

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

IN RE:  MIDAMERICAN ENERGY COMPANY	DOCKET NO. RPU-2014-0002
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**ORDER ON REHEARING**

(Issued February 6, 2015)

**I. INTRODUCTION AND PROCEDURAL HISTORY**

On October 10, 2014, MidAmerican Energy Company (MidAmerican) filed with the Utilities Board (Board) a request for advance ratemaking principles that would apply to up to 162 MW of new wind generation. MidAmerican calls the project Wind IX and asked for expedited review. MidAmerican said that with expedited review, MidAmerican will be able to take full advantage of the federal production tax credit, which MidAmerican said is a prerequisite for the economics of Wind IX. (MidAmerican "Request for Approval of Ratemaking Principles," pp. 9-10).

Ratemaking principles proceedings are conducted pursuant to Iowa Code § 476.53 (2013). Section 476.53 was enacted during the 2001 Legislative Session as part of House File 577. This section provides that when eligible new electric generation is constructed by a rate-regulated public utility, the Board, upon request, shall specify in advance, by order issued after a contested case proceeding, the ratemaking principles that will apply when the costs of the new facility are included in electric rates. Wind IX as proposed by MidAmerican falls within the purview of § 476.53. Alternate energy production facilities, such as these wind facilities, were

added to the list of eligible facilities for ratemaking principles by House File 391, enacted during the 2003 Legislative Session. Section 476.53(1) states that the General Assembly's intent in enacting ratemaking principles legislation is to "attract the development of electric power generating and transmission facilities within the state ... ."

On October 16, 2014, the Board issued an order docketing the filing, setting a procedural schedule, and setting an intervention deadline. The Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed prepared direct testimony pursuant to the procedural schedule on November 14, 2014. There were no other intervenors.

On November 19, 2014, MidAmerican and Consumer Advocate filed a proposed settlement which, if adopted, would resolve all outstanding issues. The proposed settlement adopted MidAmerican's requested ratemaking principles, except for modifications to the two items contested by Consumer Advocate in its prefiled testimony, return on equity (ROE) and allowance for funds used during construction (AFUDC). A clarifying change was also made. A hearing on the proposed settlement was held on December 17, 2014.

The Board issued orders on November 14, December 2, December 11, and December 31, 2014, requiring MidAmerican to provide additional information. MidAmerican filed responses to each of the information requests.

On January 20, 2015, the Board issued an "Order Approving Settlement with Modifications" (Final Order). Among other things, the Board lowered the cost cap

contained in the Settlement Agreement and added one additional ratemaking principle, which provided that upon completion of 50 MW of Wind IX and until MidAmerican's next rate adjustment in a rate proceeding, MidAmerican is to flow to its customers an additional \$2 million per year in energy adjustment clause (EAC) benefits.

On January 22, 2015, MidAmerican filed a petition for limited consideration. MidAmerican said it did not object to and accepted all the ratemaking principles contained in the Board's January 20, 2015, order except the principle that provided that upon completion of 50 MW of Wind IX and until MidAmerican's next rate adjustment in a rate proceeding to include Wind IX in rate base, MidAmerican is to flow to its customers an additional \$2 million per year in EAC benefits. MidAmerican asked that the Board reject this ratemaking principle, or, in the alternative, approve a modified principle that would allow MidAmerican to incorporate the \$2 million EAC credit into the revenue sharing mechanism approved in Docket No. RPU-2013-0004. MidAmerican filed additional information in support of its petition for limited consideration on January 22 and 28, 2015.

The January 22 filing contained a request that the Board act on MidAmerican's petition for limited reconsideration on or before February 6, 2015, or 15 days after MidAmerican's initial filing for reconsideration. The January 28 filing extended the request to February 12, 2015. Iowa Code § 476.12 allows the Board 30 days to grant or refuse an application for rehearing or reconsideration.

