BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN

Application of Wisconsin Power and Light Company for a Certificate of Public Convenience and Necessity to Build an Approximately 650 Megawatt Natural Gas-Fueled Power Plant at its Riverside Energy Center Facility in the Town of Beloit, Rock County, Wisconsin

Docket No. 6680-CE-176

INITIAL BRIEF OF WISCONSIN INDUSTRIAL ENERGY GROUP

INTRODUCTION AND DISCUSSION

In this proceeding the Applicant Wisconsin Power and Light Company ("WPL") is seeking a Certificate of Public Convenience and Necessity ("CPCN") to construct an approximately 650 megawatt natural gas-fueled power plant ("Riverside" or "RECE"), at its existing Riverside Energy Center Facility, at a cost of $700 million. The Wisconsin Industrial Energy Group ("WIEG") is a member organization of businesses, many of which are customers of WPL, that use substantial amounts of energy in their operations. WIEG's remaining interests in this proceeding are (1) minimizing Riverside construction costs that WPL will recover in rates and (2) reducing the risk that construction costs in excess of those currently estimated by WPL will be passed on to ratepayers. WIEG does not take a position as to whether WPL has made the showing necessary for the Public Service Commission of Wisconsin (the "Commission") to approve the request, with the following exception: the Commission should not grant a CPCN without conditions that offer ratepayers reasonable financial protections. As the Commission considers WPL's request for a CPCN, **now** is the best opportunity we will have to minimize project costs to the benefit and protection of ratepayers.

WPL's ratepayers are best protected with conditions that will minimize project costs and align WPL's recovery of project costs from the customers who benefit from the project. WIEG witness Mr. Kollen set forth six conditions that provide ratepayer protections. No witness challenges Mr. Kollen's assertions that each of the conditions benefits ratepayers. Moreover, no witness asserts that Mr. Kollen's proposals, alone or in combination, will harm WPL. Objections to his proposed conditions, to the extent that the responses may even be characterized as objections, are of two types: either Mr. Kollen's proposal is premature and should be addressed in WPL's next rate case, or should not be adopted merely because the proposal is new to Wisconsin. The Commission should reject these objections in favor of securing certainty for customers.

Mr. Kollen has proposed, and WIEG urges the Commission to adopt should it grant the CPCN, the following conditions:

- A "hard cap" on the cost of the Project for ratemaking purposes, limited to the lesser of WPL's $700 million cost estimate or actual construction costs, plus reasonable financing costs.

- Use of Allowance for Funds Used During Construction ("AFUDC") with no Construction Work In Progress ("CWIP") in rate base.

- Use of mirror CWIP in the event the Commission authorizes any CWIP in rate base.

- Use of lower cost short-term debt to the maximum extent possible.

- Use the Federal Energy Regulatory Commission ("FERC") methodology for AFUDC rather than the use of the Company's authorized rate of return.

- Use of a forty-year service life for depreciation purposes.

Of these six, no one challenges a forty-year service life for depreciation purposes. The

Commission should readily embrace each of these conditions.

A. THE COMMISSION SHOULD PLACE A "HARD CAP" ON CONSTRUCTION COSTS.

In the event that the Commission grants the CPCN, it should ensure that ratepayers get the benefit of the bargain WPL has asserted. That bargain is a construction cost of $700 million, an amount that must figure in the Commission's decision that RECE is economic compared with those other alternatives that WPL considered. The most secure way in which to ensure that customers do get that benefit of this least-cost Project is in limiting WPL's future recovery of construction costs to its $700 million cost estimate, or actual construction costs if those costs are less than $700 million. (Direct-WIEG-Kollen-7)

First, ratepayers should have certainty regarding the cost of the Project, particularly where WPL has offered RECE as least cost on a net present value basis. WPL alone controls the project and, as such, it should not share excessive costs with its ratepayers, particularly where the Commission has approved the Project based in large measure upon the assertion that it will cost no more than $700 million. Second, the $700 million cost estimate is overstated as it is, given that it includes significant contingencies. For instance,. "the differences in actual contractor and owner's costs compared to estimated costs, and actual contractor and owner performance and actual costs compared to estimated costs." (Direct-WIEG-Kollen-7-8) Third, the $700 million cost has already accounted for the "expected increases in materials, labor, and other costs during the construction period in addition to the contingency." (*Id.* at 8)

The importance of a hard cap is of even greater significance following the Settlement Agreement that WPL entered into with Wisconsin Electric Power Company, through which

WPL has agreed not to offer RECE into the MISO capacity market before 2020. This Settlement Agreement effectively delays the RECE project by a year. (Supplemental Rebuttal-WIEG-Kollen-4) Even now the in-service date is not clear. (Supplemental Direct-WPL-Kitchen-4) As Mr. Kitchen explained, the "specific date that RECE will be available for energy production will remain flexible." (*Id.*)

