ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

IN THE MATTER OF THE PETITION OF INDIANA MICHIGAN POWER COMPANY FOR APPROVAL OF CERTAIN TRANSACTIONS RELATING TO THE LEASING OF NUCLEAR FUEL FOR THE DONALD C. COOK NUCLEAR PLANT OF INDIANA MICHIGAN POWER COMPANY	)	CAUSE NO. 43682 APPROVED: AUG 26 2009

BY THE COMMISSION:
David E. Ziegner, Commissioner
Angela Rapp Weber, Administrative Law Judge

On May 4, 2009, Indiana Michigan Power Company ("Petitioner" or "Company") filed a petition ("Petition") in this Cause with the Indiana Utility Regulatory Commission ("Commission"). An Evidentiary Hearing was held in this matter on July 14, 2009, at 10:00 a.m., EST in Room 224, National City Center, 101 W. Washington Street, Indianapolis, Indiana 46204. The Petitioner and Office of Utility Consumer Counselor ("OUCC" or "Public") appeared and participated. At the Evidentiary Hearing, Petitioner presented the prefiled direct and supplemental testimonies of Jerald R. Boteler, Jr. Director of Corporate Finance for American Electric Power Service Corporation. The OUCC presented the prefiled testimony of Duane P. Jasheway, a Utility Analyst for the OUCC. Members of the general public were not in attendance at the Evidentiary Hearing.

The Commission, having considered the evidence presented in this matter, and being duly advised in the premises, now finds that:

1. **Petitioner's Characteristics and Commission Jurisdiction.** Petitioner is a corporation organized and existing under the laws of the State of Indiana, having its principal executive office at One Summit Square, Post Office Box 60, Fort Wayne, Indiana 46801. It owns and operates electric utility properties for service to the public in Indiana and southwestern Michigan. Petitioner is a public utility within the meaning of the Public Service Commission Act, as amended, Indiana Code 8-1-2, and is subject to the jurisdiction of this Commission in the manner and to the extent provided by the laws of the State of Indiana.

Petitioner owns and operates the Donald C. Cook Nuclear Plant ("Cook Plant"), a nuclear fueled, steam, electric, generating station, located near Bridgman, Michigan. The Cook Plant consists of two generating units, both of which are in commercial operation, with an aggregate net generating capacity of 2,110,000 kilowatts. The Cook Plant requires nuclear fuel in its production of power. In the past, Petitioner has financed nuclear fuel required for use in the Cook Plant by engaging in the sale and leaseback of the nuclear fuel or through borrowing. The Company desires at this time to enter into an arrangement with one or more as yet unspecified commercial banks, other financial institutions, insurance companies or other institutional

investors ("New Lessor") whereby New Lessor will purchase from, and lease-back to the Petitioner, nuclear fuel.

2. **Direct Evidence Presented by the Petitioner Regarding the Proposed Lease Transactions.** Evidence presented by the Petitioner indicates that pursuant to the terms of the proposed lease arrangements, the Company will select and pay for the milling, conversion, enrichment, fabrication, installation, and delivery of the nuclear fuel. Pursuant to the terms of one or more new leases ("New Lease"), the Company will sell the nuclear fuel to New Lessor once the nuclear fuel is installed for operation in Petitioner's nuclear reactor at the Cook Plant, or New Lessor will purchase the nuclear fuel directly from vendors. Under the terms of the New Lease, New Lessor will lease to the Company nuclear fuel with a maximum aggregate value of up to $400,000,000.

By an order dated December 12, 2007 in Cause No. 43351, the Commission authorized Petitioner to enter into a Nuclear Fuel Lease Agreement with Citicorp Leasing, Inc. ("Lessor") in an aggregate amount of $180,000,000. Thereafter, Petitioner and Lessor entered into a Nuclear Fuel Lease Agreement dated December 14, 2007 ("Current Lease"). Pursuant to the terms of the Current Lease, Lessor has purchased and leased back to Petitioner nuclear fuel in the amount of $85,000,000. The New Lease maximum aggregate value of up to $400,000,000 is inclusive of the remaining $95,000,000 of authority granted in Cause No. 43351.

Net rent to be paid by the Company, computed on a monthly basis, will be the sum of (i) the monthly burn rate for such month, and (ii) the product of (A) the unamortized value of the nuclear fuel on the first day of such month, (B) a fraction having the numerator equal to the number of days in such month and the denominator of 360, and (C) the sum of (1) a credit-adjusted spread and (2) either (a) the London Interbank Offered Rate ("LIBOR") or (b) a fixed rate. The monthly burn rate will be determined by multiplying (a) the number of Btu's consumed by such nuclear fuel during the month the nuclear fuel is producing electricity by (b) the dollar amount per Btu ("the "Btu Charge") set forth in the final leasing record covering such nuclear fuel. Alternately, Petitioner and New Lessor may agree upon a different manner of computing rent, such as assuming equal monthly consumption of the nuclear fuel. Each group of fuel assemblies inserted into a nuclear reactor (a "Batch") will be amortized to zero, other than Batches still in heat production on the last day of the lease term, which will be purchased by the Company on the termination date for the then-unamortized value of such nuclear fuel.

