

**STATE OF MINNESOTA
BEFORE THE PUBLIC UTILITIES COMMISSION**

Beverly Jones Heydinger	Chair
Dr. David C. Boyd	Commissioner
Nancy Lange	Commissioner
Dan Lipschultz	Commissioner
Betsy Wergin	Commissioner

IN THE MATTER OF A REQUEST FOR APPROVAL OF THE ASSET PURCHASE AND SALE AGREEMENT BETWEEN INTERSTATE POWER AND LIGHT COMPANY AND SOUTHERN MINNESOTA ENERGY COOPERATIVE **DOCKET NOS. E001, E132, E114, E6521, E142, E135, E115, E140, E105, E139, E124, E126, E145, PA-14-322**

REPLY OF THE OFFICE OF THE ATTORNEY GENERAL-ANTITRUST AND UTILITIES DIVISION TO THE SEPTEMBER 4, 2014 COMMENTS OF INTERSTATE POWER AND LIGHT COMPANY AND THE SOUTHERN MINNESOTA ENERGY COOPERATIVE

I. INTRODUCTION

The Office of the Attorney General - Antitrust and Utilities Division (“OAG”) submits the following reply to the September 4, 2014 joint comments of Interstate Power and Light Company (“IPL”) and the Southern Minnesota Energy Cooperative (“SMEC”). IPL and SMEC (“Petitioners”) seek approval of their Asset Purchase and Sale Agreement (“Agreement”) that would transfer IPL’s Minnesota service territory and associated electric distribution system with current rights to serve more than 42,000 customers in southern Minnesota to 12 separate electric cooperatives, which jointly formed SMEC.¹

¹ See Joint Petition of Interstate Power and Light Company and Southern Minnesota Energy Cooperative for Approval of Asset Purchase and Sale Agreement and Transfer of Service Rights and Obligations at 9 (April 15, 2014) (“Petition”).

On May 9, 2014, the OAG and the Department of Commerce (“Department”) each filed comments discussing the proper procedure for the Commission to follow in evaluating the Agreement.² The OAG noted that the transaction was important and that the Commission should establish a procedure allowing for a thorough review of the Agreement.³ The OAG stated that it had not identified material facts in dispute and, therefore, did not request a contested case proceeding.⁴ The Department recommended that the Commission order a contested case proceeding, stating that material facts would likely be disputed as parties continued to review the proposal.⁵

To further assess whether a contested case is appropriate, the Commission initiated additional proceedings in which interested parties could submit questions to Petitioners, who were required to file responsive comments within 30 days.⁶ Parties thereafter had a brief period of 30 days to reply.⁷ This procedure was designed to generate “additional substantive comments . . . under time frames designed to permit a prompt decision on whether contested-case proceedings are necessary.”⁸ It did not purport to provide a process for parties to fully evaluate and comment on the substantive aspects of the transaction, or to develop detailed positions on whether the transaction should or should not be approved or, if it should be approved, whether any conditions should be attached to an approval.

² See Notice of Schedule for Filing Procedural Comments (April 22, 2014).

³ OAG Reply Comments at 4 (May 9, 2014).

⁴ OAG Reply Comments at 4 (May 9, 2014).

⁵ See Letter of John Kundert to Burl W. Haar (May 9, 2014); Comments of the Department of Commerce at 4 (May 9, 2014).

⁶ Order Requiring Additional Record Development at 5 (June 30, 2014).

⁷ Order Requiring Additional Record Development at 5 (June 30, 2014). In addition to the written comment procedure, interested parties conducted two days of formal meetings to discuss the transaction with Petitioners.

⁸ Order Requiring Additional Record Development at 4 (June 30, 2014).

