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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. 44025

APPROVED: AUG 31 2011

BY THE COMMISSION:

Kari A.E. Bennett, Commissioner
Loraine L. Seyfried, Chief Administrative Law Judge

On May 20, 2011, Indiana Michigan Power Company ("Petitioner" or "I&M") filed a petition ("Petition") with the Indiana Utility Regulatory Commission ("Commission") seeking approval of certain proposed leasing transactions relating to nuclear material ("Nuclear Fuel") for the Donald C. Cook Nuclear Plant ("Cook Plant").

Pursuant to notice, duly published as required by law, an Evidentiary Hearing was held in this matter on August 8, 2011, at 9:30 a.m. in Room 224, PNC Center, 101 West Washington Street, Indianapolis, Indiana. Petitioner and the Indiana Office of Utility Consumer Counselor ("OUCC") appeared and participated in the Evidentiary Hearing. At the hearing, the prefiled testimony and exhibits of Petitioner and the OUCC were offered and admitted into evidence without objection. No other members of the general public were in attendance.

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

1. Notice and Jurisdiction. Due, legal and timely notice of the hearing in this Cause was given as required by law. 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. Petitioner is a public utility within the meaning of the Public Service Commission Act, as amended, Ind. Code ch. 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. Therefore, the Commission has jurisdiction over Petitioner and the subject matter herein.

2. Petitioner's Characteristics. I&M owns and operates electric utility properties for service to the public in Indiana and southwestern Michigan, including the 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 a combined nominally-rated net electric output for both units of over 2,100 megawatts. The Cook Plant requires Nuclear Fuel in its production of power.

3. Petitioner's Direct Evidence. Mr. Jerald R. Boteler, Managing Director, Corporate Finance for American Electric Power Service Corporation ("AEPSC"), testified that I&M is seeking Commission approval for the leasing of Nuclear Fuel with a maximum aggregate value of up to \$600 million. Petitioner proposes that such approval would terminate on the later of (1) the leasing of four separate nuclear fuel assemblies inserted into a reactor (each assembly being referred to hereinafter as a "Batch"), or (2) December 31, 2013.

Citing to prior Commission Orders, Mr. Boteler stated the Commission has previously approved similar leasing arrangements. He stated the Commission's most recent August 26, 2009 Order in Cause No. 43682, authorized Petitioner to enter into one or more Nuclear Fuel lease agreements with Citicorp Leasing, Inc., an affiliate thereof, or one or more as yet unspecified commercial banks, other financial institutions, insurance companies or other institutional investors (each a "Lessor"), under which Petitioner was authorized to lease from Lessor the Nuclear Fuel required for operation of the Cook Plant in an aggregate amount of up to \$400 million. Thereafter, Petitioner entered into (i) a Nuclear Fuel Lease Agreement dated as of September 24, 2009, with DCC Fuel, LLC in the aggregate amount of \$102,300,000, (ii) a Nuclear Fuel Lease Agreement dated as of April 13, 2010, with DCC Fuel II, LLC in the aggregate amount of \$84,564,063.20 and (iii) a Nuclear Fuel Lease Agreement dated as of December 7, 2010, with DCC Fuel III, LLC in the aggregate amount of \$67,900,000 (collectively, the "Current Leases"). The remaining \$145,235,936.80 of authority granted in Cause No. 43682 terminated on December 31, 2010.

Mr. Boteler stated, in this Cause, Petitioner is proposing to enter into one or more lease agreements ("New Lease") with one or more as yet unspecified commercial banks, other financial institutions, insurance companies or other institutional investors ("New Lessor"). He noted under the terms of the Current Leases, the Lessors have purchased from, and leased back to, Petitioner the Nuclear Fuel once installed for operation in the reactor. However, pursuant to the terms of the New Lease, either the New Lessor or I&M will pay for the milling, conversion, enrichment, fabrication, installation and delivery of the Nuclear Fuel. Consequently, the New Lessor will finance and lease to I&M, or the New Lessor will purchase from, and lease back to, I&M the Nuclear Fuel.

