ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF NORTHERN INDIANA PUBLIC SERVICE COMPANY FOR APPROVAL OF AN UPDATED ENERGY SUPPLY PLAN IN COMPLIANCE WITH THE INDIANA UTILITY REGULATORY COMMISSION'S ORDER DATED JULY 13, 2011 IN CAUSE NO. 43849, INCLUDING RECOVERY OF CERTAIN COSTS ASSOCIATED WITH THAT POLICY PURSUANT TO IND. CODE § 8-1-2-42(d), CONSISTENT WITH THE APPROVALS GRANTED TO PETITIONER IN CAUSE NO. 43849.	**CAUSE NO. 44205** **APPROVED:** SEP 05 2012

ORDER OF THE COMMISSION

Presiding Officers:
David E. Ziegner, Commissioner
Aaron A. Schmoll, Senior Administrative Law Judge

On May 31, 2012 Northern Indiana Public Service Company ("Petitioner," "Company" or "NIPSCO") filed its Petition for approval of an updated energy supply plan in compliance with the Indiana Utility Regulatory Commission's ("Commission") Order dated July 13, 2011 in Cause No. 43849, including recovery of certain costs associated with that policy pursuant to Ind. Code § 8-1-2-42(d), consistent with the approvals granted to Petitioner in Cause No. 43849. NIPSCO also filed its prepared testimony and exhibits constituting its case-in-chief on May 31, 2012.

A Petition to Intervene was filed by NIPSCO Industrial Group,[1] which was subsequently granted. The Indiana Office of Utility Consumer Counselor ("OUCC") also participated in this proceeding as the statutory representative of the consumers.

Pursuant to notice given as provided by law, proof of which was incorporated into the record, an evidentiary hearing was held in this matter on July 31, 2012, at 10:00 a.m. in Room 222 of the PNC Center, 101 West Washington Street, Indianapolis, Indiana. At the hearing, NIPSCO presented its testimony, which was admitted into evidence without objection. No member of the public appeared or participated at the hearing.

The Commission, having considered the evidence and being duly advised, now finds that:

1. **Notice and Jurisdiction.** Due, legal and timely notices of the public hearings in this Cause were given and published by the Commission as required by law. Petitioner is a

[1] NIPSCO Industrial Group is comprised of Arcelor Mittal USA, Praxair, Inc., and United States Steel Corporation.

public utility within the meaning of the Public Service Commission Act, as amended, Ind. Code § 8-1-2 and is subject to the jurisdiction of the Commission in the manner and to the extent provided by the laws of the State of Indiana. This Commission has jurisdiction over Petitioner and the subject matter of this proceeding.

2. **Petitioner's Characteristics.** Petitioner is a public utility with its principal place of business located at 801 East 86th Avenue, Merrillville, Indiana. Petitioner is authorized by the Commission to provide electric and gas utility service to the public in northern Indiana and owns, operates, manages and controls, among other things, plant and equipment within the State of Indiana used for the production, transmission, delivery and furnishing of such services to the public.

3. **Background and Relief Requested.** In our Order dated July 13, 2011 in Cause No. 43849 ("43849 Order"), we (1) approved NIPSCO's initial Hedging Plan ("Initial Hedging Plan"), (2) authorized NIPSCO to request recovery of the transactional costs associated with hedging its fuel supply in accordance with its Initial Hedging Plan as a fuel cost through its quarterly fuel adjustment clause, (3) authorized NIPSCO to request its hedging gains and losses resulting from transactions made in accordance with its Initial Hedging Plan for inclusion as credits and/or charges to the fuel costs recovered through its quarterly fuel adjustment clause, and (4) ordered NIPSCO to file its updated energy supply plan covering the succeeding two year period on or before May 31 of each year beginning in May 2012. In compliance with the 43849 Order, NIPSCO requests Commission approval of its updated energy supply plan covering the succeeding two year period (July 2012 through June 2014) (the "2012 Hedging Plan") applicable to its electric utility service and for authority to seek recovery of certain costs associated with transactions undertaken consistent with its 2012 Hedging Plan through Petitioner's fuel adjustment clause proceedings, consistent with the approvals previously granted in the 43849 Order.