After receiving additional information on the transaction and conducting a further review, the OAG agrees that a contested case proceeding would provide valuable information to the Commission regarding the public interest aspects of the proposed transaction. Specifically, while the OAG has identified several potential detriments in the Agreement for ratepayers, some of the purported benefits suggested by Petitioners remain unclear. The OAG acknowledges, however, that even a contested case may leave some questions unresolved—such as how rates would compare in three, four, or five years if the transaction moves forward versus if it does not. Accordingly, the OAG recognizes that the Commission may not elect to refer the matter for contested case proceedings. In that case, the OAG recommends the Commission establish a process to allow parties to make detailed submissions on substantive aspects of the transaction. Based on its current review, the OAG anticipates recommending that the Commission approve the transaction only if IPL agrees to forego its gain on sale, that IPL pay for other transaction costs of the Agreement, and that the transaction be adjusted to compensate ratepayers for increased power costs. The OAG continues, however, to evaluate the documents and information filed in this proceeding.

II. SUMMARY OF PETITION

As the Commission is aware, the Agreement proposes a complex transaction. If approved, IPL would transfer its Minnesota electric distribution assets as well as its rights and obligations to provide service to its Minnesota customers to SMEC.⁹ The rights and obligations to serve IPL's current customers would be divided among the twelve electric cooperatives that make up SMEC, and IPL's current customers would become members of the respective

⁹ Petition at 1.

cooperatives from which they receive service.¹⁰ SMEC and IPL would also enter into a Wholesale Power Agreement (“WPA”), whereby IPL would provide the electricity required to serve IPL’s current customers for a minimum of ten years.¹¹ The price paid by SMEC to IPL for power pursuant to the WPA would be based on IPL’s existing FERC formula rates.¹² The WPA mandates that SMEC and its respective cooperatives purchase power from IPL for a minimum of 10 years.

SMEC member cooperatives will agree to charge IPL’s current customers uniform distribution rates for three years.¹³ These rates reflect IPL’s base rates, adjusted to reflect both the anticipated economies of scale from SMEC and changes in the cost of transmission and power supply from the amount currently collected through IPL’s base rates.¹⁴ Following the initial three-year period, SMEC member cooperatives would limit base rate increases for IPL’s current customers to a maximum of five percent per year, for two years, to facilitate the merger of rates between current IPL customers and SMEC members.¹⁵ Five years after the transaction is finalized, rates charged to IPL’s former current customers will be governed by their respective cooperatives.

Petitioners executed their Agreement on September 3, 2013, and amended their Agreement on October 28, 2013.¹⁶ Petitioners filed their joint request on April 15, 2014, and requested that the Commission complete its review in a time-period that allows for the

¹⁰ Petition at 1-2.

¹¹ Petition at 2. SMEC will, in turn, provide power to the various cooperatives.

¹² Responsive Comments of Interstate Power and Light Company and Southern Minnesota Energy Cooperative at 4 (Sept. 4, 2014) (“Petitioners’ Responsive Comments”); Petition at 4.

¹³ Petition at 4.

¹⁴ Petitioners’ Responsive Comments at 16; Petition at 5.

¹⁵ Petition at 26.

¹⁶ See Petitioners’ Responsive Comments at 4.

transaction to be closed by the end of 2014.¹⁷ The sale price is estimated at \$121 million subject to adjustments at the time of closing, which represents the book value of IPL's Minnesota electric assets plus a gain on sale of approximately \$8.85 million and transaction costs.¹⁸

III. LEGAL STANDARDS

Minn. Stat. § 216B.50 requires a utility to seek approval from the Commission to sell any assets worth more than \$100,000. The Commission will approve the sale if it is "consistent with the public interest."¹⁹ The public interest standard "does not require an affirmative finding of public benefit," but rather a finding that the transaction is compatible with the public interest.²⁰

The Commission has "exclusive control" to set rates for public utilities.²¹ The Commission must set rates that are "just and reasonable," and are "not unreasonably preferential, unreasonably prejudicial, or discriminatory."²² The procedures for changing rates for public utilities are codified in Minn. Stat. § 216B.16. The Commission does not typically regulate the rates of cooperative electric associations,²³ although a cooperative may elect to become subject to rate regulation.²⁴ None of the cooperative members of SMEC have elected to become subject to rate regulation.

