

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of	)	
INDIANA MICHIGAN POWER COMPANY	)	
for a certificate of necessity pursuant to	)	Case No. U-17026
MCL 460.6s and related accounting authority.	)	
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At the January 28, 2013 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. John D. Quackenbush, Chairman
Hon. Orjiakor N. Isiogu, Commissioner
Hon. Greg R. White, Commissioner

ORDER

On May 1, 2012, Indiana Michigan Power Company (I&M) filed an application, with supporting testimony and exhibits, requesting that the Commission grant a certificate of necessity (CON) pursuant to Section 6s of 2008 PA 286; MCL 460.6s. I&M also requested related accounting authority.

A prehearing conference was held on June 5, 2012 before Administrative Law Judge Thomas E. Maier (ALJ). At the prehearing conference, the ALJ granted a protective order requested by I&M and granted petitions to intervene filed by the Michigan Department of the Attorney General (Attorney General) and the Michigan Environmental Council (MEC). The Commission Staff (Staff) also participated in the proceeding. Subsequently, a late petition to intervene was filed by New Covert Generating Company, LLC, which was denied, and the parties filed a stipulation to grant late intervention to the Association of Businesses Advocating Tariff Equity (ABATE).

The Staff and intervenors filed testimony and exhibits on August 7, 2012, and I&M filed rebuttal on September 5, 2012. Evidentiary hearings were conducted on September 17 through September 19, 2012. All of the parties filed briefs and reply briefs on October 12 and October 26, 2012 respectively. The ALJ issued his Proposal for Decision (PFD) on December 17, 2012. I&M, the Attorney General, and ABATE filed exceptions to the PFD on December 27, 2012, and I&M, the Staff, the Attorney General, and ABATE filed replies to exceptions on January 4, 2012. The record in this case consists of 814 pages of testimony and 61 exhibits admitted into evidence.¹

I&M's Application

I&M stated that Units 1 and 2 at the Donald C. Cook Nuclear Power Plant (Cook Plant) in Bridgman, Michigan were placed in service in 1975 and 1978 respectively and that the Nuclear Regulatory Commission (NRC) recently extended the operating licenses for the two units until 2034 and 2037. I&M claimed that significant capital investments (collectively referred to as the Life Cycle Management (LCM) project) in the Cook Plant are required so that the benefits of the extended licenses may be fully realized.

According to I&M, the LCM project is necessary “to: (1) optimize the operation, maintenance, and service life of systems, structures and components; (2) maintain an acceptable level of performance and safety; and (3) maximize return on investment over the service life of the plant.” I&M’s application, ¶ 7. I&M stated that the LCM project is comprised of 117 subprojects, with a total cost of \$1.169 billion, scheduled to be completed by 2018. I&M also claimed that its integrated resource plan (IRP) supports the LCM project as the least-cost alternative to assure safe and reliable power in its service territory for the foreseeable future.

¹ Some of the testimony and exhibits in this proceeding are designated confidential pursuant to the protective order.

I&M requested that the Commission find that the energy and capacity supplied by the Cook Plant is needed and that the LCM is the most reasonable and prudent means to continue to supply this power in the company's service territory. I&M also requested that the Commission find that the jurisdictional capital and financing costs associated with the LCM project will be recoverable from Michigan customers. Finally, I&M requested that the Commission grant a CON for the LCM and that the Commission further grant specific accounting and deferred accounting authority requested for related construction work in progress (CWIP), allowance for funds used during construction (AFUDC), and post-in service costs.

Positions of the Parties

Paul Chodak III, I&M's Chief Operating Officer, provided an overview of the company's case. Mr. Chodak testified that the Cook Plant plays a significant role in providing safe and reliable electric service to I&M's customers in Michigan and Indiana. According to Mr. Chodak, the Cook Plant produces 2100 megawatts (MW) of baseload generation, approximately 20% of which supplies retail and wholesale customers in Michigan. Mr. Chodak added that power from the Cook Plant is extremely economical and that the plant contributes substantially to I&M's low-carbon generation portfolio. 3 Tr 89.

Mr. Chodak testified that in order for I&M to continue to supply safe, reliable, and economic electric power to its customers by continuing to operate the Cook Plant through 2034, it is necessary to make LCM investments in the facility. Mr. Chodak added that if the LCM project is not undertaken, the Cook Plant will deteriorate, leading to more frequent outages and the need for higher cost replacement power. 3 Tr 93-94.

Mr. Chodak noted that I&M evaluated the potential for including a power uprate of 400 MW at the Cook Plant, and it determined that while additional capacity is feasible, it is not necessary at

this time. Nevertheless, the company decided that upsizing certain components as part of the LCM project, in anticipation of a possible uprating in the future, was a reasonable strategy.

3 Tr 92.

Mr. Chodak testified that in addition to the benefits of continued reliable power from the Cook Plant, the LCM project will provide employment opportunities in Michigan and Indiana and will provide benefits in terms of customer service, environmental stewardship, and operational performance. 3 Tr 93-94.

Mr. Chodak stated that based on the analyses performed so far, the LCM project is estimated to cost \$1.169 billion dollars. While this is a significant amount, Mr. Chodak opined that the LCM project will result in more long-term savings for customers than alternative approaches to providing electric capacity and energy. Mr. Chodak added that the capital spending for the LCM project is substantially more than the typical spending at the Cook Plant. See, Exhibit I&M-1. Mr. Chodak explained that it was for these reasons that I&M is requesting approval of LCM project costs under Section 6s rather than through periodic rate cases. 3 Tr 95-96.

Mr. Chodak testified that I&M is committed to transparency in the implementation of the LCM project and is proposing to submit construction review filings to the Staff and other stakeholders every six months. In addition, Mr. Chodak indicated that the company is willing to retain a third-party expert to monitor and report findings to the Commission and other stakeholders. 3 Tr 96-97.

John Torpey, Director-Integrated Resource Planning for American Electric Power (AEP) Service Corporation, testified concerning I&M's IRP. Mr. Torpey explained that AEP and I&M prepare an IRP for submission to the Indiana Utility Regulatory Commission (IURC) every two years and that the company's most current IRP, covering a 20-year planning period, was submitted

to the IURC on November 1, 2011. Mr. Torpey testified that I&M's report showed that the capacity of I&M's existing resources is 5,546 MW; however, in light of anticipated environmental regulations, I&M anticipates retiring several of its coal-fired units. 4 Tr 549.

Mr. Torpey testified that in its IRP analysis, I&M included the Cook Plant as a generation resource available until the renewed licenses expire in 2034 and 2037. Mr. Torpey added that the LCM costs are likewise included in the analysis because the capacity supplied by the Cook Plant can only be assumed if the LCM project is undertaken. 4 Tr 550. Mr. Torpey testified that screening curves for the Cook Plant and other potential supply side resources are presented in Exhibit I&M-4. According to Mr. Torpey, Exhibit I&M-4 shows that the existing Cook Plant, including the LCM project, is the preferable resource at capacity factors over 20%, thus demonstrating that the continued operation of the Cook Plant, including LCM costs, is the least-cost option. 4 Tr 551-552.

