

ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

**VERIFIED PETITION OF INDIANA MICHIGAN)
POWER COMPANY (“I&M”), AN INDIANA) CAUSE NO. 44331 ECR 1
CORPORATION, FOR APPROVAL OF AN)
ADJUSTMENT TO ITS RATES THROUGH ITS)
FEDERAL MANDATE RIDER BEGINNING WITH) APPROVED:
THE BILLING MONTH OF JANUARY 2015.)**

DEC 30 2014

ORDER OF THE COMMISSION

**Presiding Officers:
Angela Rapp Weber, Commissioner
Jeffery A. Earl, Administrative Law Judge**

On August 20, 2014, Indiana Michigan Power Company (“I&M”) filed a Verified Petition initiating this Cause. Also on August 20, 2014, I&M filed the direct testimony, exhibits, and workpapers of the following witnesses:

- Robert L. Walton, Managing Director of Projects at American Electric Power Service Corporation (“AEPSC”);
- Andrew J. Williamson, Director of Regulatory Services at I&M; and
- Nancy A. Heimberger, Principal Regulatory Consultant in Regulated Pricing and Analysis at AEPSC.

On October 17, 2014, the Indiana Office of Utility Consumer Counselor (“OUCC”) filed the testimony and exhibits of Wes R. Blakely, Senior Utility Analyst in the OUCC’s Electric Division.

On October 27, 2014, I&M filed rebuttal evidence and workpapers from Mr. Williamson and Ms. Heimberger.

The Commission held an evidentiary hearing in this Cause at 9:30 a.m. on November 3, 2014, in Hearing Room 222, 101 West Washington Street, Indianapolis, Indiana. I&M and the OUCC appeared and participated at the hearing. No members of the general public attended the hearing.

Based upon the applicable law and the evidence presented the Commission finds:

1. Notice and Jurisdiction. Notice of the evidentiary hearing in this Cause was given and published by the Commission as required by law. I&M is a “public utility” under Ind. Code § 8-1-2-1 and an “energy utility” under Ind. Code § 8-1-8.4-3. The Commission’s November 13, 2013 Order in Cause No. 44331 (the “44331 Order”) granted a certificate of public convenience and necessity to I&M for I&M’s Rockport Clean Coal Technology (“CCT”) Project to install a Dry Sorbent Injection (“DSI”) system (“Rockport CCT Project”) pursuant to

Indiana Code ch. 8-1-8.4 (“Chapter 8.4”). The Commission also authorized the recovery of the Rockport CCT Project costs as Federally Mandated Costs in accordance with Chapter 8.4 and the terms of the 44331 Settlement Agreement. Therefore, the Commission has jurisdiction over I&M and the subject matter of this Cause.

2. I&M’s Organization and Business. I&M, a wholly owned subsidiary of American Electric Power Company, Inc., is a corporation organized and existing under the laws of the State of Indiana, with its principal offices at One Summit Square, Fort Wayne, Indiana. I&M is engaged in, among other things, rendering electric service in the States of Indiana and Michigan. I&M owns, operates, manages, and controls plant and equipment within the States of Indiana and Michigan that are in service and used and useful in the generation, transmission, distribution, and furnishing of such service to the public.

3. Relief Requested. I&M seeks approval of an adjustment to its rates through its Federal Mandate Rider (“FMR”) and the initial FMR factors, effective with the first billing cycle for the billing month of January 2015 (beginning December 31, 2014) or the first full billing month following a Commission order. If approved, the factors, upon becoming effective, shall remain in effect for approximately six months or until replaced by different factors approved in a subsequent filing. The proposed factors include the Indiana Retail Jurisdictional Share of the historical and forecasted Federally Mandated Costs for the Rockport CCT Project.

Pursuant to the Commission’s Order in Cause No. 43636 ECR 7, I&M has also included in the initial FMR factors the residual over- or under-recovery balance from I&M’s Clean Coal Technology Rider (“CCTR”) related to the Selective Non-Catalytic Reduction (“SNCR”) and Activated Carbon Injection (“ACI”) Projects, along with the recovery of the regulatory assets arising from the deferred post-in-service return on the ACI and SNCR Projects.

