

**IN THE TENNESSEE PUBLIC UTILITY COMMISSION
AT NASHVILLE, TENNESSEE**

IN RE:

**COMPLIANCE FILING OF
PIEDMONT NATURAL GAS
COMPANY, INC. REGARDNG
THE IMPACT OF FEDERAL TAX
REFORM ON PUBLIC UTILITY
REVENUE REQUIREMENTS**

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**DOCKET NO.
18-00040**

DIRECT TESTIMONY

OF

DAVID DITTEMORE

January 15, 2019

IN THE TENNESSEE PUBLIC UTILITY COMMISSION
AT NASHVILLE, TENNESSEE

IN RE:)
)
COMPLIANCE FILING OF PIEDMONT) Docket No. 18-00040
NATURAL GAS COMPANY, INC.)
REGARDING THE IMPACT OF)
FEDERAL TAX REFORM ON PUBLIC)
UTILITY REVENUE REQUIREMENTS)

AFFIDAVIT

I, David N. Dittmore, Financial Analyst, on behalf of the Consumer Advocate Unit of the Financial Division of the Attorney General's Office, hereby certify that the attached Direct Testimony represents my opinion in the above-referenced case and the opinion of the Consumer Protection and Advocate Division.



David N. Dittmore
DAVID N. DITTEMORE

Sworn to and subscribed before me this 14th day of January, 2018.

Emily Knight

NOTARY PUBLIC

My commission expires: May 6, 2019

CONTENTS

I. FINANCIAL IMPLICATIONS OF TCJA ON UTILITIES	3
A. Cash Flow Negative for Utilities	3
B. Rate Base Will Increase, Increasing Piedmont Earnings	3
II. IDENTIFICATION OF TCJA IMPACTS	4
A. TCJA Impacts on Income Tax Expense	4
B. TCJA Impacts on Accumulated Deferred Income Taxes (ADIT)	4
C. Amortization Methodology Applicable to Excess “Protected” ADIT	6
III. OVERVIEW OF PIEDMONT PROPOSAL	6
IV. CONSUMER ADVOCATE UNIT RESPONSE AND RECOMMENDATION	8
A. Income Tax Expense	8
B. Excess ADIT	13
V. PIEDMONT’S DEFERRED TAX LIABILITY BALANCE, INCLUDING	
DETERMINATION OF EXCESS ADIT	16

ATTACHMENTS

Exhibit DND-1

Exhibit DND-2

Exhibit DND-3

1 **Q1. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND OCCUPATION**
2 **FOR THE RECORD.**

3 **A1.** My name is David N. Dittemore. My business address is Office of the Tennessee
4 Attorney General, War Memorial Building, 301 6th Ave., North, Nashville, TN 37243.
5 I am a Financial Analyst employed by the Consumer Advocate Unit of the Financial
6 Division of the Tennessee Attorney General's Office (Consumer Advocate).

7 **Q2. PLEASE PROVIDE A SUMMARY OF YOUR BACKGROUND AND**
8 **PROFESSIONAL EXPERIENCE.**

9 **A2.** I received a Bachelor of Science Degree in Business Administration from the University
10 of Central Missouri in 1982. I am a Certified Public Accountant licensed in the state of
11 Oklahoma (#7562). I was previously employed by the Kansas Corporation Commission
12 (KCC) in various capacities, including Managing Auditor, Chief Auditor and Director
13 of the Utilities Division. For approximately four years, I was self-employed as a Utility
14 Regulatory Consultant representing primarily the KCC Staff in regulatory issues. I also
15 participated in proceedings in Georgia and Vermont, evaluating issues involving
16 electricity and telecommunications regulatory matters. Additionally, I performed a
17 consulting engagement for Kansas Gas Service (KGS), my subsequent employer during
18 this time frame. For eleven years I served as Manager and subsequently Director of
19 Regulatory Affairs for KGS, the largest natural gas utility in Kansas serving
20 approximately 625,000 customers. KGS is a division of One Gas, a natural gas utility
21 serving approximately two million customers in Kansas, Oklahoma and Texas. I joined
22 the Tennessee Attorney General's Office in September 2017 as a Financial Analyst.
23 Overall, I have thirty years' experience in the field of public utility regulation. I have
24 presented testimony as an expert witness on many occasions. Attached as Exhibit 1 is
25 a detailed overview of my background.

1 **Q3. HAVE YOU PREVIOUSLY PROVIDED TESTIMONY BEFORE THE**
2 **TENNESSEE PUBLIC UTILITY COMMISSION (TPUC)?**

3 **A3.** Yes. I have submitted testimony in TPUC Docket Nos. 17-00014, 17-00108, 17-00138,
4 17-00124, 17-00143, 18-00017, 18-00022, 18-00034, 18-00038, 18-00067 and 18-00097.

5 **Q4. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

6 **A4.** The purpose of my testimony is to offer the Consumer Advocate's recommendations on
7 the appropriate ratemaking treatment resulting from the federal Tax Cut and Jobs Act
8 (TCJA) for Piedmont Natural Gas - Tennessee division (Piedmont).

