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**INDIANA UTILITY
REGULATORY COMMISSION**

I&M Exhibit: _____

Cause No. 45576

INDIANA MICHIGAN POWER COMPANY

PRE-FILED VERIFIED DIRECT TESTIMONY

OF

JESSICA M. CRISS

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**DIRECT TESTIMONY OF JESSICA M. CRISS
ON BEHALF OF
INDIANA MICHIGAN POWER COMPANY**

I. Introduction of Witness

1 **Q1. Please state your name and business address.**

2 My name is Jessica M. Criss and my business address is 1 Riverside Plaza,
3 Columbus, OH 43215.

4 **Q2. By whom are you employed and in what capacity?**

5 I am employed by American Electric Power Service Corporation (AEPSC) as a
6 Tax Accounting and Regulatory Support Manager. AEPSC supplies
7 engineering, accounting, planning, advisory, and other services to the
8 subsidiaries of the American Electric Power (AEP) system, one of which is
9 Indiana Michigan Power Company (I&M or the Company).

10 **Q3. What are your responsibilities as a Tax Accounting and Regulatory
11 Support Manager?**

12 I participate in the recording of the tax accounting entries and records and the
13 review of federal and state tax returns of AEP and its subsidiaries. I am also
14 responsible for coordinating and developing state and federal tax data provided
15 by the AEPSC Tax Department for use in regulatory proceedings. I have
16 attended numerous tax, accounting, and regulatory seminars throughout my
17 professional career.

1 **Q4. Briefly describe your educational background and professional**
2 **experience.**

3 I earned a Bachelor of Science in Business Administration with a focus in
4 Accounting and a Masters of Accounting from St. Louis University School of
5 Business. I have been a Certified Public Accountant in the State of Ohio since
6 2015.

7 While pursuing my degrees I was employed part time at a regional public
8 accounting firm in Chesterfield, MO from February 2012 to December 2013. I
9 was hired at a regional public accounting firm in Akron, OH as a Tax Accountant
10 in January 2014 and was promoted to Senior Tax Accountant in January 2016.

11 In December 2016 I was hired at L Brands, Inc., a retail corporation in
12 Columbus, OH as a Tax Analyst and was promoted to Senior Tax Analyst in
13 April 2019. I joined AEPSC in January 2020 as a Principal Tax Analyst and was
14 promoted to my current position of Tax Accounting and Regulatory Support
15 Manager effective February 20, 2021.

II. Purpose of Testimony

16 **Q5. What is the purpose of your testimony?**

17 I present and support:

- 18 • Federal and state income tax expense for the historical period ended
19 December 31, 2020 (Historical Period) and for the forward-looking test
20 period ended December 31, 2022 (Test Year);
- 21 • Accumulated Deferred Federal Income Taxes (ADFIT) and Accumulated
22 Deferred Investment Tax Credit (ADITC) incorporated in the capital
23 structure used by Company Witness Messner to calculate the Weighted
24 Average Cost of Capital (WACC);

- 1 • Income tax expense adjustments related to certain ratemaking
2 adjustments made to the Test Year as supported by other Company
3 witnesses;
- 4 • Certain adjustments to income tax expense and accumulated deferred
5 income taxes;
- 6 • Calculation of the gross revenue conversion factor and certain taxes
7 other than income taxes;
- 8 • Calculation of effective federal income tax rates; and
- 9 • Illustrative calculation of the potential effects of a future change in the
10 federal statutory tax rate.

11 **Q6. Are you sponsoring any exhibits?**

12 I am fully or partially sponsoring:

- 13 • Exhibit A-8: Test Year Calculation of Gross Revenue Conversion Factor
- 14 • Exhibit A-9: Test Year Effective Tax Rate

15 **Q7. Are you sponsoring any attachments?**

16 Yes, I am sponsoring:

- 17 Attachment JMC-1 Test Year state income tax rate
- 18 Attachment JMC-2 Test Year interest synchronization
- 19 Attachment JMC-3 Test Year Net Operating Loss Carryforward (NOLC)
- 20 Attachment JMC-4 Illustrative calculation of 28% Federal Statutory Rate
21 Change using Test Year data

1 **Q8. Are you sponsoring any workpapers?**

2 Yes, I am sponsoring:

3 WP-JMC-1 Test year tax expense calculations and tax
4 adjustments

5

6 In addition, I am co-sponsoring:

7 WP-A-RIDER-4 Excess Unprotected ADFIT Adjustment

8 I also sponsor the following sections of I&M-WP-1 (Total Company):

9 I&M WP 1-7 Historical tax expense

10 I&M WP 1-8 Historical parent company net interest tax benefit

11 I&M WP 1-9 Historical Gross Revenue Conversion Factor

12 I&M WP 1-10 Historical effective federal income tax rate

13 I&M WP 1-11 Historical effective state income tax rate

14 **Q9. Were the exhibits, attachments, and workpapers that you are sponsoring**
15 **prepared or assembled by you or under your direction and supervision?**

16 Yes.

17 **Q10. Please summarize your testimony.**

18 The methods used in this case to develop the federal and state income tax
19 expense for the Test year are consistent with prior rate filings. The Company's
20 state and federal income tax expense has been properly recomputed to reflect
21 the appropriate tax effects resulting from the various ratemaking adjustments
22 supported in this case.

1 The Company's ADFIT balances have been properly recomputed to reflect the
2 balance of deferred assets and liabilities necessary as an adjustment to the
3 capital structure. The adjusted Test Year level of other tax expense is
4 appropriate and necessary and reflects the proper amount of going-level
5 expense. The Company's treatment of its net operating loss carryforward is
6 reasonable and consistent with stand-alone ratemaking practices and IRC
7 normalization requirements.

III. Federal and State Income Tax Expense

8 **Q11. Please describe the methodology used to develop the federal and state**
9 **income tax expense for the Test Year.**

10 Consistent with prior rate filings and Commission Orders, including Cause Nos.
11 45235, 44967, and 44075, the Company's federal tax expense and ADFIT in the
12 capital structure are calculated using stand-alone ratemaking practices using a
13 normalized method of tax accounting. As in prior rate filings, the Company's
14 state income tax expense is calculated using a stand-alone basis using a flow-
15 through method of tax accounting.