4. I&M’s Direct Evidence.

A. Compliance Project Report. Mr. Walton discussed the progress of the Rockport CCT Project, including expected in-service dates and provided an updated capital cost estimate for the Rockport CCT Project and the actual capital costs incurred through June 30, 2014. He also provided forecasted capital and operations and maintenance (“O&M”) expenses associated with the Rockport CCT Project. Mr. Walton summarized the capital costs incurred during a historical period, which extended from the start of the Rockport CCT Project through June 30, 2014, and the forecasted capital costs for the period of July 1, 2014, through June 30, 2015.

B. Cost Recovery and FMR Factors. Mr. Williamson supported the initial FMR factors and associated revenue requirement. He sponsored Petitioner’s Exhibit 2, Attachment AJW-8, which identified the revenue requirement components included for recovery in the FMR factors. The proposed factors include projected costs related to the Rockport CCT Project, projected preconstruction costs, amortization of deferred DSI costs incurred through December 2014, and amortization of the regulatory assets and liability balances from Cause No. 43636 ECR 7. The proposed FMR factors are based on actual costs through June 2014 and forecasted costs through June 2015.

Mr. Williamson also addressed the exhibits prepared to calculate the semi-annual FMR factors to be used by I&M in this and ongoing semi-annual ECR proceedings. Because the FMR statute allows inclusion of 80% of costs in the FMR factors, I&M has built the schedules in this proceeding utilizing the full 100% value of all applicable costs then subsequently adjusted these costs to 80%. Mr. Williamson believes that this approach provides the clearest ratemaking methodology because it allows I&M to easily substantiate the costs with I&M's accounting and forecasting records.

Ms. Heimberger explained how I&M's jurisdictional FMR costs are allocated to the rate classes and how the proposed FMR factors were calculated. She discussed the four components of the FMR cost calculation, including (1) the forecasted Rockport CCT Project costs, (2) forecasted Rockport preconstruction costs, (3) the residual CCTR balance and regulatory assets from Cause No. 43636 ECR 7, and (4) the reconciliation of actual costs to actual billing to determine the over- or under-recovery amount, which is set to zero for this initial filing. Ms. Heimberger also provided the estimated rate impact on I&M's Indiana customers.

5. OUC's Direct Evidence. Mr. Blakley reviewed I&M's filing and recommended two adjustments to the proposed initial factors.

A. PJM 4 Settlement Agreement. Mr. Blakley recommended that I&M adjust its return on equity ("ROE") to 9.95% per the settlement agreement in Cause No. 43774 PJM 4 ("PJM 4 Settlement Agreement"), which was approved on October 2, 2014, after the submission of I&M's case-in-chief. Mr. Blakley recommended I&M recalculate its weighted average cost of capital ("WACC") to be applied to eligible construction costs in this Cause and apply the new WACC to actual completed construction.

B. Forecasted Costs. Mr. Blakley also recommended that the initial FMR factors exclude recovery of forecasted construction costs and forecasted depreciation and O&M expenses not associated with CCT equipment completed as of June 30, 2014. He said such costs, when incurred and known, will be eligible for treatment in future ECR tracker proceedings. Mr. Blakley testified that I&M's attempt to include forecasted qualified pollution control property ("QPCP") construction costs is inconsistent with established practice and the Commission's rules. More specifically, he said 170 IAC 4-6-14(1)(A) requires the utility to include in its WACC calculation "[t]he amount, ratio, and cost rate for the utility's long term debt and preferred equity capital as of the date of valuation of the utility's [QPCP] under construction for which the utility is seeking ratemaking treatment." He testified that the date of valuation of the QPCP cannot be in the future because it is not possible to determine cost rates for debt in the future. He added that a utility's capital structure balances of debt, equity, and zero cost capital cannot be forecast because the balances are constantly changing. He stated that 170 IAC 4-6-14 requires the calculation of the WACC be established at a point in time when the value of the construction project can be determined. In his view, the rule does not contemplate or allow for a forecasted capital structure or forecasted construction costs. He said 170 IAC 4-6-20 allows for the continued accrual of funds used during construction ("AFUDC") until the property is included in the tracker for recovery, at which time the AFUDC stops. Mr. Blakley stated he was unaware of any other Indiana electric utility with CCT projects that has asked for or received recovery of a return on, depreciation, and O&M on forecasted construction that will be built in the future.