On January 23, 2015, Consumer Advocate filed a response to MidAmerican's petition for limited reconsideration. Consumer Advocate recommended that the Board approve MidAmerican's alternative proposal. Under MidAmerican's proposal, Consumer Advocate said that 100 percent of the first \$2 million of revenue sharing money would be credited to customers as a reduction to rate base instead of the 80 percent approved by the Board in Docket No. RPU-2013-0004. The revenue sharing approved in Docket No. 2013-0004 only takes affect if MidAmerican's return on equity is above 11 percent.

## **II. SUMMARY OF MIDAMERICAN'S PETITION AND CONSUMER ADVOCATE'S RESPONSE**

MidAmerican argued that the Board's order did not cite evidence or analysis justifying the nature and amount of the EAC credit. MidAmerican cites various cases at page 6 of its request for limited reconsideration which support the standard set forth in Iowa Code § 17A.16 that the agency's findings must be supported by substantial evidence when that record is viewed as a whole. MidAmerican also claims that the Board acted arbitrarily or capriciously without regard to law or facts.

MidAmerican's alternative proposal is to incorporate the EAC credit into the revenue sharing calculation approved in Docket No. RPU-2013-0004. MidAmerican said that such a modification would result in the first \$2 million of revenue sharing (assuming earnings exceed the revenue sharing trigger by at least that amount) being credited 100 percent to customers as a reduction to rate base, with any incremental net income thereafter being shared by customers (80 percent) and

MidAmerican (20 percent) until the revenue sharing agreement's 14 percent threshold is met, when 100 percent would be credited to customers as a reduction in rate base.

MidAmerican pointed out that the Board's Final Order acknowledged various benefits of Wind IX, including a reduction in fuel costs and reduction in MidAmerican's reliance on fossil-fueled generation. (Final Order pp. 7, 16). MidAmerican said the Board erred in imposing a new ratemaking principle for a \$2 million EAC credit after acknowledging Wind IX's benefits.

Consumer Advocate in its response also pointed out the benefits of Wind IX and noted that while the addition of Wind IX will impact future revenue sharing amounts, Consumer Advocate concluded that in light of the overall benefits of Wind IX MidAmerican's customers are better off with Wind IX than without Wind IX. Consumer Advocate supported MidAmerican's alternative proposal to credit 100 percent of the first \$2 million of revenue sharing to customers as a reduction to rate base, assuming the revenue sharing threshold is met.

### **III. SUBSTANTIAL EVIDENCE**

Subrule 199 IAC 7.2(11) provides that the Board will not approve a settlement unless it "is reasonable in light of the whole record, consistent with law, and in the public interest." While the Settlement Agreement may not decide each issue the way the Board would after a contested hearing, the Board, viewing the Settlement Agreement as a whole, must find it to be reasonable, in the public interest, and not contrary to any law.

As the Board acknowledged in its Final Order, there are several benefits of Wind IX. Every Settlement Agreement the Board has reviewed contained at least some positive aspects. However, this does not mean every Settlement Agreement as filed is reasonable in light of the whole record, consistent with law, and in the public interest. The Board views the Settlement Agreement as a whole and determined that this Settlement Agreement was not reasonable or in the public interest without the modifications contained in the Final Order, including the EAC credit.

MidAmerican also complained that the Board did not adequately support its decision to include the EAC credit as a ratemaking principle. This alleged failure (if there is one) to provide adequate support for the Board's finding in the Final Order largely rests on how MidAmerican presented its case. Much of the information MidAmerican filed was confidential in nature and could not be referred to in the Final Order without releasing that confidential information.

The Board used a notational process to issue its Final Order. This process begins with what the Board refers to as a gold memo (because it is printed on gold paper), that is prepared by the Board's staff. The memorandum contains staff's summary of the case, analysis, and recommendation to the Board. This particular memorandum contains analysis of substantial amount of the confidential evidence, along with several options for the Board to consider. The Board could accept, reject, or modify the staff's recommendations.

