

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Commission's)	Case No. 18-47-AU-COI
Investigation of the Financial Impact)	
of the Tax Cuts and Jobs Act of 2017)	Comments of Environmental
on Regulated Ohio Utility Companies.)	Defense Fund, Ohio Environmental
)	Council, Environmental Law & Policy
)	Center, Natural Resources Defense Council,
)	and Sierra Club

The Tax Cuts and Jobs Act of 2017 (“TCJA”) reduced the corporate income tax rate from 35% to 21%. The Commission opened this case to consider how Ohio’s public utility companies should revise their rates to reflect the tax cut. To that end, the Environmental Defense Fund (“EDF”), Ohio Environmental Council (“OEC”), Environmental Law & Policy Center (“ELPC”), Natural Resources Defense Council (“NRDC”), and Sierra Club (collectively, the “Environmental Advocates”) submit these comments to recommend the best approach to accounting for the tax cut. First, the tax cut impacts the balance sheet of the utilities’ holding companies and the earnings of their merchant subsidiaries. The Commission should therefore reconsider the impacts of its recent Orders that provided customer-funded financial support to Ohio’s utilities to help improve their credit rating, and also ensure the tax reduction is accounted for in the utilities’ energy efficiency (and other) riders. Second, the Commission should refund the entirety of the funds back to ratepayers. However, if the Commission does not simply refund the entire amount of the tax cut through reduced rates, consistent with past rulings, the Commission should consider allocating some of the tax savings to new projects that leverage and maximize the value of the tax savings for customers while providing a public benefit, such as modernizing the utilities’ grids to allow for better incorporation of clean energy resources.

I. The Commission Should Reevaluate Rate Impacts of Recent Orders and Incorporate Impacts from the Tax Reduction on Energy Efficiency Riders.

The tax cut will have a mixed, but major financial impact on utilities and their holding companies. For example, AEP estimates that it has collected \$4.4 billion in excess deferred taxes.¹ In January, Moody's downgraded several utilities, including AEP (from "positive" to "stable") and Duke (from "stable" to "negative") because the rate reductions will tilt the utilities' capital structures toward a higher ratio of debt.² At the same time, these companies will benefit from the lower tax rate and the deferred taxes impact, while lower net operating losses may have a negative effect. Discussing these mixed impacts, Ernst & Young notes:

Tax rates and normalization requirements — For nonregulated entities, the reduction in the corporate tax rate is an income statement benefit given the preponderance of deferred tax liabilities on the balance sheet due to bonus depreciation related to plant assets.³

As a result, the Commission should reevaluate the impact of its Orders in cases where utilities have been approved for rate increases for credit support to their holding companies – the FirstEnergy⁴ and Dayton Power & Light Company⁵ distribution modernization rider cases – and

¹ American Electric Power 4th Quarter 2017 Earnings Release Presentation at 12 (Jan. 25, 2018), available at: <https://www.aep.com/newsroom/resources/earnings/2018-01/4Q17EarningsReleasePresentation.pdf>.

² Market Realist, *Moody's Downgrades Could Fuel a Fall in Utilities* (January 22, 2018), available at: <https://marketrealist.com/2018/01/moodys-downgrades-fuel-fall-utilities>.

³ Ernst & Young, LLP, *US Tax Cuts and Jobs Act and its Impact on the Energy Sector* at 7 (Dec. 29, 2017), available at: [http://www.ey.com/Publication/vwLUAssets/US_Tax_Cuts_and_Jobs_Act_and_its_impact_on_the_energy_sector/\\$FILE/2017G_07180-171Gbl_US%20Tax%20Cuts%20and%20Jobs%20Act%20and%20its%20impact%20on%20the%20energy%20sector.pdf](http://www.ey.com/Publication/vwLUAssets/US_Tax_Cuts_and_Jobs_Act_and_its_impact_on_the_energy_sector/$FILE/2017G_07180-171Gbl_US%20Tax%20Cuts%20and%20Jobs%20Act%20and%20its%20impact%20on%20the%20energy%20sector.pdf).