6. I&M's Rebuttal and Supplemental Testimony.

A. PJM 4 Settlement Agreement and Revised FMR Factors. Mr. Williamson agreed with Mr. Blakley that I&M's ROE should be adjusted for purposes of the WACC calculation pursuant to the terms of the PJM 4 Settlement Agreement. He provided revised exhibits reflecting the change in ROE from 10.2% to 9.95% for investments as of January 1, 2015. He said updating the WACC reduces the FMR revenue requirement by \$53,982.

Mr. Williamson also explained that I&M discovered a miscalculation in the initial filing that, once corrected, results in a decrease to the revenue requirement. He explained that part of the initial calculation incorrectly used an Indiana jurisdictional consumables balance rather than a total company balance in a calculation. He provided updated exhibits reflecting a reduction to the consumables balance, modified I&M's proposed FMR factors to reflect the changes from the revised WACC and consumables, and presented revised tariff sheets. Mr. Williamson explained that these revisions produce a reduction in the proposed factors. Under the new factors, the bill of a typical residential customer using 1,000 kWh per month would increase by \$1.24 or 1.2%.

B. Forecasted Costs. Mr. Williamson disagreed with Mr. Blakley's proposal to exclude forecasted costs after June 30, 2014, from the FMR factors. Mr. Williamson explained that Mr. Blakley's proposal varied from the process provided by the settlement agreement approved in Cause No. 44331 ("44331 Settlement Agreement"). Mr. Williamson said that the settlement testimony in that Cause explained that the FMR "uses the same structure currently in place for timely recovery of costs and expenses through I&M's CCTR" and that "[m]irroring the cost recovery of the 80% of Federally Mandated Costs with the CCTR recovery avoids potential disputes about how such cost recovery will occur."

Mr. Williamson also disagreed with Mr. Blakley's claim that forecasted construction costs have never been sought in QPCP tracker proceedings. Mr. Williamson explained that I&M used a forecasted revenue requirement in each of its CCTR proceedings filed in Cause Nos. 43636 ECR 1 through ECR 7 and the Commission approved ECR factors based on the forecasted revenue requirements during the respective rate period for this QPCP. He said the Commission has therefore included forecasted costs in the very rider that the FMR was designed to mirror.

Mr. Williamson also disagreed with Mr. Blakley's view that 170 IAC 4-6-14 precludes use of a forecasted period to develop rates that provide for timely cost recovery. Mr. Williamson explained that Mr. Blakley's opinion appears to be that the words "date of valuation" as used in this rule can only be a historical date, but from an accounting and ratemaking standpoint, Mr. Williamson did not see anything in the rule that would require the use of a historical date to determine the value of the QPCP under construction. Mr. Williamson explained that the rule allows I&M to forecast QPCP costs for each month within each rate period and use the historical WACC as a proxy in those periods, subject to over- or under-accounting on the date of valuation at the end of the period. He testified that this is sound ratemaking because it allows I&M to establish rates that align with the expected cost of service for each rate period. He said the process proposed in the FMR and used previously in I&M's CCTR is appropriate and follows the language found in the rule. Mr. Williamson explained that the Commission has approved rates based on a forecast in several periodic rate adjustment proceedings, including I&M's Fuel Cost Adjustment ("FAC"), Cook Life Cycle Management, PJM Cost Rider, and OSS Margin

Sharing Rider. He also said that I&M will utilize over/under accounting to ensure customers ultimately only pay rates that reflect costs approved for recovery.

Mr. Williamson disagreed with Mr. Blakley's view that it is not possible to forecast the WACC but stated that this is an academic question because I&M used a historical WACC. Mr. Williamson explained that it is possible to forecast debt, equity, and zero cost of capital, including changes in costs due to debt maturities, debt issuances, debt refinancing, capital dividends, capital infusions, and change in ROE. He explained that a forecast of changes in debt and equity cost would be supported by the AEPSC Finance Department, which has considerable knowledge of debt, or bond, market conditions, I&M's debt ratings, I&M's capital position, and I&M's current debt obligations. He stated that the AEPSC Tax Department also forecasts accumulated deferred income taxes, which is the biggest component of zero cost of capital.

Mr. Williamson explained that I&M's level of debt, equity, and zero cost of capital balances are considerably large and would require a sizable transaction in the near term to cause a significant deviation from a historical WACC. He stated that it is unlikely that a significant transaction affecting I&M's WACC would not be reasonably known at the time of a forecast. He added that even if an unforeseen event significantly affecting I&M's WACC did occur between the filing date and the end of the rate period, the period of time it would impact FMR factors would be no more than six months because FMR factors are updated semi-annually and this difference would be trued-up through the over/under accounting process.

