STATE OF IOWA

DEPARTMENT OF COMMERCE

UTILITIES BOARD

IN RE: INTERSTATE POWER AND LIGHT COMPANY	DOCKET NO. RPU-2009-0002

FINAL DECISION AND ORDER

(Issued January 19, 2010)

TABLE OF CONTENTS

I. PROCEDURAL HISTORY

On March 17, 2009, Interstate Power and Light Company (IPL) filed with the Utilities Board (Board) proposed electric tariffs, identified as TF-2009-0048 and TF-2009-0049. In TF-2009-0049, IPL proposed a temporary annual increase in its Iowa retail electric revenue of approximately $84 million, or 7 percent over current Iowa retail electric revenue. Pursuant to Iowa Code § 476.6(10), IPL implemented its proposed temporary rates ten days after its March 17, 2009, filing; the rates are subject to refund. In TF-2009-0048, IPL proposed a permanent annual increase in its Iowa retail electric revenue of approximately $171 million, or about 16.6 percent over its current revenues.

The Board docketed IPL's filing as Docket No. RPU-2009-0002 and set a procedural schedule by order issued April 13, 2009. In addition to the Consumer Advocate Division of the Department of Justice (Consumer Advocate), Ag Processing Inc., the Large Energy Group (LEG), and the Iowa Consumers Coalition (ICC) intervened in the proceeding.

The Board held seven consumer comment hearings throughout IPL's service territory. Prefiled testimony was submitted by all intervenors.

In its rebuttal testimony, IPL reduced its request for final rates to approximately $146 million. Consumer Advocate's rebuttal testimony reduced its rate reduction request to about $30 million; its original proposal was for a $50 million reduction. The changes were the result of some issues being agreed to or dropped by the two parties.

Although not part of the rate case filing, the Board on September 9, 2009, approved IPL's fourth-step equalization tariff in Docket No. TF-2009-0143. Originally set to become effective on June 30, 2009, the fourth-step was delayed so that it could be revised to reflect temporary rates in the rate case. The fourth-step was effective September 16, 2009, which coincided with the switch from summer to winter electric rates. Only one equalization step remains for residential and general service classes. Equalization was completed in 2008 for the large general service and lighting classes.

A hearing was held beginning October 5, 2009. Simultaneous initial and reply briefs were filed by the parties.

The primary drivers for IPL's rate case filing include capital costs related to the 2008 floods and transmission costs from ITC Midwest, LLC (ITC Midwest), as well as overall increases in expenses since IPL's last electric rate case, which used a 2003 test year. While IPL is not seeking a management efficiency bonus, management inefficiency became an issue in this proceeding when Consumer Advocate proposed a $50 million reduction to revenues because of IPL's alleged management inefficiency.

II. INTRODUCTION

This is a difficult rate proceeding, not because there are new or novel issues but because it comes during challenging economic times. IPL suffered substantial damage to its infrastructure during the 2007 winter storms and 2008 floods. Many of IPL's customers suffered devastating flood damage that destroyed homes and businesses. Cedar Rapids and other areas are still recovering from the floods' impacts. After the floods, IPL customers experienced the economic downturn that began in the fall of 2008 and continues today, with significant job losses and unemployment rates that have not yet abated. Many of IPL's customers live in rural areas, and most crop and livestock prices have recently been depressed. At the consumer comment hearings, many of IPL's customers told the Board about the impacts of these events on their lives and finances.

In determining the rates of a regulated public utility, regulation does not assure that the utility make a profit, but regulation must give the utility the opportunity to operate successfully. Davenport Water Co., v. Iowa State Commerce Comm'n, 190 N.W.2d 583, 601 (1971), citing Market St. Ry. Co., v. Railroad Commission, 324 U.S. 548, 566-567. In Davenport Water, the Iowa Court at 590 quoted favorably from 43 Am.Jur., Public Utilities and Services, § 186:

> In general, a rate fixed by an authorized rate-making body for a public utility is presumed to be valid and reasonable. Accordingly, the courts will not enjoin or interfere with the collection of rates established under legislative sanction unless they are plainly and palpably unreasonably, confiscatory, or excessive ... .

In Davenport Water, the Iowa Court at 602 cited and quoted a treatise by Nichols, who indicated that "[c]hanges in economic conditions, as indicated in an earlier chapter, must be considered in determining a proper return allowance." Nichols went on to say that when interest rates are low, the cost of capital to a public utility is correspondingly low; when interest rates are high, the cost of capital to a public utility is correspondingly higher.

In setting rates, the Board must balance the interests of the utility and its shareholders and ratepayers. As the Board considers the various issues in this proceeding, it is mindful of the economic consequences of its decisions on IPL's ratepayers. At the same time, IPL must be given an opportunity to operate profitably, and over the long term, the Board believes that both ratepayers and shareholders are best served by a financially healthy utility that is able to invest in its infrastructure and new technology so that customers continue to receive reliable service at a just and reasonable price. Cutting costs on such things as operations and maintenance or capital projects can produce savings in the short term, and can be appropriate responses in difficult economic times, but over the long term the failure to maintain existing facilities and invest in appropriate new facilities can have negative impacts both on the utility and its ratepayers. The Board must consider both the short-term and long-term impacts of its decisions.

The Board gave close consideration to these short and long-term impacts in connection with certain issues where the argument for cost recovery was based more upon policy considerations than strict legal requirements (accelerated retirement of electromechanical meters, for example). The Board’s decision not to allow that proposed adjustment does not mean that the adjustment will never be allowed, but when we balance customer and company interests, the current economic situation tips the balance in favor of denial in the absence of a thorough and compelling case.

It should also be noted that that IPL’s request for recovery of expenses for responding to and restoring service from the 2007 winter storms and 2008 floods was uncontested. Because these expenses are primary drivers for the rate increase in this case, the Board wants to be clear in this Order that it is allowing for recovery of these expenses. Finally, for reference, in several places in the order, the Board refers to IPL’s next rate proceeding. IPL has notified the Board, and the parties, that it will be filing for an electric rate increase in 2010, primarily because IPL’s Whispering Willows 200 MW wind facility came on line at the end of 2009.

III. RATE BASE ISSUE

Cash Working Capital

IPL developed its cash working capital requirements based on a lead lag study that calculated a total 42.5-day lag between the rendering of service and the receipt of payment for service. IPL said that the 42.5-day lag consists of a 15.3-day metering lag, a 2.9-day bill processing lag, and a 24.3-day collection period lag. (Tr. 495). The only part of the total 42.5-day lag that is being challenged is IPL's proposed 24.3-day collection period lag.

Consumer Advocate and ICC both recommend that the collection period be calculated at no more than 20 days. The Board's rules provide that a late payment charge may be imposed if payments are received after 20 days of the date the bill is rendered. 199 IAC 20.4(12). Because IPL can impose a late fee, Consumer Advocate and ICC argue that IPL is fully reimbursed for payments received after 20 days through the late payment charge. (Tr. 1161, 1879). Also, Consumer Advocate claims the collection period lag used was not representative because of the devastating flood that occurred during the 2008 test year, which is the year for which the study was performed. (Tr. 1160-61).

IPL explained that Consumer Advocate's and ICC's recommendation does not take into account that IPL allows a four-day grace period for customer bill payment, which allows for delays in mail delivery and avoids unnecessary customer disputes. (Tr. 470-71). IPL said if it was held to a strict 20-day billing cycle, it would have to increase expenses by $1.6 million to open local offices for walk-in payments. (Tr. 545-46). IPL also pointed out that the Board's rules provide, among other things, that at least one late payment penalty for each electric account be waived annually; IPL said that if its four-day grace period were eliminated, its computer systems would have to be changed to segregate these accounts. 199 IAC 20.4(11)"c"(4) and 199 IAC 20.4(12)"d."

Consumer Advocate noted that IPL's new expense adjustment was unsupported and, if adopted, would have the same revenue impact as if IPL's 24.3-day collection lag time was approved because the expense adjustment would increase IPL's revenue requirement. (Tr. 1166-67). Consumer Advocate argued that the evidence supported a 20-day lag period and that the expense adjustment should be rejected in its entirety. Consumer Advocate maintained that this unsupported expense adjustment is simply a way for IPL to account for its four-day grace period.

The Board will reject IPL's $1.6 million expense adjustment in its entirety. These proposed adjustments were not fully developed by IPL until hearing and was not supported by any studies or cost estimates that could be verified. This leaves the collection lag period as the only remaining issue.

IPL has used the four-day grace period for a number of years. While such a grace period is not mandatory, the Board believes that it does in fact reduce the number of customer complaints that could arise because of mail delivery issues and provides a benefit to customers. In IPL's last litigated electric rate case, Docket No. RPU-02-3, the Board allowed 21.9 days for the collection period lag.

The Board is not persuaded that either IPL’s or Consumer Advocate’s proposal is reasonable. IPL's 24.3-day test year lag period is likely an anomaly because the study was done during 2008, a year when devastating floods impacted much of IPL's service territory and it would be expected that utility payments would lag while customers were dealing with flood impacts. On the other hand, Consumer Advocate's and ICC's 20-day proposal is not supported by a lead lag study and does not take IPL's four-day grace period into account.

Based on the evidence presented in this case, the Board will use the 21.9-day collection period from IPL's last litigated electric case. IPL's four-day grace period was in effect and the test year for that study did not include a significant weather event like the 2008 flood.

The Board does have some concerns about the methodology used in IPL’s study. In determining the appropriate collection lag period, the Board questions whether the study should include those customers who are late in payment but ultimately pay (including late fees) since IPL would be compensated by the late fees.

In IPL's next study, IPL will be required to break down the percentage of customers that pay and the percentage of revenue that is collected within 20 days, within 21-24 days, and after 24 days. IPL should also offer additional testimony on its preferred methodology and why it views that methodology to be correct.

IV. INCOME STATEMENT ISSUES

Salaries and Wages

There is only one disputed issue with respect to various salary and wage adjustments proposed by IPL and accepted (or not objected to) by the other parties. Consumer Advocate recommended the exclusion of $1,280,761 related to IPL's enhanced 401(k) matching plan for its employees. (Tr. 434, 1126-28, 1147). Consumer Advocate maintained that this amount is above and beyond the contribution made by IPL to the plan for the 2008 test year and that because of workforce reductions and announced 401(k) cuts for 2009, this amount will not be contributed to employee plans in 2009. Consumer Advocate said that in response to various data requests IPL identified no enhanced 401(k) contributions in 2009. ICC supported Consumer Advocate's adjustment.

IPL said that it was responsible for confusion over this issue. IPL said it has referred to two contributions with respect to its 401(k) plan; the 401(k) match and the enhanced 401(k) plan. IPL said that while it has only one 401(k) plan for employees, two types of contributions are made. The first is a cash contribution that is made by IPL regardless of any employee contribution and is in lieu of a 5 percent benefit credit previously made to IPL's cash balance pension plan. This contribution has been labeled by IPL as the enhanced 401(k) plan and contributions began in August 2008. (Tr. 346). IPL said contributions have been made continuously since that date.

The second type of contribution from IPL to employees' 401(k) plans is a matching of employees' contributions by IPL. IPL suspended its matching contributions in June 2009. These contributions are referred to by IPL as the 401(k) match.

IPL said the $1,280,761 amount that Consumer Advocate seeks to exclude represents enhanced 401(k) contributions, which began in 2008 and continued throughout 2009. IPL noted that an adjustment has already been made to salaries and wages reflecting the suspension of the matching 401(k) contributions in 2009.

IPL acknowledged that it did not refine its enhanced 401(k) contributions adjustment to reflect the impacts of IPL's workforce reduction. IPL said this would reduce the enhanced 401(k) contributions by $45,058. (Tr. 1149-50).

The terminology used did cause confusion and initially made it appear that IPL had two 401(k) plans for its employees, rather than one plan with two types of contributions. The evidence demonstrates that IPL made the enhanced 401(k) contributions beginning in 2008 and continuing throughout 2009. (Tr. 345, 1146). The $1,280,761 in contributions initially requested by IPL must be reduced by $45,058 to reflect the impacts of IPL's workforce reduction. The total allowed for enhanced 401(k) contributions will be $1,235,703.

Pension Expense

The dispute between IPL and Consumer Advocate regarding pension relates to the method for determining a representative amount to include in IPL's rates. IPL initially based its 2009 pension cost estimate upon an actuarial study performed by Tower Perrin. (Tr. 436). Using the results of this study would result in a significant increase to pension expense due to the impacts of the economic recession and reduction is stock market values. Because of the rate impact if the study were used, IPL said it might be more appropriate to use a five-year inflation-adjusted average. Consumer Advocate proposed using a two-year average of 2008 and 2009 costs.

The dispute is whether to use IPL's five-year inflation-adjusted average or Consumer Advocate's two-year average. Consumer Advocate argued that a five-year average was inappropriate here because it included years for nuclear plant employees and transmission employees that no longer work for IPL because of IPL's sales of its nuclear plant and transmission system. Consumer Advocate pointed out that IPL made no adjustment for those employees leaving IPL due to the asset sales. (Tr. 503-04, 557-59).

The Board would not have used IPL's study as a basis for determining a representative amount to include for pension expense because the Board is not persuaded that the drop in pension value is permanent, as IPL's original adjustment assumed, and IPL appeared to recognize this when it proposed using a five-year inflation-adjusted average. While the Board in most cases might prefer a five-year average to a two-year average for pension expense because a longer average moderates anomalies for any one year, use of the two-year average is more appropriate here because it excludes employees who no longer work for IPL due to asset sales. No adjustments were made to IPL's five-year average to account for the loss of these employees after the asset sales. Also, while IPL's witness advocated a five-year inflation-adjusted average at hearing, he agreed that Consumer Advocate's two-year average produces reasonable results in this case. (Tr. 437). The Board will use the two-year average here because it produces a representative amount to include in IPL's electric rates, but understands that arguments may be presented in future cases to use something longer than a two-year average as more data becomes available that is subsequent to the asset sales and therefore excludes those employees no longer working for IPL.

Other Post-Employment Benefit (OPEB) Costs

The dispute and arguments in support of the respective positions are the same as for pension costs. IPL proposed a five-year inflation adjusted average for OPEB costs and Consumer Advocate argued for a two-year average.

The Board acknowledges that a five-year average reduces the variability of the average and might be appropriate for adjustments in other cases. However, a five-year average is not appropriate here because the two-year average excludes former IPL employees impacted by asset sales. IPL's five-year average did not adjust for these employees. Again, IPL's witness acknowledged that the two-year average produced reasonable results in this proceeding. (Tr. 437).

The Board notes that IPL agreed with a corresponding adjustment Consumer Advocate made to IPL's rate base for the 13-month average of OPEB related funds to be deposited in a Board approved external trust account as required by 199 IAC 16.9(1). (Tr. 433). These early collections represent customer contributed capital and are an offset to IPL's rate base. (Tr. 1177-79). This adjustment will be reflected in the final rate base determination.

Variable Pay Plan (VPP)

IPL said the purpose of its VPP was to attract and retain a skilled workforce and that the VPP is triggered when both Alliant Energy, IPL's parent company, and the employee perform at an appropriate level. Because the VPP triggers at various amounts (and some years not at all), IPL based its VPP amount on a five-year inflation-adjusted average in order to levelize fluctuations. (Tr. 441-43).

Consumer Advocate objected to including any amount for IPL's VPP because it is speculative and not known and measureable. Consumer Advocate pointed out that IPL's witness testified there would likely be no VPP awards in 2009 and no awards were included in future budgets. Consumer Advocate noted the evidence at hearing demonstrated that the earnings per share threshold that would trigger a VPP award would not be met in 2009. (Tr. 501, 547).

ICC argued that no amount should be included for IPL's VPP because no awards were made in the 2008 test year. ICC maintained that IPL's customers should not pay a cost for a benefit they did not receive and any future VPP payments are speculative.

The Board agrees that VPPs are important to attract talented people, but ratepayers should not pay for these plans in today's economic circumstances and when no payments are made because the payment thresholds are not met. In Docket Nos. RPU-02-3 and RPU-02-7, the Board did not include in rates any amounts for VPP payments because while payments were made in the 2001 test year, no payments were made in 2002 (the year the rate cases were heard) and it was uncertain when future payments would be made. Consistent with this prior Board precedent, the Board will not include any amount in electric rates for VPP payments.

The case for disallowing any amount for VPP payments in rates is stronger here than in the prior dockets. The evidence established not only that no payment was made in the 2008 test year but also that no payment would be made in 2009 because the earnings per share threshold could not be met. In addition, it is speculative as to whether the threshold for a VPP payment will be met in 2010. Given the lack of recent VPP payments and the uncertainty over future payments, ratepayers should not pay for an expense that has not produced recent benefits. The issue can be revisited in a future rate filing if payments are once again made pursuant to the plan.

Accelerated Depreciation Rate for Existing Electric Meters

IPL proposed to accelerate the depreciable life of its existing electric meters from 23 years to 10 years because it anticipates installing advanced metering infrastructure (AMI) in the future. IPL said while it was not making a specific proposal to install AMI/Smart Grid, the benefits are well known. IPL did commit at hearing to installing AMI within three years if federal stimulus money was received (which it was not) or ten years without the funding, assuming its accelerated depreciation proposal was approved. (Tr. 262-63). IPL viewed acceleration of depreciable life as a first step towards AMI deployment. (Tr. 241-42).

Consumer Advocate noted that initially IPL said it had not made a decision whether to proceed with meter replacement, and that the three and ten year commitments were only made at hearing. (Tr. 240-43, 262-63). Consumer Advocate argued that IPL should not accelerate depreciation until it demonstrates that AMI deployment is beneficial to customers and AMI is actually deployed. (Tr. 1106-07). While IPL provided some hypothetical and speculative benefits of AMI in its rebuttal testimony, Consumer Advocate said that IPL was unable to quantify any actual benefits to its customers. (Tr. 248-54, 310-20).

ICC, LEG, and Ag Processing also objected to IPL's accelerated depreciation proposal. ICC pointed out that IPL relied, at least in part, on Section 1307 of the Energy Independence and Security Act of 2007 (EISA), which provides a new Public Utility Regulatory Policies Act of 1978 (PURPA) standard for consideration of Smart Grid investments, including obsolete equipment. ICC pointed out that AMI is far from a Smart Grid system envisioned by EISA, particularly because IPL has not spelled out what it means by AMI. In addition, both ICC and LEG objected to IPL's proposal because there are no definitive plans for AMI deployment and the general cost information submitted by IPL fails to show that AMI would be cost-beneficial to IPL's customers. (Tr. 1398-99).

The Board wants to do what it can to encourage utilities to invest in cost-effective AMI and Smart Grid technology. In fact, the Board’s support of deployment of new technology has been demonstrated in prior proceedings. For example, the Board has shortened depreciation periods in prior telephone cases to reflect the planned installation of new technology to replace old technology that was still in use but functionally obsolete. In this situation, all parties agree that AMI brings benefits to electric utilities' systems and that utilities should consider investing in AMI and Smart Grid technology, but the problem here is that IPL has not made a specific proposal and has not provided specific studies on the benefits of AMI projects to IPL customers. IPL did not come up with its three and ten-year proposals until hearing, indicating to the Board that IPL's AMI plans have not been fully vetted in the company. EISA, cited by some of the parties, focuses on obsolete equipment, but because IPL has not formulated a specific plan, no information is available on what equipment is or will be obsolete and will be replaced with new technology.

The Board does not believe that AMI or Smart Grid installation must begin before accelerated depreciation can be awarded or that a definitive cost study must be provided, but certainly a utility must present more than a general idea with no study support. For example, Wisconsin Power and Light Company (WPL), Alliant Energy’s affiliate in Wisconsin, presented specific plans and studies for the commission there to evaluate before the commission approved a proposal to reduce the depreciation schedule for existing meters to 15 years. (Tr. 241-42). Here, IPL asked for a more dramatic reduction to 10 years without the level of study or support presented in Wisconsin.

