STATE OF IOWA

DEPARTMENT OF COMMERCE

UTILITIES BOARD

IN RE: INTERSTATE POWER AND LIGHT COMPANY AND FPL ENERGY DUANE ARNOLD, LLC	DOCKET NO. SPU-05-15

ORDER

(Issued November 30, 2005)

PROCEDURAL HISTORY

On July 29, 2005, Interstate Power and Light Company (IPL) and FPL Energy Duane Arnold, LLC (FPLE Duane Arnold), collectively referred to as Applicants, filed a joint application for reorganization pursuant to Iowa Code §§ 476.76 and 476.77 to allow IPL to sell and transfer its ownership interest in the Duane Arnold Energy Center (DAEC), including nuclear fuel, to FPLE Duane Arnold. IPL owns 70 percent of DAEC; the remainder is owned by Central Iowa Power Cooperative (CIPCO-20 percent) and Corn Belt Power Cooperative (Corn Belt-10 percent).

FPLE Duane Arnold is an indirect, wholly owned subsidiary of FPL Energy, LLC (FPL Energy). FPL Energy is the unregulated power generation arm of FPL Group, a public utility holding company incorporated in Florida. FPL Group also has a regulated utility affiliate, Florida Power and Light. FPL Energy owns and operates 4,177 MW of generation in the Midwest, including wind farms in Iowa.

Iowa Code § 476.77(2) states that "[a] proposal for reorganization shall be deemed to have been approved unless the board disapproves the filing within 90 days after the filing." This section further provides "[t]he board, for good cause shown, may extend the deadline for acting on the application for an additional period not to exceed ninety days."

In its August 19, 2005, order setting a hearing and procedural schedule, the Utilities Board (Board) extended the decision deadline, pursuant to a request by the Consumer Advocate Division of the Department of Justice (Consumer Advocate), for the full 90 days permitted by statute, or to January 25, 2006. However, in the order the Board said it would set the procedural schedule, with a hearing date of November 1, such that the Board could complete its work by November 30, 2005, if circumstances warrant. The Board recognized, pursuant to arguments set forth by IPL, that timely action is important because of a provision in the DAEC purchase agreement that reduces the purchase price by $128,000 per day for each day that the closing of the transaction is delayed beyond January 31, 2006.

Intervenors in this proceeding, in addition to Consumer Advocate, are CIPCO, Cornbelt, and the Iowa Consumers Coalition (ICC). CIPCO and Cornbelt filed a joint intervention. Midwest Renewable Energy Projects LLC was denied intervention by order issued September 6, 2005, because it is not a current customer of IPL and it identified no interest that distinguished it from the general public to any significant degree.

Hearings were held beginning November 1, 2005, and all parties had the opportunity to file a post-hearing brief. No post-hearing motions were filed.

HISTORY OF DAEC OPERATIONS

Before describing the proposed transaction, it is important to understand the context of this reorganization. DAEC began operation in 1974 and is the only nuclear facility located in Iowa and the only one owned by IPL. DAEC consists of a fully licensed and operational General Electric Mark 1 Boiling Water Reactor and associated electric generation equipment with a monthly net capability of 598 MW. DAEC is located on a 550 acre site in Palo, Iowa, about 10 miles northwest of Cedar Rapids. IPL owns 70 percent of the plant; CIPCO and Corn Belt have elected, at least as of this date, not to sell their minority interests in DAEC. (Ex. 1, Sch. TLA-1, Sch. D at pp. 2-5). Because CIPCO and Corn Belt are not rate-regulated public utilities, sale of their interests would not be subject to the Board's reorganization statutes and rules.

For most of its years of operation, employees of IPL's predecessor utilities operated DAEC. In 1999, one of IPL's predecessors entered into a Nuclear Power Plant Operating Agreement (NPPOA) with the Nuclear Management Company (NMC). The NPPOA provided that NMC would act as IPL's agent in connection with the operation, management, maintenance, and repair of DAEC, the making of capital improvements to DAEC, and the performance of decommissioning work required upon DAEC's retirement. With approval from the Nuclear Regulatory Commission (NRC), IPL transferred operating authority for DAEC to NMC.

Under the NPPOA, there were limits to what NMC could do. NMC could not obligate IPL to pay costs of capital improvements materially different from those agreed to in the annual budget, could not obligate IPL to pay costs of capital improvements not agreed to by IPL’s board of directors, and could not sell or otherwise encumber DAEC. IPL remained the title owner of DAEC and continued to be entitled to 70 percent of all energy and capacity from DAEC and have the right to determine the electric output from DAEC. The NPPOA had no impact on the current book value of DAEC because the authority to operate DAEC had no value separate from physical ownership of the plant and therefore had no book value.

At the time of the transaction, Alliant Energy had a 25 percent interest in NMC. Northern States Power, Wisconsin Electric Nuclear Power Company, and Wisconsin Public Service also each owned 25 percent. IPL stated the purpose of NMC was to sustain and improve the overall performance of the nuclear plants currently operated by the affiliated utilities of NMC member companies. Substantially all of IPL’s operating personnel who were dedicated to DAEC were transferred to NMC, either as direct employees or as contracted employees under the supervision of NMC. The Board granted IPL a waiver of the reorganization statutes and rules with respect to the NMC NPPOA. See, IES Utilities Inc. and Nuclear Management Company, “Order Granting Waiver,” Docket No. WRU-99-54-151 (SPU-99-33), March 31, 2000.

At the hearing, no IPL witness expressed dissatisfaction with NMC. However, IPL noted that even after NMC took over operations, the risks associated with ownership of a nuclear power plant remained with IPL. Although there was some thought that NMC might evolve into a company that actually owned nuclear generating assets, this has not materialized and NMC did not bid on DAEC in the auction process. In addition to DAEC, NMC operates three other nuclear facilities.

FPLE DUANE ARNOLD

If the reorganization is approved, FPLE Duane Arnold will own 70 percent of Iowa's only nuclear plant. FPLE Duane Arnold is committed to relicensing the plant for an additional 20-year period, through 2034. Because FPLE Duane Arnold would have a significant presence in this state for over two decades, some background on its corporate family is useful to understand the context of Applicants' reorganization proposal.

FPL Group, Inc. (FPL Group), is a public utility holding company incorporated in 1984 in the state of Florida. FPL Group operates and develops power generation facilities under two different subsidiaries. One is FPL Energy, LLC (FPLE), which is the unregulated power generation arm. FPLE Duane Arnold is a limited liability company, wholly owned by FPLE, formed for the sole purpose of owning and operating DAEC. The other subsidiary operating and developing power generation is Florida Power and Light Company (FPL), which is a regulated public utility.

FPLE currently has 11,838 MW of net generation, including 1,076 MW, or 9.1 percent, in nuclear plants. Over 4,000 MW of this generation is in the central United States and FPLE has a growing presence in the Midwest, including wind generation in Iowa. FPLE has received several awards for its nuclear plant operation. FPL began its involvement with nuclear power in the mid-1960's and operates four nuclear plants at two different locations in Florida. The performance of these four units ranks among the best in the United States, both from the safety and production perspectives. (Tr. 271-75.)

DESCRIPTION OF THE PROPOSED REORGANIZATION

The purpose of this proposed reorganization is to allow IPL to sell its 70 percent interest in DAEC, including nuclear fuel, to FPLE Duane Arnold. The primary transactional document to effectuate the sale is an Asset Sales Agreement (ASA). In addition to the ASA, Applicants have entered into a Purchase Power Agreement (PPA) that begins when the sales transaction closes and terminates in 2014. IPL has a right of first negotiation to extend the PPA beyond 2014, but as of the hearing this was an oral commitment only. The terms and conditions of this right have not been reduced to writing and no monetary consideration for this right was paid by IPL.

The key elements of the transaction are:

1. FPLE Duane Arnold agrees to pay IPL $380.3 million at closing, plus or minus any adjustments pursuant to the ASA, for IPL's interest in DAEC, including nuclear fuel. These are the total proceeds of the sale.

2. FPLE Duane Arnold and IPL agree to execute a PPA extending from the time of closing (projected to be on or about January 31, 2006) to the end of DAEC's current licensed life with terms designed to mirror the costs that IPL's customers would have paid in base rates and through the EAC if IPL continued to own its 70 percent share of DAEC.

3. FPLE Duane Arnold assumes IPL's obligation for: a) long term storage of spent nuclear fuel, b) decommissioning DAEC in accordance with NRC regulations sufficient for termination of the NRC license, and c) restoring the DAEC site to greenfield status. IPL will transfer its external decommissioning trust funds to FPLE Duane Arnold at the time of closing to be accounted for in an external trust and to be used for DAEC's decommissioning.

4. IPL transfers its Department of Energy (DOE) spent nuclear fuel litigation claim rights to FPLE Duane Arnold. Out of any ultimate proceeds, FPLE Duane Arnold will first be reimbursed for expenses. After expenses, IPL is to be paid the first $10 million of any recovery, and 50 percent of any recovery above $10 million up to a cap of $21 million in total IPL recovery. FPLE Duane Arnold receives the remainder of the proceeds that do not go to IPL under this formula.

