STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter, on the Commission's own motion, to initiate a proceeding to establish a state compensation mechanism for alternative electric supplier capacity in **INDIANA MICHIGAN POWER COMPANY's** Michigan service territory.	))))))	Case No. U-17032

At the January 31, 2013 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. John D. Quackenbush, Chairman
Hon. Orjiakor N. Isiogu, Commissioner
Hon. Greg R. White, Commissioner

ORDER

On February 29, 2012, on behalf of Indiana Michigan Power Company (I&M), American Electric Power Service Corporation filed a formula rate template with the Federal Energy Regulatory Commission (FERC) under which I&M would calculate its capacity charges pursuant to Section D.8 of Schedule 8.1 of the Reliability Assurance Agreement (RAA) among load serving entities (LSEs) in the PJM Interconnection, L.L.C. (PJM) region. *See*,16 USC 824d; and 18 CFR 35.1 and 35.13. The PJM capacity market allows for a method of participation known as the Fixed Resource Requirement (FRR) Alternative, which provides an LSE with the option to submit an FRR Capacity Plan. The RAA sets forth the rules of participation in the PJM capacity market and establishes the capacity obligations of PJM LSEs in Section D.8 of Schedule 8.1 as follows:

> In a state regulatory jurisdiction that has implemented retail choice, the FRR Entity must include in its FRR Capacity Plan all load, including expected load growth, in

> the FRR Service Area, notwithstanding the loss of any such load to or among alternative retail LSEs. In the case of load reflected in the FRR Capacity Plan that switches to an alternative retail LSE, where the state regulatory jurisdiction requires switching customers or the LSE to compensate the FRR Entity for its FRR capacity obligations, such state compensation mechanism will prevail. In the absence of a state compensation mechanism, the applicable alternative retail LSE shall compensate the FRR Entity at the capacity price in the unconstrained portions of the PJM Region, as determined in accordance with Attachment DD to the PJM Tariff, provided that the FRR Entity may, at any time, make a filing with FERC under Sections 205 of the Federal Power Act proposing to change the basis for compensation to a method based on the FRR Entity's cost or such other basis shown to be just and reasonable, and a retail LSE may at any time exercise its rights under Section 206 of the FPA.

Thus, a state regulatory jurisdiction may formulate a state compensation mechanism (SCM) for determining capacity charges applicable to choice customers in the PJM region; and, in the absence of an SCM, the utility may make a filing with FERC seeking authorization for a cost based compensation method.

Consistent with I&M's capacity obligations under the RAA, I&M proposed that it recover capacity costs from alternative electric suppliers (AESs) in Michigan, and requested that FERC issue an order permitting the proposed capacity rate to become effective on May 1, 2012. I&M's FERC filing was docketed as Docket No. ER12-1173-000. At the time of the FERC filing, I&M had no open access distribution (OAD) customers, and there was no SCM in Michigan. In anticipation of enrolling choice customers, I&M made the FERC filing pursuant to its right under the RAA to seek FERC's approval of a cost-based compensation method.

Notice of I&M's filing was published in the Federal Register, 77 Fed. Reg. 14,357 (2012). The Commission filed a notice of intervention in order to seek an opportunity to establish its own SCM. On April 30, 2012, FERC issued an order in Docket No. ER12-1173-000 accepting I&M's proposed formula rate but suspending implementation of that rate for five months, and setting the matter for hearing and settlement procedures. The rate would become effective on October 1, 2012. Thus, FERC afforded the Commission five months to create an SCM.

On May 14, 2012, I&M began enrolling OAD customers, and the program initially reached its 10% cap in July 2012.

On May 24, 2012, the Commission issued an order in this docket stating:

> Because the rules of participation in the PJM Capacity Market recognize and give prevalence to how a duly created state compensation mechanism provides for a switching customer or its LSE to compensate the FRR Entity for its FRR capacity obligations, the Commission is persuaded that it should commence this proceeding, on its own motion, to establish a state compensation mechanism for AES capacity in I&M's Michigan service territory.

Order, p. 4. The Commission set an aggressive hearing schedule in order to issue a final order before the October 1, 2012 deadline set by FERC. In addition, the Commission required, "I&M [to] file a cost of service based proposal in this docket for the creation by the Commission of a state compensation mechanism for alternative electric supplier capacity in its Michigan service territory." *Id.* A prehearing conference was held on June 28, 2012, at which Administrative Law Judge Sharon L. Feldman granted intervention to, among others, Energy Michigan. Evidentiary hearings were held, and the Commission read the record.

