

**STATE OF MICHIGAN
IN THE SUPREME COURT**

**Appeal from the Michigan Court of Appeals
Judges: Markey, PJ. and Saad and Wilder, JJ. (Nos. 134667-9)**

**ATTORNEY GENERAL MICHAEL A. COX
Appellant,**

v

**MICHIGAN PUBLIC SERVICE COMMISSION,
DETROIT EDISON COMPANY, ENERGY
MICHIGAN, INC., and CONSTELLATION
NEW ENERGY, INC.,
Appellees,**

**Supreme Court No. 134667
Court of Appeals No. 259845
MPSC No. U-13808**

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**BRIEF OF MICHIGAN ELECTRIC AND GAS ASSOCIATION, MICHIGAN
ELECTRIC COOPERATIVE ASSOCIATION, WOLVERINE POWER SUPPLY
COOPERATIVE, INC., INTERNATIONAL TRANSMISSION COMPANY, MICHIGAN
ELECTRIC TRANSMISSION COMPANY, AMERICAN TRANSMISSION COMPANY
LLC and ATC MANAGEMENT INC. AS *AMICUS CURIAE* ON THE ISSUE OF
INCLUDING TRANSMISSION COSTS IN THE POWER SUPPLY COST RECOVERY
PROCEDURES**

Dated: January 8, 2009

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**STATE OF MICHIGAN
IN THE SUPREME COURT**

**Appeal from the Michigan Court of Appeals
Judges: Markey, PJ. and Saad and Wilder, JJ. (Nos. 134667-9)**

**DETROIT EDISON COMPANY,
Appellee,**

v

**Supreme Court No. 134668
Court of Appeals No. 264099
MPSC No. U-13808**

**MICHIGAN PUBLIC SERVICE COMMISSION,
ASSOCIATION OF BUSINESSES ADVOCATING
TARIFF EQUITY, MICHIGAN ENVIRONMENTAL
COUNCIL, PUBLIC INTEREST RESEARCH
GROUP IN MICHIGAN, and CONSTELLATION
NEWENERGY, INC.,
Appellees,**

and

**ATTORNEY GENERAL,
Appellant.**

**ATTORNEY GENERAL,
Appellant,**

v

**Supreme Court No. 134669
Court of Appeals No. 264191
MPSC No. U-13808**

**MICHIGAN PUBLIC SERVICE COMMISSION,
DETROIT EDISON COMPANY, ENERGY
MICHIGAN, INC., CONSTELLATION
NEWENERGY, INC., and ASSOCIATION OF
BUSINESS ADVOCATING TARIFF EQUITY,
Appellees.**

[Caption continued on next page]

(Caption Page 2)

**STATE OF MICHIGAN
IN THE SUPREME COURT**

**Appeal from the Michigan Court of Appeals
Judges: Markey, PJ. and Saad and Wilder, JJ. (Nos. 13431)**

**ATTORNEY GENERAL OF THE
STATE OF MICHIGAN
Appellant,**

**Supreme Court No. 136431
Court of Appeals No. 261747
MPSC No. U-13197**

v

**MICHIGAN PUBLIC SERVICE COMMISSION,
CONSUMERS ENERGY COMPANY, ADRIAN
ENERGY ASSOCIATION, L.L.C., CADILLAC
RENEWABLE ENERGY, L.L.C., GENESSEE
POWER STATION, L.P., GRAYLING GENERATING
STATION, L.P., HILLMAN POWER COMPANY,
L.L.C., TES FILER CITY STATION, L.P., VIKING
ENERGY OF LINCOLN, INC., VIKING ENERGY
OF McBAIN, INC., and MIDLAND COGENERATION
VENTURE, L.P.**

Appellees.,

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JURISDICTIONAL STATEMENT

Amicus curiae Michigan Electric and Gas Association (“MEGA”), Michigan Electric Cooperative Association (“MECA”), Wolverine Power Supply Cooperative, Inc. (“Wolverine”), International Transmission Company (“ITC*Transmission*”), Michigan Electric Transmission Company LLC (“METC”), American Transmission Company LLC and ATC Management Inc. (referred to together as “ATC”) (collectively all of the preceding entities are called the “Electric Service Providers”) adopt by reference the jurisdictional statements of Appellees The Detroit Edison Company (“Detroit Edison”) and Consumers Energy Company (“Consumers Energy”). The Court’s consideration of this brief is pursuant to Supreme Court rules governing *amicus curiae* briefs, including MCR 7.306(D)(1).

