

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

IN RE:  ELECTRIC ENERGY ADJUSTMENT CLAUSE	DOCKET NO. RMU-07-11
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**ORDER GRANTING PETITION AND COMMENCING RULE MAKING**

(Issued February 7, 2008)

On December 14, 2007, Interstate Power and Light Company (IPL) filed with the Utilities Board (Board) a petition for rule making. IPL proposed various changes to the definitions in 199 IAC 20.1(3) and the energy adjustment clause (EAC) rules in 199 IAC 20.9, 20.13, and 20.17 to reflect new emissions allowances under the federal Clean Air Interstate Rule (CAIR) and the Clean Air Mercury Rule (CAMR). IPL noted that the CAIR and CAMR programs are to be implemented in Iowa by a cap and trade program that will rely on interstate emission allowance markets to achieve reductions. The Board's current rules only address emissions allowances created by the federal Clean Air Act to address sulfur dioxide (SO<sub>2</sub>) and nitrogen oxide (NO<sub>x</sub>) discharges. With the adoption of CAIR and CAMR, there are additional SO<sub>2</sub> and NO<sub>x</sub> requirements as well as requirements for mercury reductions.

On December 27, 2007, the Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed a response to IPL's petition. Consumer Advocate did not object to the Board commencing a rule making as proposed by IPL,

but Consumer Advocate said a rule making should not be specifically limited to the topics addressed by IPL. Consumer Advocate did not endorse IPL's proposed changes, but is willing to address them in a rule making proceeding.

IPL's petition would allow the Board and all interested parties an opportunity to reexamine the EAC rules to see if changes are necessary to reflect the new emissions allowances. IPL argued that because the Board's current rules require proceeds from the sale of emissions allowances to flow through the EAC, while purchases of allowances are valued at historical cost, this creates a generational mismatch. IPL's proposal would exempt from the EAC refund what it calls "vintage trades" (sale or trade of allowances for one year for allowances from another year). Under IPL's proposal, the proceeds from any such sale could be used for the purchase of another vintage of allowances with any difference flowing through the EAC. Other changes proposed by IPL include an amendment to the definition of "historical costs" and a definition of options to use as a recognized hedging strategy.

The best way to understand the intergenerational inequity argument is by example. As the Board understands IPL's statements, allowances for a given year, such as 2008, have no monetary value once the year is over; a utility with surplus allowances for 2008 will want to sell them by year-end. If a utility with an EAC sold its surplus 2008 allowances for \$50 million, all the sales proceeds would flow through the EAC under current rules. If the utility used \$48 million of the proceeds to purchase 2012 allowances, the \$48 million would be booked as inventory and added

to rate base in the utility's next rate case, where it would earn a return; only when the allowances were used for environmental compliance in 2012 would they be expensed through the EAC. Under IPL's proposed rule changes, only the difference in cost between the two vintages of allowances, or \$2 million, would flow through the EAC.

The Board believes that the EAC rules should be reexamined in light of the new emissions allowances and concerns regarding intergenerational equity. Therefore, the Board will grant IPL's petition for rule making pursuant to the authority of Iowa Code §§ 17A.4, 17A.7, 476.1, and 476.6(8) and commence a rule making proceeding to consider the adoption of IPL's proposed changes. Consumer Advocate or others may also propose additional changes to the EAC rules; these proposals may be considered in this rule making or subsequent rule making proceedings.

**IT IS THEREFORE ORDERED:**

1. The petition for rule making filed by Interstate Power and Light Company on December 14, 2007, is granted.
2. A rule making proceeding, identified as Docket No. RMU-07-11, is commenced for the purposes of receiving comments on the proposed amendments in the notice attached hereto and incorporated by reference in this order.

3. The Executive Secretary is directed to submit for publication in the Iowa Administrative Bulletin a notice in the form attached to and incorporated by reference in this order.