Mr. Torpey testified that the specific modeling tool used in developing the IRP is the Strategist® optimization model.² Strategist® allows the user to input various assumptions concerning, among other things, resource characteristics, operating parameters, fuel and emissions allowance prices, and reliability constraints. 4 Tr 553. Mr. Torpey stated that I&M used Strategist® to compute the cumulative net present value (NPV) of investing in the Cook Plant compared to retiring and replacing the nuclear plant with some mix of natural gas facilities. Mr. Torpey noted that the result of I&M's analyses (including sensitivity analysis) very clearly showed that the present value revenue requirements for keeping the Cook Plant in operation, including the LCM costs, were superior to retirement. Specifically, Mr. Torpey testified that the

² "Strategist® determines the least-cost resource mix for the generation system being assessed. The solution is bounded by a user-defined set of resource technologies, commodity pricing, and prescribed sets of constraints." 4 Tr 552.

NPV of continued operation of the Cook Plant was \$3.1 to \$4.5 billion less than the lowest-cost replacement option. 4 Tr 555-556.

Mr. Torpey opined that while specific analyses were not performed concerning an uprating of the Cook Plant, the small, incremental investment in upsizing certain components “provides a relatively low cost hedge or insurance policy against increased costs for other technologies and/or future environmental restrictions or compliance costs.” 4 Tr 557.

Mr. Torpey testified that I&M will meet the renewable energy portfolio standard mandated by 2008 PA 295; MCL 460.1001 *et seq.*, but given the intermittent nature of renewables, it is not reasonable to assume that wind and solar resources could replace the significant baseload generation provided by the Cook Plant without additional back-up capacity from gas facilities. Mr. Torpey added that I&M also considered the effects of energy efficiency and load management in its IRP. 4 Tr 560-561.

Michael Carlson, Vice-President of Support Services at the Donald C. Cook Nuclear Power Plant, described the Cook Plant and its operation, noting that the plant’s performance is excellent, with a record of improvement over the past decade. 3 Tr 287-289.

Mr. Carlson testified that as part of the license renewals, I&M was required to make commitments to the NRC for managing the aging of certain plant components. 3 Tr 292-294; Exhibit I&M-15. Mr. Carlson added that in addition to the investments required by the NRC, I&M needs to maintain, refurbish, and replace components to assure that the Cook Plant can continue to operate for an additional 20 years.

Mr. Carlson explained that LCM “is a process for the timely detection and mitigation of aging effects in [systems, structures, and components] SSCs that are important to plant safety, reliability, and economics.” 3 Tr 295. According to Mr. Carlson, the 117 sub-projects that make up the LCM

are required to meet NRC standards and regulations and to ensure that the Cook Plant continues to operate in a reliable and secure manner until the end of the company's renewed operating license. Mr. Carlson noted that it would be imprudent to wait until an LCM component fails because in some cases this would necessitate an expensive, unscheduled outage. 3 Tr 296.

Mr. Carlson described the planning process I&M used to identify the subprojects to be included in the LCM project. Mr. Carlson explained that I&M used a contractor to perform a feasibility study for the possible uprating of the Cook Plant. As part of this feasibility study, the contractor provided information on necessary LCM at the Cook Plant, considering the recent license extension. After a series of additional studies, I&M developed a list of subprojects necessary for LCM at the Cook Plant. According to Mr. Carlson, "LCM sub-projects are capital projects associated with critical SSCs or regulatory functions. In addition, they are onetime replacements being done to address aging, obsolescence or unit reliability associated with the license extension." 3 Tr 299. The screening criteria used for selecting LCM subprojects is shown in Exhibit I&M-16.

Mr. Carlson testified that some of the components to be replaced as part of the LCM project are no longer available, and I&M will instead install the more technologically advanced equipment available today. Mr. Carlson highlighted the replacement of the Unit 2 low and high pressure steam turbines, which are approaching the end of their service lives and which are scheduled to be replaced with modern, more efficient equipment. As a result, Mr. Carlson testified that I&M expects a capacity gain of 50 to 60 MW resulting from the turbine replacement. 3 Tr 301-302.

Finally, Mr. Carlson testified that none of the component replacements are unique or experimental, and similar LCM projects have been implemented at nuclear plants around the country. 3 Tr 303. Mr. Carlson sponsored Exhibit I&M-17 showing the schedule for the LCM

subprojects, and he presented Table 1, which shows the estimated LCM project cash flows for 2011 through 2018. 3 Tr 306.

Paul G. Schoepf, I&M's Director of Nuclear Projects at the Cook Plant,³ provided an overview of the Cook Plant Projects Department and outlined the project engineering, management, construction, contracting, and cost controls to be used to implement the LCM project.

Mr. Schoepf testified that I&M uses a broad array of procedures for planning and execution of projects at the Cook Plant and that all projects costing more than \$500,000 are subject to several levels of review. 4 Tr 394-395, 401. Mr. Schoepf testified that there are a number of groups involved in approving projects including the Project Screening Committee, the Plant Health Committee, the Executive Project Review Committee, the Subsidiary Company Board, and the Project Design and Project Review Boards. Mr. Schoepf also explained that the Cook Project Management Group, composed of five subgroups, is tasked with managing major projects from inception to close out. 4 Tr 399-401.

Mr. Schoepf testified that the LCM project will be implemented through four phases of project management. Phase 1 involves project initiation; Phase 2 (A and B) involves project planning including preliminary and detailed engineering design, planning and procurement; Phase 3 is project implementation; and Phase 4 involves Project Closeout. 4 Tr 403. Mr. Schoepf explained that a Capital Improvement Requisition (CI)⁴ is initiated at each phase of the project, noting that at

³ Mr. Schoepf adopted the revised, prefiled direct testimony and exhibits of Terry J. Brown and filed rebuttal testimony and exhibits.

⁴ "A CI requisition represents a formal request for authorization of project expenditures, including engineering, construction and support activities, which will be financed by the Company's own capital. A CI must include the entire scope of a project/program or distinct phase with all overheads and loadings." 4 Tr 402.

Phase 1, the CI has an accuracy level of +/- 50% that decreases to +/- 10% at the beginning of Phase 3. 4 Tr 404-405.

Mr. Schoepf testified that none of the LCM subprojects are first of a kind and that the subprojects included in the LCM project are of the type that have been done before at the Cook Plant or other nuclear plants. 4 Tr 408. Mr. Schoepf explained that this allows I&M to benchmark certain projects thereby reducing the level of risk. 4 Tr 409. Mr. Schoepf also testified that most of the construction work for the various LCM subprojects is scheduled to be performed during planned outages, thus reducing the need for the Cook Plant to be offline. 4 Tr 414.

Mr. Schoepf testified that the estimated cost of the LCM project is \$1.169 billion from 2011 through 2018. 4 Tr 417. The individual cost of each of the 117 subprojects, along with the expected year of installation and projected in-service year, is contained in Confidential Exhibit I&M-22. Mr. Schoepf explained that the cost estimate for the LCM project was developed using a bottom up approach, meaning that cost estimates were developed for each subproject. Mr. Schoepf noted that while for the first phase of project execution AEP uses a management accuracy guideline of +/- 50%, this does not mean that the actual project cost is expected to vary that much. Mr. Schoepf reiterated that because many of the LCM projects are not unique, certain cost estimates have been benchmarked, some of the projects are entering Phase 2A (where the CI accuracy improves to +/- 25%), and because preliminary indications from more advanced projects indicate that costs are decreasing, the LCM project has a smaller range of accuracy. Nevertheless, Mr. Schoepf stated that because not all cost variances could be accounted for, I&M added a 20% management reserve to its overall estimate. 4 Tr 417-419.

