STATE OF IOWA

DEPARTMENT OF COMMERCE

UTILITIES BOARD

IN RE:

HOUSE FILE 617 REVIEW OF SPECIFIED PROVISIONS AND UTILITY RATEMAKING PROCEDURES

DOCKET NO. NOI-2023-0001

FINAL COMMENTS IN CHARRETTE #1

Comes now, Cecil I. Wright, and offers the following comments regarding the discussion of issues in Charrette #1.

BACKGROUND

On July 5, 2023, the Board opened Docket No. NOI-2023-0001 to fulfill the mandate in HF 617. The mandate required the Board to initiate and coordinate an independent review of current Iowa Code provisions and ratemaking procedures. The review is required to take into account the policy objectives of “ensuring safe, adequate, reliable, and affordable utility services provided at rates that are nondiscriminatory, just, reasonable, and based on the utility’s cost of providing service to its customers within the state.” The Board is required to submit a report with findings and recommendations to the General Assembly by January 1, 2024.

On August 5, 2023, the Board issued an order establishing a procedural schedule to allow for stakeholder input into the review required by HF 617. The Board has scheduled three charrettes to allow for participants to discuss the issues involved in the inquiry. Charrette #1 was held as scheduled and the participants discussed the issues identified by the Board.

On September 6, 2023, the Board issued a letter that included a request from London Economics International (LEI), the consultant for the docket, for participants to
address specific issues in final comments. My final comments will address some of the
issues requested by LEI and some of the issues raised in Charrette #1 discussions.

A. Board Authority

Iowa Code chapter 476 grants the Board authority to set rates for services
provided by investor-owned electric, natural gas, sanitary sewer, and water utilities
(rate-regulated utilities). The basic provisions that establish the authority of the Board to
approve rates in accordance with the rate-regulation scheme are set out in Iowa Code
§§ 476.6 and 476.33. Iowa Code § 476.8 provides that the rates approved by the Board
provide the funds for a utility to meet the statutory requirement that “[E]very public utility
is required to furnish reasonably adequate service and facilities.” The rates charged for
the services provided shall be just and reasonable and every unjust and unreasonable
rate for service is prohibited and declared unlawful. The Board is to consider all factors
relating to value in determining just and reasonable rates.

Rates charged to ratepayers based upon the procedures established in the
statutory sections described above, and rules adopted by the Board to implement these
statutory provisions, are considered just and reasonable. Ratepayers, utilities, and
stakeholders may not agree with the rates approved by the Board; however, this system
of rate regulation has served Iowa customers of rate-regulated utilities well over the
years. The answer to the General Assembly’s inquiry in HF 617 is that this regulatory
scheme for setting rates ensures safe, adequate, reliable, and affordable utility services
that are provided at rates that are nondiscriminatory, just, reasonable, and based on the
utility’s cost of providing service to its customers within the state.
The reason that this basic scheme meets the policy objective raised by HF 617 is because the flexibility this rate-regulation scheme has allowed, and allows, the Board to make decisions regarding rates and services based upon evidence presented in contested case proceedings. These proceedings allow issues to be raised by the utilities and parties involved in the rate-regulation process. Under this rate-regulation scheme, the Board is tasked with balancing the interests of, ratepayers, the public, and the utilities when setting rates. Rates are to be set to recover the reasonable costs of providing utility service and a reasonable return on equity to the utility. Setting rates is not a science with strict rules, but is more of an art where the needs of customers, the public interest, and the cost to provide the services offered by the utility are considered.

The Board has the authority under the provisions in Iowa Code §§ 476.6 and 476.33 to address almost all issues related to the services provided and the rates charged that are raised by utilities and ratepayers in a general rate case proceeding. Several statutory provisions have been enacted to modify this basic rate-regulation scheme where the legislature has determined that public policies require exceptions to the Board’s authority, or has granted the Board additional authority. Most of these exceptions establish requirements for recovery of costs and setting rates outside of the full review of utility costs and revenues in a general rate case proceeding.