9 **I. FINANCIAL IMPLICATIONS OF TCJA ON UTILITIES**
10

11 **A. Cash Flow Negative for Utilities**

12 **B. Rate Base Will Increase, Increasing Piedmont Earnings**

13 **Q5. WHAT ARE THE IMPLICATIONS OF THE TCJA ON UTILITIES CASH FLOW?**

14 **A5.** The provisions of the TCJA are cash flow negative for utilities.¹ The provisions of the
15 TCJA no longer permit Bonus Depreciation, which historically² has allowed utilities to
16 deduct fifty percent of the costs of capital expenditures from taxable income. The
17 availability of this deduction, coupled with the effective requirement to normalize income
18 taxes at a 35% federal tax rate, resulted in collections from ratepayers for income taxes that
19 were not remitted to the Internal Revenue Service (IRS), creating favorable cash flows for
20 utilities, including Piedmont. With the significant reduction in the federal tax rate, a
21 portion of the tax prepayments collected from ratepayers are effectively cancelled and
22 ratepayers' funds will be returned over an extended period, translating to a cash outflow.
23 The effective cancellation of a portion of these pre-payments is referred to as "excess"
24 Accumulated Deferred Income Taxes (ADIT).

25 However, these cash flow impacts should be put in context. The normalization requirement
26 remains in the tax code and coupled with the availability of accelerated tax depreciation

¹ Atmos Response to Consumer Advocate No. 1-11, Attachment 1, TPUC No. 18-00034, (Nov. 5, 2018).

² Bonus Depreciation was available beginning May 6, 2003. Bonus Depreciation was extended under the Job Creation Act of 2010.

ensures cash flow from Operation will remain strong, albeit not as strong as it was with availability of Bonus Depreciation.

Q6. WHAT ARE THE IMPLICATIONS OF THE TCJA ON UTILITIES EARNINGS?

A6. The TCJA will result in an increase in utility earnings, including Piedmont, in the long-run. The amount of prepaid taxes collected from ratepayers will not be as great as it has historically as a result of the reduction in the tax rate. The tax pre-payments are reflected within the balance of ADIT and are a reduction to rate base. Also, this balance will be reduced as ratepayer funds are returned to them through the amortization of the excess deferred taxes, thus increasing rate base. In summary, the rate of growth in the ADIT balance will not be as great as it has been historically, resulting in an increase in rate base. As rate base increases, earnings will increase.

II. IDENTIFICATION OF TCJA IMPACTS

- A. TCJA impacts on Income Tax Expense
- B. TCJA impacts on Accumulated Deferred Income Tax
- C. Amortization Methodology applicable to excess "Protected" ADIT

A. TCJA Impacts on Income Tax Expense

Q7. DISCUSS THE IMPLICATIONS OF THE TCJA ON A UTILITY'S INCOME TAX EXPENSE

A7. The largest impact of the TCJA is simply the reduction in Income Tax Expense resulting from the reduction in the federal income tax rate from 35% to 21%. The computation of the reduction in Income Tax expense is relatively straight-forward.

B. TCJA Impacts on Accumulated Deferred Income Taxes (ADIT)

Q8. DISCUSS THE IMPLICATIONS OF THE TCJA ON A UTILITY'S ACCUMULATED DEFERRED INCOME TAX BALANCE (ADIT).

A8. The more complex TJCA issue is the quantification of the impact of the tax rate change on the utility's ADIT Balance and how the cancellation of these prepaid taxes should be treated for ratemaking purposes. The balance of ADIT represents taxes that have been

provided by ratepayers within rates (base rates or IMR surcharge rates), but which the utility will not pay until some point in the future.³ Because these balances represent funds provided by ratepayers, they have a zero cost to the utility. These customer-provided funds finance utility operations and are properly reflected as a reduction in rate base since it reduces the funds necessarily provided by the utility. The reduction in the tax rate effectively cancels a portion of these future tax payments. The reduction in these future tax obligations is referred to as excess ADIT, since the funds are no longer required to pay future taxes.

Q9. ARE THERE DIFFERENT TYPES OF EXCESS ADIT?

A9. Yes. There are two categories of excess ADIT, “Protected” and “Unprotected”. Excess “Protected” ADIT relates to book and tax timing differences associated with Depreciation Expense. The tax code requires that for ratemaking purposes, the lower depreciation expense, relying upon lower regulatory-determined depreciation rates, be used within the calculation of Income Tax Expense⁴ included in the determination of rates. With respect to ratemaking, the use of a lower book expense within the income tax calculation yields a higher taxable income for ratemaking purposes, resulting in a higher level of Income Tax Expense included in base rates. This calculation contrasts with the calculation of taxable income for federal income tax payment purposes, which permits much higher depreciation rates and historically permitted Bonus Depreciation⁵ generally resulting in a tax deduction equal to fifty percent of capital expenditure in the year the asset was placed in service. All of the large Tennessee jurisdictional utilities are in a Net Operating Loss (NOL) position, meaning they have not paid Income Taxes in some time. Thus ratepayers have been pre-funding Income Tax Expense that will not be paid for an indefinite period.

The “Unprotected” aspect of ADIT refers to that ADIT whose treatment is not specified within the TCJA. Excess “Unprotected” ADIT is comprised of all other book tax timing differences other than Depreciation.

³ The timing of if and when future payment of taxes may occur is not certain.

⁴ IRC § 168 (i)(9).

