

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

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VERIFIED PETITION OF INDIANAPOLIS )  
POWER & LIGHT COMPANY FOR )  
APPROVAL OF AN ADJUSTMENT TO ITS )  
RATES THROUGH ITS APPROVED )  
ENVIRONMENTAL COMPLIANCE COST )  
RECOVERY ADJUSTMENT COMMENCING )  
WITH THE MARCH 2012 BILLING CYCLE IN )  
ACCORDANCE WITH THE ONGOING )  
REVIEW PROCESS )

CAUSE NO. 42170 ECR 19

APPROVED:

NOV 21 2012

ORDER OF THE COMMISSION

**Presiding Officers:**

**Carolene Mays, Commissioner**

**Jeffery A. Earl, Administrative Law Judge**

On June 22, 2012, Indianapolis Power & Light Company (“IPL”) filed its petition for approval of a modification to its certificate of public convenience and necessity (“CPCN”) for the use of clean coal technology (“CCT”) and qualified pollution control property (“QPCP”) and for approval of an adjustment to its environmental compliance cost recovery adjustment (“ECCRA”) commencing with the September 2012 billing cycle. Also on June 22, 2012, IPL prefiled the direct testimony and exhibits of David Kehres, Thomas Moore, Greg Daeger, Dwayne Burke, Craig Forestal, and James Cutshaw.

On July 25, 2012, the Indiana Office of the Utility Consumer Counselor (“OUCC”) filed an Unopposed Motion to Modify Procedural Schedule, which the Presiding Officers granted by Docket Entry dated July 26, 2012. On August 28, 2012, the OUCC prefiled the testimony and exhibits of Wes R. Blakley, Cynthia M. Armstrong, and Maclean O. Eke. On September 28, 2012, IPL and the OUCC filed a Joint Motion for Leave to Submit Settlement Agreement and Request for Settlement Hearing (“Joint Motion”), which included a copy of the Stipulation and Settlement Agreement (“Settlement Agreement”). The Presiding Officers granted the Motion in a Docket Entry dated October 4, 2012. IPL and the OUCC each submitted testimony in support of the Settlement Agreement on October 5, 2012.

Pursuant to public notice duly given and published as required by law, proof of which was incorporated into the record by reference and placed in the Commission’s official file, a public hearing in this Cause was held on October 16, 2012, at 1:30 p.m., in Hearing Room 224, 101 W. Washington Street, Indianapolis, Indiana. At the hearing, IPL and the OUCC appeared by counsel and offered their prefiled testimony and exhibits, which were admitted into evidence without objection. No other party or members of the general public appeared.

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

1. **Commission Jurisdiction and Notice.** Proper notice of the hearing in this Cause was given as required by law. IPL owns and operates an electric utility and is subject to the jurisdiction of this Commission as provided in the Public Service Commission Act, as amended, Ind. Code ch. 8-1-2. Thus, the Commission has jurisdiction over IPL and the subject matter of this Cause.

2. **IPL's Characteristics.** IPL is an electric generating utility and is a corporation organized and existing under the laws of the State of Indiana with its principal office at One Monument Circle, Indianapolis, Indiana. IPL is engaged in rendering electric public utility service in the State of Indiana and owns, operates, manages, and controls, among other things, plants and equipment within the State of Indiana used for the production, transmission, delivery, and furnishing of such service to the public.

3. **Proposed Rider Adjustment.** The Commission's November 14, 2002 Order in Cause No. 42170 granted IPL a Certificate of Public Convenience and Necessity ("CPCN") for IPL's projects to comply with new environmental regulations restricting the emission of nitrogen oxides ("NO<sub>x</sub>") from IPL's generation units ("November 14 Order"). The November 14 Order also approved use of the ECCRA and procedures for implementing the ECCRA, including standardized forms for purposes of submission of information. On February 28, 2007, in Cause No. 42170 ECR 8, the Commission approved modifications to IPL's CPCN to include the installation of a sodium bisulfite ("SBS") injection system for the Selective Catalytic Reduction ("SCR") projects for Petersburg Units 2 and 3 to mitigate sulfur trioxide ("SO<sub>3</sub>") emissions and for recovery of the cost of the SBS injection system.

The Commission's November 30, 2004 Order in Cause No. 42700 approved modifications to the CPCN to construct a Flue Gas Desulphurization ("FGD") system at Harding Street Unit 7 and FGD Enhancements on Petersburg Unit 3 ("November 30 Order"). On August 31, 2005, in Cause No. 42170 ECR 5, on August 16, 2006, in Cause No. 42170 ECR 7 and on February 28, 2007, in Cause No. 42170 ECR 8, the Commission approved modifications to IPL's CPCN regarding IPL's cost estimates of the clean coal technology ("CCT") projects. On September 13, 2007, in Cause No. 42170 ECR 9, the Commission found that the catalyst replacement and refurbishment expenditures incident to the operation of IPL's SCR equipment are an ongoing cost appropriate for recovery in IPL's ECR semi-annual proceedings.

The projects approved in the November 14 and November 30 Orders and our subsequent orders in various ECR proceedings, concern the first step of IPL's Multi-Pollutant Plan ("MPP"). The Commission's April 2, 2008 Order in Cause No. 43403 approved a modification to the CPCN to construct FGD Enhancements on Petersburg Unit 4 and to install mercury monitors ("April 2 Order") to allow IPL to reliably and economically achieve compliance with the Environmental Protection Agency's ("EPA") air emission regulations (the second step of IPL's Multi-Pollutant Plan). On February 24, 2010, in Cause No. 42170 ECR 14 and on July 7, 2011, in Cause No. 42170 ECR 16 S1, the Commission approved modifications to IPL's CPCN regarding IPL's cost estimates of the Multi-Pollutant Plan projects.

In this Cause, IPL seeks Commission approval of an ECCRA to earn a return on construction costs incurred through May 31, 2012, and to timely recover depreciation and operation and maintenance ("O&M") expenses. IPL also requests approval of a revised cost estimate for the Petersburg Unit 4 FGD Enhancements.

4. **IPL's Testimony.** IPL submitted testimony regarding the status of the CCT projects. IPL Witness Kehres provided a progress report as part of the ongoing review of IPL's NO<sub>x</sub> and Multi-Pollutant compliance projects approved in Cause No. 42170. He also stated that all projects are in service and the SBS Injection Systems remain suspended pending further evaluation. The completion date for the SBS Injection Systems has not been determined as these projects have been suspended, and the final costs for those projects will be reported once they are completed and placed into service.

David Kehres testified regarding the two Multi-Pollutant Plan projects that were approved in the November 30 Order. The first, an enhancement to the existing FGD system on Petersburg Unit 3, has been completed, and the project entered service on June 24, 2006. The performance of the upgraded scrubber has exceeded the original design emission target of 0.4 lbs SO<sub>2</sub>/MMBtu as the current emissions from Unit 3 are less than 0.2 lbs SO<sub>2</sub>/MMBtu. This better than expected performance will likely result in lower future SO<sub>2</sub> compliance costs as fewer SO<sub>2</sub> emissions allowances will be consumed on Unit 3.

The second Multi-Pollutant Plan project, a new FGD system for Harding Street Unit 7, went into service on September 17, 2007, and all construction completion activities have been completed. In addition, Mr. Kehres stated that the following work on Harding Street Unit 7 FGD has been completed since IPL's most recent ECR filing: (a) installation of the third and final access opening to the FGD recycle piping header for personnel to enter for inspection and/or repair has been completed; (b) installation of winterization hardware and engineering controls on the SO<sub>3</sub> removal system has been completed; and (c) extensions were added to the existing FGD Limestone and Gypsum Conveyor Covers to provide 100% and better protection from the weather.

Mr. Kehres provided an update on the progress of the winterization work and engineering controls that are planned for the SO<sub>3</sub> removal system. The SBS injection equipment is located in the SCR structure just downstream of the SCR reactor duct. This area of the SCR structure is prone to severe icing during the winter months from the cooling tower plume, which blows through the outdoor SCR. In the past, occasional icing was tolerated because the SCR was out of service during the winter months and operating personnel were not required to work as often in the icy areas of the SCR structure. However, the icing problem has become more of a safety issue now that both the SBS and SCR are operated year round. Construction of the winterization enclosures has been completed. Mr. Kehres also stated that the Breen Probe analyzer systems approved in ECR 14 have been installed and the probes have been placed into service. Final controls implementation has been completed.

