

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

IN RE:  MIDAMERICAN ENERGY COMPANY	DOCKET NO. RPU-2014-0002
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**ORDER APPROVING SETTLEMENT WITH MODIFICATIONS**

(Issued January 20, 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.

Although Iowa Code § 476.53(3)"d" allows the ratemaking principles proceeding to be combined with a proceeding for issuance of a certificate under Iowa Code chapter 476A, the two proceedings were not combined. MidAmerican noted in its request for ratemaking principles that it obtained a declaratory order in Docket No. DRU-03-3 (issued June 6, 2003) indicating that a 476A certificate was not necessary for another wind project when it was configured such that less than 25 MW of capacity was connected to each gathering line. Iowa Code §§ 476A.1 and 476A.2. MidAmerican believed all the relevant facts and law with respect to Wind IX are indistinguishable from those on which the declaratory order in Docket No. DRU-03-3 was based. MidAmerican concluded that it is reasonable to rely upon the declaratory ruling and that no 476A certificate is necessary for Wind IX.

## **II. SUMMARY OF SETTLEMENT AGREEMENT**

On November 19, 2014, MidAmerican and Consumer Advocate filed a proposed Settlement Agreement. The Settlement Agreement, if approved, would resolve all issues in the proceeding.

Among other things, the Settlement Agreement stated that the signatories agree that MidAmerican had satisfied the two conditions precedent for a ratemaking principles proceeding. MidAmerican and Consumer Advocate also agree to the ratemaking principles as proposed by MidAmerican, except for modifications to the ROE principle.

The proposed Settlement Agreement contains three modifications to MidAmerican's ROE principle. MidAmerican initially proposed an ROE of 11.75 percent, while Consumer Advocate proposed 11.3 percent. The Settlement Agreement provides for an ROE of 11.5 percent. In addition, the Settlement Agreement specifies an ROE of 10 percent for use in calculating the AFUDC rate. MidAmerican initially used its requested ROE of 11.75 percent while Consumer Advocate filed testimony supporting a 10 percent return for use in calculating the AFUDC rate; the Settlement Agreement uses the AFUDC rate proposed by Consumer Advocate. Finally, MidAmerican and Consumer Advocate deleted the language "50 percent of the capital invested" from the ROE principle as originally proposed by MidAmerican because it created confusion. The deletion made the language consistent with that used in Wind VIII, which was MidAmerican's prior ratemaking principle proceeding for wind generation, identified as Docket No. RPU-2013-0003.

### **III. CONDITIONS PRECEDENT**

Before determining applicable ratemaking principles for Wind IX, the Board must make two findings pursuant to Iowa Code § 476.53(3)"c." These are conditions precedent to a determination of ratemaking principles, because if the Board cannot make these findings, the utility cannot receive ratemaking principles. First, the Board must determine that the public utility has in effect a Board-approved energy efficiency plan. Second, the utility must demonstrate that it has considered other sources for

long-term supply and that the facility is reasonable when compared to other feasible alternative sources of supply. MidAmerican and Consumer Advocate agreed in the Settlement Agreement that these conditions were satisfied.

**1. Energy Efficiency Plan**

With respect to the first condition precedent, MidAmerican has in effect a Board-approved energy efficiency plan. MidAmerican witness Fehr provided testimony regarding MidAmerican's current energy efficiency plan, identified as Docket No. EEP-2012-0002. The Board approved the plan on December 31, 2013, and the plan will remain in effect through December 31, 2018, subject to any modifications. Witness Fehr detailed the success of MidAmerican's energy efficiency efforts from 2009 through 2013, with MidAmerican spending 101 percent of budget on energy efficiency for customers and reaching 85 percent of planned electric savings and 110 percent of the peak shaving goal. Total electric savings between 2009 and 2013 were 1,167,162,105 kWh with a reduction in peak load of 560 MW.

MidAmerican has a Board-approved energy efficiency plan and the Board has issued no orders finding that MidAmerican is not in compliance with any Board orders in its EEP docket. The first condition precedent is satisfied.

**2. Reasonableness of the Facility**

The second condition precedent is whether a utility has considered other long-term sources of supply and shown that the facility is reasonable when compared to other feasible supply sources. Iowa Code § 476.53(4)"c"(2). In making this

determination, the Board must look at the need for the facility, that is, whether the facility is a reasonable alternative to meet one of the statute's goals, "to attract the development of electric power generating ... facilities within the state in sufficient quantity to ensure reliable electric service to Iowa consumers ... ."

