

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

NORTH SHORE GAS COMPANY	:	
	:	No. 11-0280
Proposed general increase in rates for gas service.	:	
	:	(cons.)
THE PEOPLES GAS LIGHT AND COKE COMPANY	:	
	:	No. 11-0281
Proposed general increase in rates for gas service.	:	

Surrebuttal Testimony of

JOHN P. STABILE
Tax Director
Integrays Business Support, LLC

On Behalf of
North Shore Gas Company and
The Peoples Gas Light and Coke Company

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1 **I. INTRODUCTION**

2 **A. Identification of Witness**

3 Q. Please state your name.

4 A. My name is John P. Stabile.

5 Q. Are you the same John P. Stabile who submitted direct and rebuttal testimony on behalf
6 of each of North Shore Gas Company (“North Shore”) and The Peoples Gas Light and
7 Coke Company (“Peoples Gas”) (together, the “Utilities”) in these consolidated Dockets?

8 A. Yes.

9 Q. On whose behalf are you offering this surrebuttal testimony?

10 A. I am offering this rebuttal testimony on behalf of North Shore and Peoples Gas.

11 **B. Purpose of Surrebuttal Testimony**

12 Q. What is the purpose of your surrebuttal testimony?

13 A. I am addressing the rebuttal testimony of Governmental and Consumer Intervenors¹
14 (“GCI”) witnesses Mr. David Efron (GCI Ex. 7.0) and Mr. Lafayette K. Morgan (GCI
15 Ex. 6.0) related to the risks associated with the tax accounting method changes elected by
16 the Utilities. I also respond to Mr. Efron’s rebuttal testimony regarding the inclusion of
17 accumulated deferred income taxes (“ADIT”) in Rider ICR.

18 **C. Summary of Conclusions**

19 Q. Please summarize the conclusions of your surrebuttal testimony.

¹ Governmental and Consumer Intervenors are comprised of the Illinois Attorney General, the Citizens Utility Board and the City of Chicago.

20 A. In brief, I conclude that there is substantial risk related to the Utilities' election of both
21 the change in method of accounting related to the determination of unit of property used
22 for repairs and retirements ("Repairs Change") and a non-automatic change to the
23 capitalization of certain indirect and overhead costs ("Overhead Change"). I also
24 conclude that including ADIT in Rider ICR creates more risk for customers than the
25 benefits that they would receive.

26 **D. Itemized Attachments to Surrebuttal Testimony**

27 Q. Please describe the attachments to your surrebuttal testimony.

28 A. Yes. Attached as NS-PGL Ex. 44.1 is Private Letter Ruling 9202029.

29 **II. RISKS RELATED TO TAX ACCOUNTING METHOD CHANGES**

30 Q. In his rebuttal testimony, Mr. Morgan states "It is misleading to imply that I testified that
31 there are no risks related to the tax accounting change because I make no such statement.
32 To be clear, in my direct testimony, I state the Companies' risks are 'diminished' not
33 eliminated." GCI Ex. 6.0 at 4. How do you respond?

34 A. Mr. Morgan provides no support for his statement that risks are diminished and does not
35 provide an assessment of the diminished risks. For all the reasons that I stated in my
36 rebuttal testimony (NS-PGL Ex. 26.0, 5:100- 15:374), Mr. Morgan's assertions must be
37 rejected.

38 Q. Mr. Effron states that, with respect to the Overhead Change, he does not believe that the
39 Utilities have shown the risks are significant enough to support the Utilities' proposed
40 adjustment to include 50% of the related benefit in rate base. Do you agree?

41 A. I do not. As I indicated in my rebuttal testimony (NS-PGL Ex. 26.0, 10:231-16:374), the
42 Overhead Change is still an Internal Revenue Service Tier I issue, which includes some
43 of the riskiest positions.

44 **III. ACCUMULATED DEFERRED INCOME TAXES AND RIDER ICR**

45 Q. In disagreeing with your position that normalization rules may be violated if ADIT were
46 included in Rider ICR, Mr. Efron states: “If the ADIT are calculated appropriately, there
47 is no more risk of violation of the normalization rules from recognition of ADIT in the
48 computation of Rider ICR than there is from deducting ADIT from plant in service in the
49 context of a base rate case. ADIT are recognized in the determination of base rates, and
50 they should be recognized in the computation of Rider ICR.” (GCI Ex. 7.0, 7:138-142)
51 Do you agree?

52 A. No, I do not. Mr. Efron does agree that normalization would apply, and in general he
53 seems to agree that care and caution should apply. He acknowledges that if a Net
54 Operating Loss (“NOL”) exists in the period that Rider ICR needs to be calculated to
55 include the NOL. He also agrees that there can be no overlap of ADIT in multiple
56 recovery proceedings. However he disagrees that the proration formula applies and he
57 still maintains that the taxes should be included in the computation. Failure to ensure that
58 there is no overlap of all these moving pieces would result in the Utilities losing their
59 ability to claim accelerated depreciation.