Mr. Schoepf testified that a risk reserve has been allocated to each project based on the project phase. According to Mr. Schoepf, risk reserve is to be used for "known unknowns" such as

changes from projected inflation rates, construction delays resulting from abnormal seasonal weather, and changes in commodity prices. 4 Tr 423. In contrast, Mr. Schoepf testified that management reserve is more carefully controlled and is to be used for “unknown unknowns” such as unforeseen world events, natural disasters, or unexpected issues in project construction. 4 Tr 424. In summary, Mr. Schoepf testified that I&M has “robust project management processes” such that he “fully expect[s] that the entire LCM Project will be executed within the overall Project cost estimate and the projected schedule.” 4 Tr 427.

Scott M. Krawec, Director of Regulatory Services for I&M testified regarding the company’s requested accounting treatment for LCM project costs. Mr. Krawec stated that I&M is asking the Commission to authorize the company to defer incremental depreciation, property tax costs, and carrying costs, along with study, analysis, and development costs, until these costs are included in I&M’s retail electric rates. 3 Tr 209.

Mr. Krawec testified that I&M is proposing to include study, analysis, and development costs in Account 107, CWIP, and eventually in the cost of plant in service, for rate base and depreciation purposes. Mr. Krawec explained that if for some reason the LCM project does not go forward, the company proposes to record the study, analysis, and development costs in Account 182.2, as a regulatory asset, amortized over five years. 3 Tr 210.

Mr. Krawec testified that for the purpose of this filing, I&M requests Commission approval to defer unrecovered LCM project costs, beginning January 1, 2013, and to maintain these deferrals until the costs are recovered in rates. Mr. Krawec testified that LCM capital costs are recorded in CWIP in accordance with the Uniform System of Accounts (USoA). Mr. Krawec noted that I&M will record AFUDC on LCM subproject CWIP balances, including study, analysis and development costs, until recovery of the CWIP carrying cost is included in the company’s retail

rates. Mr. Krawec added that the AFUDC rate that I&M uses for equity is the rate established in the company's most recent rate case in Indiana, and the debt cost is set at the company's current debt cost rate. 3 Tr 211-212.

With respect to post in-service costs, Mr. Krawec testified that when a subproject is placed in service, the company will transfer the costs from CWIP to Completed Construction and then to Electric Plant in Service. Mr. Krawec stated that, subject to Commission approval, I&M will then begin recording depreciation over the remaining useful life of the Cook Plant unit where the LCM subproject was placed in service. Mr. Krawec further testified that property taxes will be assessed on LCM subprojects both when they are part of CWIP and Plant in Service. Mr. Krawec indicated that property taxes will be included in depreciable plant balance when the property is placed in service, and incremental property taxes assessed on LCM property in service will be charged to Tax Expense, Account 408 and will be recovered through Michigan retail rates. 3 Tr 212-214. Finally, Mr. Krawec testified that deferred accounting is consistent with Generally Accepted Accounting Practices and with the USoA and is reasonable and necessary in the case of a significant investment like the LCM project. 3 Tr 214-215.

Steven E. Kulesia, Manager of the Generation and Certificate of Need Section of the Commission's Electric Reliability Division, testified that the Staff reviewed I&M's IRP and determined that the plan complied with Section 6s(11); the analysis in the IRP demonstrated a need for the power supplied by the Cook plant; and that the LCM project was the most reasonable and prudent means of meeting I&M's power needs compared to other resource options. 4 Tr 364. Mr. Kulesia noted that Section 6s(4)(e), which requires, to the extent practicable, the use of a workforce comprised of Michigan residents, does not apply given the location of the plant in a county bordering Indiana. 4 Tr 365.

With respect to I&M's compliance with Section 6s(7), Mr. Kulesia testified that the Staff agreed with Mr. Chodak's proposal to provide the Commission with reports every six months and that such reporting would comply with the statutory requirements. Mr. Kulesia added that in addition to the information delineated in Section 6s(7), the Staff also expects, at minimum, that "I&M will provide sufficient detail regarding the status of each project, describe any changes in timing and/or scope, the money expended on each project, etc." 4 Tr 367.

Lisa M. Kindschy, a Public Utilities Engineering Specialist in the Act 304 and Sales Forecasting section of the Commission's Regulated Energy Division, testified that the Staff reviewed the scope and cost of the LCM project and individual subprojects, along with the DC Cook Phase 1 Report prepared by Shaw (Shaw Report, Exhibit I&M-25), and other reports, bids, and independent evaluations. 5 Tr 767-768. Ms. Kindschy testified that it was the Staff's view that I&M has sufficient expertise to develop a cost estimate for a project the size of the LCM project. 5 Tr 768.

Ms. Kindschy testified that the Staff made two adjustments to I&M's \$1.169 billion cost estimate. The first adjustment was to remove LCM project costs for the third and fourth quarters of 2011 and for all of 2012. Ms. Kindschy explained that because Section 6s applies to a six-year time frame the Staff only included costs for 2013 through 2018 in the CON. 5 Tr 768-769.

Ms. Kindschy testified that the second adjustment removed the management reserve contingency from the amount I&M requested for the CON. Ms. Kindschy observed that the company's testimony indicates that there is a risk reserve contingency built into each subproject, along with a management reserve contingency that is over and above the risk reserve. In addition, Ms. Kindschy testified that, in response to an audit request, I&M indicated that the projects included in Shaw Report also included subproject contingencies in the range of 15% to 25%.

Ms. Kindschy opined that it would be unreasonable to approve the management reserve in addition to the contingencies already built into the individual subproject budgets. 5 Tr 769-770.

Ms. Kindschy added that the costs to be covered by the management reserve are quite speculative, and I&M does not know if these funds will need to be spent or on what they might be spent.

Nevertheless, the company is requesting preapproval of recovery of the management reserve in this case. According to Ms. Kindschy, the Staff believes that it is appropriate for the Commission to review these unknown costs, if and when they are incurred, so that ratepayers have some assurance that LCM project costs are being reasonably controlled. Ms. Kindschy added that Section 6s(9) has an allowance for costs up to 110% of the CON amount if the Commission finds these excess costs to be reasonable and prudent. Ms. Kindschy pointed out that adding the statutory 10% to the 20% management reserve results in a 30% contingency over and above the 15% to 25% already included in risk reserve. 5 Tr 770. Ms. Kindschy explained that the Staff's removal of the management reserve does not imply that reasonably and prudently incurred costs above the CON amount are not recoverable. 5Tr 770-771.

Ms. Kindschy summarized that the Staff was recommending that the Commission approval of a CON in the amount of \$773,611,000 for the 117 subprojects shown on Exhibit I&M-22.

Ms. Kindschy further testified that the Staff believes that as the subprojects become used and useful and are included in rate base, the Commission should evaluate each subproject to determine if any are substantially over budget. 5 Tr 771-772.

In rebuttal, Mr. Shoenpf testified that the inclusion of a management reserve is based on accepted industry practices and is reasonable and prudent. According to Mr. Shoenpf, "Management reserve is a real project cost that is routinely forecast in construction projects and ultimately held for necessary cost growth due to unknown unknowns within the project (or

sub-projects for the LCM). Unknown unknowns occur when internal or external factors impact the project that a project manager cannot reasonably predict or estimate.” 4 Tr 430. Mr. Shoepf added that both risk reserve and management reserve were included in the LCM project cost because these two reserves have significantly different uses. Mr. Shoepf pointed out that the risk reserve is directed by the project manager whereas management reserve funds are highly controlled and can only be released with the approval of Director of Nuclear Projects, the Chief Nuclear Officer, and the President of I&M. Mr. Shoepf testified that this level of control is necessary to “ensure the funds are not spent on scope growth or known unknowns that should reasonably be controlled by the Project Manager.” 4 Tr 431.