COUNTER-STATEMENT OF QUESTION PRESENTED

Did the Michigan Public Service Commission act within the scope of its statutory authority in authorizing state-regulated public utilities to recover, through the Power Supply Cost Recovery (“PSCR”) process established by MCL 460.6j, the costs for federally-regulated transmission services paid to electric transmission providers?

Appellant Attorney General says, “No.”

Amicus Curiae Electric Service Providers say, “Yes.”

Appellees The Detroit Edison Company and Consumers Energy Company say, “Yes.”

The Michigan Public Service Commission and the Michigan Court of Appeals said, “Yes.”

BRIEF OF MICHIGAN ELECTRIC AND GAS ASSOCIATION, MICHIGAN ELECTRIC COOPERATIVE ASSOCIATION, WOLVERINE POWER SUPPLY COOPERATIVE, INC., INTERNATIONAL TRANSMISSION COMPANY, MICHIGAN ELECTRIC TRANSMISSION COMPANY, AMERICAN TRANSMISSION COMPANY LLC and ATC MANAGEMENT INC. AS *AMICUS CURIAE* ON THE ISSUE OF INCLUDING TRANSMISSION COSTS IN THE POWER SUPPLY COST RECOVERY PROCEDURES

STATEMENT OF INTEREST

The Attorney General’s position concerns the Electric Service Providers because it would require a full contested case rate proceeding, in which all aspects of a state rate-regulated utility’s cost structure must be examined, in order to adjust rates for retail electric service to recover the costs of electric transmission service federally-approved by the Federal Energy Regulatory Commission (“FERC”). This may result in procedural delay and could impair the recovery of actual transmission service costs incurred for the benefit of utility customers. Even under recently enacted Michigan regulatory law changes, general rate proceedings will take 12 months or more to process for the larger state regulated utilities and the ability to obtain timely recovery of transmission expense changes will be restricted. The procedures for power supply cost recovery (or “PSCR”) under MCL 460.6j provide full protection for utility customers because they are contested cases with public notice and regulatory hearings and customer representatives including the Attorney General have public funding for intervention available in these types of proceedings.

The Electric Service Providers include, through their associations, state regulated public utilities with a direct financial interest in timely recovery of costs paid to federally regulated

third party transmission service providers. Their regulatory and financial interests are similar to those of the major utilities involved in this case, Detroit Edison and Consumers Energy.

The Electric Service Providers also include federally regulated transmission service providers ATC, *ITCTransmission* and METC as well as Wolverine, the generation and transmission service provider for its rural electric distribution cooperative members. They have a financial interest insofar as upgrades to the transmission grid are ultimately dependent on the effective and timely ability of the state regulated public utilities to recover their transmission service expenses from customers. All of the Electric Service Providers have an interest in efficient and practical regulatory procedures that also provide adequate protection for utility customer interests.

The Electric Service Providers do not claim an interest regarding the Detroit Edison “control premium” issue also being considered by the Court in these combined cases. Accordingly, they take no position on that issue and the argument presented here concerns only the PSCR question.

STATEMENT OF FACTS AND DESCRIPTION OF THE ELECTRIC SERVICE PROVIDERS

A. Material Facts and Proceedings

The Electric Service Providers adopt the Statements of Fact contained in the briefs of Appellees Detroit Edison, Consumers Energy and the Michigan Public Service Commission (“MPSC” or “Commission”).

The Attorney General’s factual statements characterize the underlying regulatory action of the MPSC as “shifting recovery” of transmission costs from base rates to the PSCR process.

The MPSC actions challenged in this case followed electric industry restructuring in Michigan and elsewhere during the 1990's, which caused a significant portion (but not all) of transmission costs to change from being internal costs of the state regulated utilities, which formerly owned the transmission grid, to a purchased service from newly formed separate transmission service providers. Prior to restructuring, some transmission costs associated with power purchase and exchange transactions were included as PSCR costs of power supply. This distinction was described by the MPSC in its September 16, 2002 Opinion and Order in Wisconsin Electric Power Co., MPSC Case No. U-12725, attached to the Attorney General's brief in Supreme Court Nos. 13667/13668 - Attachment A, pp 15-16.

B. Electric Service Providers

This *amicus curiae* brief uses the term Electric Service Providers as a short form to reference all of the participating utility trade associations and transmission providers. These participants and their operations are further described as follows.

