UTILITY CONSUMER PARTICIPATION BOARD

August 5, 2013

MINUTES

A meeting of the Utility Consumer Participation Board was held Monday, August 5, 2013, in the Ottawa Building, 4th Floor Training Room, Lansing, Michigan.

I. Call to Order
Jim MacInnes called the meeting to order at 11:10 a.m. Board members present: James MacInnes, Chairperson, Paul Isely, Vice Chairperson, Conan Smith, Susan Licata Haroutunian, Ryan Dinkgrave. Members absent: none.

Others present: Michelle Wilsey, UCPB Board Assistant, David Shaltz, Residential Ratepayer Consortium (RRC), John Liskey, Citizens Against Rate Excess (CARE), Robert Burns, CARE, Ken Rose, CARE, Don Keskey, Michigan Community Action Agency Association (MCAAA), Christopher Bzdok, Michigan Environmental Council (MEC), Shawn Worden, LARA, Wes VanMalsen, LARA, Kwafo Adarkwa, ITC, Dan Dundas, House Republican Policy Office, Sally Talberg, MPSC.

II. Approval of Consent Agenda
MacInnes proposed approval of the consent agenda. Isely moved, second by Dinkgrave and motion carried to approve the consent agenda as presented.

III. Board Education

MacInnes introduced the board education session and speaker, Kwafo Adarkwa, Sr. Regulatory Analyst, ITC Holdings. Adarkwa provided an update on transmission.

A copy of the presentation and additional materials referenced in the presentation are attached and included by reference to these minutes. The transcript of the meeting is also available with the presentation included.

Presentation questions and answers: Wilsey asked Adarkwa to expand on his reference to the "Thumb Loop Project shrinking the queue" and the impact of the wind projects coming on line. Adarkwa responded that 5-6 years ago the MISO generator interconnection queue was really bogged down. As the projects come on line the queue is reduced.

Keskey asked if the purchase of Entergy included just the transmission facilities or does it include any generation. Adarkwa responded it was just the transmission facilities.

MacInnes asked if Adarkwa had a figure for transmission line losses on the ITC system? Adarkwa responded that he did not. He thought the losses for an average transmission system were on the order of three to five percent.

MacInnes asked if he had any statistics on capacity utilization on the lines, or, how heavily they are loaded on an annual basis? Adarkwa responded that they try to maintain a rating that is compliant with NERC reliability standards. It is dependent on season, load levels, etc. There is tolerance built in cases where you are above

100% but you don't want to be in that position long term. That is where reliability projects come in to alleviate some of those issues. Rose commented that this is where redispatch comes in to get around the congestion. Adarkwa noted that is another avenue.

MacInnes noted the arrival of board members Conan Smith and Susan Licata Haroutunian to the meeting. He also welcomed Sally Talberg, newly elected Michigan Public Service Commissioner to the meeting. Talberg introduced herself and shared information on her background.

MacInnes moved the discussion to capacity markets. He recently attended the IEEE Power and Energy Sector meeting in Vancouver. He met Ben Hobbs, Johns Hopkins University, who was instrumental in preparing the capacity market plan for PJM. After discussions with him as well as a number of people from PJM, work of the IEEE USA energy policy committee on the issue, and review of a report by the Brattle Group, there seems to be some comfort with the efficacy of capacity markets, recognizing some tweaks and improvement can be made. PJM is in a different situation than MISO given their costs are higher. But as coal fired plants are retired, MISO may have a need for capacity markets.

He also noted the issue of demand side management citing a recent article by outgoing FERC Chairman Jon Wellinghoff commenting on how capacity markets allowed demand-side management to be more easily incorporated into the system. He noted that CARE is involved in this area with funding from the UCPB and he thought it was important to share the information, keep the discussion active as change occurs, and for the board to stay informed. MacInnes introduced Ken Rose to provide an update and respond to his comments on capacity markets.

Rose noted that CARE predicted that capacity markets would be an issue the board should be concerned with two years ago. He also noted that he had personally worked with Ben Hobbs. They do not have ideological differences but do hold different views of the world. Ben is an engineer and Rose is an economist.

Rose first commented on the so called, "missing money problem." The problem as engineers tend to see it is that there are certain units of capacity, and in some cases owners of capacity, in PJM that operate so few hours, they're basically peaking units, that the revenue that they generate from energy and from ancillary services isn't sufficient to cover all their costs. To Rose as an economist that means average costs. Basically the notion is that if you have a peaking unit, generally defined as a plant or unit that is operational 10 percent of the time or less. A unit like that is probably not going to have sufficient revenue. And Ben raised in his issue, and this came up again in PJM, too, that you wouldn't need the capacity market if you allowed the price to spike all the way up to whatever it is that that unit would need to operate 400 hours a year or whatever. But they put a cap of a thousand dollars on all the offers that are placed in PJM, so they can't exceed that.