Kevin S. Krause, an auditor in the Revenue Requirements Section of the Commission’s Financial Analysis and Audit Division, testified that the Staff recommended approval of most of I&M’s accounting requests. Nevertheless, Mr. Krause testified that the incremental property tax treatment requested by the company should be adjusted so that the deferred property taxes are recorded with appropriate accruals for property tax expense. Mr. Krause explained that because property tax is determined for the following year, based on the balance of plant in service at the end of the current year, the recording of deferred property tax for any item placed in service during a given year should not begin until January 1 of the year after the project goes in service.

3 Tr 189.

In addition, Mr. Krause testified that the Staff disagreed with the company’s proposal to simply depreciate LCM plant over the remaining life of the unit in which the component is installed. According to Mr. Krause, such treatment fails to take into account net salvage and rebalancing of the depreciation reserve. Mr. Krause therefore recommended that I&M calculate

deferred depreciation expense in accordance with the nuclear depreciation rates authorized in Case No. U-16801, as updated by subsequent depreciation cases. 3 Tr 190.

Mr. Krause testified that the Staff did not oppose I&M's request to defer carrying costs, noting that the request nevertheless requires Commission approval. Mr. Krause added that if I&M files a rate case using a projected test year, then appropriate amounts of CWIP, Plant in Service, AFUDC, depreciation expense, and property tax expense would be projected in the case. Mr. Krause testified that in that circumstance, the recording of deferrals would not be necessary for the period of time covered by the rate case application which uses a projected test period. Mr. Krause testified that the Staff believes that the accounting authorizations requested by I&M are reasonable, given the size of the LCM project, and should allow the company to access credit and avoid earnings erosion. Finally, Mr. Krause testified that the Commission should make clear that the accounting approvals granted in this case are specific to this CON and may not be granted in future CON proceedings. 3Tr 191-193.

On rebuttal, Mr. Krawec testified that he agreed with the Staff's proposed adjustment for incremental property tax and with Mr. Krause's explanation that the recording of deferrals was not necessary in a rate case application using a projected test year. 3 Tr 224-225. Mr. Krawec disagreed with the Staff's proposed treatment of depreciation expense for the LCM project. Mr. Krawec noted that the nuclear depreciation rates approved in Case No. U-16801 were developed using December 31, 2010 plant balances, when the remaining service life of the plant was 25 years. Mr. Krawec pointed out that some of the LCM components may only have a remaining service life of 17 years at the time they are installed. Mr. Krawec therefore recommended that LCM components be depreciated over the remaining life of the plant until these components can be incorporated into a new depreciation study. 3 Tr 223-224.

John Hosmer, P.E., President of Hosmer Consulting LLC, testified on behalf of the Attorney General. Mr. Hosmer stated that he reviewed I&M's application and submitted several discovery questions concerning the LCM subprojects. According to Mr. Hosmer, I&M's discovery responses were general and did not include sufficient specific information justifying the \$1.169 billion investment in the LCM project. 5 Tr 711.

Mr. Hosmer testified that the options for addressing LCM range from simply changing maintenance procedures, to refurbishment, to component replacement, which Mr. Hosmer characterized as a last resort. 5 Tr 710. In developing a strategy for LCM, the life cycle costs of these options should be assessed to come to an optimal decision. Mr. Hosmer opined that neither I&M's application nor its discovery responses indicated that the company undertook a comprehensive and technical assessment of LCM with respect to root cause analysis, failure basis, or comparisons of the Cook Plant components to industry standards. 5 Tr 710-711.

Mr. Hosmer also raised concerns about the LCM subprojects that are being upsized to accommodate a potential future uprating. According to Mr. Hosmer, the additional costs associated with the uprating are not justified because any uprating would occur after 2020, when only 10 to 12 years are left on the licenses. Mr. Hosmer opined that at that point, an uprating would be unlikely. 5 Tr 712-716.

Mr. Hosmer testified that certain other projects that I&M included as LCM are misclassified and that the CON should be limited to LCM only. Mr. Hosmer emphasized the Unit 2 turbine replacement, noting that while I&M claims that the turbine is approaching the end of its service life the company provided no service life comparisons or other documentation to justify the need for this replacement. 5 Tr 717-718. Mr. Hosmer added that several other projects, totaling \$10 million in cost, were reclassified and inappropriately added to the LCM project. Mr. Hosmer

claimed that these subprojects should not be included as part of the LCM project.

Mr. Hosmer testified that I&M provided no justification for the time frame for implementing the LCM project. According to Mr. Hosmer, the work proposed could be accomplished over a longer time period, an approach that would be more likely to optimize site performance.

Mr. Hosmer testified that based on I&M's proposed schedule, the company will need to complete ten major modifications during each outage. Mr. Hosmer stated that given I&M's recent experience at the Cook Plant, it is unlikely that all of these projects can be implemented during the scheduled outages without potential overruns in both cost and schedule. 5 Tr 720-722.

Mr. Hosmer therefore recommended that the Commission, "warn I&M that the Commission may disallow recovery of any cost overruns resulting from extended outages arising from current ambitious plans to perform plant modification as scheduled." 5 Tr 722.

With respect to issuance of the CON, Mr. Hosmer recommended that the Commission reject I&M's request because the company failed to show that the LCM project is the most reasonable and prudent means to achieve LCM at the Cook Plant. In the alternative, Mr. Hosmer recommended that the Commission limit the CON amount to \$848 million. 5 Tr 723.

In rebuttal, Mr. Schoepf claimed that the replacement of the Unit 2 turbine as part of the LCM project was fully justified by the company. Mr. Schoepf pointed to the Shaw Report that documents the extensive wear on the turbine which, coupled with the age of the equipment, justifies its replacement. Regarding plant components that I&M proposes to upsize, Mr. Schoepf reiterated that if I&M waits to upsize this equipment in the event of a future plant uprating, the parts will have to be replaced again at a much higher cost. Finally, with respect to Mr. Hosmer's claim that I&M lacks the capacity to complete the LCM project within the projected timeframe, Mr. Schoepf testified that the company provided substantial evidence that it has the experience and

expertise to accomplish the LCM project within the time frame proposed. Mr. Schoepf pointed to I&M's performance in addressing the catastrophic failure of the Unit 1 turbine, a response that has been positively recognized industry-wide.

John G. Athas, a Principal Consultant and Treasurer of La Capra Associates, Inc. testified on behalf of MEC on issues concerning the company's IRP. Mr. Athas stated that he had several concerns about the company's IRP; specifically, that I&M failed to address fuel diversification as a goal, noting that the company's current generating fleet is 90% coal and nuclear. Mr. Athas also testified that I&M's originally filed IRP relied on outdated natural gas prices, whereas more recent forecasts project much lower gas costs.

Mr. Athas testified that he would like to see I&M perform more sensitivity analysis with respect to demand side management (DSM), energy efficiency, and load management to reduce the company's load and capacity needs. According to Mr. Athas, I&M's IRP shows that the company may need to purchase significant power from the market from 2013 through 2024 and may need to build a new generating plant in 2025. Mr. Athas opined that the company should have further explored whether demand-side resources could offset some of these costs. Mr. Athas added that I&M's IRP does not clarify at what point energy efficiency and DSM cease to be cost effective. Mr. Athas testified that I&M only assumed that it would undertake energy efficiency and DSM up to the statutory requirement, rather than exceeding the statutory mandates.

