

PUC DOCKET NO. 58964

BEFORE THE PUBLIC UTILITY COMMISSION OF TEXAS

**APPLICATION OF
TEXAS-NEW MEXICO POWER COMPANY
FOR AUTHORITY TO CHANGE RATES**

**PREPARED DIRECT TESTIMONY AND EXHIBITS
OF
LARRY T. MORRIS**

**ON BEHALF OF
TEXAS-NEW MEXICO POWER COMPANY**

NOVEMBER 14, 2025

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1 **I. INTRODUCTION AND QUALIFICATIONS**

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS**

3 A. My name is Larry T. Morris. My business address is 414 Silver Avenue SW,
4 Albuquerque, New Mexico 87102.

5 **Q. PLEASE STATE YOUR EMPLOYER AND POSITION THEREIN.**

6 A. I am Director of Tax for TXNM Energy, Inc. (“TXNM Energy”) and Subsidiaries. I
7 am employed by PNMR Services Company (“PNMR Services”), a wholly owned
8 subsidiary of TXNM Energy.

9 **Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND**
10 **BUSINESS EXPERIENCE.**

11 A. My educational and professional background is outlined in Exhibit LTM-1

12 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE ANY REGULATORY**
13 **COMMISSION?**

14 A. Yes, I have provided testimony before the Public Utility Commission of Texas and
15 the New Mexico Public Regulation Commission. Please see Exhibit LTM-1 for a
16 list of my previous experience in regulatory proceedings.

17 **Q. PLEASE DESCRIBE YOUR AREAS OF RESPONSIBILITY AS DIRECTOR OF**
18 **TAX.**

19 A. I am responsible for managing the tax department and its functions, which include
20 the preparation and filing of all tax returns, all tax accounting for both internal and
21 external purposes, all tax planning, and managing all federal and state tax audits.
22 The only exception is payroll taxes, which are managed by the payroll group. I
23 provide support for the payroll group as requested for technical payroll tax matters
24 and responses to inquiries from tax authorities. These services are provided for
25 TXNM Energy and all its affiliated companies, including Texas-New Mexico Power
26 Company (“TNMP” or “Company”).

27 **II. PURPOSE AND OVERVIEW OF TESTIMONY**

28 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

1 A. I will present the tax schedules and tax amounts included in the cost of service and
2 rate base. Specifically, I will discuss:

- 3 • Federal income tax expense and Accumulated Deferred Federal Income
4 Taxes (“ADFIT”) included in the cost of service.
- 5 • Pro forma adjustments to income taxes.
- 6 • Accounting Standards Codification Topic 740 (“ASC 740”), *Income Taxes*,
7 as well as ASC 980, *Regulated Operations*, which together incorporate the
8 former Statement of Financial Accounting Standards No. 109 (“SFAS 109”).
- 9 • Adjustments to the SFAS 109 regulatory liability included on schedule II-B-
10 11.
- 11 • Texas franchise (margin) tax included on schedule II-E-2.
- 12 • Excess ADFIT.
- 13 • Tax Department expenses.

14 **Q. WHAT EXHIBITS ARE INCLUDED WITH YOUR TESTIMONY?**

15 A. Exhibit LTM-1 summarizes my educational and professional background.

16 **Q. WHAT RFP SCHEDULES DO YOU SPONSOR?**

17 A. I sponsor the II-E-3 schedules related to federal income tax treatment. I co-
18 sponsor certain II-E-2 schedules with TNMP witness Kyle Sanders. I also co-
19 sponsor Schedule V-K.

20 **Q. WERE THE SCHEDULES AND EXHIBITS PREPARED BY YOU OR UNDER
21 YOUR DIRECTION AND SUPERVISION?**

22 A. Yes, they were. The information presented there is true and correct to the best of
23 my knowledge and belief.

24 **Q. WHAT IS THE SOURCE OF THE INFORMATION USED IN THE SCHEDULES?**

25 A. The source of the income tax amounts included in the schedules is the books and
26 records of the Company as of June 30, 2025.

1 **III. INCOME TAXES AND ADFIT IN THE COST OF SERVICE**

2 **1. Federal Income Tax Expense and ADFIT**

3 **Q. HOW WAS THE FEDERAL INCOME TAX EXPENSE INCLUDED IN THE COST**
4 **OF SERVICE CALCULATED?**

5 A. The federal income tax expense included in the cost of service has been calculated
6 using the return method. This calculation is presented in Schedule II-E-3.

7 **Q. PLEASE DESCRIBE THE RETURN METHOD.**

8 A. The calculation of federal income tax expense on Schedule II-E-3 is known as the
9 return method because it uses the after-tax return on rate base as the starting point
10 for the calculation of federal income tax expense. Federal income tax expense is
11 calculated on total return on rate base, first reduced by synchronized interest
12 expense, and then adjusted for permanent book/tax differences and temporary
13 book/tax differences for which the current benefit are flowed through to customers.
14 These differences include amortization of excess ADFIT resulting from prior tax
15 rate changes, the current period's equity portion of Allowances for Funds Used
16 During Construction ("AFUDC Equity"), depreciation on prior years' AFUDC Equity,
17 lobbying expenses, fines and penalties, and 50% of meals and entertainment
18 expenses. Income tax expense calculated using this method is total income tax
19 expense. The method does not differentiate between the current and deferred
20 components of income tax expense.

21 **Q. ON WHAT BASIS DOES THE RETURN METHOD CALCULATE FEDERAL**
22 **INCOME TAX EXPENSE?**

23 A. The return method calculates federal income tax expense on a stand-alone basis.

24 **Q. PLEASE ELABORATE ON THE STAND-ALONE BASIS.**

25 A. The stand-alone basis for the calculation of income taxes means that such taxes
26 are calculated only on the revenues and expenses included in the revenue
27 requirement of the utility. It excludes both the revenues and expense of affiliated
28 companies. It also excludes any unregulated revenues and expenses incurred by
29 the utility. The income tax expense resulting from these excluded sources of
30 income and expense is borne by shareholders.

1 **Q. WHY IS THE STAND-ALONE METHOD THE CORRECT METHOD OF**
2 **DETERMINING THE INCOME TAX EXPENSE TO BE INCLUDED IN THE COST**
3 **OF SERVICE CALCULATION?**

4 A. The stand-alone methodology ensures that rates are determined based solely on
5 the income and expense generated by the regulated electric utility operations. The
6 tax effects of the unregulated activities of TNMP and other affiliated non-utility
7 companies are excluded. Just as with other expenses, the stand-alone
8 methodology ensures that electric rate-payers pay for only the expenses relating
9 to electric operations, and are not charged for costs associated with other
10 unregulated or non-utility operations. The stand-alone method prevents cross-
11 subsidization between the regulated electric utility and other activities and entities
12 included in the consolidated group.