Mr. Kehres also provided an update on the two Multi-Pollutant projects approved in Cause No. 43403, the Petersburg Unit 4 FGD Enhancements ("Pete 4 FGD upgrade"), and the Mercury Monitoring Systems. The Petersburg Unit 4 turbine overhaul outage was rescheduled for 2011 to match the revised project completion schedule for the Pete 4 FGD upgrade. The Unit 4 turbine overhaul has been completed, and the Unit 4 FGD Enhancements were placed into service on November 25, 2011. Start up activities, initial tuning, and performance testing have been completed. Mr. Kehres reported that the Pete 4 FGD upgrade met all of the required performance guarantees during the Baseline Test. The average SO<sub>2</sub> removal during the test was 95.5%. Mr. Kehres provided further details on the completion of the Pete 4 FGD upgrade in Petitioner's Exhibit DK-3.

Mr. Kehres testified that, as explained in the ECR 14 proceeding, IPL previously delayed the Mercury Monitoring System projects due to the uncertainty surrounding the Clean Air Mercury Rule (“CAMR”), which was vacated by the courts. IPL is currently reviewing the final Mercury and Air Toxics Standards (“MATS”) rule to determine what actions, including the addition of Mercury Monitoring Systems, may be required to comply with this new rule.

Mr. Kehres explained that IPL has updated the projected construction costs for the Pete 4 FGD upgrade in Petitioner’s Exhibit DK-4 with the latest cost information available to the project team. On May 21, 2012, IPL informed the Commission and the OUCC that the current cost estimate for the project is \$129.6 million, an increase of \$1.6 million from the cost estimate approved by the Commission in the ECR 16 proceeding. Accordingly, IPL is requesting in this proceeding a modification to its current CPCN.

Mr. Kehres testified that the Pete 4 FGD upgrade was recently placed into service, and start-up and performance testing have been completed. With the exception of several minor punchlist items, field construction activities have been completed. The startup activities, initial tuning, and performance testing identified additional necessary work, resulting in some additional costs. However, IPL was able to reduce some costs through work scope reductions and the use of the existing FGD System vendor rather than a third-party contractor for the performance testing. As discussed in Mr. Kehres’s testimony in ECR 18, IPL incurred additional costs including additional stiffening of the existing booster fan foundation at an approximate cost of \$234,000 and the initial ball charge of approximately \$126,000 for the new limestone ball mill. These costs were partially offset by approximately \$10,000 in miscellaneous adjustments for various field activities.

Mr. Kehres next described the major components of the cost increase for the Pete 4 FGD upgrade. Petitioner’s Exhibit DK-4 shows the updated projected construction costs using the latest cost information available to the project team. Mr. Kehres described the major components of the remaining \$1,250,000 cost increase identified on Petitioner’s Exhibit DK-4, in the column entitled “ECR 18 to 19 Increment.”

- Mechanical subcontract Additional Work Authorizations: Start-up, initial tuning, and performance testing identified the need for additional mechanical work, including additional test ports at an approximate cost of \$56,000. In addition, productivity losses associated with the IPL Lock Out Tag Out (LOTO) Safety program exceeded the costs included in prior estimates by approximately \$72,000.
- Steel Platforms: Adjustments to conveyor, hydroclone, and scrubber platforms were determined to be necessary to improve operator and maintenance access and to resolve potential safety concerns, resulting in a cost increase of \$43,000.
- Chimney Extension: Final costs for the chimney extension were higher than previously estimated by approximately \$275,000, primarily due to alloy material escalation costs between the time of the contractor’s proposal and the contractor’s procurement of the alloy materials. Mr. Kehres explained it is standard industry practice for the owner to accept the price risk for volatile alloy materials during the time between bids being accepted and the alloy materials being procured and that this approach allows the owner to pay the actual cost of the alloy materials rather than for a pricing contingency that may not be necessary.
- Electrical subcontract: The use of contractor support personnel during start up was required to meet the unit and project start-up schedules, resulting in approximately 3890

additional man hours spent by field crews to support start-up activities at an approximate cost of \$260,000. Mr. Kehres testified the use of additional field support personnel to assist with start up and performance testing was managed prudently by the IPL start-up team.

- Performance testing: As previously noted, final costs for performance testing were reduced by avoiding the use of a third-party testing contractor. However, Mr. Kehres explained that some of these savings were offset by additional start-up engineer costs of approximately \$73,000 for the FGD System vendor, who performed the testing in lieu of a third-party testing contractor.
- Start-up support personnel: Start-up support personnel costs were higher than previously estimated by approximately \$139,000 due to the extended start-up time period required for the plant to achieve stable operating conditions that would allow contractual performance testing on the Pete 4 FGD upgrade.
- Instrument air piping: Installation costs for the new instrument air piping exceeded original estimates by approximately \$111,000 due to field conditions and congestion during the major outage and various field interferences that resulted in alternate piping routing.
- Slurry valve replacement: The mechanical contractor provided and installed 193 slurry valves that have started to fail and that the valve supplier has stated are not suitable for the intended slurry service. Mr. Kehres testified that although the costs to replace the valves, estimated at \$191,000, will be backcharged to the contractor, they are currently being included until the backcharge is formally agreed to with the contractor.
- Additional coating work: Coating work on the new pump house trench was not previously included in the cost estimates and is approximately \$34,000.
- Additional items: Mr. Kehres also described several miscellaneous items, resulting in a net impact of a \$4,000 cost decrease.

Mr. Kehres testified that IPL proactively managed project costs during the final outage and start-up period and that it was not unusual that additional work needed to be completed that could not have been identified prior to the time when start-up and other final activities were actually conducted. Maintaining the outage schedule was of utmost importance to the project management team so that Unit 4 could return to service in a timely manner to meet customers' load requirements. IPL exercised opportunities in several areas to reduce costs without sacrificing quality and while maintaining the overall outage schedule.

Finally, Mr. Kehres testified that IPL is continuing to investigate issues arising under a contract related to work performed on the Pete 4 FGD upgrade. Once the investigation is complete and a resolution has been reached, IPL will address the issue in a future ECR filing. While IPL does not know at this time the estimated impact of this issue on the final costs of the Pete 4 FGD upgrade, IPL has identified approximately \$900,000 of extra work tickets for labor that will likely increase the final cost by at least that amount. IPL will seek to minimize the impact of this issue on the final cost of the project.

Thomas Moore provided a review of the implementation of IPL's SCR Catalyst Management Program. Mr. Moore provided information regarding the replacement and refurbishment expenditures that will be incurred incident to operation of IPL's SCR systems at Petersburg Units 2 and 3 and Harding Street Unit 7, for which recovery will be sought in future

proceedings. Mr. Moore also presented new and updated information regarding the continuing processes for the SCR Catalyst Management Program and SCR System modifications to be undertaken as a result of year-round operation of the SCR Systems presently installed, as well as updates for the Petersburg Unit 3 FGD System and the SBS Injection System.

Mr. Moore stated that previously several system modifications were identified to provide safe and efficient SO<sub>2</sub> and NO<sub>x</sub> reduction throughout the year. From 2009 through the end of 2011, IPL completed much of this work for the Petersburg Units 2 and 3 SCR Systems as well as the Harding Street Unit 7 SCR System. The next scheduled outages for these units are in the fall of 2012 (Unit 3) and the fall of 2013 (Unit 2 and Unit 7). Most of the remaining tasks cannot be performed while the equipment is in operating mode. Therefore, only periodic and routine Unit 3 activities relating to the SCR reactors, including ash removal, catalyst layer change out, and sonic horn maintenance, are planned for the next six-month period.

Mr. Moore identified and described equipment modifications and additions. While most of the modifications and additions identified in IPL's ECR 13 through ECR 18 proceedings were completed and placed in service, a few remain to be initiated during the next six-month period. These include the following: (1) erection of horizontal walkways and platforms for safety access to the outlet slope areas of the Petersburg Unit 2 SCR, including a direct walkway access from the sixth floor of Unit 2 to the SCR outlet dampers; and (2) replacement of critical safety-related equipment in certain portions of the Process Safety Management system.