⁵ Bonus Depreciation is no longer available under the TCJA; however, it is still relevant due to its historic impact on balances of ADIT, including excess ADIT, the subject of this docket. <https://www.irs.gov/newsroom/new-rules-and-limitations-for-depreciation-and-expensing-under-the-tax-cuts-and-jobs-act>

1 **Q10. WHAT IS THE SIGNIFICANCE OF THE EXCESS ADIT CATEGORIES**
2 **“PROTECTED” VERSUS “UNPROTECTED” ADIT?**

3 **A10.** The language of the TCJA prescribes how the excess “Protected” ADIT may be treated in
4 the ratemaking process.⁶ The TCJA requires that the balance of the “Protected” ADIT
5 must be amortized as a reduction to the revenue requirement using the Average Rate
6 Assumption Method (ARAM). If the utility’s records are insufficient to use the ARAM
7 method, it must rely upon the Reverse South Georgia Method (RSGM).⁷ Both methods
8 result in an amortization of the excess over the life of the assets giving rise to the liability,
9 although the amortization amount will vary year to year with the ARAM methodology,
10 while the annual amortization is constant under the RSGM method.

11 **C. Amortization Methodology Applicable to Excess “Protected” ADIT**

**Q11. WHAT METHODOLOGY IS PIEDMONT PROPOSING TO USE TO
AMORTIZE THIS EXCESS ADIT TO CUSTOMERS?**

12 **A11.** Piedmont proposes using the ARAM to amortize its “Protected” ADIT. The ARAM
13 amortization methodology is required by the TCJA in those situations where sufficient
14 plant accounting data exists to use the methodology.⁸

15 **III. OVERVIEW OF PIEDMONT PROPOSAL**

16 **Q12. PROVIDE AN OVERVIEW OF THE REGULATORY TREATMENT**
17 **PIEDMONT IS PROPOSING RELATIVE TO IMPACT OF THE TCJA.**

18 **A12.** As discussed earlier in my testimony, there are differing components of the TCJA that
19 affect Piedmont. Piedmont’s proposal regarding these components are discussed below:

- 20 1. Reduction in costs associated with Income Tax Expense embedded within
21 Piedmont’s IMR.

⁶ *Tax Cuts and Jobs Act*, Pub. L. No. 115-97 § 1561(d)(1) (2017).

⁷ *Tax Cuts and Jobs Act*, Pub. L. No. 115-97, § 1561 (d)(2)(2017).

⁸ Piedmont Response to Consumer Advocate Discovery Request No. 1-22.

1 Piedmont is charging the 21% federal tax rate within its IMR calculation.⁹ Since the IMR
2 is an annual calculation it is only appropriate that the correct Income Tax rate be applied
3 within the IMR revenue requirement calculation.

4 2. Reduction in costs associated with Income Tax Expense embedded in base rates.

5 Piedmont is deferring the Income Tax Expense savings accruing from January 1, 2018,¹⁰
6 calculated at nearly \$5.6 million annually. Through August 2018 the Company had
7 deferred nearly \$4.9 million associated with this reduction based upon an application of
8 the annual reduction into a specific rate calculation by customer class. Piedmont
9 proposes to continue to collect the \$5.6 million annually from customers at the former
10 35% federal tax rate and defer this excess and refund to customers over an undefined
11 period to begin at the date rates become effective from its next rate case.

12 3. Prepaid taxes (excess ADIT) that were effectively cancelled with the reduction in
13 the federal tax rate.

14 Piedmont proposes to defer the excess ADIT until such time as its next rate case at which
15 point it would then be amortized as an offset to base rates, effectively offsetting an
16 assumed rate increase. Missing from Piedmont's position is any reference to the
17 distinction between "Protected" and "Unprotected" ADIT". "Protected" ADIT will be
18 amortized to the cost of service using the ARAM methodology, while "Unprotected"
19 ADIT may be amortized over a period that is at the sole discretion of the applicable state
20 regulatory body.

⁹ Pia Powers direct testimony p. 6, lines 1-8, TPUC Docket No. 18-00040.

¹⁰ Pia Power direct testimony p. 6, lines 9 – 19, TPUC Docket No. 18-00040.

1 **IV. CONSUMER ADVOCATE UNIT RESPONSE AND RECOMMENDATION**

2 **A. Income Tax Expense**

3 **Q13. BEGIN WITH ADDRESSING THE CONSUMER ADVOCATE’S POSITION**
4 **RELATED TO THE FIRST POINT, THE REDUCTION IN INCOME TAX**
5 **EXPENSE ASSOCIATED WITH THE IMR.**

6 **A13.** I agree with Piedmont’s statement that the Income Tax Expense reduction associated with
7 its IMR surcharge has and continues to be flowed-back to the benefit of ratepayers. The
8 Commission need not take any action concerning this aspect of the Piedmont rate
9 structure.

10 **Q14. CONTINUE BY ADDRESSING THE CONSUMER ADVOCATE POSITION ON**
11 **THE SECOND ISSUE, THE REDUCTION IN INCOME TAX EXPENSE**
12 **EMBEDDED WITHIN BASE RATES.**

13 **A14.** The Consumer Advocate strongly disagrees with the Piedmont proposal to defer (retain)
14 such cost reductions to flow back to ratepayers in a future rate case proceeding. The
15 points supporting a more rapid flowback are discussed below:

16 1. Under the Piedmont proposal, there is no certainty when ratepayers would benefit
17 from a reduction in base rates associated with the significant tax reduction. Piedmont has
18 not determined when it will seek to increase base rates.¹¹ Piedmont has also indicated it
19 has not committed to filing a case within the next two years.¹² Under the Piedmont
20 proposal, ratepayers will continue to incur income tax expense within base rates at the
21 former 35% rate for an indefinite period, which will extend at the complete discretion of
22 Piedmont. Further, Piedmont believes it should be permitted to retain this excess
23 customer funding without the application of any carrying charges.¹³

24 2. Piedmont’s proposal would permit it to retain some of the benefits of the
25 reduction in Income Tax Expense. Piedmont claims that it will flow the full amount of
26 excess Income Tax Expense collections back to ratepayers must be put in context. The

¹¹ Piedmont response to Consumer Advocate Discovery Request No. 1-13, Docket No. 18-00040.

