

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of **INDIANA
MICHIGAN POWER COMPANY** for a
power supply cost recovery reconciliation
proceeding for the 12-month period ended
December 31, 2021.

U-20805

**EXCEPTIONS TO PFD
BY ATTORNEY GENERAL DANA NESSEL**

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I. INTRODUCTION

This case concerns an application by Indiana Michigan Power Company (I&M or the Company) for approval to reconcile revenues collected pursuant to its 2021 power supply cost recovery (PSCR) plan. On December 1, 2023, Administrative Law Judge (ALJ) Sharon L. Feldman issued her Proposal for Decision (PFD) recommending that the Michigan Public Service Commission (MPSC or the Commission) 1) revise I&M's filed beginning balance as recommended by the Commission Staff; 2) disallow costs incurred under I&M's inter-company power agreement (ICPA) with Ohio Valley Electric Corporation (OVEC) that exceed the market price cap for affiliate transactions under the MPSC Code of Conduct; 3) reject the Attorney General's proposed disallowance for Rockport plant generation costs incurred under I&M's unit power agreement (UPA) with AEP Generating Company (AEG) that exceed the market price cap for affiliate transactions under the Code of Conduct¹, but consider requiring an evaluation of the UPA in another docket; and 4) disallow costs that I&M would have avoided had it met its energy waste reduction (EWR) plan target. The Attorney General files these exceptions with respect to the ALJ's recommendations regarding the Rockport UPA. The PFD erred in not recommending a disallowance for the 2021 Rockport UPA costs because I&M did not meet its burden of proving the costs were reasonable and prudent and in compliance with the Code of Conduct, and the Attorney General specifically addressed the Commission's reasons for not disallowing a portion of the 2020 Rockport UPA costs

¹ The Attorney General's recommendation is fully explained in her initial brief at pp. 39-45.

in Case No. U-20530. However, if the Commission does not disallow any 2021 UPA costs in this proceeding, at a minimum the Commission should adopt the PFD's recommendation to open a separate docket to fully evaluate the Rockport costs.

II. EXCEPTIONS

The PFD erred in not recommending a disallowance for I&M's 2021 Rockport UPA costs based on a comparison to I&M's 2020 Rockport UPA costs. I&M failed to meet its burden of proof and the Attorney General specifically addressed the Commission's reasons for not disallowing a portion of the 2020 UPA costs in Case No. U-20530. The Attorney General specifically addressed the Commission's reasons for not disallowing some of the 2020 costs – *i.e.*, the prior review and partial approval of those costs and the impact of COVID-19 on the 2020 energy market. Further, a comparison of the 2021 and 2020 Rockport UPA costs cannot relieve I&M of its burden to prove the 2021 costs were reasonable and prudent and in compliance with the Code of Conduct – a burden the Company failed to meet.

The Commission should reject the ALJ's conclusion and disallow the Michigan share of 2021 Rockport UPA costs that exceed the Code of Conduct's market price cap for four reasons: 1) I&M has not met its burden of proving the costs are reasonable and prudent and in compliance with the Code of Conduct; 2) I&M has done nothing to pursue changes to the Rockport UPA to minimize costs to ratepayers as directed by the Commission; 3) to the extent some costs were previously reviewed and approved, they are subject to reevaluation because ratepayers are no longer fairly

compensated for them; and 4) the Commission’s primary justification for declining to adopt a disallowance in 2020 – *i.e.*, the “unique circumstances” of COVID-19 – are not present in 2021 and do not preclude evaluation of the costs in this proceeding. If the Commission is still not inclined to disallow any 2021 UPA costs in this proceeding, at a minimum the Commission should adopt the PFD’s recommendation to open a separate docket to review the costs I&M recovers attributable to its Rockport ownership interest and the costs the company recovers through the PSCR factor attributable to the UPA.

A. Background

The Code of Conduct prohibits discrimination in favor of a utility’s affiliates and addresses “the potential lack of arms-length bargaining and improper subsidization of the affiliate’s unregulated operations through the utility’s rates”² by capping at market price what a utility may pay an unregulated affiliate for goods and services.³ More than four years ago, in I&M’s 2018 PSCR plan case, Case No. U-18404, the Commission considered the 12.16% return on equity (ROE) included in the demand charge I&M pays AEG for capacity under the Rockport UPA and directed I&M to “demonstrate . . . that its wholesale purchases from affiliates are just and reasonable under current market conditions” and that it is “taking appropriate actions to minimize costs to ratepayers.”⁴ The Commission put I&M on notice that it has a “responsibility” to “examin[e] existing contracts as market conditions or other

² *Midland Cogeneration Venture Ltd Partnership v Public Service Comm’n*, 199 Mich App 286, 313-14; 501 NW2d 573 (1993) (citations omitted).

