

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Commission's)
Investigation of the Financial Impact of the)
Tax Cuts and Jobs Act of 2017 on)
Regulated Ohio Utility Companies) Case No. 18-0047-AU-COI

**TESTIMONY
OF
JONATHAN J. BORER
RESEARCH AND POLICY DIVISION
RATES AND ANALYSIS DEPARTMENT**

STAFF EXHIBIT NO. _____

TESTIMONY OF JONATHAN J. BORER

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22

1. Q. **Please state your name and business address.**

A. My name is Jonathan J Borer. My business address is 180 East Broad Street, Columbus, Ohio 43215-3793.

2. Q. **By whom are you employed and in what capacity?**

A. I am employed by the Public Utilities Commission of Ohio (PUCO) as a Utility Auditor 2 in the Research and Policy Division of the Rates and Analysis Department. My duties include conducting investigations of assigned phases of rate case applications and other financial audits of public utility companies subject to the jurisdiction of the PUCO.

3. Q. **Would you briefly state your educational background?**

A. I earned a Bachelor of Science in Accounting and a Bachelor of Science in Management from Purdue University in 2014. In 2017, I attended the Annual Regulatory Studies Program offered by the Institute of Public Utilities as well as the National Association of Regulatory Commissioners (NARUC) Utility Rate School.

4. Q. **Please briefly outline your work experience.**

A. I have been with the PUCO since November 2016 with my entire time spent in the Rates and Analysis Department. Prior to working at the PUCO,

1 I was employed with Morgan Stanley within the Global Wealth
2 Management Group.

3
4 5. Q. **What is the purpose of your testimony in this proceeding?**

5 A. The purpose of my testimony is to address the accounting authority
6 pertaining to the Commission’s directive that Ohio public utilities record
7 the estimated reduction in federal income tax related to the Tax Cuts and
8 Jobs Act (TCJA) as a deferred liability on their books. More specifically,
9 this testimony will address whether or not the Commission’s directive
10 adheres to Generally Accepted Accounting Principals (GAAP). In addition,
11 I will discuss a framework to assess the reasonableness of imposing a
12 deferred liability.

13
14 6. Q. **What is Staff’s understanding of the Commission’s directive?**

15 A. Staff’s understanding of the directive is that the Commission ordered
16 utilities to record the savings from the TCJA as a deferred liability on their
17 books. This liability would include in part, the savings resulting from a
18 reduced federal income tax expense and the “excess” accumulated deferred
19 income taxes (ADIT), which represent money that must be returned to
20 customers since it is no longer owed to the IRS. Staff believes the savings
21 resulting from a reduced federal income tax expense will be deferred from

1 January 1, 2018 until rates are adjusted to reflect the reduced income tax
2 rate.

3
4 7. Q. **What is being used as an authoritative reference in making this**
5 **determination?**

6 A. The Financial Accounting Standards Board (FASB) has the authority to
7 establish and interpret GAAP in the United States. The Security and
8 Exchange Commission and American Institute of Certified Public
9 Accountants both recognize FASB standards as the official authority for the
10 basis and preparation of financial statements in the United States. The
11 FASB Accounting Standards Codification (ASC or the "Codification")
12 organizes nongovernmental US GAAP using a topic-based model
13 consisting of individual Topics.

14 The primary source of industry-specific accounting guidance for regulated
15 operations is currently codified into ASC 980, Regulated Operations.

16
17 8. Q. **Does the Commission’s directive comport with GAAP?**

18 A. Yes. FASB ASC 980 addresses regulated operations, and subsection 405-
19 25-1 provides guidance on the required criteria, timing, and location for
20 recognizing and recording regulator-imposed liabilities. This subsection
21 states, “Rate actions of a regulator can impose a liability on a regulated
22 entity. Such liabilities are usually obligations to the entity’s customers.”

1 This clearly supports the fact that the Commission’s directive adheres to
2 GAAP.

3
4 9. Q. **Does the Commission have a standard of review for authorizing**
5 **deferrals?**

6 A. Yes, the Commission has a standard of review for deferral requests
7 associated regulatory *assets*; however, due to the infrequency of
8 occurrence, there is no standard of review for authorizing deferrals
9 associated with regulatory *liabilities*. These review standards, which were
10 most recently addressed in Case No. 17-2118-GA-AAM¹, are based on the
11 following five criteria:

- 12
13 1. Whether the utility’s current rates or revenues are sufficient to cover the
14 costs associated with the requested deferral;
- 15 2. Whether the costs are material;
- 16 3. Whether the reason for requesting the deferral is outside the utility’s
17 control;
- 18 4. Whether the expenses are atypical and infrequent; and
- 19 5. Whether the financial integrity of the utility will be significantly and
20 adversely affected, if the deferral is not granted.

¹ *In the Matter of the Application of Duke Energy Ohio, Inc., for Approval to Change Accounting Methods, Case No. 17-2118-GA-AAM, Finding and Order (April 18, 2018).*

1 While these standards were intended to be applied to deferred assets, they
2 could be used to provide an approximate review of the reasonableness of a
3 deferred liability.