13 **Q. PLEASE DESCRIBE THE CALCULATION OF FEDERAL INCOME TAX**
14 **EXPENSE ON SCHEDULE II-E-3.**

15 A. Schedule II-E-3 provides the calculation of total federal income tax expense
16 utilizing the return method for the test year on a stand-alone basis. The calculation
17 begins with Return on Rate Base, then adjusts for deductions and additions to
18 arrive at the Taxable Component of Return. The tax factor, which is the statutory
19 federal tax rate for the test period plus a gross-up for the tax-on-tax, is applied to
20 the Taxable Component of Return to arrive at the Federal Income Taxes Before
21 Adjustment. Tax credits and other adjustments are then applied to compute Total
22 Federal Income Taxes.

23 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.1.**

24 A. Schedule II-E-3.1 provides a reconciliation of book income to taxable income for
25 the test year and for the most recent filed federal income tax return, which was for
26 the year ended December 31, 2024.

27 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.2.**

28 A. Schedule II-E-3.2 provides a list of items which produce an effective federal
29 income tax rate which differs from the federal statutory rate of 21% These items
30 include AFUDC Equity and the depreciation adjustment resulting therefrom,

1 lobbying, the amortization of excess ADFIT, fines and penalties, the limitation on
2 deductibility of meals and entertainment expenses, and the expense for corporate
3 owned life insurance. The amounts shown on this schedule represent the tax
4 effect of those items.

5 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.3.**

6 A. Schedule II-E-3.3 provides the tax in-service date, tax basis, tax depreciation
7 method, tax depreciation expense for the test year and for the two subsequent
8 years (projected) for assets placed in service since the last-filed TNMP rate case.
9 TNMP's last filed rate case used a test year ended December 31, 2017. Additions
10 after 2017 have been included in this schedule. Additionally, TNMP's fixed asset
11 records do not include accumulated book depreciation by vintage. Therefore,
12 ADFIT by vintage cannot be calculated and is not included in this schedule.

13 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.4.**

14 A. Schedule II-E-3.4 discusses the agreement which governs inter-company income
15 tax allocations among the members of the TXNM Energy consolidated group.

16 **Q. PLEASE DESCRIBE SCHEDULES II-E-3.5, II-E-3.6, AND II-E-3.7.**

17 A. Schedule II-E-3.5 presents the specific ADFIT balances making up the total ADFIT
18 included in rate base on Schedule II-B-7. Schedule II-E-3.6 provides descriptions
19 for each temporary book/tax difference giving rise to the ADFIT included on
20 Schedule II-E-3.5. Schedule II-E-3.7 provides a description of all pro-forma
21 adjustments to the ADFIT included on Schedule II-E-3.5. These adjustments will
22 be discussed later in this testimony.

23 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.8.**

24 A. Schedule II-E-3.8 refers to Schedule II-E-3.3 regarding ADFIT and investment tax
25 credits ("ITC") on assets placed in service since TNMP's last filed rate case.
26 TNMP's fixed asset records do not include accumulated book depreciation by
27 vintage. Therefore, ADFIT by vintage cannot be calculated and is not included in
28 this schedule.

29 **Q. PLEASE DESCRIBE SCHEDULES II-E-3.9 THROUGH II-E-3.14.**

1 A. Schedule II-E-3.9 presents an analysis of ITC included in the cost of service.
2 TNMP has fully amortized all of its ITC prior to the test period. Therefore, no ITC
3 amortization is included in this filing. Schedule II-E-3.10 provides detail regarding
4 ITC generated and used for tax return purposes. Schedule II-E-3.11 discusses
5 ITC generated but not utilized. Schedule II-E-3.12 mirrors the information provided
6 in Schedule II-E-3.10, but on a stand-alone basis. Schedule II-E-3.13 provides all
7 elections made by TNMP with regard to ITC. Schedule II-E-3.14 shows the test
8 year balance of unamortized ITC in FERC account 255. TNMP has no unamortized
9 ITC in the test period.

10 **Q. PLEASE DESCRIBE SCHEDULES II-E-3.15 AND II-E-3.16.**

11 A. Schedule II-E-3.15 calculates federal income tax expense included in the cost of
12 service using Tax Method 2. This method calculates federal income tax expense
13 based on the revenues and expenses included in the cost of service, rather than
14 based on return, as in Schedule II-E-3. Tax Method 2 also calculates current
15 federal income tax expense and deferred federal income tax expense, the two
16 components of the total income tax expense calculated on Schedule II-E-3. The
17 two methods in Schedules II-E-3 and II-E-3.15 each result in the same total federal
18 income tax expense. Schedule II-E-3.16 provides the detail behind the calculation
19 of deferred federal income tax expense on Schedule II-E-3.15.

20 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.17.**

21 A. Schedule II-E-3.17 provides information regarding additional depreciation
22 deductions to be included in the calculation of federal income tax expense.

23 **Q. PLEASE DESCRIBE SCHEDULES II-E-3.18 AND II-E-3.19.**

24 A. Schedule II-E-3.18 presents the amortization of protected and unprotected excess
25 deferred federal income taxes and the amortization method, including excess
26 deferred federal income taxes resulting from the Tax Cuts and Jobs Act of 2017.

27 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.20.**

28 A. Schedule II-E-3.20 details the effects on federal income tax expense and ADFIT
29 of any post-test year adjustments to plant.

30 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.21.**

1 A. Schedule II-E-3.21 provides a list of all testimony presented in this case regarding
2 federal income tax expense and ADFIT.

3 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.22.**

4 A. Schedule II-E-3.22 discusses the normalization policy and history of the utility. A
5 detailed normalization history for TNMP is not available.

6 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.23.**

7 A. Schedule II-E-3.23 lists all federal income tax elections and Private Letter Ruling
8 requests since TNMP's last filed rate case. It also provides TNMP's IRS audit
9 status.