**UTILITIES BOARD**

/s/ John R. Norris

/s/ Krista K. Tanner

ATTEST:

/s/ Judi K. Cooper  
Executive Secretary

/s/ Darrell Hanson

Dated at Des Moines, Iowa, this 7<sup>th</sup> day of February, 2008.

## **UTILITIES DIVISION [199]**

### **Notice of Intended Action**

Pursuant to Iowa Code sections 17A.4, 17A.7, 476.1, and 476.6(8), the Utilities Board (Board) gives notice that on February 7, 2008, the Board issued an order in Docket No. RMU-07-11, In re: Electric Energy Adjustment Clause, "Order Granting Petition and Commencing Rule Making." The Board is noticing for public comment proposed amendments to 199 IAC 20.1(3), 20.9, 20.13, and 20.17. The amendments impact the energy adjustment clause (EAC) and were proposed by Interstate Power and Light Company (IPL) in a petition for rule making filed with the Board.

In its petition for rule making, IPL said amendments to the current EAC rules were necessary to reflect new emissions allowances under the federal Clean Air Interstate Rule (CAIR) and the Clean Air Mercury Rule (CAMR). IPL noted that the CAIR and CAMR programs are to be implemented in Iowa by a cap and trade program that will rely on the interstate emission allowance markets to achieve reductions. The Board's current rules only address emissions allowances created by the federal Clean Air Act to address sulfur dioxide (SO<sub>2</sub>) and nitrogen oxide (NO<sub>x</sub>) discharges. With the adoption of CAIR and CAMR, there are additional SO<sub>2</sub> and NO<sub>x</sub> requirements as well as requirements for mercury reductions.

IPL also argued in its petition that the Board's current rules create a generational mismatch because proceeds from the sale of emissions allowances flow through the EAC, while purchases of allowances are valued at historical cost. IPL's proposal would

exempt from the EAC refund what it calls "vintage trades" (sale or trade of allowances for one year for allowances from another year). Under IPL's proposal, only the difference between the sale or trade values of the different vintages of allowances would flow through the EAC. Other changes proposed by IPL include an amendment to the definition of "historical costs" and a definition of options to use as a recognized hedging strategy.

An example illustrates the intergenerational equity argument. According to IPL, allowances for a given year, such as 2008, have no monetary value once the year is over; a utility with surplus allowances for 2008 will want to sell them by year-end. If a utility with an EAC sold its surplus 2008 allowances for \$50 million, all the sales proceeds would currently flow through the EAC. If the utility used \$48 million of the proceeds to purchase 2012 allowances, the \$48 million would be booked as inventory and added to rate base in the utility's next rate case, where it would earn a return; only when the allowances were used for environmental compliance in 2012 would they be expensed through the EAC. Under IPL's proposed rule changes, only the difference in cost between the two vintages of allowances, or \$2 million, would flow through the EAC.

The Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed a response to the petition for rule making on December 27, 2007. Consumer Advocate did not take a position on IPL's proposed rule changes, but said it was willing to consider them in a rule making proceeding. Consumer Advocate also noted that additional changes might be proposed by Consumer Advocate or others. The Board indicated in its order granting the rule making petition that other changes could be considered in this or subsequent rule makings.

Pursuant to Iowa Code sections 17A.4(1)"a" and "b," any interested person may file a written statement of position pertaining to the proposed amendments. The statement must be filed on or before March 18, 2008, by filing an original and ten copies in a form substantially complying with 199 IAC 2.2(2). All written statements should clearly state the author's name and address and should make specific reference to this docket. All communications should be directed to the Executive Secretary, Iowa Utilities Board, 350 Maple Street, Des Moines, Iowa 50319-0069.

A public hearing to receive comments on the proposed amendment will be held at 10 a.m. on April 8, 2008, in the Board's hearing room at the address listed above. Persons with disabilities who require assistive services or devices to observe or participate should contact the Utilities Board at (515) 281-5256 in advance of the scheduled date to request that appropriate arrangements be made.