¹² Piedmont response to Consumer Advocate Discovery Request No. 1-12, Docket No. 18-00040.

¹³ Piedmont response to Consumer Advocate Discovery Request No. 1-13, Docket No. 18-00040.

1 value of a dollar at a point in the future is worth less than a dollar today. Piedmont's
2 proposal to retain excess Income Tax Collections paid by ratepayers represents a lost
3 opportunity cost for its ratepayers. Therefore, Piedmont seeks to retain some value of the
4 Income Tax Expense reductions for its own benefit since the nominal amounts of savings
5 will not flow to ratepayers until some undefined future date. In the interim, Piedmont
6 will have the use of the ratepayer overpayment over an undetermined time period at zero
7 cost.

8 3. Piedmont's comments concerning the potential impact on the financial condition
9 of Piedmont must be put in context.¹⁴ It is important to understand that the collection of
10 Income Tax Expense from ratepayers has historically represented a cash flow stream to
11 the Piedmont. Prior to its acquisition by Duke, Piedmont had not paid federal income
12 taxes since late 2011.¹⁵ Further, since the acquisition, Duke has not paid federal income
13 taxes.¹⁶ Duke has a consolidated Net Operating Loss (NOL) balance of \$655 million.¹⁷ It
14 is uncertain when Duke/Piedmont may actually begin to pay federal income taxes in the
15 future. I agree that Piedmont will incur a diminished cash-flow from the TCJA, however
16 the continuation of the normalization requirements within the TCJA continue to be very
17 cash flow positive for utilities. The cash flow resulting from the collection of Income
18 Tax Expense from customers at the 35% rate is now cut to 21% and represents a
19 reduction in cash flow. However, it must be remembered that the collection of an expense
20 at a rate of 21% from ratepayers, coupled with Income Tax Expense payments of zero,
21 continue to represent a very consistent cash flow stream provided by ratepayers.

22 4. Concerns with the financial implication of a more rapid flow-back are overstated
23 as it relates to this TPUC proceeding. Piedmont's results are dominated by its North
24 Carolina operations. The Tennessee portion of total gas plant is only 16.33%, reflective
25 of the overall size of Tennessee's operations relative to total Piedmont Gas operations.¹⁸

¹⁴ Pia Powers, Direct Testimony, p. 8, lines 18-20 TPUC Docket No. 18-00040.

¹⁵ Piedmont response to Consumer Advocate Discovery Request No. 1-3, TPUC Docket No. 18-00040.

¹⁶ Piedmont response to Consumer Advocate Discovery Request No. 1-2, TPUC Docket No. 18-00040.

¹⁷ Piedmont response to Consumer Advocate Discovery Request No. 1-5, TPUC Docket No. 18-00040.

¹⁸ See October Monthly Operating Report filed within Piedmont's overall IMR filing, Docket No. 18-00126.

Therefore, the decisions made by TPUC in this Docket will not be the driving force in the impacts of the TCJA on Piedmont's overall financial status.

5. The North Carolina Utilities Commission (NCUC) ordered that base rates be reduced to reflect the reduction in Income Tax Expense as a result of the TCJA. In Docket No. M-100, Sub 148 (order issued October 5, 2018¹⁹), the NCUC required that rates be reduced prospectively to reflect the reduction in Income Tax Expense from 35% to 21%. It also required jurisdictional utilities, including Piedmont, to continue to defer as a liability the overcollection of Income Tax Expense accruing from January 1, 2018 and to apply interest at the overall weighted cost of capital as identified in the last rate case proceeding. Such balances would continue to accrue interest and the benefit returned to ratepayers at the earlier date of the next base rate case or three years.

Q15. WHAT IS THE CONSUMER ADVOCATE RECOMMENDATION REGARDING THE TREATMENT OF THE REDUCTION IN INCOME TAX EXPENSE?

A15. The Consumer Advocate recommends that the benefits from the Income Tax Expense reduction be flowed back to ratepayers through establishment of a credit rider, similar to the Federal Tax Rate Adjustment Rider proposed by Kingsport Power in Docket No. 18-00038 and included in the unanimous Settlement Agreement (at this time) currently pending before the Commission. The attributes of the Federal Tax Rate Adjustment Rider (FTAR) should contain the following:

- The annualized level of Income Tax Expense savings is \$5,581,438 as referenced in Ms. Powers testimony.²⁰
- The current regulatory liability balance reflecting Income Tax Expense savings accruing from January 1, 2018 to date should be added to the annualized Income Tax Expense savings to be flowed back to ratepayers. That balance as of August 31, 2018 was nearly \$4.9 million.²¹ This amount should be updated through the most recent data available.

¹⁹ A copy of this order can be found at this link to the NCUC website <https://starw1.ncuc.net/NCUC/ViewFile.aspx?id=5cadbd2d-1876-43c7-a616-fe3b720663d3>.

