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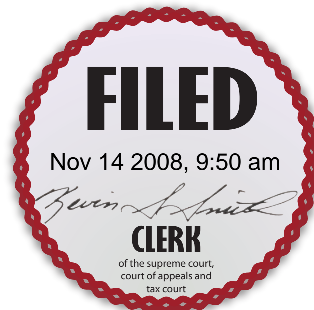

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IN THE
COURT OF APPEALS OF INDIANA

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR,	)	
Appellant,	)	
vs.	)	No. 93A02-0803-EX-236
DUKE ENERGY INDIANA, INC,	)	
Appellee-Petitioner.	)	

APPEAL FROM THE INDIANA UTILITY REGULATORY COMMISSION
The Honorable David Lott Hardy, Chairman
The Honorable Jeffrey L. Gole
The Honorable Larry S. Landis
The Honorable Gregory D. Server
The Honorable David E. Ziegner, Commissioners
Cause No. 42061-ECR10

November 14, 2008

MEMORANDUM DECISION - NOT FOR PUBLICATION

BARNES, Judge

Case Summary

The Office of Utility Consumer Counselor ("OUCC") appeals an order of the Indiana Utility Regulatory Commission ("IURC") granting a rate increase request by Duke Energy Indiana, Inc. ("Duke") related to qualified pollution control property ("QPCP") it is constructing. We affirm.

Issues

The restated issues before us are:

I. whether there is sufficient evidence to support the IURC's order; and

II. whether the IURC's order amounts to impermissible retroactive ratemaking.

Facts

In 2002, the IURC approved a plan submitted by Duke with respect to special construction work in progress ("CWIP") ratemaking treatment for clean coal technology plants, or QPCP, it was constructing. As part of the IURC's 2002 order, it permitted Duke to update the value of its QPCP for CWIP ratemaking purposes every six months. These update filings and proceedings are known as Environmental Cost Recovery ("ECR") proceedings.

On June 30, 2007, Duke filed its tenth ECR petition since the original 2002 order ("ECR 10"). Among several other matters, this petition sought to correct an accounting mistake that Duke had made for several years, in ECRs 4 through 9, with respect to its calculation of allowance for funds used during construction ("AFUDC"). The Indiana Administrative Code defines AFUDC as "the cost for the period of construction of borrowed funds used for the construction of qualified pollution control property . . . and a reasonable rate on other funds when so used." 170 Ind. Admin. Code 4-6-1 (2008) (see http://www.in.gov/legislative/iac/). Basically, the "cost . . . of borrowed funds" means interest on borrowed funds and costs associated with equity financing. See Centerior Fuel Corp., v. Zaino, 740 N.E.2d 255, 257 (Ohio 2001). AFUDC is a construction cost that is a component of CWIP when calculating the value of QPCP for ratemaking purposes. The particular problem in this case concerned a failure to properly account for proceeds from tax-exempt bonds that Duke had issued in December 2003 to finance QPCP construction, which proceeds were placed in a trust fund and bore interest until they were needed to pay construction costs as they arose.

With respect to the AFUDC issue, Duke pre-filed the direct and rebuttal testimony of its employee, Diana Douglas, along with documentary exhibits. This evidence indicated that the total amount of AFUDC understatement was approximately $18,018,000. Including this amount in CWIP resulted in a stated revenue requirement, or the amount it was entitled to collect from consumers, in the ECR 10 proceeding that was $1,721,000 higher than it would have been without the AFUDC adjustment. Douglas

also indicated that if the proper AFUDC amounts were individually recalculated in every proceeding going back to ECR 4 in June 2004, when the accounting errors first would have impacted CWIP calculations, the increase in revenue requirement over the course of time would have been over $3.1 million, not $1,721,000.[1] The OUCC objected to Duke claiming any AFUDC accounting adjustment. It contended that allowing any such adjustment would amount to impermissible retroactive ratemaking.