Iowa Code § 476.6(8) provides the Board with the authority to approve automatic adjustment mechanisms that allow for recovery of costs for a single item outside of a general rate case proceeding. This statutory provision specifically allows for an automatic adjustment mechanism for transmission costs approved by the Federal Energy Regulatory Commission.
Iowa Code §§ 476.6(13) and (15) provide for the pass through of the cost of energy efficiency and demand response plans outside of a rate case through an automatic adjustment mechanism. Iowa Code § 476.6(18) allows an electric utility with coal generation to recover reasonable costs associated with implementing a plan to meet applicable state environmental requirements and federal ambient air quality standards approved by the Board in a subsequent general rate case proceeding. Iowa Code § 476.53 requires the Board to approve advance ratemaking principles to recover the costs of certain electric generation facilities. Iowa Code § 476.84 requires that a rate-regulated utility obtain Board approval to acquire a non-rate-regulated sanitary sewer or water facility. Iowa Code § 476.84(2) requires the Board to specify in advance ratemaking principles that will apply when the costs of the acquisition are included in regulated rates and approval of a tariff for providing service to the customers of the acquired utility.

The statutory provisions and the Board’s rules implementing those provisions, have allowed the Board to address almost all of the issues raised by a utility or a party as part of the general rate case proceeding. In compliance with these statutory provisions, the Board has approved just and reasonable rates for utilities that balance the interests of ratepayers, utilities, and the public interest. While a utility or a ratepayer may disagree with a specific rate, courts have rarely overturned the Board’s decisions with regard to the rates approved by the Board.

Under the authority established by the above provisions, the Board has approved a revenue sharing mechanism for MidAmerican Energy Company (MidAmerican) that has allowed MidAmerican to operate its utility without the need for frequent rate cases,
thus providing ratepayers with stable rates over the past 20 plus years. With the
authority provided in Iowa Code § 476.6(8), that allows the Board to approve automatic
adjustment mechanisms, the Board has addressed issues raised by utilities concerning
regulatory lag for recovery of capital costs for infrastructure that is required to meet
standards for the safe operation of the facilities. The use of automatic adjustment
mechanisms has allowed the Board to approve farm tap replacement costs for a natural
gas utility and the recovery of costs of renewable generation facilities by Interstate
Power and Light Company (IPL) when those facilities become in service and used and
useful, instead of requiring IPL to file another rate case to recover those costs.

The provisions of Iowa Code chapter 476 discussed above have given the Board
sufficient authority to address almost all ratemaking issues that have come before the
Board. Where the Legislature determined that exceptions to setting rates in general
rate case proceedings were necessary, the Legislature has enacted separate statutes
that address those issues. As part of its review of the Board’s authority under the rate-
regulation scheme, the Legislature should consider whether separate statutes have met
the purpose for which they were enacted and whether those separate statutes are still
necessary.

B. Specific Issues Discussed

The initial comments filed by participants and the discussions at Charrette #1
covered most of the important issues raised by the participants regarding the regulatory
authority of the Board and participants provided recommendations on revising the rate-
regulation scheme in the statutes. Several specific issues were brought up for
consideration and my comments address some of those specific issues. In addition, LEI requested comments on two specific issues.

1. The first issue that LEI requested comments on is definitions of policy objectives about “stability,” “affordability,” “efficiency,” and the definitions and terms identified at the Charrette. I do not have comments regarding the definitions requested by LEI, except to suggest that the definitions of any of the terms do not limit the flexibility of Board’s authority under chapter 476. Limiting definitions can inhibit consideration of solutions to problems or mandate approaches to problems that over time become outdated. Rate stability and affordability are part of the consideration of setting just and reasonable rates. Because rates are set to be in effect over a period of time, utilities are required to operate in an efficient manner to earn a return on equity (ROE) at or above the ROE approved by the Board. Statutory requirements attempting to mandate efficiency may very likely have the opposite effect, since a utility may take actions to meet the definition rather than adopt efficiencies that may not be considered in the definition. A term used in the current statutory requirements is “cost-effective” which in some instances has been the subject of extensive litigation. Any metrics or statutory requirements proposed should be designed so that compliance with the definitions does not become the issue before the Board rather than the Board addressing issues raised by the parties.

2. The second item that LEI requested the participants comment on involves Iowa Code § 476.53. Specifically, LEI requested comments on whether the advance ratemaking statute has achieved its purpose and may no longer be necessary. LEI asks comments on: (1) Does Iowa no longer require the development of new generation
assets and the advance ratemaking principles statute can be removed, (2) will new generation assets be developed without the advance ratemaking principles statute and therefore the statute is not needed, or (3) does the advance ratemaking statute need to be revised for continued development of generation assets.

