S T A T E   O F   M I C H I G A N

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of **INDIANA MICHIGAN POWER COMPANY** for approval to implement a power supply cost recovery plan for the 12 months ending December 31, 2022.	)	Case No. U-21052

At the June 22, 2023 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. Daniel C. Scripps, Chair
Hon. Katherine L. Peretick, Commissioner

ORDER

On May 13, 2021, the Commission issued an order in Case Nos. U-21046 *et al*. directing Indiana Michigan Power Company (I&M) to file its 2022 power supply cost recovery (PSCR) plan in its assigned docket number. On September 30, 2021, I&M filed its application with supporting testimony and exhibits, pursuant to Public Act 304 of 1982, MCL 460.6j (Act 304), requesting approval of its PSCR plan and monthly PSCR factor of 6.23 mills per kilowatt-hour (kWh) or $0.00623 per kWh for the 12-month period ending December 2022. Application, p. 3. Also included in the application is the company's request for approval of its five-year forecast of projected power supply requirements, anticipated sources of supply, and projections of power supply costs and approval to continue the roll-in methodology approved in the company's 2007 PSCR plan case, Case No. U-15004. Application, p. 3.

A prehearing conference was held on December 14, 2021, before Administrative Law Judge Jonathan F. Thoits (ALJ), at which the ALJ recognized the right of intervention by the Michigan Department of Attorney General and granted intervention to the Sierra Club and the Citizens Utility Board of Michigan (CUB).[1] I&M and the Commission Staff (Staff) also participated in the proceeding. The ALJ issued a protective order in this matter on December 16, 2021. An evidentiary hearing was held on May 10, 2022, at which testimony and exhibits were bound into the record and cross-examination was conducted.[2] Initial briefs were filed on June 7, 2022, by I&M, the Staff, and the Sierra Club. Reply briefs were filed on June 28, 2022, by I&M and the Sierra Club, with the Staff indicating in a letter filed in the docket that it would not be filing a reply brief.

The ALJ issued a redacted proposal for decision (PFD) in this matter on March 29, 2023, with a confidential PFD filed under seal.[3] Exceptions to the PFD were filed on April 19, 2023, by I&M. Replies to exceptions were filed on May 3, 2023 by the Staff and the Sierra Club. The record in this matter consists of 404 pages of transcript and 48 exhibits admitted into evidence.[4]

Proposal for Decision, Exceptions, and Replies to Exceptions

Following a recitation of the applicable legal standards to the instant proceeding, the ALJ stated that the following elements of I&M's PSCR plan and five-year forecast were not contested

[1] CUB did not participate in this proceeding beyond its petition to intervene.

[2] A portion of the testimony and exhibits was confidential and, therefore, filed under seal on the record.

[3] Citations to the PFD in this order refer to the redacted PFD available in this docket for public viewing.

[4] As stated, portions of the transcript and some exhibits admitted into evidence were filed confidentially. Citations to the record in this order refer to the redacted transcript and exhibits available in this docket for public viewing.

by the parties and recommended that the projections used for these elements to develop the company's PSCR factor should be accepted by the Commission:

> sales forecast by customer class; energy requirements; generating capacity; annual peak energy and load factors; energy sources from generation and purchased power; costs associated with those energy sources, i.e., fossil, nuclear, hydro, wind and solar; and coal purchasing strategy.

PFD, p. 5. The ALJ explained that the issues disputed by the parties consist of I&M's projected costs for purchased power from 2020 through 2024 under an Inter-Company Power Agreement (ICPA) with the Ohio Valley Electric Corporation (OVEC) and I&M's unit commitment decisions at the Rockport power plant. As discussed in further detail below, the ALJ: (1) agreed with the Sierra Club that the costs that I&M proposes to recover are unreasonable under Act 304 and in excess of the market price cap in the Michigan Code of Conduct (Code of Conduct), Mich Admin Code, R 460.10108 (Rule 8)[5]; (2) concluded that the Code of Conduct applies to the ICPA; (3) recommended that the Commission issue a Section 7 warning that I&M is unlikely to recover uneconomic costs associated with the ICPA without good faith efforts to renegotiate the ICPA; (4) declined to recommend that the Commission amend its PSCR plan by removing the cost of the ICPA from the maximum PSCR factor for the 2022 plan year; and (5) recommended that the Commission decline to issue a Section 7 warning with respect to the Rockport units.

a. Inter-Company Power Agreement

In describing the parties' positions regarding the ICPA issue, the ALJ recounted that the Sierra Club argued that the ICPA contract with OVEC has a substantially higher cost than the value of its products and services in comparison to equivalent capacity market prices in the PJM Interconnection, L.L.C. (PJM) market since 2017, and thus, is not reasonable and prudent for the

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[5] MCL 460.10ee(1) authorized the Commission to establish a code of conduct applicable to all utilities that includes measures to prevent cross-subsidization, preferential treatment, and unauthorized information sharing between a utility and a utility's affiliated entities.

