

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the approval of a code of conduct)	
for CONSUMERS ENERGY COMPANY and)	Case No. U-12134
THE DETROIT EDISON COMPANY.)	
_____)	

At the October 29, 2001 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. Laura Chappelle, Chairman
Hon. David A. Svanda, Commissioner
Hon. Robert B. Nelson, Commissioner

ORDER ON REHEARING

I.

HISTORY OF PROCEEDINGS

On June 5, 2000, Public Act 141 of 2000, the Customer Choice and Electricity Reliability Act (Act 141), MCL 460.10 et seq., took effect. Subsection 10a(4) of Act 141 directed the Commission to issue, within 180 days, an order establishing a code of conduct for all electric utilities regulated by the Commission and for all alternative electric suppliers. On December 4, 2000, the Commission issued an order in this case adopting a code of conduct.¹

¹Hereafter, when referring in general to the code of conduct required by Act 141, the terms “code” or “code of conduct” will be used. The term “December 4 code” will be used when referring to the specific code of conduct adopted by the order dated December 4, 2000.

On January 3, 2001, petitions for rehearing were filed by Energy Michigan, The Detroit Edison Company (Detroit Edison), Consumers Energy Company (Consumers), Michigan Electric Cooperative Association (MECA), and Unicom Energy, Inc.

On January 3, 2001, Detroit Edison, Consumers, and MECA also filed a joint request to extend the deadline for filing code of conduct compliance plans. On January 23, 2001, the Commission issued an order extending the deadline until 60 days after the order on rehearing.

On January 24, 2001, responses to petitions for rehearing were filed by Energy Michigan, Detroit Edison, Consumers, the Association of Businesses Advocating Tariff Equity (ABATE), Wisconsin Public Service Corporation, Upper Peninsula Power Company, Northern States Power Company-Wisconsin, and Wisconsin Electric Power Company (UP Utilities), Michigan Alliance for Fair Competition (MAFC), and Exelon Energy, Inc. (Exelon).²

II.

POSITIONS OF THE PARTIES

Consumers

Consumers contends that the code of conduct should apply only to retail open access activities because that is the primary focus of Act 141. According to Consumers, extending the code to other activities is not essential to the development of a successful retail open access program. Consumers argues that the December 4 code would involve a wide spectrum of unregulated activities and would destroy economies of scale and efficiencies that have provided significant benefits to Michigan utility customers. Consumers indicates that it can accept the December 4 code if its application is restricted to activities related to retail open access.

²Between the filing of petitions for rehearing and responses, Unicom Energy, Inc., changed its name to Exelon Energy, Inc., as a result of a merger.

Consumers requests that the Commission confirm that the December 4 code applies only to electric utilities. Consumers notes that its gas division already is subject to a gas code of conduct approved by the Commission.

Consumers requests clarification that various activities traditionally performed by electric utilities for outside third-parties will continue to be permitted, such as “transmission and distribution construction activities, joint trenching, fiber optic networking services, forestry services, metering and meter installation, meter-reading services, technical training of generating, transmission and distribution employees, and many other similar services.” Consumers’ petition, p. 8.

Consumers argues that services provided to multiple affiliates and divisions should not be prohibited. Examples of these services include legal, governmental affairs, computer services, and corporate financial activities. According to Consumers, these services are sharable because they do not benefit only one specific part of the overall corporation and they do not interfere with the competitive energy marketplace initiated by Act 141.

Consumers contends that the December 4 code would prohibit the utility from operating pursuant to Act 141 and other statutes. For example, Consumers indicates that its transmission assets will be transferred to an affiliate prior to being sold to a third-party – an action encouraged by Act 141. Consumers intended to staff the affiliate with its employees. In addition, Consumers intended to provide engineering services through a subsidiary formed for the sole purpose of complying with the State of Michigan’s professional engineering licensing requirements. According to Consumers, the December 4 code would prohibit the sharing of employees with these affiliates.

Consumers argues that the code should provide an exemption for obligations of contracts entered into prior to the effective date of the code. In addition, Consumers recommends that the compliance process permit waivers and suspend enforcement during periods when waiver requests are under consideration.

