

**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION**

**IN RE: INTERSTATE NAVIGATION COMPANY :
EARNINGS REPORTS : DOCKET NO. 4373**

**IN RE: REVIEW OF INTERSTATE NAVIGATION :
COMPANY'S REVENUE REQUIREMENT UNDER :
R.I. GEN. LAWS § 39-3-11 IN LIGHT OF THE TAX : DOCKET NO. 4792
CUTS AND JOBS ACT :**

ORDER

On April 29, 2013, the Public Utilities Commission (Commission or PUC) approved Interstate Navigation Company's (Interstate) revenue requirement and associated rates for effect May 24, 2013.¹ As part of the PUC Order, Interstate was allowed a Return on Equity of 11%, but with an Earnings Sharing Mechanism that begins at 12%. Interstate is required to file annual earnings reports that are based on a methodology agreed to by the parties and approved by the PUC.² Specifically, the PUC approved the following: "Earnings in excess of 12% will be shared 50% for the stockholders and 50% for the ratepayers. Prior to proposing a method of crediting earnings above the [12]% threshold applicable to the ratepayers, Interstate will consult with the Division [of Public Utilities and Carriers (Division)] to propose a mutually acceptable method. The agreed upon method will then be filed with the Commission for review and approval."³

Interstate filed earnings reports for Fiscal Years 2014, 2015, 2016, and 2017, with the two most recent filed in December 2017 and March 2018, respectively. The Division disputed Interstate's methodology and proposed modifications which Interstate accepted. The Division had proposed allowing the excess earnings to accrue with disposition of the funds determined at a

¹ Order No. 21069 (Docket No. 4373), In re: Interstate Navigation Company – General Rate Filing – Traditional Service Rates (June 30, 2013); [http://www.ripuc.org/eventsactions/docket/4373-Interstate-Ord21069\(6-20-13\).pdf](http://www.ripuc.org/eventsactions/docket/4373-Interstate-Ord21069(6-20-13).pdf).

² *Id.* at App. A, Section III (Docket No. 4373, Settlement Agreement).

³ *Id.*

future date. Accordingly, Interstate maintained a record of excess earnings. As of May 31, 2017, Interstate's accumulated excess earnings to be used for the benefit of ratepayers was \$1,819,701.⁴

On December 22, 2017, the federal Tax Cuts and Jobs Act of 2017 was signed into law. One significant modification was to reduce the corporate income tax rate from 35% to 21% effective January 1, 2018. Like other investor-owned utilities in Rhode Island and across the country, Interstate's current rates were calculated based on the 35% tax rate. The tax change prompted the PUC and other public utilities commissions across the country to open dockets to investigate whether and how the new lower corporate tax rate should be reflected in the utility revenue requirements and rates for calendar year 2018 and beyond.

Interstate was the subject of one such investigation. In response to PUC discovery requests in the investigation, Interstate calculated the tax savings on its approved revenue requirement relating solely to the reduction in the corporate tax rate to be \$42,880.⁵ This reduction would result in a 0.45% decrease in rates or five cents on a one-way adult ticket.⁶ Interstate proposed that, rather than reducing ticket prices, it might be appropriate to deposit the "savings" into a new capital reserve account that would be used to offset the cost of future capital projects.⁷

On July 9, 2018, Interstate filed a Settlement Agreement between itself and the Division resolving both matters. The parties agreed on a method for crediting to ratepayers, earnings above the 12% threshold for the period FY 2014 through FY 2017, plus any future excess earnings. The parties also agreed on a method for crediting ratepayers with the tax savings from the reduction to the corporate tax rate.⁸ The Settlement Agreement provided for the creation of a new capital

⁴ Interstate's FY 2017 Earnings Report at DGB-ROE-3; <http://www.ripuc.org/eventsactions/docket/4373-Interstate-EarningsRept-FYE5-31-2017.pdf>.

⁵ Interstate's Response to PUC-1-1; [http://www.ripuc.org/eventsactions/docket/4792-InterstateNav-DR-PUC1-TaxChanges\(2-16-18\).pdf](http://www.ripuc.org/eventsactions/docket/4792-InterstateNav-DR-PUC1-TaxChanges(2-16-18).pdf).

⁶ Interstate's Response to PUC-1-2.

⁷ Interstate's Response to PUC-1-4.