2022 plan year or the forecasted 2022-2026 years. PFD, p. 8 (citing 3 Tr 263-264; Sierra Club's initial brief, pp. 13-14). The Sierra Club contended that from 2022-2026, the ICPA is expected to cost I&M $83.7 million, or $20.1 million annually, in present value terms more than the market value of its services. 3 Tr 310; Sierra Club's initial brief, p. 14. According to the Sierra Club, I&M has known about the uneconomic nature of the ICPA since 2016 when AES Services Corporation conducted an analysis of the contract. 3 Tr 267; Sierra Club's initial brief, pp. 15-16. The Sierra Club pointed to evaluations performed for the Ohio Public Utilities Commission by Duke Energy Ohio, Inc. (Duke Energy), a credit rating assessment by Moody's Analytics, and benchmark comparisons with other long-term supply agreements to show that the ICPA cost is excessive. 3 Tr 261, 266-267, 275; Sierra Club's initial brief, pp. 16-19.

The Sierra Club also refuted I&M's comparisons of the ICPA to two power purchase agreements (PPAs) held by Consumers Energy Company (Consumers) and the transfer price construct under Public Act 295 of 2008, MCL 460.1047(2)(b)(iv). Sierra Club's initial brief, pp. 20-24. The Sierra Club also described I&M's management of the ICPA as unreasonable in that the company has not taken steps to minimize the losses and harm to customers associated with the operation as must run units and environmental compliance investment decisions for the OVEC units. Sierra Club's initial brief, pp. 24-28. The Sierra Club ultimately asked that the Commission issue a Section 7 warning that the Commission will likely disallow I&M's recovery of the Michigan jurisdictional share of compensation for the ICPA in 2022-2026. Sierra Club's initial brief, pp. 28-29.

The Staff's position is that I&M's PSCR plan and forecast are reasonable and should be approved, finding in its review that the plan utilizes existing resources and reasonable projections to arrive at its PSCR factors, and is consistent with past Commission approvals. 3 Tr 375; Staff's initial brief, pp. 1-5. The Staff specified that I&M complied with the Commission's directive for the company to show that the ICPA, as an affiliate contract, is compliant with the pricing provisions of Rule 8. Staff's initial brief, pp. 3-4. Turning to costs, the Staff asserted that OVEC's cost of capacity of $182,393.44 per megawatt (MW)-year was significantly less than I&M's embedded cost of capacity for Michigan customers of $264,317 per MW-year, and further, that with the exception of 2020, OVEC has been profitable on an energy-only basis. 3 Tr 382; Staff's initial brief, pp. 3-4. However, the Staff qualified its position by stating that its recommended approval for the 2022 PSCR plan year is not a long-term recommendation and that the reasonableness of the ICPA would be evaluated again in the 2023 PSCR plan case. 3 Tr 383; Staff's initial brief, p. 5. The Staff contended that, while it agrees with some of the Sierra Club's claims, none of those arguments warrant a disallowance. Staff's initial brief, pp. 5-6.

In his analysis, the ALJ recounted I&M's 2018 PSCR plan case (Case No. U-18404), 2019 PSCR reconciliation case (Case No. U-20223), 2020 PSCR plan case (Case No. U-20529), and 2020 PSCR reconciliation case (Case No. U-20530) where the Commission reiterated that I&M must demonstrate that its wholesale purchases from affiliates are just and reasonable under current market conditions and that the company is taking steps to minimize costs. Further, because the Commission has a duty to continuously evaluate the costs of the ICPA in comparison to other long-term supply options, the ALJ stated that additional scrutiny of I&M's Code of Conduct compliance pertaining to the ICPA was appropriate. The ALJ also noted that the Commission was concerned with the economics of the OVEC units and that I&M must meet the standards of Act 304 as well as the Code of Conduct for its affiliate contracts. PFD, pp. 13-15 (citing and quoting the June 7, 2019 order in Case No. U-18404 (June 7 order), pp. 7-8; May 13, 2021 order in Case No. U-20529 (May 13 order), pp. 13-15, 17-19; the June 23, 2021 order in Case

No. U-20224 (June 23 order), p. 12; the February 2, 2023 order in Case No. U-20530 (February 2 order), pp. 12-13, 18).

