STATE OF MICHIGAN

COURT OF APPEALS

FILED

NOV 19 2003

MICHIGAN PUBLIC SERVICE COMMISSION

CONSUMERS ENERGY COMPANY,

Appellant,

v

MICHIGAN PUBLIC SERVICE COMMISSION, MIDLAND COGENERATION VENTURE LIMITED PARTNERSHIP, ABATE, ENERGY MICHIGAN, INC, DETROIT EDISON COMPANY, WISCONSIN PUBLIC SERVICE CORPORATION, UPPER PENINSULA POWER COMPANY, WISCONSIN ELECTRIC POWER COMPANY, WE ENERGIES, EDISON SAULT ELECTRIC COMPANY, NORTHERN STATES POWER COMPANY WISCONSIN, XCEL ENERGY, DOW CORNING CORPORATION, HEMLOCK SEMICONDUCTOR CORPORATION, CITIZENS FOR POWER AND RELIABILITY, and ATTORNEY GENERAL,

Appellees.

UNPUBLISHED
November 18, 2003

No. 241990
PSC
LC No. 00-012639

DETROIT EDISON COMPANY,

Appellant,

v

MICHIGAN PUBLIC SERVICE COMMISSION, ABATE, ENERGY MICHIGAN, INC, WISCONSIN PUBLIC SERVICE CORPORATION, UPPER PENINSULA POWER COMPANY, WISCONSIN ELECTRIC POWER COMPANY, WE ENERGIES, EDISON SAULT ELECTRIC COMPANY, NORTHERN STATES POWER COMPANY WISCONSIN, XCEL ENERGY, CONSUMERS ENERGY COMPANY,

No. 241991
PSC
LC No. 00-012639

DOW CORNING CORPORATION, HEMLOCK SEMICONDUCTOR CORPORATION, CITIZENS FOR POWER AND RELIABILITY, and ATTORNEY GENERAL,

Appellees.

Before: O'Connell, P.J., and Jansen and Wilder, JJ.

PER CURIAM.

In these consolidated appeals, appellants Consumers Energy Company and Detroit Edison Company appeal as of right the order of the Public Service Commission (PSC) implementing provisions of the Customer Choice and Electricity Reliability Act, MCL 460.10a(1). We affirm.

This case arises out of a significant restructuring of Michigan utilities law to allow retail customers of electric utilities to purchase electricity from alternative suppliers. The retail open access (ROA) program began as an experimental program offered by Detroit Edison and Consumers Energy under the direction of the PSC. After a number of orders were issued implementing the program, the Supreme Court found that the PSC exceeded its statutory authority in establishing the program. *Consumers Power Co v Public Service Comm,* 460 Mich 148; 596 NW2d 126 (1999).

Partly in response to the Supreme Court's decision, the Legislature passed the Customer Choice and Electricity Reliability Act, 2000 PA 141 and 2000 PA 142. The purposes of the act are to ensure choice of electric suppliers, to encourage the PSC to foster competition in the provision of electric supply, encourage the development and construction of merchant plants, to ensure that all persons are provided safe, reliable power at a reasonable rate, and to promote economic development. MCL 460.10(2). The act provides that previous PSC orders concerning alternative electricity providers are enforceable by the PSC. MCL 460.10a(5).

In the prior cases, the PSC considered how to handle certain stranded costs incurred by utilities in instituting the ROA program. In PSC Case No. U-11290, the PSC defined these costs as costs incurred during the regulated era that will be above market prices, and costs necessary to facilitate the transition to competitive markets. Five categories of stranded costs were identified: (1) Regulatory assets consisting of unrecovered costs of demand side management programs, (2) capital costs of nuclear plants, (3) contract capacity costs arising from power purchase agreements, (4) employee retaining costs, (5) and costs related to the implementation of restructuring.

In addition to validating the prior PSC orders concerning alternative electric suppliers, the Legislature included specific provisions concerning stranded costs. MCL 460.10a(1) provides:

> No later than January 1, 2002, the commission shall issue orders establishing the rates, terms, and conditions of service that allow all retail

customers of an electric utility or provider to choose an alternative electric supplier. The orders shall provide for full recovery of a utility's net stranded costs and implementation costs as determined by the commission.

The PSC initiated this action to determine net stranded costs as required by MCL 460.10a(1). The Legislature granted the PSC broad power to determine stranded costs:

> (10) The commission shall consider the reasonableness and appropriateness of various methods to determine net stranded costs, including, but not limited to, all of the following:
>
> (a) Evaluating the relationship of market value to the net book value of generation assets and purchased power contracts.
>
> (b) Evaluating net stranded costs based on the market price of power in relation to prices assumed by the commission in prior orders.
>
> (c) Any other method the commission considers appropriate. [MCL 460.10a(10)].

The PSC adopted its staff's proposal for determining net stranded costs by using historical information. Stranded costs would be the difference between each year's revenue requirement associated with fixed generation assets, generation-related regulatory assets, and capacity payments associated with PPAs (power purchase agreements) and that year's revenues available to cover those costs. Variable costs would be excluded, as they are avoidable. Net stranded costs were defined as costs that would have been recovered under regulation that cannot be recovered under competition, offset by mitigation and stranded benefits.