IV. ANALYSIS

The OAG has several concerns with the Agreement as it is currently structured that should be further explored before it is considered for approval. Specifically, the OAG's analysis

¹⁷ Petition at 6.

¹⁸ Petitioners' Response to Department's IRs 57 & 63, Attached as Exhibits 1 & 2.

¹⁹ Minn. Stat. § 216B.50, subd. 1.

²⁰ *In the Matter of N. States Power Co., a Minnesota Corp., and ITC Midwest LLC for Approval of a Transfer of Transmission Assets and Route Permit*, Docket No. E-002/PA-10-685, 2010 WL 5462980 (2010).

²¹ *Computer Tools & Eng'g, Inc. v. N. States Power Co.*, 453 N.W.2d 569, 572 (Minn. Ct. App. 1990); Minn. Stat. § 216B.03.

²² Minn. Stat. § 216B.03.

²³ See Minn. Stat. §§ 216B.01, 216B.03.

²⁴ Minn. Stat. § 216B.026 Subd. 1.

indicates that IPL's ratepayers could be subject to significant cost increases, and that Petitioners' claimed benefits are overstated.

A. THE AGREEMENT SUBJECTS RATEPAYERS TO SIGNIFICANT ADDITIONAL COSTS OF SERVICE.

The OAG's analysis to date indicates that the Agreement could significantly harm IPL's current ratepayers by increasing the costs of providing their utility service without providing equivalent offsetting benefits. Information produced by Petitioners indicates that ratepayers will be subjected to substantial additional costs of service if the Agreement is approved. These costs include increased costs associated with maintaining the distribution assets being sold and increased costs associated with obtaining power from IPL's generating units that will not be sold.

With respect to the distribution assets, the Agreement substantially increases the rate base serving IPL's customers by adding significant transaction costs—including an \$8.85 million gain on sale for IPL—and eliminating deferred taxes that currently reduce the company's rate base. In addition to increasing the rate base of IPL's existing distribution system, the Agreement necessitates that millions of dollars be spent to interconnect IPL's existing customers with their respective cooperatives.

Information provided by Petitioners indicates that the current rate base for IPL's distribution system is \$82.5 million.²⁵ This rate base reflects \$105.2 million in plant-in-service, offset by \$22.7 million in accumulated deferred taxes. Accordingly, if IPL were to file a rate case, the rates implemented would presumably be set to reflect its current rate base. But if the proposed transaction is approved, Petitioners estimate the rate base supporting these distribution assets is estimated to rise from its current level to \$122.1 million—an increase of 48 percent.²⁶

²⁵ See Exhibit 1.

²⁶ See *id.*

This dramatic increase in rate base does not result from the addition of equipment used for the benefit of ratepayers, but rather reflects the loss of deferred taxes currently benefiting ratepayers and the addition of \$16.9 million in transaction costs—including the \$8.85 million gain for IPL.²⁷ In other words, IPL’s ratepayers will be required to support a rate base increase of nearly 50 percent if the Agreement is approved without receiving any capital additions that would provide them benefits.

In addition to increasing the rate base for IPL’s distribution assets without providing any additional capital assets, Petitioners estimate that the various SMEC cooperatives will need to spend millions of dollars to interconnect IPL’s current customers with their respective cooperatives. Specifically, Petitioners have provided a “preliminary list” of projects that are necessary to interconnect these customers.²⁸ This preliminary list indicates that, at this time, the SMEC cooperatives anticipate needing to pay nearly \$1.6 million just to interconnect approximately 5000 customers. Presumably, this preliminary list could grow, subjecting IPL’s ratepayers to additional costs necessary to interconnect them with their cooperatives.

