

ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

[Handwritten signature]
SD4
JLG

[Handwritten signature]

APPLICATION OF DUKE ENERGY INDIANA,)
INC. FOR APPROVAL OF A CHANGE IN ITS)
FUEL COST ADJUSTMENT FOR ELECTRIC)
SERVICE, FOR APPROVAL OF A CHANGE IN)
ITS FUEL COST ADJUSTMENT FOR HIGH)
PRESSURE STEAM SERVICE, AND TO UPDATE)
MONTHLY BENCHMARKS FOR CALCULATION)
OF PURCHASED POWER COSTS IN)
ACCORDANCE WITH INDIANA CODE § 8-1-2-42,)
INDIANA CODE § 8-1-2-42.3 AND VARIOUS)
ORDERS OF THE INDIANA UTILITY)
REGULATORY COMMISSION.)

CAUSE NO. 38707 FAC 80

APPROVED: JUN 30 2009

BY THE COMMISSION:

David E. Ziegner, Commissioner
Loraine L. Seyfried, Administrative Law Judge

On April 29, 2009, pursuant to Ind. Code §§ 8-1-2-42 and 8-1-2-42.3, and various Orders of the Indiana Utility Regulatory Commission ("Commission"), Duke Energy Indiana, Inc. ("Duke Energy Indiana", "Company" or "Petitioner") filed with the Commission its Verified Application for approval of a change in its fuel cost adjustment for electric service, approval of a change in its fuel cost adjustment for steam service, and to update monthly benchmarks, together with its case-in-chief testimony.

On May 6, 2009, May 12, 2009, and May 29, 2009, Nucor Steel, a division of Nucor Corporation ("Nucor"), Duke Energy Indiana Industrial Group ("Industrial Group") and Steel Dynamics, Inc. – Engineered Bar Products Division ("SDI") filed Petitions, respectively, to Intervene in this proceeding, which the Presiding Officers granted on May 8, 2009, May 18, 2009, and June 8, 2009, respectively.

The Indiana Office of Utility Consumer Counselor ("OUCC") filed its audit report and direct testimony on June 3, 2009. On June 8, 2009, Duke Energy Indiana filed its Notice of Substitution of Witness related to substituting the prefiled, direct testimony of Mr. James F. Eckstein for the prefiled, direct testimony of Mr. John D. Swez. On June 9, 2008; Duke Energy Indiana filed its Notice of Substitution of Witness and Adoption of Testimony related to Mr. Scott A. Burnside adopting the prefiled, direct testimony of Ms. Mary Ann Amburgey. Supplemental testimony was filed by the OUCC on June 8, 2009.

On June 5, 2009, a Motion for a Subdocket in this Proceeding was filed by SDI requesting establishment of a subdocket proceeding to permit additional time for further discovery and investigation into SDI's concerns regarding recent increases in fuel costs. Duke Energy Indiana

filed its Opposition to Motion for Subdocket on June 12, 2009 and SDI filed a reply thereto on June 19, 2009.

Pursuant to proper notice of hearing, published as required by law, proof of which was incorporated into the record by reference, a public evidentiary hearing was held in this Cause on June 16, 2009, at 9:30 a.m., in Room 224, of the National City Center, 101 West Washington Street, Indianapolis, Indiana. At the outset of the hearing, Duke Energy Indiana withdrew its two Notices of Substitution of Witness. Duke Energy Indiana then offered into evidence its Verified Application in this Cause, including exhibits thereto, the direct verified testimonies, including corresponding exhibits, of Ms. Mary Ann Amburgey, Mr. Scott A. Burnside, Ms. Diana L. Douglas, Mr. Stephen M. Herrera, Mr. Vincent E. Stroud, and Mr. John D. Swez. The OUCC offered the testimonies and exhibits of Mr. Gregory T. Guerrettaz, including the Supplemental Testimony of Mr. Guerrettaz, and Mr. Michael D. Eckert, as corrected at the hearing. All evidence and exhibits were admitted into the record without objection. No members of the general public appeared or participated at the hearing.

Based upon the applicable law and the evidence herein, the Commission now finds:

1. **Commission Jurisdiction and Notice.** Due, legal and timely notice of the hearing in this Cause was given as required by law. Duke Energy Indiana is a public utility within the meaning of Ind. Code § 8-1-2, *et seq.*, as amended, and is subject to the jurisdiction of the Commission in the manner and to the extent provided by the laws of the State of Indiana. Therefore, the Commission has jurisdiction over the parties and the subject matter of this Cause.

2. **Duke Energy Indiana's Characteristics.** Duke Energy Indiana is a public utility corporation organized and existing under the laws of the State of Indiana with its principal office in Plainfield, Indiana, and is a second tier wholly-owned subsidiary of Duke Energy Corporation. Duke Energy Indiana is engaged in rendering electric utility service in the State of Indiana. The Company owns, operates, manages and controls, among other things, plant and equipment within the State of Indiana used for the production, transmission, delivery and furnishing of such service to the public. The Company also renders steam service to one customer, Premier Boxboard Limited LLC, hereafter referred to as ("Premier").

