

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of)	
Vectren Energy Delivery of Ohio, Inc. for)	Case No. 19-29-GA-ATA
Approval of a Tax Savings Credit Rider)	

INITIAL BRIEF OF VECTREN ENERGY DELIVERY OF OHIO, INC.

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OCTOBER 9, 2020

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OHIO, INC.**

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I. INTRODUCTION

The question before the Public Utilities Commission of Ohio (“Commission”) here is whether Vectren Energy Delivery of Ohio, Inc. (“VEDO”) can appropriately reflect the changes to its Accumulated Deferred Income Tax (“ADIT”) balance in its calculation of the total tax credits to flow to customers. The ADIT liability balance is a rate base deduction because it represents cost free capital. As VEDO provides tax credits related to ADIT to customers, VEDO’s source of cost-free capital is in turn reduced as well. What VEDO proposes here is a standard component of ratemaking and is reflected in the litany of annual reconciling riders authorized by the Commission. In fact, the ADIT adjustment has already been recognized as an appropriate adjustment by the Commission when it approved the *AEP Ohio Tax Case*¹ and then directed all rate-regulated utilities, including VEDO, to follow the AEP Ohio approach.

Despite VEDO mirroring the *AEP Ohio Tax Case* proposal in its Application in this case, the Commission Staff recommends a deviation to that model that would prevent VEDO from recognizing legitimate costs in calculating VEDO’s total tax savings to pass

¹ See *In re Ohio Power Company*, Case Nos. 18-1007-EL-UNC and 18-1841-EL-ATA (“*AEP Ohio Tax Case*”).

back to customers. Instead of reflecting the reduction in ADIT liabilities in VEDO's Tax Savings Credit Rider ("TSCR"), Staff recommends that the issue be addressed in a rate case. But, under the Commission-approved Stipulation and Recommendation in Case Nos. 18-298-GA-AIR, et al. ("*Rate Case*") ("*Rate Case Stipulation*"), all Excess Accumulated Deferred Income Tax ("EDIT") issues were removed from the *Rate Case* for resolution here. And, if the Commission rejects this component of VEDO's Application and adopts Staff's recommendation, the Commission will be going much further than requiring VEDO's tax savings be passed back to customers; the Commission would be creating an unlawful and unreasonable windfall for customers. Accordingly, the Commission should adopt Component D of VEDO's Application and reject Staff's proposed modification.

II. FACTUAL BACKGROUND

The Tax Cuts and Jobs Act of 2017 ("TCJA") went into effect on January 1, 2018, and among other things, lowered the federal corporate income tax rate from 35 percent to 21 percent.² In response, the Commission opened an investigation in Case No. 18-47-AU-COI ("*Tax COI*"), and ultimately directed each utility to file applications to "address the remaining issues relating to the effects of the TCJA, including rider rates, ADIT [accumulated deferred income tax], and base rates."³ VEDO has resolved most of these issues through either its recent *Rate Case* or through the Stipulation previously approved

² *In re the Commission's Investigation of the Financial Impact of the Tax Cuts and Jobs Act of 2017 on Regulated Ohio Utility Companies*, Case No. 18-47-AU-COI, Entry at 1 (Jan. 10, 2018).

³ *Tax COI*, Finding and Order at 18 (Oct. 24, 2018) ("*Tax COI Order*").

in this matter.⁴ There remains one issue related to ADIT/EDIT, reflected as Component D of VEDO's Application, that must be resolved by the Commission.

The remaining issue will determine whether VEDO can properly reflect the reduction in the ADIT rate base credit (thereby capturing the incremental return on rate base) as VEDO amortizes and reduces its Normalized EDIT balance through credits issued to customers through its Tax Savings Credit Rider ("TSCR"). The genesis of ADIT liabilities frequently lies in tax laws that permit accelerated depreciation rates for certain assets, and that is specifically true with VEDO's Normalized EDIT at issue here. For federal income tax purposes, a public utility may have assets that are eligible to utilize accelerated depreciation. For ratemaking, however, a public utility uses straight-line depreciation for the same assets. An ADIT liability is essentially a point-in-time tax-affected difference between income tax depreciation expense and the depreciation expense typically used to compute a utility's revenue requirement.