4. **Evidence Presented.** Daniel T. Williamson, Executive Director of Energy Supply and Trading for NIPSCO, filed testimony to present and support NIPSCO's 2012 Hedging Plan consistent with the framework and process approved by the 43849 Order.

Mr. Williamson testified that in accordance with the process approved by the 43849 Order, NIPSCO reached out to the OUCC and the NIPSCO Industrial Group to discuss the draft electric hedging plan two months prior to its filing and the 2012 Hedging Plan incorporates the input and addresses the comments from its stakeholders.

Mr. Williamson explained the objectives of the 2012 Hedging Plan are to reduce the relative movement in the Fuel Adjustment Clause ("FAC") factor from one period to the next and to limit upside price exposure.

Mr. Williamson explained that the Initial Hedging Plan assumed that all of the coal-fired generation facilities within the NIPSCO asset portfolio were fixed in price. He stated that since a majority of NIPSCO's coal contracts are between 3 and 5 years in length, and since coal pricing has historically been less volatile than natural gas pricing and the Midwest Independent Transmission System Operator, Inc. ("MISO") market price of power, it was determined that any coal-fired generation used to meet the power supply needs of NIPSCO customers could be classified as a fixed price resource. Mr. Williamson stated that any remaining resources that would likely be needed to meet the power supply needs of NIPSCO customers, however, would be classified as floating in price and thus would be considered when developing the hedge plan. He stated the 2012 Hedging Plan also addresses NIPSCO's exposure to both natural gas and electricity price volatility associated with supplying electricity to native load customers.

Mr. Williamson explained how the 2012 Hedging Plan is constructed. He stated that NIPSCO determines the monthly volume of megawatt hours ("MWhs") to be hedged by starting with the total number of on-peak MWhs that would be needed to serve NIPSCO's internal load. The expected number of on-peak MWhs for each month is determined through NIPSCO's demand forecasting process based upon historical usage, estimated economic growth rates and normalized weather. Once the expected number of on-peak MWhs for each calendar month is determined, the PROMOD model is run to determine what resources would be used to meet this expected demand. He explained that due to the lower variable cost and cycling limitations associated with NIPSCO's coal-fired generation supply, the PROMOD model ordinarily applies these resources first before dispatching other NIPSCO generation, and in conjunction with spot energy purchases from the MISO energy markets when economic, to meet the supply needs of NIPSCO's customers. If any additional resources would be required, the model would determine how many MWhs should be provided by NIPSCO's natural gas-fired Sugar Creek Generating Station ("Sugar Creek") and how many MWhs should be purchased from the MISO spot energy market. The model would determine this allocation between producing at Sugar Creek and purchasing from the MISO spot energy market based on the estimated price for each resource at each point in the future.

Mr. Williamson explained that modifications were made to the PROMOD model to refine the resource allocation process. He stated that the PROMOD model is run with forecast hourly spot market prices for electric energy in the MISO spot market floored at a price just above the variable cost of NIPSCO's available coal-fired generation. This is done to remove forecast purchases from the MISO spot energy market that would be made in lieu of producing energy at NIPSCO's available coal-fired generation facilities when it is economical to do so. He stated that these economic spot market energy purchases were removed from PROMOD modeling because they are made at a price below the cost of production of NIPSCO's coal-fired fleet. As such, the price exposure for these spot market energy purchases is already capped at the production cost of NIPSCO's coal-fired generation and do not need to be further hedged. Mr. Williamson testified NIPSCO's remaining on-peak energy requirements were modeled as being supplied either from Sugar Creek or by purchasing energy from the MISO spot energy market. He stated these are the energy requirements for which NIPSCO is subject to market price volatility, and these are the energy requirements that NIPSCO addressed in the Initial Hedging Plan.

Mr. Williamson explained how NIPSCO addresses the market price volatility associated with energy requirements it anticipates will be met either by power generated at Sugar Creek or with purchases made in the MISO spot energy market. He testified that consistent with the methodology approved in the 43849 Order, NIPSCO is proposing in the 2012 Hedging Plan to hedge market price volatility associated with 50% of the projected power volumes that would be supplied by either Sugar Creek or by purchases made in the MISO spot energy market. He stated the OUCC, NIPSCO Industrial Group and NIPSCO originally agreed that hedging 50% of

NIPSCO's exposure to market price volatility, after accounting for the inherent value of the hedge associated with NIPSCO's coal-fired generation, represented an appropriate figure for NIPSCO's Initial Hedging Plan. Mr. Williamson noted that in Cause No. 43849 the level of hedging that results from hedging 50% of NIPSCO's expected power volumes associated with Sugar Creek and MISO purchases would be monitored and evaluated in future hedging plans.

