IN THE
SUPREME COURT OF INDIANA

Case No. ____________

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR, DUKE INDUSTRIAL GROUP, SIERRA CLUB, CITIZENS ACTION COALITION OF INDIANA, INC., ENVIRONMENTAL WORKING GROUP, and INDIANA COMMUNITY ACTION ASSOCIATION,	)	Indiana Court of Appeals Cause No. 20A-EX-01404
	)	Appeal from the Indiana Utility Regulatory Commission
	)	Cause No. 45253
Appellants,	)	Hon. James F. Huston, Chairman, Hon. Sarah E. Freeman, Hon. Stefanie Krevda, Hon. David Ober, Hon. David E. Ziegner, Commissioners
v.	)	
DUKE ENERGY INDIANA, LLC, and INDIANA UTILITY REGULATORY COMMISSION,	)	
Appellees.	)	Honorable David E. Veleta, Senior Administrative Law Judge

APPELLEE DUKE ENERGY INDIANA, LLC'S RESPONSE IN OPPOSITION TO JOINT PETITION TO TRANSFER

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BACKGROUND AND PRIOR TREATMENT OF ISSUES ON TRANSFER

Like other public utilities, Duke's base electricity rates "are traditionally set or adjusted through a general ratemaking case . . . before the Commission. This is a comprehensive process in which the Commission examine[s] every aspect of the utility's operations and the economic environment in which the utility functions . . . ." *NIPSCO Indus. Grp. v. N. Ind. Pub. Serv. Co.*, 125 N.E.3d 617, 620 (Ind. 2019) (quotation omitted). This "detailed review allows the Commission to ensure that utility rates are fair to both the utility and its customers." *Id.*

In 2019, Duke initiated a rate case with the Commission, seeking to increase its base electricity rates for the first time since 2004. (App.Vol.II:22, 28.) Numerous entities intervened, including Appellants. The Commission conducted 11 days of evidentiary hearings with testimony from 59 witnesses, and it ultimately issued a 175-page Order granting Duke's request in part. (*Id.* at 20–194.) Appellants appealed three aspects of the Order, two of which are at issue here.[1]

<u>Retail/Wholesale Allocation</u>

Duke primarily serves retail electric customers. (Slip Op. pp.3, 7–8.) It therefore builds its infrastructure towards that end, and its retail customers' rates reflect that investment. Duke also sells a relatively small percentage of its electricity to wholesale customers (*id.*), which benefits retail customers because fixed costs are

[1] Appellants previously challenged the Order's approval of Edwardsport's operating expenses, and Appellants rely on their prior briefing for that issue. (Pet. p.10 n.1.) Duke similarly relies upon its prior briefing (Appellee's Br. pp.52–60) and the Court of Appeals' opinion.

then shared with wholesale customers. As part of its rate case, and to ensure Duke doesn't collect the same costs twice—once from retail customers and again from wholesale customers—Duke performed a "jurisdictional" separation study to apportion the costs for serving customers outside the Commission's jurisdiction (i.e., wholesale customers) from costs attributable to those within the Commission's jurisdiction (i.e., retail customers). (App.Vol.II:134.)

These separation studies involve sophisticated engineering and accounting analysis. (*See generally* Duke's Appellee's Br. pp.12–13; IURC Appellee's Br. pp.13–15.) Duke's witness presented the results of that study in support of its proposed allocation of costs between its retail and wholesale customers, allocating roughly 8% of costs to wholesale customers. (Ex.Vol.12:197; App.Vol.II:134.) This reflected a slight *decrease* in the allocation to retail customers compared to the allocation at the time Duke initiated its rate case. (Ex.Vol.3:36; App.Vol.II:135.) So while Appellants refer to a "shift in responsibility" to them (Pet. p.6), they have the shift going in the wrong direction.

Appellants did not introduce evidence that Duke's witness deviated from a standard approach to performing a jurisdictional separation study, or that Duke's engineering or accounting inputs were wrong. Instead, their witness proposed "the Commission should impute as long-term wholesale sales for jurisdictional study purposes, the amount of historical long-term wholesale sales that have terminated since 2013 that have not been replaced with long-term wholesale contracts." (App.Vol.II:134.) In other words, rather than using current data, their witness recommended imputing a hypothetical wholesale contract that was based on a comparison of Duke's wholesale load in 2013 to its wholesale load at the time of the rate case. But the only reason for picking 2013 as the point of comparison is that comparison minimizes the allocation to retail customers. To the extent any comparison to past allocations is appropriate, the relevant comparison is the allocation customers were paying when Duke initiated this rate case (set in the last rate case in 2004) and the allocation proposed in this rate case.