³ Mich Admin Code R 8(1), (4).

⁴ Case No. U-18404, Order dated June 7, 2019, p. 5.

factors change over time and pursu[e] amendments or new contractual arrangements,” and that it is not reasonable and prudent to be “complacent by not pursuing changes” to existing agreements.⁵

In I&M’s 2020 PSCR reconciliation case, Case No. U-20530, Attorney General witness Devi Glick calculated the cost of the AEG power I&M purchased under the Rockport UPA in 2020 to be \$122.24 per MWh.⁶ In his PFD for Case No. U-20530, ALJ Jonathan Thoits found that I&M’s purchase of Rockport power under the UPA is an affiliate transaction subject to the Code of Conduct and its market price cap. ALJ Thoits found the 2020 Rockport UPA costs unreasonable and recommended a disallowance of \$7.1 million – the Michigan share of the 2020 Rockport UPA costs that exceeded the amount ALJ Thoits found to be the most appropriate proxy for market price.⁷

In its Order resolving Case No. U-20530, the Commission agreed that I&M’s purchase of power from AEG under the Rockport UPA is an affiliate transaction subject to the Code of Conduct and its market price cap:

The Commission agrees that the UPA is subject to the pricing provisions of the Code of Conduct. I&M and AEG are wholly owned subsidiaries of AEP, and the agreement provides for I&M to compensate AEG for power and energy. The Commission agrees with the Attorney General that the transactions for power and energy equate to affiliate transactions for products and possibly services and are thus subject to Rule 8(4).⁸

⁵ *Id.* at p. 7.

⁶ Case No. U-20530, PFD dated April 18, 2022, p. 44.

⁷ Case No. U-20530, PFD dated April 18, 2022, pp. 61-62.

⁸ Case No. U-20530, Order dated February 2, 2023, p. 15.

Nonetheless, the Commission declined to adopt ALJ Thoits' recommended disallowance, "not[ing]" that the Rockport UPA costs had been "reviewed and at least partially approved" in a 1991 settlement agreement, finding that the "unique circumstances created by COVID-19 during 2020 d[id] not allow for a proper evaluation of the UPA during the PSCR period in question," and summarily concluding that the UPA costs were "not unreasonable."⁹

B. The Commission should disallow excess 2021 Rockport UPA costs.

In 2021, the Rockport UPA costs rose even higher. I&M purchased 70% of AEG's share of energy and capacity from the Rockport plant under the UPA at an average cost of \$129.60 per MWh for a total cost just under \$218 million.¹⁰ The Attorney General presented testimony from Ms. Glick supporting a disallowance of either \$18.3 million or \$20.6 million, each of which represents the Michigan share of the amount by which the 2021 Rockport UPA costs exceed a reasonable benchmark for long-term supply contracts.¹¹ In her PFD, ALJ Feldman recognized that the Rockport UPA costs were "well above market prices" but found that the Commission's reasons for not adopting a disallowance in Case No. U-20530 had not been adequately addressed. Comparing the 2021 Rockport UPA costs to those the Commission found were "not unreasonable" in 2020, the ALJ found "no substantial basis on this record to reach a different conclusion."¹² However, the Attorney General's testimony did

⁹ Case No. U-20530, Order dated February 2, 2023, pp. 14-15.

¹⁰ AG Initial Brief at p. 39.

¹¹ *Id.* at pp. 44-45.

¹² PFD, p. 65.

address the decision in U-20530 and there is substantial evidence in this record to disallow the excess UPA costs here.

- i. The “unique circumstances” that precluded evaluation of the Rockport UPA costs in 2020 are not present in 2021 and do not preclude evaluation of the Rockport UPA costs in this proceeding.*

First, as the ALJ acknowledged, the Attorney General specifically addressed the Commission’s primary basis for declining to adopt a disallowance for the 2020 Rockport UPA costs by presenting evidence that the energy market had rebounded from the effects of the COVID-19 pandemic that began in 2020. Ms. Glick testified that the “unique circumstances” of 2020 “did not persist in 2021,” and “[t]he energy market had recovered by 2021.”¹³ I&M did not rebut this testimony. Therefore, the “unique circumstances” that the Commission found precluded evaluation of the Rockport UPA costs in 2020 do not preclude evaluation of the Rockport UPA costs in this proceeding.

