

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

IN RE:  INTERSTATE POWER AND LIGHT COMPANY	DOCKET NO. WRU-05-17-150
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**ORDER GRANTING WAIVER**

(Issued May 31, 2005)

On April 1, 2005, Interstate Power and Light Company (IPL) filed with the Utilities Board (Board) a "Petition for Waiver or Variance" of 199 IAC 20.9(2)(2). IPL asked for the waiver so that it can flow electric hedging costs through the energy adjustment clause (EAC). The Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed a response to the waiver request on April 20, 2005.

In support of its waiver request, IPL pointed out that the formula for calculating the purchased gas adjustment explicitly provides for the inclusion of "appropriate hedging tools costs" in the weighted average of applicable commodity prices or rates. 199 IAC 19.10(1). However, IPL noted there is no comparable provision in the EAC formula for the flow through of hedging costs. IPL said that the only hedging tool available under the EAC is the extremely limited tool of forward contracting. IPL argued that there is significant customer benefit to be derived from more effective risk management through the use of hedging methods other than forward contracting,

particularly with respect to management of the natural gas supply for electricity generation and purchases in electricity markets.

IPL maintained that with regard to the gas supply for electricity generation, the same risk factors that justify hedging methods allowed in the PGA support the use of more flexible hedging methods for the purchase of gas to generate electricity. Price spikes that have occurred in the electricity markets in recent years have shown the value of hedging tools to protect customers from unacceptable price volatility. As is true with hedging costs that flow through the PGA, IPL argued that hedging costs associated with the cost of gas to generate electricity or purchased power should flow through the EAC as a legitimate part of the cost of fuel and purchased power and not be a part of base rates. IPL noted that the corporate governance of the hedging program, which is set forth in Alliant Energy Corporate Services, Inc., Energy Trading “Business Unit Risk Management Plan” (BURMP) attached to the waiver request, strictly prohibits speculation and allows hedging only for the purpose of reducing risk.

IPL requested a permanent waiver, stating that a temporary waiver would be impractical because of significant changes occurring in electricity markets. IPL said that at some point, when the functioning of the markets becomes clearer, a rule making proceeding to amend the EAC rules might be appropriate.

Consumer Advocate in its response agreed that the current EAC rules limit recovery of financial hedging costs and that a waiver of both 20.9(1) and 20.9(2)(2) would be necessary for recovery of costs of hedging tools advocated by IPL in its

filing. While Consumer Advocate does not necessarily agree with IPL's assertion that financial hedging costs do not belong in base rates, Consumer Advocate acknowledged that prudently incurred hedging costs are generally legitimate costs associated with the supply of electricity. Consumer Advocate noted that with IPL's addition of the Emery Generating Station (Emery), the benefits and importance of mitigating electric energy price risk are heightened because Emery's primary fuel is natural gas.

Consumer Advocate cited IPL's commitments that it will only engage in hedging for the purpose of reducing risk and not for speculative purposes. Consumer Advocate noted IPL's proposed hedging strategy was described in the waiver request and the BURMP attached to the request. The BURMP imposes financial limits on costs for hedging that could be assigned to IPL, and also sets forth accounting, reporting, and cost allocation procedures.

Consumer Advocate said it does not object to IPL's waiver request provided that the hedging costs sought to be recovered through the EAC are incurred and allocated in accordance with the BURMP and are accompanied by reporting requirements comparable to those required for hedging transactions in the PGA rules. 199 IAC 19.10(7)"a." Consumer Advocate argued the quarterly report provided by the BURMP would not provide the level of information and detail required by the PGA rules. Consumer Advocate said if the waiver were granted under these

terms, it would carefully evaluate the hedging reports and might revisit the propriety of base rate treatment for hedging costs in a future IPL electric rate proceeding.

There are two aspects to IPL's waiver request. First, IPL asks for a waiver of the EAC rules so that it can use hedging tools in the natural gas markets to procure natural gas for its electric generating plants. IPL has experience using hedging tools in its natural gas procurement program of end-use customers.

Second, IPL wants to use hedging tools in purchasing power in electricity markets. These hedging tools should provide similar benefits to the hedging tools used by IPL in the gas markets, such as price certainty and stability. While IPL has not used such hedging tools in electricity markets, the basic hedging principles are the same as for the gas markets.

The Board will grant the waiver, but explicitly condition the waiver on IPL's compliance with its BURMP procedures and reporting requirements like those for hedging transactions in the PGA rules, 199 IAC 19.10(7)"a." The quarterly reports contemplated by the BURMP do not provide a sufficient level of detail to the hedging transactions. The reports with information comparable to the gas rule shall initially be filed on a quarterly basis, with the first report due on September 1, 2005. The Board views the reporting requirements as a work in progress and requirements may be added or deleted after the first reports are reviewed. In addition, IPL will be required to account for hedging activity in separate subaccounts to accounts 555 (Purchased Power), 447 (Sales for Resale), 501 (Fuel), and 547 (Fuel) that the BURMP lists as

the appropriate accounts for hedging activities. Use of subaccounts will assist the Board and Consumer Advocate in readily identifying and tracking hedging activity in IPL's reports.

The Board notes that while IPL only specifically cited 199 IAC 20.9(2)(2) in its waiver request, Consumer Advocate pointed out a waiver of subrule 20.9(1) may also be required because hedging costs do not fit neatly into the description of costs that can be recovered through the EAC. Hedging is not specifically addressed in any EAC rule. IPL's waiver spoke to a waiver of the EAC rules generally to allow for hedging transactions, and the Board believes it is appropriate to also waive 199 IAC 20.9(1), to the extent necessary.

The statutory authority for the EAC is Iowa Code § 476.6(11) and the statute contains no limitation on the types of energy costs and credits that can flow through the EAC. The waiver benefits customers by providing some price certainty and stability. The standards for a waiver of 199 IAC 1.3 have been satisfied.

IPL asked for a permanent waiver that would remain in effect until there is a rule making to amend the EAC rules, claiming that a temporary waiver is impracticable because of significant changes occurring in electricity markets. The Board will grant the permanent waiver, but without prejudice to any future Consumer Advocate proposal to recover hedging costs in base rates. If subsequently some costs are recovered in base rates, there will not be double recovery through the EAC.

**IT IS THEREFORE ORDERED:**

The request for waiver filed by Interstate Power and Light Company on April 1, 2005, is granted, conditioned on compliance with the requirements set forth in this order.

**UTILITIES BOARD**

/s/ John R. Norris

/s/ Diane Munns

ATTEST:

/s/ Judi K. Cooper  
Executive Secretary

/s/ Elliott Smith

Dated at Des Moines, Iowa, this 31<sup>st</sup> day of May, 2005.