone Corporation (Oriskany Falls); Pattersonville Telephone Company (Pattersonville); Township Telephone Company, Inc. (Township) and Vernon Telephone Company, Inc. (Vernon). Staff subsequently added Port Byron Telephone Company (Port Byron) to the affected group.

[15] Edwards is not currently drawing from the SUSF but is recovering the revenue requirement established in its last rate case by amortizing a deferred customer liability established because of an ice storm in 1998. See Case 14-C-0402 et al., Port Byron, Edwards and Township – Rates, Order Approving Rate Increases and State Universal Service Fund Support (issued: March 26, 2015), pp. 3-4.

approach. In May 2017, the Commission commenced a proceeding, 17-W-0232, to quantify the impact of the elimination of the Qualifying New York Manufactures credit (QNYM). For companies this is applicable to, the QNYM credit had essentially eliminated New York State income taxes from 2014 through 2017. An amendment to this law reinstated state income taxes for water companies beginning in 2018. It is expected that the amended law will result in a deferred asset, with amounts being owed by customers to the companies. Staff recommended that impacts of the Tax Act, and the net tax benefits that result, be addressed in the ongoing QNYM proceeding for the applicable companies.

Smaller water companies' benefits will likely be less than the administrative cost of preparing and submitting a rate or sur-credit filing to refund ratepayers. Accordingly, Staff recommended that Classes C and D water utilities be exempted from the deferral accounting and sur-credit requirements.

Like water, Staff believed that small gas companies (Classes B, C and D) will not receive material benefits from the Tax Act and should be exempted from the proposed treatment.

UTILITY RESPONSES

Joint Utilities (JU)[16]

The JU's comments consist of a main section addressing the common view of all member utilities, and separate appendices for individual utilities' comments. In the main section of JU's comments, the utilities generally agree with Staff's position on the preservation of benefits through the use of deferral accounting, the revaluing of ADFIT balances to

[16] JU consists of Con Edison, O&R, Central Hudson, Niagara Mohawk, KEDNY, KEDLI, NYSEG, and RG&E, and provided a single response on areas of agreement, as well as appendices for individual utilities.

determine the excess balances to be deferred, the incorporation of the impact of the bonus depreciation change, the treatment of NOLs, and taxation of CIACs, although JU proposes to allow utilities the choice of using an alternative CIAC treatment option if the materiality threshold of ten basis points of common equity is met for a specific project.[17] With respect to the measurement of the net benefit impact of the tax changes, JU agrees the use of revenue requirement projections is appropriate, although there should be no gross up for revenue taxes and uncollectibles in the calculation of the deferred benefit amount. JU further agrees with the Staff Proposal that the carrying charge rate to be applied to the deferral balances should be the rate that is contained in each utility's existing rate plan, or the utility's Commission approved pre-tax weighted average cost of capital if there is no rate provided in the utility's respective rate plan.

The JU argues against imposing a sur-credit, out of concern for future financial stability and unnecessary rate volatility for customers, and instead argues that utilities that are owed large outstanding deferrals, or face known future infrastructure investments, should be allowed to use funds derived from the Tax Act to satisfy these needs, and to mitigate future rate increases. According to the JU' response, managing the impact on cash flows is necessary to insure the maintenance of strong investment grade credit ratings that will benefit both utilities and their customers by reducing overall financing costs and aiding in access to needed capital.

[17] JU indicates the use of the proposed alternative CIAC approach would permit utilities to equitably charge financing costs to the customer causing the tax payment related to the CIAC rather than socializing such financing costs among all customers.

The JU argues that with large-scale public policy projects on the horizon it is an inopportune time to implement ratemaking mechanisms such as Staff's proposed sur-credit, which it suggests could threaten credit ratings. Instead, to relieve pressure on credit ratings the JU argues that balances from the Tax Act savings would best be used to offset the revenue requirement impact of projected capital spending. Accordingly, the individual utilities propose methodologies that address their particular situations in a manner which the JU describes as combining short and long-term benefits to customers while maintaining financial stability for the utilities.

Central Hudson

Central Hudson individually states that its current rate plan, adopted by the Commission on June 14, 2018,[18] fully addressed the accounting and ratemaking of the Tax Act changes in determining the electric and gas revenue requirements. The revenue requirements incorporate the lower 21% federal income tax rate, and the accrued benefits for the excess taxes collected from the effective date of the Tax Act change, January 1, 2018, through June 30, 2018 have been deferred for future customer benefit. In addition, Central Hudson disagrees with Staff's recommendation and argues that the deferred benefit amounts should not be grossed up for revenue taxes or uncollectibles.

In its comments, Central Hudson identifies a separate issue not included in Staff's proposal with respect to unbilled revenues, which first became taxable under TRA-86. Central

[18] Cases 17-E-0459 and 17-G-0460, Central Hudson Gas & Electric Corporation - Electric and Gas Rates, Order Adopting Terms of Joint Proposal and Establishing Electric and Gas Rate Plan (issued June 14, 2018).

Hudson does not agree with the regulatory and accounting treatment of deferring unbilled revenues that was implemented by the Commission's TRA-86 Policy Statement, and states now is the appropriate time to revisit the issue.

Con Edison

Con Edison asserts that an October 1, 2018 sur-credit is appropriate for Con Edison's gas and steam services, but that its electric service will have a projected balance of approximately $485 million in under-recovered deferrals on its books as of December 31, 2019, related to interference, supporting infrastructure and property taxes. Con Edison also expects substantial future investments related to energy efficiency, other public policy priorities, storm hardening and resiliency programs. Con Edison notes that imposing a sur-credit for its electric service is not in the long-term interest of customers and would result in unnecessary rate volatility and rate shock when the sur-credit expires, and could affect the company's credit rating. The company would instead amortize the protected excess ADFIT balance over the life of the assets, and the unprotected excess over five years to match the anticipated amortization period of the regulatory asset balances, when base rates are next reset. The tax savings could then be used to mitigate a future rate increase. Con Edison proposes that the benefits related to reduction in annual federal income tax expense for 2018 and 2019 be deferred as a regulatory liability until base rates are reset, and then a five-year pass back could be implemented. In the event the Commission determines an electric sur-credit is necessary, Con Edison indicates the allocation of benefits should be allocated based on each service classification's contribution to annual delivery revenue used to set electric delivery rates.

For its gas service, Con Edison proposes to implement a sur-credit effective October 1, 2018 to begin the pass back of tax benefits to customers until base rates are reset to reflect the changes. The gas sur-credit would include a five-year amortization of the net reduction of annual federal income tax expense for 2018 and 2019, including the offsetting impact of the elimination of bonus depreciation, and the pass back of the excess ADFIT for protected and unprotected balances, be amortized over the remaining book life of its assets. Con Edison proposes to allocate the sur-credit amount to its firm gas service customer classifications based on each service classification’s contribution to annual delivery revenue used to set delivery rates. The sur-credit would terminate when new base rates become effective.

For its steam service, Con Edison proposes to implement a sur-credit effective October 1, 2018, that would include a five-year amortization of the deferred net reduction of annual federal income tax expense for the period January through September 2018, and the pass back of the excess ADFIT for protected and unprotected plant, as well as the collection of the tax benefit asset for unprotected non-plant, all amortized over the remaining book life of existing plant assets. For the reduction in annual federal income tax expense for the period beginning October 2018 and until steam base rates are reset, Con Edison proposes to pass back the current tax benefits on a monthly basis. The sur-credits would be allocated to the company’s firm steam customer service classifications based on each service classification’s contribution to pure base revenue used to set current steam rates.

Orange and Rockland

O&R has electric and gas rate cases pending before the Commission and the company agrees with the Staff Proposal to have the immediate and ongoing effects of the Tax Act changes incorporated in the proceeding when new electric and gas rates are implemented. New rates for O&R are expected to become effective January 1, 2019.[19]

Niagara Mohawk

Niagara Mohawk states that its recently adopted electric and gas rate plans[20] provide more than $75 million of annual Tax Act savings to customers, reflects the new 21% federal income tax rate, including the impact of the elimination of bonus depreciation, and requires a compliance filing quantifying the total impacts of the Tax Act, by March 31, 2019. Niagara Mohawk rates do not currently reflect any amortization of the excess ADFIT, however the company proposes its protected excess ADFIT amounts for electric and gas service be amortized over 50 years, and that its unprotected excess ADFIT balances be amortized and passed back to ratepayers over the average remaining life of the assets, 33 and 31 years for electric and gas respectively, when its rates are reset in 2021.[21] Niagara Mohawk proposes that the deferred benefits that accrued before

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[19] Cases 18-E-0067 and 18-G-0068, Orange and Rockland Utilities, Inc. Electric and Gas Rates, (commenced January 26, 2018).

[20] Cases 17-E-0238 and 17-G-0239, Niagara Mohawk Power Corporation d/b/a National Grid, Order Adopting Terms of Joint Proposal and Establishing Electric and Gas Rate Plans (Issued and Effective March 15, 2018).

[21] Niagara Mohawk will receive an allocation of its service company’s excess ADFIT, and proposes a pass back period of 3.4 years, based on the expected reversal of the underlying assets and liabilities.

its current rate plan became effective (January 1, 2018 – March 31, 2018) be disposed of in its next rate case.

KEDLI and KEDNY

KEDLI and KEDNY's current rates do not reflect the impacts of the Tax Act and are scheduled to increase as part of their current rate plans, in January 2019, and the companies propose, in the interest of rate stability, any sur-credit for the Tax Act savings be delayed until the January 2019 rate changes go into effect. The companies anticipate by implementing the sur-credit at January 1, 2019, there will be offsets to the previously authorized increases of approximately 4.5% for KEDLI and 3.7% for KEDNY. The sur-credits would reflect the tax benefits associated with the prospective changes beginning January 1, 2019 due to the corporate tax rate reduction from 35% to 21%, and the elimination of bonus depreciation. Both KEDLI and KEDNY propose the deferred 2018 savings, as well as any amortization of excess ADFIT, due to the Tax Act changes, be deferred until base rates are next reset in 2020, and be used as a rate moderator to offset future rate increases. KEDLI and KEDNY propose to allocate the sur-credits that will be implemented January 1, 2019 based on each customer service classification's contribution to federal income tax expense in the most recent filed embedded cost of service studies.

