STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF INDIANAPOLIS POWER & LIGHT COMPANY ("IPL") FOR AUTHORITY TO INCREASE RATES AND CHARGES FOR ELECTRIC UTILITY SERVICE AND FOR APPROVAL OF: (1) ACCOUNTING RELIEF, INCLUDING IMPLEMENTATION OF MAJOR STORM DAMAGE RESTORATION RESERVE ACCOUNT; (2) REVISED DEPRECIATION RATES; (3) THE INCLUSION IN BASIC RATES AND CHARGES OF THE COSTS OF CERTAIN PREVIOUSLY APPROVED QUALIFIED POLLUTION CONTROL PROPERTY; (4) IMPLEMENTATION OF NEW OR MODIFIED RATE ADJUSTMENT MECHANISMS TO TIMELY RECOGNIZE FOR RATEMAKING PURPOSES LOST REVENUES FROM DEMAND-SIDE MANAGEMENT PROGRAMS AND CHANGES IN (A) CAPACITY PURCHASE COSTS; (B) REGIONAL TRANSMISSION ORGANIZATION COSTS; AND (C) OFF SYSTEM SALES MARGINS; AND (5) NEW SCHEDULES OF RATES, RULES ANDREGULATIONS FOR SERVICE.	**)**	**CAUSE NO. 44576**
IN THE MATTER OF THE INDIANA UTILITY REGULATORY COMMISSION'S INVESTIGATION INTO INDIANAPOLIS POWER & LIGHT COMPANY'S ONGOING INVESTMENT IN, AND OPERATION AND MAINTENANCE OF, ITS NETWORK FACILITIES	**)**	**CAUSE NO. 44602**

TESTIMONY OF

LAFAYETTE MORGAN – PUBLIC’S EXHIBIT NO. 6

ON BEHALF OF THE

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

JULY 27, 2015

PUBLIC'S EXHIBIT NO. 6

BEFORE THE

INDIANA UTILITY REGULATORY COMMISSION

INDIANAPOLIS POWER AND LIGHT COMPANY	))	**CAUSE NOS. 44576/44602**

DIRECT TESTIMONY

OF

LAFAYETTE K. MORGAN, JR.

ON BEHALF OF THE

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

JULY 27, 2015

EXETER

ASSOCIATES, INC.
10480 Little Patuxent Parkway
Suite 300
Columbia, Maryland 21044

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TESTIMONY OF LAFAYETTE K. MORGAN, JR.
CAUSE NOS. 44576/44602
INDIANAPOLIS POWER AND LIGHT COMPANY

Qualifications

Q. Would you please state your name and business address?

A. My name is Lafayette K. Morgan, Jr. My business address is 10480 Little Patuxent Parkway, Suite 300, Columbia, Maryland 21044. I am a Public Utilities Consultant working with Exeter Associates, Inc. (Exeter). Exeter is a firm of consulting economists specializing in issues pertaining to public utilities.

Q. Please describe your educational background.

A. I received a Master of Business Administration degree from The George Washington University. The major area of concentration for this degree was Finance. I received a Bachelor of Business Administration degree with concentration in Accounting from North Carolina Central University. I was previously a CPA licensed in the state of North Carolina, but elected to place my license in an inactive status as I pursued other business interests.

Q. Would you please describe your professional experience?

A. From May 1984 until June 1990, I was employed by the North Carolina Utilities Commission – Public Staff in Raleigh, North Carolina. I was responsible for analyzing testimony, exhibits, and other data presented by parties before the North Carolina Utilities Commission. I had the additional responsibility of performing the examinations of books and records of utilities involved in rate proceedings and summarizing the results into testimony and exhibits for presentation before that Commission. I was also involved in numerous special projects, including participating in compliance and prudence audits of a major utility and conducting research on several issues affecting natural gas and electric utilities.

From June 1990 until July 1993, I was employed by Potomac Electric Power Company (Pepco) in Washington, D.C. At Pepco, I was involved in the preparation of the cost of service, rate base, and ratemaking adjustments supporting the company's requests for revenue increases in the State of Maryland and the District of Columbia. I also conducted research on several issues affecting the electric utility industry for presentation to management.

From July 1993 through 2010, I was employed by Exeter as a Senior Regulatory Analyst. During that period, I was involved in the analysis of the operations of public utilities, with particular emphasis on utility rate regulation. I reviewed and analyzed utility rate filings, focusing primarily on revenue requirements determination. This work involved natural gas, water, electric, and telephone companies.

In 2010, I left Exeter to pursue other business interests. In late 2014, I returned to Exeter to continue to work in a similar capacity to my work prior to my hiatus.

Q. Have you previously testified in regulatory proceedings on utility rates?

A. Yes. I have previously presented testimony and affidavits on numerous occasions before the North Carolina Utilities Commission, the Pennsylvania Public Utility Commission, the Virginia Corporation Commission, the Louisiana Public Service Commission, the Georgia Public Service Commission, the Maine Public Utilities Commission, the Kentucky Public Service Commission, the Rhode Island Public Utilities Commission, the Vermont Public Service Board, the Illinois Commerce Commission, the Indiana Utility Regulatory Commission, the West Virginia Public

Service Commission, the Maryland Public Service Commission, and the Federal Energy Regulatory Commission (FERC).

Q. On whose behalf are you appearing?

A. I am presenting testimony on behalf of the Indiana Office of Utility Consumer Counselor (OUCC).

Purpose and Conclusion

Q. What is the purpose of your testimony?

A. Exeter has been asked by the OUCC to review the reasonableness of the level of revenues that Indianapolis Power and Light Company (IPL or Petitioner) is proposing to charge its customers. As part of an Exeter team, our assignment in this proceeding was to examine and investigate Petitioner's revenue requirements, and to present the findings regarding IPL's test year rate base and net operating income at present rates. In developing my recommendations with regard to net operating income, I have incorporated the recommendations of the OUCC's other witnesses regarding certain adjustments to revenues and expenses. Based on my findings, I have determined the revenues that are required to generate the OUCC's recommendation regarding the overall rate of return on rate base.

