

ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

VERIFIED PETITION OF INDIANAPOLIS)
POWER & LIGHT COMPANY REQUESTING)
THE INDIANA UTILITY REGULATORY)
COMMISSION TO APPROVE AN ENERGY)
EFFICIENCY SCHOOLS PROGRAM – AUDITS)
("SCHOOL AUDITS") AS A CORE DSM)
OFFERING AND RELATED REGULATORY)
TREATMENT, INCLUDING TIMELY COST)
RECOVERY, IN ACCORDANCE WITH)
INDIANA CODE 8-1-2-42(a) AND 170 IAC 4-8-1)
ET SEQ. AND FOR AUTHORITY TO TIMELY)
RECOVER LOST REVENUE ON CORE AND)
CORE PLUS PROGRAMS PURSUANT TO 170)
IAC 4-8-6.

CAUSE NO. 43911

APPROVED: NOV 04 2010

BY THE COMMISSION:

David E. Ziegner, Commissioner

Loraine L. Seyfried, Administrative Law Judge

On June 11, 2010, Indianapolis Power & Light Company ("Petitioner," "IPL," or "Company") filed its Verified Petition with the Indiana Utility Regulatory Commission ("Commission") for approval to implement an Energy Efficiency Schools Program – Audits ("School Audits") and related regulatory treatment and to recognize the lost revenue incurred as a result of the implementation of Core and Core Plus Programs. Petitioner also filed its direct testimony and exhibits constituting its case-in-chief on June 11, 2010.

On July 22, 2010, the Commission conducted a Prehearing Conference and Preliminary Hearing in this Cause. Petitioner and the Indiana Office of Utility Consumer Counselor ("OUCC") appeared and participated at the Prehearing Conference. On July 28, 2010, the Commission issued its Prehearing Conference Order establishing the schedule and other procedural requirements for this Cause. Petitioner filed supplemental testimony on August 11, 2010. On August 20, 2010, the OUCC filed its Notice of Intent Not to File Testimony. On September 21 and September 27, 2010, the Commission issued questions to Petitioner by Docket Entry to which Petitioner responded on September 23 and September 27, 2010, respectively.

Pursuant to public notice duly given and published, proof of which was incorporated into the record by reference and placed in the Commission's official file, a public hearing was held in this Cause on September 28, 2010 at 1:30 p.m. EDT in Room 224 of the PNC Center, 101 W. Washington Street, Indianapolis, Indiana. At the hearing IPL and the OUCC appeared by counsel and IPL offered its prefiled testimony and exhibits which were admitted into evidence without objection. No members of the general public appeared.

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

1. Notice and Jurisdiction. Proper notice of the hearing in this Cause was given as required by law. IPL is a “public utility” within the meaning of Ind. Code § 8-1-2-1 of the Public Service Commission Act, as amended, and is subject to the jurisdiction of the Commission. The Commission has jurisdiction over Petitioner and the subject matter of this Cause in the manner and to the extent provided by the laws of the State of Indiana.

2. Petitioner’s Organization and Business. Petitioner is an operating public utility, incorporated under the laws of the State of Indiana, with its principal office and place of business in the City of Indianapolis, Indiana. IPL renders retail electric utility service to approximately 470,000 retail customers located principally in and near the City of Indianapolis, Indiana, and in portions of the following Indiana counties: Boone, Hamilton, Hancock, Hendricks, Johnson, Marion, Morgan, Owen, Putnam and Shelby Counties. IPL owns, operates, manages and controls electric generating, transmission and distribution plant, property and equipment and related facilities, which are used and useful for the convenience of the public in the production, transmission, delivery and furnishing of electric energy, heat, light and power.

3. Background. In its December 9, 2009 Order in Cause No. 42693 (“Generic DSM Order”), the Commission determined that certain actions needed to be taken to address specific shortcomings with respect to electric demand-side management programs. To this end, the Commission established annual energy savings goals and other requirements, including the implementation of certain demand-side management and energy efficiency programs referred to as “Core Programs.”¹

The Commission’s Phase I Order in *Re Petition of Indianapolis Power & Light Co.*, Cause No. 43623 (IURC 2/10/10) (“Phase I Order”) authorized IPL to implement a portfolio of demand-side management programs and approved ratemaking to provide cost recovery for the Core and Core Plus Programs through Standard Contract Rider No. 22 (“Rider 22”). IPL has begun to implement the portfolio of programs in order to attempt to achieve the savings goal set forth in the Generic DSM Order.