MEGA is a Michigan nonprofit corporation serving as a trade association for its member electric and gas public utilities providing service in Michigan. Its electric utility members are Alpena Power Company, Edison Sault Electric Company ("ESE"), Indiana Michigan Power Company ("I&M"), Upper Peninsula Power Company ("UPPCO"), We Energies ("WE"), Wisconsin Public Service Corporation ("WPS") and Northern States Power – Wisconsin d/b/a Xcel Energy ("Xcel"). All of these companies incur costs for transmission of electricity and have rates, including PSCR clauses, regulated by the MPSC. The natural gas distribution utility members of MEGA include Aurora Gas Company, Citizens Gas Fuel Company, Michigan Gas Utilities ("MGU"), WPS and Xcel. Of these gas utilities, MGU, WPS and Xcel are subject to

rate regulation and have gas cost recovery clauses (or “GCR”) under 1982 PA 304 (similar to the electric PSCR clauses but for purchased natural gas supply) regulated by the MPSC. Certain MEGA members – ESE, UPPCO, WE and WPS – are filing a separate proposed brief *amicus curiae* in this case. MEGA participates in the present brief for the association and its other members.

MECA is a Michigan nonprofit corporation serving as the statewide association representing the collective interests of Michigan’s nine rural electric distribution companies, one generation and transmission (“G&T”) cooperative, Wolverine, and one licensed alternative electric supplier. The distribution company members are: Alger Delta Cooperative Electric, Cherryland Electric Cooperative, Cloverland Electric Cooperative, Great Lakes Energy Cooperative, HomeWorks Tri-County Electric Cooperative, Midwest Energy Cooperative, Ontonagon County REA, Presque Isle Electric & Gas Co-op and Thumb Electric Cooperative. These nine distribution members incur costs for transmission of electricity and have PSCR clauses regulated by the MPSC.

Wolverine is a Michigan-based nonprofit, member-owned G&T electric cooperative. Wolverine has four traditional distribution cooperative members: Cherryland Electric Cooperative, Great Lakes Energy Cooperative, Presque Isle Electric & Gas Co-op and HomeWorks Tri-County Electric Cooperative (“Distribution Members”). These Distribution Members purchase generation and transmission service from Wolverine and resell that power at retail to nearly 225,000 customers in the northern and western portions of Michigan’s Lower Peninsula. Wolverine’s two non-distribution cooperative members, Spartan Renewable Energy,

Inc. and Wolverine Power Marketing Cooperative, Inc. are licensed alternative electric suppliers in Michigan.

Wolverine owns and operates approximately 1,200 miles of 69 kV and 138 kV looped transmission lines and associated facilities. In January, 2006, Wolverine became a transmission-owning member of the Midwest Independent Transmission System Operator, Inc. (“MISO”).

ITCTransmission and METC are wholly owned subsidiaries of ITC Holdings Corp. ITC Holdings Corp. invests in the electricity transmission grid to improve electric reliability, improve access to markets, and lower the overall cost of delivered energy. It is the largest independent electricity transmission company in the country. *ITCTransmission* and METC operate contiguous, regulated, high-voltage electric transmission systems in Michigan’s Lower Peninsula serving a combined peak load in excess of 22,000 megawatts. *ITCTransmission* owns and operates over 2,700 miles of high voltage electric transmission lines and related facilities in 13 counties of Southeast Lower Michigan including the Detroit and Ann Arbor metropolitan areas. METC owns and operates over 5,400 miles of high voltage electric transmission lines and related facilities in 60 counties in Michigan’s Lower Peninsula. ITC Holdings Corp. is also focused on new areas where significant transmission system improvements are needed through subsidiaries ITC Midwest, ITC Grid Development, ITC Great Plains and ITC Panhandle Transmission.

ATC owns and operates over 9,300 miles of high voltage electric transmission lines and related facilities in an area including Michigan’s Upper Peninsula and extending throughout the eastern half of Wisconsin and into portions of Illinois and Minnesota. ATC began operating in January, 2001 as the first multi-state, transmission-only electric utility in the country. American Transmission Company LLC is structured as a limited liability company, with other companies

that transferred assets or cash to ATC being equity owners. ATC Management Inc. manages and controls the electric transmission facilities of American Transmission Company LLC and jointly they function as a transmission-only electric utility. ATC provides transmission service to Michigan electric utilities serving in the Upper Peninsula.