On September 25, 2012, the Commission issued an order (September 25 order) establishing an SCM and setting capacity rates for I&M's OAD customers. The Commission found that Section D.8 of Schedule 8.1 of the RAA provides for an SCM, and that FERC intended FRR entities to be compensated based on state ratemaking principles, rather than federal wholesale rates. In setting cost based rates, the Commission relied on the cost of service study (COSS) produced by I&M in its last rate case, Case No. U-16801, which was slightly adjusted for this proceeding by both I&M and the Commission Staff (Staff). *See,* February 15, 2012 order in Case No. U-16801; 3 Tr 404-407.

On October 19, 2012, Energy Michigan filed a petition for reopening under 1999 AC, R 460.17401(1) (Rule 401(1)) and rehearing under 1999 AC, R 460.17403 (Rule 403). On

November 2, 2012, I&M filed a response to the petition, and on November 9, 2012, the Staff filed a response to the petition.

In its petition Energy Michigan contends that, in the September 25 order, the Commission indicated its willingness to reconsider the rate set for OAD customers, and to consider changes to the off system sales (OSS) sharing of revenues, in the next I&M rate case. Energy Michigan argues that instead of waiting for an indefinite time period for the next rate case, the Commission should reopen this case and require the new COSS now, and set new rates.

Energy Michigan repeats the argument made in the proceeding that the COSS from Case No. U-16801 is not accurate or binding as to Rate OAD because it did not include cost allocations to OAD customers. Energy Michigan rejects the Commission's claim that the October 1, 2012 FERC deadline created any time pressure. Energy Michigan points to the Commission's acknowledgement that the capacity rate established in Case No. U-16801 pursuant to settlement should be reevaluated when I&M files its next general rate case. Energy Michigan posits that the capacity rates set in the September 25 order will produce large losses for OAD customers, and will force OAD customers to abandon choice service immediately.

Energy Michigan further contends that the Commission made demonstrable errors in setting the mandatory 75/25 allocation method, because OAD customers do not use energy. Because OAD customers use no energy supplied by I&M, Energy Michigan argues, the 75/25 allocation violates MCL 460.11(6), which requires the setting of cost based rates. Energy Michigan maintains that it "is not discriminatory to reduce the allocation of costs to a rate class based upon the actual energy use of the rate class as compared to costs allocated to rates that use more energy." Petition for reopening and rehearing, p. 4. Energy Michigan contends that its request is

consistent with Michigan ratemaking principles, and is consistent with how ratemaking is applied to other low energy use rates such as standby service.

Energy Michigan further argues that the "amount of OSS credit to OAD customers is insufficient because full service customers get the benefit of low cost I&M energy in the below-market price they pay for I&M energy, plus they get a share of the OSS revenues." *Id.*, p. 6. Energy Michigan claims that, since it is understood that OAD service was not addressed in Case No. U-16801, there is no record to support the suitability of the OSS mechanism for OAD service determined in the September 25 order. Energy Michigan complains that the OSS credit is fixed at a low point because it is based on the low projection of OSS submitted by I&M in the last rate case, whereas the credit given to full service customers escalates as the amount of OSS volume escalates. Energy Michigan claims that OAD customers are not able to participate in the increased benefit which they created for full service customers. Energy Michigan concludes that the September 25 order will end competition on I&M's system. *Id.*, p. 9.

In response, I&M argues that Energy Michigan fails to explain what additional evidence has been discovered or what change in circumstances has taken place such as to warrant reopening or rehearing. I&M notes that reopening is not proper when the newly proposed evidence was available at the time of the hearing; and that rehearing is not proper when the petition simply disagrees with the result reached by the Commission. With regard to the allocation of production costs, and Energy Michigan's statements about the demise of competition, I&M argues that the Commission squarely addressed these issues in the September 25 order, and states that, since issuance of that order, OAD customers have increased and no OAD customer has returned to full service. I&M's response, p. 4, n. 1. Likewise, I&M notes, the Commission addressed the issue of

the reliability of the COSS, and the allocation of OSS margins in the September 25 order. I&M points out that Energy Michigan had every opportunity to present evidence regarding the COSS.

The Staff also opposes the petition to reopen and rehear this matter. The Staff notes that Energy Michigan simply reiterates the arguments made and rejected in the proceeding. The Staff contends that evidence regarding a new or revised COSS, and evidence concerning the allocation of OSS credits, could have been presented by Energy Michigan in the proceeding. Finally, the Staff points out that the Commission took into account, in its consideration of the issues, the fact that the timing of the next rate case is unknown.