7. Commission Discussion and Findings.

A. Disputed Issue. The one dispute in this proceeding is whether I&M should be permitted to include forecasted costs in its proposed FMR factors. As discussed below, we find I&M's FMR factors properly include forecasted costs.

The FMR was established by the Commission's 44331 Order approving the 44331 Settlement Agreement. Paragraph 6 of the 44331 Settlement Agreement sets forth how cost recovery via the FMR will be implemented. In pertinent part, the 44331 Settlement Agreement provides that the FMR "will be set up to use the same structure currently in place for timely recovery of costs and expenses through I&M's Clean Coal Technology Rider (CCTR)." The record demonstrates that the CCTR is structured to reflect forecasted CCT costs in the rider factors. The record also shows that I&M's testimony in support of the 44331 Settlement Agreement explained that mirroring the CCTR cost recovery in the FMR was an important part of I&M's decision to enter into the 44331 Settlement Agreement. The 44331 Order also supports the inclusion of forecasted costs in the FMR and use of the CCTR cost recovery structure.

Mr. Blakley's position is not consistent with the 44331 Settlement Agreement, the tariff, or the supporting settlement testimony. I&M used a forecasted revenue requirement in its CCTR tracker mechanism approved in Cause No. 43636 and implemented in Cause Nos. 43636 ECR 1 through ECR 7. The 44331 Settlement Agreement says that the FMR will be set up using the same structure as the CCTR.

We further find that 170 IAC 4-6-14 does not prohibit the use of a forecasted capital structure or forecasted construction costs. The phrase "date of valuation" as used in 170 IAC 4-6-

14 refers to the property under construction. There is no language in 170 IAC 4-6-14 that requires the use of a historical date of valuation for the utility's QPCP under construction for which the utility is seeking ratemaking treatment. In this case, I&M has forecasted the progress of construction through June 30, 2015. We have previously authorized the use of forecasted costs in numerous rate adjustment mechanisms.

The evidence demonstrates that I&M calculated its FMR factors in conformance with the 44331 Order and the 44331 Settlement Agreement. I&M's proposed factors are also consistent with the methodology set forth in the FMR tariff, which specifically provides for the use of an estimated period for both kWh sales and the FMR revenue requirement. Therefore, we find that I&M properly based its proposed FMR factors on actual and forecasted costs.

B. Amount of Rockport CCT Construction Costs. Mr. Walton sponsored Petitioner's Exhibit 1, Attachment RLW-1, which set forth the construction costs for which I&M seeks ratemaking treatment in this Cause. Mr. Williamson stated the 44331 Order approved recovery of I&M's Indiana Retail Jurisdictional share of preconstruction costs to be amortized and recovered over the remaining life of the Rockport facility, and approved that the preconstruction costs will earn a return based on I&M's WACC. He explained I&M's filing in this Cause also includes the residual balance from I&M's CCTR from Cause No. 43636 ECR 7. As shown on Petitioner's Exhibit 2, Attachment AJW-4, this final net over-recovery balance/amount of \$7,117 results in a one-time reduction to FMR rates. In addition, the filing includes the recovery of the regulatory assets related to the deferred post in-service return on the ACI and SNCR Projects, as approved in Cause No. 43636 ECR 7. The amount of this regulatory asset to be collected in the FMR is an under-recovery balance of \$51,336 as shown on Petitioner's Exhibit 2, Attachment AJW-4.

C. Rate of Return on Approved QPCP Construction Costs. Mr. Williamson agreed with Mr. Blakley that I&M's ROE should be adjusted for purposes of the WACC calculation pursuant to the terms of the PJM 4 Settlement Agreement. Petitioner's Exhibit 2-R, Revised Attachment AJW-7 reflects the calculation of I&M's gross revenue conversion factors utilizing a ROE of 9.95% instead of 10.2%. He said updating the WACC for investments as of January 1, 2015, results in an FMR revenue requirement reduction of \$53,982. Therefore, we find I&M has properly reflected the PJM 4 Settlement Agreement in its proposed factors.

