


State of Florida



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: June 23, 2010
TO: Ann Cole, Commission Clerk, Office of Commission Clerk
FROM: Marshall W. Willis, Director, Division of Economic Regulation 
RE: Docket No. 080677-EI, Petition for increase in Rates by Florida Power & Light Company

Please file the attached staff memorandum, dated June 23, 2010, in the above docket file. The memorandum is staff's analysis of the anonymous complaint, received on January 4, 2010, regarding tax implications of Production Tax Credits generated by NextEra energy Resources, LLC and utilized by FPL Group.

c: Tim Devlin
Curt Kiser
Cheryl Bulecza Banks
Andrew Maurey
Natalia Salnova

RECEIVED FPSC
10 JUN 23 PM 2:06
COMMISSION
CLERK

TELEPHONE NUMBER - DATE
5200 JUN 23 2010
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Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: June 23, 2010
TO: Marshall Willis, Director, Division of Economic Regulation
FROM: Natalia Salnova, Regulatory Analyst, Division of Economic Regulation *NS*
RE: Analysis of Allegations Raised in Anonymous Letter Related to Florida Power & Light Company, NextEra Energy Resources, and FPL Group, Inc.

On January 4, 2010, the Florida Public Service Commission (Commission) received an anonymous letter regarding tax implications for certain Production Tax Credits (PTCs) generated by NextEra Energy Resources, LLC (NextEra). The issue is whether tax benefits related to PTCs generated by a non-regulated affiliated entity, in this case NextEra, and utilized by the parent company (FPL Group, Inc. or FPL Group, now known as NextEra Energy, Inc. or NEE) on a consolidated basis should be recognized in the determination of the income tax expense for a regulated affiliate (Florida Power & Light Company or FPL) for regulatory purposes. Commission staff conducted an investigation and has performed a thorough analysis of the issue. Staff believes that FPL is in compliance with regulatory requirements with respect to FPL Group's treatment of the PTCs.

As stated in the anonymous letter to the Commission, "3 current senior level management employees of Next Era Energy Resources" raised a concern of improper treatment of NextEra's PTCs by FPL. The issue of whether FPL's income tax expense should be computed based on the statutory tax rate applicable to FPL or the effective tax rate for the consolidated entity has been raised previously on at least two occasions. Although it was not identified as a specific issue in the case, the question of whether a regulated company should use the statutory tax rate of the regulated entity or the effective tax rate of the consolidated entity for ratemaking purposes was discussed during the 2006 storm damage cost recovery hearing for FPL. The statutory tax rate for FPL was used for purposes of the storm damage cost recovery proceeding.¹ This same issue was raised again later in 2006 in a lawsuit filed by Extraordinary Title Services, LLC against FPL and FPL Group.² This latter case was dismissed, brought back on appeal, and ultimately dismissed again.

Staff requested FPL produce information regarding this issue through staff Data Requests dated January 12, 2010 and March 4, 2010. Staff reviewed the Company's responses and FPL

¹ Order No. PSC-06-0464-FOF-EI, issued May 30, 2006, in Docket No. 060038-EI, In re: Petition for issuance of a storm recovery financing order, by Florida Power & Light Company.

² Extraordinary Title Services, LLC, v. Florida Power & Light Company and FPL Group, Inc., 1So.3d 400 (Fla. 3rd DCA 2009)

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Group's tax-sharing agreement.³ The tax-sharing agreement, effective January 1, 2003, provides the principles for allocating the consolidated federal income tax liability and combined state tax liability by and among FPL Group. According to FPL's response to the March 4 Data Request, the tax liability recorded by each subsidiary of FPL Group, including FPL, is calculated on a stand alone basis, or the "separate return" method. This treatment is consistent with the tax-sharing agreement. Thus, the tax liability and charges to customers for the tax liability are the same regardless of whether FPL is filing individually or as part of a consolidated tax return. Tax benefits, if any, in excess of those that could be used by a subsidiary on a separate return basis are utilized on the consolidated tax return and recorded by the subsidiary that generated the tax benefits.

