

STATE OF MICHIGAN
IN THE SUPREME COURT

CITY OF HOLLAND,

Plaintiff-Appellee,

v

CONSUMERS ENERGY COMPANY,

Defendant-Appellant.

Supreme Court No. 151053

Court of Appeals No. 315541

Ottawa County Circuit Court
Case No. 12-002758-CZ

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***AMICUS CURIAE* BRIEF OF MICHIGAN MUNICIPAL
ELECTRIC ASSOCIATION**

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STATEMENT OF QUESTION INVOLVED

Should the Supreme Court issue a peremptory order affirming the decision of the Court of Appeals but making it clear Michigan Public Service Commission Rule 411 has no application to municipally-owned electric utilities?

The Trial Court did not address this question.

The Court of Appeals did not address this question.

Defendant-Appellant Consumers Energy Company would answer "No."

Plaintiff-Appellee City of Holland answers "Yes."

Amicus Curiae Michigan Municipal Electric Association answers "Yes."

I. INTRODUCTION AND STATEMENT OF INTEREST

This brief *amicus curiae* is filed by the Michigan Municipal Electric Association (“MMEA”) in support of the request by Plaintiff-Appellee City of Holland (“Holland”) that this Court issue a peremptory order affirming the Court of Appeals’ decision in this case but also making it clear that Michigan Public Service Commission (“MPSC”) Rule 411 is not applicable to municipally-owned electric utilities, their existing customers or prospective customers. MMEA is a statewide association of 40 municipally-owned electric utilities. Also among MMEA’s members are two public joint action agencies formed by municipal utilities under 1976 PA 448 to supply wholesale electric power to certain of MMEA’s members.¹ MMEA believes the position advocated here by Defendant-Appellant Consumers Energy Company (“Consumers”) in its application for leave to appeal is contrary to the constitutional and statutory system governing municipal electric utilities and would have devastating consequences both to the cities and villages currently operating municipal utilities and their customers as well as to the constitutional right of cities and villages to establish new municipal electric utilities. Among other things, the position advocated by Consumers would effectively subject municipal utilities and their customers to an administrative rule (Rule 411)² which (1) was never intended to apply to

¹ MMEA’s municipal members are: Baraga, Bay City, Charlevoix, Chelsea, Clinton, Coldwater, Croswell, Crystal Falls, Daggett, Dowagiac, Eaton Rapids, Escanaba, Gladstone, Grand Haven, Harbor Springs, Hart, Hillsdale, Holland, L’Anse, Lansing, Lowell, Marquette, Marshall, Negaunee, Newberry, Niles, Norway, Paw Paw, Petoskey, Portland, St. Louis, Sebewaing, South Haven, Stephenson, Sturgis, Traverse City, Union City, Wakefield, Wyandotte, and Zeeland. Its public agency members are Michigan Public Power Agency and Michigan South Central Power Agency.

² Mich Adm Code, R 460.3411.

them; (2) on its face does not apply to them;³ (3) was issued by a state agency with no jurisdiction over them;⁴ and (4) if applied to municipal utilities, is inconsistent with at least seven statutory provisions.⁵

The Court of Appeals correctly held that Rule 411 does not apply to municipal utilities. However, citing this Court's decision in *Great Wolf Lodge of Traverse City v Public Service Commission*, 489 Mich 27, 38-39; 799 NW2d 155 (2011), the Court of Appeals also said that Rule 411 may limit the right of a landowner to select service from a municipal utility under certain circumstances. This statement is not correct. The MPSC has no authority to regulate -- by rule or otherwise -- (1) whether a landowner may obtain electric power from a municipal utility because Rule 411 on its face applies only to *utilities* regulated by the MPSC (and not to landowners), and (2) the Legislature has given the MPSC no authority to regulate the behavior of landowners. Whether a landowner may obtain electric power from a municipal utility is governed not by Rule 411 but by statute. See MCL 117.4(f); MCL 124.3(2).

Holland has thoroughly briefed the legal infirmities with Consumers' position. Those arguments will not be repeated here. The purpose of this Brief is to apprise the Court of the potentially devastating implications of Consumers' position to municipal utilities.