If a facility does not meet the needs of Iowa consumers, it is not eligible for ratemaking principles treatment. The Board addressed the meaning of this statement in a previous ratemaking principles proceeding for a wind facility with a nameplate capacity of up to 554 MW. The Board said:

While MidAmerican has not demonstrated an immediate need for the wind facility (or any other generation facility) in the sense that it will be unable to meet customers' demand in 2007-2009 without the facility, the Board does not believe a determination of need requires a showing that the lights will go out if the facility is not built. That would not be a prudent planning criterion.

(MidAmerican Energy Company, "Order Approving Stipulation and Agreement,"

Docket No. RPU-05-4 (April 18, 2006), p. 6). The issue of whether a proposed facility is reasonable was first addressed in Docket No. RPU-01-9. In its final order, the Board said:

The ratemaking principles statute does not refer to "least-cost" alternatives. Instead, Iowa Code § 476.53(3)"c"(2) only requires that the "rate-regulated public utility has demonstrated to the board that it has considered other sources for long-term electric supply and that the facility or lease is reasonable when compared to other feasible alternative sources of supply." (Emphasis added). In a ratemaking principles proceeding, the Board does not have to conduct the least-cost analysis formerly required in a siting proceeding involving a public utility. The proposed

facility need only be reasonable when compared to other alternative sources of supply.

While cost remains a factor, elimination of the least-cost requirement is consistent with the intent of the ratemaking principles statute, which is to attract electric power generating facilities to this state. Elimination of the least-cost requirement now allows non-cost factors to play a role in the Board's decision that a public utility has satisfied this requirement as a condition precedent to receiving ratemaking principles. These non-cost factors, such as security and reliability, could in some cases be determinative.

(Docket No. RPU-01-9, "Order," May 29, 2002, p. 6).

MidAmerican demonstrated that Wind IX was part of its continuing strategy to reduce its carbon footprint. MidAmerican said that Wind IX would allow it to take advantage of federal production tax credits (PTCs). MidAmerican said Wind IX compared favorably to conventional generation resources because of the zero emissions, no fuel price volatility, economic benefits, and improved fuel diversity. (Tr. 148-160). MidAmerican said that Wind IX could be added at no net cost to customers. (Tr. 160). Also, MidAmerican said Wind IX compared favorably with other renewable generation sources.

Wind brings environmental compliance benefits at a price that cannot yet be obtained from other renewable sources at a utility scale. The addition of Wind IX will not degrade the transmission network and MidAmerican will perform all required transmission upgrades. MidAmerican's analysis shows that it has satisfied the second condition precedent and is therefore eligible to receive ratemaking principles.

The Board will address the economic benefits of Wind IX in a subsequent section. While the two statutory conditions have been satisfied to justify awarding ratemaking principles, those principles may need to be modified for the risks and benefits of Wind IX to be better balanced between MidAmerican and its ratepayers.

In addition, in any future ratemaking principle proceedings, MidAmerican is to provide in its prefiled testimony not only a comparison of the proposed generation facility with other feasible long-term sources of supply, but additional analysis regarding interaction of generating resources which might be added within reasonably short time frames. Also, MidAmerican is to address in any future ratemaking principles filings whether there is an upper limit to the amount of wind needed in MidAmerican's resource portfolio and how MidAmerican plans to meet any projected capacity shortfall.

#### **IV. RATEMAKING PRINCIPLES**

MidAmerican asked for approval of eight advance ratemaking principles that would govern the recovery of project costs and treatment of project benefits. The Settlement Agreement asked the Board to approve MidAmerican's principles as filed, except for two modifications (and a clarification by deleting language) to the ROE principle. 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." The Board will address each ratemaking principle contained in the proposed Settlement Agreement.

**1. Iowa Jurisdictional Allocation**

A portion of Wind IX will be allocated to Iowa in the same manner as prior MidAmerican wind projects that received advance ratemaking principles. This principle is consistent with prior cases and allocates to Iowa customers most of Wind IX's costs and benefits because Wind IX is being proposed in response to Iowa legislation that promoted the expansion of rate-regulated utility-owned generation in Iowa.

**2. Cost Cap**

The proposed cost cap for Wind IX is \$1.725 million per MW (including AFUDC) for the completed project. If actual capital costs of Wind IX are lower, the amount included in rate base in the future will be equal to actual capital costs. If actual costs exceed the cap, MidAmerican will be required to establish the prudence and reasonableness of such excess costs before they can be included in rates.

MidAmerican said the cap was set at a price that provides customer benefits over the life of the facilities with no net costs to customers. MidAmerican noted that the cost cap is below the approved cap in Wind VIII and estimates the final costs of Wind IX will be below the cap.