5. FPLE Duane Arnold agrees to reimburse IPL for the $7 million exit fee owed to NMC pursuant to IPL's termination of their agreement.

6. FPLE Duane Arnold assumes two collective bargaining agreements covering DAEC employees and offers all of the existing workforce employment with total compensation and benefits that are substantially equivalent for a period of 18 months.

7. DAEC sales proceeds are defined as portions of the total proceeds of sale ($380.3 million) that either constitute a return of the net book value of DAEC (at year-end 2004, $219.1 million) or will otherwise be used by IPL to fund DAEC-related costs IPL incurs as it exits ownership of DAEC.

8. IPL will retain half of the net book value return of sales proceeds ($109.55 million) to retire IPL short-term debt and distribute the remaining half ($109.55 million) as an extraordinary dividend to IPL's parent company, Alliant Energy Corporation (Alliant Energy).

9. At closing, FPLE Duane Arnold assumes pension obligations for DAEC's workforce, and associated pension assets will be transferred to FPLE Duane Arnold for that purpose. In addition, IPL will use $13.16 million of DAEC sales proceeds to fund the difference between current pension assets and accrued liabilities.

10. IPL retains ownership of transmission facilities connecting DAEC to IPL's system, but the parties have entered into a Large Generator Interconnection Agreement.

Net proceeds from the DAEC sale price ($380.3 million) are defined as those proceeds made available by IPL to its customers. Net proceeds plus sales proceeds (as defined in number 8 above) equal total proceeds or sale price. In its initial testimony, IPL committed $10 million from the total proceeds to be used for the benefit of customers. The money would be placed in a regulatory liability account and used to offset the allowance for funds used during construction (AFUDC) for future investments in new generation in Iowa. In rebuttal testimony, IPL committed that all net proceeds resulting from the sale would be returned to customers, with the exception of an estimated $5.3 million necessary to ensure the retention of IPL's tax normalization benefits. IPL estimates net proceeds available for customers will be about $33 million. If this amount is allowed by the Internal Revenue Service to be tax affected at IPL's marginal tax rate, the $33 million translates into $56 million in net proceeds returned to customers. IPL will place this money in a regulatory liability account, or return it to customers in any manner ordered by the Board, such as a bill credit or cash refund. In addition to the net proceeds from the sale, IPL's calculations show ratepayers will save $23.6 million from the PPA pricing.

In addition to the quantifiable benefits from the reorganization, IPL believes there are significant non-quantifiable benefits of the reorganization, such as the transfer of risk. IPL states that the transaction “transfers virtually 100 percent of the operating, and associated financial risk to FPLE Duane Arnold and away from IPL and its customers.” (Aller Rebuttal, p. 21). Among the risks cited are costs associated with unplanned outages and nuclear decommissioning risk.

There are two items facilitating the reorganization for which Applicants request specific Board approval. First, as noted above, IPL initially proposed to use all net proceeds from the DAEC sale, except those needed to retain income tax normalization, to benefit electric customers through a regulatory liability account that will be used to offset future plant construction costs. IPL asks for explicit Board approval to create this regulatory liability account and for language stating that none of the funds placed into the regulatory liability account relate to the flow-through of either the unamortized deferred investment tax credit or accumulated deferred income taxes related to excess deferred taxes to customers. Without this approval, IPL could violate normalization requirements of the Internal Revenue Code and lose the use of accelerated depreciation for income tax purposes, to the potential detriment of its customers.

At hearing, IPL offered to use the net proceeds to benefit customers in any manner chosen by the Board, including refunds or bill credits. If the reorganization is approved, and the Board orders refunds or bill credits, approval of the regulatory liability account becomes moot and is not required. The testimony at hearing indicated that IPL was not clear whether proceeds placed in a regulatory liability account could be tax affected, or only proceeds if there was a direct refund to customers.

Second, if the reorganization is approved, FPLE Duane Arnold will be operating DAEC as an exempt wholesale generator (EWG). Therefore, approval by each state with jurisdiction over any utility within the Alliant Energy holding company family is required for the transfer of DAEC to EWG status pursuant to section 32(c) of the Public Utility Holding Company Act of 1935 (PUHCA). The Board must specifically find, for DAEC to obtain EWG status, that allowing it to be an eligible facility will benefit consumers, is in the public interest, and does not violate state law.

STATUTORY FACTORS FOR REVIEWING A REORGANIZATION PROPOSAL

Iowa Code § 476.77 provides that a reorganization of any public utility shall not take place if the Board disapproves. Subrule 199 IAC 32.2(2) requires that a reorganization proposal be filed if a public utility subject to the reorganization statute's jurisdiction directly or indirectly disposes of assets, with a value of more than $10 million that are used in the delivery of utility services. The sale of DAEC clearly falls with the purview of the reorganization statutes and rules.

Iowa Code § 476.77(3) lists the following factors that the Board may consider in its review of a proposal for reorganization:

> a. Whether the board will have reasonable access to books, records, documents, and other information relating to the public utility or any of its affiliates.

b. Whether the public utility's ability to attract capital on reasonable terms, including the maintenance of a reasonable capital structure, is impaired.

c. Whether the ability of the public utility to provide safe, reasonable, and adequate service is impaired.

d. Whether ratepayers are detrimentally affected.

e. Whether the public interest is detrimentally affected.

In this reorganization, the important questions are the impacts of the proposed reorganization on the utility's ability to provide reasonable and adequate service, on the utility's ratepayers, and on the public interest generally.

The Board will discuss each of the five statutory factors. Some of the issues raised in the proceeding may relate to more than one statutory factor. In this proceeding, the primary focus by all parties was on issues impacting ratepayer and the public interest. Before beginning this discussion, though, the Board will provide some background on what it sees as the primary disagreement between the parties in this docket.

BACKGROUND

IPL testimony indicates it decided to sell DAEC because it no longer wanted to own a nuclear plant because the financial risks were not commensurate with the potential return. The nuclear industry in the United States is consolidating, in part because the risks of ownership are more difficult to manage for utilities that own only one unit, like IPL. While turning management over to the NMC has provided some economies of scale, the fact that NMC does not own any of the nuclear plants somewhat limits its ability to optimally operate the plants. FPLE Duane Arnold would not have this issue because the FPLE group owns all the nuclear plants it operates.

One of the risks unique to nuclear plants is regulatory. Problems at one nuclear plant can cause the NRC to change its regulatory requirements, imposing additional costs on facilities. For example, since 9/11 security costs for nuclear plants have escalated in response to an increased threat of terrorism. Nuclear plants may have a greater potential as targets, when compared to other types of generating facilities. Partly because of these regulatory risks, IPL asserts that the costs of running a nuclear plant are generally more volatile than those of conventional coal or gas plants or newer renewable facilities.

IPL said it was selling DAEC to transfer risk associated with operations and maintenance, capital, and purchased power risks away from ratepayers. IPL witness Aller testified that while IPL wanted to continue to purchase the output of DAEC, it no longer wanted to own the facility that manufactured the product because of the risks involved. IPL witness Aller said if the reorganization was not approved, IPL would not relicense DAEC and the plant would cease operations when its current NRC operating license expires in 2014.

Throughout the testimony, the parties presented arguments about projected PPA savings, flaws in the ASA and PPA agreements, and numerous other issues affecting ratepayer interests. However, underlying all the testimony is a fundamental disagreement between the parties on how IPL can best serve its customers. This fundamental disagreement, with IPL on one side and Consumer Advocate and the ICC on the other, is whether IPL's decision not to relicense DAEC and continue to own it beyond 2014 is imprudent. Consumer Advocate and the ICC argue there are significant benefits to ratepayers if IPL retains ownership of the plant and pursues relicensing; IPL states relicensing by IPL is not an option because of the imbalance between financial risks and rewards. Although not directly stated in Consumer Advocate's or the ICC's testimony, there appears to be an underlying belief on the part of those parties that IPL will pursue relicensing if this reorganization is denied.

The Board shares the concerns expressed in the dissent that IPL did not adequately explore the relicensing option, particularly legislative options regarding advance ratemaking principles for a relicensed DAEC. A relicensed DAEC owned by IPL would guarantee that IPL's ratepayers would have access to DAEC's output through 2034, continuing to provide diversity to IPL's fossil fuel and purchased power generation mix. Nuclear power does not have the emissions issues that are present with coal or the fuel price volatility issues associated with natural gas.

That being said, the Board must rule on the reorganization proposal before it. IPL testified, in direct, rebuttal, and at hearing, that it would not relicense DAEC under any circumstances. The Board takes IPL at its word. It is important to note that the Board does not have the authority pursuant to Iowa Code chapter 476 to order IPL to relicense DAEC or even to begin the relicensing process. The Board also does not have the statutory authority to make fundamental management decisions for a regulated utility, although some such decisions, such as the one to sell DAEC, are subject to Board review.

