STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of **THE DETROIT EDISON COMPANY** for authority to implement a power supply cost recovery plan in its rate schedules for 1999 metered jurisdictional sales of electricity.	))))))	Case No. U-11800

At the April 24, 2000 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. John G. Strand, Chairman
Hon. David A. Svanda, Commissioner
Hon. Robert B. Nelson, Commissioner

OPINION AND ORDER

History of Proceedings

On September 30, 1998, The Detroit Edison Company (Detroit Edison) filed an application to implement a power supply cost recovery (PSCR) plan for 1999, pursuant to 1982 PA 304, as amended, MCL 460.6h et seq.; MSA 22.13(6h) et seq., (Act 304). The application also presented Detroit Edison's five-year forecast.

At a prehearing conference on November 3, 1998, Administrative Law Judge James N. Rigas (ALJ) granted leave to intervene to the Attorney General,[1] Energy Michigan, the Residential

[1]On January 1, 1999, Jennifer M. Granholm was sworn in to replace Frank J. Kelley as the Attorney General.

Ratepayer Consortium (RRC), and the Association of Businesses Advocating Tariff Equity (ABATE). The Commission Staff (Staff) also participated.

The ALJ conducted evidentiary hearings on January 13 and April 19, 1999. Thereafter, the parties, except for Energy Michigan, filed briefs, and, except for Energy Michigan and ABATE, they filed reply briefs. On June 30, 1999, the ALJ issued a Proposal for Decision (PFD). Detroit Edison and the Staff filed exceptions, and Detroit Edison, the Staff, the RRC, and the Attorney General filed replies to exceptions.

Positions of the Parties

The disputed issues in this case relate primarily to Detroit Edison's forecast of its 1999 system peak demand. As a result of its forecast, Detroit Edison expected its generating capacity and long-term purchased power to fall short of its customers' requirements during peak conditions in the summer months of June, July, and August. The shortfall between its system capacity resources and peak demand determines how much capacity Detroit Edison will plan to acquire through short-term summer purchase arrangements. There are two types of these short-term arrangements assumed in Detroit Edison's plan: summer contracts and summer call options. Summer contracts take the form of "5x16" standard contracts, which means that the monthly contract price entitles the buyer to take energy for 16 peak hours during weekdays. Summer daily call options are slightly different, in that the buyer purchases them at a quoted premium price to acquire an option to purchase energy during the 16 peak hours of a weekday by paying an energy charge of $200 per megawatt-hour (MWh). Because both summer arrangements provide for delivery of the energy purchases at the Cinergy hub, Detroit Edison must also secure transmission service to move the energy to its own service territory.

The significance of the short-term summer arrangements is that they are some of the more costly resources that Detroit Edison relied upon to meet its customers' requirements. According to the projections in Detroit Edison's plan, the average expected cost of the capacity and energy in 1999 is $134 per MWh for summer contracts and $571 per MWh for summer calls. See Ex. A-3, at 2.

a. Detroit Edison

Detroit Edison forecasted that, in 1999, its net system output[2] would be 51,389 gigawatt-hours (GWh), including interruptible loads. Exs. A-1, A-11. The forecast indicated a decline in net system output of 2,172 GWh as a result of sales lost due to customers choosing open access. Exs. A-8, A-11.

For its 1999 forecast of peak demand, Detroit Edison used an 80% confidence level; i.e., the probability that the actual peak would exceed the forecast is 20%. Tr. 246. Detroit Edison further assumed that it would be required to provide backup service for 492 megawatts (MW) of expected retail open access loads in 1999. With these assumptions, Detroit Edison projected peak demand to be 11,059 MW. By further assuming that it would maintain a 15% capacity reserve requirement, Detroit Edison determined that the capacity resources required to meet the peak demand in 1999 would be 12,718 MW (115% x 11,059 MW) and that the shortfall in its capacity would be 1,978 MW. Detroit Edison proposed to cover the shortfall by purchasing 400 MW of summer contracts and 1,578 MW of summer calls. Ex. A-4; Tr. 54-55.

