

Proposal Concerning Modifications to LIPA's Tariff for Electric Service

Requested Action:

The Long Island Power Authority ("LIPA") staff ("Staff") proposes to modify LIPA's Tariff for Electric Service (the "Tariff") effective August 1, 2022, to introduce a cost recovery solution to ensure that rates recover no more and no less than the actual transmission and distribution ("T&D") property tax PILOT expenses paid by LIPA, at the lowest cost to customers.

Background:

Taxes, payments-in-lieu-of-taxes ("PILOTs")¹, and assessments are LIPA's third largest expense. LIPA's approved 2022 budget includes a projected \$711 million² in taxes, PILOTs, and assessments for 2022, which accounts for approximately 18.5 percent of customer bills. As a result, LIPA continually strives to minimize the impacts on bills caused by taxes.

LIPA pays PILOTs on the T&D property LIPA acquired from its predecessor, LILCO, consisting of power lines, substations, and transformers used to connect electricity to customers. In the years following the LILCO acquisition, property PILOT³ payments to local governments grew at a rapid pace – on average 6.6 percent per year between 2004 and 2014, including increases in excess of 10 percent per year in 2010 and 2011. This high rate of growth more than doubled the amount of taxes on LIPA's T&D property from \$125 million in 2000 to \$304 million projected in 2022.

This high tax burden was partially addressed with the LIPA Reform Act of 2013 ("LRA"), which effectively capped the annual future increase in property tax payments on any parcel to no more than 2% over the payment made in the prior calendar year. The LRA also eliminated a portion of LIPA's revenue tax obligation, which saved an additional \$40 million per year for customers. The LRA produced an estimated cumulative savings of nearly \$400 million through 2021.

LIPA's efforts to reduce PILOT payments on the T&D system focus on ensuring that all taxing jurisdictions abide by the two percent tax cap of the LRA and on challenging unreasonably high assessments for T&D property.

A lawsuit filed in January 2016 by 45 Nassau County school districts reached a settlement that affirms the LIPA's tax calculations and the implementation of the two percent tax cap.

LIPA continues to urge certain Suffolk County municipalities to comply with the two percent tax cap and, late in 2017, filed suit to enjoin Suffolk County municipalities from taking actions that ignore this statutory requirement. LIPA continues to meet and work with municipalities in Suffolk

¹ Payments that LIPA makes to other governmental authorities in replacement of the taxes which were previously collected on utility revenues, assets or operations.

² \$224 million of property taxes on power plants owned or under contract to LIPA; \$304 million of local property taxes on transmission and distribution ("T&D") property; and \$41 million of state and gross revenue taxes and assessments, \$131 million of sales taxes, and \$12 million of other assessments.

³ LIPA is exempt from property taxes. PAL 1020-p. It pays statutory PILOTs that are calculated similarly to property taxes. PAL 1020-q(1).

County to ensure proper implementation of the two percent cap. All taxing jurisdictions in Nassau County and the City of New York currently comply with the two percent cap.

LIPA’s efforts directly result in lower electric bills for LIPA’s customers. LIPA currently does not pay (or recover in rates) any property tax PILOTs in excess of the LRA’s two percent tax cap. However, as explained above, certain Towns in Suffolk County continue to refuse to apply the two percent cap. If LIPA’s property tax fairness lawsuits are ultimately unsuccessful, a litigation loss could result in a \$90 million judgment, raising customer rates as soon as 2023. Each additional year adds approximately \$22 million, in the event of an adverse judgment.

Proposal:

LIPA is a not-for-profit public power utility that collects from its customers its costs to provide service. LIPA’s budgets and base delivery rates include the recovery of property tax PILOTs consistent with the LIPA Reform Act’s 2% cap on PILOT tax increases.

Staff proposes a cost recovery solution to ensure that rates recover no more and no less than the actual T&D property tax PILOT expenses paid by LIPA, including any adverse final court judgments, at the lowest cost to customers and gradually over time.

To accomplish this, Staff proposes to recover (or refund) variances between budgeted and actual T&D property tax PILOTs as a component of the Delivery Service Adjustment (“DSA”). The DSA is mechanism to reconcile actual costs to budgeted costs, for cost categories that are unknown when budgeted and outside of LIPA’s control, such as storms, other emergencies, and interest rates. The new DSA component will recover (or refund) the difference between actual T&D property tax PILOTs paid (including court-ordered payments or refunds) and budgeted T&D property tax PILOTs.

The proposed approach is consistent with Public Service Commission policy for investor-owned utilities, which utilize deferral mechanisms for recovery of property taxes that differ from those in electric rates. The proposed approach is also the lowest cost solution. The alternatives are either (i) collecting in electric rates today for property tax PILOTs billed by Suffolk Towns above the 2% cap, or (ii) in the event of an adverse court judgment, financing the cost of the judgment, including collecting coverage on the principal amount financed. Both alternatives result in millions of dollars in higher costs to customers. Depending on the size of any adverse judgment in the Suffolk County litigation, the proposed solution could avoid \$41.5 million in higher customer bills over five years.