16 The Company's income tax expense is based in large part on the components
17 of Company pre-tax book income and expense presented by Company witness
18 Heimberger, and the forecast of other various Schedule M items that would
19 impact the computation of current and deferred income tax expense for the Test
20 Year. The computations also include reversals of deferred taxes and
21 amortization of deferred investment tax credits utilized in prior years.

22 Workpaper WP-JMC-1 shows the calculation of Test Year federal income tax
23 expense. All deferred federal income taxes were computed based on the related
24 Schedule M items as presented in the Company's forecast. (The Company's
25 forecast process is explained in detail by Company witness Heimberger.) In
26 addition, the workpapers show the calculation of the Test Year state income tax

1 expense. This was developed using the most recent available state tax rates
2 and apportionment factors.

3 The Company's state and federal income tax expense has been properly
4 recomputed to reflect the appropriate tax effects resulting from the various
5 ratemaking adjustments supported in this case.

6 **Q12. Please describe the methodology used to develop Taxes Other Than**
7 **Income tax expense for the Test Year.**

8 The Test Year level of forecasted Taxes Other Than Income Tax expense is
9 representative of these types of ongoing tax expenses except for those tax
10 adjustments that I am sponsoring in this proceeding. The adjusted Test Year
11 level of other tax expense is appropriate and necessary and reflects the proper
12 amount of going-level expense.

13 **Q13. Please describe the calculation of the effective state income tax rate as**
14 **shown on Attachment JMC-1.**

15 Attachment JMC-1 shows the composite state income tax rate developed using
16 the appropriate state income tax rates and apportionment factors. This
17 composite rate is used to compute current state income tax expense and is
18 used in the development of the Gross Revenue Conversion Factor.

19 **Q14. Please describe the calculation of interest synchronization for federal**
20 **income tax as shown on Attachment JMC-2.**

21 Attachment JMC-2 shows the calculation of the amount of interest expense
22 deduction used by the Company for purposes of computing income tax
23 expense. This amount is calculated by multiplying the adjusted rate base by the
24 weighted cost of long-term debt. As explained later in my testimony, this interest
25 expense deduction is calculated as part of Current Federal Income Tax (CFIT)

1 and is consistent with past Commission practice including Cause Nos. 45235,
2 44967, and 44075.

3 **Q15. Please describe the development of the federal and state income tax**
4 **expense for the Historical Period.**

5 The Company's historical income tax expense is based on the actual amounts
6 recorded on I&M's books. The historical income tax expense has been adjusted
7 for out-of-period or non-ongoing items and is presented in I&M-WP-1-7 for
8 informational purposes only.

9 As with federal and state income tax in the Test Year, the Company's historical
10 federal and state income tax expense is calculated using the stand-alone
11 methodology as described in further detail in my testimony.

IV. Determination of Income Tax Components of Filing

12 **Q16. How was Income Tax Expense within Cost of Service and ADFIT and**
13 **ADITC within the capital structure determined in the filing?**

14 Income Tax Expense, ADFIT, and ADITC were each determined on a stand-
15 alone basis using a normalized method of tax accounting for Federal Income
16 Taxes. State Income Taxes are being presented on a stand-alone basis using
17 flow-through method of tax accounting.

18 **Q17. What is meant by determination of income tax expense, ADFIT, and ADITC**
19 **on a "stand-alone" basis?**

20 The determination of income tax expense and ADFIT on a stand-alone basis
21 means that taxes associated with revenues and expenses (operations) of the
22 entity's rate regulated operations and assets only are included within this filing.
23 All aspects of the Company's income taxes, including attributes such as NOLCs,

1 were computed based only on these items. The Company's taxable income or
2 loss and ADFIT was determined based on the revenues and expenses included
3 in this filing.

4 **Q18. Does I&M file a separate corporate income tax return?**

5 No.

6 **Q19. If I&M does not file a separate income tax return, how are the associated**
7 **revenues and expenses of the regulated operations and the assets of the**
8 **Company calculated?**

9 The operations of the Company are separately stated within the schedules of
10 the consolidated return of the AEP Consolidated Group. In addition, the
11 operations and the assets of the Company are maintained with separate books
12 and records and only consolidated for tax and book filing purposes.

13 **Q20. Why is it appropriate to determine income tax expense and ADFIT in the**
14 **Capital Structure using a stand-alone approach?**

15 The stand-alone approach is consistent with ratemaking principles as well as
16 required to comply with the normalization rules of the Internal Revenue Code
17 (IRC) regarding tax benefits of accelerated depreciation. Such rules require
18 consistency among tax expense and the corresponding components of cost of
19 service and the capital structure as a part of determining the WACC.

20 The stand-alone approach ensures that income taxes within the filing represent
21 only those associated with the revenues and expenses of the regulated
22 operations and assets of the Company, without regard to the Company's
23 unregulated activities or the operations of the AEP Consolidated group.

24 As such, income taxes are consistent with the regulated assets reported in the
25 capital structure as a part of determining the WACC and the regulated revenues

1 and expenses included in Cost of Service. The use of a separate entity
2 approach prevents the cross-subsidization among the Company's affiliates.

3 **Q21. You stated the use of a stand-alone approach is necessary to comply with**
4 **the IRC's normalization rules. What is normalized tax accounting?**

5 Normalization is a method of tax accounting in which the taxes reflected within
6 an entity's income statement for a given period are matched with the associated
7 revenues and expenses.

8 This methodology, also known as "deferred income tax" accounting, is required
9 for financial reporting under Generally Accepted Accounting Principles (GAAP)
10 (Financial Accounting Standards Board Accounting Standards Codification
11 Topic 740 ("ASC 740"), formerly Statement of Financial Accounting Standards
12 No. 109).

