

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)
INDIANA MICHIGAN POWER COMPANY)
for approval of a power supply cost recovery)
plan (2011).)
_____)

Case No. U-16433

At the meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. Orjiakor N. Isiogu, Chairman
Hon. Greg R. White, Commissioner

ORDER

On September 30, 2010, Indiana Michigan Power Company (I&M) submitted an application with supporting testimony and exhibits requesting approval of its power supply cost recovery (PSCR) plan and factors for the year ending December 31, 2011 pursuant to 1982 PA 304, MCL 460.6j (Act 304). Ultimately, I&M seeks a plan factor of negative 0.27 mills per kilowatt-hour (kWh).

A prehearing conference was held on December 7, 2010 before Administrative Law Judge Mark E. Cummins (ALJ). The ALJ granted intervention to the Citizens Against Rate Excess (CARE). The Commission Staff (Staff) also participated in the proceedings.

An evidentiary hearing was held on April 20, 2011. I&M presented the testimony of five witnesses and the Staff sponsored the testimony of one witness. CARE did not sponsor any

witnesses and the parties waived cross-examination. The pre-filed testimony of the witnesses was then bound into the record. The record consists of 116 pages of transcript along with 41 exhibits.

On May 4, 2011, the ALJ transmitted a letter to the docket indicating that the Commission would read the record in this case.

On May 19, 2011, CARE filed a letter stating that it would not be filing a brief in this case. On May 20, 2011, I&M and the Staff filed their initial briefs. On June 1, 2011, I&M and the Staff filed replies.

Overview of the Record

I&M's direct case includes the testimony and exhibits of five witnesses. Charles F. West, Manager of Fuel Procurement in the Fuel, Emissions, and Logistics Department for American Electric Power Service Corporation¹ (AEPSC), testified to I&M's actions related to coal procurement and delivery. Mr. West explained the factors I&M considered in making its coal procurement decisions, including price, quality, and contract terms. Mr. West also testified regarding the existing major coal supply agreements for each of I&M's generating stations, including descriptions of how forecasted coal prices were determined. Mr. West concluded that I&M aggressively pursues and manages its coal supply and transportation costs.

Mickey L. Bellville, Manager of I&M's Nuclear Engineering Department, testified to I&M's nuclear fuel requirements and nuclear fuel related activities. Mr. Bellville described the major contracts for supplying nuclear fuel to the Cook Plant as they relate to fuel costs. Mr. Bellville explained the efforts undertaken by I&M to minimize the cost of fuel and related activities at the Cook Plant.

¹I&M is a wholly-owned subsidiary of the American Electric Power Company, and is an operating subsidiary in the American Electric Power System.

Jennifer S. McLavy, Director of Financial Forecasting for AEPSC, presented I&M's forecast of monthly power supply costs and net energy requirements for 2011. Ms. McLavy also provided similar data for the years 2011 through 2015. Ms. McLavy testified about methodologies and assumptions I&M utilized to develop its power supply cost requirements and power supply costs for 2011 through 2015. Ms. McLavy also testified regarding I&M's calculations for fossil fuel costs, nuclear fuel costs, expenses and credits for emission allowances, the cost of purchased power, and system sales revenues.

Jon R. MacLean, Manager of Production Resource Modeling in the Corporate Planning & Budget Department of AEPSC, testified about I&M's expected sources of power supply for 2011. Mr. MacLean further testified to I&M's 2011 through 2015 five-year forecast of the company's electric power and energy requirements, and anticipated sources of power supply. Mr. MacLean described the load forecast methodology used and the significance of the forecast. Mr. MacLean also testified about the major contracts and power supply agreements entered into by I&M for providing power. Mr. MacLean further explained the generation resource planning process of American Electric Power Company (AEP) and I&M. Mr. MacLean sponsored exhibits showing AEP System and I&M internal demand and energy requirements, as well as peak demands, generating capabilities and margins. Finally, Mr. MacLean testified regarding the reasonableness of I&M and AEP reserve levels and the reasonableness of I&M's 2011 PSCR plan.

David L. Hille, Principal Regulatory Consultant in the Regulatory Services Department, testified in support of the calculations related to the proposed PSCR factors for each of the billing months of January 2011 through December 2011. Mr. Hille sponsored Exhibits IM-34 and IM-35, which are the proposed revised tariff sheets showing the calculations of the proposed PSCR factor and determinations of the line loss factor multiplier for the unified rate case.