Iowa Code § 476.53 was enacted to address the uncertainty raised by rate-regulated electric utilities that a utility would not recover the costs for investments in large generation facilities. The statute was amended to include renewable energy generation facilities. Over the years, using the approval of advance ratemaking principles, including a ROE, and Production Tax Credits (PTCs) provided by the federal government, electric utilities have been able to make Iowa a leader in wind generation and fulfill their responsibilities as rate-regulated utilities to provide reasonably adequate service and facilities at just and reasonable rates.

The first question asked by LEI creates a dichotomy that is not realistic. Iowa needs its utilities to continue to consider and develop plans to construct new generation facilities using new technologies as they become available. However, the question is whether rate-regulated utilities require incentives, and in some instances excessive incentives, to plan for new technologies and construct those generation facilities. Iowa Code § 476.53 in its current form is no longer needed. The federal government is providing significant incentives for the development of wind and solar facilities and, where facilities are needed to serve customer load, utilities will construct those facilities.

If the Legislature determines that public policy requires incentives for utilities outside of rates set in a general rate case, the focus of a new or revised statute should be on the reliability of the electric system. Ensuring that there is electricity available
throughout each day regardless of weather conditions should be the focus of any incentives. Utilities do not need to be provided incentives to construct generation facilities that are required to meet customer load and wind and solar energy generated in excess of that necessary to meet a utility’s load can be exported without the support of a utility’s ratepayers. Ratepayers should not pay for the facilities that provide that exported energy. Questions about what is needed to serve a utility’s load are best addressed through an integrated resource plan (IRP) where long-term planning can be reviewed by the Board and stakeholders.

The issue of whether Iowa Code § 476.53 has fulfilled its purpose and should be rescinded or significantly modified was discussed during Charrette #1. The initial comments and discussions laid out the arguments for and against this question. I believe the Board should include the following points in its consideration of what to recommend to the Legislature.

a. Wind and solar generation are no longer new technologies that require incentives to construct those generation facilities. Wind facilities are being constructed throughout the region and Iowa is exporting wind because it produces more wind than is required to meet its native load. The federal government, through the IRA, is providing significant incentives for construction of wind and solar facilities and arguably supplants the need for state incentives. Under ratemaking principles approved by the Board, utilities have ROEs that are higher than would be set in a general rate case proceeding and these higher ROEs will be recovered from ratepayers for the useful life of the generation facilities. Iowa Code § 476.53 has shifted the risk of recovery of the costs of generation facilities from a balance between ratepayers and utilities to ratepayers.
b. Recommendations to expand the size and type of generation facilities for which advance ratemaking is required should be rejected. Allowing a rate-regulated electric utility to set advance ratemaking principles outside of a general rate case proceeding will distort the underlying ratemaking principle that rates are to be just and reasonable. Incentives for constructing generation facilities using new technologies, especially when there is no need for the additional generation, should not be provided by ratepayers. Ratepayers should only be required to pay for generation facilities that meet their needs.

Setting a time limit on the Board to issue an order addressing proposed advance ratemaking principles is not reasonable. Advance ratemaking dockets prior to the current hearings were done efficiently and final orders were issued within the time requested by the utilities. Statutory changes should not be recommended to address what are unique issues raised by the advance ratemaking proceedings currently before the Board.

3. One issue that was discussed at Charrette #1 is whether the Board has the necessary authority to require electric utilities to file IRPs for Board consideration and input from stakeholders. Without an IRP, the Board and stakeholders have little input into how a utility is planning on meeting its obligation to provide reasonable and adequate service in the future. The electric industry has changed significantly with the creation of regional transmission organizations (RTOs), the introduction of competition into the electric generation and transmission market, and the increase in the number of independent power producers that produce electric energy that is sold into the market.
An IRP is needed to ensure that electric utilities are making decisions that will benefit ratepayers and not just the utility and that reflect future market conditions.

Construction of generation facilities is costly and requires years of planning. The Board, ratepayers, and other stakeholders should be included in a discussion of the utility’s plans for future construction, whether that construction is necessary, and how the costs of that construction will be recovered. Under current statutes where a utility is not required to file an IRP, the Board, stakeholders, and ratepayers first see the utility’s decision about constructing generation facilities in a general rate case proceeding or an advance ratemaking principles proceeding where the decisions about the size and type of facilities have already been made. An IRP would make the process more transparent and allow for discussions of options that might be available to the utility prior to final decisions being made.

