S T A T E O F M I C H I G A N

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of **THE DETROIT EDISON COMPANY** for reconciliation of its choice incentive mechanism for the period from January 14 through December 31, 2009.	))))))	Case No. U-16262

NOTICE OF PROPOSAL FOR DECISION

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on March 4, 2011.

Exceptions, if any, must be filed with the Michigan Public Service Commission, P.O. Box 30221, 6545 Mercantile Way, Lansing, Michigan 48909, and served on all other parties of record on or before March 21, 2011, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before March 31, 2011. **The Commission has selected this case for participation in its Paperless Electronic Filings Program. No paper documents will be required to be filed in this case.**

At the expiration of the period for filing exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for Decision is reviewed by

action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before the date they are due.

STATE OFFICE OF ADMINISTRATIVE
HEARINGS AND RULES
For the Michigan Public Service Commission

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Mark E. Cummins
Administrative Law Judge

March 4, 2011
Lansing, Michigan
drr

STATE OFFICE OF ADMINISTRATIVE HEARINGS AND RULES

FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

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PROPOSAL FOR DECISION

I.

BACKGROUND AND HISTORY OF PROCEEDINGS

The Commission's August 31, 2006 order in Case No. U-14838 (the August 31 order) approved a settlement agreement that, among other things, established a Choice Incentive Mechanism (CIM)[1] for The Detroit Edison Company (Detroit Edison). As indicated by the Commission, the CIM was designed to create an incentive for Detroit Edison to further reduce its costs in the event that sales to electric choice customers changed from the level of sales used in establishing the related revenue reduction assumed in the settlement agreement.

The August 31 order, as well as its appended settlement agreement, directed Detroit Edison to file its first CIM reconciliation on or before March 31, 2008, the purpose of which would be to reconcile actual 2007 electric choice sales with the 3,400

[1] The CIM is a "tracking mechanism that determines the change in total non-fuel revenue associated with increases or decreases in annual Electric Choice sales from a total approved Electric Choice sales level, which is established in a utility's general rate case. 2 Tr 18.

gigawatt-hour (GWh) base sales level assumed in the settlement agreement, albeit adjusted for a 200 GWh deadband. Moreover, that order indicated that all provisions contained therein--including those establishing the CIM itself--would expire on the later date of March 31, 2008 or 12 months following the filing date of Detroit Edison's next general rate case. The utility filed such a case on April 13, 2007 in Case No. U-15244, thus causing the CIM to expire effective April 13, 2008.

The Commission's December 23, 2008 order in Case No. U-15244 (the December 23 order) re-established the CIM for Detroit Edison, while also (1) adding a sharing mechanism for any declines in sales, (2) removing the rate cap on non-fuel power supply revenue, and (3) recalculating the CIM base level of sales to be 1,561 GWh. See, the December 23 order, p. 87. Subsequently, through its January 11, 2010 order in Case No. U-15768 (the January 11 order), the Commission approved a continuation of the CIM, increased the base level of sales to 1,586 GWh, and provided that if a 12-month reconciliation period for any tracker or decoupling mechanism (such as the CIM) covers a period of time during which the utility has self-implemented rates as allowed by MCL 460.6a(1), the actual value being tracked during the corresponding self-implementation period must be reconciled with the sales level of expense reflected in Detroit Edison's most recent rate case.[2] See, the January 11 order, p. 86.

On March 15, 2010, Detroit Edison filed the present application--with supporting testimony and exhibits--requesting reconciliation of its CIM for the period running from January 14 through December 31, 2009. According to that application, actual sales to electric choice customers fell within the deadband previously established by the

[2] Detroit Edison did, indeed, self-implement a general electric rate increase on July 26, 2009, as provided for by the Commission's July 16, 2009 order in Case No. U-15768.

Commission. Thus, the application asserts that no CIM-related refund or surcharge is required for the period in question.

Pursuant to due notice, a prehearing conference was held in this matter on July 15, 2010 before Administrative Law Judge Mark E. Cummins (ALJ). In the course of that prehearing, the ALJ granted intervenor status to the Association of Businesses Advocating Tariff Equity (ABATE). The Commission Staff (Staff) also participated in the proceedings.