The Staff presented the direct testimony and exhibits of one witness. Ronald J. Ancona, Manager of the Act 304 and Sales Forecasting Section of the Regulated Energy Division, testified regarding two specific adjustments to I&M's PSCR plan. First, Mr. Ancona testified that the PSCR plan should be adjusted by \$4,000,000 because, as he alleges, coal ash disposal costs should be excluded. Regarding the second adjustment, Mr. Ancona testified that I&M's line loss factor of 4.2% should be replaced with a line loss factor of 3.7%, the same line loss factor used in Case No. U-16180.

I&M rebutted the Staff's two proposed adjustments with the testimony and supporting exhibits of one witness. William A. Allen, Director of Regulatory Case Management for AEPSC, testified that I&M's inclusion of net coal ash disposal costs as a PSCR cost in Case No. U-16180 is well founded and should not have been a surprise in this case. Mr. Allen further testified that ash disposal is the by-product of burning coal and the disposal costs are properly included in Account 501 Fuel. I&M proposes, as Mr. Allen states, to include all appropriate Account 501 fuel costs as PSCR costs. In conclusion, Mr. Allen testified that there is a direct relationship between the fuel burned for generation and the resulting ash, which Act 304 allows as a PSCR cost.

Mr. Allen also rebutted the adjustment proposed by the Staff to the line loss factor. Mr. Allen testified that the line loss factor should not be fixed to that agreed upon in Case No. U-16180. Mr. Allen explains that PSCR cases have historically used a five-year average and thus the line loss factor should be adjusted accordingly as new data related to transmission losses become available.

Discussion

The two contested issues in this case are whether the ash disposal costs I&M included in its PSCR plan are recoverable as PSCR costs pursuant to Act 304 and whether the transmission line loss factor should be set at the company's proposed rate of 4.2% or at the 3.7% rate the Staff

alleges. In all other respects, the Commission finds that the PSCR plan submitted by I&M is reasonable and prudent and should be approved.

Ash Disposal

In its brief, the Staff argues that the Commission should adjust I&M's PSCR plan to account for improper inclusion of ash disposal costs. The Staff argues that the inclusion of ash disposal costs as PSCR costs was not approved by the Commission, and that the Commission has been clear about excluding ash disposal costs as a PSCR cost without prior approval.

In rebuttal, I&M argues that the Staff relied on extra record material in its brief to support its basis for excluding ash disposal costs. Specifically, I&M argues that the Staff relied on testimony submitted in Case No. U-16180, which was not introduced as evidence in this case. I&M contends that the Commission must only consider the record evidence in the present case.

I&M also argues that the Commission should not take judicial notice of the testimony from Case No. U-16180. I&M contends that the Commission has made it clear that the briefing stage is not the time for requesting and taking notice pursuant to Section 77 of the Administrative Procedures Act (APA).²

I&M further argues that even if the Commission were to consider the extra-record evidence, it is clear that the company did include ash disposal costs as part of the PSCR plan and proceeding. I&M argues that the Staff did not contest the substantive reasons for allowing ash disposal costs. In the case of ash disposal, I&M argues, the ash is the direct consequence of burning fuel and is consistent with Act 304 and the company's PSCR clause. I&M argues that the ash disposal costs are booked costs of disposing fuel burned for electric generation and should be allowed as a PSCR cost. Furthermore, as I&M provided in rebuttal testimony, the company filed Exhibit I&M-28 and

²I&M br. p. 3, citing the Commission's December 18, 2007 order in Case No. U-15245, p. 30.

its associated working paper, WAA-5³, in its rate case that set forth I&M's proposal to include all Account 501 fuel costs in the PSCR plan. I&M argues that under the Federal Energy Regulatory Commission's chart of accounts, ash disposal costs are properly included in 501 accounts. Thus, as I&M contends, the company did not need to make a separate request to include ash disposal costs and the Staff should not have been surprised by its inclusion.

In its reply, the Staff argues that the issue of ash disposal costs arose only through its discovery following I&M's application. The Staff further contends that I&M never specifically addressed the inclusion of ash disposal costs in its rate case testimony. Additionally, the Staff maintains that I&M's reliance on the allowance of treated emissions as PSCR costs in other cases is misplaced because in those instances the allowance was preceded by a specific request of the utility for inclusion.

The Commission finds that I&M's request to pass its ash disposal costs through its PSCR clause should be rejected. At the heart of the dispute over the determination whether to include or exclude the ash disposal costs in the calculation of I&M's 2011 PSCR factor are two issues. First, is the question of whether the Commission's approval of the settlement agreement in Case No. U-16180 constitutes a Commission determination that ash disposal costs shall be included in I&M's PSCR factors. Second, assuming that Case No. U-16180 did not involve a determination that approval of the settlement agreement in Case No. U-16180 constitutes a Commission determination that ash disposal costs shall be included in I&M's PSCR factors, then the issue becomes whether the Commission should in this proceeding approve I&M's request to have ash disposal costs included in its 2011 PSCR factor.