Mr. Boteler testified Petitioner anticipates the New Leases whereby New Lessor finances then leases the Nuclear Fuel to Petitioner will be substantially similar to the Current Leases, with the addition of provisions governing New Lessor's payment for the nuclear fuel prior to installation in the nuclear reactor. He also said the net rent to be paid by Petitioner will be determined in substantially the same manner as under the Current Leases. Alternately, Petitioner and New Lessor may agree upon a different manner of computing rent, such as assuming equal monthly consumption of the Nuclear Fuel. He said each 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 I&M on the termination date for the then-unamortized value of such Nuclear Fuel.

Mr. Boteler stated unless the New Lease is earlier terminated or extended, Nuclear Fuel will be leased under the New Lease for a period up to 60 months. After a minimum time following the execution of the New Lease, I&M or the New Lessor may terminate the New Lease for any reason, upon 180 days prior written notice. The New Lessor may terminate the New Lease prior to a scheduled termination date under certain circumstances, including if (a) it 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, Mr. Boteler stated I&M will purchase all of the New Lessor's interests in the unamortized Nuclear Fuel then subject to the New Lease. Title to the Nuclear Fuel will be transferred to Petitioner or, under certain circumstances, a party designated by I&M and approved by the New Lessor. Petitioner will be obligated to pay the 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 I&M under the New Lease will terminate, except to the extent provided therein.

Mr. Boteler testified the final interest rate spread will be based on one month LIBOR or a fixed rate plus a spread based upon Petitioner's credit ratings. He said that although the interest rate will not be known until the transaction is closed, the proposed method of financing Petitioner's Nuclear Fuel should be 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.

4. Petitioner's Supplemental Testimony. Mr. Boteler explained that since the filing of his direct testimony, Petitioner held a number of discussions with representatives of the OUCC. During the course of these discussions, Mr. Boteler stated that I&M agreed to provide the latest rating reports and, 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 sets forth the monthly calculations for a term of 54 months that compares the cost of Petitioner owning the Nuclear Fuel versus the cost of Petitioner leasing the Nuclear Fuel for the Cook Plant as proposed in this proceeding. He stated he used a term of 54 months because once the Nuclear Fuel is installed at the Cook Plant it generally has a useful life of 54 months and is then removed.

Mr. Boteler testified he used several basic assumptions in performing the hypothetical analysis. Those assumptions included: a weighted average cost of capital of 7.71%, a Nuclear Fuel inventory of \$600 million, a lease start date of November 1, 2011 and a lease rate of 4%. Mr. Boteler explained that in developing the weighted average cost of capital rate of 7.71%, he started with the capital structure that Petitioner submitted in Cause No. 43306. He noted the Commission's March 4, 2009 Order in that Cause approved a settlement agreement that reflected a 10.5% return on equity and an overall cost of capital of 7.62%. He said for this analysis, Petitioner utilized the same equity return and then updated the capital structure to March 31, 2011, which resulted in a weighted average cost of capital of 7.71%. Mr. Boteler stated that the 4% lease rate was developed utilizing the terms of the expected New Lease. He testified Petitioner's analysis shows the net present value of the capital lease option is \$19,527,338 less than the net present value of the owned option over the 54 month term. Therefore, he said, Petitioner estimates that under reasonable financial market conditions, the lease option will result in reduced revenues collected from ratepayers. He also stated that if the lease option ends up being more expensive than the owned option, I&M would simply purchase, rather than lease, the Nuclear Fuel until market conditions became more reasonable.

Mr. Boteler also sponsored Petitioner's Exhibit 2B containing I&M's Balance Sheets as of December 31, 2010 and 2009, Statements of Income for the 12 month periods ended December 31, 2008, and Statements of Changes in Common Shareholder Equity and Comprehensive Income (Loss) for the 12 month periods ending December 31, 2008.

5. OUCC's Testimony. Duane P. Jasheway, a Utility Analyst in the Electric Division of the OUCC, testified that the cost of Petitioner's Nuclear Fuel is recovered through its semi-annual FAC applications, whether the fuel is owned by I&M or leased through a third party. Accordingly, he stated, 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 noted that Petitioner's Exhibit 2-A demonstrates those savings currently are projected to yield a net present value of approximately \$19 million. Given Petitioner's commitment not to enter into any lease at a higher cost than ownership, he opined that any leasing activity should benefit ratepayers. He also noted that I&M calculations demonstrate a net present value benefit of approximately \$8.9 million since 2007 when comparing the cost of leasing versus ownership.