10 **Q. PLEASE DESCRIBE SCHEDULE II-E-3.24.**

11 A. Schedule II-E-3.24 provides TNMP's accounting method for deferred Net
12 Operation Loss ("NOL") carryforwards.

13 **2. Pro Forma Adjustments to Income Taxes**

14 **Q. WHAT PRO FORMA ADJUSTMENTS TO INCOME TAX AMOUNTS ARE
15 INCLUDED IN TNMP'S COST OF SERVICE?**

16 A. I describe below a series of adjustments affecting recoverable federal income tax
17 expense in the test year, adjustments to temporary book/tax differences affecting
18 the deferred component of federal income tax expense in the test year, and
19 adjustments to ADFIT included in rate base in the test year.

20 **3. Adjustments Affecting Federal Income Tax Expense**

21 **Q. PLEASE DISCUSS THE ADJUSTMENT TO MEALS AND ENTERTAINMENT
22 EXPENSE.**

23 A. Meals and entertainment expense was adjusted to reflect deductible meals in the
24 test period. This adjustment is shown on Schedules II-E-3, II-3.2, II-E-3.15, and II-
25 E-3.18.

26 **Q. PLEASE DISCUSS THE ADJUSTMENT OF NON-DEDUCTIBLE MEALS AND
27 ENTERTAINMENT EXPENSES, AND ELIMINATION OF FINES AND
28 PENALTIES, AND LOBBYING EXPENSE.**

1 A. For tax purposes, 50% of meals and entertainment expenses are considered non-
2 deductible. In the cost of service, meal expenses (WP/II-D-1.1) were reduced to
3 reflect the 50% limitation. Additionally, 100% of fines and penalties and lobbying
4 expenses are considered non-deductible. No fines, penalties, or lobbying
5 expenses are included in recoverable expenses. Therefore, there should be no
6 add-back of such expenses in the tax calculation. These adjustments are shown
7 on Schedules II-E-3, II-E-3.2, and II-E-3.15. They are also reflected in Schedule
8 II-E-3.1.

9 **4. Adjustments to Temporary Book / Tax Differences**

10 **Q. PLEASE DISCUSS THE ADJUSTMENT TO THE TEMPORARY DIFFERENCE**
11 **FOR DEPRECIATION.**

12 A. The temporary difference between book and tax depreciation is adjusted to reflect
13 the change to book depreciation expense in the test year (Schedule II-E-1, line 72)
14 which is non-deductible for tax. This adjustment is shown on Schedule II-E-3.15.
15 It is also reflected in Schedules II-E-3.1 and II-E-3.16.

16 **Q. PLEASE DISCUSS THE ELIMINATION OF THE TEMPORARY DIFFERENCE**
17 **FOR CONTRIBUTIONS IN AID OF CONSTRUCTION (“CIAC”).**

18 A. CIAC is taxable when received. For book purposes, CIAC reduces the depreciable
19 basis in the underlying assets. TNMP charges a tax gross-up to customers paying
20 CIAC, in order to compensate the Company for the time value of money related to
21 the income tax prepayment thereon. Because the customer is directly charged
22 this gross-up, the CIAC temporary difference is eliminated from the cost of service.
23 This adjustment is shown on Schedule II-E-3.15. It is also reflected in Schedules
24 II-E-3.1 and II-E-3.16..

25 **Q. PLEASE DISCUSS THE TEMPORARY DIFFERENCE FOR TAX REPAIRS.**

26 A. Certain repairs and maintenance expenditures are deductible for income tax
27 purposes, but are capitalized for book accounting purposes. A temporary
28 difference is included in the test year for these deductible amounts. This amount
29 is shown on Schedule II-E-3.15. It is also reflected in Schedules II-E-3.1 and II-E-
30 3.16.

1 **Q. PLEASE DISCUSS THE TEMPORARY DIFFERENCE FOR GENERAL**
2 **RESERVE.**

3 A. Expense accruals for reserves of future expected expenses are generally non-
4 deductible for tax purposes. An accounting adjustment was made to increase
5 expenses for general liabilities for book purposes. This expense would be non-
6 deductible for tax. Therefore, a temporary difference is included in the test year
7 for this item. This adjustment is shown on Schedule II-E-3.15. It is also reflected
8 in Schedules II-E-3.1 and II-E-3.16.

9 **Q. PLEASE DISCUSS THE TEMPORARY DIFFERENCE FOR TRANSMISSION**
10 **COST RECOVERY FACTOR.**

11 A. The decrease in the regulatory asset for Transmission Cost Recovery Factor is
12 non-deductible for tax purposes. An adjustment was made to increase taxable
13 income for the decrease in the regulatory asset during the test period. Therefore,
14 a temporary difference is included in the test year for this item. This adjustment is
15 shown on Schedule II-E-3.15. It is also reflected in Schedules II-E-3.1 and II-E-
16 3.16.

17 **Q. PLEASE DISCUSS THE ADDITION OF A TEMPORARY DIFFERENCE FOR**
18 **HURRICANE BERYL COSTS.**

19 A. Costs related to storm damage are deductible for tax purposes when the costs are
20 incurred. For book purposes, the costs were accumulated in an asset account.
21 An adjustment was made to reduce taxable income for the deductible Hurricane
22 Beryl costs during the test period. Therefore, a temporary difference is included in
23 the test year for this item. This adjustment is shown on Schedule II-E-3.15. It is
24 also reflected in Schedules II-E-3.1 and II-E-3.16.

25 **5. Adjustments to ADFIT included in Rate Base**

26 **Q. PLEASE SUMMARIZE THE ADJUSTMENTS TO ADFIT SHOWN ON**
27 **SCHEDULES II-E-3.5.**

28 A. Briefly, the adjustments fall into several categories. First, certain ADFIT balances
29 are eliminated in the test year because the underlying asset or liability is not
30 included in rate base in the test year. These ADFIT items are:

- 1 Compensation Expense
- 2 Stock Compensation
- 3 Transaction Costs

4 In addition, the ADFIT account for CIAC was eliminated in the test year. As
5 discussed above, TNMP charges a tax gross-up to customers paying CIAC, in
6 order to compensate the Company for the time value of money related to the
7 income tax prepayment thereon. Therefore, the associated ADFIT asset should
8 not be included in the rate base.

9 **IV. ASC 740 – ACCOUNTING FOR INCOME TAXES**

10 **Q. PLEASE DISCUSS ASC 740.**

11 A. Accounting Standards Codification Topic 740 (“ASC 740”), *Income Taxes*, is the
12 pronouncement that governs the accounting requirements for income taxes under
13 GAAP. It incorporates the former Statement of Financial Accounting Standards
14 109 (“SFAS 109”). It requires the recording of income taxes payable (or
15 receivable) during the current year, as well as deferred tax liabilities and assets for
16 the future tax consequences of events that have been recognized in an entity’s
17 financial statements or tax returns. The deferred tax liabilities and assets result
18 from differences between a company’s book income and taxable income, which
19 are temporary in nature, and will reverse over time.