4
5 10. Q. **Would the deferred liability associated with the TCJA meet the criteria**
6 **used to review deferred assets?**

7 A. Yes, however, certain criteria need to be reworded in order to properly be
8 applied to deferred liabilities. Modifications to the language have been
9 identified where appropriate.

10 1. *Are the utility's current rates or revenues insufficient to cover the costs*
11 *associated with the deferral?*

12 The utilities meet this criterion because rates have been developed based on
13 a 35% Federal Income Tax rate (FIT rate), so current rates would be
14 sufficient to cover the deferral associated with reducing the FIT rate to
15 21%.

16
17 2. *Are the expense reductions material?*

18 The Commission has directed the utilities to defer all tax savings associated
19 with the TCJA, which broadly speaking, represent a reduction in tax
20 expense. As a result of Ohio's ratemaking formula, the tax expense
21 reductions are material. Ohio's ratemaking formula allows federal income
22 taxes to be recovered on a dollar-for-dollar basis in the revenue

1 requirements of base rates, riders, etc. Since the current and deferred
2 income taxes are directly affected by the FIT rate, the expense reductions
3 are material because changing the FIT rate from 35% to 21% represents a
4 reduction of 40%. In addition, there is an approximate reduction of 18% to
5 the Gross Revenue Conversion Factor (GRCF), exclusive of other taxes. In
6 addition to the materiality of the reduction to income tax expenses, there is
7 the separate issue of excess ADIT. Based on Staff's analysis, the balance of
8 the excess ADIT is tens or even hundreds of millions of dollars, which Staff
9 believes to be material.

10
11 *3. Is the reason for requesting the deferral outside the utilities' control?*

12 Yes. The tax reduction was outside the utilities' direct control. The decision
13 to reduce Federal Income Taxes was an act of Congress and signed by the
14 President of the United States.

15
16 *4. Are these expense reductions atypical and infrequent?*

17 Yes. While minor changes to the tax code are relatively more frequent²,
18 major overhauls to the Federal Income Tax rate are quite rare. The last
19 major change to the corporate tax rate occurred in 1986.

20

² For example, in 1992, the top tax bracket increased from 34 to 35%.

1 5. Will the financial integrity of the utility be significantly and adversely
2 affected if the deferral is required?

3 No. Utilities' revenues are not impacted by the TCJA; therefore, cash
4 inflows will otherwise remain the same as they would have had the TCJA
5 not been enacted. Conversely, cash outflows to the federal government
6 have *decreased*. All else being equal, this means the utilities are seeing an
7 increase in net income, so in effect, the Commission is ordering the utilities
8 to defer an amount such that net income at the current 21% FIT rate would
9 be the same as net income at the previous 35% FIT rate.

10
11 11. Q. **Does this conclude your testimony?**

12 A. Yes it does. However, I reserve the right to submit supplemental testimony
13 as described herein, as new information subsequently becomes available or
14 in response to positions taken by other parties.

CERTIFICATE OF SERVICE

This is to certify that the foregoing **Testimony of Jonathan J. Borer** has been served upon all of the parties of record in Case No. 18-0047-AU-COI by electronic and/or U.S. mail, postage pre-paid mail this 29th day of June, 2018.

/s/Jodi J. Bair

Jodi J. Bair

Assistant Attorney General

PARTIES OF RECORD:

Amy.spiller@duke-energy.com
bbingaman@firstenergycorp.com
campbell@whitt-sturtevant.com
cdunn@firstenergycorp.com
cblend@aep.com
Christopher.healey@occ.ohio.gov
cmooney@ohiopartners.org
dstinson@bricker.com
dsawmiller@nrdc.com
Elizabeth.watts@duke-energy.com
fdarr@mwncmh.com
gkrassen@bricker.com
Jeanne.kingery@duke-energy.com
jkylercohn@bkllawfirm.com
jfinnigan@edf.org
joliker@igsenergy.com
josephclark@nisource.com
kathybuckley@verizon.com
bojko@carpenterlipps.com
kboehm@bkllawfirm.com
kevin.moore@occ.ohio.gov
mleppla@theoec.org
mfleisher@elpc.org
whitt@whitt-sturtevant.com

mpritchard@mwncmh.com
mkurtz@bkllawfirm.com
mlozich@securustechnologies.com
mnugent@igsenergy.com
Michael.schuler@aes.com
mwhelan@egas.net
neil.waggoner@sierraclub.org
paul@carpenterlipps.com
glover@whitt-sturtevant.com
randell.griffin@aes.com
rocco.dascenzo@duke-energy.com
selisar@mwncmh.com
sseiple@mwncmh.com
stnourse@aep.com
trhayslaw@gmail.com

This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

6/29/2018 3:56:54 PM

in

Case No(s). 18-0047-AU-COI

Summary: Testimony of Jonathan J. Borer electronically filed by Ms. Tonnetta Scott on behalf of PUC