Using the costs developed from its sales and peak demand forecasts, Detroit Edison projected that it would incur $801,851,000 in PSCR costs in 1999 and computed a PSCR plan factor of 1.02

[2]Net system output is the total production of energy from generating resources and purchased power that a utility uses to meet its system requirements.

mills per kilowatt-hour (kWh). Exs. A-1, A-13. However, Detroit Edison later accepted the Staff's proposed adjustment to return retail open access loads to a full-service basis, as explained below. This adjustment increased Detroit Edison's proposed PSCR factor to 1.57 mills per kWh. Detroit Edison's initial brief, Attach. A; Detroit Edison's exceptions at 8.

b. RRC

The RRC disputed Detroit Edison's projected peak demand and reserve margin assumptions, arguing that they inflated the amount of the short-term summer capacity that Detroit Edison would need. RRC witness Don Scott Norwood proposed to modify several of the assumptions used in Detroit Edison's analysis. First, because Mr. Norwood believed that forecasting peak demand at an 80% confidence level was too conservative, he proposed a demand forecast of 10,620 MW based on a 50% confidence level, as set forth in Detroit Edison's Exhibit A-11. Second, he reduced the forecast by 700 MW to account for Detroit Edison's demand-side management programs and its ability to shed interruptible loads during peak periods. (10,620 MW - 700 MW = 9,920 MW, as proposed by the RRC. 9,920 MW x 115% = 11,408 MW of capacity required to maintain a 15% reserve margin.) Third, he made an adjustment to remove Detroit Edison's 15% reserve requirement for the 300 MW of power purchases from Ontario Hydro, reasoning that a supplier of firm power maintains the operating reserves for the sale. Fourth, he disputed Detroit Edison's inclusion of 492 MW of backup capacity for retail open access in its system requirements, arguing that Detroit Edison would be required to maintain only an operating reserve requirement of 74 MW to supply the backup for that load (15% x 492 MW). In total, Mr. Norwood's adjustments reduced the projected capacity shortfall to be made up with summer purchases from 1,978 MW to 205 MW. Tr. 314.

Mr. Norwood also criticized Detroit Edison's projected cost for summer capacity as based on an atypically high market price of $122.70 per MWh, as quoted for 5x16 standard contracts on November 10, 1998. Using a three-month average quoted price of $109.40 per MWh, he repriced the 205 MW shortfall without relying on summer call options. Mr. Norwood computed a PSCR factor of negative 1.94 mills per kWh.[3] Tr. 317.

c. Staff

Staff witness Paul A. Carlson proposed two adjustments to Detroit Edison's 1999 plan. First, noting that it was uncertain whether Detroit Edison's retail open access program would begin in 1999, he proposed to restate the open access loads on a "business as usual basis," i.e., as though the customers remained on full service. This adjustment reduced PSCR costs by $29,285,808 for the summer call options used in Detroit Edison's plan to provide backup service for 492 MW of open access load and, at the same time, increased PSCR costs by $90,717,637 for the additional summer contracts that Mr. Carlson assumed would be necessary to serve 492 MW of additional full-service load. The net effect is an increase of $61.4 million. Ex. S-32, at 1-4.

Mr. Carlson's second adjustment related to the costs that Detroit Edison planned to incur to maintain service to interruptible loads under peak conditions. Mr. Carlson testified that serving those loads would shift the costs of the incremental resources necessary to avoid the interruptions to non-interruptible customers. Mr. Carlson proposed to eliminate $76.8 million of the summer call options assigned to 300 MW of load attributable to R-10 and special manufacturing and large

[3]Because reducing the short-term summer capacity in Detroit Edison's plan eliminated the associated energy from the PSCR plan, Mr. Norwood made a cost adjustment to replace the energy. Mr. Norwood also made an adjustment to the method for allocating total power supply costs between PSCR and non-PSCR (R-10 and special manufacturing and large commercial contract) sales.

commercial contract (R-10) customers[4] and 440 MW of other interruptible loads. Mr. Carlson further assumed that the energy associated with the 440 MW portion would be avoided and removed that energy from Detroit Edison's requirements. Id. at 1-2, 5-6.