Finally, Consumers argues that there is no statutory authority for the Commission to adopt a code of conduct that extends beyond retail open access activities and that a code that did so would impermissibly intrude on management prerogatives.

In its response, Consumers argues that Act 141 does not allow for separate codes for electric utilities and alternate electric suppliers and that there must be a single code applicable to both.

Detroit Edison

Detroit Edison claims that the code of conduct should only apply to the relationship between an electric utility or alternative electric supplier and an affiliated entity providing unregulated competitive retail service in Michigan. According to Detroit Edison, the December 4 code can be interpreted to apply more broadly than that and the Commission should clarify that it does not do so.

In addition, Detroit Edison argues that the code should not apply to interactions between regulated entities. Detroit Edison cites its relationships with International Transmission Company, which is regulated by the Federal Energy Regulatory Commission (FERC), and with Michigan Consolidated Gas Company, as examples that should not be included under the code.

Detroit Edison contends that the Commission should change or clarify the December 4 code so “that it does not apply to unregulated services provided to or by an electric utility that do not involve a recognized retail Michigan market and/or are necessary to provide regulated electric supply service.” Detroit Edison’s petition, p. 6. Detroit Edison cites the acquisition and

transportation of fuel as an example of a retail service without a recognized retail Michigan market. In addition, Detroit Edison indicates that fundamental corporate support services shared by an electric utility and its affiliates would be an example that should not be subject to the code because these “services are a necessary function that support continued delivery of regulated electric supply service to customers, and have no material impact on the competitive retail marketplace.” Detroit Edison’s petition, p. 6. In addition, Detroit Edison requests that the Commission clarify that the code does not apply to the relationship between two unregulated entities.

Detroit Edison argues that there are several provisions of the December 4 code that are too vague or unclear to reasonably permit compliance. According to Detroit Edison, these include: (1) various provisions that use “include but are not limited to” or similar language; (2) various provisions where it is unclear whether different terms are synonymous; (3) apparent inconsistencies between the pricing provisions in the code and those adopted in the affiliate guidelines in Case No. U-11916; and (4) various provisions where it is unclear whether the geographic scope includes the service territory, the state, or some other region.

Detroit Edison indicates that it was previously operating under an interim code of conduct that was approved by the Commission in its September 14, 1999 order in Case No. U-11290. Detroit Edison asserts that the burden of proof was on parties seeking to change the interim code of conduct. According to Detroit Edison, the order fails to cite evidence that parties had successfully met their burden.

Finally, Detroit Edison argues that “[t]o the extent that the Commission has attempted to regulate non-retail access affiliates, the Commission has exceeded the scope of its jurisdiction, which is limited under state law, and in addition, has encroached upon matters that are exclusively

regulated by FERC.” Detroit Edison contends that the December 4 code encroaches on FERC’s exclusive jurisdiction over unbundled retail transmission under the Federal Power Act if it is applied to affiliates not participating in retail open access.

Detroit Edison also includes an attachment, which proposes specific language changes to the December 4 code.

In its reply, Detroit Edison indicates that serious consideration should be given to the proposal to exempt an alternative electric supplier from the code if there is a showing that an out-of-state utility affiliated with the supplier is subject to similar code provisions in its home state.

Detroit Edison contends that the code should recognize the benefits derived from economies of scope and scale and not arbitrarily ban any existing or potential economies.

MECA

MECA claims that the code of conduct should not apply to non-electric activities. Specifically, MECA indicates that rural electric cooperatives would be unable to loan or co-sign loans to affiliates and would be required to use separate employees and locations for affiliate operations.

MECA also includes an attachment, which proposes specific language changes to the December 4 code.

Exelon

Exelon contends that applying the code of conduct to alternative electric suppliers not affiliated with Michigan utilities will have the unintended effect of driving such suppliers away from Michigan. Exelon notes that the Staff’s testimony did not support applying the code to non-affiliated suppliers. Exelon points out that the December 4 code “did not apply all of its provisions uniformly to all [suppliers] regardless of their affiliation with Michigan utilities or lack thereof.”

