



A CMS Energy Company

October 13, 2011

Ms. Mary Jo Kunkle
Executive Secretary
Michigan Public Service Commission
6545 Mercantile Way
P.O. Box 30221
Lansing, MI 48909

Re: Cases No. U-16794, U-16811, U-16820, and U-16864

Dear Ms. Kunkle:

Enclosed are "Joint Comments" which are being submitted by the following electric and gas service providers: Consumers Energy Company, The Detroit Edison Company, Michigan Gas Utilities Corporation, Upper Peninsula Power Company, Wisconsin Public Service Corporation, Michigan Consolidated Gas Company, Wisconsin Electric Power Company, Indiana Michigan Power Company, Northern States Power Company - Wisconsin, SEMCO Energy Gas Company, and Alpena Power Company. These comments are being submitted pursuant to the Michigan Public Service Commission's September 13, 2011 "Notice and Opportunity for Comment" in the listed dockets.

Sincerely,

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STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of CONSUMERS	)	
ENERGY COMPANY for authority to increase its	)	
rates for the generation and distribution of	)	Case No. U-16794
electricity and for other relief.	)	
_____	)	

In the matter of the application of MICHIGAN	)	
GAS UTILITIES CORPORATION for accounting	)	
treatment for the remeasurement of deferred tax	)	
balances caused by enactment of 2010 health care	)	Case No. U-16811
reform legislation.)	)	
_____	)	

In the matter of the application of MICHIGAN	)	
GAS UTILITIES CORPORATION, UPPER	)	
PENINSULA POWER COMPANY, and	)	
WISCONSIN PUBLIC SERVICE	)	Case No. U-16820
CORPORATION for deferred accounting treatment for	)	
the remeasurement of deferred tax balances resulting	)	
from recent revisions to Michigan's tax structure.	)	
_____	)	

In the matter, on the Commission's own motion,	)	
to seek comments from ALPENA POWER	)	
COMPANY, CONSUMERS ENERGY	)	
COMPANY, THE DETROIT EDISON	)	
COMPANY, INDIANA MICHIGAN POWER	)	
COMPANY, NORTHERN STATES POWER	)	
COMPANY – WISCONSIN, UPPER PENINSULA	)	Case No. U-16864
POWER COMPANY, WISCONSIN PUBLIC	)	
SERVICE CORPORATION, WISCONSIN	)	
ELECTRIC POWER COMPANY, MICHIGAN	)	
GAS UTILITIES CORPORATION, SEMCO	)	
ENERGY GAS COMPANY, and MICHIGAN	)	
CONSOLIDATED GAS COMPANY for	)	
deferred accounting treatment for the	)	
remeasurement of deferred tax balances resulting	)	
from recent revisions to Michigan's tax structure.	)	
_____	)	

**ELECTRIC AND GAS UTILITY SERVICE
PROVIDERS' JOINT COMMENTS**

A. Introduction

On September 13, 2011, the Michigan Public Service Commission issued a Notice and Opportunity for Comment (“Notice”) in the above-entitled cases. The Notice solicits comments regarding the accounting treatment for the remeasurement of deferred tax balances arising out of certain changes in federal tax law enacted by The Patient Protection and Affordable Care Act (“PPACA”) in 2010, and the changes to Michigan business tax laws, enacted by the Michigan Corporate Income Tax (“MCIT”) Act in 2011. The Notice further stated:

“The Commission wants all utilities to account for these changes by using the same accounting treatment for these issues. Therefore, the Commission is soliciting comments regarding what accounting treatment is best in each situation.”

These joint comments are submitted by the following electric and gas service providers: Consumers Energy Company, The Detroit Edison Company, Michigan Gas Utilities Corporation, Upper Peninsula Power Company, Wisconsin Public Service Corporation, Michigan Consolidated Gas Company, Wisconsin Electric Power Company, Indiana Michigan Power Company, Northern States Power Company - Wisconsin, SEMCO Energy Gas Company, and Alpena Power Company (collectively, the “Providers”). Although participating in these joint comments, one or more of the Providers may choose also to offer separate additional comments.

The Providers appreciate the opportunity to submit these written comments to address the Commission’s desire that all utilities use the same treatment to account for the remeasurement of

deferred taxes resulting from tax law changes enacted by the PPACA and the new MCIT. The Providers believe that they are using or proposing to use substantially the same or similar accounting treatment for these issues, and that, although certain differences, as noted below, may exist, the requests made in Case Nos. U-16794, U-16811 and U-16820 use substantially consistent accounting treatment in conformance with appropriate accounting guidance and previous Commission orders. The Providers therefore seek to explain the accounting and regulatory principles that apply when accounting for the deferred tax effects of tax law changes.