Mr. Jasheway noted the settlement agreement approved in Cause No. 43306, Petitioner's most recent base rate case, included approximately \$50 million of Nuclear Fuel inventory in its rate base, due to I&M's inability to find a lease counter-party at that time. He said that Petitioner expects the \$50 million to be fully amortized in fall 2011 and will address this issue in a subsequent filing.

Mr. Jasheway concluded his testimony with two recommendations: (1) the Commission approve Petitioner's request for authorization for its nuclear financing arrangements; and (2) I&M be required to provide regular updates of its leasing developments, including all terms of said agreements and a calculation of the comparative annual savings to ratepayers of leasing the Nuclear Fuel versus ownership.

6. Commission Discussion and Findings. I&M requests Commission approval to enter into a New Lease(s) with one or more New Lessors. Pursuant to the terms of the New Lease, New Lessor will finance and lease to Petitioner, or New Lessor will purchase from, and lease back to, Petitioner, Nuclear Fuel with a maximum aggregate value of up to \$600 million. Unless the New Lease is earlier terminated or extended, Nuclear Fuel will be leased under the New Lease for a period up to 60 months.

I&M was first authorized by the Commission to enter into a leasing transaction related to the Nuclear Fuel for the Cook Plant in the Commission's December 5, 1990 Order in Cause No. 39051. As noted by the parties, the Commission has approved similar leasing arrangements in Cause Nos. 34795, 41748, 43351 and most recently in Cause No. 43682.

Based on the evidence presented, we find Petitioner's request for approval to enter into a New Lease(s) as set forth herein is reasonable, in the interest of the public and should be approved. The proposed transaction(s) is reasonable in the operation and management of Petitioner's business so as to 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. In addition, I&M has committed to only entering into such leases that cost less than ownership. The capital structure of Petitioner, after giving effect to the

proposed transactions, will be reasonable and in the public interest. After the proposed transactions, the total amount of Petitioner's outstanding stock, notes maturing more than 12 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 Evidentiary Hearing, I&M indicated it did not object to the OUCC's recommendations. We find those recommendations are reasonable and should be implemented. Therefore, I&M shall provide annual updates, through FAC testimony, of its Nuclear Fuel leasing activity.

7. Petitioner's Request for Confidential Treatment. On May 31, 2011, Petitioner filed a Motion for Protection of Confidential and Proprietary Information ("Motion") requesting confidential treatment for trade secret information it intended to submit in this Cause, which was supported by the Affidavit of Mr. Boteler. Mr. Boteler stated that Schedule A of the Current Leases includes information and formulae for determining lease pricing ("Confidential Information"). He stated the Confidential Information has actual or potential economic value to I&M and could cause significant financial damage if publicly disseminated. He further stated that Petitioner and its affiliate, AEPSC, have taken all reasonable steps to protect the Confidential Information from disclosure. On June 14, 2011, the Presiding Officers issued a Docket Entry granting confidential treatment on a preliminary basis.

Pursuant to Ind. Code §§ 8-1-2-29 and 5-14-3-4(a)(4) and based on the evidence presented, we find the Confidential Information to constitute a "trade secret" and should continue to be afforded confidential treatment. Accordingly, this information is exempted from public disclosure and will continue to be held as confidential by the Commission.

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

1. Petitioner's request to enter into a New Lease(s) for Nuclear Fuel with one or more New Lessors is hereby approved. This Order constitutes the certificate of authority.
2. Petitioner shall annually notify the Commission of its nuclear fuel leasing activity, including all terms of said agreements and a calculation of the comparable savings to ratepayers of leasing the Nuclear Fuel versus ownership, through testimony in its FAC proceeding.
3. This Order shall be effective on and after the date of its approval.

ATTERHOLT, BENNETT, LANDIS, MAYS AND ZIEGNER CONCUR:

APPROVED: AUG 31 2011

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


Brenda A. Howe
Secretary to the Commission