NYSEG and RG&E

NYSEG and RG&E oppose the implementation of a sur-credit in October 2018, and instead propose to defer the Tax Act benefits associated with the reduction in the federal income tax rate from 35% to 21%, including the offset for the elimination of bonus depreciation, for 2018, 2019 and up to five months of

2020, to offset the costs of the first five years of their proposed advanced meter infrastructure (AMI) projects,[22] deferred storm costs, unfunded tax obligations, and anticipated future rate increases. The utilities also argue that beginning a sur-credit would harm the utilities' cash flow and credit metrics and cause rate volatility.

While NYSEG and RG&E have identified estimates of the tax benefits associated with excess ADFIT balances separately for both NYSEG and RG&E, they are still in the process of determining the segregation between protected and unprotected balances. The amortization of the ultimately determined protected balances is proposed to be over the life of the plant in service, while the amortization of the unprotected balances, is anticipated to be passed back over the remaining book life or a period of years that aligns with the collection of other regulatory assets.

NYSEG and RG&E are concerned about negative cash flow and credit metric implications of a Commission action requiring sur-credits. They were the only two utilities that provided projections of the cash flow implications of the Tax Act together with the impact on each company's credit metrics. Their analyses indicated a weakening in credit metrics for NYESG and a potentially material weakening for RG&E. Finally, if a sur-credit is required, the Companies request that it only be applicable to their gas businesses, and that the income statement savings be passed back over five years, with interest calculated at the pre-tax rate of return on the deferred balance.

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[22] See Cases 17-E-0058 and 17-G-0059, New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation – AMI (commenced December 20, 2016).

NFGD

In its filed comments[23] NFGD generally agrees with Staff's position on the use of deferral accounting to capture the benefits of the change in corporate tax rate on current and originating deferred tax expense, the revaluation of ADFIT balances to determine the excess ADFIT to be deferred, the reflection of the elimination of bonus depreciation in the net benefit calculation, the revaluation and treatment of NOLs, and taxation of CIACs. However, NFGD identifies one additional offsetting impact that it believes is applicable and should be considered when calculating the net benefits resulting from the Tax Act changes. The company argues that the Tax Act has had the effect of improving the equity ratio of its parent company, National Fuel Gas Company (NFGC, or Parent) which was used to set NFGD current rates, and that this improvement should be reflected prospectively.

NFGD's current rates and Commission-determined revenue requirement were based upon the use of a 42.9% common equity ratio in the capital structure, based on the equity ratio of NFGD's parent.[24] NFGD explains that its Parent's actual equity ratio increased by 500 basis points to 47.9% as of March 31,

[23] In addition to its filed comments, NFGDC has filed a separate petition. NFGD has specifically incorporated by reference that petition into its comments in this proceeding. The petition proposes to implement a customer refund program to return to customers the net benefits, as calculated by the Company, resulting from the implementation of the Tax Act changes. See Case 18-G-0337, National Fuel Gas Distribution Corporation – Refund, Verified Petition of National Fuel Gas Distribution Corporation for Disposition of Income Tax Savings (filed June 4, 2018).

[24] Case 16-G-0257 – Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of National Fuel Gas Distribution Corp. for Gas Service, Order Establishing Rates for Gas Service (issued and effective April 20, 2017).

2018. Additionally, it argues much of the improvement is a result of the passage of the Tax Act. Because of this, NFGD argues that its equity ratio for ratemaking purposes has effectively increased to 45.01% for fiscal year 2018 and to 45.71% for fiscal year 2019. Therefore, NFGD argues, just as the Tax Act's lower federal corporate income tax rate produces benefits that should be passed back to customers, the use of the 45.01% and 45.71% equity ratios should be considered as an offset, when determining the overall net benefits due back to customers, the company asserts that both items are "inextricably interwoven." NFGD believes that ignoring the Tax Act's impact to the company's equity ratio would be akin to single issue ratemaking, a practice it argues is not appropriate.

NFGD agrees with, or does not oppose Staff's proposals on ratemaking issues, specifically the use of revenue requirements to measure the net benefit impact of the tax changes, and the use of the utility's Commission approved pre-tax rate of return as a carrying charge rate on the deferred net benefits, although NFGD indicates it could also be appropriate to use a shorter term carrying charge rate to provide a proper matching of net benefits to the refunds provided to customers.

NFGD supports the use of a sur-credit to provide the pass back of tax change benefits to customers. Included in the company's sur-credit computations are the annual revenue requirement impacts of net benefits for fiscal years 2018 and 2019, the amortization of excess ADFIT for protected balances over the life of the assets, and the amortization of unprotected excess ADFIT balances over five years.[25]

[25] NFGD proposes the sur-credit, or refund, will be calculated annually and updated rates will be effective each October 1 until such time the impacts of the Tax Act changes can be reflected in a new base rate filing, or such other time as ordered by the Commission.

Finally, NFGD proposes that reconciliation of benefits and related deferral accounting treatment should be ongoing, and allowed to capture the impacts of any prospective changes in the federal income tax rates.

Corning

Corning states that it calculates the impact of the Tax Act to be a $69,993 sur-credit to customers for the company's fiscal year starting October 1, 2018, and a $96,180 surcharge for the fiscal year starting October 1, 2019, with a net rate increase of .09% for the two years. Given this minimal amount, Corning proposes that all Tax Act impacts be deferred and disposed of when the company's rates are next reset.

Small Telecom Group[26]

The Small Telecom Group argues that Staff's proposal, as it relates to its members, should not be adopted and that there should be no reduction in SUSF payments to recipients, nor reimbursement made to the SUSF because the utilities have not been able to achieve their authorized returns, because of the declining demand in the regulated telecom industry.

Heritage Hills

Heritage Hills, a water company serving over 2,600 customers, with revenues exceeding $1,000,000, is a Class A water utility. The Company requests that Staff's proposed utility finance method to be used in accounting for the new federal income tax on CIAC not be applicable to it, and instead it be treated as a small water company, with the ability to use

[26] The Small Telecom Group consists of: Chazy & Westport, Germantown, Newport, and TDS Telecommunications Corp for Edwards, Port Byron, Township, and Vernon.

the present value method, and in some cases, the gross-up method. Heritage Hills argues the required use of the utility finance method could create a financial hardship situation.

New York American Water, Inc. (NYAW)

NYAW argues that the savings from the Tax Act should be addressed in conjunction with the current QNYM case[27] addressing a recent change to State income tax law as it applies to water utilities.

In 2014, New York State tax law was changed to reduce the state income tax (SIT) for QNYM to 0%. At the time, water utilities qualified as a QNYM, and the rates for NYAW and the other water utilities were adjusted and accumulated deferred state income (ADSIT) tax was returned to ratepayers. Starting in 2018, water utilities no longer qualified as QNYMs and must reestablish their ADSIT liabilities, and the QNYM Case was established to determine the proper method. On January 11, 2018,[28] a ruling was issued suspending the QNYM case until the present case is resolved.

NYAW estimates the cost of restoring ADSIT is a $15.8 million regulatory asset, and its amount of the regulatory liability related to excess ADFIT (protected and unprotected) is $50.3 million. The company cannot currently segregate the excess ADFIT into protected and unprotected portions, but is working to implement necessary computer software changes to be able to do so. Once the unprotected amount of excess ADFIT can be determined, NYAW proposes to use the ADFIT regulatory

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[27] Case 17-W-0232, Water Utilities – Qualified New York Manufacturers, Notice Establishing Proceeding Concerning Rate Impacts Due to a Change in the Tax Law (issued May 25, 2017) (QNYM Case).

[28] Case 17-W-0232, supra, Ruling Granting Delay (issued January 11, 2018).

liability first as an offset against the restored ADSIT regulatory asset until the regulatory asset is eliminated. At that point, customers would be entitled to credits for the remaining ADFIT regulatory liability. NYAW, however, proposes to not return the net of the federal savings and state costs until its rates are reset.

SUEZ Water New York Inc., SWW, and SWON (collectively, SUEZ)

SUEZ generally agrees with Staff's proposals on Tax Act savings, but notes the ongoing QNYM issue facing it and proposes that both federal and state tax issues be resolved in the QNYM Case. SUEZ also notes that the joint proposal in SWON's current rate proceeding[29] reflects the Tax Act's 21% tax rate.

NON-UTILITY PARTIES

American Association of Retired Persons (AARP)

AARP argues for a rapid return of tax savings to ratepayers, arguing for a deadline of 30 days, with utility rates reduced by the undisputed amounts of the savings, with an ultimate true up after the actual amount is determined. AARP states that New York is behind other states in reacting to the Tax Act.

AARP supports Staff's plan to use deferral accounting for the tax savings until they are returned to ratepayers, but advocates for a one-time refund of the savings, rather than spreading the payment out over time. AARP supports the Staff proposal that the tax benefits resulting from the Tax Act be

[29] Case 17-W-0528, SUEZ Water Owego Nichols Inc. – Rates, Joint Proposal (filed March 30, 2018). The Commission adopted the terms of the joint proposal on July 13, 2018.

calculated retroactively to January 1, 2018 to ensure ratepayers will realize the full benefit of all tax law changes.

As to the rate design of the sur-credit, AARP proposes the rate reductions be equally applied to all rate classes and to all rate components, including reductions to fixed customer charges.

Public Utility Law Project of New York, Inc. (PULP)

PULP supports Staff's proposal to return the savings from the Tax Act, from the date the Tax Act went into effect. PULP requests clarification from the Commission, that the net benefits used in calculating the October 1, 2018 sur-credit will include all current and ongoing benefits beginning with the implementation date of the Tax Act, January 1, 2018 through September 30, 2018. Thereafter, PULP advocates the monthly sur-credit provided to customers should represent the net benefit for the month. PULP indicates the Commission should not approve any proposal to use the net benefits to offset other approved utility costs, but if it does, the determination should be made in the context of a rate case proceeding. PULP does not oppose Staff's proposal that accommodations may need to be made for smaller gas, water and telecom utilities.

Municipal Coalition[30]

The Municipal Coalition supports a pass back period of Tax Act savings to ratepayers of no longer than three years (excluding protected excess ADFIT).