⁴ *In the Matter of the Application of Ohio Edison Company, the Cleveland Electric Illuminating Company and the Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan*, Case No. 14-1297-EL-SSO (Fifth Entry on Rehearing) (Oct. 12, 2016) (hereinafter "*In re FirstEnergy Bailout*").

⁵ *In the Matter of the Application of the Dayton Power & Light Company for Approval of its Electric Security Plan*, Case No. 16-0395-EL-SSO (Opinion and Order) (Oct. 20, 2017).

the Ohio Valley Electric Corporation (“OVEC”) rider cases which provided a customer-funded bailout of two outdated coal plants, one of which is located in Indiana.⁶

In the FirstEnergy proceeding, for example, the PUCO approved the recovery of an estimated \$132.5 million annually plus a “gross-up” to pay the company’s federal taxes on that money under the newly created Distribution Modernization Rider. The Commission’s stated purpose of approving that rider was to ensure that FirstEnergy retained a certain level of financial health and creditworthiness so that it could then invest in future distribution modernization endeavors. When grossed up for federal taxes, this amount was estimated to be over \$204 million annually charged to FirstEnergy’s customers.⁷

The Commission explained that the purpose of the increase was to help the company avoid a credit rating downgrade that would limit its ability to borrow to make system upgrades. When combined with other recent events that have attracted new money into the FirstEnergy Corporation,⁸ the Commission should be properly motivated to protect Ohio’s electricity customers by now revisiting the financial impacts of this and other similar riders continuing to be collected by Ohio’s electric distribution utilities.

The Commission made clear that it intended “to provide the minimum amount necessary to provide credit support for the Companies to facilitate access to the credit markets.” Case No. 14-1297-EL-SSO, Fifth Entry on Rehearing at 93 (Oct. 12, 2016). The TCJA may have a significant effect on that calculation. The Commission should consider the tax law impacts on the nonregulated companies because the tax law is a material change that will impact Ohio’s

⁶ *In the Matter of the Application Seeking Approval of Ohio Power Company’s Proposal to Enter into an Affiliate Purchase Power Agreement for Inclusion in the Purchase Power Agreement Rider*, Case No. 14-1693-EL-RDR. (Second Entry on Rehearing) (Nov. 3, 2016); *In the Matter of the Application of Duke Energy Ohio, Inc. for Approval to Modify Rider PSR*, Case No. 17-0872-EL-RDR (Application) (Mar. 31, 2017) (pending). Sierra Club takes no position on the effect of the TCJA on the order in Case No. 14-1693-EL-RDR.

⁷ See, <https://www.puco.ohio.gov/be-informed/consumer-topics/firstenergy-s-electric-security-plan/>.

⁸ See, <https://www.ohio.com/akron/business/utilities/firstenergy-shares-soar-after-akron-utility-gets-2-5-billion-capital-infusion>.

electricity customers. The Commission should also require utilities to provide information about the impacts of the TCJA on OVEC costs in order to help determine the prudence of recovery and reduce customer rates accordingly. While we maintain that ratepayers should not be paying any subsidies for uneconomic coal or nuclear plants, the utilities certainly should not be allowed to collect greater subsidies than needed to operate the plants or to bolster the holding companies' finances.

Further, the Commission should incorporate any impacts from the tax reduction on electric utility energy efficiency riders. Each of the utilities is authorized to recover both efficiency program costs and "shared savings" incentive payments based on energy savings above the annual benchmark under R.C. 4928.66. The shared savings component of the rider is grossed up for income taxes. *See, e.g., In re Duke Energy Ohio*, Case No. 16-576-EL-POR, Opinion and Order (Sept. 27, 2017) at 17. Accordingly, the Commission should ensure that utilities do not over collect on this component of their energy efficiency riders now that the TCJA has lowered the applicable income tax, and should determine whether there has been any prior overcollection and make the appropriate rate adjustments. It is particularly important to accomplish this quickly because spending by each of the Ohio electric utilities is currently limited by a cap on energy efficiency rider costs. *In re Dayton Power & Light Co.*, Case Nos. 17-1398-EL-POR *et al.*, Opinion and Order (Dec. 20, 2017) at 8; *In re Ohio Edison Co., Cleveland Electric Illuminating Co., and Toledo Edison Co.*, Case No. 16-743-EL-POR, Opinion and Order (Nov. 21, 2017) at 23; *In re Duke Energy Ohio*, Case No. 16-576-EL-POR, Opinion and Order (Sept. 27, 2017) at 15-16; *In re Ohio Power Co.*, Case No. 16-574-EL-POR (Jan. 18, 2017) at 8. Once the utilities can know with certainty that the shared savings component of those costs

will decrease and by how much, they can plan to spend more funds on cost-effective energy efficiency that benefits Ohio customers.