The Core Programs established by the Generic DSM Order include an energy efficient schools program, described as including “[i]nformation and energy efficiency kits for K-12 schools, school building energy audits and access to prescriptive incentives available for commercial customers.” Generic DSM Order at 36. IPL’s Energy Efficiency Schools – Kits Program approved in the Phase I Order does not include the school building energy audits component of the Core Program.

In Cause No. 43623, IPL also sought Commission approval for IPL to recover lost revenue due to the decreased kWh consumption and kW demand resulting from the DSM programs. The Commission found that it could not approve the lost revenue request because the record lacked “sufficient evidence demonstrating the revenue margin rates per kWh and kW to be used in determining such lost revenue amounts are reasonably reflective of [IPL’s] present operating system.” Phase I Order at 58. The Commission invited IPL to submit the additional evidence to address this issue via a subdocket to be established in Cause No. 43623. *Id.* The

¹ As used herein the term “Core Programs” refers to those programs required by the Commission’s Phase II Order in Cause No. 42693 dated December 9, 2009. The term “Core Plus Programs” refers to DSM programs or portions thereof that exceed or go beyond the type of programs contemplated to be Core Programs.

Commission also noted that requests to recover lost revenue may be considered in a new docket, such as one seeking approval of programs required by the Generic DSM Order. *Id.* at 56. On March 30, 2010, IPL filed a notice in Cause No. 43623 setting forth IPL's belief that judicial economy would be served by IPL providing the additional information relevant to lost revenue at the time of IPL's next DSM filing.

4. Petitioner's Request. In this proceeding, IPL seeks Commission approval of IPL's implementation of School Audits as a Core DSM Program offering, and Commission approval of associated regulatory treatment, including timely cost recovery for the direct and indirect costs associated with this program through Rider 22. IPL also requests the Commission authorize IPL to recognize through Rider 22 the lost revenue incurred on and after the date of this Petition as a result of the implementation of its Core and Core Plus Programs, including the School Audits.

5. Petitioner's Case-In-Chief.

A. Ken Flora. Ken Flora, Director, Regulatory Affairs for IPL, summarized the Company's request and explained why approval of IPL's proposal for the School Audits and lost revenue recovery is in the public interest. He explained that the School Audits is the only Core Program identified by the Generic DSM Order that IPL does not have authority to implement. He stated approval to implement this program will allow IPL to offer all five of the Core Programs established in the Generic DSM Order. Mr. Flora stated this audit program will help schools in IPL's service territory be more efficient and reduce their energy bills through actions recommended in the audit reports.

Mr. Flora testified IPL proposes that all K-12 schools (except for schools served under Rate PL) be permitted to participate in this program. Mr. Flora stated IPL proposes to align the initial term of the School Audits program with the other programs approved for IPL's Core and Core Plus Programs approved in Cause No. 43623 (referred to herein as IPL's "Current DSM Program"), which are currently set to expire on February 9, 2013.

Mr. Flora stated that in this proceeding IPL is presenting the testimony of Mr. Kerry A. Heid, a consultant with Heid Rate and Regulatory Services, to address the deficiency identified by the Commission in the Phase I Order relating to IPL's previous request for recovery of lost revenue. He explained that the recovery of lost revenue helps to mitigate the negative consequences of offering DSM programs, while still providing significant benefits to IPL's customers. He stated a robust DSM program with lost revenue recovery and performance based incentives will advance integrated resource planning and energy efficiency and will thus further the overall goal of providing safe, reliable and cost effective electric service. Mr. Flora also explained the Commission promulgated DSM rules that recognize the need to provide supportive regulation to place DSM on a more level playing field with utilities' supply-side resource options. He stated regulatory policy that supports timely cost recovery, including lost revenue and incentives, through rider and adjustment mechanisms, will encourage the growth of DSM in Indiana.

B. Lester H. Allen. Lester H. Allen, Team Leader, Marketing and Program Management for IPL, described IPL's historical involvement in and experience with DSM, and discussed the status of the delivery of IPL's current Core and Core Plus DSM programs. Mr. Allen provided additional details regarding the School Audits, explained how this program will

transition to the statewide DSM Third Party Administrator (“TPA”) and discussed the proposed approach to evaluate, measure and verify the results of the School Audits program.