[30] The Municipal Coalition is composed of: the Towns of Clarkstown, Haverstraw, Orangetown, Ramapo and Stony Point, and the Rockland County Solid Waste Management Authority.

Multiple Intervenors[31]

Multiple Intervenors (MI) responds to three aspects of Staff's proposal. First, MI supports Staff's proposal that the benefits from the Tax Act are captured for ratepayer benefit. Second, MI supports returning all Tax Act savings to ratepayers through the implementation of a sur-credit beginning October 1, 2018. Third, MI argues that the sur-credit should be allocated between service classes based on cost causation principles, with savings returned to service classes in the same proportion that service classes contributed to paying the initial tax related expenses.

NOTICE OF PROPOSED RULE MAKING

Pursuant to the State Administrative Procedure Act (SAPA) §202(1), a Notice of Proposed Rulemaking was published in the State Register on April 18, 2018 [SAPA No. 17-M-0815SP1]. The time for submission of comments pursuant to the Notice expired on June 17, 2018, and 1342 comments were received.

State Senator John E. Brooks submitted comments urging the Commission to order rebates to customers as quickly as possible. State Senator David Carlucci argued that ratepayers should receive physical rebate checks rather than lower future rates.

In addition to the senators' comments, 1,342 public comments were received. Of these, 1,334 were form letters stating that the tax savings should be returned to ratepayers, that the Commission was acting too slowly, and that the refund should be retroactive to the beginning of 2018, when the Tax Act

[31] Multiple Intervenors are an unincorporated association of approximately 60 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State.

went into effect. LI Clean Air Water & Soil, Ltd. (CAWS) filed comments stating that New York American Water, Inc. (NYAW) should revise its rates immediately to reflect the lower tax rate, stating that other utilities had already done so, and that NYAW should be penalized for not reducing its rates as the Commission ordered.

The remaining comments argue that the tax savings should be invested in utility infrastructure to reduce costs, used to reduce prospective rates rather than as a one-time credit, that the Commission should ensure that utilities do not attempt to shield the tax windfall from ratepayers, that tax benefits should be flowed through rather than normalized, and that all effects of the tax change should be considered by the Commission.

This order determines how New York utilities' rates reflect the Tax Act's impacts and ensures an appropriate timeline to recognize the benefits of the Tax Act for ratepayers while considering individual utility circumstances and therefore addresses the bulk of the comments received. Regarding CAWS's comments, the Commission notes that this order is the first instance in which the Commission authorizes changes to utilities' rates for the pass back of the tax benefits, and that NYAW has complied with Commission requirements since the proceeding was commenced.

STATUTORY AUTHORITY

Under Public Service Law (PSL) §§65(1), 79(1), 89-b(1), and 91(1), all gas, electric, steam, water and telecommunication utilities are required to provide safe and adequate service at just and reasonable prices. The Commission, under PSL §§66(1), 80(1), 89-c(1), and 94(2) has general supervision of all gas, electric, steam, water and telecommunication utilities. Further, under PSL §§66(4), 79(7), 89-c(3), and 95(2), the Commission has the authority to prescribe uniform methods of keeping accounts, records and books used by all gas, electric, steam, water and telecommunication utilities. Under the broad authority to establish rates granted by the PSL, the Commission has the authority to review utilities' existing rates to determine if they are just and reasonable under current conditions.

DISCUSSION

Staff's Proposal contained recommendations associated with the accounting and ratemaking treatment of the major tax changes required by the Tax Act, preservation of the net benefits, measurement of the net benefits, the ratemaking mechanism to return ongoing and deferred benefits to customers, and the interest rate to be applied to the deferred benefits until the benefits are passed back to customers. The Commission will address each of Staff's recommendations separately.

Corporate Tax Rate Reduction

Staff recommended that the utilities defer the now-excess revenue requirement amounts contained in rates, due to the reduction in the top corporate tax rate of 35% to 21%, with the effective date of January 1, 2018, noting utilities that use a non-calendar tax year will have to account for a blended tax rate until the start of their next fiscal year when the statutory rate of 21% becomes fully applicable. No utility or other party disagrees with Staff's recommendation. NFGD, however, requests that ongoing deferral treatment be approved in the instance that there are additional prospective changes in the federal income tax rate. The Commission sees no need to address NFGD's request at this time. If there are future federal income tax law changes, the Commission will review the impact and materiality of those changes and determine whether generic action is needed. The Commission approves Staff's deferral accounting recommendation.

Excess Accumulated Deferred Federal Income Taxes

Staff recommended that the excess ADFIT amounts be deferred and passed back to ratepayers, with utilities needing to recalculate their ADFIT balances under the new framework, identify protected and unprotected amounts, and establish regulatory liabilities for the excess amounts, until the reversal of the protected excess ADFIT is reflected in rates and the amortization of the unprotected excess amounts are addressed in a utility's next general rate change or in a sur-credit filing. There is no disagreement by the utilities or other parties with Staff's proposal, and the Commission adopts Staff's accounting and ratemaking recommendations for the excess ADFIT created by the Tax Act changes. Deferred tax expenses are allowed in revenue requirements used to establish utility rates. To the extent that amounts provided in rates are no longer needed to satisfy future tax liabilities because of the Tax Act, they should be captured and returned to ratepayers.

Bonus Depreciation

The Tax Act terminates the use of bonus depreciation by utilities as of September 27, 2017, and the Staff Proposal stated that this will result in revenue requirement deficiencies and lower cash flows, and recommended that the utilities include this offset when calculating the total net benefit impact of the Tax Act. Again, all commenting utilities agree and no other parties have opposed Staff's recommendation. The Commission approves Staff's recommendation.

Net Operating Losses

Staff recommended the ratemaking treatment to be applied to the 14% excess (35% minus 21%) associated with NOLs, be similar to that applied to other unprotected deferred tax balances, and that utilities should calculate the impact of this, and include it in the calculation of the Tax Act net benefits. No utility or party disagrees with Staff's recommendation, and the Commission agrees that the impact shall be included in the calculation of the net benefits.

Contributions in Aid of Construction

The TRA-86 Order adopted the utility-financing method as the ratemaking treatment for the taxation on CIACs for electric, gas and telephone companies. The Tax Act provides no change in the taxability of CIACs for any industry other than water, therefore Staff supported no change in the use of the utility-financing method for those industries. Staff recommended a departure from the TRA-86 Order for major water companies, proposing major water companies should now use the utility-finance method, consistent with the other industries. Or, in the alternative, the present value method could be used if it was shown that the utility-finance method would have a significant adverse effect on the utilities' finances or customers. For the smaller water companies (Class B, C and D), Staff recommended the present-value method be used, but also allowed for the possibility of using the gross-up method. Heritage Hills is the only water company to comment on Staff's recommendation.

As a relatively small Class A water utility, Heritage Hills commented that it believes that the requirement that all Class A companies use the utility-finance CIAC accounting method creates financial hardship for it. Heritage Hills requested that the Commission consider classifying it as a small utility, for CIAC accounting purposes. Although the Staff Proposal does allow Class A water companies to use the present-value method where a company can show adverse effects of the utility-finance method, it can be burdensome for relatively small companies, and potentially delay contracts moving forward. As the Commission did with the deferral accounting threshold for the water utilities as discussed below, the annual revenue threshold for requiring the use of the utility financing method for water companies should be increased to $2.5 million, to avoid the need for the smaller Class A companies to file for an accounting waiver.

The JU proposed to be permitted to use the present value method if the CIAC cost associated with a project meets a materiality threshold equal to ten basis points of common equity. The sole reason given by the JU for the proposed change is that this would allow the costs to be charged to the customer causing the tax payment related to the CIAC rather the financing costs to be socialized among all customers.

The Commission is not approving the JU' request. The proposal is outside the scope of this proceeding, which is to address the changes stemming from the Tax Act. The Tax Act does not modify the taxability on CIACs for electric, gas and telephone companies. The Tax Act does however, reduce the rate by which CIACs are taxed by 40%. In light of the significantly lower financing requirements for future CIAC, it appears that the utilities concerns are less significant as a result of the Tax Act. Additionally, there is no justification, support or details provided for the proposal put forth, including why ten basis points is the appropriate materiality threshold. Furthermore, it is unclear if the use of the present-value method would be at the discretion of the utility if the materiality threshold was met. The JU may file a separate, more fully developed, petition if they wish for the Commission to consider such a change.

Ratemaking Approaches and Refund Mechanisms

Measurement of the Net Benefit

To properly quantify the net tax benefits, Staff proposed two measurement methodology options to be considered, the first would use the rate year revenue requirement projections that were used to establish utilities' existing rates, and the second would use a utility's actual operating results for the rate year. Staff's preferred methodology measures the impact of the Tax Act by the effect on the rate year revenue requirement projections used to set utilities' current rates. With the exception of NFGD, the commenting parties either agree with or do not oppose Staff's defined measurement approach to calculate the net tax benefits. In this case, the Commission is determining the impact on rates that customers pay due to the Tax Act changes. It is only appropriate to use the revenue requirements that underlie the tariff rates in place for each utility as the baseline when measuring the Tax Act changes. The Commission therefore adopts Staff's proposed measurement approach to determine the net tax benefits of the Tax Act.

The JU identify a concern and disagreement with Staff's proposed interim benefit calculation to the extent that gross ups for revenue tax and uncollectibles would be required to be included in the calculation. The JU indicate that generally deferrals are not calculated with a revenue tax gross up or uncollectibles, but rather revenue taxes and other gross ups are reflected only when designing new delivery rates. The Commission agrees with the JU that the measured tax benefit deferral should not be grossed up for revenue taxes and uncollectibles. However, the purpose of putting the sur-credits in place is to return excessive collection of delivery revenue requirement to customers. When the delivery revenue requirement for income tax related costs were initially collected from customers, customers also funded the revenue taxes and uncollectible costs associated with the revenue requirement as part of the utility's tariffed rates. It is only appropriate that customers now not only get the net tax benefits returned to them, but also a return of the attached revenue tax and uncollectibles is required to make the customer whole.

