CAUSE NO. 45990

SOUTHERN INDIANA GAS AND ELECTRIC COMPANY
d/b/a CENTERPOINT ENERGY INDIANA SOUTH
(CEI SOUTH)

DIRECT TESTIMONY
OF
JENNIFER K. STORY
VICE PRESIDENT, TAX

ON

FEDERAL AND STATE INCOME TAXES

SPONSORING PETITIONER'S EXHIBIT NO. 15,
ATTACHMENT JKS-1

DIRECT TESTIMONY OF JENNIFER K. STORY

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Jennifer K. Story. My business address is 1111 Louisiana Street, Houston, Texas 77002.

Q. BY WHOM ARE YOU EMPLOYED?

A. I am employed by CenterPoint Energy Service Company, LLC ("Service Company"), a wholly owned subsidiary of CenterPoint Energy, Inc. The Service Company provides centralized support services to CenterPoint Energy, Inc.'s operating units, one of which is Southern Indiana Gas and Electric Company d/b/a CenterPoint Energy Indiana South ("CEI South", "Petitioner", or "Company").

Q. ON WHOSE BEHALF ARE YOU SUBMITTING THIS DIRECT TESTIMONY?

A. I am submitting testimony on behalf of CEI South.

Q. WHAT IS YOUR ROLE WITH THE SERVICE COMPANY?

A. I am Vice President, Tax for CenterPoint Energy, Inc. and its subsidiaries, including CEI South. I am responsible for all federal and state tax matters.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.

A. I received a Bachelor of Science in Accounting from the University of Texas at Dallas in 2002. I am a licensed certified public accountant in the States of Texas and Hawaii.

Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.

A. I joined Service Company in October 2022. Prior to then, I worked for gas and electric public utilities for 16 years in tax and regulatory leadership roles. In these roles, I was responsible for all income tax matters for these companies, including accounting for income taxes (Accounting Standards Codification, or "ASC", 740 and 980), federal and state income tax compliance, overseeing federal and state income tax audits, and sponsoring all income tax calculations in regulatory filings.

Q. WHAT ARE YOUR PRESENT DUTIES AND RESPONSIBILITIES AS VICE PRESIDENT, TAX?

A. My primary responsibilities include leading the tax function that is responsible for accurately and efficiently reporting the federal, state, and local taxes of CenterPoint Energy, Inc. and its subsidiaries, including CEI South.

Q. HAVE YOU EVER TESTIFIED BEFORE THE INDIANA UTILITY REGULATORY COMMISSION ("COMMISSION")?

A. Yes. I have testified before the Commission on behalf of CEI South in support of its request for a certificate of public convenience and necessity ("CPCN") for a Wind Project and the Posey County Solar Project, in Cause Nos. 45836 and 45847, respectively.

II. PURPOSE & SCOPE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. My direct testimony addresses four topics. First, I discuss the impact of the Inflation Reduction Act of 2022 ("IRA"), specifically addressing the corporate alternative minimum tax ("CAMT") and the Company's proposed Tax Adjustment Rider ("TAR"). Second, I support the computation of the income tax expense included in the Company's cost of service determination. I sponsor **Schedules C-3.38, C-3.39, C-4** and **C-5** in Petitioner's Exhibit No. 20. Third, I address the accumulated deferred income taxes ("ADIT") and excess accumulated deferred income tax ("EADIT") regulatory liability balances included in the Company's cost of capital calculation. In addition, I sponsor the property tax forecast on **Schedule C-3.27** as well as the Medicare Part D regulatory liability and associated amortization adjustment on **Schedule C-3.30** in Petitioner's Exhibit No. 20.

Q. ARE YOU SPONSORING ANY ATTACHMENTS OR SCHEDULES IN THIS PROCEEDING?

A. Yes. In addition to the previously mentioned Schedules, I am sponsoring the following attachment in this proceeding:

- Petitioner's Exhibit No. 15, **Attachment JKS-1**: Calculation of the Consolidated Tax Return Interest Benefit under the "Muncie Remand" Method

Q. WERE THE ATTACHMENTS AND SCHEDULES PREPARED BY YOU OR UNDER YOUR SUPERVISION?

A. Yes, they were.

III. INCOME TAX LEGISLATION AND PROPOSED TAR

Q. PLEASE DESCRIBE THE IRA.

A. H.R. 5376, commonly referred to as the IRA, was signed into law on August 16, 2022.[1] The stated purpose of this legislation was to fight inflation through deficit reduction and to advance climate initiatives. The IRA generally applies to tax years beginning after December 31, 2022. The IRA contains significant benefits for clean energy and renewable investments impacting the utility industry. In an effort to achieve the goal of providing these benefits, without adding to the deficit, the IRA includes the CAMT to offset the cost of tax incentives. That is, the CAMT is inextricably linked to the IRA's renewable incentives.