Q. Have you prepared schedules to accompany your testimony?

A. Yes, I have. Schedules LKM-1 through LKM-18 are attached to my testimony. These schedules present my findings and recommendations regarding Petitioner's test year revenue requirements.

Q. Please summarize your findings regarding Petitioner's revenue requirement.

A. IPL has requested an increase in base rate revenues of $67,774,000. As shown on page 1 of Schedule LKM-1, I have determined that IPL has a base rate revenue deficiency of $5,916,000 for the test year ended June 30, 2014. This is the amount by which revenues are less than the amount necessary to generate the OUCC's recommended overall rate of return of 6.26 percent after accounting for the OUCC's adjustments to IPL's claimed rate base and operating income. The return of 6.26 percent represents the OUCC's recommendation regarding Petitioner's overall rate of return on rate base, taking into account OUCC witness Edward Kaufman's recommended return on equity. Page 2 of Schedule LKM-1 shows the derivation of the revenue deficiency that I have identified and provides a comparison of the OUCC's overall recommendation with IPL's request.

Schedule LKM-2 summarizes my adjustments to IPL's proposed test year rate base. Schedule LKM-3 provides a summary of my adjustments to test year revenues and expenses and the resulting net operating income at present rates. Schedules LKM-4 through LKM-18 present each of the adjustments to IPL's claimed rate base and net operating income that I have incorporated in developing the OUCC's recommended revenue requirement. Schedule LKM-18 presents the OUCC's capital structure and overall rate of return.

Q. How is the remainder of your testimony organized?

A. In the remainder of my testimony, I document and explain each of the adjustments to rate base and net operating income that I have made to arrive at the test year revenue deficiency shown on Schedule LKM-1. My discussion of these adjustments is organized into sections corresponding to the issue being addressed. These sections are set forth in the Table of Contents for this testimony.

Prepaid Pension Asset

Q. Please explain the adjustment you made to remove the prepaid pension asset Petitioner included in rate base.

A. IPL included the balance of its prepaid pension asset, net of the balance of the OPEB[1] liability, in its original cost rate base. As recommended by OUCC witness Margaret Stull, I removed the prepaid pension asset, net of IPL's OPEB liability, from rate base. The elimination of this balance of $138,461,000 from rate base is shown on the rate base summary presented on Schedule LKM-2.

Off System Sales Margins

Q. Please explain the adjustment to off system sales margins shown on Schedule LKM-4.

A. I have adjusted off system sales (OSS) margins to reflect the amount recommended by OUCC witness Stacie Gruca. Ms. Gruca is recommending that the credit for OSS margins embedded in base rates be set at a level of $9,488,000 instead of $6,324,000 as proposed by IPL. As shown on Schedule LKM-4, this results in an increase in OSS margins of $3,164,000.

[1] Post-retirement benefits other than pension or other post-employment benefits pursuant to what has traditionally been known as SFAS No. 106, now ASC 715.

IPL Employee Vacancies

Q. Please summarize how IPL developed its *pro forma* claim for base salaries and wages for IPL employees.

A. Petitioner developed its claim for base salaries and wages by annualizing wages for all employees as of June 30, 2014. To this amount, IPL added annualized wages for an additional 36 vacant or open positions as of that date. The total annualized wages as of June 30, 2014 were then further adjusted to account for wage increases scheduled to occur through June 30, 2015.

Q. Do you agree with Petitioner's inclusion of vacant positions in determining *pro forma* base salaries and wages?

A. No. It is inappropriate to include the wages and benefits for the 36 vacant positons because it is unreasonable to assume that a full complement of employees will exist throughout the year. That is, because employee turnover occurs continually due to a variety of factors, such as retirement, employees moving or accepting new jobs, and termination for cause, there will always be unfilled postions for which IPL will be incurring no wage expense. Therefore, wages and benefits for those positons should not be included in *pro forma* expenses.

Q. Has IPL's workforce increased since June 30, 2014, thereby indicating that these 36 vacant positions have been filled during the 12-month period following the test year?

A. No. IPL's workforce has decreased subsequent to the end of the test year. According to the response to OUCC Data Request 5-27, there were 1,411 employees as of June 2014. The number of employees since that time (through January 2015) has been less than 1,411 in every month and has averaged 1,403 employees.

Q. What adjustment are you proposing to make to account for employee vacancies?

A. I have adjusted test year wages and benefits to exclude the *pro forma* wages and benefits for the 36 vacant positions that IPL included in *pro forma* operation and maintenance (O&M) expense for IPL employees. I have also adjusted the associated FICA taxes. As shown on Schedule LKM-5, this adjustment reduces wages and benefits by $3,076,000 and reduces payroll taxes by $235,000.

Q. Do you have any additional comments on your adjustment?

A. Yes. As noted above, the employee data that IPL provided in discovery only includes information through January 2015. To the extent IPL provides updated data that demonstrates it has increased employees above the 1,411 that existed as of June 30, 2014, I am prepared to review that information and revise my adjustment as appropriate.

AES U.S. Services Employee Vacancies

Q. Please explain your adjustment related to AES U.S. Services, LLC employee vacancies.

A. Similar to the manner in which it developed its claim for base salaries and wages for its own employees, IPL projected base salaries and wages for AES U.S. Services, LLC (AES U.S. Services) employees by annualizing wages as of June 30, 2014 for all employees plus open positions as of that date. These wages were then adjusted to account for wage increases scheduled to occur through June 30, 2015. As with my adjustment for vacant IPL employee positions, I have adjusted IPL's claim to eliminate the wages and benefits for the eight vacant positions included by IPL for AES U.S. Services employees.

Q. How does the number of AES U.S. Services employees subsequent to June 30, 2014 compare to the number of employees as of June 30, 2014?

