



# The Commonwealth of Massachusetts

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## DEPARTMENT OF PUBLIC UTILITIES

D.P.U. 18-15

February 2, 2018

Investigation by the Department of Public Utilities, on its own Motion, into the Effect of the Reduction in Federal Income Tax Rates on the Rates Charged by Electric, Gas, and Water Companies.

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### ORDER OPENING INVESTIGATION

## I. INTRODUCTION

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (“Act”) was signed into law.<sup>1</sup> Among other things, the Act reduces the federal corporate income tax rate from 35 percent to 21 percent, effective January 1, 2018.<sup>2</sup> This reduction in the federal corporate income tax rate has implications for the investor-owned electric distribution, natural gas distribution, and water companies under the jurisdiction of the Department of Public Utilities (“Department”).

Pursuant to the Department’s ratemaking precedent, companies reflect a representative level of tax expense in their rates. In determining a company’s total cost of service, the Department permits a company to include as an expense a normalized level of federal corporate income taxes. In general, the Department calculates the amount of federal corporate income tax expense by applying the effective tax rate to the allowed rate of return on rate base. See e.g., Fitchburg Gas and Electric Light Company, D.P.U. 1270/1414, at 45-46 (1983).

Because the federal corporate income tax expense reflected in current rates for the Department-jurisdictional electric distribution companies, gas distribution companies, and certain water companies is based on the former higher tax rate, the Department finds that it is

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<sup>1</sup> Pub. L. No. 115-97, 131 Stat. 2054: An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018.

<sup>2</sup> Prior to January 1, 2018, federal corporate income tax was imposed at graduated rates. As of January 1, 2018, the corporate income tax rate is a flat rate.

appropriate to promptly adjust rates so that ratepayers receive the benefits from the decrease in the federal corporate income tax rate. Investigation Into Effect of the Reduction in Federal Income Tax Rates on Utility Rates as a Result of the Tax Reform Act of 1986,

D.P.U. 87-21-A at 22 (1987). To this end, and consistent with our statutory mandate to require just and reasonable rates for utility service, the Department votes pursuant to G.L. c. 164 §§ 76, 93, 94 and G.L. c. 165, §§ 2, 4 to open an investigation into the effect on rates of the decrease in the federal corporate income tax rate on the Department's regulated utilities.

In addition, on December 20, 2017, the Attorney General of the Commonwealth ("Attorney General") filed a complaint and petitioned the Department to open an investigation, pursuant to G.L. c. 164, § 93 ("Petition"), to reduce the rates of the following companies based upon the decrease in the federal corporate income tax rate: Aquarion Water Company of Massachusetts, Inc. ("Aquarion Water"); Bay State Gas Company d/b/a Columbia Gas of Massachusetts; Boston Gas Company and Colonial Gas Company, each d/b/a National Grid ("Boston Gas and Colonial Gas"); Fitchburg Gas and Electric Light Company d/b/a Unitil; Liberty Utilities (New England Natural Gas Company) Corp. d/b/a Liberty Utilities; Massachusetts Electric Company and Nantucket Electric Company, each d/b/a National Grid; Milford Water Company ("Milford Water"); NSTAR Electric Company and Western Massachusetts Electric Company, each d/b/a Eversource Energy ("Eversource"); NSTAR Gas Company, d/b/a Eversource Energy; and The Berkshire Gas Company (collectively, "Respondents"). The Attorney General maintains that because a

higher federal corporate income tax expense is reflected in the revenue requirement used to establish the rates for each of the Respondents, the Department should immediately adjust the Respondents' rates to pass through to ratepayers the benefits of the decrease in the federal corporate income tax rate (Petition at 2-4).

In her Petition, the Attorney General also maintains that the Department should require the Respondents to adjust any excess reserves for accumulated deferred income taxes ("ADIT") related to the Act.<sup>3</sup> In particular, the Attorney General maintains that any ADIT that had been accumulated at the higher federal corporate income tax rate of 35 percent should be ultimately passed back to ratepayers at the lower tax rate of 21 percent, over the remaining lives of the property that gave rise to the reserve (Petition at 4-5). Finally, the Attorney General maintains that the ratemaking effect of the reduction in the federal corporate income tax rate requires a straightforward calculation based on facts adjudicated in each Respondent's most recent rate case (Petition at 5, citing D.P.U. 87-21-A at 10).

The Department docketed the Attorney General's Petition as D.P.U. 17-181.