Mr. Allen testified the proposed School Audits program will give schools (grades K-12) the opportunity to request and receive from representatives of IPL a detailed school building energy audit that will provide schools with a report that identifies and prioritizes energy savings opportunities. A copy of the School Audits Description was provided as Petitioner’s Exhibit LHA-3. Mr. Allen stated that while the energy audit alone does not provide any direct energy savings, it is assumed that the audit information will be used to make additional investments in energy efficiency opportunities. He explained that these energy efficiency investments will be further facilitated by incentives provided by both the Commercial and Industrial Prescriptive Program and Custom Program approved in the Phase I Order. He said that IPL will require that the schools pay for a portion of the audit costs up front to ensure that there is some buy-in to the audit process and recommendations. The customer investment in the audit will be refunded to the extent investments are made in an equal or greater amount than the customer’s contribution to the audit cost.

Mr. Allen stated IPL proposes a total three year budget of \$560,000 for this program. For illustrative purposes, he gave the following annual program budgets for the School Audits: \$151,000 for Program Year 1; \$191,000 for Program Year 2; and \$218,000 for Program Year 3. He said these amounts are approximately 10% of the previously-approved spending authority for the Commercial and Industrial Prescriptive, Custom, Retro-Commissioning and New Construction Programs approved in the Phase I Order. He explained that IPL considers the spending authority to be a three (3) year spending authority that will be moved from one program year to another as market conditions dictate.

Mr. Allen testified that all K-12 schools (except for schools served under Rate PL) would be permitted to participate in the School Audits. Mr. Allen explained that while there are a few larger schools in IPL’s service area that are served under Rate PL, these customers are currently excluded from participating in the other programs included in IPL’s Current DSM Program. Mr. Allen noted that excluding these larger school customers from participating in the proposed School Audits provides consistency with the Current DSM Program in terms of eligibility.

Mr. Allen testified the proposed School Audits, in concert with the other programs that IPL is currently delivering, will provide IPL a meaningful start towards meeting the energy savings goals established by the Generic DSM Order. He stated that IPL anticipates that a significant gap between its Current DSM Program (and expected results) and the targets established in the Generic DSM Order will remain -- even after the approval of the proposed School Audits. He noted that in an effort to close this gap, IPL expects to make an additional filing in the second half of 2010 to request authority to expand its Current DSM Program both in scale and scope. This future request will reflect the costs and impacts that are derived from the TPA proposals received in the current Request for Proposal (“RFP”) process.

Mr. Allen testified that during the transition of the School Audits and IPL’s other Core Programs to the statewide program delivered by the TPA, IPL will seek to minimize customer and marketplace confusion by communicating closely and consistently with both its customers and the TPA. He stated IPL will work with its program delivery contractors, key account managers and other employees who have customer interaction, utilizing various forms of

communication, such as IPL's web-site, e-mails, and customer newsletters, to communicate the program transition to the statewide program delivered by the TPA.

Mr. Allen stated that because start-up costs for the School Audits are limited, IPL does not believe there will be material efficiency lost by beginning to deliver this program and then transferring program delivery to the TPA. He stated that as with the other programs that IPL is currently delivering, an Evaluation, Measurement and Verification ("EM&V") contractor will be selected by the Oversight Board as directed by the Phase I Order to conduct an evaluation of the program results using the appropriate protocols. As directed by the Commission in its Generic DSM Order, IPL will await the outcome of the RFP process being conducted by the DSM Coordination Committee to determine if there is an opportunity to engage the contractor selected in this process to complete the EM&V for the proposed School Audits program. He added that the EM&V process is expected to determine actual customer participation rates, program costs and program demand and energy impacts that result from the proposed School Audits program. Following a review of the EM&V, the demand and energy impacts will be modified as appropriate and applied on a prospective basis.

C. Matthew F. Rose. Matthew F. Rose, a Principal with Terra Vista Energy Group, LLC, discussed the design, methodology and results of the economic analysis of the School Audits program. He explained that role included (1) conducting discussions with IPL staff to better understand the size, vintage, and characteristics of the K-12 schools marketplace in IPL's service area, reviewing facility billing data and discussing various design options for delivering the program; (2) conducting discussions with selected implementation contractors and performance contract managers focused on the schools and education market in order to identify the types of measures installed, decision-making processes, and costs associated with conducting a facility audit and installing energy efficiency measures in the school's market; (3) working with IPL to develop a prototype elementary school building to use as a baseline in the analysis calculations; and (4) working with IPL to develop the necessary information to properly conduct an economic analysis of the program.