Exelon's petition, p. 7. Exelon contends that the December 4 code reflects a decision by the Commission that distinctions should be made, on a case-by-case basis, between suppliers that are affiliated with Michigan utilities and those that are not.

According to Exelon, the distinctions made in the December 4 code would have unintended consequences that would prohibit suppliers from participating in the Michigan market. As an example, Exelon cites its plan to provide integrated energy services, which it claims would be prohibited by provisions of the December 4 code requiring structural separation of affiliates providing generation service.

Exelon also includes an attachment, which discusses specific changes to the December 4 code.

In its response, Exelon argues that the code must recognize differences between utilities and alternative electric suppliers. Exelon argues that Act 141 requires that the code be applied to alternative electric suppliers only to the extent that such application is consistent with the remainder of Act 141.

Exelon also contends that many of the proposed changes in Detroit Edison's attachment would retard the development of a competitive market in Michigan. Exelon argues that Consumers' proposed changes are difficult to evaluate because no specific language was offered and would create practical difficulties for market participants.

Energy Michigan

Energy Michigan contends that the December 4 code "prevents Alternate Electric Suppliers or their affiliates which do not sell rate regulated electricity from sharing facilities or supplying one another with power at market rates even though they compete in an unregulated market and are not subsidized by a rate regulated entity." Energy Michigan's petition, p. 2. Energy Michigan argues that the code of conduct should not apply in circumstances where the supplier or its affiliate does

not sell rate regulated electric service in Michigan. According to Energy Michigan, suppliers “not subsidized by Michigan electric utilities which sell only non-rate regulated services do not and cannot exercise market power in the Michigan market and therefore should not be subject to prohibitions or restrictions in dealing with their affiliated entities which do not sell rate regulated services.” Energy Michigan’s petition, p. 3 (emphasis deleted).

Energy Michigan contends that the prohibition on alternative electric suppliers transferring goods and services at less than fully allocated cost is unneeded because the suppliers are prohibited from receiving subsidies from affiliated electric utilities. Energy Michigan also argues that prohibitions against alternative electric suppliers sharing facilities, equipment, or operating employees or cosigning loans are unneeded for the same reason. Energy Michigan proposes that the December 4 code be revised to prohibit such activities only for electric utilities or alternative electric suppliers who sell rate regulated service.

Energy Michigan also argues that the rationale for the transfer pricing standard and the preferential treatment provisions in the December 4 code derives from the ability of a utility to recoup losses from captive customers. Energy Michigan requests that the Commission provide for waivers from these provisions where there is a showing that the non-Michigan utility that is affiliated with an alternative electric supplier is subject to restrictions equal to or greater than those in the December 4 code.

Energy Michigan states that the December 4 code would prohibit an alternative electric supplier from entering into supply arrangements with an affiliate. Energy Michigan contends that this restriction is necessary only if the supplier is subject to rate regulation in Michigan.

Energy Michigan also includes an attachment, which discusses specific changes in the December 4 code.

In its reply, Energy Michigan contends that restricting the code to only retail open access activities would prohibit most open access marketing activities in the Detroit Edison service territory. According to Energy Michigan, this occurs because the Detroit Edison Electric Choice Tariff virtually mandates use of two unregulated entities to serve customers. Energy Michigan argues that this problem can be eliminated by restricting application of the code to activities between rate regulated entities and non-rate regulated entities.

Energy Michigan contends that the proposal to exempt the sharing of all service functions would provide existing utilities with significant advantages in the marketplace.

Energy Michigan also contends that Detroit Edison's proposed changes to the December 4 code would remove virtually all restraints from the utility or its holding company regarding assistance to affiliates and would handicap alternative electric suppliers attempting to enter the market.

ABATE

ABATE argues that the code of conduct should not be limited to "recognized retail markets" as Detroit Edison suggests. In addition, ABATE disagrees with claims that the December 4 code is vague.