3. **Order in Cause No. 42359.** On May 18, 2004, the Commission issued an Order in Cause No. 42359 ("May 18 Order") approving base retail electric rates and charges for Duke Energy Indiana. Among other matters, the Commission's May 18 Order found that Duke Energy Indiana's base cost of fuel should be 14.484 mills per kWh and that the Company's base rates for electric utility service should reflect an authorized jurisdictional net operating income of \$267,500,000, prior to any additional return on qualified pollution control property approved by the Commission, pursuant to Ind. Code §§ 8-1-2-6.6 and 6.8, not taken into account in the May 18 Order.

4. **Orders in Cause Nos. 41744 S1 and 42061, 42061 ECR3 through 42061 ECR12, the November 20, 2007 Order in Cause Nos. 43114 and 43114-S1 ("IGCC Order") and the Order in Cause No. 43114 IGCC 1.** The Commission's July 3, 2002, Order in Cause Nos. 41744 S1 and 42061 ("CWIP Order"), and subsequent update orders up to and including the December 23,

2008, update in Cause No. 42061 ECR12 (“CWIP Update”), authorized Petitioner to add the value of certain qualified pollution control property to the value of the Company’s property for ratemaking purposes. The Commission’s CWIP update Order in Cause No. 42061 ECR3, dated March 11, 2004, stated that the applicable incremental increase to Duke Energy Indiana’s authorized return, approved in that proceeding, shall be phased-in over the period of time that Petitioner’s net operating income was affected by the applicable CWIP update. The value of the Company’s plant and level of authorized jurisdictional net operating income are also subject to increase as a result of the IGCC Order and subsequent updates thereto, approved by the Commission pursuant to Ind.Code § 8-1-8.8-11. The Commission’s IGCC Order and subsequent update Order in Cause No. 43114 IGCC1 authorized the Company to add the value of property at the Edwardsport Integrated Gasification Combined Cycle Generating Facility (“IGCC Project”) to the value of the Company’s property for ratemaking purposes. The Company has applied the same phase-in concepts ordered by the Commission in its Order in Cause No. 42061 ECR3 for CWIP updates to the IGCC Project update in making the calculations for this filing. In accordance with these Orders, Duke Energy Indiana calculated its authorized jurisdictional net operating income level for the 12-month period ending February 28, 2009, to be \$339,006,000. No party objected to the calculation of the authorized jurisdictional net operating income level proposed by Duke Energy Indiana, and we find it to be proper.

5. Fuel Purchases. Mr. Vincent E. Stroud, Vice President, Regulated Fuels, testified regarding Duke Energy Indiana’s fuel procurement practices. Petitioner generally purchases coal under long-term contracts. All of Duke Energy Indiana’s major generating stations are covered by long-term contracts except Edwardsport Station. For 2008 and 2009, Gibson, Wabash River, Gallagher and Cayuga Stations are supplied by long-term agreements for more than 90% of their annual requirements. Mr. Stroud stated that Edwardsport is an older station and is used by the Company essentially for peaking; therefore, a long-term contract is not necessary. The requirements for Edwardsport are supplied by either diverting contract tonnages from other stations or from spot market purchases. Mr. Stroud noted that many of the long-term contracts either contain provisions for periodic price re-opener negotiations, some type of price escalation, or a mechanism to adjust prices based upon a published market price index. In addition, all of the Company’s coal transportation contracts in Indiana contain fuel price surcharge provisions that are based upon published fuel price indices. Mr. Stroud testified that fuel transportation prices rose for much of the period because of increasing fuel surcharges. However, diesel fuel prices peaked during the 3rd quarter of 2008 and have fallen since October 2008. Petitioner supplements these long-term commitment purchases with the purchase of coal on the open market.

Mr. Stroud testified that Duke Energy Indiana’s average cost of coal per million BTU applicable to its long-term contracts has historically been lower than the cost of the coal the Company would have incurred on the open market. During the twelve month period ended February 28, 2009 coal purchased under long-term commitments comprised approximately 92.54% of total coal receipts. Mr. Stroud testified that if the Company were to purchase all of its coal requirements on the open market, spot prices would be driven upward to accommodate a demand influx of over 16 million tons annually. Mr. Stroud explained that when spot coal is required, the purchase commitments are usually made for small quantities, over short durations, and are based on the lowest delivered cost and best overall utilization characteristics. Mr. Stroud discussed other steps the Company takes to keep coal prices down, including its execution of and continued

negotiation of several mine opening contracts.