A. According to the response to OUCC DR 5-37, AES U.S. Services had 361 employees as of June 2014. The number of employees since that time (through January 2015) has been less than 361 in every month and has averaged 350 employees. Accordingly, adjusting to exclude the eight vacant positions claimed by IPL is conservative.

Q. What is the effect of your adjustment on *pro forma* O&M expense?

A. As shown on Schedule LKM-6, adjusting *pro forma* O&M expense to exclude the wages and benefits for the eight vacant positions that IPL included in *pro forma* expense for AES U.S. Services employees reduces expenses by $572,000. The associated reduction in payroll taxes (FICA) is $44,000. As with my adjustment for IPL employee vacancies, I am prepared to reevaluate my recommendation if IPL provides additional monthly data that demonstrates AES U.S. Services employee levels increased above the 361 that existed as of June 30, 2014.

<u>Overtime Expense</u>

Q. How did IPL develop the allowance for overtime wages included in its *pro forma* wage claim?

A. IPL developed its projection of overtime wages included in *pro forma* salaries and wages on the number of overtime hours experienced during the test year ending June 30, 2014, excluding plant outage and storm related overtime, which were separately accounted for in IPL's plant outage and storm related adjustments. The cost associated with the test year overtime hours was adjusted to reflect wage increases through June 30, 2015.

Q. What adjustment are you proposing to make to overtime expense?

A. During the test year ended June 30, 2014, IPL employees worked 339,006 hours of overtime, excluding plant outage and storm related overtime. This level of overtime is well in excess of the hours incurred in recent years, including the two calendar years that the test year overlaps. In particular, overtime in the test year ended June 30, 2014 was substantially greater than both the 254,881 hours of overtime excluding plant outage and storm related hours incurred in 2013 and the 277,992 hours of non-plant outage, non-storm related overtime experienced in 2014.[2] These data demonstrate that the level of overtime experienced during the test year is abnormally high. In order to reflect a normal level of overtime expense, I am proposing to adjust overtime to reflect a three-year average number of hours based on the three most recent calendar years (2012 through 2014).

Q. What is the effect of this adjustment on *pro forma* overtime expense?

A. Schedule LKM-7 presents my adjustment to overtime expense. As shown there, adjusting overtime expense to reflect the average number of overtime hours over the three-year period from 2012 through 2014 results in a reduction of overtime expense of $3,732,000. The associated reduction in FICA taxes is $285,000.

Q. Do you have any comments regarding the calculation of your adjustment?

A. Yes. I would like to point out that in calculating my adjustment, I did not include any change in overtime by non-union employees. Although the test year level of overtime for non-union employees was above the three-year average, the test year non-union overtime included amounts for retirees and terminations which IPL eliminated. Accordingly, I accepted IPL's claim for non-union employees.

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[2] Overtime hours are per the responses to OUCC DR 5-35 and OUCC DR 15-06.

Incentive Compensation Expense

Q. Please explain the adjustment to incentive compensation expense incorporated in the determination of IPL's revenue requirements.

A. IPL's *pro forma* expense claim includes the cost of two incentive compensation plans. The first is the Short-Term Compensation (STC) plan under which compensation is based on performance as measured by the achievement of safety, financial, operation, and enterprise-wide objectives. All employees are eligible for the STC.

The second incentive plan is the Long-Term Compensation (LTC) plan. The LTC applies only to Senior Management employees and consists of two components—Performance Units and Restricted Stock Units. Performance Units make up 50 percent of the LTC and are awarded based on achieving a targeted Adjusted EBITDA (Earnings Before Income Taxes, Depreciation, and Amortization). Restricted Stock Units make up the other 50 percent of the total LTC award and are not subject to meeting performance goals.

Q. Do these incentive plans apply to both IPL and AES U.S. Services employees?

A. Yes. Both IPL and AES U.S. Services employees are eligible for the STC and LTC plans and the Petitioner's *pro forma* expense claims include STC and LTC expense for both IPL and AES U.S. Services employees.

Q. Which IPL and AES U.S. Services employees are eligible for the Long-Term Compensation Plan?

A. In response to OUCC Data Request 5-08, IPL stated that a combined total of only 143 IPL and AES U.S. Services employees are eligible to receive benefits under the LTC plan. These 143 employees must be a salary grade 19 or above according to the response to OUCC Data Request 5-11.

Q. Did IPL recognize that the full amount of the costs of the LTC are not fully recoverable from ratepayers?

A. Yes. In its filing, IPL excluded 10 percent of the LTC plan costs for IPL employees from its *pro forma* expense claim. In response to OUCC DR 15-5, IPL indicated that its rationale for excluding 10 percent of LTC costs "…is that, for long-term compensation to be includable in ratemaking, we understand that a portion of the cost must be allocated to shareholders." The response went on to indicate that "there was no computational basis for choosing 10%, but we believe 10% is reasonable and satisfies the standard."

Q. Do you agree with IPL's proposal to eliminate only 10 percent of LTC plan costs?

A. No. I am proposing to adjust the amount included in rates for LTC plan compensation to exclude the Performance Shares component for both IPL and AES U.S. Services employees. The effect of this adjustment is to eliminate approximately 50 percent of LTC plan expense from rate recovery.

Q. What is the basis for your recommendation?

A. As noted previously, the Performance Shares component of LTC plan compensation is based solely on corporate financial performance as measured by Adjusted EBITDA. These awards are not properly recoverable from ratepayers for several reasons. First, if the financial goals are set properly, achieving the necessary performance should be self-supporting. That is, measures that achieve additional cost savings, improve sales, or otherwise improve the financial results of the Petitioner should provide the income necessary to fund the awards. Second, the payouts are made independent of the quality of service, efficiency, or safety goals. Finally, the incentive to improve financial performance is not necessarily consistent with ratepayers' interests.

Q. Are you proposing any adjustment to IPL's claimed STC plan expense?

A. No. I have accepted the full claim for STC plan payments because those appear to be primarily a function of meeting quality of service, efficiency, and safety goals even though financial goals must be met at the 80 percent level for any STC (and LTC) awards to be made.