Mr. Rose stated a formal economic analysis of the program was conducted to identify the associated costs and benefits as compared to projected electric supply costs to determine cost-effectiveness. The analysis included all the relevant program costs including program start-up, administration, incentives and evaluation, as well as estimated annual program participation. He stated these costs were compared to electric avoided costs to provide a net present value impact of all costs and benefits. The result was a cost-benefit ratio and estimate of the economic value of the proposed School Audits. He stated by simulating the results of the program using a dedicated cost-effectiveness model, the range of economic impacts was determined.

Mr. Rose stated the economic analysis included a range of market perspectives, including four economic tests: the Participant Test, Utility Cost Test, Rate Impact Measure Test and the Total Resource Cost Test. The results of each of the tests were determined for the School Audits. He stated the analysis used to estimate savings from the School Audits program was based on treating the facility audit as a vehicle to identify energy savings opportunities. As noted by Mr. Allen, he indicated that audits, by themselves, do not result in any direct energy savings, but rather guide the participant by identifying packages of relevant DSM measures for consideration. Mr. Rose explained the economic analysis is based on an assumed level of investment and measure installation by participants based on discussions with contractors.

Mr. Rose stated the avoided costs were developed by IPL using its planning models. In this analysis, the electric avoided costs are used as a proxy for utility supply costs to assess the relative cost effectiveness of the School Audits. He stated the avoided costs consist of both avoided energy (cents per kilowatt-hour) and capacity (dollar per kilowatt) per year. All the relevant economic analyses are based on modeling the net present value of costs and benefits to address the time value of money. Mr. Rose stated the end result is a direct comparison of whether a candidate DSM program is more or less expensive than the supply alternative. He stated programs with positive net present value results and a positive benefit-cost ratio indicate the DSM program is less expensive than specified supply options.

Mr. Rose stated the results indicate that the School Audits program passes the Total Resource Cost Test, Participant Test and the Utility Cost Test, but does not pass the Rate Impact Measure Test. He sponsored the analysis results for the School Audits as Petitioner's Exhibit MFR-2.

D. Kerry A. Heid. Mr. Heid supported IPL's request for recovery of its lost revenue resulting from the Current DSM Program, including the proposed School Audits. He began by explaining that the Commission's DSM Rules, promulgated following passage of the National Energy Policy Act of 1992 and found at 170 IAC 4-8-1 *et seq.*, provide, among other matters, for recovery of program costs, lost revenue and shareholder incentives in an effort "to eliminate or offset regulatory or financial bias against DSM, or in favor of a supply-side resource, a utility might encounter in procuring least-cost resources." 170 IAC 4-8-3(a). He stated that lost revenue, as defined by the Commission rules at 170 IAC 4-8-1, refers to revenue lost less the variable operating and maintenance costs saved as a result of not generating electricity because of a utility-sponsored DSM program.

Mr. Heid testified that IPL's lost revenue recovery proposal in this proceeding is consistent with the Commission's DSM Rules. He stated that in Cause No. 43623, IPL requested approval of an alternative regulatory plan for the offering of DSM programs and associated rate treatment, including among other things, the recovery of lost revenue through a rider due to decreased kilowatt-hour ("kWh") consumption and kilowatt ("kW") demand resulting from its DSM programs. Referring to Mr. Cutshaw's testimony in Cause No. 43623, Mr. Heid explained that the methodology used to calculate the lost revenue by rate class in that Cause was previously approved by the Commission and utilized by IPL in prior quarterly DSM filings in Cause No. 40292.

Mr. Heid addressed the deficiency identified by the Commission in the Phase I Order by using present operating revenues and costs to determine the DSM Lost Revenue Rates. Mr. Heid explained that the electric utility's business consists predominantly of fixed costs that do not vary with usage. He stated IPL operates its electric generation, transmission and distribution system to provide electric service to a customer's premises whether that customer uses 1 kWh or 10,000 kWh. In addition, IPL maintains a significant infrastructure to provide customer service, to administer its accounting and billing systems, and to provide other critical internal and external services. Such costs are fixed and cannot be avoided even when kWh consumption and kW demand decrease.

Mr. Heid stated an electric utility's operating revenue is derived from its Commission-approved rate schedules. He stated that although a utility's costs could change significantly between rate cases, the utility's operating revenues are solely a function of its rate schedules.