Mr. Stroud stated that Duke Energy Indiana recently entered into a mine opening contract with Peabody Coal Company for the Bear Run Mine, located in Sullivan County, Indiana. The Bear Run Mine will be the largest surface mine in the state and is expected to eventually produce up to 8.5 million tons per year. Mr. Stroud testified that without the addition of this mine, the Indiana coal market would become materially undersupplied by 2012 because of reserve depletion at existing mines. Mr. Stroud further stated that as the Company is the largest consumer of Indiana coal and most Illinois Basin mines will not produce the low chlorine coal necessary to ensure system reliability, it was critical for the Company to encourage the development of new sources of supply to ensure that a large supply/demand imbalance did not develop. Mr. Stroud noted that Peabody was unwilling to expend the hundreds of millions of dollars to develop this mine without long term commitments to purchase the coal. Mr. Stroud testified that the Company has made a long-term commitment to purchase up to 5.5 million tons per year (once the mine is in full production in 2012) for a 20-year period. In addition, Mr. Stroud said the Bear Run Mine is strategically located to provide coal with the necessary quality to Duke Energy Indiana's generating stations at a price that is competitive to any new production alternatives in the region. Mr. Stroud further testified the coal quality from this mine is suitable for most of the Company's generating stations and is accessible via rail and truck. The Company expects to receive shipments from Bear Run Mine within the next few months, and the fuel forecast in this proceeding includes coal to be shipped under this contract. Finally, Mr. Stroud stated that this contract will replace tonnage from other long-term contracts that will expire over the next few years.

Mr. Stroud also stated that domestic and international coal prices in general peaked in the third quarter of 2008 and have fallen significantly over the past six months. He explained that even though Indiana coal prices never escalated as much as in the Central and Northern Appalachian Basins, they also have not fallen as steeply. He explained that there is currently very little market activity, due in large part to the weak economic climate that has reduced demand for electricity and resulted in high coal inventories at most utilities, including Duke Energy Indiana. He testified that he expects to see continued volatility in coal prices, but that the high inventory levels should put downward pressure on coal prices, particularly in the spot market.

Mr. Stroud testified that in his opinion Duke Energy Indiana is purchasing coal at the lowest cost reasonably possible. Mr. Stroud concluded his testimony by offering his opinion that oil purchased by Duke Energy Indiana for peaking units, unit cycling purposes and Duke Energy Indiana's one oil-fired boiler at Edwardsport Station is purchased at the lowest cost reasonably possible.

Mr. John D. Swez, Director, Bulk Power Marketing and Trading, discussed Duke Energy Indiana's natural gas purchasing contracts and practices. Mr. Swez described how the price of natural gas has changed over the three-month period from December 2008 to February 2009, with the Company experiencing about a 36% decrease in the price of delivered natural gas at its gas burning generation stations during this period. Mr. Swez testified that, in his opinion, Duke Energy Indiana is purchasing natural gas at the lowest cost reasonably possible.

Mr. Stephen M. Herrera, Director, Financial Trading, Bulk Power Marketing and Trading, testified concerning the recent volatility of power and natural gas prices. He explained that through the end of February 2009, the average peak daily Midwest ISO CIN Hub real-time LMP was \$58.66/MWH. However, there was a wide range of prices, from as low as \$18.59/MWH to as high as \$188.99/MWH. He also noted recent volatility in natural gas prices.

Based upon the evidence presented, we find that Duke Energy Indiana has made reasonable efforts to acquire fuel for its own generation so as to provide electricity to its retail customers at the lowest fuel cost reasonably possible.

6. Hedging Activities. In his testimony, Mr. Herrera provided updates of the Company's gas and power hedging activities. He explained that the Company relies more on natural gas for fuel for the Company's peaking plants than it has in the past and cited recent historical occurrences of gas price volatility. He testified that, in his opinion, it makes sense for the Company to take advantage of the hedging tools available to protect against price fluctuations. Mr. Herrera discussed the results, and the factors influencing the results, of the gas hedging for the December 2008 through February 2009 reconciliation period. He also stated that the Company planned to purchase August and September 2009 forward contracts to hedge approximately one-half of its expected burn for July and August 2009 to mitigate price exposure during these periods.

Mr. Herrera also cited recent historical occurrences of power price volatility and explained the Company's use of forward power purchase contracts to hedge against this volatility. Mr. Herrera explained that the Company has been making power hedging purchases since January 2006. Mr. Herrera explained that in order to determine the Company's appropriate hedging action Duke Energy Indiana measures the forward purchase price of power against the expected cost of operating Company generation. When this comparison yields an economic advantage from buying forward (i.e., forward purchase price is lower than the expected cost of operating internal generation), the Company utilizes forward power purchase contracts that are financially settled on a specific future date and pays then-current market prices for these products. This action essentially fixes a price for purchased power at a cost lower than the expected cost of operating the Company's own generation for a portion of its expected load. Mr. Herrera also explained the Company is constantly assessing conditions and adapting its forward power positions accordingly with the goal of maintaining forward power hedges only in the amount necessary to economically cover its forecasted load. Mr. Herrera discussed the results, and the factors influencing those results, of the power hedging for the December 2008 through February 2009 reconciliation period.

Mr. Herrera also explained that, consistent with the Commission's June 25, 2008 Order in Cause No. 38707 FAC68 S1, beginning on August 1, 2008, and continuing until permanent hedging protocols are developed and approved by the Commission, Duke Energy Indiana will not utilize its flat hedging methodology. Rather, Duke Energy Indiana will hedge up to approximately flat minus 150 MW on a forward, monthly and intra-month basis, and up to approximately flat on a Day Ahead/Real-Time basis. This methodology will leave the Company with approximately 150 MW of expected load unhedged on a forward forecasted basis.

