

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)
THE DETROIT EDISON COMPANY to increase)
rates, amend its rate schedules governing the)
distribution and supply of electric energy, implement)
power supply cost recovery plans, factors, and)
reconciliations in its rate schedules for jurisdictional)
sales of electricity and for miscellaneous accounting)
authority and regulatory asset recovery.)
_____)

Case No. U-13808

At the February 20, 2004 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. J. Peter Lark, Chair
Hon. Robert B. Nelson, Commissioner
Hon. Laura Chappelle, Commissioner

ORDER GRANTING INTERIM RATE RELIEF

History of Proceedings

On June 20, 2003, The Detroit Edison Company (Detroit Edison) filed an application seeking to increase rates, amend its rate schedules governing the distribution and supply of electric energy, implement power supply cost recovery (PSCR) plans, factors, and reconciliations in its rate schedules for jurisdictional sales of electricity, and for miscellaneous accounting authority and

regulatory asset recovery of not less than \$416,000,000¹ above the level of its then frozen rates.² Detroit Edison also requested an additional rate surcharge designed to collect amounts associated with its proposal for the recovery of various regulatory assets.

Contemporaneously, Detroit Edison submitted a motion pursuant to MCL 460.6a(1) for partial and immediate rate relief in the annual amount of not less than \$399,000,000.³ However, as Section 10d(2) of Act 141 requires its rates for commercial and manufacturing customers with peak demands of less than 15 kilowatts (kW) to remain capped until January 1, 2005, and the rates for its residential customers to remain capped until January 1, 2006, Detroit Edison represented that the actual annual amount of enhanced revenues to be recognized from a rate increase of that magnitude would be limited to and collected entirely from commercial and manufacturing customers with 15 kW or greater demands. Detroit Edison also stated that \$31,400,000 of its proposed interim rate relief would be used to recover the 2004 portion of the regulatory assets sought in its application for rate relief.

Detroit Edison requested that the Commission authorize the use of an electric choice mitigation adjustment to adjust costs associated with customers leaving under electric choice, which it proposed should operate in tandem with its PSCR mechanism. Moreover, according to Detroit

¹Detroit Edison's initial suggestion that this case involves a \$416,000,000 rate increase is somewhat misleading, which is illustrated by the fact that the amount of interim relief requested by Detroit Edison in its February 4, 2004 brief is \$536,029,000. Currently, the positions supported by Detroit Edison equate to a \$553,427,000 request for final rate relief. See, Exhibit A-9, Schedule A1-2 [Revised].

²The rates schedules in effect for Detroit Edison as of June 20, 2003 were those approved by the January 21, 1994 order in Case No. U-10102, as amended from time to time by the Commission and as reduced and frozen through application of 2000 PA 141 (Act 141), MCL 460.10 et seq. In addition, Detroit Edison charges certain customers rates set forth in special contracts that have been approved by the Commission.

³See, footnote 1, supra.

Edison, the Commission should not reinstate the utility's PSCR clause until the issuance of a Commission order granting the company's motion for interim rate relief.⁴

Detroit Edison proposed to charge new rates authorized by the Commission's order granting partial and immediate relief in a manner consistent with the freeze and cap provisions of Act 141, which means that, based on their peak demands, some of the utility's customers would receive adjustments to their rates in periods different than others. For customers receiving electric service under capped rates, Detroit Edison requested authority to increase their rates to the lesser of the maximum permitted under the cap or the maximum authorized by the Commission in the event that the company were to be ordered to reduce its billed PSCR factor.

Detroit Edison also stated that its request for interim rate relief was based on an overall rate of return of 7.66% and a rate of return on common equity of 11.0%, which were authorized by the Commission in Case No. U-10102. According to Detroit Edison, its application, supporting testimony, and exhibits demonstrate that its rates should ultimately be set through use of an overall rate of return of 7.75% and a rate of return on common equity of not less than 11.5%. Because issuance of the interim rate relief order will reset the company's base rates, Detroit Edison maintains that coincident with resolution of its motion for partial and immediate rate relief, the Commission should terminate all securitization and transition charge credits for choice customers.⁵

Finally, Detroit Edison indicated that, to preclude the possibility of excess revenue being retained as a result of an order granting partial and immediate rate relief, Detroit Edison agreed to refund the amount, if any, by which the revenue collected under an order granting partial and

⁴The Commission's December 18, 2003 order in this proceeding required Detroit Edison to reinstate its PSCR clause on January 1, 2004.

⁵The rate reduction equalization credit was eliminated by the Commission in the January 15, 2004 order in Case No. U-13933.

immediate rate relief exceeds the amount of final rate relief granted by the Commission. Detroit Edison also represented that, concurrently with its filing of the rates authorized by an order granting partial and immediate rate relief, the utility would file a bond ensuring its obligation to make such refund.

On July 28, 2003, Administrative Law Judge Daniel E. Nickerson, Jr., (ALJ) conducted the initial prehearing conference in this matter,⁶ at which petitions for leave to intervene filed by the Association of Businesses Advocating Tariff Equity (ABATE), the Residential Ratepayer Consortium (RRC), Energy Michigan, Inc., the Michigan Environmental Council and the Public Interest Research Group in Michigan (MEC/PIRGIM), Attorney General Michael A. Cox (Attorney General), the National Energy Marketers Association, Constellation NewEnergy (CNE), The Kroger Company (Kroger), Energy Conversions, LLC, North American Wind Energy, LLC, and Mackinaw Power, LLC, Utility Workers Local 223, Pietro Zebri, and Douglas Moore, and Nordic Marketing, LLC, were granted.⁷ The Commission Staff (Staff) also participated in the proceedings.

On November 7, 2004, Detroit Edison filed a set of revised exhibits and workpapers that raised its request for a revenue increase from \$416 million to \$427 million. In so doing, Detroit Edison increased its originally requested rate relief by \$10.992 million to reflect an increase in the

⁶Other prehearing conferences were held on August 8 and December 16, 2003.

⁷Commonwealth Energy Corporation d/b/a electricAmerica filed a petition to intervene, but failed to file an appearance in the proceeding. MidAmerican Energy Company also filed a petition to intervene, but later withdrew from the proceeding.

amount of its proposed control premium adjustment related to the Michigan Consolidated Gas Company (Mich Con) merger,⁸ as shown on Exhibit A-9, Schedule A1-2 [Revised].

From January 5 to January 13, 2004, the ALJ conducted evidentiary hearings on Detroit Edison's motion for partial and immediate rate relief. During the course of the interim hearings, 18 witnesses testified and at least 65 separate documents⁹ were received into evidence. The interim record consists of 1,810 pages of testimony and argument in 10 transcript volumes.

On February 4, 2004, briefs were filed by Detroit Edison, the Staff, the Attorney General, ABATE, the RRC, MEC/PIRGIM, Kroger, and Energy Michigan. On February 10, 2004, reply briefs were filed by Detroit Edison, the Staff, the Attorney General, ABATE, the RRC, Kroger, Energy Michigan, and CNE. Preparation of a Proposal for Decision was unnecessary because the Commission agreed to read the record.

II.

POSITIONS OF THE PARTIES

Detroit Edison

Detroit Edison presented 12 witnesses and 37 exhibits in support of its motion. For the purposes of interim relief, Detroit Edison relies upon fully projected 2004 test year data. Detroit Edison maintains that it has demonstrated a need for additional annual revenues of \$536,029,000¹⁰ effective immediately in order to pay for the revenue effects of the electric choice program,

⁸The merger was between DTE Energy Company and MCN Energy Company, the corporate parents of Detroit Edison and Mich Con, respectively. For simplicity, the Commission will refer to this transaction as the Detroit Edison/ Mich Con merger.

⁹The methodology used in the marking of Detroit Edison's exhibits, which features repetitive use of the same exhibit number for different documents -- seven separate documents are identified as Exhibit A-16 -- is awkward and explains why the number of documents marked for admission and received into evidence does not correspond to the traditional numbering approach.

¹⁰See, Exhibit A-24, Schedule A-1 [Revised], sum of line 26 columns C and D and line 45.

increased costs associated with environmental compliance, increased costs associated with providing employee and retiree pension and healthcare benefits, the costs associated with the maintenance and operation of its electric distribution system and generation capability, the increased costs associated with the physical security of its electric system, the capital costs associated with the addition of plant over the past decade, continuation of its low-income and energy assistance fund (LIEEF), and to recognize for ratemaking purposes certain regulatory assets approved by the Commission.

Detroit Edison maintains that it began experiencing serious financial erosion in 2002. Although its return on equity appeared strong in 2002, Detroit Edison asserts that the financial erosion was offset by non-sustainable factors. According to Detroit Edison, its 2003 net income showed further erosion to \$265 million, down \$91 million, or more than 25% from the 2002 level, and its actual 2003 earnings reported on February 3, 2004 are significantly lower at \$246 million, which represents a 31% drop in earnings from 2002 reported earnings of \$356 million.¹¹ Detroit Edison anticipates this trend to continue with projected 2004 net income expected to decline by \$101 million, or to a level that is 67% below the 2002 level. Without the requested rate relief, Detroit Edison contends that its return on equity will fall to an unreasonable level of less than 3% for 2004. Even with rate relief, Detroit Edison asserts that its earnings will be reduced in 2004 and 2005 due to the existence of customers with capped rates. Simply stated, Detroit Edison argues that it must receive substantial interim rate relief to avoid significant financial harm.

In the interim phase of this case, Detroit Edison is requesting \$126 million annually of class-specific choice transition charges to recover net generation margin lost due to choice sales, a

¹¹Detroit Edison attached information about its 2003 earnings to its brief. According to Detroit Edison, it was appropriate to attach this extra record information because its 2003 actual financial information was the subject of a hearing room request and subject to administrative notice by the ALJ. 7 Tr. 882-887.

\$25 million annual increase in its Retail Access Service Tariff (RAST) rates, a \$227 million annual increase in rates for bundled customers, of which only \$117 million can be implemented in 2004 due to rate caps, a \$31 million surcharge on customers having a demand greater than 15 kW (allocated \$21 million to retail tariff customers, and \$10 million to ROA customers) to recover accumulated regulatory asset balances, and a \$126 million PSCR rate reduction adjustment. Detroit Edison also requests affirmation of future regulatory asset accounting treatment for ROA implementation costs. Detroit Edison states that approval of these measures by the Commission will serve as a constructive and creative first step towards ensuring a financially healthy utility, quality customer service, and an unbiased, economically sustainable choice program.

Detroit Edison's revenue deficiency calculation, taken from Exhibit A-9, Schedule A1-2 [Revised] and adjusted for interim purposes, is as follows:

| <u>Description</u> | <u>Jurisdictional Electric</u> |
|--|--------------------------------|
| 1. Rate Base for 2004 Test Year | \$7,468,548,000 |
| 2. 2004 Adjusted Net Operating Income (NOI) | \$331,157,000 |
| 3. Overall Rate of Return [line 2 / line 1] | 4.43% |
| 4. Requested Rate of Return | 7.75% |
| 5. Income Requirements [line 1 x line 4] | \$578,812,000 |
| 6. Income Deficiency [line 5 – line 2] | \$247,655,000 |
| 7. Revenue Conversion Factor | 1.573 |
| 8. Unadjusted Revenue Deficiency [line 6 x line 7] | \$389,561,000 |
| 9. Detroit Edison's Adjustments to Revenue Deficiency | |
| Deferred Depreciation – CAA | \$5,909,000 |
| Deferred Return on CAA | \$21,748,000 |
| Deferred Depreciation – Capital in Excess of Base Depreciation Levels | \$2,299,000 |
| Return On – Capital in Excess of Base Depreciation Levels | \$19,274,000 |
| Deferred Return on Customer Choice Implementation Costs | \$2,872,000 |
| Midwest Independent System Operator (MISO) Costs | <u>\$6,082,000</u> |

| | |
|---|----------------------|
| 10. Total Adjustments | \$58,183,000 |
| 11. Total Revenue Deficiency [line 8 + line 10] | \$447,744,000 |
| 12. Additional Control Premium Adjustment | \$10,992,000 |
| 13. Less Regulatory Asset Recovery Surcharge | \$31,358,000 |
| 14. Adjusted Revenue Deficiency | \$427,378,000 |
| 15. PSCR Effect | \$126,049,000 |
| 16. Less Adjustments for Interim Relief Proposals | <u>\$48,756,000</u> |
| 17. 2004 Adjusted Base Rate Revenue Deficiency | \$504,671,000 |
| 18. 2004 Regulatory Asset Recovery | <u>\$31,358,000</u> |
| 19. Detroit Edison's Interim Rate Relief Request | \$536,029,000 |

Detroit Edison claims that \$151,253,000 of the interim revenue deficiency should be assigned to retail open access (ROA) customers for rate design purposes. Detroit Edison calculates a gross margin loss of \$273 million due to operation of the choice program. Detroit Edison concedes that it can recover \$133 million by making non-jurisdictional sales freed up by customers that have migrated to alternative electric suppliers (AESs) for generation services, which it maintains should be netted against its gross margin loss to mitigate the stranded costs and minimize transition charges for choice customers. Detroit Edison proposes recovery of only 90% of the \$140 million of net margin loss from ROA customers, or \$126 million. To that amount, Detroit Edison would add distribution-related infrastructure costs of \$18,419,000 and \$6,834,000 associated with Detroit Edison's proposal for continuation of the LIEEF.

