

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

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IN RE:  MIDAMERICAN ENERGY COMPANY	DOCKET NO. RPU-05-4
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**ORDER APPROVING STIPULATION AND AGREEMENT**

(Issued April 18, 2006)

**INTRODUCTION AND PROCEDURAL HISTORY**

On December 16, 2005, MidAmerican Energy Company (MidAmerican) filed with the Utilities Board (Board) an application for determination of ratemaking principles pertaining to a proposed wind-powered generation project with a maximum nameplate capacity of 545 MW. MidAmerican said it had not yet determined the ultimate nameplate size and location for the project, but it will be installed at more than one location.

As part of its application, MidAmerican filed a stipulation and agreement (Settlement) signed by MidAmerican and the Consumer Advocate Division of the Department of Justice (Consumer Advocate). The Settlement asks that the Board approve MidAmerican's requested ratemaking principles. The Settlement provides that MidAmerican commits not to seek any general increase in Iowa electric base rates to become effective during 2012, unless its return on equity falls below 10 percent. A revenue sharing mechanism is also contained in the Settlement, which extends an existing arrangement for another year, until the end of 2012.

On January 4, 2006, the Board issued an order requiring MidAmerican to file additional information. The Board noted there were significant pieces of information missing from the filing that were necessary for the Board to conduct its review. MidAmerican filed its response on January 12, 2006.

Subsequent to reviewing the additional information filed, the Board issued an order on January 20, 2006, scheduling a technical conference. The Board noted that the responses MidAmerican filed to the Board's January 4, 2006, order were not comprehensive and did not contain sufficient information for the Board to carry out its statutory responsibilities under the ratemaking principles statute. The Board said that under the current state of the record, the Board could not proceed to a decision in the docket.

The technical conference was scheduled to enable the Board's staff to discuss with MidAmerican the type of information required for the Board to begin its work. The conference was held on January 26, 2006, and was open to all parties and any others interested in the docket. No formal record was kept of the discussions. On February 2, 2006, MidAmerican filed additional information as a result of the discussions at the technical conference.

After reviewing MidAmerican's February 2 filing, the Board determined that it contained sufficient information to proceed and, on February 16, 2006, the Board docketed MidAmerican's filing and issued a procedural schedule. The Board also granted a petition to intervene filed on February 7, 2006, by the Iowa Farmers Union (IFU). The petition to intervene included a request for hearing. The Board's docketing order scheduled a hearing to begin on April 11, 2006. MidAmerican, in its

initial filing, asked for expedited treatment, although its original requested decision deadline (January 27, 2006) could not be met because MidAmerican did not file complete initial information until February 2, 2006. The Board set the schedule for an expedited hearing, taking into consideration the time the IFU required to evaluate MidAmerican's filing.

On March 6, 2006, the IFU filed a withdrawal of its request for hearing. The IFU said that it had obtained its objective, which was to facilitate the opportunity for small community based-wind projects to make sales to MidAmerican. Included in IFU's pleading were the terms of an agreement it reached with MidAmerican.

The agreement with IFU provides that MidAmerican will purchase energy and capacity from wind projects of 2.5 MW or less interconnected directly to MidAmerican's distribution system up to a total aggregate nameplate capacity of 40 MW. The energy rate to be paid for a levelized 20-year term is 2.6 cents per kWh; the capacity rate for a levelized 20-year term shall be \$4.62 per kW-month for the minimum monthly accredited capacity during the preceding 12 months. Renewable energy credits and environmental attributes of wind power will remain with the seller and are not included in the referenced prices. The agreement between IFU and MidAmerican appears to be filed for informational purposes only; IFU does not ask for Board approval of the agreement or any of its terms as part of or as a condition to issuing ratemaking principles in this docket.