³Filed as Exhibit I&M-37 (WAA-R2) in this case.

Turning to the first issue, the Commission finds that approval of the settlement agreement in Case No. U-16180 did not reflect any determination by the Commission to resolve this issue. Indeed, the Commission finds that I&M's contrary contentions are without merit.

The Commission has examined the settlement agreement and its October 14, 2010 order in Case No. U-16180.⁴ Nothing in either of these documents indicates that the parties were asking the Commission to make an explicit policy determination on the inclusion or exclusion of ash disposal costs in I&M's PSCR factors. Indeed, the settlement agreement approved by the Commission in Case No. U-16180 expressly provided that: "It is the understanding of the parties that a final authorized 2011 PSCR factor will be determined subject to the contested case proceeding in Case No. U-16433," which completely undermines I&M's arguments in this proceeding.

The fact that I&M's rate case positions and workpapers in Case No. U-16180 may have had baked into them a proposed change of the Commission's longstanding policy regarding the constituent parts of the utility's PSCR factor does not mean that the other parties to the proceeding or the Commission actually realized the existence of such a position and chose to silently agree to it. Rather, the Commission finds that, absent an open and obvious request in a settlement agreement by the parties to a position that constitutes a material change in an existing position of the Commission and the Commission's express approval of that material change, a party proffering an argument based on an alleged *sub silento* approval of a position unmentioned in a settlement agreement must fail.

⁴The Commission always may consider and interpret its prior orders and settlement agreements without them being introduced into evidence. The Commission finds that it does not need to base any part of its determination in this case on testimony or exhibits from Case No. U-16180.

Turning to the second issue, the Commission finds that I&M's position that ash disposal costs should be passed through the PSCR factor is not well taken. As stressed by the Staff, the Commission has previously considered and rejected this position in its November 20, 2001 order in Case No. U-12615. Moreover, I&M has failed to cite any case in which the Commission has expressly approved the inclusion of ash disposal costs in a PSCR factor.

A PSCR factor should include only the booked costs of fuel burned by the utility for electric generation and the booked costs of purchased and net interchanged power transactions. MCL 460.6j(1)(a). While ash is a typical byproduct of combustion, the Commission remains unconvinced that ash disposal costs constitute a booked cost of fuel within the meaning of Act 304. The central purposes of Act 304 were (a) to allow utilities to quickly adjust their rates to avoid the consequences of rapidly rising fuel expenses, and (b) to provide sufficient scrutiny to ensure that only costs that were reasonably and prudently incurred would be passed on to customers via the Act 304 process. The Commission finds no evidence that ash disposal costs are inherently tied to the booked cost of fuel burned or are naturally volatile.⁵

Line Loss Factor

The second contested issue is the Staff's contention that the line loss factor should be set at 3.7% and not the 4.2% requested by the utility. The Staff bases its figure on the rate set for I&M during the previous rate case, Case No. U-16180. The Staff acknowledges that I&M was allowed to update the line loss factor in previous PSCR cases, but those instances were not preceded by a rate case in which the line loss factor was specifically established. The Staff contends that if I&M

⁵In rejecting I&M's ash disposal arguments, the Commission also rejects any notion that I&M's PSCR base should be revised in this proceeding. I&M has a currently pending rate case (Case No. U-16801, filed July 1, 2011), which is the appropriate venue for the utility to address this issue.

were allowed to continue updating the line loss factor, it would be the only utility to adjust the factor outside of a rate case.

In rebuttal testimony, I&M's witness, Mr. Allen, testified that the established rate agreed upon in Case No. U-16180 did not preclude new line loss factors in subsequent PSCR cases. I&M further contends that no party contested the company's plan to employ an average line loss factor in this case.

The Commission finds that the line loss factor was properly set during the rate case proceeding. The parties in the last I&M rate case agreed to a line loss factor of 3.7%. Thus, the Commission finds that the line loss factor should be set at 3.7%.

THEREFORE, IT IS ORDERED that:

A. Indiana Michigan Power Company's application for a 2011 power supply cost recovery plan and monthly factors, as modified by this order, are approved.

B. Indiana Michigan Power Company shall file a tariff sheet within 30 days that reflect the modifications in this order.

C. As modified by this order, Indiana Michigan Power Company's 2011 power supply cost recovery factor shall be set at negative 0.53 mills per kilowatt-hour for service rendered on and after the day following issuance of this order.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, under MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

Orjiakor N. Isiogu, Chairman

Greg R. White, Commissioner

By its action of

Mary Jo Kunkle, Executive Secretary