The memorandum was circulated to the individual Board members, who added their comments and signatures. The memorandum was recirculated until all Board members agreed. It is important to note that the agreement reached by the Board on the memo is not the Board's final decision but merely an agreement to have the Board's staff draft an order consistent with the recommendations agreed to by the Board, which is then circulated to the Board for further consideration. The staff memorandum is not a part of the Board's decision as contained in an order and, as pointed out by MidAmerican in footnote 4 on page 4 of its request for limited consideration, neither supplements nor supplants the Final Order as the legal basis for the Board's decision.

The confidential information contained in the memorandum was supplied by MidAmerican and the memorandum has been made available to MidAmerican. Consumer Advocate, the other party to this proceeding, by law has access to this memorandum.<sup>1</sup> Thus, the parties have seen the detailed basis for the Board's decision, including the confidential analysis. This is not a substitute for the Board's order, by any means, but it should help to inform the parties about the Board's reasoning.

In most cases where confidential information is filed, the confidential information does not need to be revealed in the Board's final decision as it generally

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<sup>1</sup> The Board's reasoning and conclusions are supported by the public filings and by MidAmerican's confidential responses to Question 3 of the Board's December 2, 2014, order; Questions 2 and 3 of the Board's December 11, 2014, order; Question 13 of the Board's November 14, 2014, order; and MidAmerican confidential table 2.1-1c. A detailed analysis of the economic information provided by MidAmerican is contained on pages 4 through 10 of the staff's January 12, 2014, gold memorandum.

supplements similar public information in the evidentiary record. This case is different because of the amount of information which was held confidential, its importance to the Board's decision to modify the Settlement Agreement by adding the EAC principle, and the lack of equivalent public information in the record. Thus, the Board's order may have been less detailed than usual.

The Board could consider MidAmerican's request for limited reconsideration based on a failure to cite substantial evidence as a waiver of confidentiality of material filed prior to the reconsideration request. However, the Board does not want to jeopardize MidAmerican's negotiating status for those Wind IX contracts that are not yet finalized, so instead the Board will describe the confidential information in this order without revealing the details.

#### **IV. BOARD DISCUSSION**

Ratemaking principles proceedings are conducted pursuant to Iowa Code § 476.53 (2013). Section 476.53 was enacted during the 2001 Legislative Session as part of House File 577. This section provides that when eligible new electric generation is constructed by a rate-regulated public utility, the Board, upon request, shall specify in advance, by order issued after a contested case proceeding, the ratemaking principles that will apply when the costs of the new facility are included in electric rates. Wind IX as proposed by MidAmerican falls within the purview of § 476.53. Alternate energy production facilities, such as these wind facilities, were added to the list of eligible facilities for ratemaking principles by House File 391, enacted during the 2003 Legislative Session. Section 476.53(1) states that the

General Assembly's intent in enacting ratemaking principles legislation is to "attract the development of electric power generating and transmission facilities within the state ... ."

In ratemaking principles decisions, the Board is not limited to traditional ratemaking mechanisms or traditional cost recovery mechanisms. Iowa Code §476.53(b). If MidAmerican rejects the ratemaking principles awarded in this proceeding, MidAmerican retains the option to build Wind IX (or any other appropriate generating facility) through use of traditional procedures and ratemaking, including cost recovery in a subsequent rate case.

The \$2 million EAC credit adopted by the Board is not indefinite. The \$2 million EAC principle begins when 50 MW of Wind IX is complete and ends when MidAmerican brings its next general rate proceeding. In other words, MidAmerican controls the timing of how long the \$2 million payment will continue because it generally determines the timing of a rate proceeding.<sup>2</sup> The public version of Appendix A to the reconsideration request filed by MidAmerican projects the credit will be paid until 2024; this would only happen if MidAmerican did not elect to bring a general rate proceeding prior to that year.