Q. PLEASE SUMMARIZE THE MAIN ELEMENTS OF FEDERAL TAX REFORM UNDER THE IRA THAT AFFECT PUBLIC UTILITIES.

A. The IRA changes certain elements of the United States tax law. Several provisions are applicable to public utilities, including:

- Restoration and extension of the renewable electricity production tax credit ("PTC") and clean electricity investment tax credit ("ITC");[2]
- Creation of new tax credits designed to incentivize investment in renewable energy;[3]
- Establishment of a non-deductible 1% excise tax on certain corporate share repurchases;[4] and
- Imposition of a 15% CAMT based upon adjusted financial statement income ("AFSI").

[1] Pub. L. No. 117-169, 136 Stat. 1818 (2022).
[2] I.R.C. § 45; I.R.C. § 48.
[3] I.R.C. § 45; I.R.C. § 45E; I.R.C. § 45Y.
[4] I.R.C. § 4501(a).

Q. HOW DOES THE IRA POTENTIALLY IMPACT THE COMPANY?

A. As discussed in Petitioner's Witness Brett A. Jerasa's testimony, the imposition of this minimum tax payment has the potential to negatively impact the Company's credit rating and, correspondingly, its ability to access financial markets and obtain debt at a reasonable cost. This is because the IRA imposes a new 15% CAMT based upon AFSI. Applicable corporations, as defined by Internal Revenue Code ("IRC" or "I.R.C.") §59(k), will now generally pay tax equal to the greater of 15% of adjusted book income (or, AFSI) or their regular federal tax liability.

Q. PLEASE DESCRIBE THE TAX CREDITS RELEVANT TO THE COMPANY.

A. The IRA includes $369 billion in climate and energy related provisions intended to address climate change, improve energy efficiency, and encourage renewable energy development.[5] Tax credits and incentives are the primary incentives set forth in the IRA to accomplish these goals.

Included in the tax credit provisions are the extensions of the ITC for solar energy and the eligibility for the solar PTC. In addition, for wind technologies an ITC or a PTC is also available. Energy storage technologies now qualify for the ITC, as do microgrid controllers and fuel cells. CEI South has already requested and received approval to flow PTCs to customers as part of its base rates and its annual Clean Energy Cost Adjustment ("CECA") fillings (Cause Numbers 45836 and 45847).

Q. PLEASE DESCRIBE THE NEW CAMT.

A. The IRA imposes the new CAMT prospectively on AFSI of an Applicable Corporation for taxable years beginning after December 31, 2022.[6] The CAMT represents the means within the IRA to fund the tax credit benefits described above.

AFSI is defined as the net income or loss reported on a taxpayer's applicable financial statement ("AFS")[7] for a taxable year, with certain adjustments.[8] An AFS is a financial statement prepared in accordance with generally accepted accounting principles

[5] "Clean Energy Economy Guidebook" White House at https://www.whitehouse.gov/wp-content/uploads/2022/12/Inflation-Reduction-Act-Guidebook.pdf.

[6] I.R.C. § 59(k)(1).

[7] I.R.C. § 451(b)(3).

[8] I.R.C. § 56A.

("GAAP") and reported to the United States Securities and Exchange Commission, generally in the form of an annual Form 10-K.

Adjustments are then made to the AFS, an example of which is an adjustment for depreciation allowed under IRC §168 in lieu of book depreciation. Other adjustments include, but are not limited to, federal income taxes and certain adjustments related to the accounting for defined benefit pension plans.[9]

The determination of whether CAMT must be paid is made by comparing the regular income tax liability to the CAMT tentative tax due.[10] If the CAMT tentative tax due exceeds the regular income tax liability, CAMT must be paid.

Q. PLEASE DESCRIBE INTERIM GUIDANCE PRESCRIBED BY INTERNAL REVENUE SERVICE ("IRS") NOTICE 2023-7 REGARDING THE CAMT.

A. On December 27, 2022, the IRS released Notice 2023-7,[11] providing taxpayers with interim guidance regarding time sensitive issues in the immediate application of the new CAMT.

Issues addressed in the interim guidance include (1) interpretation of rules with respect to depreciation of property subject to IRC § 168 and related adjustments for gain or loss on the sale or disposition of assets under the CAMT, (2) safe harbor rules in determining Applicable Corporation status, (3) interpretation of rules addressing the determination of Applicable Corporation status for affiliated groups and certain partnerships, and (4) guidance regarding treatment of certain federal income tax credits under the CAMT.