60 Q. Would the denial of accelerated depreciation only apply to the property in the scope of
61 Rider ICR?

62 A. No. All public utility property would no longer qualify. Essentially not only would the
63 benefit Mr. Efron is trying to include in Rider ICR become non-existent, all the benefits

64 related to all of the utility property would not be available to the Utilities and their
65 customers.

66 Q. Does Mr. Efron agree that if his proposal is accepted, the Illinois Commerce
67 Commission (“Commission”) should make it clear that no adjustment can be made in a
68 reconciliation process if the Utilities believe that there would be a resulting violation of
69 the normalization rules until the Utilities could obtain a private letter ruling?

70 A. No. This is a significant issue. The Utilities need this assurance because loss of
71 accelerated depreciation is devastating, both to the Utilities and to their customers. This
72 is evident by Mr. Efron’s very proposal. In his rebuttal testimony, Mr Efron states

73 To the extent that Rider ICR incorporates forecasts of future plant additions, the
74 proration requirements cited by Mr. Stabile would also arguably be applicable.
75 However, the reconciliation of the actual QIP to the forecasted QIP is based on
76 actual plant and actual accumulated depreciation. To comply with the consistency
77 requirements, the balance of ADIT in the annual reconciliation should also be the
78 actual balance of applicable ADIT, with no proration.

79 (GCI Ex. 7.0, 6:129-134) His proposal would result in a violation. If Mr. Efron’s
80 proposal were adopted, no accelerated depreciation would be available to the Utilities.

81 Q. Why is the exclusion of the proration in the Rider ICR computation a violation of the
82 normalization rules?

83 A. In the late 1980’s and early 1990’s, Commission Staff decided to challenge the proration
84 computation contained in the Treasury regulations regarding the normalization rules. In
85 doing so, Staff proposed various adjustments to the proration formula computed by the
86 Utilities in several rate cases affecting possibly four Illinois utilities, including Peoples
87 Gas and North Shore. In all cases, the utilities sought Private Letter Rulings (“PLR”) to
88 protect themselves and customers from any violation of the normalization rules. Both

89 Peoples Gas and North Shore sought and received PLRs. Ruling 9202029 issued to
90 North Shore states

91 Critical to the interpretation of [Treasury Regulation] section 1.167(l)-1(h)(6)(ii)
92 of the regulations is the meaning of the terms “historical” and “future” in relation
93 to the period for determining depreciation for ratemaking tax expense (this test
94 period might not be coextensive with the taxpayer's test year; see, e.g., section
95 1.157(l)- 1(h)(6)(iv) Example (2)). The meaning of these terms does not depend
96 on the type or quality of the data used in the ratemaking process -- whether the
97 data used is actual or estimated -- but on when the utility's rates become effective.
98 The historical period is that portion of the test period before rates go into effect,
99 while the portion of the test period after the effective date of the rate order is the
100 future period.

101 NS-PGL Ex. 44.1, Private Letter Ruling 9202029, p. 6 (emphasis added). Thus, Mr.
102 Effron’s assertion that the use of actual data eliminates the need for the proration formula
103 is a violation of the normalization rules.

104 Q. Mr. Effron also raises the consistency requirement. How do you respond?

105 A. In the very same PLR issued to North Shore, the question was raised regarding the fact
106 that only a portion of the year was being prorated. North Shore was concerned that this
107 violated the consistency requirement and proposed an argument very similar to Mr.
108 Effron. The Internal Revenue Service rejected the argument stating:

109 Though the [Treasury] regulations under section 167 of the [Internal Revenue]
110 Code were promulgated before the enactment of the consistency provisions of
111 section 168(i)(9)(B), they give a good indication that the **proration** formula does
112 not run afoul of the consistency requirement, or more accurately in this situation,
113 the requirement of consistent periods. Section 1.167(l)-1(h)(6)(i) of the
114 regulations provides for consistent periods in determining the amount of the rate
115 base exclusion, followed by section 1.167(l)-1(h)(6)(ii), which provides for the
116 **proration** of deferred tax accruals attributable to any future portion of the test
117 period. Clearly, in regards to determining the maximum amount of deferred taxes
118 excludable from rate base, consistency and timing are two separate, though
119 related, issues.

120 NS-PGL Ex. 44.1, Private Letter Ruling 9202029, p. 8 (emphasis added)

121 Q. Do you still maintain that the risks of a normalization violation to the Utilities and their
122 customers far outweigh the benefits the Utilities and their customers may receive under
123 Mr. Effron's proposal?

124 A. Yes, I do. I also note that Staff witness Mr. Daniel Kahle agrees that ADIT should not be
125 included in the Rider ICR calculation. *See* Staff Ex. 10.0, 22:473-23:502.

126 Q. Does this complete your surrebuttal testimony?

127 A. Yes.