Ratepayers should not be asked to begin the process of paying for AMI or Smart Grid deployment on a large scale until the utility can present evidence showing that deployment of the new technology will bring ratepayers benefits, especially in these economic times. The Board is also concerned that IPL's plan was extremely vague in its initial filing, with no commitment on a time frame for making a decision on whether such technology is cost effective today and therefore the project should proceed. Based on the lack of support for the adjustment provided by IPL, which did not even include an updated depreciation study for existing meters, the proposal to accelerate depreciation of existing electric meters will be denied in this proceeding, but the Board encourages IPL to re-file its proposal when it has additional support.

Recovery of Sutherland Generating Station Unit 4 (SGS Unit 4) Cancellation Costs

IPL initially sought to recover $42.6 million in cancellation costs related to SGS Unit 4, a proposed coal-fired generating facility. After questions were raised by Consumer Advocate and ICC, IPL revised its request by removing costs related to land purchases and costs that might be assigned to IPL's partners in the plant; IPL now seeks recovery of $26,549,298, amortized over five years.

SGS Unit 4 has been the subject of two prior Board proceedings, a generation siting proceeding and a ratemaking principles proceeding. On August 25, 2008, the Board issued its final decision granting a generating certificate, with conditions, to

SGS Unit 4 in Docket No. GCU-07-1. On February 13, 2009, the Board awarded advance ratemaking principles to IPL for SGS Unit 4 in Docket No. RPU-08-1 pursuant to Iowa Code § 476.53. One of the ratemaking principles involved canceled costs, and provided as follows:

> If IPL cancels construction of the proposed SGS Unit 4 for good cause, IPL's prudently incurred costs shall be amortized over a period of no more than five years no later than six months after the cancellation. The annual amortization shall be included in the calculation of IPL's revenue requirement, but the unamortized balance shall not be included in rate base in any determination of interim and final rates thereafter during the period of amortization, provided however, that the prudence of the costs and the good cause for cancellation may be disputed by any party and shall be subject to determination by the Board.

On March 13, 2009, IPL filed with the Board a notice that SGS Unit 4 would not be built. IPL said it based this decision on several factors including, cost, the economic and financial climate, increasing environmental concerns and risks associated with the Board's approved ratemaking principles. In this proceeding, IPL is seeking to recover cancellation costs over a five-year amortization period, and is further proposing to offset the cancellation costs by using proceeds from the sale of Duane Arnold Energy Center (DAEC) that are in a regulatory liability account. IPL said its two-part proposal would remove the impact of the cancellation costs from customer rates because there are sufficient funds from the DAEC sale to cover cancellation costs. It is important to note that IPL is only seeking recovery of the cancellation costs; the unamortized balance will not be included in rate base and therefore IPL will not earn a return on the unamortized balance.

Consumer Advocate opposed recovery of any of the costs associated with the canceled plant, but as an alternative said that no more than 50 percent of the costs should be charged to ratepayers. If the Board decided that some or all of cancellation costs should be recovered, Consumer Advocate did not oppose use of the DAEC proceeds. ICC said that only the costs of SGS Unit 4 associated with the portion of the project expected to serve Iowa retail load should be recovered from ratepayers.

There is a back and forth discussion between IPL and Consumer Advocate in post-hearing briefs as to whether the advance ratemaking principle awarded by the Board with respect to cancellation costs is applicable because IPL never accepted the ratemaking principles in their entirety. Based on Consumer Advocate's reasoning, cancellation costs pursuant to the principle could only be recovered if IPL had initially accepted the ratemaking principles but later canceled SGS Unit 4 for good cause.

This is not an issue the Board needs to decide here. Regardless of whether the ratemaking principle or general law is applied, the standard for recovery of cancellation costs is the same — the cancellation must be for good cause and the costs must have been prudently incurred. <u>See</u>, <u>Office of Consumer Advocate v. Iowa Utilities Board</u>, 454 N.W.2d 883 (1990).

In support of its decision to cancel SGS Unit 4, IPL cited, among other things, discussions with its contractors indicating that SGS Unit 4 could not be built for the approved cost cap and uncertainty relating to carbon emissions at the federal level.

IPL concluded that there was too much financial and regulatory uncertainty to proceed with the plant. IPL said there was good cause for its decision to cancel the plant and that the costs incurred were prudently incurred. IPL argued that disallowing cancellation costs would add additional risk to any future generation proposals. In response to Consumer Advocate's proposal to assign half of the costs to ratepayers and half to shareholders, IPL noted that by not seeking recovery of carrying costs through rate base, shareholders are covering some of the costs associated with cancellation of SGS Unit 4.

Consumer Advocate maintained that good cause did not exist to cancel SGS Unit 4 because it was largely canceled due to IPL's dissatisfaction with the ratemaking principles awarded by the Board. Consumer Advocate said that IPL's cancellation was not prompted by any new load projections showing that the plant was no longer needed or that costs had increased to a point that the plant was no longer justified.

Consumer Advocate also made the argument that SGS Unit 4 was not actually cancelled, because actual construction hadn’t begun before it was terminated and therefore there was nothing to cancel. The Board considered this a meaningless distinction. The planning and regulatory approval stages are necessary parts of the construction process and ground does not need to be broken before the project is considered to have started. The arguments appear to come down to whether there was good cause to cancel SGS Unit 4. No arguments were presented by Consumer Advocate or any other party that the costs generally or specific costs were not prudently incurred, other than with respect to land costs and partner costs, which IPL removed from its final request.

None of the parties presented any evidence to support an argument that IPL's real reasons for cancelling SGS Unit 4 were different from their stated reasons, or that those stated reasons did not constitute reasonable grounds to cancel SGS Unit 4. Without revisiting the ratemaking principles proceeding to rehash the merits of the principles awarded (or not awarded) by the Board, there are changes that occurred that the Board will find constitutes good cause for canceling the plant. The federal elections in November 2008 resulted in a belief by many that federal carbon constraints, either in the form of new statutes or regulations, would come sooner, rather than later; the costs of any carbon constraints were unknown. The environmental uncertainty combined with the economic downturn and fluctuation in costs for items such as steel and concrete, which increased rapidly in the spring and summer of 2008 and then fell with the economic downturn, combined to create cost uncertainty for the costs of construction and for ongoing environmental compliance.

The Board does not want to discourage utilities from forward-thinking with respect to generation options, and significant costs, such as engineering costs, must often be incurred to explore those options. IPL was justified in expending the initial sums towards SGS Unit 4 and justified in stopping those expenditures when it concluded the economic and regulatory environment with respect to carbon changed significantly. There is no evidence to suggest that the costs incurred were imprudent, so recovery will be allowed, amortized over five years. Because of the difficult economic factors facing IPL's customers, IPL will be allowed to fund the amortization with the DAEC regulatory liability account so there will be no rate impact from recovery of these costs. This account was initially designed to offset allowance for funds used during construction with respect to new generation, and while the Board would prefer to continue using the account for new generation, using some of the funds for canceled plant costs is generally consistent with the intent of the account. However, in better economic times, the Board might not have allowed the DAEC fund to be used for an offset.

The Board notes that while IPL ultimately excluded from its request in this proceeding costs allocated to its DAEC partners, IPL said that it might seek recovery in a future proceeding if the costs could not be recovered from the partners. While that is an issue that cannot be decided here, on the surface the Board is skeptical that it would allow recovery from IPL's ratepayers of costs allocated to partners if the partners refuse to pay; that appears to be a risk that is more appropriately shouldered by IPL's shareholders.

Interest Synchronization

The interest synchronization adjustment is an adjustment to federal and state income taxes to match the tax-deductible interest included in the revenue requirement. The method of calculating this adjustment is not in dispute and the final interest synchronization adjustment will reflect the debt interest expense included in the revenue requirement as a portion of the overall return on rate base. The differences in the calculations among the parties are based on their various proposals for weighted cost of debt and size of IPL's rate base. Once the Board determines these issues, the adjustment for interest synchronization can be determined and reflected in the schedules attached to this order.

Workforce Reduction

IPL said that in May 2009, Alliant Energy instituted a workforce reduction in order to deal with sales reductions and create greater efficiencies. Given current economic conditions, IPL assumed this workforce reduction would be long-term and incorporated it as an ongoing adjustment. (Tr. 435). One adjustment specifically related to the workforce reduction, severance costs, remains in dispute.

IPL proposed to recover $3.3 million of severance costs amortized over four years. (Tr. 434-36). Consumer Advocate maintained that IPL's severance costs were offset by other limited time cost savings the company exercised in 2009, such as IPL's one-week company-wide furlough and suspension of matching 401(k) contributions. IPL said that these offsets were temporary cost savings measures that would not continue indefinitely and using temporary cost savings measures to offset costs related to a long-term employee reduction is illogical and punishes IPL for taking prudent long and short term cost-cutting actions that benefit customers.

At hearing, the evidence demonstrated that the savings resulting from IPL's suspension of matching 401(k) contributions and the savings from the one-week furloughs was approximately $2.4 million. (Tr. 1132-34). Consumer Advocate would amortize the $900,000 difference between IPL's severance costs ($3.3 million) and cost savings ($2.4 million) over four years. IPL continued to maintain it was inappropriate to offset costs associated with long-term savings with temporary, one-time savings.

While IPL and Consumer Advocate treated the two adjustments as interrelated, they are separate adjustments and the Board will address and treat them separately. First, with respect to severance costs, IPL appears to have made some difficult decisions regarding its work force and the one-time severance costs associated with those decisions should be recovered over four years; IPL's ratepayers benefit from any long-term work force reduction by the continuing cost savings that are reflected in salaries and wages, although IPL made no specific commitment as to how many of the reductions were permanent.

The second adjustment relates to the 401(k) savings and furloughs. Customers should benefit from the short-term cost savings measures taken by IPL, particularly when they are asked to bear the one-time costs associated with the long-term workforce reduction savings. The Board will amortize the one-year cost savings identified by Consumer Advocate over a four-year period. Allowing both IPL's and Consumer Advocate's adjustments balances the interests of ratepayers and shareholders, because shareholders also should receive some of the benefits from the workforce reduction in the form of higher earnings.

Management Efficiency

Introduction

Consumer Advocate proposed a $50 million reduction to IPL's revenue requirement for what it said were IPL's poor management decisions, focusing on the sale of DAEC and IPL's electric transmission system, as well as a comparison of IPL's rates with that of Iowa's other investor-owned electric utility, MidAmerican Energy Company (MidAmerican), and an examination of the unregulated activities of Alliant Energy. The proposed $50 million reduction is equivalent to an approximate 380 basis point reduction to IPL's ROE. ICC argued for a management efficiency penalty of 30 basis points, which would translate to an approximate $3.7 million reduction to IPL's revenue requirement. IPL opposed any management efficiency penalty.

Iowa Code § 476.52 deals with management efficiency. The statute provides:

> 1. That it is the policy of the state that a public utility shall operate in an efficient manner.
>
> 2. In a rate case proceeding, if the Board determines that a utility is operating in an inefficient manner, or is not exercising ordinary, prudent management, or in comparison with other utilities in the state the utility is performing in a less beneficial manner than other utilities, the Board may reduce the level of profit or adjust the revenue requirement of the utility to provide incentives to the utility to correct its inefficient operation.
>
> 3. In a rate case proceeding, if the Board determines that a utility is operating in such an extraordinarily efficient manner that tangible financial benefits result to the ratepayer, the Board may increase the level of profit or adjust the revenue requirement for the utility. Energy efficiency programs may be considered.
>
> 4. The statute also provides that the Board shall adopt rules for determining the level of profit or the revenue requirement adjustment that would be appropriate and also that the Board shall adopt rules establishing a methodology for an analysis of a utility's management efficiency.

When rules were initially adopted regarding management efficiency in the mid-1980s, much of the focus was on annual management efficiency reports that the utilities were required to file. The reports were designed to provide a basis for utility-to-utility comparisons. However, prior Boards found that comparisons to other utilities in the state were of limited value because of differences in service territories, customer mix, weather patterns and disasters, and other factors. The current management efficiency rules (last revised in 1997) provide that "[t]he efficiency or inefficiency of a utility will be evaluated on a case-by-case basis, based upon the utility's particular facts and circumstances," as well as noting that management efficiency does not lend itself to an absolute measure. 199 IAC 29.3(1). In evaluating management efficiency, 199 IAC 29.3(1) lists several factors the Board <u>may</u> consider, including price per unit of service, operation and maintenance costs per unit of service, quality of service, executive compensation, fuel costs, utility-wide load factors, innovative ideas implemented by management, and bad debt ratio. For electric utilities, 199 IAC 29.3(2)”d” lists development and implementation of energy efficiency programs as an additional factor the Board may consider. Much of this information used to be required in the annual management efficiency reports; the current rule provides that the Board can request that information at its discretion. In the order adopting the 1997 revisions and rescinding the annual report requirement, the Board said:

> The Board intends to continue closely scrutinizing management efficiency. The adopted amendments are simply recognition that the management efficiency reports are not, in many cases, a useful tool to determine

> management efficiency or inefficiency. Also, much of the information contained in these reports is duplicated in other regulatory filings. The Board's limited resources can be better applied in other areas and in focusing on a particular utility's unique attributes which, judging from prior cases, are a better determinant of management efficiency. In re: Management Efficiency, "Order Adopting Rules," Docket No. RMU-97-2 (10/17/1997).

In determining whether a utility is run well or poorly, the Board is not limited to test year data. 199 IAC 29.4. The rule provides for an upward adjustment to return on equity for an exceptionally managed utility, and a downward adjustment to return on equity for a poorly managed utility. Finally, the rule provides that the Board will not establish any reward or penalty if the utility has been managed satisfactorily but not exceptionally well or poorly, because satisfactory management is expected from all public utilities.

State commissions, including Iowa, have addressed management efficiency issues and imposed penalties for inefficient management. Some jurisdictions have a specific management efficiency statute (like Iowa) and others address management efficiency issues under the just and reasonable rates standard. In the cases reviewed by the Board, rate comparisons between utilities played little, if any, role in management efficiency decisions; most of the various commissions' decisions appear to be directed at specific decisions management has made.

The Board imposed a 1 percent reduction (100 basis points) in Great River Gas Company's (Great River) ROE, which resulted in a reduction in rate base of about $20,000, in an order issued on April 3, 1986, in Docket No. RPU-85-16. The Board was critical of Great River for signing a 20-year supply contract where Great

River agreed to pay demand charges for that period of time with no exit clause for changing conditions. The Board was generally critical of Great River's supply planning because while it planned for growth it expected the Board to protect it from losses. The Board did not disallow the costs of the contract, however, because the contract was not imprudent when entered into—the criticism was directed at Great River's supply planning in general and the lack of an escape clause in the contract. Rate comparisons between utilities were not an issue.

Another example is the Board's imposition of a 1 percent reduction (100 basis points) on Iowa Gas Company's (Iowa Gas) ROE, which translated to a reduction in rate base of about $250,000, in an order issued June 27, 1986, in Docket No. RPU-85-22. Here, the Board compared Iowa Gas to other gas utilities in Iowa and found the company deficient, particularly with respect to the quality of its service because of the large number of complaints regarding reading meters and lack of responsiveness to customers. However, rate comparisons did not play a role in the penalty.

Among decisions from other jurisdictions, one in Vermont imposed a substantial penalty. The Vermont Supreme Court upheld the Vermont commission's 525 basis point reduction in return on equity for a Vermont utility in Citizens Utilities Company, 769 A.2d 19 (2000). The Court noted the record was replete with examples of inadequate and misleading accounting practices that obscured the true nature of the utility's expenditures and activities, failure to comply with demand-side management obligations, failure to implement least-cost planning for transmission and distribution facilities, failure to obtain necessary Board approval prior to converting distribution lines to transmission lines, and resisting the Commission's efforts to obtain information about the utility's activities. The Court noted the return on equity reduction was not to penalize the company for certain conduct, but rather to set reasonable rates in cases where the consumers are not being adequately served due to inefficiency or improvidence or other like reasons. The Court rejected constitutional arguments that the rate of return reduction was confiscatory. Vermont did not have a management efficiency statute like Iowa's but had the just and reasonable rate standard in its statute. Once again, rate comparisons were not an issue.

Closer to Iowa, the North Dakota commission in Otter Tail Power Company, 53 PUR 4th 296, 310 (1983) reduced Otter Tail's return on equity by 1 percent (100 basis points) where the utility was found deficient in controlling its rates (a large wage increase was cited). Also, the Commission cited a decline in capital costs and the inflation rate from the time of the rate application to the time of the Commission's order as supporting the reduction. This was done under the just and reasonable rate standard and not a specific management efficiency statute. No rate comparisons were made.

The Board will now examine the positions of the parties that presented testimony on this issue, and then discuss the Board's findings and conclusions with respect to whether a management efficiency penalty should be imposed. Because Consumer Advocate and ICC proposed the penalty, the Board will summarize their positions first.

Consumer Advocate Position

Consumer Advocate recommendation that IPL be penalized $50 million is to reflect the fact that IPL is performing at a level that is less beneficial to its ratepayers than other Iowa utilities are performing with respect to their ratepayers and to provide an incentive for IPL to improve its inefficiencies. In developing its recommendation, Consumer Advocate first compared the retail prices of IPL to those of MidAmerican. During 2008, Consumer Advocate found that IPL customers paid over $248 million more than MidAmerican customers for the same electric service. Over the past five years, Consumer Advocate noted that this difference exceeded $1 billion. (Tr. 1002). Over this time period, Consumer Advocate maintained that IPL saw average usage for large customers reduced by 14 percent while MidAmerican realized average usage increases of 12 percent for large customers over the same time period. In addition, Consumer Advocate said the number of large customers at IPL grew by 9.1 percent compared to 21.6 percent for MidAmerican.

During this same timeframe, Consumer Advocate pointed out that MidAmerican added 2,255 MW of capacity with a total cost of over $3 billion, without raising prices. During this same period, Consumer Advocate noted that IPL added the Emery Generating Station at a cost of $402 million, while liquidating both DAEC and the IPL transmission system, and is before the Board for a substantial rate increase.

Consumer Advocate also compared Alliant Energy's unregulated activities to those of MidAmerican. Consumer Advocate argued that while MidAmerican focused on its core utility operations, Alliant Energy/IPL focused on its unregulated business, thereby diverting management focus from IPL. Consumer Advocate maintained that Alliant Energy's 2000 strategic plan was focused on large earnings from its unregulated businesses, and that by 2004, Alliant Energy had invested over $700 million in foreign markets. Consumer Advocate said that combined with the dramatic loss in the value of IPL's McLeodUSA stock in 2001, Alliant Energy made the decision to reduce its dividend. Consumer Advocate contended that the non-regulated activities by Alliant Energy reduced the focus put on IPL by upper management.

Another factor cited by Consumer Advocate as supporting a management efficiency penalty was the sale of DAEC. Consumer Advocate argued that the sale of DAEC allowed Alliant Energy the opportunity to repurchase shares and also the ability to "trade in" depreciated assets earning low returns for new assets receiving inflated returns resulting from Iowa Code § 476.53, the ratemaking principles statute. (Tr. 1010-13). By repurchasing shares, Consumer Advocate said that IPL's earnings per share would increase, potentially leading to higher incentive compensation payments to management.

Consumer Advocate said that as a result of the DAEC sale, IPL customers are paying approximately $13 million/year for decommissioning costs that the purchaser of DAEC is not paying. Consumer Advocate stated that if IPL had decided to relicense the plant, those benefits would have gone to IPL's customers. Consumer Advocate also noted that the DAEC purchase power agreement was structured to mirror the costs of IPL retaining ownership of DAEC until decommissioning in 2014, which could have resulted in IPL paying a higher rate than otherwise might have been negotiated. Finally, Consumer Advocate pointed out that IPL's sale of DAEC removed the protection of the carbon-free generation that DAEC provides. Consumer Advocate believed generation like DAEC will only become more valuable once carbon legislation is enacted. (Tr. 1014-15).