Taxpayers may rely on interim guidance until the Treasury's issuance of proposed regulations. The IRS has since issued additional interim guidance to address other issues in interpretation and application of the CAMT.[12] The issuance of proposed regulations is still forthcoming in response to comments submitted upon request made by the Treasury Department and IRS.

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[9] I.R.C. § 56A.
[10] I.R.C. § 55(a).
[11] See https://www.irs.gov/pub/irs-drop/n-23-07.pdf.
[12] See https://www.irs.gov/pub/irs-drop/n-23-20.pdf and https://www.irs.gov/pub/irs-drop/n-23-64.pdf.

Q. PLEASE PROVIDE AN EXAMPLE OF AN AFSI CALCULATION.

A. **Table JKS-1**, below, shows an example of how the AFSI is calculated.

Table JKS-1 – Example of AFSI Calculation

Description	Amount
PreTax Book Income	$ 5,000
Less: Federal Income Tax Expense	(1,050)
Financial Statement Income	3,950
Adjustments	
Add: Federal Income Tax Expense	1,050
Add: Book Depreciation	500
Deduct: Tax Depreciation	(3,000)
Total Net Adjustments	(1,450)
Adjusted financial statement income, or AFSI	$ 2,500

In this example, financial statement income is $3,950. Adjustments to financial statement income include additions of federal income tax expense of $1,050 and book depreciation of $500, and a deduction of $3,000 for tax deprecation for a net adjustment to financial statement income of ($1,450). AFSI of $2,500 is derived by reducing financial statement income of $3,950 by net adjustments of $1,450.

Q. PLEASE EXPLAIN THE DIFFERENCE BETWEEN AFSI AND REGULAR TAXABLE INCOME.

A. AFSI has limited adjustments for the differences between the recognition of income and expense for financial statement purposes and CAMT purposes. In contrast, the calculation of income for regular tax incorporates many differences in the recognition of income and expense. **Table JKS-2**, below, is a comparison of the differences in the calculation of AFSI and the calculation of regular taxable income.

Table JKS-2 – Illustrative Comparison of AFSI and Regular Taxable Income

Description	AFSI	Taxable Income
PreTax Book Income	$ 5,000	$ 5,000
Less: Federal Income Tax Expense	(1,050)	(1,050)
Financial Statement Income	3,950	3,950
Adjustments		
Add: Federal Income Tax Expense	1,050	1,050
Add: Book Depreciation	500	500
Deduct: Tax Depreciation	(3,000)	(3,000)
Add: Book/Tax Differences	0	200
Deduct: Book/Tax Differences	0	(1,200)
Total Net Adjustments	(1,450)	(2,450)
AFSI / Taxable Income	$ 2,500	$ 1,500

In this illustrative comparison, taxable income for regular tax includes adjustments of $200 (addition) and $1,200 (deduction) for various book tax differences not included in the calculation of AFSI. Common examples of these timing differences include cost of removal, mixed service cost, and bad debt.

Q. WHAT TAX RATES APPLY TO AFSI AND REGULAR TAX?

A. The statutory tax rate applied to taxable income is 21%. The calculation of CAMT applies a 15% rate to AFSI.

Q. PLEASE GIVE AN EXAMPLE OF THE CALCULATION OF CAMT.

A. The CAMT is the excess of the CAMT tentative tax over the regular 21% income tax liability. **Table JKS-3**, below, is an illustrative CAMT tax calculation.

Table JKS-3 – Illustrative CAMT calculation

Description	Amount
AFSI	$ 2,500
CAMT Rate	15%
CAMT Tentative Tax	375
Regular Taxable Income	1,500
Regular Tax Rate	21%
Regular Income Tax	315
CAMT	$ 60

In this example, the CAMT tentative minimum tax of $375 exceeds the regular income tax of $315 by $60. Because the CAMT tentative tax exceeds the regular income tax, the taxpayer is liable for the CAMT of $60 plus the regular income tax of $315 for a total federal tax liability of $375. Here, the enactment of the CAMT resulted in an increase of $60 in the taxpayer's current tax liability and also generates a $60 CAMT carryforward. The CAMT credit carryforward is an asset and should be included in the cost-free capital calculation in utility regulatory filings.