Mr. Athas testified that I&M gave minimal consideration to renewable energy in its IRP, claiming that it was unreasonable to replace baseload generation with intermittent supply like solar and wind. Mr. Athas opined that this is generally unacceptable in an IRP and that I&M should have included a more rigorous analysis of the inclusion of renewables in its modeling.

Mr. Athas testified that while I&M undertook some sensitivity analysis in its IRP, most notably considering a low cost natural gas scenario and a high carbon tax sensitivity, I&M failed to include an analysis of potential cost overruns in the LCM project. Mr. Athas stated that while the benefits of the LCM appear to be significant, there should still be some attempt to quantify the risk of higher-than-projected costs for the project.

In response, Mr. Torpey contended that I&M provided a comprehensive IRP and that many of the concerns raised by Mr. Athas were either addressed by the company in response to discovery requests or would not change the outcome of its analysis; namely that the LCM project is the optimal means of assuring future capacity at the least cost. Mr. Torpey nevertheless noted that some of the issues raised by Mr. Athas have merit in the context of general resource planning, but these issues have limited relevance in this specific proceeding.

James T. Selecky, Managing Principal of Brubaker and Associates, testified on behalf of ABATE. Mr. Selecky observed that although Mr. Chodak testified that I&M was requesting a rate adjustment mechanism (i.e. a tracker), Mr. Krawec requested deferred accounting with special ratemaking treatment. According to Mr. Selecky, these are two conflicting positions and the Commission should reject both.

Mr. Selecky testified that although I&M made reference to the need to mitigate earnings erosion through deferred accounting, the company failed to provide any detail to demonstrate the potential for actual harm. Further, Mr. Selecky testified that I&M's proposals shift regulatory risk from the company to ratepayers. Mr. Selecky added that the rate recovery mechanism I&M proposes circumvents the traditional ratemaking paradigm by singling out certain costs for guaranteed recovery without taking other costs, which might decrease as a result of the investment, into account. Mr. Selecky opined the enactment of 2008 PA 286, which allows for annual rate

cases, projected test years, and self-implemented rate increases, has eliminated the need for trackers and deferred accounting.

In rebuttal, Mr. Chodak testified that I&M is not requesting a tracker and that his reference to a periodic rate adjustment mechanism was meant to indicate that the company will be filing periodic rate cases.

Some additional issues were raised in the parties' briefs. The Attorney General claimed that the LCM project does not qualify for a CON under the plain language of Section 6s(1). According to the Attorney General, the LCM project is merely an enumeration of subprojects that do not serve a "singular" purpose, in the sense that the subprojects are usual or ordinary and not exceptional.

In response, the Staff argued that the Attorney General construed the statute far too narrowly and that the phrase "such as" is a term of enlargement and that the term "singular" means more than just "exceptional" or "different."

The Attorney General also posited that if the Commission determines that the LCM project qualifies for a CON under Section 6s(1), then the Commission is limited to granting or denying the CON under Section 6s(4). The Attorney General argued that because the statute contains no clear, unmistakable authority granting the Commission the power to modify the filing, the Commission may not do so.

The Staff disagreed and pointed out that reading Section 6s as a whole it is clear that the Commission has the authority to modify the CON request. The Staff highlighted Section 6s(5), which allows the Commission to consider cost information, and Section 6s(6), which provides that the Commission specify the costs approved by the CON, as support for its position. The Staff

claimed that adopting the Attorney General's view of the statute would render these sections a nullity.

With respect to I&M's accounting requests, the Attorney General argued that the company failed to show by a preponderance of the evidence that including its carrying costs would result in just and reasonable rates. Further, the Attorney General asserted that the Commission lacks subject matter jurisdiction to adjust I&M's rates in accordance with the company's deferred accounting request. Specifically, the Attorney General observed that Financial Accounting Standards Board Standard No. 980-340-25-1a requires that to book a deferred asset, a regulated provider must obtain reasonable assurance of future recovery from the Commission. As such, the Attorney General claimed that I&M's deferred accounting request is tantamount to a request for an illegal rate adjustment mechanism.

In response, I&M argued that the Attorney General and ABATE are mistaken and that the company at no point requested a rate adjustment mechanism. Further, I&M argued that timely recovery of costs is essential in a project the size of the LCM project; thus, deferred accounting is appropriate.

Proposal for Decision

The ALJ found that, contrary to the claims made by the Attorney General and ABATE, the LCM qualifies for a CON under Section 6s. The ALJ agreed with I&M and the Staff that the LCM project comports with the language under Section 6s(1) as "a significant investment in an electric generation facility" that "includes a group of investments reasonably planned to be made . . . for a singular purpose[.]" The ALJ found that the Attorney General's interpretation of the statute was too narrow and that Section 6s was intended to cover projects necessary to extend the life of a nuclear generation facility, as is the intent of the LCM project.

The ALJ rejected I&M's claim that investments made in the LCM in 2011 and 2012 should be included as part of the costs covered by the CON. The ALJ agreed with the Staff, the Attorney General, and ABATE that the language of Section 6s(1) is clear and unambiguous that the CON applies to a continuous six-year period when investments are made, not when plant is placed in service. The ALJ agreed with the Staff that I&M's interpretation would result in a situation where the Commission is pre-approving investments that have already been made.

The ALJ also rejected I&M's claim that the six-year time frame should only cover scheduled outage periods when the majority of LCM work is to be performed. The ALJ noted that such an application of the statute would render the time limit virtually meaningless. Thus, the ALJ recommended that the Commission adopt the Staff's proposal and approve only investments made from 2013-2018 for the CON.

The ALJ agreed with the Staff that Section 6s provides the Commission with the requisite authority to amend I&M's filing. However, he disagreed with the Staff's claim that Section 6s(5) would be rendered meaningless if the Attorney General and ABATE's interpretation of Section 6s(4) were adopted. According to the ALJ, the Commission could take costs and other information under consideration, as provided in Section 6s(5), in deciding whether to grant a CON under Section 6s(4). On the other hand, the ALJ agreed that the language in Section 6s(6), requiring the Commission to specify the costs covered by the CON, clearly provides authority for the Commission to modify the filing. The ALJ added that there is additional support under Section 6s(8), which provides that if the Commission denies any of the relief requested, the provider may withdraw the application and refile, or it may proceed with the investment without a CON.

With respect to the merits of I&M's application, the ALJ found that the company had presented sufficient evidence demonstrating the need for the LCM project to assure that energy and capacity from the Cook Plant will be available now and in the future, thus complying with Section 6s(4)(a). Further, the ALJ noted that no party contested that I&M's request complies with Sections 6s(4)(b) and (e).⁵ The ALJ added that no party took issue with I&M's offer to file semi-annual reports under Section 6s(7).

The ALJ found persuasive the reasoning set forth by the Staff and the Attorney General regarding the disallowance of the \$220 million management reserve included in I&M's cost estimate. The ALJ observed that the very fact that the statute precludes the Commission from disallowing any costs covered by a CON:

strongly suggests that the Commission should be very cautious in approving contingency amounts in the CON setting. The purpose of Section 6s is to provide an electric utility with some assurance of recovery of the costs of its investments in projects permitted by the statute; it is not to provide an electric utility the opportunity for a potential windfall, at the expense of ratepayers, of allowing extra and unneeded spending if the utility is able to bring a project in under budget.

PFD, p. 39.