II. The Commission Must Ensure the Entirety of the Tax Cut Benefits Ratepayers.

The Commission opened this case to consider the tax cut's impact on Ohio's regulated utilities and their customers. The Environmental Advocates believe that the entirety of the tax cuts should be refunded to ratepayers. However, we recognize that in past cases the Commission has allocated a portion of tax cut savings to other projects that provided customer benefits. To that end, if the Commission does not refund the entirety of the money to ratepayers, the Commission must ensure that the funds are spent in a manner that maximizes the benefit to ratepayers.

Prior cases in which some of the funds were used for projects that provided customer benefits arose from the tax cut provided under the Tax Reform Act of 1986, which cut the corporate tax rate from 46% to 34%. The Commission allowed AEP to allocate \$1.2 million to improving customer service⁹ and allowed DP&L to allocate \$4.1 million for conservation programs, which saved energy as well as money for consumers.¹⁰ Consistent with these past cases, and to the extent the Commission decides not to refund the entire amount of the tax cut to consumers through reduced rates, the Commission should ensure that those funds are used to maximize the benefit to consumers, by leveraging that tax savings to support new projects that

⁹ *In the Matter of the Application of Columbus Southern Power Company for Authority to Reduce Rates to Reflect the New Federal Corporate Income Tax Rate*, Case No. 87-2049 (Finding and Order) (Dec. 17, 1987).

¹⁰ *In the Matter of the Application of the Dayton Power and Light Company for Authority to Modify and Reduce its Rates for Gas and Electric Service to Jurisdictional Customers to Reflect Federal Corporate Income Tax Rate Changes*, Case No. 87-842 (Finding and Order) (June 16, 1987).

modernize the utilities' grids and facilitates the incorporation of clean energy resources, using the following approach:

- The utilities identify all rate impacts of the new tax law.
- Most of the tax law savings should be flowed back to customers in the form of lower rates.
- The utilities work with interested stakeholders to identify projects to be funded by the identified portion of the tax law savings.
- The identified projects should help modernize the utilities' grids, through projects that will help incorporate clean energy resources to provide customer benefits, such as using distributed generation and energy efficiency resources as non-wires alternatives to avoid or defer additional grid investments, or grid investments to support a network of electric vehicle charging stations (complementing planned spending on charging stations from the \$71 million fund arising from the Volkswagen emission scandal settlement¹¹).

III. Conclusion

In light of the recent tax cuts, the Environmental Advocates strongly recommend that: (1) the Commission reconsider the impacts of its recent Orders that provided customer-funded financial support to Ohio's utilities to help improve their credit ratings, and ensure the tax reduction is accounted for in the utilities' energy efficiency (and other) riders; and, (2) ensure that all funds are returned to ratepayers or, alternatively, if the Commission chooses not to refund

¹¹ Ohio Environmental Protection Agency, *Updated: VW Mitigation Fund Planning – Volkswagen Mitigation Grants* (March 13, 2017), available at: <http://epa.ohio.gov/Portals/42/documents/VW/VW%20update%20WEB%20mar17.pdf>

the entirety of the money through reduced rates, ensure those funds are used to maximize benefits to ratepayers as identified above.

Respectfully submitted,

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Summary: Comments of Environmental Defense Fund, Ohio Environmental Council, Environmental Law & Policy Center, Natural Resources Defense Council, and Sierra Club electronically filed by Ms. Miranda R Leppla on behalf of Environmental Defense Fund and Ohio Environmental Council and Environmental Law & Policy Center and Natural Resources Defense Council and Sierra Club