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STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

VERIFIED PETITION OF DUKE ENERGY INDIANA,)
INC. PURSUANT TO INDIANA CODE SECTIONS 8-1-)
8.4-1 ET SEQ., 8-1-2-19, AND 8-1-2-42(a) REQUESTING)
THE APPROVAL OF AND FOR (1) A CERTIFICATE)
OF PUBLIC CONVENIENCE AND NECESSITY FOR)
FEDERALLY MANDATED COMPLIANCE PROJECTS)
AND COSTS; (2) ESTIMATED COSTS OF ITS)
FEDERALLY MANDATED COMPLIANCE)
PROJECTS; (3) RECOVERY OF 80% OF FEDERALLY)
MANDATED COSTS ON A TIMELY BASIS THROUGH)
AN APPLICABLE RATE ADJUSTMENT)
MECHANISM; (4) DEFERRAL OF 20% OF)
FEDERALLY MANDATED COSTS ON AN INTERIM)
BASIS, WITH CARRYING COSTS, UNTIL THE)
APPLICABLE COSTS ARE REFLECTED IN)
PETITIONER'S BASE RETAIL ELECTRIC RATES; (5))
ONGOING REVIEW OF THE FEDERALLY)
MANDATED COMPLIANCE PROJECTS; AND (6))
CONFIDENTIAL TREATMENT OF CERTAIN)
INFORMATION RELATING TO PETITIONER'S)
FEDERALLY MANDATED COMPLIANCE PROJECTS)

CAUSE NO. 44367

APPROVED: JUN 25 2014

ORDER OF THE COMMISSION

Presiding Officers:

Carolene Mays, Vice-Chair
Jeffery A. Earl, Administrative Law Judge

On July 17, 2013, Duke Energy Indiana, Inc. ("Duke") filed its Petition in this Cause. On August 23, 2013, Duke filed the testimony and exhibits of the following:

- Diane L. Jenner, Director, Regulatory Strategy at Duke Energy Business Services LLC ("DEBS");
- Gregory D. Rowland, Franchised Electric and Gas Policy Development Director at DEBS;
- John Anderson, Director—Transmission Compliance Coordination at Duke Energy Progress, Inc.;
- Kent K. Freeman, Rate Strategy and Projects Director, Rates—Indiana at DEBS; and
- Mark G. Powell, Director, Fossil/Hydro Compliance at DEBS.

Also on August 23, 2013, Duke filed a Motion for Protection of Proprietary and Nondisclosure of Confidential Information and Critical Energy Infrastructure Information, which

the Presiding Officers granted by Docket Entry dated September 10, 2013. On September 16, 2013, Duke filed Mr. Powell's confidential testimony.

On November 5, 2013, the Indiana Office of the Utility Consumer Counselor ("OUCC") filed the direct testimony and exhibits of the following:

- Ronald L. Keen, Senior Analyst in the OUCC's Resource Planning and Communications Division; and
- Stacie R. Gruca, Senior Analyst in the OUCC's Electric Division.

On November 19, 2013, Duke filed the rebuttal testimony of Msrs. Powell and Freeman.

The Commission held an evidentiary hearing in this Cause at 9:30 a.m. on December 16, 2013, in Hearing Room 222, 101 West Washington Street, Indianapolis, Indiana. Duke and the OUCC appeared and participated at the hearing. No members of the general public appeared or participated at the hearing.

Having considered the evidence presented and the applicable law, the Commission finds:

1. Notice and Jurisdiction. Notice of the hearings in this Cause was given and published as required by law. Duke is a public utility as that term is defined in Ind. Code § 8-1-2-1(a) and an energy utility as that term is defined in Ind. Code §§ 8-1-2.5-2 and 8-1-8.4-3. Under Ind. Code §§ 8-1-8.4-6 and 8-1-8.4-7, the Commission has authority to issue a certificate of public convenience and necessity and to approve cost recovery for projects necessary to comply with federally mandated requirements. Under Ind. Code § 8-1-2-42, the Commission has authority over changes to Duke's rates and charges. Therefore, the Commission has jurisdiction over Duke and the subject matter of this proceeding.

2. Petitioner's Characteristics. Duke is an Indiana corporation with its principal office located at 1000 East Main Street, Plainfield, Indiana. Duke supplies electric utility service to the public in the State of Indiana. Duke owns, operates, manages, and controls plant, property, and equipment used and useful for the production, transmission, distribution, and furnishing of electric utility service to the public in the State of Indiana. Duke directly supplies electric energy to approximately 794,000 customers in 69 counties in the central, north central, and southern parts of the State of Indiana. Duke also sells electric energy for resale to municipal utilities, Wabash Valley Power Association, Inc., the Indiana Municipal Power Agency, and other public utilities.

3. Background and Relief Requested. Duke requests a Certificate of Public Convenience and Necessity ("CPCN") under Ind. Code ch. 8-1-8.4 for its North American Electric Reliability Corporation ("NERC") Critical Infrastructure Protection ("CIP") Compliance Phase I projects that are necessary to comply with Version 4 of the CIP Reliability Standards ("CIP 4 Standards") approved by the Federal Energy Regulatory Commission ("FERC") ("CIP Compliance Projects").

NERC CIP Reliability Standards were first approved by FERC on January 18, 2008, in Order No. 706 (Docket No. RM06-22-000) and required certain users, owners, and operators of the Bulk Power System to comply with specific requirements to safeguard critical cyber assets. There are currently eight CIP Reliability Standards. The CIP 4 Standards were approved by FERC on April 19, 2012, in Order No. 761 (Docket No. RM11-11-000).

