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May 25, 2018

General Counsel Beth E. Heline
Indiana Utility Regulatory Commission
101 West Washington Street, Suite 1500 E
Indianapolis, IN 46204

Re: GAO 2017-3: Backup, Maintenance, and Supplemental Power Rate Review

Dear Ms. Heline:

Indiana Michigan Power Company ("I&M" or the "Company") submits these Reply Comments in response to the comments filed in this proceeding by the Midwest Cogeneration Association ("MCA"), the Alliance for Industrial Efficiency ("Alliance"), and the Indiana Industrial Energy Consumers, Inc. ("INDIEC," and collectively with MCA and the Alliance, the "Commenters").

I&M supports the state policy to encourage cogeneration facilities, *see* IC 8-1-2.4-1, and recognizes the need to balance this policy with other state policies, such as the utility requirement to "furnish reasonably adequate service and facilities," to assess charges that are "reasonable and just," and to "avoid discrimination in rates." IC 8-1-2-4. Indeed, IC 8-1-2.4-4 specifically requires that "supplemental or backup power to alternate energy production facilities, cogeneration facilities, or small hydro facilities" be offered "on a nondiscriminatory basis and at just and reasonable rates."

I&M has implemented these state policies by offering a number of options for backup, maintenance, and supplemental service for customers with generation, and I&M's current offerings are appropriate. For customers with generation less than 100 kW,

I&M offers two tariff options, its Tariff COGEN/SPP (Cogeneration and/or Small Power Production Service) and Rider NMS (Net Metering Service Rider). For customers with generation greater than 100 kW, I&M permits service under the otherwise-applicable I&M tariff, and I&M also offers customized solutions for backup, maintenance, and supplemental service by means of special contracts.

Special contracts are appropriate because they allow I&M and the customer to discuss and design backup, maintenance, and supplemental rates based on the customer's individual usage patterns and the unique characteristics of the customer's generation system. Special contracts also allow I&M and its customers to structure backup, maintenance, and supplemental rate solutions that are unique to I&M's own cost structure, RTO requirements, and service territory. The Commenters incorrectly claim that I&M's approach has "discouraged" investment in cogeneration projects. In fact, I&M has successfully worked with customers to develop special contracts for backup, maintenance, and supplemental service that have allowed cogeneration projects to go forward. In I&M's experience, the primary reason that cogeneration projects do not go forward is not utility rates, but rather the substantial upfront capital costs and long-term commitment to facilities that these projects require. There is no basis for concluding that I&M's backup, maintenance, and supplemental service rates are inadequate or unreasonable.

I. I&M Offers Just and Reasonable Rates for Backup, Maintenance, and Supplemental Service

I&M's backup, maintenance, and supplemental service offerings are just and reasonable. As explained above and in I&M's initial comments, I&M offers multiple options for customers with generation facilities less than 100 kW, including its Tariff

COGEN/SPP (Cogeneration and/or Small Power Production Service) and Rider NMS (Net Metering Service Rider), which the Commenters ignored. For customers with generation greater than 100 kW, I&M offers two options. First, I&M offers customized solutions for backup, maintenance, and supplemental service by means of Commission-approved special contracts. I&M has previously implemented two such special contracts for customers with generation greater than 100 kW. Second, customers with generation may take service under the otherwise-applicable I&M tariff with an additional provision modifying the customer's demand charge.

The value of addressing backup, maintenance, and supplemental service rates through special contracts is that special contracts account for the unique characteristics of each customer's load and generation. As INDIEC notes (at 3), cogeneration facilities are "tailored to meet the specific needs of a customer." In the same vein, a utility's backup, maintenance, and supplemental power rates should be "tailored to meet" the customer's specific situation. Cogeneration facilities come in myriad configurations and can vary widely in characteristics such as generating capacity, energy production, and the frequency and duration of planned and unplanned outages, just to name a few. These characteristics depend on the specifications and reliability of the cogeneration system and how the customer operates it in connection with its regular operations. A special contract allows I&M and the customer considering cogeneration projects to discuss the customer's individual needs and set backup, maintenance, and supplemental rates based on the unique characteristics of the customer's cogeneration system – and to do so in a way that is fair for both the cogeneration customer and all of I&M's other customers.