Since its inception, ATC has undertaken an aggressive construction program to improve electric grid reliability in Michigan's Upper Peninsula and to allow the region to participate in the operation of a developing power market in the Midwest. To date, over \$354 million has been invested by ATC in the Upper Peninsula. ATC, as the transmission service provider for the U.P., will continue to investigate, plan, construct and operate necessary transmission upgrades to assist all Michigan electric service providers in providing reliable electric service.

ITCTransmission, METC and ATC, like Wolverine, are members of the MISO, which controls multi-state electric system activity in the Great Lakes and upper Midwest region including most of Michigan. Collectively, *ITCTransmission*, METC and Wolverine own the electric transmission grid covering almost all of the Lower Peninsula. *ITCTransmission*'s and METC's business includes the transmission of electricity from generating power plants in Michigan or interconnected transmission systems at the state boundaries to the local distribution systems serving Lower Michigan. Wolverine's business includes the generation and purchase of electricity from generating power plants in Michigan or interconnected transmission systems at the state boundaries and the transmission of that electricity to its member owners. The rates for electric transmission service are set by the FERC under federal laws governing the interstate movement of electricity. In turn, the FERC-regulated costs of service by *ITCTransmission*, METC, Wolverine and ATC to Michigan's regulated electric utilities are recovered from end-

users through the distribution rates set by the MPSC under state ratemaking mechanisms, presently including the PSCR clauses of individual utilities.

C. Electric Industry Restructuring

Electric industry restructuring or deregulation was a major policy issue at the federal and state levels during the 1990s and beyond. Historically, many electric utilities functioned as vertically integrated entities owning the generating plants, high voltage transmission lines and distribution grid and providing electric utility service in a defined exclusive service territory. The retail rates for electric service are regulated by state commissions such as the MPSC, due to the monopoly characteristics of the industry. Federal policy changes, including the Energy Policy Act of 1992, led to an increase in unregulated exempt wholesale generators (“EWGs”) and improved access to the high voltage transmission grid for these independent power generators to sell electricity to public utilities. At the same time, industrial customers urged legislators to allow access to purchases from competing suppliers of electricity, such as the EWGs and other utilities with surplus power, in the belief that more competition in the generating sector would result in lower electricity costs.

California began the restructuring movement among the states in 1994 and other states followed. Michigan restructured by adopting electric retail choice and encouraging competitive power suppliers. The “Customer Choice and Electric Reliability Act” 2000 PA 141; MCL 460.10 – 460.10bb (“Act 141), established a customer choice program for most regulated electric utilities. The utilities were required to open up their systems to provide a delivery service for alternate electric suppliers who could market “generation” service to the utilities’ customers. The local utility would continue to provide “distribution” service. The new laws also

encouraged the development of more independent electric generating plants by requiring their interconnection to the utility grid. MCL 460.10e.

Act 141 addressed electric transmission in part by requiring the larger electric utilities to increase the capability of Michigan to import power from other states by at least 2,000 megawatts. MCL 460.10v The law also directed investor-owned Michigan utilities to either join a FERC-approved multi-state regional transmission organization (“RTO”) such as MISO or divest its interest in its transmission facilities to an independent transmission owner. MCL 460.10w(1). As a result of the policy encouraging separation of the transmission function, ITCTransmission and METC acquired the transmission assets of Detroit Edison and Consumers Energy, respectively. The transmission grid for most of the Upper Peninsula and a large part of Wisconsin, formerly owned by investor-owned utilities, was transferred to ATC. ATC was formed Wisconsin state law and the utilities contributing transmission assets retain interests in the company and some serve on ATC’s board of directors¹. At the time of electric restructuring, Wolverine already functioned as a separate generation and transmission cooperative for its member-owned cooperatives operating local distribution systems. Some transmission facilities in Southwest Lower Michigan and Northern Indiana continue to be owned and operated by American Electric Power, which is a member of another RTO called PJM. Electric restructuring is described as above and in more detail in Jonathan A. Lesser and Leonardo R. Giacchino, *Fundamentals of Energy Regulation*, pp 9-12 (PUR, Inc., 2007); Michigan Public Service Commission Annual Reports – *Status of Electric Competition in Michigan* available at <http://www.dleg.state.mi.us/mpsc/electric/restruct/status.htm> and Suzanne Lowe, *Electric*

¹ ITCTransmission and METC are completely independent of any electric generation or distribution companies.

Industry Restructuring in Michigan, Michigan Senate Fiscal Agency (2000) available at www.senate.michigan.gov/sfa (under Publications - State Notes).