The Board does not find it necessary to propose a separate waiver provision in this rule making. The Board's general waiver provision in 199 IAC 1.3 is applicable to this rule.

These amendments are intended to implement Iowa Code section 476.6(8).

The following amendments are proposed.

Item 1. Amend rule **20.1(3)** as follows:

**20.1(3)** Definitions. The following words and terms when used in these rules, shall have the meaning indicated below:

"Acid Rain Program" means the sulfur dioxide and nitrogen oxides air pollution control program established pursuant to Title IV of the Act under 40 CFR Parts 72-78.

"Act" means the Clean Air Act, 42 U.S.C. Section 7401, et seq., as amended by Pub. L. 101-549, November 15, 1990.

"Affected unit" means a unit or source that is subject to any emission reduction requirement or limitation under the Acid Rain Program, the Clean Air Interstate Rule (CAIR), and/or the Clean Air Mercury Rule (CAMR), or a unit or source that opts in under 40 CFR Part 74.

"Allowance" means an authorization, allocated by the United States Environmental Protection Agency (EPA) under the Acid Rain Program, to emit ~~up to one ton of~~ sulfur dioxide ( $\text{SO}_2$ ), any  $\text{SO}_2$  and nitrogen oxide ( $\text{NO}_x$ ) emissions subject to the Clean Air Interstate Rule (CAIR), and/or mercury (Hg) emissions subject to the Clean Air Mercury Rule (CAMR), during or after a specified calendar year.

"Allowance forward contract" is an agreement between a buyer and seller to transfer an allowance on a specified future date at a specified price.

"Allowance futures contract" is an agreement between a futures exchange clearinghouse and a buyer or seller to buy or sell an allowance on a specified future date at a specified price.

"Allowance option contract" is an agreement between a buyer and seller whereby the buyer has the option to transfer an allowance(s) at a specified date at a specified price. The seller of a call or put option will receive a premium for taking on the associated risk.

"Board" means the utilities board.

"Clean Air Interstate Rule" means the requirements EPA published in the Federal Register (70 Fed. Reg. 25161) on May 12, 2005.

"Clean Air Mercury Rule" means the requirements EPA published in the Federal Register (70 Fed. Reg. 28605) on May 18, 2005.

"Complaint" as used in these rules is a statement or question by anyone, whether a utility customer or not, alleging a wrong, grievance, injury, dissatisfaction, illegal action or procedure, dangerous condition or action, or utility obligation.

"Compliance plan" means the document submitted for an affected source to the ~~Environmental Protection Agency~~ EPA which specifies the methods by which each affected unit at the source will meet the applicable emissions limitation and emissions reduction requirements.

"Customer" means any person, firm, association, or corporation, any agency of the federal, state or local government, or legal entity responsible by law for payment for the electric service or heat from the electric utility.

"Delinquent" or "delinquency" means an account for which a service bill or service payment agreement has not been paid in full on or before the last day for timely payment.

"Distribution line" means any single or multiphase electric power line operating at nominal voltage in either of the following ranges: 2,000 to 26,000 volts between ungrounded conductors or 1,155 to 15,000 volts between grounded and ungrounded conductors, regardless of the functional service provided by the line.

"Economy energy" is energy bought or sold in a transaction wherein the supplier's incremental cost is less than the buyer's decremental cost, and the differential in cost is shared in an equitable manner by the supplier and buyer.

"Electric plant" includes all real estate, fixtures and property owned, controlled, operated or managed in connection with or to facilitate production, generation, transmission, or distribution, in providing electric service or heat by an electric utility.

"Electric service" is furnishing to the public for compensation any electricity, heat, light, power, or energy.

"Emission for emission trade" is an exchange of one type of emission for another type of emission. For example, the exchange of SO<sub>2</sub> for NO<sub>x</sub> emission allowances.

"Energy" means electric energy measured in kilowatt hours.