13 **Q22. Why is normalized tax accounting necessary?**

14 The determination of net income for financial reporting purposes under GAAP
15 differs from the determination of taxable income under the IRC. As a result,
16 revenues and expenses may be reflected in taxable income earlier or later than
17 when such items are reflected within an income statement under GAAP. These
18 "book-to-tax" differences result in a determination of taxes payable for a given
19 period that differs from the amount of financial statement income tax expense.

20 Under a normalized method of tax accounting, the tax liability that would have
21 been payable if determined solely under GAAP principles is merely deferred and
22 not saved permanently. Therefore, financial statement reporting in accordance
23 with GAAP requires a provision for deferred taxes to account for the tax effects
24 temporary book-to-tax differences.

1 **Q23. Can you provide an example of normalized tax accounting?**

2 Yes. As an example, in the early years of an asset's life, accelerated tax
 3 depreciation often exceeds depreciation expense reported in the financial
 4 statements allowing for the deferral of income taxes due to the taxing authority.
 5 In such an instance, the taxes deferred are debited to a deferred tax expense
 6 account with a corresponding credit to a deferred tax liability.

7 In later years, when the book-to-tax difference reverses, the increase in tax due
 8 is mitigated by also reversing the deferred tax liability through a corresponding
 9 credit to deferred income tax expense. *Figure JMC-1* illustrates this point.

Figure JMC-1. Example of Normalized Accounting

	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Revenues	1,000	1,000	1,000	1,000	1,000	5,000
Operating Expenses	(500)	(500)	(500)	(500)	(500)	(2,500)
Book Depreciation	(100)	(100)	(100)	(100)	(100)	(500)
Pre-tax Book Income (PTBI)	400	400	400	400	400	2,000
Tax Depreciation	(250)	(100)	(75)	(50)	(25)	(500)
Federal Taxable Income	250	400	425	450	475	2,000
Federal Current Tax Expense	53	84	89	95	100	420
Federal Deferred Tax Expense	32	-	(5)	(11)	(16)	-
Total Federal Tax Expense	84	84	84	84	84	420
Book/ Tax Depreciation Difference	(150)	-	25	50	75	-
DTA/ (DTL)	(32)	(32)	(26)	(16)	-	

10 Normalization is necessary to maintain inter-generational equity; that is,
 11 customers receive the income tax benefits commensurate with the expenses
 12 reflected in the cost of service.

13 **Q24. What is the alternative to normalized accounting?**

14 The alternative to a normalized method of tax accounting is referred to as "flow
 15 through" accounting. A flow-through approach bases income tax expense
 16 reported within the financial statements on the tax liability as reported on the tax
 17 return as opposed to that determined in accordance with ASC 740. As shown in

1 *Figure JMC-1*, the total amount of income tax expense is the same under both
2 normalized and flow-through approaches – the difference is simply timing.

3 The term “normalization” evolved with respect to utilities, because income taxes
4 computed on a the normalization basis caused net income to appear “normal”,
5 in contrast to an approach based on the cash liability reported on the tax return.

6 **Q25. In addition to GAAP reporting, are there normalization requirements within
7 the IRC?**

8 Yes. The Internal Revenue Code contains provisions requiring utility ratemaking
9 to apply a normalized method of accounting with respect to tax benefits
10 associated with accelerated tax depreciation, NOLCs due to accelerated
11 depreciation, and Investment Tax Credits.

12 **Q26. What are the normalization requirements for accelerated depreciation
13 within the IRC?**

14 The normalization requirements found within IRC Section 168 and former IRC
15 Section 167(l), as well as regulations thereunder, prohibit the direct or indirect
16 flow-through to customers of the tax benefits from accelerated depreciation of
17 rate-regulated utility property.

18 A taxpayer applies a normalized method of tax accounting if the taxpayer:

- 19 1) Determines income tax expense within cost of service using book
20 depreciation expense as opposed to accelerated tax depreciation
21 expense allowed under the IRC;
- 22 2) Establishes a reserve account for the difference in income taxes due as
23 the result of the use of accelerated tax depreciation for purposes of filing
24 its federal income tax return (i.e. income tax deferred);
- 25 3) Maintains such reserve account and only reduces the aggregate reserve
26 to (a) reflect the amount by which federal taxes due are higher as the

1 result of book depreciation exceeding tax depreciation or (b) reflect an
2 asset's retirement; and

3 4) Excludes from rate base (or treats as zero-cost capital) a reserve amount
4 for a period not in excess of the reserve for the period used in
5 determining income tax expense within cost of service (i.e. maintains
6 "consistency" among ratemaking assumptions for elements of rate base,
7 depreciation expense and depreciation-related deferred taxes.

8 The Company follows the above guidelines for applying a normalized method of
9 accounting.

10 **Q27. Why do the normalization provisions of the IRC exist?**

11 The provisions of the IRC providing for accelerated tax depreciation were
12 enacted for the purpose of promoting investment in property and equipment.

13 However, Congress was concerned that, in the case of regulated utilities whose
14 rates for providing service are set by reference to costs (including tax expense),
15 such investment incentives could be extracted from the utility and flowed directly
16 to customers through the rate-setting process.

17 Additionally, were this to occur, Congress had the secondary concern regarding
18 how this would impact the government's taxable revenue base. As a result, the
19 normalization rules were enacted to prevent these instances from occurring.

20 **Q28. Are there consequences of violating the normalization requirements of the**
21 **IRC?**

22 Yes. As a condition for claiming accelerated tax depreciation on a tax return, a
23 utility must comply with the IRC's normalization requirements. If a utility does not
24 comply with the normalization rules applicable to accelerated tax depreciation,
25 the consequence is that the utility loses the ability to claim accelerated tax
26 depreciation for all property subject to the ratemaking jurisdiction of the
27 regulatory body issuing an order inconsistent with normalization.

1 The IRS allows taxpayers to change to a practice or procedure that is consistent
2 with the normalization rules with the taxpayer's next available opportunity before
3 the IRS will assert that a normalization violation has occurred.