Thus, there was a factual dispute over how to properly allocate costs—Duke's approach of using current data or Appellants' proposed approach of imputing a hypothetical wholesale contract based on a cherry-picked date. The Commission agreed with Duke, concluding Duke's jurisdictional separation study was "a reasonable allocation of costs among the various jurisdictions . . . ." (*Id.* at 135.) Among other things, the Commission found persuasive that the level of sales allocated to wholesale customers is approximately the same as it was in Duke's last rate case, while Duke's "retail customers are being allocated a *lower* percentage of production demand costs than they were in the last base rate case." (*Id.*) (emphasis added).

The Court of Appeals correctly characterized this issue as a mixed question of fact and law, concluding there was "substantial evidence in the record to support the [Commission]'s findings, and the findings support [the Commission]'s conclusion to accept the study as a reasonable allocation of costs." (Slip Op. pp.18, 19.) The court observed the Commission, "as the finder of fact, weighed the parties' evidence and credited Duke's analysis of its production capacity over that of the [Appellants]." (*Id.* at 19.)

Coal Ash Remediation

Coal ash is a byproduct of Duke's generators that burn coal to produce electricity. (*Id.* at 5.) Duke sought recovery of its costs incurred to comply with recent developments in federal and state environmental laws which required Duke to take significant action to maintain and store its coal ash in a more protective manner. (App.Vol.II:50, 60-61.) These costs significantly prolong the life of the generation facilities because without the remediation, Duke would be required to retire those facilities much sooner. (*Id.* at 67; Slip Op. p.16.) In other words, these costs are in the nature of capital costs.

Duke sought to include in its rate base a "regulatory asset" consisting of the retail jurisdictional portion of its past coal ash analysis, engineering, closure, and related costs, and to recover those costs over 18 years. (App.Vol.II:50.) A "regulatory asset" is also referred to as "deferred accounting," and it is a financial vehicle for utilities to defer costs from an income statement to a balance sheet and to include the asset in rate base. (*See* IURC's Appellee's Br. p.17 n.5.) Considered differently, deferred accounting is "a method of preserving for Commission consideration non-test-year expenses that would otherwise not be reflected on a test year ledger." *South Haven Sewer Works, Inc.*, 2002 WL 31107491 (IURC June 5, 2002).

Utilities may not use deferred accounting for any costs they choose. They may only utilize deferred accounting where doing so is proper under the applicable accounting rules, which require, among other things, that recovery of the costs be probable. *Id.* (App.Vol.II:54.) The accounting rules specify that one way to determine probability is by reference to previous rate orders from regulators approving recovery for similar costs. (*Id.*) Moreover, recovery of deferred costs is only available for costs which are significant, infrequently incurred, and will provide long-lasting benefits. *South Haven*, 2002 WL 31107491. Where utilities seek to use deferred accounting for other types of costs, the Commission denies those requests. *Id.* And while utilities sometimes mitigate risk by seeking pre-approval of deferred accounting, there is no requirement that they do so.

Here, Duke used deferred accounting for costs incurred between 2015 and 2018 to comply with the EPA's Coal Combustion Residuals ("CCR") Rule, as well as costs incurred through 2018, and to be incurred in 2019 and 2020, to comply with the Indiana Department of Environmental Management's ("IDEM") solid waste management rules. In its Order, the Commission concluded "the [Coal Ash] costs were properly deferred and preserved for recovery consideration in this proceeding," and were therefore recoverable under traditional ratemaking. (App.Vol.II:67.)

Appellants make much of the fact that this request to approve deferred accounting through traditional ratemaking was Duke's "alternative" argument after first relying on the Federal Mandate Statute. (Pet. p.2, 8, 16.) There is no reason that should make a difference, and, as the Commission explains in its Response, the Federal Mandate Statute is irrelevant on appeal because that was not the basis for the Commission's order. The Commission merely pointed to the Federal Mandate

Statute for collateral support because Duke's request also satisfied overlapping requirements of that statute.