"Firm power" is power and associated energy intended to be available at all times during the period covered by the commitment.

"Gains and losses from allowance sales" are calculated as the difference between the sale price of allowances sold during the month and the weighted average unit cost of inventoried allowances.

"Meter" means, unless otherwise qualified, a device that measures and registers the integral of an electrical quantity with respect to time.

"Meter shop" is a shop where meters are inspected, repaired and tested, and may be at a fixed location or may be mobile.

"Operating reserve" is a reserve generating capacity required to ensure reliability of generation resources.

"Operational control energy" is energy supplied by a selling utility to a buying utility for the improvement of electric system operation.

"Outage energy" is energy purchased during emergency or scheduled maintenance outages of generation or transmission facilities, or both.

"Participation power" means power and associated energy or energy which is purchased or sold from a specific unit or units on the basis that its availability is subject to prorate or other specified reduction if the units are not operated at full capacity.

"Peaking power" is power and associated energy intended to be available at all times during the commitment and which is anticipated to have low load factor use.

"Power" means electric power measured in kilowatts.

"Price hedging" means using futures contracts or options to guard against unfavorable price changes.

"Rate-regulated utility" means any utility, as defined in 20.1(3), which is subject to board rate regulation under Iowa Code chapter 476.

"Secondary line" means any single or multiphase electric power line operating at nominal voltage less than either 2,000 volts between ungrounded conductors or 1,155 volts between grounded and ungrounded conductors, regardless of the functional service provided by the line.

"Service limitation" means the establishment of a limit on the amount of power that may be consumed by a residential customer through the installation of a service limiter on the customer's meter.

"Service limiter" means a circuit breaker device that limits a residential customer's power consumption to 15 amps at 120 volts (or some higher level of usage approved by the board) and that either resets itself automatically or can be reset by the customer.

"Speculation" means using futures contracts or options to profit from expectations of future price changes.

"Tariff" means the entire body of rates, tolls, rentals, charges, classifications, rules, procedures, policies, etc., adopted and filed with the board by an electric utility in fulfilling its role of furnishing service.

"Timely payment" is a payment on a customer's account made on or before the date shown on a current bill for service, or on a form which records an agreement between the customer and a utility for a series of partial payments to settle a delinquent account, as the date which determines application of a late payment charge to the current bill or future collection efforts.

"Transmission line" means any single or multiphase electric power line operating at nominal voltages at or in excess of either 69,000 volts between ungrounded conductors or 40,000 volts between grounded and ungrounded conductors, regardless of the functional service provided by the line.

"Utility" means any person, partnership, business association or corporation, domestic or foreign, owning or operating any facilities for providing electric service or heat to the public for compensation.

"Vintage trade" is an exchange of one vintage of allowances for another vintage of allowances with the difference in value between vintages being cash or additional allowances.

"Weighted average unit cost of inventoried allowances" equals the dollars in inventory at the end of the month divided by the total allowances available for use at the end of the month.

"Wheeling service" is the service provided by a utility in consenting to the use of its transmission facilities by another party for the purpose of scheduling delivery of power or energy, or both.

Item 2. Amend subrule **20.9(2)"b"(8)** as follows:

(8) The gains and losses, as described in rule 20.17(9)(476), from allowance sales transactions occurring during the month. Allowance transactions shall include vintage trades and emission for emission trades.

Item 3. Amend subrule **20.9(2)"e"(1)** as follows:

e. A rate-regulated utility desiring to collect expensed allowance costs and the gains and losses from allowance transactions through the energy adjustment must file with the board monthly reports including:

(1) The number and weighted average unit cost of allowances used during the month to offset sulfur dioxide emissions from the utility's affected units;

Item 4. Amend subrule **20.13(1)"h"** as follows:

h. Compliance plans. Each utility shall file its SO<sub>2</sub> emissions compliance plan as submitted to the EPA. Revisions to the compliance plan shall be filed with each subsequent procurement plan.