There is evidence that the actual cost of Wind IX will be lower than the cost cap contained in the Settlement Agreement. While the Board understands that MidAmerican sets the cap at its calculation of no net costs to customers, the Board believes the cap in this case should be set closer to the projected actual costs of

Wind IX. This project is not justified by customer needs; it is justified by economic benefit. It would not be reasonable to shift risks to customers (by means of these advance ratemaking principles) while potentially offering those customers no share of the resulting economic benefit. The Board will set the cost cap at no more than \$1.5 million per MW (including AFUDC) and expects that actual costs will be less, based on the evidence at the hearing.

This lower cap reduces the risk to customers and provides an incentive to MidAmerican to keep costs low. Also, if costs exceed the cap, MidAmerican can seek to recover any costs above the cap that are reasonably and prudently incurred in a subsequent rate proceeding.

### **3. Size Cap**

The size cap principle states that the ratemaking principles would be applicable to all new MidAmerican wind capacity, up to 162 MW, which is built as part of Wind IX. If MidAmerican later decides to install additional wind, it would have to make another ratemaking principles filing to receive advance ratemaking treatment for any wind installed above 162 MW. Previous wind applications have included a size cap.

### **4. Depreciation**

The depreciable life of Wind IX for ratemaking purposes will be 30 years, which is the same as approved in Wind VIII. MidAmerican provided letters from turbine manufacturers GE Energy and Siemens Energy supporting a 30-year

depreciation life. (Tr. 81). MidAmerican noted that higher capacity factors or running rates should not reduce the overall life of a unit, although maintenance expenses would increase. (Tr. 82-86).

## **5. Return on Equity**

MidAmerican and Consumer Advocate modified the original ratemaking principles proposed by MidAmerican with respect to ROE. The Settlement Agreement provides that the allowed return on the common equity portion of Wind IX that will be included in Iowa electric rate base will be 11.5 percent. This is between MidAmerican's initial request (11.75 percent) and Consumer Advocate's initial recommendation (11.3 percent). The 11.5 percent agreed to in the Settlement Agreement is lower than the 11.625 percent approved for Wind VIII.

There is also a separate AFUDC rate provision that establishes an ROE of 10 percent to be applied to AFUDC for Wind IX. MidAmerican initially requested 11.75 percent to be used for AFUDC but in the Settlement Agreement agreed to Consumer Advocate's proposed 10 percent. This is identical to the AFUDC rate approved in Wind VIII.

The final change to the ROE principle from MidAmerican's filing was to remove the language "50% of the capital invested" to eliminate confusion the language created. This change is also consistent with the Wind VIII approved ratemaking principles.

MidAmerican's initial ROE proposal and Consumer Advocate's initial recommendation were fairly close and the agreed-upon ROE is between the two proposals. Both parties agreed that the cost of equity should be higher than current capital costs because the ratemaking principle fixes Wind IX's ROE for the 30-year life of the facilities. Also, both agreed that the legislative intent embodied in Iowa Code § 476.53 and prior Board decisions justify a return above current market conditions. Finally, the Board notes that the agreed-upon ROE is lower than that awarded in MidAmerican's last wind ratemaking principles proceeding for Wind VIII.

With respect to AFUDC, MidAmerican initially sought to apply the general ROE to AFUDC. Consumer Advocate proposed a separate ROE for AFUDC that was lower than the return on common equity for the overall project. The separate AFUDC rate agreed to reflects that AFUDC costs are incurred under current market conditions, not the 30-year life of the Wind IX facilities.

The Settlement Agreement also removed some confusing language in MidAmerican's initial ratemaking principles proposal regarding capital structure. It is now clear that, consistent with prior ratemaking cases, MidAmerican's capital structure and costs (except for ROE for Wind IX) shall be determined in each rate proceeding in a manner that will be identical to the capital structure used for the remainder of MidAmerican's rate base.

## **6. Cancellation Cost Recovery**

MidAmerican's cost recovery principle states that in the event MidAmerican cancels any Wind IX site for good cause, MidAmerican's prudently-incurred costs shall be amortized over a period of ten years beginning no later than six months after cancellation. The principle further provides that the annual amortization is to be recorded above-the-line and included in MidAmerican's revenue sharing or revenue requirement calculations, but the unamortized balance is not to be included in those calculations. This is similar to a principle previously approved and requires that the prudence of any cancellation costs be established in a future proceeding before there can be any recovery.