One issue that electric utilities face that has not been presented to the Board is how the electric utilities will maintain reliability of their systems when the wind does not blow and the sun does not shine. There appears to be no question that large coal fired generation facilities will be retired and those types of facilities will not be constructed in the future. Battery storage has not reached the level of maturity to ensure the reliability of the electric grid. How a utility will ensure the reliability of its system would be one issue addressed by an IRP.

Whether rate-regulated natural gas utilities and rate-regulated sewer and water utilities should be required to file long-term plans for forecasting future infrastructure requirements and service areas expansions was also discussed. My recommendation is that both gas and sewer and water utilities be required to file long-term plans. Safety
requirements for natural gas systems are being revised at the federal level which
require construction of new and improved infrastructure. Water quality standards and
wastewater disposal standards are being revised and additional facilities will be required
to meet those revised standards. In addition, there is the potential that the source of
water may need to be considered in the future and that issue should be presented to the
Board sooner rather than later.

Whether long-term plans should require Board approval is an open question.
Approval by the Board would mean that recovery of the costs of any capital expenses
would be more likely; however, Board approval might remove some of the ability of the
utility to change plans if conditions change.

4. Historically, rates were set by the Board based upon an historic 12-month
test year, with certain exceptions specified in the statute. The Legislature amended the
ratemaking process to allow for future test years that requires the Board to approve
rates based upon projected costs for a 12-month period beginning no later than the date
on which the proposed rates are to go into effect. The statute requires the Board to
conduct a subsequent proceeding to determine if the costs and revenues approved
based upon a future test year are reasonably consistent with the actual costs and
revenues experienced by the utility.

Rates based upon an historic test year and rates based upon a future test year
are to be based upon evidence presented in a contested case proceeding and are to be
just and reasonable. Discussions at Charrette #1 included a proposal that the future
test year requirements be amended to allow a utility to make a multi-year filing that
would require the Board to approve rates for an extended period of time beyond the
current statute. The proposal discussed at Charrette #1 included in the multi-year proposal an attrition relief mechanism (ARM) so the utility could recoup cost increases that occur during the multi-year plan.

Adoption of a requirement that would allow a utility to file a multi-year plan does not appear on its face to be reasonable. Under such a plan, it appears that a utility would be able to adjust rates without a full review of the utility’s costs and revenues and appears to guarantee a utility the approved ROE rather than providing a utility the opportunity to earn its approved ROE. There appears to be no need for a multi-year plan using projected costs and revenues. A future test year should allow a utility to project its costs and revenues for the next few years after those rates are approved and, with the subsequent proceeding to check on the reasonableness of the approved rates, there is already a mechanism for adjusting rates if actual costs and revenues are significantly different than those approved by the Board. Without a multi-year plan, a utility is more likely to adopt efficiencies that reduce the cost of providing service.

5. Another issue raised by the participants is whether the Legislature should amend the Board’s authority to require rate-regulated utilities to file general rate case proceedings at least every five years so that rates can reflect a current allocation of costs and revenues among customer classes. Although disputed by some participants, the issue is raised because the revenue sharing mechanism approved by the Board for MidAmerican has allowed MidAmerican to only file one application for a general rate increase in over 20 years. The last general rate case proceeding filed by MidAmerican was in 2013 and MidAmerican has projected that it will not be required to file another application until around 2030. Some participants suggest that the fact that MidAmerican
has not filed a general rate case increase application since 2013 means that the
allocations among customer classes approved by the Board in 2014 in Docket No.
RPU-2013-0004 are out of date and do not reflect the proper allocation of current costs
and revenues. Other utilities have filed applications for general rate increases with
more frequency and, in setting rates in those dockets, the Board has reviewed the
allocation of costs among customer classes.

The participants recognize that, even if the Board reviewed the allocation of costs
outside of a general rate case proceeding, a new rate design based upon the results
from that review could not shift costs among customer classes, and change rates,
outside of a general rate case proceeding. The adjustment in rates is the ultimate goal
of the review of the general rate case.