Duke also requests approval to recover the costs incurred in connection with the CIP Compliance Projects. Duke requests a finding that the CIP 4 Standards and Version 5 of the NERC CIP Reliability Standards (“CIP 5 Standards”)¹ are (or will be) federally mandated requirements under Ind. Code § 8-1-8.4-5 and that Duke’s CIP Compliance Projects meet the requirements of a federally mandated compliance project under Ind. Code § 8-1-8.4-2. In addition, Duke requests approval of an annual federally mandated cost adjustment mechanism (“FMCA”) under Ind. Code §§ 8-1-8.4-7 and 8-1-2-42 to allow the recovery of 80% of the federally mandated project costs and ongoing expenses. Consistent with Ind. Code § 8-1-8.4-7, Duke proposes to defer 20% of the federally mandated project costs and ongoing expenses incurred in connection with the CIP Compliance Projects for recovery in Duke’s next general rate case.

4. Duke’s Direct Evidence.

A. Diane Jenner. Ms. Jenner testified about whether the CIP 4 Standards meet the statutory definition of federally mandated requirements under Ind. Code § 8-1-8.4-5 and whether Duke meets the statutory requirements of Ind. Code § 8-1-8.4-1. Under the statute, a federally mandated requirement is a requirement that the Commission determines is imposed on an energy utility by the federal government related to various federal laws including any law, order, or regulation administered or issued by FERC. CIP 4 is a regulation administered or issued by FERC and compliance with it is mandatory.

The estimated total costs for Duke’s CIP Compliance Projects are \$817,091 of capital in 2013, \$64,002 of capital in 2014, and \$15,000 of operations and maintenance costs (“O&M”) in 2014. Ms. Jenner acknowledged the possibility that CIP 5 would be approved prior to the end of this case, but said that the CIP Compliance Projects would still need to be completed in order to comply with CIP 5. In addition, the projects will help protect Duke’s critical assets from physical and electronic security breaches. If the projects are not completed, Duke could be subject to financial penalties. In addition, the bulk electric system would be at risk of physical or cyber attacks that could cause large-scale power outages.

B. Gregory Rowland. Mr. Rowland discussed the CIP 4 and CIP 5 Standards. On April 19, 2012, FERC approved the CIP 4 Standards with implementation required by April 1, 2014. On August 12, 2013, FERC granted an extension for compliance until October 1, 2014. The CIP 4 Standards include the following:

¹ FERC approved the CIP 5 Standards on November 21, 2013, while this case was pending. For purposes of this Order, we address only the requirements for compliance with the CIP 4 Standards as they existed prior to the approval of the CIP 5 Standards.

- CIP-002-4—Cyber Security—Critical Cyber Asset Identification. This standard requires the identification and documentation of critical cyber assets supporting the bulk electric system.
- CIP-003-4—Cyber Security—Security Management Controls. This standard requires that minimum security management controls be in place to protect critical cyber assets.
- CIP-004-4—Cyber Security—Personnel & Training. This standard requires that personnel who have authorized cyber or unescorted physical access to critical cyber assets have an appropriate level of personnel risk assessment, training, and security awareness. This standard also applies to contractors and service vendors.
- CIP-005-4—Cyber Security—Electronic Security Perimeters. This standard requires the identification and protection of electronic security perimeters around all critical cyber assets and all access points.
- CIP-006-4—Cyber Security—Physical Security of Critical Cyber Assets. This standard requires implementation of a physical security program to protect critical cyber assets.
- CIP-007-4—Cyber Security—Systems Security Management. This standard requires a utility to define methods, processes, and procedures for securing critical cyber assets and non-critical cyber assets inside the electronic security perimeter.
- CIP-008-4—Cyber Security—Incident Reporting & Response Planning. This standard requires the identification, classification, response, and reporting of cyber security incidents related to critical cyber assets.
- CIP-009-4—Cyber Security—Recovery Plans for Critical Cyber Assets. This standard requires a utility to have a recovery plan for critical cyber assets that follows established business continuity and disaster recovery techniques and practices.

In order to comply with the standards, Duke must define new physical and cyber boundaries and install access control and monitoring mechanisms, implement tools and processes to prevent malicious code, implement tools and processes to apply security patches to mitigate known vulnerabilities, and implement tools and processes to monitor individual and system access to protected systems. While these types of measures were required by earlier CIP Standards, CIP 4 expanded the scope of the assets to which the standards apply.

On January 31, 2013, NERC submitted CIP 5 Standards for FERC approval. The CIP 5 Standards allow for consideration of applicable features of the National Institute of Standards and Technology (“NIST”) Risk Management Framework, consideration of mechanisms for identifying critical cyber assets by examining communication paths between cyber resources and any asset supporting a reliability function, and the provision of a method of review and approval of critical cyber asset lists from external sources. The CIP 5 Standards use a NIST-Based approach to categorize all cyber systems that impact the bulk electric system as high-, medium-, or low-impact, which is a change from the critical or non-critical categorization of the CIP 4 Standards. The addition of a low-impact category requires protection of systems not included in the CIP 4 Standards. The CIP 5 Standards also include USB security, which requires tools and processes for the appropriate use and protection of thumb drives and other external media.

Compliance with CIP 4 is mandatory. Non-compliance would result in financial penalties as determined by ReliabilityFirst, the regional compliance authority.

C. **John Anderson.** Mr. Anderson testified about the CIP Compliance Projects at Duke's transmission facilities.

Four of Duke's transmission substations and transmission switchyards are now designated critical assets under the CIP 4 Standards. Duke will enhance the physical and electronic security perimeters at each of the identified facilities. The physical enhancements include badge readers, upgraded door locks, and securing physical openings larger than 96 square inches. The electronic enhancements include installing equipment to form the electronic security perimeter, protecting necessary access ports, and disabling unnecessary access ports. The project will also address malicious software prevention, patching, and account management. In addition, Duke will install security cameras and communication between the security command center and the critical assets. While these projects will help to protect the assets from cyber attacks, they are not intended to extend the useful lives of the facilities.

The estimated capital cost of the CIP 4 Compliance Projects for transmission assets is \$516,350. Mr. Anderson opined that the cost estimates are reasonable, but noted that vendor cost estimates and delays in the project could affect vendor quotes and the final project costs. Duke spent two years assessing the impacts of the CIP 4 Standards, identifying new critical assets, and preparing for compliance. Duke evaluated other alternatives to its proposed plan, including disconnecting or restricting communications to the transmission sites; however, those plans were rejected because they could have a negative impact on the reliability of the bulk electric system. In addition, Duke has reviewed the CIP 5 Standards and determined that all actions taken to comply with the CIP 4 Standards will also be required under the CIP 5 Standards.