There's a chance that they'll be mitigated because there's market power mitigation for units that are dispatched out of merit order. That happens when there's transmission congestion, they may get mitigated downward. PJM does have this feature of scarcity pricing, meaning under scarcity conditions, the price is allowed to go above that price. On very rare occasions the entire footprint of PJM is at a thousand dollars a megawatt hour.

This summer is a good example of the problem for those specific units. It's very cool and those units are not running very often, so their revenue must be way down. It is likely that those units are being dispatched even much lower than they in a normal summer because it's been relatively cool for at least the western part of PJM.

In the Eastern part there has been some hot weather, so maybe in that region they're being dispatched. So here's the problem. How do you make up the revenue lost, that missing money problem, how do you fix that? I think a lot of engineers in particular looked at the problem. And the RPM, by the way, was invented by kind of the higher ups in PJM, which are primarily engineers, they look at the world that way and say, O.K., I can see that you're not getting sufficient revenue, so how do we make that up. And that's kind of where the idea for the auction, for the capacity market auction was arrived at.

But if you look at it as an economist, you say, well, the average cost curve for any supplier, a supplier that owns multiple units, is not a straight line. It's certainly not the same for everybody across the whole footprint, and that's what I tried to point out in that paper. Basically what we've done and what PJM has done is to design a program that compensates that unit, that it would potentially compensate that unit whose costs or average costs exceed whatever they can get in the market price. And I explained in there, if you're below average variable costs, those shut down, right, they'll just shut down the unit, and I could understand why you would want to make up the revenue between the average cost and whatever they get in those markets, you know, what they're getting, but that's not what we're doing. A lot of units have average costs that's below the cost, which means that's economic profit. We have a word for that in economics, it's called economic profit. And, economic profit is not the same.

FERC is very confused about this. When we commented to FERC on the issue, FERC responded that if they're earning economic profit, they have ways of dealing with market power. But, market power is something different, this is not the same thing. FERC is not differentiating between market power and economic profit.

So to summarize, basically what I said in the paper is that FERC came up with a system that is probably compensating the people that are losing money, but we're overcompensating maybe 90 percent of the suppliers in PJM to be able to compensate that small number, because the average cost is just not the same for everyone.

So if I'm a supplier in PJM that owns a lot of units, coal plants, nuclear power plants and gas units, intermediate gas and peaking units, your average cost for your whole system is probably well below what they get in the energy ancillary services market, and I think that's pretty fair. But, we're overcompensating suppliers in order to fix this missing money problem that I agree that occurs. Rose noted that in his paper he did not address how to fix this problem. In a follow-up paper he would like to present alternatives before MISO to fix this missing money problem besides compensating everybody. In MISO this is a particular problem because you have so many units that probably have very low average costs and don't really need the subsidy. There also needs to be continued study of recent developments in PJM related to the auctions.

Adarkwa asked Rose if there are any changes to the voluntary capacity market contemplated? Rose responded that MISO has entertained the idea of having a forward capacity market. There is no formal proposal, but it is a concept out there that is being discussed. The only difference from PJM of note is having a longer capacity commitment.

Liskey asked if Rose could provide a general estimate of how much money this could cost Michigan residential ratepayers. A back of the envelope calculation that if the numbers were comparable to PJM's average for the whole RTO applied in Michigan it would be in the realm of $1 billion per year. That was not using the $1.05 that MISO had in their last auction, it was based on the $56 or so from PJM a couple of years ago.

Burns added that MISO has projected capacity shortages in 2016. So, this is a date where prices in the capacity market would start to increase well above the $1.05 initial auction price. Rose noted that is what will drive interest in the PJM style auction.

Burns noted this projected shortage is driven by EPA regulations and the resulting retirements and suspensions of generation capacity within MISO footprint.

MacInnes asked Rose if this is a demand-side opportunity for Michigan. How might that work with v. without a capacity market? Is there an advantage one way or another? Rose responded that you could have a demand response auction and it could give you a pretty good result that he did not think would differ from a capacity auction. Burns added that if you had a DSM-only capacity market, the people engaged in it would take into account their own value of lost load so that you would get rational decision-making by the participants.