Item 5. Amend rule **20.17(1)** as follows:

**20.17(1)** Applicability and purpose. This rule applies to all rate-regulated utilities providing electric service in Iowa. Under Title IV of the Clean Air Act Amendments of 1990, each electric utility is required to hold sufficient emission allowances to offset sulfur dioxide emissions at all affected and new units. The acquisition and disposition of emission allowances will be treated for ratemaking purposes as defined in this rule.

Item 6. Amend rule **20.17(2)** as follows:

**20.17(2)** Definitions. The following words and terms, when used in this rule, shall have the meaning indicated below:

"Allowance futures contract" is an agreement between a futures exchange clearinghouse and a buyer or seller to buy or sell an allowance on a specified future date at a specified price.

"Allowance option contract" is an agreement between a buyer and seller whereby the buyer has the option to transfer an allowance(s) at a specified date at a specified price. The seller of a call or put option will receive a premium for taking on the associated risk.

"Auction allowances" are allowances acquired or sold through EPA's annual allowance auction.

"Boot" means something acquired or forfeited to equalize a trade.

"Direct sale allowances" are allowances purchased from the EPA in its annual direct sale.

"Emission for emission trade" is an exchange of one type of emission for another type of emission. For example, the exchange of SO<sub>2</sub> for NO<sub>x</sub> emission allowances.

"Fair market value" is the amount at which an allowance could reasonably be sold in a transaction between a willing buyer and a willing seller other than in a forced or liquidation sale.

"Historical cost" is the amount of cash or its equivalent paid to acquire an asset, including any direct acquisition expenses. Any commissions paid to brokers shall be considered a direct acquisition expense.

"Original cost" is the historical cost of an asset to the person first devoting the asset to public service.

"Statutory allowances" are allowances allocated by the EPA at no cost to affected units under the Acid Rain Program either through annual allocations as a matter of statutory right and those for which a utility may qualify by using certain compliance options or effective use of conservation and renewables.

"Vintage trade" is an exchange of one vintage of allowances for another vintage of allowances with the difference in value between vintages being cash or additional allowances.

Item 7. Amend rule **20.17(8)** as follows:

**20.17(8)** Expense recognition and recovery of allowance costs.

a. Expense recognition. Electric utilities shall charge allowances (including fractional amounts) to expense in the month in which related ~~sulfur dioxide~~ emissions occur.

b. Expense recovery. The expense associated with allowances used for compliance shall be passed through the energy adjustment as specified in rule 20.9(476). The expense associated with allowances used for compliance shall include expenses associated with vintage trades and emission for emission trades.

c. Allowance inventory shortage. If a utility emits more ~~sulfur dioxide~~ emissions in a month than it has allowances in inventory, the utility shall pass the estimated cost of acquiring the needed allowances through the energy adjustment. When the needed allowances are acquired, any difference between the estimated and actual cost of the

allowances shall be passed through the energy adjustment as specified in rule 20.9(476).

Item 8. Amend rule **20.17(9)** as follows:

**20.17(9)** Gains/losses from allowance transactions. The gains and losses, including net gains and losses, from allowance transactions shall be passed through the energy adjustment as specified in rule 20.9(476). Allowance transactions shall include vintage trades and emission for emission trades.

Item 9. Amend rule **20.17(10)** as follows:

**20.17(10)** Allowance futures or option contracts.

a. Price hedging. Electric utilities shall defer the costs or benefits from hedging transactions and include such amounts in inventory values when the related allowances are acquired, sold, or otherwise disposed of. Where the costs or benefits of hedging transactions are not identifiable with specific allowances, the amounts shall be included in inventory values when the futures contract is closed.

b. Speculation. Allowance transactions entered into for the purpose of speculation shall not affect allowance inventory pricing.

February 7, 2008

/s/ John R. Norris

John R. Norris  
Chairman