165 FERC ¶ 61,275
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Neil Chatterjee, Chairman;
Cheryl A. LaFleur, Richard Glick.

PJM Interconnection, L.L.C.
Public Service Electric and Gas Company

Docket No. ER19-204-000

ORDER ACCEPTING TARIFF REVISIONS SUBJECT TO THE ADDITION OF FOOTNOTE AND TO THE CORRECTION OF ACCOUNT NUMBERS

(Issued December 28, 2018)

1. On October 29, 2018, pursuant to section 205 of the Federal Power Act (FPA),[1] PJM Interconnection, L.L.C. (PJM) filed on behalf of Public Service Electric and Gas Company (PSEG) proposed revisions to PJM's Open Access Transmission Tariff (OATT, or Tariff)[2] transmission formula rate (Formula Rate) to address various income tax-related items relating to the effects of the Tax Cuts and Jobs Act of 2017 (TCJA) and other Commission formula rate determinations.[3] In this order, we accept the proposed revisions, subject to the correction of account numbers, the addition of a clarifying footnote, and submission of a compliance filing, effective January 1, 2019, as discussed more fully below.

I. Background

2. Among other things, the TCJA reduced the federal corporate income tax rate from a maximum of 35 percent to a flat 21 percent, effective January 1, 2018. This tax rate reduction also results in a reduction in accumulated deferred income tax (ADIT) liabilities and ADIT assets on the books of rate-regulated companies. Moreover, a portion of an ADIT liability that was collected from customers will no longer be owed to the Internal Revenue Service (IRS) and is considered excess ADIT. On November 15,

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[1] 16 U.S.C. § 824d (2012).

[2] PJM Interconnection, L.L.C., Intra-PJM Tariffs, OATT ATT H-10A, OATT Attachment H-10A - Public Service Electric and Gas Comp (11.0.0).

[3] Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054 (2017) (TCJA).

2018, the Commission issued a Notice of Proposed Rulemaking to address the effects of the TCJA on the ADIT reflected in all transmission rates under an OATT, a transmission owner tariff, or a rate schedule of public utility transmission providers (ADIT NOPR).[4]

II. Filing

3. PSEG proposes to revise its Formula Rate template under PJM's Tariff to address income tax-related items that are the result of the TCJA and other recent Commission precedent. Specifically, PSEG proposes the following three changes: (1) a modification to allow the return to (or recovery from) customers of the excess (or deficient) ADIT resulting from changes in the income tax laws; (2) a revision to prospectively account for deferred income taxes associated with the equity component of the Allowance for Funds Used During Construction (AFUDC Equity); and (3) the elimination of the two-step averaging method of calculating the prorated ADIT balance. PSEG states the result of its proposed changes will be an 11.7 percent reduction in 2019 transmission rates, or a reduction of approximately $157 million. PSEG requests that the Commission treat this as a single-issue rate filing, consistent with recent precedent, and requests an effective date of January 1, 2019.[5]

A. Flow-Back of Excess (or Recovery of Deficient) ADIT

4. PSEG proposes modifications to Appendix A of its Formula Rate in order to return to customers the excess deferred taxes that it collected as a result of the reduction in the federal income tax rate from 35 percent to 21 percent under the TCJA. PSEG explains that this proposed change will also enable the flow-back to, or recovery from, customers of excesses or deficiencies if there are future changes in income tax rates.

5. First, PSEG proposes to add line items to its Formula Rate that will adjust rate base for excess ADIT recorded in Account 254 (Other Regulatory Liabilities), or for deficient ADIT recorded in Account 182.3 (Other Regulatory Assets). PSEG states that the addition of lines 44a, 44b, and 44c (Regulatory Assets and Liabilities) are necessary to ensure that its rate base is adjusted to reflect the sum of any excess and deficient deferred taxes. PSEG states that it recorded excess deferred tax balances at the end of

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[4] *Pub. Util. Transmission Rate Changes to Address Accumulated Deferred Income Taxes*, 165 FERC ¶ 61,117, at P 1 (2018) (ADIT NOPR); *see also Inquiry Regarding the Effect of the Tax Cuts and Jobs Act on Commission-Jurisdictional Rates*, 162 FERC ¶ 61,223 (2018) (seeking comment on whether, and if so how, the Commission should address the effects of the TCJA on ADIT and bonus depreciation in Commission-jurisdictional rates).

[5] PSEG Filing Letter at 1–2.