4 **Q29. What is a Tax NOLC?**

5 A tax NOLC occurs when, in a given year, a taxpayer has more deductions than
6 taxable revenues, resulting in negative taxable income within its tax return.
7 When a NOLC occurs, the IRC allows the taxpayer to carry the NOLC forward to
8 subsequent years and offset otherwise taxable income produced in that year.

9 **Q30. What might cause a taxpayer to incur a Tax NOLC?**

10 Tax NOLCs are the product of tax return deductions exceeding taxable
11 revenues. Due to the capital-intensive nature of the utility industry, deductions
12 associated with accelerated tax depreciation can lead to tax years in which
13 overall deductions exceed taxable revenues.

14 More specifically, bonus depreciation provisions of the IRC providing for
15 enhanced tax depreciation in the year an asset is placed in service, have
16 resulted in the creation of tax NOLCs for many utilities.

17 **Q31. Is the AEP Consolidated group in a Tax NOLC position for the Test Year?**

18 No.

19 **Q32. Is the Company in a stand-alone Tax NOLC position for the Test Year?**

20 Yes. As the result of accelerated depreciation, on a stand-alone basis, the
21 Company incurred losses in tax years 2009- 2011, 2013, and 2016-2017.

22 As of 12/31/2022, the Company has a forecasted cumulative NOL balance of
23 \$205,672,569 as presented in Attachment JMC-3.

1 **Q33. Do the accelerated depreciation normalization requirements pertain to**
2 **NOLCs resulting from Accelerated Depreciation Deductions?**

3 Yes. Regulations under former IRC Section 167(l) require the amount of tax
4 deferred (and for which a reserve is allowed to be included as a reduction to
5 WACC or treated as zero-cost capital) subject to normalization to be based on a
6 calculation of tax due with accelerated tax depreciation compared to tax due
7 without (“with-and-without” method).

8 In a series of Letter Rulings, the IRS has concluded that in order to avoid a
9 normalization violation, the reserve for deferred taxes for the period used in
10 determining tax expense in cost of service and reflected as a reduction to rate
11 base (or zero-cost capital) must take into account instances in which taxes are
12 not deferred due to accelerated tax depreciation creating a NOL.

13 These rulings further provide that any approach to determining the amount of
14 tax deferral other than a “with-and-without” or “last dollars deducted” method,
15 would violate normalization requirements¹.

16 **Q34. How has the Company reflected the stand-alone NOLC into this filing?**

17 The stand-alone NOLC generated by the Company has been included as a
18 deferred tax asset (DTA), which is a reduction to ADFIT balances included in the
19 capital structure as a component of WACC. This specific adjustment is
20 discussed later in my testimony.

21 **Q35. Did the Company include the stand-alone NOLC as a reduction to the**
22 **ADFIT balances included in the capital structure as a component of WACC**
23 **in previous filings?**

24 No. During the preparation of this case, the Company determined the approved
25 revenue requirement currently includes a reduction to adjusted capital but does

¹ Private Letter Rulings 201436037; 201438003; 201519021; 201534001; 201548017; 201709008.

1 not include the corresponding DTA. Accordingly, the NOLC ADFIT as proposed
2 by the Company is necessary to correct this inconsistency.

3 **Q36. Are there any other adjustments necessary to account for the stand-alone**
4 **NOLC and comply with normalization requirements?**

5 Yes. As discussed in the next section, tax reform legislation known as Tax Cuts
6 and Jobs Act of 2017 (TCJA) was signed into law effective December 22, 2017.
7 The TCJA includes provisions requiring adjustments to ADFIT.

V. Tax Cuts and Jobs Act of 2017 (TCJA)

8 **Q37. What are the most notable provisions of the TCJA having an impact on the**
9 **Company?**

10 The most notable provisions of the Act include:

- 11 • *Corporate Tax Rate* – The TCJA lowered the federal corporate income
12 tax rate to a flat 21 percent rate effective January 1, 2018, whereas under
13 prior law, corporations were subject to a graduated tax rate with a
14 maximum 35 percent rate.
- 15 • *Excess ADFIT* – The reduction in the corporate tax rate gives rise to
16 “excess” ADFIT. Excess ADFIT represents deferred tax expense
17 recovered in customer rates based upon a 35 percent tax rate, which
18 beginning in 2018 will be paid to the IRS based upon the lower 21
19 percent tax rate.
- 20 • *Normalization requirements for property-related excess ADFIT* – The
21 TCJA provides that utilities are not treated as applying normalization if
22 they reduce their excess ADFIT in computing cost of service for
23 ratemaking purposes and for purposes of reflecting operating results in
24 their regulated book of account, more rapidly or to a greater extent than

1 the amount determined using the average rate assumption method
2 (“ARAM”).

- 3 • *Discontinuation of Bonus Depreciation* – Under the TCJA, rate regulated
4 utilities are generally no longer eligible for bonus depreciation after
5 December 31, 2017.

6 **Q38. How did the Company determine its excess ADFIT?**

7 To determine the amount of excess ADFIT, the Company performed a re-
8 measurement of its cumulative ADFIT balances as of December 31, 2017, from
9 values based upon the historical 35 percent tax rate to the 21 percent rate under
10 the TCJA.

11 The Company then segregated excess ADFIT amounts associated with
12 accelerated depreciation related book-to-tax differences into a category referred
13 to as “protected” or “normalized” due to the requirements to normalize under the
14 IRC. Remaining excess ADFIT amounts were classified as “unprotected” or
15 “non-normalized”.

16 **Q39. Could you describe ARAM and how it is applied to protected excess**
17 **ADFIT?**

18 Section 13001(d)(3)(A)(i) of the TCJA requires that protected ADFIT (*i.e.*, those
19 deferred taxes associated with accelerated tax depreciation book-to-tax
20 differences) follow a normalization method of accounting.