Mr. Herrera offered his opinion that the Company's gas and power hedging practices are reasonable. He stated that the Company never speculates on future prices, that its practice is

economic at the time the hedging decisions are made, that it reduces volatility, and that it benefits customers by reducing customers' risk of paying potentially higher spot market prices.

In her testimony, Ms. Diana L. Douglas, Director, Rates, explained that the amount included in fuel costs for hedging activity in this proceeding was a realized net loss of \$211,680 for gas hedging activity and a realized net loss of \$227,723 for power hedging activity (exclusive of Midwest ISO virtual activity).

OUCG witness Mr. Michael D. Eckert testified that the OUCG and the Company have been meeting collaboratively to discuss Duke's hedging transactions pursuant to the settlement agreement in Cause No. 38707 FAC68 S1, most recently meeting on May 15, 2009.

The Commission's Order in Cause No. 38707 FAC67, dated April 6, 2006, found gas hedging activities to be reasonable. The Company has included a negative gas hedging value of \$211,680 in the computation of the current fuel adjustment clause factor. The gas hedging amount was properly included, and we so find.

The issue of the appropriateness of the inclusion of realized gains/losses relating to the Company's power hedging activities in the computation of the fuel adjustment charge was the subject of a proceeding established by the Commission in Cause No. 38707 FAC68 S1. On June 25, 2008, the Commission issued an Order approving a Stipulation and Agreement ("Settlement") between Duke Energy Indiana and the OUCG and resolving all disputed issues evaluated within that sub-docket. Under the Settlement terms, the parties agreed that all cost recovery issues through February 29, 2008, were resolved and that any power hedging activities entered into by Duke Energy Indiana from November 30, 2007, through July 31, 2008, would not be challenged on the basis that Duke Energy Indiana utilized a flat hedging methodology. However, such hedging activities entered into during that time period could be challenged on the basis of other prudence criteria. No party has expressed concerns regarding the realized net loss for power hedging included in the fuel costs in this proceeding or challenged the prudence of the power hedging activities that gave rise to the realized net loss. In addition, the Company presented evidence that its hedging practices relevant to this proceeding were consistent with the Settlement. Thus, we will allow Petitioner to include the loss of \$227,723 of realized power hedging losses in the calculation of fuel costs in this proceeding.

7. Orders in Cause Nos. 42685 and 38707 FAC70 and Open Docket in Cause No. 43426. On June 1, 2005, the Commission issued its final Order in Cause No. 42685 ("June 1 Order"). In the June 1 Order, we approved certain changes in the operations of Duke Energy Indiana and the other investor-owned Indiana electric public utilities that are participating members of the Midwest Independent Transmission System Operator, Inc. ("Midwest ISO"). Additionally, we addressed the timing and manner of recovery of costs incurred by Duke Energy Indiana as a result of the Midwest ISO's implementation of day-ahead and real-time markets for electric energy (the "Energy Markets"). In the June 1 Order, we determined the Energy Markets charges and credits that should be included in the cost of fuel for purposes of subsequent fuel cost proceedings, including certain charges and credits listed on page 37 of the June 1 Order.

In this proceeding, Mr. Swez testified that Duke Energy Indiana included the following

Energy Markets charges and credits incurred as a cost of reliably meeting the power needs of Duke Energy Indiana's load: (1) Energy Markets charges and credits associated with Duke Energy Indiana's own generation and bilateral purchases that were used to serve retail load; (2) purchases from the Midwest ISO at the full locational marginal price ("LMP") at Duke Energy Indiana's load zone; (3) other Energy Markets charges and credits included in the list on page 37 of the June 1 Order; and (4) credits and charges related to auction revenue rights ("ARRs") and Schedule 27-A involving Manual Re-Dispatch Make Whole Payments that resulted in credits from testing prior to the start of the ASM market, as authorized by the Commission in Cause No. 38707 FAC77.

The Commission Order in Cause No. 38707 FAC70, dated December 28, 2006, subsequently amended the June 1 Order regarding uninstructed deviation ("UD") amounts. In that Order the Commission found UD penalties incurred on or after June 1, 2006 are a reasonable cost of generating power in the Midwest ISO market and may be properly included as a cost of fuel in FAC proceedings, unless it is demonstrated that the utility failed to use good utility operating practice. The Commission further found that the Company should credit customers with UD revenues in future FAC proceedings and cease doing so in Rider 68. The Commission also required an explanation in support of cost recovery for any given month in which UD charges exceeded such revenues.

Ms. Douglas testified in her direct testimony that for the months of December 2008 through January 2009, the Company included in its fuel cost \$14,892 of UD charges and a credit of \$29,618 for UD revenues. Mr. Swez testified that UD charges did not exceed UD revenues for any month for which recovery of charges was sought in this proceeding. OUCC witness Mr. Michael D. Eckert testified that the OUCC recommends the Commission allow the recovery of the UD charges.