The ALJ further determined that I&M failed to meet its burden of proof concerning the reasonableness of the management reserve. The ALJ agreed with the Staff that the only evidence that the management reserve is the sole source of contingency funds came late in the process, in cross examination, without any documentary support. In addition, the ALJ found that the record was still not clear regarding whether or not there were multiple levels of contingency in the project, as the Staff and the company dispute. In support of this finding, the ALJ quoted testimony

⁵ MCL 460.6s(4)(b) requires a showing that the proposed investment will comply with state and federal environmental statutes and regulations. MCL 460.6s(4)(e) requires the use of a Michigan work force "to the extent practicable." This provision does not apply to investments made in a county that borders another state, as is the case here.

from Mr. Shoepf that showed that a risk reserve was built into several projects in addition to the management reserve.

The ALJ disagreed with the Attorney General's contention that costs for certain projects should be removed from the LCM because these projects are more closely related to a capacity uprating than with continued operation of the Cook Plant. The ALJ determined that the sub projects challenged by the Attorney General meet the requirements of Section 6s(4)(a).

The ALJ found that the LCM project meets the requirements of Section 6s(4)(d), as the most reasonable means to meet I&M's future power needs, as supported by the company's IRP. The ALJ recommended that the Commission accept the IRP and added that the issues raised by the MEC concerning the appropriate content of an IRP should be left to the Commission to decide.

With respect to the accounting authority requested by I&M, the ALJ found that the provisions of Section 6s(12) are clear and undisputed. Any additional relief may be determined in I&M's next general rate case. The ALJ also agreed with the Staff's position that there should be ongoing prudence reviews of the LCM project components as each sub-project is phased into rate base. Finally, the ALJ agreed with the Staff's position that, pursuant to Section 6s(6), the specific costs approved for the CON should be for the 117 subprojects identified in I&M's application.

Exceptions and Replies

I&M takes exception to the ALJ's finding that the \$220 million management reserve should be excluded from the CON. I&M claims that the ALJ's reasoning "harken[s] back to a different day in utility regulation" and that today, "in order to finance major construction projects, utilities need to assure lenders and investors of cost recovery." I&M's exceptions, p. 1. I&M contends that Section 6s does not permit the Commission to exclude reasonable and prudent costs, including contingency costs. According to I&M if the ALJ's logic were to apply in future cases, CONs

would consistently be issued approving amounts that are less than the total project cost, thus rendering the intent of Section 6s moot.

I&M argues that the clear record evidence shows that that there is no dispute that some level of contingency should be included in the CON and that the management reserve is the only source of contingency funds in the request. I&M urges the Commission to reject the Staff's claim, adopted by the ALJ, that the LCM project includes multiple levels of contingency. I&M further argues that it is incorrect to presume that the 10% allowance in Section 6s(9) also serves as a source of contingency funds. I&M claims that the only advantage to Section 6s(9) is that any cost overrun of 10% or less is presumed reasonable. In sum, I&M argues that adopting the CON amount recommended by the ALJ virtually assures that the LCM will be underfunded and that a second prudency review will be required.

In a related exception, I&M asserts that the ALJ's recommendation to exclude the management reserve amounts from the approved CON was not based on substantial and material evidence. According to I&M, the PFD "ignores the testimony of the only witnesses who are qualified by experience and education to opine regarding management reserve, and instead embraced the testimony of witnesses with no actual experience in constructing nuclear power plants." I&M's exceptions, p. 25. I&M reiterates the education and experience of Mr. Chodak and Mr. Schoepf and characterizes Ms. Kindschy's testimony as "closer to 'invalid assertions of [an] unqualified witness' – the very type of testimony about which the Supreme Court has warned. *Gilbert*, 470 Mich at 789. Such testimony cannot serve as 'the competent, material and substantial

evidence’ as required by MCL § 24.285.” I&M’s exceptions, p. 26, apparently quoting *Gilbert v Daimler Chrysler Corp*, 470 Mich 749; 685 NW 2d 391 (2004).⁶

In response, the Staff claims that neither the Staff nor the ALJ take issue with the policies embodied by Section 6s, noting that the PFD is consistent with the requirements of the statute. Nevertheless, the Staff points out that if the Legislature had intended that the Commission approve any amount proposed by a utility in a CON filing, it would not also have required a contested case proceeding.

The Staff takes issue with I&M’s claim that, according to the ALJ, contingency costs should not be included as part of a CON. The Staff points out that this is a mischaracterization of the ALJ’s finding, which was simply that the Commission should be cautious in approving contingency amounts, not that the Commission lacks authority to approve a reasonable amount of contingency funds in a CON. The Staff adds that while no party disputes I&M’s claim that the LCM project is the least-cost alternative for future capacity needs this does not mean that the project should not be undertaken as prudently and economically as possible.

In response to I&M’s allegation that the Staff is mistaken about the existence of multiple levels of contingency in the LCM, the Staff points out that Mr. Chodak amended his rebuttal testimony at the evidentiary hearing, a point when no party had the opportunity to examine or rebut Mr. Chodak’s statement that the management reserve was the only source of contingency in the project. The Staff adds that Mr. Chodak’s testimony was unaccompanied by any exhibits or other documentary support. With respect to I&M’s argument that there is no support for the Staff’s claim that the cost estimate includes multiple layers of contingency, the Staff replies that I&M is attempting to shift the burden of proof to the Staff or other parties to the case.

⁶ The purported quote concerning the “invalid assertions of [an] unqualified witness” does not actually appear in *Gilbert* on page 789, or at any other point in that opinion.

The Staff argues that the PFD was based on substantial, material, and competent evidence on the record and that the Staff's and intervenors' witnesses were fully qualified to testify regarding the matters contained in I&M's application. The Staff characterizes I&M's assertion that only the company's witnesses were sufficiently competent to testify regarding the management reserve as "an affront, not only to the many qualified and competent witnesses in this case, but to the administrative process in general." Staff's replies to exceptions, p. 9. The Staff contends that rather than arriving at his recommendation by conjecture or surmise, as I&M claims, the ALJ simply applied the preponderance of the evidence standard.

I&M takes exception to the ALJ's recommendation that individual subprojects be reviewed as each becomes part of rate base. I&M claims that it is not requesting pre-approval of the cost for each individual subproject, but rather is requesting that the entire LCM project cost be reviewed and approved *ex ante*. I&M argues that the series of "mini" prudence reviews that the Staff recommends would be inefficient and a poor regulatory paradigm.

In response, the Staff again points out that because the LCM project consists of a series of 117 subprojects that will be coming into service over six years, it will be important to review each subproject to make sure that none are significantly over budget.

Finally, I&M takes issue with the ALJ's recommendation to defer decisions on the company's accounting requests to a future rate proceeding. I&M notes that while Section 6s addresses certain accounting issues, the additional accounting requests were made pursuant to the Commission's broad ratemaking authority and are appropriately addressed here.

The Attorney General and ABATE contend that the ALJ erred in finding that the LCM project qualifies for a CON under Section 6s. The Attorney General reiterates his argument that, when read in context, the phrase "such as increasing the capacity of an existing electric generation plant"

is one of limitation, and not enlargement as the ALJ found. The Attorney General points out that the examples contained in the statute that illustrate the types of projects eligible for a CON all involve increasing or expanding service (and therefore benefits) to customers. The Attorney General argues that the purpose of the LCM project is simply to continue service, with no additional customer benefit. The Attorney General and ABATE also claim that the LCM is simply an inventory of ordinary capital projects necessary for maintaining a nuclear plant, and thus do not meet the common definition of “singular.”