Another factor Consumer Advocate cited as supporting its proposed management efficiency penalty is the sale of IPL's transmission system. Consumer Advocate said that while the sale included an Alternative Transaction Adjustment (ATA) designed to offset cost increases for eight years, the evidence is clear that the added costs resulting from the sale to ITC Midwest far exceed the offset coming from the ATA.

Two final factors cited by Consumer Advocate with respect to management efficiency are wind development and fuel cost variances. Both involved comparisons of IPL with MidAmerican. In wind development, Consumer Advocate faulted IPL for not being proactive in developing wind generation, noting that MidAmerican began installing wind in 2004 at a cost of $1,143/MW and now has an overall average cost of $1,721/MW. In comparison, Consumer Advocate said that IPL's Whispering Willows project will cost about $2,125/MW, significantly higher than if IPL had built the plant earlier. Consumer Advocate calculated that if IPL had installed wind generation at the same time as MidAmerican, IPL could have avoided $94 million in purchased power costs. (Tr. 1021).

Regarding fuel costs, Consumer Advocate pointed out that MidAmerican has significantly lower fuel costs than IPL, partly due to the low fuel costs at MidAmerican's Quad City Nuclear Station. Also, Consumer Advocate noted that MidAmerican has a much greater incentive to keep fuel costs low, since it does not have an Energy Adjustment Clause (EAC), and that IPL's failure to outline any efforts to reduce fuel costs indicates that it is content to pass the costs of fuel to its customers via the EAC.

Consumer Advocate said that its proposed reduction to IPL's revenue requirement of $50 million from IPL's is only 20 percent of the roughly $248 million in costs that IPL customers pay compared to MidAmerican customers receiving the same service. Consumer Advocate argued that its proposed adjustment was necessary to send a loud signal to senior management that the focus needs to be on IPL, and not other activities.

Consumer Advocate noted that IPL customers expressed their disagreement with the way IPL is managed at the consumer comment hearings. (Tr. 27-28). Consumer Advocate argued that IPL's attempts to explain the differences between its rates and MidAmerican's reinforces Consumer Advocate's contentions that IPL's rates are largely the result of poor management decisions over the past several years. For example, IPL argued that it has no capacity to sell on the wholesale market; Consumer Advocate said this is because of IPL's own actions and that the sale of DAEC left IPL in a position of relying heavily on purchased power, rather than lower cost self-generation.

<u>ICC Position</u>

ICC said that IPL's transmission expense increased substantially due in large part to management inefficiencies in managing transmission expenses. ICC said a 30 basis point reduction in ROE should be enough to get the attention of IPL's management while at the same time not materially undermining IPL's ability to attract capital. ICC noted that in brief IPL admitted that its transmission expenses were too high and that IPL filed a complaint at Federal Energy Regulatory Commission (FERC) for FERC to investigate ITC Midwest's transmission charges. (IPL Initial Brief, pp. 25-26). ICC also noted that IPL witness Aller admitted that IPL never considered that selling its transmission system to ITC Midwest could lead to the doubling of transmission rates.

<u>IPL Position</u>

IPL addressed each of the issues which Consumer Advocate and ICC claimed should result in a management efficiency penalty. While IPL admitted that its rates are currently higher than MidAmerican's, IPL said this does not indicate that IPL is operating in an inefficient manner, noting that Consumer Advocate admitted that MidAmerican is in a rare position and may not be similar to any other utilities. (Tr. 1062). IPL stated that its rate levels are consistent with those of other utilities in the region and that MidAmerican's capacity availability is based on decisions that were made decades ago, not several years ago.

IPL said that the main differences between IPL and MidAmerican relate to decisions on generation units, retail rates prior to 2000, variable cost differences due to the size, location, and age of generation (Tr. 581-591), and the ability to offset cost increases through wholesale sales. While Consumer Advocate argues that IPL should have been more aggressive in adding generation, IPL maintained that Consumer Advocate failed to include in its reasoning the substantial capital costs and associated rate increases necessary to pay for these new generating assets.

IPL noted that in Docket No. RPU-91-8, a case involving Iowa Southern Utilities Company, a predecessor to IPL, the utility requested a management efficiency award based on its ability to keep costs low. In that case, IPL pointed out that Consumer Advocate argued that the lack of spending could in the long run lead to less reliable service along with safety issues. IPL maintained that Consumer Advocate appears to argue both sides of the management efficiency issue by arguing criticizing a utility in one case for spending too much and in another for not spending enough.

While Consumer Advocate argued that investments in unregulated activities negatively impacted IPL's rates, IPL pointed out that all foreign investments were sold by 2007. In IPL's 2008 test year, IPL said that no costs could be related to foreign investments because there were not any.

IPL said it sold DAEC in January 2006 and that the sale was fully litigated and the sale allowed to go forward by the Board. IPL maintained that the sale of DAEC was not based solely on declining earnings, but also on the risks associated with owning a nuclear facility, including operations, decommissioning, relicensing, and storing spent fuel, which Consumer Advocate failed to identify. IPL pointed out that it was a small utility that owned one nuclear asset and that by selling DAEC while retaining the access to the capacity from the plant, IPL was able to reduce risk and retain the benefits from DAEC without increasing costs. (Tr. 60-61).

Consumer Advocate also argued that IPL is paying for decommissioning funding that is not needed. However, IPL said that the Nuclear Regulatory Commission clearly stated that the DAEC decommission fund has not met minimum funding levels; the DAEC purchase power agreement was designed to mirror the costs that IPL would incur if it were to retain DAEC through the end of the license in 2013, including decommissioning.

The second asset sale criticized by Consumer Advocate was the sale of IPL's transmission system to ITC Midwest, which was finalized in December 2007. Consumer Advocate claimed that the sale was driven by the motivation to insure that short term earnings targets were met. (Tr. 1017).

IPL pointed out that it began discussions in 1998 about forming a transmission-only company and filed a proposal in 2002 to transfer its transmission assets to TRANSLink, a proposed independent transmission company. IPL said that this request was disapproved by the Board (without prejudice) in June 2003. The subsequent agreement with ITC Midwest in 2007 was prompted, in part, by incentives provided in the Energy Policy Act of 2005 to build transmission and incentives to encourage the divestiture of transmission assets to independent transmission companies like ITC Midwest. IPL said it is being proactive in keeping ITC Midwest costs down and that IPL was able to achieve a $10 million reduction in costs for 2009; IPL also filed a complaint with FERC and will continue to challenge ITC Midwest on cost issues, where appropriate.

IPL noted that Consumer Advocate criticized the use of the DAEC and transmission sale proceeds, claiming they were used for unregulated purchases along with share repurchases. (Tr. 1018-19). In addition, IPL said that Consumer Advocate claimed that the sales boosted earnings per share (EPS) and the incentive compensation that is tied to it. IPL argued that what Consumer Advocate failed to note was that all net proceeds from the DAEC sale were put into a regulatory liability account and did not affect EPS. In addition, IPL pointed out that while the sale of the transmission system did increase EPS, the proceeds were not included in calculations for 2008 incentive compensation calculations. (Tr. 69).

In response to Consumer Advocate's criticism of its management, IPL listed some of its recent accomplishments. IPL discussed its response to the 2008 floods, energy efficiency programs, and many other areas where IPL maintained it operated extremely well. (Tr. 71).

IPL said Consumer Advocate failed to identify any of its $50 million proposed reduction as being based on imprudent or inefficient expenses that IPL can eliminate from its 2008 cost of service and that Consumer Advocate focused on the past but provided guidance as to what should be done by IPL to fix the perceived problem. In effect, IPL said that Consumer Advocate seeks to punish IPL for past wrongs that can no longer be rectified while, at the same time, offering no meaningful actions that IPL can take that would not add further increases to rates due to the large capital outlays necessary for additional generation. (Tr. 74). IPL noted that it has gone five years without a rate increase while at the same time working through two ice storms and a major flood; this should not result in a management efficiency penalty.

Board Discussion

Before addressing some of the arguments made by the parties regarding deficiencies in IPL's management, the Board believes it is appropriate to highlight two of the areas where IPL has performed well. These are appropriate considerations and are contemplated in the Board's rules establishing criteria used to evaluate management efficiencies and penalties (See 199 IAC 29.3(1) and 29.3(2)"d.". First, IPL has an award-winning energy efficiency plan that has been a factor in allowing IPL to defer building some expensive generation. IPL has also proposed several innovative programs, including a pilot renewable energy component, in its plan and continues to seek cost-effective ways for its customers to save energy and capacity. Second, IPL's service restoration efforts, particularly after the 2008 floods, are commendable. In particular, the Board wants to highlight the effort to restore Prairie Creek. IPL employees and management worked countless hours to restore service.

The Board also notes that disagreement with some management decisions does not necessarily equate to poor management. Reasonable persons can disagree over management decisions, but such disagreement alone, particularly when the decisions appear to be appropriate when made, should not result in management efficiency penalties simply because intervening events cause the original decisions to be questioned. Unfortunately, management decisions must be made contemporaneously, and not with the benefit of hindsight.

The decisions to sell DAEC and the transmission system, which were not disapproved by the Board, resulted in IPL being more dependent on purchased power and purchasing transmission service from other transmission owners. While individual Board members might have wished IPL made different decisions, the decisions made do not form the basis for a management efficiency penalty. The federal government, for example, encouraged utilities to divest their transmission system through incentives and both sales were the subject of litigated proceedings before the Board.

As will be discussed in greater detail in Section IV in this order, the Board is not persuaded, as argued by Consumer Advocate, that the ATA presented by IPL during the transmission sale proceedings was designed to shield IPL customers from all rate impacts from the transmission sale. Rather, the ATA was designed to protect customers from the impact of transferring transmission assets from state to federal jurisdiction; for example, FERC allows a higher ROE on transmission assets than has been traditionally allowed by states.

With respect to the comparisons Consumer Advocate seeks to make between IPL's and MidAmerican's rates, the Board finds it odd that Consumer Advocate criticizes IPL for not building generation sooner. IPL's energy efficiency successes played a role in its ability to defer generation additions. When the time came for IPL to add base load generation it proposed to build a coal plant, SGS Unit 4, which

Consumer Advocate opposed. Among the reasons for Consumer Advocate's opposition was that IPL would then have some excess generation capacity. In this proceeding, Consumer Advocate compares IPL's and MidAmerican's electric rates; IPL's are higher. Perhaps the primary reason for MidAmerican's success in maintaining its rate freeze and lower rates is its ability to sell excess generation in the wholesale market, yet Consumer Advocate opposed IPL's proposed facility because it would result in IPL having excess generating capacity.

The differences in IPL's and MidAmerican's excess capacity situation is only one reason the Board finds rate comparisons between utilities to be of little use. The two utilities also have different corporate histories, service territories, and customer bases that make rate comparisons of little or no value in determining management efficiency issues. A more relevant comparison for management efficiency purposes might have been a comparison of complaints filed with the Board against the two utilities, but no such comparison was made. IPL also adequately explained the differences in fuel costs between IPL and MidAmerican, and there is no persuasive evidence that Alliant Energy's unregulated activities had a negative impact on IPL.

While there is no single decision made by IPL at which the Board can point to specific disagreement, taken together the Board has concerns as to whether Alliant Energy and IPL have a clear vision and mission going forward with respect to providing service to Iowa consumers at just and reasonable rates. Individual corporate decisions should not be made in isolation but should be consistent with a company's overall vision and mission. For example, the Board questions whether

IPL conducted sufficient due diligence with respect to the transmission sale with respect to the impacts on its customers of trends in the industry, such as more stringent North American Electric Reliability Corporation (NERC) standards, which have resulted in some of the transmission cost increases. Also, IPL is heavily dependent on purchased power agreements to provide baseload power to its customers. The Board has concerns with this. Customer impact should be one of the focuses of IPL's decision making process. These concerns do not justify a management efficiency penalty, but the Board expects its mission and vision questions to be addressed ., either before IPL's next rate proceedings or during those proceedings . Management efficiency requires a balancing of both the good and bad and, on balance, the evidence does not support a penalty. There are concerns, however, that the Board expects to be addressed.

V. TRANSMISSION ISSUES

Introduction

IPL sold its transmission system to ITC Midwest, a transaction that was not disapproved and allowed to go forward by the Board pursuant to Iowa Code § 476.77 in Docket No. SPU-07-11. IPL proposed various transmission adjustments to reflect the costs its now pays to ITC Midwest (through MISO) for transmission service. IPL sought an adjustment for 2009 transmission expense increases, an adjustment for the 2008 undercollection true-up, and an adjustment for estimated 2010 transmission expenses. IPL also proposed an automatic adjustment mechanism similar to the EAC to recover transmission costs.

In its testimony regarding the various proposed transmission adjustments for 2009, 2010, and the 2008 true-up, Consumer Advocate focused on the cost-benefit analysis presented by IPL in Docket No. SPU-07-11 and what Consumer Advocate viewed as IPL's commitments that should limit what transmission charges are recoverable. Consumer Advocate proposed to disallow all ITC transmission costs that exceed the estimates presented in Docket No. SPU-07-11, arguing that to do otherwise would be to allow IPL to ignore its commitments. (Tr. 76). IPL disagreed, saying that the commitments made in that docket were not designed to shield customers from cost increases due to ITC Midwest's grid expansion or actual operations and maintenance and administrative and general expenses.

The ITC transmission rate approved by the FERC is based on projected costs, with a subsequent true-up. ICC objected to recovery of projected costs as violating the known and measureable standard. ICC argued that other than the true-up of 2008 costs, no transmission adjustments should be allowed because 2009 and 2010 ITC Midwest rates are not yet known and measureable and inclusion in this case would cause collection of more than one year of transmission costs within a single year.

The Board no longer has specific rate authority over IPL's transmission costs because FERC has exclusive jurisdiction over the rates charged by ITC Midwest. Several state courts have held that a state utility commission setting retail rates must allow, as reasonable operating expenses, costs incurred as a result of paying a FERC-determined wholesale price (such as transmission), basing their decisions on the filed rate doctrine; such state decisions have been approved by the U.S. Supreme Court. Nantahala Power & Light Co., v. Thornburg, 476 U.S. 953, 966 (1986). Consumer Advocate's and ICC's proposals would in effect require IPL to sell the transmission service it purchases to retail customers at less than the cost it paid, as determined by FERC. Under Nantahala, not allowing recovery of costs pursuant to a FERC-approved rate is called "trapping" costs and is prohibited. 476 U.S. at 969. When that FERC-approved rate includes projected costs (subject to true-up), it is part of a FERC-approved tariff and the state commission must allow recovery. United Gas Corp., v. Mississippi Pub. Ser. Comm'n, 127 So.2d 104 (Miss. 1961).

While these court decisions indicate that the Board must allow recovery of the FERC-approved rate paid by IPL for transmission service, there is no requirement that an automatic recovery mechanism must be approved and significant transmission increases, such as those that would result from the 2008 true-up, could be amortized over time to mitigate the immediate rate impact to IPL's customers. Also, the cases do not require recovery of costs in advance of a state's normal ratemaking process and do not require that a transmission-dependent utility like IPL be allowed to earn a return on any of its transmission costs that are not immediately recovered but amortized over time.

The Board will first address whether any transmission adjustments are warranted, focusing on Consumer Advocate's arguments that IPL should not recover more ITC Midwest costs than are included in the ATA cost-benefit analysis introduced in Docket No. SPU-07-11. The Board will then address the three proposed adjustments individually and IPL's proposal for a transmission rider.

Alternative Transmission Adjustment (ATA) Cost-Benefit Analysis and Are Any Transmission Adjustments Warranted

Consumer Advocate Position

Consumer Advocate said that IPL's pro forma transmission adjustments are intended to recover from IPL's customers all of the higher transmission expense for ITC Midwest rates. Consumer Advocate concluded all these adjustments should be rejected as wholly inconsistent with an unconditional commitment made by IPL in Docket No. SPU-07-11 to hold retail customers harmless from any rate increase effects resulting from the transmission sale for at least eight years. (Tr. 861-63, 909, 914). Consumer Advocate argued that in Docket No. SPU-07-11, IPL made this commitment in the sworn testimony of IPL witness Larsen (Tr. 911); through revenue requirement amounts submitted by IPL witness Hampsher (Ex. CEF-1, Sch. A, p. 1, line 2) that dramatically understated ITC Midwest's actual revenue requirements for 2008-2010; through assurances in IPL's initial and reply legal briefs; and through IPL's failure to file an application for rehearing to correct what it now claims is a misconception that customers would actually be held harmless for eight years.

At page 30 of its reply brief in Docket No. SPU-07-11, Consumer Advocate pointed out that IPL stated: "The ATA shields IPL's full requirements customers from any expected ratepayer impact resulting from the sale of IPL's transmission assets to ITC-Midwest for at least eight years and potentially for 20 years." (Tr. 118). Consumer Advocate concluded that based on IPL's statements, the Board permitted the sale to go forward pursuant to Iowa Code § 476.77. Consumer Advocate pointed out that IPL took no action to inform the Board that IPL's hold harmless assurances were meaningless empty promises dependent on the accuracy of its witnesses' estimates.

Consumer Advocate noted that IPL did not inform the Board during the pendency of Docket No. SPU-07-11 that customers would be subject to significant rate increases during the eight year period following the transaction, notwithstanding its hold harmless assurances. (Tr. 121-22, 512). Consumer Advocate concluded that IPL apparently believed that holding customers harmless for eight years would cost shareholders nothing.

Consumer Advocate argued that IPL essentially promised transmission costs based on its share of ITC Midwest post–transaction revenue requirement (PTTR) estimates for 2008-2010. Consumer Advocate said that IPL's adjustments proposed in this rate proceeding are inconsistent with commitments made in the transmission sale to hold customers harmless for at least eight years and therefore should be rejected.

Consumer Advocate proposed three smaller adjustments consistent with IPL's hold harmless commitments, essentially requiring IPL's shareholders to absorb the costs. Consumer Advocate said this was not unfair to shareholders because they received an after-tax gain on the transmission sale of over $218 million. (Tr. 527, 878). Consumer Advocate argued that it is unfair to allow IPL to renege on its hold harmless assurances, forcing customers to pay dramatically higher transmission costs, while shareholders retain a handsome profit. (Tr. 528-29). Consumer Advocate pointed out that when IPL made these statements in Docket No. SPU-07-11, it knew or should have known that shareholders would be at risk for ITC Midwest costs that substantially exceeded the SPU-07-11 estimates. Consumer Advocate concluded that its proposal does not call FERC-approved rates into question, undermine federal law or violate filed rate doctrine and, to the contrary, allowing IPL to negate its eight-year hold harmless commitment would undermine the reorganization provisions of Iowa Code §§ 476.76 and 476.77 and the integrity of the regulatory process.

ICC Position

ICC did not base its arguments just on statements made in Docket No. SPU-07-11, but instead argued that transmission expenses should be limited to actual costs incurred by IPL for the test year. ICC maintained that the only known and measurable adjustment for 2008 is the true-up amount ($46.9 million). However, ICC noted that any adjustment for ITC Midwest costs must be kept in the context of the original IPL and ITC Midwest relationship and the promises made to IPL customers. ICC said that both it and Consumer Advocate warned of the potential for costs to be substantially higher than those presented by IPL and ITC Midwest in Docket No. SPU-07-11. ICC stated that it is wholly inappropriate for IPL to be allowed to pass through the higher costs it steadfastly denied in the prior proceeding and unjust for IPL's customers to pay for IPL's mistakes.

ICC pointed out the test year for this rate proceeding is 2008. ICC proposed that IPL be permitted to collect actual 2008 expenses, and that whether ITC Midwest's rates are exclusively within FERC's jurisdiction is irrelevant because the Board has the authority and responsibility to regulate IPL's retail rates.