ABATE points out that Act 141 requires the Commission to establish a code of conduct to prevent cross-subsidization, information sharing, and preferential treatment and that no burden of proof was assigned to any particular party by Act 141. ABATE contends that the voluminous record in this proceeding supports the Commission's decision and the Commission has clear authority to establish the code mandated by Act 141. ABATE argues that the plain language of Act 141 requires that the code apply to both regulated and unregulated services.

ABATE argues that the Commission should reject the request by Consumers and MECA to continue activities prohibited by the code because they have traditionally engaged in such activity. Finally, ABATE argues that the limited exception requested by Consumers would have the effect of removing all service functions from the code.

MAFC

MAFC argues that the petitions for rehearing do not raise any new allegations that the December 4 code is erroneous as a matter of law or has any unintended consequences that were not previously considered. MAFC contends that almost all arguments advanced in the petitions were previously advanced in the petitioners' briefs and addressed by the Commission.

MAFC argues that Act 141 requires that the code apply to all regulated and unregulated operations of utilities operating in Michigan and should not be restricted to just retail open access functions. In addition, MAFC argues that the proposal to exempt out-of-state utilities and alternative electric suppliers from the code should be rejected because that would permit out-of-state suppliers to subsidize unregulated ventures in Michigan.

MAFC argues that utilities should not be allowed to shift costs from their competitive ventures through the sharing of common corporate support services and notes that it had previously asked the Commission to impose structural separation to prevent cross-subsidization. MAFC also contends that exemptions should not be used to permit utilities to engage in anti-competitive activities that would otherwise be prohibited by the code.

MAFC argues that the record in this proceeding is voluminous and fully supports the Commission's decision. MAFC also contends that the Commission should reject Detroit Edison's claim regarding the burden of proof. MAFC notes that Act 141 requires the Commission to establish a code that complies with the statute and does not assign a burden of proof to any party.

UP Utilities

UP Utilities contend that the 60-day deadline for filing compliance plans should be extended to 90 days.

UP Utilities support the proposal to limit the code to retail open access activities. If the Commission decides to apply the code more broadly, then UP Utilities recommend that the code not apply to activities between two regulated affiliates or two unregulated affiliates.

Finally, UP Utilities support Detroit Edison's and Consumers' proposals to clarify the code provisions regarding sharing of services and employees.

III.

DISCUSSION

Rehearing Standard

Rule 403 of the Commission's Rules of Practice and Procedure, 1992 AACS, R 460.17403, provides that a petition for rehearing may be based on claims of error, newly discovered evidence, facts or circumstances arising after the hearing, or unintended consequences resulting from compliance with the order. A petition for rehearing is not merely another opportunity for a party to argue a position or to express disagreement with the Commission's decision. Unless a party can show the decision to be incorrect or improper because of errors, newly discovered evidence, or unintended consequences of the decision, the Commission will not grant a rehearing.

In this proceeding, the petitioners have demonstrated that there are potentially significant unintended consequences arising out of the December 4 code. Accordingly, the Commission grants rehearing and modifies that code to the extent discussed herein. In all other respects, the petitions fail to meet the standard for rehearing and are denied.

Scope

Two issues regarding the scope of the code of conduct have been raised in the petitions for rehearing. First, should the code apply to all affiliate relationships or just those between regulated and unregulated functions? Second, should the code apply to all activities or just those directly related to retail open access?

Subsection 10a(4) of Act 141 provides:

Within 180 days after the effective date of the amendatory act that added this section, the commission shall establish a code of conduct that shall apply to all electric utilities. The code of conduct shall include, but is not limited to, measures to prevent cross-subsidization, information sharing, and preferential treatment, between a utility's regulated and unregulated services, whether those services are provided by the utility or the utility's affiliated entities. The code of conduct established under this subsection shall also be applicable to electric utilities and alternative electric suppliers consistent with section 10, this section, and sections 10b through 10bb.

MCL 460.10a(4).

Act 141 sets forth three requirements for the code of conduct. First, the code must include, at a minimum, measures to prevent cross-subsidization, information sharing, and preferential treatment. Second, the relationship that the code must address is that between the utility's regulated and unregulated services, whether those services are provided by the utility or its affiliates. Third, the code must apply to both utilities and alternative electric suppliers, consistent with the remainder of Act 141.