WPL alone controls the schedule for the construction of RECE. (Supplemental Rebuttal-WIEG-Kollen-5) WPL alone will negotiate the Engineering, Procurement and Construction ("EPC") contract. (*Id.*) WPL alone will manage the project, including the management of the EPC contractor. (*Id.*) WPL alone can hold the contractor to WPL's own hard cap on costs. (*Id.*) And, significantly, WPL has asserted that the delay will provide its EPC contractor schedule relief, which should reduce costs as it will relieve the EPC contractor from the "overtime money and some other costs in there to accelerate work to meet [WPL's] original timeline." (Newell, Tr., at 288) WPL knows "that at least most of [these costs] would disappear with the relaxed schedule that WPL is now looking at." (*Id.*)

WPL's response to a hard cap, though, is not substantive. Instead, it asks that the Commission not treat its RECE project any differently than the Commission has other recent construction cases. (Rebuttal-WPL-Kouba-10) Ironically, though, Mr. Kouba immediately thereafter allows for the fact that the Commission does not treat all such projects similarly, stating that the Commission typically includes a 10% cost cap that is greater than the proposed construction costs. (*Id.*) The Commission deviated from the "typical" as recently as 2013, when it granted Wisconsin Public Service Corporation a CPCN for its environmental controls at

Weston 3, subject to a 5% cost cap. *See* Final Decision, Order Point 2, *Application of Wisconsin Public Service Corporation for Authority to Construct and Place in Operation a New Multi-Pollutant Control Technology System for Unit 3 of the Weston Generating Station, Marathon County, Wisconsin* (April 13, 2013) (PSC REF#: 183440). For the reasons set forth above, to the extent there is a "typical," in light of the specific facts of this case and exclusive control WPL has over the cost of the Project, the Commission should condition a CPCN on a hard cap.

B. THE COMMISSION SHOULD CONDITION THE CPCN ON USE OF AFUDC, WHICH NO WITNESS DISPUTES IS LESS COSTLY TO RATEPAYERS THAN CWIP.

In all cases, the utility recovers Project costs (materials, labor, and other costs of construction) over the life of the Project once it is used and useful. (Direct-WIEG-Kollen-9-r) At issue here is the mechanism through which the utility will recover the financing costs of construction that it incurs during construction. A utility recovers the financing costs it incurs during construction in one of two ways: AFUDC or CWIP. The significant difference between AFUDC and CWIP is the timing of the utility's recovery of its financing costs. AFUDC adds all of the financing costs to the other project costs and recovers those costs through rates over the life of the project. On the other hand, CWIP places financing costs immediately into the utility's rates, allowing the utility near immediate recovery of those costs. (*Id.* 9-10)

The Commission should condition the CPCN on the use of the AFUDC approach because that approach results in a lower net present value cost to customers and, as equally important, "promotes intergenerational equity and matches the recovery of the costs to the service provided." (Direct-WIEG-Kollen-9-r) In other words, when financing costs are included as construction costs over the 40-year life of the project, those customers who are using RECE over

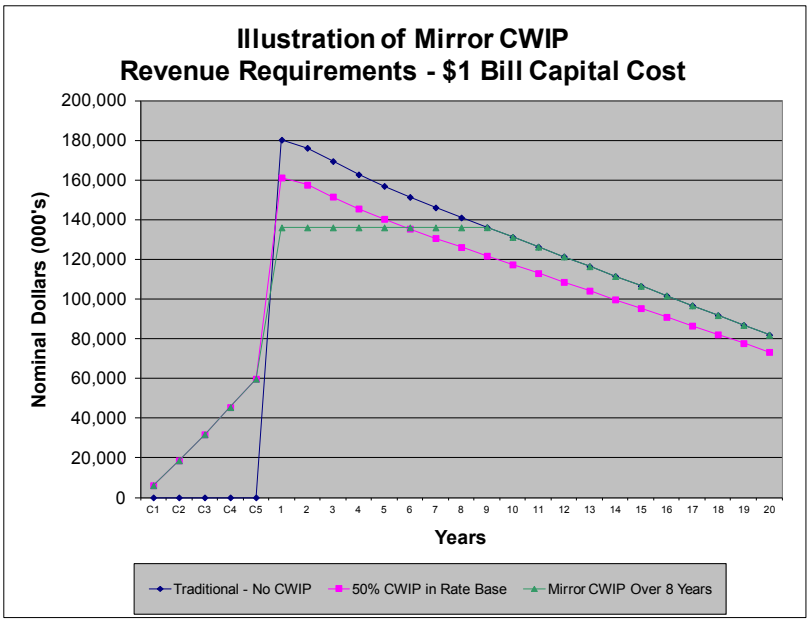
the 40-year life of the project will be paying the financing cost, when they are benefiting from that project. On the other hand, use of CWIP results in the utility's current customers paying these upfront costs of financing, even though they are not receiving any benefit.