Q. PLEASE DESCRIBE HOW THE CAMT CREDIT IS APPLIED TO FUTURE INCOME TAX LIABILITIES.

A. The CAMT paid in prior years can be used as a tax credit against future income tax liabilities to the extent an income tax liability exceeds the CAMT tentative tax in a tax year. In the illustration in **Table JKS-4**, below, the taxpayer has a CAMT tentative tax of $375 and regular tax of $420 in Year 2. Because the CAMT tentative tax does not exceed the regular tax, there is no CAMT due in Year 2. In Year 1, the taxpayer paid CAMT of $60 and is eligible to claim a CAMT credit against regular tax liabilities in future years to the extent its regular tax liability exceeds its CAMT tentative tax in a given year. In Year 2, the regular tax liability ($420) exceeds the CAMT tentative tax liability ($375) by $45. The CAMT credit available to offset the Year 2 regular income tax liability is $45. In Year 2, the taxpayer's total tax liability is $375 ($420 regular tax + 0 CAMT - $45 CAMT credit). After utilization of the credit, the CAMT carryforward is $15 ($60 CAMT in year 1 less $45 utilization in year 2).

Table JKS-4 – Illustrative Application of CAMT Credit

Description	Year 1	Year 2
AFSI	$ 2,500	$ 2,500
CAMT Rate	15%	15%
CAMT Tentative Tax	375	375
Regular Taxable Income	$ 1,500	$ 2,000
Regular Tax Rate	21%	21%
Regular Income Tax	315	420
CAMT	60	0
Tax Before CAMT Credit	375	420
Less: CAMT Credit	-	45
Net Tax Due	$ 375	$ 375

Q. IS CEI SOUTH AN APPLICABLE CORPORATION FOR PURPOSES OF THE CAMT?

A. Yes.

Q. IS THE COMPANY CURRENTLY SUBJECT TO THE CAMT?

A. Yes. Based on the statutory language included in the IRA and interim guidance issued, CEI South is subject to the CAMT beginning in 2023. However, because CEI South and other members of the CenterPoint Energy, Inc. consolidated income tax return are expected to pay regular income tax in excess of the CAMT in 2023, there will be no CAMT due.

Q. DOES THE COMPANY EXPECT TO PAY THE CAMT IN 2024?

A. Yes. Based on current guidance, the company expects to pay the CAMT in 2024 and 2025 and in future years. Please see **Schedule C-5** in <u>Petitioner's Exhibit No. 20</u> for the calculation of CAMT for 2024 and 2025.

Q. PLEASE EXPLAIN THE IMPACT OF THE CAMT TO CASHFLOW AND CREDIT METRICS.

A. Payment of the CAMT means that the Company is no longer able to defer a portion of taxes to future periods and therefore must finance additional amounts to pay taxes in the current period. It may be necessary to increase borrowing to finance planned capital investments. As discussed in the direct testimony of Petitioner's Witness

Jerasa, this need for additional borrowing increases the cost of capital for CEI South and could impact the CEI South credit metrics. This was apparent after passage of the Tax Cut and Jobs Act of 2017 (the "TCJA"), when many utilities did receive credit downgrades.

Q. HOW HAS THE CAMT BEEN CALCULATED FOR THIS CASE?

A. The CAMT for CEI South was calculated using CEI South jurisdictional amounts and in the manner consistent with the examples outlined previously in my testimony. Adjustments to financial statement income were made for depreciation, pension expense, and federal income taxes.

Q. HOW DOES THE COMPANY PROPOSE TO TREAT THE CAMT CARRYFORWARD?

A. As previously stated, the CAMT credit carryforward is an asset and has been included in the cost-free capital calculation in this filing. When the minimum tax is paid, a CAMT credit is generated and can be carried forward indefinitely to offset the future regular income tax liabilities in periods where the regular federal income tax liability exceeds the CAMT liability. The CAMT credit cannot be carried back to previous taxable years. As explained above, the CAMT is a mechanism that Congress enacted to provide renewable tax incentives, the benefits of which come with the cost of the CAMT. Including the CAMT carryforward in the capital structure is a corollary consequence to the realization of benefits derived from the related IRA tax incentives. This is how the forecasted CAMT in 2024 and 2025 has been reflected in this case. On a going forward basis, CAMT carryforwards would be addressed through the Company's proposed TAR.

Q. WHAT IS THE PROPOSED TAR?

A. Petitioner's Witness Matthew A. Rice also testifies to the Company's proposed TAR. The TAR would capture tax rider adjustments that have already been approved by the Commission in other dockets and would also be expanded to include the effects of the CAMT and passback of Indiana State excess deferred income taxes ("EADIT").