The Agreement will also increase the costs of generation assets used to provide power to IPL’s ratepayers. As indicated above, the Agreement is conditioned on the Petitioners executing the WPA that requires the SMEC cooperatives to purchase the power needed to serve IPL’s existing customers for 10 years. Pursuant to the WPA, the costs of IPL’s generation assets used to serve its current customers will be billed as a pass-through at FERC formula rates. Currently,

²⁷ See *id.* Attachment C of Response to Commission Additional Questions for Joint Petitioners issued on July 14, 2014 at 2 (Aug. 1, 2014). The OAG questions the justification for providing IPL a gain of nearly \$9 million above the book value of its assets, which Petitioners claim will “compensate IPL for the reasonable value of its utility property and is within the typical range of premiums in similar transactions.” September 4, 2014 Comments of Joint Petitioners at 16. Petitioners do not reference any other transactions for their claim. Regardless, the OAG acknowledges that any gain or loss that IPL may incur on the sale is only indirectly related to determining whether the transaction is in the public interest.

²⁸ Petitioners’ Response to Department’s IR 52, attached as Exhibit 3. (Emphasis in original).

these rates incorporate a return on equity of 10.97 percent.²⁹ If IPL remained a Minnesota utility, the same generation assets used to serve the company's Minnesota customers would be subject to the return on equity established by the Commission. Past practice indicates that this return will almost assuredly be lower than the 10.97 percent return generated through application of FERC formula rates. For example, the rate of return on equity last approved for IPL in its 2010 rate case was 10.35 percent, 62 basis points lower than the return that would be paid for generation assets if the Agreement is approved.³⁰

Moreover, if IPL filed a rate case, its authorized return on equity would be modified to reflect changes in the economic conditions over the last several years. As the Commission is aware, returns on equity have generally declined since IPL's last rate case was decided in 2011. In the two rate cases decided by the Commission this year, CenterPoint and MERC, the Commission authorized a lower return on equity than in each company's last case. Similarly, the Commission lowered the return on equity for Xcel's electric assets in the company's rate case decided last year. Therefore, while it is impossible to predict the exact return that would be awarded to IPL if it filed a rate case, it is reasonable to assume that IPL would likely be awarded a return lower than the 10.35 percent it was awarded in 2011 and, at a minimum, likely lower than the 10.97 percent IPL would receive pursuant to the WPA. Accordingly, applying FERC's formula rates to IPL's generation assets, as contemplated in the Agreement, will likely lead to higher costs for serving the company's existing customers.

²⁹ See Petitioners' Response to OAG Question 11, attached as Exhibit 4.

³⁰ Findings of Fact, Conclusions, and Order, *In the Matter of the Application of Interstate Power and Light Company for Authority to Increase Rates for Electric Service in Minnesota*, at 10, Dkt. No. E-001/GR-10-276 (Aug. 12, 2011).

B. PETITIONERS HAVE NOT DEMONSTRATED THAT ANY BENEFITS OUTWEIGH THE POTENTIAL COSTS OF THE TRANSACTION.

The Petitioners do not dispute that ratepayers will be subjected to the additional costs described above. In fact, the Petitioners indicate that the transaction will lead to compounding rate increases of 5.7 percent in 2015, 4.5 percent in 2016, and 5.2 percent in 2017.³¹ They claim, however, that the transaction will reduce costs for ratepayers overall due to a combination of SMEC's five-year rate plan and the reduced costs associated with cooperatives' lower cost of capital and exemption from income tax payments. The OAG is not convinced by Petitioners' argument, which appears to rely on speculative, exaggerated, and seemingly contradictory evidence.

At a high level, Petitioners' claim that the Agreement leads to an overall reduction in the cost of service appears to be based only on their own estimates and comparisons of the revenue requirements needed to maintain IPL's distribution system with and without the Agreement. Petitioners assert that the three years of rate increases that would occur if the transaction is approved are "lower than the increased rates that *could be justified by IPL . . .* absent the Transaction."³² But the rates that a utility "could" justify is, quite obviously, a heavily disputed aspect to any rate case. Petitioners' comparison of the rate increases for customers with and without the Agreement assumes that IPL will justify all of the costs it claims in multiple rate cases. Such an assumption is not reasonable.

In addition to this high level concern, a closer look at Petitioners' analysis reveals what appear to be inconsistencies with how they calculate the purported ratepayer benefits of the Agreement. For instance, when asked to explain why IPL should receive a gain on the sale of its

³¹ See Comments of Joint Petitioners at 15-16 (Sept. 4, 2014).