Mr. Carlson computed the cumulative effect of his adjustments and proposed a PSCR factor of negative 0.02 mills per kWh. Id. at 1.

d. Attorney General

Although the Attorney General did not sponsor witnesses, her initial brief adopted the Staff's sales and peak demand forecasts together with the RRC's pricing adjustments for summer contracts. The Attorney General proposed a PSCR factor of negative 0.91 mills per kWh. Attorney General's initial brief at 14-15. Subsequently, the Attorney General conceded an irregularity in her calculation and revised the proposed factor to negative 0.29 mills per kWh. Attorney General's replies to exceptions at 8.

PFD

The ALJ found that the Staff's adjustments related to the removal of incremental costs to serve interruptible loads during peak conditions as well as the restatement of the retail open access loads on a business as usual basis were appropriate. The ALJ also found that the RRC's proposal to reprice the summer capacity at a three-month average of $109.40 per MWh was more reasonable than Detroit Edison's higher estimate. The ALJ adopted the Attorney General's proposed PSCR factor of negative 0.91 mills per kWh. PFD at 9-13.

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[4]Customers taking service under Detroit Edison's R-10 tariff rider obtain interruptible service at a discounted rate. Their service is not subject to the PSCR clause. Special manufacturing and large commercial contract customers do not take service under a tariff, but the terms and conditions provided in their contracts with Detroit Edison are comparable to the R-10 rider. As a shorthand reference, this order will refer to these classes of service as R-10.

Detroit Edison had opposed the Staff's adjustments based on the assumption that interruptible loads would be curtailed during peak conditions, arguing that using this assumption would signal a major policy shift and would undermine the reliability of interruptible service. In rejecting this argument, the ALJ defined the issue as "whether or not the marginal costs of serving interruptible customers should be included in calculating a PSCR factor for all PSCR customers." PFD at 11. He said that the Staff's position would avoid inappropriate subsidization of interruptible customers while permitting Detroit Edison to maintain the reserves necessary to meet its service obligations.

Discussion

Detroit Edison objects to the Staff's adjustment reducing the capacity requirements that the utility had projected as necessary to meet its 1999 summer peak demand. As previously noted, Detroit Edison projected peak demand with an 80% confidence level, assumed that it would maintain service to interruptible customers during peak conditions, and developed its requirements with a 15% reserve margin. Although the Staff reduced Detroit Edison's capacity requirements by 740 MW to adjust for the interruptible loads, the Staff also asserted that even the reduced capacity would be adequate to maintain service to interruptible loads under normal peak conditions. As explained by the Staff, continuous service to all loads would be achieved if Detroit Edison's peak demand is consistent with its forecast at a 50% (not 80%) confidence level and it maintains a 12.2% reserve margin. Staff's brief at 7-8.

Detroit Edison says that it was inconsistent for the Staff to develop capacity requirements by accepting the utility's parameters of an 80% forecasting confidence level and a 15% reserve margin and then to proceed with an alternative analysis using a 50% confidence level and a 12.2% reserve margin. According to Detroit Edison, the Staff's alternative analysis implies a belief that the

utility's forecast was unreasonable. Detroit Edison notes that the difference between a 15% and a 12.2% reserve margin equates to 300 MW of capacity requirements. Detroit Edison says that the Staff's position would in fact lower the reserve margin to 8%.

In response, the RRC and the Attorney General argue that Detroit Edison's objections to the Staff's alternative analysis are misleading. The RRC explains the Staff's use of a 12.2% reserve margin as corroborating the reasonableness of the Staff's assumptions regarding peak demand. The Staff says that its reserve calculations are accurate.

The Commission finds that the Staff's overall approach in developing Detroit Edison's projected capacity requirements based on expected 1999 peak conditions is reasonable. Demand projections are necessarily imprecise, and Detroit Edison apparently attempted to protect itself from the risk of underestimating its capacity requirements by using conservative assumptions in its forecast. The Staff used Detroit Edison's projections as a starting point and made adjustments that appear to be reasonable.