Appellants object to three aspects of the PSC decision. The PSC retained a securitization credit for ROA customers that appellants believe violates the statute and provides an unreasonable subsidy, discriminating against full service customers. The PSC rejected appellants' proposal to make an adjustment for the skewing of rates, so that residential and commercial customers have equal incentive to use the ROA program. Finally, appellants assert that the PSC adopted a deferred method for recovering stranded costs that violates the statute and constitutes improper retroactive ratemaking.

Appellate review of PSC orders is narrow in scope. All rates, fares, regulations, practices and services prescribed by the PSC are deemed prima facie to be lawful and reasonable. MCL 462.25. The party attacking an order of the PSC bears the burden of proving by clear and satisfactory evidence that the order is unlawful or unreasonable. MCL 462.26(8). A decision of the PSC is unlawful when it involves an erroneous interpretation or application of the law and it is unreasonable when it is unsupported by the evidence. *ABATE v PSC*, 219 Mich App 653, 659; 557 NW2d 918 (1996). To the extent that the decision is based on findings of fact, the challenger must show that those findings are not supported by competent, material, and substantial evidence on the whole record. *Id.* This Court gives due deference to the administrative expertise of the PSC, and will not substitute its judgment for that of the PSC. *Id.*

I.

Along with authorizing the ROA program, the Legislature simultaneously enacted other measures to reorganize the utility industry. 2000 PA 142 allowed the PSC to issue financing orders authorizing Detroit Edison and Consumers Energy to issue securitization bonds to refinance certain qualified costs. MCL 460.10i. Qualified costs include the utility's regulatory assets plus costs the utility will not be able to recover in a competitive market, including ROA implementation costs, costs of restructuring, costs of buying out or buying down power purchase contracts, and the costs of the securitization process. MCL 460.10h(g). Appellants were authorized to collect securitization charges from their customers under financing orders. MCL 460.10h(i); MCL 460.10j. Implementation costs of the ROA program for the years before 2000 were recovered through securitization.

MCL 460.10d(1) provides for a 5% rate reduction from rates in effect for appellants on May 1, 2000. These reduced rates are frozen until December 31, 2003, unless otherwise reduced by the PSC. The rate reduction was enabled by the securitization financing of qualified costs provided for by MCL 460.10i. MCL 460.10d(6) states:

> (6) Except for savings assigned to the low-income and energy efficiency fund under subsection (7), securitization savings greater than those used to achieve the 5% rate reduction under subsection (1) shall be allocated by the commission to further rate reductions or to reduce the level of any charges authorized by the commission to recover an electric utility's stranded costs. The commission shall allocate approved securitization, transition, stranded, and other related charges and credits in a manner that does not result in a reallocation of cost responsibility among the different customer classes.

Securitization bonds are to be paid off through a securitization charge that is not bypassable. MCL 460.10k(2). A nonbypassable charge is a charge in a financing order payable by a customer to an electric utility regardless of the identity of the customer's electric generation supplier. MCL 460.10h(f). Thus, securitization charges must be paid by both full service and ROA customers.

An offsetting credit, effectively eliminating the securitization charge, was established in the previous cases involving the securitization orders. The PSC found that the credit was necessary to give both full service and ROA customers the benefit of the 5% rate reduction mandated by MCL 460.10(d)(1). The former rates were based on assets for which the securitization charge was also assessed, creating the possibility of charging twice for the same service.

The PSC noted that it had assumed in the securitization case that a transition charge would be imposed before January 1, 2002, rendering the securitization offset unnecessary. The PSC found that the determination of a transition charge, that recognized the effect of securitization on stranded costs, had yet to be made.

> Because neither utility has stranded costs at this time, the Commission has found that each is recovering all of its fixed generation costs, including the costs that

were securitized. Thus, there is no basis for requiring ROA customers to pay the securitization and tax charges without a full offset.

The PSC opinions in the securitization cases provide that full service customers will continue to receive the offset to the securitization charge until a full rate case removes the qualified securitized assets from the rate base. This case merely preserves the status quo. Appellants have failed to show a change in circumstances that has led to a violation of the Act. Although appellants expected the PSC to make changes, there is no showing that the decision of the PSC was unreasonable or unlawful. See MCL 462.26(8); *ABATE, supra* at 659.

II.

Electricity rates in Michigan are skewed to the benefit of residential customers. Consumers Energy proposed to adjust for this skewing to equalize the incentive for all customers to participate in ROA, and to balance its loss of lucrative commercial accounts with a loss of residential accounts.