Q. WHAT ARE THE ALREADY APPROVED TAX ADJUSTMENT MECHANISMS THAT WOULD BE REFLECTED IN THE TAR?

A. There are two already approved tax riders that would move to the TAR. First, as a result of the Commission's investigation into the effects of the TCJA, the Company is flowing back to customers federal EADIT from the TCJA through its Transmission, Distribution, and Storage System Improvement Charge ("TDSIC") rider.[13] This passback would continue outside of base rates but would instead be done through the TAR rather than the TDSIC. Second, PTCs realized from approved wind and solar projects are to be tracked through the Company's CECA mechanism. This adjustment would move from the CECA to the TAR.

Q. HOW WOULD THE CAMT BE REFLECTED IN THE TAR?

A. As I described previously, the effect of paying the CAMT is to pay a tax currently that would have otherwise been deferred. It creates a tax asset which can be used in later tax years to offset regular tax liability. Mathematically, including the CAMT carryforward as an offset to zero cost capital in the capital structure produces a similar effect on required return as including the incremental CAMT carryforward in the calculation of rate base upon which a return is authorized. Accordingly, CEI South proposes that between rate cases, the TAR would include a return on the CAMT carryforward to be calculated using the Company's weighted average cost of capital determined in this rate case.

Q. WHY IS IT APPROPRIATE TO INCLUDE THE CAMT IN THE TAR?

A. This is necessary to reflect the net impact of both the CAMT and PTCs from renewable projects. The CAMT provisions of the IRA were used to fund the extended and enhanced tax credits, so it is reasonable to include the impacts of both in this rider. Since the Company will always be subject to the CAMT, this calculation will need to be performed annually and compared with the regular tax calculation.

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[13] *In the Matter of the Indiana Utility Regulatory Commission's Investigation into the Impacts of the Tax Cuts and Jobs Act of 2017 and Possible Rate Implications Under Phase 2 for Vectren Energy Delivery of Indiana, Inc.*, Cause No. 45032 S21 (IURC Aug. 29, 2018), approving the Stipulation and Settlement Agreement among the Settling Parties (the "45032 S21 Settlement Agreement"), which included the Indiana Office of Utility Consumer Counselor and the Indiana Industrial Group, thereby resolving all Phase 2 issues for CEI South.

Including both the PTCs and the incremental return on the CAMT payment in the TAR is necessary to capture the full impact of the IRA. A rider is necessary since annual results could vary significantly, making this a more reasonable approach than including these items in base rates. Similar to the process after TCJA was enacted, additional guidance is expected to clarify provisions of the IRA.[14] A rider will allow the Company to capture the impact of these rules as they become available.

Q. WHEN AND HOW SHOULD IRA TRACKING BEGIN UNDER THE TAX ADJUSTMENT RIDER?

A. For PTCs, tracking should begin in 2025. If approved, the Company will file a TAR in November 2025 that will include an estimate of the 2025 PTCs. For the CAMT carryforward, tracking should begin in 2026 after the test period. The second TAR filing in November 2026 will include the difference between the minimum tax 2026 carryforward estimated balance and the carryforward included in cost free capital in base rates, the result of which will be multiplied by the approved cost of capital from this proceeding. Additionally, it will include an estimate of the 2026 PTCs and a true-up of the 2025 estimated PTCs to actual. With additional guidance and proposed regulations still expected, it is most appropriate to commence tracking with this rate case, since it coincides with the IRA recently becoming law. Please see the direct testimony of Petitioner's Witness Rice for further explanation on the Tax Adjustment Rider tariff.

Q. YOU ALSO MENTIONED STATE EADIT. HOW IS STATE EADIT PROPOSED TO BE REFLECTED IN THE TAR?

A. There is a regulatory liability for Indiana state EADIT of $11,412,319. This results from the implementation of a gradual period decrease of the Indiana corporate income tax by the Indiana General Assembly. This rate decrease began in 2012 and was implemented as follows:

July 2002 – June 2012:	Increased rate from 3.4% to 8.5%
July 2012 – June 2016:	Decrease in rate from 8.5% to 6.5%
July 2016 – June 2021:	Decrease in rate from 6.5% to 4.9%

[14] Comments have been requested on various tax credits and on the CAMT. Additional IRS Notices will likely be issued before Proposed Regulations come out. Taxpayers have opportunities to comment and request clarification during this process and until Final Regulations are issued.

The state deferred tax balances were remeasured to capture the decrease from 8.5% to 4.9%. These combined decreases in the tax rate resulted in excess state accumulated deferred income taxes. Consistent with Cause Nos. 45447 and 45468, the Company is proposing to refund these excess deferred taxes to customers over five years. The Company proposes to include the refund of the excess deferred state taxes in the TAR along with the federal EADIT. Like federal EADIT, the amortization of State EADIT would be outside base rates.