ABATE similarly argues that the intent of Section 6s is to provide pre-approval for extraordinary investments that increase power supply, and because Section 6s is an exception to Michigan law, it should be interpreted narrowly. ABATE posits that the ALJ’s overly broad determination that the LCM project qualifies for a CON would allow any utility to file an application under Section 6s whenever projected routine capital expenditures over 6 years exceed the \$500,000 threshold set by the statute. According to ABATE, granting the CON in this case would set an extremely poor precedent.

In response, the Staff and I&M argue that the Attorney General and ABATE mistakenly assume that because the LCM project was broken into 117 subprojects for analysis purposes, it somehow does not qualify for a CON. I&M argues that because the LCM project as a whole will allow the Cook Plant to continue operations through the extended license period, this is indeed the type of “singular purpose” envisioned by Section 6s. In response to ABATE’s argument that Section 6s should be narrowly applied, I&M contends that ABATE’s legal authority does not actually support its argument.

The Attorney General further argues that the Commission’s authority under Section 6s extends only to granting or denying the CON pursuant to Section 6s(4), thus the Commission cannot

modify the company's request as the PFD recommends. The Attorney General asserts that the ALJ erred in finding that this limited construction of the statute would negate the provisions contained in other sections of the statute. The Attorney General contends that there are other statutes wherein the Commission is clearly authorized to modify an application, but Section 6s does not contain clear and unequivocal language allowing for amendment, and the Commission cannot use other parts of Section 6s to find this authority by implication.

I&M and the Staff respond that the ALJ's analysis of the statute was correct and that reading the statute as a whole clearly provides the Commission with authority to approve specific costs within the CON application.

Finally, the Attorney General argues that I&M did not provide sufficient evidence to show that subprojects that were not part of LCM, and certain projects that were upsized for a possible future uprating, should be included as part of the CON or are necessary for the continued operation of the Cook Plant. The Attorney General pointed to the testimony by Mr. Hosmer where the witness explained that there are important distinctions between LCM investments and other projects, and he recommended removing a total of \$262 million in costs associated with non-LCM projects and plant uprating.

I&M replies that Mr. Hosmer's evidence was clearly rebutted, as the ALJ recognized, and the preponderance of the evidence demonstrates that the Attorney General's position should be unavailing.

Discussion

In this case of first impression under MCL 460.6s, the Commission is being asked to evaluate a proposed, significant investment in an existing, recently relicensed, nuclear power plant so that,

according to the company, the plant can meet the conditions of relicensing and continue to operate in a safe and reliable manner for the next 20 years or more.

Legal Standards for Issuance of a Certificate of Need

Section 6s(1) of 2008 PA 286, MCL 460.6s provides:

An electric utility that proposes to construct an electric generation facility, make a significant investment in an existing electric generation facility, purchase an existing electric generation facility, or enter into a power purchase agreement for the purchase of electric capacity for a period of 6 years or longer may submit an application to the commission seeking a certificate of necessity for that construction, investment, or purchase if that construction, investment, or purchase costs \$500,000,000.00 or more and a portion of the costs would be allocable to retail customers in this state. A significant investment in an electric generation facility includes a group of investments reasonably planned to be made over a multiple year period not to exceed 6 years for a singular purpose such as increasing the capacity of an existing electric generation plant. The commission shall not issue a certificate of necessity under this section for any environmental upgrades to existing electric generation facilities or for a renewable energy system.

The Commission finds that an LCM project, for the singular purpose of assuring that safe and reliable power can continue to be produced from a nuclear generation facility until the end of its extended license, comports with the requirements of Section 6s(1) and thus is eligible for a CON. The Commission therefore rejects the exceptions filed by the Attorney General and ABATE. The Commission agrees with the company, the Staff, and the ALJ that the phrase “such as” is a means of providing an example of a “singular purpose” and is not meant to limit the types of projects that meet the criteria of a “singular purpose” to only those that increase capacity.

For the reasons stated in the PFD, the Commission also rejects the Attorney General’s argument that the Commission’s authority under Section 6s is limited to approving or disapproving a CON application as filed by the provider. The Commission agrees with the ALJ’s comprehensive analysis and his conclusion that, when read *in pari materia*, the Commission is

permitted, indeed is required, to limit a CON to reasonable and prudent costs if the record shows that costs are excessive.

As discussed previously, there is no dispute that Sections 6s(4)(b) and 6s(4)(e) are either inapplicable or have been satisfied. Other legal standards and issues are addressed, as required, *seriatim*.

Timing Issues and Costs Included in I&M's Certificate of Need Application

I&M's application requested approval of a CON in the amount of \$1.169 billion for LCM expenditures beginning in the third quarter of 2011 and continuing through 2018. Subsequently, the company agreed with the Staff that 2011 expenditures should be removed and updated its requested amount to \$1.129 billion. The Staff, the Attorney General, and ABATE argued that only costs from 2013 through 2018 should be included in the CON, in conformance with the 6-year statutory time frame contained in Section 6s(1). The ALJ agreed with the Staff and the intervenors that the CON should only preapprove investments beginning in 2013 and ending in 2018, resulting in an additional reduction of \$142 million for 2012 LCM project investments.⁷ There were no exceptions filed to this recommendation.⁸ The Commission therefore adopts the ALJ's recommendation to include costs from 2013 through 2018 in the CON. This results in an adjusted CON amount of \$773.6 million, not including management reserve.

The Attorney General argues that costs associated with the Unit 2 turbine replacement, along with incremental costs to upsize certain components and costs associated with projects he claims are not required for LCM, should be removed from the CON amount. The Staff and the company

⁷ Because a portion of the management reserve was assigned to 2012 expenditures, the removal of these costs reduces the management reserve amount from \$220 million to \$213 million.

⁸ Although I&M's exceptions continue to use the \$1.129 billion amount that reflects the base LCM project cost, less 2011 LCM investments, the company did not file a specific exception to the ALJ's recommendation to exclude 2012 LCM costs.

supported these challenged subprojects as reasonable and necessary, and the ALJ agreed. The Commission also finds that, based on substantial evidence on the record, that these subprojects should be covered as part of the CON. The company's rebuttal testimony demonstrated that the Unit 2 turbine is nearing the end of its life and has been showing significant signs of wear. It is reasonable therefore to undertake the replacement of this component as part of the LCM rather than wait for a catastrophic failure that could result in an extended and costly outage. In addition, the Commission agrees with I&M that the modest incremental cost associated with upsizing certain components is justified in light of the possibility that the plant may be uprated in the not-too-distant future. The Commission also agrees that the other contested subprojects meet the LCM screening criteria.

Contingency

The most contentious issue in this proceeding involves I&M's request for a \$220 million⁹ management reserve to cover what it generally characterized as "unknown unknowns." The company objects to the ALJ's agreement with the Staff's position and his recommendation to remove the management reserve from the costs approved for the CON.

At various points in its testimony, rebuttal, and exceptions, I&M posits, among other things, that: (1) risk reserve and management reserve are two different things available to address two different types of risk ("known unknowns" versus "unknown unknowns") and thus there is no duplication in contingency funding; (2) all parties agree that some level of contingency is reasonable and appropriate in a large construction project like the LCM; (3) the management

⁹ The management reserve amount is variously characterized in the company's testimony and exhibits as \$200 million, \$220 million, or "approximately 20% of the project cost." Based on a review of the record and Exhibit I&M-32, it appears that with the adjustments thus far made, the management reserve amount, likewise adjusted, totals \$214 million, or approximately 28% of the remaining \$774 million project cost.

reserve of \$220 million is a reasonable amount because unknown unknowns, by definition, cannot be quantified; and (4) management reserve is the sole source of contingency in the LCM project.