The underlying issue is whether a utility that has an approved revenue sharing
mechanism should be required to file a general rate case application at least every five
years to update its rate design. Currently, MidAmerican files updated data that shows
how the allocation approved by the Board is allocating costs. Those updates have not
demonstrated that a new rate case would change the allocation of costs. It appears
from the discussion that the real issue is how to keep the rates paid by the large
commercial and industrial customers competitive with rates in other jurisdictions.
Frequent rate cases may not be the best way to address that issue, except that large
commercial and industrial customers could propose new services for Board
consideration in a general rate case proceeding. The issue with any new service is
whether costs shifted to other customers is reasonable.
The other issue is whether the Legislature should include a requirement as part of the rate-regulation scheme in Iowa that a utility file a revenue sharing mechanism plan with the Board. The success of MidAmerican’s revenue sharing mechanism in stabilizing rates is clear and requiring other rate-regulated utilities to file similar plans could make Iowa more competitive because rates would be stabilized over a period of time.

One of the primary criticisms of cost-of-service rate regulation is that it provides an incentive for utilities to increase rate base to increase revenue. How to remove that incentive and still allow a utility to recover the cost of providing service is an ongoing inquiry that might be solved by a revenue sharing mechanism. Especially for rate-regulated electric utilities. Using the PTCs provided by the IRA and the change in tax laws that allow a utility to transfer the PTCs to third parties, a properly designed revenue sharing mechanism could provide an alternative to the frequency of increasing rates.

As MidAmerican has shown, a revenue sharing mechanism could allow a utility to operate in a semi-deregulated way and still maintain the protections afforded by cost-of-service and exclusive service territory regulation.

6. As part of the discussion in Charrette #1 and in initial comments, issues were discussed regarding rate regulation of sewer and water utilities. Several of the proposals for consideration involve automatic adjustment mechanisms. These mechanisms remove consideration of specific costs from a general rate case proceeding and should be used sparingly. The Board has approved a Qualified Infrastructure Plant (QIP) automatic adjustment mechanism for recovery of fixed costs for certain non-revenue producing distribution systems improvement projects for rate-
regulated water utilities. The Board has also approved a Non-Recurring Expense automatic adjustment mechanism that captures rate effects of certain temporary items that are not included in rate base.

These automatic adjustment mechanisms were approved in general rate case proceedings and the approval of any additional automatic adjustment mechanisms should also be considered as part of a general rate case proceeding. The Legislature should not create exceptions to the review and approval of automatic adjustment mechanisms outside of a general rate case where the Board can consider the issues involved and balance the interests of ratepayers and the utility in setting just and reasonable rates.

Another example of the Legislature determining that public policy required an exception to the general rate-regulation statute is in Iowa Code § 476.84. That statute requires Board approval of the acquisition by a rate-regulated utility of a non-rate-regulated public utility system valued at $500,000 or more. Iowa Code § 476.84(2)(b) provides that the acquiring utility may apply for approval of the tariffed rates to be charged to the customers of the acquired utility. Iowa Code § 476.84(2)(c) requires the Board to specify in advance the ratemaking principles that will apply when the costs of the utility are included in regulated rates. Iowa Code §§ 476.84(2)(c) and (d) describe considerations for the Board in setting advance ratemaking principles for setting rates for the customers of the acquired utility.

The Board has approved acquisitions of non-rate-regulated utilities by a rate-regulated water utility. From the discussion at Charrette #1, and filings in the dockets, it appears that the language requiring the Board to approve a tariff for the acquired
customers and to establish advance ratemaking principles has caused the cost of these proceedings to be significant and has resulted in issues in the dockets about what the advance ratemaking principles language requires. As a result of those discussions, it appears evident that the statute needs to be amended to clarify what is necessary for the Board to decide if an acquisition is approved. One statutory requirement that needs to be considered is that the acquiring rate-regulated utility cannot charge the acquired utility’s customers for service without a tariff and the tariff has to be approved by the Board. How to implement that ratemaking requirement and make the review more efficient and less costly needs to be addressed. Proposed statutory changes will be addressed in Charrette #3.

C. Conclusion

These final comments address some of the issues discussed at Charrette #1. I respectfully request that the Board also consider my oral comments about other issues raised during the Charrette and thank the Board for the opportunity to provide comments in this docket. I look forward to the discussions in the next two Charrettes.

Dated: September 8, 2023

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