The Commission should readily provide this order point. Doing so does not harm the utility, because both approaches provide the utility full recovery. (Direct-WIEG-Kollen-9-r) And doing so does benefit ratepayers because the AFUDC approach results in a lower net present value cost to customers, and results in customers that benefit from RECE paying those costs. (*Id.*)

C. IN THE EVENT THAT THE COMMISSION ALLOWS ANY AMOUNT OF CWIP IN RATE BASE, IT SHOULD ALSO USE "MIRROR CWIP".

As explained above, when any amount of CWIP is included in rate base, the utility is immediately recovering construction financing costs from its customers, even though the customers are not yet benefiting. Thus, WPL's revenue requirement is greater in the years before the construction is completed than would be the case if financing costs of construction were not immediately placed into rates. Mirror CWIP works to reduce the utility's revenue requirement immediately after the project is complete and placed in service. With mirror CWIP, amounts recovered in rates from customers during the construction period are returned to customers, reducing the utility's revenue requirement, in the first few years after the project is completed. (Direct-WIEG-Kollen-11) The period during which these amounts are returned to customers is the same as the period during which the construction costs were being recovered from customers before the in-service date. The benefit of using mirror CWIP is to levelize the utility's revenue requirements once the project is placed in service. Immediately below is an

illustration comparing AFUDC, 50% CWIP, and mirror CWIP. (*Id.*)



As is seen from this illustration, use of mirror CWIP reduces the peak revenue requirement during the years soon after the project is placed in service, and then follows the AFUDC approach for the remainder of its useful life.

WPL's response to this condition is not substantive. It notes only that the approach has not been used in Wisconsin and is an issue that should wait until the next rate case. (Rebuttal-WPL-Michek-9)

D. THE COMMISSION SHOULD EMPLOY THE FERC AFUDC METHODOLOGY.

While the FERC AFUDC methodology does differ from the Commission's historic AFUDC methodology, it should be adopted for this case because it more closely parallels WPL's actual financing costs of construction, while the historic method tends to exceed the actual financing costs of construction. (Direct-WIEG-Kollen-14) Thus, the FERC methodology results

in a lower net present value cost to customers. (*Id.*) Moreover, the FERC methodology is consistent with the Company's actual practice and more closely reflects its actual cost to finance the construction. (*Id.*)

WPL's response does not dispute Mr. Kollen's assertions as to the benefits of FERC AFUDC methodology in this case. Indeed, Mr. Michek acknowledges that WPL follows the FERC methodology for FERC purposes. His "objection" to using FERC methodology for PSCW purposes is that the methodology is not current practice. (Rebuttal-WPL-Michek-8) While Mr. Michek asserts that the use of FERC AFUDC methodology would increase costs for other ratemaking purposes, that is not the case where WPL would maximize short term debt. (Surrebuttal-WIEG-Kollen-28-rc)

D. THE COMMISSION SHOULD REQUIRE WPL TO EMPLOY MORE SHORT-TERM DEBT.

No one disputes that short-term debt is "unequivocally and substantially the lowest cost form of financing." (Direct-WIEG-Kollen-15) Therefore, short-term debt (at a cost of as little as 0.25%) should be the first and primary source of financing construction—before issuing long-term debt (at a cost of over 5%) and common equity (at a cost of 10.4%)—the use of which will result in lower net present value cost to customers than if short-term debt is not maximized. (*Id.*) In combination with the FERC AFUDC methodology, short-term debt to finance $100 million in construction costs provides considerable ratepayer benefits. (*Id.*) Over a three-year construction period, the use of short-term debt will reduce AFUDC by $25.6 million for each $100 million so financed. (*Id.*)

WPL's response does not challenge Mr. Kollen's proposal on grounds that it is not

correct. On this issue, like those others, WPL responds only that the Kollen proposal deviates from the Commission's past practice and is an issue that should be saved for the utility's next base rate case. (Rebuttal-WPL-Michek-8)

F. THE COMMISSION SHOULD CONDITION THE CPCN ON WPL'S USE OF A 40-YEAR LIFE FOR DEPRECIATION PURPOSES.

WPL agrees with WIEG witness Mr. Kollen that RECE should have a forty-year service life for purposes of depreciation. Although WPL initially proposed a depreciation life of 35 years, in his testimony Mr. Michek acknowledged that a 40-year life for depreciation is consistent with the authorized depreciation rates in effect at Riverside Energy Center. (*See* Direct-WPL-Michek-8) He accepts that a 40-year life for depreciation for RECE is appropriate. (Rebuttal-WPL-Michek-2)

CONCLUSION

The greatest opportunity that the Commission has to protect WPL ratepayers is right now, while WPL's request for a CPCN is before it. WPL and its ratepayers should know with certainty the cost of the Project—and the proposals that WIEG supports here will provide that certainty. Particularly in such a case as this, where the proposed conditions are not challenged on substantive grounds, the Commission should embrace those elements that will minimize the overall cost to ratepayers. Thus, for each of the above-stated reasons, WIEG asks that the Commission provide in the CPCN now, and not leave to future uncertainty, the following conditions:

- A "hard cap" on the cost of the Project for ratemaking purposes, limited to the lesser of the $700 million nominal dollar direct cost estimate or actual construction costs, plus reasonable financing costs.

- Use of AFUDC with no CWIP in rate base.
- Use of mirror CWIP if any CWIP is allowed in rate base.
- Use of the FERC AFUDC methodology.
- Use of lower cost short-term debt to the maximum extent possible.
- Use of a forty-year service life for depreciation purposes.

Adoption of these conditions will be of substantial benefit to ratepayers.

Respectfully submitted this 19th day of January 2016.

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