As a result of the electric industry restructuring encouraged by regulatory authorities and lawmakers, high voltage electric transmission in Michigan became primarily a service provided by the newly formed federally regulated transmission providers and Wolverine to the regulated public utilities, Wolverine's distribution members and the new alternative electric service providers during the present decade. From a physical standpoint, the systems remained essentially as they were before restructuring, except that there are ongoing transmission upgrade and improvement projects and operational control has shifted to the RTOs, including MISO.

In 2008, the Michigan Legislature addressed a comprehensive package of reform measures for electric and natural gas utilities and MPSC regulation. New laws enacted include 2008 PA 295, the "Clean, Renewable and Efficient Energy Act" requiring greater use of renewable energy electric generating sources and new utility energy efficiency programs. 2008 PA 286 amended existing statutes to streamline the MPSC's utility rate setting procedures, provide for new MPSC regulation of utility mergers and asset transfers, allow the MPSC to conduct an optional certificate of need procedure for advance review and approval of major new generating projects and limit the retail electric choice program to no more than 10% of an electric utility's load in most circumstances. MCL 460.6j, governing the PSCR process, was not amended in this latest reform even though shift to independent transmission companies and recovery of additional third party transmission costs in the PSCR cases was well under way. In 2004, however, the Legislature had acknowledged the increased role of independent transmission providers in amending the Electric Transmission Line Certification Act, 1995 PA 30; MCL

460.461 *et seq.* to define transmission providers formed after the divestiture of transmission assets that occurred with electric restructuring. 2004 PA 192. *See* MCL 460.562(a) and (f).

STANDARD OF REVIEW

The Electric Service Providers agree with the other parties that a *de novo* review standard applies to the question of law in this case regarding the MPSC’s statutory authority. As restated by this Court in Complaint of Rovas, 482 Mich 90;754 NW 2d 259 (2008), the MPSC’s interpretation of its statutory authority is entitled to “most respectful consideration” and should not be overturned “without cogent reasons” although it is not binding and cannot conflict with legislative intent. If the law is doubtful or obscure, the agency interpretation can be an aid in discerning legislative intent. Earlier review standard formulations assigning “great weight” or unyielding “deference” to the agency interpretation of a law were thus modified or clarified.

ARGUMENT

I. MCL 460.6j(1) PROVIDES AUTHORITY FOR THE MPSC TO ALLOW RECOVERY OF FEDERALLY APPROVED TRANSMISSION EXPENSES THROUGH THE PSCR MECHANISM.

A. The Statutory Language Supports the MPSC Decision

The issue is whether the PSCR statute, MCL 460.6j, allows the MPSC to include federally approved costs paid to transmission service providers by a regulated electric utility in the PSCR rate adjustment process.

The rules of statutory interpretation are well established. The cardinal rule of statutory construction is to discern and give effect to the intent of the Legislature. Drouillard v Stroh’s Brewery Co, 449 Mich 293, 302; 536 NW2d 530 (1995). The first step in ascertaining such

intent is to focus on the language in the statute itself. Thornton v Allstate Ins Co, 425 Mich 643, 648; 391 NW2d 320 (1986). If the statutory language is certain and unambiguous, judicial construction is neither required nor permitted, and courts must apply the statute as written. Turner v Auto Club Ins Assn, 448, Mich 22, 27; 528 NW2d 681 (1995). All words and phrases shall be construed and understood according to the common and approved usage of the language; but technical words and phrases, and such as may have acquired a peculiar and appropriate meaning in the law, shall be construed and understood according to such peculiar and appropriate meaning. MCL 8.3a.

This case can be resolved by a plain reading of the language. MCL 460.6j(1) states:

(a) “Power supply cost recovery clause” means a clause in the electric rates or rate schedule of a utility which permits the monthly adjustment of rates **for power supply** to allow the utility to recover the booked costs, including transportation costs, reclamation costs, and disposal and reprocessing costs, of fuel burned by the utility for electric generation and **the booked costs of purchased and net interchanged power transactions** by the utility incurred under reasonable and prudent policies and practices.

(b) “Power supply cost recover factor” means that element of the rates to be charged for electric service **to reflect power supply costs** incurred by an electric utility and made pursuant to a power supply cost recovery clause incorporated in the rates or rate schedule of an electric utility.

(Emphasis added.)