Also on March 6, 2006, MidAmerican filed a motion to cancel the hearing. MidAmerican said there was sufficient information before the Board to make its required findings and enter an order approving MidAmerican's requested ratemaking

principles. The Board issued an order on March 31, 2006, canceling the evidentiary hearing scheduled for April 11, 2006. In the order, the Board said that after it had completed its review of all the information submitted by MidAmerican, the Board would either reschedule the hearing or proceed to rule on the merits of the stipulation and agreement. After reviewing all the information filed, the Board has determined a hearing is not necessary and will proceed to rule on the merits of the stipulation and agreement.

Although Iowa Code § 476.53(3)"d" allows the ratemaking principles proceeding to be combined with a proceeding for issuance of a generation certificate under Iowa Code chapter 476A, the two proceedings were not combined here. MidAmerican states that the proposed wind project will have no more than 25 MW of generating capacity located on any single collector or "gathering" line. Under those circumstances, a generation certificate is not required. See, MidAmerican Energy Company, "Declaratory Order," Docket No. DRU-03-3 (6/6/03).

Ratemaking principles proceedings are conducted pursuant to Iowa Code § 476.53 (2005). 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. Alternate energy production facilities, such as the wind project proposed by MidAmerican, 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. . . ."

### **CONDITIONS PRECEDENT**

Before determining the applicable ratemaking principles for the wind project, 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 a reasonable alternative to meet its electric supply needs when compared to other feasible alternative sources of supply.

With respect to the first condition precedent, MidAmerican has in effect a Board-approved energy efficiency plan. MidAmerican witness Stevens provided prefiled testimony regarding MidAmerican's energy efficiency plan. For 2004, MidAmerican said its actual plan expenditures exceeded the budget by 12 percent; for 2005, expenditures are expected to exceed the budget by 23.9 percent. MidAmerican received approval of its current energy efficiency plan on June 23, 2003, in Docket No. EEP-03-1. (Stevens Direct, pp. 21-22).

The second condition precedent is whether a utility has considered other long-term sources of supply and shown that the facility is a reasonable alternative to meet

its electric supply needs when compared to other feasible supply sources. In making this determination, the Board must look at the need for the facility; that is, is the facility 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 and provide economic benefits to the state." If a facility does not meet the needs of Iowa consumers, the Board does not believe it is eligible for ratemaking principles treatment.

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 has shown that the proposed facility is projected to benefit both the present and future needs of MidAmerican's customers in several ways and the proposed facility is a feasible and reasonable way to attain these benefits.

First, MidAmerican indicates it is facing a 235 MW capacity deficiency for regulated load (hot weather) by 2010 and a 104 MW deficiency (normal weather) in 2011. The proposed project is to be in service by 2007, three years before the projected capacity deficit. If load growth is greater than expected, there could be a capacity deficit based on hot weather or normal weather prior to 2010. The proposed wind project will contribute up to approximately 109 MW toward MidAmerican's accredited capacity, because approximately 20 percent of wind capacity is generally accredited to contribute towards system peak. Thus, the proposed facility would

eliminate the projected 104 MW deficiency in 2011 (based on normal weather conditions).

Second, there are immediate benefits to customers (upon project completion) from the expansion of an electricity source with a price that does not fluctuate with fossil fuel prices, like coal and natural gas. Wind is also not subject to projected increases in transportation rates that have been experienced and are projected for coal transport.

Third, MidAmerican states that the new wind project would improve operational flexibility for MidAmerican's new coal plant in Council Bluffs (and other generation units) and its resource portfolio. The new Council Bluffs plant should be on-line in 2007.

In generation planning, the general rule has traditionally been that the longer a utility can avoid building generation, the better off customers are, because new generation costs are deferred. However, general rules often have exceptions. A question posed to MidAmerican was whether the project would be more cost-effective if delayed for two to three years. The economic analysis filed showed it would not be and that, in fact, it might not be feasible for MidAmerican to pursue the project in two or three years, depending on the level of the federal production tax credit at that time.

MidAmerican has shown in the additional information provided that there is a current opportunity to economically add wind generation that will meet future needs and provide customers an immediate hedge against the price fluctuations of fossil fuels. MidAmerican's market projections, which are based on what appear to be

conservative price forecasts, demonstrate a significant additional benefit to customers through increased revenue sharing if the wind project is completed. The risk to customers, who are in effect guaranteeing the wind project through ratemaking principles, is minimal; the greater financial risk to customers is if the project does not proceed, according to MidAmerican's analysis.