Q. Have you prepared a schedule that shows the calculation of your adjustment to eliminate the Performance Share component of LTC plan expense?

A. Yes. My adjustment to exclude the Performance Share component of LTC plan expense is presented on Schedule LKM-8. As indicated there, I have determined the portion of LTC plan costs attributable to Restricted Stock Units and subtracted this from IPL's *pro forma* claim for both Performance Shares and Restricted Stock Units to determine the adjustment necessary to eliminate the expense for Performance Units. As shown on this schedule, this adjustment reduces *pro forma* O&M expense by $444,000 for IPL employees and $77,000 for AES U.S. Services employees. I have also calculated the effect of these adjustments on FICA tax expense on this schedule.

Q. Do you have any other comments regarding this adjustment?

A. Yes. I would like to emphasize that I am not recommending these LTC Performance Units not be paid or that the program be discontinued. Rather, it is my position that these costs should not and need not be recovered from ratepayers because achieving the financial goals should be self-funding as well as for the other reasons discussed previously.

Employee Relocation Costs

Q. Please explain your adjustment to employee relocation costs.

A. In conjunction with the formation of AES U.S. Services at the end of 2013, IPL incurred employee relocation costs that it eliminated from its *pro forma* expense claims. In response to OUCC DR 9-01, IPL indicated that AES U.S. Services also incurred a relatively small amount of employee relocation costs for which IPL was billed its share in May 2014. However, these cost were not identified and removed from *pro forma* expenses. Consistent with IPL's adjustment to remove the relocation costs that it incurred, I have adjusted *pro forma* expenses to exclude the relocation costs included for AES U.S. Services. As shown on Schedule LKM-9, the relocation costs billed to IPL by AES U.S. Services in May 2014 was $11,000. Because January through June 2014 AES U.S. Services non-labor costs were doubled to determine the *pro forma* expense, the effect of removing these costs is to reduce *pro forma* expenses by $22,000.

Pension and OPEB Expense

Q. What adjustments have you made to the amounts that IPL has included in its claimed cost of service for pension expense and OPEB expense?

A. As noted in the prefiled testimony of IPL witness Edward J. Kunz, IPL agreed to update its claimed pension and OPEB expense when the actuarial reports for the 2014 plan year were received in February 2015. On March 12, 2015, IPL submitted these updates and I have incorporated the revised amount in my calculation of the OUCC's revenue requirement recommendation. As shown on schedule LKM-10, these updates reduce pension expense by $1,845,000 and OPEB expense by $26,000.

Uncollectibles Expense

Q. How did IPL develop its claim for uncollectibles expense?

A. In its filing, IPL adjusted test year uncollectibles expense by applying its uncollectible accounts experience rate for the 12 months ended June 2014 to *pro forma* rate year revenue at present rates. Petitioner used this same uncollectible accounts experience rate in its revenue conversion factor to account for the increase in uncollectibles expense associated with its proposed rate increase.

Q. What adjustment are you proposing to IPL's claim?

A. IPL used an uncollectible accounts experience rate of 0.3891 percent in its calculation of *pro forma* uncollectibles expense. A review of the historical data reveals that this is the highest uncollectible accounts experience rate for any 12-month period ending with January 2011 through June 2014. Uncollectibles experience varies from year to year due to economic conditions and other factors. Therefore, it is appropriate to utilize a multi-year average uncollectibles experience rate to normalize uncollectibles expense for ratemaking purposes. As shown on Schedule LKM-11, I have adjusted uncollectibles expense to reflect the average uncollectible accounts experience rate for the three years ending June 30 of 2012, 2013, and 2014. This results in an uncollectibles experience rate of 0.3259 percent. As shown on that same schedule, this results in a reduction in *pro forma* uncollectibles expense at present rates of $749,000. I have also revised the revenue conversion factor used to develop the OUCC's recommended rate increase to reflect the 0.3259 percent uncollectibles experience rate.

Storm Costs

Q. Please explain your adjustment to storm costs.

A. In his testimony, OUCC witness Wes Blakley rejects IPL's proposal to amortize a portion of test year Level 3 & 4 storm expenses over two years on the grounds that these expenses are already included in the 5.5 year average IPL used to determine its *pro forma* storm expense. As shown on Schedule LKM-12, elimination of the amortization expense as recommended by Mr. Blakley reduces *pro forma* operating expenses by $1,292,000.

MISO

Q. What adjustment to the amortization of deferred MISO costs have you incorporated in your analysis of IPL's revenue requirements?

A. In its filing, IPL has proposed that it be allowed to amortize deferred Midcontinent Independent System Operator (MISO) costs over six years. OUCC witness Blakley identifies MISO revenues earned by IPL during the deferral period. Mr. Blakley recommends these MISO revenues be properly recognized as an offset to MISO costs. I have incorporated Mr. Blakley's recommendation into my analysis of IPL's revenue requirements on behalf of the OUCC. As shown on Schedule LKM-13, this adjustment reduces IPL's proposed MISO amortization expense by $10,141,000.

Rate Case Expense Amortization

Q. Please explain your adjustment to Petitioner's claimed amortization of rate case expense.

A. As discussed in detail in the testimony of Mr. Eckert, the OUCC is proposing to reduce IPL's claimed rate case expenses to exclude certain costs that he has determined were improperly included in IPL's claim. Based on his review, Mr. Eckert is recommending an allowance for rate case expense amortization of $2,209,000 (rounded), which is $44,000 less than IPL's claim. This adjustment is presented on Schedule LKM-14.

Non-Recurring Regulatory Commission Expense

Q. What adjustment to regulatory commission expense have you included in your analysis of IPL's revenue requirements?

A. As explained in his direct testimony, Mr. Eckert is recommending that the amounts included in test year regulatory commission expense be adjusted to exclude the amounts incurred for Cause Numbers 44339 and 44478 because those amounts reflect infrequent occurring or non-recurring expenses. As shown on Schedule LKM-15, this adjustment results in a reduction in *pro forma* operating expenses of $197,000.