²⁰ Pia Powers Direct Testimony, page 3, lines 3-4. Also, see Exhibit PKP-1.

²¹ Pia Powers, Direct Testimony, page 2, line 16, Docket 18-00040.

- 1 • The “Unprotected” excess ADIT should be amortized over a three-year period in
2 the amount of \$6,023,720 (as discussed later in my testimony).
- 3 • The amount of excess “Unprotected” ADIT (positive or negative) using the
4 Tennessee specific tax rate should be determined and amortized over three-year
5 period along with the approximate \$6 million in excess “Unprotected” ADIT
6 mentioned above. This issue will be discussed later in my testimony.
- 7 • The methodology described in Ms. Powers’ testimony²² computing a rate per-
8 therm should be used to determine the appropriate FTAR credit per rate class,
9 reflective of both the accrued and annualized Income Tax Expense savings
10 components.
- 11 • The credit per-therm should be reflected on customers’ bills as a separate line
12 item identified as a “Reduction in Income Tax Expense – TCJA”
- 13 • The FTAR credit shall apply to all customer classes other than Special Contract
14 customer classes.
- 15 • The filing should be made annually by March 1, and rates should be adjusted for
16 over/under collected amounts. The FTAR should reflect the changes in the
17 annual target collections incorporating a one-year flow-back of the regulatory
18 liability and three-year amortization of excess “Unprotected” ADIT.
- 19 • The FTAR should be effective until such time as new base rates are implemented
20 which fully incorporate the 21% federal tax rate.

21 **Q16. WHAT ARE THE BENEFITS OF ESTABLISHING A CREDIT RIDER RATHER**
22 **THAN SIMPLY REDUCING BASE RATES?**

23 A16. Bill transparency is important and is a general public policy that should be afforded great
24 weight by TPUC. To that end, I recommend that the credit rider be clearly identified on
25 customers’ bills as an Income Tax Expense credit resulting from the TCJA.

²² Pia Powers, Direct Testimony, Exhibit PKP-2, Docket 18-00040.

1 **Q17. HAVE YOU CALCULATED THE ESTIMATED IMPACTS OF YOUR**
2 **PROPOSAL TO ESTIMATED RATEPAYER IMPACTS BY CLASS?**

3 **A17.** Yes. However, it is important to understand that the accrued Income Tax Expense
4 savings (stated at \$4.88 million as of August 31, 2018) will be greater than what is
5 contained in the estimate. Further, the impact associated with synchronizing the
6 determination of excess ADIT by incorporating the specific Tennessee state tax rate has
7 not been quantified. With those two caveats, the estimated first-year impact for the
8 average residential customer under the Consumer Advocate proposal would result in an
9 annual bill reduction of \$63.11 as set forth in Exhibit DND-2. The estimated annual
10 impacts for the Small/Medium Commercial and Large Firm and Interruptible customer
11 classes are also identified. As discussed above these annual impacts would decline as the
12 deferred 2018 tax savings are recovered.

13 **Q18. DO YOU HAVE AN ALTERNATIVE RECOMMENDATION IN THE EVENT**
14 **THE COMMISSION PERMITS PIEDMONT TO DELAY REFUNDS**
15 **ASSOCIATED WITH DEFERRED INCOME TAX EXPENSE SAVINGS**
16 **ACCRUING SINCE JANUARY 1, 2018?**

17 **A18.** Yes. If the Commission permits Piedmont to defer the return of the accrued to-date
18 Income Tax Expense savings, I recommend that the Company's Rate of Return of
19 9.878%, calculated monthly, be applied to the monthly balances accruing from January 1,
20 2018. This carrying rate ensures ratepayers are compensated for their financing of
21 Piedmont's operations. This is the same regulatory treatment that is applied to other
22 customer supplied capital such as ADIT. In other words, ADIT is an offset to Rate Base
23 effectively providing ratepayers an avoided cost savings equal to the utilities Rate of
24 Return multiplied by the balance of ADIT. In this instance, customers are funding utility
25 operations just as is the case with ADIT. Therefore, consumers should receive
26 compensation for Piedmont's use of their funds.

B. Excess ADIT

Q19. SHOULD THE REGULATORY CONSIDERATION OF EXCESS ADIT BE SPLIT BETWEEN ITS TWO COMPONENT PARTS, “PROTECTED” AND “UNPROTECTED”?

A19. Yes. The consideration of ADIT must be split between its two components, “Protected” and “Unprotected”. Piedmont proposes to delay amortization of both components until their next rate case. I agree with Piedmont with respect to its proposal to defer amortization of its “Protected” ADIT balance; however, I disagree with the Company’s proposal to retain excess “Unprotected” ADIT until its next rate case is completed, whenever that may be.

Q20. WHAT IS THE SPLIT OF EXCESS ADIT BETWEEN “PROTECTED” AND “UNPROTECTED”?

A20. The amounts of “Protected” and “Unprotected” ADIT are shown below.

Table DND-1	Amount	Source
Protected ADIT	\$ 50,817,283	Conf 1-16 Attachment
Unprotected ADIT	\$ 13,782,965	
Total Excess ADIT	\$ 64,600,248	Exhibit 3 attached to initial response

It should be noted that when amortizing these amounts for refunds to customers, they need to be grossed-up for taxes,²³ to properly reflect that such refunds will be tax deductible. The pre-tax excess “Unprotected” ADIT is nearly \$18.1 million.