The ALJ stated his agreement with the Sierra Club's estimates that I&M would lose $83.7 million in energy market revenue and capacity value over the 2022 plan year and the five-year forecast period (2022-2026) by purchasing energy from OVEC under the ICPA and that recovery of the ICPA costs above market prices is unreasonable. The ALJ recited the Sierra Club's support for its arguments that the ICPA is uneconomical as well as the Staff's argument that the ICPA costs are reasonable when comparing the ICPA cost of capacity to I&M's embedded cost of capacity and that OVEC has been profitable on an energy-only basis. PFD, pp. 15-17. The ALJ agreed with the Sierra Club that comparing OVEC's capacity cost to I&M's embedded capacity costs is not an apt comparison because "the Commission asked for a comparison of OVEC costs to other long-term supply benchmarks, and as I&M's embedded cost of capacity includes OVEC and thus is not a comparison of OVEC to something else." *Id.*, p. 18.

The ALJ next addressed I&M's assertion that the Sierra Club's analysis of the company's capacity costs is invalid because it was based on ICPA capacity at reliability pricing model (RPM) auction capacity prices when I&M is a Fixed Resource Requirement (FRR) that does not participate in RPM auctions. The ALJ noted that in I&M's 2019 PSCR reconciliation case, Case No. U-20224, the Commission, while unpersuaded that comparisons of the ICPA with short-term PJM capacity market prices warranted a disallowance, found that evidence in that case suggested that the ICPA costs would exceed revenues for the foreseeable future. PFD, pp. 18-19 (citing June 23 order, pp. 7, 12 and May 13 order, p. 18).

Regarding I&M's assertion that the Sierra Club omitted from its benchmark analysis two PPAs with Michigan Limited Power Partnership (MLPP) and with North American Natural

Resources, Inc., that I&M used in its analysis, the ALJ points out that I&M used these PPAs to reference how PPAs were priced and that the MLPP is priced lower than the ICPA. PFD, pp. 19-20. The ALJ further rejected I&M's argument that the OVEC Merchant Analysis, the Duke Energy analysis, the FirstEnergy Solutions Corp. (FirstEnergy) analysis, and Moody's Analytics assessment should be disregarded stating that I&M did not object to the admission of these analyses into evidence and that the Commission relied on these analyses in the November 18, 2021 order in Case No. U-20804 (November 18 order) where it issued a Section 7 warning for the ICPA costs. PFD, pp. 20-21 (citing November 18 order, p. 20).

As to Sierra Club's arguments regarding discrepancies between I&M's net present value (NPV) analysis that it presented in its integrated resource plan (IRP) case and the NPV data presented in the instant case, the ALJ agreed with I&M that the NPV analysis is not part of the evidentiary record in this case. The ALJ also noted that the Commission stated in the order approving the settlement agreement in I&M's IRP case, Case No. U-21189, that the settlement agreement did not include a cost approval of the ICPA because such costs would be reviewed in the company's PSCR plan and reconciliation proceedings. PFD, p. 21 (citing the February 2, 2023 order in Case No. U-21189, p. 101).

Turning to the market comparisons with the ICPA, the ALJ concluded that:

> while all the comparisons offered by Sierra Club may not be comparable to the OVEC ICPA in every respect for some of the reasons offered by I&M, these nevertheless provide general benchmarks showing that there are other, lower cost options of long-term supply that are less expensive than the ICPA. Moreover, the Commission recently recognized this point as well. This PFD finds the comparison of the ICPA to the Consumers-MCV [Midland Cogeneration Venture Limited Partnership] PPA particularly relevant given the Commission's most recent statement that comparisons with past power transactions "are the fairest benchmark" for calculating a disallowance.

PFD, p. 22 (quoting the February 2 order, p. 11) (footnote omitted).