Mr. Williamson testified NIPSCO supports hedging 50% of its exposure to market volatility. He indicated that because the Initial Hedging Plan has only been in existence since 2011, NIPSCO believes that one year is an insufficient amount of time to evaluate the effectiveness of a long term hedging plan. Further, he stated that NIPSCO has not identified any reason that would suggest that 50% is not an appropriate level to hedge and that NIPSCO will continue to monitor and evaluate the appropriateness of its hedging strategy.

Mr. Williamson testified the 2012 Hedging Plan is composed of two types of swap/futures contracts. The first type of swap/futures contract (approved by the 43849 Order) will be used to hedge the on-peak MWhs exposure that relates to Sugar Creek, a combined cycle gas turbine plant that uses natural gas to generate power. He stated the modeled volumes of power from Sugar Creek are converted to dekatherms by multiplying the number of MWhs for each calendar month by the heat rate of the Sugar Creek plant, which is approximately 7.5 dekatherms per MWh. Once the number of dekatherms per calendar month is determined, this number is divided by 10,000 (the number of dekatherms in each natural gas futures contract) to arrive at the number of natural gas futures contracts to be purchased for each calendar month of delivery. Mr. Williamson indicated these contracts settle financially as opposed to physically so they will not have any impact on the physical purchase and delivery of natural gas that is required to run the Sugar Creek plant. He noted that a natural gas futures contract settles financially by comparing the purchase price to the settlement price, netting the difference, and then multiplying this dollar difference by 10,000 to get the dollar amount per contract. Dollars change hands without any physical flow of the commodity itself.

Mr. Williamson testified the Initial Hedging Plan utilized two contracts to establish a hedge against the electricity price volatility – Midwest ISO Cinergy Hub Peak Calendar Month/Real Time Locational Marginal Pricing ("LMP") Swap Future contracts and MISO Cinergy Hub Peak Calendar Month/Day Ahead LMP Swap Futures contracts. He stated these types of swap contracts allowed NIPSCO to purchase power at a fixed price for all on-peak hours of a given month, and then settle the price against the average on-peak hourly Real Time LMP price and then the Day Ahead LMP price for that same calendar month. He stated that while the MISO Cinergy Hub Peak Calendar Month/Real Time LMP Swap Future was the most liquid and actively traded contract type out into the future, it did not perfectly match up with the type of exposure that NIPSCO was attempting to mitigate. Mr. Williamson stated that since NIPSCO purchases its power from MISO on a Day Ahead basis, in order to match this hedge exposure with the most closely linked derivative product, NIPSCO converted MISO Cinergy Hub Peak Calendar Month/Real Time LMP Swap Futures contracts into MISO Cinergy Hub Peak Calendar Month/Day Ahead LMP Swap Futures contracts. He stated this converted swap ultimately settled the original fixed price purchase against the Day Ahead MISO prices. He noted that this type of swap also settles financially as opposed to physically so there will be no impact to MISO supply including the dispatch of NIPSCO's generation facilities and NIPSCO's wholesale sales and purchases of electricity. He indicated that if the fixed price is below the average Day Ahead

LMP price, NIPSCO will receive payment; if the fixed price is above the average Day Ahead LMP price, NIPSCO will make a payment.

Mr. Williamson testified that since approval of the Initial Hedging Plan, NIPSCO has gained further experience operating in the LMP swap futures market. First, on January 1, 2012, MISO Indiana Hub became one of the new hub definitions developed by MISO's Trading Hub Task Force which was approved by MISO members to replace MISO Cinergy Hub in late 2011. Second, NIPSCO has found that the MISO Indiana Hub Peak Calendar Month/Day Ahead LMP Swap Futures contracts are much more liquid and readily available. Therefore, he stated NIPSCO is not planning to utilize the MISO Indiana Hub Peak Calendar Month/Real Time LMP Swap Futures contracts as an intermediate step; rather, NIPSCO will simply execute the number of proposed contracts directly using the Day Ahead type of contracts. Mr. Williamson stated this will provide a direct and more efficient mechanism to hedge the amount of desired contracts and eliminates having to pay additional broker and clearing fees.