IPL Position

IPL noted that Consumer Advocate wanted all transmission costs (2008, 2009, 2010, and 2008 true-up) capped at the levels shown in the ATA cost-benefit analysis provided in Docket No. SPU-07-11. (Tr. 447-48). Under this treatment, IPL argued that it would suffer long-term impairment since the Consumer Advocate suggests capping transmission costs at this level through 2016. (Tr. 952).

IPL maintained that ITC Midwest rates are subject to the exclusive jurisdiction of FERC in an authorized rate/tariff that IPL is obligated to pay, and that Consumer Advocate acknowledged that IPL has no choice but to pay the FERC tariff rate. (Tr. 75, 877). IPL pointed out that it cannot take transmission service from a different provider to provide electric service to IPL's retail customers and that because FERC has approved the ITC Midwest tariff, the tariff charges are just and reasonable. (Tr. 915).

IPL argued the Board has no legal authority to change ITC Midwest's rates or revenue requirement. Pursuant to Iowa Code § 476.33(4), IPL said the Board must allow recovery of ITC Midwest costs that IPL incurs or will incur within 12 months of the filing of IPL's rate application.

IPL contended that its proposed transmission adjustments are not inconsistent with the commitments it made in Docket No. SPU-07-11. IPL said it had met all those commitments and that its current rate increase request is not inconsistent with Docket No. SPU-07-11 commitments.[1]

IPL argued that the purpose of the ATA cost benefit study was to hold customers harmless from the transfer of transmission assets from Board to FERC jurisdiction, not to shield customers from cost increases due to ITC Midwest's expansion of the grid or increased operations and maintenance (O&M) or administrative and general (A&G) costs. IPL said that Consumer Advocate misunderstood, overlooked, or ignored that the ATA cost-benefit analysis and also assumed ITC Midwest would operate the transmission system in the same manner as IPL, with capital spending, O&M and A&G remaining the same. (Tr. 45).

At hearing, IPL noted that IPL witness Hampsher explained the BLRR as transmission costs if IPL were to continue to own and operate the assets; the PTRR included the additional costs if assets were transferred to ITC Midwest and subject to FERC jurisdiction. IPL noted that four additional costs were quantified in the PTTR. First, a higher ROE, consistent with FERC decisions regarding transmission assets. Second, FERC would allow a higher percentage of common equity in the capital structure. Third, FERC would allow higher cash working capital. Fourth, the

[1] IPL stated that its commitments were: (1) limit the common equity in IPL's next electric rate case to no more than 50 percent; (2) IPL to make eight cash refunds of $13 million per year; (3) ITC Midwest to make eight rate discounts of $4 million per year; and (4) ITC Midwest would not seek recovery of the first $15 million of expenses associated with the sale. (Tr. 449).

transaction would result in a reduction to IPL's rate base for the accumulated deferred income taxes that could not be transferred to ITC Midwest. IPL said the ATA was designed to hold ratepayers harmless for costs associated with transferring transmission assets to FERC jurisdiction, not new costs from investments to rebuild and upgrade the system. (Tr. 506-10).

IPL believed there would be different levels of O&M and A&G once the transmission company took over its assets and began operations. IPL said that these increased costs, by design, were not factored into the cost-benefit analysis presented in Docket No. SPU-07-11. (Tr. 506-10).

IPL argued that Consumer Advocate's recommendation to cap transmission costs unfairly penalizes IPL by disallowing legitimate transmission expenses and that IPL customers should expect to pay for prudent transmission investments and related expenses. (Tr. 452-53). IPL pointed out that at the end of 2009 capital additions to the transmission system were more than $115 million above levels presented in the cost benefit analysis in Docket No. SPU-07-11. (Ex. CAH-2, Sch. H). IPL noted that at the hearing in Docket No. SPU-07-11, ITC Midwest witness Welch emphasized the increased investment ITC Midwest was prepared to make; this investment increased ITC Midwest's 2009 Attachment O revenue requirement by over $23.8 million. (Tr. 453-54). In addition, IPL noted that NERC standards are much tougher now than during the time IPL owned the transmission system, explaining ITC Midwest's higher O&M expense it its 2009 Attachment O. (Tr. 207, 457).

With respect to ICC's position, IPL noted that ICC contends 2009 ITC Midwest costs are not known (Tr. 1295, 1324-26) and 2010 costs are outside of the test year and are speculative (Tr. 1287). IPL disagreed, and noted the impact of ICC's recommendation would be to reduce IPL's revenue requirement by $40.8 million. (Tr. 77).

Board Discussion

The commitments made by IPL in Docket No. SPU-07-11 were designed to hold ratepayers harmless for eight years from known effects of the transfer of transmission assets from Board jurisdiction to FERC jurisdiction, taking into account such things as the higher ROEs awarded by FERC for transmission assets than had been awarded by the Board and the higher common equity and working capital allowed by FERC. The Board did not believe the hold harmless representations meant that ratepayers would not have to pay higher costs because of increased transmission investment or increased O&M expenditures. The testimony in Docket No. SPU-07-11 indicated that ITC Midwest would pursue an ambitious construction schedule. The Board is not persuaded that the costs of this construction would be covered by the ATA commitments. Further, nothing in the multiple cost-benefit scenarios or arguments presented by the various parties in Docket No. SPU-07-11 suggested that transmission rates would not increase if there was increased investment, either capital or maintenance, in the transmission system.

The record clearly demonstrates that some adjustment for increased transmission costs is appropriate and that the ATA commitments were limited in scope and were not designed to hold transmission rates steady for eight years when significant transmission upgrades would be built. However, as will be highlighted in the discussion of the 2010 costs, the Board does not believe Iowa Code § 476.33(4) mandates recovery of all costs that IPL incurs or will incur within 12 months of the filing of IPL's rate application; the statute only requires that the Board consider recovery of those costs. The Board will now address the three adjustments proposed by IPL.

2008 True-Up Adjustment

IPL Position

IPL noted that the 2008 true-up represents recovery of costs that are included in ITC Midwest's 2010 revenue requirement and will be charged to and paid by IPL beginning on January 1, 2010. IPL said the 2008 true-up represents the difference between rates charged by ITC Midwest in 2008 and actual costs incurred by ITC Midwest, and that an annual true-up is required pursuant to ITC Midwest's FERC-approved tariff. IPL proposed two alternatives to recover these costs. The first would amortize these costs ($46.4 million) over four years and include the unamortized balance in rate base; the second, and IPL's preferred alternative, would offset the true-up costs in their entirety with a portion of the Docket No. SPU-07-11 ATA regulatory liability account.

Consumer Advocate Position

Consumer Advocate would limit the 2008 true-up to the estimate provided by IPL in Docket No. SPU-07-11 ($104.41 million), less 2008 test year charges ($91.64

million), amortized over four years. Consumer Advocate opposed including the unamortized balance in rate base, asking that the decision be deferred to IPL's next rate case. Consumer Advocate also opposed using the regulatory liability account to offset the 2008 true-up, arguing that this would deny customers in later years the benefits provided by the ATA. (Tr. 987-89).

ICC Position

ICC said the full 2008 true-up is the only adjustment to test year transmission expenses that should be made.

LEG Position

LEG said that refunds due to customers pursuant to the ATA over eight years should be accelerated and would accept IPL's proposal to offset the 2008 true-up costs with a portion of the regulatory liability account provided that the balance of the account is refunded to customers through the EAC over a 12-month period commencing at the conclusion of this docket. LEG noted that accelerating the refund has the advantage of increasing value to customers because of the relatively low discount rate (4 percent) used in Docket No. SPU-07-11 for the eight-year period. (Tr. 1380, 1390).

Ag Processing Position

Ag Processing supported LEG's position with regard to accelerating refunds from the Docket No. SPU-07-11 ATA regulatory liability account.

Board Discussion

The Board will allow recovery of the 2008 true-up costs, amortized over a five-year period. The costs are known and measureable and were incurred by ITC Midwest in 2008, which is IPL's test year, but not immediately charged to IPL because of the projected revenue requirement and true-up mechanism used by ITC Midwest in FERC-approved transmission rates.

Consistent with LEG's proposal to accelerate use of the ATA regulatory liability account from the transmission sale to provide immediate benefit to ratepayers, and to negate the rate impact of the 2008 true-up for IPL's customers, the 2008 true-up costs will be offset with proceeds from the ATA account over the five-year amortization period. IPL will not be allowed to include the unamortized balance in rate base. IPL made the decision to sell its transmission assets and become a transmission purchaser rather than a transmission owner, and while it is appropriate and consistent with federal law that IPL recover amounts charged to it pursuant to ITC Midwest's FERC-approved tariff, it is not appropriate that IPL earn a return on those charges.

2009 Transmission Costs Adjustment

IPL began paying 2009 transmission costs beginning January 1, 2009. Consumer Advocate maintained these should not be recovered due to the hold harmless provision from the transmission sale, which the Board addressed earlier. Others argued that the 2009 costs should not be recovered now because the costs are based on projections and subject to a subsequent true-up.

Because IPL began paying the costs in 2009, they are known and measureable and incurred pursuant to rates charged by a FERC-approved tariff. While the rates are subject to subsequent refund and adjustment as part of the true-up mechanism used by FERC, they were not subject to change during 2009. Merely because FERC has adopted a mechanism for recovery of transmission costs that uses a forward-looking rate with a true-up mechanism does not mean that recovery should be delayed until the final true-up is complete, because the true-up will be reflected in future rates charged by ITC Midwest to IPL. However, consistent with LEG's proposal and to mitigate the rate impact of the 2009 transmission costs, up to $8 million of the ATA regulatory liability account will be used to offset those costs. The mechanics of this offset will be discussed under Section VII, Rate Design/Cost of Service, Compliance Tariffs and 2009 Offset.

2010 Transmission Costs Adjustment

Similar to its adjustment for 2009, IPL proposed an adjustment for ITC Midwest cost increases in 2010. IPL claimed that the costs were known and measureable when they were posted in its Attachment O in September 2009 (within nine months of the end of the test year) and billing will begin on January 1, 2010 (within 12 months of the commencement of this rate case). Consumer Advocate opposed inclusion of any 2010 costs higher than what were shown by the ATA cost-benefit analysis in Docket No. SPU-07-11. ICC also opposed the adjustment, consistent with its prior arguments that only the 2008 true-up is known and measureable.

The Board will deny this adjustment. These are projected costs and were not charged or paid by IPL until beginning January 1, 2010, three days before the Board's decision meeting and less than three weeks before a final decision in the case was issued. While those costs were posted sometime in September, the costs were still subject to challenge or change before their effective date.

The Board does not share IPL's view that Iowa Code § 476.33(4) mandates that the Board allow recovery of 2010 transmission costs. The statute directs the Board to consider certain adjustments outside the test year (within nine months of the test year or 12-months from the date of filing the rate proceeding), but does not mandate that the Board adopt any of those adjustments. Here, the costs came too late in the proceeding for it to be appropriate for inclusion in rates from this proceeding. While IPL complains that without recovery it would be denied a portion of the costs due to regulatory lag, the Board notes that IPL controls the timing of the filing of its rate cases and the selection of a test year, and that split test years have been utilized in the past.

Taken to its extreme, IPL's interpretation of the statute would require the Board to reopen IPL's rate case if a significant expense were incurred after a rate case decision was issued by the Board but within one-year of the rate case filing. This could often happen because the Board has a statutory ten-month deadline to decide rate cases. IPL's interpretation is not a reasonable interpretation of the statute and is inconsistent with the statute's terms, which only require that the Board consider these adjustments.

Transmission Cost Rider

Introduction

Iowa Code § 476.6(8) allows a utility to pass through costs to ratepayers via an automatic adjustment clause, if the Board approves. The Board has adopted rules in 199 IAC 20.9 providing that a rate-regulated electric utility can use an automatic adjustment clause to recover only those costs which are incurred in supplying energy, are beyond the direct control of management, are subject to sudden important change in level, are an important factor in determining the total cost to serve, are readily, precisely, and continuously segregated in the accounts of the utility.

IPL currently has an EAC and an energy efficiency cost recovery rider (EECR). In this proceeding, IPL proposed an automatic adjustment clause for transmission-related costs, including costs paid to ITC Midwest for transmission service. ICC, LEG, and Ag Processing opposed establishment of the clause. While Consumer Advocate said it shared some of the intervenors' concerns, it supported establishment of the clause, at least until transmission rates become more stable.

IPL Position

IPL argued that an automatic adjustment clause would help minimize the number of rate cases that are needed in order to address transmission expenses, principally, ITC Midwest's transmission charges, and thereby avoid the administrative burden that affects all interested parties. IPL said its proposal fits the basic requirements of an automatic adjustment clause pursuant to Iowa Code § 476.6(8) and 199 IAC 20.9(1). (Tr. 231). Specifically, IPL said the rider would recover expenses associated with various MISO schedules; ITC Midwest charges are billed to IPL by MISO, which in turn reimburses ITC Midwest. IPL said it would pass through the proposed automatic recovery clause only the share of expenses attributable to its Iowa retail load. IPL stated that MISO schedule 9, network integration transmission service, would be the predominate costs passed through the proposed clause.

IPL said it would develop cost recovery factors for each customer class, based on expected costs and sales volumes. Under IPL's proposal, these factors would remain in effect for one year and collections are reconciled against actual costs for an annual period. (Tr. 230). IPL proposed that the automatic adjustment clause for transmission costs would be reflected on customers' bills as a separate line item similar to IPL's EAC. IPL said its transmission rider would indicate a charge per kWh applicable to the all kWh usage for the applicable billing cycle for the residential, general service, and lighting customer classes, and a charge per kW applicable to the billing demand for the applicable billing cycle for the Large General Service (LGS), Bulk Power, and Standby customer classes. (Tr. 764). IPL proposed that the annual transmission expense be allocated to customer classes based on an average and excess methodology.

IPL said the factors in the proposed transmission clause would be revised annually, similar to what is done with the EECR. IPL noted that new factors will become effective January 1st each year going forward, and will remain in effect for the calendar year. IPL said it will file annually in November of each year for the factors that will become effective on January 1st. (Tr. 765).

IPL said its transmission costs, including costs from ITC Midwest, are expected to vary widely over the next several years. IPL projected that its costs for MISO schedule 9 service would range from $77,391,000 in 2008 to $170 million in 2011. IPL argued that traditional ratemaking practices are not well suited to address cost changes of this magnitude, especially when IPL has no direct control over these costs. (Tr. 231). IPL said that an automatic adjustment clause would allow for a one-to-one matching of costs incurred and costs recovered from customers and the proposed mechanism will insure that neither the company nor the customer pays more or less than the actual costs incurred. (Tr. 232).

IPL argued that its proposal satisfied the criteria for an adjustment clause found in 199 IAC 20.9, and that the Board has previously approved automatic adjustment clauses, such as EACs, EECRs, and MidAmerican's Cooper Nuclear Tracker. (Tr. 906-07). IPL maintained that the issue surrounding an automatic adjustment clause for transmission costs is more a question of regulatory and pricing policy than it is a question of whether the criteria in the Board's rules can be interpreted as a perfect match for these costs. (Tr. 255).

IPL addressed each of the five criteria in 199 IAC 20.9. The first criterion is incurred in the supplying of energy. IPL said it is now invoiced monthly by MISO for costs that ITC Midwest incurs to provide IPL transmission service and that the costs billed by MISO are required in the supply of energy to IPL's customers from IPL's generation sources. (Tr. 233). IPL noted that ICC argued that these transmission costs are not incurred in the supplying of energy, but failed to explain how IPL's customers would get access to energy without the high voltage transmission lines provided by ITC Midwest. IPL also noted that ICC suggested that transmission charges would then be no different than distribution or generation costs regulated by the Board, but IPL said this ignored the fact that ITC Midwest rates are directly regulated by the FERC and distribution and generation costs are regulated by the Board. (Tr. 256).

The second criterion is that the costs are beyond the control of management. IPL pointed out that ITC Midwest costs are part of the FERC-approved MISO tariff and that IPL does not control the FERC-approved MISO formula rates or the underlying costs reflected in those rates. IPL also maintained that the costs are difficult for IPL to indirectly manage. (Tr. 235).

IPL said that both ICC and LEG argued that IPL could influence these costs, but IPL argued there is a clear difference between controlling costs and influencing costs. IPL said it cannot control those costs, as they are the result of business decisions made by IPL's independent transmission provider, resulting in rates approved by the FERC. (Tr. 258). IPL volunteered routine (annual) filings to keep the Board apprised on activities IPL has taken to influence transmission costs, which could provide some level of indirect Board oversight that IPL is taking appropriate steps to positively influence both ITC Midwest and the FERC when it comes to the cost-benefit trade-off. (Tr. 259).

The third criterion for costs to be included in an adjustment mechanism is that they are subject to sudden and important change in level. IPL pointed out that the nominal change in transmission costs between 2008 and 2010 is projected to be as high as $70 million. In the foreseeable future, IPL said it expects both cost increases and cost decreases from the MISO/ITC Midwest charges, due in part to the reconciliation process that ITC Midwest will utilize as part of its formula rate process. (Tr. 233-34).

The fourth criterion is that the costs are an important factor in determining the total cost to serve. IPL said its total costs from ITC Midwest in 2010 are expected to be about $200 million, which represents about 15 percent of IPL's overall revenue requirement. (Tr. 234).

The fifth and final criterion is that the costs are readily, precisely, and continuously segregated in the accounts of the utility. IPL said that since the end of 2007, it has been receiving MISO invoices related to providing transmission service to IPL for the benefit of all of IPL's electric customers. IPL said it utilizes separate accounting strings so that the MISO transmission invoices related to ITC Midwest costs can be separately tracked from other MISO-related charges, allowing IPL to readily ascertain the actual monthly transmission expenses related to ITC Midwest transmission costs. IPL argued that LEG's claim that transmission costs are not clearly segregated in the accounts of the utility is erroneous, because similar to fuel costs, transmission costs are accounted for separately by FERC account. (Tr. 257).

IPL also argued that LEG's other assertions that costs billed to IPL and WPL cannot be easily identified is incorrect and that no IPL charges are paid by Alliant Energy Service Corporation. IPL said that schedules provided by IPL demonstrate the ease of tracking the charges to each utility (Ex. DV-2), and that all IPL charges are booked to FERC account 565. (Tr. 804-05).

IPL said that lack of an automatic adjustment clause could place IPL in a position where it can never fully recover its costs, because the rates approved by FERC are placed into effect January 1 of each year. Under the traditional ratemaking structure in Iowa, IPL (assuming a calendar year test period) said that it cannot place temporary rates into effect until late March. As a result, there would be a lag between the change in ITC Midwest transmission rates and IPL's ability to recover those increases in rates. (Tr. 236). IPL said it did not believe an annual rate case to recover increases in transmission costs is a realistic long-term solution.

IPL disagreed with LEG's assertion that a decision on a proposed Black Hills[2] Capital Additions Tracker in Docket No. RPU-08-3 set a precedent for this proceeding. IPL pointed out several differences in its proposal, noting that the Black Hills' costs could be projected accurately, were not extraordinary, and were under the direct control of the utility's management.

[2] On May 7, 2009, the Board issued an order rejecting a nonunanimous settlement agreement filed by Black Hills/Iowa Gas Utility Company, LLC, d/b/a Black Hills Energy (Black Hills), and Consumer Advocate that purported to settle all issues related to the revenue requirement in Docket No. RPU-08-3 and proposed a capital additions tracker as a pilot project.

Consumer Advocate Position

Consumer Advocate did not object to an automatic adjustment clause for IPL's transmission costs, at least until transmission rates become more stable, noting that transmission costs are significant and subject to large fluctuations from year to year. (Tr. 883-84). Consumer Advocate said, however, that implementation of an automatic adjustment clause did not release IPL from honoring its hold harmless commitment to customers that it made in the transmission sale docket.

ICC Position

ICC argued that IPL's transmission clause proposal did not meet the criteria set forth in 199 IAC 20.9. ICC noted that the EECR, which IPL cited as support for its proposal, is based on stakeholder input, Board review of the utility's energy efficiency plan, and Board approval of recovery cost levels; none of these factors are present here and IPL's proposal lacks such Board oversight and protection.