MacInnes noted a comment received from a professor at UC Berkley. ERCOT, which has an energy-only market design, commissioned a study by the Brattle Group on low investment level and concerns with the impact on reliability. The main conclusion by Brattle is that even with a $9,000 per megawatt hour price cap, scarcity prices will not assure a sufficient level of investment to meet reliability criteria. So, it seems we're not dealing with efficient market theory. These markets really aren't efficient in many cases. Rose noted that is why many aspects of this business are regulated. That is why he argues that it makes more sense to target adequate compensation to the kind of units that the RTO or ISO needs rather than compensating everything in the RTO.

MacInnes asked how you make sure there is enough to incent people to look forward far enough to assure sufficient capacity? Rose responded that this is not a new question. Utilities have had to do this for a hundred years. They became very sophisticated with forecasting and the RTO forecasting is not that different than a utility, except it is on a much bigger scale.

Isely asked how much trading is going on after the initial auction? Rose responded that the base residual auction is run three years ahead of time. There is an auction one year later where the suppliers can either buy capacity from another source if needed. PJM can also run another auction if it turns out they need more capacity than forecasted. There are also bilateral arrangements. Isely raised concern with strategic choices in the auction. Rose said it is a concern he raised in his paper. The market monitor examines each of the zones and tries to assess the competitiveness. Almost every zone in PJM is judged by the market monitor as uncompetitive because they are highly concentrated. Rose provided an explanation of the market concentration measure used (Herfindahl Hirschman Index, HHI). High market concentration does not necessarily mean you have market power. The market monitor looks at the result of the auction and determined it looked competitive. Rose cited some examples of concern.

At 12:17 p.m., the meeting was adjourned for a fifteen-minute recess.

III. Business Items

a. MEC UCRF Grant Amendment Requests

Bzdok explained MEC has a two-prong transfer requests. He provided a brief update on the status and direction in the renewable energy cases to provide context for their requests.

He then explained that in the current request before the board, MEC's expectation was that Consumers would file an amended filing setting the residential surcharge at 13 cents. MEC intended to argue the residential surcharge, for the reasons provided, should be set at zero. MEC was asking for a budget increase of $10,000 to support intervention on the residential surcharge issue as well as advocating for additional development of Consumers' solar program. The funding and second prong of the transfer was to move $4,000 in returned funds from Synapse to apply to the work on the solar issue. When Consumers made the renewable energy case filing, the proposed residential surcharge was zero. MEC feels the movement of the residential surcharge from $3 to 0 in five years is significant. Therefore they are not asking for the $10,000 budget increase for the case. They still want to advance solar and transfer the $4,000. Bzdok noted the language from the statute the board works under and emphasized the sections MEC believes makes that an appropriate subject of advocacy.

Bzdok concluded with a summary of the work in Consumers Renewable Energy Case. They settled in a case setting a 29 year depreciation life based on Staff transfer prices that arose out of the case that MEC did, and based on self-build versus PPA. That's still probably not totally competitive given the production tax credits apply to the new utility project in the Thumb. The reserve fund is at a hundred some odd million, going to spend down to zero. The capacity factors, which MEC argued needed to be much higher than 27 percent, are now much higher. The numbers projected from Thumb projects are up in the 40s.

There is still work to be done with DTE. MEC has a depreciation case pending. There self-build versus PPA numbers came in very close. The reserve fund is at $260 million. MEC has an issue with the DTE proposals for the rate and level of spending down of that account. They have been aggressive about capacity factors. MEC still wants to continue work on all of those issues. They are not requesting new money, just a transfer of a small amount from the expert line to legal. That is a $2,500 transfer request. It was incorrectly written as $3,500, so the request is amended to $2,500.

Bzdok also mentioned other issues MEC is pursuing with DTE including transfer prices, personal property taxes, ppt replacement mechanisms and easements.

b. RRC UCRF 2013 Grant Request for GCR Reconciliation Cases

Shaltz presented the RRC grant application for GCR Reconciliation cases for Michigan's four major gas companies. The application was originally submitted in August but deferred until closer to the actual filing date. The cases were filed at the commission in June. RRC has done a preliminary review of the filings and prepared an update memo that outlined what they view as the likely issues in the cases. They anticipate a prehearing conference in September and petitions to intervene will be due in mid August. The timing is right for funding decisions on these cases.

Shaltz briefly explained the purpose and process for GCR Plan and GCR Reconciliation cases. He summarized the main points of the memo highlighting what RRC believes may be the key issues in each of the cases. In Consumers Energy GCR Reconciliation U-16924-R they will review and audit operation of storage facilities during the plan year for prudency and possible over-recovery. RRC will also continue to document the performance of the fixed-price purchases so there is a robust historical record to rely on if the issue needs to be addressed going forward. They will monitor effects of gas Customer Choice program on GCR customers , and monitor data for sales forecasting, especially for peak day conditions, to determine if modifications should be made to more accurately reflect what's been going on on their systems.