³² *Id.* at 16.

distribution system, Petitioners provided a Transaction/Customer Benefit Analysis (“Benefit Analysis”) that purports to quantify the net present value of ratepayer’s annual benefit over the next 10 years. This Benefit Analysis, however, failed to consider any of the increased costs of purchased power through the WPA. Rather, to calculate this annual benefit of the Agreement, Petitioners first assumed a rate of return of 7.98 percent for IPL, and applied this return to the \$82.5 million that IPL claims to have in rate base for its distribution assets. The result of this exercise was then adjusted upwards for taxes to produce an assumed annual cost of maintaining IPL’s distribution assets—absent the Agreement. Petitioners then ran a similar calculation to produce an assumed cost of service for IPL’s distribution assets if the Agreement was approved. This calculation assumed a higher rate base of \$122.1 million (to account for transaction costs, IPL’s gain on sale, and the loss of deferred taxes), a return on equity of 1.57 percent for three years, and a return on equity of 3.38 percent thereafter. According to Petitioners, this analysis demonstrates that the transaction reduces customer costs by \$8.4 million annually for three years, and by \$5 million annually from years four through ten. Petitioners also applied an eight percent discount rate to these “savings” to calculate a net present value of \$42.4 million, which they claim more than justifies the \$8.85 million gain for IPL.

The OAG has significant concerns that Petitioners’ Benefit Analysis does not provide accurate comparisons of the applicable costs of providing utility service to IPL’s customers with or without the proposed transaction. First, the Benefit Analysis only contemplates the difference in costs associated with IPL’s distribution assets; it ignores any effect of increasing the return on equity for generation assets from 10.35 percent ordered in IPL’s last rate case to 10.97 percent through application of FERC formula rates or any costs of interconnecting IPL’s customers with their respective cooperatives.

Second, Petitioners' Benefit Analysis incorporates several questionable assumptions. For instance, while the OAG has not conducted a detailed economic analysis of the cooperatives' likely rate of return, the information at this time indicates that Petitioners estimated rates of return for the SMEC cooperatives are likely far too low. In the 2009 rate case for Dakota Electric Association, a rate-regulated cooperative utility in Minnesota, the cost of equity for cooperative members was established at 6.26 percent.³³ There is no reason to believe that the cost of equity for SMEC cooperatives will be significantly lower than for Dakota Electric Association. Adjusting for a cost of equity of 6 percent in and a capital structure of 50 percent debt and 50 percent equity, the net present value of ratepayers' anticipated benefit diminishes greatly to \$3.7 million—less than half of IPL's gain on sale.³⁴ After considering the increased costs of generation and the costs of interconnecting IPL's customers, the transaction is likely a detriment to ratepayers. In any event, the OAG anticipates that the inputs and methodology supporting Petitioners' Benefit Analysis would be disputed if sent to a contested case.

V. CONCLUSION

The purported benefits to ratepayers suggested by Petitioners remain unclear, although some detriments are clear. Petitioners admit that rates for IPL customers will increase immediately following the transaction but have failed to provide credible analysis to substantiate their claim that ratepayers would receive an overall benefit. These are important aspects of the Agreement that should be fully discussed by parties through a robust comment process or contested case. Therefore, the OAG recommends, that at a minimum, the Commission establish

³³ Findings of Fact, Conclusions of Law, and Order, *In the Matter of the Application of Dakota Electric Association for Authority to Increase Rates for Electric Service in Minnesota*, at 11, Dkt. No. E-111/GR-09-175 (May 24, 2010).

³⁴ See Exhibit 5.

a procedure that allows parties to make additional, substantive comments on the proposed transaction.

Dated: October 6, 2014

Respectfully submitted,

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ATTORNEYS FOR OFFICE OF THE
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DOC Information Request No. 57

Reference: Page 2 of Attachment C of IPL and SMEC's Response to Commission's additional questions issued on July, 14, 2014 submitted on August 1, 2014.