All parties agreed that DAEC should be relicensed, but they disagreed on who should do it. There is no disagreement among the parties, or the Board, that DAEC provides significant benefits beyond that of its power output. There is undisputed testimony that DAEC's operation has a positive impact on transmission system reliability by providing critical voltage support and there are substantial economic benefits to its continued operation. If DAEC were shut down in 2014, 500 jobs would be lost. Annual spending for labor, contractors, and materials during non-refueling years was $56 million in 2004 and projected at $58 million in 2005. This goes up dramatically during a refueling year; as up to 2,000 additional people augment the DAEC staff, representing millions of dollars in hotel and restaurant spending.

The Board would have preferred that the relicensing and continued ownership option had been more thoroughly explored before a sale was made. It was not, and the Board cannot change that. The Board must therefore review the individual statutory factors as they apply to this reorganization.

ACCESS TO BOOKS AND RECORDS

The first statutory factor the Board may consider in reviewing a proposal for reorganization is "whether the board will have reasonable access to books, records, documents, and other information relating to the public utility or any of its affiliates."

Iowa Code § 476.77(3)"a." It is uncontested that this statutory factor has been satisfied.

IPL's accounting policies, procedures, and system of accounts will remain essentially the same after the reorganization, including its continuing use of the Federal Energy Regulatory Commission (FERC) uniform system of accounts. The Board will continue to have reasonable access to IPL's books and records, if the reorganization is approved. The Board, through IPL, will have access to information regarding the PPA and other relevant contract items through 2014. After 2014, the Board will still require information on items that may impact IPL or its ratepayers, such as nuclear decommissioning and the spent nuclear fuel litigation. For example, information on decommissioning may be required in 2034 (assuming relicensing) or after to see if a refund is due to IPL's customers. FPLE Duane Arnold has committed to provide the Board the information it needs to perform its regulatory functions, and the Board's decision in this docket explicitly takes into account this commitment. (Tr. 1532-33.) FPLE Duane Arnold's counsel noted, and the Board agrees, that providing this information does not make FPLE Duane Arnold a public utility subject to the Board's general jurisdiction. (Tr. 1532.)

ABILITY TO ATTRACT CAPITAL

In reorganization proceedings, the Board examines whether the public utility's ability to attract capital on reasonable terms, including the maintenance of a reasonable capital structure, is impaired. In making this finding, the Board looks at the utility's capital structure and whether the utility will have reasonable access to the capital markets by protecting its credit rating.

In determining what to do with the proceeds from the proposed sale of DAEC, IPL looked at three scenarios, guided by three directives: 1) the sale should not negatively impact IPL's credit rating; 2) IPL's ratepayers should not be negatively impacted by the sale by having to pay a higher cost of capital for IPL that is reflected in subsequent rate proceedings; and 3) earnings per share should not diminish as a result of the transaction. (Tr. 434.)

The three scenarios IPL examined were retaining 100 percent of the proceeds at IPL to retire IPL debt; dividend 100 percent of the proceeds to Alliant Energy, the parent company; and retain one-half the proceeds at IPL to retire IPL short-term debt and dividend the other half to Alliant Energy. (Tr. 435.) The third scenario is the only one that met all three directives. (Tr. 437.) Because the PPA is viewed by the credit rating agencies as debt equivalent, reducing short-term debt with one-half of the proceeds will offset the impact of the PPA on IPL's credit rating. Reducing short-term debt, rather than long-term debt, will not impact the cost of capital for future rate cases. (Tr. 438.) Due to the transaction, the common equity component will actually be reduced, resulting in a lower weighted average cost of capital. (Tr. 437.) Earnings will not be impacted by the third scenario due to the portion of the proceeds allocated to the parent holding company.

Consumer Advocate believes that IPL is proposing to dividend one-half of the proceeds to its parent because the parent needs a cash infusion to cover losses in foreign investments made by its unregulated subsidiary, Alliant Energy Resources. (Tr. 1553.) Consumer Advocate, though, did not present direct evidence to support these assertions. As explained in prefiled testimony and at hearing by IPL, retaining all the proceeds at IPL would increase its cost of capital, to ratepayers' detriment. The extraordinary dividend to IPL's parent was specifically designed to lower IPL's overall after-tax cost of capital in subsequent rate cases. (Tr. 440-41.) The Board finds nothing in the record to suggest that the proposed sale of DAEC is motivated by the cash needs of IPL's unregulated affiliates, and notes that at hearing Consumer Advocate's witness appeared to effectively agree with IPL's proposed use of the proceeds, if the Board allowed the reorganization to go forward. (Tr. 1591-92.)

The ICC was concerned about the amount of the PPA that the rating agencies would consider as a debt equivalent. The ICC said the sale will increase IPL's non-DAEC cost of service because the rating agencies will treat the fixed cost portion of the PPA as a debt equivalent. If common equity is increased to offset this debt, the cost of service is increased, to the potential detriment of ratepayers. (Tr. 1238-39.) The IPL and ICC witnesses agreed that adjustments are needed to offset the increased amount of debt attributed to debt equivalence. The disagreement is on the solution.

The ICC argued that IPL's plan to reduce short-term debt is not a permanent solution because short-term debt is for seasonal working capital (e.g., construction work in progress) and replacing the sales of accounts receivable, which is recurring short-term debt. (Tr. 461.) The ICC said a permanent solution would be for IPL to reduce its on-balance sheet long-term debt, which will increase IPL's common equity ratio.

IPL's testimony demonstrates that the allocation of proceeds it has proposed would render the transaction neutral from a credit rating viewpoint because reduction of short-term debt would offset the impact of the PPA. (Tr. 438-40.) IPL said it had received a written statement from Standard & Poor's (S&P) that the amount of short-term debt reduction combined with the reduced risk of removing DAEC from IPL's rate base would offset the PPA debt equivalence. (Tr. 455.)

Nothing in the record from IPL indicates that the reduction in short-term debt is a temporary solution to the debt equivalency issue. All indications are that the transaction will be neutral from S&P's point of view. If the transaction is completed, IPL's weighted average cost of capital is reduced from 8.824 percent to 8.748 percent. The Board does not find that the transaction would impair IPL's capital structure. However, if evidence in future rate cases demonstrates the solution to the debt equivalency issue chosen by IPL was only a temporary fix, the Board could reverse the impact on the capital structure to insure that ratepayers are not negatively impacted by the use of proceeds from the sale.

Another issue raised that perhaps best fits under ability to attract capital relates to FPLE Duane Arnold. Although FPLE Duane Arnold will not be a public utility regulated by the Board, the ICC raised concerns that FPLE Duane Arnold does not have the credit standing to back up its PPA and that guarantees provided by FPLE Duane Arnold's parent are not sufficient. The Board does not share these concerns. The credit strength of the FPL Group exceeds that of Alliant Energy and the guarantees appear adequate to meet all obligations. There is nothing substantial in the record that calls the credit ratings of the FPL Group into question or suggests that the financial resources do not exist to meet the guarantees and, in fact, Consumer Advocate at hearing said it did not have concerns about FPLE Duane Arnold as the buyer.

SAFE, REASONABLE, AND ADEQUATE SERVICE

Consumer Advocate and the ICC did not directly comment on the issue of IPL's ability to provide safe, reasonable, and adequate service. They both raised issues regarding future power costs paid by ratepayers, but these issues are discussed under the category of ratepayer interest. There appears to be no serious dispute that after the reorganization IPL will continue to provide safe, reasonable, and adequate service to its customers and that the reorganization will have no adverse or detrimental impacts on IPL's electric operations.

In fact, if DAEC's capacity factor is improved to 90 percent by FPLE Duane Arnold, there should be enhancement of reliability after the reorganization. Because of possible loss of major load offset by load growth, it is unclear what amount of capacity and energy IPL will need in 2014 to replace the DAEC PPA. IPL's current EGEAS analysis identifies coal capacity and energy as the most probable replacement after February 2014. There is sufficient time to install a new-base load resource if the PPA is not extended past February 2014 and using coal to replace DAEC-related capacity would not adversely impact service and reliability. (Tr. 942.)

IPL acknowledged the value of continued operation of DAEC for the transmission system in the Cedar Rapids area. Because IPL has decided not to relicense DAEC, IPL notes these benefits will be captured by FPLE Duane Arnold's plans to relicense the plant. The most significant operational benefit provided by relicensing is the continued Volt Ampere Reactive (VAR) support for the Cedar Rapids area. Without relicensing, additional improvements to the transmission system, as well as additional generation, will likely be necessary after 2014 to address voltage and overload problems.

RATEPAYER INTEREST

The key arguments in this case relate to ratepayer interest. There is disagreement about the costs and benefits to ratepayers during the period of the PPA and the costs and benefits after 2014. To bring these disagreements in focus, some initial discussion of the parties' positions with respect to the decision-making process is required. After this initial discussion, the ASA and PPA terms and various models used in the cost-benefit analysis will be discussed.

1. Decision to sell DAEC and auction process

IPL's president, Thomas Aller, testified that the basis for the recommendation to sell DAEC made to the IPL and Alliant Energy Boards of Directors was the cash flow analyses of various DAEC ownership scenarios. (Tr. 23.) The following ownership scenarios were examined: a) shut down DAEC in 2014 at the end of the current license period, b) continue to own DAEC and relicense to 2034, c) seek legislation on ratemaking principles of a relicensed DAEC (including a fixed return on equity of 13 percent), and d) seek legislation allowing ratemaking principles of a relicensed DAEC (including fixed earnings of 13 percent for the life of the plant).