D. **Mark Powell.** Mr. Powell testified about the CIP Compliance Projects at one of Duke's generating facilities.

One of Duke's generation facilities is now designated a critical asset under the CIP 4 Standards. Mr. Powell provided confidential testimony regarding the specific actions that will be taken to comply with the CIP 4 Standards. The estimated capital costs of the CIP 4 Compliance Projects for the generation facility is \$300,739 in 2013 and \$79,002 in 2014 of which \$7,500 of the 2014 costs is internal labor O&M, which Duke is not asking to recover. Mr. Powell opined that the costs are reasonable, but noted that vendor cost estimates and delays in the project could affect vendor quotes and final project costs. Duke performed numerous site walks and discussions with operations personnel, engineering support, and compliance staff to identify potential options for compliance. Duke also evaluated alternative compliance plans, and Mr. Powell provided confidential testimony about the alternatives. The alternative proposals were rejected because they were not cost effective. Duke has reviewed the CIP 5 Standards and determined that all actions taken to comply with the CIP 4 standards will also be required under the CIP 5 Standards.

E. **Kent Freeman.** Mr. Freeman testified about the ratemaking and accounting aspects of this filing.

Duke requests authority under Ind. Code § 8-1-8.4-7 to recover 80% of the retail jurisdictional share of the costs of the CIP 4 Compliance Projects, including capital, allowance

for funds used during construction (“AFUDC”), O&M, depreciation, tax, and financing costs, through the FMCA under proposed Rider 72. Duke also requests authority to accrue post-in-service carrying costs at rates equal to the overall cost of capital most recently approved by the Commission. Finally, Duke requests authority under Ind. Code § 8-1-8.4-7 to defer the remaining 20% of the retail jurisdictional share of the costs of the CIP 4 Compliance Projects, including post-in-service carrying costs, O&M, taxes, and depreciation, until its next rate case.

AFUDC will be applied to project costs until those costs are included for CWIP recovery in the FMCA, the costs are included in retail base rates, or the projects are placed into service. Post-In-Service carrying costs will be accrued on federally mandated costs from the in-service date until those costs are included in Duke’s rates under the FMCA or retail base rates. Mr. Freeman said that the proposed accounting treatment accords with U.S. Generally Accepted Accounting Principles and Ind. Code § 8-1-8.4-7.

Duke proposes to recover the CIP 4 Compliance Project costs through the FMCA using the then-current return on common equity (currently 10.5% as approved in 42359 Order). A portion of the CIP 4 Compliance Project costs will be recovered from wholesale customers based on the Separation Study that was approved in the 42359 Order. Duke will allocate the revenue requirement to the rate groups within Rider 72 based on the groups’ respective contribution to the direct combined production and transmission plan original cost depreciated from its last retail base rate case. The costs will be billed to individual customers based on kWh sales except for industrial customers served under Rate HLF, who will be bill based on non-coincident kW demands, similar to Duke’s ECR and IGCC tracker proceedings.

5. OUCC’s Direct Evidence.

A. Ronald Keen. Mr. Keen recommended that the Commission approve Duke’s CIP Compliance Projects subject to the changes and recommendations offered by the OUCC.

The OUCC conducted a thorough examination of Duke’s proposed CIP 4 Compliance Projects. Mr. Keen said he is convinced that the projects comply with the CIP 4 Standards, are prudent and justified, and will help to protect Duke’s infrastructure assets against a wide variety of natural disasters, accidents, and incidents.

The OUCC recommends that the Commission develop a reporting methodology for utilities to update the Commission and the OUCC about their compliance with the CIP requirements. The OUCC believes that a successful reporting methodology must simplify the regulatory process to monitor CIP assets and projects by state agencies, ease regulatory uncertainty about the federal CIP monitoring and reporting process, and impose little or no additional regulatory burdens on the utility.

The OUCC suggests that the parties to this case and the Commission could work together to develop a fully-functional set of reporting requirements that could be used as a template for all jurisdictional utilities engaged in CIP compliance. This would include an annual certification that, to the best of the utility’s ability and with consideration given to its ongoing activities, the

utility is in compliance with all applicable federal and state CIP-Related rules, regulations, and requirements; the utility has accomplished all necessary threat analysis and vulnerability studies; and the utility will answer, with proper safeguards and security, questions about CIP activities and the threat to or vulnerability of its assets. The certification would also include safeguards to the utility from liability and would acknowledge the utility's on-going efforts to remain in compliance.

The OUCC also proposes that the utility file a semi-annual report describing the status of CIP assets undergoing modification due to CIP-related requirements. However, this report should not contain any information that could be deemed valuable to adversarial entities. This report would be included in the utility's semi-annual CIP tracker proceedings. In order to protect sensitive information, the OUCC suggests that assets or facilities be identified with a generic designator, e.g., a, b, c, etc. If concerns arise, the Commission or the OUCC could work with the utility in a properly secured environment to discuss the issues in more detail.

B. Stacie Gruca. Ms. Gruca presented her review, analysis, and recommendations regarding Duke's proposed FMCA. The OUCC does not oppose the proposed FMCA. However, the OUCC does have concerns with Duke's proposed Tariff for Rider 72. The OUCC recommends narrowing the scope of tariff, which refers to the recovery of "costs associated with [Duke's] compliance with federally mandated requirements for electric utilities," to refer specifically to costs associated with a Commission-Approved CPCN under Ind. Code ch. 8-1-8.4.

With respect to the determination of Duke's capital structure for the FMCA, the OUCC agrees with Duke's proposal to use the most current capital structure, which is consistent with Duke's practices in its ECR and IGCC trackers. However, the OUCC disagrees with Duke's proposal to apply the post-in-service weighted average cost of capital to its projects. Rather, the OUCC believes Duke should use the AFUDC rate in calculating post-in-service carrying costs because this is the proper carrying charge rate to apply to post-in-service recovery on completed construction projects until those projects are recovered through the FMCA. Ms. Gruca explained that the AFUDC rate is more appropriately designed for construction projects than WACC, because it includes short-term debt.