| <u>Components of Revenue Deficiency</u> | <u>Revenue Deficiency/ (Sufficiency)</u> |
|---|--|
| <u>Choice Customers:</u> | |
| A) Net Choice Margin Loss | |
| Gross Margin Loss | \$273,000,000 |
| Less: Wholesale Mitigation | <u>(\$133,000,000)</u> |
| Net Choice Margin Loss (unadjusted) | \$140,000,000 |
| Offset for 90% Recovery | <u>(\$14,000,000)</u> |
| Net Choice Margin Loss | <u>\$126,000,000</u> |

| | |
|---|-----------------------------|
| B) Distribution (RAST) Related Infrastructure Costs | \$18,419,000 |
| Low Income Energy Efficiency Fund | |
| Continuation (Choice Share) | <u>\$6,834,000</u> |
| Total RAST | <u>\$25,253,000</u> |
| Choice Interim Deficiency | <u><u>\$151,253,000</u></u> |

Detroit Edison contends that the base rates of its full service customers should increase by \$113,475,000 for pension and health care costs, \$68,033,000 for federal Clean Air Act¹² (CAA) compliance costs, and by \$72,863,000 for a variety of infrastructure costs. However, Detroit Edison states that these customers will see a \$59,827,000 cost reduction associated with elimination of the excess securitization savings formerly used to fund customer choice credits. The net effect of these adjustments produces a revenue deficiency of \$194,544,000 to which Detroit Edison adds \$32,825,000 for continuation of the LIEEF, for an interim base revenue deficiency of \$227,369,000. To this amount, Detroit Edison adds \$126,049,000 associated with the potential PSCR refund due to PSCR customers if Detroit Edison were to overcollect its 2004 PSCR costs, which brings the amount of the revenue deficiency to be assigned to full service customers for rate design purposes to \$353,418,000, as shown below:

| <u>Components of Revenue Deficiency</u> | <u>Revenue Deficiency/ (Sufficiency)</u> |
|--|--|
| <u>Full Service Tariff Customers:</u> | |
| C) Base Components Pension/Health Care Costs | \$113,475,000 |
| Clean Air Act Costs | \$68,033,000 |
| Infrastructure Costs | \$72,863,000 |
| Less: Elimination of Excess | |
| Securitization Savings | <u>(\$59,827,000)</u> |
| Net Base Components | <u>\$194,544,000</u> |
| D) Low-Income Energy Efficiency Fund | |
| Continuation | <u>\$32,825,000</u> |
| Interim Base Revenue Deficiency | <u><u>\$227,369,000</u></u> |

¹²42 USC 7401 et seq., and 42 USC 7651 et seq.

| | |
|---------------------------------|----------------------|
| E) PSCR Reinstatement | |
| PSCR Savings Refund | <u>\$126,049,000</u> |
| Full Service Interim Deficiency | \$353,418,000 |

Detroit Edison then combines the respective revenue deficiencies of the ROA customers and the full service customers to get the total interim base rate request of \$504,671,000, to which it adds \$31,358,000 for its proposed regulatory asset recovery surcharge (\$21 million to full service customers and \$10 million to ROA customers), which accounts for assignment of the entire \$536,029,000 revenue deficiency.

Detroit Edison also filed a 2004 PSCR plan and five year forecast in this proceeding pursuant to MCL 460.6j(18), which permits an electric utility to conduct its PSCR proceedings in the context of a general rate case. James H. Byron, Detroit Edison's Manager of Generation Optimization – Power Planning and Reliability testified that Detroit Edison's 2004 power supply actions and costs are reasonable and prudent in light of the significant and ongoing changes in the electric industry.

Detroit Edison also proposes an electric choice mitigation adjustment be added to its 2004 PSCR factor calculation, which would collect an additional \$133.1 million on an annual basis. As explained by Mr. Byron, the purpose of the mitigation adjustment is to allow the utility to retain the value of mitigation of generation stranded costs arising from the resale of generating capacity and energy made available as a result of load loss arising from its customers' participation in retail choice. Mr. Byron testified that Exhibit A-16, Schedule F11-2 shows the forecast of the mitigation revenues and the adjustment to fuel and net purchased power expense proposed by Detroit Edison. According to Mr. Byron, the mitigation expense is the forecasted expense that Detroit Edison would incur if it were to serve the service area system output including the choice load. This

expense was calculated based on the forecasted annual choice load multiplied by the projected cost to serve this load. By subtracting the fuel and purchased power costs from the mitigation revenues, Detroit Edison derives the mitigation adjustment, which corresponds to the non-fuel component of the mitigation revenues.

In its brief, Detroit Edison maintains that because the Commission reinstated the PSCR clause effective January 1, 2004, the effect of the sales mitigation proposal should appear in base rates rather than as a part of the PSCR mechanism. Accordingly, Detroit Edison proposes that approval of its 2004 PSCR plan should include an authorization for Detroit Edison to charge a PSCR factor of up to negative 1.05 mills per kWh. However, if the effects of sales mitigation are included in tandem with the PSCR mechanism rather than in its base rates, then Detroit Edison requests the implementation of a positive PSCR factor of 2.18 mills per kWh.

The Staff

The Staff presented one witness and four exhibits in support of its contention that partial and immediate rate relief should be granted to Detroit Edison. William G. Aldrich, a Cost of Service Specialist in the Commission's Energy Operations Division, presented the Staff Report¹³ on Detroit Edison's motion for partial and immediate rate relief. Mr. Aldrich testified that the Staff assessed Detroit Edison's overall financial and operational situation and determined that the utility was experiencing a revenue deficiency that depends upon the level of the transition charges to be paid by ROA customers and upon whether the company's PSCR clause is reinstated.¹⁴ As an example, Mr. Aldrich stated that, with a transition charge of 2 mills per kilowatt-hour (kWh), the

¹³Exhibit S-50.

¹⁴As previously noted, the Commission's December 18, 2003 order in this proceeding required Detroit Edison to reinstate its PSCR clause on January 1, 2004.

revenue deficiency to be recovered through tariffed rates would be \$132,685,000 if the PSCR clause were not reinstated and \$258,734,000 if it were reinstated. Further, Mr. Aldrich recommended that a portion of the interim rate relief should be recovered by means of a transition charge applied to the energy deliveries to ROA customers, with the remainder to be recovered from all rate classes on an equal percentage basis, to be applied to the customer's total pre-sales tax amount due.

Pursuant to MCL 460.6a(1), an investigation and report by the Staff is a prerequisite for interim relief. The Staff Report reveals that the Staff conducted its investigation between August and November 2003. During this time, the Staff thoroughly reviewed Detroit Edison's filings, issued hundreds of audit requests, met with Detroit Edison officials on numerous occasions, and submitted five discovery requests.

The Staff Report indicates that Detroit Edison will experience a tariff revenue deficiency ranging from a high of \$163,465,000 with no transition charge to a low of negative \$580,000 with a transition charge of 12 mills per kWh if Detroit Edison's PSCR clause remains suspended, or between \$289,514,000 with no transition charge and \$125,468,000 with a transition charge of 12 mills per kWh if the PSCR clause is reinstated. The Staff explained that the difference is caused by a reduction in the PSCR factor that would occur upon reinstatement of the PSCR mechanism. In other words, the Staff believed that the anticipated PSCR factor reduction would reduce Detroit Edison's revenues by \$126,049,000. However, in the event that the PSCR clause is not reinstated, the Staff indicated that \$126,049,000 of PSCR revenue would be available to offset costs that would otherwise be recovered through a base rate increase.

Like Detroit Edison, the Staff based its position on fully projected 2004 test year data. According to the Staff, the use of such future projections is reasonable in light of the significant

changes that have occurred in the past two years. However, in its report, the Staff recommended one upward and eight downward adjustments to positions supported by Detroit Edison for interim relief totaling \$264,086,000.¹⁵

First, because Detroit Edison forecasted the need for an overall return of 7.75% during 2004 (which equates to a pretax return of 10.66% for final relief), for interim purposes Detroit Edison and the Staff made adjustments to reflect the difference between their interim proposals and Detroit Edison's final proposal. Detroit Edison recommended use of a 10.01% pretax rate of return, which is the basis of the \$48,756,000 adjustment shown in the calculation on page 7 of this order. The Staff is recommending a pretax return of 9.88% for interim relief, which yields a \$58,255,000 adjustment.

Second, the Staff proposed an \$8,677,000 reduction related to construction expenditures. According to the Staff, Detroit Edison's proposed construction spending should be reduced to reflect only the utility's average expenditures for the previous five years. The Staff's adjustment reduces rate base by \$63 million, with a total rate effect of \$8,677,000 on the revenue deficiency.

Third, the Staff removed \$13,101,000 from the revenue deficiency calculation due to the return on regulatory asset accruals that results from Act 141 deferred costs. The Staff insisted that the recovery of these regulatory asset costs should be accomplished through separate surcharges to customers, and will be addressed by the Staff in its final rate relief recommendation.

The fourth adjustment, which totals \$28,127,000, is related to the limitation of certain administrative and general (A&G) expenses to the projected inflation rate for 2003 and 2004 and to a reduction in Detroit Edison's projected increase in operation and maintenance (O&M) expenses.

¹⁵In its brief, the Staff increased this amount by \$2,756,000 to \$266,842,000 to reflect a revision suggested by ABATE.

Fifth, the Staff deleted the entire \$83,634,000 “control premium” adjustment proposed by Detroit Edison as an allowance for its acquisition of Michigan Consolidated Gas Company (Mich Con). It is Detroit Edison’s theory that it should be allowed to recover the purchase price of Mich Con that it paid in excess of the market value of Mich Con. The Staff maintains that this item is not appropriate to include in an interim relief request.

The sixth adjustment proposed by the Staff involves \$16,325,000 of capitalized A&G expenditures. Unlike other utilities, Detroit Edison does not capitalize any indirect labor included in A&G expense accounts. The Staff maintains that the adjustment is necessary to correct Detroit Edison’s improper accounting.

Seventh, the Staff originally imputed \$37,845,000 of additional revenue to reflect the Commission’s policy that the discounts from regular tariff rates granted customers on special manufacturing contract (SMC) rates because the Staff believes that this item is not appropriate to include in an interim relief request. As previously noted, in its brief, the Staff accepted an adjustment suggested by ABATE that would increase this adjustment by \$2,756,000 to \$40,601,000 to reflect a similar adjustment for large contract customers (LLC).

Eighth, is an upward \$21,736,000 adjustment, which relates to Detroit Edison’s assumption that many of its SMC customers will switch to customer choice when their contracts expire in late 2004, which will increase its customer choice volumes and reduce its sales levels. The Staff reversed Detroit Edison’s adjustment because the transfer of SMC volumes to choice is not expected to occur during the effective period of interim rates.

Finally, the Staff eliminated \$40 million associated with Detroit Edison’s proposal to finance the low-income and energy efficiency fund (LIEEF), which the Staff believes should not be resolved during the interim phase of this proceeding.

The Staff stresses that the amount of Detroit Edison's revenue deficiency to be collected pursuant to its tariffs depends upon the level of transition charges collected from ROA customers. As noted by the Staff, before this proceeding, Detroit Edison's transition charges were decided in stranded cost cases. The Staff states that the inclusion of transition charges in a general rate case complicates the process in two ways. First, the revenue deficiency and the transition charge are interrelated – a revenue deficiency cannot be determined without determining a transition charge. Second, the stranded cost methodology adopted by the Commission was designed for use between rate cases and its application within a rate case is unclear. The stranded cost methodology involves calculating the revenue deficiency associated with generation for a specified time period and recovering that revenue deficiency from ROA customers in the form of a transition charge. This methodology works between rate cases because it assumes that the generation revenue deficiency results from customers moving from regular bundled rates to ROA service. However, within a rate case, the methodology gives dramatically different results depending upon when it is applied. If the stranded cost calculation is done before the rest of the rate case, then all of generation-related revenue deficiency is assigned to ROA customers, who actually use little of the utility's generation. If the stranded cost calculation is done after the rest of the rate case, the calculation will always result in zero, because rates for bundled customers will pick up the shortfall. The Staff maintains that neither approach is appropriate.

The Staff included tables on pages 9 and 10 of Exhibit 50 to illustrate how the revenue deficiency to be collected from bundled customers varies at one mill increments between zero and 12 mills per kWh.¹⁶

¹⁶Given changes to the Staff's recommended revenue deficiency, these tables are simply illustrative of the Staff's methodology.

Although the Staff conceded that arguments could be constructed for any number on these tables, it was the Staff's opinion that a reasonable transition charge would be in the 2 to 4 mill range. According to the Staff, this range of transition charges would be reasonable because Detroit Edison filed for recovery of approximately \$30 million in stranded costs for 2003, which equates to a transition charge of approximately 4 mills [\$30 million divided by 7,565 gigawatt-hours (GWh)]. However, suggesting a need to be conservative, the Staff also indicated that it would be equally appropriate to use half of the utility's request, or approximately 2 mills, as the transition charge pending a final resolution of this case. Another method suggested by the Staff recognizes that Detroit Edison's proposed revenue deficiency associated with generation production fixed costs (\$168 million) adjusted for modifications as proposed by the Staff results in a revenue deficiency of \$122 million. By assigning the \$122 million revenue deficiency ratably between bundled and ROA customers (\$122 million divided by 51,835 GWh) a transition charge of approximately 2.5 mills is developed. Further, the Staff indicates that because the prior stranded cost methodology is not appropriate for use in the context of a rate case, the recommended range for the transition charge in Exhibit S-50 is only appropriate for interim purposes. According to the Staff, a different approach will be necessary for the final order.

Finally, the Staff indicates that when the PSCR clause was reinstated, the Staff had anticipated that the PSCR factor charged by Detroit Edison would be reduced by 3.23 mills per kWh to align the revenue collection with projected PSCR costs for 2004. However, the Staff notes that Detroit Edison continues to use the frozen PSCR factor of 2.04 mills per kWh instead of the projected PSCR factor of a negative 1.05 mills per kWh. According to the Staff, the effect of Detroit Edison's action in this regard is to increase its cash flow (and its potential 2004 PSCR over-collection, which is subject to interest computed at the utility's authorized rate of return on

common equity) by \$126 million on an annual basis. Due to this circumstance, the Staff suggests that the Commission may want to consider basing the rate relief granted for interim purposes on the revenue shortfall levels shown on pages 7 and 9 of Exhibit S-50.