Consumer Advocate said there were errors in the cash flow analysis and that the real reason for the sale was Alliant Energy's need for cash because of poor investments of non-regulated affiliates. (Tr. 1553-54.) In other words, shareholder interests, not ratepayer interests, motivated the decision to sell DAEC.

IPL maintained that its decision to sell was based on the perceived mismatch of risks and rewards between earnings on DAEC in cost of service rate regulation and the risks associated with owning a nuclear plant. (Tr. 26.) Consumer Advocate is critical of IPL for not pursuing legislative options that might have at least reduced the alleged mismatch, and maintains the risk of owning a nuclear plant can be effectively managed by IPL.

The Board also believes legislative options should have been pursued, particularly in the 2001-2003 time frame when the advance ratemaking principles legislation was adopted and several new generating plants were proposed and subsequently built, in large part because of the statute's encouragement and the regulatory certainty it provides. However, it is uncertain whether adoption of favorable legislation would have caused IPL to change course. The record indicates that IPL's decision was primarily based on its desire to exit the business of owning nuclear power to manufacture electricity. IPL wants to continue to buy the power, but views the risks of owning the power plant as being too great. IPL stated this is consistent with industry trends for utility owners of a single nuclear plant, although other, larger utilities are expanding their nuclear business. The evidence does not support Consumer Advocate's assertion that the motive behind the sale is to provide cash to the parent, Alliant Energy, to cover losses in unregulated businesses. In fact, IPL's plan to dividend half of the sale proceeds to Alliant Energy actually reduces IPL's cost of capital, to the benefit of ratepayers. IPL's motivation is not a reason to disapprove this reorganization.

The proposed sale versus relicensing by IPL will be discussed later in a separate subsection. It is touched on here to provide background to IPL's decision to sell DAEC using a competitive auction process.

IPL retained Concentric Energy Advisors (CEA) as its auction advisor. CEA designed, executed, and managed the auction process. IPL's intent was to structure a transaction that maximized total transaction value, including cash purchase price, PPA terms, decommissioning terms, and other transaction terms. IPL testified its principal objectives were to maintain or reduce power supply costs for customers, reduce IPL's nuclear operating and decommissioning risks, and maximize the value received for DAEC.

Consumer Advocate argued that IPL failed to meet its burden under 199 IAC 32.4(1)"b" because it failed to compare the rate impacts of other bids received in the DAEC auction process. This subrule provides that reorganization applicants provide an analysis of the alternatives to the proposed reorganization that were considered and their impacts on rates and services, if any.

IPL witness Boston described the bid implementation process in detail. Because the bids were analyzed to meet the principal objectives of the DAEC auction, including the ability to maintain or reduce power supply costs, the alternatives were analyzed with an eye toward their impacts on rates and services. This analysis is sufficient to satisfy the rule. The Board does not believe that modeling revenue requirement impacts of losing bids would be helpful in making a decision on the reorganization. The testimony was clear as to where the other bids fell short. Although Consumer Advocate thought another bid might provide more ratepayer benefit, the Board's review indicates that, as a total package, the FPLE Duane Arnold bid is superior. In evaluating the bids, the total package must be examined, not just individual pieces. Because IPL is providing all the net benefits to ratepayers, any arguments that the bidding process was designed to maximize purchase price over PPA benefits are negated—benefits from both pieces will flow to ratepayers and not be shared with shareholders.

Other than challenging whether appropriate analysis of all the bids was provided and appropriate guidelines given to CEA, Consumer Advocate and the ICC did not challenge the auction process itself. IPL noted that competitive auctions for generation divestitures have been endorsed by numerous state regulatory commissions as providing the fair market value for these assets if sufficient competition exists in the auction. This appears to be the case for DAEC. (Tr. 356-57.) No issues were raised about the transparency of the auction process.

IPL noted that it met with Consumer Advocate several times during the bid process to keep Consumer Advocate informed and solicit any feedback. Consumer Advocate had access to all documents the bidders had access to through a "virtual document room." IPL said that at no point did Consumer Advocate offer any feedback on many of the points raised in this proceeding, such as the PPA terms or pricing and the DOE litigation.

The Board does not view it as Consumer Advocate's role to be IPL's "consultant" on this transaction offering contemporaneous advice on the ongoing process. Consumer Advocate's responsibility is to investigate and comment on the transaction ultimately consummated by IPL's management. While Consumer Advocate could have offered suggestions or raised issues during the auction process, the Board does not give any weight to the fact that Consumer Advocate did not do so. It simply was not Consumer Advocate's job to manage the auction process or bid instructions, and Consumer Advocate's silence during the investigative process is not acquiescence to the resulting transaction.

2. Asset Sale Agreement (ASA)

The terms of the ASA generally were not challenged, other than Consumer Advocate's assertion that another bid may have provided more ratepayer benefits. Consumer Advocate is not arguing the other bid should have been accepted, however, because Consumer Advocate believes IPL should have pursued relicensing and continued ownership of DAEC.

The ASA provides that IPL will receive $380.3 million for its 70 percent interest in DAEC, with possible adjustments for decommissioning obligations and funding, spent nuclear fuel issues, and environmental issues. Spent nuclear fuel will be addressed as a separate subissue because there is some dispute on allocation of potential lawsuit proceeds.

Under the ASA, FPLE Duane Arnold assumes IPL's obligations for: a) long-term storage of spent nuclear fuel, b) decommissioning DAEC in accordance with NRC regulations, and c) restoring the DAEC site to greenfield status. IPL will transfer its external decommissioning trust funds to FPLE Duane Arnold at the time of closing to be accounted for in an external trust and to be used for DAEC's decommissioning. The ASA also addresses pension obligations, payment of IPL's exit fee to the NMC, and numerous other transactional issues.

One final aspect of the ASA worth noting is that IPL shall indemnify, defend, and hold harmless FPLE Duane Arnold from any losses under or related to environmental laws that were caused by the presence or release of hazardous substances at the DAEC site prior to the closing date of the sale, if the aggregate of such claims exceeds $1 million. This is a liability that IPL has today. It is significant that this obligation to indemnify for environmental claims only lasts until three years after the closing date.

3. Purchase Power Agreement (PPA)

Under the PPA, IPL will purchase capacity, associated energy, and ancillary services from FPLE Duane Arnold through the end of the current NRC operating license in 2014. The PPA starts at the closing of the proposed DAEC sale. (Tr. 40.) IPL's primary directive in negotiating the PPA was, at a minimum, to make its customers indifferent to whether IPL or FPLE Duane Arnold owns DAEC, while shifting operational risk away from IPL and its customers. Price terms of the PPA were designed to mirror the costs that IPL's customers would have paid in base rates and through the EAC if IPL continued to own its share of DAEC and reflect the rate design in IPL's current rates. (Tr. 850.) IPL said this policy is advanced through the PPA by establishing monthly capacity payments that reflect IPL's projected and fixed costs of owning and operating DAEC until the end of its license. The monthly energy payment will be calculated as the product of the fixed energy charge and the monthly delivered energy. (Tr. 32.) The fixed energy charge has been designed to match a forecast level of fuel costs that IPL would have incurred if it continued to own DAEC. (Tr. 681.)

In addition, the PPA has a target capacity factor equal to 90 percent, which exceeds DAEC's average four-year historical capacity factor of 86.79 percent, providing an incentive for FPLE Duane Arnold to improve performance at the plant. The PPA also gives FPLE Duane Arnold the ability to provide replacement power during times when DAEC is operating at less than full power and reductions in capacity prices (up to 100 percent) if FPLE Duane Arnold does not provide replacement power, ensuring that ratepayers only pay for what they receive. (Tr. 860-82.)

Consumer Advocate argued that while IPL's stated goal was a revenue-neutral PPA, the prices established in the PPA are based on speculative, unsupported assumptions that are higher than the levels provided by known and measurable data. (Tr. 1023, 1028, 1030, 1032-34, 1036, 1039.) Consumer Advocate argued that the costs used appear to be higher than NMC's recent production costs. In effect, Consumer Advocate appears to be saying that the PPA negotiations promoted terms more beneficial to shareholders, at customer expense. As acknowledged by IPL, bidders would be willing to pay a higher cash price for DAEC if they are confident in their abilities to perform more efficiently than the base PPA standards. (Tr. 165, 709.) Because IPL has agreed to return all net proceeds to customers, the Board does not see a motive to skew the transaction in favor of either the PPA or the sales price; even if it were, customers receive all the benefits of both the sales price and the PPA.

While the Board does not find that IPL skewed the bidding instructions to favor one aspect of the total transaction, Consumer Advocate's arguments that the prices in the PPA are based upon speculative, unsupported assumptions that are higher than the levels indicated by known and measurable data must be addressed. In particular, Consumer Advocate questioned the use of NMC budgets and projections because these budgets and projections were not specifically evaluated by IPL. The ICC also argued that the PPA was excessive, noting that projected increases for nuclear fuel are higher than the U.S. Department of Energy's Energy Information Administration forecast of stable nuclear fuel cost escalations of 2 percent per year. (Tr. 1120.)