Mr. Moore stated that now that the SCR Systems have accumulated in excess of 40,000 hours of operation, it is prudent to repair and replace equipment to maintain the safe and efficient operation of the SCR systems. The types of equipment most likely to require replacement due to wear and failure are analyzers, pumps, valves, piping, and acoustic horns. During the recent outage for the Petersburg Unit 2 SCR, sonic horn insulation modules were found to be brittle from thermal shock during year-round operation. The modules were subsequently replaced with new thermal blankets that serve the same function. Similar conditions were found to exist on the Unit 3 system and several insulation modules will be replaced on that system as well. In addition, one of the redundant ammonia vaporizers on the Unit 2 system recently failed and is scheduled for replacement later this year. During early 2012, the Petersburg Unit 3 SCR sustained roof and structural damage. To assist in the determination of the primary cause of the structure damage, additional internal inspections will be conducted during the fall 2012 outage. Although additional repairs are not anticipated, any necessary remediation will be performed during the outage period. IPL also anticipates a need to replace two catalyst layers for Petersburg Unit 2 during the next scheduled unit outage in the fall of 2013.

Mr. Moore stated that the process upgrade project to the existing FGD System on Petersburg Unit 3 has been completed and the project was placed in service on June 24, 2006. A later inspection of the stack liner revealed several buckling problem areas with the alloy wallpaper and the carbon steel base material on upper sections of the stack liner. The alloy wallpaper was repaired during the planned unit outage during the fall of 2009. Further investigation found several additional damaged areas and the need for bracing to prevent additional damages. An action plan was implemented during the unit outage in the first half of 2011. A plan for external stiffening of the stack liner was executed during the same outage. During the next Unit 3 scheduled outage, in the fall of 2012, the repairs will be inspected and the need for additional work will be determined.

Greg Daeger described the ongoing capital maintenance projects and IPL's projected O&M expenses related to IPL's emissions control equipment. The two Harding Street Unit 7 ID Fan Discharge Duct Expansion Joints, the 7-1 Booster Fan Outlet Expansion Joint, the Wet Stack Breach Expansion Joint, and the FGD Inlet Expansion Joint failed and required replacement to prevent excessive air in-leakage and duct corrosion. In addition, the Harding Street Unit 7 FGD Ball Mill, Ball Handling Equipment was replaced to provide a safe means of loading balls into the Ball Mills. The Harding Street Station Unit 7 FGD Reagent Feed Valve, SBS Soft Water Tank Heaters, and two SCR Seal Air Expansion Joints and the Vaporizer also failed and required replacement.

Mr. Daeger also identified the capital maintenance projects planned for the next 6-month period. The Harding Street Unit 7 FGD Reagent Feed Piping is failing frequently due to internal erosion and requires replacement to eliminate leaks and subsequent FGD downtime.

Finally, Mr. Daeger testified that IPL has worked with its plant personnel to adjust the O&M estimate prepared for this filing to reflect any known changes from the most recent annual budget. An opportunity was identified and implemented to sell additional gypsum from Harding Street Station Unit 7 FGD, resulting in lower future gypsum disposal costs. A Petersburg Station Unit 4 FGD Ball Mill overhaul was budgeted for early 2012 and will be completed in fall 2012. In addition, funds originally allocated for a spring 2012 Petersburg Station Unit 2 SCR outage were reallocated to a fall 2012 Petersburg Station Unit 3 SCR outage.

Dwayne Burke provided an update on IPL's compliance plan with the EPA-mandated Clean Air Interstate Rule ("CAIR") emission reduction requirements. The NO<sub>x</sub> annual and summer ozone season emission reduction requirements have remained the same since CAIR was expanded in 2009. At that time, an annual NO<sub>x</sub> emission reduction requirement was added to the already existing summer ozone season (May 1 through October 31) requirement. The SO<sub>2</sub> emission reduction requirements have remained the same for approximately the last decade.

Mr. Burke stated that IPL will meet the 2012 annual and summer ozone season emission reduction requirements in the same manner as IPL has done over the last several years. First and foremost, IPL will meet the requirements primarily through the successful operation of its NO<sub>x</sub> pollution control equipment and the existing SCR catalyst management plan for Petersburg Unit 2, Petersburg Unit 3, and Harding Street Unit 7. As IPL has done in the past, it may be required to supplement its compliance plan with the purchase of allowances on the open market. In a similar fashion to NO<sub>x</sub>, IPL will meet its 2012 SO<sub>2</sub> obligations primarily through the successful operation of its existing pollution control equipment, which includes scrubbers on all of IPL's Big 5 units. In addition, IPL may be required to purchase SO<sub>2</sub> allowances on the open market to supplement its compliance plan. Any NO<sub>x</sub> or SO<sub>2</sub> allowance purchases would not be material because the allowance markets for both NO<sub>x</sub> and SO<sub>2</sub> collapsed following the court-ordered stay of the Cross-State Air Pollution Rule ("CSAPR") and vintage allowance markets for SO<sub>2</sub>, NO<sub>x</sub> season, and NO<sub>x</sub> annual continue to trade at historical lows.

Mr. Burke explained that implementation of CSAPR, which was scheduled to become effective on January 1, 2012, was stayed in December 2011 by order of the U.S. Court of Appeals for the District of Columbia pending resolution of legal challenges to the rule. The stay puts CSAPR on hold pending resolution by the Court. A hearing on the legal challenges was held by the Court in April 2012, but a final decision date from the Court is unknown. It appears CAIR will

remain in effect for at least 2012 and 2013. Thus, the new CSAPR, if one is issued, will not become effective until 2014 at the earliest in order to allow the regulated community ample time to prepare. Until that time, CAIR will remain the regulatory obligation for NO<sub>x</sub> and SO<sub>2</sub>.

Craig Forestal addressed the costs that IPL has incurred for its CCT projects from the date such projects commenced construction until May 31, 2012. He also addressed IPL's request for recovery of depreciation, O&M expenses, and the benefit IPL proposes to provide to its customers related to its disposition of NO<sub>x</sub> and SO<sub>2</sub> emission allowances that will be included in this filing. IPL accrued Allowance for Funds Used During Construction ("AFUDC") on construction expenditures for each ECR filing until their respective ECCRA factors became effective. He stated that the CCT projects for which IPL is seeking recovery have been under construction at least six months, at a cost of \$620 million, inclusive of AFUDC and net of retirements through May 31, 2012.

Mr. Forestal explained the process by which IPL revises its AFUDC rate and explained that IPL's accounting procedures for accrual of AFUDC costs are consistent with the USOA and the Commission's prior practice. He said that IPL has established accounting procedures and maintains its records to reflect the discontinuance of AFUDC on the CCT projects, or portions of CCT projects, once they are included in the ECCRA. He added that the ratemaking treatment will continue until the CCT projects are found to be used and useful and included in rate base, in a proceeding that involves the establishment of IPL's basic rates and charges.

Mr. Forestal stated IPL's Exhibits CF-2 NO<sub>x</sub> and CF-2 MPP contain items that were approved in ECR 14 through ECR 16 and that IPL is also requesting recovery of an incremental \$0.5 million of capital maintenance items added during the period ending May 31, 2012, including accumulated AFUDC. The ECCRA factor also includes forecasted depreciation and O&M expenses for all projects that are now in service for the billing period of September 2012 through February 2013. The amount of estimated depreciation expense included in this proceeding is \$18.8 million, and IPL has estimated O&M expense of \$9.3 million associated with the CCT controls that are now in service. These estimated O&M expenses were for ammonia and urea costs that will be consumed for the operation of the SCRs and selective non-catalytic reduction ("SNCR") systems, limestone, chemicals, and labor costs (including benefits) for the operation of the FGDs, as well as for maintenance of the equipment.

Mr. Forestal testified that in the Order in Cause No. 43403, the Commission required IPL to include in each ECCRA filing the actual amount of SO<sub>2</sub> allowances consumed in the sale of off-system power from the jurisdictional portion of the Pete 4 FGD upgrade project. Mr. Forestal indicated there were \$374 worth of SO<sub>2</sub> allowances consumed for the period ended May 31, 2012.