The IURC conducted a hearing on ECR 10 on December 17, 2007. On January 30, 2008, the IURC issued an order approving, inter alia, Duke's AFUDC accounting adjustment and allowing it to increase its revenue requirement for ratemaking purposes accordingly. The OUCC filed a petition for rehearing and reconsideration, which the IURC denied on April 16, 2008. This appeal followed.

Analysis

The IURC is a fact-finding body with the technical expertise to administer the utility regulatory scheme devised by the legislature. United States Gypsum, Inc. v. Indiana Gas Co., 735 N.E.2d 790, 795 (Ind. 2000). An order of the IURC is subject to appellate review to determine whether it is supported by specific findings of fact and by sufficient evidence, as well as to determine whether the order is contrary to law. Id. The IURC enjoys wide discretion on matters within its jurisdiction. Id. We will not lightly

[1] There was another accounting error that Duke sought to correct that reduced its revenue requirement by $114,000, resulting in a net revenue requirement adjustment of $1,607,000. This negative revenue requirement adjustment, while not completely irrelevant, is not directly at issue in this appeal.

override the IURC's findings and decision just because we might have reached a contrary opinion on the same evidence. Id.

I. Sufficiency of Evidence

The OUCC first contends Duke did not present sufficient evidence to support its claim of entitlement to an AFUDC accounting adjustment. When reviewing a claim of insufficient evidence to support an IURC decision, we first must determine whether the decision contains specific findings on all the factual determinations material to its ultimate conclusions. Citizens Action Coal. of Indiana, Inc. v. Northern Indiana Pub. Serv. Co., 485 N.E.2d 610, 612 (Ind. 1985). Second, we must inquire whether there is substantial evidence in light of the whole record to support the IURC's findings of basic fact. Id. We may set aside the IURC's findings of fact only if we determine, after a review of the entire record, that the agency's decision clearly lacks a reasonably sound basis of evidentiary support. Nextel West Corp. v. Indiana Util. Regulatory Comm'n, 831 N.E.2d 134, 144-45 (Ind. Ct. App. 2005), trans. denied. "In determining whether the evidence supports the IURC's decision, we neither reweigh the evidence nor substitute our judgment for that of the IURC." Spring Hills Developers, Inc. v. Reynolds Group, Inc., 792 N.E.2d 955, 958 (Ind. Ct. App. 2003).

Specifically, the essence of the OUCC's argument is that Duke failed to provide adequately detailed documentation regarding the nature and extent of the AFUDC accounting errors. We begin by noting the Federal Energy Regulatory Commission ("FERC") accounting rule, AR-13, that is at issue in this case:

> Electric (Gas) Plant Instruction no. 3(17) provides a formula for computing rates used to capitalize allowances for funds used during construction rates used to capitalize allowances for funds used during construction (AFUDC). The formula includes a component for the weighted average cost of long-term debt. The entire issue of the use-restricted long-term debt should be included with other long-term debt used in calculating AFUDC rates. Average balances of the trust or other special funds should be included in the computation of the average balance of construction work in progress (AW@) used in the formula.
>
> AFUDC assigned to the project should be determined by applying AFUDC rates to the eligible project expenditures and also balances in the trust or special funds. Fund earnings during construction should be credited to the cost of construction of the project facilities.

See http://www.ferc.gov/legal/acct-matts/docs/ar-13.asp (last visited Oct. 24, 2008). Furthermore, the IURC has adopted a regulation stating, "A utility seeking ratemaking treatment for the value of its qualified pollution control property under construction under this rule shall compute the AFUDC amounts and relevant AFUDC rates for the qualified pollution control property in accordance with the FERC or [National Association of Regulatory Utility Commissions] Uniform System of Accounts." 170 I.A.C. 4-6-13.