Unless the New Lease is earlier terminated or extended, nuclear fuel will be leased under the New Lease for a period up to sixty months. After a minimum time following the execution of the New Lease, agreed upon by Petitioner and New Lessor, the Company or New Lessor may terminate the New Lease for any reason, upon 180 days prior written notice. New Lessor may terminate the New Lease prior to a scheduled termination date under certain circumstances, including if (a) New Lessor becomes subject to certain adverse rules, regulations or declarations with respect to its status or the conduct or its business; (b) certain changes occur in the Price-Anderson Act or Atomic Energy Act; (c) there is a nuclear incident of sufficient magnitude; or (d) certain adverse regulatory events occur in connection with the New Lease or the Cook Plant.

At termination of the New Lease, the Company will purchase all of New Lessor's interests in the unamortized nuclear fuel then subject to the New Lease. Title to the nuclear fuel

will be transferred to the Company or, under certain circumstances, a party designated by the Company and approved by the New Lessor. The Company will be obligated to pay New Lessor a purchase price equal to the then-unamortized value of the nuclear fuel then under lease. Upon consummation of such purchase, all obligations of the Company under the New Lease will terminate, except to the extent provided therein.

Although the final interest rate spread will not be fixed until the transaction is closed, Petitioner indicates that the proposed method of financing Petitioner's nuclear fuel is of a lower cost than would be the case if Petitioner financed the nuclear fuel directly by the issuance of its own notes and equity, because Petitioner's weighted average cost of capital is in excess of the interest rate Petitioner will pay under the New Lease.

Mr. Boteler sponsored Petitioner's Exhibit C containing the Company's Balance Sheets as of December 31, 2008 and 2007, Statements of Income for the twelve month periods ended December 31, 2008, 2007 and 2006 and Statements of Changes in Common Shareholder Equity and Comprehensive Income (Loss) for the twelve month periods ending December 31, 2008, 2007 and 2006.

3. **Petitioner's Supplemental Testimony**. On June 23, 2009, Petitioner submitted the supplemental testimony of Mr. Boteler. Mr. Boteler explained that on June 11, 2009, Company representatives, including him, had a telephonic technical conference with representatives of the OUCC and the Commission Staff. During the course of that technical conference, Mr. Boteler stated that the Company agreed to provide the latest rating reports for the Company and provide, by way of supplemental testimony, a spreadsheet showing the expected benefit of the leasing financing proposal as detailed in his direct testimony.

Mr. Boteler sponsored Exhibit 2-A, which is a five-page spreadsheet setting forth the monthly calculations for a term of fifty-four months that compares the cost of the Company owning the nuclear fuel versus the cost of the Company leasing the nuclear fuel for the Cook Plant as proposed in this proceeding. He stated he used a term of fifty-four months because once the nuclear fuel is installed at the Cook Plant it generally has a useful life of fifty-four months and is then removed.

Mr. Boteler testified that he used several basic assumptions in performing the hypothetical analysis. Those assumptions were a weighted average cost of capital of 7.71%, a nuclear fuel inventory of $400 million, a lease start date of August 1, 2009 and a lease rate of 6%. Mr. Boteler explained that in developing the weighted average cost of capital rate of 7.71%, he started with the capital structure that the Company submitted in Cause No. 43306. He noted that pursuant to an order issued March 4, 2009, the Commission approved a settlement agreement which reflected a 10.5% return on equity. He said for this analysis, the Company utilized the same equity return and then updated the capital structure that was submitted by the Company in Cause No. 43306. He noted that an overall cost of capital of 7.62% was approved by the Commission's March 4, 2009 Order. He said that for purposes of the analysis, the Company updated the capital structure to May 30, 2009 which resulted in a weighted average cost of capital of 7.71%. Mr. Boteler stated that the 6% lease rate was developed utilizing the terms of the expected New Lease as discussed on pages six and seven of his direct testimony. Mr. Boteler testified that the analysis shows that the net present value of the capital lease option

is $6,000,792 less than the net present value of the owned option over the fifty-four month terms. Therefore, he said the Company estimates under reasonable financial market conditions, the lease option will result in reduced revenues collected from the Company's ratepayers. He also stated that if the lease option ends up being more expensive than the owned option, the Company would simply purchase the nuclear fuel and not lease the nuclear fuel until market conditions became more reasonable.

4. **OUCC's Testimony**. The OUCC prefiled the direct testimony of Duane P. Jasheway, a Utility Analyst in the Electric Division of the OUCC. Mr. Jasheway testified that the cost of the Company's nuclear fuel is recovered through the Company's semi-annual FAC applications, whether the fuel is owned by the Company or leased through a third party. Accordingly, any nuclear fuel cost savings that may be realized by lease financing will be passed through to ratepayers via the FAC in a timely manner. He said as shown in Petitioner's Exhibit 2-A, those savings currently are projected to yield a net present value of approximately $6 million. Given the Company's commitment not to enter into any lease at a higher cost than ownership, he opined that any leasing activity will be beneficial to the ratepayers.