Residential and small commercial or general service customers are typically served on a two-part rate, with a uniform monthly Customer Charge and a volumetric Energy Charge (*i.e.*, a price per kWh). Larger non-residential customers typically have a three-part rate, with a uniform monthly Customer Charge, a volumetric Energy Charge (*i.e.*, a price per kWh), and a Demand Charge (*i.e.*, a price per kW), based on individual customers' monthly peak demands.

Mr. Heid stated IPL will calculate the amount of lost revenue to be recovered by multiplying the estimated kWh consumption and kW demand reductions by rate class, net of the effects of free riders, times the DSM Lost Revenue Rates per kWh and kW for the corresponding rate class. He stated the calculated lost revenue will be included on Line 39 of Rider 22 for recovery.

Mr. Heid sponsored Petitioner's Exhibit KAH-3, which provides the derivation of the DSM Lost Revenue Rates used to calculate IPL's lost revenue. Mr. Heid's testimony discussed each column of that exhibit in detail. He noted that the Energy Charge rate component (billed in \$ per kWh) is used to determine the lost revenue resulting from decreased kWh consumption. The Demand Charge rate component (billed in \$ per kW) is used to determine the lost revenue resulting from decreased kW demand.

Mr. Heid explained that the unit rates of the rate blocks at which customers' marginal energy consumption or demand occurs are used to determine the lost revenue because they reflect the actual present revenue impact on IPL of a decrease in one kWh of consumption or one kW of demand. He further explained that fuel is included as an offset in the lost revenue calculation because any reduction in kWh consumption due to the utility's DSM programs would enable the utility to avoid related base rate fuel costs on the utility's system.

Mr. Heid noted that in Phase I of Cause No. 43623, IPL used margin rates (the basic rate for the applicable rate block as set forth in IPL's Electric Tariff less the Base Cost of Fuel as reflected on IPL's Tariff Sheet No. 157) for purposes of calculating the DSM lost revenue, which is the same methodology as was approved and utilized in prior IPL DSM filings. Mr. Heid's review and analysis determined the need to make two additional adjustments to IPL's previous calculation of its margin rates to address the deficiency identified by the Commission in its Phase I Order. First, he determined that present variable operation and maintenance ("O&M") expenses should be deducted from the margin rates in order to be consistent with the Commission's DSM Rules. As noted previously, the Commission's DSM Rules define lost revenue at 170 IAC 4-8-1 as "revenue lost less the variable operating and maintenance costs saved as a result of not generating electricity because of a utility-sponsored DSM program." Mr. Heid explained any reduction in kWh consumption due to the utility's DSM programs would allow IPL to avoid variable O&M expense and thus variable O&M expense should be included as a cost offset in the lost revenue calculation. Second, Mr. Heid determined that both the Base Cost of Fuel and the variable O&M expenses should be adjusted (*i.e.*, grossed up) for associated Indiana Utility Receipts Taxes ("IURT"). As a result, the IURT related to the Base Cost of Fuel and the variable O&M expenses were also removed from basic rates for purposes of determining the DSM Lost Revenue Rates.

IPL's variable O&M expenses include chemicals associated with the operation of scrubbers and boilers (*i.e.*, lime, soda ash and limestone); coal combustion byproduct disposal (*i.e.*, fly ash, bottom ash, and scrubber byproduct); fuel handling; and a portion of production maintenance (*i.e.*, for furnaces and cooling towers). Mr. Cutshaw provided an analysis of

variable O&M expenses incurred at IPL's power generation stations during the 2009 calendar year. Mr. Heid stated the identified present variable O&M expenses were divided by annual kWh sales for the same period to determine the present unit variable O&M expenses of \$0.002259 per kWh used on Petitioner's Exhibit KAH-3 to determine the DSM Lost Revenue Rates.²

Mr. Heid explained that he calculated present variable O&M unit cost rather than using the variable O&M unit cost embedded in basic rates because the relevant cost for purposes of DSM lost revenue recovery is the present variable O&M costs that are avoided when kWh consumption decreases. He stated the present day variable O&M unit cost, which serves as a deduction in the determination of the DSM Lost Revenue Rates, produces accurate DSM Lost Revenue Rates reflecting present operating conditions. According to Mr. Heid, this addresses the deficiency identified by the Commission in its Phase I Order because these present variable O&M unit costs are reasonably reflective of IPL's present operating system.