Evidentiary hearings in this matter took place on October 26, 2010. In the course of those hearings, testimony was provided by one utility witness, Theresa M. Uzenski. The parties waived cross examination of Ms. Uzenski, and neither ABATE nor the Staff offered testimony of their own. The resultant record consists of 23 pages of transcript and two exhibits, each of which was received into evidence. Pursuant to the schedule established for this case, all of the parties filed briefs on November 16, 2010. Detroit Edison and the Staff also filed reply briefs on December 3, 2010.

II.

TESTIMONY AND POSITIONS OF THE PARTIES

As noted earlier, Detroit Edison was the only party to provide testimony in this proceeding. Ms. Uzenski, the Manager of Regulatory Accounting for both Detroit Edison and Michigan Consolidated Gas Company (Mich Con), testified regarding the calculation and allocation of the CIM for the period in question. According to her testimony, the actual electric choice sales "for the period ending December 31, 2009 were 1,477 GWh, and were [therefore] within the +/− $7.3 million 'deadband' of base

levels of Electric Choice sales." 2 Tr 18; See also, Exhibit A-2. Ms. Uzenski further confirmed that, because Detroit Edison self-implemented new rates on July 26, 2009, her calculation reflected--on a prorated basis--the respective sales level established by the December 23 and January 11 orders. See, 2 Tr 19-21. She concluded by stating that, based on those various calculations, there "was no asset or liability created in 2009." 2 Tr 21. In light of the testimony and exhibits provided by Ms. Uzenski, Detroit Edison contends that her reconciliation calculations should be accepted, and that the Commission should rule that "no refund or collection is required" concerning the utility's CIM for the period from January 14 through December 31, 2009. Detroit Edison's initial brief, p. 4.

The Staff concurs with the utility's conclusion "that the calculated sales level resulted in no incremental increase or decrease in non-fuel revenue" for the period in question, and contends that "no refund or collection is required" as a result of this CIM reconciliation proceeding. Staff's initial brief, p. 2. In support of its contention, the Staff asserts (as did Detroit Edison) that actual electric choice sales from January 14 through December 31, 2009 were within the +/− $7.3 million deadband arising from application of the relevant Commission orders. See, Id.

Although not taking issue with the computations provided by Detroit Edison's witness, ABATE contends (as it has in several other cases) that "single expense item trackers such as the CIM are illegal because the [Commission] lacks the legal authority to approve them." ABATE's initial brief, p. 1. In support of its contention, ABATE cites several cases to the effect that the Commission "has no common law powers, has only statutory powers created by affirmative, clear, and unmistakable statutory language,

and has no implied or inferred powers." Id. (citations omitted). While conceding that the Legislature has, "in certain instances . . . acted to empower the Commission to adopt adjustment clauses or mechanisms to track and adjust, retroactively, revenues and expenses," no such power has been granted with regard to "a single expense tracking mechanism" like the CIM. Id., p. 3.

ABATE further asserts that the CIM constitutes retroactive ratemaking, in violation of the principles set forth in Michigan Bell Telephone Co. v Public Service Comm, 315 Mich 533 (1946), and Detroit Edison v Public Service Comm, 416 Mich 510 (1982), because it is clearly a "mechanism designed to recover prior costs" incurred by the utility. ABATE's initial brief, p. 3. Specifically, ABATE claims that the description of how the CIM would operate, as set forth in the above-cited orders authorizing its application, shows that it is "designed to insure that the utility collects costs that [Detroit Edison] experienced during the preceding calendar year" by increasing retail electric rates to "compensate the utility for any increase over and above the amount [of electric choice sales] established in base electric rates." Id. It goes on to contend that, due to the statutory mandate that the Commission establish "just and reasonable rates" as part of any rate case order, "any subsequent adjustment to what once was [deemed] just and reasonable" for a particular period is, *a priori*, a violation of the prohibition against retroactive ratemaking." Id., p. 4.

In response to ABATE's assertions, Detroit Edison contends that the Court of Appeals previously determined that "the Commission was permitted by statutory authority to authorize expense tracking mechanisms such as the CIM." Detroit Edison's reply brief, p. 5. The utility further notes that the Courts have also determined, as a

matter of law, that mechanisms like the CIM do not constitute retroactive ratemaking. See, Id.