State Income Tax Rate

Q. Please explain your adjustment to the state income tax rate.

A. In its filing, IPL used a state income tax rate of 6.75 percent, which appears to be a blend of the 7.0 percent rate that is in effect in the 2015 fiscal year (FY) ending June 30, 2015 and the 6.50 percent rate that goes into effect on July 1, 2015 for FY 2016. Although the 6.50 percent rate does not take effect until the day after the end of the *pro forma* adjustment period on June 30, 2015, I have adjusted the state income tax rate to 6.50 percent because that is the state income tax rate that will be in effect when the rates approved in this proceeding go into effect.

Q. Have you prepared a schedule showing the effect of your adjustment?

A. Yes. Schedule LKM-16 shows the effect of reducing the state income tax rate from 6.75 percent to 6.50 percent on the state and federal income taxes included in IPL's filing. As indicated there, the effect of this reduction in the state income tax rate based on net income at present rates as reflected in IPL's filing is a reduction of $169,000 in state income tax expense. The reduction in state income taxes results in an increase in federal income taxes of $59,000, resulting in a net reduction in income tax expense at present rates of $110,000.

Q. Have you made any additional changes to reflect the effect of the reduction in the state income tax rate?

A. Yes. In calculating the after-tax net income effect of each of the OUCC's adjustments to revenue and expenses on Schedule LKM-3, I have utilized a state income tax rate of 6.50 percent. I have also included the 6.50 percent income tax rate in the gross-up factor used to calculate the required rate increase as shown on page 2 of Schedule LKM-1.

Tax Deductibility of Interest on Customer Deposits

Q. Please explain your adjustment related to the tax deductibility of interest on customer deposits.

A. Consistent with accepted practice in Indiana, IPL has included customer deposits in capital structure and has recognized those customer deposits as having a cost rate of 6.0 percent in calculating the weighted cost of capital. However, in calculating the weighted cost of debt used to calculate synchronized interest expense, IPL has not included customer deposits. As a result, IPL has failed to recognize that interest on customer deposits is tax deductible. This results in interest on customer deposits being "grossed-up" for income taxes in calculating IPL's revenue requirement. I have revised the calculation of the cost of debt used to calculate synchronized interest expense to include the weighted cost of customer deposits in order to recognize that interest on customer deposits is tax deductible.

Interest Synchronization

Q. Please explain your adjustment to synchronize interest expense.

A. To determine the interest deduction for income tax purposes, I have multiplied the OUCC's recommended rate base by the weighted cost of debt included in the OUCC's recommended capital structure. This procedure synchronizes the interest deduction for income tax purposes with the interest component of the return on rate base to be recovered from ratepayers. As shown at the bottom of Schedule LKM-17, this adjustment reduces the interest deduction by $2,546,000 compared to the synchronized interest deduction recognized by IPL. This increases state income taxes by $165,000 and federal income taxes by $833,000. I would note that I have used a state income tax rate of 6.50 percent in the calculation of this adjustment.

Capital Structure and Rate of Return

Q. Have you prepared a schedule which presents the OUCC's recommended capital structure and rate of return?

A. Yes. Schedule LKM-18 presents the OUCC's recommended capital structure and rate of return. To develop this capital structure, I utilized IPL's proposed capital structure and cost rates for all components other than the return on equity as the starting point. I then incorporated Mr. Kaufman's recommended return on equity of 9.2 percent. As shown on Schedule LKM-18, this results in an overall rate of return of 6.26 percent.

In addition to showing the OUCC's overall capital structure, I have also shown the calculation of the rate of return assigned to post-1970 Investment Tax Credits (ITCs) and the rate of return utilized for interest synchronization purposes. The calculation of the return assigned to the ITC balance differs from IPL's calculation only in the use of the OUCC's recommended return on equity in place of IPL's proposal. The synchronized interest rate differs from IPL's due to the recognition of interest on customer deposits being tax deductible, as discussed previously.

Q. Does this complete your Direct Testimony?

A. Yes, it does.

PUBLIC'S EXHIBIT NO. 6

BEFORE THE

INDIANA UTILITY REGULATORY COMMISSION

INDIANAPOLIS POWER AND LIGHT COMPANY	))	**CAUSE NOS. 44576/44602**

SCHEDULES ACCOMPANYING THE

DIRECT TESTIMONY

OF

LAFAYETTE K. MORGAN, JR.

ON BEHALF OF THE

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

JULY 27, 2015

EXETER

ASSOCIATES, INC.
10480 Little Patuxent Parkway
Suite 300
Columbia, Maryland 21044

INDIANAPOLIS POWER AND LIGHT COMPANY

Summary of Operating Income
Test Year Ended June 30, 2014
($000)

	Petitioner Amounts at Present Rates	OUCC Adjustments	Amounts per OUCC at Present Rates	Revenue Increase/ (Decrease)	Amounts After Revenue Incr. / (Decr.)
Operating Revenues					
Total Operating Revenues	$ 1,203,560	$ 3,164	$ 1,206,724	$ 5,916	$ 1,212,640
Operating Expenses					
Fuel & Purchased Power	$ 839,451	$ -	$ 839,451	$ -	$ 839,451
Other O&M Expense	-	(22,217)	(22,217)	19	(22,198)
Depreciation Expense	208,582	-	208,582	-	208,582
Taxes Other Than Income	45,115	(604)	44,511	90	44,601
State Income Taxes-Current	-	-	-	-	-
Federal Income Taxes-Current	-	-	-	-	-
State Income Taxes-Deferred	3,695	1,686	5,381	383	5,764
Federal Income Taxes-Deferred	12,608	9,396	22,004	1,898	23,902
Investment Tax Credits	(1,803)	-	(1,803)	-	(1,803)
Total Operating Expenses	$ 1,107,648	$ (11,739)	$ 1,095,909	$ 2,390	$ 1,098,299
Utility Operating Income	$ 95,912	$ 14,903	$ 110,815	$ 3,526	$ 114,341
Rate Base	$ 1,964,992		$ 1,826,531		$ 1,826,531
Rate of Return	4.88%		6.07%		6.26%