20 **Q. IS THE TAX ACCOUNTING OF REGULATED ENTERPRISES SPECIFICALLY**
21 **ADDRESSED IN THE ACCOUNTING STANDARDS CODIFICATION?**

22 A. Yes, it is. In addition to the general principles included in ASC 740, ASC 980,
23 *Regulated Operations*, provides that:

24 A deferred tax liability must be recognized for both temporary tax benefits
25 that have been flowed through to rate-payers, and the equity component of
26 AFUDC.

27 A deferred tax asset or liability must be established for any change in tax
28 laws or tax rates.

1 If the tax effect of the above items will be recovered or returned to rate-payers
2 through rates, then a regulatory asset or liability is recorded to reflect that future
3 revenue or expense pursuant to ASC 980-740-25-2. This regulatory asset or
4 liability is also a temporary difference for which deferred taxes must be recognized
5 (i.e., it must be grossed-up for tax).

6 **Q. WHAT IS THE NET EFFECT OF ASC 740 ON THE COST OF SERVICE**
7 **CALCULATION?**

8 A. The recording of the deferred taxes and the regulatory assets and liabilities related
9 to the above paragraph of ASC 980 have no effect on the revenue requirement of
10 the regulated enterprise, as long both the deferred taxes and the SFAS 109
11 regulatory assets and liabilities are included in rate base.

12 **Q. ARE THERE OTHER TAX-RELATED ITEMS FOR WHICH A REGULATORY**
13 **ASSET OR LIABILITY HAS BEEN INCLUDED IN THE COST OF SERVICE?**

14 A. Yes. The most recent prior TNMP rate case provided that, "TNMP shall track both the
15 plant-related and non-plant-related excess ADFIT amortization and preserve any excess
16 or deficiency in the return of excess ADFIT in a regulatory liability or asset, respectively.
17 [PUC Docket No. 48401 Stipulation and Settlement Agreement – 4].

18 **Q. HAS TNMP TRACKED THE EXCESS ADFIT AMORTIZATION AND PRESERVED ANY**
19 **EXCESS OR DEFICIENCY IN A REGULATORY LIABILITY OR ASSET?**

20 A. Yes. TNMP has tracked the excess ADFIT amortization and has preserved the cumulative
21 over-return to customers in a regulatory asset.

22 **Q. WHAT IS THE AMOUNT OF THE CUMULATIVE EXCESS OVER-RETURN AS OF THE**
23 **END OF THE TEST PERIOD?**

24 A. As of the end of the test period, the regulatory asset for the over return of excess ADFIT
25 was \$10,884,347.

26 **Q. HOW DOES TNMP PROPOSE TO COLLECT THE REGULATORY ASSET FOR THE**
27 **OVER-RETURN OF EXCESS ADFIT?**

28 A. TNMP proposes to collect the over-return of excess ADFIT over a period of five years

29 **V. TEXAS FRANCHISE (MARGIN) TAX**

30 **Q. CAN YOU EXPLAIN THE TEXAS MARGIN TAX?**

1 A. The Texas Franchise Tax is levied on entities that are located in Texas or do
2 business in Texas. In 2006, the Texas Legislature re-structured the Franchise
3 Tax. The restructured Franchise Tax is often referred to as the Margin Tax, to
4 distinguish it from the pre-2006 Franchise Tax. Generally, the Margin Tax is levied
5 on total revenues less the greater of (1) cost of goods sold, (2) employee
6 compensation, or (3) 30% of the aforementioned revenues. For TNMP, 30% of
7 revenues yields the largest deduction, and is most beneficial to both the Company
8 and its customers.

9 **Q. HOW IS TEXAS FRANCHISE (MARGIN) TAX CALCULATED ON SCHEDULE**
10 **II-E-2?**

11 A. The tax included in the test year cost of service is calculated based on the current
12 law. The tax calculation is shown on WP/II-E-2.5.

13 **VI. TAX DEPARTMENT AFFILIATE EXPENSES**

14 **Q. WHAT AFFILIATE EXPENSES ARE YOU DISCUSSING?**

15 A. I am discussing Tax Department costs, including payroll taxes, and indirect effects.

16 **Q. WHAT IS INCLUDED IN THIS SECTION OF YOUR TESTIMONY?**

17 A. This section of my testimony includes the following:

18 **Tax Department Costs:** This section describes the organization of the Tax
19 Department and the services it provides to TNMP and other companies. It
20 provides an overview of the department’s cost levels and trends as well as
21 an explanation of the allocation of its costs. This section also explains the
22 necessity and reasonableness of the department’s services and associated
23 costs. It also summarizes how the Tax Department employs budgeting and
24 cost control processes to manage and limit costs.

25 **Payroll Taxes and Indirect Effects:** These costs are included in the below
26 explanation of Tax Department costs.

27 **1. Organization of the Tax Department**

28 **Q. PLEASE SUMMARIZE THE TAX FUNCTION.**

29 A. The Tax Department is responsible for ensuring that TXNM Energy and its affiliates
30 comply with all governmental, accounting, and regulatory rules and regulations
31 related to taxes while minimizing their respective tax liabilities.

1 **Q. PLEASE PROVIDE AN OVERVIEW OF HOW THE TAX DEPARTMENT IS**
2 **ORGANIZED.**

3 A. Currently, the Tax Department consists of nine employees who report to the
4 Director, Tax, who reports to the TXNM Energy Vice President & Controller.

5 **Q. PLEASE DESCRIBE ANY INITIATIVES THAT HAVE BEEN INTRODUCED IN**
6 **RECENT YEARS TO PROVIDE FOR ORGANIZATIONAL FLEXIBILITY AND**
7 **OPTIMAL SERVICE DELIVERY.**

8 A. Since the prior test period, the Tax Department has efficiently performed its
9 compliance and tax planning roles. While TNMP's assets and revenues have
10 increased by 143% and 74% respectively since 2017, the Tax Department has
11 added only one employee (a 13% increase in headcount), indicating efficiencies
12 have been gained to maintain service levels with a disproportionately small
13 increase to labor.