Ms. Gruca also said that FASB 71 only allows the debt portion of AFUDC to be recovered in post-in-service accounting. Ms. Gruca said that the Commission may include the equity component of post-in-service AFUDC if it believes that serious financial hardship may occur. However, she said that Duke has provided no evidence or hardship in this case. In summary, Ms. Gruca recommended that the Commission allow Duke to recovery post-in-service carrying costs using the debt portion of the AFUDC rate. In the alternative, Ms. Gruca recommended that the Commission use the lower of the updated WACC rate or the most current AFUDC rate to calculate post-in-service carrying costs.

Ms. Gruca raised the same issue with respect to Duke's proposed treatment of post-in-service carrying costs on the 20% deferred costs. Although Ind. Code § 8-1-8.4-7(c)(2) refers to post-in-service carrying costs based on the overall cost of capital most recently approved by the Commission, Ms. Gruca said that using post-in-service AFUDC follows the Commission's

standard practice for recovery of construction project costs and benefits the utility because the accrual on capital costs reduces interest expense. Ms. Gruca made the same alternative proposal for the 20% deferred costs as that discussed above for the 80% costs recovered through the FMCA. Ms. Gruca also said that the 20% portion of Duke's deferred depreciation, O&M, and property taxes should be deferred without carrying charges. Ms. Gruca argued that Ind. Code § 8-1-8.4-7(c)(2) does not specifically authorize carrying charges to be applied to these types of expenses.

Finally, Ms. Gruca said that the OUCC has no concerns with Duke's proposed estimated O&M costs or depreciation rates. However, Ms. Gruca recommended that Duke be required to work with the OUCC when it files its initial FMCA case to develop a standard audit package similar to that used in other tracker proceedings.

6. Petitioner's Rebuttal Testimony. Mr. Powell responded to Mr. Keen's CIP Compliance reporting recommendation. In general, Mr. Powell said that Duke is willing to work with the OUCC to recommend a reporting framework. He agreed with Mr. Keen's proposal that Duke attest that it is in compliance with all applicable federal and state CIP-related rules, regulations, and requirements, so long as it does not rise to the level of certification detail required to be made to NERC Regional Regulatory Organizations. Mr. Powell also agreed with Mr. Keen's proposal that Duke certify that it has accomplished all necessary threat analysis and vulnerability studies and that Duke personnel should be available to answer questions regarding CIP activities and the vulnerability of assets. Mr. Powell is concerned, however, that additional reporting requirements may be overly burdensome.

Mr. Freeman responded to the issues raised by Ms. Gruca. Mr. Freeman said that Duke does not oppose the OUCC's proposed change to the language of Rider 72 to refer to costs associated with a Commission-Approved CPCN under Ind. Code ch. 8-1-8.4.

With respect to the proper rate to be used in calculating post-in-service carrying costs, Mr. Freeman disagreed with Ms. Gruca's recommendation to use the AFUDC rate. Mr. Freeman noted that Ind. Code § 8-1-8.4-7(c)(2) refers to recovery of post-in-service carrying costs based on the overall cost of capital most recently approved by the commission. The overall weighted cost of capital is also known as the WACC. Although that section addresses the 20% deferred recovery, Mr. Freeman argued that it is reasonable to use the same rate for the corresponding 80% of costs in the FMCA.

Mr. Freeman also disagreed with Ms. Gruca's recommendation to use the debt portion of the AFUDC rate only. He argued that Ind. Code § 8-1-8.4-4(a) includes financing costs in the definition of federally mandated costs and that the post-in-service carrying costs are the financing costs that Duke incurs on project costs that are not yet in rates. It is common practice for a utility to finance its rate base with both debt and equity, and equity return is a financing cost the same as debt cost. Therefore, he argued that Duke should be allowed to recover both debt and equity through AFUDC rates.

With respect to the issue of including carrying charges on deferred depreciation, O&M, and property taxes, Mr. Freeman argued that Ind. Code § 8-1-8.4-7 allows the recovery of on-

going carrying costs on the deferred balance of federally mandated costs, which, by definition, include depreciation, O&M, and property taxes. Mr. Freeman said that Duke will have to acquire capital to carry or finance the 20% deferred amount until that amount is recovered in its next base rate case.

With respect to the development of a standard audit package, Mr. Freeman said that Duke is not opposed to the OUCC's proposal and would commit to meeting with the OUCC prior to Duke's first filing under the FMCA tracker. Duke is also not opposed to number the FMCA cases as proposed by the OUCC, i.e., Cause No. 44367 FMCRA XX, or as assigned by the Commission.

7. Commission Discussion and Findings.

A. CPCN. Before granting a CPCN under Ind. Code ch. 8-1-8.4, we must (1) find that public convenience and necessity will be served by the proposed compliance project, (2) approve the costs associated with the project, and (3) make a finding on each of the factors in Ind. Code § 8-1-8.4-6(b). Those factors are:

- (A) A description of the federally mandated requirements ... that the energy utility seeks to comply with through the proposed compliance project.
- (B) A description of the projected federally mandated costs associated with the proposed compliance project
- (C) A description of how the proposed compliance project allows the energy utility to comply with the federally mandated requirements described by the energy utility under Clause (A).
- (D) Alternative plans that demonstrate that the proposed compliance project is reasonable and necessary.
- (E) Information as to whether the proposed compliance project will extend the useful life of an existing energy utility facility and, if so, the value of that extension.

Ind. Code § 8-1-8.4-6(b).