Several petitions ask for clarification on the scope of the code as it relates to regulated and unregulated functions. Act 141 expressly provides that the code is to address the relationship between regulated and unregulated services. No mention is made of the relationship between two or more regulated services or between two or more unregulated services. Moreover, these relationships do not raise the type of concerns that arise between regulated and unregulated

services. When both regulated and unregulated services are provided, there can be an incentive to use regulated rates to subsidize unregulated services that are provided in a more competitive market, or use other means, such as preferential treatment, to provide the unregulated service offering with a competitive advantage. The same incentive does not exist when both services are regulated or both are unregulated. Thus, the Commission concludes that the code of conduct should apply only in instances where both regulated and unregulated services are provided and should not apply to those relationships involving only regulated services or only unregulated services.

Several petitions ask the Commission to find that the code of conduct should be limited to only retail open access activities. In the December 4, 2000 order, the Commission analyzed the issue as follows:

The Commission concludes, from the language of the statute, that the Legislature intended the code of conduct to apply beyond activities in the retail open access market. The language of subsection 10a(4) is broad in declaring that the code of conduct shall prevent subsidization, information sharing, and preferential treatment “between a utility’s regulated and unregulated services.” The Commission does not view it as an oversight that the Legislature did not say “between a utility’s regulated electric services and retail open access services.” In addition, the scope of the code was before the Legislature. In that context, the use of expansive language about the scope of the code of conduct is a further indication that the Legislature did not intend to limit the scope to only retail open access.

December 4, 2000 order, Case No. U-12134, pp. 9-10.

Despite the plain meaning of the statutory provision, two arguments are advanced that the code of conduct should be restricted to retail open access activities. The first argument is that the purpose of Act 141 is to foster competition in the provision of electric supply. While it cannot be doubted that the promotion of electric competition through retail open access is certainly an important purpose of Act 141, it is not the only purpose. Act 141 lists five specific purposes, including improving opportunities for economic development in Michigan and promoting

financially healthy and competitive utilities in the state. Electric utilities in Michigan are involved in a variety of activities beyond retail open access that affect economic development.³ Moreover, the utility can be financially impaired if these unregulated activities are subsidized by regulated utility revenues—exactly the kind of activity that the code of conduct is intended to prevent. Thus it is clear that a broad code, rather than one limited only to retail open access, is consistent with the purposes stated in Act 141.

The second argument is that application of the code beyond retail open access would involve practical problems and reduce available economies of scale. However, the arguments presented in this regard assume that the code would be applied to all regulated and unregulated relationships involving utilities and their affiliates. As discussed above, the Commission has clarified that the code only applies to the relationship between regulated and unregulated service offerings. A utility or alternative electric supplier may not utilize its regulated services to subsidize, provide competitively sensitive information, or grant preferential treatment to its unregulated affiliates. The petitioners have not demonstrated that this limited application of the code would be impractical to implement or would significantly reduce economies of scale.

Accordingly, the Commission finds that the code of conduct should apply to all relationships involving both regulated and unregulated services among electric utilities⁴ or alternative electric suppliers offering regulated services in Michigan and their affiliates.

³Some examples cited in the petitions for rehearing filed by the utilities include: forestry services, appliance repair, sale of smoke and carbon monoxide detectors, and professional engineering services.

⁴Natural gas utilities are covered by codes of conduct adopted by the Commission in other proceedings.

Utilities and Alternative Electric Suppliers

The petitions and responses raise the issue of whether the code should differentiate between utilities and alternative electric suppliers. The December 4 code applied to both electric utilities and alternative electric suppliers, but not every provision applied equally to both. For example, Section II-A provides that “[a]n electric utility shall not offer unregulated services or products except through one or more affiliates or through other entities within the existing corporate structure, such as divisions.” This provision does not apply to alternative electric suppliers because the main business of an alternative electric supplier is to offer an unregulated service (i.e., unbundled electric generation under a retail open access program), whereas an electric utility’s main business is to sell regulated service (i.e., bundled electric generation, transmission and distribution service). Prohibiting an alternative electric supplier from offering unregulated service would be, for all practical purposes, the equivalent of prohibiting it from engaging in its primary business. Act 141 requires that the code apply to both electric utilities and alternative electric suppliers consistent with the various provisions of Act 141. It would be inconsistent with Act 141 for the code to prohibit alternative electric suppliers from carrying out their functions pursuant to that act. Consequently, although the same code of conduct applies to both, not every provision of the code can logically be applied in an identical fashion to both. The code of conduct attached as Exhibit A reflects this.