Mr. Forestal provided additional support for IPL's treatment of capital maintenance items as substantial additions. IPL uses the term "capital maintenance" to refer to items installed in its pollution control equipment which replace equipment that (1) was capitalized and is included in IPL's utility plant balance, (2) was included in the original CPCN granted for pollution control equipment, (3) has since failed or been damaged, (4) was determined to be a unit of property when it was originally installed, and (5) is not considered a substantial betterment compared to the original equipment being replaced. Replacement of items that were originally capitalized but not considered to be units of property are expensed as maintenance, and IPL uses the term "unit of property" to be synonymous with the term "retirement unit." IPL consistently capitalizes items that

replace failed or damaged equipment that was designated to be a unit of property regardless of whether the original equipment was included in the CPCN and eligible for timely recovery. This practice is required by the Uniform System of Accounts (“USOA”) (CFR Part 101, Section 10) and Federal Energy Regulatory Commission Order No. 598 issued on February 5, 1998. IPL’s financial practices and procedures are established to ensure proper compliance with the USOA’s treatment of asset acquisition, depreciation, transfer and disposition.

Mr. Forestal stated that while FERC does not provide a definition for the term “unit of property” or “retirement unit,” the Edison Electric Institute defines units of property as, “an assemblage of equipment consisting of individual items usually considered as a whole for determining the accounting treatment for replacement of the equipment.” Based on this guidance, the items included in this filing as capital maintenance were determined to be units of property by IPL accounting personnel years ago independent of the regulatory tracker process.

Mr. Forestal explained that capital maintenance costs are recovered in the same manner as Utility Plant included in the CPCN, which is over the estimated useful life of the item and including a return. Both the estimated useful life (18 years) and the return were agreed upon in the Stipulation and Settlement Agreements for the NO<sub>x</sub> (Cause No. 42170) and Multi-Pollutant Plan (Cause No. 42700) programs. Conversely, maintenance expenses are recovered by IPL over a six-month period without a return.

Mr. Forestal stated that IPL’s Exhibit CF-2 NO<sub>x</sub> and IPL’s Exhibit CF-2 MPP reflect retirements related to the capital maintenance items replaced. To reflect the recorded retirement entries, the original cost of the retired assets has been shown separately as a reduction from clean coal technology utility plant, and accumulated depreciation was reduced. Additionally, the forecasts for depreciation have been adjusted to remove depreciation for the items replaced.

Finally, Mr. Forestal explained that IPL’s Exhibit CF-6 summarizes demolition costs related to the Pete 4 FGD upgrade, as required by Cause No. 43403. These amounts are shown for illustrative purposes only and are not included in the calculation of the ECCRA. These costs were excluded from accumulated depreciation on IPL’s Exhibit CF-2 MPP2 and, therefore, do not impact the amount requested as “Allowed Return on CCT Utility Plant.”

James L. Cutshaw explained how the revenue requirements calculated by IPL Witness Forestal are to be allocated between jurisdictional and non-jurisdictional customers and further explained the allocation of the resulting jurisdictional revenue requirements between the retail customer classes. The retail allocation factor is based on the retail jurisdictional share of the twelve monthly average system peaks used to allocate production plant, operating expenses and depreciation expenses respectively from IPL’s cost of service study as used in IPL’s last general rate proceeding, Cause No. 39938. The use of this methodology was proposed by IPL and approved by the Commission in the Orders in Cause Nos. 42170, 42700, and 43403. IPL’s Exhibit JC-2 shows the allocation of jurisdictional revenue requirements as calculated in IPL’s Exhibit JC-1 to each individual rate class.

Mr. Cutshaw testified that the reconciled ECR 17 O&M and depreciation expense variances are calculated by Mr. Forestal and then transferred to IPL’s Exhibit JC-3 and allocated between jurisdictional and non-jurisdictional customers in the same manner as the revenue requirements on

IPL's Exhibit JC-1. The resulting jurisdictional revenue requirements are allocated to each individual rate class in the same manner as the revenue requirements on IPL's Exhibit JC-2.

Mr. Cutshaw stated the approved ECCRA factor will remain in effect until it is replaced by a different ECCRA factor that is approved in a subsequent filing or until the Commission determines that the projects are used and useful in a proceeding that involves the establishment of new base rates and charges. IPL anticipates that filings for approval for the recovery of environmental compliance related costs will be made approximately every six months.

5. **OUCC's Testimony.** Wes R. Blakley described the ratemaking treatment requested by IPL in this Cause and the OUCC's recommendation that IPL recalculate its revenue requirement using total construction costs for the Pete 4 FGD upgrade in the amount of \$124,535,848, which is equal to the \$128 million approved in ECR 16 S1 for the Pete 4 FGD upgrade less the \$3,464,152 for demolition costs. The OUCC recommended that the currently-approved construction cost amount not be increased to reflect the most recent cost overruns, as further explained by Ms. Armstrong and Mr. Eke. Mr. Blakley stated IPL has previously agreed that demolition costs should not be recovered through the ECCRA.

OUCC Witness Maclean O. Eke testified regarding the project scope of the Pete 4 FGD upgrade and related cost increase. The OUCC was concerned that IPL found, subsequent to the Petersburg Unit 4 FGD going into service, that additional work was needed on the project. The OUCC was also concerned that IPL failed to properly scope the Petersburg Unit 4 FGD Enhancements project and develop a detailed description of the project. Mr. Eke concluded that IPL's project management did not control the scope of the project. The project experienced movements in the individual line items and incurred Project Adders throughout the construction phases.

Mr. Eke said the OUCC was concerned that IPL failed to improve the accuracy in the breakdown of IPL's cost estimates as set forth in IPL's Exhibit DK-4. A review of the electronic version of the exhibit showed inconsistencies and vagueness in the input data used to populate the cells. There was ambiguity in the way the project cost estimate under the ECR 16 column was depicted. He identified several columns that appeared to be inconsistent because they alternated between hard-keyed numbers and formula calculations. Mr. Eke stated that the OUCC observed similar inconsistencies in the formulas of some Excel spreadsheet cells used to produce the charts in IPL's Exhibit DK-3.

Mr. Eke said there also seems to be some ambiguity in the way IPL has treated the Removal Costs line items throughout the various ECR columns presented in IPL's Exhibit DK-4. It seems IPL treats the Removal Costs as a cushion to maintain and support the overall cost estimate level. The various components of the Removal Cost were netted out of line items above the Total Construction Cost line, before Project Adders were included. However, under the ECR 18 column, these components were not subtracted from (or netted out of) the line items above the Total Construction Cost line.

Mr. Eke observed that some line items, whose costs can generally be locked in early in the project, still experienced movements all through the late stages of construction. Some typical late-stage construction work programs and activities, such as testing and inspection of equipment that should have been included in the project-scope phase were added at a very late stage of

construction. The combination of the movements in the individual line-item costs and the Project Adders occurring at the late stages of construction were signs that the project scope was not properly defined. The consequences of failing to properly define and scope the project were uncontrollable changes in costs, processes, labor, materials, and equipment, resulting in project scope creep.

According to Mr. Eke, IPL poorly managed the necessary project scope process, which resulted in the uncontrollable changes in costs, processes, labor, materials and equipment seen in this Cause. These uncontrolled changes directly translated to cost increases, thereby placing the ratepayers in the precarious position of bearing additional risk. The OUCC understands that change is inevitable, but it was the persistent and uncontrolled changes transpiring throughout the project life cycle that raised questions and concerns. The primary reason for actual costs varying from contractors original bid price were changes in the work scope and incorrect work quantity estimates included in the original bid specifications.

Mr. Eke concluded that IPL has not demonstrated diligence in administering the enhancement of the Pete 4 FGD upgrade, and recommended that the Commission disapprove IPL's requested cost increase. He said that IPL needs to establish better procedures that will ensure more accurate contract design quantities that will provide better engineering estimates of costs before projects go out to bid.

Cynthia M. Armstrong testified that the OUCC opposes IPL's latest request for an increase in the project cost that can be recovered through the ECCRA. She agreed that many of the additional project items are necessary to complete the project, which has been in service since the end of November 2011. However, the OUCC does not agree that IPL's ratepayers should continue to bear the risk of cost increases due to inaccurate cost estimates presented in the initial case requesting a CPCN for the Pete 4 FGD upgrade. Ms. Armstrong stated the LOTO productivity loss appeared to have been caused by another contractor and therefore the OUCC does not view the additional expense to be reasonable for inclusion in project costs recovered from ratepayers. The OUCC has concerns regarding IPL's management of project costs and enforcement of strict budget and timeframes with its contractors and claimed that the cost overruns on pollution control projects illustrate there is little incentive for IPL to curb project costs if the utility knows it will receive rate relief for increased project spending within 6 to 10 months.