1. Federally Mandated Requirements. Ind. Code § 8-1-8.4-5 defines a federally mandated requirement to include "a requirement that the commission determines is imposed on an energy utility by the federal government in connection with ... any other law, order, or regulation administered or issued by ... the Federal Energy Regulatory Commission, or the United States Department of Energy." Ind. Code § 8-1-8.4-5. Mr. Rowland and Ms. Jenner testified that the NERC CIP requirements at issue in this proceeding are federally mandated requirements under Ind. Code § 8-1-8.4-5. Mr. Rowland testified that Section 215 of the Federal Power Act requires a FERC certified Electric Reliability Organization ("ERO") to develop mandatory and enforceable Reliability Standards, which are subject to FERC review and approval. Mr. Rowland testified that FERC certified NERC as the ERO to establish and enforce reliability standards for the bulk power system. He testified that once approved, the Reliability Standards may be enforced by the ERO, subject to FERC oversight, or by FERC independently.

FERC approved the CIP 4 Standards on April 19, 2012, in Order No. 761. Based on the evidence presented, we find that the CIP 4 Standards are federally mandated requirements under Ind. Code § 8-1-8.4-5.

2. Projected Costs. Ms. Jenner testified that Duke's total capital cost estimate for the CIP Compliance Projects is \$817,091 of capital in 2013 and \$64,002 of capital in 2014. Ms. Jenner testified that Duke anticipates that annual O&M expenditures in 2014 to be \$15,000. Mr. Anderson testified that for the identified transmission sites the estimate is \$516,350 to comply with the CIP 4 Standards. Petitioner's Exh. C-1 provides a summary of the estimated CIP 4 transmission project compliance costs. Mr. Powell testified the capital costs are estimated to be \$300,739 for 2013 for Duke's generation assets and \$79,002 for 2014, of which \$64,002 is capital, \$7,500 is contract labor O&M, and \$7,500 is internal labor O&M. Petitioner's Exhibit D-1 summarizes the estimated CIP 4 generation project compliance costs. Messrs. Anderson and Powell described the alternative plans that Duke evaluated, the rigor undertaken to compile the estimate, and that they believe these cost estimates are reasonable. Messrs. Anderson and Powell testified that delays in the project could affect the vendor quotes and the final cost estimate of the projects and that Duke will provide updates to the Commission in subsequent filings.

The evidence presented sufficiently describes the projected federally mandated costs associated with the CIP Compliance Project and demonstrates that the estimates are based on multiple sources of information. The evidence also adequately identifies the factors that could cause the cost estimates to change. Based on the evidence presented, we find that Duke's cost estimates for the CIP Compliance Project are reasonable. Therefore we approve the projected federally mandated costs associated with the CIP Compliance Project as required by Ind. Code § 8-1-8.4-7(b)(2). In addition, we find that Duke has satisfied the requirement of Ind. Code § 8-1-8.4-6(b)(1)(B).

3. CIP Compliance Project. Messrs. Rowland, Anderson, and Powell testified that Duke worked with subject-matter experts to assess the impacts, identify the new Critical Assets, and prepare for efforts to meet compliance with the CIP 4 Standards and, in part, the proposed CIP 5 standards. Because the CIP 4 Critical Asset Criteria designates four transmission and one generation facility as critical assets that were not previously designated as critical, Duke will need to implement additional physical and security measures at these sites to comply with the CIP Reliability Standards. Petitioner's Exhs. C-1 and D-1 provide the costs associated with Petitioner's CIP Compliance Projects.

Mr. Keen testified that the OUCC is convinced that the projects comply with the CIP 4 Standards, are prudent and justified, and will help to protect Duke's infrastructure assets against a wide variety of natural disasters, accidents, and incidents.

Based on the evidence presented, we find that Duke's CIP Compliance Project will allow the utility to comply with CIP 4. Therefore, we find that Duke has satisfied the requirements of Ind. Code § 8-1-8.4-6(b)(1)(C).

4. Alternative Plans. Messrs. Powell and Anderson testified that Duke carefully considered all available options for complying with the CIP 4 Standards to develop a CIP Compliance Project that will balance the interest of Duke's customers in

maintaining affordable and reliable electricity along with the need to protect Duke's Critical Assets. In doing so, Duke considered various options, the cost-effectiveness of those options, potential overlap of the CIP 4 and CIP 5 Standards, and the impact on Duke's efforts to comply with the CIP 4 Standards. They both testified that the CIP 4 Compliance Projects will allow Duke to comply with the CIP 4 Standards and that the CIP Compliance Projects will be necessary to comply with CIP 5, but that additional actions would need to be undertaken in order to fully comply with CIP 5, if approved as proposed.

Based on the evidence presented, we find that Duke considered alternative plans for compliance with CIP 4. The evidence shows that the CIP Compliance Project is reasonable and necessary. Therefore, we find that Duke has satisfied the requirements of Ind. Code § 8-1-8.4-6(b)(1)(D).

5. Useful Life of the Facility. Mr. Anderson testified that although the CIP Compliance Projects do not extend the life from an accounting or physical standpoint, they are intended to help protect the assets from cyber-attacks, which could impact the useful life of the facilities.

Based on the evidence presented, we find that Duke has satisfied the requirements of Ind. Code § 8-1-8.4-6(b)(1)(E).

6. Conclusion. The evidence presented demonstrates that the CIP Compliance Project will allow Duke to comply with the requirements of CIP 4. The project will also allow Duke to reasonably ensure its facilities are secure from both physical and cyber threats. As discussed above, we have made a finding on each of the factors described in Ind. Code § 8-1-8.4-6(b) and approved the projected federally mandated costs associated with the CIP Compliance Project. Therefore, we approve the CIP Compliance Project and issue Duke a CPCN for the project under Ind. Code § 8-1-8.4-7(b).

B. Cost Recovery. Ind. Code § 8-1-8.4-7(c) states:

If the commission approves under subsection (b) a proposed compliance project and the projected federally mandated costs associated with the proposed compliance project, the following apply:

(1) Eighty percent (80%) of the approved federally mandated costs shall be recovered by the energy utility through a periodic retail rate adjustment mechanism that allows the timely recovery of the approved federally mandated costs. The commission shall adjust the energy utility's authorized net operating income to reflect any approved earnings for purposes of IC 8-1-2-42(d)(3) and IC 8-1-2-42(g)(3).