ICC disagreed with IPL's assertion that IPL's proposal will benefit all parties as it will help minimize number of rate cases that are needed to address ITC Midwest charges, thereby avoiding administrative burden on all parties. To the contrary, ICC argued that IPL's proposal could harm the interested parties as transmission costs would be passed through to retail customers without Board oversight. Despite its shortcomings, ICC maintained that a rate case still remains the best course for the Board, Consumer Advocate, and customers to participate in the oversight and control of IPL costs.

ICC pointed out that IPL might experience future cost decreases that may offset increases in transmission costs, thereby obviating the need of an automatic adjustment. ICC said a utility's overall costs could decrease for many reasons, such as a reduction in rate base as a result of the build-up of accumulated depreciation and deferred income taxes, additional revenues from growth, improved operation efficiencies by means such as automation, and work force reduction.

ICC said that IPL's proposal fails under the five criteria outlined under 199 IAC 20(9). Under the first criteria, ICC said that the charges must be incurred in the supplying of energy. According to IPL's logic, ICC said that the same treatment could be allocated to other costs including distribution costs, generation costs, and the like, all of which are required in the supply of energy. ICC argued transmission costs are not the kind of costs envisioned by the first criterion.

Although IPL argued its proposal meets the second criterion because IPL does not control the FERC approved formula rates nor the underlying costs reflected in those rates, ICC countered that IPL can influence these costs by managing its relationship with ITC Midwest and participating at FERC proceedings. To the extent that IPL is not doing this and trying to manage other transmission costs, ICC said IPL should not be given a license to pass those expenses on to ratepayers.

ICC said the third criterion (subject to sudden important change in level) is also not met. While the 2008 ITC Midwest formula rates are different from the initial rates, ICC maintained that this is more likely a solitary event and future changes and true-ups are likely to be smaller as parties gain experience in actual operations.

ICC acknowledged that the final two criteria (important factor in cost to serve and segregated accounts) were satisfied, but that this is not sufficient for establishment of an adjustment clause. ICC said that a rate case was the appropriate mechanism for recovering transmission costs.

LEG Position

LEG said that in a recent Black Hills gas rate case, Docket No. RPU-08-3, the Board on May 7, 2009, issued an order rejecting a Capital Additions Tracker for recovery of the costs of non-revenue-producing system integrity capital costs. LEG argued that the evidentiary record in the Black Hills docket and the precedent set by this recent decision compels an identical analysis and conclusion. LEG maintained that historically automatic adjustment clauses have been allowed on a limited basis and have been for costs that are beyond the control of management and are subject to change levels. LEG said IPL's proposal does not meet the criteria normally required for an automatic adjustment, because the evidence shows that transmission costs recovered through the automatic adjustment clause can be projected fairly accurately, will not fluctuate dramatically from year to year, IPL has significant control of these costs, and transmission costs are not an important factor in determining total cost to serve. (Tr. 1292-93, 1372-74, 1385, 1404-05).

LEG claimed an automatic adjustment would allow IPL to increase rates for electric service and increase revenues outside of a rate case without any risk of non-recovery and without matching costs with reduced expenses. For the Board to approve this mechanism, LEG argued that it would have to find that there was an extraordinary need for the mechanism or the benefits outweigh the costs. LEG noted the evidence in this proceeding does not show that the projected expenditures are extraordinary and require extraordinary treatment, and that transmission costs were not shown to be much different in magnitude than distribution costs, meaning that transmission costs are not unique. Even if the Board approves IPL's proposal, LEG said that it is unreasonable since it does not include an adjustment of the ROE for the reduced risk that the adjustment clause provides. (Tr. 184, 233, 1533). Without this adjustment and without an agreement to delay the next rate case filing, LEG said that IPL's proposal does provide any benefits that outweigh the costs of deviating from traditional regulation. At a minimum, LEG said a decision on the clause should be deferred until IPL's impending 2010 rate case filing.

While LEG maintained that IPL's proposal should be rejected in its entirety, LEG said if the proposal is adopted, charges per kW of demand should be cost-based by delivery level. (Tr. 1360). LEG said that IPL proposed to develop rates for the automatic adjustment by reducing the Large General Service base rate demand charges by $2.13/kW/month to remove the estimated demand charges from existing base rates and introducing an estimated $3.92/kW/month adjustment factor for this class. LEG argued that this proposal would result in an immediate increase in rates for many Large General Service customers. (Tr. 1375). LEG said the problem could be solve by including the discount in the transmission $/kW adjustment as well, and IPL appears to have agreed with this solution at hearing. (Tr. 813-15).

Ag Processing Position

Ag Processing opposed IPL's automatic recovery clause. Ag Processing said that if the proposal was approved, the charges per kW demand should be cost-based by voltage delivery level.

Board Discussion

The Board will defer a decision on this issue until IPL's next rate case. At that time, there will be one year's additional experience with ITC Midwest/MISO transmission costs to see how those costs might fluctuate. In addition, there are details with respect to the rider that must be worked out, if it is adopted, such as whether it should be included as a separate line item on the bill like the EAC or rolled into rates like the EECR, what the estimated costs per kWh and per kW demand of the rider would be for each customer class, and more detailed information on the costs to be included in the rider.

VI. COST OF CAPITAL

There are two primary issues the Board needs to determine with respect to cost of capital. The first issue is to set the appropriate return on equity, and the second is to determine the appropriate capital structure for ratemaking purposes for IPL. In determining the appropriate capital structure, there are three contested issues the Board must decide, year-end vs. 13-month average capital structure, preferred equity, and double leverage.

Return on Equity (ROE)

Introduction

In setting an allowed rate of return on equity investment, the Board is to balance investor and consumer interests. For example, if rates produce earnings that are below a fair and reasonable level, they are unjust or confiscatory to the owners of the utility property; if rates produce earnings that are above a fair and reasonable level, the rates are oppressive to the utility's ratepayers. Davenport Water Co., v. Iowa State Commerce Comm'n, 190 N.W.2d 583, 604-05 (Iowa 1971). In addition, the U.S. Supreme Court, in FPC v. Hope Natural Gas Company, 320 US 591, (1944) held that "the return to the equity owner [the utility] should be commensurate with returns on investments in other enterprises having corresponding risks. The return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise so as to maintain credit and attract capital ... ."

In determining the allowed return, the various models generally produce a range for the Board to consider. There is no precise return on equity that is accurate or appropriate, but a reasonable range of return. Within that reasonable range, the Board determines what it finds to be the most appropriate return, balancing the interests of shareholders and ratepayers. IPL and its ratepayers have gone through an extremely difficult period because of the devastation caused by the 2008 floods and the recent economic downturn. The Board believes that under such circumstances it is appropriate to consider whether the equity return selected, in addition to producing fair and reasonable rates, provides adequate incentives to IPL to ensure that it exercises due diligence in managing its costs.

IPL, Consumer Advocate, and ICC presented ROE testimony. All three of the ROE witnesses used the discounted cash flow (DCF) model and the capital asset pricing model (CAPM). IPL and ICC also used the risk premium method. IPL initially provided testimony regarding the comparable earnings model but did not use the results in its ROE recommendation because it determined the results from the model were unreasonably high. The Board will not address the comparable earnings model in this order since it was not used to formulate any of the parties' ROE recommendations.

IPL's expert witness recommended an 11.8 percent ROE, which was reduced to 11.4 percent by IPL to help mitigate ratepayer impacts from the proposed rate increase; IPL's witness later adjusted his recommendation to 11.2 percent to reflect more recent market data. IPL's 11.2 percent ROE includes adjustments for both business and financial risks. Consumer Advocate and ICC each recommended a 10 percent ROE.

<u>IPL Position</u>

IPL used the DCF model, CAPM, and the risk premium method to develop its recommendation. IPL's DCF model produced a 10.66 to 10.78 percent ROE range while the CAPM using utility proxies produced a 11.33 percent ROE and the risk premium using utility proxies produced a 12.26 percent ROE. In addition, IPL used a risk premium model that added 400 to 500 basis points to the 12-month average A3 public utility bond yield of 6.92 percent, producing a range of 10.92 to 11.92 percent. IPL also added 0.16 to 0.19 percent to the recommended ROE as a business risk adjustment for utility proxies and 0.20 percent as a financial risk adjustment for utility proxies. In considering the results of the various models and subsequent market conditions, IPL recommended an 11.2 percent ROE.

IPL used a group of ten electric and combination electric and gas companies for its proxy group and reviewed Alliant Energy separately. IPL noted that ICC used the same proxy group but included Alliant Energy as part of the proxy group. (Tr. 1829).

IPL noted that while all three parties offering ROE recommendations used at least one form of the DCF model, IPL's methodology was the most reliable because it used a median cost rate for the proxy group and Alliant Energy, rather than an average cost rate that is much higher. (Tr. 1499-1500). Also, IPL did not rely on spot market price when the market is volatile, but used an average dividend yield and reflected only half of the growth of its dividend yield estimate. (Tr. 1500-01).

IPL criticized ICC's DCF analysis because of comparisons of senior secured credit ratings; IPL pointed out it had no senior secured debt in its capital structure. (Tr. 1931; IPL Ex. EB-1, Schs. B-1, p. 94 and B-3, p. 19). IPL said this means that ICC improperly reflected IPL's risks relative to the proxy group. IPL also said ICC chose to exclude the results of its constant growth DCF model because of issues with its growth rate, even though the growth rate appeared to fall within a normal range. (Tr. 1919).

Included in IPL's ROE recommendation are adders for business and financial risk. IPL argued that these were appropriate given IPL's small size relative to the proxy group and its lower bond rating. (Tr. 1480, 1481-85, 1485-86).

Consumer Advocate Position

Consumer Advocate focused its DCF and CAPM analysis on determining the appropriate ROE for IPL's parent, Alliant Energy, and then applying the models to its utility proxy group. Consumer Advocate's DCF range is 9.7 to 10.8 percent (Tr. 35), and its CAPM range is 8.2 to 8.6 percent. (Tr. 1735). Consumer Advocate's recommendation is 10 percent, which it noted compares favorably to the 4.1 percent yield on 20-year Treasury bonds for the 12-month period ending May 2009, the 4.2 percent yield on 20-year Treasury bonds in May 2009, the 6.6 percent average yield on A-rated utility bonds for the 12-month period ending May 2009, and the 9.6 percent market return on Standard & Poor's (S&P) 500 with a beta of 1 compared to Alliant Energy's beta of 0.70. (Tr. 1748-49).

Consumer Advocate was particularly critical of the growth estimates of 6.4 to 6.8 percent used by IPL in the models claiming that those are not sustainable and not probable in the next five years when the economy is coming out of a major recession. (Tr. 1751-53). In addition, Consumer Advocate said using five-year models now means too much reliance on an atypical trough in the business cycle and that IPL's ROE estimates are therefore overstated, unreliable, and unrepresentative. (Tr. 1760-65).

Consumer Advocate in its analysis first reviewed data for Alliant Energy and noted the distinction between Alliant Energy's and IPL's cost of common equity is difficult to measure. (Tr. 1695). Consumer Advocate also used a proxy group of four combination gas and electric companies that are similar to Alliant Energy in that each has their own generation plants and depend mainly on coal to generate electricity. (Tr. 1697-98). Consumer Advocate said IPL's proxy group was not representative because some of the utilities used are not similar to Alliant Energy. (Tr. 1696-97).

Consumer Advocate opposed the business and financial adders proposed by IPL. Consumer Advocate pointed out that such adjustments have previously been rejected by the Board.

ICC Position

ICC used three variations of the DCF model, CAPM, and two risk premium methods to arrive at its overall recommendation of 10 percent. The various DCF models produced overall ranges of 10.65 to 11.76 percent (Tr. 1842), the CAPM 8.83 to 8.88 percent (Tr. 1852), and the risk premium methods 9.0 to 11.0 percent. ICC noted that the outlook for the electric utility industry is good and that analysts believe electric utilities generally will be able to weather the current economic downturn and maintain their credit ratings. ICC said that because IPL is not publicly traded, it used the same proxy group as IPL to arrive at its ROE recommendations.

ICC criticized IPL for using high growth rates that inflate its DCF results and are not sustainable. Also, because of the many outliers in IPL's analysis, it uses median instead of average results, which produce excessive growth rates. ICC also questioned IPL's criticism regarding comparison of secured credit rates; regardless of whether IPL has a secured or unsecured debt rating, ICC said its conclusion that IPL's risk is comparable to the proxy group is unchanged.

ICC opposed IPL's business and financial risk adders. ICC noted that the Board has previously rejected such adjustments and that the risks identified by IPL are already reflected in the recommendations.

Board Discussion

In presenting the various ROE models, there were arguments presented not only with respect to the final recommendation but also with respect to some of the inputs and the validity of some of the models. One of the disagreements was with respect to the proxy group used. Market-based models like DCF and CAPM cannot be applied directly to IPL because IPL's stock is not traded in the open market; only the stock of Alliant Energy, IPL's parent, is publicly traded. While Alliant Energy's ROE is one estimate for IPL's ROE, proxy groups have also been used as one of many tools in determining IPL's ROE.

No proxy group is perfect. IPL used ten combination electric and gas companies and electric only companies in its proxy group. Consumer Advocate argued that IPL's group included companies that were not similar to Alliant Energy because they are either distribution-only or transmission-only companies. Consumer Advocate used four companies that were similar to Alliant Energy; IPL claimed that this proxy group was too small to produce meaningful results, and that proxy companies should be similar to IPL, not Alliant Energy.

The Board will look at the ROE results produced by both proxy groups. Both IPL and Consumer Advocate attempted to develop a meaningful proxy group and the ROE results from both proxy groups should be considered in determining IPL's ROE.

Another area of dispute was with respect to the appropriate DCF model. All three parties used at least one form of the DCF model, and each claimed that the model it used was superior. Consumer Advocate used the continuous form of the DCF model where the dividend is not grown, IPL used the FERC version where the dividend is increased by one-half the growth rate, and ICC used the constant growth model where the dividend is grown by the full growth rate. ICC also used two other versions of the DCF model, the sustainable growth and multi-stage growth models.

In the past, the Board has placed more reliance on the FERC version because it represents a compromise between the continuous and constant growth models. Again, however, there is no perfect DCF model and the Board looks at the results of all the DCF models as another tool in determining IPL's ROE.

Various risk premium models were also presented. In its simplest form, the risk premium model takes a specific long-term debt interest rate and adds an associated risk premium to estimate the ROE. The Board in recent years has given weight to its own risk premium method, which takes the current A-rated utility bond rate or the 12-month average yield and adds a risk premium range of 250 to 450 basis points. While IPL argued that the Board's risk premium range should be increased, the Board believes that its model has worked well over time as another tool in determining a utility's ROE. The Board's range provides significant latitude to select an ROE near the higher or lower end of the range, depending on the facts and circumstances of a particular case.

All the parties used the traditional form of CAPM, and IPL also used the empirical CAPM (ECAPM). Traditionally, the Board has not given much weight to any CAPM analysis because there were concerns about its reliability. The Board has, and will in this proceeding, examine the results from the CAPM method as another tool in its ROE determination.

IPL recommended an upwards ROE adjustment for IPL based on two risks, its business and financial risk. IPL based the business risk adjustment on IPL's relative small size to the proxy group and the financial risk adjustment based on IPL's lower bond rating. (Tr. 1480, 1481-85, 1485-86). The other parties opposed this adjustment, and Consumer Advocate noted that the Board has said that "[b]ecause the various [ROE] models consider so many factors, it is difficult to isolate any one item, such as size, and make that the basis for an additional adjustment." Interstate Power and Light Company, "Final Decision and Order," Docket No. RPU-02-3, p. 63.

The Board is not persuaded that either upwards adjustment is appropriate. The proxy groups contain both large and small companies and should reasonably capture IPL's small size risk. In addition, proxy companies with similar bond ratings reflect similar business and financial risks. There is simply no persuasive evidence to isolate individual factors to adjust ROE, because the models already take into account numerous factors, including business and financial risk. See, Interstate Power and Light Company, "Final Decision and Order," Docket No. RPU-08-1, p. 62.

At hearing, IPL argued that factors that reduce IPL’s relative risk, such as the DAEC sale and Iowa’s favorable regulatory climate, are fully accounted for in bond ratings, but those bond ratings do not account for size-related risk, requiring an adjustment to compensate for this deficiency. However, the very source cited by IPL to support the relationship between size and business risk does not appear to give much support for IPL’s approach to adjusting for that risk. According to that source, IPL’s approach opens the door to a series of other adjustments that should also be made (but which IPL did not make), and a better method would be to identify the economic reasons underlying the size premium and measure those reasons directly. There is evidence in this docket, submitted by IPL, that at least one of these underlying reasons (unusual reliance on a few large customers) is already taken into account by at least one bond rating service. Therefore, based on IPL’s own evidence, it appears that IPL’s adjustment for size-related business risk may overcompensate for at least some portion of any such risk that may exist.Consumer Advocate and ICC have a final ROE recommendation of 10 percent. IPL's final recommendation, without the two adders discussed above, is approximately 10.8 percent. In this proceeding, unlike many others, the parties' ranges from their various DCF results are not dramatically far apart. Taking all three parties' recommended DCF results, the DCF range is 10.2 to 11 percent. The CAPM models produce dramatically different results, with the overall range from 8.4 (Consumer Advocate's low end) percent to 11.33 (IPL's high end) percent. The risk premium methods also produce dramatically different results, with the overall range from 9.84 (ICC low end) percent to 12.26 (IPL's high end) percent.

The Board in recent years has used the risk premium method as a check on reasonableness when determining return on equity. The risk premium model often used by the Board adds 250 to 450 basis points to the most current A-rated utility bond yield, rather than to the 12-month average. The most recent bond yield available is August's 5.71 percent, producing a return on equity range of 8.21 to 10.21 percent. Because yields have been historically low, it is appropriate here to also look at the 12-month average from September 2008 to August 2009, excluding the months of October and November, which appear to be anomalies because of the economic and market downturn. The average 6.3 percent A-rated bond yield produces a risk premium range of 8.8 to 10.8 percent, which is close to the range produced by ICC.

In reviewing current market data and the ranges produced by the Board's risk premium analysis and the other market-based models, a return on equity range between 10.2 and 10.6 percent is reasonable, with more reliance placed in this proceeding on the DCF methods because of the convergence of their results. The Board will set the ROE at 10.5 percent, which the Board believes appropriately balances the interests of the shareholders and ratepayers and is consistent with recent ROE decisions.

Year-End vs. 13-Month Average Capital Structure

IPL advocated the use of a year-end capital structure (December 31, 2008) that reflects post-test year financings, because it is more representative of IPL's capital structure. (Tr. 654). IPL also said that a year-end capital structure is more forward-looking and better reflective of the current environment.

Consumer Advocate used a 13-month average capital structure reflecting pro forma adjustments that occurred between January 2009 and September 2009, noting that this was consistent with Iowa Code § 476.33(4). While the differences in IPL's and Consumer Advocate's proposed capital structures are negligible in this case, Consumer Advocate said that adopting a year-end capital structure would enable utilities to achieve greater profit in future cases. Consumer Advocate argued that because Alliant Energy controls equity infusions, the payments of IPL's dividends to Alliant Energy, and IPL's issuance or replacement of long-term debt and preferred stock, Alliant Energy can control the timing of these transactions such that IPL's year-end capital structure could provide a higher return than a capital structure based on a 13-month average.

Consumer Advocate also maintained that the matching principle would be violated if a year-end capital structure was used. Iowa Code § 476.33(4). In addition, the year-end capital structure does not represent the actual capital that was invested in a test year average rate base, and instead relies on account balances that occurred on a single day.