14 **2. Services Provided by the Tax Department**

15 **Q. PLEASE DESCRIBE THE SERVICES FOR WHICH THE TAX DEPARTMENT IS**
16 **RESPONSIBLE.**

17 A. The Tax Department is responsible for processes and activities specific to
18 federal, state and local tax compliance and reporting. These activities involve
19 preparing and filing tax returns, making tax payments, accounting for taxes for
20 both internal and external purposes, performing tax research, designing tax
21 plans, evaluating tax effects of actual and proposed transactions, and managing
22 tax exams and audits.

23 **Q. WHAT IS THE PROCESS OR FORUM TO SET AND EVALUATE SERVICE**
24 **LEVELS AND PROVISIONS?**

25 A. Because tax compliance is mandated by laws and regulations, the provision of
26 services is largely dictated by legal requirements. The processes to set and
27 evaluate service levels and provisions include meetings with senior management
28 and managers in the affiliated companies to discuss service needs and levels.
29 PNMR Services uses General Services Agreements ("GSA") to document terms
30 and provisions of services provided by PNMR Services to the affiliated companies.

1 Senior management from PNMR Services as well as the affiliated companies
2 signed off on the General Services Agreements.

3 **Q. HOW DO THE AFFILIATED COMPANIES OBTAIN TAX DEPARTMENT**
4 **SERVICES?**

5 A. The Tax Department continually performs general tax activities to meet company
6 tax obligations, which benefit the entire TXNM Energy organization and affiliated
7 companies. The Tax Department staff also coordinates with affiliated company
8 managers about their specific Tax Department needs on an informal and ad-hoc
9 basis. Additionally, affiliated company managers may also request special projects
10 that would require Tax Department services. Such services are outlined in the
11 GSAs mentioned above. The GSAs provide transparency to the cost of Tax
12 Department services.

13 **3. Cost Levels and Cost Trends**

14 **Q. WHAT IS THE TOTAL TAX DEPARTMENT COST IN THE TEST YEAR?**

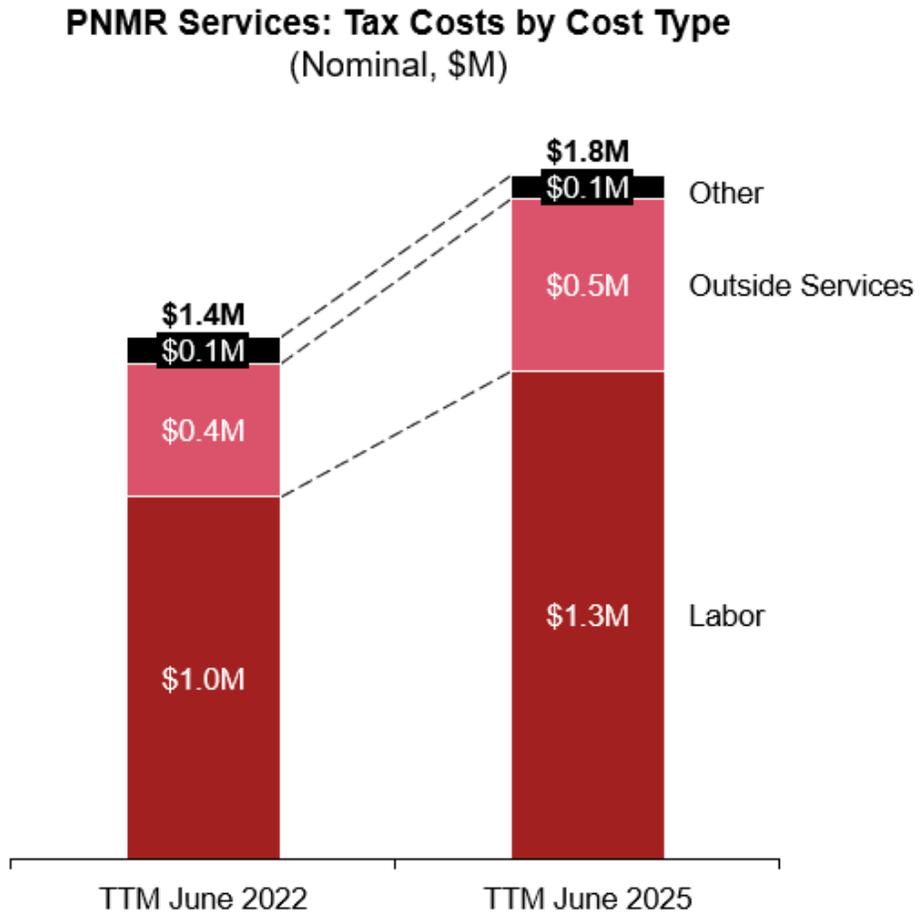
15 A. The total test year Tax Department costs for TXNM Energy and its affiliated
16 companies was \$1.8 million.

17 **Q. WHAT HAS BEEN THE TREND IN TAX DEPARTMENT COSTS IN RECENT**
18 **YEARS?**

19 A. From 2022 to the test year, Tax Department costs increased by \$0.4 million from
20 \$1.4 million to \$1.8 million.

1
2

TABLE 1: TOTAL TAX DEPARTMENT COSTS BY COST TYPE



Notes: 1. Other includes Employee Expense, Tax, Postage Expenses, Insurance Premiums and Other Expenses
 Source: PNMR Billings to Affiliates, Strategy& Analysis

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Q. WHAT ARE THE TOTAL TAX DEPARTMENT COSTS CHARGED TO TNMP IN THE TEST YEAR?