IPL's PPA capacity charges were modeled using IPL witness Hampsher's reorganization model, which provides a revenue requirement analysis for each year 2006-2014. This analysis indicates that customers benefit from the fixed capacity charges included in the PPA pricing over traditional revenue requirements by $23.6 million in present value terms. (Tr. 547.) The analysis assumes DAEC would be shut down in 2014.

Consumer Advocate provided three revenue requirements for the same years using different assumptions and inputs. In looking at the differences in the results, the inputs must be examined, because the IPL and Consumer Advocate witnesses agreed on the basic or base model.

In analyzing the DAEC sale with PPA scenario, IPL used what it termed its “best case plus” scenario. The “best case plus” scenario assumes that DAEC runs at a higher capacity factor than it ever has, that O&M and capacity spending are 50 percent less than NMC projections, and that IPL will earn no more on its DAEC investment than is currently allowed in its last electric rate case, despite low A-rated utility bond yields. If these “best case plus” scenario assumptions prove too low, ratepayer benefits from the PPA are increased. Using this “best case plus” scenario, IPL determined there were $23.6 million in present value PPA benefits for customers.

Consumer Advocate’s three scenarios change some of the assumptions. The first removes 50 percent of the NMC cost increase estimate, the second removes the 50 percent NMC cost increase and replaces it with a 2.5 percent inflation factor based on 2005 approved budget levels, and the third is identical to the second except it uses a 1 percent inflation factor. Consumer Advocate’s scenarios show different benefits/detriments than IPL’s calculation, but only its third scenario, with a 1 percent inflation rate, shows customers are worse off with the PPA than with continued IPL ownership of DAEC through 2014.

However, it is important to note that the PPA does not stand by itself in this transaction. In addition to any PPA benefits, the net proceeds of $56 million (tax affected), added to the $23.6 million of PPA benefits projected by IPL, yield total customer benefits in excess of $79 million. When net proceeds are added to the analysis, any of Consumer Advocate's three scenarios show there are total net benefits to this transaction, when considering both net proceeds and the PPA, through 2014.

The Board could spend additional time dissecting the assumptions, but it would not change the fact that under any of Consumer Advocate's three scenarios, there is still a projected benefit to ratepayers, at least through 2014, when net sales proceeds are considered. The Board will comment on one assumption used in Consumer Advocate's third scenario, the 1 percent inflation rate. The 1 percent inflation rate does not seem reasonable on a long-term basis, especially when considering escalating wages and health insurance costs.

The Board believes the "best case plus" assumptions to be reasonable. The assumptions use 50 percent of NMC's projected increases. While the 50 percent amount is higher than past O&M levels, these goals appear to have been met, at least in part, by delaying spending on capital projects and leaving positions vacant. (Tr. 666-69.) Also, the price for fuel used by IPL appears reasonable and consistent with recent industry projections. Because of limits placed on operating expenditures in the past, the projections provide a more realistic estimate of future costs, particularly with the improvements planned for DAEC.

4. Purchase Power Agreement terms and conditions

The PPA sets fixed prices for both capacity and energy. The ICC argued a PPA should have been negotiated that tied PPA pricing to FPLE Duane Arnold's actual cost of production. (Tr. 1050-52.) While it is possible that this would result in lower purchase power costs, the impact on the purchase price is unknown. More importantly, such an agreement would subject ratepayers to risks associated with, among other things, unforeseeable and unexpected increases in the cost of fuel, O&M expenses, unplanned capital improvements, and repairs. The fixed PPA provides price certainty and eliminates these risks. The ICC's suggestion removes operating decisions from IPL's control but leaves it with the risk of unforeseen operating costs.

Consumer Advocate and the ICC both argued the PPA should allow IPL the opportunity to enter into negotiations to renew and extend the terms of the PPA following the 2014 expiration date. IPL presented testimony that it has a natural competitive advantage in any negotiation for post-2014 DAEC power. (Tr. 87.) In addition, a right of first negotiation was recently offered, although its terms have not been reduced to writing. (Tr. 1149.) The Board believes IPL will have every opportunity to extend the contract, if it is in the company's, and its ratepayers', best interests.

5. Decommissioning

The NRC requires certain minimum funding levels to cover the costs of future decommissioning and financial assurance of those levels must be demonstrated before the NRC will allow a license transfer. The NRC minimum funding level for DAEC at year-end 2005 will be approximately $260 million; IPL will transfer $203.3 million in decommissioning funds to FPLE Duane Arnold when the transaction closes. FPL Group Capital will provide a parent guaranty pursuant to NRC regulations for the difference. (Tr. 1152-53.) IPL estimates there will be approximately $8.4 million in excess decommissioning funds returned to ratepayers as part of the net proceeds of $56 million.

Under the ASA, FPLE Duane Arnold assumes full responsibility to return DAEC to a greenfield state at the time of decommissioning. Once IPL transfers the $203.3 million in decommissioning funds, it has no further decommissioning liability. There is a “clawback” provision in the ASA that provides for a return of decommissioning funds to IPL if decommissioning costs are less than IPL’s share of the amount transferred. IPL has committed that any monies received would benefit ratepayers.

There was some discussion that FPLE Duane Arnold will receive a windfall if it does not have to return any earnings on decommissioning funds in excess of what is ultimately required. However, FPLE Duane Arnold noted that if the clawback provision allowed for return of any earnings on the funds transferred at closing, there would have been a corresponding adjustment in the purchase price. If DAEC is not relicensed, FPLE Duane Arnold would have to make up any shortfall. The Board does not believe there is any windfall and the decommissioning funds have been adequately distributed in the context of the entire transaction.

The ICC questioned whether IPL was adequately indemnified for any future decommissioning costs. The Board is satisfied with the arrangement. In the event of a premature shutdown of DAEC, decommissioning can be delayed to allow time for additional returns on the fund. The NRC also must approve this reorganization and it is the primary regulatory body with respect to the adequacy of decommissioning funds and the adequacy of the corporate guaranty for the unfunded amount.

6. Spent nuclear fuel

If the reorganization goes forward, IPL will transfer to FPLE Duane Arnold all risk associated with spent nuclear fuel currently stored at DAEC and produced at DAEC in the future. (Tr. 72.) A permanent repository for spent nuclear fuel is likely many years away. Numerous utilities, including IPL, have sued DOE for its failure to accept spent nuclear fuel at a repository site.

The ASA contains a formula, discussed earlier under “Description of Proposed Reorganization,” that provides IPL and its customers could receive up to $21 million in proceeds from this litigation, if it is successful. FPLE Duane Arnold has agreed to take over this lawsuit.

Consumer Advocate and the ICC both questioned whether the formula for distributing lawsuit proceeds is equitable. Consumer Advocate's witness noted that one utility will receive a payment of $80 million for spent nuclear fuel costs already incurred and reimbursements for future costs. On rebuttal, IPL pointed out this settlement covered 11 stations and 20 units, for a per unit and per station value far less than $21 million. (Tr. 361-62.) Because FPLE Duane Arnold will incur costs associated with on-site storage if it assumes ownership of DAEC, which it will probably seek to recover from DOE, the distribution of any lawsuit proceeds is not inequitable. (Tr. 73.) IPL will receive the first $10 million, after litigation expenses, and IPL will no longer have to front the costs of prosecuting the litigation.

7. Proposed sale vs. relicensing

IPL claimed there are intangible benefits from the proposed transaction, as opposed to continued ownership of DAEC by IPL, which are not reflected in Consumer Advocate's case. IPL stated the proposed reorganization transfers the following risks to FPLE Duane Arnold:

a. Operating Risk, such as premature shut downs, unplanned outages, and accidents. Both DAEC and Kewaunee Nuclear Power Plant (formerly owned by an Alliant Energy affiliate) have experienced costly, unplanned outages. (Tr. 66-67.)

b. Decommissioning risk. While Consumer Advocate's witness believes there is little risk that the funding transferred will be inadequate, IPL points out there is no certainty as to what costs and legal requirements will be in 2034. Decommissioning was discussed in greater detail in a prior subsection.

c. Spent Nuclear Fuel. This was discussed in a prior subsection.

d. NRC and Industry risk. A problem at one nuclear plant impacts the regulatory requirements imposed on other nuclear plants. Ongoing performance reviews may require expensive operational changes or capital improvements.

e. Relicensing risk. A large investment is required to relicense, which becomes a sunk cost if unsuccessful.

Consumer Advocate and the ICC maintained that the risks of owning a nuclear plant are overstated by IPL or that these risks can be effectively managed, as IPL has done by turning over DAEC operations to NMC. Consumer Advocate maintained the decision to sell was made by IPL based on a flawed cash flow analysis that examined only four scenarios: 1) cost of service regulation without license extension, 2) cost of service rate regulation with license extension, 3) enabling legislation with fixed return on equity ratemaking principles, and 4) enabling legislation with fixed earnings ratemaking principles. Consumer Advocate said no analysis was done of the costs and benefits of continued ownership. In other words, Consumer Advocate and the ICC said the decision to sell was made for shareholders, not customers.