MidAmerican demonstrated in the prefiled testimony of its witnesses, application, and additional information filed that it has considered other sources for long-term electric supply and that the proposed wind project is a reasonable alternative to meet its electric supply needs when compared to other feasible alternative sources of supply. The statute does not require that the wind project be the least-cost alternative, but a reasonable alternative to other sources of supply. Information provided subsequent to the application demonstrated the wind project is reasonable when compared to both renewable and conventional alternatives.

Fuel diversity is more important than ever, given price fluctuations and price projections for fossil fuels, which include rail transport for coal. Reducing this price risk to customers is significant, although difficult to value. The economics of this transaction also reduce the risk to customers. The federal production tax credit is currently scheduled to end on December 31, 2007; many believe that even if extended, the credit will be of less value. MidAmerican's analysis showed that delay would only increase the project's costs, perhaps to the extent it would no longer be feasible, denying customers the benefits of the project discussed above (which include environmental benefits). The economics of the project are currently expected to be favorable to customers and the wind project promotes Governor Vilsack's



announced goal of having 1,000 MW of renewable resources in Iowa and the General Assembly's goal of encouraging the development of renewable energy. Iowa Code § 476.41; Iowa Code § 476.53.

### **SUMMARY OF STIPULATION AND AGREEMENT (SETTLEMENT)**

The Settlement provides for a return on equity of 11.9 percent on the portion of the wind project included in Iowa electric rate base. This is less than the 12.2 percent return approved in MidAmerican's two prior wind power filings. Using the same empirical study as in other wind projects, MidAmerican produced results somewhat lower than the earlier studies due to the decrease in the yield on A-rated utility bonds. MidAmerican indicates the overall risks for this project are similar to its other wind projects. The Settlement contains a per MW installed cost cap, which remains confidential pursuant to Board orders because negotiations with project developers are continuing and release of the cost cap information could increase project costs. If costs fall below the cap, MidAmerican does not need to further establish the prudence or reasonableness of the expenditures. The cost cap is inclusive of associated costs necessary for the reliable integration of the wind project into the MidAmerican delivery system. MidAmerican would be required to establish the prudence and reasonableness of any costs in excess of these amounts. The depreciation life of the wind facilities for ratemaking purposes is 20 years.

In addition to ratemaking principles specifically addressing the wind project, the Settlement continues, for one additional year, the revenue freeze and revenue sharing settlement approved in MidAmerican's most recent rate case, Docket Nos.

RPU-01-3 and RPU-01-5, as extended in Docket Nos. RPU-03-1 and RPU-04-3.

MidAmerican commits not to file for a general increase in rates that will be effective prior to December 31, 2012, unless its return on equity falls below 10 percent. As determined in prior dockets, through 2010 the customers' portion of the revenue sharing calculation will be used to offset allowance for funds used during construction (AFUDC) on MidAmerican's new gas, coal, and wind facilities. If AFUDC is covered, the excess will be used to offset depreciation on these facilities. If depreciation is fully offset, any excess will be returned to ratepayers. After 2010, the customers' portion of the 2011 and 2012 revenue sharing calculations will be returned to ratepayers.

Certain credits and sales that will affect the revenue sharing calculation are also addressed. The Settlement provides that the Iowa jurisdictional portion of any revenues from the sale of renewable energy credits and carbon dioxide credits associated with the wind project will be recorded above the line and included in the revenue sharing mechanism. Likewise, the Iowa jurisdictional portion of any federal production tax credit associated with the wind project will be recorded above the line and included in the revenue sharing mechanism. Finally, the Iowa jurisdictional portion of wholesale sales revenues associated with the portion of the wind project included in Iowa's jurisdictional electric rate base will be recorded above the line and included in the revenue sharing mechanism.