Special contracts tailored to an individual cogeneration customer can ensure that costs are not shifted to I&M's other customers, resulting in unjust subsidies. For instance, through a special contract, a cogeneration customer can coordinate its planned outages with I&M. This allows cogeneration customers to considerably reduce their demand charges while at the time allowing I&M to manage its system in order to reduce I&M's costs of providing maintenance service. Cogeneration customers can also contract with I&M for a specific number of backup hours for unplanned outages. Unplanned outage rates vary considerably based on the type of system and the customer's maintenance practices, so allowing the customer to negotiate for a specific number of backup hours for unplanned outages ensures that the customer receives the amount of backup service that it needs for its system while also ensuring that I&M's cost of providing this backup service is appropriately reflected in rates.

MCA (at 7) critiques I&M's approach of using special contracts for backup, maintenance, and supplemental service by claiming that it causes a "lack of transparency" and "makes it impossible to evaluate whether contracted rates are non-discriminatory." As for the alleged "lack of transparency," I&M communicates with its customers often and is always willing to discuss options for a special contract for backup, maintenance, and supplemental rates. MCA does not suggest otherwise. As for "evaluat[ing] whether contracted rates are non-discriminatory," MCA overlooks the fact that special contracts are submitted to the Commission. The Commission and any parties granted intervention have every opportunity to ensure that special contracts for backup, maintenance, and supplemental service are non-discriminatory.

If a customer does not want to negotiate a special contract, it may take service under the otherwise-applicable I&M tariff with an additional tariff provision that modifies the customer's demand charge so that the "the billing demand each month shall be the highest determined for the current and previous two billing periods." This is equitable because it provides a simple alternative to a specific contract for backup, maintenance, and supplemental service while recognizing that there are additional costs imposed on the utility to stand ready to provide backup and maintenance and have facilities sized to meet the customers' unique increase in demand resulting from generator outages. Nonetheless, as noted above, I&M encourages customers to work with I&M to enter into special contracts in order to tailor the customer's demand charges to reflect the actual planned and unplanned outages the customer expects.

II. I&M's Rates Have Appropriately Encouraged Investment in Cogeneration Facilities

The Commenters claim that I&M's rates for backup, maintenance, and supplemental service have discouraged customers from developing cogeneration projects. The fact is, as the Commenters acknowledge, I&M has successfully negotiated and received approval for two special contracts providing customer-specific backup, maintenance, and supplemental service rates for customers with generation.

In I&M's experience, backup, maintenance, and supplemental power rates are not an impediment to the development of cogeneration projects. Instead, the main reason customers do not go forward with such projects is the large upfront capital costs that the customer must incur. Manufacturing processes are already highly capital-intensive ventures, and the addition of a cogeneration facility requires even further capital investment and a long-term commitment to the facility that many customers do not wish

to make. I&M's discussions with customers have led to solutions that enabled customers to go forward with cogeneration projects; there is no basis for concluding that backup, maintenance, and supplemental power rates stand in the way of cogeneration project development.

III. The Commenters' Approach to Demand Charges Is Flawed

The Commenters make a number of comments on how to design backup, maintenance, and supplemental service rates. As an initial matter, the Commenters' comments are in the form of general "policy suggestions" (INDIEC Comments at 10) and do not address how their "policy suggestions" would be applied to specific tariffs, be reflected in a cost-of-service study, or impact other customers. This exemplifies a problem with attempting to address backup, maintenance, and supplemental service rates through a generic proceeding. Rate design is best determined in individual rate cases for each utility so that it can be based on the specific costs and customer characteristics of each utility. A state-wide review of backup, maintenance, and supplemental power tariffs would be an inefficient and unnecessary approach to reviewing tariffs that must reflect each utility's unique cost structure, RTO requirements, and service territory. Thus, each utility's backup, maintenance, and supplemental service rates should be reviewed in individual proceedings, such as I&M's recent base case (Cause No. 44967), not through a "one-size-fits-all" generic proceeding.