- a. In Entry #116 – Record gain on asset sale IPL identifies a gain of \$8,555,000.
 - i. Please explain in detail the basis for this gain.

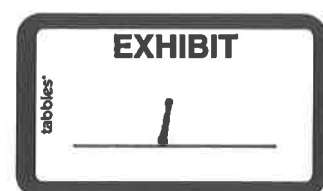
RESPONSE:

The purchase price (with the acquisition premium, including gain) and the ratio of the purchase price to the net book value of the assets (the multiple) were the result of arms-length negotiations between IPL and representatives of SMEC and the SMEC Member Cooperatives. The sale was the result of a private negotiation initiated by representatives of the SMEC Member Cooperatives and did not reflect a request for proposals or other effort by IPL to obtain multiple proposals for consideration.

The multiple to net book value was determined to be reasonable and consistent with the range of multiples to net book value of publicly announced electric distribution asset sales of similar nature and size that had recently occurred as the Transaction was being negotiated by and between IPL and SMEC and SMEC Member Cooperatives.

The purchase price (including the gain and acquisition premium, including costs incurred by the SMEC Member Cooperatives in connection with the Transaction) also represents an amount that the SMEC Member Cooperatives' determined to be reasonable in relation to the benefits that are expected to accrue over time.

The Transaction will provide clear and substantial benefits to customers that more than offset the acquisition premium to be recovered, with the result being that the acquisition premium is more than fully offset by cost savings. Among the benefits that



are expected to accrue are expected cost benefits as a result of: (1) the SMEC Member Cooperative's substantially lower cost of capital in relation to IPL's cost of capital; and (2) the income tax exemption of the SMEC Member Cooperatives, which further reduces the costs that will accrue to customers and provides a further relative advantage in relation to the costs of continued operation by IPL. These cost advantages apply to the distribution assets that are to be transferred from IPL to the SMEC Member Cooperatives. An approximation of the annual benefit resulting from the lower cost of capital is as follows:

Transaction / Customer Benefit Analysis

\$ In Millions

Initial 3-year period	IPL costs	SMEC costs
Gross Plant	\$175.5	
Accumulated Depreciation	-\$70.3	
Net Plant Value	\$105.2	
Accumulated Deferred Taxes & Other Rate Base Adjustments*	-\$22.7	
Net Rate Base	\$82.5	
Acquisition Cost (Assets + Premium + SMEC Transaction Costs)**		\$122.1
x Cost of Capital	7.98%	1.57%
= pretax cost	\$6.6	\$1.9
x Income Tax Effect (Federal + State)	1.71	1.0
x TIER	N/A	1.5
= After tax cost	\$11.2	\$2.9
Benefit		\$8.4

Long-Term	IPL costs	SMEC costs
Net Rate Base	\$82.5	
Acquisition Cost (Assets + Premium + SMEC Transaction Costs)*		\$122.1
x Cost of Capital	7.98%	3.38%
= pretax cost	\$6.6	\$4.1
x Income Tax Effect (Federal + State)	1.71	1.0
x TIER	N/A	1.5
= After tax cost	\$11.2	\$6.2
Benefit		\$5.0

Customer Benefit	
Annual Benefit Years 1 - 3	\$8.4
Annual Benefit Year 4 -10	\$5.0
Net Present Value (NPV) at 8% discount rate	\$42.4
Acquisition Price over Net Book Value	\$16.9
Benefit to Cost Ratio	2.5

* Proxy estimate for Accumulated Deferred Income Taxes associated with the assets being sold

** Excluding working capital adjustments (\$8.8 Debit, \$5.2 Credit)

While further refinements could be made to these calculations, these calculations show that the Transaction will provide a substantial benefit in the form of a reduced cost of service after recovery of the acquisition premium.

The net benefits provided by the Transaction are also reflected in the anticipated cost savings discussed on pages 36-38 of the Joint Petition. Further, cooperative members have the added protection of cooperative membership, which includes obtaining an allocated ownership interest in margins resulting from rates paid and in some cases credits based on those margins.