Preservation of Benefits

Staff recommended deferral accounting, with interest, be used to preserve all net benefits for ratepayers, until the tax changes are fully incorporated into each utility's rate structures. As Staff noted in its proposal, deferred accounting treatment is often used to address the impacts of material events or transactions that occur between rate proceedings. The Tax Act is a material event that has resulted in a significant reduction of income tax expenses and liabilities of New York State utilities. The Commission previously stated the intent to protect ratepayers' interests, by ensuring that any federal income taxes currently built into rates and accumulated deferred income taxes which, under the Tax Act, would result in excess collection, are captured for ratepayer benefit.

Through the comments filed, the various utilities support the use of deferral accounting to capture and preserve the tax benefits, while no other party has expressed opposition to the deferral accounting recommended by Staff. The Commission is requiring utilities to preserve the net benefits for ratepayers by means of deferred accounting until all net benefits have been reflected in rates.

Refund Mechanisms

The deferred accounting approach will protect ratepayers' interest and preserve the tax benefits but, as Staff recognized in its proposal, returning the tax benefits to ratepayers in a timely manner is also important. Staff provided two options for returning the tax benefits to ratepayers: instituting a sur-credit (pass back tariff), which would serve as an offset on customer bills, or reopening existing rate plans for utilities that have not incorporated tax benefits into revenue requirements or that have not filed a rate case in 2018 to adjust rates to reflect the Tax Act's effects. Between the two refund options, Staff recommended the sur-credit methodology be implemented with an effective date of October 1, 2018, and cited the advantages of adopting this approach.[32] Specifically, this option could be implemented quickly with minimal effort, and would also allow the utilities' rate plans to operate and continue as intended without a need to reopen them.

Many of the utilities argue against imposing a sur-credit, while the non-utility parties, including MI, AARP, PULP, and the Municipal Coalition, support a more timely pass back of the tax benefits to customers. The public comments received urge the tax savings be returned to ratepayers without further delay, retroactive to January 1, 2018 to ensure that ratepayers realize the full benefit of the tax reductions.

[32] For any company that has a pending rate filing before the Commission as of October 1, 2018, Staff recommended that rather than a sur-credit implementation, the immediate and ongoing effects of the Tax Act changes be incorporated into the pending case and the associated revenue requirement(s).

The Commission agrees that the sur-credit is the preferable option, but recognizes that the implementation date of the sur-credit, and the elements of the sur-credit calculation, will not be the same for each affected utility, as explained below.[33]

Sur-Credit Filings

Each commenting utility has proposed its own plan and timeline for the pass back or use of tax benefits. In determining the timing and elements of the sur-credit, various factors and principles need to be identified and considered.

First, consideration should be given as to whether the Tax Act changes have been reflected in a recently approved rate plan, and to what extent.

Second, if there is a pending rate case before the Commission, it may be preferable to incorporate the tax benefits in the pending case, where a more comprehensive resolution of all changes can be addressed.

Third, if there is a scheduled rate change in the near future, delaying implementation of the sur-credit may be in customers' best interests to avoid rate volatility and to mitigate the rate increase.

Fourth, if a utility expects to file a rate case in the near future, and there are large outstanding deferred asset balances to be recovered from customers, or the rate increases are expected to be significant, consideration should be given to allowing some portion of deferred tax benefits to remain on the company's books to mitigate the future rate increase.

[33] For the sur-credit tariff filings required by this Order, each affected utility shall include in that filing all supporting workpapers.

Fifth, if there is a demonstrated cash flow and credit metric concern, customers' long-term interest could be better served by returning the deferred tax savings to ratepayers in a future rate case.

Niagara Mohawk

In its recently adopted rate plans[34], the new 21% federal income tax rate, offset by the change in bonus depreciation has produced more than $75 million of ongoing annual Tax Act savings that are reflected in electric and gas rates and underlying revenue requirements effective April 1, 2018. The remaining tax benefits due back to ratepayers are the tax savings related to the time from January 1, 2018 (effective date of the Tax Act changes) through March 31, 2018, and the amortization of the excess ADFIT balances. Niagara Mohawk, however, indicates it is still trying to determine the protected and unprotected excess ADFIT balances and what the proper amortization of the balances should be, but should have more reliable amounts when its deferred tax computer software project is implemented later this year.

In the recent rate case, a portion of previously deferred regulatory liabilities that the Company had available could not be used as a rate moderator, due to cash flow metrics and credit quality concerns. This portion, approximately 25% of the total deferred credits available, was instead preserved for future rate moderation purposes. These credit quality concerns still exist. Therefore, to avoid any negative implications

[34] Case 17-E-0238 et al., Niagara Mohawk Power Corporation d/b/a National Grid – Electric and Gas Rates, Order Adopting Terms of Joint Proposal and Establishing Electric and Gas Rate Plans (issued March 15, 2018).

related to its cash flow and credit metrics, and to allow the Company to complete its analysis on its excess ADFIT balances, the Commission will not require Niagara Mohawk to implement sur-credits. Most revenue requirement reductions related to the Tax Act changes have already been reflected in Niagara Mohawk's rates. In addition, ratepayers are fully protected, as Niagara Mohawk's rate plan provides for a full reconciliation of the tax benefits, with 100% of the tax savings dedicated to customers.

Central Hudson

In its recently adopted rate plans[35], electric and gas revenue requirements reflect annual ongoing tax benefits of approximately $18 million associated with the lower 21% federal income tax rate effective July 1, 2018. The remaining tax benefits due ratepayers are the tax savings related to the January 1, 2018 through June 30, 2018 time period, and the amortization of the excess unprotected ADFIT balances. However, because a review of Central Hudson's underlying data indicates that the net impact of these two elements would result in a net cost, there is no additional amount to be sur-credited. Instead, Central Hudson shall continue to defer the remaining impact of the tax changes that are not yet reflected in the revenue requirements, and address the disposition of the deferral in its next rate case, as it proposed in its comments.

Central Hudson is the only party that requests ratemaking related to unbilled revenues be considered in this proceeding. Although Central Hudson agrees the tax treatment of unbilled revenues was not changed by the Tax Act, it argues that

[35] Cases 17-E-0459 and 17-G-0460, Central Hudson Gas & Electric Corporation – Electric and Gas Rates, Order Adopting Terms of Joint Proposal and Establishing Electric and Gas Rate Plan (issued June 14, 2018).

it is appropriate to address the subject here because the tax and rate treatment for unbilled revenues was addressed in the Commission's TRA-86 Policy Statement that the Staff Proposal refers to and relies on to make its recommendations in this proceeding.

Unbilled revenues represent amounts owed from customers for service rendered but not yet billed. Prior to TRA-86, unbilled revenues were not taxable for federal income tax purposes and also were not considered by most utilities for either regulatory accounting or ratemaking purposes. TRA-86 called for unbilled revenues to be subject to federal income taxes and the Commission's TRA-86 Policy Statement concluded that it was also appropriate for unbilled revenues to be recognized for regulatory accounting and rate purposes. However, the TRA-86 Policy Statement did not specify how unbilled revenue accounting should be implemented and indicated a separate proceeding would be instituted to address the matter. Such a proceeding has never been instituted but instead the matter has been handled on an individual company basis.

Central Hudson argues the temporary regulatory and deferral accounting treatment prescribed by the TRA-86 Policy Statement for unbilled revenues is not appropriate because: (1) unbilled revenues are excluded from the development of revenue requirements, (2) the Commission properly recognized that unbilled revenues represent amounts owed to the utility for service already rendered to customers but not yet billed, and accrual for such revenues is proper under Generally Accepted Accounting Principles; therefore unbilled revenues cannot be owed back to customers in the form of a regulatory liability, and (3) unbilled revenues fail to meet the definition of a regulatory liability under the Uniform System of Accounts. As such, deferral accounting should have never been ordered related to these accrued revenues and should have instead been recorded as accrued non-cash revenues to the income statement. Based on these facts, Central Hudson requests that the Commission address this issue and provide a policy for unbilled revenues that authorizes proper and consistent accounting and ratemaking treatment of unbilled revenues.

As noted, no other party requested unbilled revenues be addressed in this proceeding. This is because all issues regarding the proper accounting and rate treatment for unbilled revenues have been fully resolved for the other utilities regulated by the Commission except for Central Hudson. In addition, the Commission did address unbilled revenues for Central Hudson in an Order issued in 2016.[36]

The genesis of the 2016 Unbilled Order was a petition filed by Central Hudson requesting to begin reflecting unbilled revenues for regulatory accounting and rate purposes as of a specified date to offset the impact of an alleged unintended error due to incorrect revenue decoupling mechanism targets in its prior rate plan related to the transition from bimonthly to monthly billing that would otherwise result in Central Hudson experiencing a significant earnings shortfall.[37] The 2016 Unbilled Order found allowing the unbilled revenue change would increase revenues by approximately $13 million whereas the unintended error was only about $9 million. As Central Hudson's petition provided no reasons why customers should be denied the benefit of the extra $4 million of revenues provided by Central Hudson's proposal, the Order required Central Hudson to record

[36] Cases 14-E-0318 and 14-G-0319, Central Hudson - Rates, Order Approving Accounting Change with Modifications (issued July 20, 2016) (2016 Unbilled Order).

[37] Cases 14-E-0318 and 14-G-0319, supra, Order Approving Rate Plan (issued June 17, 2015).

the $4 million net revenue impact as a regulatory liability for future customer benefit.

Central Hudson did not file a petition for rehearing to the 2016 Unbilled Order and while it did address that Order in its testimony in its recently concluded rate proceeding, Staff's direct testimony objected to the company's proposal and the $4 million regulatory liability was not addressed in the Joint Proposal ultimately approved by the Commission. As no other party requests the Commission to address unbilled revenues here and Central Hudson has provided no new information or evidence regarding unbilled revenue, the Commission finds no basis for changing its decision in the 2016 Unbilled Order and finds no need to address unbilled revenues in any manner in this proceeding.

O&R

O&R has electric and gas rate filings[38] pending before the Commission, with new rates expected to become effective January 1, 2019. Accordingly, the Commission anticipates that all of the effects of the Tax Act will be incorporated into the revenue requirements with a comprehensive resolution of all net benefits addressed in the proceeding, when the rate case is brought to us for determination. Therefore, the Commission decides not to require sur-credit filings be made by O&R at this time.