Q21. HAS THE COMMISSION RECENTLY ADDRESSED THE APPROPRIATE REGULATORY TREATMENT OF EXCESS ADIT INVOLVING PIEDMONT?

A21. Yes. In TPUC Docket No. 14-00017 Piedmont petitioned the Commission for approval to flow back excess ADIT it had quantified during an analysis of its ADIT balance.²⁴ The base amount of excess ADIT identified by Piedmont at that time was \$2.8 million, while

²³ See notes to Exhibit 3 of original Petition.

²⁴ See page 3, paragraph 9 of Petition filed February 20, 2014.

on a revenue requirement basis (grossed-up for taxes) the amount was nearly \$4.7 million. Piedmont proposed to flow the excess it had identified back to its customers through a reduction in base rates.

Q22. WHAT AMORTIZATION PERIOD DID PIEDMONT PROPOSE OVER WHICH TO SPREAD THIS RATE DECREASE?

A22. Piedmont proposed to amortize excess ADIT over a three-year period.

Q23. WHAT AMORTIZATION PERIOD OF FLOW-BACK WAS ADOPTED BY TPUC?

A23. The Commission approved a Settlement Agreement (SA) in Docket No. 14-00017 calling for a one-year flow-back of this excess ADIT. However, the Order adopting the SA was clear that those terms should not establish a binding precedent before the Commission, or any court.

Q24. WHAT AMORTIZATION PERIOD ARE YOU PROPOSING TO FLOW BACK EXCESS ADIT?

A24. I am proposing to flowback excess “Unprotected” ADIT over a three-year period, resulting in an annual amortization for revenue requirement purposes of \$6,023,720 as set for on Exhibit DND-3.

Q25. WHAT IS THE BASIS FOR THE THREE-YEAR AMORTIZATION RECOMMENDATION?

A25. First, as a matter of public policy, ratepayer funds should be returned to customers as quickly as reasonably possible. Certain ratepayers are undoubtedly under personal financial constraints and would benefit from the return of their funds sooner, rather than later. Secondly, ratepayers deserve some certainty on when their funds will be returned. The Piedmont proposal fails to define when the amortization of excess “Unprotected” ADIT would begin as well as the number of years over which the balances would then be amortized. Further, a more rapid return to ratepayers provides a better matching of the refund with those customers providing the source of the excess ADIT funding.

1 Importantly, the three-year amortization period proposed by the Consumer Advocate is
2 identical to the period proposed by Piedmont in Docket No. 14-00017 to refunds its
3 excess ADIT.

4 **Q26. HOW DOES THE THREE-YEAR AMORTIZATION PERIOD COMPARE WITH**
5 **THAT RECOMMENDED BY OTHER UTILITIES AND THE CONSUMER**
6 **ADVOCATE IN DOCKETS PENDING BEFORE TPUC?**

7 **A26.** In Docket No. 18-00017, Chattanooga Gas Company proposed a five-year amortization of
8 its excess “Unprotected” ADIT.²⁵ The Consumer Advocate proposed a three-year
9 amortization. TPUC issued a written order on January 11, 2019 authorizing a five-year
10 amortization of excess “Unprotected” ADIT.

11 In Docket No. 18-00038, Kingsport Power and the Consumer Advocate have entered into
12 a Settlement Agreement whereby the “Unprotected” excess ADIT would be flowed back
13 to ratepayers, through the elimination of deferred storm damage costs and the reduction of
14 its unrecovered fuel cost balance.²⁶ The elimination of the deferred storm damage
15 regulatory asset and the reduction in fuel cost balances translates to an immediate benefit
16 for Kingsport customers. The Settlement Agreement is pending TPUC approval as of the
17 filing of this testimony.

18 In Docket No. 18-00039 Tennessee American Water Company (TAWC) has indicated that
19 once it determines its balance of excess ADIT it will propose an appropriate amortization
20 period.²⁷ Presumably this would include the portion of excess ADIT that is “Protected”.
21 TAWC has indicated it believes the amortization of excess ADIT should be used to offset
22 charges under its capital rider program.²⁸

23 With respect to Atmos, Docket No. 18-00034, there is a disagreement between the parties
24 on the definition of “Unprotected” ADIT, and whether there exists an “Unprotected”
25 ADIT asset or liability. The Consumer Advocate has proposed a three-year amortization
26 of the “Unprotected” ADIT Liability, while Atmos proposes to collect what it defines as

²⁵ Gary A. Tucker Rebuttal Testimony, p. 38, lines 12-17, TPUC Docket No. 18-00017, (Aug. 3, 2018).

²⁶ Stipulation and Settlement Agreement, pp. 9-10, ¶ 20, TPUC Docket No. 18-00038 (Dec. 7, 2018).

²⁷ John. R. Wilde Direct Testimony, p. 7, line 18 – p. 8, line 7, TPUC Docket No. 18-00039 (Apr. 2, 2018).

²⁸ Linda C. Bridwell Direct Testimony, p. 8, lines 14-18 TPUC, Docket No. 18-00039 (Apr. 2, 2018).

1 “Unprotected” ADIT assets over a twenty-nine-year period, the same period used to
2 amortize its excess “Protected” ADIT.