In setting the budget and base rates for an upcoming year, the budgeted amount for T&D tax PILOTs will be equal to the prior year’s PILOTs (as adjusted by any final court actions) plus 2%. Any actual judgment that LIPA is required to pay by court order for past periods will be tracked for recovery from customers. Lump sum payments will be spread over a period of 5 years.

Financial Impacts:

The financial impact of the proposal depends on the outcome of LIPA's property tax fairness lawsuits. If no adverse judgments are issued, the proposal will have no financial impact. If an adverse judgment is issued and upheld on appeal, customer rates will increase with or without the adoption of this proposal. However, rates will increase significantly less if the proposal is approved. Assuming a \$90 million adverse judgment, the proposal will result in estimated savings to LIPA customers of \$41.5 million if the appeal is decided in 2022, and with even more potential savings if the appeal is decided later.

Affected Tariff Leaves:

182P, 182Q. Leaf 182O and Delivery Service Adjustment (DSA) Statement are included for reference.

Summary of Proposed Changes:

Staff is proposing to develop a cost recovery solution to ensure that electric rates recover actual T&D PILOT expenses consistent with the LIPA Reform Act's 2% cap on PILOT tax increases. The new DSA component will recover (or refund) the difference between actual T&D tax PILOTs paid (including court-ordered payments or refunds) and budgeted T&D tax PILOTs.

VII. ADJUSTMENTS TO RATES AND CHARGES OF SERVICE CLASSIFICATIONS: (continued):**K. Delivery Service Adjustment**1. Purpose and Applicability

The Delivery Service Adjustment is a rate mechanism that reconciles on an annual basis the difference between the amount of certain costs included in the Authority's base delivery rates ("Base Rate Costs") and the amount of such costs that the Authority actually incurs in an annual period.

2. Applicability

- a) The Delivery Service Adjustment will be assessed to Service Classification Nos. 1, 1-VMRP, 1-VTOU, 2, 2-VMRP, 2-L, 2-L-VMRP, 2-MRP, 5, 7, 7-A, 10, 12 and 16.
- b) Retail Customers participating in the Long Island Choice or Green Choice program are subject to the Delivery Service Adjustment as applied to their Service Classification.
- c) The Delivery Service Adjustment does not apply to:
 - (1) Energy Service Companies (ESCOs) receiving service under Service Classification No. 14.
 - (2) Service Classification Nos. 11 and 13 (Rate Codes 289, 278).
 - (3) All load delivered under the Empire Zone Program, Excelsior Jobs Program, Manufacturer's Competitiveness Business Attraction/Expansion Program, Business Incubation, and Recharge New York Programs.

3. Relevant Terms and Conditions

- a) The Base Rate Costs subject to the Delivery Service Adjustment are as follows:
 - (1) Storm Event Reserve Funding: Base Rate Costs include funding for a Storm Event Reserve. All Storm Event costs will be charged to the Storm Event Reserve. "Storm Events" are defined as set forth in the LIPA amended and restated, Operations Service Agreement ("OSA"), dated December 13, 2013. The recovery will be net of any anticipated reimbursements received from outside sources for Storm Events. Should the actual reimbursements vary from the anticipated reimbursements the difference will be added to subsequent tracking periods. Storm preparation costs associated with storms that do not materialize may be recoverable through the Delivery Service Adjustment if a budget amendment recommending recovery of such costs is approved by the Authority Board of Trustees.

VII. ADJUSTMENTS TO RATES AND CHARGES OF SERVICE CLASSIFICATIONS: (continued):**K. Delivery Service Adjustment****Relevant Terms and Conditions: (continued)**

- (2) Debt Service Costs: In accordance with the Department Rate Recommendation dated September 28, 2015, Base Rate Costs include the amount of interest and principal payments on the Authority's debt adjusted for amounts associated with its fixed coverage ratio, plus all amounts of interest and principal payments including coverage collected on behalf of the Utility Debt Securitization Authority (and any similar authority).
- (3) Non-Storm Emergency: Beginning January 2021, the incremental costs authorized by the Board of Trustees for Non-Storm Emergency Events as set forth in the LIPA amended and restated Operations Service Agreement ("OSA"), dated December 13, 2013, will be eligible for recovery. The recovery will be net of any anticipated reimbursements received from outside sources for that Non-Storm Emergency event or condition. Should the actual reimbursements vary from the anticipated reimbursements the difference will be added to subsequent tracking periods. Consistent with Section 5.2.B.7 of the OSA:
 - i. The recovery will include the amount of the Budget Amendment approved by the Board for that budget year.
 - ii. The recovery will not include amounts for the expenditures that are designated for inclusion in future budget (contract) years.
 - iii. The materiality of the costs are considered as part of the determination to request and ultimate approval by the Board for a Budget Amendment to recover for Non-Storm Emergencies and will be included for recovery without further standards or requirements for materiality upon approval by the Board.
- (4) Bad Debt Expense: Beginning January 2021, any variance of accrued bad debt expense from the amount in an approved LIPA budget during periods affected by a government-ordered or Board-authorized moratorium on service disconnections and for up to 2 years following the end of such moratorium will be eligible for recovery.
- (5) Service Provider Pension and Other Post-Employment Benefits (OPEB) Expense: Beginning January 2021, any variance from the amount in the Approved Annual Budget for pension and OPEB expenses related to the Service Provider's operations excluding Pension and OPEB allocated to Capital, Storms or Utility 2.0 as they are tracked separately will be eligible for recovery.
- (5)(6) Transmission and Distribution Property Tax PILOTs: Beginning August 1, 2022, any variance from the amount in the LIPA approved annual budget for Transmission and Distribution property tax PILOTs to actual transmission and distribution property tax PILOTs (including final court-ordered payments or refunds) will be tracked separately and eligible for recovery. In setting the budget and base rates for an upcoming year, the budgeted amount for Transmission and Distribution Property Tax PILOTs will be equal to the prior year's PILOT liability (as adjusted by any Final Court Action) plus 2%. ("Final Court Action" means LIPA has exhausted its appeals or otherwise accepted the litigation outcome, including any court-approved settlements.)
- b. Tracking Period: The Tracking Period shall be the twelve months beginning October 1 and ending September 30 of each year.
- c. Storm Event Reserve Cap: The Storm Event Reserve Cap will be set to \$75 million and will be shown on the Statement of Delivery Service Adjustment.