Consumer Advocate and MidAmerican agreed at the hearing that this provision should be clarified to explicitly recognize the principle's intent that only unreimbursed cancellation costs are to be recovered. The Board will modify the cancellation cost recovery principle to read as follows:

In the event MidAmerican cancels any Wind IX site for good cause, MidAmerican's prudently incurred and unreimbursed costs shall be amortized over a period of ten years beginning no later than six months after cancellation. The annual amortization shall be recorded above-the-line and included in MidAmerican's revenue sharing or revenue requirement calculations, but the unamortized balance shall not be included in rate base in any such calculations. (new language underlined).

**7. Renewable Energy Credits, CO2 Credits, and Other Similar Credits**

In this principle, MidAmerican proposed that the Iowa portion of any revenues or benefits from the sale of environmental attributes from Wind IX (RECs, CO2 credits, and perhaps others) be recorded in MidAmerican's Iowa electric operating income and reflected in a future rate proceeding. By recognizing all costs and benefits of Wind IX in a future rate proceeding, there will be a proper matching of customer benefits and customer costs.

The principle provides that revenues from the sale of environmental attributes be flowed through MidAmerican's energy adjustment clause (EAC). This principle is consistent with those approved in prior MidAmerican wind ratemaking principle dockets.

**8. Federal Production Tax Credit**

The federal PTC principle provides that the Iowa portion of the federal PTC benefits associated with Wind IX will be recorded in MidAmerican's Iowa electric operating income and reflected in a future rate proceeding. In those subsequent proceedings, the principle provides that the Iowa portion of federal PTCs will flow through MidAmerican's EAC. This principle is also consistent with similar principles approved in prior MidAmerican wind ratemaking dockets.

**9. Economic Analysis and Additional Payments to Customers**

While MidAmerican's customers will receive a reduction of fuel costs that flow through the EAC as a result of Wind IX, including Wind IX in MidAmerican's revenue

sharing calculation that was approved in Docket No. RPU-2013-0004 will reduce any revenue sharing benefits to customers until such time as MidAmerican has a rate case that includes Wind IX in the company's rate base. Overall customer benefits vary significantly over time and are dependent on projected values and events that may or may not in fact occur.

The proposed Settlement Agreement does not represent a reasonable balance of the risk undertaken by MidAmerican and the risk assumed by its customers if Wind IX goes forward, particularly since much of MidAmerican's risk had been fixed by the time of the hearing. In the Wind VIII settlement, MidAmerican included a ratemaking principle that flowed an additional \$10 million per year to customers through the EAC prior to Wind VIII units being put into rate base, once certain installed capacity amounts are met.

A ratemaking principle like that included in Wind VIII more appropriately balances the risks and rewards between MidAmerican and its customers. The Board will modify the Settlement Agreement by including the following ratemaking principle:

Upon completion of at least 50 MW of the Wind IX project and in addition to all other benefits that will flow to customers, prior to a future rate case customers will receive \$2 million per year in energy adjustment clause credits.

Without such a principle, the proposed Settlement Agreement does not appropriately balance the risks and rewards of Wind IX, placing too much of the risk on MidAmerican's customers. The additional \$2 million in payments, like the payments

in Wind VIII, provide a reasonable balance of risks and rewards between MidAmerican and its ratepayers. This additional \$2 million per year is not to be offset by the mechanics of MidAmerican's revenue sharing mechanism approved in Docket No. RPU-2013-0004.

#### **V. REASONABLENESS OF SETTLEMENT**

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, as modified by the Board, finds it to be reasonable, in the public interest, and not contrary to any law.

As discussed previously in Section III, MidAmerican has satisfied the two conditions precedent in Iowa Code § 476.53(3)"c" and is therefore eligible for advance ratemaking principles. The ratemaking principles associated with Wind IX, as modified by the Board, are reasonable. The Settlement Agreement as a whole will further the diversity of MidAmerican's generation resources, reduce its reliance on fossil-fueled generation, and position MidAmerican to meet ongoing and future environmental mandates and potential renewable mandates in a manner that is more likely to benefit its ratepayers. The Settlement Agreement's benefits to retail

customers will help ensure that MidAmerican's current and future customers continue to enjoy adequate service and facilities at just and reasonable rates. Iowa Code §§ 476.6 and 476.8.

## **VI. ADDITIONAL CONCERNS AND REQUIREMENTS**

The Board will require MidAmerican to file semi-annual reports regarding the construction and operation of Wind IX, with the reporting requirement ending when Wind IX's assets are included in MidAmerican's rate base. The reports are to include information regarding the actual operating and capital costs of Wind IX, the amount of customer rate relief flowed through the EAC, the retail fuel cost reduction attributable to Wind IX, and income from PTCs, REC sales, capacity sales, and net system benefits attributed to Wind IX. Reports shall be due on June 1 and December 1 of each year, with the first report due on or before June 1, 2015.