In her pre-filed testimony, Douglas stated in part:

> Capital project balances are cumulative amounts, consisting of all charges incurred during the life of the project. When a mistake has been made recording charges to a capital project, it is standard practice to correct the mistake, regardless of the number of accounting periods involved. [Duke]'s AFUDC amounts were calculated incorrectly since December 2003 when the company first received and deposited into an escrow account the proceeds from its first issuance of the tax exempt use-restricted bonds (for funding environmental capital

> expenditures at Duke Energy Indiana plants). Without the full correction, the cumulative project balance would remain incorrect.

Exhibits p. 153. Douglas also stated, "In the case of the AFUDC adjustment, our external auditors concurred with our corporate accounting recommendation that the adjustment should be corrected dating back to when the mistake first occurred, at the end of 2003." Id. at 151.

At the evidentiary hearing, Douglas further testified about the accounting adjustment as follows:

> There were really three things that they [the Duke accounting department] changed. One was changing the rate to incorporate the balances of the trust fund in the calculation. They also computed AFUDC on the balance of the trust fund, and they also credited the pollution control project balance amounts with the amount of interest that was earned in the trust fund all per the FERC guidance on how AFUDC should be calculated when trust funds are involved.

Tr. p. 24. Douglas also submitted an exhibit breaking down the amount of improperly excluded AFUDC that could have been claimed in each ECR proceeding dating back to June 2004 if the FERC accounting guideline had been followed. Finally, Duke submitted more detailed documentation regarding the AFUDC calculations in off-the-record meetings with the OUCC.

The OUCC argues that the foregoing was insufficient to prove that there was any actual AFUDC miscalculation or the accuracy of the amount Duke claimed. We agree that, in theory, Duke could have provided to the IURC more thoroughly detailed

accounting documentation regarding the AFUDC corrections, and not just to the OUCC during off-the-record meetings. However, the OUCC does not direct us to any requirement that such documentation was necessary. Instead, we conclude the OUCC is requesting that we reweigh evidence, which we cannot do.

Douglas testified that Duke's accountants made mistakes regarding calculation of AFUDC dating back to December 2003; that such mistakes were inconsistent with FERC AR-13; and that Duke's outside auditors agreed that the mistakes had been made and should be corrected. She also specified the three accounting changes that had been made to rectify the prior mistakes, and indicated that if the mistakes were not corrected, Duke's capital project balances would remain inaccurate. The total amount of improperly excluded AFUDC since December 2003 was provided to the IURC. This was a reasonably sound evidentiary basis sufficient to support the IURC's determination regarding the AFUDC accounting adjustment.[2]

II. Alleged Retroactive Ratemaking

Next, we address the OUCC's argument that the IURC permitting Duke to claim AFUDC in ECR 10, based on accounting errors that occurred in previous years, amounts to retroactive ratemaking. The OUCC relies upon Indiana Code Section 8-1-2-68, which states:

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[2] We further observe that in the OUCC's own proposed order in ECR 10 that it submitted to the IURC, it stated, "We note that the OUCC did not challenge the accuracy of the calculations to correct the accounting errors, or that the methodology that Petitioner used to calculate the AFUDC for the QPCP was proper." App. p. 33. Rather, the proposed order focused solely upon whether the AFUDC correction amounted to retroactive ratemaking. The OUCC's current attack on the sufficiency of the evidence for the AFUDC correction is inconsistent with its proposed order to the IURC.

> 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).

Interpreting this statute, this court has held:

> We find nothing in the statute giving the Commission the power to cancel, or to fix, rates retroactively. The statute provides the Commission with the power to fix rates for the future if it finds the rates in effect to be unreasonable or unjust; but we look in vain to find statutory authority for the Commission to fix rates for the past. The Commission has no powers except those conferred by statute.