The tone that appears to underlie Consumer Advocate's and the ICC's testimony is a belief that IPL will relicense DAEC if the reorganization is rejected. The testimony does not support this. In fact, given IPL's evident desire to exit the nuclear business, the Board believes it is possible that there would not be any advance ratemaking principles (even if those were statutorily available for DAEC) that would entice IPL to continue with nuclear plant ownership.

The Board believes there are risks to owning a nuclear facility that cannot be effectively managed by an operator such as NMC. For example, operation and maintenance expenses at nuclear plants may be driven by unexpected events at other plants. Problems at other plants may result in industry-wide inspections by the NRC and new regulatory requirements. Complying with new requirements may result in significant capital expenditures and the plant being off-line for a significant period so that the work can be performed. Compliance may also cause ongoing expenses. For example, security costs at nuclear plants have increased dramatically in the post-9/11 era. The transfer of these risks to FPLE Duane Arnold benefits both ratepayers and shareholders. While the Board would have liked to see the ratemaking principles options explored in the legislature, it understands IPL's conclusion that it would be difficult to obtain acceptable principles on an established plant, particularly given the risks of ownership.

While the Board acknowledges the risks associated with nuclear ownership, it does not believe that these risks are dramatically higher than risks associated with other generating plants, as argued by IPL. Coal plants have environmental risks; gas plants have fuel source price increases and volatility. That said, for a utility IPL's size, the financial risks associated with a nuclear plant, if there is an accident or increased regulatory requirements, could have a more dramatic impact on the utility's financial health than the risks associated with a coal or gas plant. A larger company may be better able to manage the risks associated with owning nuclear power.

There was much discussion on what the trends in the industry were. IPL claimed that utilities, particularly those owning one plant, were selling because the risks of continued ownership were too great. Consumer Advocate maintained many of the sales were the result of restructuring legislation in various states that required or encouraged the sale. The Board's review indicates that both views have merit, but there appears to be a movement for utilities that own only one nuclear plant to exit the business. These sales appear to be motivated primarily by a desire to transfer the risk of nuclear ownership because often, as in the sale of Kewaunee Nuclear Station in Wisconsin, there is a PPA involved.

While the Board believes that significant risks are being transferred, the question is at what cost. There are immediate transactional benefits to ratepayers, and additional projected PPA benefits through 2014, but what of the longer view? The next subsection examines the relicensing models presented by the parties as costs and benefits of IPL's decision not to relicense are examined.

8. Relicensing model

The ICC maintained that in order for IPL to demonstrate that the reorganization benefits Iowa ratepayers, IPL would need to conduct a long-term revenue requirement analysis that compares continued ownership and relicensing of DAEC to the next best alternative. (Tr. 1223.) Although IPL did not provide this analysis in its initial case, the analysis was provided in rebuttal. IPL provides a model that compares the DAEC transaction with IPL's projected revenue requirements for the years 2006 through 2034. PPA pricing is assumed through February 2014, followed by a market price forecast. (IPL Ex. 7, Sch. A and A-1.) IPL shows customer benefits (at net present value) from the reorganization as compared to IPL relicensing of approximately $31 million.

IPL's revenue requirement projections are based on assumptions that are consistent with the "best case plus" scenario used in the analysis to 2014, with some exceptions. First, a slightly higher inflation rate is used post-2013 (3 percent vs. 2.5 percent) reflecting the longer time horizon of the relicensing model. Second, DAEC's future performance was modeled in a manner consistent with its recently improved performance. Third, rate of return was projected to be 11 percent through 2014 and 11.5 percent thereafter, recognizing a likely increase in bond yields from current historically low levels. Fourth, a capital structure and cost rates that reflect the 2004 13-month average capital structure consistent was used, with Board precedent. Fifth, O&M and capital costs reflect one-half the increase projected in NMC's proposed 2005-2009 budget plan, rather than the draft plan. Sixth, DAEC relicensing costs reflect NMC projections. (Tr. 94-95.)

IPL also conducted sensitivity analyses using multiple capacity factors. The benefits to customers from the decision to sell DAEC increase as the projected capacity factor is reduced. (Tr. 95.) There is a risk of lower availability as the plant ages.

The electric market forecast used in IPL's relicensing model is the same forecast used to evaluate bids received in the auction process, except the forecast was for a longer period. IPL said it did not revise its methodology in an attempt to inflate market prices used in the relicensing model, adopting a conservative approach, and in fact the forecast used by IPL is somewhat higher than the Platts market price forecast.

Consumer Advocate's cost benefit analysis, performed by Consumer Advocate witness Habr, shows significant economic benefits resulting from continued ownership and relicensing of DAEC. Dr. Habr incorporated IPL witness Boston's cash flow analyses into a cost-benefit study from the customer's perspective. The analyses show benefits to IPL's ratepayers of between $350-$731 million during the 2006 through 2034 time period.

IPL said there were numerous flaws to the assumptions used in Consumer Advocate's relicensing model. First, the model assumes IPL will operate DAEC until 2034, which it will not. Second, market prices used reflect carbon taxes and coal burning technology. IPL argues these taxes do not exist (Tr. 1447) and a 30 percent increase in projected market prices between 2014 and 2015 makes this analysis suspect. Third, the model uses a capacity factor for DAEC, 90 percent, which has never been achieved over any reasonable period of time. Fourth, the analysis assumes an uprate to DAEC's accredited generating capacity in 2009, which is somewhat speculative. (Tr. 678-80.) Fifth, the model assumes NRC regulatory burdens remain unchanged. Sixth, future inflation is projected to be as low as 1 percent. No sensitivity analysis was conducted using different rates. Seventh, spent nuclear fuel costs are assumed not to exceed current estimates, despite a recent increase. (Tr. 1583.) Eighth, O&M costs are assumed to be substantially less than forecasted by NMC. Ninth, DAEC license renewal is reflected in 2010, rather than 2012, which affects the depreciation and decommissioning fund calculations. Tenth, relicensing costs are capitalized, which IPL believes is contrary to Board precedent.

IPL also argued that Consumer Advocate's model was built from scratch and that its model design was never communicated to IPL. (Tr. 803-11.) IPL further states that the model inappropriately converts a cash flow/earnings model into a revenue requirement model. IPL is particularly critical of the assumption that there will be carbon taxes and that relatively new coal power plant technology, called Integrated Gasification Combined Cycle (IGCC), was used as a cost of service measurement. IPL notes that this technology is unproven and costlier than the technology currently used for most coal plants. (Tr. 954.)

The ICC questioned the projections provided by IPL and said the analysis did not compare the next best alternative to replacing DAEC capacity and energy in 2014, which would be a coal plant. The ICC does not believe that IPL's market forecasts, which presume market prices are below the cost of replacement capacity, are credible. (Tr. 1231.) Because DAEC is a base-load facility, the ICC argues the only logical replacement for it, at least for modeling purposes, is a base-load facility.

The only thing that can be said of all the projections for the period from now through 2034 is that none of them will likely be entirely accurate. That being said, the Board finds IPL's forecast for the period to 2034 to be the most reasonable. The Board questions some of the assumptions in Consumer Advocate's model, such as relicensing in 2010 as opposed to 2012, a capacity uprate in 2009, and a 90 percent capacity factor, which is above historical levels and may be particularly difficult to maintain in the plant's later life years (post-2014). The model also does not factor in the net proceeds from the sale going to ratepayers, an immediate benefit.

9. Consumer Advocate's EGEAS analysis

Consumer Advocate witness Shi used the Electric Generation Expansion Analysis System (EGEAS) program to compare, from the least cost resource planning standpoint, IPL's decision to eliminate DAEC from its resource portfolio in 2014 versus IPL's continued ownership and relicensing of DAEC through 2034. The analysis included emissions cost estimates. (Tr. 1447-53; 1351-60; 1502-03.) The analysis shows benefits of $809 million for the license extension, when compared to eliminating DAEC from IPL's portfolio. (Tr. 1505-06; 1511-12; Ex. 207.)

The Board does not give significant weight to Consumer Advocate's EGEAS analysis. While EGEAS is widely used in the utility industry for generation planning purposes, the model is not designed to forecast revenue requirements. In addition, market-based options to replace the DAEC capacity in 2014, such as another PPA, were not included in the analysis. While IPL's resource plan, which uses EGEAS, also does not model a market-based option, this is because IPL's resource plan is used to model utility-owned generation primarily for reliability purposes.

Perhaps most important, the analysis did not take into account the divergent useful lives of a new coal plant put into service in 2014 and a relicensed DAEC. (Tr. 1504.) The coal plant would have a much longer life (at least 40 years) than a relicensed DAEC (20 years). By understating the benefits of a new coal plant, the benefits of relicensing are overstated. Also, the analysis did not factor in the $56 million in net benefits to customers from this transaction.

In short, Consumer Advocate used EGEAS not for resource planning but to project revenue requirements from various options. While it may be possible to use EGEAS for that purpose, the assumptions used here have too many flaws.