Pursuant to 220 CMR 1.09, the Department finds that the proceedings involve common

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<sup>3</sup> Deferred income taxes are accrued when a company has a current deduction or credit for tax purposes, but not for book purposes. The Berkshire Gas Company, D.P.U. 90-121, at 136 (1990). The ADIT balance is a source of interest-free funds provided by ratepayers that a company can use without incurring borrowing costs or invest and accrue interest until the balance is needed to fund the taxes due and payable in later years. Therefore, for ratemaking purposes, ADIT represents an offset to a company's rate base. Essex County Gas Company, D.P.U. 87-59, at 63 (1987); AT&T Communications of New England, Inc., D.P.U. 85-137, at 31 (1985); Boston Edison Company, D.P.U. 1350, at 42-43 (1983); Boston Edison Company, D.P.U. 18200, at 33-34 (1975).

questions of law and fact and, therefore, consolidates D.P.U. 17-181 with the instant investigation.<sup>4</sup>

## II. DISCUSSION

The Department opens this investigation to examine the effect of the Act on the rates of the investor-owned electric, gas, and water companies in Massachusetts. Consistent with our statutory mandate to require just and reasonable rates, the Department is obligated to ensure that Massachusetts ratepayers receive the immediate benefit of this significant change in the federal tax code. D.P.U. 87-21, at 3.

The focus of the investigation will be the electric, gas, and water companies with rates that were established using a federal corporate income tax expense based on a tax rate that was higher than the rate established by the Act. These companies include the Respondents listed by the Attorney General, as well as Agawam Springs Water Company (“Agawam Springs”), Blackstone Gas Company, Pinehills Water Company, and Whitinsville Water Company (“Whitinsville Water”) (together with the Respondents, “Affected Companies”).<sup>5</sup> For the Affected Companies, the reduction in the federal corporate income tax rate results in both a lower tax expense on current income and booked ADIT that are in excess of future liabilities. Accordingly, the Department finds that the statutory reduction in

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<sup>4</sup> All documents filed in this consolidated proceeding will be docketed in D.P.U. 18-15.

<sup>5</sup> A number of water companies have rates established using a federal corporate income tax expense based on a tax rate lower than 21 percent. See e.g., Plymouth Water Company, D.P.U. 14-120 (2015). Therefore, these companies are not included in this investigation.

the federal corporate income tax rates pursuant to the Act constitutes evidence that the rates being charged by each Affected Company may no longer be just and reasonable as of January 1, 2018.

To address this issue, each Affected Company shall, as of January 1, 2018 (i.e., the effective date of the reduction in the federal tax rate), account for any revenues associated with the difference between the previous and current corporate income tax rates. In addition, each Affected Company shall account for excess recovery in rates of ADIT resulting from the lower federal corporate income tax rate. Such amounts shall be booked as regulatory liabilities, effective January 1, 2018, to be refunded to ratepayers in a manner to be determined by the Department in this proceeding. The Department fully expects that under this review, ratepayers will be made whole for any delay in flow back of ADIT.

On or before May 1, 2018, each Affected Company shall file a proposal to address the effects of the Act and, in particular, a proposal to reduce its rates through the establishment of a revised cost of service incorporating the lower federal corporate income tax rate as of January 1, 2018, and holding all other components used to design rates constant. Such proposals must address the adjustment of rates going forward and also incorporate the timely refund of revenues associated with the lower tax expense on current income and excess ADIT, and any other related adjustment necessitated by the Act.<sup>6</sup> To the

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<sup>6</sup> The filings are due on or before May 1, 2018, in order to allow the Affected Companies sufficient time to conduct a comprehensive review of the Act. NSTAR Electric Company and Western Massachusetts Electric Company, D.P.U. 17-05-C at 14 (2018).

extent practical, the Department encourages the Affected Companies to collaborate on the development of a joint proposal for Department review regarding the appropriate methods to implement the above adjustments in rates.<sup>7</sup>

The calculation of the revised cost of service and methods to implement adjustments in rates shall be accompanied by testimony and supporting documentation from each Affected Company.<sup>8</sup> Each Affected Company shall base all calculations on the cost of service and billing determinants approved in its most recent rate case. All calculations shall assume that, for ratemaking purposes, adjustments will occur for rates effective July 1, 2018.<sup>9</sup>

In addition, each Affected Company shall identify the effect, if any, of the federal corporate income tax rate decrease on its various reconciling mechanisms. Finally, the filing may include any other issues related to the effects of the Act that the Affected Companies find appropriate to raise.

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<sup>7</sup> In the event that a joint proposal is filed by some but not all of the Affected Companies, each Affected Company unable to join in such proposal should be prepared to discuss the unique nature of the circumstances that ultimately precluded its participation in such an effort.