Indiana Tel. Corp. v. Public Serv. Comm'n of Indiana, 131 Ind. App. 314, 340, 171 N.E.2d 111, 124 (1960). Put another way, "Past losses of a utility cannot be recovered from consumers nor can consumers claim a return of profits and earnings which may appear excessive." Indiana Bell Tel. Co., Inc. v. Office of Util. Consumer Counselor, 717 N.E.2d 613, 625 (Ind. Ct. App. 1999), modified on rehearing on other grounds, 725 N.E.2d 432 (Ind. Ct. App. 2000). The general purposes of the rule against retroactive ratemaking include enhancing "utility planning, investor confidence, utility credit rating, and the integrity of service." Alaska Pub. Utils. Comm'n v. Municipality of Anchorage, 902 P.2d 783, 788 (Alaska 1995).

We agree with Duke that this is not the type of situation that should be controlled by the rule against retroactive ratemaking.[3] What occurred in this case is that Duke, in previously mis-stating its AFUDC balances in ECRs 4 through 9 between June 2004 and December 2006, failed to comply with FERC accounting guidelines. This resulted in an erroneous stating of the total project balances of Duke's under-construction QPCP. It would appear that if Duke had not made this accounting correction in the ECR 10 proceeding, the capital balances for those projects would continue to be erroneous in the future. Duke chose instead to correctly state the total AFUDC that should have been calculated according to FERC guidelines. Additionally, the IURC has adopted a regulation that AFUDC "shall" be computed according to FERC accounting guidelines. See 170 I.A.C. 4-6-13. More generally, the IURC also has enacted a regulation explicitly adopting by reference all FERC "rules and regulations governing the classification of accounts for all major private electric utilities . . . ." 170 I.A.C. 4-2-1.1.

This was not a situation in which either Duke's expenses or revenues greatly exceeded expectations at the time of a prior rate proceeding, in which case Duke clearly would not be entitled to recoup its losses or Duke's customers would not be entitled to a refund. Instead, Duke was attempting to bring its accounts into compliance with FERC and IURC regulations. We also fail to perceive how permitting Duke to make this accounting correction would negatively affect utility planning, investor confidence,

[3] Duke also contends that Indiana Code Section 8-1-2-68 does not apply in this case because it concerns special ratemaking treatment for clean energy technology, which is governed by different statutes. We need not address this argument because of our conclusion that the IURC's order does not violate the general prohibition against retroactive ratemaking.

utility credit rating, or integrity of service. If Duke was seeking retroactive ratemaking, it would have recalculated its CWIP/AFUDC amount for ECRs 4 through 9, calculated the rates it could have charged in each of those proceedings, and sought to recoup the difference from current customers. Instead, Duke is just now accurately valuing its QPCP investment for the entirety of the project, and seeking current rates based on that correct value.

The OUCC also asserts that Duke is overstating its case when it claims that its prior AFUDC accounting clearly violated FERC guidelines. In addition to AR-13, mentioned earlier, the OUCC directs our attention to FERC's Electric Plant Instruction 17(3), upon which AR-13 is based and which states in part that claimed AFUDC is "not to exceed, without prior approval of the Commission, allowances computed in accordance with the formula prescribed . . . ." See Amendments to Uniform System of Accounts for Public Utilities and Licensees and for Natural Gas Companies (Classes A, B, C and D) to Provide for the Determination of Rate for Computing the Allowance for Funds Used During Construction and Revisions of 57 F.P.C. 608, 614, 1977 WL 16195. The OUCC contends that because Duke's accounting errors did not cause its claimed AFUDC to exceed the permissible amount, but instead fell below the permissible amount, Duke should not now be permitted to correct this mistake.

We defer substantially to the IURC on its decisions concerning accounting methods for utilities. The IURC "has the authority to determine accounting practices for rate regulated companies, and so long as they are within reason and prudence, courts may

not interfere." Indiana Gas Co., Inc. v. Office of Util. Consumer Counselor, 675 N.E.2d 739, 747 (Ind. Ct. App. 1997), trans. denied. Here, Duke contended and the IURC found that it had not computed AFUDC "in accordance with the formula prescribed" by FERC and the IURC. The Indiana Code requires utilities "to keep and render its books, accounts, papers and records accurately and faithfully in the manner and form prescribed by the commission . . . ." Ind. Code § 8-1-2-12. We conclude it is immaterial that Duke's accounting errors resulted in AFUDC that fell below, rather than above, the maximum permitted by FERC guidelines. Either way, the accounting did not comply with those guidelines and, by extension, IURC regulations.