2017 in Account 254, and the addition of these line items will ensure that plant-related excess deferred tax remains a reduction to rate base.[6]

6. Second, PSEG proposes additional lines 128a to 128e, and Notes S and T to provide for the flow-back of excess (or recovery of deficient) deferred income taxes to customers.[7]

7. PSEG proposes to amortize the "protected" excess ADIT amounts using the IRS-mandated average rate assumption methodology (ARAM).[8] For "unprotected" excess ADIT amounts, PSEG proposes to flow back the amounts to customers evenly over calendar year 2019.[9] PSEG states that during its annual Formula Rate update, it will provide a work paper identifying and describing the excess or deficient deferred income taxes being amortized, which will come directly from its tax accounting records.

8. PSEG states that these proposed revisions are consistent with Commission guidance and recent Commission precedent. For example, PSEG states that the Commission has previously approved tariff revisions to enable amortization of the effect of tax law or tax rate changes in the income tax calculation of formula rates, and reflect the effect of excess or deficient ADIT on rate base by reducing or increasing the tax expense.[10] PSEG asserts that the Commission has approved similar formula rate

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[6] *Id.* at 5.

[7] PSEG proposes that lines 128a and 128b will include the "amortized deficient deferred taxes" recorded to Account 407.3 (Regulatory Debits) and "amortized excess deferred taxes" recorded to Account 407.4 (Regulatory Credits), respectively. Line 128c is the total of 128a and 128b. Line 128d is the tax gross-up percentage. Line 128e is the total net deficient and excess deferred tax amortization grossed up for taxes (Line 128c multiplied by Line 128d). PSEG Filing Letter at 5.

[8] Protected excess ADIT consists of tax depreciation associated with plant assets. *Id.* at 6.

[9] Unprotected excess ADIT consists of items not subject to tax depreciation, such as book-to-tax basis adjustments. *Id.*

[10] *Id.* (citing *Midcontinent Indep. Sys. Operator, Inc.*, 163 FERC ¶ 61,163, at P 7 (2018) (Ameren)).

modifications that permit the return of excess deferred taxes (or the recovery of deficient taxes) because they provide for a more accurate annual revenue requirement.[11]

9. Finally, PSEG states that its proposed revisions are consistent with the Commission's normalization rules and the Commission's Chief Accountant's guidance on accounting for income taxes.[12]

B. AFUDC Equity

10. PSEG proposes to modify Appendix A of its Formula Rate to recognize that the portion of depreciation expense associated with AFUDC Equity is not deductible for income tax purposes. PSEG states that, currently, its Formula Rate treats the depreciation component of its revenue requirement as if it was fully deductible. PSEG states that this fails to collect its actual tax expense associated with AFUDC Equity, resulting in a deficiency in tax revenues. PSEG states that this modification is intended to be prospective in nature, starting in 2019, so that it captures on-going amounts that have not yet been recovered in rates.[13]

11. PSEG estimates that this change to its Formula Rate will result in a $1.7 million transmission rate increase – approximately 0.1 percent – in 2019. As with its other proposed changes to Appendix A of the Formula Rate, PSEG states that it will provide a work paper during its annual Formula Rate filing that identifies and describes the amount of AFUDC Equity (and associated depreciation), and the effect on its income tax

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[11] *Id.* (citing *Midcontinent Indep. Sys. Operator, Inc.*, 153 FERC ¶ 61,374, at P 12 (2015) (ITC Companies)).

[12] *Id.* at 6–7 (citing, *e.g.*, *Regulations Implementing Tax Normalization for Certain Items Reflecting Timing Differences in the Recognition of Expenses or Revenues for Ratemaking and Income Tax Purposes*, Order No. 144, FERC Stats. & Regs. ¶ 30,254 (1981), *order on reh'g*, Order No. 144-A, FERC Stats. & Regs. ¶ 30,340 (1982), *aff'd sub nom. Pub. Sys. v. FERC*, 709 F.2d 73 (D.C. Cir. 1983)).

[13] PSE&G proposes to add lines 128f, 128g, and 128h, labeled "AFUDC Equity Permanent Difference," to its Formula Rate – Appendix A. Specifically, line 128f includes the addback of book deprecation related to AFUDC Equity. Line 128g is the tax gross-up percentage (1/(1-T)). Line 128h computes the AFUDC Equity Permanent Difference Tax Adjustment by multiplying the tax gross-up percentage on Line 128g by the depreciation expense associated with AFUDC included on Line 128f. PSEG also proposes to add Note U to provide further explanation. PSEG Filing Letter at 7.

expense. PSEG states that the work paper will come directly from its tax accounting records.