A PSCR clause may therefore include the following costs of a utility in the rate recovery mechanism:

- power supply costs,
- costs of fuel burned by the utility for electric generation (including transportation, reclamation, disposal and reprocessing costs),
- costs of purchased power, and
- costs of net interchanged power

Inclusion of “power supply costs” in the above list is also indicated by other sections of the statute. MCL 460.6j(3) refers to the “expected sources of electric power supply” and “changes in the cost of power supply” to be addressed in a complete PSCR plan filed with the MPSC. Similarly, in addressing the required 5-year forecast filed in PSCR cases, MCL 460.6j (4) refers to “anticipated sources of supply” and “projections of power supply costs”. MCL 6j(1)(b) quoted above says that the PSCR rate factor is an element to reflect “power supply costs” incurred by an electric utility.

At issue in this case are the costs paid by a state regulated utility to a federally regulated electric transmission service provider such as *ITCTransmission*, METC, ATC or Wolverine. Do these costs fall under any of the categories listed above? Electric Service Providers believe such costs are clearly within the categories of “power supply”, “purchased power” and “net interchanged power”. Transmission costs are not part of the cost of fuel burned or the subcategories of fuel transportation, reclamation, etc. The Attorney General’s argument is correct on the narrow question whether transmission costs can be considered as costs of fuel transportation under the statutory wording. However, the reasoning of the MPSC and reviewing courts treating transmission costs as power supply or purchased power costs should be affirmed.

The key words and phrases relevant to the statutory analysis can be analyzed based on the common meanings which likely encompass any “peculiar and appropriate” or “technical” meaning². Under common definitions, “power” means a source or means of supplying energy, or the time rate at which energy is transferred; for electricity this amount is expressed in watts or

² Plain meaning analysis is adequate; however, if technical or peculiar regulatory meaning is considered, the views of the MPSC should be afforded “respectful consideration” under the Rovas standard. Including necessary components of power supply such as transmission as a PSCR expense because of the actual relationship is a “cogent reason” for the MPSC determination. A utility needs transmission to obtain electricity from distant sources.

kilowatts (1000 watts) as the power increases. Webster's Ninth New Collegiate Dictionary, Merriam-Webster, Inc (1983), p 922; Jacobowitz, Electricity Made Simple (Doubleday 1959, pp 81-82. When used as a noun, "supply" means something supplied, or made available for use. Websters, *supra*, p 1186. The term "interchange" means "to put each of (two things) in the place of the other." Websters, *supra*, p 630. The "cost" means the amount paid for something and a "purchase" is to obtain something by paying money. *Id.*, pp 295, 956.

Applying the common definitions above, the PSCR statute allows the recovery clause to include the amount of money paid by a utility for electric power made available for the utility's use.

The word "transmission" has not appeared in this analysis and the essential question is whether transmission is an element of power supply or purchased power. Electric Service Providers maintain that transmission is an essential element of the transaction because there can be no supply or exchange of electric power without its transmission from the generating source to the distribution utility. As the MPSC described in its September 16, 2002 Opinion and Order in Case No. U-12725, p 16 (Attachment A to Attorney General's Brief in Supreme Court Nos. 13667/13668):

Historically, vertically integrated electric utilities acquired transmission services in conjunction with wholesale power purchases, either as a bundled part of those purchases or as standalone wheeling services used to deliver the power to its system, and the wholesale charges paid by a utility for those services have been treated as part of the utility's purchased and net interchanged power transactions and recovered through the PSCR clause.

The Attorney General does not dispute this historic relationship between transmission and purchased power costs. Based on the above analysis, the PSCR statute authorized the MPSC's

challenged decisions to approve recovery of a state regulated utility's transmission expenses through the PSCR mechanism.

B. The MPSC Did Not Unlawfully Expand its Statutory Powers

The Attorney General's briefs characterize the challenged MPSC action as an unlawful expansion of agency's statutory authority. Because transmission costs are properly considered as part of a purchased power or power supply transaction, there was no unlawful extension of authority. Further, the MPSC has been given comprehensive statutory authority to regulate the rates and services of Michigan electric utilities. This case involves setting electric rates and the dispute is over the use of the PSCR procedures versus a general rate case proceeding for recovery of transmission expenses. The Attorney General acknowledges that, even if not through the PSCR mechanism, the MPSC could authorize utility rate recovery of these federally approved transmission expenses in a general rate case. Thus, at its core, this is a matter of whether expenses clearly incurred to serve the public should be allowed to be recovered in a timely manner through the PSCR process or whether utilities should be forced to prosecute an expensive, time-consuming full general rate case as a condition to any recovery of prudent transmission expense. The Court should not regard a procedural decision on the type of administrative proceeding in which to conduct the legitimate agency function of setting rates as the agency's attempt to unlawfully expand its regulatory authority. Instead, the Court should recognize that the Commission's decision to allow for the timely recovery of federally approved transmission costs is consistent with the statute and a matter of good public policy.