Detroit Edison takes exception to the ALJ's adoption of the Staff's $30.1 million adjustment to remove the costs of the summer call options that Detroit Edison had planned to use to provide continuous service to R-10 customers. Although Detroit Edison allocated power supply costs to R-10 customers at an estimated $25 per MWh, the Staff's adjustment in effect increased the allocation to $36.49 per MWh. (Because R-10 customers' sales are not subject to the PSCR clause, their allocated share of power supply costs acts as a negative adjustment to total power supply costs in computing PSCR costs. By increasing the R-10 cost allocation, the Staff effectively reduced PSCR costs.) Detroit Edison contends that there was no showing that $25 per MWh was an unreasonable cost projection. Detroit Edison also argues that the determination of the actual costs to be incurred on behalf of R-10 customers should be deferred until the PSCR reconciliation. Because Detroit

Edison bills R-10 loads separately from PSCR loads, it says, the power supply costs will not be intermingled or shifted from one customer class to another. Moreover, Detroit Edison argues, planning for interruptible loads provides additional capacity that further insulates firm PSCR customers from system interruptions and enhances system reliability.

In reply, the RRC contends that Detroit Edison did not provide evidentiary support for its projected $25 per MWh cost of serving R-10 customers. The Staff and the Attorney General assert that it is important to allocate projected costs between customer classes as accurately as possible. They add that the high cost of the incremental summer capacity projected by Detroit Edison raises the R-10 cost allocation well beyond the historical levels reflected in Detroit Edison's estimate of $25 per MWh.

The Commission finds that the Staff's use of the price of summer call options to allocate power supply costs to R-10 customers was reasonable. In making this finding, the Commission adopts the Staff's rationale that, for planning purposes, the higher cost incremental resources are assigned to the non-PSCR loads that can be interrupted if necessary to maintain reliable service. The Staff's adjustment is appropriate because a PSCR factor should include only those costs that Detroit Edison expects to incur on behalf of its PSCR customers and should exclude costs incurred on behalf of the R-10 customers. As Detroit Edison observes, the allocation of the actual power supply costs incurred to serve both types of customers will be addressed in the PSCR reconciliation.

Detroit Edison also opposes the Staff's adjustment for interruptible service other than R-10, which include residential air conditioning and water heating tariffs. Detroit Edison argues that the Staff's adjustment would force it either to plan not to serve those customers during peak conditions, causing disruptions of their service, or to maintain their service at the risk of incurring

disallowances. Detroit Edison characterizes the Staff's position as a major policy shift and argues that the Commission should announce new policies dictating how a utility should provide interruptible service on a prospective basis only. Detroit Edison faults the Staff and others taking similar positions for not articulating specific standards that would guide the utility's discretion in implementing a policy of relying on interruptions to avoid expensive power purchases.

The RRC, the Attorney General, and the Staff argue that the proposed adjustment is not a directive to Detroit Edison regarding how it should serve its interruptible customers. The RRC and the Attorney General say that Detroit Edison is free to serve interruptible customers as though they were taking firm service, but that it should not recover the added costs of that choice through the PSCR clause.

The considerations presented by interruptible residential air conditioning and water heating service are somewhat different than the interruptible R-10 service. Unlike the R-10 customers, the air conditioning/water heating customers take their service pursuant to Detroit Edison's PSCR clause. The service provided under the air conditioning/water heating tariffs enables the customers to obtain a modest rate discount in exchange for their willingness to accept occasional curtailments in a separately metered service. As such, the tariffs provide the company with an additional resource for fine-tuning loads under hot-weather conditions. Although the interruptible tariff customers cannot legitimately expect Detroit Edison to provide them with fully firm service at a discounted rate, as it does to firm PSCR loads, the service is not as curtailable in practice as non-PSCR R-10 service. Treating air conditioning/water heating customers as fully interruptible could eviscerate the load management benefits of the programs by deterring potential customers from signing up or by driving existing customers off the programs.