Ms. Armstrong proposed a soft cap for the Pete 4 FGD upgrade costs at an amount of \$124.535 million. She explained that a soft cap would mean that IPL could seek recovery of any costs incurred above the cap in a general rate case.

**6. Settlement Agreement and Testimony in Support of the Settlement Agreement.**

A copy of the Settlement Agreement is attached and incorporated by reference into this Order. The Settlement Agreement provides the following terms:

1. IPL agrees not to seek recovery through the ECR tracker filings for construction costs related to the Pete 4 FGD upgrade over \$128 million (the CPCN amount as approved in ECR 16 S1) less actual removal/demolition costs of \$3,364,169 (per Exhibit CF-6).

2. IPL will file modified accounting schedules in ECR 19 to reflect the removal of \$1,129,000 (from Exhibit CF-2 MPP2 page 2) related to the amount over \$124,635,831, which is the previously approved amount of \$128 million less actual removal costs of \$3,364,169 (per Exhibit CF-6).
3. The OUCC agrees to support the increase to the CPCN for the Pete 4 FGD upgrade by \$1.6 million to a new total of \$129.6 million, understanding that IPL will not seek recovery of the additional \$1.6 million in the ECR tracker filings but will include these costs in rate base in its next basic rate case. The OUCC will not challenge these costs (i.e. the additional \$1.6 million) for recovery during IPL's next rate case. There will be no special accounting treatment (such as post-in service AFUDC or other "carrying charges" or deferred depreciation) for amounts not recovered through the ECR tracker filings.
4. IPL may include amounts (if any) related to the Pete 4 FGD upgrade over the \$1.6 million modification to the CPCN in its proposed rate base at the time of its next rate case. However, all of the OUCC's rights will be preserved to review and potentially challenge the reasonableness of any costs in excess of the \$129.6 million CPCN amount at the time of the next base rate case.
5. IPL agrees to credit any reduced charges or concessions received from contractors involved in the Pete 4 FGD upgrade toward the final cost of the project.

Mr. Cutshaw offered testimony in support of the Settlement Agreement. He provided an overview of the terms of the Settlement Agreement. He explained that the Settlement Agreement is the result of serious negotiations and bargaining, with the parties considering various options, evaluating the issues, and ultimately reaching a settlement in the public interest to resolve the issues pending before the Commission in this proceeding. He stated the Settlement Agreement reflects compromise and resolves the disputed issues in this proceeding without further expenditure of the time and resources of the Commission and the parties in litigating the contested issues to a conclusion. He added that the Settlement Agreement reasonably responds to concerns raised by the OUCC. He said that IPL disagrees that there was any mismanagement of the Pete 4 FGD upgrade and believes that IPL's request in this proceeding is consistent with the ongoing review process. Mr. Cutshaw said the Settlement Agreement mitigates controversy and reasonably addresses the OUCC's desire that no further changes in the Commission-approved cost estimate be sought in the ECR proceedings, but that such costs should be treated as rate base additions in IPL's next general rate case.

Mr. Cutshaw also responded to some of the concerns raised in the OUCC's direct testimony. Mr. Blakley's calculation of the construction cost approved in ECR 16 S1 for the Pete 4 FGD of \$124,535,848 was determined by deducting estimated removal costs (shown in the ECR 18 and ECR 19 filings) from the \$128 million CPCN amount. Actual removal costs were \$3,364,169, as shown on IPL's Exhibit CF-6. These costs have not been included in the amounts IPL submitted for ECR recovery in any of the filings since they began to be incurred in ECR 16. He said the Settlement Agreement provides that the soft cap of \$124,635,831 (determined by deducting actual demolition costs from \$128 million) will be the maximum amount recoverable through the ECR filings.

Mr. Cutshaw disagreed with Mr. Eke's characterization of Removal Costs as a cushion to maintain the overall cost estimate level. He noted that removal costs have always been included in the overall cost estimate level, but were not separately identified on IPL's Exhibit DK-4 until ECR 18.

Mr. Cutshaw testified that at this time, the only known additional project costs that are not included in the \$129.6 million updated cost estimate relate to on-going negotiations with a contractor for work performed on the Pete 4 FGD upgrade. He said this item was discussed in the Direct Testimony of IPL Witness Kehres and in further detail in the Settlement Testimony of IPL Witness Scott. Mr. Cutshaw explained that although IPL believes such costs would be appropriately recoverable through the ECR filings once resolved, it is willing to abide by the agreed upon soft cap and wait until its next rate case to begin recovery.

With respect to the provision of the Settlement Agreement regarding reduced charges or concessions received from contractors involved in the Pete 4 FGD upgrade, Mr. Cutshaw stated that this provision memorializes what IPL would have done of its own accord, and is consistent with the OUCC's stated desire of ensuring that IPL is holding contractors responsible for their performance. At this time, the only outstanding item is the replacement of 193 failing slurry valves estimated at \$191,000 to be backcharged to the contractor as discussed in the Direct Testimony of Mr. Kehres.

Finally, Mr. Cutshaw discussed the steps taken by IPL to keep the Commission and other parties informed as to the status of the Pete 4 FGD upgrade. IPL has maintained an open and transparent approach to communicating potential cost increases associated with the Pete 4 FGD upgrade. In ECR 15, IPL worked with the OUCC to improve the future flow of cost information between IPL, the OUCC, and the Commission. Mr. Cutshaw discussed the informal communications provided by IPL to the OUCC and the Commission identifying specific items that resulted in a need to increase the cost estimate in ECR 16 and in this proceeding. He stated that in ECR 16, ECR 18 and ECR 19, IPL technical staff met with OUCC staff to discuss IPL's cost estimates and the construction progress on the project. IPL has also responded to significant discovery, both formal and informal, regarding the progress of the Unit 4 upgrade. Mr. Cutshaw concluded that the Settlement Agreement reflected a fair and reasonable resolution of the contested cost estimate issues.

Bradley Scott, Senior Director, Plant Operations, testified in support of the Settlement Agreement and addressed certain issues raised in the direct testimony of OUCC witnesses Armstrong and Eke. He testified that the resolution of the soft cap recommendation set forth in the Settlement Agreement is reasonable and reflects that there is no significant dispute that the \$1.6 million in costs presented for Commission review in this proceeding were necessary. He said the resolution of the soft cap recommendation set forth in the Settlement Agreement recognizes that the \$1.6 million in costs presented during the ongoing review process are reasonable and necessary, mitigates controversy, and reasonably addresses the OUCC's desire that no further changes in the Commission-approved cost estimate be sought in the ECR proceedings. The Settlement Agreement recognizes that such costs should be treated as rate base additions in IPL's next general rate case and not subject to challenge at that time.

Mr. Scott stated that Ms. Armstrong's suggestion that the project has exceeded its original cost estimate by more than 40% warrants clarification and must be viewed in context. The original cost estimate approved by the Commission was lower than the cost estimate IPL presented in the

initial CPCN proceeding for this particular project, which was \$98.49 million. IPL agreed to Commission approval of a \$90 million cost estimate based on the express understanding that IPL could seek approval of additional costs through the ongoing review process as the project continued. Further, the cost study IPL presented in the CPCN proceeding explained that while an escalation rate was included, due to volatile market conditions with respect to materials, equipment, and the labor market, the pricing summary should be used with caution. He said that in other words, costs can and have increased due to the passage of time and market conditions.

Mr. Scott said the passage of time is relevant here because the Pete 4 FGD upgrade was reasonably postponed due to the uncertainty associated with the federal CAIR. He testified that the postponement of the project was disclosed to the Commission and the OUCC and undertaken without objection. While IPL ended up moving forward with the project, the postponement was reasonable because it preserved the option to change course or eliminate this project and its associated cost for the benefit of customers in the event of a change in the underlying regulation.

Mr. Scott next addressed why the Settlement Agreement was reasonable in light of Mr. Eke's concerns that IPL failed to ensure that the project included only the work required to complete the project successfully. He explained that Mr. Eke's assertion was made without the benefit of a detailed knowledge of IPL plant operations and the limitations that are created when design decisions are required to be made without the ability to physically inspect many of the components that need to be modified. In order for IPL to have completely scoped the project in advance the unit would have been required to be out of service for an extended period of time to allow for such an analysis of the systems, their condition, and current operating environment. Because Unit 4 is currently one of the lowest cost producers of electricity in IPL's fleet and also one of its largest, removing it from service for an extended period would have increased the cost of power to IPL's customers but would not have changed the overall project cost, because the overall scope is still what was required to complete the upgrade. Mr. Scott pointed out that the project team did look into other ways to gain further insight into the requirements and challenges that could occur during the outage.