The Court of Appeals affirmed the Commission's Order, rejecting Appellants' argument that the Commission had engaged in retroactive ratemaking and noting the Commission did not alter any past rates or charges in connection with the Coal Ash costs. (Slip Op. p.13–15.) Rather, the court confirmed this issue was also a mixed question of law and fact, and there was substantial factual support in the Record for the Commission's conclusion. (*Id.* at 16–17.) Here, the Commission, as the factfinder, had the authority to approve Duke's accounting practices and associated ratemaking proposal, so long as they were reasonable—and they were. (*Id.* at 17.)

ARGUMENT

Both issues on appeal turn on sophisticated engineering and accounting analysis for cost allocation and recovery, presenting mixed questions of fact and law squarely within the Commission's expertise. After considering conflicting testimony, the Commission reached reasonable conclusions agreeing with Duke. Those conclusions were drawn from and supported by factual findings, and those findings were supported by substantial evidence. The Court of Appeals was therefore correct to affirm, and no issues merit transfer.

I. The Commission's conclusion that Duke's cost allocation was reasonable was properly supported by factual findings and substantial evidence.

Appellants claim the Commission and Court of Appeals have "eroded" the "used and useful" standard by approving and affirming Duke's cost allocation between its retail and wholesale customers. (Pet. pp.10–15.) Just the opposite: no Indiana case has ever concluded that a utility's allocation *reducing* the percentage of costs allocated to retail customers violates the "used and useful" standard, and there is no reason this case should have been the first. Further, to make their argument, Appellants ignore long-standing Commission precedent as to what constitutes "excess capacity" that is not "used and useful."

A. There is no evidence Duke has excess capacity.

First and foremost, Appellants' "proof" supporting their excess capacity/"used and useful" argument is simply a table showing Duke's generating capacity is currently (and temporarily) greater than its 15% planning reserve margin. (*See* Industrial Group Appellee's Br. p.32.) Appellants claim this demonstrates Duke has excess capacity that is not used and useful to support retail service. (Pet. p.12.) But there is no law, rule, or precedent that equates excess capacity with capacity above a target reserve margin. In fact, longstanding Commission precedent makes clear a finding of excess capacity may *not* be based solely on a utility's reserve margin.

Indiana Code section 8-1-2-6 requires the Commission to "value all property of every public utility actually used and useful for the convenience of the public at its fair value[.]" *See In re N. Ind. Pub. Serv. Co. ("NIPSCO")*, 1985 WL 1208669, 67

P.U.R.4th 396, 399 (Ind. P.S.C. June 19, 1985). Before any generation facility may be included in a utility's rate base, the Commission must find the facility to be "used and useful." *Id.* at 399–400. Specifically, it must find: "(1) that the utility plant be actually devoted to providing utility service, and (2) that the plant's utilization be reasonably necessary to the provision of utility service." *City of Evansville v. S. Ind. Gas & Elec. Co.*, 339 N.E.2d 562, 589 (Ind. Ct. App. 1975).

The Commission has never adopted an approach requiring all capacity above an arbitrarily established margin be excluded from rate base, whether the utility's decision to construct the facility(ies) was prudent. *NIPSCO*, 67 P.U.R.4th at 401 (listing numerous shortcomings to adopting such an approach). Even if a singular focus on reserve margin were appropriate (it is not), in *NIPSCO*, the Commission found no excess capacity and concluded NIPSCO's generating units were used and useful, with reserve margins of up to 62.8%. *Id.*; *see also Office of Util. Consumer Couns. v. Pub. Serv. Co. of Ind.*, 463 N.E.2d 499 (Ind. Ct. App. 1984) (reserve margins of up to 47% were "used and useful"). These cases demonstrate the reality of utility additions to generating capacity. To achieve economies of scale, utilities construct sizable generating units. When a sizable unit is added to a utility's portfolio, the reserve margin is (temporarily) high, until either an increase in customer demand or the retirement of an existing unit allows it to "grow into" that generating addition.