INDIANAPOLIS POWER AND LIGHT COMPANY

Determination of Revenue Increase/(Decrease)
Test Year Ended June 30, 2014
($000)

		Amount per Petitioner (1)	Amount Per OUCC	Source
Recommended Rate Base		$ 1,964,992	$ 1,826,531	Schedule LKM-2
Required Rate of Return		6.91%	6.26%	
Net Operating Income Required		$ 135,781	$ 114,341	
Fair Rate of Return Differential		386	$ -	
		$ 136,167	$ 114,341	
Net Operating Income at Present Rates		95,912	110,815	Schedule LKM-1, p.1
Net Income Surplus/(Deficiency)		$ (40,255)	$ (3,526)	
Revenue Multiplier (2)		1.6836028	1.6779667	
Base Rate Revenue Increase		$ 67,774	$ 5,916	
Verification				
Revenue Increase/(Decrease)		$ 67,774	$ 5,916	
Less: IURC Fee	0.1217%	83	7	0.1217%
Bad Debt	0.3891%	264	19	0.3259%
State Taxable Income		$ 67,427	$ 5,890	
State Income Tax	6.7500%	4,551	383	6.5000%
Indiana Utility Receipts Tax	1.4000%	945	83	1.4000%
Federal Taxable Income		$ 61,931	$ 5,424	
Federal Income Tax	35.0000%	21,676	1,898	35.0000%
Net Income Surplus/(Deficiency)		$ (40,255)	$ (3,526)	

Notes:

(1) Per IPL Financial Exhibit IPL-REVREQ, Schedule REVREQ1.

(2) Calculation of Conversion Factor	Per IPL Tax Rates	Per IPL	Per OUCC Tax Rates	Per OUCC
Revenues		1.000000		1.000000
IURC Fee	0.1217%	0.001217	0.1217%	0.001217
Bad Debt	0.3891%	0.003891	0.3259%	0.003259
Subtotal		0.994892		0.995524
Indiana Utility Receipts Tax	1.4000%	0.013946	1.4000%	0.013954
Gross Revenue Conversion Factor		0.980946		0.981570
State Taxable Income		0.994892		0.995524
State Income Tax	0.067500	0.067155	0.065000	0.064709
Net Federal Taxable Income		0.913791		0.916861
Federal Income Tax	0.35000	0.319827	0.35000	0.320901
Revenue Conversion Factor		0.5939643		0.5959594
Revenue Multiplier		1.68360281		1.67796674

INDIANAPOLIS POWER AND LIGHT COMPANY

Summary of Rate Base
Test Year Ended June 30, 2014
($000)

Description	Indiana Jurisdictional Amount per Petitioner (1)	OUCC Adjustments	Adjusted Per OUCC
Utility Plant	$ 4,533,729	$ -	$ 4,533,729
Accumulated Depreciation & Amortization	(2,835,610)	-	(2,835,610)
Net Utility Plant in Service	$ 1,698,119	$ -	$ 1,698,119
Less: Non-Jurisdictional Plant in Service	(8,970)	-	(8,970)
Accumulated Depreciation & Amortization	454	-	454
Net Utility Plant in Service	$ (8,516)	$ -	$ (8,516)
Less: Asset Retirement Obligation	(16,133)	-	(16,133)
Materials & Supplies	74,179	-	74,179
Fuel Stock Inventory	58,038	-	58,038
Regulatory Assets	20,844	-	20,844
Prepaid Pension Asset (2)	138,461	(138,461)	-
Original Cost Rate Base	$ 1,964,992	$ (138,461)	$ 1,826,531

Notes:
(1) Per IPL Financial Exhibit IPL-RB, Schedule RB1.

(2) Refer to testimony for explanation of adjustment.

INDIANAPOLIS POWER AND LIGHT COMPANY

Summary of Adjustments to Net Income
Test Year Ended June 30, 2014
($000)

	Amount	Source
Net Income per Petitioner	$ 95,912	See Note (1)
OUCC Adjustments		
Off System Sales Margins	1,923	Schedule LKM-4
IPL Employee Vacancies	2,013	Schedule LKM-5
AES US Services Employee Vacancies	374	Schedule LKM-6
Normalized Overtime Expense	2,441	Schedule LKM-7
Incentive Compensation	341	Schedule LKM-8
AES US Services Employee Relocation Costs	13	Schedule LKM-9
Pension Expense	1,121	Schedule LKM-10
OPEB Expense	16	Schedule LKM-10
Uncollectibles	455	Schedule LKM-11
Storm Costs	785	Schedule LKM-12
MISO Deferred Cost Amortization	6,163	Schedule LKM-13
Rate Case Expense Amortization	27	Schedule LKM-14
Non-Recurring Regulatory Commission Expense	120	Schedule LKM-15
State Income Tax Rate Reduction to 6.50 Percent	110	Schedule LKM-16
Interest Synchronization	(999)	Schedule LKM-17
Total OUCC Adjustments	$ 14,904	
Net Income Per OUCC	$ 110,816	

Note:
(1) Per IPL Financial Exhibit IPL-OPER, Schedule OPINC.