It is important to note that the Settlement constitutes a revenue freeze, not a rate freeze. The Settlement does not prohibit revenue neutral changes to minimize

or reduce zonal rate disparities between MidAmerican's pricing zones. The Board is considering such changes in an ongoing docket, Docket No. RPU-04-2.

### **DISCUSSION**

No objections to the proposed Settlement were filed. 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."

MidAmerican's initial filing contained little information about the economics of the project or potential impacts on reliability of the electric delivery system. After subsequent orders and a technical conference, sufficient information was ultimately filed that allows the Board to proceed in determining whether ratemaking principles should be awarded.

In its application, MidAmerican asked for an expedited Board ruling by January 27, 2006, or 42 days after the filing. If MidAmerican had filed complete information in its initial application, the Board would likely have been able to meet this request (assuming a settlement with IFU was timely reached). MidAmerican filed the final portion of the necessary information for Board review on March 17, 2006; this order is being issued about 30 days after that date.

Both in evaluating a case and settlement, Consumer Advocate has broad discovery and investigatory tools at its disposal to perform its statutory obligations, which are different from those of the Board. The results of this extensive investigation and discovery are generally not filed with the Board (and need not be), although selected items may be used as exhibits. Utilities are reminded that when filing a settlement, particularly at the onset of a case, the utility has the burden to

ensure that its filing contains adequate information for the Board to perform its separate and distinct statutory responsibilities, even if the information has already been provided to Consumer Advocate. The Board cannot rely on a settlement standing alone without comprehensive support. This underlying support provides much of the information required for the Board to make the required determination of whether the settlement is reasonable, consistent with law, and in the public interest.

Initial and subsequent information filed by MidAmerican demonstrated the project was a reasonable alternative to meet its electric supply needs when compared to other feasible generation sources and information about fuel diversity and price volatility in coal and natural gas prices was provided. MidAmerican has taken steps to mitigate construction and operating risks and the project will have a positive economic impact on the state as a whole and on the local areas where construction will take place. (Budler Direct, pp. 13-18). The information provided projects a positive benefit from the project for both MidAmerican and its customers under the sharing agreement. While the value of any carbon credits is speculative, the wind project has projected value even if the value of these credits is assumed to be zero.

The wind project will be built at various locations and MidAmerican stated it would not go forward with any of the parts of the proposed project that exceed the cost cap. Sensitivity analyses related to carbon credits, capacity factors, and margins on wholesale sales demonstrate the projected value of the wind project under various scenarios. Transmission costs that MidAmerican included in its overall cost cap could more than triple and the wind project would continue to have positive

projected value, although MidAmerican does not plan to go forward if there are significant transmission costs above the amounts included in the cost cap.

The additional information provided by MidAmerican demonstrates it is more economic to begin the project now than to wait until wind turbines may be more readily available. The analysis shows that if MidAmerican does not add additional wind generation prior to the end of 2007, it might not be cost effective after that date (depending on the federal production tax credit level and other factors). Iowa Code § 476.53(1) states the legislative intent behind the ratemaking principles statute is both to ensure reliable electric service and provide economic benefits to the state. If the project is not built now, the projected economic benefits to the state and MidAmerican's ratepayers might be lost.

MidAmerican's initial filing did not contain adequate information about how the proposed wind project would affect both the reliability of MidAmerican's electric system and the remainder of the transmission system. Later-filed information demonstrates that MidAmerican has operated its current 470 MW of wind generation in a manner that has not adversely affected transmission system reliability and its projections indicate adding the proposed wind project will not impair its ability to meet reliability standards. MidAmerican has assured the Board that if transmission concerns are too costly to mitigate at any given site, the plan for that site will be modified or abandoned.

MidAmerican filed preliminary transmission analysis as part of the information filed in response to various Board orders. Additional detailed transmission studies for the Mid-Continent Area Power Pool (MAPP) should be completed by December

2006. These studies will address, among other things, transmission interconnection and any modifications or additions necessary to the electric delivery system.