Mr. Heid stated Column (9) of Petitioner's Exhibit KAH-3 sets forth the DSM Lost Revenue Rates to be used in the lost revenue calculation. He stated the DSM Lost Revenue Rates are calculated using the basic rates as set forth in IPL's Electric Tariff, less the Base Cost of Fuel and present unit variable O&M expenses (both grossed up for IURT). The DSM Lost Revenue Rates are then applied to the estimated decreases in kWh consumption and kW demand resulting from its DSM programs to determine the lost revenue to be recovered through Rider 22.

Mr. Heid testified that regulatory policy supporting timely cost recovery through rider and tracking mechanisms, including incentives and lost revenue, will encourage the growth of DSM in Indiana. He stated there is widespread support for creating incentives or removing financial or regulatory bias to encourage the use of DSM. As an example, he noted the National Energy Policy Act of 1992 urged state utility regulatory commissions to establish such regulation.

Mr. Heid discussed various NARUC Resolutions, as well as the Hoosier Homegrown Energy-Indiana's Strategic Energy Plan, Energy Independence and Security Act of 2007 and the Commission's April 23, 2008 Phase I Order in Cause No. 42693, all of which he stated also support regulatory pricing mechanisms that encourage utilities to promote efficiency and conservation by their customers without the utilities incurring negative financial results so as to align utility incentives with the delivery of cost-effective energy efficiency practices and investments.

Mr. Heid explained that the Commission's Generic DSM Order increased the urgency of approval of IPL's lost revenue recovery mechanism. He noted for utilities subject to the Commission's jurisdiction (including IPL), "the Order establishes an overall annual energy savings goal of 2% to be achieved within 10 years, with interim savings goals to be achieved in years one through nine." Mr. Heid noted that the reduction in customers' electric consumption is not voluntary nor is it subject to IPL's timing. He stated the reduction in customers' electric consumption will reduce IPL's revenue, with only a minimal offsetting reduction in non-fuel operation and maintenance expenses. Mr. Heid asserted that given this mandatory reduction in customers' electric consumption and the mandated expenditures necessary to achieve the

² Mr. Heid noted certain variable O&M expenses are recovered through environmental riders and were therefore omitted from this calculation.

E. James L. Cutshaw. James L. Cutshaw, Revenue Requirements Manager described the impact of the proposed School Audits on the approved cost recovery mechanism utilized in the Company's semi-annual filings (Cause No. 43623 DSM X), introduced revisions to Rider 22 to reflect the proposed recovery of lost revenue on the Current DSM Program, and described the reconciliation process. Mr. Cutshaw sponsored Petitioner's Exhibit JLC-2 (Rider 22 approved in Phase I Order) reflecting the addition of subparagraph A.3 which describes the process for determining the estimate of lost revenue. Mr. Cutshaw also sponsored Petitioner's Exhibit JLC-3 (cost allocation basis and target performance incentive by program) reflecting the addition of the School Audits. He stated the program costs will be allocated in the same manner as the Commercial and Industrial ("C&I") customer programs approved in the Phase I Order, which are also applicable to Rate SL customers. He stated the approved allocation factors for these C&I customer programs were based upon the relationship of the small C&I and Rate SL allocation factors in Cause No. 39938. Mr. Cutshaw sponsored Petitioner's Exhibit JLC-4 (determination of the impact of Core and Core Plus adjustment for Years 1, 2 and 3 by program) reflecting the addition of the School Audits program.

Mr. Cutshaw stated that IPL is proposing recovery of lost revenue due to decreased kWh consumption and kW demand from the program measures which will continue for a 10-year period following installation based upon the weighted average life of the program measures. He stated that in IPL's semi-annual filings, lost revenue will be forecast for the same period as the estimated costs of the Current DSM Program, including the proposed School Audits, based upon each program's estimated participation, and reconciled to actual participation in the same subsequent semi-annual filing as the expenditures are reconciled.

Mr. Cutshaw explained how the projected lost revenue by rate class was determined. He stated estimates of the kWh consumption and kW demand reductions per participant and the number of participants for each program were determined from the analysis prepared by IPL Witness Rose in Phase I of Cause No. 43623. Estimated participants for each program were allocated between the individual rates based upon the ratio of the annual historical kWh consumption within their rate class. Allocated participants by rate were then multiplied by the kWh consumption and kW demand reductions by participant to determine the total kWh consumption and kW demand amounts by rate within each program and then totaled by rate. Mr. Cutshaw stated that since the per participant reductions and the number of participants are annual amounts; the incremental total by rate was divided by two in order to reflect a pro-rata implementation of the measures during the year. He stated these amounts for each individual rate were then multiplied by the lost revenue rates per kWh and kW supplied by IPL Witness Heid. Mr. Cutshaw added that the estimates of program impacts include free ridership consistent with the estimates from IPL's DSM market potential study.