In addition, the Board is aware that there could be multi-billion dollar additions to MidAmerican's rate base over the next decade; the impact on rates would depend on the timing of the rate case. At least the following could be eligible for inclusion in MidAmerican's next full rate proceeding:

1. Undepreciated amount of Wind VIII.
2. Undepreciated amount of Wind IX.
3. The amount in the depreciation deferral account established in MidAmerican's last rate case, which can be up to \$300 million.
4. Generation which may need to be added to address MidAmerican's projected capacity shortfall.
5. Capital additions associated with maintenance and upgrade of MidAmerican's distribution, transmission, and generating systems.

The Board intends to conduct a review of MidAmerican's electric energy supply later this year. The proceeding is known as an ARC proceeding. In its ARC filing, the Board will require MidAmerican to provide an analysis of the rate issues identified above and their potential impact on customers' rates.

Finally, the Board is disappointed that MidAmerican did not always fully respond to the Board's requests for information the first time, requiring subsequent requests by the Board. Prompt and full response is particularly important when MidAmerican asks for expedited review. Moreover, it was apparent at the hearing that MidAmerican had sufficient information to file its petition at least two or three months prior to the filing date. Rather than filing at that time to allow the Board adequate time for review, MidAmerican chose to file at a later date and provide incomplete information and responses. To be clear, in future ratemaking principle filings the Board expects to see an analysis that accurately reflects all customer impacts included in the initial filing, and MidAmerican should also use as a guide the information requests issued in this docket and include similar information, unless it is clearly irrelevant (in which case MidAmerican should explain why the information is not included).

## **VII. FINDINGS OF FACT**

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

1. It is reasonable to find that MidAmerican has in effect a Board-approved energy efficiency plan as required under Iowa Code § 476.6(19).

2. It is reasonable to find that MidAmerican has a need for Wind IX and that Wind IX benefits ratepayers by, among other things, enabling MidAmerican to meet current and future environmental regulations, providing low-cost energy to retail customers, reducing MidAmerican's reliance on carbon-based generation, and diversifying MidAmerican's supply portfolio.

3. It is reasonable to find that MidAmerican considered other long-term sources of electric supply and that Wind IX is reasonable, both for cost and non-cost reasons, when compared to other feasible alternative sources of supply.

4. It is reasonable to clarify the cancellation cost recovery principle to ensure that only unreimbursed cancellation costs are recovered.

5. It is reasonable to modify the cost cap contained in the Settlement Agreement and set the cost cap at no more than \$1.5 million per MW.

6. Upon completion of 50 MW of Wind IX and until MidAmerican's next rate adjustment in a rate proceeding, it is reasonable to flow to MidAmerican's customers an additional \$2 million per year in EAC benefits.

7. It is reasonable to approve the ROE principle agreed to by MidAmerican and Consumer Advocate, which includes an 11.5 percent ROE and a 10 percent ROE for use in calculating the AFUDC rate.

8. The remaining ratemaking principles not specifically addressed in these findings are reasonable.

9. The Settlement Agreement between MidAmerican and Consumer Advocate, subject to the conditions and modifications contained in this order, is reasonable, consistent with law, and in the public interest.

### **VIII. CONCLUSIONS OF LAW**

The Board has jurisdiction of the parties and the subject matter in this proceeding, pursuant to Iowa Code chapter 476 (2013).

### **IX. ORDERING CLAUSES**

#### **IT IS THEREFORE ORDERED:**

1. The Settlement Agreement filed by MidAmerican Energy Company and the Consumer Advocate Division of the Department of Justice on November 19, 2014, is approved, subject to the modifications and conditions contained in this order.

2. MidAmerican shall file semi-annual reports containing the information identified in the body of this order on June 1 and December 1 of each year, with the first report due on or before June 1, 2015. This reporting requirement shall end when Wind IX's assets are included in MidAmerican's rate base.

3. MidAmerican is to provide the information identified in this order in the appropriate dockets.

4. Motions and objections not previously granted or sustained are denied or overruled. Any argument 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.

**UTILITIES BOARD**

/s/ Elizabeth S. Jacobs

/s/ Nick Wagner

ATTEST:

/s/ Judi K. Cooper  
Executive Secretary, Deputy

/s/ Sheila K. Tipton

Dated at Des Moines, Iowa, this 20<sup>th</sup> day of January 2015.