INDIANAPOLIS POWER AND LIGHT COMPANY

Summary of Adjustments to Net Income
Test Year Ended June 30, 2014
($000)

	Revenues	O&M Expenses	Depreciation Expense	Taxes Other Than Income	State Income Taxes	Federal Income Taxes	Net Operating Income
Net Income per Petitioner	$ 1,203,560	$ 839,451	$ 208,582	$ 45,115	$ 3,695	$ 10,805	$ 95,912
OUCC Adjustments							
Off System Sales Margins	3,164	-	-	-	206	1,035	1,923
IPL Employee Vacancies	-	(3,076)	-	(235)	215	1,084	2,013
AES US Services Employee Vacancies	-	(572)	-	(44)	40	202	374
Normalized Overtime Expense	-	(3,732)	-	(285)	261	1,315	2,441
Incentive Compensation	-	(521)	-	(40)	36	184	341
AES US Services Employee Relocation Costs	-	(22)	-	-	1	7	13
Pension Expense	-	(1,845)	-	-	120	604	1,121
OPEB Expense	-	(26)	-	-	2	9	16
Uncollectibles	-	(749)	-	-	49	245	455
Storm Costs	-	(1,292)	-	-	84	423	785
MISO Deferred Cost Amortization	-	(10,141)	-	-	659	3,319	6,163
Rate Case Expense Amortization	-	(44)	-	-	3	14	27
Non-Recurring Regulatory Commission Expense	-	(197)	-	-	13	64	120
State Income Tax Rate Reduction to 6.50 Percent	-	-	-	-	(169)	59	110
Interest Synchronization	-	-	-	-	165	833	(999)
Total OUCC Adjustments	$ 3,164	$ (22,217)	$ -	(604)	$ 1,686	$ 9,396	$ 14,904
OUCC Adjusted Net Income	$ 1,206,724	$ 817,234	$ 208,582	44,511	$ 5,381	$ 20,201	$ 110,816

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Off System Sales Margins
Test Year Ended June 30, 2014
($000)

Off System Sales Margins per OUCC (1)	$	9,488
Test Year Amount per Petitioner (2)		6,324
Adjustment to Off System Sales Margins	$	3,164

Note:
(1) Per testimony of OUCC Witness Stacie Gruca.

(2) Per IPL Financial Exhibit IPL-OPER, Schedule REV6.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Recognize IPL Employee Vacancies
Test Year Ended June 30, 2014
($000)

Salary and Benefits for 36 Vacant Positions (1)		
Salary	$	2,576
Premiums		53
Short-Term Incentive Comp		280
Total Pay Components	$	2,910
Life		10
Medical		600
Dental		35
Vision		4
Disability		7
401k Matching		81
Total Benefits	$	737
Total Pay and Benefits	$	3,647
Percent Charged to O&M (2)		84.36%
Adjustment to O&M Expense	$	(3,076)
FICA Taxes at 7.65%	$	(235)

Notes:
(1) Per response to OUCC DR 5-37.

(2) Per IPL Workpapers for Schedule OM17, page /9. Includes no amount for non-utility operations.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Recognize AES US Services Employee Vacancies
Test Year Ended June 30, 2014
($000)

Salary and Benefits for 8 Vacant Positions (1)		
Salary	$	433
Premiums		-
Short-Term Incentive Comp		63
Total Pay Components	$	497
Life		2
Medical		52
Dental		4
Vision		0
Disability		2
401k Matching		15
Total Benefits	$	75
Total Pay and Benefits	$	572
Percent Charged to IPL O&M		100.00%
Adjustment to O&M Expense	$	(572)
FICA Taxes at 7.65%	$	(44)

Note:
(1) Per response to OUCC DR 5-37.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Normalize Overtime Expense
Test Year Ended June 30, 2014
($000)

Annual Overtime (1)	Physical Union	Clerical/ Technical Union	Non-Union
2012 Non-Outage, Non-Storm Hours	201,205.75	18,501.50	122.50
2013 Non-Outage, Non-Storm Hours	232,928.50	21,465.00	487.00
2014 Non-Outage, Non-Storm Hours	255,769.25	22,081.50	141.25
Average	229,968.00	20,683.00	250.00
Test Year Non-Outage, Non-Storm Hours	313,774.00	23,364.00	1,868.00
Adjustment to Normalize Overtime Hours	(83,806.00)	(2,681.00)	See Note (2)
Hourly Rate (3)	$ 51.33	$ 45.36	
Adjustment to Overtime Wages	$ (4,302)	$ (122)	
Percent to O&M (4)	84.36%	84.36%	**Totals**
Adjustment to O&M Expense	$ (3,629)	$ (103)	$ (3,732)
FICA Taxes at 7.65%	$ (278)	$ (8)	$ (285)

Notes:

(1) Amounts per response to OUCC 5-35 and 15-06..

(2) Test year non-union overtime included amounts for retirees and terminations that were eliminated. Therefore, comparison of adjusted hours to historical average is not available.

(3) Based on overtime at pro forma levels divided by overtime hours per IPL Workpaper OM17 and responses to OUCC 5-35, 15-7 and 15-8.

(4) Based on average percentage of wages charged construction.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Long-Term Incentive Compensation Expense
Test Year Ended June 30, 2014
($000)

	IPL Employees	AES U.S. Services Allocation
Amount per Petitioner (1)	$ 950	$ 151
Portion of LTC attributable to Restricted Stock Units (1)	$ 506	$ 73
Adjustment to exclude Performance Shares	$ (444)	$ (77)
FICA Taxes at 7.65%	$ (34)	$ (6)

Notes:
(1) Per response to OUCC 5-09. Total for IPL employees reflects add back of 10 percent reduction included by IPL.

(2) Amounts for Restricted Share Units per OUCC 5-09. IPL amount adjusted to add back 10% excluded by IPL.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Remove AES U.S. Services Relocation Costs
Test Year Ended June 30, 2014
($000)

Employee Relocation Costs included in May Billings to IPL (1)	$	11
Annualization factor based on Doubling of January-June 2014 Costs		2
Adjustment to Remove Employee Relocation Costs	$	(22)

Note:
(1) Per response to OUCC DR 9-01.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Update Pension and OPEB Expense
Test Year Ended June 30, 2014
($000)

	Pension Expense	OPEB Expense
Amounts per Original Filing (1)	$ 13,734	$ (6)
Updated Expense per March 12 Submission (2)	11,889	(33)
Adjustment to O&M Expense	$ (1,845)	$ (26)

Notes:
(1) Per IPL Workpapers for Schedule OM17, page /49.