A. The total Tax Department costs allocated to TNMP during the test year was \$0.7 million.

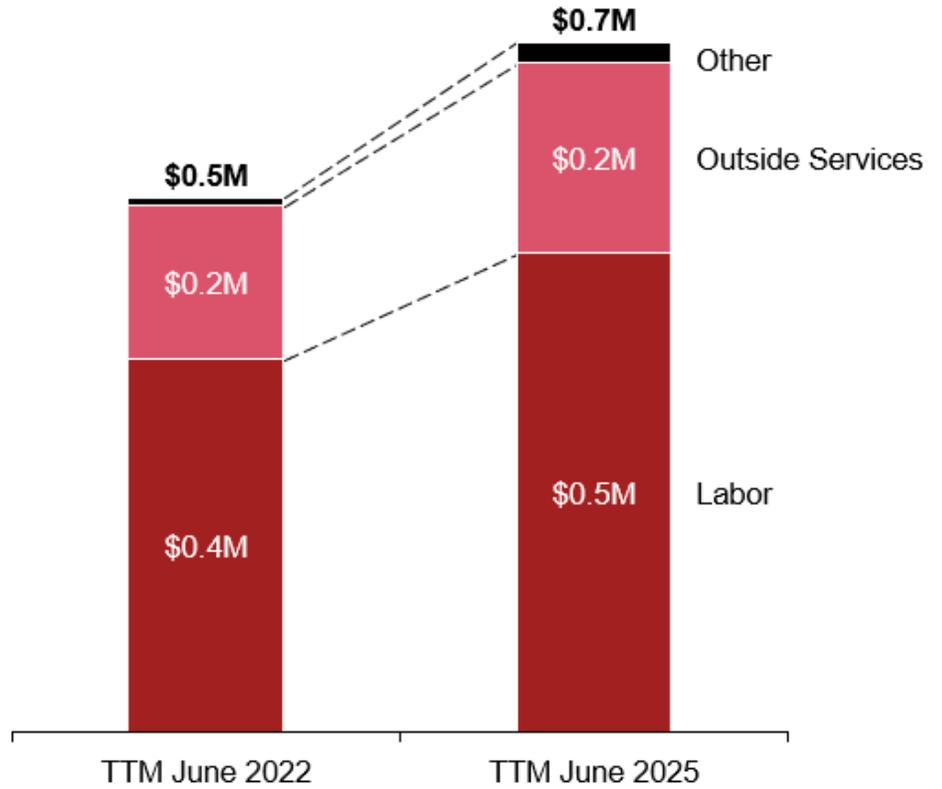
Q. WHAT HAS BEEN THE TREND IN COSTS BILLED TO TNMP BY THE TAX DEPARTMENT IN RECENT YEARS?

A. Tax Department costs billed to TNMP have increased by \$0.2 million, from \$0.5 million to \$0.7 million, between TTM 2022 and the test year. Tables 2 and 3 below show TNMP billings between TTM June 2022 and the test year broken down by cost type and sub-category.

1
2

TABLE 2: TAX DEPARTMENT COSTS BY COST TYPES – TNMP ALLOCATION

TNMP Allocations: Tax Costs by Cost Type
(Nominal, \$M)

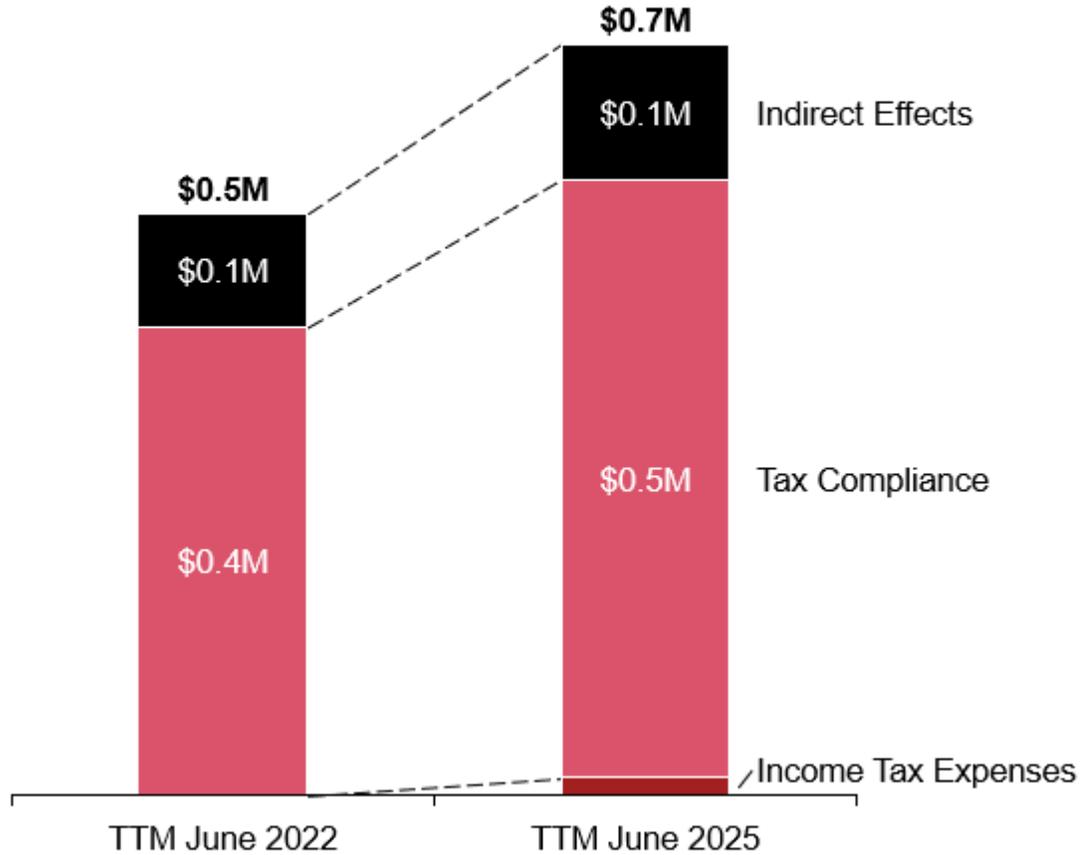


3

Notes: 1. Other includes Employee Expense, Tax, Postage Expenses and Other Expenses
Source: PNMR Billings to Affiliates, Strategy& Analysis

1 **TABLE 3: TAX COSTS BY SUB-CATEGORY – TNMP ALLOCATION**

TNMP Allocations: Tax Costs by Sub-Category
(Nominal, \$M)



2

3 **Q. ARE THE CHANGES IN THE COSTS PREVIOUSLY DESCRIBED**
 4 **REASONABLE?**

5 A. The changes previously described are reasonable. Overall Tax Department costs
 6 have increased consistently with TNMP's growth.

7 **4. Cost Allocation**

8 **Q. WHAT ARE THE PREDOMINANT BILLING METHODS USED FOR TAX**
 9 **DEPARTMENT COSTS?**

10 A. As indicated in the figure below, the predominant billing method for Tax
 11 Department costs is the Transactional Allocation. This allocation method is used
 12 for costs that cannot be directly charged. This method uses a formula based on

1 the volume of transactions for each company to allocate charges to multiple
 2 entities. The allocation method is used for time and expenses that are not specific
 3 to any one organization or do not involve corporate matters.

4 Direct charging is used for Tax Department costs that benefit a single business
 5 unit. This cost allocation method is primarily used for the time and expenses of Tax
 6 Department work for non-utility corporate matters or work that can be specifically
 7 tied to a single business unit. It ensures that costs are allocated to the appropriate
 8 companies.