Ms. Douglas explained in her direct testimony that effective with the January 6, 2009, implementation of the ASM, the Company will no longer be assessed UD charges or credited with UD revenues. Therefore, other than any adjustments to UD charges and revenues that the Midwest ISO may include on resettlement statements for prior periods up through January 2009, there will be no UD charges or revenues for new reconciliation months to be included in future FAC filings.

Ms. Mary Ann Amburgey, Lead Accounting Analyst, testified as to the procedures followed by the Company to verify the accuracy of the charges and credits allocated by the Midwest ISO to the Company. She also discussed the process by which the Midwest ISO issues multiple settlement statements for each trading day and the dispute resolution process with respect to such statements. She stated that every daily settlement statement received by the Company from the Midwest ISO is reviewed utilizing the computer software tools described in her testimony. Ms. Amburgey testified that she is confident that the amounts paid by Duke Energy Indiana to the Midwest ISO, net of any credits, are proper and that such amounts billed to customers through the fuel adjustment clause are proper.

Ms. Amburgey also explained that the Company had received credits under Schedule 27 (Real-Time Price Volatility Make Whole Payment) during January and February 2009. She explained that in Cause No. 38707 FAC77, Duke Energy Indiana requested that the Commission authorize the Company to treat credits it received pursuant to Schedule 27 and 27-A (Manual Re-Dispatch Make Whole Payment) as credits to fuel expense. The Commission found that the

Schedule 27-A charge type was properly includable as a component of fuel cost in FAC proceedings and, as such, was properly includable in that proceeding as well as future FAC fuel costs and credits. However, as the Schedule 27 Price Volatility Make Whole Payments had not yet been implemented by the Midwest ISO at the time of that proceeding, and the Company had not received any credits or charges, the Commission postponed any decision on this charge type at that time. In its Order dated September 24, 2008, the Commission authorized the Company to bring this charge type to its attention in a future FAC proceeding when more information was available about its implementation by the Midwest ISO.

Mr. Swez explained in his direct testimony that the Real-Time Price Volatility Make Whole Payment is a credit designed to compensate generators during instances where a unit clears in the day-ahead market and then settles in the real-time market at a level that erodes their margin due to price volatility in the real-time market. He gave an example of a situation which would give rise to the credit and explained that even though the Real-Time Price Volatility Make Whole Payment is not specifically related to ASM, the January 6, 2009, ASM start date was used by the Midwest ISO as the start date for this new charge type.

Ms. Douglas testified that the Commission previously found in its June 1, 2005 Order in Cause No. 42685 that the costs of the load purchase and the generation compensation, including Revenue Sufficiency Guarantee ("RSG") Make Whole Payments, in the day ahead and real time energy markets are fuel-related and should be included as a cost of fuel in FAC proceedings. She explained that because these Real Time Price Volatility Make Whole Payments are additional compensation to generators and similar in nature to RSG Make Whole Payments, the Company is asking the Commission to authorize it to include credits or charges for Schedule 27 as a cost of fuel in this and its future FAC proceedings.

Ms. Douglas explained that in accordance with the Commission's Order in Cause No. 38707 FAC 77, Excessive and Non-Excessive Energy Amount charge types had been included in the fuel cost amounts for January and February 2009 on an interim basis, subject to refund pending a final Order by the Commission determining ASM cost recovery in Phase II of Cause No. 43426. She also explained that in accordance with the Commission's August 13, 2008, Phase I Order in Cause No. 43426 ("Phase I Order"), deferral accounting had been used for all other new charge types resulting from the ASM, pending the Commission's Order in in Phase II of that proceeding and that the fuel cost being requested for recovery in this proceeding did not include any of these other new ASM related charge types or credits.

OUCG witness Mr. Eckert testified that Applicant's proposed ratemaking treatment for the new ASM Charge types follows the treatment ordered by the Commission in its Phase I Order. He also recommended the Commission allow Applicant to recover its UD charges.

Based upon the evidence presented, we find that Duke Energy Indiana's inclusion of the Energy and ASM charges and credits in its cost of fuel is consistent with the June 1 Order, the December 28, 2006 Order in Cause No. 38707 FAC70, as well as our Phase I Order and our Order regarding treatment of the Company's costs and credits resulting from ASM in Cause No. 38707 FAC77, pending the final decision of the Commission in Phase II of Cause No. 43426. We further find that Duke Energy Indiana is authorized to include as a cost of fuel in this and future FAC

proceedings credits and charges, if any, under the Midwest ISO's Schedule 27 Real-Time Price Volatility Make Whole Payments charge type.

8. **Participation in the Energy and ASM Markets and Midwest ISO Directed Dispatch.** As mentioned above, in the June 1 Order, the Commission approved certain changes in the operations of Duke Energy Indiana as a result of the implementation of the Energy Markets. Specifically, we found that Duke Energy Indiana (and the other electric utilities participating in Cause No. 42685) "should be granted authority to participate in the Midwest ISO directed dispatch and Day 2 energy markets as described in their testimony." *Id.* at p. 13. Mr. Swez described Duke Energy Indiana's participation in the Energy Markets and testified that it was consistent with the testimony presented in Cause No. 42685.