12. PSEG argues that these proposed revisions are consistent with: recent Commission precedent; the Commission's recognition that the depreciation associated with AFUDC Equity is not tax-deductible; and, the Commission's normalization rules detailed in Order No. 144-A.[14]

C. <u>Averaging Method Used to Calculate ADIT</u>

13. PSEG states that, in Attachment 1 of its current Formula Rate, PSEG calculates the ADIT balance by prorating the projected monthly change in plant-related deferred taxes, and then averaging the beginning and end-of-year balances. PSEG states that this is referred to as the two-step averaging method. PSEG notes that following a 2017 private letter ruling by the IRS to a public utility taxpayer on this issue, the Commission rejected a proposal that applied the two-step averaging method; moreover, the Commission later identified additional entities that use this method and could address the Commission's concerns with it by eliminating its use in determining ADIT balances.[15] Accordingly, PSEG proposes in the instant filing to eliminate the two-step averaging method so that the calculation method is consistent with a methodology recently supported by the Commission.[16] Based upon its 2019 annual Formula Rate forecast,

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[14] *Id.* at 8 (citing, *e.g.*, Ameren, 163 FERC ¶ 61,163 at P 57; Order No. 144-A, FERC Stats. & Regs. ¶ 30,340 at 30,136).

[15] *Id.* at 9 (citing, *e.g.*, *Ameren Ill. Co.*, 163 FERC ¶ 61,200 (2018)).

[16] PSEG proposes to revise Formula Rate Attachments 1 and 1A by separating the amounts in Account 282 (Accumulated Deferred Income Taxes—Other Property) in to two categories: those that are not prorated, and those that are. The former will continue to use the simple average of the beginning and end-of-year balances. The latter will reflect the pro rata amount of any increase during the future portion of the period as determined by multiplying the monthly increase or decrease by a fraction: the number of days remaining in the period at the time the increase is to accrue, divided by the total number of days in the future portion of the period. PSEG states that the monthly prorated amounts will be shown in the ADIT – 282 (Subject to Proration) section of Attachment 1 – ADIT Worksheet. The prorated balance included in Total ADIT – 282 (Subject to Proration) will be added to the simple average of ADIT Accounts 190 (Accumulated Deferred Income Taxes), 282 (Not Subject to Proration), and 283 (Accumulated Deferred Income Taxes—Other). PSEG Filing Letter at 9.

PSEG estimates this change will result in an approximately $1 million reduction in its revenue requirement.

III. Notice and Responsive Pleadings

14. Notice of PSEG's filing was published in the *Federal Register*, 83 Fed. Reg. 55,158 (2018), with interventions and protests due on or before November 19, 2018. The New Jersey Board of Public Utilities, PPL Electric Utilities Corporation, and the Public Power Association of New Jersey each filed timely motions to intervene. The New Jersey Division of Rate Counsel (Rate Counsel) filed a timely motion to intervene and limited protest. PSEG filed a motion for leave to answer and answer to Rate Counsel's limited protest.

A. Protest

15. Rate Counsel's protest is limited to PSEG's proposal to flow back excess/deficient ADIT amounts, and it states that it does not oppose PSEG's proposals regarding rate treatment of AFUDC Equity and elimination of the two-step averaging method to calculate ADIT balances.[17]

16. Rate Counsel argues that PSEG's proposal to flow back excess/deficient ADIT amounts violates Commission policy with respect to ratemaking treatment of regulatory assets/liabilities, because PSEG seeks to include these amounts in rates without prior Commission approval, which Rate Counsel argues requires a separate FPA section 205 filing.[18] Rate Counsel also notes that the Commission stated in the ADIT NOPR that the return of excess ADIT or collection of deficient ADIT is not a "one-size-fits-all" proposition for all utilities, and Rate Counsel thus argues that the Commission should require a utility to show that its rate—after including a regulatory asset or liability—is just and reasonable.[19]

17. Rate Counsel also argues that PSEG's proposed formula rate revisions do not meet the Commission's requirements because PSEG has not provided sufficient data to enable review of its calculations. Rate Counsel objects to PSEG's reliance on a promise to provide a work paper and data as part of its formula rate annual update. Rate Counsel

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[17] Rate Counsel Protest at 4.

[18] *Id.* at 4–5 (citing *Piedmont Mun. Power Agency v. Duke Energy Carolinas, LLC*, 162 FERC ¶ 61,109, at P 32 (2018) (*Piedmont*) (citing *Virginia Elec. and Power Co.*, 128 FERC ¶ 61,026, at PP 22, 31–34 (2009))).