9 Table 4 below presents a detailed breakdown of allocation factors used by the Tax
 10 Department in the test year.

11 **TABLE 4: TAX DEPARTMENT COSTS BY BILLING METHOD – TEST YEAR**

Allocation Method@	Location	Allocation Driver	PNMR Allocations	TNMP Allocations
General	941	MMF - Employee Headcount, Gross Margin, Net Plant.	2.6%	2.3%
Direct	953	TNMP - Texas	1.3%	3.5%
Transactional	911	Number of General Ledger Transactions	95.9%	94.0%
	993	Employee Headcount	0.2%	0.2%

13

14 **Q. PLEASE EXPLAIN THE RATIONALE AND IMPORTANCE OF THE BILLING**
 15 **METHODS USED.**

16 A. The billing methods used are based on the nature of the activities performed and
 17 the beneficiaries. Compliance with federal, state and local tax requirements, tax
 18 accounting, and general tax planning, are performed on a consolidated basis, for
 19 the benefit of all companies. Specific initiatives that benefit a single company are
 20 billed directly to the benefiting company.

21 **Q. TO WHICH COMPANIES ARE TAX DEPARTMENT COSTS BILLED, AND HOW**
 22 **ARE THOSE COSTS BILLED?**

23 A. The Tax Department bills to the companies it serves. The Tax Department
 24 currently bills to PNM, TNMP and TXNM Energy. Each entity is billed for its direct
 25 costs and an allocated share of the PNMR Services costs according to the cost
 26 allocation manual.

1 **Q. WHAT PERCENTAGE OF TAX DEPARTMENT COSTS WAS DIRECTLY**
2 **BILLED AND WHAT PERCENTAGE WAS ALLOCATED TO THE AFFILIATED**
3 **COMPANIES?**

4 A. In the test year, approximately 1.3% of Tax Department costs were directly billed,
5 approximately 2.6% was allocated under the general allocation method, and 96.1%
6 was allocated via the transactional method. Of the Tax Department costs billed to
7 TNMP, approximately 3.5% was directly billed, 94.2% was allocated under the
8 transactional method, and 2.3% was generally allocated.

9 **Q. WHAT IS YOUR OVERALL CONCLUSION WITH RESPECT TO THE**
10 **APPROPRIATENESS OF THE COST ALLOCATIONS AND BILLING METHODS**
11 **USED FOR TAX DEPARTMENT COSTS?**

12 A. The cost allocations and billing methods used by the Tax Department are
13 appropriate in the allocation of costs necessary to provide reliable electrical
14 services to TNMP rate-payers. Positive time keeping is required and direct billing
15 is utilized to the extent practicable.

16 **5. Necessity and Reasonableness of Services**

17 **Q. ARE THE SERVICES PROVIDED BY THE TAX DEPARTMENT NECESSARY**
18 **TO SUPPORT THE BUSINESS OF THE AFFILIATED COMPANIES?**

19 A. Yes, the services provided by the Tax Department are necessary to ensure
20 compliance with federal, state, and local tax laws. These services minimize the
21 companies' tax exposure and thereby reduce financial risk.

22 **Q. WHAT CORPORATE OVERSIGHT EXISTS TO ENSURE THAT TAX**
23 **DEPARTMENT SERVICES ARE THOSE THAT ARE THE MOST BENEFICIAL**
24 **FOR THE SUPPORT OF THE AFFILIATED COMPANIES' UTILITY SERVICE?**

25 A. To ensure that the services provided by the Tax Department are the most
26 beneficial to supporting the affiliated companies, affiliated company managers
27 coordinate with the Tax Department on an as-needed basis for specific projects or
28 IRS audits.

29 **Q. IN ANY INSTANCE, ARE TAX DEPARTMENT SERVICES DUPLICATED BY**
30 **PERSONNEL OUTSIDE OF THE TAX DEPARTMENT?**

1 A. There are no Tax Department services duplicated by other employees outside the
2 Tax Department. The services provided by the Tax Department require
3 specialized tax expertise and software that employees in other departments do not
4 provide.

5 **Q. DO ANY OTHER DEPARTMENTS HAVE THE CAPABILITY TO PROVIDE THE**
6 **SERVICES CURRENTLY PROVIDED BY THE TAX DEPARTMENT?**

7 A. There are no other departments that have the capability to provide such services.
8 Other departments lack the human and capital resources to offer the same
9 services.

10 **Q. IS IT NECESSARY AND REASONABLE FOR THESE ACTIVITIES TO BE**
11 **PROVIDED BY AN AFFILIATE (AS OPPOSED TO WITHIN EACH AFFILIATED**
12 **COMPANY)?**

13 A. Yes, PNMR Services provides services that are necessary for the operation of
14 more than one company. The Tax Department provides services to TXNM Energy,
15 benefiting all affiliated companies, as well as to the individual affiliated companies.
16 Common services that are shared among affiliated companies can be provided
17 more efficiently on a consolidated basis than if they were performed separately
18 within multiple affiliated companies. Centralization also minimizes the potential for
19 duplication of resources and efforts among the affiliated companies.

20 **Q. IN SUMMARY, ARE THE SERVICES THAT THE TAX DEPARTMENT**
21 **PERFORMS NECESSARY TO PROVIDE RELIABLE ELECTRIC SERVICE TO**
22 **TNMP'S RATE-PAYERS?**

23 A. Yes, the services that the Tax Department performs are necessary to minimize tax
24 exposure as well as reduce legal and financial risks.

25 **Q. WHAT SYSTEMS ARE IN PLACE TO ENSURE THAT TNMP IS NOT CHARGED**
26 **A HIGHER PRICE FOR SERVICES DELIVERED BY THE TAX DEPARTMENT**
27 **THAN OTHER SUBSIDIARIES OF TXNM ENERGY?**

28 A. The accounting system at TXNM Energy is configured whereby PNMR Services'
29 actual costs are allocated. No mark up or additional calculations are systematically

1 applied to costs. The costs are simply assigned to affiliates using the allocation
2 methodology associated with the location code applied to the costs.

