

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)
UPPER PENINSULA POWER COMPANY)
for authority to increase retail electric rates.)
_____)

Case No. U-16166

DIRECT TESTIMONY OF

JOHN R. WILDE

FOR

UPPER PENINSULA POWER COMPANY

June 30, 2010

STATE OF MICHIGAN

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**QUALIFICATIONS
OF
JOHN R. WILDE
PART I**

1 **Q. Please state your name, business address and position.**

2 A. My name is John R. Wilde. My business address is Integrys Business Support, LLC
3 (“IBS”), 700 North Adams Street, P.O. Box 19001, Green Bay, WI 54307-9001. I am
4 an Assistant Vice President, and am responsible for various tax issues for Integrys
5 Energy Group, Inc (“Integrys”). Both IBS and Upper Peninsula Power Company
6 (“UPPCO”) are wholly-owned subsidiaries of Integrys.

7

8 **Q. For whom are you providing testimony?**

9 A. I am providing testimony on behalf of UPPCO.

10

11 **Q. Please describe briefly your educational, professional, and utility background.**

12 A. I graduated from Saint Norbert College, DePere, Wisconsin in 1984 with a Bachelor
13 of Business Administration degree in Accounting. I have a graduate certificate in
14 state and local taxation, as well as a Masters Degree in Taxation, from the University
15 of Wisconsin-Milwaukee. I have been employed by Integrys or its predecessors
16 since 1984, and since 1986 I have been employed in the Corporate Tax Department.

17

18

1 **Q. Have you previously testified before any regulatory agency?**

2 A. Yes, I have. I have testified before the Federal Energy Regulatory Commission
3 (“FERC”) and the Public Service Commission of Wisconsin (“PSCW”) on behalf of
4 Wisconsin Public Service Corporation (“WPS Corp”) on various tax and book
5 depreciation matters.

**JOHN R. WILDE
DIRECT TESTIMONY
PART II**

1 **Q. What is the purpose of your pre-filed direct testimony?**

2 A. I am presenting and supporting the change in tax methods of accounting that
3 UPPCO has proposed to the Internal Revenue Service (“IRS”) for 2009 related to the
4 capitalization of repairs and overheads. If allowed these changes will be applicable
5 for UPPCO’s state and federal income tax filings beginning in 2009.

6
7 Further, I discuss proposed claims for additional casualty losses that have been
8 submitted to the IRS.

9
10 Lastly, I present and support UPPCO’s regulatory accounting treatment of the re-
11 measurement of deferred tax balances related to post retirement medical obligations
12 caused by recent changes in tax law, namely the Patient Protection and Affordable
13 Care Act (“PPACA”), and the Health Care and Education Affordability Reconciliation
14 Act of 2010 (“HCEARA”). These acts were signed into law on March 23, 2010 and
15 March 30, 2010, respectively.

16

17 **Q. Are you sponsoring any exhibits in this proceeding?**

18 A. No, I am not.

19

20 **Q. Please describe the change in the capitalization of repairs for tax purposes.**

21 A. Conceptually, the change in the capitalization of repairs for tax purposes is to align
22 the determination of what is a repair or maintenance activity vs. a capital expenditure
23 based on what is allowed for tax purposes as opposed to our historic practice, which
24 generally followed the determination made for financial and regulatory accounting

1 purposes. As a result, certain expenditures that previously would have been
2 considered “capitalized for tax purposes” will now be defined as “operations and
3 maintenance expense for tax purposes.” This will result in a current year tax
4 deduction to adjust the tax basis for the cumulative effect of this change in the tax
5 method of accounting.

6
7 At the same time, determinations of repair and maintenance versus capital will not
8 change for regulatory and financial accounting purposes. This will result in book-to-
9 tax difference (\$5.9 million reflected in this filing) that will result in an increased
10 deferred tax liability (\$2.3 million reflected in this filing) associated with plant in
11 service. This increased deferred tax liability will decrease UPPCO’s capital
12 requirement needs, and lower UPPCO’s revenue requirement.

13
14 **Q. Please describe the change in the capitalization of overheads for tax purposes.**

15 A. Conceptually, the change in the capitalization of overheads for tax purposes
16 redefines what overheads will be allocated to plant and capitalized for tax purposes,
17 and what overheads will be allocated to production costs or expensed for tax
18 purposes. As a result, certain overheads that previously would have been
19 considered “capitalized to plant for tax purposes” will now be defined as “operations
20 and maintenance expense”, or “production costs for tax purposes.” This will result in
21 an increased current year tax deduction to adjust the tax basis for the cumulative
22 effect of this change in the tax method of accounting.