ABATE

ABATE presented the testimony of one witness and one exhibit in support of its contention that Detroit Edison' request for interim rate relief should not be granted. James T. Selecky, a consultant in the field of public utility regulation, testified that his review of Detroit Edison's actual returns on equity following approval of its most recent rate proceeding (January 21, 1994 order in Case No. U-10102) reveals that the utility earned over its authorized return of equity (11%) from 1994 to 2002. For 2002, he stated that Detroit Edison's unadjusted results as filed in Exhibit A-1, Schedule A-1 show that the utility's jurisdictional electric revenues were \$155.9 million in excess of the level required for Detroit Edison to earn the return authorized by the Commission. Moreover, Mr. Selecky argued that the adjustments made by Detroit Edison to its 2002 historical data were controversial and inappropriate for interim purposes. Rather, Mr. Selecky insisted that Detroit Edison would have a 2004 revenue sufficiency of \$34.3 million based on its 2002 historic data and assuming that the company's PSCR clause is reinstated. In the event that the PSCR factor remains frozen in 2004, Mr. Selecky opined that the revenue sufficiency would reach \$170 million.

Mr. Selecky also insisted that Detroit Edison's proposal for determination of its stranded costs utilized a methodology previously found to be objectionable by the Commission on several occasions. For this reason, he concluded that it was improper for Detroit Edison to propose use of a discredited stranded cost methodology to establish its interim rates. Moreover, Mr. Selecky maintained that Detroit Edison's approach of relying on fully projected 2004 data to support its

huge interim rate relief request was improper because its forecast and assumptions are likely to be wrong. Indeed, citing Detroit Edison's reliance of questionable assumptions for weather conditions, customer choice penetration levels, economics factors, price levels, fuel costs, and the operation of wholesale power markets, Mr. Selecky contended that these variables were so uncertain that Detroit Edison's customers would likely be required to pay unreasonable rates.

In any event, Mr. Selecky insisted that the rates for Detroit Edison's large commercial and industrial customers should not be increased. According to him, Detroit Edison's filed cost of service study clearly shows that the rates currently paid by Detroit Edison's large commercial and industrial customers exceed their cost of service. Indeed, citing Exhibit A-5, Schedule E-1, Mr. Selecky argued that the large commercial and industrial customers require rate decreases ranging from 6.6% to 24.7%. Mr. Selecky maintained that absent implementation of the rate decreases outlined in his testimony, Detroit Edison's inability to compete with AESs will be exacerbated and contribute further to the utility's lost sales.

Energy Michigan

Energy Michigan presented the testimony of one witness and four exhibits. Richard A. Polich, an independent energy consultant, testified that many of Detroit Edison's proposals for interim rate relief are controversial and will seriously erode electric competition in Michigan. Mr. Polich stated that Detroit Edison's proposal to use forecasted stranded costs for 2004 is contrary to prior Commission orders and should be rejected. According to Mr. Polich, past Commission orders make it clear that transition charges are to be set based on the need to recover historical stranded costs and that the utilities bear the burden of proof on these determinations. He also asserted that Detroit Edison used the lost revenue approach to determine its stranded costs, which was rejected by the Commission in its orders in Cases Nos. U-12639, U-13350, and U-13380.

Mr. Polich maintained that Detroit Edison is basing its interim rate relief request on new and controversial theories, such as the use of class specific transition charges that relies on unsupported rate design theory by performing calculations using average full service costs, estimated 2004 ROA sales levels, estimated transmission charges, and other gross assumptions instead of actual customer class billing determinates. As examples, Mr. Polich cited Detroit Edison's request to recover costs during the interim phase of this proceeding related to transmission costs, electric restructuring costs, electric production costs, and the assignment of 100% of new infrastructure costs to ROA customers, which he categorized as involving issues that the Commission has never previously reviewed for reasonableness or prudence. Citing the devastating effect that Detroit Edison's ROA proposals would have on choice customers, Mr. Polich recommended that the Commission defer consideration of them to the final phase of the proceeding.

Mr. Polich also indicated that Detroit Edison's proposal to incorporate recovery of its stranded costs in the revenue deficiency calculation and its proposed transition charge is inconsistent with Section 10a(9) of Act 141. According to Mr. Polich, Section 10a(9) specifies that stranded cost recovery is to occur outside of a utility's normal tariffs and should not be included in the revenue deficiency calculation of a general rate case. Additionally, Mr. Polich asserts that the stranded cost recovery charge is to be adjusted only after review of historical data, not on the basis of forecasts or projections. Arguing that Detroit Edison's approach to the determination of stranded costs conflicts with the approach approved in Cases Nos. U-12639, U-13350, and U-13380, Mr. Polich insists that the record is devoid of any showing that Detroit Edison would incur any stranded costs during 2004. At best, he maintained that reliance on the approved methodology for determination of stranded costs reveals that Detroit Edison had a stranded benefit of \$48.3 million for 2002.

Mr. Polich urged the Commission to use stranded benefits to avoid subsidization of full service customers by continuing the securitization offset. He argued that the securitization offset should be maintained through the issuance of a final order and until Detroit Edison is able to demonstrate that the effect of the migration of customers to choice justifies a subsidy.

Mr. Polich also complained that Detroit Edison has failed to comply with Section 10b(2) of Act 141, MCL 460.10b(2), which requires Detroit Edison to unbundle its existing commercial and industrial rate schedules and separately identify and charge for their discrete services. According to him, without unbundling of full service rates into comparable components to ROA Rate EC-2, it is impossible to determine if Detroit Edison applied the same billing determinates, cost allocations, rate of return, and revenue requirement methodology to all of its rates. Mr. Polich's solution would be to require Detroit Edison to refile its rate case with all rates containing unbundled components.

In the event that the Commission deems it appropriate to approve interim rates for Detroit Edison, Mr. Polich suggested that the Commission apply the same percentage increase to all customers, which would defer controversial rate design issues to the final phase of the proceeding. Additionally, Mr. Polich argued that the Commission should make several adjustments to Detroit Edison's requested interim relief. First, he maintained that the regulatory asset recovery surcharge has been improperly designed and should not be included in interim rate relief. Second, he stated that Detroit Edison did not properly include the revenues of special contract customers at full service rates and the rate request should be reduced accordingly. Third, he believed that Detroit Edison failed to comply with Case No U-13646 and that it should therefore be required to apply 50% of the net proceeds from the sale of its transmission system to reduce rates.

Finally, Mr. Polich proposed a Low Income Program (LIP) that would annually provide funds to pay electric bills of customers subject to shut off notices due to delinquent payments. Moneys would be used to pay electric bills of low income customers subject to shut off notices, which could free up customer funds to be used toward payment of delinquent heating bills. Participating customers would be required to participate in low income weatherization programs or other energy efficiency programs. According to Mr. Polich, funding would be administered by The Heat and Warmth Fund and other such existing agencies that have been delivering benefits under the LIEEF programs. Under Mr. Polich's proposal, funding would be provided by a uniform surcharge applicable to all customers. The surcharge would commence immediately upon an order in this case. According to Mr. Polich, \$23 million per year could be collected through use of a program surcharge of \$0.000444 per kWh.¹⁷

Residential Ratepayer Consortium

The RRC presented the testimony of one witness and five exhibits. Scott Norwood, a consultant knowledgeable in a variety of utility matters, provided testimony regarding Detroit Edison's proposed 2004 PSCR plan and factors. Mr. Norwood supported reinstatement of Detroit Edison's PSCR clause on January 1, 2004. Additionally, Mr. Norwood contended that, under the current rate scenario, Detroit Edison will significantly overrecover its PSCR costs due in large measure to the migration of Detroit Edison's larger customers to ROA service. According to Mr. Norwood, when customers switch to ROA service, the average cost to supply the remaining PSCR customers decreases as the amount of relatively high-cost purchased power and gas-fired generation that was required to serve native system customers decreases. Because Detroit Edison

¹⁷The surcharge might be inadequate to generate the proposed funding during the first two years because rates are capped for several classes of customers.

forecasts an increase in customer migration to choice, Mr. Norwood testified that the utility's system average PSCR costs should continue to decrease.

Mr. Norwood explained that Detroit Edison's proposed 2004 PSCR plan costs (including the \$133.2 million mitigation adjustment) total \$891.2 million. According to Mr. Norwood, Detroit Edison proposes to initially implement an interim PSCR factor of 2.18 mills per kWh, which includes the costs of the proposed mitigation adjustment.¹⁸ Added to the PSCR cost currently collected through base rates, Detroit Edison would recover a total PSCR charge of 18.88 mills per kWh.

Mr. Norwood also testified that Detroit Edison's proposals to increase its 2004 PSCR costs by more than \$260 million to account for reclassified transmission expenses and its proposed mitigation adjustment are unreasonable. Although he recommends that the Commission reinstate Detroit Edison's PSCR clause for calendar year 2004, he argued that the Commission should disallow Detroit Edison's proposed adjustments for transmission expenses (\$126.9 million) and customer choice mitigation (\$133.2 million). Mr. Norwood explained that the mitigation adjustment is aimed at stranded costs that are primarily fixed investment and non-fuel operating costs, which have little to do with the costs recovered through the PSCR mechanism. Accordingly, he insisted that the appropriate forum for considering a mitigation adjustment would be Detroit Edison's stranded cost true-up proceeding, and not the PSCR plan or reconciliation process.

¹⁸Detroit Edison is currently collecting 16.70 mills per kWh in its base rates. In the final phase of the rate relief request, Detroit Edison proposes to increase the PSCR base rate, including its proposed mitigation adjustment, to 21.40 mills per kWh and to reset its PSCR factor to zero.

Mr. Norwood opposed allowing Detroit Edison to collect transmission investment and operating expenses and MISO charges through the PSCR process. Citing MCL 460.6j¹⁹ and Rule B-4.6 of Detroit Edison's tariffs,²⁰ Mr. Norwood stated that that the PSCR clause permits the recovery of only the reasonable and prudent booked costs of fuel and purchased and net interchanged power transactions, not projections of transmission expenses of the nature sought by Detroit Edison. According to the RRC, although it is appropriate to include transmission expenses required to wheel power purchased from other areas into Detroit Edison's system as a legitimate PSCR cost, Detroit Edison's proposal to include MISO and transmission investment and operating costs associated with transmission assets originally constructed to serve its native system would improperly shift costs from retail access and off-system wholesale customers to Detroit Edison's bundled service customers.

Attorney General

The Attorney General presented the testimony of one witness and six exhibits. Charles W. King, a consultant knowledgeable in ratemaking proceedings, expressed a belief that Detroit Edison's interim rate relief involved many matters that are very controversial issues of first impression, such as the mitigation adjustment, and rate design proposals that are inconsistent with existing Commission policies, such as the methodology for determining stranded costs. He also observed that Acts 141 and 142 affect Detroit Edison's request for interim relief in several ways. According to Mr. King, Acts 141 and 142 preclude any adjustment of rates. Mr. King believed

¹⁹MCL 460.6j defines allowable PSCR costs in terms of expenses related to fuel burned for electric generation and booked costs of purchased power and net interchanged power transactions by the utility.

²⁰Rule B-4.6 "permits the monthly adjustment of rates for power supply to allow recovery of the booked costs of fuel and purchased and net interchanged power transactions incurred under reasonable and prudent policies and practices in accordance with 1982 PA 304."

that, under Section 10d(2) of Act 141, MCL 460.10d(2), the rate freeze is still in effect because the Commission has not yet found that Detroit Edison meets the market test under Section 10f, MCL 460.10f. He also asserted that once Detroit Edison's rate freeze ends, Section 10d(2) still provides that the rates for certain customers cannot be increased until after specified dates. Indeed, Mr. King maintained that the only rates and costs at issue in this proceeding are those applicable to commercial and manufacturing customers with annual peak demands 15 kW or above, unless the Commission determines that Detroit Edison is experiencing a revenue sufficiency. Mr. King opposed consideration of rate increases for under 15 kW commercial and manufacturing customers and residential customers, arguing that their rates should be based on 2005 and 2006 data, respectively.

Mr. King stated that Detroit Edison understands that MCL 460.10d(2) imposes rate caps. However, he opined that Detroit Edison's rate proposal, which includes an interim increase in its PSCR factor and a request for approval of interim rate relief surcharges, is flawed because Detroit Edison plans to implement its rate requests with a qualification. According to Mr. King, the problem is that Detroit Edison's proposed tariffs, proposed PSCR factor, and proposed interim rate surcharges apply to customers whose rates are subject to a cap as well as to customers whose rates are not subject to a cap, and the only rates Detroit Edison can legally charge are those stated in its tariffs. Mr. King stresses that MCL 460.10d(2) prohibits rate increases, not billing increases or increased collection from approved rates. Therefore, he maintained that Detroit Edison's proposal must be refined before the Commission decides to approve any interim rate relief. In any event, Mr. King observed that, given that Detroit Edison has experienced substantial benefit from passage of Act 141 and securitization of \$1.75 billion in assets, it might be just and reasonable in

this case for the Commission to strictly implement the rate caps and prohibit cost shifting pursuant to Section 10d(2).

Mr. King opposed inclusion of transmission and MISO costs in Detroit Edison's PSCR factor for three reasons. First, he stated that these costs are not defined as includable by Act 304. Second, he pointed out that the MISO costs would be predictable and not susceptible to adjustment in a true-up proceeding. Third, he contended that the MISO transmission costs are not based on consumption, but aggregate demand.