RRC will also review the normal audit items listed in their original application.

MichCon is now DTE Gas Company. In their GCR Reconciliation Case U-16921-R, there are some deviations from their plan that RRC wants to investigate. For example, gas use and loss figures are lower than what they've shown in prior reconciliations. This has flow-through cost consequences for the GCR customers. DTE Gas has been advocating for third-party sales, so RRC will look closely at storage operations to assure their strategy has not adversely impacted the GCR customers in this period.

Fixed-price purchases resulted in losses of approximately $165 million for their GCR customers in this period. RRC will examine how they actually made their fixed price-purchases in this period to determine if they were compliant with their own guidelines and approved plan.

RRC will also look at the gas Customer Choice issue and the use factors and peak day issues to examine whether to those need to be modified.

In SEMCO GCR Reconciliation case U-16922-R, RRC will investigate if fixed-price purchases, especially intra-month service, and if the use of peaking service were made in accordance with their plan.

In MGUC GCR Reconciliation case, RRC will examine the company's storage operations, their monthly purchases, their hedging program, and audit their reported over- and under-recoveries.

The budget requested for each of the four cases is the same as in the original grant application, $27,270 each, for a total budget of $109,080, with administrative expenses at or below one percent of the authorized budget. Budget amendments may be requested based on what actually happens in the case.

MacInnes commented that in the previous year, RRC achieved some successful results and cost savings to ratepayers. He also noted that deferring grant funding until there is more information available really helps the board to decide how to best award limited UCRF funds.

Isely asked Shaltz to spend a few minutes discussing the anticipated workload among the four cases, especially compared to their experience and resources in the cases the previous year. Shaltz noted that the board's approach of awarding more limited funds initially and asking grantees to return to the board if the workload or case requires additional resources has resulted in grantees acting with more prudency and discernment on the issues they pursue in cases. It has been positive. MacInnes commented that as they get into the cases further, and there are real opportunities for benefit, the board is open to considering additional funding if it makes sense.

c. RRC UCRF ~~12-04~~ 13-05 Grant Amendment Request

Shaltz commented that RRC has an amendment request before the board. He noted a typographical error in the grant number. The correct grant number is 13-05, not 12-04. The purpose of the request is to reallocate funding among approved cases U-16920, 21, 22, and 24. The result is an overall reduction of $2,000 from the total budget of the approved grant. Two of the cases settled and, therefore, required less funding than expected. The other two cases were fully litigated and require slightly more funding than anticipated but, the full amount of the grant will not be required.

MacInnes conveyed Wilsey's comment that this was the first time in her history working with the board that a grantee had requested a reduction in the grant awarded prior to the expiration of the grant period. Shaltz noted that he had heard the board discuss this as one of their goals – to get timely information from the grantees and if there is a way to better allocate the money or save it for future opportunities, the board would like to know about it as soon as possible.

MacInnes thanked Shaltz for his recognition and action. MacInnes said the board wants to meter the money out carefully and provide resources for the best opportunities.

At 1:18 p.m. there was a 30 minute recess.

MacInnes called for motions on the business items presented to the board.

Isely moved, second by Dinkgrave, and motion carried to approve MEC grant request to transfer $2,500 from the expert to legal line item in case U-17302, DTE Renewable Energy Biennial Plan Review (2013).

Isely moved, second by Dinkgrave, and motion carried to approve the RRC Grant Amendment to UCRF 13-05 as presented.

Cases	**Authorized Budget**	**Change Requested**	**Amended Budget**
MGUC Case No. U-16920	$ 17,409.60	$ 225.00	$ 17,634.60
MichCon Case No. U-16921	$ 27,590.40	$ (1,229.40)	$ 26,361.00
SEMCO Case No. U-16922	$ 17,409.60	$ (865.80)	$ 16,543.80
Consumers Case No. U-16924	$ 27,590.40	$ (138.60)	$ 27,451.80

Isely moved, second by Haroutunian, and motion carried to approve the RRC fiscal year 2013 UCRF grant request in a total amount of $70,000 for the Consumers energy, DTE Gas Company, SEMCO and MGU GCR Reconciliation cases for the 2012-13 year.

In discussion, Smith noted that the amount recommended for approval was in line with historic expenditures on these cases and that a new grant cycle was approaching. If there are issues or need for additional resources, RRC should return to the board for further funding consideration.