Mr. Jasheway noted that the settlement agreement in Cause No. 43306 approved by the Commission's March 4, 2009 Order included approximately $50 million of nuclear fuel inventory in Petitioner's rate base as result of the Company's inability to find a lease counter-party at that time. He said that the settlement agreement provided that if the Company successfully leases this particular batch of nuclear fuel, then the Company must remove the related rate of return revenue requirement from its rate base. He noted that one potential mechanism for implementing this rate of return removal from rate base would be to reflect a credit in Petitioner's FAC application.

Mr. Jasheway stated that during discussions with Petitioner's representatives, the OUCC learned that the nuclear fuel lease counterparties are more interested in full life leases or longer life leases in the four- to five-year range. He said the rate based batch of nuclear fuel is more than halfway through its amortization life and has an expected life of less than two years depending on unit operation. He said that to the extent counterparties prefer longer life leases, the recent spring batch and the scheduled 2010 batches will be more attractive to fuel lease counterparties. Thus, the rate base batch of nuclear fuel will be less attractive and would be probably leased later in the financing authorization, if at all.

Mr. Jasheway testified that conceptually the inclusion of the $50 million in rate base provides shareholders with a return on and a return of the unamortized balance of owned nuclear fuel to compensate them for the shareholders financing that inventory asset. Once the batch of nuclear fuel is fully amortized, the shareholders will have received compensation for their investment by receiving a return of $50 million as amortized through the FAC and return on the $50 million through the corresponding revenue requirements reflected in the rate base. He said that the full amortization of the fuel inventory by the Company would be analogous to the Company entering into a lease financing arrangement for the batch of nuclear fuel in that both scenarios represent a discontinuation of shareholder financed status for the batch of nuclear fuel. He said, therefore, once the rate base batch of nuclear fuel is fully amortized as owned fuel, he recommended that Petitioner be required to implement the same credit to remove the rate of

return component from the rate base that would occur upon successful leasing of the nuclear fuel as provided in the settlement agreement in Cause No. 43306.

Mr. Jasheway concluded his testimony with three recommendations: (1) the Commission approve Petitioner's request for authorization for its nuclear lease financing arrangements; (2) the Commission require Petitioner to provide regular updates of its leasing developments, including the status of leasing the existing owned inventory, annually through FAC testimony as required by the settlement agreement; and (3) the Commission require the Company to implement the same credit mechanism for full amortization of the owned batch of nuclear fuel as it would have done for the successful leasing of the nuclear fuel.

5. Commission Findings and Discussion. In its Petition, the Company requests Commission approval to enter into a New Lease with New Lessor. Pursuant to the terms of the New Lease, New Lessor will purchase from, and lease back to, Petitioner nuclear fuel with a maximum aggregate value of up to $400,000,000. Unless the New Lease is earlier terminated or extended, nuclear fuel will be leased under the New Lease for a period up to sixty months.

The New Lease is the latest iteration of prior lease arrangements presented to the Commission for review over the past nineteen years. In an Order issued in Cause No. 39051 *(Ind. Util. Reg. Comm'n,* December 5, 1990) this Commission authorized the Petitioner to enter into a Nuclear Material Lease Agreement ("Prior Lease") with DCC Fuel Corporation ("DCC"). Under the Prior Lease, the Petitioner leased certain nuclear material required for the operation of the Cook Plant. See, Petition at 2. The Commission subsequently approved a revised lease arrangement with DCC in Cause No. 41748 *(Ind. Util. Reg. Comm'n,* September 27, 2000).

We find that Petitioner's request for approval to enter into a New Lease is in the Company's and the public's best interest, and should be approved. The proposed transactions are reasonably necessary to the operation and management of Petitioner's business in order that Petitioner may provide adequate service to the public at a reasonable cost. The evidence demonstrates that the leasing activity is projected to result in ratepayer savings when compared to the ownership option. Petitioner's capital structure, after giving effect to the proposed transactions, will be reasonable and in the public interest. After the proposed transactions, the Petitioner's total amount of outstanding stock, notes maturing more than twelve months from the date hereof and other evidence of indebtedness will not be in excess of the fair value of Petitioner's utility property.

At the July 14 hearing, Petitioner stated that it did not object to Mr. Jasheway's recommendations. We find those recommendations are reasonable and should be implemented. Therefore, the Company shall provide annual updates, through FAC testimony, of its nuclear fuel leasing activity and implement the same credit mechanism for the full amortization of currently owned nuclear fuel as it would have done for the leasing of the same batch.

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

1. Petitioner's request to enter into a New Lease for nuclear fuel with one or more New Lessors is hereby approved, and the Commission hereby issues this certificate of authority for that purpose. This Order constitutes the certificate of authority. Petitioner shall annually notify the Commission of its nuclear fuel leasing activity through annual FAC testimony. Petitioner shall also implement, when conditions discussed herein warrant, a credit mechanism consistent with the recommendation approved in Paragraph No. 5.

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

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

APPROVED: AUG 2 6 2009

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

Brenda A. Howe

Brenda A. Howe
Secretary to the Commission