In the Phase I Order, the Commission approved certain changes in the operations of Duke Energy Indiana as a result of the implementation of the ASM. Specifically, we found that Duke Energy Indiana (and the other electric utilities participating in Cause No. 43426) "are authorized to transfer additional balancing authority functions in accordance with the Amended Balancing Authority Agreement and implement the operational changes necessary to permit Joint Petitioners to participate in the Midwest ISO's ASM." *Id.* at p. 23. Mr. Swez explained that up until the start of the ASM on January 6, 2009, Duke Energy Indiana continued to provide regulation and contingency reserve service through the intra five-minute dispatch of its generating units; however, once ASM began, Duke Energy Indiana offers these ancillary services to and purchases these ancillary services from the ASM. He also described the Company's experience under ASM. He explained that to his knowledge the ASM has functioned without any major issues. Duke Energy Indiana's generators have been able to follow real-time signals from the Midwest ISO with minimal issues. Day-ahead and real-time Market Clearing Prices for Regulating, Spinning, and Supplemental Reserves appear to be at reasonable price levels consistent with market conditions. In addition, he opined that Duke Energy Indiana's generating units appear to be appropriately receiving day-ahead and real-time awards for Regulating, Spinning, and Supplemental Reserves.

Based upon the evidence presented, we find that Duke Energy Indiana's participation in the Energy and ASM constituted reasonable efforts to generate or purchase power, or both, to serve its retail customers at the lowest fuel cost reasonably possible.

9. **New Source Review Impacts on Operations.** Mr. Swez explained in his testimony that in the liability phase of the new source review ("NSR") lawsuit against Cinergy Corp. ("Cinergy" – the Company's immediate parent company), the jury found against Cinergy with regard to projects undertaken at the Company's Wabash River Units 2, 3, and 5 from 1989 to 1992. In the remedy phase, among other matters, the plaintiffs requested the judge to order the Company to either install scrubbers and SCRs on Wabash River Units 2, 3, and 5 by 2013, or retire Wabash River Units 2, 3, and 5 within 30 days of the judge's order. In order to mitigate the risk of reliability problems that could result from the premature closure of Wabash River Units 2, 3, and 5, Cinergy proposed waiting to retire the units until the Edwardsport IGCC plant and its associated transmission system upgrades, as well as any additional transmission upgrades needed as a result of the retirements, can be completed. In the interim, Cinergy proposed limiting the operation of these units to keep emissions at or below "baseline" levels that prevailed before the units were modified. Mr. Swez testified that the Company began limiting the dispatch of Wabash River Units 2, 3 and 5

consistent with this proposal earlier this year, with the goal that these units will be available to operate during peak load conditions, or as required by the Midwest ISO for reliability purposes, while complying with the emissions cap. He noted that operating the units under an emissions cap is not unusual and that the Company has done so at the Edwardsport station for at least 15 years and it did so at the Noblesville station until it was repowered.

OUCC witness Mr. Eckert provided an additional update in his testimony. He explained that on May 29, 2009 the U.S. District Court for the Southern District of Indiana issued a ruling requiring Duke Energy Indiana to shut down its Wabash River Units 2, 3 and 5 no later than September 30, 2009. Mr. Eckert stated that the ruling did not affect this current FAC since the months being forecasted are July, August and September 2009, but that it will affect the Company's next quarterly FAC. Mr. Eckert recommended that Duke Energy Indiana be required to provide an explanation in its next FAC as to (1) how the shutdown of Wabash River Units 2, 3, and 5 will impact the Company's future fuel costs and ability to meet future summer peak demands, and (2) how the Company intends to meet those future summer peak demands. The Company agreed to provide testimony in its next FAC filing concerning these potential impacts associated with the District Court's ruling as recommended by the OUCC.

10. Operating Expenses. Ind. Code § 8-1-2-42(d)(2) requires the Commission to determine whether actual increases in fuel costs have been offset by actual decreases in other operating expenses. Accordingly, Duke Energy Indiana filed operating cost data for the twelve months ended February 28, 2009. Duke Energy Indiana's authorized jurisdictional operating expenses (excluding fuel costs) are \$785,863,000. For the twelve-month period ended February 28, 2009, Duke Energy Indiana's jurisdictional operating expenses (excluding fuel costs) totaled \$1,019,200,000. Accordingly, Duke Energy Indiana's actual operating expenses exceeded jurisdictional authorized levels during the period at issue in this Cause. Therefore, the Commission finds that Duke Energy Indiana's actual increases in fuel costs for the above referenced periods have not been offset by decreases in other jurisdictional operating expenses.

11. Return Earned. Ind. Code § 8-1-2-42(d)(3), subject to the provisions of Ind. Code § 8-1-2-42.3, generally prohibits a fuel cost adjustment charge which would result in regulated utilities earning a return in excess of its applicable authorized return ("earnings test"). Should the fuel cost adjustment factor result in the utility earning a return in excess of its applicable authorized return, it must, in accordance with the provisions of Ind. Code § 8-1-2-42.3, determine if the sum of the differentials between actual earned returns and authorized returns for each of the twelve-month periods considered during the relevant period is greater than zero. If so, a reduction to the fuel adjustment clause factor is deemed appropriate.