For its part, the Staff claims that ABATE "misconstrues the distinction between the jurisdiction of the Commission and the grant of specific powers" to it. Staff's reply brief, p. 13. Unlike the cases relied upon by ABATE, it points out that the current proceeding does not "involve a Commission order that extends beyond ratemaking, or otherwise reflect an order for which the Commission lacks specific statutory authority." Id. The Staff further contends that, notwithstanding ABATE's apparent argument that every aspect of the ratemaking process--including all conceivable formulas or rate adjustment mechanisms--must be specifically mentioned in some Legislative grant of authority, Michigan's Courts have never imposed such constraints on the Commission's general ratemaking authority. See, Id. Finally, the Staff claims that Court rulings have consistently rejected ABATE's claim to the effect that all tracking mechanisms--like the CIM--constitute retroactive ratemaking.

III.

DISCUSSION AND FINDINGS

Notwithstanding ABATE's assertion that single expense trackers like the CIM are illegal, both Detroit Edison and the Staff correctly note that "a significant body of case law supports the lawfulness of the Commission's approval of [such] cost recovery mechanisms." Staff's reply brief, p. 3. For example, in *In re* Application of Michigan Consolidated Gas Co, 281 Mich App 545 (2008), the Court of Appeals held that a similar recovery mechanism--specifically, Mich Con's Uncollectible Expense Tracking

Mechanism, commonly referred to as the UETM--was lawful and within the scope of the Commission's statutory authority.[3] See, *in re* Mich Con, supra, at p. 547. The holding in that case was specifically based on the Court's conclusion that the Commission acted within its general ratemaking powers in adopting the UETM, and that the rates ultimately established by that action are presumed to be both lawful and reasonable pursuant to MCL 462.25.[4] See, Id., at 547-549.

Similarly, in *In re* Application of Consumers Energy Co, 279 Mich App 180 (2008), the Court affirmed a Commission order allowing Consumers to implement an equalization mechanism for the recovery of post-employment benefit costs, despite the Attorney General's contention that no clear and unmistakable statutory authority existed for approving such an expense tracker. In reaching that decision, the Court noted that the Commission's action in approving the equalization mechanism was supported by the broad, albeit general, ratemaking powers conferred by MCL 460.6.

In addition to the two above-described cases, the Court of Appeals has explicitly upheld at least three other expense tracking mechanisms. First, in Attorney General v Public Service Comm #1, 133 Mich App 719 (1984), *lv den* 422 Mich 910 (1985), the Court found that Commission approval of an operation and maintenance (O&M) expense indexing mechanism--which tied a utility's O&M costs to the National Consumer Price Index--was lawful and reasonable, and was again supported by the

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[3] The Attorney General's application for leave to appeal the Court of Appeals' ruling was subsequently denied by the Michigan Supreme Court in *In re* Mich Con, 483 Mich 1017 (2009).

[4] That statutory provision states, in pertinent part, that:

> All rates, fares, charges, classification and joint rates fixed by the commission . . . shall be in force and shall be prima facie lawful and reasonable until finally found otherwise in an action brought for the purpose pursuant to the provisions of Section 26 of this act, or until changed or modified by the commission as provided for in Section 24 of this act.

ratemaking authority granted under MCL 460.6. Second, in Attorney General v Public Service Comm #2, 133 Mich App 790 (1984), *lv den* 419 Mich 960 (1984), it upheld the Commission's decision to allow Detroit Edison to implement a System Availability Incentive Program (SAIP) and to subsequently recover a SAIP-related surcharge due to the utility's improvement in the availability of its electric generating units. Third and finally, in Consumers Power Co v ABATE, 205 Mich App 571 (1994), *lv den* 448 Mich 871 (1995), the Court held that the eventual recovery of costs related to Energy Assistance Programs--established by 1989 PA 200 [Act 200] and designed to assist customers who received benefits from the Department of Social Services--was lawful and supported by the Commission's general ratemaking authority, independent of Act 200's dictates.

In light of the five cases cited above, ABATE's claim that single-expense tracking mechanisms are *per se* illegal unless supported by specific statutory authority is clearly incorrect and must be rejected.