MCL 460.10(2)(a) states that one of the purposes of the act is "[t]o ensure that all retail customers in this state of electric power have a choice of electric suppliers." Another purpose is to "promote financially healthy and competitive utilities in this state." MCL 460.10(2)(e). MCL 460.10a(1) requires the commission to issue orders "establishing the rates, terms, and conditions of service that allow all retail customers of an electric utility or provider to choose an alternative electric supplier..." MCL 460.10d(6) provides in part:

> The commission shall allocate approved securitization, transition, stranded, and other related charges and credits in a manner that does not result in a reallocation of cost responsibility among the different customer classes.

Rates were skewed before 2000 PA 141 was adopted. The Legislature is presumed to be aware of the prior rulings of an administrative agency when it enacts legislation. *Parker v Byron Center Public Schools Bd of Education,* 229 Mich App 565, 570; 582 NW2d 859 (1998). Had the Legislature intended to eliminate skewing, it would not have included language in the statute barring the reallocation of cost responsibility among the customer classes. Therefore, the PSC properly interpreted § 10d(6), and rejected the proposed skewing adjustment. See *ABATE, supra* at 659.

III.

MCL 460.10a(1) provides:

> No later than January 1, 2002, the commission shall issue orders establishing the rates, terms, and conditions of service that allow all retail customers of an electric utility or provider to choose an alternative electric supplier. The orders shall provide for full recovery of a utility's net stranded costs and implementation costs as determined by the commission.

Appellants read this provision as requiring the PSC to enter an order allowing them to recover all their stranded costs by January 1, 2002. The PSC made the future recovery contingent on the success of the ROA program.

The PSC is given wide power to determine stranded costs by MCL 460.10a(10). In ruling on implementation costs, the PSC stated:

> The commission rejects Consumers' and Detroit Edison's proposals to use a portion of the securitization savings to pay implementation costs. The Commission has addressed the recovery of implementation costs in prior orders, and finds no reason to change those determinations at this time. The Commission has ruled that recovery of implementation costs is conditioned upon the success of the utilities in implementing the ROA programs. July 11, 2001 order, Case No. U-12358, p. 10, and October 24, 2002 order, Case Nos. U-11955 and U-12956, p. 5. The record in this case does not provide a basis for concluding that the utilities' programs have been sufficiently successful to merit full recovery of previously reviewed implementation costs, must less costs that are at issue in pending cases or costs that have not even been incurred.
>
> The Commission reaffirms that it will permit the utilities to recover prudently incurred implementation costs as provided for in the Commission's prior orders. It expects to provide recovery at the conclusion of the rate freeze. Except for any costs that should be assigned solely to ROA customers, implementation costs will be recovered from all customers. The Commission may provide for residual securitization savings to fund all or a portion of the recovery.

The PSC held that the parties did not present sufficient record evidence to make the calculation. Appellants have not shown that this decision was erroneous. See *ABATE, supra* at 659.

Appellants argue that the PSC improperly deferred a recovery, and made it contingent on factors outside of their control. However, the methodology used by the PSC is in accord with standard utility rate determination practice.

Retroactive ratemaking in utility cases is prohibited. *Detroit Edison Co v PSC,* 416 Mich 510, 523; 331 NW2d 159 (1982). Utility rates are set on the basis of estimates of costs. When the estimates prove inaccurate, the previously set rates cannot be changed to correct the error. *Id.* The only step the PSC can take is to prospectively revise rates in order to better estimate costs. *Id.*

The reasonableness of a utility's costs cannot always be predetermined. A utility runs the risk that the PSC will determine after the fact that costs were not prudently incurred, and that a recovery will be denied. The PSC held that it would determine the prudence of implementation expenses in light of the success of the ROA program. There is no showing that this poses a greater than normal risk to the utilities.

Appellants argue that the deferral of a ruling violates § 10a(1), requiring the PSC to issue orders by January 1, 2002, providing for the full recovery of net stranded costs and implementation costs. The PSC stated:

> The Commission agrees that it is necessary to explicitly establish the stranded cost charges to be in effect as of January 1, 2002, and sets the charge at zero for both Consumers and Detroit Edison. The record shows both utilities to have stranded benefits at this time. The utilities bear the burden of proof to establish any charge greater than zero, and neither has carried that burden in this case. Rather, they have offered methodologies that the Commission finds fundamentally flawed, and have not offered data upon which to make revised calculations.

Appellants are entitled to a full recovery of their implementation costs. The PSC could reasonably conclude that the evidence presented was insufficient to support the implementation cost claim. The PSC order allows the utilities to recover appropriate costs in the future:

> The Commission reaffirms that it will permit the utilities to recover prudently incurred implementation costs as provided for in the Commission's prior orders. It expects to provide recovery at the conclusion of the rate freeze. Except for any costs that should be assigned solely to ROA customers, implementation costs will be recovered from all customers. The Commission may provide for residual securitization savings to fund all or a portion of the recovery.

The decision of the PSC was consistent with the statute, and does not constitute retroactive ratemaking. Where the evidence was insufficient to allow the PSC to accurately determine the proper amount of implementation costs and whether those costs were prudently incurred, the PSC properly deferred that determination.

Affirmed.

/s/ Peter D. O'Connell
/s/ Kathleen Jansen
/s/ Kurtis T. Wilder