The Board has consistently used the 13-month average capital structure. In deciding to use a 13-month average instead of a year-end capital structure, the Board has said that "[i]t is undesirable to adopt a single date as the time for determining a Company's capital structure. It affords an opportunity to alter the structure to the Company's advantage should it choose to do so." Interstate Power and Light Company, "Final Decision and Order," Docket No. RPU-83-27, p. 11.

Because there is little difference in the two proposed capital structures, the Board is not persuaded to depart from its precedent in this proceeding. The use of the 13-month average capital structure is consistent with Iowa Code § 476.33(4), which provides that the Board "consider verifiable data that exists within nine months after the conclusion of the test year, reflecting known and measureable changes in costs not associated with a different level of revenue, and known and measureable revenues not associated with a different level of costs." This legislation allows the Board to consider pro forma adjustments beyond the test year and addresses, at least to some extent, IPL's concerns that test year rate cases do not reflect major changes going forward. Using a 13-month average capital structure matches the Board's use of a 13-month average rate base.

The Board also continues to have concerns that use of a year-end capital structure gives too much weight to the capital structure that exists on one day of the year. A 13-month average capital structure smoothes any aberrations in the capital structure that might occur on a single day or over a single month. For example, Consumer Advocate demonstrated that for nine out of ten years, IPL's retained earnings were higher at year end as compared to an average balance. (Tr. 1215; Ex. SPJ-1, Sch. D, p. 1). A 13-month average also removes any incentive for a utility to make adjustments to its capital structure at the end of the test year to artificially increase its estimated cost of capital going forward.

In addition to the issues addressed by the parties, there is one item regarding capital structure that the Board will point out. In the case involving the sale of IPL's transmission system to ITC Midwest (Docket No. SPU-07-11), IPL committed to not filing a capital structure with a common equity ratio greater than 50 percent. The Late-Filed Exhibit 23 submitted by IPL to correct an error in not reflecting $25 million in unamortized debt balances for its new debt issue (along with changes to the common equity balance) caused the common equity ratio to increase to 50.382 percent. However, since the Board is using Consumer Advocate's proposed common equity balance, no adjustment is necessary.

Preferred Equity Adjustment

Consumer Advocate proposed to make three preferred stock adjustments to IPL's capital structure. Consumer Advocate noted that two of the adjustments have been approved by the Board in prior IPL rate cases, and both deal with IPL's 1979 preferred stock exchange. IPL disagreed with all three adjustments.

The three stock exchanges or redemptions at issue are:

1. In 1979, Interstate Power Company (IPC), a predecessor to IPL, chose to exchange two series of preferred stock with more expensive preferred stock, resulting in an equity gain to IPC of approximately

$5.5 million. In prior cases, the Board reversed this preferred stock exchange as if it had not occurred for purposes of determining a capital structure used to set electric rates. (Tr. 1220-21). The two series exchanged had rates of 4.36 and 4.68 percent; the new preferred stock had a rate of 9.0 percent.

2. The second adjustment is related to the 1979 preferred stock exchange. In 1993, IPL redeemed $25,473,750 of 9 percent preferred stock issued in 1979 with $27,250,000 of 6.4 percent preferred stock; the Board reflected the amount of the 6.4 percent preferred stock above the redeemed amount in IPL's capital structure. (Tr. 122-23; Ex. SJP-1, Sch. E, p. 2).

3. In 2002, IPL retired seven series of preferred stock. Four of series were issued by IPC and three by IES Utilities, Inc., another predecessor to IPL. IPL initially planned to call the preferred stock using so-called trust preferred stock that would be treated both like equity and debt. However, after the collapse of Enron this type of financing became unattractive, and IPL issued new preferred stock at a higher cost rate. (Tr. 722-27).

In the 1979 preferred stock exchange, the exchange of two series of preferred stock with more expensive preferred stock resulted in a paper gain to IPC of about $5.5 million. By increasing the common equity, ratepayers had to pay higher capital costs without receiving any benefit; therefore, previous Boards have reversed this transaction as if it had not occurred. IPL did not address this historic adjustment in prefiled testimony or hearing other than to say it did not understand the logic behind the adjustment. (Tr. 728-29). The 1993 proposed adjustment is related to the 1979 exchange.

With the 2002 retirements, all of the old series of preferred stock issued by predecessors to IPL have been retired. IPL said that these seven series, which were issued in the late 1940s and 1950s, contained covenants that were outdated, including limiting the amount of unsecured debt. While the preferred stock was issued by IPL's predecessor companies, IPL was subject to those covenants as various mergers occurred to form the present day IPL and Alliant Energy. IPL maintained that retiring the preferred stock benefited ratepayers, although it was unable to quantify the benefits. IPL said it could not quantify opportunities missed in terms of financing on an unsecured basis when stock covenants do not allow for additional unsecured financing. (Tr. 726). IPL said other benefits from the retirements included eliminating preferred stockholder approval for asset sales and mergers and elimination of legacy covenants that required certain assets to be separated within IPL. (Tr. 702-03).

Consumer Advocate proposed to reverse the impacts of the 2002 preferred stock retirements because Consumer Advocate claimed that costs to ratepayers due to the retirements increased by at least $1.7 million annually. (Tr. 1225; Ex. SJP-1, Sch. E, pp. 7-8). Consumer Advocate pointed out that the 2002 transactions increased the cost of preferred equity in 2009 by nearly 50 percent.

The retirement of the seven series of preferred stock was not done to benefit common shareholders but to eliminate outdated covenants that affected financing. The retirements clearly benefited ratepayers, although those benefits cannot be quantified. Given the time that has passed since IPL’s current corporate structure was put in place, the Board believes it was time to eliminate the legacy covenants associated with predecessor companies. The Board will disallow Consumer Advocate’s proposed adjustments. The Board will allow the $5.5 million adjustment related to the 1979 exchange to reverse the paper gain, as suggested by Consumer Advocate if the Board agreed with IPL's retirement of the seven series of preferred stock in 2002. The adjustment has been made in prior cases and reverses a transaction that resulted in a paper gain only to the utility with no benefit to ratepayers.

Double Leverage

In looking at a rate-regulated utility's capital structure, the Board traditionally considers the capital structure of the utility company, which includes debt, or the first layer of leverage, as well as any debt at the parent holding company level that could be used for a capital infusion into the utility, which is the second layer of leverage. Without the double leverage adjustment, the subsidiary utility company could earn a higher rate of return, as affected by the capital structure, than any utility company not in such a position.

The Board has rejected utility efforts to avoid double leverage adjustments in several cases, including Docket Nos. RPU-02-3, RPU-02-8, and ARU-02-1.

However, the Board in those cases said it would not apply double leverage mechanically in each case, but rather would examine the particular facts and circumstances in each case where the adjustment is proposed.

The Iowa Supreme Court affirmed the Board's use of double leverage on two occasions, although it is important to note the Court did not mandate that double leverage be applied in all situations. General Telephone Co., of the Midwest v. Iowa State Commerce Comm'n, 275 N.W.2d 364, 369 (Iowa 1979); United Telephone Co., v Iowa State Commerce Comm'n 257 N.W.2d 466, 479-480, 482 (Iowa 1977). The Board made a narrow exception to the application of double leverage in an Iowa Electric Light and Power rate case. In Docket No. RPU-89-3, the utility provided four factors that demonstrated how the parent's debt did not result in an increase in the utility's common equity. In other words, it was shown that the parent company's debt did not support the utility's capital structure. (Docket No. RPU-89-3, "Final Decision and Order" (4/30/1990), pp. 47-49). In Docket No. RPU-91-9, one of the factors changed so the Board once again applied double leverage.

The following is a summary of the transactions that Consumer Advocate argued should result in application of double leverage:

Alliant Energy Resources (AER) issued debt in February 2000 for about $402.5 million (nominal value); Alliant Energy guaranteed the debt. (Tr. 734). In November 2008, Alliant Energy assumed the debt, but there was no cash that flowed to Alliant Energy as a result of this transaction, and IPL itself did not assume the debt. (Tr. 693-95, 731-32, 734). Alliant Energy later submitted a tender offer with a September 28, 2009, deadline; holders tendered 99.96 percent of the notes.

Initially, Alliant Energy used $68.8 million of cash on hand and drew down a $170 million bridge loan to pay off the notes. (Tr. 736-37, 1252). Subsequently, Alliant Energy issued $250 million of five-year debt with a coupon rate of 4 percent to repay the bridge loan and to pay the additional expenses. (Tr. 735-36).

Consumer Advocate argued that this series of transactions, and particularly the final transaction that resulted in the issuance by Alliant Energy of $250 million of senior notes, should result in the application of double leverage; it was the financial strength of Alliant Energy's utility subsidiaries that helped Alliant Energy obtain this debt. (Tr. 1202-03). Consumer Advocate said that recognizing and accounting for double leverage is an attempt to more accurately reflect the capital structure of IPL and, consequently, an attempt to insure a fair rate of return determination that properly balances the interests of investors and consumers.

IPL argued that when Alliant Energy assumed the AER debt in November 2008, there was no cash that flowed to Alliant Energy that could be used to fund an equity infusion into IPL. (Tr. 693, 731-32, 734). IPL said that in no way did IPL itself ever assume, whether directly or indirectly, any right, obligation, detriment or benefit under Alliant Energy's assumption of AER's debt. (Tr. 694-95). Likewise, IPL said the funding of the tender offer (short term borrowing or funds replaced with five-year notes) was a "zero-sum process." (Tr. 736-37).

While IPL acknowledged Consumer Advocate's argument that Alliant Energy's cash on hand could be used for equity infusions into IPL, this was not the case here as none of Alliant Energy's cash on hand is attributable either to the assumed debt or to the $250 million debt issuance. IPL noted that as of the date of the hearing it would have been impossible for any cash replacing the cash on hand used in the tender offer to be used for any equity infusions because the money was deposited in Alliant Energy's bank account before the hearing began. (Tr. 739).

The proposed application of double leverage begins with AER's debt issue that Alliant Energy fully and unconditionally guaranteed in 2000. In Docket No. RPU-02-3, Consumer Advocate proposed including this debt issue as part of Alliant Energy's capital structure and then applying double leverage, because Alliant Energy guaranteed the debt. The Board denied Consumer Advocate's adjustment because the evidence showed that none of the proceeds from that debt could have been used to support the equity in Alliant Energy's utility subsidiaries. The Board said:

> Consumer Advocate in its double leverage adjustment not only included the $24 million debt issue but also included Alliant Resources' debt that is guaranteed by Alliant. This is a non-traditional use of double leverage and is contrary to the premise that the parent issues debt in order to infuse equity into a utility subsidiary. (Tr. 1610, 1699-1700). Alliant Resources is the non-regulated subsidiary of Alliant, IPL's parent. Alliant Resources' debt is kept separate from IPL and has not been used to infuse equity into IPL. Each company issues its own debt to fund its own operations. Consumer Advocate admitted that Alliant cannot use the proceeds from Alliant Resources' debt issues. (Tr. 2099-2101).

> While Alliant has fully and unconditionally guaranteed Alliant Resources' debt, IPL is not responsible for paying the debt if there is a default and none of its assets were pledged as collateral for the debt. Alliant Energy can use any source of funds it has to pay the debt in the event of a default, such as dividends or the issuance of equity or debt. IPL noted that it has several restrictions on its bonds and equity ratios such that it is unlikely that IPL could be a significant source of money for Alliant Energy to repay the debt. (Tr. 1701-1701A). Even if Alliant Energy wanted to sell some or all of IPL's assets to pay the debt, Board approval would be required pursuant to Iowa's reorganization statutes, Iowa Code §§ 476.76 and 476.77. Most importantly, the proceeds from the debt were not used to invest in the common equity of IPL or any other subsidiary, so the underlying theory behind a double leverage adjustment is not present.
> Interstate Power and Light Company, "Final Decision and Order," Docket No. RPU-02-3 (4/15/2003), pp. 59-60.

Since the Board's decision in Docket No. RPU-02-3, Alliant Energy assumed AER's debt, meaning that the debt was included on Alliant Energy's books and was part of its capital structure. More recently, the AER debt that was assumed by Alliant Energy has been largely replaced with new debt issued by Alliant Energy. Alliant Energy initially used cash on hand and a bridge loan to fund the replacement, later issuing $250 million of five-year notes.

In Docket No. RPU-02-3, the Board noted that double leverage is one regulatory tool available to help protect the utility from abuse by the parent company, but that double leverage should not be applied mechanically because of the complex nature of these relationships and transactions. Rather, the Board said it would examine the particular facts and circumstances in each case.

Here, there has been no real change from Docket No. RPU-02-3 in the sense no cash was available to invest in IPL's common equity. Because the proceeds from the debt were not used to invest in the common equity of IPL or any other subsidiary, the underlying theory behind a double leverage adjustment is not present. If there is an equity infusion into IPL after the date of the debt issuance, then double leverage might be appropriate to apply. Based on the evidence presented, there was no cash available from the issuances for an equity infusion. Double leverage will not be applied.

VII. RATE DESIGN/CLASS COST-OF-SERVICE

Design of Base Rates

IPL proposed a uniform across-the-board percentage adjustment for allocating its proposed revenue increase among customer classes. Within each customer class, this uniform percentage increase is applied by IPL to each rate classification, by pricing zone, excluding the revenue associated with the EAC, EECR, and excess facilities charges. The resulting revenue increase is then applied to the rates per kW and rates per kWh on a uniform percentage basis. IPL did not apply the uniform percentage adjustment to customer charges, because customer charges are being addressed through the rate equalization process approved by the Board in Docket No. RPU-05-3.

The Consumer Advocate and ICC generally agreed with IPL that any rate changes should be uniform percentage changes in the rates per kW and the rates per kWh. (Tr. 754-55, 849-50, 1266, 1268, 1278-79, 1282-83, 1288, 1300). LEG and Ag Processing were also in agreement concerning rate changes within customer classes, except that those two intervenors also asked for three modifications in IPL's class cost-of-service study, which will be discussed in the section immediately following.

It should be noted that, if IPL's Rider RTS[3] were approved, its method for adjusting class base rate revenues seems to have the side effect of altering IPL's class rate designs, with potentially significant billing impacts for some customers. IPL's method: 1) determines the revenue increase for each customer class based on the uniform percentage adjustment factor; 2) by rate zone, subtracts each customer class subgroup's Rider RTS transmission revenue; then 3) determines the uniform percentage increase for the class subgroup's base rate elements that will bring about the remaining revenue increase. The problem the Board sees with this approach is that when the Rider RTS class transmission rates are combined with the corresponding class base rate elements (which is how customers will experience them in terms of billing impact), the resulting percentage increases for the combined base rate elements will not necessarily be uniform; and, in some cases, will vary by a wide margin. The Board believes this potential problem can be corrected by first adjusting the class base rate elements by a uniform percentage, and then subtracting the Rider RTS class transmission rates from the corresponding class base rate elements, making the implementation of Rider RTS neutral with respect to rate design.

Although the Board deferred any decision on implementation of Rider RTS until IPL's 2010 rate case, the Board wants to address the issue regarding design of

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[3] Rider RTS is IPL's proposed transmission cost rider discussed in Section IV, Transmission Issues.

base rates here so parties will have an opportunity to review the Board's methodology and comment in the event IPL proposes the same uniform method of increasing rates in its next case. IPL's basic proposal for increasing base rates by a uniform percentage is sound, but the refinements offered by the Board appear to ensure that the initial implementation of Rider RTS would be neutral with respect to rate design. The Board envisions that if Rider RTS is approved in a subsequent proceeding, it would thereafter be adjusted independently, apart from base rates – similar to adjustments for the EAC, EECR, and interruptible credits.

Class Cost of Service (CCS)

IPL conducted a CCS study, but recommended that the results of the study not be implemented in this proceeding. IPL filed its CCS study for informational purposes only, and has not based its proposed revenue allocation on the results of the study. IPL instead proposed using a uniform across-the-board percentage for allocating its proposed revenue increase among customer classes.

As part of its rate equalization plan, IPL outlined a process in Docket No. RPU-04-1 that would not shift revenues among customer classes based on a CCS study until rates had been fully equalized. Since the rate equalization process will not be completed by the conclusion of this proceeding, IPL recommended the Board not use the results from the CCS study to allocate the final revenue increase among customer classes. (Tr. 754). IPL stated that its position is consistent with what the Board approved in prior proceedings (Docket Nos. RPU-04-1 and RPU-05-3) and that both Consumer Advocate and ICC have generally accepted IPL's proposed uniform percentage adjustment among customer classes. IPL proposed to review and address any CCS issues after the rate equalization and tariff consolidation process has been concluded. (Tr. 792).

IPL argued that it is premature to litigate CCS issues in this case, since IPL's proposed final rates are not based upon the results of a CCS study. IPL pointed out that while Consumer Advocate witness Wilson's rebuttal testimony illustrates possible approaches for changing IPL's allocation methodologies, Consumer Advocate is not proposing an alternative CCS study at this time. (Tr. 1276). LEG proposed three substantial changes to IPL's CCS and argued that rates should reflect those changes, but IPL notes that LEG has not provided an alternative CCS study based on its changes for review in this proceeding. (Tr. 793). IPL concluded that there is no evidence in the record that shows the customer impacts of the alternative cost allocation methods proposed by LEG.

Consumer Advocate also noted that LEG proposes that rate changes in this case should be based on the CCS study prepared by IPL, with three significant changes to the cost allocation methodology. (Tr. 1359-60, 1362-66). However, Consumer Advocate noted that LEG agrees that IPL should adjust its base rates by a uniform percentage if the Board does not adopt a CCS study in this proceeding. (Tr. 1366).

Consumer Advocate provided some history of IPL's rate equalization process and said the Board initiated an intended five-year revenue-neutral rate equalization process in Docket No. RPU-04-1. In subsequent proceedings, Consumer Advocate maintained that the Board made it clear that it would not base its determination of IPL' s rates on any CCS study until the rate equalization process was complete.[4] Consumer Advocate pointed out that IPL has not completed its rate equalization process. (Tr. 243, 754, 849-50). Consumer Advocate said that on May 26, 2009, the Board granted IPL's motion to delay implementation of the fourth-step of its rate equalization, which was later implemented at the time IPL's winter rates began in September. Consumer Advocate said the Board should not apply the results of IPL's CCS study, or any other CCS study (either with or without the modifications proposed by LEG). Instead, Consumer Advocate asked that the Board adopt IPL's uniform percentage adjustment approach.

ICC said that in accordance with IPL's proposal, any increase in IPL rate revenues should be distributed on a uniform percentage basis. Along with the reasons advanced by IPL, ICC said that it would be too speculative, unreliable, and inherently unfair to adopt a class cost allocation based on the CCS study filed by IPL in this proceeding (which was filed for informational purposes only). ICC maintained that it would be more reasonable to wait until rate equalization is completed before taking on the likely contentious issues associated with changing class allocations based on a new CCS study.

[4] See Interstate Power and Light Co., Docket No. RPU-05-3, slip op. at 2-3, 5, 11 (April 28, 2006) and slip op. at 7-8, (June 7, 2006) (Order on Rehearing).

Regarding IPL's CCS study, ICC noted that IPL calculates its Bulk Power class tariff revenues with the assumption that part of the load will be interruptible, but does not add back the interruptible credits associated with these Bulk Power customers in determining the cost of service for the Bulk Power class. ICC's witness testified that this oversight results in an approximate $5 million per year overstatement of cost of service for the Bulk Power class. (Tr. 1301). ICC said that this testimony is un-rebutted and therefore any increase in revenues should be distributed on a uniform percentage basis, with interruptible credits credited back to the Bulk Power class. (Tr. 793, 816). IPL acknowledged ICC's point about the treatment of Bulk Power interruptible credits, but explained that it has no relevance in this proceeding since IPL is not proposing any CCS study for cost allocation purposes.

LEG said that its primary focus in this docket is to ensure that final rates approved by the Board are based on customer CCS with no subsidies among customer classes. (Tr. 1359). LEG noted that this focus is firmly rooted in the established law governing electric utility rate design and class cost allocation.