Mr. Williamson testified that because of the notable decline in natural gas prices since last year, an increase in the amount of natural gas futures contracts called for under the 2012 Hedging Plan has increased. However, he stated that on the electricity price side of the plan, there are three instances by which the updates suggest a decrease in the amount of contracts, specifically, for July, September and November 2012. Mr. Williamson stated that based upon discussions with the OUCC and NIPSCO Industrial Group, NIPSCO proposes to decrease the amount of natural gas futures contract purchases in these same months on a one-to-one basis to account for the corresponding negative amounts noted for electricity price contracts. He noted that utilizing a 1:1 ratio of natural gas futures contracts to electricity futures contracts best accomplishes the objective of accounting for the negative amounts in those months.

Mr. Williamson testified the hedges under the 2012 Hedging Plan are being solely made to address native load fuel cost price exposure. He testified that the hedges will not change the economic dispatch of NIPSCO's generation facilities or NIPSCO's wholesale electricity sales and purchases; therefore, NIPSCO continues to propose to pass all hedging gains and seek recovery of prudently incurred hedging losses through its FAC filings.

Mr. Williamson explained NIPSCO's proposal for implementing its hedging transactions. He stated that the natural gas futures contracts and the MISO Indiana Hub Peak Calendar Month/Day Ahead LMP Swap Futures contracts will be purchased following specific schedules and will be purchased on a dollar cost averaging basis up to the second to last month before the month of delivery. He stated that the MISO Indiana Hub Peak Calendar Month/Day Ahead LMP Swap Futures contracts will be purchased on a dollar cost averaging basis up through and including the month prior to the delivery month. He stated the schedule is broken up into the different types of futures/swaps contracts to demonstrate when and what number of contracts would be purchased.

Mr. Williamson testified that under the 2012 Hedging Plan, the intent is to start hedging in advance of delivery in a reasonable manner to take full advantage of dollar cost averaging. He stated that because of the updated number of contracts called for under the 2012 Hedging Plan, hedges have already been executed to accommodate the schedule.

Mr. Williamson testified NIPSCO intends to purchase the swaps/futures contracts on or around the third to last business day of the month to take market timing out of the purchase decision. NIPSCO will, however, take into account market conditions and circumstances known at that time and will use its best judgment in purchasing the swaps/futures contracts.

Mr. Williamson sponsored an analysis to determine the possible impact the 2012 Hedging Plan would have on overall purchased power costs. The analysis shows an example of what additional power supply costs could be incurred if market prices move up by 20% from where market pricing was as of close of business on April 23, 2012. He stated that in this example, there could be an additional $20,670,158 of power supply costs (inclusive of CCGT generation and MISO power purchases) if market prices rose by 20% for each month of the planned period. The plan period covers the July 2012 to June 2014 period. The analysis also includes the effect the 2012 Hedging Plan could have on these additional power supply costs. If these hedges were in place and the market was stressed upward by 20% for each month in the plan period, the additional power supply costs would be roughly 50% ($10,365,000) of what they would be without the hedge plan in place. However, if prices were to move downward by 20%, power supply costs could have been reduced by $20,670,158 through the plan period if no hedge plan had been implemented. The analysis demonstrates how a hedge plan can reduce volatility in power supply costs. While possible savings may be forgone when prices fall, the hedge plan reduces additional costs that may have been incurred when prices rise.

Mr. Williamson testified market conditions are dynamic and the analysis is only intended to show the relative impact of the program assuming that market conditions remain the same that they are today. Nevertheless, the analysis provides an indication on what sort of impact this program may have in the future.

Mr. Williamson testified NIPSCO is proposing to file its next revised electric hedging plan by March 31 of each year instead of May 31 to address the impact of entering into hedges in the early months of the hedging plan. He stated NIPSCO proposes to reach out to the OUCC and the NIPSCO Industrial Group to discuss its next revised electric hedging plan two months prior to its proposed March filing. He indicated this change will assist NIPSCO's efforts to execute hedges that are called for under the updated hedging plan at the front end of the two-year schedule.