The distribution ratemaking formula reflected in R.C. Chapter 4909 captures the accelerated depreciation benefit utilities receive for tax purposes by treating a utility's ADIT liability balance as a cost of free capital (*i.e.* a loan from the federal government) and is reflected as a reduction to rate base.⁵ This reduction from the otherwise applicable net plant in service value lowers the base value (*i.e.* rate base) at which the authorized

⁴ See Stipulation and Recommendation (May 28, 2020).

⁵ See *In re The East Ohio Gas Company d/b/a Dominion Energy Ohio*, Case Nos. 18-1908-GA-UNC et al, Staff Review and Recommendation at 7, n. 11 (Mar. 5, 2019) ("*Dominion Tax Case*") ("EDIT is treated as an offset to rate base, so it functions as a reduction [to] the revenue requirement. As the EDIT is amortized and refunded to customers, the balance by which rate base is offset is reduced, thus increasing the revenue requirement (all else equal)."); see also *In re Columbus Southern Power Co.*, Case Nos. 11-4920-EL-RDR et al, Finding and Order at 9 (Aug. 1, 2012) ("Staff contends that the ADIT are a cost-free source of funding . . .").

rate of return is multiplied against. This in turn reduces a utility's revenue requirement under the ratemaking formula reflected in R.C. Chapter 4909.⁶

When the TCJA lowered the federal corporate income tax rate to 21%, utilities were required to recalculate deferred tax obligations. When VEDO recalculated its deferred tax obligation it resulted in a reduction of \$79,357,179, net of income taxes. This amount has been labeled as EDIT. This \$79.4M of EDIT is still accounted for as a reduction to rate base. A portion of the total EDIT balance is referred to as Normalized EDIT and reflects the amount of EDIT that is "required to be amortized [by the TCJA] in accordance with the [Average Rate Assumption Method ("ARAM")]."⁷ The remaining EDIT balance is referred to as Non-Normalized EDIT. As reflected in the Commission-approved Stipulation in this matter, VEDO's Normalized EDIT balance is \$58.9M and its Non-Normalized EDIT balance is \$20.4M.⁸

In the Stipulation in this matter, VEDO's return of its EDIT balance was unanimously settled and approved by the Commission. And, as VEDO amortizes the \$79.4M and credits the amount to customers through the TSCR, its source of cost-free capital will be reduced and will be accounted for as a reduction to rate base credits. In Component D of the Application, consistent with the resolution of the *AEP Ohio Tax Case*, VEDO is only seeking to account for the reduction in its Normalized EDIT balance in calculating the total tax credit to customers. More specifically, to capture the reduction in the rate base credit, the mechanics of Component D would be to multiply the rate of return authorized in the *Rate Case* by the amount of Normalized EDIT returned to customers

⁶ See *Dominion Tax Case*, Staff Review and Recommendation at 7, n. 11 (Mar. 5, 2019).

⁷ Staff Review and Recommendation at 4.

⁸ Stipulation at 4-5.

through the TSCR. This will allow VEDO to appropriately apply its authorized rate of return to its net plant in service that is funded by VEDO's debt or equity (*i.e.* not funded by the ADIT, which is commonly viewed as an interested free loan from the federal government).

III. ARGUMENT

A. The PUCO's *Tax COI* endorses an approach consistent with VEDO's Application

In its *Tax COI* Order, the Commission directed utilities to pass back all TCJA savings to customers, identified AEP Ohio's approach to resolving its tax case as an approach that passed back all savings, and encouraged other utilities to follow AEP Ohio's approach.⁹ The *AEP Ohio Tax Case* resulted in AEP Ohio accounting for the reduced rate base credit in calculating the total tax savings to pass on to customers. VEDO's Application mirrors the *AEP Ohio Tax Case* approach and therefore satisfies the Commission's requirement of passing back all tax savings to customers.

The *Tax COI* was clearly focused on creating an annual adjustment to the distribution ratemaking formula under R.C. Chapter 4909. The Commission directed utilities to file an application under R.C. 4909.18 and encouraged utilities to propose crediting the tax savings to customers through annual reconciling rider mechanisms.¹⁰ The Commission also acknowledged in the *Tax COI* that some tax savings would flow to customers as a result of the various annual reconciling riders that had already been authorized for rate-regulated utilities.¹¹ These various reconciling riders (*e.g.*, AEP Ohio's

⁹ *Tax COI* Order at 18-19.