Mr. Scott testified that in his opinion, and given the circumstances and difficulty of trying to scope an upgrade project on a generating unit that is in service, IPL controlled the scope of the project as well as can be expected. He said that had this been a new construction project or even an additional piece of equipment that was to be added to the unit, one could expect better control of the scope. In IPL's perspective, the contention that IPL has not controlled supplier and vendor scope does not properly characterize the situation. Total material purchases were approximately \$44 million, of which one item, the initial ball charge for the ball mill (totaling \$125,849), was inadvertently omitted from the cost estimate submitted during ECR 17. Total field labor contracts for this project are approximately \$58 million. Of that total amount, the one item not included in the vendor scope concerned a coating application in the modified trench in the pump house. The cost of this work was \$33,852. Mr. Scott testified that only \$159,701 out of approximately \$102 million in materials and labor costs (0.16%) was not reflected in the original scope for the vendor and suppliers. This small amount is not a material change and does not give rise to mismanagement. Even if these costs had been identified and tracked earlier, the same project costs would have occurred for both items and both were required for safe and effective operation of the upgraded FGD.

Mr. Scott testified that he believed IPL managed the project very well given the requirements of its various stakeholders. IPL first and foremost attempted to continue to provide low cost electricity to its customers by keeping Unit 4 in-service whenever possible. IPL also tried to minimize the cost of the project by developing many of the design requirements while the unit was in service and by attempting to perform as much of the construction as possible without removing the unit from service. Some parts of the project were completed at less than their estimated cost, as described by Mr. Kehres' direct testimony. This discussion shows that IPL has worked to manage and control costs.

Mr. Scott next addressed Mr. Eke's suggestion that repeated requests for increases in the approved cost estimate are cause for concern. The Settlement Agreement is reasonable despite this concern because regardless of when the scope was ultimately defined, the overall cost of the project would not have changed. None of the cost increases were for frivolous or unwarranted components. Mr. Scott acknowledged that while it is preferable to have a fully defined scope, that goal is not reasonably possible for the reasons discussed above. Further, upgrade projects always carry a significant level of uncertainty that cannot be mitigated ahead of time. Having good technical resources available to the project team minimizes the impact of these unknowns. At the time the project was first approved, it was subject to the understanding that IPL would use the ongoing review process to present additional costs for review as the project proceeded through engineering, construction, and installation. The presentation of additional costs in the ongoing review process is reasonable given the size and complexity of the project.

Mr. Scott explained how IPL worked to control costs and quality with regard to the Unit 4 upgrade. All field work was competitively bid and awarded to the contractor with the best qualified price. Project field engineers oversaw the field work and managed any extra work, which included daily time sheets with field engineer signoff. Field engineers also oversaw quality assurance/quality control activities, while plant personnel provided input to the project team if they observed or questioned the quality of any work installed by the contractor. Mr. Scott pointed out that in ECR 18 Ms. Armstrong testified regarding a number of the items that are included in the revised cost estimate submitted in this Cause and concluded that the OUCC was confident that IPL was adequately pursuing contractors for errors and questioning contractor's requests for additional funding, at least for the situations identified in that filing. IPL's project management has continued its efforts to pursue contractors for errors and to question requests for additional funding. The one remaining contractor issue is addressed in the Settlement Agreement provision that provides that amounts (if any) related to the Pete 4 FGD upgrade over the \$1.6 million modification of the CPCN may be included in IPL's proposed rate base at the time of its next rate case and shall be subject to challenge at that time.

According to Mr. Scott, the LOTO productivity loss identified by Ms. Armstrong relates to compliance with the LOTO process, which exists to protect worker safety. The \$1.6 million underlying IPL's request for an increase in the approved cost estimate for the Pete 4 FGD upgrade includes \$72,000 in costs IPL actually incurred for the LOTO Safety program. Much of this cost is associated with the complexity of trying to turn over completed equipment to the plant to allow them to begin commissioning activities. Mr. Scott described the LOTO process and testified that it is a common industry practice and that its cost is difficult to estimate with precision in advance of the actual work being performed. He opined that the fact that the actual cost for this safety program does not match the estimated cost is not an indicator that the safety program or its associated cost is unreasonable.

Mr. Scott explained that IPL has affordable rates for its customers and has an incentive to manage costs and keep them as low as possible for customers. He did not agree with Ms. Armstrong's characterization of the ongoing review process and in particular the suggestion that the utility knows that it will receive rate relief for increased project spending. He said that if the cost of the project exceeds the Commission approved estimate, the utility does not know that it will receive approval of the additional costs. Rather, the utility must seek and obtain approval of an increase in the project costs as part of the ongoing review process. The utility request will be scrutinized and may be challenged, as occurred in this proceeding. Because IPL does not have assurance that the cost increases will be approved, the incentive to manage costs is not affected by the ongoing review process. The fact that IPL was able to complete some of the individual components of the overall project at a cost that was lower than the estimate shows that IPL has worked to manage and control costs and has not adopted a view that cost recovery is assured. If the Commission were to adopt the view that a mere change in cost signals something is wrong, it could inadvertently send the signal that approved cost estimates should remain unchanged even though this may not be the reasonable choice in the long run. Mr. Scott said the better approach is to structure the ongoing review process in such a way that supports changes that are reasonable, efficient and consistent with good utility practice.

Mr. Scott stated that IPL did not include in its request to modify the CPCN cost estimate the costs associated with the ongoing negotiations with a contractor related to work performed on the Unit 4 upgrade. The mere existence of, or potential for, additional costs is not evidence that something has gone awry, but is the reason the ongoing review process exists. It would be unreasonable to conclude that the existence of ongoing vendor discussions casts a shadow of doubt on the costs reflected in the request for approval of the \$1.6 million increase to the approved cost estimate. Mr. Scott testified that the treatment of this issue in the Settlement Agreement recognizes that: a) it is reasonable for IPL and its contractor to try and resolve this contract issue on a business to business basis; b) because the discussions are ongoing, these matters cannot be discussed in detail at the time because doing so could adversely affect the negotiations; and c) IPL continues to work to control its costs and to hold its vendors accountable.

Mr. Scott also addressed Mr. Eke's concerns that some of the cost and scope increases IPL identified as new are actually "Project Adders" included in ECR 16 and ECR 18 work items. Mr. Scott said that the costs identified as "Project Adders" were items included in other line items that were pulled out and given specific line items in order to better track their costs. While IPL's reporting of these line items may have caused some confusion in the ongoing review process, the fact remains that from an operational perspective the work needed to be done to allow for the safe and efficient operation of the system.

With respect to Mr. Eke's comments regarding IPL's Exhibits DK-3 and DK-4, Mr. Scott explained that these exhibits reflect a snapshot of the project at given points in time and were prepared for use by the Project Manager and IPL's internal project management. These documents are tools, not formal reports, and were used by the Project Manager to identify or explain any major issues or concerns that were or could affect the project cost or schedule. Mr. Scott explained how these documents were used on a daily basis by the Project Manager and were subject to constant review and updating to reflect the latest information that was available to the Project Manager. During the course of the ECR proceedings, IPL agreed to share a copy of this tool with the OUCC in an effort of transparency, but in doing so, IPL did not intend to change the nature of this tool into something it is not.

Mr. Scott testified that it is reasonable for the approved cost estimate for the Pete 4 FGD upgrade to be increased to \$129.6 million. This work needed to be done in order to upgrade Unit 4's FGD to perform at a level necessary to achieve compliance with the various requirements described in Ms. Armstrong's testimony. The FGD on Unit 4 has been operating very well following its upgrade. Scrubbing efficiency is running in the 95% to 97% range and gypsum quality has been excellent, allowing it to be utilized in the production of wallboard, which reduces disposal costs. This performance illustrates that the scope of the FGD upgrade was reasonable and appropriate and has allowed the unit to achieve compliance with the CAIR and NAAQS requirements. This allows IPL to continue to provide low cost electricity to its customers from the output of Petersburg Unit 4.