Con Edison

The Commission must consider each of Con Edison's businesses, electric, gas and steam, independently to determine

[38] Cases 18-E-0067 and 18-G-0068, Orange and Rockland Utilities, Inc. – Electric and Gas Rates (commenced January 26, 2018).

the appropriate timing of sur-credit implementation, and also the savings elements to be included in the sur-credit calculation.

Con Edison identifies rate volatility and credit rating concerns, as well as concerns of expected large increases in costs and deferral balance recoveries that will be included in its planned January 2019 electric rate case filing (for rates effective January 1, 2020), and recommends no sur-credit be implemented for its electric business, but instead use the tax benefits as a rate moderator in the next rate case.

While the Commission understands Con Edison concerns, the Commission also recognizes the substantial tax savings that Con Edison will realize on an ongoing basis. It is, therefore, not in customers' interest to delay the pass back of savings from electric service until 2020. Con Edison electric has an already approved rate increase that will be effective January 1, 2019, for the third year of its current rate plan, and in the interest of limiting rate volatility for customers, the Commission will allow the sur-credit to coincide with that increase, rather than beginning October 1, 2018. The Commission will limit the sur-credit amount to provide for the annual ongoing savings effective January 1, 2019, to customers. In recognition of the large projected deferral balances and significant cost increases identified by Con Edison that will need to be recovered and reflected in the next rate case, the Commission will allow for continued deferral of the net benefits realized in calendar year 2018, and the excess protected and unprotected ADFIT balances, to be deferred and addressed in Con Edison's next rate case.

For Con Edison's gas business, like its electric business, there is a rate increase effective January 1, 2019, and the Commission authorizes the gas sur-credit to coincide with this increase. However, unlike electric, Con Edison gas does not express a concern as to a projected significant deferred asset balance, therefore, the Commission requires the following tax savings elements be included in Con Edison's gas sur-credit calculation: the annual ongoing savings effective January 1, 2019, an amortization of the calendar year 2018 savings over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below, and an amortization of the protected and unprotected excess ADFIT balances over the life of the assets as proposed by Con Edison. A more comprehensive review of the excess ADFIT balances shall be undertaken in the next rate case, where an alternative amortization period for the remaining unprotected balances may be determined to be appropriate.

For Con Edison's steam business, unlike its electric and gas businesses, there is no anticipated rate change, nor is there the concern of large deferred asset balances on the company's books. The Commission requires an October 1, 2018 implementation date of the sur-credit, with the following tax savings elements included in the company's steam sur-credit calculation: the annual ongoing savings effective October 1, 2018, an amortization of the January 1, 2018 through September 30, 2018 savings over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below, and an amortization of the protected and unprotected excess ADFIT balances over the life of the assets as proposed by Con Edison. A more comprehensive review of the excess ADFIT balances will be undertaken in the next steam rate case, where an alternative amortization period for the remaining unprotected balances may be determined to be appropriate.

KEDLI and KEDNY

KEDLI and KEDNY have already approved rate changes that will take place January 1, 2019. As with Con Edison, in the interest of limiting rate volatility for customers and mitigating the significant rate increases, the sur-credit will be aligned with the timing of the rate increases.

KEDNY and KEDLI both project large deferral balances as of the end of the current rate plans, December 31, 2019, and indicate that the recovery of these balances will need to be addressed in their next rate cases.[39] The two companies propose deferring both the pass back of calendar year 2018 tax savings, and the amortization of excess ADFIT balances, and instead use the benefits as a rate moderator when their base rates are next revised in 2020. In addition, the same situation exists with KEDNY and KEDLI as it does with Niagara Mohawk, in that they are still working to determine the protected and unprotected excess ADFIT balances and what the proper amortization of the balances should be, and expect to have more reliable amounts when its deferred tax computer software project is implemented later this year.

The Commission determines that it is in customers' best interest to allow KEDLI and KEDNY to continue to defer the calendar year 2018 savings, as well as the tax benefits of the excess ADFIT balances, and instead address the disposition of the deferred benefits in the next filed rate case. This will also allow for a more comprehensive review of the excess ADFIT balances, along with the appropriate determination and design of

[39] In the existing rate plans for both KEDNY and KEDLI, amortization of the deferred regulatory asset balances was limited to the site investigation and remediation deferral balances. There was no consideration given at that time to allow for recoveries in the rate plans for any other outstanding deferred asset balance.

amortization periods for the balances. The Commission, therefore, requires KEDNY and KEDLI to implement sur-credits effective January 1, 2019 that provides for the return of only the annual ongoing tax savings on a prospective basis beginning with the January 1, 2019 date.

NYSEG

NYSEG does not believe it is appropriate, nor in the best interests of its customers, to implement a sur-credit at October 1, 2018 for either of its electric or gas businesses, and proposes instead to offset the tax savings with the incremental costs it expects to experience for its AMI project and substantial future infrastructure investments, as well as the large regulatory asset balances for its storm costs it expects to have at the end of its current plan,[40] which ends April 30, 2019. These incremental costs will need to be addressed in its next filed rate case that is expected to be filed no later than May 2019.

While the Commission agrees with the Company that consideration should be given to what potential rate increases are on the horizon, the Commission also recognizes the need to balance that consideration with the fact that the Tax Act has generated substantial savings, and customers are entitled to these savings in a timely manner. It is not appropriate to delay the return of all tax benefits to customers until sometime in 2020, which would be the effective date of any rate change for a rate case expected to be filed by May 2019.

[40] Case 15-E-0283 et al., New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation – Electric and Gas Rates, Order Approving Electric and Gas Rate Plans in Accord with Joint Proposal (issued June 15, 2016).

The Commission, therefore, requires NYSEG to implement an electric service sur-credit on October 1, 2018 to reflect the annual ongoing savings realized by the Company beginning October 1, 2018. In recognition of NYSEG's expected deferred costs and the credit quality implication concerns, the Commission determines that it is in customers' best interest to allow the NYSEG electric business to continue to defer the tax savings realized by the Company from January 1, 2018 through September 30, 2018, as well as the tax benefits of the excess ADFIT balances, and instead address the disposition of the deferred benefits in the next filed rate case. This will allow NYSEG to continue analyzing the proper segregation of excess ADFIT balances into the protected and unprotected portions. This will also allow for a more comprehensive review of the excess ADFIT balances, along with the appropriate determination and design of amortization periods for the balances.

As to NYSEG's gas business, other than the unfunded tax obligations, for which there is already some recovery amount built into rates and an ongoing proceeding[41], there does not exist the same large regulatory asset balance concern. The Commission, therefore, requires a different design of the sur-credit calculation, although the timing of the implementation of the sur-credit will remain the same, October 1, 2018. The sur-credit should reflect the annual ongoing savings realized by the company beginning October 1, 2018, as well as amortization of the January 1, 2018 through September 30, 2018 tax savings over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below. For the same reasons identified for NYSEG's electric business, the Commission

[41] Case 18-M-0013 – Operations Audit to Investigate the Income Tax Accounting of Certain New York State Utilities, (commenced January 11, 2018).

will allow the disposition of the tax benefits of the excess ADFIT balances to instead be addressed in the next filed rate case.

RG&E

Like NYSEG, RG&E proposed to defer all the tax benefits for use in its next filed rate case, which it indicates will be filed no later than May 2019. Removing the matter being addressed in Case 18-M-0013 from the projected regulatory asset balances, RG&E's electric and gas businesses, unlike NYSEG, based on Staff's review, look to have regulatory liabilities that will be due back to customers.

The Commission, therefore applies the same sur-credit criteria for RG&E's electric and gas businesses as was applied to NYSEG gas. The design of the sur-credit calculation will provide for an implementation date of October 1, 2018, and will be required to reflect both the annual ongoing savings realized by RG&E beginning October 1, 2018, and an amortization of the January 1, 2018 through September 30, 2018 tax savings over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below. For the reasons identified for NYSEG's electric and gas business, the Commission will allow the disposition of the tax benefits of the excess ADFIT balances to be addressed in the next rate filing.

NFGD

NFGD proposed to implement a sur-credit effective October 1, 2018 that would flowback the revenue requirement impacts of savings realized by the company from October 1, 2017 through September 30, 2018, a period that aligns with its fiscal year, as well as amortization of both protected and unprotected excess ADFIT balances. Due to the timing of the NFGD's fiscal year, the blended federal income tax rate of 24.5% would apply for the period October 1, 2017 through September 30, 2018, with the statutory federal income tax rate of 21% fully applicable in the next fiscal year period, October 1, 2018 through September 30, 2019. The savings identified by NFGD for the period October 1, 2017 through September 30, 2018 are not what the Commission considers the full run-rate of annual ongoing savings, which should be reflected in the sur-credit when implemented.

Therefore, as with other utilities, NFGD shall implement a sur-credit effective October 1, 2018 that reflects the annual ongoing savings associated with the statutory federal income tax rate of 21% being in place for a full twelve months. In addition, the sur-credit that will be effective October 1, 2018 shall also include amortization of the tax benefits that were required to be deferred through September 30, 2018, over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below, and the amortization of the protected and unprotected excess ADFIT balances as proposed by NFGD in its filed comments. A more comprehensive review of the excess ADFIT balances shall be undertaken in the next rate case, where an alternative amortization period for the remaining unprotected balances may be determined to be appropriate.

With respect to Staff’s proposed methodology for measuring the net benefit, NFGD argues that Staff’s proposal does not provide complete descriptions of the major tax changes as they apply to the revenue requirements and rates charged by investor owned public utilities. Specifically, it argues that the Tax Act directly and materially impacted the equity ratio of its parent NFGC, whose then 42.9% equity ratio was used to establish NFGD’s rates, and that the impact of the Tax Act on that ratio should be reflected in determination of the savings to be returned to customers. NFGD argues that just as the lower income tax rate of 21% is now the proper income tax rate for the Commission to use to reset rates due to the Tax Act, it is likewise proper to use NFGC's equity ratio adjusted to reflect improvements that are directly attributable to the Tax Act.

When NFGD's rates were set on April 20, 2017, the Commission used the Parent's then most recent actual equity ratio of 42.9% as of December 31, 2016. NFGD's stand-alone equity ratio is not used for rate setting purposes because of the lack of financial separation and insulation between it and its riskier parent. In its response to Staff's proposal, NFGD indicates that NFGC's equity ratio has been increasing since its rates were set and that it stood at 47.9% as of March 31, 2018. NFGD attributes a substantial portion of the increase in the parent's equity ratio to the Tax Act, which purportedly contains provisions that are advantageous to NFGC's unregulated businesses.