C. "Booked Costs" Is Given Meaning Under the MPSC Interpretation

The Attorney General contends that the MPSC position on transmission cost recovery via

the PSCR clause violates a rule of construction by failing to give meaning to the phrase “booked costs”. This argument presents the different regulatory Uniform System of Accounts (“USOA”) numbers assigned to transmission costs payable to others (Account 565), fuel costs (Accounts 501, 520 and 547) and purchased and net interchanged power costs (Account 555). The Attorney General reasons that the separate accounting classification for third party transmission costs controls interpretation of MCL 460.6j and means that such costs cannot be viewed as part of purchased power or power supply costs under the statute.

There is no basis for concluding that the Legislature intended to adopt USOA accounting classifications in the statute or require a particular accounting treatment by the MPSC, however. Accounting rules are not mentioned at all in the statute. A reasonable interpretation based on the plain meaning rule of statutory construction is that the term “booked costs” means simply those costs that are entered in the utility’s books or records for purchased power transactions. The organization of a utility’s books under the MPSC accounting rules has no bearing on the question under the statute whether the costs were in fact “booked.” Once the transmission costs are recorded somewhere in the utility’s financial records (as costs actually incurred), they are “booked” for purposes of the statutory requirement and the MPSC determination that such costs, wherever recorded, are part of power supply costs eligible for PSCR treatment does not render the phrase “booked costs” meaningless.

D. There Was No Improper Deference to the Agency Ruling

Whether or not one of the Court of Appeals panels may have cited a rule of deference inconsistent with the Rovas decision is not grounds for reversal, given this Court’s *de novo* review of the MPSC’s statutory authority. While the Attorney General asserts improper

deference was given to the MPSC statutory interpretation, the following passage from the *per curiam* opinion in Court of Appeals Nos. 244354 and 246744 is instructive:

Nothing in Act 304 in general or in MCL 460.6j in particular prohibits the recognition of transmission costs as PSCR costs. Power must be transmitted in order for it to be distributed to a utility's customers. This holds true whether the power is generated by the utility itself or purchased by the utility from a third-party provider. PSC witnesses testified that historically, transmission costs have been accounted for in PSCR proceedings.

This language demonstrates that the Court of Appeals viewed transmission as part of a utility's power supply based on the underlying fact that transmission is an essential component of a power supply transaction and the historical treatment of some transmission costs in the PSCR process. This represents an independent analysis by the appellate panel rather than giving inappropriate deference to the MPSC legal reasoning.

E. The Attorney General's Policy Arguments Are Matters for the Legislature

The Attorney General asserts that whether or not transmission costs should be included in PSCR factors is a policy decision that was made by the Legislature when it adopted MCL 460.6j. As discussed above, Electric Service Providers believe that the language of the PSCR statutes encompassed transmission expenses as part of power supply costs and if a party seeks a change or narrowing of the previous language, the Legislature is available to consider possible amendments.

The Attorney General's argument described the challenged MPSC actions as "switching recovery" of transmission expenses from base rates to PSCR factors. What actually occurred, after the PSCR statute was adopted in 1982 and applied for many years, was a state and federal government-driven electric industry restructuring. This restructuring led to divestiture of high

voltage transmission systems by most of the public utilities serving Michigan, a large increase in purchased power transactions because of the MISO operational control of regional transmission and electric generation, and transmission expenses being paid to an increased number of third-party transmission service providers such as ITC*Transmission*, METC and ATC³. Transmission system operation and expenses formerly part of the regulated utility system operations became separate market transactions between multiple parties and MISO operational control of the regional generation mix took the place of individual utility control or smaller power pool arrangements. The Michigan Legislature, having adopted major electric industry reform legislation in 2000 PA 141 and 142 and very recently in 2008 PA 286 and 295, has not determined to impose any new limits on the category of costs eligible for PSCR ratemaking treatment. There are strong policy reasons for preserving the status quo, which includes allowing transmission cost recovery in the PSCR process.