The basic principles generally covered in these comments include:

1. Deferral of changes in deferred taxes caused by changes in tax law through establishment of a regulatory asset or liability;
2. Full normalization of deferred taxes based on long-standing regulatory policy; and
3. Amortization of the deferred income statement effects of the change in law, reflected in the regulatory asset or liability, over a period of time that reasonably approximates the reversal of the actual book-tax basis differences underlying the deferred taxes.

Differences that may exist in accounting treatment among the Providers primarily relate to the method by which each Provider proposes to amortize the effect of these tax law changes based on each Provider's specific facts and circumstances. Therefore, these differences will only impact the timing of when the deferral is reversed, as will be discussed later in more detail.

B. Accounting Principles Governing Changes in Tax Law or Rates

Financial Accounting Standards Board Accounting Standards Codification 740 ("ASC 740"), formerly Statement of Financial Accounting Standards No. 109 ("FAS 109") states, "Deferred tax liabilities and assets shall be adjusted for the effect of a change in tax laws or rates

(ASC 740-10-35-4).” The deferred income tax effects of the change in tax laws or rates are required to be recorded in the period of enactment as either income tax expense or benefit (ASC 740-10-45-15) or as a regulatory asset or liability for regulated entities applying the principles of ASC 980 (ASC 980-740-25-2), formerly Accounting for the Effects of Certain Types of Regulation (FAS 71), with recovery from or refund to customers in the future authorized by the regulator.

C. Regulatory Policy for Accounting for Deferred Income Taxes

In response to implementation of FAS 109 in 1993, the Commission in its February 8, 1993 Order in Case No. U-10083 set forth the following income tax policy for ratemaking and accounting purposes:

1. Implemented comprehensive deferred income tax accounting as the preferred method of accounting for ratemaking purposes.
2. Provided general authorization to prospectively use deferred income tax accounting.
3. Provided regulatory asset/deferred cost authority for book-tax temporary differences as of the date of implementation to offset the recognition of any additional deferred tax liabilities. This authorization was necessary to comply with FAS 109 requirements and allow temporary differences that previously flowed through net income to continue to flow through when the temporary differences reverse.
4. Provided assurance of continued recovery of regulatory assets/deferred costs and continued refunding of regulatory liabilities related to FAS 109 through current ratemaking practices.

This Commission policy of comprehensive deferred income tax accounting has been reaffirmed implicitly by Commission orders in numerous subsequent general ratemaking and accounting cases, and expressly in other Commission orders, including orders affirming the application of this policy with respect to the enactment of the Michigan Business Tax (“MBT”) to replace the Michigan Single Business Tax.¹ This long-standing consistently applied policy conforms to generally accepted accounting principles, results in fair and reasonable ratemaking, is widely used in other utility rate-making jurisdictions, avoids unintended windfalls or detriments caused solely by the enactment of tax law changes, and should continue to be affirmed by the Commission.

D. Applying the Accounting and Regulatory Guidance to the Tax Law Changes

Both the PPACA and the MCIT eliminate a future tax benefit (i.e., a net deferred tax asset) that previously existed. In both cases, the previously expected future tax benefit had been deferred in accordance with the Commission’s comprehensive deferred income tax accounting policy. Similarly, the repeal of these future tax benefits as discussed below should be accounted for in accordance with the Commission’s comprehensive deferred income tax accounting policy, which would result in changes to the previous deferrals.

Prior to federal health care reform, the Medicare Part D subsidies for prescription drug benefits that companies expected to receive in the future were treated as a tax-free subsidy from the federal government. The PPACA and the related Health Care and Education Reconciliation

¹ See for example Case Nos. U-15645 and U-15986 (Consumers Energy Company), U-15244 (Detroit Edison Company), U-15985 (Michigan Consolidated Gas Company) and U-16169 (SEMCO Energy Gas Company).

Act (the “Health Care Acts”) passed by Congress and signed into law by President Obama in March 2010 effectively eliminated this tax benefit by eliminating the deductibility of future retiree health payments to the extent of Medicare Part D subsidies received after December 31, 2012. Thus, the change in tax treatment did not affect the taxability of the Medicare Part D subsidy itself, but instead reduced the employer’s tax deduction starting in 2013 by the amount of subsidy received. The future tax deductions relating to retiree health payments were previously accounted for as a deferred tax asset since the obligation for retiree health payments is deductible for tax purposes when paid. As a result of this loss of future tax deductions, the Providers were required to decrease their deferred tax assets in accordance with ASC 740. In conformance with the Commission’s income tax policy, this decrease in deferred tax assets was offset by an equal increase in regulatory assets.