The Commission agrees with the Staff and I&M and rejects the petition for reopening or rehearing on grounds that the petition fails to meet the standards set out in Rules 401 and 403. Energy Michigan has failed to show that further evidence is necessary in order to have a full and complete hearing in this matter, or that there has been a change in facts or law; nor has the intervenor shown errors, newly discovered evidence, or unintended consequences of the September 25 order. Energy Michigan has presented only arguments that were presented in the proceeding and explicitly rejected by the Commission in the September 25 order. The Commission's indication that it will reevaluate capacity rates in a future rate case does not constitute an error, a change in facts, or an unintended consequence, nor is it evidence that the record was incomplete. Rate cases are for reevaluating rates. *See,* September 25 order, p. 29.

With regard to Energy Michigan's complaints about the COSS, the Commission stated:

> The Commission finds persuasive I&M's and the Staff's arguments that the COSS may be considered as a starting point for the SCM. The Commission notes that during the evidentiary hearing, the ALJ stated that "it is not clearly unreasonable or improper for I&M to look to its most recent cost-of-service study in responding to the Commission's order in this proceeding." 2 Tr 78. The Commission agrees. And, as argued by I&M, the company is not using the settlement agreement to foreclose a challenge to the SCM and is not attempting to change any of the rates set by the settlement agreement. As a result, the Commission finds that because

> the COSS is merely a starting point for the SCM, the parties were free to propose modifications to the COSS.
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> The Commission also finds that I&M was not required to provide testimony and evidence to again support the COSS. A review of the record in this case shows that the intervenors made no attempt to challenge the evidence underlying the COSS in Case No. U-16801. Citing *Pennwalt v Public Service Comm*, 166 Mich App 1 (1992), the Commission has found that, "the Commission does not have to expend resources on repetitious litigation of ratemaking issues." December 20, 1995 order in Case No. U-10490-R, p. 5. Therefore, the Commission finds that, absent a challenge by the intervenors, I&M was not required to place into evidence any documents or testimony to support its COSS in this proceeding, and the Staff was not required to perform any additional independent analysis or investigation of the COSS.

September 25 order, pp. 28-29. Turning to Energy Michigan's complaints about the allocation method, the Commission stated:

> Regarding I&M's 75/25 allocation method, Energy Michigan argued that I&M should have reduced the OAD rate by 25% to account for zero energy supplied by I&M to OAD customers. The Commission finds that the intervenors did not demonstrate that I&M's cost allocation actually allocates energy costs to OAD customers. Therefore, the Commission is persuaded that I&M's 75/25 cost allocation accurately and fairly allocates energy costs to classes. In addition, the Commission notes that if the capacity rate is reduced by 25% as recommended by Energy Michigan, OAD customers will only be paying for 75% of capacity costs, while standard service customers will pay 100%. Such ratemaking is discriminatory and inconsistent with Michigan's ratemaking principles.

Id., p. 30. With regard to competition:

> The intervenors argued that adoption of I&M's and the Staff's proposed capacity rates would result in the elimination of competition in I&M's service territory. The Commission agrees with I&M and the Staff that MCL 460.10 does not direct the Commission to elevate competition above all other ratemaking principles. Competition is one of several goals outlined in the statute, but it does not take precedence over the other Michigan-specific ratemaking principles. In addition, the Commission notes that adoption of I&M's proposed SCM will not end competition in I&M's Michigan service territory. The fact that AESs cannot provide energy service to choice customers at a lesser price than I&M does not mean competition does not exist.

Id., p. 31. And with regard to the OSS margins, the Commission found:

> In reviewing the record, the Commission notes that I&M made the persuasive distinction that OAD customers are paying for capacity *service*, not capacity in the literal sense. OAD customers are not paying for depreciation or other operating expenses, and they are not entitled to any ownership interest, legal or equitable, in the property used to provide service. Therefore, the Commission finds that because OAD customers are paying for service, they do not have a legal or equitable claim to more of the OSS margins. In addition, all of the cases cited by intervenors as support are distinguishable from the present case because they involve stranded costs, which are not at issue in this case. As a result, the Commission does not find persuasive any of the intervenors arguments to alter or increase the OSS credit for OAD customers.

Id., pp. 31-32. Thus, Energy Michigan makes no argument in its petition that was not explicitly addressed in the September 25 order. The petition for reopening and rehearing is denied.

THEREFORE, IT IS ORDERED that the petition for reopening and rehearing filed by Energy Michigan is denied.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, under MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

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John D. Quackenbush, Chairman

By its action of January 31, 2013.

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Orjiakor N. Isiogu, Commissioner

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Mary Jo Kunkle, Executive Secretary

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Greg R. White, Commissioner