The \$2 million EAC credit is also not a new ratemaking principle. A similar principle was contained in the Settlement Agreement executed by MidAmerican and

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<sup>2</sup> In the Settlement Agreement in Docket No. RPU-2013-0004, MidAmerican agreed not to file a general rate case until January 1, 2018, unless its return on equity fell below 10 percent.

others in MidAmerican's last ratemaking principles proceeding, Docket No. RPU-2013-0003. That credit was larger because the project (Wind VIII) was larger, but the principle is similar. MidAmerican Energy Company, "Order Approving Settlement and Requiring Reports," Docket No. RPU-2013-0003 (8/9/2013), p. 15. Throughout its filing in this proceeding, MidAmerican noted that the Wind IX project and ratemaking principles were similar to those in Wind VIII. The Board's inclusion of the \$2 million EAC credit made the principles awarded in the two proceedings almost identical, based on the projects' respective sizes.

Wind IX has rewards and risks for both MidAmerican and its captive retail customers. Wind IX was presented by MidAmerican as an opportunity to provide emission-free energy at no net cost to MidAmerican's retail customers. Wind IX is not required in order to provide reliable service to MidAmerican's customers.<sup>3</sup> This opportunity exists largely because of the existence of federal production tax credits, which are expiring; MidAmerican said that Wind IX would not be built without those credits. Wind IX does very little to resolve MidAmerican's projected capacity needs and MidAmerican did not provide an adequate explanation as to how those capacity needs will be met and how Wind IX is consistent with those plans. Customers generally face significant cost risks when any capacity issues need to be addressed. Customers will face this risk regardless of whether Wind IX is built, which reinforces the Board's finding that there must be an appropriate balance of risk and reward for a

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<sup>3</sup> Iowa Code § 476.53(1) provides that part of the intent behind the ratemaking principles statute is to "ensure reliable electric service to Iowa consumers... ." MidAmerican did not contend that Wind IX was necessary to ensure reliable electric service.

facility that will have little impact on meeting future capacity needs and is not required for reliability.

MidAmerican's statement at page 3 of its petition for limited reconsideration refers to the "cost-free energy Iowa customers will receive without incurring cost for MidAmerican's Wind IX capital costs, depreciation expenses, and other operating and maintenance expenses until a future rate case." This statement fails to acknowledge that prior to the next rate case the effect of Wind IX on the revenue sharing calculation (reducing the revenues shared with customers) will offset a significant portion of the "cost-free energy" benefit. MidAmerican's statement also ignores the fact that the existing base rates include recovery of book depreciation, return on investment in plant, and maintenance expense on the plant(s) that would have been generating in the absence of Wind IX. Those costs will continue even when the plant is not running.

The information supplied by MidAmerican indicates that the company's risks associated with Wind IX are well-hedged; in particular, the PTC benefits appear to be relatively certain. (Tr. 126-27). If the costs of Wind IX have too much of a negative impact on post-revenue sharing earnings, MidAmerican has the option to initiate a rate proceeding. Also, once Wind IX is added to rate base, MidAmerican's customers will be under an obligation to pay increased rates to allow MidAmerican to recover the return on equity specified in the ratemaking principles if the project does not deliver the anticipated results even if it were for no fault of theirs, despite

MidAmerican's stated goal of no harm to customers. Thus, MidAmerican's risks associated with this project are relatively low.

The overall customer benefits projected by MidAmerican vary over time and are dependent on the assumptions made by MidAmerican. Under MidAmerican's projections, there are periods when the projected customer benefits are negative. MidAmerican estimated the customer benefits for the first ten years at \$93.5 million. MidAmerican argued that customers will benefit through a reduction in fuel costs without bearing any of the capital costs, depreciation expenses, and operating benefits until MidAmerican's next rate proceeding.