Here, although Duke added a sizeable generating facility in 2013 (Edwardsport), the reserve margins Appellants rely upon in support of their excess capacity argument are much lower than the reserve margins previously found to be "used and useful" in *NIPSCO* and *Public Service*. (Conf.Ex.Vol.17:180.) Thus, the "dispositive fact" forming the basis for Appellants' transfer argument is neither dispositive nor undisputed. (Pet. p.15.)

Further, Appellants did not present any evidence concerning the numerous other factors the Commission considers relevant to an excess capacity determination—such as prudence, changed circumstances, the utility's obligation to serve, financial implications, etc. *NIPSCO*, 67 P.U.R.4th at 401. Even if Duke's reserve margin was out of line (it is not), there was still insufficient evidence to conclude Duke has excess capacity.

B. Appellants misunderstand and misapply the "used and useful" doctrine.

Appellants' reliance on the "used and useful" doctrine is itself misplaced. Again, "used and useful" requires "(1) that the utility plant be actually devoted to providing utility service, and (2) that the plant's utilization be reasonably necessary to the provision of utility service." *City of Evansville*, 339 N.E.2d at 589.

Appellants overlook that Indiana law draws a clear distinction between new facilities that have never been used, and facilities that have been used to provide utility service to customers for years. In *Citizens Action Coalition of Indiana, Inc. v. Northern Indiana Public Service Company*, this Court noted there is

> a long-adhered to administrative interpretation of allowing amortization of abandoned plants, i.e. plants that were "used and useful" property and then retired from service. This is clearly distinguishable from allowing amortization of cancelled plants that never became "used and useful." Allowance of amortization of cancelled plants would encourage uneconomical or unproductive ventures; whereas, allowance for amortization of abandoned or retired plants

> encourages utilities to remove obsolete plants and property from the ratebase. This treatment also benefits consumers because obsolete and inefficient property is removed from the ratebase.

485 N.E.2d 610, 616 (Ind. 1985).

All the major components of Duke's current generating portfolio have been "used and useful" for years. The majority of Duke's portfolio is comprised of plants added as recently as 2013 (Edwardsport), along with plants that were constructed in the 1980s and earlier. Accordingly, this case involves neither a cancelled nor a brand-new plant. Even if Duke were found to have excess capacity (it does not), the Court's decision above demonstrates Duke would nevertheless be entitled to recover the costs of its generating plants that have been used for years to serve customers.

Appellants cite to this Court's decision in *Citizens Action Coalition* in support of their "used and useful" argument. But as Appellants note, that case involved a utility's attempt to charge ratepayers for a cancelled plant that was never put into service, which is not at issue here. (Pet. pp.13–14.) Importantly, Appellants have not identified *any* Duke property, other than the alleged "excess capacity"—which, as set forth above, does not exist—that is not used to serve Duke's customers.

Indiana's CPCN (Certificate of Public Convenience and Necessity) Statute further supports the conclusion that even if there were excess capacity (there is not), Duke would be entitled to recover the costs of such capacity for which it obtained CPCNs. Indiana Code ch. 8-1-8.5 provides that, absent fraud, concealment, or material mismanagement, a utility is entitled to recover the costs of its generating plants for which it has obtained a CPCN—including a return thereon. All of Duke's generating plants constructed or purchased since 1983 were preapproved and received CPCNs. (*See* Duke's Appellee's Br. p.31 n.3.) Accordingly, the Commission and Court of Appeals correctly determined the "used and useful" doctrine plays no role in this base rate case.

The Court of Appeals correctly determined this issue presented a mixed question of law and fact, which is reviewed for reasonableness. *NIPSCO Indus. Grp.*, 125 N.E.3d at 624. As the Court of Appeals detailed, there is substantial evidence supporting the Commission's approval of Duke's separation study as an allocation of costs between its retail and wholesale customers. (Slip Op. pp.18–20.) And the Commission properly credited Duke's witnesses and accounting, including Duke's analysis of its production capacity. (*Id.* at 19–20.) The Court of Appeals' refusal to second-guess the expertise of the Commission does not warrant transfer.