(2) Twenty percent (20%) of the approved federally mandated costs, including depreciation, allowance for funds used during construction, and post in service carrying costs, based on the overall cost of capital most recently approved by the commission, shall be deferred and recovered by the energy utility as part of the next general rate case filed by the energy utility with the commission.

(3) Actual costs that exceed the projected federally mandated costs of the approved compliance project by more than twenty-five percent (25%) shall require specific justification by the energy utility and specific approval by the commission before being authorized in the next general rate case filed by the energy utility with the commission.

1. **FMCA.** Duke requests authority to implement a new annual FMCA mechanism to allow the timely recovery of 80% of the federally mandated costs associated with the CIP Compliance Projects. Duke also requests approval of proposed changes to its electric service tariff relating to the proposed FMCA mechanism, including the proposed Rider 72.

Mr. Freeman testified that Duke proposes to update the FMCA on an annual basis. He stated that Duke proposes to use the then current return on common equity approved by the Commission in the most recent general retail rate case. Duke's current return on common equity of 10.5% was approved in the May 18, 2004 Order in Cause No. 42359 ("42359 Order"). Consistent with Duke's other environmental filings (42061 ECR and 43114 IGCC), the return on equity would remain the same but the capital structure would be updated with each filing, along with the debt costs.

Duke proposes that a portion of the federally mandated project costs will be allocated to wholesale customers based on the Separation Study included in Duke's last general retail rate case. He stated that a wholesale percentage will also be determined for any joint owned facilities.

Duke proposes to allocate the revenue requirement developed for the FMCA to rate groups based on their contribution to the direct combined production and transmission plant original cost depreciated from the last retail base rate case. Costs will be billed to individual customers within a rate group based on kWh sales except for industrial customers served under Rate HLF, who will be billed based on non-coincident kW demands. The revenue requirement calculation will be consistent with current ECR filings, except that both the return on investment and expense recovery, including depreciation expense, will be included in one rider. Duke also proposes to increase the allowed net operating income with the incremental net operating income from the FMCA, as provided for in I.C. § 8-1-8.4-7, which is consistent with the ECR and IGCC filings.

Duke proposes to use estimated amounts for O&M, depreciation, and property taxes. The financing costs on invested capital would be on an actual basis based on annual cut-off dates and Duke would true-up both amounts to actual levels. This would be a slight deviation from the ECR and IGCC filings in that Duke does not true-up the return on capital in those filings; however, based on the lower amounts of capital currently projected for this Rider, and ease of administration, it will be easier to true-up all items included in this filing.

Ms. Gruca testified that the OUCC did not oppose the implementation of Duke's proposed FMCA. However, the OUCC recommended narrowing the scope of the tariff language to avoid inclusion of federally mandated costs that have not received Commission approval. Mr.

Freeman agreed to this limitation.

Based on the evidence presented, we find that the proposed FMCA mechanism should allow for the timely and periodic recovery of 80% of Duke's approved federally mandated costs. We also find that the proposed changes to Duke's Rider 72 as revised by the OUCC are reasonable. Finally, we find that Duke's request for approval to adjust its authorized net operating income to reflect an approved earnings associated with the CIP Compliance Project for purposes of Ind. Code §§ 8-1-2-42(d)(3) and 8-1-2-42(g)(3) is consistent with Ind. Code § 8-1-8.4-7(c)(1).

2. Accounting and Ratemaking Treatment. Duke proposes that post-in service carrying costs be accrued on the federally mandated costs, including accrual on previously computed post-in-service carrying cost amounts, from the in-service date until such costs are included in Duke's retail rates under the FMCA or in retail base rates. Duke also proposes that the retail jurisdictional portion of post-in-service O&M, depreciation, and tax expense be deferred as well. He explained that this accounting treatment is in accordance with GAAP.

Mr. Freeman testified that Duke's requested deferred accounting treatment and the action required by the Commission to allow for the requested deferred accounting treatment is provided for in Ind. Code § 8-1-8.4-7 and that such a request is reasonable and appropriate from both a ratemaking and an accounting perspective.

Ms. Gruca testified that the OUCC has concerns with Duke's proposal for calculating post-in-service carrying costs. The OUCC argues Duke should use only the debt portion of the AFUDC rate to calculate post-in-service carrying costs. Mr. Gruca argues that the Commission may include the equity component in the post-in-service AFUDC if it believes serious financial hardship may occur without such relief, but that Duke has made no showing of hardship in this case. Ms. Gruca testified that in the alternative, the OUCC recommends the lower of the updated WACC rate or the most current AFUDC rate.

In rebuttal, Duke argues that although Ind. Code §8-1-8.4-7(c)(1) does not specify the rate that should be used for post-in-service carrying charges on the 80% of the capital expenditures, Ind. Code § 8-1-8.4-7(c)(2) specifies that the post in-service carrying costs on the 20% deferred amount should be based on the overall cost of capital most recently approved by the Commission. Mr. Freeman testified that it is reasonable to use the same rate for the corresponding 80% of the capital costs on which post-in-service carrying costs are accrued.

Mr. Freeman testified that Ind. Code § 8-1-8.4-7 allows recovery of approved capital, O&M, depreciation, tax, and financing costs. He testified that post-in-service carrying costs are the financing costs Duke incurs on project costs from the time the project enters service until the costs are recovered in a new base rate case. Mr. Freeman further testified that it is common practice that a Company finances its rate base with both debt and equity and that Duke should be allowed to recover all financing costs, both debt and equity, whether through AFUDC calculations, return calculations in trackers or base rates, or through post-in-service carrying costs.