⁸ Settlement Agreement; [http://www.ripuc.org/eventsactions/docket/4373-Interstate-ROE-Settlement\(8-2-18\).pdf](http://www.ripuc.org/eventsactions/docket/4373-Interstate-ROE-Settlement(8-2-18).pdf).

reserve account to be used by Interstate for capital projects including fixed asset purchases such as new vessels and/or overhauls of vessels, buildings, ramps, docks, pilings, etc. The initial funding will be \$1,519,701 and the account will accrue interest at the Washington Trust Company money market rate. The following conditions will apply: (1) ratepayers will be credited when Interstate excludes the depreciation on the appropriate portion of any asset paid for from the capital reserve account funds; (2) if only a portion of the asset was paid for from the capital reserve account funds, the depreciation will be prorated; (3) any portion of the assets purchased from the capital reserve account funds will be excluded from rate base; and (4) because there will be no book depreciation on assets purchased from the capital reserve account, to account for tax depreciation, a credit will be added at the end of each fiscal year to the capital reserve account to capture the benefit for ratepayers. The credit will reflect the tax savings from the tax depreciation at the 21% corporate tax rate and will be added to the ratepayer's portion of the earnings in excess of 12% on each year's Return on Equity report.⁹

The remaining \$300,000 of the total \$1,819,701 accrued excess earnings will be deposited into the existing fuel reserve account, grossed up for a flat tax of 21%. This account will also accrue interest at the Washington Trust Company money market rate commencing June 2017 (the start of FY 2018). The fuel reserve account will be reviewed annually by Interstate and the Division to determine whether any additional future excess earnings should be deposited into the fuel reserve account.¹⁰

Commencing with Interstate's FY 2018 earnings report, Interstate will annually credit \$42,880 to customers. It shall continue to do so as long as the corporate tax rate remains at 21% or until Interstate's revenue requirement and rates are changed through a general rate case. The

⁹ Settlement Agreement at 2-3.

¹⁰ *Id.* at 3.

FY 2018 earnings report will be prorated to conform with the effective date of the 2017 Tax Reform Act.¹¹ Interstate has previously calculated the amount for savings for FY 2018 at \$17,867.50 based on the period January 1, 2018 through May 31, 2018.¹²

The PUC has previously held that the appropriate carrying charge on deferral accounts depends on the purpose of the fund. Accounts set up for capital needs, for example, typically earn at the utility's weighted average cost of capital while operating accounts typically accrue at a short-term debt or interest rate. In a joint response to a PUC data request, Interstate and the Division contended that although the funds in the capital account will be subject to a short-term carrying charge, because the assets paid for by funds within the capital reserve account will be excluded from rate base, customers will be effectively receiving the benefit at the weighted average cost of capital.¹³

At an Open Meeting held on August 9, 2018, the PUC considered the merits of the Settlement Agreement based on the filings in the docket and found that the terms were just and reasonable and provided an appropriate balance between Interstate and its ratepayers. The PUC approved the creation of a capital reserve account consistent with the terms of the Settlement Agreement. The PUC found that the Settlement Agreement fairly allocates excess earnings to the benefit of ratepayers as anticipated by PUC Order No. 21069. Furthermore, the Settlement Agreement presents a reasonable solution to the impact of the reduction in the corporate income tax rate. Using the excess earnings and tax savings toward funding of the capital reserve account with the limitations provided for in the Settlement Agreement provides a long-term ratepayer

¹¹ *Id.* at 4.

¹² Interstate's Response to PUC-1-3. Interstate's fiscal year runs June through the following May.

¹³ Joint Response to PUC-1-1 (Interstate and Division (Aug. 8, 2018); http://www.ripuc.org/eventsactions/docket/4373-Interstate-DIV-DR-PUC1_8-8-18.pdf).

benefit. In particular, the tax savings solution will likely provide a greater positive benefit to Interstate's ratepayers than a small direct credit on tickets.

Accordingly, it is hereby

(23287) ORDERED:

The Settlement Agreement filed on July 9, 2018 is hereby approved.

EFFECTIVE AT WARWICK, RHODE ISLAND ON AUGUST 9, 2018 PURSUANT TO AN OPEN MEETING DECISION. WRITTEN ORDER ISSUED OCTOBER 4, 2018.

PUBLIC UTILITIES COMMISSION



Margaret E. Curran

Margaret E. Curran, Chairperson

Marion S. Gold

Marion S. Gold, Commissioner

Abigail Anthony

Abigail Anthony, Commissioner

NOTICE OF RIGHT OF APPEAL: Pursuant to R.I. Gen. Laws §39-5-1, any person aggrieved by a decision or order of the PUC may, within seven days from the date of the order, petition the Supreme Court for a Writ of Certiorari to review the legality and reasonableness of the decision or order.