³ "These rules apply to electric utilities that operate within the State of Michigan under the jurisdiction off the public service commission." Mich Adm Code, R 460.3101(1).

⁴ See MCL 460.6; MCL 460.10y(11); MCL 460.54.

⁵ The statutes are MCL 117.4f; MCL 124.3(2); MCL 460.10y(2); MCL 460.10y(3); MCL 460.6; MCL 460.10y(11); and MCL 460.54.

II. ARGUMENT

A. Municipal Utilities

The Constitution of 1963 authorizes cities and villages to own and operate utility systems to provide electric service both within and outside their corporate limits. Const 1963, art 7, § 24. Two statutes limit service outside the corporate limits to adjacent municipal units or areas being served as of June 20, 1974. See MCL 117.4f and MCL 124.3.

Municipal utilities are not regulated by the MPSC. MCL 460.6; MCL 460.10y(11); MCL 460.54. Rates and terms and conditions of service are set by the cities and villages that own the utility. Municipal utilities are permitted to operate in adjacent municipalities if they have been granted a franchise by the municipality. MCL 117.4(f) and MCL 124.3. Some municipal utilities generate their own power, others purchase wholesale power, and others utilize a combination of power resources.

With limited exceptions, all public utilities including municipal utilities have a duty to serve all customers who request service, provided they are legally permitted to serve. See *City of Lansing v Michigan Power Co*, 183 Mich 400, 410; 150 NW 250 (1914). Many utility franchises also expressly impose a duty on the recipient electric utility to serve all customers who request service. The corollary is that prospective customers have a right to request and receive service from a municipal utility if they are not already receiving that service from another utility.

Rates charged by municipal utilities are published in tariffs or rate books. Charges may not be discriminatory⁶ and are generally uniform within each rate class. Municipal utilities are not permitted to offer special discounts to attract new customers if the same

⁶ See *Alexander v City of Detroit*, 392 Mich 30; 219 NW2d 41 (1974).

rates are not available to similarly-situated customers. *Id.* Rates charged by municipal utilities are generally lower than those of MPSC-regulated utilities and thus provide a benchmark for comparison of electric rates in Michigan.

B. Competition

For the most part, MPSC-regulated utilities have exclusive service territories and in most areas do not compete with other utilities.⁷ Municipal utilities, on the other hand regularly compete for new customers in areas adjacent to the city or village that owns the utility. In almost all of the adjacent municipal units where municipal utilities operate, there is at least one MPSC-regulated utility also operating. Where a municipal unit such as a township has granted franchises to more than one utility, it is usually because the local unit has decided to allow its residents and businesses their initial choice of electric service providers when purchasing or developing property that does not have existing buildings or facilities already receiving electric service. Given the option, property owners usually select the lowest-cost option.

C. Statutory Restrictions

Inside their corporate limits, cities and villages may -- in fact they must -- provide electric service on a nondiscriminatory basis to anyone requesting service.⁸ Outside their corporate limits, the only constraint is that they cannot provide service to customers (e.g. buildings and facilities) already receiving service from another utility:

(2) A municipal corporation shall not render electric delivery service for heat, power, or light to customers outside its

⁷ When MPSC utilities compete with other MPSC-regulated utilities, Rule 411 is applicable.

⁸ See *Alexander v Detroit*, supra.

corporate limits already receiving the service from another utility unless the serving utility consents in writing.

MCL 124.3(2).

Similarly, an MPSC-regulated utility may not extend service to buildings and facilities already receiving electric service from a municipal utility:

(2) Except with the written consent of the municipally owned utility, a person shall not provide delivery service or customer account service to a retail customer that was receiving that service from a municipally owned utility as of June 5, 2000, or is receiving the service from a municipally owned utility. For purposes of this subsection, 'customer' means the building or facilities served rather than the individual, association, partnership, corporation, governmental body, or any other entity taking service.

MCL 460.10y(2).

These provisions preclude extension of service to buildings and facilities already receiving service without the consent of the serving utility, but they enable the customer to choose which properly franchised utility will serve new buildings and facilities.

The constitutional and statutory system governing municipal utilities worked smoothly and with little controversy for many years prior to this Court's decision in *Great Wolf Lodge, supra*.