Similarly, Michigan enacted a significant change in tax law in 2011. On May 25, 2011 Governor Rick Snyder signed a number of tax bills into law, eliminating the MBT and creating the MCIT. Notably, the law change eliminated certain future tax deductions (sometimes referred to as the “FAS 109 Deductions”) that would have been available under the MBT beginning in 2015. The FAS 109 Deductions would have effectively offset increased future taxes resulting from the taxpayer’s book-tax basis differences that existed when the MBT was enacted. The MCIT replaces the MBT effective January 1, 2012. The MCIT imposes a 6% income tax while the predecessor MBT comprised a 4.95% tax on income, a 0.8% tax on gross receipts, and a surcharge. The MCIT is considered a state income tax, as was the MBT, and therefore also is subject to accounting for income taxes under ASC 740. As such, the same requirements for financial statement accounting of deferred income taxes apply to the MCIT as applied to the

MBT. In accordance with ASC 740 and Commission income tax policy, the Providers were required to remeasure deferred tax assets and liabilities that had already been established upon enactment of the MBT to reflect the impact of the new MCIT tax rate and the elimination of the FAS 109 Deductions. In addition, the Providers remeasured the regulatory assets and liabilities established upon enactment of the MBT, primarily related to the loss of the FAS 109 Deductions.

E. Amortization Methods Available For Deferred Net Income Effects of a Change in Tax Law

As stated previously, ASC 980 directs regulated entities with assurance of future recovery to defer the net income effects of the change in tax laws or rates in the period of enactment by offsetting the remeasurement of the deferred income tax accounts with regulatory assets or regulatory liabilities. As also noted, since 1993, the Commission has applied a consistent policy of comprehensive income tax normalization with assurance of continued recovery of regulatory assets/deferred costs and continued refunding of regulatory liabilities. The remaining issue, however, is the specific method by which the income tax regulatory assets or liabilities should be recognized through the income statement in future periods for accounting and ratemaking purposes.

As is generally well-understood, the deferred taxes and related regulatory assets or regulatory liabilities associated with most temporary differences reverse when the underlying book-tax basis differences have been reflected in both the income statement for financial reporting purposes, and the tax return filed for tax reporting purposes. For example, if an item is expensed for book accounting purposes in year one, but can't be deducted on the tax return until year two, the deferred taxes booked in year one will reverse and be recognized through the income statement when the item is deducted on the tax return in the following year. However,

although infrequent in occurrence, it should be noted that not all deferred taxes have an underlying book-tax basis difference and may instead be established based upon a specified provision prescribed by law. In this situation, the deferred tax and related regulatory asset or liability will reverse over the period prescribed by the specific provision in the law.

When a remeasurement of deferred taxes is required by a tax law change, however, determining how much of the deferred taxes resulting from that change reverses in each subsequent tax year is not straightforward. Accordingly, the Providers propose that a method of amortization (or “reversal”) of the regulatory tax assets or liabilities resulting from a tax law change is acceptable if it occurs over a period reasonably related to the reversal of the underlying book-tax basis differences. The Providers recommend, however, that some flexibility in precise methodology and period continue to be permitted based upon each Provider’s specific facts and circumstances, consistent with historical practices, provided that each Provider apply its method consistently. Permitting flexibility of amortization methodology takes into account factual differences among the Providers, such as the average remaining service lives of employees or utility plant, the detailed way historical accounting records have been maintained, the software systems used, and the record-keeping needs of multi-state utility operations. Further, variations in annual amortization amounts are unlikely to be particularly material among the various amortization alternatives and will only affect the timing of when the regulatory asset or liability reverses.

A situation analogous to these recent tax law changes arising from the Health Care Acts and MCIT occurred with enactment of the Tax Reform Act of 1986 (“TRA 1986”).² TRA 1986 reduced federal corporate income tax rates from 46 percent to 34 percent. As a result, the deferred federal income tax liabilities of most utilities were reduced. The bulk of deferred tax liabilities related to book and tax basis differences of property, plant and equipment. In order to assure an orderly recognition in utility ratemaking of the effect of the tax rate reduction, Congress included a special rule in TRA 1986 in Section 203(e) that set forth the Average Rate Assumption Method (“ARAM”), as the normalization requirement for excess deferred federal income taxes of public utilities resulting from the reduction in federal corporate income tax rates. The ARAM method basically reverses the change to deferred taxes by amortizing the change over the period in which the underlying book-tax basis differences specifically reverse. This requires an annual determination of the specific book-tax basis differences that reverse and usually results in different amortization amounts each year.