Mr. Williamson testified that under the proposed framework, stakeholders would have until May 15 to provide feedback on NIPSCO's next revised hedging plan so that purchases under the plan could commence by May 28 of that same year.

5. <u>Commission Discussion and Findings</u>. In Cause No. 43849, we found that:

> the mitigation of volatility in fuel procurement is consistent with the provisions of Ind. Code § 8-1-2-42(d), and that implementation of a process to evaluate the risk of fuel price volatility and mitigate such risk through a comprehensive and well-developed hedging plan, is a reasonable step in furtherance of the acquisition of fuel so as to provide electricity to customers at the lowest fuel cost reasonably possible.

43849 Order at 10. The 2012 Hedging Plan is an update to the plan approved in that Cause that was filed by NIPSCO generally consistent with the approach we approved.

The evidence demonstrates that NIPSCO has communicated with the OUCC and the NIPSCO Industrial Group in the interest of improving the plan. Mr. Williamson's testimony documents how the changes from the approach approved in Cause No. 43849 were developed to adapt to changes in market conditions for both natural gas and contractual purchases of energy to accomplish the mitigation of risk consistent with the goals of the plan and to strike an appropriate balance between the mitigation of volatility and exposure to transactional costs. No evidence was presented that the 2012 Hedging Plan is inconsistent with our findings in the 43849 Order. Based on the evidence of record, we find the proposed 2012 Hedging Plan is reasonable, consistent with the public interest and should be approved.

With respect to future annual updates to NIPSCO's energy supply plan, we approve the following process:

- Each year, at least two months before its annual March 31 filing of its updated energy supply plan, NIPSCO will meet with the OUCC and NIPSCO's interested retail customer stakeholders to discuss whether the specifics of the hedging plan methodology warrant adjustment.

- Each year on or before March 31, NIPSCO shall file under Cause Number 44205 S "X" its updated energy supply plan along with testimony explaining why or why not any changes to the methodology or hedging plan are warranted.

- The OUCC and Intervenors shall file objections or comments (if any) under the subdocket no later than 45 calendar days (unless extended by the Presiding Officers) after NIPSCO files its updated energy supply plan and supporting testimony ("Stakeholder Objections").

- If any Stakeholder Objections are filed, NIPSCO shall file its Reply to Stakeholder Objections no later than seven calendar days after the date Stakeholder Objections were due (unless extended by the Presiding Officers).

- If Stakeholder Objections are timely filed, the Commission shall convene an evidentiary hearing to allow the parties to present their respective evidence and cross-examine the witnesses.

- If no Stakeholder Objections are filed, the Commission may issue an Order on NIPSCO's request for approval of the updated energy supply plan without a hearing, given that the prudency of any costs incurred as a result of a subsequent hedging plan will be addressed in the FAC hearing process. Petitioner shall file its proposed order within 10 days of the date Stakeholder Objections were due.

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

1. NIPSCO's proposed 2012 Hedging Plan is hereby approved. For subsequent years, NIPSCO shall file in the appropriate subdocket its updated energy supply plan covering the succeeding two year period on or before March 31 of each year beginning in March of 2014 and the Commission shall consider NIPSCO's request for approval of subsequent updated energy supply plans based on the process outlined in paragraph 5.

2. NIPSCO is authorized to request recovery of the transactional costs associated with hedging its fuel supply in accordance with its 2012 Hedging Plan as a fuel cost through its quarterly FAC. Such transactional costs should be separately identified in the schedules supporting each such filing, and upon a finding of prudency shall be recoverable through NIPSCO's quarterly FAC.

3. NIPSCO is authorized to request its hedging gains and losses resulting from transactions made in accordance with NIPSCO's 2012 Hedging Plan for inclusion as credits and/or charges to the fuel costs recovered through NIPSCO's quarterly FAC. Such credits and/or charges should be separately identified in the schedules supporting each such filing, and upon a finding of prudency shall be recoverable through NIPSCO's quarterly FAC.

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

ATTERHOLT, BENNETT, LANDIS, MAYS AND ZIEGNER CONCUR:

APPROVED: SEP 05 2012

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