Exemptions

Several parties argue that various provisions of the code lead to unreasonable results when applied to specific activities. For example, MECA contends that the code should not apply to internet services and credit card operations because these only produce small amounts of revenue. Other examples include the obligations of contracts entered into before the effective date of the

code, appliance service programs, smoke alarm sales, fiber optic networking services, forestry services, etc. The Commission is not prepared to rule on specific exemptions in a factual vacuum. The code permits electric utilities and alternative electric suppliers to request waivers from one or more provisions of the code upon a demonstration that the waiver will not inhibit the development or functioning of a competitive market. That provision is sufficient to ensure that the code will not be applied in situations where it produces unreasonable results.

Conflict with Federal Regulation

Detroit Edison argues that the code of conduct is pre-empted by the Federal Power Act because it encroaches upon the exclusive jurisdiction of the FERC. According to Detroit Edison, “the FERC (1) concluded that it has exclusive jurisdiction over the rates, terms and conditions of unbundled retail transmission by electric utilities in interstate commerce, and (2) set forth a seven-factor test to separate an electric utility’s transmission facilities from its local distribution facilities.” Detroit Edison fails to explain how the code conflicts with these FERC determinations and no conflict is apparent. The code does not set rates, terms, or conditions for transmission of electricity in interstate commerce. In addition, this Commission has applied the FERC seven-factor test to separate Detroit Edison’s transmission facilities from its distribution facilities and the FERC has concurred in that separation. Moreover, Detroit Edison has now transferred its interstate transmission facilities determined pursuant to the seven-factor test to a separate affiliate (the International Transmission Company), so that the utility no longer has any such facilities subject to FERC jurisdiction. Thus, the code does not conflict with any FERC rulings.

Conflict with Affiliate Guidelines

Detroit Edison argues that the pricing provisions for transactions with affiliates in the December 4 code conflicts with equivalent provisions for affiliate transactions adopted by the Commission in its order of May 3, 2000 in Case No. U-11916. In the affiliate transaction proceeding, the Commission directed that services and supplies provided to utilities by unregulated affiliates shall be transferred at the lower of market price or 10% over fully allocated cost. The December 4 code required that these transfers be at the lower of fully allocated cost or market price, which is clearly in conflict with the affiliate transactions requirement. The code of conduct in Attachment A has been revised to be consistent with the affiliate transaction requirement.

The Commission FINDS that:

- a. Jurisdiction is pursuant to 1909 PA 106, as amended, MCL 460.551 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACCS, R 460.17101 et seq.
- b. The petitions for rehearing should be granted to the limited extent discussed in this order and denied in all other respects.
- c. A code of conduct consistent with this order should be adopted.

THEREFORE, IT IS ORDERED that the code of conduct, attached as Exhibit A, is adopted.

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.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ Laura Chappelle
Chairman

(S E A L)

/s/ David A. Svanda
Commissioner

/s/ Robert B. Nelson
Commissioner

By its action of October 29, 2001.

/s/ Dorothy Wideman
Its Executive Secretary

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.

MICHIGAN PUBLIC SERVICE COMMISSION

Chairman

Commissioner

Commissioner

By its action of October 29, 2001.

Its Executive Secretary

In the matter of the approval of a code of conduct)
for **CONSUMERS ENERGY COMPANY** and)
THE DETROIT EDISON COMPANY.)
_____)

Case No. U-12134

Suggested Minute:

“Adopt and issue order dated October 29, 2001 addressing issues raised on rehearing and adopting a code of conduct consistent with the Customer Choice and Electricity Reliability Act, as set forth in the order.”