D. Rule 411

If Rule 411 is applied directly or indirectly to municipal utilities, the equation shifts dramatically. Subsection (11) of Rule 411 establishes the "rule of first entitlement" or "premises" rule. As interpreted by this Court in *Great Wolf Lodge*, Rule 411(11) provides

the first “utility” (defined as the first MPSC-regulated utility⁹) ever to have served a parcel of land with the exclusive right to serve all parts of the parcel in perpetuity.¹⁰ Because a municipal utility is not a “utility,” a municipal utility can never be the first “utility” to serve a premises even if in reality it was the first. This means that an MPSC-regulated utility will *always* win the right to serve a customer under Rule 411.

If Rule 411 is, contrary to its own terms, made binding on municipal utilities, it will mean the following:

- initial customer choice as to which utility will provide service will be eliminated and replaced with the rule of first entitlement;
- head-to-head competition will be eliminated;
- the statutory distinction between service inside and outside the corporate limits of the municipal utility will be eliminated;
- municipal utilities will never be the first utility ever to have served because they are not “utilities” as that term is defined in MPSC Rules and, thus, property owners will forever be prohibited from choosing to receive service from a properly franchised municipal utility.
- the constitutional and statutory system governing municipal utilities will effectively be amended or even repealed as the result of a rule promulgated by an agency which has expressly been denied jurisdiction over municipally-owned utilities.
- the policies of municipal units which have granted multiple franchises to enable customer choice will be thwarted.

⁹ “‘Utility’ means an electric company, whether private, corporate, or cooperative that operates under the jurisdiction of the [public service] commission.” Mich Adm Code, R 460.3102(l).

¹⁰ As interpreted by this Court, subsection (11) has effectively displaced other parts of Rule 411 which provide generally that the utility with the distribution facilities closest to the customer has the right to serve.

E. Implications Of Applying Rule 411(11) To Municipal Utilities

1. Implications On Existing Municipal Utilities

All electric utilities have high fixed costs. Long term investments must be made in transmission and distribution systems and generating facilities. In the case of municipal utilities and joint action agencies formed by municipal utilities, the long term investments are ordinarily financed with proceeds from the sale of municipal bonds. Utility plant and infrastructure are sized to meet current and expected demand. Fixed costs are spread over the entire customer base. If the customer base declines, costs must be spread over a smaller base and rates must be increased to cover fixed costs, including interest and principal on outstanding debt.¹¹

In many, if not most, areas of Michigan population inside cities is declining. Most of the growth is occurring in suburban areas. If a municipal utility is not able to compete for new load in these growing areas, its customer base will shrink, its rates will rise, and eventually it may fail. As discussed above, applying Rule 411 to municipal utilities will destroy their ability to compete, thereby ultimately shrinking their customer base. Capital investments made by municipal utilities and municipal joint action agencies have been made on the assumption that municipal utilities will be able to compete freely for new load without Rule 411 barriers. If that assumption is invalidated by the courts, the consequences to municipal utilities and municipal joint action agencies will be dire.¹²

¹¹ In addition to the debt load of the municipal utilities themselves, MMEA members, Michigan Public Power Agency and Michigan South Central Power Agency have incurred extensive debt in connection with generating facilities owned by them.

¹² The term "stranded investment" is used in the utility industry to describe utility assets that become uneconomic because of a decline in demand for electricity. For example, if a

There is a scenario even more serious which is entirely possible under Rule 411. As interpreted by this Court, the rule of first entitlement is applicable regardless of whether the "first utility" is the currently serving utility. Thus, it is literally possible for the "first utility" (which can never be a municipal utility) to claim the right to displace the currently serving utility.¹³ This kind of raid on a municipal utility's customer base could even occur inside the corporate limits of the owner of the utility since Rule 411, unlike MCL 124.3, makes no distinction between service inside and outside of the city or village owning the utility.