II. The Commission reasonably concluded Duke properly utilized deferred accounting for its coal ash costs.

A. The Commission did not rely on the Federal Mandate Statute.

Appellants make much of the fact that this request to approve deferred accounting through traditional ratemaking was Duke's "alternative" argument after first relying on the Federal Mandate Statute. (Pet. pp.2, 8, 16.) There is no reason it should make a difference whether this was Duke's first or second argument and, as the Commission explains in its Response, the Federal Mandate Statute is irrelevant on appeal because that was not the basis for the Commission's Order. The Commission merely pointed to the Federal Mandate Statute for collateral support because the requirements of that statute the Commission concluded Duke did satisfy are also requirements for recovery of properly deferred costs. Regardless, no party ever objected to Duke's deferred accounting evidence and no party has ever suggested Duke waived the argument.

B. Deferred accounting is not retroactive ratemaking regardless of whether it is pre-approved.

The principle against retroactive ratemaking stems from Indiana Code section 8-1-2-68, which states:

> Whenever, upon an investigation, the commission shall find any rates, tolls, charges, schedules, or joint rate or rates to be unjust, unreasonable, insufficient, or unjustly discriminatory, or to be preferential or otherwise in violation of any of the provisions of this chapter, the commission shall determine and by order fix just and reasonable rates, tolls, charges, schedules, or joint rates to be imposed, observed, and followed *in the future* in lieu of those found to be unjust, unreasonable, insufficient, or unjustly discriminatory or preferential or otherwise in violation of any of the provisions of this chapter.

(emphasis added). Put another way, "[p]ast losses of a utility cannot be recovered from consumers nor can consumers claim a return of profits and earnings which may appear excessive." *Ind. Bell Tel. Co., Inc. v. Office of Util. Consumer Counselor*, 717 N.E.2d 613, 625 (Ind. Ct. App. 1999), *modified on reh'g on other grounds*, 725 N.E.2d 432 (Ind. Ct. App. 2000).

Appellants argue allowing recovery of Duke's previously incurred coal ash costs violates the principle prohibiting "retroactive ratemaking." (Pet. pp.18–21.) But the Court of Appeals correctly rejected this argument, pointing out Duke did not seek—and the Commission did not alter—any past rates or charges, nor impose any interim rates, in connection with its coal ash costs. (Slip Op. pp.13–14.)

Critically, Appellants do *not* argue that recovery of deferred costs constitutes retroactive ratemaking even though deferred accounting, by definition, entails recovery of previously incurred costs. Just the opposite, they acknowledge the Commission has long had the authority to approve recovery of deferred costs, albeit in limited circumstances. (Pet. p.20.) Their argument is instead that only deferred accounting that is not *pre-approved* constitutes retroactive ratemaking. But pre-approval makes no difference with respect to whether the ratemaking is retroactive. Pre-approved or not, the rates are to recover costs that were *previously* incurred. Again, that is the whole point of deferred accounting, and it is not retroactive ratemaking because deferring the costs makes them expenses in the year to which they were deferred. *See, e.g.*, *South Haven*, 2002 WL 31107491 ("The deferred debit accounting system can be viewed as a method of preserving for Commission consideration non-test-year expenses that would otherwise not be reflected on a test year ledger."); *In re Consumers Energy Co.*, No. 338592, 2018 WL 5304913, at *7 (Mich. Ct. App. Oct. 25, 2018) ("Once these expenses were deferred, they became expenses incurred in the year to which they were deferred, and, thus, are prospective in nature and not retroactive.").

Appellants' argument that "[w]ithout preapproval, subsequent recovery is *retroactive*, altering the status of past costs for ratemaking purposes after the fact," (Pet. p.20), cannot be squared with this Court's decision in *NIPSCO Indus. Group v. NIPSCO*, 100 N.E.3d 234 (Ind. 2018). In the very first sentence of that decision, the Court explained: "Under traditional rate regulation, an energy utility must *first* make improvements to its infrastructure before it can recover their cost through regulator-approved rate increases to customers. The process for recouping these costs, *sometimes not until years after they were incurred*, is an expensive, onerous ratemaking case, which involves a comprehensive review of the utility's entire business operations." *Id.* at 236 (emphases added). That is precisely what occurred here. Duke incurred significant costs to improve its infrastructure—environmental remediation prolonging the life of its facilities—and can now recover those deferred costs through traditional ratemaking. Notably, Appellants do not cite any cases concluding that deferred counting without preapproval constitutes retroactive ratemaking.