Kroger

Kroger presented the testimony of one witness and six exhibits. Kevin C. Higgins, a consultant specializing in economic and policy analysis applicable to energy production, transportation, and consumption, testified that Detroit Edison's interim rate relief was both controversial and contrary to existing Commission policy. According to Mr. Higgins, Detroit Edison proposes "to levy draconian stranded cost charges in the amount of \$126 million" on its ROA customers. 10 Tr. 1533. He stated that these proposed stranded cost charges, when combined with the other charges that Detroit Edison was attempting to place on choice customers, would result in a 137% increase in ROA rates. Additionally, Mr. Higgins claimed that if all of the regulatory changes proposed by Detroit Edison were to be adopted, the costs of ROA customers would actually increase by 526% or an average of 2.555 cents per kWh. The additional cost items cited by Mr. Higgins included \$18 million associated with a 30% increase in unbundled distribution rates, \$7 million for LIEEF-related charges, the phase-in of a regulatory asset surcharge, the elimination of the securitization offset credit and the rate reduction equalization credit.

Mr. Higgins complained that Detroit Edison's case embraces the "revenues lost" stranded cost methodology that was previously considered and rejected by the Commission. He opined that the

utility's stranded cost proposal was "fundamentally misguided." 10 Tr. 1539. Mr. Higgins suggested that a far better approach would be to use traditional cost allocation procedures to fully allocate Detroit Edison's prudently incurred costs to all customers. According to Mr. Higgins, if fully allocated costs are accompanied by a rate spread between bundled and ROA customers that reflects cost-of-service principles, then stranded costs are necessarily zero at the start of the rate-effective period. Indeed, he stressed that Detroit Edison followed such an approach with regard to the elimination of excess securitization reserve that is used to fund the securitization offset and rate reduction equalization credits to ROA customers.

Mr. Higgins recommended that if the Commission grants Detroit Edison interim rate relief, all generation and transmission costs should be assigned to bundled service customers and that the distribution costs should be recovered from both bundled and ROA customers on a non-discriminatory basis. On Exhibit I-45, Mr. Higgins proposed that every customer class should be assessed the same increase (irrespective of the specific future treatment of PSCR charges) based on full interim revenue amount sought by Detroit Edison.

With regard to Detroit Edison's proposal to eliminate the securitization offset credit and the rate reduction equalization credit, Mr. Higgins stated "if the general rate increase proceeds as proposed by Detroit Edison, then the rate reduction equalization credit can not be sustained." 10 Tr. 1548. However, he recommended that, given the importance of the securitization offset credit to the ROA program, "it is essential that the Commission retain this credit and fund it from other sources" to avoid double charging ROA customers for generation costs. 10 Tr. 1548. In so doing, he reasoned that after implementation of a new rate structure, bundled customers will realize the benefits of securitization through reduced rates, whereas ROA customers will not share in these savings and they will therefore be forced to subsidize the generation costs.

Citing Exhibit A-11, Schedule C1-1, Mr. Higgins noted that the savings from securitization are \$271 million per year, which works out to be 6.3 mills per kWh. As shown on Exhibit I-47, a reduction of the bundled customers average securitization savings of only 0.884 mills per kWh would be sufficient to preserve the securitization offset credit for the ROA customers. As an alternative, Mr. Higgins suggested using a combination of the excess securitization savings (\$20 million) and a contribution from bundled customers (\$18 million) to fund the securitization offset credit during 2004.

Mr. Higgins also maintained that Detroit Edison's proposal to require ROA customers to contribute to the funding of its regulatory asset surcharge proposal was anticompetitive. According to him, only 44.61 % of the regulatory asset surcharge costs -- those exclusively associated with electric restructuring expenses -- should be paid by ROA customers.

MEC/PIRGIM

MEC/PIRGIM did not offer any testimony at the hearing, but it presented two exhibits and participated in the cross-examination of the witnesses of the other parties. In its brief, MEC/PIRGIM states that the amount of rate relief sought by Detroit Edison is excessive. According to MEC/PIRGIM, Detroit Edison's request for rate relief is greatly overstated due to the utility's reliance on uncertain forecasts and highly theoretical non-cost factors. Specifically, MEC/PIRGIM cites the Detroit Edison merger with Michigan Consolidated Gas Company (Mich Con) as problematic. MEC/PIRGIM insists that the Detroit Edison/Mich Con merger needs careful scrutiny to protect Detroit Edison's customers from subsidizing Mich Con's gas services or any of its unregulated affiliates. MEC/PIRGIM also opposes any relief based on Detroit Edison's merger premium argument.

MEC/PIRGIM supports the Staff's effort to scrutinize Detroit Edison's cost projections, but urges the Commission to go beyond the Staff's recommendations. While MEC/PIRGIM supports the nine specific adjustments totaling \$266,842,000, it believes that the Staff's recommended revenue deficiency of \$289 million is excessive. Citing the Staff's use of a "top-down" approach, MEC/PIRGIM contends that the Staff's position reflects myriad revenue deficiency exaggerations hidden within Detroit Edison's calculations. Among the additional adjustments supported by MEC/PIRGIM are rejection of Detroit Edison's mitigation adjustment for lost generation contribution margin, which MEC/PIRGIM argues is beyond the scope of the Commission's 1982 PA 304 (Act 304) jurisdiction, and Detroit Edison's \$80 million increase in annual pension expenses, which MEC/PIRGIM insists is inflated and not supported by the record.

MEC/PIRGIM also maintains that the Commission should reject Detroit Edison's position that issuance of this rate order eliminates contributions to the LIEEF from excess securitization savings. Citing MCL 460.10d(7), MEC/PIRGIM insists that the Legislature intended the LIEEF to exist for at least six years.

Finally, MEC/PIRGIM opposes consideration in the interim phase of the proceeding of Detroit Edison's position that it should be allowed to cease recognizing amounts reimbursed to Detroit Edison from insurance for storm damage.

Constellation NewEnergy

CNE filed a reply brief. In so doing, CNE takes no position regarding any of the revenue deficiency issues, such as pension and health care costs, environmental costs, or infrastructure improvements. However, CNE opposes consideration of the attempt by Detroit Edison to impose \$151 million in costs on choice customers. According to CNE, any effort to impose cost barriers to competition deserves to be fully litigated and resolved in the final phase of this proceeding.

III.

STANDARDS FOR PARTIAL AND IMMEDIATE RATE RELIEF

The statutory authority for the Commission to grant partial and immediate rate relief is set forth in MCL 460.6a(1), which states in part:

When a finding or order is sought by a gas or electric utility to increase its rates and charges, or to alter, change, or amend any rate or rate schedules, the effect of which will be to increase the cost of services to its customers, notice shall be given within the service area to be affected. The utility shall place in evidence facts relied upon to support the utility's petition or application to increase its rates and charges, or to alter, change, or amend any rate or rate schedules. After first having given notice to the interested parties within the service area to be affected and affording interested parties a reasonable opportunity for a full and complete hearing, the commission, after submission of all proofs by any interested party, may in its discretion and upon written motion by the utility make a finding and enter an order granting partial and immediate rate relief. A finding or order shall not be authorized or approved ex parte, nor until the commission's technical staff has made an investigation and report.

The parties do not contest that the procedural requirements have been met, but they are deeply divided on whether Detroit Edison's proposal for interim relief should be granted. Detroit Edison argues that it has more than satisfied all aspects of the "test" described in the testimony of Michael G. VanHaerents, Detroit Edison's Manager of Revenue Requirements. According to Mr. VanHaerents, Detroit Edison's proofs establish that there is evidence of a significant revenue deficiency and that the utility's rates are unreasonable. He also maintained that the interim rate relief proposed by Detroit Edison is not based on highly controversial issues and does not involve matters that clearly depart from past Commission ratemaking practices. Finally, he ensured that Detroit Edison would file a bond guaranteeing a refund of interim amounts if the final order reflects a rate increase in an amount less than the interim revenue deficiency.

In its brief and reply brief, Detroit Edison contends that any debate over whether its \$536 million revenue deficiency consists of highly controversial issues or represents a clear

departure in part or in whole from past ratemaking policies is extinguished by the fact that the utility's 2003 actual net income is significantly lower than the company's own estimates originally filed in the case. According to Detroit Edison, this fact alone demonstrates that Detroit Edison is already suffering under unreasonable and unjust rates.

Detroit Edison insists that the intervenors' claim that the requested relief is controversial or inconsistent with past practices is not supported by fact or law. Detroit Edison asserts that simple disagreement does not make the root cause of the deficiency in any way controversial. Moreover, Detroit Edison contends that its requested rate relief does not depart from any prior Commission practices. According to Detroit Edison, even if the choice-related aspects of the requested relief deviate from existing policies in some minor respects, the magnitude of the recent effect of the choice program and Act 141 coupled with the severity of Detroit Edison's earnings decline, more than outweigh any small measure of past Commission precedent that could conceivably be applied to these issues. Detroit Edison insists that all allegations that Detroit Edison has not met the standards for interim relief are merely a reflection of disagreements with the level of requested rate relief and not evidence that the utility's proposals are controversial, unsupported, or contrary to prior Commission policy. Indeed, Detroit Edison maintains that the severity of its demonstrated earnings decline is sufficient on its own to support approval of interim rate relief.

Detroit Edison's belief that all aspects of its interim proposal qualify for interim rate relief is not shared by any of the other parties to this proceeding. The Staff recommends nine revisions to Detroit Edison's calculation of its proposed revenue deficiency, which it maintains are not appropriate for consideration during the interim phase of the proceeding. It also failed to incorporate several of Detroit Edison's rate design proposals, which the Staff argued should be resolved in the Commission's final order.

Kroger maintains that Detroit Edison's proposals for the ROA program are controversial matters that involve clear departures from existing policy determinations. According to Kroger, the calculation of stranded cost has always been controversial. Additionally, Kroger maintains that Detroit Edison is relying on stranded cost calculation methodologies that have been rejected by the Commission.

The Attorney General argues that although MCL 460.6a(1) does not prohibit a utility from requesting partial and immediate rate relief equal to or almost equal to its requested final rate relief, the showing required to obtain interim relief differs from the standard for granting final rate relief. Therefore, the Attorney General asserts that the Commission should carefully review Detroit Edison's interim rate request.

Energy Michigan is highly critical of Detroit Edison's interim relief request. According to Energy Michigan, Detroit Edison's recent financial setbacks are due to problems other than choice, such as the August 14, 2003 blackout (\$16 million), an abnormally warm winter (\$63 million), and pension costs (\$28 million). Moreover, Energy Michigan insists that Detroit Edison's interim case is based on controversial issues, rejected positions, and a radical rate design that calls for collection of generation-related costs from ROA customers.

ABATE contends that the "top-down" methodology used by Detroit Edison and the Staff was recently rejected by the Commission. For that reason alone, ABATE insists that interim relief should be rejected. Additionally, ABATE asserts that each item of Detroit Edison's interim rate relief request is highly controversial and a clear departure from existing Commission policy. As examples, ABATE cites the regulatory asset surcharge, Detroit Edison's "lost revenue" stranded cost methodology, the mitigation adjustment, the inclusion of a huge pension expense increase, and recovery of a control premium.

The RRC argues that most of Detroit Edison's case does not meet the Commission's standards for interim relief. Citing case law identified by Energy Michigan, the Attorney General, and ABATE, the RRC insists that Detroit Edison misrepresents its positions as non-controversial and unrefuted. According to the RRC, Detroit Edison's mitigation adjustment is clearly contrary to existing law because, if approved, it would allow Detroit Edison to collect non-fuel base rate costs through the PSCR clause in violation of Act 304. Indeed, the RRC maintains the same defect is readily applicable to Detroit Edison's efforts to pass its transmission and MISO expenses through the PSCR clause.

MEC/PIRGIM contend that Detroit Edison's interim rate relief request is highly inflated and based on novel non-cost factors. MEC/PIRGIM maintain that the mitigation adjustment, merger control premium, and request for pension relief are clearly improper. However, MEC/PIRGIM support continuation of the LIEEF, albeit only after development of a complete record.

CNE limited its opposition of interim relief to rate design issues, which it maintained should only be addressed in the final phase of this proceeding.

MCL 460.6a(1) does not specify any substantive standards for the granting of a motion for partial and immediate rate relief. Over the years, the Commission has adopted various standards through the issuance of interpretive statements, guidelines, and case-by-case determinations.

In a January 11, 1971 order in Case No. U-3740, the Commission recognized that Section 6a(1) did not require the existence of an emergency or any other extraordinary condition as a precondition for granting partial and immediate rate relief. Rather, the Commission stated that partial and immediate rate relief was "an intermediate step in the normal course of determining final rates." Order, Case No. U-3740, p. 4. Indeed, after examining numerous cases,

the Commission observed that a denial of interim relief could be based on one or more of the following criteria:

1. The Staff's investigation and report did not reveal a revenue deficiency.
2. A final order was expected within a few weeks.
3. The motion did not comply with the statutory requirements.
4. There was no indication that future regulatory lag would be harmful to the utility.

However, the Commission also found that proof of an apparent existing revenue deficiency coupled with proof of one or more of the following criteria could entitle a utility to interim relief even if a final order could be issued within a short period of time:

1. An inability to arrange debt financing at reasonable rates without improved revenues.
2. A distinctive and sudden decline in revenues.
3. The existence of evidence indicating that deferral of interim relief until issuance of the final order would cause an unreasonable and harmful loss of revenues.
4. The existence of reasonable grounds for the Commission to believe that a denial of interim relief would cause irreparable harm to the utility.

In Case No. U-3740, the Commission was persuaded that Michigan Consolidated Gas Company (Mich Con) was entitled to interim relief because it had proven that awaiting a final order would cause it an unreasonable and harmful loss of revenues. More specifically, the Commission recognized that gas utilities earn a disproportionate share of their revenues during the winter heating season. Therefore, because the order in Case No. U-3740 was issued in January, unless given interim relief, the Commission concluded that Mich Con would forever lose a substantial amount of its revenues during its peak revenue months.