- ii. Any Rockport UPA costs that were previously reviewed and approved are subject to reevaluation in this proceeding.*

Second, the Attorney General specifically addressed the 1991 settlement agreement that the Commission “note[d]”¹⁴ in Case No. U-20530 and presented evidence that any prior review and partial approval of Rockport UPA costs was limited and remains subject to reevaluation. The 1991 settlement agreement authorized inclusion of the capacity charges for Rockport Unit 2 only.¹⁵ It expressly

¹³ Direct testimony of Devi Glick, 2 Tr 193.

¹⁴ Case No. U-20530, Order dated February 2, 2023, pp. 15-16.

¹⁵ AG Initial Brief, p. 5 (citing Ex. AG-25, Settlement Agreement in Case No. U-9656). The relationship between I&M and each of the two Rockport units is fully detailed in the PFD at p. 51 (quoting Case No. U-20804, Order dated November 18, 2021, pp. 23-24).

permits any party to challenge the Rockport 2 capacity charges “if circumstances change such that Michigan ratepayers are no longer fairly compensated for the cost of the generating capacity which I&M makes available to the AEP System.”¹⁶ Here, circumstances have changed such that Michigan ratepayers are receiving just \$38.56 in energy value and \$21.78 in capacity value for Rockport services that cost \$129.60 per MWh under the Rockport UPA – a premium of \$67.97 per MWh for costs incurred under the Rockport UPA.¹⁷ This excess and unjustified premium satisfies the 1991 settlement agreement’s condition for challenging the Rockport 2 capacity charges, and the agreement never included the Rockport 2 energy charges or any charges for Rockport 1.¹⁸ The terms of the 1991 settlement agreement also would not apply to the current version of the UPA, which was amended in 2018¹⁹ and has never been presented to the Commission for review.

iii. I&M has done nothing to pursue changes to the Rockport UPA as directed by the Commission.

Third, I&M has presented no evidence that it has done anything to pursue changes to the Rockport UPA to minimize costs to ratepayers as the Commission directed it to four years ago. The Attorney General has twice asked I&M in discovery to identify all actions it has taken to seek changes to the Rockport UPA since the Commission’s Order in Case No. U-18404, and twice I&M has identified nothing. In

¹⁶ AG Initial Brief, p. 5 (citing Ex. AG-25, Settlement Agreement in Case No. U-9656, paragraph 10).

¹⁷ AG Initial brief, p. 41.

¹⁸ While the Commission noted only the 1991 settlement agreement in declining to adopt a disallowance in Case No. U-20530, the Attorney General notes there was an older settlement agreement that did address Rockport 1 charges. However, that settlement agreement, which relates to Case No. U-8037, applied only to the years 1985 and 1986, and does not impact the evaluation of Rockport 1 charges today. *See* AG Initial Brief, p. 5.

¹⁹ AG Initial Brief, p. 5.

Case No. U-20530, I&M pointed to the 2018 amendment, which predates the Order in Case No. U-18404 and has never been presented to the Commission.²⁰ In this case, I&M simply asserted that the Rockport UPA is a beneficial financing arrangement.²¹ Whatever benefits may exist, they “do[] not absolve a utility from monitoring and responding to market conditions and system needs and making good faith efforts to manage existing contracts.”²² The Rockport UPA’s 12.16% ROE remains as inflated as it was in Case No. U-18404, when the Commission clarified I&M’s obligations with respect to its long-term supply contracts and put I&M on notice that complacency is neither reasonable nor prudent.

iv. I&M has not met its burden of proving the Rockport UPA costs are reasonable and prudent and in compliance with the Code of Conduct.

Fourth, and perhaps most importantly, the burden of proof with respect to the reasonableness and prudence of the Rockport UPA costs and their compliance with the Code of Conduct is on I&M, and I&M has not met its burden.²³ While the Attorney General has presented evidence demonstrating that the Rockport UPA costs are unreasonable and exceed the Code of Conduct’s market price cap, it is not the Attorney General’s burden to prove the Rockport UPA costs are *not* reasonable and prudent or *not* compliant with the Code of Conduct.