NFGD projects that for fiscal years 2018 and 2019, the improvement in NFGC's equity ratio due specifically to the Tax Act will be 2.11% and 2.81% respectively. Accordingly, it argues for purposes of calculating the amount of the net savings to be returned to customers, its ratemaking equity ratio be increased to 45.01% and 45.71% respectively, for the two fiscal years. NFGD argues that the additional return associated with the increased equity ratio resulting from the Tax Act must be netted against any tax savings to ratepayers. It argues that such treatment is warranted because the tax rate and the equity ratio are inextricably interwoven.

While the Commission agrees with NFGD that the Tax Act may have had a material impact on NFGC's equity ratio, the Commission finds its proposed treatment unreasonable in several aspects. First, the Commission finds that Staff's preferred methodology for measuring the net benefit, an approach endorsed by every other commenting utility, appropriately captures the direct impacts of the difference in the rates customers are currently paying versus rates that would result if the change in the Tax Law were known at the time rates were set. NFGD's proposal, at best, is an indirect impact of the Tax Act on its unregulated parent, which may not be durable since the parent is free to dividend any benefits from the Tax Act to its shareholders and is not required to preserve the benefits for ratepayers.

NFGD's argument fails to recognize that knowledge of the provisions of the Tax Act when its rates were set in April 2017 would have had absolutely no impact on NFGC's latest known (December 2016) actual capitalization ratios. Use of the latest known actual capitalization ratios of NFGC, as opposed to rate year projections, was reasonable because of the great uncertainty surrounding the financial prospects of NFGC's unregulated businesses. Furthermore, it should be noted that NFGD itself had projected NFGC's equity ratio would fall to 38.2% at September 30,2018.

The Company's proposal is also flawed because it ignores the fundamental link between financial risk and the cost of equity. When NFGD's rates were set and the Commission authorized a return on equity (ROE) of 8.7%, the Commission specifically acknowledged this link when the Commission included in the ROE authorization an adder of 20 basis points in recognition of the increased financial risk implied by utilizing a relatively low 42.9% equity ratio.[42] For these reasons, NFGD's proposal is rejected. If the company desires to have its rates

[42] Case 16-G-0257, National Fuel Gas Distribution Corp. – Rates, Order Establishing Rates for Gas Service (issued April 20, 2017), p. 57.

set using NFGC's improved equity ratio it is completely within its ability to file a rate case.

While this is intended to be a comprehensive resolution to the issues raised by NFGD in its comments, the Commission recognizes that the SAPA comment period has not yet expired and comments received in Case 18-G-0337 will be addressed as appropriate in the future.

Corning

Corning indicates its analysis of the potential tax savings results in minimal amounts and impacts on customer bills, and proposed that all federal income tax change implications should be deferred and disposed of in the company's next rate case filing. Upon review the Commission finds that revenue requirement impacts of the tax benefits are material, and rejects Corning's proposal. Corning shall work with Staff to develop a more accurate estimate prior to submitting its sur-credit tariff filing. Although Corning has an already approved rate increase that will be effective June 1, 2019, for the third year of its current rate plan, the Commission determines it is not in the customers' best interest to delay the pass back of tax savings until its next rate case.[43] Therefore, Corning will be required to implement a sur-credit effective October 1, 2018.

The sur-credit shall reflect both the annual ongoing savings beginning with the October 1, 2018 time period, and an amortization of the savings associated with the corporate income tax rate change to 21% for the period January 1, 2018 through September 30, 2018, over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below.

[43] Case 16-G-0369 - Corning Natural Gas Corporation for Gas Service, Order Adopting Terms of Joint Proposal and Establishing Gas Rate Plan (issued June 15, 2017).

A more comprehensive review of Corning's excess ADFIT balances, for both the protected and unprotected segments, needs to be performed before a determination can be made as to the appropriate amortization periods to be implemented. As with other companies, the Commission will allow the disposition of the tax benefits of the excess ADFIT balances to be addressed in the company's next rate case filing.

St. Lawrence

St. Lawrence did not submit comments to this proceeding, nor did it provide any tax savings calculations. The Commission considers the change in the federal income tax rate from 35% to 21%, to be significant, and it will substantially modify the current federal tax expense payable, deferred tax provisions and the company's revenue requirement. The Commission therefore will require St. Lawrence to implement a sur-credit on October 1, 2018. The sur-credit calculation shall include both the annual ongoing savings beginning with the October 1, 2018 time period, and an amortization of the savings associated with the corporate income tax rate change to 21% for the period January 1, 2018 through September 30, 2018, over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below. Due to a lack of information on St. Lawrence, a more comprehensive review of the company's excess ADFIT balances, for both the protected and unprotected balances, must be performed before a determination can be made as to the appropriate amortization periods to be implemented. Like Corning, we will allow the disposition of the tax benefits of the excess ADFIT balances to instead be comprehensively addressed in the company's next rate case filing.

SUEZ Westchester (SWW)

SWW did not provide any tax savings calculations in its comments. Similar to St. Lawrence, the change in the federal income tax rate from 35% to 21%, is considered to be significant, will substantially modify the current federal tax expense payable, deferred tax provisions and the company's revenue requirement. The Commission therefore will require SWW to implement a sur-credit on October 1, 2018. The sur-credit calculation shall include both the annual ongoing savings beginning with the October 1, 2018 time period, and an amortization of the savings associated with the corporate income tax rate change to 21% for the period January 1, 2018 through September 30, 2018, over a three-year period, unless a cash flow or credit quality concern is demonstrated, as discussed below. SWW is expected to file a rate case in early 2019. Due to both a lack of information on SWW, and the upcoming expected rate filing, a more comprehensive review of the company's excess ADFIT balances, for both the protected and unprotected balances, will be required to be performed as part of the rate case filing and review, with a determination made as to the appropriate amortization periods to be implemented. The disposition of the tax benefits of the excess ADFIT balances shall be comprehensively addressed in the company's next rate case filing.

New York American Water, SUEZ New York

NYAW and Suez New York are involved in the QNYM Case to quantify the impact of the elimination of their QNYM status, which will result in a deferred regulatory asset owed by customers. Staff's Proposal recommended that the impacts of the Tax Act, and the tax benefits that result, be addressed in that ongoing proceeding. Both NYAW and Suez New York filed comments agreeing with Staff's recommendation.

Within the QNYM Case, the parties can look holistically at the two significant tax changes, which have opposite impacts for customers, and make a recommendation on how best to process the revenue requirement impacts of both tax changes. The Commission agrees with Staff's recommendation to have the comprehensive impacts of the Tax Act addressed in the QNYM Case, but finds it should not delay providing customers benefits related to the federal Tax Act via sur-credit. The final determination on disposition of the benefits and costs may reduce the sur-credits, however, that is not reason enough to delay customers the benefits of the Tax Act. The Commission therefore will require NYAW and Suez New York to implement sur-credits on October 1, 2018. The sur-credit calculation shall include both the annual ongoing savings as of October 1, 2018, and a three-year amortization of the deferred savings for the period January 1, 2018 through September 30, 2018, unless a cash flow or credit quality concern is demonstrated, as discussed below.

Sur-Credit Allocation to Service Classes

The Staff Proposal stated that the determination of the appropriate ratemaking mechanism to pass back the net benefits to customers need to be addressed. While Staff recommended the sur-credit approach be implemented to provide the net tax benefits to customers, the Staff Proposal did not specify how the refunds would be allocated between a utility's service classes (SC). In their responses, however, several parties recommended allocation methodologies.

Con Edison gas and steam utilities proposed to allocate the sur-credit amount to their firm gas and steam SCs based on each SC's contribution to annual delivery revenue used to set the companies' firm delivery rates.[44] KEDNY and KEDLI proposed to allocate the respective sur-credit amount to their gas SCs based on each SC's contribution to federal income tax expense in their most recently filed Embedded Cost of Service (COS) Study. NFGD proposed to utilize the revenue requirement increase allocation percentages approved by the Commission in its last base rate case. MI stated that the benefit should be allocated equitably, and in accord with cost causation principles, and should be returned to a utility's various SCs using the same allocation factors that were used to collect corporate federal income tax expense. AARP recommended that rate reductions be equally applied to all rate classes and to all rate components equally, including reductions to fixed customer charges.

The Commission adopts Staff's proposed ratemaking approach to implement a sur-credit for specific utilities, which will minimize disruptions in existing rate plans, and provide customers with the significant tax savings generated by the changes contained in the Tax Act as soon as possible. The Commission has evaluated the SC allocation proposals put forth by the commenters with the goal of developing an allocation methodology that fairly distributes the tax benefits to each utility's SC. To that end, a review of COS study processes and rate case revenue allocation was conducted.

In a rate case the incremental revenue requirement is allocated to each SC based on the base delivery revenue from each SC with adjustments guided from the indications of a COS

[44] Con Edison, while opposed to the Commission refunding the tax savings for the electric customers, had the same proposal for its electric customers if the Commission determined a sur-credit for its electric customers was necessary.

study, which indicates SCs that are over or under contributing to the system. Often, gradual adjustments are made to bring SCs that are over or under contributing to the system closer to the system average rate of return.

COS studies, however, are frequently contentious exercises that are best left to the rate case process. The return results of a COS study produce an average return for the SC, not a return by cost component and the SC’s return is dependent on how the items are allocated to the SC. Moreover, some COS studies are based on a historic period and others are forward looking. Depending on the timing of the COS studies, there may be mismatches in the accrual of the benefit and the indications of the returns of each SC. Many of the current rate plans the utilities are operating under were a result of negotiations with multiple parties and their concerns with the COS results, and those parties made compromises to get to an agreed upon settlement; that balance should not be upset here.

Based on the foregoing and our preference to have a consistent statewide approach, KEDNY and KEDLI, and NFGD’s proposed methodologies to allocate the respective sur-credit amount to their gas SCs, using the allocation of federal income tax expense or the allocation factor used to distribute the incremental revenue requirement stemming from COS studies, will not be used to allocate the sur-credit to each SC. The Commission adopts Con Edison’s proposed approach for each of the affected utilities, which is to allocate the benefits to the SCs based on each SC’s contribution to annual delivery revenue used to set each company’s delivery rates because the method is fair and can easily be applied.