Based on the evidence presented, we conclude that the OUCC's proposal that Duke use only the debt portion of its AFUDC rate for post-in-service carrying costs rather than the most recently approved overall cost of capital is not consistent with Ind. Code ch. 8-1-8.4. Although Ind. Code § 8-1-8.4-7(c)(1) does not specify the rate that should be used for post-in-service carrying charges on the 80% of recoverable capital expenditures in the FMCA, Ind. Code § 8-1-8.4(c)(2) requires that post-in-service carrying costs for the 20% deferred amount be based on the overall cost of capital most recently approved by the commission. We find that recovery of the 80% portion of the approved federally mandated costs should be consistent with the recovery of the 20% deferred portion; hence, it is reasonable for Duke to use the overall cost of capital most recently approved by the Commission for the 80% portion. We also authorize Duke to recover both the debt and equity portion of the post-in-service carrying costs for the 80% of the approved federally mandated costs as well as the 20% deferred costs.

3. Deferred Costs. Duke proposes to defer 20% of all federally mandated costs, including, but not limited to, capital costs, O&M expenses, tax and depreciation expenses, and financing costs associated with its CIP Compliance Projects, including expenses incurred prior to receiving a final Order in this Cause, as a regulatory asset for recovery as part of its next general rate case. Duke also requests that carrying costs on the deferred costs be accrued using the overall cost of capital most recently approved by the Commission.

Ms. Gruca testified that the OUCC doesn't have concerns with Duke's estimated O&M costs or proposed depreciation rates, but that the OUCC has the same concern regarding Duke's treatment of the 20% deferred portion as it did regarding the 80% portion. The OUCC argues that post-in-service AFUDC should be calculated net of depreciation based on Duke's most current AFUDC rate, debt portion only, from the time projects are placed in-service until the project costs are recovered in rates. In addition, the OUCC proposes that the 20% deferred depreciation, O&M, and property expenses should be deferred without carrying charges until Duke's next rate case.

Mr. Freeman testified that using the WACC for the carrying costs on the 20% deferral is consistent with what is applied to rate base once the project is in service. He also testified that this treatment is consistent with the proposed calculation of return in the proposed tracker on the 80% of federally mandated projects eligible for recovery. Duke believes the overall cost of capital is the appropriate rate to use for post-in-service carrying costs and carrying charges on the 20% portion of other post-in-service deferred costs. In addition, Duke believes Ind. Code § 8-1-8.4-7 allows for on-going carrying costs on the deferred balance of federally mandated costs, which include depreciation, O&M, and property taxes, until such costs can be recovered as part of the next general rate case.

Ind. Code § 8-1-8.4-7(c)(2) allows Duke to defer 20% of the approved federally mandated costs, including depreciation, AFUDC, and post-in-service carrying costs, based on the overall cost-of-capital most recently approved by the Commission, for recovery in its next general rate case. We find that the evidence presented supports Duke's request to calculate the ongoing carrying charges on deferred depreciation, O&M, and property taxes. The federally mandated cost statute provides for ongoing carrying charges on the deferred federally mandated costs. This statutory policy makes sense because, as the evidence shows, Duke will have to

acquire additional capital on an ongoing basis to carry (and continue carrying) the uncollected 20% deferred balance. Consistent with the statute, Duke would carry those costs at its WACC. If Duke were not permitted to record ongoing carrying charges on the deferred depreciation and O&M expenses, Duke would recover something less than all of the federally-mandated costs, which would be inconsistent with the statute. Therefore, we approve Duke's request to calculate ongoing carrying charges on deferred depreciation, O&M expenses, and property tax.

Duke is authorized to defer 20% of the federally mandated costs incurred in connection with the CIP Compliance Project and Duke may recover the deferred costs in its next general rate case as allowed by Ind. Code § 8-1-8.4-7(c)(2). Duke is authorized to record ongoing carrying charges based on the current overall WACC on all deferred approved federally mandated costs including deferred depreciation, O&M expenses, and property tax, until the costs are included for recovery in its next general rate case.

C. Ongoing Review. The OUCC recommended working with Duke to develop a standard audit package similar to other tracker proceedings and the use of the same Cause No. and extension in subsequent filings to provide consistency. Duke agreed to the OUCC's recommendations.

Based on the evidence presented, we order Duke and OUCC to work together prior to Duke's first filing for cost recovery in the FMCA to develop a standard audit package for ongoing review of the CIP Compliance Project.

D. Reporting Requirements. Mr. Keen proposed state-wide CIP reporting for all utilities. Specifically, he recommended the following three tenets to update the Commission on CIP-related programs and projects to ensure that assets/facilities are not at any level of increased risk and/or vulnerability: (1) simplify the regulatory process dealing with the monitoring of CIP assets and projects by state agencies; (2) ease regulatory uncertainty with regard to the federal CIP monitoring and reporting process; and (3) impose little to no additional regulatory burden on the utilities themselves when factored into normal utility actions relative to CIP compliance activities. Mr. Keen also recommended an annual certification process where the utility attests, to the best of its ability and with consideration given to its ongoing activities, (a) it is in compliance with all applicable federal and state CIP-related rules, regulations, and requirements, (b) it has accomplished all necessary threat analysis and vulnerability studies with regard to its facilities, and (c) that the utility make itself available, under proper safeguards and with security in place, to answer questions regarding CIP activities and the threat to or vulnerability of its assets.

Mr. Powell testified that Duke understands the OUCC's concerns about the vulnerability of the nation's utility infrastructure. Mr. Powell testified that this was not the right proceeding to determine a state-wide CIP reporting plan for all utilities. He stated that, to the extent the Commission decides that it is necessary to have a state-wide CIP reporting plan for all utilities, it needs to be done in a forum where all affected utilities can participate.

Mr. Powell expressed his agreement with the first and third tenets of Mr. Keen's recommended reporting concept and requested clarification to better understand what is meant

by regulatory uncertainty in the second recommended tenet. With regard to Mr. Keen's proposal for a certification process, Mr. Powell agreed for a utility to attest, to the best of the utility's ability and with consideration given to its ongoing activities that it is in compliance with all applicable federal and state CIP-related rules, regulations and requirements. Mr. Powell testified that he would not be supportive of a state-wide certification process at the level of detail similar to the annual self-certification required for the NERC Regional Regulatory Organizations. Mr. Powell agreed with the OUCC's certification proposal that the utility certify that it has accomplished all necessary threat analysis and vulnerability studies with regard to its facilities and that utility personnel be available to answer questions, with appropriate safeguards and security in place, regarding CIP activities and the threat to or vulnerability of the assets.