10. Conditions

Consumer Advocate urged the Board to protect ratepayers from what it views as IPL's imprudent decision to sell and not relicense DAEC. Consumer Advocate asked the Board to determine that IPL ratepayers should not pay for ongoing decommissioning expenses contained in the PPA and that IPL's imprudent decision to sell may be the subject of a management efficiency adjustment in future rate case proceedings and may be taken into account in future ratemaking principle proceedings.

While the subject of this reorganization is the proposed sale of DAEC, the evidence regarding that sale is intertwined with evidence regarding the prudence of IPL's decision not to relicense DAEC. As pointed out by IPL in brief, the relicensing decision is not directly within the Board's jurisdiction, although management decisions such as this one may have consequences in future rate or other proceedings before the Board. The Board will decline to make a finding on the prudency of the relicensing decision both because the decision on relicensing is not directly at issue in this proceeding and because such a finding may have little or no impact in a future rate or other proceeding. Iowa-Illinois Gas and Electric Company v. Iowa State Commerce Commission, 412 N.W.2d 600 (Iowa 1987). However, as noted by the dissent, the Board's ability to "punish" a utility after the fact may be limited and may have adverse consequences to ratepayers. The Board will not condition the sale as requested by Consumer Advocate and further notes that it has consistently held it does not have statutory authority to condition a reorganization.

The ICC asked for some minor conditions, such as a liquidated damages clause, to keep IPL whole in the event FPLE Duane Arnold fails to deliver energy when DAEC is running. FPLE Duane Arnold has a specific contractual obligation to provide such power and IPL would have legal remedies in the event of a breach. A liquidated damages clause does not appear necessary and such a provision may cause price and other terms to be renegotiated. The ICC also asked that any approval be conditioned on IPL agreeing not to seek recovery of any future decommissioning costs in rates. Because FPLE Duane Arnold assumes this responsibility, this condition would not add anything significant to the agreement and the Board is approving this reorganization with the understanding that IPL ratepayers, after closing and transfer of decommissioning funds, have no further decommissioning liability associated with DAEC.

11. Conclusion on ratepayer interest

The Board believes that IPL should have pursued the relicensing option much more forcefully than it did. The Board believes there are significant benefits associated with owning a diverse generation mix that includes nuclear power, although there are different risks associated with nuclear power than other generation sources. Some of the benefits are nonquantifiable, such as the price certainty that comes with ownership. The cost of that price certainty, though, may be the payment, at least at times, of higher-than-market prices.

While the Board might prefer that another option had been pursued, IPL established on this record that the proposed organization is not detrimental to ratepayer interests. While there are positives and negatives regarding the DAEC sale, on balance the evidence shows that there will be immediate ratepayer benefits of $56 million, PPA benefits through 2014 with a net present value of $23.6 million, and benefits, although more speculative, through 2034. The statutory standard has been satisfied.

The Board notes that there was some discussion as to the appropriate time frame for the Board to examine in making its determination. There is no hard and fast standard. The Board's rules require an applicant to file an analysis of the projected financial impact of the proposed reorganization on ratepayers for the first five years. 199 IAC 32.4(4)"b." However, the statute does not limit the Board's authority to a five-year period. The subrule is a filing requirement only; the Board can examine information, as it did in this docket, beyond five years.

PUBLIC INTEREST

It is often difficult to separate ratepayer from the broader public interest and some of the issues impacting the public interest have been discussed. In examining the public interest, the Board looks at concerns broader than ratepayer interest alone and looks at the impact of the reorganization on the state and its citizens. Paragraph

199 IAC 32.4(4)"c" specifically requires Applicants to provide an analysis of the effect of the reorganization on the public interest. Public interest is specifically defined as "the interest of the public at large, separate and distinct from the interest of the public utility's ratepayers." The analysis should include impacts on the state and local communities.

The public interest issues remaining relate primarily to the importance of DAEC to reliability in the area and the economic benefits associated with the plant. FPLE Duane Arnold plans to increase the DAEC workforce by 10 percent, or approximately 50 employees. This would bring the workforce to 550 employees.

All employees of DAEC will be offered continued employment for at least 18 months at like salary and benefits and all collective bargaining contracts will be assumed. (Tr. 280.) About half the DAEC employees are members of a bargaining unit. As a practical matter, and this was not contested in testimony or brief, current staff will likely be retained at DAEC longer than the 18 months provided for in the ASA at like salary and benefits because of the scarcity of qualified labor in the nuclear field.

Annual spending for labor, contractors, and materials during non-refueling years was $56 million in 2004 and projected at $58 million in 2005. This goes up significantly during a refueling year, as up to 2,000 additional people augment the DAEC staff, representing millions of dollars in hotel and restaurant spending. (Tr. 637.) DAEC generates $423.3 million in total regional industrial output, $92.8

million in total regional labor income, and 1,456 jobs. (Tr. 106-08.) For the benefit of the state as a whole, DAEC paid state replacement property taxes of $2 million in 2004. (Tr. 108.) The total economic, non-ratepayer benefits provided by the reorganization are estimated to be in excess of $8 billion. (Tr. 262.)

DAEC provides electrical support for transmission in the Cedar Rapids area, primarily reactive support for voltage levels. (Tr. 982.) If DAEC were to shut down in 2014, significant investment in the transmission system and/or additional generation would be required to safely and reliably operate the system. (Tr. 988.) Some improvements beyond the Cedar Rapids area could also be required. The beneficial impact DAEC has on the transmission system not only positively affects the reliability of service for IPL customers in the area but also improves reliability of the utility systems that are electrically interconnected to IPL's transmission systems. The evidence establishes that DAEC's continued operation past 2014 is necessary for optimal operation of the transmission system with the least amount of additional investment. IPL noted in brief that because CIPCO and Corn Belt have elected, at this time, not to sell their interests in DAEC, they will not be able to continue to receive the benefits of DAEC unless it is relicensed. There is nothing in the record to indicate that Corn Belt and CIPCO have any interest in purchasing IPL's 70 percent of DAEC and relicensing on their own.

The Board recognizes that the public interest benefits associated with DAEC could be largely retained if IPL relicensed the plant. However, IPL clearly stated its intent, in prefiled testimony, cross-examination at hearing, and in brief, that IPL would not relicense DAEC in 2014. Absent a sale of DAEC to another entity who is committed to relicensing, as is FPLE Duane Arnold, all tangible public benefits associated with the operation of DAEC would be lost in 2014.

FPLE Duane Arnold is committed to relicensing DAEC. FPLE Duane Arnold also committed to hiring additional employees and engaging in capital spending to improve DAEC performance. These additional expenditures will enhance the public benefits currently associated with DAEC and provide the best assurance that these benefits will continue through 2034. The evidence demonstrates that the reorganization is in the public interest.

POSSIBLE CHANGES TO THE PROPOSAL

The Board understands that to date no material conditions or changes to Applicant's proposal have been imposed by the NRC or FERC, which are the federal agencies reviewing certain aspects of this reorganization. The Board also understands that no state reviewing Applicant's proposal have imposed material conditions or changes. The Board will reach its conclusions based upon the reorganization proposal submitted to it. Any material changes in the proposed reorganization may change the basis for the conclusions the Board has reached and may require submission of a revised proposal. Therefore, if there are any material changes to the proposed reorganization prior to final closing, Applicants will be required to file those changes with the Board, along with an analysis of the impact of the changes.

EWG STATUS

FPLE Duane Arnold wants to operate DAEC as an EWG under federal law. In order to obtain this status, Iowa and other states with jurisdiction over any utility within the Alliant Energy holding company group must make a determination that, subsequent to the sale of DAEC to FPLE Duane Arnold, allowing DAEC to be an "eligible facility" pursuant to the provisions of the Public Utility Holding Companies Act of 1938 (PUHCA) will benefit consumers, is in the public interest, and does not violate Iowa law. An eligible facility is defined under section 32(c) of PUHCA as "a facility . . . used for the generation of electric energy exclusively for sale at wholesale." No party, other than Applicants, presented evidence concerning FPLE Duane Arnold's request for EWG status.

Applicants have presented sufficient evidence for the Board to make the required PUHCA findings. Allowing DAEC, including its nuclear fuel, to become an "eligible facility" will benefit consumers and be in the public interest because the sale to FPLE Duane Arnold will result in DAEC continuing to operate in Iowa, rather than being retired. The PPA ensures that DAEC power will be available to IPL's retail customers through 2014. If DAEC is relicensed, the power will be available, perhaps to IPL retail customers, for an additional 20 years. The testimony indicated that DAEC provides significant benefits to the area for transmission and reliability, benefiting all electric users. As noted in earlier sections, significant risks are transferred from IPL to FPLE Duane Arnold, benefiting IPL's current and future ratepayers.

In addition, DAEC provides significant economic benefits to the state. Annual spending for labor, contractors, and materials during non-refueling years was $56 million in 2004 and projected at $58 million in 2005. FPLE Duane Arnold plans to increase DAEC's workforce by approximately 10 percent or about 50 employees. Spending goes up significantly during a refueling year, as up to 2,000 additional people augment the DAEC staff, representing millions of dollars in hotel and restaurant spending. (Tr. 637.) The sale of DAEC to FPLE Duane Arnold does not violate Iowa law.