The Commission agrees with the ALJ that I&M failed to carry its burden of proof to show that its proposed management reserve, over and above what appears to be a risk reserve added to at least some projects, is reasonable. The portion of the record in this case dedicated to I&M's testimony is rife with contradictions and late attempts to correct misstatements made in the course of the proceeding. While I&M argues that the ALJ and the other parties to the case do not understand the intent of Section 6s, what is most apparent from this record is that I&M failed to comprehend that Section 6s did not alter the burden of proof in an administrative proceeding before the Commission.

The Commission therefore agrees with the ALJ that the \$220 million management reserve originally proposed by the company (adjusted to \$214 million) should be removed from the cost approved by the CON. Nevertheless, because the Commission understands that knowledge of the future is not achievable given the complexity of the LCM project and the tasks and resources required to achieve it, the Commission finds it appropriate to include a management reserve of 10% of the base cost of the project. The Commission therefore approves a total CON amount of \$850,972,100.00 for the LCM project, comprised of 117 LCM subprojects identified by the company. This amount includes \$773,611,000 for projected project costs and \$77,361,100 for management reserve.

Accounting Requests

The ALJ did not address I&M's request for approval of deferred accounting on grounds that such approval was not required under Section 6s. I&M argues that the ALJ misconstrues its application and that the additional accounting requests are properly before the Commission

pursuant to the Commission's broad ratemaking authority. The Staff agreed with most of the company's deferred accounting proposals. The Attorney General and ABATE argue that the Commission should reject I&M's accounting requests. ABATE claims that there is no statutory authority or policy reason to approve deferred accounting, and the Attorney General claims that I&M failed to show by a preponderance of the evidence that authorizing the company to defer carrying costs for the LCM would result in just and reasonable rates. The Attorney General adds that I&M's request essentially results in an automatic rate adjustment mechanism, which the Commission lacks statutory authority to approve.

The Commission disagrees and finds that I&M's deferred accounting requests should be granted. As I&M points out, with the concurrence of the Staff, to avoid earnings erosion, timely recovery of costs is crucial in a project of the size proposed here. The Commission also clarifies that the approvals granted in this order apply only to the facts in this case.

Therefore, the Commission agrees with I&M's request to record AFUDC relating to both debt and equity capital and approves I&M's request to record deferred carrying costs as proposed in Mr. Krawec's direct testimony. However, as the Staff indicated, during the projected year of a rate case, the appropriate amounts of plant are included in rate base and the appropriate return on that plant is included in base rates, thus recording deferrals during a projected test year is unnecessary.

The other remaining accounting issue concerns depreciation rates to be applied to the LCM subprojects. I&M requests to depreciate these components over the remaining life of the unit in which they are installed, while the Staff recommends that the company use the depreciation rates for nuclear plant established in I&M's last depreciation case. The Commission finds that depreciation rates are appropriately established in a depreciation case and exceptions, such as the one proposed here by I&M, should not be made in other proceedings that are not primarily

concerned with depreciation. The Commission therefore agrees with the Staff's recommendation and finds that for the LCM subprojects I&M should use the depreciation rates approved in the February 15, 2012 order in Case No. U-16801. As the Staff and I&M point out, the settlement agreement approved in that proceeding does not include a date for I&M's next depreciation case filing. The Commission therefore directs I&M to file its next depreciation case by July 1, 2017 using December 31, 2016 plant balances. I&M may of course file sooner, using different year-end plant balances, if it so chooses.

Integrated Resource Planning Issues

The MEC raised concerns about the comprehensiveness of the IRP submitted by I&M. In MEC's brief and reply brief, the organization admitted that I&M's IRP, as supplemented by discovery and responses at the hearing, did support the LCM project as the least-cost alternative for maintaining capacity and energy in the company's service territory. Nevertheless, the MEC recommended that the Commission caution other providers and parties to future CON proceedings regarding the Commission's expectations about the content and analyses in an IRP submitted under Section 6s. Specifically, the MEC recommends:

First, the Commission should emphasize that CON applicants must perform all of the minimum IRP analyses specified in PA 286, regardless of whether a given investment appears at the outset to be the most cost-effective. Second, the Commission should base its decision in this case – and in every CON case – on the entire body of evidence properly introduced and entered into the record. Each of these recommendations will help ensure that the IRP provisions of PA 286 are given full effect, and that properly rigorous integrated resource planning becomes an important tool for utilities, intervenors, and the Commission in future CON proceedings.

MEC's reply brief, p. 11.

The Commission agrees with the MEC's recommendations and emphasizes that in future CON applications, a provider seeking a CON is expected to provide an IRP that, at minimum,

contains analyses that conform to the requirements of Section 6s(11) and the December 23, 2008 order in Case No. U-15896, Exhibit B.

Other Issues

The Commission agrees with I&M's proposal to engage a third-party contractor to provide semi-annual updates on the progress of the LCM, including information on construction progress and budget information. Within 60 days of the date of this order, I&M shall consult with the Generation and Certificate of Need Section Staff to discuss the appropriate contents of the first report. Finally, while the Commission recognizes the Staff's concerns about projects potentially running significantly over budget as these projects are phased into rate base, the Commission agrees with I&M that the CON applies to, and pre-approves, the LCM project as a whole. Thus, no additional reviews of the 117 subprojects is required or legally permitted under Section 6s.

THEREFORE, IT IS ORDERED that:

A. Indiana Michigan Power Company's request for a certificate of necessity for a life cycle management project at the Donald C. Cook Nuclear Power Plant is approved as modified by this order.

B. Indiana Michigan Power Company's request for accounting approval to defer carrying costs for the life cycle management project for 2013 through 2018 is approved as set forth in the order.

C. Indiana Michigan Power Company shall file a new depreciation case by July 1, 2017.

D. Indiana Michigan Power Company shall contract with a third party to provide semi-annual updates on the progress of the life cycle management project to the Commission and other stakeholders. Within 60 days of the date of this order, Indiana Michigan Power Company shall consult with the Commission Staff concerning the required content of the first update.

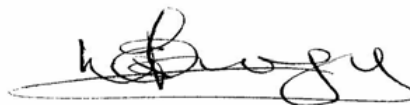
The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order under MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION



John D. Quackenbush, Chairman



Orjiakor N. Isiogu, Commissioner



Greg R. White, Commissioner

By its action of January 28, 2013.



Mary Jo Kunkle, Executive Secretary

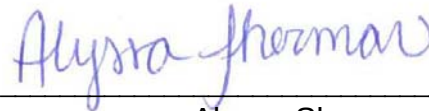
P R O O F O F S E R V I C E

STATE OF MICHIGAN)

Case No. U-17026

County of Ingham)

Alyssa Sherman being duly sworn, deposes and says that on January 28, 2013 A.D. she served a copy of the attached Commission order by first class mail, postage prepaid, or by inter-departmental mail, to the persons as shown on the attached service list.



Alyssa Sherman

Subscribed and sworn to before me
This 28th day of January 2013



Gloria Pearl Jones
Notary Public, Ingham County, MI
My Commission Expires June 5, 2016
Acting in Eaton County

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