The approach used by FPL is consistent with standard cost of service ratemaking principles. Under the cost of service approach to ratemaking, rates charged for regulated services shall not be affected by the results of non-regulated operations. Thus, consumers shall bear the prudent costs of providing regulated services and shall be entitled to the tax benefits derived from regulated operations. As intended by Congress, tax credits are a measure of economic incentive to offset the risks and other economic considerations related to investments in targeted projects. The benefits of PTCs are intended to be utilized by the entity making investments in eligible renewable energy projects. Consistent with the cost of service principle of ratemaking, the PTCs generated by NextEra's investments are attributable to NextEra and accounted for as if the company were a separate legal and economic entity. The same logic applies to Investment Tax Credits (ITCs) generated by FPL's investments in solar energy projects. For the same reasons that it would be inappropriate to apply the benefit of ITCs associated with the solar energy investments made by FPL to NextEra, it would be equally inappropriate to apply the benefit of PTCs generated by the wind-energy investments made by NextEra to FPL.

Generally Accepted Accounting Principles (GAAP) require an allocation of the consolidated amount of current and deferred tax expense for a group that files a consolidated tax return among the members of the group when those members issue separate financial statements. The method adopted shall be systematic, rational, and consistent with the broad accounting for income tax principles established by Subtopic 740-10.⁴ The methods that are inconsistent with the principles of this Subtopic include methods that a) allocate only current taxes payable to a member of a group that has taxable temporary differences, b) allocate deferred taxes using a method that is fundamentally different than the asset and liability method prescribed by this Subtopic, or c) allocate no current or deferred tax expense to a member of the group that has taxable income because the consolidated group has no current or deferred tax expense. (FASB

³ Amended and Restated Income Tax Allocation Agreement, effective as of January 1, 2003, by and among FPL Group, Inc. ("FPL Group" or "Parent"), a Florida corporation, and each Affiliate.

⁴ Allocation of Consolidated Tax Expense to Separate Financial Statements of Members, FASB ASC 740-10-30-27 (Paragraph 740-10-30-27 of the Financial Accounting Standards Board Accounting Standards Codification). The Codification is the single source of authoritative nongovernmental U.S. generally accepted accounting principles (US GAAP) effective for interim and annual periods ending after September 15, 2009. Cross Reference: Accounting for Income Taxes, Statement of Financial Accounting Standards No. 109, paragraph 40 (Financial Accounting Standards Board, 1992)

ASC 740-10-30-28)⁵ The separate return method meets the criteria of Subtopic 740-10 as this method allocates current and deferred taxes to each member of the group as if it were a separate taxpayer and thus is the preferred GAAP and SEC method. Moreover, the Subtopic acknowledges that the sum of the amounts allocated to individual members of the group when the separate return method is used may not equal the consolidated amount. The criteria are satisfied, nevertheless, after standard reconciling adjustments normally present in the preparation of consolidated financial statements are considered.

Deloitte & Touche LLP has audited the consolidated financial statements of FPL Group, Inc. and Subsidiaries and the separate financial statements of FPL as of and for the years ended December 31, 2007, 2008, and 2009. The certified public accounting firm has also audited FPL Group's and FPL's internal control over financial reporting for the aforementioned years. According to the reports issued by the independent auditor, FPL Group's and FPL's audited consolidated statements are presented fairly, in all material respects, and in conformity with accounting principles generally accepted in the United States of America. In addition, in the opinion of Deloitte & Touche, FPL Group and FPL has maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, 2008, and 2009.

For the reasons discussed above, staff believes that the method of accounting for income tax expense and consolidated financial reporting used by FPL is consistent with Commission practice and is in compliance with GAAP requirements. The benefits associated with the PTCs generated by NextEra's wind energy investments and reflected in the consolidated tax return of FPL Group have been properly excluded from the computation of FPL's income tax expense.

⁵ Allocation of Consolidated Tax Expense to Separate Financial Statements of Members, FASB ASC 740-10-30-28 (Paragraph 740-10-30-28 of the Financial Accounting Standards Board Accounting Standards Codification). Cross Reference: Accounting for Income Taxes, Statement of Financial Accounting Standards No. 109, paragraph 40. (Financial Accounting Standards Board, 1992)