In 1975, the Commission adopted the standard established in Case No. U-3740 as Interpretative and Informational Statement (I&I) 1975-4. However, I&I 1975-4 was temporarily

relegated to history's dustbin by the issuance of Guideline 1981-1 on October 6, 1981, which provided the following standard for the issuance of interim relief:

The Commission believes that, after a review of all evidence relating to interim relief, proof of a revenue deficiency at that juncture constitutes proof sufficient for an award of interim relief.

Guideline 1981-1, October 6, 1981.

The standard adopted as Guideline 1981-1 was applied in the January 20, 1982 order in Case No. U-6839, wherein the Commission granted Mich Con \$35,034,000 in interim relief. However, in applying Guideline 1981-1 to Case No. U-6839, the Commission criticized that standard as "too vague." Order, Case No. U-6839, p. 3. In so doing, the Commission repudiated Guideline 1981-1 and replaced it with a standard that was taken almost verbatim from I&I 1975-4, which was proclaimed as the standard to be applied in all hearings on motions for interim relief held after January 20, 1982.

In its June 1, 1983 order in Case No. U-7298, the Commission observed that:

From a substantive standpoint, the Commission will grant a utility interim relief when the evidence presented establishes that a revenue deficiency exists and the rates of the utility have become unjust or unreasonable. The Commission will also require that the probable revenue deficiency be of some significance, since a relatively minor revenue deficiency in comparison to the utility's overall revenues would not constitute a circumstance in which it could be concluded that existing rates had become unjust and unreasonable.

In determining the probable existence of a revenue deficiency and the need for interim relief, the Commission will continue to adhere to its policy not to base interim relief upon highly controverted issues. In addition, the Commission will continue to adhere to its policy not to grant interim based upon issues which are clear departures from past Commission ratemaking policies.

Id., p. 7.

Moreover, the Commission saw fit to draw a distinction between the types of controversies that would rule out an adjustment for interim purposes:

The Commission will not consider controversial matters. In defining controversial, the Commission recognizes that there are two types of controversies: (1) controversy as to the adjustment; i.e., a new concept that deviates from the previous rate case, and (2) controversy as to the amount of the adjustment. The Commission will only consider adjustments where the controversy deals with the amount for an adjustment which has been previously authorized by the Commission in Applicant's last rate case or where all parties agree that the conceptual adjustment is one that should be reviewed. Those adjustments dealing with concepts which are controversial in nature will be summarily dismissed without any discussion.

Order, Case No. U-7298, p. 9-10.

A similar standard was followed in the December 20, 1983 order in Case No U-7650.

More recently, the Commission addressed the issue of the standard that controls interim relief in its January 23, 1990 order in Case No. U-9323. In so doing, the Commission stated:

Final rate relief is intended to allow utilities an opportunity to earn a fair return on their investment. Thus, it will be granted whenever a utility proves that it has a revenue deficiency. In contrast, interim rate relief is a special measure that can be used to protect a utility from financial hardship until final rate relief can be obtained through a fully litigated rate case. Therefore, this Commission finds that it should cautiously, rather than automatically, grant motions for interim rate relief. Thus, we find that compelling circumstances should exist.

Both the language of Act 3 and the Michigan Supreme Court decisions regarding interim rate relief support this position. For example, rather than allowing a gas utility to self-implement a rate increase in the same way that it can impose a new Gas Recovery factor under 1982 PA 304, Act 3 merely authorizes the Commission—in its discretion and upon written motion by the utility—to allow interim rate relief. In doing so, the Legislature provided a way to vary the usual process, when necessary, to provide relief prior to completion of a full hearing on all ratemaking issues. Because this mechanism allows for rate increases “pending submission of all proofs by any interested parties,” we find that it should be used sparingly.

Id., p. 10.

The reference in Case No. U-9323 to decisions of the Michigan Supreme Court pertains to Consumers Power Co v Public Service Comm, 415 Mich 134, 145; 327 NW2d 875 (1982), Great Lakes Steel v Public Service Comm, 416 Mich 166; 330 NW2d 380 (1982), and ABATE v Public Service Comm, 430 Mich 33; 420 NW2d 81 (1988). This trilogy of cases established that

(1) public utilities may seek a judicial remedy to obtain immediate rate relief if “compelling circumstances indicate that such relief is necessary” and the Commission has failed to provide relief [Consumers, supra p. 145.], (2) orders regarding partial and immediate rate relief are appealable, but are not final orders within the meaning of the Administrative Procedures Act of 1969, MCL 24.201 et seq., [Great Lakes Steel, supra], and (3) the Commission’s discretion to define the issues, factors, and standards for granting or denying partial and immediate rate relief in a given case is not so broad as to allow the Commission to exclude relevant evidence from intervenors [ABATE, supra]. While these Supreme Court decisions clarified several aspects regarding how motions for partial and immediate rate relief should be litigated, they do not obligate this Commission to apply any particular standard to do so.

Perhaps the most definitive discussion regarding the Commission’s broad discretion to establish standards for interim relief appears in Attorney General v Public Service Comm, 63 Mich 69; 234 NW2d 437 (1975), wherein the Court of Appeals stated:

The Attorney General argues that it has been commission policy in but a couple of isolated cases over a period of many years to find that an “emergency” exists before a partial and immediate rate increase can be granted. We are obligated to inquire what *legal* effect does this have? *This* commission is composed of appointees who are free and indeed obliged to exercise their best judgment within the limits of the legislative grant of authority to it. The “ninety-nine year” rule, that “it’s always been done that way” does not control. The issue simply is: does what they did fall within the statutory grant?

We find no suggestion that any of the [statutory] requirements were omitted or contravened. When we add to this the proviso in section 25 of the act, MCLA 462.25; MSA 22.44, that all rates fixed by the commission are “prima facie, lawful and reasonable until found otherwise in an action brought for the purpose pursuant to the provisions of section 26 of this act”, we could hardly do other than hold the assignment of error without merit. We do so hold.

Attorney General, supra, at pp. 75-76. (Emphasis in original).

Having reviewed the Commission’s prior statements and considered current circumstances, the Commission concludes that the primary purpose of interim relief is to provide additional

revenues on an expedited basis when the utility is experiencing a significant revenue deficiency and the revenue deficiency is likely to be experienced for a prolonged period of time. See, the December 21, 2001 order in Case No. U-13000.

Detroit Edison is alleging an immediate need for a revenue increase of \$536 million. The Commission is persuaded that the failure to consider interim relief at this time could cause a hardship to the utility due to the loss of revenues that can never be recouped. It is well established that the Commission cannot set a future rate to permit a utility to recover revenue lost during the pendency of a permanent increase request. Michigan Consolidated Gas Co v Public Service Comm, 389 Mich 624; 209 NW2d 210 (1973), General Telephone Co v Public Service Comm, 341 Mich 620; 67 NW2d 882 (1954), and Michigan Bell Telephone Co v Public Service Comm, 315 Mich 533; 24 NW2d 200 (1946). Therefore, the Commission turns to the question of whether, in light of all of the evidence, the Commission should exercise its discretion to grant all, any, or none of the interim relief sought by Detroit Edison, which will be examined on an issue-by-issue basis.

IV.

DISCUSSION

A. Preliminary issues

1. Statutory requirements

Act 141 provides that Detroit Edison may not increase its rates over and above the levels established by the rate decrease and rate freeze set forth in Section 10d²¹ until Detroit Edison has

²¹MCL 460.10d.

satisfied the Act 141 requirements governing market power in Section 10f²² and the electric transmission capacity expansion requirement set forth in Section 10v.²³

In a separate order issued today in Case No. U-13797 the Commission determined that Detroit Edison has complied with the requirements of Section 10f of Act 141.

In an order issued on December 6, 2002 in Case No. U-13646, which granted regulatory approval of Detroit Edison's proposal to sell and transfer its transmission assets to an independent third-party purchaser, the Commission found that if the sale of the transmission system were to be completed in the manner described in the application and if Detroit Edison enforced the contractual obligation that the purchaser complete the transmission upgrade projects identified in the joint transmission plan approved in Case No. U-12781, Detroit Edison would have fully complied with the provisions of Section 10v of Act 141. On May 29, 2003, Detroit Edison submitted the required verification that the transmission upgrade projects had been completed and are in commercial operation.

Therefore, the Commission finds that the requirements of Sections 10f and 10v of Act 141 have been met.

2. Detroit Edison/Mich Con Merger

MEC/PIRGIM maintains that the Commission should scrutinize the ramifications of the Detroit Edison/Mich Con merger in this proceeding beyond examination of the control premium issue. However, MEC/PIRGIM did not provide any specific justification for doing so as part of

²²MCL 460.10f.

²³MCL 460.10v, which required electric utilities serving more than 100,000 retail customers in Michigan to file a joint plan to expand, by June 5, 2002, the available transmission capability by at least 2,000 megawatts over the amount in place as of January 1, 2000.

interim relief. Therefore, the Commission declines to do so. MEC/PIRGIM is free to elaborate on this issue in the final order phase of the proceeding.

3. Consideration of Detroit Edison's 2004 PSCR Plan

Detroit Edison maintains that the Commission should act on its proposed 2004 PSCR plan at the same time that it issues the interim relief order. The Commission declines to do so.

In passing Act 304, the Legislature built into the PSCR process some protections for utilities and their ratepayers. One of the protections afforded to utilities is the ability to collect their proposed PSCR costs commencing at the beginning of the PSCR plan period. Accordingly, as of January 1, 2004, Detroit Edison has been entitled to full recovery of its proposed PSCR costs, which continues until the Commission issues an order approving its 2004 PSCR plan. Therefore, there is no harm to the utility in deferring a decision on its PSCR plan until later, which is particularly important given the complexity of this proceeding and the urgency with which Detroit Edison is seeking resolution of its interim relief request.

However, the Commission is troubled by the fact that Detroit Edison is currently over-recovering its projected 2004 PSCR costs by over 3 mills per kWh. When Detroit Edison was ordered to reinstate its PSCR clause as of January 1, 2004, the Commission specifically did not act to approve Detroit Edison's scheme to add a mitigation adjustment increase to the PSCR mechanism. Nevertheless, Detroit Edison has been acting as if the Commission authorized collection of the mitigation adjustment. Detroit Edison candidly acknowledges in footnote 12 on page 17 of its reply brief that, since January 1, 2004, it has overcharged its PSCR customers "in anticipation of an affirmative order from the Commission authorizing the proposed mitigation adjustment mechanism." The Commission has combed Act 304 for any shred of authority for Detroit Edison to deliberately overcharge its PSCR customers for this (or any other) reason. No such authority

exists. Detroit Edison is therefore in direct violation of both the Commission's December 18, 2003 order in this proceeding and of Act 304. Such intentional disregard for the law and the Commission's regulatory authority cannot be tolerated. Accordingly, the Commission directs Detroit Edison to pay the maximum fine allowed by MCL 460.558 (\$300 per day) for every day that Detroit Edison violated Act 304 and the December 18, 2003 order. The Commission also directs Detroit Edison to immediately reduce its PSCR clause effective February 21, 2004 to not more than a negative 1.05 mills per kWh and to refund to its PSCR customers on a historical usage basis all PSCR amounts overcollected from January 1, 2004 through February 21, 2004, with interest at 11%.²⁴

B. Revenue deficiency issues

1. Top-Down Methodology

Detroit Edison and the Staff made their recommendations through use of the top-down methodology, which features fully projected expenditures to be made by Detroit Edison during the 2004 test year.

Many parties oppose the use of this methodology because of its focus on projections rather than on historic data. Indeed, the Commission recently commented that use of the top-down methodology is not favored by the Commission. See, the December 18, 2003 order in Case No. U-13730, p. 10. However, as this proceeding commenced and the Staff's work was completed prior to the Commission's comment in Case No. U-13730, the Commission finds no reason to reject the positions taken by Detroit Edison and the Staff simply because of their reliance on the

²⁴Having ordered Detroit Edison to reduce its PSCR factor to a negative 1.05 mills per kWh, the Commission agrees with Detroit Edison that it should base interim relief on the methodology depicted on pages 8 and 10 of the Staff Report, which assumes full implementation of Detroit Edison's PSCR clause.

top-down methodology. The question is not whether Detroit Edison and the Staff strictly adhered to a particular ratemaking methodology, but whether the resulting proposed rates are just and reasonable. “The economic judgments required in rate proceedings are often hopelessly complex and do not admit of a single correct result.” Duquesne Light Co v Barasch, 488 US 299; 109 S Ct 609; 102 L Ed 2d 646 (1989). Indeed, sixty years ago in the landmark case of Federal Power Comm v Hope Natural Gas, 320 US 591; 64 S Ct 281; 88 L Ed 333 (1944), the United States Supreme Court recognized that there was no single constitutionally acceptable method for setting rates. In so doing, the Court observed: “[I]t is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unreasonable, judicial inquiry...is at an end. The fact that the method employed to reach that result may contain infirmities is not then important.” *Id.*, at 602, 64 S Ct 281, 88 L Ed 333. Therefore, the Commission rejects all arguments that the use of the top-down methodology justifies rejection of the positions taken by Detroit Edison and the Staff. However, the parties should be on notice that the Commission does not intend to use this methodology in future cases or in the final order in this case.

2. Merger Control Premium

Detroit Edison asks the Commission to increase customer rates by \$83.6 million to reflect the 2004 portion of the control premium paid by Detroit Edison to acquire Mich Con. It is Detroit Edison’s theory that Detroit Edison’s customers have benefited from the merger, so they should be required to compensate Detroit Edison for paying a premium over market costs to acquire Mich Con.