The Sierra Club argued that I&M has the authority under the ICPA to control some operational and management decisions at OVEC and that I&M failed to show any effort to reduce costs through its ownership stake at OVEC. The ALJ disagreed, clarifying that I&M does not have an ownership interest in OVEC but is, rather, a sponsoring company without authority to exercise control over the operational and management decisions at OVEC. PFD, pp. 22-23. However, the ALJ raised I&M's obligation to examine existing contracts as market conditions change over time and to pursue amendments or contract renegotiations accordingly. The ALJ appeared to agree with the Sierra Club's contention that I&M has not shown an attempt to renegotiate the ICPA and pointed to I&M's testimony that the company is "evaluating options related to OVEC" and that "potential action under consideration with regard to renegotiation is being evaluated." *Id*., p. 24 (quoting 3 Tr 137).

In summary, the ALJ agreed with the Sierra Club that the ICPA costs that I&M seeks to recover are unreasonable under Act 304 and in excess of the market price cap in the Code of Conduct and recommended that the Commission issue a Section 7 warning for all uneconomic costs without I&M's good faith effort to manage the ICPA and renegotiate the contract. PFD, pp. 15, 33-34.

In its exceptions, I&M states that the ALJ adopted the Sierra Club's economic analyses and accepted the comparisons of the ICPA, as a long-term contract, to market prices in the third-party analyses by Duke Energy, FirstEnergy, and Moody Analytics to support his finding that the ICPA costs are unreasonable. I&M argues that these analyses and comparisons ignore the economic benefits of the ICPA, that the comparisons of long-term contracts to short-term market prices is inappropriate, and that the ALJ's findings are proven untenable by his lack of recommendation to amend the company's PSCR plan. I&M's exceptions, pp. 17-21. I&M asks the Commission to approve the company's proposed PSCR plan and factors for the 2022 plan year without a Section 7 warning and to disregard "the inappropriate market comparison theories used by the [ALJ] and the Sierra Club[.]" *Id*., pp. 20-21.

The Sierra Club, in its replies to exceptions, argues that I&M omits relevant history of the ICPA such as the 2004 amendment to the ICPA changing the calculation of energy and demand charges and the termination of the U.S. Department of Energy contract with OVEC that left costs and benefits exclusively with OVEC sponsors. Sierra Club's replies to exceptions, p. 7. The Sierra Club further argues that I&M's statement that the ICPA benefits Michigan customers is misleading because affiliate transaction requirements have been applicable since 2000 and the claims of benefits are unsupported on the record. *Id*., pp. 7-8.

Addressing I&M's issue with the ALJ's factual findings regarding the costs of the ICPA, the Sierra Club argues that I&M's statement that the ICPA results in a net benefit on an energy-only basis is irrelevant and ignores that the total costs of energy and capacity must be considered and that the energy and capacity costs of the ICPA have been and likely will be excessive. Further, the Sierra Club states that the Commission found appropriate comparisons of OVEC charges to I&M's Rockport unit 2 purchases and net cost of new entry (CONE) in PJM for capacity purposes and the allowance of such comparisons for capacity negates I&M's claims that the Commission should only consider net energy costs. Sierra Club's replies to exceptions, pp. 32-33. Next, the Sierra Club states that I&M challenged the Sierra Club's analysis as being predicated upon I&M purchasing capacity from the PJM capacity auction. The Sierra Club avers that I&M's challenge is unclear in the point it is trying to make and that the ALJ relied on price benchmarks that did not rely on PJM capacity market costs and instead involve long-term contracts like Consumers' PPA with MCV. *Id*., p. 33. As to the third-party analyses, the Sierra Club points out that I&M failed to object to the admission of these analyses into evidence. Lastly, in response to I&M's complaints regarding comparisons of present-day market proxies to judge the reasonableness of a long-term contract, the Sierra Club states that the date the company entered into the ICPA with an affiliate is not dispositive and that I&M must face the consequences of its decisions. *Id.*, p. 34.

The Staff, in its replies to exceptions, contends that the comparison on the record in this case between the short-term PJM capacity market and the ICPA is premature and that there is no justification for a disallowance of the ICPA costs from the 2022 PSCR plan and a reduction to the PSCR factor. The Staff asserts that the Commission has applied this rationale in previous PSCR plan cases and that it is appropriate to do so again in this case but notes that the ICPA costs can be evaluated in the future. The Staff maintains that:

> the Company has met its burden to show that the projected PSCR plan costs appear reasonable for purposes of the instant plan case and determination of a PSCR factor. No evidence has shown that I&M is in violation of the code of conduct at this time, but final determinations on this issue can and will be made in the 2022 PSCR reconciliation case.