Turning to ABATE's second line of argument, in which it contends that operation of the CIM would violate the long-standing prohibition against retroactive ratemaking, it again appears that ABATE is mistaken. As correctly noted by Detroit Edison and the Staff, ABATE's argument in this regard ignores the fact that the CIM actually operates as a prospective rate-adjustment device. See, Detroit Edison's reply brief, p. 3; Staff's reply brief, p. 7. Specifically, these two parties note that the CIM simply adjusts the rates to be charged by the utility in the future based on the actual level of sales made to electric choice customers during the prior year. This, they continue, fully comports with what the Supreme Court has deemed to be acceptable, prospective rate changes, as

opposed to prohibited retroactive ratemaking.[5] Thus, because the Court's stated prohibition "is merely against re-adjusting previously-charged rates, which would not happen here," the ban on retroactive ratemaking is not applicable in this instance. Id.

Consistent with the Supreme Court's view, the Court of Appeals has repeatedly rejected claims to the effect that prospective rate adjustment mechanisms like the CIM constitute unlawful retroactive ratemaking. For example, the previously-discussed ruling in *In re* Mich Con, supra, notes that:

> This Court rejected the challenge to the equalization mechanism in *In re* Consumers Energy Co, stating:
>
> The Attorney General asserts that approval of this equalization mechanism constitutes prohibited retroactive ratemaking. The PSC concluded that pursuant to its general ratemaking powers it was authorized to adopt a ratemaking formula that included this equalization mechanism, which was designed to ensure, to the extent possible, that rates would match expenses. We note that the rate is presumed, *prima facie*, to be lawful and reasonable. The Attorney General has failed to overcome this presumption. In Attorney General v Public Service Comm, this Court held that deferred expenses were an expense of the year to which they were deferred, and were therefore prospective. Specifically, this Court noted, "when capitalized expenditures are amortized, the amortization becomes a current expense even though it reflects expenditures that were capitalized in the past." There is no sound basis for distinguishing the equalization mechanism approved by the PSC in this case from deferred expenses affirmed in prior case law. Accordingly, the deferral of pension and other post-employment benefit expenses to a subsequent year did not constitute retroactive ratemaking.

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[5] Specifically, the Staff points out that, in 1982, the Court made it clear that retroactive ratemaking means that previously-established rates cannot be changed after the fact, but that rates may be prospectively revised to be more appropriate than those earlier rates. Staff's reply brief, p. 9, citing Detroit Edison v Public Service Comm, 416 Mich 510 (1982). In so doing, the Staff quotes the Court's analysis, which states that:

> [T]he essential principle of the rule against retroactive ratemaking is that when the estimates prove inaccurate and costs are higher or lower than predicted, the previously set rates cannot be changed to correct for the error; the only step that the [Commission] can take is to prospectively revise rates in an effort to set more appropriate ones. The [Commission's] adoption of the lag-adjusted factor in February 1975 was simply one more effort to better estimate current costs in future billings.

Id., quoting 416 Mich 510, 523 (citations omitted).

In re Mich Con, supra, at 549-550 (citations omitted). Similarly, in Attorney General v Public Service Comm, 262 Mich App 649 (2004), the Court of Appeals rejected claims to the effect that allowing a utility to defer extraordinary storm-related costs incurred during 1997 and to amortize them during 1998 and 1999 constituted retroactive ratemaking. Likewise, in Detroit Edison v Public Service Comm, 221 Mich App 370 (1997), the Court rejected assertions that allowing the utility to defer to 1994 the collection of expenses incurred during 1993 would constitute retroactive ratemaking. Finally, in ABATE v Public Service Comm, 208 Mich App 248 (1994), *lv den* 450 Mich 892 (1995), the Court again held that deferring the recovery of an expenditure that occurred in the past to some future period does not fall within the definition of prohibited retroactive ratemaking.

Based on this long line of case law, ABATE's argument to the effect that implementation of the CIM constitutes retroactive ratemaking is clearly without support, and must--like its claim that single-expense tracking mechanisms are *per se* illegal--be rejected.

IV.

CONCLUSION

In light of the uncontroverted testimony and exhibits provided by Ms. Uzenski, and based on the above-noted findings to the effect that ABATE's arguments regarding jurisdiction and retroactive ratemaking must be rejected, the ALJ recommends that the Commission specifically (1) accept Ms. Uzenski's reconciliation calculations pertaining to the utility's CIM, (2) approve Detroit Edison's March 15, 2010 application in its

entirety, and (3) rule that no refund or collection is required concerning the CIM for the period from January 14 through December 31, 2009.

Finally, it should be noted that any arguments or potential issues not specifically addressed in this PFD were deemed to be irrelevant to the ALJ's ultimate findings and conclusions.

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Mark E. Cummins
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