21 More specifically, Section 13001 of the TCJA limits the extent to which protected
22 excess ADFIT may be used to reduce the tax expense component of cost of
23 service. This limitation is applied via the use of ARAM, which is a method under
24 which protected excess ADFIT is reduced over the remaining life of the property
25 which gave rise to the deferred taxes.

1 Under ARAM, protected excess ADFIT will be recognized over the life of the
 2 property as the underlying book-to-tax differences reverse, for example, in years
 3 in which the book depreciation of an asset exceeds tax depreciation.

4 **Q40. How are excess ADFIT related amounts reflected in this filing?**

5 As discussed in the next sections, protected excess ADFIT is reflected in this
 6 filing as part of the balances provided to Company Witness Messner for ADFIT
 7 and incorporated into the WACC as well as included in the cost of service.

8 Excess ADFIT amortization for unprotected excess in 2022 of \$15,640,269 is
 9 removed from the cost of service as an adjustment and included in WP-A-
 10 RIDER-4 that I am co-sponsoring with Company Witness Seger-Lawson.

VI. Weighted Average Cost of Capital

11 **Q41. Did you provide the balances of ADFIT and accumulated deferred**
 12 **investment tax credits (ADFITC) used by Company Witness Messner in his**
 13 **Exhibit A-7?**

14 Yes. *Figure JMC-2* identifies the ADFIT and ADFITC balances I calculated in
 15 Schedule 1-5-8(a)(33) and provided to Company Witness Messner.

Figure JMC-2. ADFIT and ADFITC by year

Year	2020	2021	2022
ADFIT	\$941,702,490	\$1,010,598,387	\$1,098,242,295
ADFITC	\$21,260,705	\$17,469,705	\$13,678,705

1 **Q42. What adjustments have been made to ADFIT, as recorded, to arrive at the**
2 **balances shown in Exhibit A-7?**

3 Adjustments made to the ADFIT balance as of 12/31/2022 include the following:
4 (1) adjustments for ratemaking purposes, such as removing ADFIT that does not
5 relate to the IN jurisdiction or that are not related to the provision of electric
6 service; and (2) adjustments related to reducing ADFIT for the NOLC balance.

7 **Q43. Can you discuss the adjustment to ADFIT for the NOLC?**

8 The adjustment of \$159,604,598 is being made to reduce the ADFIT balance for
9 an NOLC calculated on a stand-alone basis for the year ended December 31,
10 2022. The adjustment represents the amount of ADFIT associated with
11 accelerated depreciation that has not been able to produce cash benefits to the
12 Company on the basis of a stand-alone method as of the end of the Test Year.

13 The calculation of the NOLC adjustment can be seen on Attachment JMC-3.
14 This adjustment reflects the ADFIT associated with the taxable losses the
15 Company has generated in excess of the taxable income it has generated and
16 been able to offset based on the NOLC and carryback provisions of the IRC.

17 **Q44. Was a “with-and-without” analysis performed to determine the amount of**
18 **NOL required to be normalized?**

19 Yes. A “with-and-without” calculation is required to determine if an NOL is the
20 result of accelerated depreciation and subject to normalization rules.

21 This calculation was performed to determine the amount of the NOL required to
22 reduce the ADFIT balance. The “with-and-without” calculation determined that
23 all of the \$205,672,569 NOLC is a result of accelerated tax depreciation and
24 therefore subject to the normalization rules as described in my testimony.

1 **Q45. Why is it appropriate to reflect this NOLC as a reduction to ADFIT?**

2 The NOLC balance must be included as a decrease to the ADFIT balance
3 because of the normalization rules discussed earlier in my testimony. The cash
4 benefits from deductions taken for accelerated depreciation should be reflected
5 in the cost of service consistent with the time period such cash benefits would
6 be received by the Company if filing a separate return.

7 The inclusion of the NOLC as a reduction to ADFIT offsets the rate base
8 reduction associated with deferred tax liabilities (DTLs) for accelerated
9 depreciation for which the Company would not yet receive a cash benefit for on
10 a stand-alone basis. This approach results in a neutral impact on rates as
11 compared to a utility operating on a stand-alone basis.

12 **Q46. Can you demonstrate how the inclusion of the NOLC and receipt of cash**
13 **payments via tax sharing results in a neutral impact on rates?**

14 Yes. First I will provide two examples showing the revenue requirement
15 difference between a company that operates on its own with no affiliates versus
16 a company that has affiliates and participates in tax sharing (like I&M and the
17 AEP consolidated group). Then, I will show an example of how including the
18 stand-alone NOLC as a ratemaking adjustment (as I&M proposes here) is
19 necessary to arrive at the same revenue requirement as the first example
20 involving a company with no affiliates.

1 Example 1 – Stand-Alone Company
 2 Starting with a utility that has pre-tax book income (PTBI) of \$10,000 and a
 3 deduction for accelerated tax depreciation of \$11,000. This will result in an NOL
 4 of \$1,000, a DTL of \$2,310 and DTA of \$210.

Figure JMC-3. Example 1 - Stand-Alone Company NOL, DTL, DTA calculation

	Taxable Income		Tax Rate (DTL) / DTA
Pre-Tax Book Income	10,000		
Accelerated Tax Deduction	(11,000)	x	21%
	<u> </u>		<u>(2,310)</u>
Taxable Income (Loss)	(1,000)		
Net Tax Loss Carry Forward	1,000	x	21%
Taxable Income After Net Operating Loss	<u> 0</u>		<u>(2,100)</u>
	<u> 21%</u>		
Current Tax Expense	<u><u> 0</u></u>		

5 Next, assume the utility has a basic capital structure of debt and equity both of
 6 \$100,000. Using a rate of 4% for the debt component, 10% for the equity
 7 component, and 0% for the ADFIT component, this will result in a weighted cost
 8 of capital of 1.98% and 4.95% respectively for the debt and equity for a total
 9 WACC of 6.93%.