DISPOSITION OF NET PROCEEDS

Under IPL's original proposal, net proceeds will be accounted for in a regulatory liability account to be used to offset AFUDC for investments in new generation sited in Iowa. (Tr. 38.) The account will earn interest at a rate equivalent to the monthly average U.S. Treasury 3-year constant maturities as reported by the Federal Reserve Board Statistical Release H.15. (Tr. 537.) Later, IPL offered to return net proceeds in any manner directed by the Board, including refunds or bill credits.

The Board believes it is most appropriate for net proceeds to be deposited in a regulatory liability account. The amount of any refund or bill credit would not make a significant impact on many customers' bills and IPL will be able to mitigate future rate increases by using this share of the transactional value to offset AFUDC on new generation. (Tr. 42.) Mitigation of rate increases promotes rate stability and certainty.

The testimony at hearing was unclear as to whether the net proceeds could be tax affected if placed in a regulatory liability account. The testimony was clear that the proceeds would be tax affected if there was a direct refund or bill credit. IPL's brief suggested the issue was settled and the amount would be tax affected if placed in a regulatory liability account. However, statements in a brief that are not part of the record are not evidence in the proceeding. Therefore, the Board will require IPL to file an affidavit stating whether the $33 million in net proceeds will be tax affected if placed in a regulatory liability account, bringing the total net proceeds to $56 million. If the answer is yes, then IPL is directed to set up such an account and use the proceeds as it initially proposed. If the answer is no, the Board will receive comments from the parties on how to disburse the proceeds. The Board wants to maximize the transactional benefit to ratepayers. IPL will be required to file the affidavit within seven days from the date of this order or explain when an affidavit can be filed.

FINDINGS AND CONCLUSIONS

Based upon the testimony and evidence filed pursuant to Iowa Code § 476.77 and 199 IAC 32, the Board finds that Applicants have established the proposed reorganization is not contrary to the interests of ratepayers and the public interest. The Board also finds the other statutory factors are satisfied. Therefore, the reorganization proposed by IPL will be permitted to take place by operation of law, effective immediately, and this docket will be terminated. The Board has jurisdiction over the parties and proceedings pursuant to Iowa Code chapter 476. The Board's conclusions that the reorganization will be permitted to take place is based on the following specific findings of fact:

1. It is reasonable to find that the Board will have reasonable access to books, records, documents, and other information relating to IPL or any of its affiliates after the reorganization.

2. Based on the commitments made by FPLE Duane Arnold, it is reasonable to find that the Board will have access to information necessary to perform its regulatory functions after the PPA expires in 2014.

3. It is reasonable to find that IPL's ability to attract capital on reasonable terms, including the maintenance of a reasonable capital structure, will not be impaired by the reorganization, and that its use of the proceeds of the transaction, one-half to retire IPL short-term debt and one-half as a dividend to Alliant Energy, is reasonable.

4. It is reasonable to find that IPL's ability to provide safe, reasonable, and adequate service will not be impaired by the reorganization.

5. The terms of the Asset Sale Agreement, Purchase Power Agreement, and other transaction documents, taken as a whole, are reasonable.

6. Viewing the evidence as a whole, the projected benefits of the reorganization presented by IPL, pre- and post-2014, are more reasonable than projections provided by other parties.

7. It is reasonable to find that the proposed reorganization is not a detriment to ratepayer interest and provides ratepayers with both quantifiable and nonquantifiable benefits.

8. It is reasonable to find that the proposed reorganization is not a detriment to the public interest and provides the public with quantifiable benefits.

9. Assuming the net proceeds can be tax affected, it is reasonable to utilize the net proceeds from the reorganization by placing them in a regulatory liability account to offset AFUDC associated with future generating plant construction.

10. Allowing FPLE Duane Arnold to become an eligible facility will benefit consumers and is in the public interest.

CONCLUSIONS OF LAW

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

2. Allowing FPLE Duane Arnold to become an eligible facility does not violate Iowa law.

ORDERING CLAUSES

IT IS THEREFORE ORDERED:

1. The application for reorganization filed by Interstate Power and Light Company and FPL Energy Duane Arnold, LLC, on July 29, 2005, is not disapproved. The reorganization is allowed to take place pursuant to law. This concludes Board action on the reorganization and Applicants may close the transaction at any time.

2. Pursuant to PUHCA, the Board determines that granting eligible facility status to FPLE Duane Arnold for DAEC will benefit consumers, is in the public interest, and does not violate Iowa law.

3. IPL is authorized to create a regulatory liability account for the net proceeds of the DAEC transaction. None of the funds placed into this regulatory liability account relate to the flow-through of either the unamortized deferred investment tax credit or accumulated deferred income taxes related to excess deferred taxes to customers. Authorization to create this account is contingent on IPL filing an affidavit, within seven days from the date of this order, that net proceeds placed into this account will be tax affected.

4. Applicants shall promptly file with the Board any material changes to the proposed reorganization that occur prior to final closing of the reorganization. Any filing shall include an analysis of the effect of the changes on each of the factors considered by the Board in this order.

5. Motions and objections not previously granted or sustained are denied or overruled. Any argument in the briefs 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/ John R. Norris

/s/ Curtis W. Stamp

DISSENT OF BOARD MEMBER DIANE MUNNS
DOCKET NO. SPU-05-15

I respectfully dissent. While I have no objection to much of the analysis and discussion contained in the order, and particularly agree that DAEC has continuing economic and reliability benefits to the state of Iowa, I believe that IPL has not established that the reorganization is not detrimental to the interests of ratepayers and the public. I come to this conclusion because IPL did not in a timely fashion adequately explore options that might have resulted in IPL relicensing DAEC.

I am particularly disappointed that IPL readily discarded legislative options that might result in more favorable and certain ratemaking treatment for a relicensed DAEC. The evidence indicates that these options were not explored with the Board, legislative leaders, or Consumer Advocate. The failure to explore these options further appears to be based on IPL's conclusions that legislation would not be successful and that there was not sufficient time. I am not persuaded by these justifications.

IPL in recent years has consistently indicated that it was keeping its options open regarding relicensing DAEC. The financial risks of nuclear plant ownership that IPL advances as reasons for exiting the nuclear business have been fairly constant for the last several years. Given this, I do not understand why IPL did not explore legislative options several years ago. The Legislature adopted legislation in 2001 that allows utilities to apply for advance ratemaking principles for new generation. The Legislature did this to encourage rate-regulated electric utilities to invest in needed new electric generation in Iowa. IPL did not propose that a relicensed DAEC be part of this statute and it did not discuss such legislation with significant stakeholders in subsequent years.

The advance ratemaking legislation was fully vetted in 2001 and has achieved the Legislature's goal of encouraging in-state, utility-owned generation. IPL could have proposed adding a relicensed nuclear plant to the list of generation eligible for advance ratemaking principles, but did not do so in 2001 or subsequent years. I believe by the time IPL seriously considered legislative solutions in 2004, IPL concluded it was too late to engage the process. From IPL's viewpoint, the relicensing option was then effectively foreclosed.

I also find that IPL's analysis presented in rebuttal testimony of the benefits of the sale versus continued relicensing is unpersuasive. IPL's analysis did not take into account environmental concerns, such as potential carbon taxes and sequestration, related to a new coal plant that could replace DAEC capacity and energy when the PPA expires in 2014. As utilities found out with the building surge of gas-fired generating units, there are risks in not having a diverse fuel supply. DAEC gives IPL a supply source different from gas or coal, both fossil fuels, and helps insulate customers from supply, price, and environmental risks associated with fossil fuels. IPL has effectively managed operating risks associated with DAEC by joining the NMC and the evidence was overwhelming that there is no reason DAEC cannot be relicensed. On a going forward basis, I am not persuaded by IPL's arguments that nuclear generation has a greater risk profile than gas or coal generation, particularly when environmental risks from emissions are factored in.

It would be easy to allow this reorganization to go forward by only focusing on the time period to 2014. However, this is the only docket where the Board can effectively examine the decision not to relicense. While Consumer Advocate argues that the prudency of the relicensing decision can be examined in future rate or ratemaking principles cases, I do not believe that the decision not to relicense can be effectively revisited in future proceedings. If IPL builds a coal plant in the next decade to replace DAEC capacity and energy, it will likely be before the Board for advance ratemaking principles. An intervenor might argue IPL should receive a lesser return or be otherwise financially “punished” for its decision not to relicense DAEC. However, IPL is not obligated to accept the advance ratemaking principles determined by the Board and could simply decline to build and purchase power on the market, to the potential detriment of customers. Applying this type of financial penalty after the fact may undermine a utility’s financial condition and produce results that are detrimental to customers.

It is unreasonable for this decision to be made in a vacuum with the focal point being the time period through 2014, with scant evidence on what will replace DAEC and at what cost when the PPA expires. It may be that a thorough analysis would support IPL’s decision not to relicense and to sell DAEC. I simply do not know, because that thorough analysis is not in the record.

/s/ Diane Munns

ATTEST:

/s/ Judi K. Cooper
Executive Secretary

Dated at Des Moines, Iowa, this 30th day of November, 2005.