Q. HOW WOULD THE TAR ADDRESS FUTURE CHANGES TO THE FEDERAL EADIT BALANCE IN THIS FILING SUBJECT TO CHANGE?

A. Future changes to the federal EADIT balance would be addressed in the same fashion that such changes are addressed in the TDSIC mechanism presently. Future events such as IRS audit adjustments to the Company's previously filed income tax returns, future IRS rulings and/or clarifications to the normalization rules, and changes in federal tax laws or rates could change the federal EADIT balance, as well as the split between protected and unprotected. These changes would be addressed in future TAR filings.

IV. <u>CALCULATION OF INCOME TAX EXPENSE</u>

Q. PLEASE EXPLAIN HOW THE INCOME TAX EXPENSE FOR THE TEST YEAR IS CALCULATED.

A. As discussed in the direct testimony of Petitioner's Witness Chrissy M. Behme, the Company's historic base period is the twelve months ended December 31, 2022, and the forward-looking test year is the Company's forecast for the twelve months ended December 31, 2025. In general, a company such as CEI South incurs federal and state income tax expense on the profits it earns; and as part of this rate proceeding, the Company is including those tax expenses in the revenue requirement. I have calculated the test year state and federal income tax amounts which are included on <u>Petitioner's Exhibit No. 20</u>, **Schedules C-4 and C-5**, respectively.

Q. HOW IS THE CURRENT STATE INCOME TAX DETERMINED?

A. The calculation of current state income tax expense begins with the operating income as determined in the cost of service. This amount is then adjusted for interest expense, book/tax temporary differences and permanent differences. Certain permanent differences associated with non-utility accounts and are not included in the calculation. This calculation results in the determination of taxable income or loss, which is then multiplied by the Indiana corporate income tax rate in effect in the test period to arrive at pro-forma Indiana income tax expense at present rates. I have used the currently enacted Indiana income tax rate of 4.9%.

Q. HOW IS THE CURRENT FEDERAL INCOME TAX DETERMINED?

A. Current federal income tax is calculated by starting with the operating income as outlined above. It is then reduced by the total current state income tax to arrive at the operating income before federal taxes. This amount is then adjusted for interest expense, book/tax temporary and adjusted permanent differences to arrive at federal taxable income. Taxable income is then multiplied by the federal income tax rate of 21% to determine total current federal income tax.

Q. WHY ISN'T THE INDIANA UTILITY RECEIPTS TAX INCLUDED AS AN ADJUSTMENT TO ARRIVE AT OPERATING INCOME BEFORE FEDERAL TAXES?

A. On March 15, 2022, the House Enrolled Act 1002 was enacted, which repealed the utility receipts tax effective July 1, 2022. The Company's test year, therefore, does not include utility receipts tax expenses.

Q. PLEASE DISCUSS THE CALCULATION OF THE CAMT INCLUDED IN CURRENT TAX EXPENSE.

A. As I explained previously, the effect of paying the CAMT is to pay tax currently that would otherwise be deferred. The CAMT calculation included in this rate case starts with pretax book income from Petitioner's Exhibit No. 20, **Schedule C-5**, which excludes both federal and state income taxes. Adjustments are then made for state income tax expense, IRC § 168 depreciation and covered benefit plans to arrive at the CEI South's 2024 and 2025 AFSI. The 15% minimum tax rate has been applied to AFSI to arrive at the CAMT expense. The minimum tax liability is the greater of the CEI South's regular current tax expense or the CAMT.

Q. PLEASE DISCUSS HOW DEFERRED TAX EXPENSE IS IMPACTED BY THE CAMT.

A. Deferred tax expense is reduced by the amount of current tax expense attributable to the CAMT. Total tax expense does not change due to the CAMT. Instead, it shifts from deferred to current.

Q. HOW IS THE DEFERRED STATE INCOME TAX DETERMINED?

A. The deferred state income tax expense reflects the future tax liability to the state of Indiana based on current period income. Deferred state income tax is calculated by multiplying the temporary book/tax differences by the Indiana corporate tax rate.

Q. HOW IS THE DEFERRED FEDERAL INCOME TAX DETERMINED?

A. Deferred federal income tax is calculated by subtracting the deferred state income tax expense from temporary book/tax differences and multiplying the result by the federal income tax rate of 21% in order to determine the Company's future federal income tax liability resulting from current period income.

Q. HOW IS THE COMPANY'S RESEARCH AND DEVELOPMENT ("R&D") CREDIT DETERMINED FOR FEDERAL INCOME TAX PURPOSES?

A. The Company calculates its R&D credit using the Alternative Simplified Credit method. Under such method, the Alternative Simplified Credit is calculated by multiplying any qualified research expenditures ("QREs") that exceed 50% of the average QREs (using a three-year average) by 14%.