¹⁰ *Id.* at 18.

¹¹ *Id.* at 17.

DIR, FirstEnergy's DCR, Columbia's IRP, Dominion's PIR and AMR) are all based on the ratemaking formula embedded in R.C. Chapter 4909.

As discussed above, the ADIT rate base credit exists because ADIT is treated as cost free capital (*i.e.* a zero-interest loan from the federal government). But, as VEDO and other utilities provide credits to customers and reduce their EDIT balances, they will no longer retain this cost-free capital. It is therefore appropriate to reflect the reduction in the ADIT rate base credit that will materialize as VEDO amortizes the Normalized EDIT balance through TSCR credits to customers.

This is the exact outcome the Commission authorized for AEP Ohio. AEP Ohio's tax case settlement makes this explicit:

For the normalized accumulated excess deferred income tax (ADIT) balance, the Company will begin flowing the amortization of Excess ADIT (EDIT) (effective January 1, 2018) back to customers upon approval of this Settlement by the Commission. The normalized EDIT balance as of June 30, 2018 is \$278 million. Mechanically, the DIR will be the rider mechanism used to incorporate (1) a credit for the amount of amortization for normalized ADIT recorded by AEP Ohio each month, and (2) ***a corresponding decrease from the January 1, 2018 level of the ADIT component of the DIR rate base calculation.***¹²

While Stipulations are not normally precedential, in the *Tax COI* the Commission relied upon the outcome in the *AEP Ohio Tax Case*. The Commission held that the *AEP Ohio Tax Case* represented an example of a utility providing "all tax savings [being] returned to customers" and encouraged all other utilities to implement this model.¹³

¹² *AEP Ohio Tax Case Stipulation* at 3; see also *In re Ohio Power Co.*, Case No. 14-1696-EL-RDR, AEP Ohio DIR Update at 3 (Sep. 25, 2020) (detailing mechanics of AEP Ohio's incremental return on Normalized EDIT balances returned to customers).

¹³ *Tax COI Order* at 18-19.

Recognizing a reduction in ADIT balances in annual reconciling riders is nothing new. There is a litany of utility infrastructure riders (e.g., AEP Ohio's DIR, FirstEnergy's DCR, Columbia's IRP, Dominion's PIR and AMR), that all incorporate annual updates to ADIT balances in calculating rider rates.¹⁴

In the context of reflecting TCJA changes in a natural gas company's rider, the Commission Staff is also on record as stating that it is appropriate to recognize a reduction in ADIT rate base credits in riders. In its Review and Recommendation in the *Dominion Tax Case*, Staff stated that "the Company will have the opportunity to recover this incremental revenue requirement in the PIR and AMR Riders."¹⁵ Staff reiterated this position in testimony in that proceeding, stating again that Dominion would be permitted to recognize the increase in rate base for its PIR and AMR riders.¹⁶ The Commission and its Staff thus recognize the lawfulness and reasonableness of accounting for the reduction in cost free capital (i.e. reduction in ADIT rate base credit) when calculating rates, including adjustment related to the TCJA.

Changes to federal corporate income tax are rare, and with many cases resolved by settlements, there is little precedent from the PUCO on how the exact mechanics of the tax credit should work. In approving prior tax settlements, the Commission, however, was required to find that the settlements did not violate any important regulatory practice or principle. In some of these prior tax settlements, the Commission authorized utilities to reflect the entirety of the Normalized EDIT reductions as offsets to the tax credits that flow

¹⁴ See generally *In re Ohio Power Co.*, Case No. 14-1696-EL-RDR; *In re FirstEnergy*, Case No. 19-1887-EL-RDR; *In re Columbia Gas of Ohio, Inc.*, Case No. 17-2374-GA-RDR; *In re Dominion Energy Ohio*, Case Nos. 18-1587-GA-RDR and 18-1588-GA-RDR.

¹⁵ *Dominion Tax Case*, Staff Review and Recommendation at 7.