Staff's replies to exceptions, p. 5.

b. Code of Conduct

The ALJ explained that I&M made several arguments contending that the Code of Conduct does not apply to the ICPA in this case. The ALJ rejected these arguments as unsupported in law and fact and noted that the Commission has repeatedly found that I&M and OVEC are affiliates under Rule 8 and that pricing provisions in the Code of Conduct apply to the ICPA. PFD, p. 24 (citing May 13 order, pp. 16-17; June 23 order, p. 11; February 2 order, pp. 18-19).

Addressing I&M's argument that applying the Code of Conduct's price cap supplants the legislative PSCR framework of Act 304, the ALJ countered that the Code of Conduct is itself implemented pursuant to a legislative mandate and, thus, is aligned with legislative intent. PFD, p. 25. The ALJ did not find any conflict between the Code of Conduct and Act 304 and explained that the Code of Conduct "simply provides additional, stricter rules for a specific subset of transactions, i.e. affiliate transactions" requiring I&M to meet Act 304 standards for all of its PSCR costs and Code of Conduct requirements for its PSCR costs incurred with affiliates. PFD, p. 26.

The ALJ further explained, in response to I&M's assertion that the Code of Conduct is arbitrary and capricious, that the Code of Conduct's limitations on compensation for affiliate contracts is rationally related to the legislative intent of preventing discrimination in favor of or against affiliates. *Id*. Rejecting I&M's argument that the Code of Conduct is an unlawful designation of legislative authority, the ALJ concluded that: (1) the Code of Conduct can be read in harmony with Act 304; (2) the Legislature provided a goal and a standard in MCL 460.10ee(1) for the Commission to follow in the Code of Conduct including measures, such as the price cap, that achieve that goal; and (3) the Code of Conduct has survived previous legal challenges. *Id*., pp. 27-28.

Addressing I&M's argument that the Code of Conduct cannot be applied retroactively, the ALJ noted that the Commission already applies the Code of Conduct prospectively. I&M also argued that a disallowance pursuant to the Code of Conduct would violate the contract clauses in the Michigan and U.S. Constitutions, to which the ALJ applied a three-prong test to determine whether the law violates the state or federal constitutions: (1) whether the state law has in fact operated as a substantial impairment of a contractual relationship, (2) whether the law has a legitimate public purpose, and (3) whether the means adopted to implement the law are reasonably related to the public purpose. Finding that the Code of Conduct passed all three prongs, the ALJ reasoned as follows:

> First, any disallowance from rate recovery does not impair[—]let alone substantially impair[—]the ICPA because I&M's rights and obligations under the

> ICPA remain the same; the only change would be the amount of money related to the ICPA that I&M can recover through the PSCR process. Second, even if there were a substantial impairment, the Code of Conduct serves a legitimate public purpose because it prevents preferential treatment among utilities and their affiliates. Third, the Code of Conduct's price cap is reasonably related to the proffered public purpose because it effectively prevents a utility from collecting excessive amounts under an affiliate contract. Accordingly, any potential disallowance under the Code of Conduct does not violate the Contracts Clause.

PFD, p. 29 (footnotes omitted).

The ALJ further pointed out that, with respect to the Takings Clause, I&M took an impermissible piecemeal approach by focusing only on a disallowance related to the ICPA rather than the overall PSCR plan or factors. *Id*., p. 30. I&M then relied on the August 28, 2018 order in Case No. U-18361 (a proceeding to promulgate rules establishing a code of conduct under MCL 460.10ee(1)) to suggest that the Code of Conduct does not apply to wholesale service agreements. However, the ALJ stated that the Commission has previously addressed and rejected this argument. The ALJ recounted that the Commission distinguished the circumstances in Case No. U-18361 from the ICPA in that the ICPA is used to serve retail customers and the Commission maintains authority to assess the reasonableness and prudence of purchasing decisions by I&M from OVEC, an affiliate. PFD, pp. 30-31 (citing the November 18 order, p. 16).

The ALJ concluded that, "[a]s an affiliate contract, the Code of Conduct applies to the ICPA, and the ICPA costs exceed the market price cap in Rule 8(4) of the Code of Conduct." PFD, p. 31.