23
24 At the same time, the definition of what overheads will be allocated and capitalized to
25 plant will not change for regulatory and financial accounting purposes. This will
26 result in a book-to-tax difference (\$4.1 million reflected in this filing) that will result in
27 an increased deferred tax liability (\$1.6 million reflected in this filing) associated with

1 plant in service. This increased deferred tax liability will decrease UPPCO's capital
2 requirement needs, and lower UPPCO's revenue requirement.

3

4 **Q. Please describe the proposed claims for additional casualty loss deductions**
5 **that will be taken for tax purposes.**

6 A. UPPCO is entitled to a casualty loss deduction for damages to its facilities caused by
7 various events that are beyond its control to prevent, such as damage caused by
8 extremes in the weather, and damage caused by animals coming into contact with
9 our facilities. UPPCO has engaged an outside tax expert to review its records for
10 UPPCO's open tax years to determine if UPPCO had identified all of its losses. The
11 outside tax expert identified additional tax deductions for casualty losses, for which
12 UPPCO has now filed claims with the IRS.

13

14 **Q. Will these changes benefit UPPCO's customers?**

15 A. Yes, they will, because the changes will increase the balance of UPPCO's deferred
16 income tax liability associated with plant in service. This increased deferred tax
17 liability will decrease UPPCO's capital requirement needs, and lower UPPCO's
18 revenue requirement.

19

20 **Q. Do these changes require approval from the Internal Revenue Service ("IRS")?**

21 A. These changes will be implemented with the consent of the IRS, however, they will
22 also be subject to modification upon examination by the IRS and other taxing
23 authorities. Deloitte & Touche will be assisting UPPCO in the execution of these
24 changes, and to support the resulting proposed tax deductions.

25

26 **Q. Have the changes described above been incorporated in UPPCO's instant rate**
27 **case filing for the 2011 test year?**

1 A. Yes, they have.

2

3 **Q. Have the tax changes described above been implemented at other Integrys**
4 **regulated utilities, and reflected in any of their general rate cases?**

5 A. Yes, they have, as these tax changes are part of a corporate wide initiative that was
6 implemented at all of Integrys' regulated utilities. Currently the only other Integrys
7 utility to include these changes in a general rate case has been WPS Corp, as WPS
8 Corp is the only other Integrys regulated utility to file a general rate case since the
9 implementation of these tax changes.

10

11 **Q. Please describe the re-measurement of deferred tax balances caused by**
12 **enactment of health care reform legislation in 2010.**

13 A. The PPACA, enacted in 2010, requires the amount of the Retiree Drug Subsidy
14 ("RDS") received after December 31, 2012 to be offset against the employer's
15 deduction for health care expenses, thus reducing the associated tax deduction the
16 employer was previously allowed for post-2012 health care expense. That is, the
17 change in tax treatment does not affect the taxation of the RDS itself, but reduces
18 the employer's tax deduction for the cost of health care for retirees by the amount of
19 the RDS received.

20

21 As a result of the PPACA, in 2010, UPPCO must reflect in its deferred tax accounting
22 that portion of UPPCO's expected future actual health care expenditures will not be
23 deductible as a result of the PPACA. Therefore, the non-deductible portion of
24 UPPCO's future health care expenditures will be measured based on the amount of
25 the RDS that UPPCO expects to receive after 2012.

26

27

1 **Q. Please describe UPPCO's proposed regulatory accounting for the re-**
2 **measurement of deferred tax balances caused by enactment of health care**
3 **reform legislation in 2010.**

4 A. Historically, the Commission has required UPPCO to account for a re-measurement
5 of its deferred taxes resulting from unanticipated changes in tax law following the
6 principles of full normalization, and using the average rate assumption method.
7 ("ARAM"). UPPCO proposes to account for this change in tax law, and the resulting
8 effects on its deferred tax balances, following the principles of full normalization and
9 using ARAM. Applying the principles of full normalization and using ARAM would
10 result in the re-measurement of deferred taxes for the change in tax law being offset
11 by a regulatory deferral. Both the resulting deferred tax balance and the offsetting
12 regulatory deferral would be normalized through the provision for income taxes used
13 to determine UPPCO's rates starting in 2013, when the new law takes effect, and
14 continuing over the time period that the accrued benefit expenses for post retirement
15 prescription drug charges are actually incurred.

16

17 **Q. Does UPPCO request Commission approval of UPPCO's proposed regulatory**
18 **accounting for the re-measurement of deferred tax balances caused by**
19 **enactment of health care reform legislation in 2010, as described above?**

20 A. Yes, we do. UPPCO request approval to apply the principles of full normalization
21 using ARAM, and the creation of the associated regulatory deferral, effective on and
22 after the enactment date the PPACA.

23

24 **Q. Does this complete your pre-filed direct testimony at this time?**

25 A. Yes, it does.