[19] *Id.* at 6–7 (citing ADIT NOPR, 165 FERC ¶ 61,117 at PP 27, 37).

also asserts that PSEG's proposal is inconsistent with the ADIT NOPR because it fails to provide the transparency the Commission seeks from formula rates.[20]

18. Finally, Rate Counsel expresses concerns that PSEG's proposed formula rate revisions would allow it to flow back excess/deficient ADIT amounts arising from future changes in tax law without first seeking Commission approval. Rate Counsel states that it does not oppose a one-year amortization period for unprotected excess ADIT amounts, because this adjustment promotes rate stability in light of other case-specific rate adjustments in PSEG's transmission rates. However, Rate Counsel reiterates that flowing back these amounts is case-specific and that a different amortization period may be appropriate in the future.[21]

19. Rate Counsel accordingly requests that the Commission nominally suspend PSEG's proposed changes, establish a refund effective date, and summarily rule that PSEG must seek Commission approval under FPA section 205 before recovering any future regulatory asset or liability, including flowing back any ADIT-related regulatory asset or liability created by a future change in tax law. Alternatively, Rate Counsel requests that the Commission set this matter for hearing and settlement procedures.[22]

B. <u>Answer</u>

20. PSEG argues a single change to its Formula Rate is sufficient under Commission precedent to address the return of excess or the collection of deficient ADIT. PSEG notes that in Ameren the Commission specifically rejected the argument that formula rate revisions should apply to existing ADIT only.[23] PSEG further argues that its proposal is just and reasonable because its Formula Rate identifies the nature of the specific excess deferred taxes, and customers retain their rights to review inputs.[24] PSEG next maintains that its proposal to address excess/deficient ADIT is consistent with the ADIT NOPR. PSEG states that it is significant that the ADIT NOPR does not suggest the Commission

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[20] *Id.* at 8–9.

[21] *Id.* at 10–11.

[22] *Id.* at 11.

[23] PSEG Answer at 4 (citing Ameren, 163 FERC ¶ 61,163 at P 55).

[24] *Id.* at 5.

will require a new FPA section 205 filing to address excess/deficient ADIT once utilities include a mechanism in their formula rates to address this issue.[25]

21. PSEG also argues that Rate Counsel's use of Commission precedent in its protest is unpersuasive. PSEG points out that *Piedmont* was issued before the Commission considered a FPA section 205 filing involving ADIT in Ameren, and that the ADIT NOPR suggests PSEG's single FPA section 205 filing is sufficient. PSEG further maintains that *Piedmont* is factually distinguishable because the Commission focused its discussion there on Account 407 (Amortization of Property Losses, Unrecovered Plant and Regulatory Study Costs) and specifically Account 407.3. By contrast, PSEG explains that it seeks recovery of amounts in Account 254 or 182.3 that are to be recorded in Accounts 410.1 (Provision for Deferred Income Taxes, Utility Operating Income) and 411.1 (Provision for Deferred Income Taxes—Credit, Utility Operating Income), consistent with a recent Commission policy statement (the ADIT Policy Statement).[26]

22. PSEG next points out that, because the ADIT NOPR is not a final rule, Rate Counsel's argument regarding the permanent worksheet discussed in the NOPR is premature. PSEG maintains that if a final rule makes the permanent worksheet a requirement, then PSEG will submit a compliance filing. In any case, PSEG states, it provided detailed information in the exhibits in its filing; moreover, this is the sort of information PSEG would include in the suggested worksheet. PSEG also clarifies that its proposal consists of a tariff change, not calculations. PSEG maintains that Rate Counsel will have full opportunity to review PSEG's calculations after approval of the requested revisions.[27]

23. Finally, PSEG states a commitment to submit a compliance filing to make its proposal consistent with the ADIT Policy Statement. In the compliance filing, PSEG explains, it will change references to Accounts 407.3 and 407.4 to Accounts 410.1 and 411.1.[28]

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[25] *Id.* at 5–6.

[26] *Id.* at 6–8; *see Accounting and Ratemaking Treatment of Accumulated Deferred Income Taxes and Treatment Following the Sale or Retirement of an Asset*, 165 FERC ¶ 61,115 (2018).

[27] PSEG Answer at 8–9.

[28] *Id.* at 9–10.

IV. Discussion

A. Procedural Matters

24. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2018), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

25. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2018), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We accept PSEG's answer because it has provided information that assisted us in our decision-making process.