LEG pointed out that the Board's rules establish mandatory rate design and cost study requirements applicable to electric rates subject to the Board's regulatory jurisdiction. 199 IAC 20.10. LEG cited the first paragraph of subrule 20.10(2) as establishing the following general principle:

> Rates charged by an electric utility for providing electric service to each class of electric consumers shall be designed, to the maximum extent practicable, to reasonably reflect the costs of providing electric service to the class.

> The methods used to determine class costs of service shall to the maximum extent practical permit identification of differences in cost-incurrence, for each class of electric consumers, attributable to daily and seasonal time of use of service, and permit identification of differences in cost-incurrence attributable to differences in demand, energy, and customer components of cost.

LEG said that 199 IAC 20.10(2) was promulgated by the Board pursuant to federal law; specifically, PURPA. LEG stated that PURPA required each state regulatory authority to consider and, if deemed appropriate by such authority, adopt certain federal ratemaking and cost-of-service standards applicable to rate-regulated electric utilities. (16 U.S.C. §§ 2621, 2625(a)). LEG noted that the ratemaking standards in subrule 20.10(2) were adopted by the Board at the conclusion of a rule making proceeding (Docket No. RMU-80-1) conducted to discharge the Board's PURPA obligations. LEG pointed out that the three goals of the PURPA rate design standards are: (1) conservation of energy supplied by electric utilities; (2) the optimization of the efficient use of facilities and resources of electric utilities; and (3) equitable rates to electric consumers. At the time subrule 20.10(2) was adopted, LEG said that the Board found that all three PURPA goals were furthered by the rule.

LEG stated that IPL's CCS study is the only such study in the record because no other party submitted a CCS study. Because IPL has chosen not to use its study for the purpose of allocating its revenue requirement among customer classes, but instead has elected to allocate its revenue requirement on a "uniform across-the-board percentage" basis, LEG argued that the class rates proposed by IPL do not reasonably reflect the costs of providing electric service to the classes.

LEG proposed three modifications to IPL's CCS study and urged the Board to use the modified study as the basis for allocating IPL's revenue requirement to IPL's customer classes. (Tr. 1362, 1365-1366). LEG's proposed the following exceptions and modifications:

1. The Average and Excess Demand (AED) used to allocated generation costs in IPL's CCS study should be modified to exclude interruptible load from peak demand. (Tr. 1364). IPL's CCS study allocates generation costs on the basis of a hypothetical peak demand estimate of class demand that includes interruptible loads. This approach ignores the fact that interruptible load is not contributing to firm peak demand, which is the basis for additional generation capacity.

2. The AED in IPL's study should be further modified to remove the Lighting class from the allocation of peak generation costs because of the primarily off-peak nature of Lighting usage. IPL's CCS study treats the Lighting customer class as if the peak for the class occurs in the afternoon at the time of IPL's coincident peak. This totally unrealistic assumption results in the unreasonable and unfair allocation of a significant portion of generation costs to the Lighting class. (Tr. 1364-65). As a result, municipalities, including one of LEG's members (the City of Cedar Rapids), pay Lighting rates that are significantly higher than their cost of service.

3. LEG preferred that IPL continue using the AED method for allocating transmission costs as it has in past cases, rather than the 12 monthly coincident peaks (12-CP) used in this study.

However, LEG recognized that MISO allocates its monthly transmission charges on the basis of monthly coincident peaks (Tr. 784, 1363), and for that reason would not object if the Board were to approve the 12-CP method for allocating transmission costs. (Tr. 1414).

LEG pointed out that IPL's rates were last based on a CCS study in IPL's 2002-2003 rate case, Docket No. RPU-02-3. (Tr. 808). In every subsequent IPL rate case since then, LEG said that IPL's revenue requirement has been allocated to rate classes on a uniform percentage basis rather than by a CCS study. (Tr. 808-09). LEG argued that there is no basis for believing that the rates currently in effect or proposed by IPL in this docket show any reasonable relationship to IPL's CCS study as modified by LEG. LEG maintained that IPL's proposed rates are inherently inequitable and create cross-subsidies among classes.

LEG emphasized that while it has been six years since the 2003 implementation of rates approved in Docket No. RPU-02-3, when IPL's rates last reflected a CCS-based allocation of IPL's revenue requirement, IPL does not plan to propose a CCS-based allocation of its revenue requirement in the rate case it will file in March 2010. LEG said that IPL argued this is because rate equalization will not have been accomplished until later in 2010 (and possibly later than that). (Tr. 132, 290-91, 808-09). LEG pointed out that when asked at hearing whether IPL plans to file a rate case in 2011, IPL witness Madsen answered, "At this point I hope not." (Tr. 292). LEG said that if one assumes that IPL files a rate case in 2012 and rate equalization has been completed, the earliest time at which IPL's rates would reflect a cost-based allocation would be four years from now, in 2013, meaning that for a period of ten years IPL's rates will not have been based on a CCS study.

LEG noted that IPL and Consumer Advocate offer the same rationale for rejecting a cost-based allocation of IPL's revenue requirement in this case; namely, that the rate-equalization process initiated in Docket No. RPU-05-3 was incomplete. However, LEG argued that at the time of the Board's RPU-05-3 decision in 2006, it was assumed that the rate equalization process would be complete in four more years, at which time CCS revenue realignments would be addressed.[5] However, LEG said it has shown that at the earliest it will be four more years (2013) before IPL's rates will be based on CCS. LEG maintained that this significant change in circumstances warrants a different decision on class allocation methodology from the one the Board reached in Docket No. RPU-05-3.

The Board previously decided not to shift customer class revenue requirements based on the CCS studies presented in Docket Nos. RPU-04-1 and RPU-05-3, prior to completion of the IPL rate equalization process. The purpose of this was to avoid compounding equalization increases with increases from class cost realignments. Step 4 of the 5-step equalization process was implemented on

[5] In re: Interstate Power and Light Company, “Final Decision and Order,” Docket No. RPU-05-3, at 4, 6, 10-11 (IUB Apr. 28, 2006).

September 16, 2009. Step 5 is expected to be filed next year, and its impacts will probably interact with IPL's anticipated 2010 rate case, as Step 4 has with the current proceeding.

LEG noted that none of the parties opposing LEG's position address the ratemaking standards in the Board's rules, as discussed in LEG's initial brief. This is probably because the Board's ratemaking standards in rule 199 IAC 20.10 were previously addressed in the earlier stages of the rate equalization process, in Docket Nos. RPU-04-1 and RPU-05-3. In those dockets, many of the same arguments with respect to rule 199 IAC 20.10 made by LEG in this proceeding were made by LEG's associated organization, the Community Coalition for Rate Fairness (CCRF). (Tr. 1364). In addressing this issue in Docket No. RPU-04-1, the Board stated:

> Class cost-of-service studies are a useful guide in setting rates, but such studies are not the only consideration in setting just and reasonable rates. Subrule 199 IAC 20.10(1) allows the Board to waive strict adherence to its ratemaking standards and the Board's rules do not specifically require a utility to file a new class cost-of-service study if there are no proposed changes in rate design. (Docket No. RPU-04-1, "Final Decision and Order," January 14, 2005, p. 17).

Again, in Docket No. RPU-05-3, the Board stated:

> The Board continues to believe that the class revenue relationships established in Docket No. RPU-04-1 should be preserved to avoid combining the rate impacts from potential inter-class revenue shifts and intra-class rate equalization. The principle of cost-based rates must be balanced with other ratemaking principles, such as the avoidance of unnecessary rate shock. CCRF has not persuaded the Board that the issues related to class cost-of-service and the baseline assumptions from Docket No. RPU-04-1 should be relitigated in this proceeding. (Docket No. RPU-05-3, "Final Decision and Order," April 28, 2006, p. 11).

IPL, Consumer Advocate, and ICC have adhered to the Board's previous decisions in Docket Nos. RPU-04-1 and RPU-05-3, and have advocated no changes in CCS allocation. Thus, competing CCS positions have not been fully developed in this case. A full litigation of CCS issues might have led to the fuller development of alternative class allocation methods by other parties, which might have been significantly different from those proposed by LEG.[6] Two of the modifications to IPL's AED allocation method proposed by LEG (i.e., excluding interruptible load from peak demand, and removing the Lighting class from the allocation of peak generation costs) were unsuccessfully sponsored in previous IPL rate cases; and the impacts of these changes on IPL's CCS study results in this case have not been presented.

IPL's unadjusted informational CCS study suggests lower than average increases in General Service and Lighting class revenue requirements (i.e., 11.5 percent compared to 19.4 percent overall), and a significantly higher than average increase (34.7 percent) for the Bulk Power class. (Ex. DV-1, Sch. I, page 8, line 27).

The Board is not persuaded to depart here from its previous practice of not implementing CCS revenue requirement shifts among customer classes until the IPL rate equalization process is completed, especially given the lack of a full record on competing CCS methods and their potential class impacts. Because of the Board's prior decisions, the Board did not expect arguments on CCS to be fully developed by parties in this proceeding.

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[6] The rebuttal of LEG's proposed CCS modifications by Consumer Advocate witness Wilson suggests that Consumer Advocate would have argued for a significantly different methodology than LEG. (Tr. 1266-76).

However, the Board recognizes that rate equalization will probably be completed during the pendency of IPL’s next rate proceeding. IPL will be required to file a CCS study in its next rate proceeding, along with testimony supporting any class cost realignments it proposes to make based on the CCS study. Other parties should also submit alternative CCS studies, if they desire, or propose adjustments to IPL’s study and their potential class impacts that they want to implement in future rates. With a fully developed record, the Board can consider CCS issues. The Board will examine the issues and might implement CCS changes in the next proceeding, decide not to make any CCS changes until the next rate case after rate equalization, determine CCS changes but not implement those changes until sometime after equalization is complete, or some other alternative. In determining whether any class cost realignments based on a new CCS study are appropriate, the Board will balance the impacts of rate equalization and the upcoming rate proceeding.

Design of Regional Transmission Service Clause (Rider RTS)

While the Board deferred a decision on whether to implement a RTS until IPL's upcoming rate case, the Board will briefly discuss the design of the RTS, if one is ultimately adopted by the Board. IPL proposed to allocate its annual transmission expense to customer classes based on the AED allocation methodology, which is consistent with how transmission expense has historically been reflected in IPL's base rates. By allocating according to this methodology, there should be no shift in transmission cost responsibility among customer classes.

According to IPL, the Rider RTS factors would be revised annually, similar to IPL's EECR factors. IPL proposed to file its revised Rider RTS factors in November of each year going forward, to become effective in January for the next year. Among other things, IPL said the revised factors will include a true-up based on 12 calendar months of actual data from November of the prior year through October of the current year, reconciling the actual transmission costs attributable to the Iowa retail jurisdiction with the actual cost recovery from the rider. IPL noted that any refunds related to the ATA from Docket No. SPU-07-11 will be passed through as a reduction to the transmission expense projections. (Tr. 767).

LEG argued that if the Board decides to approve IPL's proposed Rider RTS, the per kW demand charges should be cost-based by voltage delivery level. LEG said that IPL proposed to develop the Rider RTS transmission adjustment factor for the LGS class by reducing LGS base rate demand charges to remove estimated transmission costs from existing base rates, and replacing this with a separate $3.92/kW Rider RTS adjustment factor for the LGS class. However, LEG argued that this could result in an inadvertent rate increase for LGS customers that currently benefit from primary service discounts (ranging from 4.42 to 10 percent depending on delivery voltage level). By removing transmission costs from existing base rates and transferring them to the Rider RTS adjustment factor, LEG maintained that LGS primary service customers could lose their primary service discounts on the portion of demand charges removed from base rates. (Tr. 1375).

LEG said the problem can be solved by including the LGS primary service discount in the Rider RTS tariff as well. (Tr. 1375; Ex. RJL-1, Sch. 4). IPL agreed to this solution at hearing. (Tr. 813-15). In its reply brief, IPL said it would add the following language to the bottom of the Rider RTS Tariff Sheet No. 86 to address LEG's issue: "Large General Service RTS charges shall be included with base rate demand charges in the application of primary service and power factor provisions of the Large General Service tariff."

The language proposed by IPL resolves the current dispute over the Rider RTS rate design. Any proposal for a Rider RTS in a subsequent rate proceeding should include the language proposed by IPL so that any objections to the language can be made in that proceeding. The Board cannot approve the rate design now because a decision on the rider itself has been deferred. However, unless a new objection is raised, it appears that the rate design of the rider might not be an issue in the next IPL rate case.

Large General Service (LGS) Tariff Changes

The parties do not contest IPL's proposed changes to the LGS tariff. IPL accepted a wording change suggested by LEG, which inserts the phrase "less than" to the following proposed tariff language: "4.42 % for 4,160 volts to less than 34,500 volts." (Tr. 1376). A similar wording change would apply in IPL's Rider SSPS. With IPL's assent to the change, there is no contested issue regarding proposed LGS tariff changes, except for creation of the Rider RTS that would apply to all rate classes, which was addressed separately in Section IV of this order.

The purpose of IPL's proposed LGS changes is to extend primary service discounts to all customers that receive voltage at 34.5 kV, and not just to those 34.5 kV customers in locations where the 34.5 kV system functions as transmission. The changes are appropriate given that essentially all of the 34.5 kV system has been conveyed to ITC Midwest, and is now transmission by definition. (Tr. 771). LEG's language change ensures that customers with 34.5 kV (34,500 volt) service will unambiguously qualify for the 7.5 percent primary service discount, which applies to "69,000 and 34,500 volt service," rather than the 4.42 percent discount. (Tr. 1376-77; Ex. RJL-2, Sch. 2). LEG withdrew a request for a second tariff modification change after IPL's witness explained reason for the language in question. (Tr. 809-11, 1377). The Board will approve the LGS tariff changes. IPL is to submit an LGS compliance tariff with the modification suggested by LEG and agreed to by IPL.

Bulk Power Service Tariff Changes

IPL proposed several uncontested changes to the Bulk Power tariff. The most significant of these changes would extend Bulk Power service to all eligible LGS customers beyond the IPC rate zone. To effect this proposed change in a revenue-neutral manner, it appears that IPL is proposing to transfer to Bulk Power the billing determinants and revenues of LGS customers expected to transfer to the Bulk Power class (Tr. 776), which seems to have the effect of partially shifting LGS revenue responsibility to the Bulk Power class, resulting in an additional increase in Bulk Power rates beyond the uniform percentage increase. (Ex. DV-1, Schs. A, G). However, as it stated in Docket No. TF-06-336, the Board continues to believe that the best venue for addressing long-term changes to Bulk Power is in a general rate case where potential CCS and revenue effects can be assessed together.[7] Therefore, IPL's proposal to extend Bulk Power service to all eligible LGS customers beyond the IPC rate zone will be deferred to IPL's next rate case where the potential CCS and revenue effects can be assessed together.

As with the LGS tariff changes, LEG proposed a clarifying wording modification that was accepted by IPL. (Tr. 794). LEG's proposed modification clarifies that the Bulk Power tariff applies to transmission voltage of 34.5 kV or above because with the sale of IPL's transmission system to ITC Midwest, transmission voltage is defined as 34.5 kV and above. (Tr. 1379). With IPL's assent to the change, there is no contested issue regarding proposed Bulk Power changes tariff changes, except for creation of the RTS Rider that would apply to all rate classes, which was addressed separately in Section IV of this order.

Other uncontested changes to the Bulk Power tariff include making Bulk Power customers eligible for interruptible service. The Board will approve the Bulk Power tariff changes, but its availability will continue to be limited to the IPC rate zone until the potential CCS and revenue effects can be assessed together in IPL's next rate case. IPL is to submit a Bulk Power compliance tariff with the remaining uncontested changes, including the modification suggested by LEG and agreed to by IPL.

[7] Docket No. TF-06-336, "Order Approving Tariff with Changes," (August 13, 2007) p.8.

Standby and Supplementary Power Service (SSPS) Changes

IPL proposed to increase its monthly charge for standby transmission reservation service, from $2.14 to $3.95 per kW, corresponding to IPL's increased transmission service costs from ITC Midwest. ICC and LEG objected to the increase, and argued that the transmission reservation charge should be reduced to 5 percent of its proposed level (i.e., reduced to about $0.1975 per kW). None of the parties objected to any of IPL's other proposed tariff changes, which include an increase in the reactive demand charge.

ICC proposal to drastically reduce transmission reservation charges for standby customers is based on its contention that the same approach used to develop standby reservation charges for generation should be used for standby transmission reservation charges. (Tr. 1307). IPL disagreed, arguing that there are significant differences between the costs a utility incurs for standby generation versus standby transmission. Given that there is a liquid market to purchase generation, IPL said it does not have to build its generation portfolio to serve its standby customers' entire contracted load, and can consider factors such as outage rates and diversity. However, unlike generation, IPL states that it must ensure the transmission system is designed to accommodate the contract demands of standby customers, which can occur at any time.

IPL also maintained that ITC Midwest's future investment decisions regarding the transmission system will be based, in part, on standby contract demands. IPL noted that it has used the same methodology to calculate transmission reservation charges since 2003, and its methodology has not been challenged until this proceeding.

IPL argued that allowing standby customers to pay less than full transmission rates would result in subsidization between retail and standby customers. (Tr. 797). If ICC's proposal is accepted, IPL calculated that there would be a $3.7 million reduction in transmission revenues from standby customers. (Tr. 799). IPL noted that this cost shift would have to be borne by IPL's other retail customers.

ICC and LEG argued that IPL failed to justify its 85 percent increase in transmission reservation charges for standby customers. ICC and LEG noted IPL's argument that its generation reservation charges are determined on a different basis than its transmission reservation charges, given that there is a liquid market to purchase generation. However, ICC and LEG contended that this argument fails to recognize that the rationale for designing standby reservation charges (for both generation and transmission) long pre-dates the development of a "liquid market" for generation. ICC and LEG claimed that the emergence of MISO and organized wholesale generation markets have nothing to do with the reliability of standby customer-owned generation, or the probability of standby customers using the transmission system during peak times. (Tr. 1319).

ICC and LEG believed that nothing in the record demonstrates IPL's suggestion that ITC Midwest's transmission system is designed to serve 100 percent of standby customer load. ICC and LEG said that IPL claims that it provides ITC Midwest the contract demand levels of its standby customers, and makes the unrealistic assertion that ITC Midwest plans the transmission system as if the full level of that contract demand was using the system at the time of monthly system peak. However, ICC and LEG argued that the testimony offered by IPL does not support the claim that ITC Midwest invests and incurs costs on that basis and, in fact, utilities factor in the reliability of customer-owned generation and the probability of standby customers being on the system at the time of system peak. (Tr. 1341-43).

IPL countered that ICC's and LEG's proposal would not result in a reduction in the transmission expenses incurred by IPL. IPL said that ITC Midwest's revenue requirement would not change as a result of the intervenors' proposal since the revenue requirement reflects the full capacity requirements of standby reservation. IPL suggested that ICC and LEG were attempting to confuse the issue of how ITC Midwest charges IPL for the use of its transmission system versus the investment required to build and maintain a reliable transmission system. IPL pointed out that the transmission capacity is continuously available whether or not it is utilized by the standby customers; and the transmission service "stands by" to meet the immediate needs of these customers. IPL said the transmission system must not only meet the instantaneous needs of IPL's full requirements customers, but also provide for the reservation contract demands of its standby customers. (Tr. 799-800). IPL noted that ICC's witness acknowledged differences between transmission and generation reserves and costs at hearing. (Tr. 1345-47).

IPL believed that the intervenors' proposal created confusion surrounding the difference between the costs associated with the design of a transmission system and the billing units upon which those costs are recovered. While IPL acknowledged that the billing units it incurs from ITC Midwest are based on actual peak loads, it also asserted this was different than the assumptions used to design and build the system. IPL pointed out that its witness Bauer testified that ITC Midwest uses scenarios in which the contracted loads from standby customers are used to design and build the system. (Tr. 829-34). Because this is the way the system is designed and built, IPL said this standby capacity is part of what causes the costs of transmission and should be borne by those customers on standby service. Unlike generation resources, IPL noted that there are no peaking transmission resources and that the costs standby customers place on generation resources and transmission resources are different.