In addition, many of the Commenters' general suggestions are flawed and do not accurately reflect the true costs a utility incurs to provide backup, maintenance, and supplemental service for cogeneration customers. INDIEC notes that cogeneration projects can help reduce costs and thus have benefits for all of I&M's customers. While that may be true, backup, maintenance, and supplemental service rates can also shift

costs from cogeneration customers to other customers and can leave other customers responsible for charges related to utility infrastructure built to serve the cogeneration customer.

Most of the Commenters' criticisms involve the calculation of demand charges – the Commenters believe that demand charges for cogeneration customers should be calculated differently from other customers. However, the Commenters' points rest on false assumptions about the character of the service that utilities must provide. For instance, INDIEC incorrectly argues (at 6) that backup, maintenance, and supplemental service rates "should not, indeed cannot, treat customers with private energy projects as though they were full requirements customers." The fact is that *all* of a utility's retail customers are "full requirements" customers, including customers with generation, because the utility ultimately retains an obligation to provide electric service to these customers no matter how much of their load they are self-serving through "private energy projects." Essentially, INDIEC's claim assumes that cogeneration customers require only "non-firm" backup, maintenance, and supplemental service, but this is not the case. Customers with generation have no obligation to keep their systems online and generating, and when customer-owned generation goes offline – whether through planned maintenance outages or unplanned equipment failures – the utility must stand ready to serve the customer's full load. Thus, no matter what cogeneration customers' "full requirements" happen to be in any moment (i.e., whether their generation is functioning or not), the utility must serve those customers' load.

This obligation to stand ready to serve a customer's full load is why it is equitable to cogeneration customers – and a utility's customers in general – to assess demand

charges that reflect the customer's peak load. The Commenters disfavor demand "ratchets" and similar demand charges because they believe these charges are too high and do not reflect a cogeneration customer's usage pattern. But demand charges accurately reflect the fact that the utility must stand ready – at a moment's notice – to serve a cogeneration customer's full load if the customer's generation system falls offline. As with all other customers, a utility must size its system for serving a cogeneration customer based on the customer's *peak* load, such as when the customer's generation is unavailable. Thus, as with all other customers, it is appropriate to reflect the fixed costs incurred to be ready to serve a customer's peak load with demand charges that are based on that peak load.

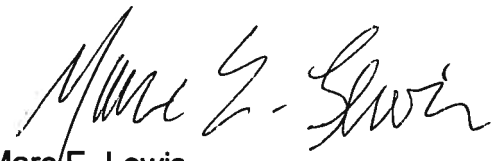
The Commenters attempt to distinguish themselves from other customers by claiming that the "load on the system necessary to serve a customer with a private energy project . . . amounts to only a fraction of the load of a full requirements customer." (INDIEC Comments at 5.) But when it comes to demand charges, customers with generation are no different from low load factor customers without generation. In both cases – whether it is due to a customer's generator going offline or a customer's load spiking – demand charges accurately measure the burden the customer places on the utility's system during times of peak demand. Further, just as low load factor customers may reduce their demand charges by carefully managing their load and reducing their peaks, customers with generation may also reduce their demand charges by managing their load and the timing of when their generation systems go offline.

In sum, I&M works with cogeneration customers to lower demand charges through special contracts in which planned outages can be coordinated with I&M and the

customer can reserve hours of peak service for unplanned outages. The Commenters' notion that customers with generation are significantly different from other customers – and should, in general, be relieved from the demand charges that other low load factor customers pay – is inaccurate and unreasonable. If that principle were followed in the way the Commenters propose, it would lead to costs inappropriately being shifted from customers with generation to all other customers.

I&M agrees that cost-of-service principles should guide the design of backup, maintenance, and supplemental power rates. These principles are being properly implemented by I&M, with the approval of the Commission, to charge customers who require I&M's system to back up the customers' own generation for the costs incurred to meet that demand.

Respectfully submitted,



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