<sup>8</sup> Documentation should include a calculation of the regulatory liability accrued from January 1, 2018 to date, and expected to be accrued through the establishment of new rates in this proceeding.

<sup>9</sup> To the extent that an Affected Company seeks to implement any part of its rate adjustment, including the refund of excess ADIT, on a date later than July 1, 2018, the Affected Company must demonstrate that ratepayers will not be harmed by the proposal and that the proposal is otherwise in the public interest. See D.P.U. 17-05-C at 14 n.11; see also, D.P.U. 17-181, Letter Clarifying The Berkshire Gas Company's Answer to the Attorney General's Initial Filing (January 9, 2018).

The Department recognizes that several Affected Companies currently have rate cases pending before the Department (i.e., Agawam Springs (D.P.U. 17-52), Aquarion Water (D.P.U. 17-90), Boston Gas and Colonial Gas (D.P.U. 17-170), Milford Water (D.P.U. 17-107), and Whitinsville Water (D.P.U. 17-108)). In addition to the filing required in this investigation, the aforementioned companies shall file supplemental testimony and exhibits addressing these issues in their applicable rate case dockets.<sup>10</sup>

In addition, the Department recently approved rates for Eversource for effect February 1, 2018, that incorporate the change to its normalized level of federal corporate income taxes as a result of the Act. D.P.U. 17-05-C at 9, 11. However, the Department deferred for consideration as part of this investigation: (1) the appropriate treatment of excess ADIT, and (2) Eversource's proposal to credit to ratepayers an amount representing the revenue requirement impact associated with the reduction of the federal corporate income tax rate for January 2018. D.P.U. 17-05-C at 13-14. Accordingly, consistent with the directives set forth above, Eversource shall file a proposal with the Department addressing each of these issues on or before May 1, 2018.

Copies of all filings also shall be served on the Attorney General and all intervenors in each Affected Company's last general rate case. This proceeding will be conducted pursuant to the Department's procedural rules at 220 CMR 1.00 et seq. Subsequent to the

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<sup>10</sup> The Department recognizes that other companies may seek to file base rate proceedings in 2018. To the extent a company files a base rate case prior to the conclusion of the investigation in the instant proceeding, it must file testimony and exhibits addressing these issues as part of its initial rate case filing.



submissions by the Affected Companies, the Department will issue a notice inviting intervention pursuant to 220 CMR 1.03 and hold a hearing to allow an opportunity for public comment. Thereafter, the Department will issue a procedural schedule for further process.

### III. ORDER

Accordingly, the Department

VOTES: To open an investigation, on its own motion, into the effect of the reduction in federal corporate income tax rates on the rates charged by electric, gas, and water companies; and it is

ORDERED: That Agawam Springs Water Company; Aquarion Water Company of Massachusetts, Inc.; Bay State Gas Company d/b/a Columbia Gas of Massachusetts; Blackstone Gas Company; Boston Gas Company and Colonial Gas Company, each d/b/a National Grid; Fitchburg Gas and Electric Light Company d/b/a Unitil; Liberty Utilities (New England Natural Gas Company) Corp. d/b/a Liberty Utilities; Massachusetts Electric Company and Nantucket Electric Company, each d/b/a National Grid; Milford Water Company; NSTAR Electric Company and Western Massachusetts Electric Company, each d/b/a Eversource Energy; NSTAR Gas Company, d/b/a Eversource Energy; Pinehills Water Company; The Berkshire Gas Company; and Whitinsville Water Company shall, as of January 1, 2018, account for as a regulatory liability any revenues associated with the difference between the previous and current federal corporate income tax rates and excess accumulated deferred income taxes resulting from the lower federal corporate income tax rate; and it is

FURTHER ORDERED: That, on or before May 1, 2018, Agawam Springs Water Company; Aquarion Water Company of Massachusetts, Inc.; Bay State Gas Company d/b/a Columbia Gas of Massachusetts; Blackstone Gas Company; Boston Gas Company and Colonial Gas Company, each d/b/a National Grid; Fitchburg Gas and Electric Light Company d/b/a Unitil; Liberty Utilities (New England Natural Gas Company) Corp. d/b/a Liberty Utilities; Massachusetts Electric Company and Nantucket Electric Company, each d/b/a National Grid; Milford Water Company; NSTAR Electric Company and Western Massachusetts Electric Company, each d/b/a Eversource Energy; NSTAR Gas Company, d/b/a Eversource Energy; Pinehills Water Company; The Berkshire Gas Company; and Whitinsville Water Company shall submit a proposal to revise rates consistent with the directives contained herein; and it is