**Response of
Interstate Power and Light Company and
Southern Minnesota Energy Cooperative
to
Minnesota Department of Commerce,
Division of Energy Resources
Information Request No. 63**

Docket No.: E-001, E-115, E-140, E-105, E-139, E-124, E-126, E-145,
E-132, E-114, E-6521, E-142, E-135/PA-14-322

Date of Request: September 8, 2014

Response Due: September 23, 2014

Information Requested By: Eilon Amit, Mark Johnson, John Kundert

Date Responded: September 23, 2014

Author: Michael Bremel

Author's Title: Dir Wholesale Svcs & Acct Mgt

Author's Telephone No.: (608) 458-5195

Subject:

Reference: Page 10 of Responsive Comments

Information Request No. 63

The Petitioners state the book value of the Minnesota electric assets and adjustments as of December 31, 2012 the purchase price would be approximately \$118 million plus customary working capital and closing adjustments.

- a. Please provide a similar estimate of the purchase price on December 31, 2014.
- b. Does the \$118 million figure listed include the \$8.55 million gain on asset sale discussed in DOC Information Request #57?

Response:

a.

Example of Computation of the Estimated Closing Purchase Price

Description	Est. Amount (\$000s)	
	2012	2014
1. Base Purchase Price	\$ 115,437	\$ 113,360
2. Construction Work in Progress	2,701	7,690
3. PPE Adjustments	TBD	TBD
4. Casualty Repair Expense	TBD	TBD
5. Adjusted Base Purchase Price	118,138	121,050

- b. The \$118 million figure reflected in the Joint Petition (and discussed in the response to DOC Information Request #57 and above) includes the estimated \$8.55 million IPL gain on sale (*after* IPL's estimated Transaction Costs and Taxes).

For clarification, the \$16.9 million Acquisition Price over Net Book Value included in the response to DOC Information Request 57 reflects the *total* SMEC Purchase Price from which the estimated \$8.55 million IPL gain on sale is determined (after adjustment for estimated IPL Transaction Costs and Taxes).

DOC Information Request No. 52

In conversations during the meetings between representatives from IPL/SMEC and interested parties in St Paul on July 17th and 18th, SMEC staff mentioned that they had identified several projects that would allow them to improve system reliability for both current IPL ratepayers and SMEC Member Cooperative customer/owners. Please provide a list of these potential projects and the costs and benefits associated with those projects.

RESPONSE:

SMEC has established an Engineering Committee that is currently evaluating the IPL system and identifying construction and/or maintenance projects that are needed over the next few years to, among other things, improve reliability. These projects include interconnecting the former distribution IPL system with the acquiring Cooperative system. A preliminary list of projects identified by the SMEC Engineering Committee for construction during 2015 that are specifically designed to interconnect the two systems and thereby to enhance reliability is attached as Attachment DOC-52A. Note that the attached list represents a portion of \$7,000,000 in capital projects that SMEC is planning for 2015. The Cooperatives will continue to identify similar reliability enhancement projects beyond 2015.

In addition, the majority of the SMEC Member Cooperatives plan to rollout AMR/AMI facilities in the former IPL area in the 2015/2016 time frame and are starting the process to identify the appropriate vendor. A number of Cooperatives (i.e., Minnesota Valley, Sioux Valley and Steele-Waseca) are also planning to install SCADA in the former IPL substations as well. The planned expansions of the Cooperatives' existing SCADA/AMR/AMI systems will also enhance system reliability.