Mr. Cutshaw sponsored Petitioner's Exhibit JLC-5 reflecting the calculation of lost revenue for each year of the three-year period for the Current DSM Program, including the proposed School Audits. He stated that in the semi-annual filings, the participants will be estimated on a monthly basis, and during the reconciliation process, actual participants by month will be utilized. Since the per participant kWh consumption and kW demand reductions are annual amounts, the total reductions calculated by rate will be divided by twelve in order to reflect a monthly amount and then totaled for the six months in the semi-annual period before being multiplied by the lost revenue rates. Mr. Cutshaw stated the first reconciliation is dependent on when approval for recovery of lost revenue is granted. Assuming recovery is granted as of the date of the Petition in this Cause, the reconciliation would first occur in Cause

being multiplied by the lost revenue rates. Mr. Cutshaw stated the first reconciliation is dependent on when approval for recovery of lost revenue is granted. Assuming recovery is granted as of the date of the Petition in this Cause, the reconciliation would first occur in Cause No. 43623 DSM 3 which would be filed in April 2011 and would include a reconciliation of lost revenue for the period July 2010 to December 2010.

Mr. Cutshaw stated the DSM lost revenue billed, including any reconciled amount of over/under recovery, should be included in the FAC earnings test. He stated it is appropriate to do so because the lost revenue would have been otherwise reflected if the Current DSM Programs, including the proposed School Audits, were not implemented.

6. Commission Discussion and Findings. This proceeding stems from the requirements imposed by the Commission's Generic DSM Order. IPL seeks relief necessary for the Company's compliance with that Order and has presented sufficient evidence demonstrating that its proposed School Audits program should be approved.

In the Generic DSM Order (at 36), the Commission found that the Core Programs to be implemented by all jurisdictional utilities in the state of Indiana, including IPL, shall include an energy efficient schools program. This program is described generally in the Generic DSM Order as a program that provides: "[i]nformation and energy efficiency kits for K-12 schools, school building energy audits and access to prescriptive incentives available for commercial customers." *Id.* The evidence in this proceeding shows that IPL's proposed School Audits program is consistent with the description of the Core Program imposed by the Generic DSM Order. The evidence also demonstrates that the proposed program plan and budget are reasonable and cost effective. The record shows that IPL has long been engaged in the provision of successful DSM programs and its plans to transition this program to the statewide Third Party Administrator are reasonable. As with the other programs that IPL is currently delivering, the record reflects that an EM&V contractor will be selected by the Oversight Board as directed by the Phase I Order to conduct an evaluation of IPL's School Audits performance. The independent EM&V evaluator will assist in satisfying the need for providing accurate verification of the energy savings achieved. We find this proposal to be reasonable. Accordingly, the Commission finds that IPL should be authorized to implement the School Audits program as a Core DSM Program and IPL shall be entitled to recover all costs incurred to implement this required program through Rider 22. We further find that the School Audits shall run concurrently with and end at the same time as the other programs included in IPL's Current DSM Program, which are currently set to expire on February 9, 2013.

With respect to IPL's request for lost revenue recovery, the Commission has previously indicated that its DSM rules, 170 IAC 4-8 *et seq.*, provide the necessary guidelines for DSM cost recovery. Phase I Order at 55. The "regulatory framework acknowledges the possibility of financial bias against DSM, recognizes the need to evaluate the extent of any bias, and provides ways for the Commission to eliminate any bias through adoption of a package of cost recovery and incentive mechanisms designed to facilitate the use of DSM to meet the long-term resource needs of customers." *Id.*; *see also*, 170 IAC 4-8-3.

In this proceeding, IPL presented evidence to respond to the concern raised in the Commission's Phase I Order. Mr. Heid updated the methodology presented by IPL in Cause No. 43623 to take into account the current level of variable O&M costs and applicable IURT saved as a result of the utility not generating the electricity that would have otherwise been consumed.

Because present day variable O&M costs, not historical costs, are the relevant costs for purposes of determining the amount of present net revenue (*i.e.* margin) lost when kWh consumption decreases, we agree that Mr. Heid's methodology reasonably reflects the amount of present net revenue lost as a result of the achievement of the energy savings.