(2) Per IPL's March 12, 2015 Submission of Updated Pension Information and Second Revisions to Direct Testimony.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Uncollectibles Expense
Test Year Ended June 30, 2014
($000)

Uncollectible Accounts Experience Rate (1)		
12 Months Ending June 30, 2012		0.2949%
12 Months Ending June 30, 2013		0.2937%
12 Months Ending June 30, 2014		0.3891%
Average Rate		0.3259%
Revenue at Present Rates Subject to Uncollectibles	$	1,185,061
Pro forma Uncollectibles at Present Rates	$	3,862
Uncollectibles at Present Rates per Company (2)		4,611
Adjustment to Uncollectibles Expense	$	(749)

Notes:
(1) Per IPL Workpaper OM-18 page 2.

(2) Per IPL Financial Exhibit IPL-OPER, Schedule OM18.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Storm Related Costs
Test Year Ended June 30, 2014
($000)

Adjustment to Test Year Storm Costs per IPL (1)	$	(1,580)
Adjustment to Test Year Storm Costs per OUCC (2)		(2,872)
Adjustment to Storm Costs	$	(1,292)

Notes:
(1) Per IPL Financial Exhibit IPL-OPER, Schedule OM8.

(2) Per testimony of OUCC witness Wes Blakley.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Amortization of Deferred MISO Costs
Test Year Ended June 30, 2014
($000)

Deferred MISO Costs (1)	$	117,675
Amortization Expense over 10 years per OUCC (2)	$	9,472
Amortization of Deferred MISO Costs per IPL (1)		19,613
Adjustment to Amortization of Deferred MISO Costs.	$	(10,141)

Notes:
(1) Per IPL Financial Exhibit IPL-OPER, Schedule OM11.

(2) Per testimony of OUCC witness Wes Blakley.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Amortization of Rate Case Expense
Test Year Ended June 30, 2014
($000)

Amortization of Rate Case Expense per IPL (1)	$	2,253
Adjustment to Rate Case Expense per OUCC (2)		2,209
Adjustment to Amortization of Rate Case Expense	$	(44)

Notes:
(1) Per IPL Financial Exhibit IPL-OPER, Schedule OM15.

(2) Per testimony of OUCC Witness Michael Eckert.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Eliminate Non-Recurring Regulatory Commission Expense
Test Year Ended June 30, 2014
($000)

Amounts Included by IPL for Expenses Related to Cause Numbers 44242, 44339, 44478 & 44540 (1)	$	642
Amount per OUCC (1)		445
Adjustment to Amortization of Regulatory Commission Expense	$	(197)

Note:
(1) Per testimony of OUCC Witness Michael Eckert.

INDIANAPOLIS POWER AND LIGHT COMPANY

Adjustment to Income Taxes to Reflect
Reduction in Indiana Corporate Income Tax Rate to 6.5 Percent
Test Year Ended June 30, 2014
($000)

		Amount
Deferred State Income Taxes at 6.75% Tax Rate (1)	$	4,552
State Taxable Income		67,437
Deferred State Income Taxes at 6.5% Tax Rate	$	4,383
Adjustment to Deferred State Income Tax Expense	$	(169)
Federal Income Tax Effect of State Tax Change at 35%		59
Net Change in Income Tax Expense	$	(110)

Note:
(1) Per IPL Financial Exhibit IPL-OPER, Schedule TX1.

INDIANAPOLIS POWER AND LIGHT COMPANY

Interest Synchronization Adjustment
Test Year Ended June 30, 2014
($000)

Rate Base per OUCC (1)	$	1,826,531
Synchronized Interest Rate (2)		2.690%
Tax Deductible Interest per OUCC	$	49,134
Tax Deductible Interest per IPL (3)		51,679
Adjustment to Tax Deductible Interest	$	(2,546)
State Income tax effect at 6.50%		165
Federal Income Tax Effect at 35%		833
Total Tax Savings	$	999

Notes:
(1) Per Schedule TSC-2.

(2) Per Schedule TSC-18.

(3) Per IPL Financial Exhibit IPL-OPER, Schedule TX2.

INDIANAPOLIS POWER AND LIGHT COMPANY

OUCC Capital Structure and Rate of Return
Test Year Ended June 30, 2014
($000)

Capital Source	Amount	Capitalization Ratio	Cost Rate	Weighted Cost Rate
Long-Term Debt	$ 1,148,446	46.20%	5.67%	2.62%
Preferred Stock	59,784	2.40%	5.37%	0.13%
Common Equity	928,034	37.33%	9.20%	3.43%
Post-1970 ITC	5,945	0.24%	7.20%	0.02%
ADIT	316,991	12.75%	0.00%	0.00%
Customer Deposits	26,688	1.07%	6.00%	0.06%
Total	$ 2,485,888	100.00%		6.26%

Post-1970 ITC Cost Rate

Long-Term Debt	$ 1,148,446	53.76%	5.67%	3.05%
Preferred Stock	59,784	2.80%	5.37%	0.15%
Common Equity	928,034	43.44%	9.20%	4.00%
	$ 2,136,264	100.00%		7.20%

Synchronized Interest Rate

Long-Term Debt	$ 1,148,446	46.31%	5.67%	2.63%
Preferred Stock	59,784	2.41%		0.00%
Common Equity	928,034	37.42%		0.00%
ADIT	316,991	12.78%		0.00%
Customer Deposits	26,688	1.08%	6.00%	0.06%
Total	$ 2,479,943	100.00%		2.69%

AFFIRMATION

I affirm, under the penalties for perjury, that the foregoing representations are true.

Lafayette Morgan Jr.

Lafayette Morgan, Jr.
Senior Regulatory Consultant
Exeter Associates, Inc.
Consultant for:
Indiana Office of Utility Consumer Counselor

July 27, 2015
Date

Cause No. 44576/44602
IPL