¹⁶ *Dominion Tax Case*, Tr. Vol. I at 83, 88-89.

to customers. In addition to the *AEP Ohio Tax Case* discussed above, the FirstEnergy tax settlement also provided the same outcome, stating that FirstEnergy “will include in the new credit mechanism a return on the cumulative amortized normalized EDIT net liabilities. The return will be calculated in the same manner as Rider DCR.”¹⁷ In the Columbia Tax Settlement, Columbia was authorized to reflect reductions in both Normalized and Non-Normalized EDIT for all EDIT amounts associated with its IRP Rider.¹⁸ These outcomes did not violate any important regulatory practices or principles. In fact, as VEDO discussed above, standard ratemaking principles, especially in the annual reconciling rider context, authorize decreases to ADIT rate base offsets as those balances are reversed and the source of cost-free capital eliminated.

Although capturing the reduction to the Normalized EDIT balance is appropriate, Staff’s Review and Recommendation recommends that the Commission reject this outcome in the TSCR. Instead, Staff indicates that a rate case is the appropriate place to address the issue.¹⁹ Initially, VEDO would note that it proposed to address its EDIT issues as part of its recent *Rate Case*, but the Staff Report proposed addressing the return of EDIT through a stand-alone rider, and through a Commission-approved settlement with Staff in the *Rate Case*, the Signatory Parties agreed to address all issues in this proceeding. More specifically, the *Rate Case Stipulation* provided:

¹⁷ *In re FirstEnergy*, Case Nos. 16-481-EL-UNC, *et al*, Stipulation and Recommendation at 8 (Nov. 9, 2018).

¹⁸ See *In re Columbia Gas of Ohio, Inc.*, Case No. 17-2202-GA-ALT, Opin. & Order at 27-28 (Nov. 28, 2018); see also *In the Matter of the Application of Columbia Gas of Ohio, Inc. For an Adjustment to Rider IRP and Rider DSM Rates*, Case No. 19-1940-GA-RDR, Application at Schedules AMRP-12 and AMRP-13, R-12 & R-13, AMRD-12 & AMRD-13 (Nov. 26, 2019) (with schedule 12 showing the change in Protected and Unprotected ADIT, and schedule 13 showing the reduction in rate base credit for the annual pass back of the total Protected and Unprotected ADIT balance).

¹⁹ Staff Review and Recommendation at 5.

Tax Reform. The Signatory Parties acknowledge that the application filed by VEDO in Case No. 19-0029-GA-ATA proposes to amortize and flow back to customers through a Tax Savings Credit Rider (TSCR) VEDO's net normalized and non-normalized accumulated excess deferred income (EDIT) tax savings and VEDO's federal income tax expense savings from January 1, 2018, until new rates are approved in this pending base rate case proceeding. The annual amortization of the respective normalized and non-normalized EDIT balances, the rate design of the TSCR, and other issues associated with the flow back of tax savings shall be addressed in the application in Case No. 19-0029-GA-ATA and implemented in accordance with the Commission's Order in that case.²⁰

This Stipulation recognizes that the “net normalized” EDIT balance was being proposed to be addressed in this proceeding in lieu of the rate case.²¹ This Stipulation also recognized that this proceeding would resolve any “other issues associated with the flow back of tax savings.”²²

In the *Tax COI*, the Commission noted that there was not a one-size-fits-all approach to passing back tax savings to customers and that therefore it would resolve issues on a case-by-case basis.²³ While Staff may prefer to address the issue in a rate case, VEDO is not expected to have another rate case for a number of years and the parties explicitly agreed to remove EDIT issues from the *Rate Case* and address those issues here. VEDO's unique circumstances warrant, and the Commission-approved *Rate Case* Stipulation requires, that the issue be addressed here.

Because capturing the reduction in ADIT rate base credit is standard practice in distribution ratemaking, because making the ADIT adjustments on an annual basis is standard practice in rider mechanisms, because the Commission-approved *Rate Case*

²⁰ *Rate Case* Stipulation at 12.

²¹ *Id.* (emphasis added).

²² *Id.*

²³ *Tax COI* Order at 17; see also *In re Suburban Natural Gas Co.*, Case Nos. 20-43-GA-ATA et al, Finding and Order at 7-8 (Sept. 9, 2020).

Stipulation requires VEDO to address its EDIT in a rider mechanism, and because VEDO's application mirrors the outcome the Commission directed VEDO to follow, the Commission should approve Component D of VEDO's Application.

B. VEDO Should At Least Be Authorized to Account for the Return of Normalized EDIT Associated with its Infrastructure Riders.