Q. IS THE R&D CREDIT INCLUDED IN THE TEST YEAR?

A. Yes, the credit will be taken in forthcoming years, so it is included in the test year.

Q. IS THE PETITIONER PART OF A CONSOLIDATED GROUP FOR PURPOSES OF FILING AN INCOME TAX RETURN?

A. Yes. CEI South is a member of the CenterPoint consolidated group. CenterPoint Energy, Inc. files its tax return on behalf of all members in the consolidated group.

Q. HOW HAS THE COMMISSION DETERMINED A UTILITY IN A CONSOLIDATED GROUP SHOULD RECOGNIZE THE BENEFITS OF FILING A CONSOLIDATED RETURN IN ITS REVENUE REQUIREMENT?

A. In the Commission's Supplemental Order on Remand in Cause No. 34571 dated September 16, 1981, the Commission outlines what is commonly referred to as the Muncie Remand Method. The methodology from that order has been followed in this proceeding and pushes down a portion of the parent company's interest expense deduction to CEI South. The Muncie Remand Method outlines a specific four-step process for calculating this adjustment. This calculation determines the tax savings from CEI South's participation in a consolidated income tax return. The four-step process is as follows:

(1) Compute the debt ratio of the parent company by dividing its outstanding long-term debt by its entire capital structure, including the retained earnings of its subsidiaries;

(2) Multiply the Indiana utility's[15] equity account by the results of step (1) above;

(3) Calculate the parent company's average net cost of long-term debt by dividing its annualized interest expense by its total outstanding long-term debt; and

(4) Multiply the result in step (2) above by the result in step (3) above.

This calculation is shown on Petitioner's Exhibit No. 15, **Attachment JKS-1** and the associated interest is included in the tax expense calculation on Petitioner's Exhibit No. 20, **Schedule C-5**.

Q. PLEASE EXPLAIN THE DIFFERENCE BETWEEN TEMPORARY AND PERMANENT DIFFERENCES.

A. A temporary difference occurs between the tax basis of an asset or liability under the IRC and its reported amount in the financial statements based on GAAP that will result in taxable income or deductions upon the reversal of the difference in future periods.[16] The gross basis of temporary differences is generally the same for book and tax. However, they are recovered over different time periods. Permanent differences, on the other hand, are treated differently for financial statement purposes and income tax

[15] CEI South

[16] *See* ASC 740-10-20.

purposes and will never reverse. An example is meals that can be recognized in book income in full but certain meals can only be deducted at 50% on the income tax return.

Q. PLEASE DISCUSS THE ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION ("AFUDC") EQUITY BOOK/TAX DIFFERENCE AND ITS IMPACT ON DEPRECIATION EXPENSE.

A. AFUDC equity is the equity portion of financing utility capital construction projects and is added to the cost of the project while it is in construction work in process. It is capitalized to plant in service as part of the underlying asset. The cumulative gross book balance of AFUDC equity has book depreciation that is included in the cost of service. While AFUDC equity has book basis it has no corresponding tax basis or associated tax depreciation. Because there is no tax depreciation expense, the book depreciation expense is not deductible for tax purposes. The book depreciation expense needs to be added back to taxable income to compute the proper income tax expense. That adjustment is included in the book depreciation on AFUDC line as a permanent difference in the income tax calculation.

Q. HAVE OTHER ADJUSTMENTS BEEN MADE TO DEPRECIATION EXPENSE IN THE TEST YEAR?

A. Yes, book depreciation expense in the test year has been adjusted by the new depreciation rates calculated by Petitioner's Witness John J. Spanos in his depreciation study. Both the depreciation tax expense temporary difference and ADIT have been adjusted for this change in depreciation in the test year.

V. ACCUMULATED DEFERRED INCOME TAX

Q. WHAT IS ADIT?

A. ADIT represents a net deferred tax liability for the estimated future tax effects attributable to temporary differences based on the provisions of enacted tax law.[17] ADIT arises from the interaction of the IRC, the Company's accounting practices under GAAP, and the Company's operations.

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[17] The effects of any possible, but not yet enacted, future changes in tax laws or rates are not contemplated as part of the calculation of ADIT in this filing.

Q. PLEASE DESCRIBE THE FORECASTING PROCESS USED TO DETERMINE THE PRO-FORMA ADIT BALANCE INCLUDED IN THIS PROCEEDING.

A. The pro-forma ADIT starts with the 2022 year-end balance. Book to tax basis differences are then forecasted using historical averages for 2019 through 2023. ADIT is calculated on that activity and the resulting change in ADIT is then added to the 2022 actual amount to get balances for 2023 and 2024.