In response to IPL's arguments, ICC and LEG argued that the implication that ITC Midwest plans and constructs its transmission system as if it were serving IPL's standby customers continuously at full contract demand levels, and that ITC Midwest's costs reflect this, is not realistic. (Tr. 1342-43). In any event, ICC and LEG said that IPL's standby transmission customers should not be held responsible for any "gold plating" of the transmission system undertaken by ITC Midwest. Also, ICC and LEG pointed out that ITC Midwest does not bill IPL for standby transmission expense based on standby contract demand levels, but rather the billings are based on actual monthly peak loads, when the standby customers may or may not be on the system. (Tr. 827-28, 831).

The focus of the dispute regarding IPL's standby transmission reservation charge appears to be whether the ITC Midwest transmission system serving IPL is designed to accommodate the full combined contract demands of IPL's standby transmission customers. IPL contends that ITC Midwest plans its system this way. ICC and LEG argue that it does not and that IPL has not presented evidence demonstrating that it does. However, IPL witness Bauer describes the ITC Midwest planning process as including the contract demands of standby customers, to ensure that ITC Midwest has adequate facilities to serve 100 percent of IPL's potential load at time of system peak, regardless of the likelihood of that load occurring; and that this capability is built into the cost structure of providing transmission service to IPL. (Tr. 833-86). In contrast, ICC's assertions about ITC Midwest system planning seem based on general observations rather than specific knowledge about the ITC Midwest system or its planning practices. (Tr. 1334-42).

How ITC Midwest plans its system is important because it reflects how the system is ultimately built, which determines the ITC Midwest revenue requirement. ICC emphasizes the fact that IPL is billed according to its actual monthly demand, rather than its maximum potential demand. However, ITC Midwest's billing is not necessarily related to how its revenue requirement is determined. Also, how IPL is billed externally does not necessarily determine how it should allocate its billing costs internally.

The most persuasive evidence in this proceeding is that ITC Midwest's planning and the resulting revenue requirement are based on maximum potential demand, (including the contract demands of IPL's standby transmission customers), which means that standby customers should pay the rate proposed by IPL because that rate represents the costs incurred to serve those customers. There is no evidence in this proceeding of "gold-plating," as LEG and ICC suggested in brief. The Board finds IPL's specific testimony regarding ITC Midwest's planning process (Tr. 829-43) more persuasive than ICC's more general testimony. (Tr. 1334-47). Also, the Board believes that there are differences in generation and transmission with respect to costs and planning for standby customers, and ICC and LEG proposal does not reflect or acknowledge those differences, although they were discussed at hearing. (Tr. 1345-47). The Board will approve IPL's proposed increase in standby transmission reservation charge and its uncontested SSPS tariff changes, adjusted to reflect the transmission costs and revenue requirement approved in this proceeding.

Other Uncontested Changes

Several other uncontested tariff changes will be approved. There are two uncontested changes to the General Service tariff. First, for new customers requesting 3-phase service, IPL would assess an additional monthly customer charge of $45, instead of the current practice of assessing a $45 excess facilities charge for the additional transformation needed to provide 3-phase service. This change will not apply to existing 3-phase customers. IPL said the change in policy is intended to make the $45 charge more understandable to customers and to streamline tariff administration. Second, IPL proposed to eliminate the minimum kVA billing demand provision for 3-phase farm customers served under Rate 820, which IPL said would have no detrimental impact on customers. (Tr. 769-70).

There are several uncontested changes to the interruptible service tariff. First, IPL proposed to eliminate the monthly $80.92 administration and dispatching charge that applies only to interruptible customers in the IPC pricing zone. Since interruptible customers are jointly dispatched and administered, IPL said there is no cost justification for this separate charge. The second and third changes would eliminate separate provisions for applying primary service discounts and determining billing demands for IPC zone customers. These changes are reflected in the test year billing determinants. IPL stated that most of the affected customers will benefit from these changes. IPL also said that only two customers will be negatively impacted and these customers could reasonably mitigate the impacts by reducing their summer billing demands. (Tr. 771-74, Ex. DV-1, Sch. F).

There is one uncontested change to the Day Ahead Hourly Pricing tariff. Consistent with what was done in a previous rate case (Docket No. RPU-05-3), IPL wants customer baseline usage to be recalibrated to reflect usage during the 2008 test year. (Tr. 777).

Compliance Tariffs and 2009 Offset

The current electric rates paid by IPL customers should not change as a result of the Board’s decision. As noted previously, IPL has notified the Board of its plans to file for an electric rate increase in 2010. Therefore, the Board will not require IPL to file compliance tariffs in this proceeding. Instead, IPL may continue to use its temporary rate tariffs in this proceeding until temporary rates in the upcoming rate case become effective. This should reduce the cost and administrative burden on IPL, the Board, and intervenors.

Earlier, the Board authorized IPL to use a portion of the ATA regulatory account to reduce the 2009 transmission adjustment to a level that reduces the final revenue increase in this case to the revenue level allowed in temporary rates. On an annual basis, the reduction would total approximately $8 million, based on an approximate $91.6 million revenue increase allowed in this proceeding. IPL is directed to use from the ATA only the amount necessary to cover the additional revenue that would be received up until the date temporary rates in the upcoming 2010 rate proceeding are effective. If compliance tariffs were filed, the Board estimates that they would be effective on or about February 10, 2010. The Board will direct IPL to base the ATA offset for the 2009 transmission adjustment on an increase in revenue from February 10, 2010, through the implementation of temporary rates in the 2010 rate proceeding. If IPL decides not to file a 2010 case on or before May 1, 2010, IPL shall notify the Board immediately and the Board will consider further direction on the use of the ATA offset for 2009 transmission costs.

VIII. FINDINGS OF FACT

Based on a thorough review of the entire record in these proceedings, the Board makes the following findings of fact:

1. A 21.9 day collection period lag is reasonable.

2. It is reasonable to allow $1,235,703 for enhanced 401(k) contributions.

3. A two-year average for pension expense is reasonable.

4. A two-year average for other post-employment benefit costs is reasonable.

5. It is not reasonable to allow recovery of any costs associated with IPL's variable pay plan.

6. It is not reasonable in this proceeding to adopt accelerated depreciation for existing electric meters.

7. It is reasonable to allow recovery of $26,549,298 in SGS Unit 4 cancellation costs, amortized over five-years, with the amortization funded by the DAEC regulatory liability account. It is not reasonable to include the unamortized balance in rate base.

8. It is reasonable to allow recovery of approximately $3.3 million in severance costs, amortized over four years.

9. It is reasonable to give IPL's ratepayers the benefits of $2.4 million in savings from matching 401(k) contributions and furloughs, amortized over four years.

10. It is not reasonable to impose a management efficiency penalty.

11. It is reasonable to allow recovery of 2008 transmission true-up costs, amortized over a five-year period, with the amortization funded by the

ATA regulatory liability account. It is not reasonable to include the unamortized balance in rate base.

12. Recovery of 2009 transmission costs, with up to $8 million of those costs funded by the ATA regulatory liability account, is reasonable.

13. It is not reasonable to allow recovery of 2010 transmission costs.

14. It is reasonable to defer a decision on IPL's proposal for an automatic adjustment mechanism for transmission rates to IPL's next rate proceeding.

15. A 10.5 percent return on equity is reasonable.

16. It is reasonable to adopt a 13-month average capital structure.

17. It is reasonable to allow one adjustment to IPL's preferred equity to reverse a $5.5 million paper gain in 1979, but unreasonable to allow other adjustments to preferred equity because IPL's retirement of seven series of preferred stock is reasonable.

18. It is not reasonable to apply double leverage based on the facts in this proceeding.

19. It is reasonable to adopt IPL's proposal for a uniform across-the-board percentage adjustment for allocating its revenue increase among customer classes.

20. It is not reasonable to adopt CCS revenue requirement shifts among customer classes in this proceeding.

21. It is reasonable to defer a decision on IPL's proposal to extend the availability of Bulk Power service beyond the IPC rate zone to IPL's next rate proceeding.

22. It is reasonable to adopt IPL's other Bulk Power and Large General Service and Bulk Power tariff changes.

23. It is reasonable to adopt IPL's method for determining the monthly charge for standby transmission reservation service.

24. It is reasonable to adopt IPL's other uncontested tariff changes.

IX. CONCLUSIONS OF LAW

The Board has jurisdiction of the parties and the subject matter in this proceeding, pursuant to Iowa Code chapter 476 (2009).

X. ORDERING CLAUSES

IT IS THEREFORE ORDERED:

1. The proposed tariffs filed by Interstate Power and Light Company on March 17, 2009, identified as TF-2009-0048 and TF-2009-0049, and made subject to investigation in this proceeding, are declared to be unjust, unreasonable, and unlawful.

2. Consistent with the discussion in the body of this order, IPL will not be required to file compliance tariffs. The ATA regulatory liability account shall be used to offset 2009 transmission costs as detailed in the body of this order. Schedules A through G are incorporated into this order by reference.

3. Motions and objections not previously granted or sustained are denied or overruled. Any argument in the briefs not specifically addressed in this order is rejected either as not supported by the evidence or as not being of sufficient persuasiveness to warrant comments.

4. This order constitutes the final decision of the Utilities Board in Docket No. RPU-2009-0002.

UTILITIES BOARD

/s/ Robert B. Berntsen

/s/ Krista K. Tanner

ATTEST:

/s/ Judi K. Cooper
Executive Secretary

/s/ Darrell Hanson

Dated at Des Moines, Iowa, this 19th day of January 2010.

Interstate Power and Light
Revenue Requirement
Test Year Ended December 31, 2008

Line No.	Description (A)			
1	Rate Base	1,505,263,347	315,686,205	
2	Rate of Return	8.763%	9.620%	
3	Return On Rate Base	131,906,227	30,369,013	162,275,240
4	2008 Net Operating Income			108,785,834
5	Income (Excess) Deficiency			53,489,406
6	Tax Effect			38,055,016
7	Revenue (Excess) Deficiency			91,544,422
8	Operating Revenue			1,184,658,758
9	Percent Increase/Decrease			7.73%
10	REVENUE REQUIREMENT			1,276,203,180

Interstate Power and Light
Revenue Requirement
Test Year Ended December 31, 2008

Line No.	Description (A)			
1	Rate Base	1,505,196,308	315,686,205	
2	Rate of Return	8.763%	9.620%	
3	Return On Rate Base	131,900,352	30,369,013	162,269,365
4	2008 Net Operating Income			113,364,932
5	Income (Excess) Deficiency			48,904,433
6	Tax Effect			34,793,039
7	Revenue (Excess) Deficiency			83,697,472
8	Operating Revenue			1,184,658,758
9	Percent Increase/Decrease			7.07%
10	REVENUE REQUIREMENT			1,268,356,230

INTERSTATE POWER AND LIGHT COMPANY
IOWA ELECTRIC UTILITY
COST OF SERVICE
YEAR ENDED DECEMBER 31, 2008

Line No.	Description	(a) Actual Test Year Results	(b) Adjustments	(c) Adjusted Test Year Results	(d) Additional Revenues Required to Yield 8.912%	(e) Total Revenues Required to Yield 8.912%
					6.9%	
1	Operating revenues	$ 1,223,995,573	$ (39,336,814)	$ 1,184,658,758	$ 83,697,471	$ 1,268,356,229
	Operating expenses:					
2	Operation expenses	803,418,321	17,582,555	821,000,876		821,000,876
3	Maintenance expenses	61,997,053	(5,496,672)	56,500,382		56,500,382
4	Depreciation and amortization	107,757,008	19,055,084	126,812,092		126,812,092
5	Property taxes	37,553,243	(10,450)	37,542,792		37,542,792
6	Miscellaneous taxes	7,500,439	175,499	7,675,938		7,675,938
	Income taxes -					
7	Current federal	(1,305,488)	(9,074,128)	(10,379,616)	26,331,224	15,951,608
8	Current state	8,875,754	(5,205,049)	3,670,705	8,461,814	12,132,519
9	Deferred	41,051,656	(10,710,693)	30,340,963		30,340,963
10	Investment tax credits	(1,870,306)	0	(1,870,306)		(1,870,306)
11	Total operating expenses	1,064,977,679	6,316,147	1,071,293,826	34,793,038	1,106,086,864
12	Operating income	$ 159,017,894	$ (45,652,961)	$ 113,364,932	$ 48,904,433	$ 162,269,365
	Rate Base:					
13	Emery Generating Station	$ 315,686,205	$ -	$ 315,686,205		$ 315,686,205
14	All Other	1,352,530,375	152,665,932	1,505,196,308		1,505,196,308
15	Total Rate base	$ 1,668,216,580	$ 152,665,932	$ 1,820,882,513		$ 1,820,882,513
16	Cost of Capital:	9.532%		6.226%		
17	Emery Generating Station					**9.620%**
18	All Other					**8.763%**

INTERSTATE POWER AND LIGHT COMPANY
IOWA ELECTRIC UTILITY
THIRTEEN MONTH AVERAGE
RATE BASE
YEAR ENDED DECEMBER 31, 2008

Line No.	Description	(a) Workpaper Reference	(b) Thirteen Month Average	(c) Adjustments	(d) Adjusted Rate Base
	Investment in plant:				
1	Utility plant in service	C-1	$ 3,455,034,082	$ 398,782,712	$ 3,853,816,794
2	Accumulated provision for depreciation and amortization	C-2	(1,590,240,673)	(167,990,229)	(1,758,230,902)
3	Accumulated deferred income taxes	C-3	(232,230,166)	(65,745,410)	(297,975,576)
4	Customer advances for construction	C-4	(4,315,069)	-	(4,315,069)
5	Customer deposits	C-5	(3,226,512)	-	(3,226,512)
6	Unclaimed Property	C-6	(13,160)	-	(13,160)
7	Accumulated provision for uncollectibles	C-7	(1,291,235)	427,813	(863,423)
8	Accrued liability for property insurance, workers compensation insurance and injuries and damages	C-8	(4,908,523)	(879,677)	(5,788,200)
9	Accrued vacation	C-9	(4,349,552)	-	(4,349,552)
10	Accrued pension plan obligations	C-10	(5,332,297)	(10,391,216)	(15,723,513)
11	Total net investment in plant		1,609,126,895	154,203,992	1,763,330,887
	Working capital:				
12	Materials and supplies inventory	C-11	19,730,345	(186,899)	19,543,446
13	Prepayments	C-12	3,243,880	337,760	3,581,640
14	Fuel inventory	C-13	55,328,706	0	55,328,706
15	Cash working capital requirements	C-14	(19,213,246)	(1,688,920)	(20,902,166)
16	Total net working capital		59,089,685	(1,538,060)	57,551,626
17	Total rate base		$ 1,668,216,580	$ 152,665,932	$ 1,820,882,513
	Rate Base:				
18	Emery Generating Station	C-15	$ 315,686,205	$ -	$ 315,686,205
19	All Other		1,352,530,375	152,665,932	1,505,196,308
20			$ 1,668,216,580	$ 152,665,932	$ 1,820,882,513

INTERSTATE POWER AND LIGHT COMPANY

IOWA ELECTRIC UTILITY

DETERMINATION OF CASH WORKING CAPITAL REQUIREMENTS

YEAR ENDED DECEMBER 31, 2008

		Days of Lag
	Estimated revenue lag:	
1	Metering period	**15.3**
2	Processing bills	**2.9**
3	Collection period	**21.9**
4	Total	40.1

						Pro Forma Adjustment		
		(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Type of Expense	Amount	Expense Per Day (1)/365	Days Cash Required	Cash Requirement (2) x (3)	Pro forma Amount	Expense Per Day (5)/365	Cash Req. for Adjust. (3) x (6)
	Labor:							
5	Bi-weekly	**$ 86,119,530**	$ 235,944	24.7	$ 5,831,859			
6	Total Labor	86,119,530	235,944	24.7	5,831,859	$ 3,597,771	$ 9,857	$ 243,468
	Fuel Burned:							
7	Coal, including freight	**165,707,065**	453,992	15.3	6,937,058			
8	Oil	**8,525,486**	23,357	25.6	598,830			
9	Natural Gas	**63,562,619**	174,144	(5.7)	(998,867)			
10	Methane Gas	**100,769**	276	16.7	4,614			
11	Other (for pro forma adjustment only)					(19,722,159)	(54,033)	(540,330)
12	Total Fuel Burned	237,895,939	651,769	10.0	6,541,635	(19,722,159)	(54,033)	(540,330)
13	Electricity purchased	**326,869,130**	895,532					
14	Off-system sales	**(21,130,586)**	(57,892)					
15	Electricity Purchased, net	305,738,544	837,640	8.3	6,925,719	(141,165)	$ (387)	$ (3,200)
	Other operation and maintenance:							
16	Total operation and maintenance	**847,629,682**	2,322,273					
17	Less: Labor	**86,119,530**	235,944					
18	Fuel Burned	**237,895,939**	651,769					
19	Electricity purchased, before Off-system sales	**326,869,130**	895,532					
20	Total Other Operation and Maintenance	196,745,083	539,028	3.1	1,691,197	32,573,592	89,243	279,999
	Other:							
21	Property taxes	**37,553,243**	102,886	(326.4)	(33,577,377)	(10,450)	(29)	9,464
22	Federal income taxes	**(1,305,488)**	(3,577)	(0.2)	714	17,257,096	47,280	(9,434)
23	State income taxes	**8,875,754**	24,317	(15.4)	(375,686)	3,256,765	8,923	(137,856)
24	Interest on long-term debt	**43,673,143**	119,652	(53.8)	(6,435,228)	10,461,694	28,662	(1,541,525)
25	Preferred dividends	**12,773,293**	34,995	(8.0)	(281,110)			
26	FICA taxes	**7,407,433**	20,294	21.8	442,757	175,499	481	10,494
27	Federal unemployment taxes	**59,253**	162	93.8	15,198			
28	State unemployment taxes	**33,752**	92	76.9	7,076			
29	Total Other	109,070,384	298,821	(134.5)	(40,203,656)	31,140,604	85,317	(1,668,857)
30	Total	$ 935,569,480	$ 2,563,202	(7.5)	$ (19,213,246)	$ 47,448,643	$ 129,997	$ (1,688,920)

INTERSTATE POWER & LIGHT COMPANY
IOWA ELECTRIC UTILITY
13 MONTH AVERAGE BALANCE ENDED 9-30-09 - *EMERY GENERATING STATION*

Line No.		(c) Adjusted Average Principal	(d) Adjusted Capitalization Ratios	(e) Adjusted Avg. Cost of Money by Components (2)	(f) Adjusted Average Cost of Capital
1	Long-term debt	$ 1,131,430,877	43.449%	6.842%	2.973%
2	Preferred Stock	183,134,419	7.033%	8.410%	0.591%
3	Common equity	1,289,503,518	49.518%	12.230%	6.056%
4	Total	$ 2,604,068,814	100.000%		9.620%

INTERSTATE POWER & LIGHT COMPANY
IOWA ELECTRIC UTILITY
13 MONTH AVERAGE BALANCE ENDED 9-30-09 - COST OF CAPITAL-OTHER THAN EMERY GENERATING STATION

Line No.		(c) Adjusted Average Principal	(d) Adjusted Capitalization Ratios	(e) Adjusted Avg. Cost of Money by Components (2)	(f) Adjusted Average Cost of Capital
1	Long-term debt	$ 1,131,430,877	43.449%	6.842%	2.973%
2	Preferred Stock	183,134,419	7.033%	8.410%	0.591%
3	Common equity	1,289,503,518	49.518%	10.500%	5.199%
4	Total	$ 2,604,068,814	100.000%		8.763%