According to Daniel G. Brudzynski, Detroit Edison’s Vice President and Controller, the merger produced a new company that immediately realized operating synergies through economies of scale and scope, the consolidation of its corporate headquarters and support staff,

and the leveraging of contiguous and overlapping service territories. Detroit Edison alleges that the cost of these “merger synergies” was the portion of the acquisition premium that Detroit Edison was required to pay to take control of Mich Con. Mr. Brudzynski testified that it is appropriate for Detroit Edison to recover that portion of cost of the acquisition premium that made the merger possible because customers will receive the benefit from cost savings that are significantly greater than the portion of the acquisition premium that Detroit Edison seeks to recover in its rates. Mr. Brudzynski testified that Detroit Edison implemented a merger transition process designed to maximize value to customers, enhance employee opportunities, and improve customer satisfaction. He explained that the centralization of corporate staff functions was key to achieving operating efficiencies and merger synergies. Functions previously residing in separate corporate entities were centralized and consolidated into support organizations that provide a variety of services, which resulted in cost savings. Mr. Brudzynski alleged that customers of Detroit Edison would benefit from the leaner, more efficient organizations and processes.

Mr. Brudzynski testified that Detroit Edison paid \$2.488 billion for Mich Con, which represents a \$1.478 billion premium above Mich Con’s book value. Detroit Edison does not propose to recognize this entire amount as the acquisition premium. Instead, Detroit Edison requests that the Commission recognize only that portion of the acquisition premium that can be identified as related to the ability to exercise day-to-day control over the operations of Mich Con. Mr. Brudzynski calculated the control premium - the difference in the purchase price of Mich Con and the market value of Mich Con immediately prior to the announcement of the merger agreement – to be \$893 million. See, Exhibit A-16, Schedule F5-8.

Detroit Edison argues that because the cost of the control premium is less than the synergy savings, which Mr. Brudzynski placed at over \$150 million on an average annual basis, Detroit

Edison's customers have clearly received a net benefit from the merger. Thus, Detroit Edison maintains that it meets the standard for recovery enunciated by the Commission in its September 29, 1990 order in Case No. U-9323.

All other parties that took a position on this issue oppose any resolution of the control premium as part of interim relief. They assert that, because the ratepayers had no role in the decision to acquire Mich Con or in the negotiations, they should not be required to bear any of the expenses of that acquisition. Moreover, they contend that utilities are obligated to make necessary improvements in cost efficiencies, and should not expect to be compensated for merely doing what is expected of them. They also contend that the control premium is very controversial because expenses incurred by a corporate parent related to an acquisition should not be borne by Detroit Edison's ratepayers as they are not an operating expense of Detroit Edison. Moreover, they insist that even if the control premium results in the savings Detroit Edison claims, interim rate relief should not be based on costs that Detroit Edison will not actually incur.

The Commission finds that the issue of recovery of the control premium should be deferred to the final phase of this proceeding. This issue is highly controversial and the June 29, 1990 order in Case No. U-9323 stops well short of establishing precedent for granting recovery of an \$83.6 million control premium as part of interim rate relief. Indeed, in Case No. U-9323, the Commission noted that Michigan Gas Company's request for an acquisition adjustment "sparked substantial controversy." Order, supra, p. 20.

3. LIEEF and LIP Proposals

As previously noted, both Detroit Edison and Energy Michigan proposed some form of assistance program for low-income customers as was created in Section 10d(7) of Act 304. The Staff urged the Commission to defer consideration of this issue to the final phase of this

proceeding. MEC/PIRGIM maintains that MCL 460.10d(7) requires the LIEEF to remain funded for 6 years. Moreover, in anticipation that the parties will be addressing LIEEF issues during the final order phase of the proceeding, MEC/PIRGIM argues that the Commission should defer all LIEEF issues at this time.

The Commission finds that the Staff's proposal to defer this issue to the final phase of the proceeding should be rejected. The concept of a LIEEF was approved by the Legislature and has been in place and fully operational for several years. For those reasons, it can hardly be contended that the LIEEF issue conflicts with existing policy or is controversial.

The same cannot be said of Energy Michigan's LIP. Although targeted at vulnerable customer groups, Energy Michigan's proposal is untested and opposed by Detroit Edison as an invasion of its management prerogative. As such, adoption of the LIP is controversial because it is well established in Union Carbide v Public Service Comm, 431 Mich 135; 428 NW2d 322 (1988), that "[t]he power to fix and regulate rates, however, does not carry with it, either explicitly or implicitly, the power to make management decisions." Union Carbide, *supra*, at 148.

The Commission agrees with Detroit Edison that upon issuance of interim relief, there will no longer be any excess securitization savings available to fund the LIEEF. Therefore, if the LIEEF program is to continue, its costs must be incorporated into the utility's cost of service. Detroit Edison proposed to continue funding LIEEF, subject to two conditions. First, the LIEEF expense must be included as a line item in Detroit Edison's distribution revenue requirement, and, in turn, recovered from all bundled and choice customers. Second, Detroit Edison's funding obligation would be limited in light of Act 141's rate caps. Detroit Edison insists that if the Commission does not adopt its proposal, then the Commission should acknowledge the elimination of LIEEF

funding entirely from its distribution revenue requirement. The Commission finds Detroit Edison's conditions acceptable.

Detroit Edison has included \$39,858,000 in its O&M costs to fund the LIEEF during 2004 and beyond. Mr. VanHaerents explained that this level of funding is equivalent to 2% of commercial and industrial revenues from both choice and retail tariff customers. Full-service tariff customers would contribute \$33 million of that amount and choice customers would contribute \$7 million as part of the proposed increase to the RAST rate.

It is Detroit Edison's contention that, due to rate caps, only uncapped customers should contribute to the LIEEF. The Commission disagrees. Having ordered Detroit Edison to reduce its PSCR factor to a negative 1.05 mills per kWh to reflect the company's proposed PSCR costs, the Commission has cleared room under the caps for recovery of some of Detroit Edison's revenue deficiency that the utility would otherwise have been unable to collect due to the rate caps. Accordingly, the Commission directs that the \$39,858,000 of O&M expenses associated with the LIEEF proposal should be collected from all customers. Moreover, the Commission directs that the first dollars of interim relief collected by Detroit Edison should be used to fully fund the LIEEF, up to the \$39,858,000 amount that has been authorized.

4. Insurance Proceeds

In 2002, Detroit Edison experienced a higher than normal amount of storm damage. Accordingly, Detroit Edison proposed an adjustment to its 2002 historical test year data that facilitates comparison of that data to its 2004 test year data.

MEC/PIRGIM argues that the interim phase of the proceeding is not an appropriate time for resolution of Detroit Edison's contention that it should be authorized to cease recognizing amounts

received from insurance for storm damage. According to MEC/PIRGIM, this issue is too controversial to be resolved at this time.

The Commission finds that MEC/PIRGIM's position is not well taken. The most important consideration is that the 2004 test year contains a just and reasonable projection of Detroit Edison's anticipated reimbursements of storm damage costs. Because the adjustment complained of by the MEC/PIRGIM is in the nature of a normalization adjustment, the Commission is persuaded that it is appropriate for inclusion for interim purposes.

5. Mitigation Adjustment

In its application, Detroit Edison requested that the Commission reinstate its PSCR mechanism for 2004 effective as of the date that the Commission approves the interim base rate relief proposed by the utility, so long as the Commission also approves Detroit Edison's proposed mitigation adjustment. For 2004, the mitigation adjustment proposed by Detroit Edison is 3.23 mills/kWh, which would be added to its 2004 PSCR base rate. Detroit Edison explained that the purpose for the mitigation adjustment is to allow the utility to retain the value of mitigation of generation stranded costs arising from the resale of generating capacity and energy made available as a result of load loss arising from its customers' participation in retail choice. The mitigation adjustment will allow Detroit Edison to recover \$133 million from its PSCR customers, which is the utility's forecast of its 2004 profits from resale of excess energy resulting from the load loss due to customer choice.

The Staff did not address the mitigation adjustment, except to recommend its deferral to the final phase of the proceeding. All intervenors that addressed this issue sided with the Staff. The Commission finds that the mitigation adjustment should not be considered as part of interim relief. On its face, the proposed mitigation adjustment would increase PSCR rates by \$133 million

in 2004 and by even larger amounts in later years. The Commission has determined that the time is not right to approve Detroit Edison's 2004 PSCR plan, which is far less controversial than the mitigation adjustment. Moreover, the mitigation adjustment stands on shaky ground because the underlying costs appear not to be those envisioned by the Legislature for inclusion in PSCR expenses. Rather, the purpose of the mitigation adjustment is to allow Detroit Edison to recover theoretical lost contribution margin amounts associated with businesses that Detroit Edison no longer serves with respect to generation. Indeed, nothing in Act 304 or Rule B-4.6 of Detroit Edison's tariffs seems to allow the recovery of such costs through the PSCR clause. Therefore, the Commission finds that the mitigation adjustment should not be incorporated into Detroit Edison's interim relief. Nonetheless, the Commission suggests that the parties fully consider mitigation issues in their testimony on final rate relief.

6. Inclusion and Reclassification of Transmission Expenses

In its brief, the RRC opposes Detroit Edison's proposal to include as PSCR expenses all costs associated with transmission and MISO expenses, which were previously embedded in the company's base rates. According to the RRC, adoption of Detroit Edison's proposal would allow ROA customers to avoid responsibility for transmission expenses that were incurred by Detroit Edison on their behalf. The RRC also suggests that Detroit Edison's proposal is inconsistent with Act 304 and Rule B-4.6, which limit recovery through the PSCR process to expenses related to fuel burned for electric generation and booked costs of purchased power and net interchanged power transactions.

The Attorney General also commented on Detroit Edison's request for recovery of new MISO charges. The Attorney General asserts that such expenses are analogous to the additional Fermi 2

investment costs, which the Commission determined in Case No. U-8789 should not be recovered via interim rate relief.

In its reply brief, Detroit Edison states that its proposal to shift the incremental transmission costs from base rates to the PSCR process should be implemented in the final order, not as a part of interim relief. However, Detroit Edison stresses that it must be allowed to collect these expenses for interim purposes because, when obtaining needed transmission services to and throughout its service territory, Detroit Edison does and will pay for its transmission associated services based on the rates approved by the Federal Energy Regulatory Commission (FERC) for transmission services provided by the International Transmission Company (ITC) and MISO.

The Commission finds that the costs projected by Detroit Edison for transmission services provided by ITC and MISO are reasonable and should be recovered in base rates as part of its interim relief. However, the Commission agrees that the issue of the vehicle for the future recovery of such costs should be deferred to the final order.

7. Pension Costs

Detroit Edison proposes to include its estimated 2004 pension expense of \$113,475,000 in the determination of rates. This represents an increase in pension costs of \$80 million over the 2002 historical level. Existing rates are based upon an annual pension expense of approximately \$5 million.

The Attorney General and MEC/PIRGIM assert that Detroit Edison's proposal to collect a significant increased amount for pension expenses during the interim phase of this proceeding is improper. They contend that the increase for pension expense is based on projections and the effects of a 2002 deferral totaling \$532 million. They stress that the Commission has not previously approved Detroit Edison's deferral and recovery of this asset and that Detroit Edison's

proposal is controversial and should be subject to additional scrutiny. Indeed, they maintain that under analogous and potentially less controversial circumstances, the Commission recognized that significant doubts existed concerning Consumers Energy Company's proposed pension expense in its last securitization case.²⁵ For similar reasons, they insist that the Commission should not include Detroit Edison's pension expense increase in interim relief.

Energy Michigan also opposed consideration of this issue. Citing recent equity market gains, Energy Michigan assert that Detroit Edison's need for increased revenues for future pension obligations has diminished.

In response, Detroit Edison argues that the Attorney General and MEC/PIRGIM have had ample time to conduct an investigation of its proposed pension costs, but that they failed to do so. Detroit Edison also chastises Energy Michigan for its references to extra record evidence of recent direction of the equity market. According to Detroit Edison, any gains experienced due to price increases have been offset by declines in interest rates.

The Commission finds that Detroit Edison's proposal to increase the amount of O&M expenses built into its rates for pension costs should be approved for interim purposes, subject to one condition. Pension expenses are determined pursuant to the Statement of Financial Accounting Standards 87, and include four components: (1) service costs, which include pension benefits earned by active employees during the current period; (2) expected return on assets invested in the pension trusts; (3) expected interest costs associated with projected benefit obligations; and (4) amortizations of prior service costs and unrecognized gains or losses. Detroit Edison attributes the increases in pension expenses to reductions in the return on assets and increases due to a lower discount rate, which more than offsets reductions in interest rates.

²⁵See, the June 2, 2003 order in Case No. U-13715

Included in the pension liability is the amortization of \$532 million liability to recognize the excess of accumulated benefit obligations over the assets in the pension fund.

Because the calculation of pension expenses is heavily dependent upon the prevailing interest rates, the level of pension expenses can be volatile. This is especially true because the interest and discount rates are applied to long-lived assets and pension obligations. This volatility also extends to the level of required contributions to the pension fund. In 1998, 1999, and 2000, Detroit Edison made no contributions because its pension plan was fully funded. The company made contributions of \$35 million in 2001 and 2002, and a contribution of \$222 million in January 2003.

Although Detroit Edison has demonstrated that its \$113 million pension expense estimate is reasonable for 2004, the inherent volatility of that estimate coupled with the significant increase from the \$5 million level currently included in rates causes the Commission to conclude that additional protections are necessary to ensure that customers receive appropriate recognition for the higher pension expenses. Accordingly, the Commission will include \$113,475,000 in the determination of rates, but only on the condition that Detroit Edison agrees that it will make minimum annual prorated pension contributions equal to that amount during the period that these rates are in effect.²⁶ This will ensure that if pension expenses unexpectedly decline, customers will receive appropriate recognition in future rate determinations.