D. Recovery of Depreciation, Carrying Costs, O&M Expenses, and Taxes. The 44331 Order provides for timely recovery of depreciation, carrying costs, O&M expenses (including consumables), and taxes. Petitioner's Exhibit 2-R, Revised Attachment AJW-2 provides the calculation of FMR jurisdictional depreciation expense, the investment balances and post in-service carrying costs on the Rockport CCT Project, construction work in progress carrying costs, and the FMR jurisdictional monthly O&M expenses and consumables for the forecasted period. Mr. Williamson stated that for this initial FMR rate filing, I&M has not included Rockport CCT Project property tax expense because property tax expense was not incurred during the actual period. He explained it is uncertain at this time whether I&M will incur Rockport CCT Project property tax expense during the forecast period. He said if I&M does incur property tax expense related to the ownership share, I&M will reconcile this

difference in subsequent FMR rate filings and through the accounting over- or under-true-up process. We find this approach to be reasonable.

E. Revenue Requirement. I&M submitted evidence regarding the derivation of its revenue requirement, including tax calculations, associated with the ratemaking treatment for the Rockport CCT Project construction costs. Mr. Williamson sponsored Petitioner’s Exhibit 2-R, Revised Attachment AJW-8, which provides the jurisdictional revenue requirement of \$6,706,303. We accept I&M’s calculation.

F. Net Operating Income for FAC Proceedings. The 44331 Order requires I&M to add the approved return on its Rockport CCT Project to its net operating income authorized by the Commission for the purposes of Ind. Code § 8-1-2-42(d)(2) and Ind. Code § 8-1-2-42(d)(3) in all subsequent FAC proceedings. For purposes of computing authorized net operating income for Ind. Code § 8-1-2-42(d)(2) and Ind. Code § 8-1-2-42(d)(3), we find that the jurisdictional portion of the increased return shall be phased-in over the appropriate period of time that I&M’s net operating income is affected by the earnings modification resulting from the Commission’s approval of this FMR Adjustment.

G. Allocation of Jurisdictional Revenue Requirement. Ms. Heimberger discussed the allocation of the revenue requirement among I&M’s customer classes. Petitioner’s Exhibit 2-R, Revised Attachment NAH-1 demonstrates the allocation of the FMR revenue requirement among I&M’s customer classes and appropriately uses the allocation factors from I&M’s most recent electric rate case in Cause No. 44075, which the Commission approved on February 13, 2013.

H. Approval of Rider Adjustments. Petitioner’s Exhibit 2-R, Revised Attachment NAH-3 sets forth the proposed FMR factors for each customer class as follows:

Tariff Class	¢/kWh
RS, RS-TOD, RS-TOD2 and RS-OPES	0.1241
GS, GS-TOD and GS-TOD2	0.1035
LGS and LGS-TOD	0.1038
IP, CS-IRP and CS-IRP2	0.0850
MS	0.1141
WSS	0.0834
IS	0.4175
EHG	0.1019
OL	0.0662
SLS, ECLS, SLC, SLCM AND FW-SL	0.0568

Based on our discussion above, we find that I&M has complied with the rules and procedures applicable to its request, including the requirements of Ind. Code § 8-1-8.4-7 and the 44331 Order and 44331 Settlement Agreement. We further find that the proposed FMR factors are properly calculated. Therefore, we approve the FMR factors contained in Petitioner’s Exhibit 2-R, Revised Attachment NAH-3, effective for all bills rendered for electric service beginning with the first full billing cycle for the billing month of January 2015.

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

1. I&M's proposed Federal Mandate Rider factors as set out in this Order are approved.

2. I&M shall add the approved return on its Rockport CCT Project to its net operating income authorized by the Commission for the purposes of Indiana Code §§ 8-1-2-42(d)(2) and 8-1-2-42(d)(3) in all subsequent FAC proceedings. For purposes of computing the authorized net operating income, the jurisdictional portion of the increased return shall be phased-in over the appropriate period of time that the I&M's net operating income is affected by the earnings modification authorized herein.

3. I&M shall file with the Electricity Division of the Commission an amendment to its tariff reflecting the approved Federal Mandate Rider factors in the form of Petitioner's Exhibit 2-R, Revised Attachment NAH-3.

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

STEPHAN, HUSTON, WEBER, AND ZIEGNER CONCUR; MAYS-MEDLEY ABSENT:

APPROVED: **DEC 30 2014**

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


Brenda A. Howe
Secretary to the Commission