3 **V. PIEDMONT’S DEFERRED TAX LIABILITY BALANCE, INCLUDING**
4 **DETERMINATION OF EXCESS ADIT**

5 **Q27. NOW TURN TO THE FINAL SECTION OF YOUR TESTIMONY. DISCUSS**
6 **YOUR CONCERN WITH RESPECT TO PIEDMONT’S IDENTIFICATION OF**
7 **ITS TENNESSEE ADIT BALANCE.**

8 **A27.** In the course of the Consumer Advocate review it became apparent that Piedmont’s
9 ADIT balances, including the calculation of its excess ADIT balances (both “Protected”
10 and “Unprotected”) were based upon the use of a composite state tax rate. However, in
11 the last base rate case, Docket No. 11-00144 the Commission ordered that the Tennessee
12 specific income tax rate of 6.5% be used in the determination of Income Tax Expense.

13 **Q28. EXPLAIN WHAT THE COMPOSITE STATE TAX RATE IS AND HOW IT IS**
14 **USED.**

15 **A28.** The composite state tax rate of 3.455% is a weighted average state tax rate across the
16 Piedmont system.²⁹ The composite rate is applied to the book/tax timing differences in
17 arriving at Piedmonts’ ADIT balances, a significant offset to Rate Base. The
18 inconsistent use of a state tax rate of 6.5% in the computation of Income Tax Expense
19 with the use of the 3.455% state tax rate poses an obvious inconsistency in the
20 development of the Piedmont ADIT balance and the associated determination of excess
21 ADIT.

22 **Q29. WHAT IS THE RELATIONSHIP BETWEEN THE INCOME TAX EXPENSE**
23 **CALCULATION AND THE BALANCE OF ADIT?**

24 **A29.** The two accounts are related. As I discussed earlier in my testimony, the ADIT balance
25 represents the account that reconciles Income Tax Expense recorded pursuant to
26 Generally Accepted Accounting Principles (GAAP) and income taxes paid to state and

²⁹ Piedmont response to Consumer Advocate Discovery Request 2-6, TPUC Docket No. 18-00040.

1 federal taxing authorities. The ADIT account is a credit balance, which indicates that
2 on a cumulative basis Income Tax Expense (according to GAAP) has exceeded income
3 taxes paid to taxing authorities.

4 **Q30. WHAT IS THE PRACTICAL EFFECT OF USING ONE RATE TO COMPUTE**
5 **INCOME TAX EXPENSE AND ANOTHER RATE TO DETERMINE THE**
6 **APPROPRIATE AMOUNT OF ADIT THAT IS A RATE BASE OFFSET?**

7 **A30.** The practical result of this inconsistent treatment is either 1) an Income Tax Expense
8 that is excessive, or 2) an understated ADIT balance that results in an overstated rate
9 base for ratemaking purposes.³⁰ From either perspective the revenue requirement is
10 overstated due to this inconsistency. There are arguments for using a Tennessee specific
11 state tax rate within the revenue requirement or a composite state tax rate, but I do not
12 believe there is any rational argument for using one state tax rate within the expense
13 calculation and another state tax rate within the Tennessee specific ADIT calculation.
14 In summary, Piedmont-Tennessee ratepayers are paying a state income tax component
15 of 6.5%, but only receiving credit for a composite rate of 3.455%.

16 **Q31. WOULD THE CORPORATE BOOKS OF PIEDMONT INCLUDE THE USE OF**
17 **A COMPOSITE RATE IN THE DETERMINATION OF INCOME TAX**
18 **EXPENSE AND ADIT?**

19 **A31.** Yes. However, that does not then require the use of a composite rate in the
20 determination of the regulatory ADIT balance used for Tennessee ratemaking purposes.
21 The Commission has adopted the use of a Tennessee specific state tax rate in Docket
22 No. 11-00144. The same state tax rate used to compute Income Tax Expense should be
23 used in the calculation of the related account, ADIT. The modification of the
24 Company's ADIT balance would naturally impact the resulting amounts of excess
25 ADIT, including both "Protected" and "Unprotected". This recommendation should not

³⁰ In response to Consumer Advocate Discovery Request 2-6, Piedmont indicates that the use of a composite rate in the determination of ADIT balances is consistent with GAAP. The CA does not dispute this claim. However, it would also be true that the use of a composite tax rate to determine Income Tax Expense is consistent with GAAP. Basic ratemaking principles require the appropriate synchronization of the use of a tax rate between the computation of Income Tax Expense and ADIT balances.

1 have any impact on the corporate recording of ADIT, but instead be limited to the
2 determination of ADIT for ratemaking purposes.

3 **Q32. DO YOU HAVE SUFFICIENT INFORMATION TO DETERMINE THE**
4 **APPROPRIATE ADJUSTMENT TO THE EXCESS ADIT?**

5 A32. No.

6 **Q33. WHAT IS YOUR RECOMMENDATION IN THIS REGARD?**

7 A33. My recommendation is two-fold. First, with respect to this Docket, the Commission
8 should require Piedmont to recalculate its Tennessee excess "Protected" and
9 "Unprotected" ADIT balances by applying the Tennessee-specific state tax rate within
10 the ADIT calculation used for ratemaking purposes. The revised "Unprotected" ADIT
11 balance should be incorporated into the Commission's ultimate determination of the
12 treatment of "Unprotected" ADIT.