Finally, Mr. Powell testified that the security of Duke's facilities is very sensitive and should not be disclosed where not allowed by federal laws and regulations. He also expressed Duke's willingness to work with the OUCC going forward to develop a compliance framework, but that in developing a framework, the parties need to be mindful of the current NERC CIP reporting requirements to the Regional Regulatory Organizations.

Based on the evidence presented, we decline to adopt the OUCC's proposed reporting and monitoring concept. The evidence demonstrates that Duke is already subject to a comprehensive monitoring and enforcement program, by FERC, NERC, and ReliabilityFirst Corporation, Duke's regional compliance entity. The OUCC's proposal would create a significant additional burden on Duke. However, we do believe the Commission, the OUCC, and stakeholders should be kept informed of the status of the CIP Compliance Project. The OUCC's certification process, where the utility attests, to the best of its ability and with consideration given to its ongoing activities, (1) it is in compliance with all applicable federal and state CIP-related rules, regulations, and requirements, (2) it has accomplished all necessary threat analysis and vulnerability studies with regard to its facilities, and (3) that the utility make itself available, under proper safeguards and with security in place, to answer questions regarding CIP activities and the threat to or vulnerability of its assets, is an appropriate mechanism to provide this information. Therefore, Duke shall include such a certification in its annual FMCA filings.

E. First FMCA Filing. Duke shall file its first FMCA under Cause No. 44367 FMCA 1.

8. Confidentiality. On August 23, 2013, Petitioner filed a motion for protective order which was supported by affidavit showing documents to be submitted to the Commission contained records or parts of records, the public disclosure of which would have a reasonable likelihood of threatening public safety by exposing vulnerability to terrorist attack and therefore may be excepted from disclosure in accordance with I.C. §§ 5-14-3-4(b)((19)(A) and 8-1-2-29. The Presiding Officers issued a Docket Entry on September 10, 2013 finding such information to be preliminarily confidential, after which such information was submitted under seal. We find that all such information is confidential

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

1. Duke is issued a Certificate of Public Convenience and Necessity for the CIP Compliance Project under Ind. Code ch. 8-1-8.4. This Order constitutes the Certificate.
2. The CIP 4 Standards constitute federally mandated requirements as defined by Ind. Code § 8-1-8.4-5.
3. The CIP Compliance Project constitutes compliance projects as that term is defined in Ind. Code § 8-1-8.4-2, and the costs incurred in connection with the CIP Compliance Project are federally mandated costs as that term is defined in Ind. Code § 8-1-8.4-4. The federally mandated costs are eligible for the ratemaking treatment described in Ind. Code § 8-1-8.4-7.
4. Duke's cost estimates for the CIP Compliance Project set forth above are approved.
5. Duke is authorized to implement its FMCA Mechanism under Ind. Code §§ 8-1-8.4-7 and 8-1-2-42 to effectuate the timely and periodic recovery of 80% of the approved federally mandated costs.
6. Duke's proposed changes to its electric service tariff, Rider 72, as modified by the OUCC are approved.
7. Duke is authorized to recover 80% of the approved federally mandated costs incurred in connection with its CIP Compliance Project through the proposed FMCA Mechanism, including capital, operating and maintenance, depreciation, taxes, financing costs, and post-in-service carrying costs based on its most recently approved overall cost of capital until such costs are recognized for ratemaking purposes through Duke's proposed FMCA Mechanism or otherwise included for recovery in Duke's base rates in its next general rate case.
8. Duke is authorized to utilize construction work in progress ratemaking treatment for the CIP Compliance Project through the proposed FMCA Mechanism.
9. Duke is authorized to accrue AFUDC relating to the CIP Compliance Project until such time as the CIP Compliance Projects are placed into service or receive ratemaking treatment.
10. Duke is authorized to defer the remaining 20% of the approved federally mandated costs incurred in connection with its CIP Compliance Project, including capital, operating and maintenance, depreciation, taxes, financing costs, and post-in-service carrying costs using the most recently approved Company overall cost of capital, and Duke is authorized to recover these deferred costs in its next general base rate proceeding.
11. Duke is authorized to record post-in-service carrying charges based on its current

overall cost of capital on all deferred federally mandated costs, including O&M, taxes, and depreciation expense, until the deferred federally mandated costs are included for recovery in Duke's base rates in its next general rate case.

12. Duke is authorized to defer all tax expenses recorded as a result of the deferral of 20% of all federally mandated costs for recovery in its next general rate case.
13. Duke's request for ongoing review of the CIP Compliance Plan Projects through the FMCA Mechanism is approved.
14. Duke's proposed cost allocation factors are approved.
15. Duke is hereby authorized to adjust its authorized net operating income to reflect any approved earnings associated with the CIP Compliance Project for purposed of Ind. Code §§ 8-1-2-42(d)(3) and 8-1-2-42(g)(3) as allowed under Ind. Code § 8-1-8.4-7(c)(1).
16. In all subsequent FMCA proceedings, Duke shall utilize the following cause numbering system – Cause No. 44367 FMCA xx.
17. Duke and the OUCC shall meet prior to the filing of the first FMCA proceeding to discuss and develop a standard audit package for the FMCA.
18. In all subsequent FMCA proceedings, Duke shall include the certification described above.
19. The information filed by Duke in this Cause pursuant to its motion for protective order is deemed confidential pursuant to Ind. Code §§ 5-14-3-4 and 8-1-2-29, is exempt from public access and disclosure by Indiana law, and shall be held confidential and protected from public access and disclosure by the Commission.
20. This Order shall be effective on and after the date of its approval.

STEPHAN, MAYS, AND WEBER CONCUR; ZIEGNER ABSENT:

APPROVED: JUN 25 2014

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



Shala M. Coe
Acting Secretary to the Commission