The Commission is not persuaded that either of the positions advanced by Detroit Edison or the other parties accurately reflects the cost effects or the load management benefits of the programs. For purposes of this case, the Commission finds that no adjustments should be made to Detroit Edison's treatment of the interruptible air conditioning/water heating programs. However, the Commission does not foreclose further refinement of these issues[5] in the reconciliation, in which issues affecting the reasonableness of the actual cost of power supplies incurred to serve combined firm and interruptible PSCR loads can be addressed.

Detroit Edison excepts to the ALJ's finding that the RRC's estimated price for summer contracts, based on a three-month average of market quotes, was more appropriate than the estimate used by Detroit Edison, based on a single day's market quote. Detroit Edison observes that the market is volatile and that last summer's price spikes reached $5,000 per MWh. Detroit Edison claims that the only rationale for the RRC's estimate is that it is lower than Detroit Edison's.

The RRC and the Attorney General respond that a three-month average better accounts for market volatility than a single day's quote occurring near the peak of a price trend.

The RRC's estimated price for summer contract capacity of $109.40 per MWh is more reasonable than Detroit Edison's comparable estimate of $122.70 per MWh. As a general matter, it is usually more appropriate to base a market price on an average over a period of time than a single day's price. The Commission finds that the RRC's estimate is reasonable for purposes of the PSCR plan. The reasonableness of the actual price paid for the short-term summer arrangements will be determined in the reconciliation case.

[5]The Commission is aware that other approaches to the PSCR effects of interruptible air conditioning/water heating programs have been proposed in pending Case No. U-12121.

As explained above, the Commission adopts the findings made by the ALJ on the issues disputed in Detroit Edison's exceptions. In addition, the ALJ recommended the factor computed in the Attorney General's initial brief, which used RRC witness Norwood's computation as a starting point. The Staff notes that the methodologies used by it and the RRC were different, in that the Staff, but not the RRC, modified Detroit Edison's forecast of the net system output. The Staff says that its methodology based on Exhibit S-32 is more appropriate.

The Commission finds that a PSCR factor of 0.67 mills per kWh should be approved as computed in Attachment A, which modifies the computations shown on three pages of Exhibit S-32. Because the Staff proposed the adjustments to address peak demand, total capacity requirements, and sales, its approach is more consistent with the adjustments than the RRC's methodology. As the Staff explains, updating its methodology for the price revision proposed by the RRC is a relatively simple adjustment.

The Commission FINDS that:

a. Jurisdiction is pursuant to 1909 PA 106, as amended, MCL 460.551 et seq.; MSA 22.151 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; MSA 22.1 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; MSA 22.13(1) et seq.; 1982 PA 304, as amended, MCL 460.6h et seq.; MSA 22.13(6h) et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; MSA 3.560(101) et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACS, R 460.17101 et seq.

b. Detroit Edison's 1999 PSCR plan and factors, as amended in this order, are reasonable and prudent, and should be approved.

THEREFORE, IT IS ORDERED that:

A. The Detroit Edison Company's 1999 power supply cost recovery plan is approved as amended in this order.

B. The authorized 1999 power supply cost recovery factor for The Detroit Edison Company is 0.67 mills per kilowatt-hour.

C. Within 30 days of the date of this order, The Detroit Edison Company shall file tariff sheets reflecting the power supply cost recovery factor approved by this order.

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, pursuant to MCL 462.26; MSA 22.45.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ John G. Strand
Chairman

(S E A L)

/s/ David A. Svanda
Commissioner

/s/ Robert B. Nelson
Commissioner

By its action of April 24, 2000.

/s/ Dorothy Wideman
Its Executive Secretary

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MICHIGAN PUBLIC SERVICE COMMISSION

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Chairman

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Commissioner

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Commissioner

By its action of April 24, 2000.

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Its Executive Secretary

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recovery plan in its rate schedules for 1999	)	
metered jurisdictional sales of electricity.	)	
	)	

Suggested Minute:

"Adopt and issue order dated April 24, 2000 amending and approving The Detroit Edison Company's power supply cost recovery plan and factors for the 12-month period ending December 31, 1999, as set forth in the order."