3 **6. Cost Management**

4 **Q. WHAT PROCESSES ARE IN PLACE TO ENSURE THAT TAX DEPARTMENT**
5 **EXPENSES INCURRED ON BEHALF OF THE AFFILIATED COMPANY ARE**
6 **REASONABLE?**

7 A. There are three primary activities performed to ensure that Tax Department
8 expenses incurred on behalf of the affiliated companies are reasonable. First,
9 PNMR Services performs monthly budget variance reviews. The monthly report
10 provides detailed information about PNMR Services charges and provides
11 transparency to the service charges. Budget variances are reviewed monthly by
12 the Corporate Controller and the individual departments. At the monthly review
13 meetings, budget variances are examined and discussed. If necessary,
14 adjustments to the current budget are proposed to ensure reasonable budget
15 targets. In addition, a monthly budget variance report is submitted to the affiliated
16 companies. The report shows detail by service company function and line items
17 charges. Thus, the affiliated company managers may review the Tax Department
18 costs, and have the opportunity to contest any costs they believe have been
19 inappropriately allocated.

20 Finally, the Tax Department utilizes direct charging when it performs special
21 projects for specific affiliated companies. This practice allows the department to
22 accurately track and charge its costs to the appropriate benefiting location.

23 **Q. DISCUSS HOW THE TAX DEPARTMENT EMPLOYS BUDGETING, PLANNING,**
24 **COST REVIEW AND REPORTING TO CONTROL ITS CHARGES TO THE**
25 **AFFILIATED COMPANIES.**

26 A. The Tax Department follows the standard PNMR Services budgeting process.
27 During the third quarter, the department develops an annual budget by month for
28 Operations and Maintenance (“O&M”) using the O&M targets developed in the
29 budgeting process. The detailed budget is created at the home center level by cost
30 type. Once the budget is established, the Tax Department tracks actual cost levels

1 and makes appropriate adjustments to control its charges through monthly budget
2 variance reviews.

3 **Q. WHAT TYPES OF CONTROLS ARE IN PLACE WITHIN THE TAX**
4 **DEPARTMENT TO ENSURE THAT COSTS ARE EFFECTIVELY**
5 **CONTROLLED?**

6 A. Tax Department costs are controlled in three ways. First, the Tax Department and
7 the accounting department perform monthly budget variance reviews to ensure
8 reasonableness of costs. The accounting department investigates material
9 variances. Second, billing reports are submitted to the affiliated companies on a
10 monthly basis. The reports show Tax Department costs billed to the affiliated
11 companies. The business unit managers review the billing reports to identify any
12 inappropriate charges.

13 **Q. HAVE THE BUDGETING AND COST CONTROL METHODS BEEN**
14 **EFFECTIVE?**

15 A. Yes, the budgeting and cost control methods described above have been effective
16 in controlling costs.

17 **Q. WHAT ARE THE RAMIFICATIONS OF DEVIATIONS FROM THE BUDGET?**

18 A. TXNM Energy's short-term incentives program links incentive pay to workgroup
19 O&M budget targets. Cost control is an essential part of performance scorecards
20 for the overall Chief Financial Officer's organization as well as the Tax Department.
21 If scorecard targets are not met, incentive pay is not received by employees,
22 according to plan. Performance against the scorecard goals impacts the manager
23 and employee's total incentive pay. Therefore, the Tax Department must carefully
24 monitor its budget in order for its staff to be eligible for incentive pay.

25 **Q. WHAT IS YOUR OVERALL CONCLUSION ON THE REASONABLENESS AND**
26 **NECESSITY OF COST MANAGEMENT PRACTICES FOR TAX DEPARTMENT**
27 **COSTS?**

28 A. The Tax Department's cost control practices are reasonable and necessary for
29 reliable operations of the company. The major costs controls include conducting
30 monthly budget variance reviews by PNMR Services and the affiliated Companies

1 as well as linking the budget targets in the performance scorecard for incentive
2 compensation.

3 **VII. CONCLUSION**

4 **Q. PLEASE SUMMARIZE YOUR CONCLUSIONS.**

5 A. Schedules II-E-3 through II-E-3.26, relating to federal income taxes, are in
6 compliance with the prescribed Rate Filing Package and are in accordance with
7 the substantive rules of the Commission. All adjustments to ADFIT, regulatory
8 assets, and tax expense are reasonable and appropriate. The tax expenses
9 included in the cost of service are reasonable and necessary. TNMP proposes to
10 track both the plant-related and non-plant-related excess ADFIT amortization and
11 preserve any excess or deficiency in the return of excess ADFIT in a regulatory
12 liability or regulatory asset.

13 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

14 A. Yes.

LARRY T. MORRIS, CPA

EDUCATIONAL AND PROFESSIONAL SUMMARY

Employment:

PNMR Services Company:

Director of Tax, 2017-Present
Senior Manager, Tax, 2007-2017

Standard Insurance Company:

Senior Tax Analyst, 2005-2006

Meyners + Company, LLC:

Tax Manager, 2001-2004

Hoffman, Stewart & Schmidt, PC:

Senior Tax Accountant, 1999-2000

Meyners + Company, LLC:

Tax Accountant/Senior Tax Accountant, 1996-1999

Education:

Bachelor of Business Administration, Accounting:

University of New Mexico, 1996

Continuing Professional Education:

Tax and Accounting CPE as required by the New Mexico and Oregon State Boards of Public Accountancy, 1999-Present

Certifications:

Certified Public Accountant

New Mexico, 1999-Present
Oregon (Inactive), 1999-Present

Affiliations:

American Institute of CPAs

Member, 1999-Present
Tax Section, 2017-Present

Edison Electric Institute

Taxation Committee, 2017-Present

Testimony in Regulatory Proceedings:

Nature of Proceeding	Regulatory Body	Docket Number
In the Matter of the Application of Texas-New Mexico Power Company for Authority to Change Rates.	PUCT	48401
In the Matter of the Application of Public Service Company of New Mexico for Revision of its Retail Electric Rates pursuant to Advice Notice No. 595.	NMPRC	24-00089-UT
In the Matter of the Application of Public Service Company of New Mexico for Revision of its Retail Electric Rates pursuant to Advice Notice No. 595.	NMPRC	22-00270-UT
In the Matter of Public Service Company of New Mexico's Application for approval of its Renewable Energy Act Plan for 2022 and Proposed 2022 Rider Rate under Rate Rider No. 36.	NMPRC	21-00143-UT

APPLICATION OF TEXAS-NEW MEXICO POWER COMPANY
FOR AUTHORITY TO CHANGE RATES

WORKPAPERS FOR
THE DIRECT TESTIMONY OF
LARRY T. MORRIS

TNMP Witness Larry T. Morris has no supporting workpapers for his direct testimony.