However, the mere ability to reasonably calculate lost revenues does not automatically lead to a conclusion that the Commission should authorize recovery of those revenues. As recognized by IPL's witnesses and noted in our Phase I Order, the DSM Rules exist to provide a regulatory framework that "attempts to eliminate or offset regulatory or financial bias against DSM, or in favor of a supply-side resource, a utility might encounter in procuring least-cost resources." Phase I Order at 55; 170 IAC 4-8-3. The Commission is required to "review and evaluate, the existence and extent of regulatory or financial bias" and to consider the utility's proposed DSM programs, cost recovery and incentives "as a package" to "ensure the utility's proposal is consistent with acquiring the least-cost mix of demand-side and supply-side resources." *Id.*

Consequently, the Commission's review of a request for DSM lost revenue recovery should be considered in an appropriately broad context so as to ensure that the utility and class specific ratepayer needs are balanced. We have previously approved components of Petitioner's DSM package in other proceedings, namely shareholder incentives and program cost recovery, and therefore limit our discussion herein to lost revenue recovery related to DSM program offerings. As noted above, the Commission's DSM regulatory framework attempts to offset any financial bias that a supply-side resource may have over a demand-side resource. One reason bias may exist is because a supply-side resource choice is primarily a capital expenditure while a demand-side resource choice is primarily an expense. Utility capital expenditures found to be used and useful provide both a return of and a return on such investments; whereas utility expenses that are authorized to be included in rates for recovery from customers provide only a return of the expenditure. We note that this financial advantage of a traditional supply-side resource requires a base rate case proceeding before such recovery occurs while authority to recover specific demand-side program expenses are regularly approved in rate adjustment tracker proceedings in the intervals between base rate cases. Bias could also result from what is known as the throughput incentive. The choice of a successful demand-side resource investment results in reduced throughput, *i.e.*, sales, which reduces the utility's revenue collections. The choice of a supply-side resource does not produce such an effect. We note that the impact of reduced throughput can be reasonably considered in the context of both the present lost revenue amount (addressed by Mr. Heid as discussed above) as well as the changes that have occurred since the revenue needs were established. We are also cognizant of the likelihood that changes over time may occur on a class specific basis or on a more global companywide scale. Lost revenue amounts are dependent on class specific factors and as such we place significant value on an up-to-date class cost of service study.

Petitioner's response to the September 21, 2010 Docket Entry indicates that the utility's jurisdictional original cost rate base, less amounts included in clean coal technology tracking mechanisms, has decreased over \$100 million since its last base rate case in Cause 39938. Petitioner's response further indicates that its residential customer count has increased and that the average energy usage of those customers has also increased since its last base rate case. The significant length of time since IPL's last base rate case can reasonably be expected to have had a measureable impact on the cost of serving Petitioner's various rate classes given the divergent paths of its investment in plant included in base rates for recovery and key factors that affect

revenue collection (e.g., the number of customers and their energy consumption). Petitioner's response also estimated the impact that the lost revenue amounts would have had on the actual historical rate of return on its invested capital. The estimated results would appear to have afforded a reasonable return to Petitioner for such investment. Further, the response indicated that Petitioner's current planning projections show no supply-side resource additions through 2013.

Accordingly, based on the entirety of the evidence and specifically recognizing the previously approved incentives for Petitioner's demand-side resource package, allowing for the recovery of lost revenue for demand-side resources in the absence of a base rate case to ensure that class specific investment and investment recovery is properly aligned would exceed reasonable actions in effectuating the intent of the regulatory framework established in the Commission's DSM rules to offset the financial bias against DSM. Accordingly, we decline to authorize the recovery of lost revenues for Petitioner's Core or Core Plus Programs at this time.

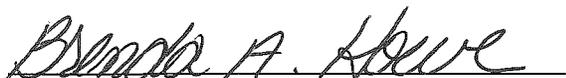
IT IS THEREFORE ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION that:

1. IPL's implementation of School Audits as a Core DSM Program offering shall be and hereby is approved.
2. IPL shall be and hereby is authorized to timely recover the costs of the School Audits through Standard Contract Rider No. 22 (Core and Advanced Demand-Side Management Adjustment).
3. IPL's request for recovery of lost revenue for its Core and Core Plus Programs is hereby denied.
4. This Order shall be effective on and after the date of its approval.

ATTERHOLT, LANDIS, MAYS AND ZIEGNER CONCUR:

APPROVED: NOV 04 2010

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


Brenda A. Howe,
Secretary to the Commission