13 Secondly, the Commission should order in this Docket that for future ratemaking
14 determinations, the Tennessee ADIT balance used for ratemaking purposes should be
15 based upon the use of the Tennessee-specific state tax rate, rather than the composite
16 state tax rate. This will ensure consistency within the revenue requirement calculation
17 and confirm that ratepayers are accurately compensated for the correct amount of cost-
18 free funds they provide to the utility.

19 **Q34. DOES THIS CONCLUDE YOUR TESTIMONY?**

20 A34. Yes.

David Dittmore

Experience

Areas of Specialization

Approximately thirty-year experience in evaluating and preparing regulatory analysis, including revenue requirements, mergers and acquisitions, utility accounting and finance issues and public policy aspects of utility regulation. Presented testimony on behalf of my employers and clients in natural gas, electric, telecommunication and transportation matters covering a variety of issues.

Tennessee Attorney General's Office; **Financial Analyst September, 2017 – Current**
Responsible for evaluation of utility proposals on behalf of the Attorney General's office including water, wastewater and natural gas utility filings. Prepare analysis and expert witness testimony documenting findings and recommendations.

Kansas Gas Service; **Director Regulatory Affairs 2014 – 2017; Manager Regulatory Affairs, 2007 – 2014**

Responsible for directing the regulatory activity of Kansas Gas Service (KGS), a division of ONE Gas, serving approximately 625,000 customers throughout central and eastern Kansas. In this capacity I have formulated strategic regulatory objectives for KGS, formulated strategic legislative options for KGS and led a Kansas inter-utility task force to discuss those options, participated in ONE Gas financial planning meetings, hired and trained new employees and provided recommendations on operational procedures designed to reduce regulatory risk. Responsible for the overall management and processing of base rate cases (2012 and 2016). I also played an active role, including leading negotiations on behalf of ONE Gas in its Separation application from its former parent, ONEOK, before the Kansas Corporation Commission. I have monitored regulatory earnings, and continually determine potential ratemaking outcomes in the event of a rate case filing. I ensure that all required regulatory filings, including surcharges are submitted on a timely and accurate basis. I also am responsible for monitoring all electric utility rate filings to evaluate competitive impacts from rate design proposals.

Strategic Regulatory Solutions; 2003 -2007

Principal; Serving clients regarding revenue requirement and regulatory policy issues in the natural gas, electric and telecommunication sectors

Williams Energy Marketing and Trading; 2000-2003

Manager Regulatory Affairs; Monitored and researched a variety of state and federal electric regulatory issues. Participated in due diligence efforts in targeting investor owned electric utilities for full requirement power contracts. Researched key state and federal rules to identify potential advantages/disadvantages of entering a given market.

MCI WorldCom; 1999 – 2000

Manager, Wholesale Billing Resolution; Manage a group of professionals responsible for resolving Wholesale Billing Disputes greater than \$50K. During my tenure, completed disputes increased by over 100%, rising to \$150M per year.

Kansas Corporation Commission; 1984- 1999

Office of the Tennessee Attorney General
Consumer Advocate Unit, Financial Division

Exhibit DND-2

Docket No. 18-00040

Regarding the Impact of Federal Tax Regorm on Piedmont's Revenue Requirement
Spread of Savings using Integrity Management Rider Rate Design

1	Annualized Income Tax Expense Savings	\$ (5,581,438)
2	Account for Income Tax Expense Savings	(4,877,400)
3	Income Taxes	(6,023,720)
4	Total 1st year savings estimate	\$ (16,482,558)

Customer Class	Residential (301)	Small/Medium General (302,352)	Large General - Firm (303,313,310)	Large General - Interruptible (304,314)	Total
5 Customer Class					
6 Customer Class Apportionment Percent	59.64%	31.20%	4.95%	4.21%	100.00%
7 Total Amount for Recovery	\$ (9,830,844)	\$ (5,142,658)	\$ (815,283)	\$ (693,774)	\$ (16,482,558)
8 Throughput from Relevant Rate Case Order (Dekatherms)	11,130,214	6,664,958	2,378,880	8,098,027	28,272,079
9 Throughput from Relevant Rate Case Order (Therms)	111,302,140	66,649,580	23,788,800	80,980,270	282,720,790
10 Rate per Dekatherm	\$ (0.88330)	\$ (0.77160)	\$ (0.34270)	\$ (0.08570)	\$ (0.58300)
11 Rate per Therm /1	\$ (0.08833)	\$ (0.07716)	\$ (0.03427)	\$ (0.00857)	\$ (0.05830)
12 Number Billed at 12 months ending January 2014	155,785	17,329	235	2	173,351
13 Average residential customer use (Therms)	714	3,846	101,229	40,490,135	
14 Yearly Impact on Residential Customer's Bill	\$ (63.11)	\$ (296.77)	\$ (3,469.12)	\$ (347,000.46)	
15 Monthly Impact on Residential Customer's Bill	\$ (5.26)	\$ (24.73)	\$ (289.09)	\$ (28,916.70)	

Office of the Tennessee Attorney General
Consumer Advocate Unit, Financial Division
Docket No. 18-00040

Exhibit DND-3

Item	Amount	Source
1 Unprotected Excess ADIT	\$ 13,782,965	Table DND-1
2 Composite Tax Factor	23.7295%	CAU Response 2-6
3 Divided By: Reciprocal Tax Rate	<u>0.762705</u>	
4 Pre-Tax Excess ADIT	\$ 18,071,161	
5 Amortization Period	<u>3</u>	
6 Annual Amortization	<u>\$ 6,023,720</u>	