Like many gas and electric utilities, VEDO has infrastructure related riders that recover the costs of some Commission-approved infrastructure development activities.²⁴ As noted above, PUCO Staff is on record indicating that the return of Normalized EDIT associated with these types of riders is appropriate to capture in updates to the riders.²⁵ VEDO's circumstances are again unique and at a minimum warrant addressing Normalized EDIT associated with its infrastructure riders in this proceeding.

As noted above, VEDO had a rate case that was pending and overlapped with the *Tax COI*. In VEDO's *Rate Case*, VEDO reset the baseline for recovery through its DRR and as part of that reset incorporated all EDIT associated with DRR accounts into the *Rate Case*.²⁶ As part of the consolidated *Rate Case*, VEDO also filed an alternative regulation application seeking approval of its Capital Expenditure Program ("CEP") Rider. And, again, because VEDO agreed in the *Rate Case* Stipulation that all EDIT related issues would be resolved here, VEDO could not turn around and seek to address the DRR- or CEP-related Normalized EDIT in VEDO's annual DRR or CEP filings. Thus, the same Normalized EDIT associated with infrastructure replacement riders that Staff acknowledged was appropriate for Dominion to recover through Dominion's riders is at

²⁴ VEDO's Distribution Replacement Rider ("DRR") focuses on the cost of replacing and retiring certain types pipes more prone to leak. See Case No. 20-101-GA-RDR, Application at 2-3.

²⁵ *Supra*, at 7, n. 15-16.

²⁶ *Rate Case*, Direct Testimony of J. Cas Swiz at 29-30 (Apr. 13, 2018).

issue for VEDO in this proceeding. The Commission has recognized that tax issues would need to be resolved differently for different utilities, and this is a prime example of why the outcome for VEDO is unique and reasonable to be addressed as part of its TSCR.

The Normalized EDIT associated with VEDO's DRR is \$18,418,357.32 and CEP is \$19,516,194.98, and together they account for approximately 64.39% of the \$58.9M Normalized EDIT balance.²⁷

While the Commission should authorize VEDO to account for the entire reduction in Normalized EDIT in the TSCR, consistent with Staff's position that it is appropriate to account for amounts related to riders outside of a rate case, the Commission should at a minimum allow VEDO to account for the 64.39% of Normalized EDIT associated with the CEP and DRR riders in the annual updates to the TSCR.

IV. CONCLUSION

VEDO is committed to returning all tax savings to customers to which they are entitled, and has demonstrated that in this proceeding by settling nearly all issues and expediting the flow of the tax credits to customers before the sole contested issue in VEDO's application could be resolved through litigation. VEDO's remaining request in Component D of the Application is an imminently reasonable one – if Staff insists that the tax savings be returned through a newly created mechanism, then VEDO is entitled to recover the cost of doing so. This is not a method of withholding part of the tax savings from customers, nor is it a method to create additional revenue for VEDO. Staff has acknowledged as much in other proceedings. Accounting for the reduction in cost free

²⁷ See Direct Testimony of J. Cas Swiz at 5.

capital as ADIT balances decreases, the issue before the Commission now, is routine practice in the ratemaking formula that applies to base rates and annual reconciling riders. VEDO respectfully requests that the Commission approve Component D of its application.

Respectfully submitted,

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CERTIFICATE OF SERVICE

In accordance with Rule 4901-1-05, Ohio Administrative Code, the PUCO's e-filing system will electronically serve notice of the filing of this document upon the following parties. In addition, I hereby certify that a service copy of the foregoing *Initial Brief of Vectren Energy Delivery of Ohio, Inc.* was sent by, or on behalf of, the undersigned counsel for Vectren Energy Delivery of Ohio, Inc., to the following parties of record on this 9th day of October 2020, *via* electronic transmission, hand-delivery or U.S. mail, postage prepaid.

/s/ Matthew R. Pritchard

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This foregoing document was electronically filed with the Public Utilities

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10/9/2020 5:07:27 PM

in

Case No(s). 19-0029-GA-ATA

Summary: Brief Initial Brief of Vectren Energy Delivery of Ohio, Inc. electronically filed by Mr. Matthew R. Pritchard on behalf of Vectren Energy Delivery of Ohio, Inc.