8. Pretax Overall Rate of Return Issues

Only Detroit Edison and the Staff took specific positions on the pretax overall rate of return that should be used to determine Detroit Edison's revenue deficiency. Detroit Edison proposes use of 10.01%, which it claims is superior to the Staff's use of 9.88%. According to Detroit Edison,

²⁶This minimum contribution requirement was proposed by the MEC/PIRGIM and Staff. The issue of whether the requirement should be continued after issuance of a final order is not ripe at this time.

not only is the Staff's position lacking in support, Detroit Edison's position is obviously superior due to the Commission's approval of that rate in its most recent rate case, Case No. U-10102.

Moreover, Detroit Edison asserts that if the Commission chooses to rely on the Staff's calculation, several adjustments to the Staff's position must be recognized.

The Commission finds that Detroit Edison's arguments are not well taken. Case No. U-10102 was based on a 1994 test year. Nothing in this record seriously suggests that the ten year old cost rates and rates of return from Case No. U-10102 are in any way pertinent to a fully projected 2004 test year. Likewise, the Commission is not persuaded that the adjustments proffered by Detroit Edison are appropriate, particularly when they result in an overall rate of return that exceeds the level supported by Detroit Edison as reasonable. In any event, because Detroit Edison did not raise these issues until its reply brief, the Commission is not persuaded that they should be considered at this time.²⁷

9. Capitalized A&G Expenses

One of the Staff's proposed adjustments is a \$16,325,000 downward adjustment to Detroit Edison's capitalized A&G expenditures. In its reply brief, Detroit Edison agrees with the adjustment, but offers that an offsetting positive adjustment for the additional revenue requirements associated with the increased capital expenditures needs to be made. Detroit Edison states that applying the Staff's methodology to both 2003 and 2004 data results in an average rate base increase in 2004 of \$24,375,000, which it maintains should have an associated \$2,456,000 revenue requirement (10.08% x \$24,375,000).

²⁷The Commission frequently refuses to consider matters raised for a first time in a reply brief. Moreover, it is unusual for the Commission to even receive reply briefs in support of interim relief.

The Commission agrees. However, the Commission finds that the proper revenue requirement adjustment is \$2,408,000 (9.88% x \$24,375,000).

10. Construction Expenditures

The Staff reduced Detroit Edison's rate base by \$63 million out of concern that Detroit Edison's projection of its 2003 and 2004 construction expenditures was inflated. The Staff based its adjustment, which had a total rate effect of \$8,677,000, on the utility's average expenditure over the prior five years, which is an accepted ratemaking approach.

In its reply brief, Detroit Edison maintains that the Staff's methodology is flawed because no supporting evidence was entered into the record. According to Detroit Edison, its positions are supported by testimony and exhibits.

The Commission finds that Detroit Edison's criticism of the Staff's adjustment to its 2003 and 2004 construction expenditures projections should be rejected. As previously noted, the Staff's position relies on a traditional ratemaking practice. MCL 460.6a(1) requires a Staff Report, which was proposed and admitted into evidence. The report specifically suggests that Detroit Edison's projection of its 2003 and 2004 construction expenses was inflated when compared to historical construction expenditures. The Commission finds the Staff's analysis is competent, credible, and more persuasive than Detroit Edison's evidence.

11. Return on Regulatory Asset Accruals and Deferred Accounting Request²⁸

The Staff Report suggests that Detroit Edison's proposed interim rate deficiency should be adjusted downward by \$13 million to remove the return on regulatory asset accruals for capped

²⁸The separate issue of Detroit Edison's proposed implementation of a surcharge to begin collecting its regulatory assets as part of its interim relief request is addressed in part IV D1 of this order.

customers that results from Act 141 deferred costs. In its reply brief, Detroit Edison seems to tacitly concede that because Act 141 characterized these assets as “cash costs,” the Staff’s adjustment may be appropriate under strict accounting principle. However, Detroit Edison insists that such approach leaves the utility at risk. According to Detroit Edison, by deferring recovery of its regulatory assets, Detroit Edison continues to incur \$23 million annually of related financing costs with no potential for recovery. Detroit Edison believes that the denial of recovery of ongoing financing costs related to its regulatory assets until the final order is totally inequitable and causes undue financial harm. Accordingly, Detroit Edison requests that, if the Commission decides to defer recovery of these regulatory asset amounts until the final order, then the Commission should authorize Detroit Edison to defer the return on regulatory asset amounts until its proposed regulatory asset surcharge is implemented.

The Commission finds that the Staff’s proposed \$13 million adjustment is reasonable and consistent with Act 141, and should be granted. Further, the Commission finds that Detroit Edison’s request for deferred accounting authority should be denied. Detroit Edison has requested that the Commission authorize deferred accounting authority for the ongoing financing costs on regulatory asset balances. The Commission rejects Detroit Edison’s request because the utility has authority pursuant to Act 141 to accrue financing costs on Section 10d(4) costs. In addition, the Commission has given Detroit Edison authority to accrue interest on accrued choice costs approved by the Commission. Any additional authority to accrue financing charges is a controversial matter that should be resolved in the final phase of this proceeding.

12. 2003 & 2004 O&M Expense Reduction

In the Staff Report, the Staff proposed to limit certain A&G expenses to the projected inflation rate for 2003 and 2004. It also proposed reducing Detroit Edison's requested O&M expense increase by 50%.

In its reply brief, Detroit Edison argues that the Staff's positions on this issue are arbitrary and completely unsupported by record evidence. According to Detroit Edison, the utility's A&G expenses are not driven by inflation. Further, Detroit Edison insists that its projections of its other O&M expenditures for 2004 are fully supported in the record and deserve more recognition than the Staff's unsupported suppositions.

The Commission finds that the Staff's recommendations should be adopted for interim purposes. The Staff's approach, which features reliance on inflation rates and halving of proposed expenditures for interim purpose, is reasonable and consistent with past ratemaking practices. MCL 460.6a(1) specifically authorizes the Commission to grant interim relief based on an exercise of "its discretion." In so doing, MCL 460.6a(1) specifically anticipates that the Commission will be able to rely on the Staff's investigation and report. After examining the record, the Commission finds that it would not be an abuse of discretion to base interim relief on the Staff's recommendation on this issue.

Moreover, the Commission places the parties on notice that, for final relief, the Commission intends to closely scrutinize the amounts of O&M expenditures to be included in Detroit Edison's rates. Toward that end, the parties should strive to place into the record all available information bearing on Detroit Edison's actual 2004 expenditures for O&M.

13. Recovery of Special Contract and Contract Discounts

In approving every special contract presented to the Commission in recent years, the Commission has specifically noted that for future ratemaking purposes, the Commission would not pass the special contract discount costs to the utility's other customers unless the utility met the significant burden of establishing that such customers actually benefited from the special contract. The Staff and intervenors contend that, for interim purposes, the Commission should impute to Detroit Edison the recovery of \$40.6 million associated with special contract discounts.

In its reply brief, Detroit Edison argues the imputation of any amount associated with its SMCs and LCCs is improper for interim purposes because the record supports a finding that Detroit Edison's other customers benefited from the existence of these contracts. Citing the testimony of Edward L. Falletich, Manager of Pricing in its Regulatory Affairs Department, Detroit Edison insists that the benefits of the company's special contracts substantially outweigh the revenue deficiency determined on a fully allocated cost-of-service analysis. See, Exhibit A-13, Schedule E6.2, which calculates a \$49 million net benefit. Moreover, citing Cincinnati Gas & Electric Co v Public Utility Commission, 86 Ohio St 3d 53; 711 NE2d 670 (1999), Detroit Edison maintains that it would be unlawful and unreasonable to impute revenue in addition to the actual contract rates.

The Commission finds that the Staff's position as adjusted to reflect the \$2.756 million revision proposed by ABATE should be accepted for interim relief. The imputation of special contract discounts is a long-standing Commission policy, which has passed scrutiny of this state's

appellate courts.²⁹ The Commission is not persuaded that it should be ignored for interim purposes.

14. Staff's Adjustment to Sales and Choice Volumes

The Staff adjusted Detroit Edison's proposed increase in choice volumes and corresponding decrease in sales volumes expected to occur in late 2004 when Detroit Edison's special contracts with certain customers are set to expire. The Staff explained that its adjustment reflects the fact that interim relief will probably be replaced by a final order before these contracts expire, so Detroit Edison's adjustment is not appropriate for interim purposes.

Detroit Edison did not oppose this adjustment in its reply brief. Therefore, the Commission finds that the Staff's adjustment should be incorporated for interim relief purposes.

15. New Infrastructure and Clean Air Act Costs

The Attorney General argues that Detroit Edison's attempt to recover new infrastructure and CAA costs totaling \$50,951,000 and \$68,033,000, respectively, as part of interim relief is inappropriate because such new costs are analogous to the additional Fermi 2 investment costs, which the Commission determined in the December 22, 1987 order in Case No. U-8789 should not be recovered via interim rate relief.

The Commission disagrees. In Case No. U-8789, Detroit Edison's request for interim relief was entirely related to Fermi 2 investment costs that had never been the subject of a prudence review. The Commission dismissed Detroit Edison's request for interim relief, in part, because the record evidence indicated that the reasonableness and prudence of the additional investment in the

²⁹In Midland Cogeneration Venture Limited Partnership v Public Service Comm, 199 Mich App 286; 501 NW 2d 573 (1993) the court upheld the imputation of revenues associated with a discounted economic development rate. Although not entirely analogous, this case is precedent from Michigan that is more persuasive than is case law from a foreign jurisdiction.

Fermi 2 plant was “highly controversial.” Order, supra, p. 4. The Commission finds that the record in this proceeding does not indicate that Detroit Edison’s expenditures for new infrastructure and CAA costs are unusually controversial. However, the Attorney General is free to pursue this issue in the final phase of this proceeding.

Nevertheless, given the amount of the CAA costs at issue (\$547 million), the effect of these costs on rates (\$68 million), the inability of the Commission and the Staff to closely scrutinize these expenditures due to use of the top-down methodology, and the fact that interim relief is within the Commission’s discretion, the Commission finds that it should apply a “reduction factor” of 30% for the purposes of interim relief.³⁰ In other words, the Commission finds that, for the purposes of interim relief, Detroit Edison’s proposal to include the entire \$68 million revenue effect associated with its CAA compliance costs should be reduced by 30% to \$47,622,000. In so doing, the Commission notes that the 30% reduction (\$20,410,000) is appropriate for interim relief in view of the fact that a number of issues that could substantially reduce Detroit Edison’s revenue deficiency have been deferred to the final phase of this proceeding.

C. Rate Design, Stranded Cost Methodology, and Transition Charges

This case deviates significantly from the routine interim proceeding in that the parties are as divided over interim rate design issues as they are over the revenue deficiency issues. Normally, the parties have little or nothing to say about rate design in an interim case, opting instead for an easy, equal percentage increase for all customer classes. This case is a dramatic departure from the norm.

³⁰Application of a similar reduction adjustment was determined to be appropriate in the Commission’s February 17, 1978 order in Case No. U-5502, which involved an earlier request by Detroit Edison for interim relief.

Detroit Edison asserts that \$151,253,000 of the interim revenue deficiency should be assigned to ROA customers for rate design purposes.

The Staff's position is that the Commission should adopt a transition charge to be paid by ROA customers in the neighborhood of 2 to 4 mills per kWh with the remainder of the revenue deficiency to be collected from bundled customers on an equal percentage basis. However, the Staff indicates that its proposal is applicable only to the interim phase of the proceeding.

Several parties assert that the Commission has previously rejected Detroit Edison's "revenues lost" methodology for determining stranded costs, and that such approach causes \$126 million of the utility's revenue deficiency to be placed on ROA customers. They urge the Commission to use traditional cost allocation procedures to fully allocate Detroit Edison's costs. Some parties, like Kroger, contend that stranded costs should be set at zero. Others, like Energy Michigan, suggest that Detroit Edison has experienced stranded benefits.

These parties are also critical of the Staff's approach. According to them, the Staff is confounded by having to deal with the issue of stranded costs in a rate case and simply resorted to a compromise position that calls for imposition of a stranded cost charge in the range of 2 to 4 mills per kWh.

The Commission concludes that an appropriate transition charge to recover stranded costs needs to be determined in the interim proceeding. The Staff has testified that a transition charge in the range of 2 to 4 mills per kWh is reasonable and is consistent with the level of stranded cost that the utility is experiencing. Detroit Edison has proposed transition charges of 8.5 mills per kWh for primary customers and more than 3 cents per kWh for secondary customers. If the appropriate transition charge is not recognized in the determination of interim rates, then regular bundled customers who do not choose an alternative supplier will be required to pay correspondingly

higher rates. Moreover, MCL 460.10a(9) requires the Commission to annually hold a contested case true-up proceeding to reconcile any over- or under-collections of net stranded costs, thereby ensuring that ROA customers are not over-charged for stranded costs. Because ROA customers are fully protected by the annual true-up, the Commission concludes that it should adopt the 4 mill per kWh charge at the high end of the Staff's range.

The Commission realizes that the effect of the interim order will not be just 4 mills per kWh on ROA customers. Rather, primary ROA customers will effectively incur an additional 7 mills, per kWh, for a total effect of 11 mills per kWh, while secondary customers will effectively incur an additional 9 mills per kWh, for a total effect of 13 mills per kWh, which is due to the termination of the securitization and the rate reduction offsets.

Detroit Edison's lost margin approach to calculating stranded cost, which this order rejects, clearly results in excessive transition charges. The Commission wishes to encourage all parties to use the final phase of this proceeding to suggest ways that stranded costs could be mitigated so as to reduce transition charges as much as possible and to analyze and make recommendations regarding the relationship between stranded cost determinations and return to service provisions for ROA customers.