The fuel cost charge test period used for earnings test computations in this Cause was the twelve months ended February 28, 2009. During this period, Duke Energy Indiana's actual jurisdictional electric operating income level was \$230,262,000, while its authorized phased-in jurisdictional electric operating income level for purposes of Ind. Code § 8-1-2-42(d)(3), was \$339,006,000. Therefore, the Commission finds that Duke Energy Indiana did not earn a return in excess of its authorized level during the twelve months ended February 28, 2009.

12. **Interim Rates.** Because we are unable to determine whether Duke Energy Indiana's actual earned return will exceed the level authorized by the Commission during the period that this fuel cost adjustment factor is in effect and because a final determination has not yet been made in Phase II of Cause No. 43426 of cost recovery of new charges and credits resulting from the implementation of the Midwest ISO's ASM, the Commission finds that the rates approved herein should be approved on an interim basis in the event an excess return is earned and pending a final determination in Cause No. 43426.

13. **Estimation of Fuel Costs.** Duke Energy Indiana estimates that its prospective average fuel cost for the months of July through September 2009 will be \$79,907,750 or \$0.027400 per kWh. Duke Energy Indiana previously made the following estimates of its fuel costs for the period December 2008 through February 2009, and experienced the following actual costs, resulting in percent deviation, as follows:

<u>Month</u>	<u>Actual Cost in Mills/kWh</u>	<u>Estimated Cost in Mills/kWh</u>	<u>Percent Actual is Over (Under) Estimate</u>
December 2008	23.889	24.131	(1.00)
January 2009	27.382	26.570	3.06
February 2009	<u>24.676</u>	<u>25.026</u>	(1.40)
Weighted Average	25.334	25.245	0.35

A comparison of Duke Energy Indiana's actual fuel costs with the respective estimated costs for these three periods results in a weighted average percentage difference of 0.35%. No party in this Cause disputed the techniques or results of Duke Energy Indiana's forecasting methodology. Duke Energy Indiana's estimating techniques appear reasonably sound and its estimates for July through September 2009 should be accepted and we so find.

14. **Purchased Power Benchmark.** Duke Energy Indiana has calculated monthly purchased power benchmarks in accordance with the Commission's August 18, 1999 Order in Cause No. 41363 and the guidance of the Commission in Cause Nos. 38706 FAC45, 38708 FAC45, 38707 FAC56, and 38707 FAC59. The benchmarks are as follows:

<u>Month / Year</u>	<u>Benchmark \$/MWh</u> ^{1/}	<u>Facility</u>
December 2008	152.40	Connersville 1
January 2009	126.45	Wabash River Diesel
February 2009	134.74	Connersville 1

^{1/} Calculated using most efficient unit heat rate

No Party objected to these calculations. Based on the evidence of record, the Commission finds that Duke Energy Indiana has met the requirements necessary to establish monthly

benchmarks for power purchases that occurred during the December 2008 through February 2009 reconciliation period.

15. Fuel Cost Factor. As discussed in Finding No. 3 above, Duke Energy Indiana's base cost of fuel is 14.484 mills per kWh. The evidence indicates that Duke Energy Indiana's fuel cost adjustment factor applicable to July through September 2009 billing cycles is computed as follows:

	<u>\$/kWh</u>
Projected Average Fuel Cost	0.027400
Net Variance	(0.000206)
Adjusted Fuel Cost Factor	0.027194
Less: Base Cost of Fuel	<u>0.014484</u>
Fuel Cost Adjustment Before Applicable Taxes	0.012710
Adjustment for Utility Receipts Tax	<u>0.000194</u>
Fuel Cost Adjustment Factor Adjusted for Applicable Taxes	0.012904

The net variance factor shown above reflects \$1,567,383 of over-billed fuel costs applicable to retail customers that occurred during the period December 2008 through February 2009. Coal, gas, and power price trends affecting fuel costs were discussed in the testimonies of Mr. Swez, Mr. Herrera and Mr. Stroud, as outlined in Finding No. 5 above.

OUCG witness Mr. Gregory Guerretaz testified, among other matters, that the fuel cost element of the Company's proposed fuel cost adjustment has been calculated in conformity with Ind. Code § 8-1-2-42 and numerous Commission Orders affecting this filing. He further concluded that the fuel cost adjustment for the quarter ended February 28, 2009, had been properly applied by the Company. In addition, he stated that the figures used in the Application for a change in the fuel cost adjustment were supported by the Company's books and records, "PACE", and source documentation of the Company for the period reviewed.

On June 25, 2008, the Commission issued its Order in Cause No. 38707 FAC76 which, among other matters, authorized a sub-docket in that proceeding to further examine whether the Gibson Unit 4 outage earlier this year resulted from imprudent maintenance by the Company. Recognizing that the variance amounts presented above may be altered by the outcome of that proceeding, we find, subject to the outcome of the sub-docket established in cause No. 38707 FAC 76 S1, the amounts presented above were calculated appropriately.