- d. The difference between the actual costs incurred by the Authority during the Tracking Period as identified in Section K.-3.-a- and the Base Rate Costs for the Tracking Period will determine the DSA recovery/credit amount as follows:
 - (1) The entire difference in Debt Service Costs, Bad Debt Expense, and Service Provider pension and OPEB expense related to operations will be included for recovery/crediting in the next Recovery Period as defined below.

VII. ADJUSTMENTS TO RATES AND CHARGES OF SERVICE CLASSIFICATIONS: (continued):**K. Delivery Service Adjustment****Cost Recovery Period and Method: (continued)**

- (2) A cumulative balance will be established for the Storm Event Reserve. Starting in January 2016, the approved amount of revenue to be collected through base delivery charges to satisfy the Storm Event Reserve will be added to that balance monthly, and actual Storm Event expenditures throughout the Tracking Period will be deducted from the balance. The balance remaining in the account at the end of the Tracking Period will be determined. If a positive balance exists below the Storm Event Reserve Cap, the balance will remain in the Storm Event Reserve to offset future expenditures for Storm Events. If a negative balance exists, one-third of that balance will be recovered in the next Recovery Period as defined below and the remaining two-thirds of the balance will be eligible for recovery during a future Recovery Period.
- (3) In the event that the balance in the Storm Event Reserve Fund exceeds the Storm Event Reserve Cap, the funds in excess of the Storm Event Reserve Cap will be used to offset future capital spending.
- (4) Amounts to be recovered for the Non-Storm Emergency Events will be recovered in equal dollar installments over the three succeeding annual Cost Recovery Periods.
- (5) Transmission and Distribution Property Tax PILOTS - Any amount due based on a "Final Court Action" will be recovered in equal dollar installments over the five succeeding annual Cost Recovery Periods. Budget variances in future annual Transmission and Distribution Property Tax PILOTS will be included for recovery/crediting in a future Cost Recovery Period as defined below.

4. Cost Recovery Period and Method**a) For the Service Classifications subject to the Delivery Service Adjustment:**

- (1) The difference in costs for the applicable Tracking Period as determined in accordance with Section K.3.d), will be credited to or recovered from the Service Classifications subject to the Delivery Service Adjustment.
- (2) A Delivery Service Adjustment refund or recovery will be determined and applied to customer bills for the 12-months beginning January 1st of each calendar year (the "Recovery Period") subsequent to the end of the Tracking Period.
- (3) To determine the Delivery Service Adjustment recovery or refund, the total Delivery Service Adjustment refund or recovery amount will be divided by the applicable forecasted Delivery Service Revenues for the Recovery Period to develop the Delivery Service Adjustment Percentage of Delivery Service Revenues.
- (4) The Delivery Service Adjustment will be included in each applicable customer's bill in an amount equal to the customer's delivery charges times the Delivery Service Adjustment Percentage of Delivery Service Revenues, rounded to the nearest cent, in each month of the Recovery Period.
- (5) Under or over recoveries of the Delivery Service Adjustment from prior Recovery Periods will be accrued at the end of each Recovery Period for refund or recovery through the Delivery Service Adjustment in a subsequent Recovery Period.

5. Statement of Delivery Service Adjustment

The calculation of the Delivery Service Adjustment Percentage of Delivery Service Revenues and the effective date will be shown on the Statement of Delivery Service Adjustment. The Authority will file such Statement annually, and the Statement will be available at the Authority's business offices.

Long Island Power Authority

Statement of Delivery Service Adjustment (DSA)

Applicable to billings under the Service Classification groups set forth in ~~First Revised~~ Leaf No. 182O through 182Q of the Long Island Power Authority Tariff for Electric Service:

DSA Rider: (Percentage of Delivery Service Revenues).....X.XXXX%

Effective: ~~January 1, 2022~~ August 1, 2022