Moreover, as the evidence makes clear, if these costs were not considered a legal obligation under applicable accounting rules, they would have been included as a "cost of removal" in Duke's depreciation rates and recovered through depreciation expense. (App.Vol.II:50–51; Ex.Vol.40:29.) Thus, Duke's requested recovery of coal ash costs through the regulatory asset is the same ratemaking treatment the costs would have received had they been treated as a cost of removal in a normal plant retirement situation, and is consistent with the historical Indiana practice of cost recovery for reasonable and necessary generating station costs of removal such as these.

Neither the Commission's Order nor the Court of Appeals' decision opens the floodgates for deferred accounting. Just as it has always been, deferred accounting remains available only in the limited circumstances permitted by the accounting rules, and the Commission denies requests for deferred accounting of other costs that do not meet its criteria for recovery. *See, e.g.*, *South Haven*, 2002 WL 31107491 (denying requests for deferred accounting).

There is also nothing new in the Commission approving deferred accounting without pre-approval, and even the OUCC has requested deferred accounting without preapproval. *See Amended Petition of NIPSCO*, 2009 WL 9509000, at *7 (IURC 2009) ("The Commission has long recognized the distinction between accounting treatment and rate recovery, and has approved the deferral of costs for possible future recovery that were incurred *prior to a grant of deferral*." (emphasis added); *In re IURC's Investigation into the Impacts of the Tax Cuts and Jobs Act*, 2018 WL 6925810, at *5 (IURC 2018) ("While we are not approving Respondent's request [for deferred accounting of costs already incurred] at this time, such decision does not preclude Respondent from seeking recovery of such costs in its next rate case."); *Petition of Duke Energy et al.*, 2019 WL 4600201, at *5 (IURC 2019) (granting the OUCC's request for deferred accounting of costs related to stays of disconnection, waivers of utility fees, and expanded payment arrangements even as to costs already incurred without preapproval).

As far back as 1995, the Commission approved a settlement with a utility that sanctioned the suspension of creating regulatory assets without preapproval for certain costs related to a corporate reorganization, illustrating that the default has always been to permit the creation of regulatory assets in appropriate circumstances without preapproval. *In re PSI Energy, Inc.*, 1995 WL 298119 (IURC Feb. 17, 1995).

To be sure, sometimes parties seek pre-approval to mitigate risk, since there is always a chance the Commission will deny recovery of deferred costs. But that is not required, nor should it be since there is not always a clear-cut answer for when to request approval. Even here, some parties argued Duke's request for deferred accounting was *premature* because IDEM had not yet given final approval for Duke's remediation plans. (Tr. Ex. Vol. 28 pp.168–70.)

As the Commission found, Duke properly deferred and preserved the coal ash costs for recovery consideration in this rate case. Once the coal ash costs were properly deferred, they became expenses incurred in the year to which they were deferred, and thus, are prospective in nature, not retroactive.

C. Duke's deferral of its coal ash costs was proper.

Our courts have long recognized, and Appellants do not dispute, "a request for a deferred accounting treatment" is an "accounting practices" issue for the Commission to decide, and "decisions regarding accounting practices followed by public utilities are policy determinations committed to the sound discretion of the Commission." *NIPSCO v. Office of Util. Consumer Couns.* 826 N.E.2d 112, 119 (Ind. Ct. App. 2005). "Hence, judicial interference is inappropriate so long as the Commission acts within reason and prudence." *Id.*

Here, Appellants do not argue there is not substantial evidence to support the Commission's factual findings, or that those findings do not reasonably support the Commission's conclusion that Duke applied the proper accounting treatment by utilizing deferred accounting. (*See, e.g.,* Slip Op. pp.16–17, detailing the 17 pages of factual findings on the coal ash costs.) Because the Commission's findings were reasonable, and supported by substantial factual support in the record, the Court of Appeals did not err in affirming the Order, and transfer is not warranted.

CONCLUSION

The Petition to Transfer should be denied.

Respectfully submitted,

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WORD COUNT CERTIFICATE

I verify that this brief contains no more than 4,200 words.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that on July 19, 2021, the foregoing was filed and served electronically via the Indiana E-Filing System upon the following persons, in accordance with Indiana Appellate Rules 24 and 68:

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