An alternative method, the Reverse South Georgia Method (“RSGM”) has also been permitted by the Internal Revenue Service (“IRS”). The RSGM basically reverses the change to deferred taxes by using a weighted average life to approximate the period when the book-tax basis differences reverse and applying the weighted average life to amortize the change on a straight line basis. This method is often used as a practical alternative when the utility does not

2 The Commission addressed the effect of TRA 1986 in its June 30, 1987 Order in Case No. U-8638 and related utility specific cases (e.g., U-8680 and U-8681 (Consumers Energy), U-8683 (Detroit Edison), and U-8684 (Michigan Consolidated Gas Company)).

have detailed data to determine when the timing differences related to plant will specifically reverse. Unlike ARAM, this method results in the same amortization amount each year.

It should be noted that both the ARAM and RSGM methods for reversal of deferred income tax reserves are required under federal tax law only with respect to normalization accounting for plant temporary differences that were required to be normalized under Section 167 or 168 of the Internal Revenue Code. Federal tax law does not require that a particular method be used for the reversal of deferred state income taxes arising from the enactment of the MCIT or deferred federal income taxes arising from the enactment of the Health Care Acts, which apply to both plant and non-plant book-tax basis differences. In this situation, more flexibility exists for choice of amortization methods with respect to the amortization of the regulatory asset or liability resulting from these changes, provided the method reasonably approximates the reversal of the actual book-tax basis differences.

The straight line method has been a practical alternative to the ARAM or RSGM for amortizing the regulatory asset or liability. Amortization on a straight line basis over a period reasonably related to the reversal of the underlying book-tax basis differences results in amortization of the deferred income statement effects of each law change in a manner similar to the RSGM.

With respect to the MCIT, a method that determines the amortization period using the weighted average remaining service life of the Provider's depreciable plant would be a reasonable method since the majority of a utility's book tax basis differences relate to plant. For example, a 20 year amortization period may be a reasonable approximation of the remaining average service life of a Provider's depreciable plant. With respect to the Health Care Acts,

straight line amortization over the projected weighted average remaining working life of the Provider's covered workforce could be such a reasonable method. This is the approach generally followed by the Providers' independent actuaries in determining the liabilities and expenses associated with the Providers' retiree health care plans, and meets the goal of reflecting this increased tax cost over the period in which covered employees will continue to provide services.

For some Providers, it is impractical to use ARAM or RSGM due to their complexity and practical constraints relative to determining the amount of regulatory assets or liabilities being reversed in the future. Use of a straight line method may be the most practical alternative since the straight line method provides a simple, fair and administratively efficient way of amortizing these regulatory assets and liabilities and provides predictability of future amounts amortized each year. Accordingly, the Provider's propose to use ARAM, RSGM or straight line methods to account for the deferred income statement effect of these tax law changes, consistent with methods used in the past and accepted by the Commission.

F. Conclusion

The Providers respectfully request that the Commission consider these comments, affirm application of long-standing Commission income tax policy of full normalization as established in Case No. U-10083, and approve the following treatment for the remeasurement of deferred taxes resulting from tax law changes related to the Health Care Acts and MCIT:

1. Deferral of the net income statement effects caused by the changes in tax law through the establishment of a regulatory asset or liability in accordance with ASC 740, ASC 980 and the Commission's order in Case No. U-10083.

2. Full normalization of the deferred tax effects of the changes in tax law on a prospective basis in accordance with the Commission's order in Case No. U-10083.
3. Reversal of the deferred income statement effects of the change in law over a period reasonably related to the reversal of the underlying book-tax basis differences, using ARAM, RSGM, straight line or, if applicable, the period prescribed by law.

Respectfully submitted,

CONSUMERS ENERGY COMPANY

THE DETROIT EDISON COMPANY

MICHIGAN CONSOLIDATED GAS COMPANY

MICHIGAN GAS UTILITIES CORPORATION

UPPER PENINSULA POWER COMPANY

WISCONSIN PUBLIC SERVICE CORPORATION

ALPENA POWER COMPANY

INDIANA MICHIGAN POWER COMPANY

NORTHERN STATES POWER COMPANY – WISCONSIN

WISCONSIN ELECTRIC POWER COMPANY

SEMCO ENERGY GAS COMPANY

Dated: October 13, 2011