16. Effect on Residential Customers. The approved factor represents an increase of \$0.001646 per kWh from the factor approved in Cause No. 38707 FAC79. The typical residential customer using 1,000 kWhs per month will experience an increase of \$1.64, or 1.9%, on his or her base electric bill compared to the factor approved in Cause No. 38707 FAC79 (excluding various tracking mechanisms and sales tax).

17. Fuel Adjustment for Steam Service. On December 30, 1992, this Commission issued its Order in Cause No. 39483 approving the June 18, 1992 Agreement between Duke Energy Indiana and Premier, which included a change in the method used to calculate Premier's fuel cost adjustment as well as an update to the base cost of fuel. The fuel cost adjustment factor for Premier

of \$1.2911311 per 1,000 pounds of steam was calculated on Exhibit B, Schedule 1, of the Verified Application; this factor will be effective for the July through September 2009 billing cycles. Exhibit B, Schedule 2, of the Verified Application is a reconciliation of the actual fuel cost incurred to estimated fuel cost billed to Premier that resulted in a \$33,780 payable to Premier for the months of December 2008 through February 2009.

The Commission finds that Duke Energy Indiana's proposed change in the fuel cost adjustment factor for Premier of \$1.2911311 per 1,000 pounds of steam has been calculated in accordance with this Commission's Order in Cause No. 39483, and that such factor should be approved. We further find that Duke Energy Indiana's reconciliation amount of \$33,780 payable to Premier has been properly determined and should be approved.

18. Shared Return Revenue Credit Adjustment for Premier. Per the June 18, 1992 Settlement Agreement, Premier will receive shared return revenue credit adjustments to the extent incurred. As indicated above in Finding No. 11, Duke Energy Indiana did not have excess earnings for the twelve months ended February 2009. Therefore, we find Premier is not due a shared return revenue credit.

19. SDI's Motion for Subdocket. As noted above, SDI filed a Motion for Subdocket on June 5, 2009. In its Motion, SDI expressed its general concern about the Company's rising fuel costs and fuel cost adjustment factor, but did not present any specific facts or verified evidence to support its belief that the Company's fuel procurement practices were imprudent. In its Reply to Duke Energy Indiana's Response opposing the Motion for Subdocket, SDI indicates that its issues include the Company's coal procurement practices and the lack of voltage differentiation. SDI provides no elaboration on its concerns with Duke Energy Indiana's coal procurement practices. SDI also proposes that because other states have addressed the issue of voltage differentiated rates the Commission should also do so here.

The OUCC's witnesses did not take issue with the Company's fuel procurement practices or the requested fuel cost adjustment factor. While neither Nucor nor the Industrial Group opposed the creation of a subdocket, neither offered any evidence in support thereof. SDI has failed to set forth sufficient information for the Commission to find that further investigation into the Company's fuel costs is warranted or necessary. Therefore, we find SDI's Motion for Subdocket should be denied.¹

IT IS THEREFORE ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION that:

1. Duke Energy Indiana's fuel cost adjustment factor for electric service to be billed jurisdictional customers, as set forth in Finding No. 15, and the fuel cost adjustment for steam service as set forth in Finding No. 17 of this Order are hereby approved on an interim basis, subject to refund, in accordance with all of the Findings above.

¹ On June 23, 2009, Duke Energy Indiana filed a Motion requesting leave to respond to SDI's Reply. As the Commission is denying SDI's Motion for a subdocket, no further response is required and Duke Energy Indiana's Motion is denied.

2. Duke Energy Indiana's inclusion of Energy and Ancillary Services Markets charges and credits in its cost of fuel, as described in Finding No. 7 of this order, is hereby approved, with treatment of ASM charges and credits subject to the outcome of the final decision in Cause No. 43426.

3. Duke Energy Indiana is authorized to include Schedule 27 Real-Time Price Volatility Make Whole Payments as a cost of fuel in this and future FAC proceedings, as described in Finding No. 7 of this order.

4. Duke Energy Indiana shall place into effect the fuel cost adjustment factors for electric service and steam service approved herein, applicable to all bills rendered beginning with and subsequent to the later of the effective date of the Commission's Order or the first billing cycle of July 2009, upon filing with the Electricity Division of the Commission, a separate amendment to its rate schedules with clear reference therein that such factor is applicable to the rate schedules reflected on the amendment.

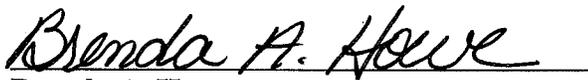
5. SDI's Motion for a Subdocket in this Proceeding is hereby denied.

6. This Order shall be effective on and after the date of its approval.

HARDY, ATTERHOLT, GOLC, LANDIS, AND ZIEGNER CONCUR:

APPROVED: JUN 30 2009

I hereby certify that the above is a true and correct copy of the Order as approved.


Brenda A. Howe
Secretary to the Commission