Sur-Credit Rate Design

Con Edison electric proposes to apply the sur-credit to customers' electric bills on a cents-per-kilowatt hour (kWh) basis for non-demand billed customers, on a dollars-per-kilowatt (kW) basis for demand billed customers (for standby service customers, the sur-credit will be applied on a per kW of contract demand basis), and on a monthly basis for customers who are billed on a monthly basis (e.g., NYPA). Con Edison gas and KEDLI/KEDNY propose to apply the sur-credit to the customers' gas bills on a cents-per-therm basis. Con Edison steam proposes to apply the sur-credit to customers' steam bills on a dollars-per-thousand pound (Mlb) basis and on a dollars-per-Mlb/hour basis for customers billed on a per Mlb/hour basis. AARP proposes that rate reductions be equally applied to all rate classes and to all rate components equally, including reductions to fixed customer charges.

The Commission will require electric, gas, steam and water utilities to calculate the sur-credit in the manner in which the utilities bill, on a per kW/kWh[45], therm, or hundred cubic feet (CCF) basis.[46] The sur-credit must be class and voltage-level specific and allocated to the rate classes as discussed herein. The Commission notes that fixed customer charges for residential customers have generally been held constant when utilities rates have been reset. For consistency and ease of application statewide, the refund of the tax benefit allocated to each SC will be given by applying a cent/kWh and/or $/kW (depending upon the specific rate class) credit to the delivery rates of electric customers, a per therm credit to the delivery rates of gas customers, a per Mlb credit to the

[45] Service Classes which are charged both the demand and delivery energy rates will be provided credits for both charges.

[46] Or on another applicable volumetric billing rate.

delivery rates of steam customers, and a per CCF credit to the rates of water customers.

In addition, each utility shall submit a tariff amendment to the Commission implementing the sur-credit on a temporary basis on not less than five days' notice. The tariff amendments shall not become effective on a permanent basis until approved by the Commission.

Sur-Credit Reconciliation

An annual reconciliation will be required once the utility's sur-credit is implemented because the sur-credit rates will be based on normal weather. A variance in customer annual usage from the forecasted normal usage from which each utility's sur-credit rate is established will result in either excessive or insufficient net tax benefits being passed back to customers. Until all aspects of the Tax Act are fully incorporated into base rates and sur-credits are eliminated, the Commission will require an ongoing annual sur-credit reconciliation, and the results to be included in the next year's annual sur-credit calculation, to adjust for prior year activity overages or shortfalls.

Carrying Charge Rate on Deferred Benefits

Staff proposed to calculate carrying charges on the deferred balances using the rate that is applied to other deferred items specified in a utility's rate plan, or if there is no specified rate, the alternative would be to use the utility's Commission approved pre-tax rate of return. The only utility submitting comments that did not affirmatively agree was NFGD, as it believes a shorter term carrying cost rate, such as the other customer capital rate, could be appropriate. The Commission does not agree that a shorter term carrying cost rate should be applied to the deferred tax benefits that will take longer than a year to flow back to customers, and as Staff makes the point, using the pre-tax rate of return is consistent with the rate base treatment of tax deferrals in ratemaking. The Commission adopts Staff's proposal.

As to the deferred balances to which the carrying charge rate is to be applied, Staff proposed to include the revenue requirement impact of the following items: the change in the corporate federal income tax rate; any required amortization of the excess accumulated deferred income taxes; and, the carrying cost impacts of the elimination of bonus depreciation and the tax rate reduction impact on use of MACRS. NYAW makes the point that no carrying charges should be applied to excess ADFIT balances as the amounts are already in rate base providing a credit, and remain in rate base until rates are modified. Therefore, to assess additional carrying charges, is not appropriate. The Commission agrees with NYAW, and clarifies that until a utility's base rates are reset, and the excess ADFIT balances are removed from rate base, there is no need to provide additional carrying charges on this balance. However, if the excess ADFIT balances are not included in rate base, carrying charges should be applied until amortization of the excess ADFIT balances is complete, and customers have received the entire tax benefit. With this caveat, the Commission adopts Staff's carrying charge proposal.

Financial Considerations/Implications

The Staff Proposal noted that utility cash flows are expected to be reduced due to bonus depreciation being eliminated, the refunding of over-collections that occur until new rates are in effect, the return of excess deferred taxes and because the lower tax rate reduces revenue requirements on an ongoing basis. Accordingly, it encouraged the individual utilities to present their unique financial and regulatory circumstances for consideration in support of their proposed method of passing back the net savings to ratepayers. According to the JU response, managing the impact on cash flows is necessary to insure the maintenance of strong investment grade credit ratings that will benefit both utilities and their customers by reducing overall financing costs and aiding in access to needed capital. The JU argues that with large-scale public policy projects on the horizon it is an inopportune time to implement ratemaking mechanisms such as Staff's proposed sur-credit which it suggests could threaten credit ratings. Instead, to relieve pressure on credit ratings, it argues that balances from the Tax Act savings would best be used to offset the revenue requirement impact of the capital spending. Accordingly, the individual utilities propose methodologies that address their particular situations in a manner which the JU describes as combining short and long-term benefits to customers while maintaining financial stability for the utilities.

With respect to submitting detailed cash flow analyses to support alternative approaches for passing back the tax savings, only NYSEG and RG&E did so. According to those two companies, Staff's proposal to provide sur-credits to customers could result in negative watch or credit downgrades with respect to rating agencies views of their securities.

The Commission acknowledges that the prospective cash flow reductions that utilities will experience because of the Tax Act warrant a careful consideration of the methodology for passing back the Tax Act savings to customers. Further, the Commission concurs with respect to the sur-credit approach that individual circumstances may warrant alternative approaches if the pass back of savings through the implementation of a sur-credit is not in customers long term interest. As explained earlier, the Commission's preferred approach for passing back 2018 net tax savings is a three-year amortization. In consideration of the long-term interests of the utilities and ratepayers, however, a longer amortization period, of no more than five years, will be permitted provided a reasonable demonstration that doing so would satisfactorily mitigate any looming credit quality concerns.

The Commission agrees with the JU that strong investment grade credit ratings benefit both utilities and their customers. In fact, credit quality concerns were an integral factor in the methodology employed to pass back savings in recent Niagara Mohawk and Central Hudson rate plans. Likewise, as discussed above, they have factored into the individual utility ratemaking approaches the Commission has determined here to delay some sur-credits and preserve the deferrals associated with 2018 savings and excess ADFIT. In particular, the Commission's approaches for Con Edison, KEDNY and KEDLI acknowledge that each of these companies has had their Moody's ratings outlook revised from "stable" to "negative" as a result of cash flow concerns arising from the Tax Act.[47]

Finally, while neither NYSEG nor RG&E had their outlooks revised downward as a result of the Tax Act, the Commission's approved approach recognizes the credit quality concerns outlined by those utilities. The Commission does note, however, that Moody's expects the financial ratios of both

[47] The Staff Proposal noted that on January 19, 2018, Moody's changed the outlook on 25 US regulated utilities primarily impacted by tax reform. Among them were four New York based utilities. In addition to Con Edison, KEDNY and KEDLI, O&R also had its outlook revised to negative. That company filed for rates earlier this year, the appropriate methodology for passing back tax savings will be decided in that proceeding.

companies to be strong enough to remain above their downgrade threshold on a sustained basis, regardless of the regulatory outcome in this proceeding.[48]

Special Considerations

Telephone Companies

The Small Telecom Group reviewed Staff's analysis and provided its own analysis, claiming to demonstrate that lower levels of revenues, due to competitive subscriber losses since their members' last rate cases, have more than offset any benefit the companies may realize because of the Tax Act.[49] A Department Staff review of the Small Telecom Group's analysis found many issues with the assumptions made and the specific data in the analysis but Staff finds that the Small Telecom Group's final conclusion is reasonable. Any potential net revenue requirement decrease because of the Tax Act income tax rate reduction, would likely be dwarfed by the potential overall revenue requirement increases these companies could justify given the competitive pressures generally affecting the wireline telephone industry. Furthermore, any temporary reduction in SUSF would not inure to the benefit of utility customers, but would simply offset other utility SUSF contributions and extend the SUSF.

The adverse financial condition of these small ILECs is demonstrated by the chart below, which shows that the actual ROE reported by the companies in their respective 2017 Annual Reports was less (and in all but one case much less) than the allowed ROE established in the companies' most recent rate case.

[48] Update to credit analysis: Rochester Gas & Electric Corporation and Update to credit analysis: New York State Electric and Gas Corporation, Moody's Investors Service, June 6, 2018.

[49] Small Telecom Group Comments, Attachments A-C.

Company	Actual 2017 Intrastate ROE	Allowed Intrastate ROE	Difference
Chazy & Westport	-14.49%	6.02%	-20.51%
Edwards	-5.53%	5.33%	-10.86%
Germantown	-14.76%	6.15%	-20.91%
Newport	-21.38%	6.00%	-27.38%
Pattersonville	-11.90%	6.25%	-18.15%
Port Byron	-6.70%	6.26%	-12.96%
Township[50]	4.91%	6.36%	-1.45%
Vernon/Oriskany[51]	-10.09%	5.33%	-15.42%

In light of this information, the Commission agrees that no adjustments to SUSF payments are needed to reflect tax savings because of the lower income tax rate resulting from the Tax Act. The disposition of the excess ADFIT that the telephone companies have reclassified as regulatory liabilities will be determined in each utility's next rate proceeding.

Small Water Utilities

Staff's Proposal recommended that water utilities over $700,000 in annual revenue be subject to deferred accounting, but determined that $2.5 million be the threshold for gas utilities. The primary reason for this difference is the definition of Class B and A utilities is much lower for water

[50] Township actually reported it earned an 8.48% ROE for 2017. However, when asked by Staff why it earned higher than its allowed ROE, the Company responded that there was a mistake in the calculation of the ROE shown in the Annual Report and the reported ROE should have only been 4.91%. Staff agrees the reported ROE was incorrect and Township has agreed to file an amended 2017 Annual Report to reflect the correction.