B. Substantive Matters

26. We find the proposed revisions to PSEG's Formula Rate to be just and reasonable, and accept the revisions, subject to the correction of account numbers, the addition of a clarifying footnote, and submission of a compliance filing, effective January 1, 2019.[29] The proposed revisions, including the revision to effectuate the return of net excess protected and unprotected ADIT resulting from the TCJA, provide for a more accurate annual revenue requirement for PSEG. We further find that PSEG's proposal to flow back unprotected net excess deferred taxes related to the 2017 tax changes over one year, as well as its proposal to flow back protected net excess deferred taxes related to the 2017 tax changes using ARAM, to be just and reasonable.[30]

27. PSEG initially proposed to amortize the deficient deferred taxes to Account 407.3 and amortize the excess deferred taxes to Account 407.4. PSEG, however, recognized that it erred in choosing these accounts and commits to submit a compliance filing to correct the references to Accounts 407.3 and 407.4 in its proposal to Accounts 410.1 and

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[29] The United States Court of Appeals for the District of Columbia Circuit has held that, in certain circumstances, the Commission has "authority to propose modifications to a utility's [FPA section 205] proposal *if the utility consents to the modifications*." *NRG Power Mktg., LLC v. FERC*, 862 F.3d 108, 114–15 (D.C. Cir. 2017).

[30] The TCJA requires public utilities to return excess protected ADIT no more rapidly than over the life of the underlying asset using ARAM, or, where a public utility's books and underlying records do not contain the vintage account data necessary, it must use an alternative method. TCJA, Section 13001(b)(6)(A), 131 Stat. at 2099. In contrast, the TCJA does not specify what method public utilities must use for excess or deficient unprotected ADIT.

411.1. Accordingly, we accept PSEG's proposed corrections, subject to a compliance filing to be submitted within 30 days of the date of this order.

28. Rate Counsel contends that PSEG's proposal to add line items in its Formula Rate to flow back or recover future excess/deficient ADIT amounts violates Commission policy with respect to ratemaking treatment of regulatory assets/liabilities. In this filing, PSEG sought only the return of net excess protected and unprotected ADIT related to the TCJA; in order to effectuate that return PSEG established a mechanism in its Formula Rate to reflect the costs of those regulatory assets and liabilities in rates. We do not find a violation of Commission policy in accepting a mechanism in a formula rate template related to the return/recovery of excess/deficient ADIT.[31] However, we agree with Rate Counsel that any future attempts to return/recover excess/deficient ADIT will require PSEG to make a FPA section 205 filing before those regulatory assets and liabilities can be reflected in rates. Accordingly, we will accept PSEG's proposal subject to the condition that, within 30 days of the date of this order, PSEG add a footnote to its Formula Rate clarifying that PSEG must submit a FPA section 205 filing to obtain Commission approval prior to reflecting in rates any regulatory assets and liabilities arising from future tax changes.

29. As for Rate Counsel's argument that PSEG has not provided sufficient data to enable review of its calculations regarding the flow-back of ADIT, we find that PSEG's filing, including Exhibits III through VI, provides sufficient detail for us to approve the proposed changes to PSEG's Formula Rate.[32] However, we note that, as the Commission has previously explained, PSEG must provide in its annual formula rate informational filings sufficient support and explanation for all inputs so that interested entities can verify that each input is consistent with the requirements of the formula without forcing interested entities to make extensive information requests to understand the implementation of the formula rate and to verify its correctness.[33] In addition, as to Rate Counsel's argument that PSEG's proposal is inconsistent with the ADIT NOPR, we remind Rate Counsel that the ADIT NOPR is only a proposal to require public utilities

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[31] Ameren, 163 FERC ¶ 61,163 at P 52; *ITC Companies*, 153 FERC ¶ 61,374 at P 1.

[32] Exhibit III is a summary of the estimated impact to the 2019 annual transmission revenue requirement relating to flow-back of excess deferred taxes. Exhibit IV is a summary of estimated excess deferred income tax amortizations. Exhibit V reflects protected and unprotected excess deferred income taxes. Exhibit VI reflects excess deferred income taxes amortization using the ARAM PowerTax Report.

[33] Ameren, 163 FERC ¶ 61,163 at P 57.

with transmission formula rates to incorporate a new permanent worksheet to track ADIT information and is not final.[34]

The Commission orders:

PSEG's proposed Tariff revisions are hereby accepted, effective January 1, 2019, subject to the submission of a compliance filing to add a clarifying footnote and to correct certain account numbers within 30 days of the date of this order, as discussed in the body of this order.

By the Commission. Commissioner McIntyre is not voting on this order.
Commissioner McNamee is not participating.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

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[34] Our action in this order does not foreclose on any potential further action to address the effects of the TCJA through a final rule.