2015 Planned System Reliability Projects				
Coop	Project Description	Estimated Cost	Estimated Customers Affected	Purpose
FMCS	Three Phase Tie into Geneva	\$ 79,200	701	Tie into southern Geneva between IPL circuits
FMCS	Three Phase Tie to FMCS System	\$ 99,000	671	Tie with FMCS Corning Sub and IPL Hayward Sub
FMCS	Convert Brownsdale from 4 KV to 15 KV / Retire Sub	\$ 350,000	383	Tie between IPL and FMCS systems and converting 4 kV transformers to 12.5 kV
FMCS	Rebuild and Relocate line on Lakeview Boulevard	\$ 100,000	1,294	Age and condition of line
SWCE	Tie line between SWCE River Point Sub and Steele Center	\$ 70,000	290	Tie between IPL and SWCE systems
SWCE	Tie line between SWCE Bixby Sub and Steele Center	\$ 70,000	310	Tie between IPL and SWCE systems
FREA	Single Phase Tie to FREA System	\$ 6,000	7	Tie between radial IPL line and FREA system
FREA	Single Phase Tie to FREA System	\$ 9,000	3	Tie between radial IPL line and FREA system
FREA	Three Phase Tie to FREA System	\$ 2,000	222	Tie between radial IPL line and FREA system
FREA	Two Phase Tie to FREA System	\$ 5,000	13	Tie between radial IPL line and FREA system
FREA	Three Phase Tie to FREA System	\$ 3,000	159	Tie between radial IPL line and FREA system
FREA	Three Phase Tie to FREA System	\$ 5,000	206	Tie between radial IPL line and FREA system
NCE	Three Phase Tie to NCE System	\$ 5,000	78	Tie between radial IPL line and NCE system
MVEC	Three Phase Road Move & Tie	\$ 250,000	300	Tie between radial IPL line and MVEC system
TCE	Three Phase Tie and Conversion	\$ 300,000	176	Tie between IPL and TEC systems and converting aerial line to underground
TCE	Voltage Conversion & Tie	\$ 100,000	201	Tie between IPL and TEC systems and converting 4 kV transformers to 12.5 kV
People	Three Phase Tie to People's System	\$ 138,600		Tie between IPL and People's system
	Total	\$ 1,591,800	5,014	

OAG Information Request No. 11

Explain why the calculations for revenue requirement use a 10.97% cost of equity, when IPL's last rate case established a 10.30% cost of equity. Provide any data or analysis used to answer the question in its original format or in an Excel spreadsheet.

RESPONSE:

The calculation pertains to IPL's wholesale power tariff under IPL's Rate Schedule RES-5, which was established in FERC Docket No. ER-06-587 and amended in Docket No. ER-07-122, for IPL's wholesale customers in Illinois, Iowa and Minnesota. Under the terms of the Asset Purchase and Sale Agreement, Southern Minnesota Energy Cooperative would enter into a Wholesale Power Supply Agreement with IPL for electric supply, with the pricing terms consistent with IPL's applicable wholesale requirements tariff, which is currently RES-5. The RES-5 tariff, which is subject to change in a future proceeding, includes a 10.97% cost of equity. The Minnesota 10.30% cost of equity is not used to determine IPL's wholesale rates under Rate Schedule RES-5.



Benefit Analysis
Initial 3 Year Period
\$ In Millions

	IPL Costs	SMEC Costs
Gross Plant	175.5	175.5
Accumulated Depreciation	-70.3	-70.3
Net Plant	105.2	105.2
Accumulated Deferred Taxes & Other Rate Base Adjustments	-22.7	
Net Rate Base	82.5	
Acquisition Cost (Assets + Premium + Transaction Costs)		122.1
x Cost of Capital	7.98%	3.92%
Equals pretax cost	6.58	4.78
x Income Tax Effect	1.71	1
x TIER	1	1.5
Equals After Tax cost	11.26	7.17

Benefit \$ 4.09

Long Term

	IPL Costs	SMEC Costs
Net Rate Base	82.5	
Acquisition Cost		122.1
x Cost of Capital	7.98%	4.82%
Equals Pretax Cost	6.58	5.89
x Income Tax Effect	1.71	1
x TIER	1	1.5
Equals After Tax Cost	11.26	8.83

Benefit \$ 2.43

Customer Benefit

Annual Benefit Years 1-3	\$ 4.09
Annual Benefit Years 4-10	\$ 2.43
Net Present Value at 8% discount rate	\$20.60
Acquisition Price over Net Book Value	\$ 16.90
Benefit to Cost Ratio	1.22
IPL Gain on Sale	\$ 8.85
SMEC Cummulative Benefit	\$ 3.70