Q. ARE THERE ANY NEW FORECASTED COMPONENTS OF ADIT THAT WERE NOT INCLUDED IN THE HISTORICAL BASE YEAR?

A. Yes, as discussed above, the CAMT results in a CAMT carryforward that is included in the forecasted period.

Q. WERE ANY ADJUSTMENTS MADE TO THE ADIT BALANCE?

A. Yes. ADIT in the test year has been adjusted to reflect a deferred tax liability on the prepaid pension asset discussed in Witness Jerasa's testimony. Additionally, ADIT related to Troy Solar[18] has been removed.

Q. HOW IS ADIT REFLECTED IN FILING SCHEDULES OF THIS PROCEEDING?

A. The pro-forma ADIT balance has been incorporated as a component of cost-free capital on <u>Petitioner's Exhibit No. 20</u>, **Schedule D-5** sponsored by Petitioner's Witness Jerasa.

VI. <u>OTHER INCOME TAX RELATED COST OF CAPITAL ITEMS</u>

Q. PLEASE DISCUSS THE EADIT INCLUDED IN COST-FREE CAPITAL.

A. As I previously stated, federal EADIT resulting from the TCJA is currently being refunded in the Company's TDSIC mechanism. Petitioner's Witness Rice discusses the Company's proposal to move these federal EADIT credits from the TDSIC mechanism to the new TAR mechanism. As stated earlier in my testimony, the Company is also proposing to include state EADIT credits into the TAR mechanism. In addition, the credits for accelerated EADIT associated with the issuance of securitization bonds related to the retirement of A.B. Brown Units 1 and 2 will be moved into the proposed TAR. The refund of protected and unprotected EADIT has been

[18] Troy Solar is non-public utility property and is not included in base rates. It will continue to be collected via a levelized rate in the CECA as approved in Cause No. 45086.

forecasted through the end of the 2025 test period. The pro-forma balance of the EADIT regulatory liabilities, as well as the associated ADIT deferred tax assets, has been included as cost-free capital on Petitioner's Exhibit No. 20, **Schedule D-5** sponsored by Witness Jerasa.

Q. PLEASE DISCUSS THE ITC INCLUDED IN THE CAPITAL STRUCTURE.

A. The pro-forma unamortized ITC balance is included in the capital structure at the overall weighted cost of investor-provided capital Petitioner's Exhibit No. 20, **Schedule D-5**. This presentation is consistent with Petitioner's prior rate cases.

VII. C SCHEDULES

Q. YOU MENTIONED PREVIOUSLY THAT YOU WERE SPONSORING CERTAIN ADJUSTMENT SCHEDULES SET FORTH IN PETITIONER'S EXHIBIT NO. 20. WHAT ARE THOSE ADJUSTMENT SCHEDULES?

A. I am sponsoring **Schedule C-3.27** (Property Tax) and **C-3.30** (Deferred Medicare Tax Liability). For property tax, there are detailed workpapers setting forth the calculation. In essence, a forecasted tax basis is computed using the Company's projected construction activities, and the tax expense is calculated. The deferred Medicare Tax Liability is reflected on the Company's books, and the Company is proposing to amortize it over a five-year period.

VIII. SUMMARY

Q. DO YOU HAVE ANY CONCLUDING OBSERVATIONS?

A. Yes, in summary, I conclude the following:

- The ADIT and EADIT regulatory liability balances, as well as the income tax expense included in the test year cost of service are fair and accurate based on the underlying rate base and recoverable expenses included in the cost of service.
- The Company's income tax calculations are all prepared on a fully normalized basis, consistent with Commission precedent and the IRC.

- The Company's calculations of tax expense, ADIT and EADIT regulatory liability comply with all IRS normalization requirements, including those related to accelerated tax depreciation.
- The Company's Tax Adjustment Rider is the appropriate mechanism to track the impacts of the recently enacted federal IRA, to refund the federal and state EADIT credits from tax rate changes, and to refund the credits for accelerated EADIT from the issuance of securitization bonds related to the A.B. Brown Units 1 and 2 retirements.

IX. CONCLUSION

Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY?

A. Yes, it does.

VERIFICATION

I affirm under penalties for perjury that the foregoing representations are true to the best of my knowledge, information, and belief.

SOUTHERN INDIANA GAS AND ELECTRIC COMPANY D/B/A CENTERPOINT ENERGY INDIANA SOUTH

Jennifer K. Story

Jennifer K. Story
Vice President, Tax

11/27/2023
Date

Attachment JKS-1 Provided in Native Excel Format