The PFD erred by finding that the Attorney General had not “specifically addressed” the Commission’s findings in Case No. U-20530 and grounding its

²⁰ Case No. U-20530, PFD dated April 18, 2022, p. 21.

²¹ Ex. AG-29, I&M response to AG 1-17.

²² Case No. U-20203, Order dated December 9, 2020, p. 26.

²³ See Case No. U-13562, Order dated June 27, 2003, p.3 (“[T]he burden is on the utility to demonstrate that its PSCR costs are attributable to reasonable and prudent management decisions.”).

conclusion that the 2021 Rockport UPA costs were not unreasonable in a comparison to 2020 Rockport UPA costs that the Commission found “not unreasonable.”²⁴ The Attorney General did specifically address the COVID-19 issue and the limited nature of any prior review and approval of Rockport UPA costs, which were the only reasons the Commission provided for declining to adopt ALJ Thoits’ recommended disallowance in Case No. U-20530. But even if the Attorney General had not done so, I&M is the party with the burden of proof and any evidentiary deficiencies must result in a finding that I&M has not met its burden. A comparison of 2020 and 2021 Rockport UPA costs is no substitute for an evaluation of the evidence I&M presented to support its position that the Rockport UPA costs are reasonable and prudent and in compliance with the Code of Conduct, and I&M presented no such evidence. Instead, I&M rehashed previously rejected arguments that the Code of Conduct does not apply to the Rockport UPA, when the Commission has already held that it does, and failed to identify any suitable alternatives to the reasonable benchmarks for long-term supply contracts the Attorney General presented.

There is no exception in the Code of Conduct for agreements that were partially approved, or approved for a limited time period decades ago. Nor is there any exception in the Code for costs incurred with an affiliate that are above market but similar to costs that were approved in a prior PSCR proceeding. The Commission has held repeatedly that a utility must demonstrate compliance with the Code’s pricing provisions in each PSCR reconciliation case.²⁵

²⁴ PFD, p. 61.

²⁵ See, e.g., Case No. U-20527, Order dated April 8, 2021, p. 22.

For these reasons, the Commission should find that I&M has not shown the Rockport UPA costs are reasonable and prudent, has not shown that its purchase of power from AEG under the Rockport UPA complies with the Code of Conduct, and is not entitled to recover from ratepayers the Michigan share of Rockport UPA costs that exceed the Code of Conduct's market price cap.

C. In the alternative, the Commission should require an evaluation of the Rockport costs in a separate docket.

If the Commission still decides to not disallow the excess Rockport UPA costs, it should at least adopt the ALJ's recommendation to "require I&M to present a review of the costs it recovers attributable to its ownership interest and the costs it recovers through the PSCR factor attributable to the UPA in a separate docket in which I&M is required to present the full terms of the UPA and referenced agreements."²⁶ The Rockport UPA costs are astronomical – they are far above the market price for energy and capacity, and far above the cost of any comparable long-term supply arrangement. If the Commission does not adopt a disallowance in this proceeding, Michigan ratepayers will bear the cost of I&M paying its affiliate more than double the market value for Rockport energy and capacity. As ALJ Thoits noted in Case No. U-20530, "[b]oth the reasonableness standard and [Code of Conduct] Rule 8(4) are specifically meant to protect ratepayers by ensuring that utility transactions are commensurate with the then-current market conditions."²⁷ Where the costs of an affiliate transaction subject to the Code of Conduct are so clearly and significantly in

²⁶ PFD, p. 66.

²⁷ Case No. U-20530, PFD dated April 18, 2022, p. 35.

excess of market value, the Commission, which has “complete power and jurisdiction” to regulate public utilities in Michigan, cannot do nothing.²⁸ It must act to ensure that Michigan ratepayers are protected from unreasonable and imprudent decision-making and discrimination in favor of affiliates in violation of the Code of Conduct.

D. CONCLUSION

For the reasons discussed above, the Attorney General respectfully excepts to the PFD. The Attorney General asks the Commission to disallow the Michigan share of Rockport UPA costs that exceed the Code of Conduct market price cap or, in the alternative, require an evaluation of the Rockport costs in a separate docket.

Respectfully submitted,

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²⁸ MCL 460.6(1).

PROOF OF SERVICE - U-20805

The undersigned certifies that a copy of the *Attorney General's Exceptions to PFD* was served upon the parties listed below by e-mailing the same to them at their respective e-mail addresses on the 5th day of January 2024.

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