Mr. Forestal sponsored modified accounting schedules and a revised tariff sheet to reflect changes discussed in the Settlement Agreement. He explained that in accordance with the Settlement Agreement, IPL's Revised Exhibit CF-2 MPP2 page 1, Line 1, column C (Incremental Clean Coal Technology Utility Plant) has been reduced by \$1,129,000. This amount represents the excess costs over \$124,635,831, which is the previously approved amount of \$128 million less actual removal costs of \$3,364,169. The schedule was also modified to reflect the corresponding reductions to Carrying Charges and Depreciation Expense. The changes on Page 1 of Revised Exhibit CF-2 MPP2 Page 1 are then reflected in the Tracker Balances on Page 2 of Revised Exhibit CF-2 MPP2. The Revenue Requirements are carried over to IPL's Revised Exhibit JC-1 and allocated by Rate Class on IPL's Revised Exhibit JC-2. The allocations by Rate Class on Revised Exhibit JC-2 are carried over to Revised Exhibit CF-3, which reflects the modified rates on line 7. After taking into consideration the changes proposed in these revised exhibits, an average residential customer using 1,000 kWh per month will experience an increase of \$0.222 or 0.301% per month, relative to the ECCRA factor and basic rates and charges currently in effect.

Ms. Armstrong also testified in support of the Settlement Agreement. She explained the terms of the Settlement Agreement and stated that the Settlement Agreement resolved the OUCC's concerns that IPL is not managing project costs effectively or containing cost increases to the best of its ability. The soft cap that the Settlement Agreement places on the Pete 4 FGD upgrade mitigates the near-term impact of the project on ratepayers and requires IPL to bear more risk associated with the project increases. With the soft cap in place, IPL will have additional incentive to keep additional project costs to a minimum, because the company will not be able to receive the accelerated rate relief provided by the ECR trackers for direct project costs over \$124.636 million. In addition, IPL will not be able to receive special accounting treatment for costs above the soft cap, which Ms. Armstrong stated would further incent the company to keep project costs as low as reasonably possible.

Ms. Armstrong explained that the OUCC's agreement not to challenge the inclusion of up to \$1.6 million in additional project costs spent on the Pete 4 FGD upgrade in IPL's next rate case was a fair term of the Settlement Agreement. The OUCC has extensively reviewed the additional project costs presented in IPL's revised cost estimate and has determined these project costs to be necessary to safely construct and operate the FGD unit. The project is still needed in order to provide reliable electric service to IPL's customers in compliance with impending environmental regulations. Second, this is not a complete ban on the OUCC's ability to challenge costs associated with the project in the future. The OUCC is reserving the right to thoroughly examine the prudence of any costs above and beyond the \$1.6 million in IPL's next rate case.

Ms. Armstrong noted that any reduced contractor fees or concessions that IPL receives as a result of its pending negotiations with contractors on the project will be applied towards the project's final direct cost, which means that ratepayers will receive the full benefit of any favorable outcomes arising from contractor disputes. In exchange for all of these conditions, IPL will be able to receive cost recovery without further presentation of evidence of up to \$126,235,831 in project costs, which is \$129.6 million (the new CPCN authorized level) in total project costs for the Pete 4 FGD upgrade less actual demolition costs incurred by the company to date.

Ms. Armstrong testified that the Settlement Agreement represents a reasonable and fair arms-length negotiation between the settling parties and is in the public interest. The settlement assists in mitigating the overall rate impact of the project and provides certainty of the costs passed through to ratepayers in the ECR tracker over the short-term. The OUCC believes that the Settlement Agreement fairly resolves the concerns it raised in its direct testimony regarding the increased costs of the Pete 4 FGD upgrade. Therefore, the OUCC recommended Commission approval of the Settlement Agreement in its entirety.

**7. Commission Discussion and Findings.** Settlements presented to the Commission are not ordinary contracts between private parties. *United States Gypsum, Inc. v. Indiana Gas Co.*, 735 N.E.2d 790, 803 (Ind. 2000). When the Commission approves a settlement, that settlement “loses its status as a strictly private contract and takes on a public interest gloss.” *Id.* (quoting *Citizens Action Coalition of Ind., Inc. v. PSI Energy, Inc.*, 664 N.E.2d 401, 406 (Ind. Ct. App. 1996)). Thus, the Commission “may not accept a settlement merely because the private parties are satisfied; rather [the Commission] must consider whether the public interest will be served by accepting the settlement.” *Citizens Action Coalition*, 664 N.E.2d at 406.

Further, any Commission decision, ruling, or order – including the approval of a settlement – must be supported by specific findings of fact and sufficient evidence. *United States Gypsum*, 735 N.E.2d at 795 (citing *Citizens Action Coalition of Ind., Inc. v. Public Service Co. of Ind., Inc.*, 582 N.E.2d 330, 331 (Ind. 1991)). The Commission's own procedural rules require that settlements be supported by probative evidence. 170 IAC 1-1.1-17(d). Therefore, before the Commission can approve the Settlement Agreement, we must determine whether the evidence in this Cause sufficiently supports the conclusions that the Settlement Agreement is reasonable, just, and consistent with the purpose of Indiana Code ch. 8-1-2, and that such agreement serves the public interest.

With the single exception discussed below, we find that the evidence presented by the parties demonstrates that the Settlement Agreement is a fair, just, and reasonable resolution of the matters pending before the commission and is in the public interest. The Settlement Agreement sets forth the resolution of the disputed issues in this proceeding and provides the method used to determine the agreed ECR-19 factor. The agreed factor reflects an adjustment of the factors proposed in IPL's case-in-chief to remove the amount over \$124,635,831 for the Pete 4 FGD upgrade. The Settlement Agreement also addresses how costs over this amount will be treated in subsequent ECR filings and in IPL's next base rate case.

In Revised Petitioner's Exhibit CF-3, the following ECCRA rate for each customer class was proposed:

\$0.007537 per kWh for Rates RS and CW (with associated Rate RS service).

\$0.011598 per kWh for Rates SS, SH, OES, UW, and CW (with associated SS service).

\$0.006467 per kWh for Rates SL, PL, PH, and HL

We find that the proposed Rider Adjustments were properly calculated. Therefore, we approve the Rider Adjustments contained in Revised Petitioner's Exhibit CF-3, as shown on Revised Petitioner's Exhibit A. The Rider Adjustments shall become effective for all bills rendered for electric services beginning with the first billing cycles for the December 2012 billing month.

The Settlement Agreement also proposes that the CPCN should be modified to increase the Pete 4 FGD upgrade cost estimate by \$1.6 million to a new total of \$129.6 million. We find that the evidence in this case shows that public convenience and necessity will be served by the construction, implementation, and use of Petitioner's CCT projects. However, we do not agree with the inclusion of a portion of the proposed \$1.6 million increase.

On October 10, 2012, the Presiding Officers issued a docket entry requesting additional information regarding approximately \$191,000 of expenses for failing slurry valves that Petitioner's evidence indicated would be backcharged to the contractor. Based on Petitioner's responses to the docket entry, it appears that the use of unsuitable valves was due to a contractor's error and that Petitioner is in the process of negotiating the backcharge with the contractor with a "high chance of a favorable outcome." In light of this evidence, we find that there is a high chance this cost will not be IPL's responsibility and, as a result, \$190,656 should be deducted from the proposed \$1.6 million CPCN increase. With this modification, we approve IPL's construction work through May 31, 2012, and we grant IPL a modification of its CPCN for the construction cost estimates of the Pete 4 FGD upgrade as discussed above.

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

1. The Settlement Agreement is approved with the modification discussed in Paragraph 7 above.
2. IPL's proposed rate adjustments in its ECCRA as set out in Paragraph 7 of this Order are approved.
3. Pursuant to 170 IAC 4-6-21, IPL shall add the approved return on its QPCP to its net operating income authorized by the Commission for the purposes of Ind. Code §§ 8-1-2-42(d)(2) and 8-1-2-42(d)(3) in all subsequent Fuel Adjustment Charge proceedings. However, for purposes of computing the authorized net operating income for Ind. Code §§ 8-1-2-42(d)(2) and 8-1-2-42(d)(3), the jurisdictional portion of the increased return shall be phased-in over the appropriate period of time that IPL's net operating income is affected by this earnings modification resulting from the Commission's approval of this QPCP Construction Cost Rider.
4. Prior to placing the proposed rate adjustment into effect, IPL shall file with the Electricity Division of the Commission an amendment to its tariff reflecting the approved QPCP Construction Cost Rider rate adjustments contained in Revised Petitioner's Exhibit CF-3, as shown in Revised Petitioner's Exhibit A.