2. Implications On Cities And Villages That Would Like To Establish An Electric Utility

Application of Rule 411 to a city or village contemplating the establishment of a municipal utility would be even more immediate. Because virtually all parcels within a city or village are currently receiving, or at some time in the past have received service, from an MPSC-regulated utility, there are *no* prospective customers available to a newly formed municipal utility and, thus there is *no* practical possibility that a new municipal utility can

generating plant is designed to produce 500 megawatts but demand drops to 400, 100 megawatts is said to be "stranded." The owner of the plant will typically attempt to sell excess power in the market, sometimes at a loss. However, generating plants owned by municipal utilities and joint action agencies are ordinarily financed with tax exempt bonds, and federal tax regulations limit the amount of excess power they can sell for non-municipal purposes.

¹³ This result would be directly contrary to MCL 460.10y(2) and is further proof that Rule 411 was never intended to apply in circumstances governed by statutes.

be established. This would completely defeat the constitutional right of a city or village to establish a new electric utility.¹⁴

F. Electing To Operate Under Rule 411

MCL 460.10y(3) provides a municipal utility with the unilateral right to elect to come under Rule 411 in areas outside the corporate limits of the city or village which owns the utility.¹⁵ This election is optional at the direction of the municipal utility, but of equal significance is that this provision clearly shows the Legislature's understanding that in the absence of an election by the municipal utility, Rule 411 is *not* applicable directly or indirectly to municipal utilities.¹⁶ There are problems and uncertainties with making such an election, however.

First, most of the adjacent townships and cities that have granted franchises to more than one utility have done so in order to provide choice to their [prospective] residents and businesses. Electing Rule 411 eliminates the customer's right to choose its initial electric provider.

¹⁴ After this Court's decision in *Great Wolf Lodge*, at least two communities in Michigan that were actively studying the establishment of electric utilities put those plans on hold as a result of the decision.

¹⁵ MCL 460.10y(3) provides: "(3) With respect to any electric utility regarding delivery service to customers located outside of the municipal boundaries of the municipality that owns the utility, a governing body of a municipally owned utility may elect to operate in compliance with R 460.3411 of the Michigan administrative code, as in effect on June 5, 2000. However, compliance with R 460.3411(13) of the Michigan administrative code is not required for the municipally owned utility. . . ."

¹⁶ It also clearly shows that it is the Legislature's intent that MCL 124.3(2) and MCL 460.10y(2) -- not Rule 411 -- are controlling in the absence of an election by the municipal utility.

Second, MCL 460.10y(3) was adopted by the Legislature prior to the interpretations under which Rule 411's proximity rules were swallowed by the rule of first entitlement.¹⁷ Electing to follow the proximity rules makes more sense to a municipal utility than electing the rule of first entitlement.

Third, it is by no means clear that electing to follow Rule 411 means that the definition of "utility" is automatically rewritten to include the municipal utility.

Finally, even if the definition of "utility" is automatically broadened to include the municipal utility, it is oftentimes very difficult to determine which utility was the "first utility" to have served a premises. Extensive research of documents and records dating to the late 1800s was recently conducted by one municipal utility trying to ascertain which utility was the "first utility." While large investor-owned utilities may have the resources to conduct such research, many small municipal utilities do not.

III. CONCLUSION

This case is of significance to Consumers because if it prevails it will be relieved of the burden of competing head-to-head with municipal utilities. It will also be relieved of the system established by the Constitution, the Legislature and by the cities, villages, and townships that have chosen to provide customers the opportunity to choose their initial electric provider through the granting of a franchise to both a municipal utility and an MPSC-regulated utility.

This case is of significance to cities and villages currently operating municipal electric utilities because of the critical importance of being able to freely compete for new

¹⁷ See footnote 9, *supra*.

load customers and to cities and villages in general because of the need to preserve their right under the Michigan Constitution to establish and operate new municipal utilities.

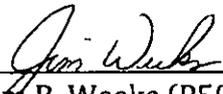
There is no legal basis for applying to municipal utilities an administrative rule promulgated by a state agency which has no jurisdiction over them. Nor is there any legal justification for allowing an administrative rule to displace no less than seven provisions duly enacted by the Michigan Legislature.

IV. RELIEF REQUESTED

Plaintiff-Appellee City of Holland has requested that the Supreme Court issue a peremptory order affirming the decision of the Court of Appeals but also making it clear that Rule 411 has no application to municipal utilities. MMEA, as *amicus curiae*, supports Holland's request.

Respectfully submitted,

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