Figure JMC-4. Example 1 - Stand-Alone Company Weighted Cost of Capital

	Initial Capital	Ratio	Cost	Weighted Cost
Debt	100,000	49.48%	4.00%	1.98%
Equity	100,000	49.48%	10.00%	4.95%
ADFIT	<u> 2,100</u>	<u> 1.04%</u>	<u> 0.00%</u>	<u> 0.00%</u>
Total	202,100			6.93%

10
 11 The net rate base is composed of plant of \$200,000 and a net ADFIT liability of
 12 \$2,100. When the rate base is multiplied by the WACC of 6.93%, the result is a
 13 revenue requirement of \$14,000.

Figure JMC-5. Example 1 - Stand-Alone Company Revenue Requirement

Plant	202,100
WACC	<u>6.93%</u>
Rev Req	<u>14,000</u>

1

Example 2 – Company Participating in Tax Sharing

2

3 The utility in this next example participates in tax sharing and has received \$210
 4 cash for its NOL. When the utility receives cash, this replaces the debt/equity
 5 otherwise needed to be raised, allowing the ADFIT balance related to
 6 accelerated depreciation only (excluding the NOL) to lower the WACC and lower
 7 the revenue requirement.

Figure JMC-6. Example 2 – Company Tax Sharing

	Initial Capital	Cash Tax Alloc	Adjusted Capital	Ratio	Cost	Weighted Cost
Debt	100,000	(105)	99,895	49.43%	4.00%	1.98%
Equity	100,000	(105)	99,895	49.43%	10.00%	4.94%
ADFIT	<u>2,100</u>	<u>210</u>	<u>2,310</u>	1.14%	0.00%	<u>0.00%</u>
Total	202,100	0	202,100			6.92%

8

9 Because of the receipt of cash, the total need for capital raised from debt and
 10 equity is reduced by the \$210 resulting in a WACC of 6.92%.

11 When the rate base is multiplied by the WACC of 6.92%, the result is a revenue
 12 requirement of \$13,985, a reduction as a result of the consolidated tax
 13 adjustment.

Figure JMC-7. Example 2 – Company Tax Sharing Revenue Requirement

Plant	202,100
WACC	<u>6.92%</u>
Rev Req	<u>13,985</u>

14

15

1 Example 3 – Rate Neutral Impact of NOLC Adjustment

2 As the Company proposes to do in this case, the utility in Example 2 will
 3 maintain rate neutrality by removing the impact to the debt equity requirements
 4 that resulted from the funds received from affiliates as those funds represent a
 5 consolidated tax adjustment. A proforma adjustment representative of the stand-
 6 alone NOLC removes the consolidated tax adjustment, allowing the WACC to
 7 reflect the operations of the utility itself.

Figure JMC-8. Example 3 – Rate Neutral Impact of the Stand-Alone NOLC

	Initial Capital	Cash Tax Alloc	Proforma Tax Alloc	Adjusted Capital	Ratio	Cost	Weighted Cost
Debt	100,000	(105)	105	100,000	49.48%	4.00%	1.98%
Equity	100,000	(105)	105	100,000	49.48%	10.00%	4.95%
ADFIT	2,100	210	(210)	2,100	1.04%	0.00%	0.00%
Total	202,100	0	0	202,100			6.93%

8 When the rate base net of ADFIT is multiplied by the WACC of 6.93%, the result
 9 is a revenue requirement of \$14,000 (the same as Example 1).

Figure JMC-9. Example 3 – Stand-Alone NOLC Revenue Requirement

Plant	202,100
WACC	6.93%
Rev Req	14,000

10 This approach results in the exact same revenue requirement as the first
 11 example in which the utility’s revenue requirement is reflective of the company’s
 12 own operations. This is important because it demonstrates that the Company’s
 13 proposed accounting is revenue neutral and designed to address the
 14 normalization violation by removing any consolidated tax adjustments from rate
 15 base. This ensures that income taxes within this filing represent only those

1 associated with the revenues and expenses of the regulated operations and
2 assets of the Company.

VII. Tax Expense Adjustments

3 **Q47. What Tax Expense Adjustments are you sponsoring?**

4 I am sponsoring ratemaking Tax Expense Adjustment Nos. 1-3, as shown on
5 Exhibit A-5. These adjustments include “pretax” expense adjustments (which
6 are adjustments made to cost of service resulting in a change in tax expense)
7 and “tax only” adjustments (which are adjustments made to tax expense that do
8 not relate to changes in pretax book income).

9 Both types of adjustments are necessary to reflect an adjusted Test Year level
10 of tax expense that is representative of ongoing operations and are consistent
11 with the Company’s prior rate case filings.

12 Exhibit A-5 presents Tax Expense Adjustments Nos. 1-3 on a total Company
13 basis. Company witness Duncan provided the allocation factors that are used to
14 calculate the jurisdictional amounts.

15 **Q48. Please describe Tax Expense Adjustment No. 1.**

16 Tax Expense Adjustment No. 1 increases total Company state income tax
17 expense by \$2,256,608 to reflect the adjustments to state taxable income
18 resulting from the ratemaking adjustments supported by various Company
19 witnesses that affect pre-tax state book income and the related Schedule M
20 adjustments.

21 This adjustment includes all state income tax expense where the Company has
22 a business presence. Consistent with past rate treatment by this Commission,
23 no deferred state income tax expense has been recorded in utility cost of
24 service, consistent with the flow-through methodology.

1 **Q49. Please describe Tax Expense Adjustment No. 2.**

2 Tax Expense Adjustment No. 2 increases total Company CFIT expense by
3 \$9,058,479 to reflect the current federal income tax effect at 21% of the federal
4 taxable income related to the ratemaking adjustments supported by various
5 Company witnesses, which affect pre-tax book income.

6 CFIT expense has been adjusted by I&M's allocated share of the tax benefit of
7 the net interest expense portion of the parent company (American Electric
8 Power Co. Inc.). This methodology is consistent with the Commission's
9 December 22, 1982 Order in Cause No. 36760, the Commission's November
10 12, 1993 Order in Cause No. 39314, and all subsequent I&M rate case orders.
11 I&M-WP-1-8 shows the computation of this amount.