MidAmerican has assured the Board the wind project will not negatively impact reliability. MidAmerican's and MAPP's complete analysis and further review may show that additional transmission system improvements or upgrades, beyond those included in MidAmerican's current budget, may be required to maintain adequate and reliable service. The Board is relying upon MidAmerican's commitment to maintain reliability in approving the Settlement and understands that MidAmerican will be required to comply with the terms and conditions of all current and future transmission authorization given by any entity having authority over interconnection and utilization of the transmission system by the expansion project. MidAmerican will be required to file with the Board copies of all transmission and system impact studies it conducts to comply with MAPP or other requirements.

The ratemaking principles contained in the Settlement generally track principles that have been awarded in other ratemaking principles dockets and are consistent with what was approved for two prior wind projects. The 11.9 percent return on equity agreed to by the parties appears to be within the zone of reasonableness given the risks associated with new generation, the lower recent returns on A-rated utility bonds, the intent of § 476.53, and the fact that this return will prevail for the regulated life of the wind facilities.

The other ratemaking principles associated specifically with the proposed wind project, including the cost cap and depreciation life, also appear reasonable. The

Settlement, however, also contains terms other than ratemaking principles for the proposed wind project and these must be addressed.

The Settlement adds another year to the revenue freeze initially approved in Docket Nos. RPU-01-3 and RPU-01-5 and extended in Docket Nos. RPU-03-1 and RPU-04-3. The extension under the current Settlement is until December 31, 2012. This will provide a predictable revenue stream for MidAmerican and provide customers some price certainty, absent revenue neutral changes in rate design. The revenue stability for MidAmerican should encourage the efficient operation of its revenue producing assets.

While a revenue freeze can encourage the deferral of maintenance and capital expenditure, MidAmerican has continued to invest during its current revenue freeze, and the Settlement provides a regulatory out if return on equity falls below 10 percent. If MidAmerican effectively maintains its generating and transmission assets and appropriately administers wholesale sales, both MidAmerican and its customers will benefit through the continuation of the revenue sharing mechanism, because some of the costs of future capital investments will be paid in advance.

The Settlement does not prohibit revenue neutral changes in rate design.

Article II, § 2(b) provides:

MidAmerican commits not to seek any general rate increase in Iowa electric base rates to become effective during 2012, unless its Iowa jurisdictional return on equity on electric operations for calendar year 2011 falls below 10%. This provision shall not be interpreted to prevent the implementation, prior to December 31, 2012, of any electric rate or tariff changes approved by the Board in Docket No. RPU-04-2 and associated dockets. (emphasis added).

The subject of revenue neutral changes to reduce or eliminate MidAmerican's zonal rate disparities is at issue in an ongoing proceeding, Docket No. RPU-04-2.

While the Settlement may not decide each issue the way the Board would after a contested hearing, the Board, viewing the Settlement as a whole, finds it to be reasonable, in the public interest, and not contrary to any law. The Settlement will facilitate the building of additional renewable energy to help meet the Governor's renewable energy goal and will further the diversity of Iowa's generation resources.

#### **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 considered other long-term sources of electric supply and the wind facilities proposed are reasonable when compared to other feasible alternative sources of supply.
3. The ratemaking principles contained in the Settlement filed on December 16, 2005, are reasonable.
4. The Settlement is reasonable in light of the whole record, consistent with law, and in the public interest.

#### **CONCLUSIONS OF LAW**

The Board has jurisdiction of the parties and the subject matter in this proceeding, pursuant to Iowa Code chapter 476 (2005).



**ORDERING CLAUSES**

**IT IS THEREFORE ORDERED:**

1. The stipulation and agreement, referred to in this order as the Settlement, filed in Docket No. RPU-05-4 on December 16, 2005, are approved.
2. MidAmerican Energy Company shall promptly file with the Board copies of all transmission and system impact studies it conducts to comply with MAPP or other regulatory requirements.

**UTILITIES BOARD**

/s/ John R. Norris

/s/ Diane Munns

ATTEST:

/s/ Judi K. Cooper  
Executive Secretary

/s/ Curtis W. Stamp

Dated at Des Moines, Iowa, this 18<sup>th</sup> day of April, 2006.