As previously noted, interim rates are normally designed to recover an equal percentage increase from all customer classes. However, Detroit Edison is currently operating under a statutory rate cap that prohibits rates for residential customers from increasing before January 1, 2006, and commercial or manufacturing customers less than 15 kW from increasing before January 1, 2005. In this order, the Commission has required Detroit Edison to reduce its PSCR factor to a negative 1.05 mills per kWh. Accordingly, any increase in base rates for capped customers would violate the rate cap if the increase is more than the reduction in the PSCR factor.

Accordingly, the Commission finds that base rates should be raised by 2.99 mills per kWh for residential customers and 3.09 mills per kWh for commercial and manufacturing customers less than 15 kW. All customers not subject to the rate cap should be assessed an interim surcharge of 7.243%,³¹ which results in an effective \$101 million revenue increase for Detroit Edison.³²

D. Miscellaneous Issues

1. Regulatory Asset Surcharge

According to Detroit Edison, the utility accrued \$236 million in regulatory assets through December 31, 2003. The utility seeks to recover \$31 million of these costs from its large commercial and industrial customers in 2004.

The Staff insists that the issue of Detroit Edison's recovery of such regulatory assets is too controversial for interim relief. The Commission agrees. Accordingly, all parties are free to renew their positions on this issue in the final phase of this proceeding.

2. Continuation of Securitization Offset Credits

Kroger contends that the securitization offset credit must be maintained. It proposed several options for the securitization offset credit to be funded. According to Kroger, failure to retain this credit means that ROA customers will end up subsidizing bundled customers. Kroger complains that the Staff completely ignored the securitization offset credit issue, thereby backing into Detroit Edison's position on this issue. For this reason, Kroger asserts that the Staff's position on the treatment of ROA customers deserves to be ignored.

³¹The 7.243% surcharge is larger than 3.09 mills per kWh.

³²This number incorporates the offsetting PSCR reduction, a recognition of the transition charge, elimination of the securitization offsets, and contributions to the LIEEF.

The Commission finds that the issuance of interim relief ends the securitization savings and eliminates the justification for the securitization offset credits.³³

3. Potential Ramifications of Change in Act 141

The Commission is aware that, in addition to seeking regulatory relief before the Commission, Detroit Edison is concurrently pressing for legislative changes to Act 141. Today's order implements Act 141 as it currently exists, which the Commission is obligated to do, and provides Detroit Edison with one of the largest amounts of interim relief ever granted by this Commission, based largely on the utility's projections of future expenditures. The final phase of the proceedings still awaits litigation, briefing, and resolution by the Commission.

The interim rates adopted by this order are just, reasonable, and consistent with the current state of the law. However, because the Commission lacks prescience, it cannot ensure that Detroit Edison's interim rates will remain just and reasonable in the event that Detroit Edison is successful in amending Act 141 before the Commission finishes its work.

By issuing interim relief to Detroit Edison less than two weeks after the case became ripe for decision, the Commission has proven its ability to act swiftly to address the utility's concerns. Having acted in accordance with Act 141 to grant Detroit Edison significant interim rate relief, and having previously granted Detroit Edison relief in the form of authority to securitize up to \$1.74 billion of its assets pursuant to Act 142,³⁴ the Commission is convinced that now is not the best time to entertain the thought of releasing Detroit Edison from its statutory and regulatory obligations.

³³By incorporating the securitization savings into base rates, interim relief also obviates the need for Detroit Edison to place a billing message on its customers' bills regarding the 5% rate decrease associated with Act 141.

³⁴See, the November 2, 2000 order in Case No. U-12478. On March 9, 2001, Detroit Edison securitized \$1.75 billion of its assets.

While the Commission agrees that Detroit Edison has demonstrated the need for partial and immediate rate relief, it must take this opportunity to stress that the relief granted by this order is predicated, in its entirety, on the case record as has been presented based on the facts, circumstances, and laws – particularly Act 141 – as they exist today and as they are presumed to exist in the future. For the reasons stated above, significant modifications of Act 141 before the issuance of a final order, which is expected by the end of the year, could require immediate action by the Commission to ensure that the delicate balance struck by the interim order remains neutral for all parties to this case, and more importantly, does not adversely effect Detroit Edison’s full service ratepayers, choice customers, and AESs. The Commission’s primary responsibility is to ensure that the rates collected by utilities and paid by ratepayers are just and reasonable. Accordingly, if the regulatory framework shifts, the Commission’s response to Detroit Edison’s application will need to be rethought.

V.

SUMMARY

The Commission finds that Detroit Edison should be granted interim relief in the annual amount of \$248,430,000, which is based on the Staff Report position adjusted to reflect a \$2.756 million reduction for additional SMC revenues, a \$2.408 million increase related to the Staff’s adjustment for capitalized A&G costs, a \$39.8 million increase associated with inclusion of funding for the LIEEF, a \$20,410,000 CAA cost adjustment, and a transition charge of 4 mills per kWh.

There will be no rate increase for residential customers as a result of the Commission’s interim order because residential rates are capped until January 1, 2006. Although the order increases the

basic residential rate by 0.299 cents per kWh, it requires an equal reduction in the PSCR factor. The net effect is no change in the total residential rate.

There will be no net rate increase for small commercial customers with a demand less than 15 kW. Rates for these customers are capped until January 1, 2005. Larger commercial customers will see a surcharge of 7.243% to collect their proportionate share of the revenue deficiency and a reduction in the PSCR factors of 0.309 cents per kWh. The net effect of these will be an average increase of approximately 4%, although the actual percentage will vary by customer depending upon usage.

Industrial customers will experience the same percentage surcharge and same reduction in power supply costs that large commercial customers experience. Because of different usage patterns, the average industrial customers will experience an increase of approximately 2.3%.

ROA customers will have their distribution rates increased by approximately 0.1 cent per kWh and will be billed a transition charge of 0.4 cents per kWh to recover stranded costs. In addition, existing securitization offsets of approximately 0.7 cents per kWh for primary customers and 0.9 cents per kWh for secondary customers will be removed.

Finally, the order requires Detroit Edison to agree to make minimum contributions into its pension fund equal to the amount included in rates.

The Commission FINDS that:

a. Jurisdiction is pursuant to 1909 PA 300, as amended, MCL 462.2 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, 1999 AC, R 460.17101 et seq.

b. There is a substantial probability that Detroit Edison is experiencing a revenue deficiency of \$248,430,000 on an annual basis.

c. An award of partial and immediate rate relief in the annual amount of \$248,430,000 is warranted.

d. Detroit Edison should be required to file with the Commission a bond suitable to ensure that appropriate refunds will be made to its customers in the event that the final rate order in this proceeding provides for an annual rate increase of less than \$248,430,000.

e. Interim rates authorized by this order should be conditioned upon the agreement by Detroit Edison that it will make minimum annual prorated pension contributions equal to \$113,475,000 during the period that the authorized rates are in effect.

f. The partial and immediate rate relief increase should be implemented through use of an equal percentage increase by rate class for those customers not subject to the rate cap provisions of Act 141, by an interim charge of 2.99 mills per kWh for residential customers, and by an interim charge of 3.09 mills per kWh for all nonresidential customers subject to the cap.

g. Detroit Edison should be authorized to implement a transition charge of 4 mills per kWh.

h. Detroit Edison should be ordered to immediately reduce its 2004 PSCR factor effective February 21, 2004 to a negative 1.05 mills per kWh.

i. Detroit Edison should be ordered to refund to its PSCR customers on a historical basis all PSCR amounts overcollected from January 1, 2004 to February 21, 2004, with interest at 11%.

j. Detroit Edison should be ordered to pay a fine of \$15,300 to the Commission's Executive Secretary within 30 days of the issuance of this order.

THEREFORE, IT IS ORDERED that:

A. The Detroit Edison Company is authorized to increase its annual electric revenues by \$248,430,000. The partial immediate rate relief increase shall be implemented through use of an equal percentage increase by rate class for those customers not subject to the rate cap provisions of 2000 PA 141, by an interim charge of 2.99 mills per kilowatt-hour for residential customers, and by the interim charge of 3.09 mills per kilowatt-hour for all nonresidential customers subject to the cap.

B. The Detroit Edison Company shall file with the Commission a bond suitable to ensure that appropriate refunds will be made to its customers in the event that the final rate order in this proceeding provides for an annual rate increase of less than \$248,430,000.

C. Within 30 days, The Detroit Edison Company shall file revised rate schedules reflecting the rates approved in this order and set forth on Exhibit A.

D. The Detroit Edison Company is authorized to increase its rates by \$248,430,000 and to place into effect the interim surcharges that are attached to this order for service rendered on and after the day following the submission of a letter signed by Anthony F. Earley, Jr., Chairman and Chief Executive Officer of DTE Energy Company, to the Commission's Executive Secretary agreeing to the minimum pension contribution adopted by this order.

E. The Detroit Edison Company is relieved of the obligation to print a billing message on its customers' bills regarding the 5% rate decrease associated with Act 141.

F. The Detroit Edison Company shall immediately reduce its 2004 power supply cost recover factor effective February 21, 2004 to a negative 1.05 mills per kilowatt-hour.

G. The Detroit Edison Company shall refund to its power supply cost recovery customers on a historical basis all power supply cost recovery amounts overcollected from January 1, 2004 to February 21, 2004, with interest at 11%.

H. The Detroit Edison Company shall pay a fine of \$15,300 to the Commission's Executive Secretary within 30 days of the date of this order.

I. The Detroit Edison Company is authorized to implement a transition charge of 4 mills per kilowatt-hour upon satisfaction of the requirement set forth in paragraph D of the ordering section of 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.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ J. Peter Lark

Chair

(S E A L)

/s/ Robert B. Nelson

Commissioner

/s/ Laura Chappelle

Commissioner

By its action of February 20, 2004.

/s/ Mary Jo Kunkle

Its Executive Secretary

G. The Detroit Edison Company shall refund to its power supply cost recovery customers on a historical basis all power supply cost recovery amounts overcollected from January 1, 2004 to February 21, 2004, with interest at 11%.

H. The Detroit Edison Company shall pay a fine of \$15,300 to the Commission's Executive Secretary within 30 days of the date of this order.

I. The Detroit Edison Company is authorized to implement a transition charge of 4 mills per kilowatt-hour upon satisfaction of the requirement set forth in paragraph D of the ordering section of 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.

MICHIGAN PUBLIC SERVICE COMMISSION

Chair

Commissioner

Commissioner

By its action of February 20, 2004.

Its Executive Secretary

Exhibit A

The Detroit Edison Company
Proposed Surcharges by Rate Schedule - Interim

| Line No. | (a) | (b) | (c) |
|----------|---------------------------|-------------------|------------------|
| | Residential | Increase (\$/kWh) | Increase (%) |
| 1 | D1 Residential | \$0.00299 | |
| 2 | D1a Farm | \$0.00299 | |
| 3 | D1.1 Int. Space Cond. | \$0.00299 | |
| 4 | D1.2 Time-of-Day | \$0.00299 | |
| 5 | D1.3 Senior Citizen | \$0.00299 | |
| 6 | D1.4 Time-of-Day | \$0.00299 | |
| 7 | D1.5 Supp. Space Ht. | \$0.00299 | |
| 8 | D1.7 Time-of-Day | \$0.00299 | |
| 9 | D2 Space Heating | \$0.00299 | |
| 10 | D2a Farm | \$0.00299 | |
| 11 | D5 Res. Water Heating | \$0.00299 | |
| 12 | D9 Res. Outdoor Ltg. | \$0.00000 | |
| 13 | | | |
| 14 | Commercial | Under 15kW | Over 15kW |
| 15 | D1.1 Int. Space Cond. | \$0.00309 | 7.243% |
| 16 | D1.7 Time-of-Day | \$0.00309 | 7.243% |
| 17 | D3 Gen.Serv. (<15kW) | \$0.00309 | 7.243% |
| 18 | D3 Gen. Serv. (15kW+) | \$0.00309 | 7.243% |
| 19 | D3.1 Unmetered | \$0.00000 | 7.243% |
| 20 | D3.3 Interruptible | \$0.00309 | 7.243% |
| 21 | D3.4 Time-of-Day | \$0.00309 | 7.243% |
| 22 | D4 Lg. General Service | \$0.00309 | 7.243% |
| 23 | D5 Comm. Water Htg. | \$0.00309 | 7.243% |
| 24 | D9 Comm. Outdoor Ltg. | \$0.00000 | 7.243% |
| 25 | R7 Greenhouse Ltg. | \$0.00309 | 7.243% |
| 26 | R8 Space Conditioning | \$0.00309 | 7.243% |
| 27 | | | |
| 28 | Primary | | |
| 29 | D6 Primary Supply | | 7.243% |
| 30 | D6.1 Alt. Primary | | 7.243% |
| 31 | D6.2 Space Cond. | | 7.243% |
| 32 | D8 Interruptible Primary | | 7.243% |
| 33 | D10 Electric Schools | | 7.243% |
| 34 | R1.1 Alt. Metal Melting | | 7.243% |
| 35 | R1.2 Elec. Process Htg. | | 7.243% |
| 36 | R3 Standby | | 7.243% |
| 37 | R10 Interruptible Supply | | 7.243% |
| 38 | | | |
| 39 | Governmental | | |
| 40 | E1 Street Lighting | | 7.243% |
| 41 | E1.1 Energy Only St. Ltg. | | 7.243% |
| 42 | E2 Traffic Lights | | 7.243% |
| 43 | E4 Primary Pumping | | 7.243% |
| 44 | E5 Secondary Pumping | | 7.243% |
| 45 | | | |
| 46 | EC1/EC2 Retail Access | | 7.243% |