[51] The analysis here combines Vernon and Oriskany Falls data because the operations and financial records of those two companies were combined pursuant to Case 17-C-0608, Vernon Telephone Company, Inc. and Oriskany Falls Telephone Corporation - Merger, Order Approving Transfer of Assets and Amended Certificate of Public Convenience and Necessity With Conditions (issued February 23, 2018).

utilities ($700,000 and $1 million, respectively)[52] than it is for gas utilities ($1 million and $2.5 million, respectively).[53]

Since the regulatory environment and tax consequences are very similar for these two industries, and for consistency purposes, the Commission believes that a revenue threshold is more appropriate than the classification thresholds. For the gas industry, Staff's Proposal found minimal, if any net tax benefits, and rather the likely possibility that most of these companies could experience a tax increase with the implementation of the Tax Act changes, if their effective tax rate prior to the change was a rate less than 21%. Additionally, if there were to be any realized benefits, requiring these small utilities to prepare and submit a rate or sur-credit filing would be administratively burdensome to their operations, and likely require reliance on outside expertise, the costs of which could be in excess of any benefits.

Since the situation is similar in both the gas and water industries, the Commission finds that the water companies under $2.5 million in revenue,[54] should also be exempt from deferral accounting requirements related to the Tax Act. However, the ongoing effects of the Tax Act changes should be included in the water companies' future rate filings. Likewise, the disposition of the excess ADFIT that the water companies have reclassified as regulatory liabilities will be determined in each utility's next rate proceeding.

[52] See 16 NYCRR §561.1(a).

[53] See 16 NYCRR §311.1(a).

[54] Since the tax benefits were already captured in recent rate orders for Fishers Island Water Works Corporation, and Suez Water Owego Nichols, this threshold increase will only impact Saratoga Water Service, Inc. and Heritage Hills Water Works Corporation.

Small Gas Utilities

As Staff identified, small gas companies in Classes B, C and D will not receive material benefits from the Tax Act. The Commission agrees with Staff's determination. Therefore, the Commission exempts the small gas utilities from the policy requiring deferral accounting and pass back of any realized benefits resulting from the Tax Act through the implementation of a sur-credit. However, the Commission will require the ongoing effects of the Tax Act changes to be included in the gas companies' future rate filings. Similar to both the exempted telephone and water companies, the disposition of the excess ADFIT that the gas companies have reclassified as regulatory liabilities will also be determined in each utility's next rate proceeding.

CONCLUSION

The Tax Act provides a significant reduction in the federal income tax rate and other changes in the tax structure to the State's regulated utilities. The purpose of this proceeding is to address these changes to ensure that ratepayers receive the benefits of the tax savings in a timely fashion, consistent with applicable accounting principles, while ensuring the utilities remain financially sound. The approaches delineated in this Order to provide for deferrals to preserve the net benefits and sur-credits until the full impacts of the Tax Act can be incorporated in utility rate filings will accomplish those goals.

While the outcome is more complex than the understandable desire to immediately refund the entire tax savings to customers, the results are consistent with the Commission's mandate to ensure safe and adequate service at just and reasonable rates. Ratepayers will benefit from the mandated sur-credits and deferrals, while addressing utilities cash flow metrics and maintaining financial strength. The Commission’s work will continue until all utilities’ rates fully reflect the new federal tax structure, but this Order establishes the framework for future actions.

The Commission orders:

1. Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., Corning Natural Gas Corporation, National Fuel Gas Distribution Corporation, New York State Electric & Gas Corporation, KeySpan Gas East Corporation d/b/a National Grid, The Brooklyn Union Gas Company d/b/a National Grid NY, Niagara Mohawk Power Corporation d/b/a National Grid, New York American Water, Inc., Orange & Rockland Utilities, Inc., Rochester Gas and Electric Corporation, St. Lawrence Gas Company, Inc., SUEZ Water New York, Inc., and SUEZ Water Westchester Inc. shall continue to defer and reconcile the net benefits of the Tax Cuts and Jobs Act of 2017 until they are fully reflected in rates.

2. Consolidated Edison Company of New York, Inc. shall, on not less than five days’ notice, file tariff revisions to institute a sur-credit to commence on October 1, 2018 for its steam customers, as described in the body of this Order.

3. Consolidated Edison Company of New York, Inc. shall, on not less than five days’ notice, file tariff revisions to institute a sur-credit to commence on January 1, 2019 for its electric and gas customers, as described in the body of this Order.

4. New York State Electric & Gas Corporation, Rochester Gas and Electric Corporation, National Fuel Gas Distribution Corporation, Corning Natural Gas Corporation, St. Lawrence Gas Company, Inc., New York American Water, Inc., SUEZ

Water New York, Inc., and SUEZ Water Westchester Inc. shall, on not less than five days' notice, file tariff revisions to institute a sur-credit to commence on October 1, 2018, as described in the body of this Order.

5. KeySpan Gas East Corporation d/b/a National Grid (KEDLI) and The Brooklyn Union Gas Company d/b/a National Grid NY (KEDNY) shall, on not less than five days' notice, file tariff revisions to institute a sur-credit to commence on January 1, 2019, as described in the body of this Order.

6. The tariff filings required by Clauses 2, 3, 4, and 5 shall include requirements for annual reconciliation filings with the Secretary, as detailed in the body of this Order.

7. The disposition of remaining Tax Cuts and Jobs Act of 2017 benefits for New York American Water, Inc., and SUEZ Water New York, Inc. shall be determined in Case 17-W-0232, as discussed in the body of this Order.

8. Gas and water utilities with annual revenues of less than $2.5 million, and telephone utilities, with the exception of Verizon New York Inc., and Frontier Telecommunications of Rochester, Inc., shall preserve on their books any excess accumulated deferred federal income taxes from the Tax Cuts and Jobs Act of 2017 for future disposition by the Commission.

9. Except as directed in Clause 8, telephone utilities shall not be subject to any of the provisions discussed in this Order.

10. For sur-credits commencing October 1, 2018, the provisions of Public Service Law §66(12)(b), applicable to gas and electric corporations, §80(10)(b), applicable to steam corporations, and §89-c(10)(b), applicable to water-works corporations, and Commission rules 16 NYCRR §§720-8.1), that require publication be completed prior to the effective date of

the amendments are waived for the amendments directed in Clause Nos. 2 and 4. Each utility is directed to file with the Secretary to the Commission, no later than six weeks following the effective date of the amendments, proof that a notice to the public of the changes set forth in the amendments and their effective date had been published once a week for four consecutive weeks in one or more newspapers having general circulation in the service territory.

11. For sur-credits commencing January 1, 2019, the provisions of Public Service Law §66(12)(b), applicable to gas and electric corporations, and Commission rules 16 NYCRR §§720-8.1 are not waived for the tariff amendments directed in Clause Nos. 3 and 5.

12. In the Secretary's sole discretion, the deadlines set forth in this order may be extended. Any request for an extension must be in writing, must include a justification for the extension, and must be filed at least one day prior to the affected deadline.

13. This proceeding is continued.

By the Commission,

(SIGNED)

KATHLEEN H. BURGESS
Secretary

Attachment

MANNER TO CAPTURE SAVINGS FROM THE TAX CUTS AND JOBS ACT OF 2017

Deferral Accounting and Reconciliation:
Unless otherwise exempted, utilities will continue deferral accounting and reconciliation to capture net savings until the net savings are fully reflected in rates.

Implementation of a Sur-credit on October 1, 2018:

1. Consolidated Edison Company of New York, Inc. (Steam)
- Annual Ongoing Net Savings[1]
- Amortization of 2018 deferred balance
- Amortization of excess protected and unprotected deferred balances

2a. New York State Electric & Gas Corporation (Electric)
- Annual Ongoing Net Savings

2b. New York State Electric & Gas Corporation (Gas)
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

3. Rochester Gas & Electric Corporation
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

4. National Fuel Gas Distribution Corporation
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance
- Amortization of excess protected and unprotected deferred balances

5. Corning Natural Gas Corporation
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

6. St. Lawrence Gas Company, Inc.
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

[1] Annual Ongoing Net Savings include the current tax expenses payable as well as deferred tax expenses (originating deferred taxes).

7. New York American Water, Inc.[2]
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

8. SUEZ Water New York, Inc.[3]
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

9. Suez Water Westchester, Inc.
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance

Implementation of a Sur-credit on January 1, 2019:

1a. Consolidated Edison Company of New York, Inc. (Electric)
- Annual Ongoing Net Savings

1b. Consolidated Edison Company of New York, Inc. (Gas)
- Annual Ongoing Net Savings
- Amortization of 2018 deferred balance
- Amortization of excess protected and unprotected deferred balances

2. KeySpan Gas East Corporation d/b/a National Grid
- Annual Ongoing Net Savings

3. The Brooklyn Union Gas Company d/b/a National Grid NY
- Annual Ongoing Net Savings

Savings Captured in Recently Approved or Pending Rate Case – No additional Sur-credit:

1. Niagara Mohawk Power Corporation d/b/a National Grid (Electric & Gas)
2. Central Hudson Gas & Electric Corporation (Electric & Gas)
3. Orange and Rockland Utilities, Inc. (Electric & Gas)
4. Suez Water Owego-Nichols, Inc.
5. Fishers Island Water Works Corporation
6. Forest Park Water Company, Inc.

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[2] To be addressed comprehensively in Case 17-W-0232, Water Utilities – Qualified New York Manufacturers, Notice Establishing Proceeding Concerning Rate Impacts Due to a Change in the Tax Law (issued May 25, 2017).

[3] Ibid.

<u>**No Sur-credit Implementation:**</u>[4]

1. **Heritage Hills Water Works Corporation**
2. **Saratoga Water Services, Inc.**
3. **Small Water Utilities**[5]
4. **Small Gas Utilities**[6]
5. **All Telco Providers**

[4] Although noted that no sur-credit is being implemented, these utilities are still required to defer the excess deferred ADFIT balances in which a determination of disposal will be decided in their next rate filing.

[5] Small water utilities include the water utilities that are under $2.5 million in annual revenues.

[6] Small gas utilities include the gas utilities that are under $2.5 million in annual revenues.