Although the issue of transmission cost recovery through the electric PSCR mechanism had been recently contested in multiple MPSC cases and addressed by the Court of Appeals, the Legislature did not act to impose limitations in the 2008 regulatory reform legislation. Instead, major reforms, such as the new advanced certificate of need process for major electric projects (2008 PA 286, Section 6s) and the rate case 12-month time requirement (Section 6a) were adopted which are aimed at providing more timely rate relief and more assurance of investment cost recovery. Limiting transmission cost recovery to general rate cases and increasing the prospects for “regulatory lag” delaying recovery, as the Attorney General supports, would have been inconsistent with these new measures. There has been growing public policy concern at the

³ Wolverine provides combined generation and transmission service to its rural electric distribution cooperative members.

national and state levels over the need to upgrade electric generation, transmission and distribution infrastructure. The financial condition of regulated utilities and transmission providers and their ability to access capital markets are vital considerations. The new Michigan legislation improves the cost recovery process and should not be countered with legal interpretations that delay cost recovery and inject unnecessary procedural hurdles for transmission expenses.

Public policy considerations start with the policy issues at the time the PSCR statute was adopted. As described by this Court in In re Proposals D and H, 417 Mich 409; 339 NW2d 848 (1983), utility rate adjustment clauses were the subject of a vigorous public policy debate in 1982, which led to competing ballot proposals, the Legislature's passage of 1982 PA 304 and court litigation. Some advocates favored a complete ban on utility rate adjustment clauses and limiting all rate adjustments to fully contested general rate cases that require review of all utility costs of business (Ballot Proposal D). Utilities and others supported the concept of adjustment clauses with limited issue hearings on the adjustment elements of fuel, purchased power and purchased gas (Ballot Proposal H). Proposal H ultimately prevailed over Proposal D by having the greater number of affirmative votes in the election. Meanwhile, the Legislature adopted 1982 PA 304, which included the Proposal H concept of rate adjustment clauses with limited issue hearings. However, Act 304 added additional measures to protect utility customers, including the requirement for full GCR and PSCR contested case hearings and the establishment of a utility consumer representation fund under MCL 460.6m to assure customer advocate representation in the adjustment clause cases for both gas and electric utilities. The consumer representation funding, currently at a level of over \$1 million per year, is collected through utility rates and controlled by a 5-member governing board. About half of the annual funding

goes to the Attorney General for participation by his office in Act 304 cases. Office of the Auditor General, Report No. 641-0425-06L (May, 2007) available at www.audgen.michigan.gov. Having adopted measures to assure full hearings and funded customer representation in PSCR cases, there has been no need for the Legislature to restrict the process based on concerns over lack of fairness to ratepayers or inadequate regulatory scrutiny regarding transmission expenses.

The Attorney General claims “sound policy reasons” support adopting his strict interpretation of MCL 460.6j (1) to exclude transmission costs from the PSCR process. There are two elements to this argument: (1) alleged reduced incentive for a utility to minimize costs and economize, and (2) alleged lack of benefit and shifting utility risks to ratepayers. Since the Attorney General and other customer advocates are paid through the statutory representation fund to protect customers in the PSCR cases, and full contested case hearings are required, these policy assertions lack merit and should not be a basis for decision by this Court. Utilities have a compelling incentive to minimize costs because excess costs can and will be disallowed for rate recovery by the MPSC, regardless of whether scrutinized in a general rate case or an adjustment clause proceeding. Even though the rates for transmission service are set by the FERC, the PSCR procedures assure state review of the reasonableness of the utility’s planning for power supply.

The Attorney General would delay the recovery of prudent costs without regard to the benefit to the public of maintaining financially healthy utilities in a misguided effort to artificially suppress rates. The recent policy changes in Michigan regulation recognize that a utility that is able to recover its costs in a more timely and certain manner can access capital at a

lower rate, which benefits customers through lower rates. Bad public policy would be mandating, by judicial ruling, the effective denial of the legitimate recovery for transmission expenses by removing them from the timely adjustment clause process in order to achieve the false economy of “regulatory lag.” Just as “justice delayed is justice denied” is a noble principle of jurisprudence, the regulatory concept of “cost recovery delayed is cost recovery denied” is invoked by the Attorney General’s policy argument.

CONCLUSION AND RELIEF

The Electric Service Providers request that the Court affirm the challenged MPSC decisions to include third party transmission costs as an element of power supply cost in the PSCR process.

Respectfully submitted,

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