5. IPL's request for a modification of its CPCN for the construction cost estimates of the CCT projects as set forth in the Settlement Agreement and modified in Paragraph 7 above is granted.

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

**ATTERHOLT, BENNETT, MAYS AND ZIEGNER CONCUR; LANDIS ABSENT:**

**APPROVED:** NOV 21 2012

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



**Brenda A. Howe  
Secretary to the Commission**

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

VERIFIED PETITION OF INDIANAPOLIS )  
POWER & LIGHT COMPANY FOR )  
MODIFICATION OF ITS CERTIFICATE OF )  
PUBLIC CONVENIENCE AND NECESSITY ) CAUSE NO. 42170-ECR-19  
TO USE CLEAN COAL TECHNOLOGY AND )  
QUALIFIED POLLUTION CONTROL )  
PROPERTY AND FOR APPROVAL OF AN )  
ADJUSTMENT TO ITS RATES THROUGH )  
ITS APPROVED ENVIRONMENTAL )  
COMPLIANCE COST RECOVERY )  
ADJUSTMENT COMMENCING WITH THE )  
SEPTEMBER 2012 BILLING CYCLE IN )  
ACCORDANCE WITH THE ONGOING )  
REVIEW PROCESS )

STIPULATION AND SETTLEMENT AGREEMENT

Indianapolis Power & Light Company (“IPL” or “Company”) and the Indiana Office of Utility Consumer Counselor (“OUCC”), (collectively the “Parties” and individually “Party”) solely for purposes of compromise and settlement and having been duly advised by their respective staff, experts and counsel, stipulate and agree that the terms and conditions set forth below represent a fair, just and reasonable resolution of the matters set forth below, subject to their incorporation by the Indiana Utility Regulatory Commission (“Commission”) into a final, non-appealable order (“Final Order”) without modification or further condition that may be unacceptable to any Party. If the Commission does not approve this Stipulation and Settlement Agreement (“Agreement”), in its entirety, the entire Agreement shall be null and void and deemed withdrawn upon written notice as provided below.

A. TERMS AND CONDITIONS

1. IPL agrees not to seek recovery through the ECR tracker filings for construction costs related to the Pete 4 FGD upgrade over \$128 million (the CPCN amount as approved in ECR-16-S1) less actual removal/demolition costs of \$3,364,169 (per Exhibit CF-6).

2. IPL will file modified accounting schedules in ECR-19 to reflect the removal of \$1,129,000 (from Exhibit CF-2 MPP2 page 2) related to the amount over \$124,635,831, which is the previously approved amount of \$128 million less actual removal costs of \$3,364,169 (per Exhibit CF-6).

3. The OUCC agrees to support the increase to the Certificate of Public Convenience and Necessity for the Pete 4 FGD upgrade by \$1.6 million to a new total of \$129.6 million, understanding that IPL will not seek recovery of the additional \$1.6 million in the ECR tracker filings but will include these costs in rate base in its next basic rate case. The OUCC will not challenge these costs (i.e. the additional \$1.6 million) for recovery during IPL's next rate case. There will be no special accounting treatment (such as post-in service AFUDC or other "carrying charges" or deferred depreciation) for amounts not recovered through the ECR tracker filings.

4. IPL may include amounts (if any) related to the Pete 4 FGD upgrade over the \$1.6 million modification to the CPCN in its proposed rate base at the time of its next rate case. However, all of the OUCC's rights will be preserved to review and potentially challenge the reasonableness of any costs in excess of the \$129.6 million CPCN amount at the time of the next base rate case.

5. IPL agrees to credit any reduced charges or concessions received from contractors involved in the Pete 4 FGD upgrade toward the final cost of the project.

**B. PRESENTATION OF THE SETTLEMENT TO THE COMMISSION**

1. The Parties shall support this Agreement before the Commission and request that the Commission expeditiously accept and approve the Agreement. The concurrence of the Parties with the terms of this Agreement is expressly predicated upon the Commission's approval of the Agreement in its entirety without any modification or any condition that may be unacceptable by any Party. If the Commission does not approve the Agreement in its entirety and without change, the Agreement shall be null and void and deemed withdrawn upon notice in writing by any Settling Party within fifteen (15) business days after the date of the Final Order that any modifications made by the Commission are unacceptable to it.

2. The Parties shall jointly move for leave to file this Agreement and supporting evidence. In lieu of prefiling rebuttal evidence, IPL's evidence in support of the Agreement will include a response to the evidence prefiled by the OUCC prior to the Agreement. The prefiled evidence should be offered into evidence without objection and the Parties intend to waive cross-examination. The Parties propose to submit this Agreement and evidence based on the condition that if the Commission fails to approve this Agreement in its entirety without any change or with condition(s) unacceptable to any Party, the Agreement and supporting evidence shall be withdrawn and the Commission will continue to hear Cause No. 42170-ECR 19 with the proceedings resuming at the point they were suspended by the filing of this Agreement.

3. A Final Order approving this Agreement shall be effective immediately, and the agreements contained herein shall be unconditional, effective and binding on all Parties as an Order of the Commission.

4. The Parties shall jointly agree on the form, wording and timing of public/media announcement (if any) of this Agreement and the terms thereof. No Party will release any information to the public or media prior to the aforementioned announcement. The Parties may respond individually without prior approval of the other Parties to questions from the public or media, provided that such responses are consistent with such announcement and do not disparage any of the Parties. Nothing in this Agreement shall limit or restrict the Commission's ability to publicly comment regarding this Agreement or any Order affecting this Agreement.

**C. EFFECT AND USE OF SETTLEMENT AGREEMENT**

1. It is understood that this Agreement is reflective of a negotiated settlement and neither the making of this Agreement nor any of its provisions shall constitute an admission by any Party to this Agreement in this or any other litigation or proceeding. It is also understood that each and every term of this Agreement is in consideration and support of each and every other term.

2. This Agreement shall not constitute and shall not be used as precedent by any person in any other proceeding or for any other purpose, except to the extent necessary to implement or enforce the terms of this Agreement.

3. This Agreement is solely the result of compromise in the settlement process and except as provided herein, is without prejudice to and shall not constitute a waiver of any position that any of the Parties may take with respect to any or all of the items resolved here and in any future regulatory or other proceedings.

4. The Parties agree that the evidence in support of this Agreement constitutes substantial evidence sufficient to support this Agreement and provides an adequate evidentiary basis upon which the Commission can make any findings of fact and conclusions of law necessary for the approval of this Agreement, as filed. The Parties shall prepare and file an agreed proposed order with the Commission as soon as reasonably possible.

5. The communications and discussions during the negotiations and conferences and any materials produced and exchanged concerning this Agreement all relate to offers of settlement and shall be privileged and confidential, without prejudice to the position of any Party, and are not to be used in any manner in connection with any other proceeding or otherwise.

6. The undersigned Parties have represented and agreed that they are fully authorized to execute the Agreement on behalf of their designated clients, and their successors and assigns, who will be bound thereby.

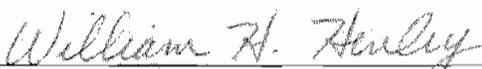
7. The Parties shall not appeal or seek rehearing, reconsideration or a stay of the Final Order approving this Agreement in its entirety and without change or condition(s) unacceptable to any Party (or related orders to the extent such orders are specifically implementing the provisions of this Agreement). The Parties shall support or not oppose this Agreement in the event of any appeal or a request for a stay by a person not a party to this Agreement or if this Agreement is the subject matter of any other state or federal proceeding.

8. The provisions of this Agreement shall be enforceable by any Party before the Commission and thereafter in any state court of competent jurisdiction as necessary.

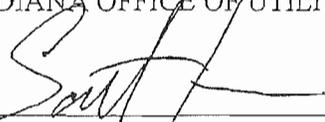
9. This Agreement may be executed in two (2) or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

ACCEPTED and AGREED as of the 26th day of September, 2012.

INDIANAPOLIS POWER AND LIGHT COMPANY

  
Name: William A. Henley  
Its: Vice President, Corporate Affairs

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

  
Name: Scott C. Franson  
Its: Deputy Consumer Counselor