12 **Q50. Please describe Tax Expense Adjustment No. 3.**

13 Tax Expense Adjustment No. 3 increases total Company Deferred Federal
14 Income Taxes (DFIT) by \$29,311,955. This adjustment can be broken down into
15 two parts: to reflect total Company excess amortization including excess related
16 to the stand-alone NOLC and the adjustment for unprotected excess related to
17 the IN jurisdiction.

18 The latter is an adjustment included in WP-A-RIDER-4 in which \$15,640,269 of
19 unprotected excess ADFIT amortization is removed from 2022 test year base
20 rates. This remaining benefit will be credited to customers through a tax rider
21 until unprotected excess ADFIT is fully amortized. The remaining \$13,671,686 is
22 a reduction to total company excess ADFIT to reflect the stand-alone NOLC
23 which is outlined on Attachment JMC-3.

1 **Q51. Does total DFIT expense reflect the amortization and treatment agreed to**
2 **in the settlement agreement approved in Cause No. 44967, for the excess**
3 **protected and unprotected ADFIT?**

4 Yes. The Final Order in Cause No. 44967 provided that the total annual
5 amortization of protected and unprotected excess ADFIT was to equal \$29.9
6 million. To the extent that the actual annual amortization using ARAM differed
7 from the estimated amount in the filing, the amortization of unprotected ADFIT is
8 increased or decreased to equal the \$29.9 million.

9 For test year 2022, amortization of protected excess ADFIT related to Indiana is
10 \$3,132,997. Before the end of the test period, unprotected excess will be fully
11 depreciated and only \$15,640,269 will be amortized through August 2022.

12 The total DFIT expense reflects a \$3,132,997 million credit to Indiana
13 jurisdictional deferred federal income tax expense relative to the amortization of
14 protected excess ADFIT using ARAM.

15 A credit of \$15,640,269 of unprotected excess is removed from cost of service
16 and included in WP-A-RIDER-4 co-sponsored by myself and Company Witness
17 Seger-Lawson to be credited to customers through a tax rider until unprotected
18 excess ADFIT is fully amortized

19 **Q52. Does amortization of protected excess ADFIT related to Indiana include**
20 **amortization of excess related to the NOLC?**

21 Yes. Protected excess amortization related to Indiana has been adjusted to
22 reflect the excess related to the NOLC. Excess related to the NOLC is
23 considered deficient and will offset the excess related to the deferred liability
24 and therefore reduces the total excess benefit presented in the cost of service.

VIII. Gross Revenue Conversion Factor (GRCF)

1 **Q53. Please describe the calculation of the Gross Revenue Conversion Factor**
2 **(GRCF) as shown on Exhibit A-8.**

3 The GRCF calculated on Exhibit A-8 indicates the appropriate factor that should
4 be applied to the income deficiency in order to determine the amount of
5 incremental revenue needed to obtain the required level of operating income.

6 It is necessary to apply this factor to the income deficiency in order to provide
7 sufficient revenues to cover the additional federal and state income tax expense,
8 the Indiana Utility Receipts Tax expense, the public utility assessment fees and
9 uncollectible accounts expense.

IX. Effective Federal Income Tax Rate

10 **Q54. Please describe the calculation of the effective federal income tax rate as**
11 **shown on Exhibit A-9.**

12 Exhibit A-9 calculates the Company's effective federal income tax rate after
13 taking into consideration permanent and flow-through timing differences, excess
14 deferred federal income taxes, and deferred investment tax credit amortization.

15 The overall effective federal income tax rate before rate relief is 16.08% and is
16 calculated by dividing total federal income tax expense by pre-tax electric
17 operating income including interest expense.

X. Future Implications of Federal Statutory Rate Change

18 **Q55. Company witness Seger-Lawson discusses the Company's proposed**
19 **treatment of any subsequent change in the federal statutory tax rate. Have**

1 **you prepared an illustrative calculation of how a hypothetical increase to a**
2 **28% tax rate would impact the Company?**

3 Yes. As discussed by Company witnesses Seger-Lawson, Ross, and Messner,
4 an increase in the federal statutory rate would cause changes to current and
5 deferred federal income tax expense, ADFIT balances, the GRCF, and WACC.

6 Attachment JMC-4 illustrates that, using Test Year data, federal income tax
7 expense, ADFIT, and GRCF would increase assuming a 28% tax rate.

8 **Q56. Does this conclude your pre-filed verified direct testimony?**

9 Yes.

VERIFICATION

I, Jessica M Criss, Tax Accounting and Regulatory Support Manager for American Electric Power Service Corporation, affirm under penalties of perjury that the foregoing representations are true and correct to the best of my knowledge, information and belief.

Date: _____



Digitally signed by Jessica
Criss
Date: 2021.06.16 14:36:32
-04'00'

Jessica M. Criss

INDIANA MICHIGAN POWER COMPANY

Calculation of Effective State Income Tax Rate
Forecast Year Ended December 31, 2022

Line No.	Column A	Column B	Column C
1	State Income Tax Rate - Indiana	4.900%	
2	Apportionment Factor	<u>77.2360%</u>	
3	Effective Indiana State Income Tax Rate		3.7846%
4	State Income Tax Rate - Illinois	9.500%	
5	Apportionment Factor	<u>0.6365%</u>	
6	Effective Illinois State Income Tax Rate		0.0605%
7	State Income Tax Rate - Kentucky	5.000%	
8	Apportionment Factor	<u>1.0927%</u>	
9	Effective Kentucky State Income Tax Rate		0.0546%
10	State Income Tax Rate - Michigan	6.000%	
11	Apportionment Factor	<u>15.3361%</u>	
12	Effective Michigan State Income Tax Rate		0.9202%
13	State Income Tax Rate - West Virginia	6.500%	
14	Apportionment Factor	<u>2.3311%</u>	
15	Effective West Virginia State Income Tax Rate		0.1515%
16	Total Effective State Income Tax Rate		<u><u>4.9714%</u></u>