Also, as noted by Duke and the IURC, retroactive correction of accounting errors can, and sometimes does, cut both ways. Generally the OUCC does not object to retroactive corrections that benefit consumers. It did not in this case, with respect to an accounting adjustment that resulted in an $114,000 decrease in Duke's revenue requirement, nor did it to an accounting adjustment that benefited consumers in ECR 9. The OUCC's failure to object in these situations may be logical, given that the OUCC's statutory mandate is to represent ratepayers, consumers, and the public, not utilities. See I.C. § 8-1-1.1-4.1(a). It strikes us as inconsistent to allow retroactive accounting corrections when they benefit consumers, but not when they benefit a utility. The OUCC attempts to distinguish these other corrections on the basis that they were legally required; we believe the AFUDC correction was also equally required, by the Indiana Code, the Indiana Administrative Code, and FERC guidelines.

The OUCC further contends that the IURC violated one of its own regulations when it permitted the AFUDC accounting adjustment. Specifically, it notes the following:

> A utility that receives ratemaking treatment under this rule for the value of its qualified pollution control property under construction shall not accrue AFUDC amounts for the qualified pollution control property under construction receiving such ratemaking treatment as of the date the commission issues its order granting the ratemaking treatment.

170 I.A.C. 4-6-20. The OUCC argues that under this rule, once the IURC calculated CWIP figures for Duke's QPCP in ECRs 4 through 9, which figures would have included Duke's erroneous AFUDC calculations, the IURC was absolutely prohibited from recalculating the appropriate AFUDC amount for that time period.

The IURC interpreted its own regulation very differently. In its order, it stated that the purpose of this regulation was to "avoid double recovery of costs, not to prohibit corrections of past mistakes." App. p. 15. Because the AFUDC amounts Duke was seeking to collect had not been accounted for in any previous ECR proceeding, the IURC concluded Duke was not prohibited from currently seeking CWIP ratemaking treatment for these amounts in the ECR 10 proceeding.

"Our supreme court has repeatedly said that 'when the meaning of an administrative regulation is in question, the interpretation of the administrative agency is given great weight unless the agency's interpretation would be inconsistent with the regulation itself.'" Citizens Action Coal. of Indiana, Inc. v. Northern Indiana Pub. Serv.

Co., 804 N.E.2d 289, 301 (Ind. Ct. App. 2004) (quoting State Bd. Of Registration for Prof. Eng'rs v. Eberenz, 723 N.E.2d 422, 427-28 (Ind. 2000)). The IURC's interpretation of this regulation is not inconsistent with the regulation itself. The regulation does not appear to contemplate a situation like this one, where there has been a mistake in computing AFUDC amounts. Rather, it clearly operates under the assumption that AFUDC was properly calculated and included in CWIP in the first place. In that type of situation, the regulation would prohibit a utility from continuing to accrue AFUDC on the project.

Here, the AFUDC Duke now seeks to include in CWIP had never been previously accounted for. We defer to the IURC's interpretation of a regulation it drafted and adopted in agreeing that the regulation did not prohibit retroactive correction of this accounting mistake. We cannot say the IURC was required to allow Duke to make the retroactive accounting adjustment, but neither can we say it was prohibited from doing so. Instead, we believe it was uniquely a matter within the IURC's discretion to decide whether to do so, and it acted accordingly.

Conclusion

There is substantial evidence in the record to support the IURC's decision, which does not amount to impermissible retroactive ratemaking. We affirm.

Affirmed.

FRIEDLANDER, J., and DARDEN, J., concur.