MacInnes asked if there were any further motions. Isely noted that the MEC request to transfer $4,000 from the general rate case to the biennial review case was not overlooked, there just was no motion for approval made. MacInnes concurred.

d. Final Approval of Annual Report

Wilsey presented the 2012 Annual Report to the Board and requested it be approved. She reported that the substantive comments received after the draft was issued included:
Don Keskey requested his decision rendered in 2012 on UCRF 2010 grant made to PIRGIM be included in the report. It was reviewed and included. It was a decision affirming a previous MPSC ruling. There was no direct monetary claims, it didn't change the benefits calculation. It simply was an order and additional information related to a previously funded case. The content was incorporated in the attached Item A, at page 21.

David Shaltz provided additional detail for the results section on benefits achieved in various cases decided in 2012. Many of these cases were settled and results could not be attributed solely from the public record.

RRC's summary was consistent with results reported in previous case status reports provided to the board. These results did impact the net benefits highlighted in the annual report. The explanation and details are included "verbatim" in the report on p. 27 and were distributed for public comment. No issues with the claims were raised during the review.

Chris Bzdok requested a breakdown of remittances from Consumers Energy gas and electric customers, he also provided comment on the legislative review, Section 5, Items 2 and 3. I did receive from data from Shawn Worden of LARA that will allow us to do the breakdown of remittances between Consumers gas and electric customers. This information was not revised in this report as it will need further verification. The breakdown will be presented in future annual reports.

The comments on the legislative review section were incorporated at pages 11 and 12 of the report. The legislative review of 1986 is incorporated in the annual report and has been in the form that it was presented when the review was done. This is not modified. However, this year comments received relative to the legislative review are included to provide documentation of questions, comments, observations of parties that have interest in UCPB over time. There
were some additional, nonmaterial edits, formatting, et cetera.

MacInnes suggested possibly looking at cost / benefit for the electric and gas cases separately in future reports. This may help determine where funds are producing the most benefit.

Wilsey stated that for this report, the total amount of benefits reported (50 million and the 133.22 million) can be calculated from Section 3, UCRF grant recipient results. The 50 million is the total of item 1, and items 5-19. The $133 million is the total of items 2-4.

<u>Smith moved, second by Dinkgrave, and motion carried to approve the final draft of the annual report as presented.</u>

e. UCPB Staff Contract Extension

MacInnes asked if there was any comment or motion on the one-year contract extension proposal for Michelle Wilsey. Positive comments were made by the board. <u>Smith moved, second by Isely, and motion carried to approve the one-year contract extension for Michelle Wilsey as presented.</u>

MacInnes asked Wilsey to comment on the technology initiative mentioned in her recommended scope of work. Wilsey noted she would like to allocate a portion of the existing contract to investigating automation of some of the routine workflow and business processes of the board. She will work with LARA to understand the technology resources that may already be available to the board through the State of Michigan. Other opportunities will be considered as well, in close consultation with LARA management. The intent is to use 40-45 hours of the existing contract to initial research. MacInnes noted that there is an executive directive 2012-1 from John Nixon to the Governor about using IT more extensively and strategically. Dinkgrave commented that he supported the concept and volunteered his assistance in the process. MacInnes noted that capturing this information more systematically would also be a benefit to future boards.

f. Grantee Reports

MacInnes invited Keskey to provide a status report. Keskey focused his report on the REF issues. The Commission issued a decision at the end of June in Detroit Edison's PSCR plan case, U-17892, that essentially ruled against the issue. He elaborated on the arguments in the case and expressed disappointment in the

Commission decision. MacInnes asked if it makes the market more uncompetitive on a marginal basis. Keskey responded affirmatively.

Liskey stated that CARE had submitted it's report to the board and would entertain any questions. MacInnes asked if CARE was participating in the capacity market study group with MISO. Liskey responded that Rose was participating in the group – it is called the Supply Adequacy Working Group. Other groups deal with the issue as well but SAWG is the primary committee.

Burns commented that he had additional information on loop flows. Burns generally explained the concept of loop flows and provided an example of the Lake Erie loop flow. He described how problematic they can be and technology they are using to reduce the problems from loop flow.

IV. Public Comment
Wilsey noted that UCRF grant applications submitted for the 2014 cycle would be reviewed beginning at the August 26, 2013. Prospective grantees are invited to give oral presentations.

The retirement of Wes VanMalsen, LARA was announced.

V. Next meeting - MacInnes announced the next meeting of the board is scheduled Monday, August 26, 11:00 a.m.

VI. Adjournment – <u>Isely moved, second by Haroutunian, and motion carried to adjourn at 2:30 p.m.</u>

Recorded by:
Michelle Wilsey, Board Assistant
Utility Consumer Participation Board

Transcript available.