INDIANA MICHIGAN POWER COMPANY

Calculation of Interest Synchronization for FIT
Test Year Ended December 31, 2022

<u>Line No.</u>	<u>Column A</u>	<u>Total Company</u>	<u>Indiana Jurisdiction</u>
1	Adjusted Original Cost Rate Base	\$ 7,056,724,189	\$ 5,235,969,265
2	Weighted Cost Rate of Long-Term Debt	<u>1.81%</u>	<u>1.81%</u>
3	Synchronized Interest Deduction	<u>\$ 128,030,617</u>	<u>\$ 94,996,539</u>

INDIANA MICHIGAN POWER COMPANY
Calculation of Separate Return NOLC
Forecast Year Ended December 31, 2022

Column A		Column B
Description	FERC Account No.	Total Company
Increase rate base to include the stand-alone Net Operating Loss ("NOL") Deferred Tax Asset ("DTA") and Protected Excess ADIT balance related to the NOL as 12/31/2017, the date of Tax Cuts and Jobs Act ("TCJA"), and decrease Protected Amortization expense due to offsetting protected excess benefit related to the NOL.		
2017 - Pre TCJA		
Entry to reflect Stand Alone NOL as of 12.31.17	2821001	\$ 349,622,011
	Debt/Equity	\$ (349,622,011)
2017 - Post TCJA		
Entry to reflect remeasurements of NOL and corresponding deficient deferred taxes	2544001	\$ 139,848,804
	2824001	\$ (136,171,425)
	2544001	\$ (3,677,379)
	2544001	\$ 48,967,244
	1904001	\$ (48,967,244)
2018 through Forecasted 2022 Activity		
Entry to recognize NOL utilized 2018 through end of test period activity	2821001	\$ (166,581,967)
	Debt/Equity	\$ 166,581,967
Adjustment to Test Year Protected Amortization		
Entry to reflect reduced amortization of Protected Excess for 12 Month Test Period	2544001	\$ (5,914,719)
	4101001	\$ 5,914,719
	2821001	\$ (5,914,719)
	2824001	\$ 5,914,719
	2544001	\$ (2,126,933)
	1904001	\$ 2,126,933
Adjustment to Test Year Unprotected Amortization		
Entry to reflect change in amortization of Unprotected Excess in order to comply with Cause No. 44967 of total excess amortization of \$29.9M. Unprotected EADIT is fully amortized as of August 2021.	2544001	\$ (7,756,966)
	4101001	\$ 7,756,966
	2831001	\$ (7,756,966)
	2834001	\$ 7,756,966
	2544001	\$ (2,789,405)
	1904001	\$ 2,789,405
Adjustment to Pre-Test Year Protected Amortization		
Entry to reflect reduced amortization of Protected Excess for activity in 2018 through Forecasted 2021.	2544001	\$ (17,992,230)
	Debt/Equity	\$ 17,992,230
	2821001	\$ (17,992,230)
	2824001	\$ 17,992,230
	2544001	\$ (6,470,006)
	1904001	\$ 6,470,006
Adjustment to Pre-Test Year Unprotected Amortization		
Entry to reflect increased amortization of Unprotected Excess in order to comply with Cause No. 44967 of total excess amortization of \$29.9M.	2544001	\$ 10,123,159
	Debt/Equity	\$ (10,123,159)
	2831001	\$ 10,123,159
	2834001	\$ (10,123,159)
	2544001	\$ 3,640,288
	1904001	\$ (3,640,288)
Total Company NOLC Forecasted as of 12/31/2022		\$ 205,672,569
Total Company DTA Related to NOLC Forecasted as of 12/31/2022		\$ 43,191,239
Total Adjustment to WACC as of 12/31/2022		\$ 159,604,598

Indiana Michigan Power Company
Calculation of Forecast Test Year at 28% Federal Statutory Rate
Twelve Months Ended December 31, 2022

Line No.	Summary Information	(1) Total Co Electric Utility After Assign & Adjust 12/31/2022		(2) Indiana Jurisdictional Allocated Amount 12/31/2022	
		21%	28%	21%	28%
1	Pre-Tax Book Income before Federal Tax	276,790,888	276,790,888	172,590,373	172,590,373
2	Total Book/Tax Income Differences	(226,658,199)	(226,658,199)	(151,203,550)	(151,203,550)
3	Taxable Income	50,132,690	50,132,690	21,386,823	21,386,823
4	Federal Statutory Rate	21%	28%	21%	28%
5	Tax Before Credits	10,527,865	14,037,153	4,491,233	5,988,311
6	Tax Credits and Adjustments	(61,553)	(28,266)	(965,306)	(965,306)
7	Total Current Federal Tax	10,466,312	14,008,887	3,525,927	5,023,005
8					
9	Total Book/Tax Income Differences	226,658,199	226,658,199	151,203,550	151,203,550
10	Federal Statutory Rate	21%	28%	21%	28%
11	Deferred Income Tax Expense Before Adjustments	47,598,222	63,464,296	31,752,746	42,336,994
12	Flowthrough & Perms	(1,447,904)	(2,399,800)	321,871	83,416
13	Embedded Feedback	(2,689,584)	(2,689,584)	(1,973,290)	(1,973,290)
14	Excess	(16,531,475)	(16,531,475)	(3,132,997)	(3,132,997)
15	Total Deferred Income Tax	26,929,259	41,843,437	26,968,330	37,314,124
16					
17	Total Deferred Investment Tax Credits	(3,790,599)	(3,790,599)	(2,734,312)	(2,734,312)
18					
19	Total Federal Income Tax	33,604,972	52,061,726	27,759,945	39,602,816
20					
21	Total Change in Federal Tax Expense		18,456,754		11,842,871
22					
23	Total Utility Deferred Taxes as of 12/31/2021	(769,851,109)	(1,026,468,145)		
24	Deficient ADFIT as a result of 7% Statutory Rate Increase		256,617,036		
25					
26	GRCF (Exhibit A-8)	1.358	1.490		
27	Change		(0.132)		
28					