All the factors cited in the Board's discussion support a conclusion that the risks and rewards under the Settlement Agreement are unreasonably tilted in MidAmerican's favor. Under the Settlement Agreement, the customers' risk is much greater than MidAmerican's risk, with Appendix A showing that MidAmerican would reap about 75 percent of the benefits over the first ten years. Under the \$2 million EAC principle included by the Board, the customer-utility split is closer to 50-50. The scenarios provided by MidAmerican at the Board's request demonstrate that Wind IX will likely not leave customers unharmed without the \$2 million credit. The Board believes the scenarios it requested contained more reasonable assumptions than those initially presented by MidAmerican, which overstated the benefits to customers. It also must be remembered that MidAmerican largely controls the timing of its next rate proceeding, another risk borne by customers.

The Board cannot find that the Settlement Agreement is reasonable or in the public interest as submitted because of this imbalance of the risks and rewards; this is unlike the Settlement Agreement in Wind VIII, which contained an EAC credit and better balanced the project's risks and rewards between customers and ratepayers. The majority of Wind IX's cost has been fixed with contracts and purchases, leaving less than half the project's capital cost at issue. Captive ratepayers, who will be shouldering the costs of a large portion of the project through payment for Wind IX once it is included in MidAmerican's rates, undertake a disproportionate share of the risk for the amount of potential reward provided for in the Settlement Agreement. Because Wind IX is not based on an immediate need for energy or capacity, the risks and rewards must be more evenly balanced between MidAmerican and its ratepayers, particularly for the period immediately after Wind IX begins operation. Not only must the project avoid customer harm, it must provide positive, quantifiable customer benefits, particularly in the short term, that are shared between customers and the utility. The longer term benefits are based on assumptions that may not prove to be correct over a 30-year period and the immediate benefits provided by the \$2 million clause mitigate some of the risk and provide benefits to ratepayers even if the longer term assumptions prove to be incorrect.

The Board's decision in Wind IX focuses on the costs, benefits, and risks specific to Wind IX. For the risks and rewards to be appropriately balanced, the EAC credit is necessary for the time prior to Wind IX's inclusion in MidAmerican's rate base, regardless of the impact on revenue sharing or return. In response to question

3 contained in the Board's December 11, 2014, order, MidAmerican provided estimated earnings levels for the years 2015 through 2024. While the actual estimates are confidential, the Board used MidAmerican's projections in its most recent earnings report to show how the impact of the \$2 million EAC credit on MidAmerican's overall return on equity is negligible.<sup>4</sup>

Under MidAmerican's alternative proposal, the customer benefit would be in the form of a reduction to rate base rather than a direct EAC credit. Only the EAC credit would immediately be reflected on customers' bills. Thus, the alternative proposal fails to provide the near-term benefit to customers that is necessary to balance the risks and rewards of this project.

The Board affirms the adoption of the \$2 million EAC credit as a ratemaking principle. Without such a principle, the rewards of Wind IX are skewed too much towards MidAmerican for the Settlement Agreement to be reasonable and in the public interest. Wind projects have many benefits and the Board appreciates the economic benefits wind development brings to the state. While the Board has and will continue to encourage such projects, the projects must provide customers benefits commensurate with the risk that customers will be bearing. The Board's addition of the EAC credit provides a more appropriate balance of risks and rewards between customers and MidAmerican, like the Settlement Agreement agreed to by

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<sup>4</sup> The projected impact on MidAmerican's return on equity is approximately 5 to 7 basis points, or .05 to .07 percent, and might be less if tax considerations were included.

MidAmerican and approved by the Board in Wind VIII. The Board's Final Order is amended to include the discussion contained in this order.

**V. ORDERING CLAUSE**

**IT IS THEREFORE ORDERED:**

The decisions contained in the Board's January 20, 2015, "Order Approving Settlement with Modifications" are affirmed, but the order is amended to include the discussion contained in this order.

**UTILITIES BOARD**

/s/ Elizabeth S. Jacobs

/s/ Nick Wagner

ATTEST:

/s/ Joan Conrad  
Executive Secretary

/s/ Sheila K. Tipton

Dated at Des Moines, Iowa, this 6<sup>th</sup> day of February 2015.