In its exceptions, I&M contends that the ALJ erred in finding the Code of Conduct applied to the ICPA. I&M's exceptions, p. 6. I&M avers that the ALJ unlawfully conflated the reasonableness standard under Act 304 with the price caps in the Code of Conduct and that rather than the statutes being read in harmony, as posited by the ALJ, I&M argues that the ALJ's application of the Code of Conduct renders Act 304 meaningless. According to I&M, the Code of Conduct's price cap predetermines the reasonableness and prudence standard of Act 304 setting the two standards in conflict with each other. I&M further argues that applying the Code of Conduct is arbitrary and capricious in that comparisons of market prices to long-term contracts ignore the benefits that long-term contracts provide over the life of the contract. I&M's exceptions, pp. 6-10.

I&M also argues that the ALJ's application of the Code of Conduct constitutes an unlawful retroactive application because the ICPA was entered into decades before the Code of Conduct was enacted and the company draws comparisons between a Court of Appeals decision barring retroactive application of price caps to insurance contracts under the Michigan No-Fault Act. I&M's exceptions, pp. 10-12 (citing *Andary v USAA Cas Ins Co*, ___ Mich App ____; __NW2d___; 2022 Mich App LEXIS 5127, slip op at 7 (2022) (Docket No. 356487)). I&M further argues that applying the Code of Conduct violates the Contract Clause of the Michigan Constitution and the Takings Clause of the U.S. Constitution and that a disallowance of ICPA costs pursuant to the Code of Conduct is unlawful since the ICPA is a wholesale service regulated by the Federal Energy Regulatory Commission (FERC). I&M's exceptions, pp. 13-17.

In its replies to exceptions, the Sierra Club states that I&M makes inaccurate claims about the Code of Conduct's history to support the company's argument that the ALJ applied the Code of Conduct retroactively. Contrary to I&M's claims in exceptions, the Sierra Club contends that the 2000 and 2018 versions of the Code of Conduct apply to regulated and unregulated services of affiliates and that the market price cap remained the same in both versions of the Code of Conduct. Sierra Club's replies to exceptions, pp. 2-5. The Sierra Club also points out that, while the original ICPA predates the Code of Conduct, I&M has since amended the ICPA in 2004 and 2011, and argues that the Code of Conduct "embodies longstanding and well-founded law regarding the potential for abuses and unfairness in transactions between utilities and their affiliates[.]" *Id*., p. 6.

The Sierra Club also disputes I&M's arguments that the Code of Conduct does not apply to the ICPA. First, the Sierra Club points out that the Code of Conduct price cap was in effect in 2004 when I&M amended the ICPA and that the Commission has never made a finding that the ICPA is reasonable and prudent, but instead, merely approved recovery costs under the ICPA. *Id*., pp. 8-9. Second, the Sierra Club agrees with the ALJ that no conflict exists between the Code of Conduct and Act 304, that the Commission has repeatedly held that the Code of Conduct applies in PSCR cases, and that Michigan courts have rejected I&M's argument that the Code of Conduct exceeds the scope of legislative intent. *Id*., pp. 9-11. Turning to I&M's claims of retroactive application of the Code of Conduct, the Sierra Club contends that: (1) the Commission has held that its decisions in PSCR cases are prospective; (2) I&M is wrong that the Code of Conduct's limits on affiliate transactions did not exist when I&M executed the current ICPA; (3) the Commission previously informed I&M of its Code of Conduct obligations going forward in orders in Case Nos. U-20529 and U-20804, which I&M did not appeal; and (4) I&M's reliance on *Andary v USAA Cas Ins Co* is an improper comparison because the Code of Conduct is not being applied retroactively, the Code of Conduct is a different legal standard as a creature of statute imposing an obligation on highly regulated utilities to minimize the cost of power, and regulated utility proceedings are distinguishable from the facts in *Andary v USAA Cas Ins Co*. Sierra Club's replies to exceptions, pp. 11-19.

Addressing I&M's claims of violations of the Contract Clause of the Michigan constitution, the Sierra Club reasons that the Contract Clause is not implicated in this case because, first, a disallowance does not impact the ICPA itself. The Sierra Club explains that all rights and obligations under the ICPA remain intact but that I&M is not entitled by law or contract to recover from ratepayers costs that are in excess of market price. Second, the Contract Clause prohibits a state law from interfering with contractual rights if the impairment is substantial and the state law does not serve a legitimate public interest. Per the Sierra Club, the Commission is statutorily authorized to regulate I&M and its cost recovery to serve the public interest, and I&M's contractual rights are unimpaired by the Code of Conduct. Sierra Club's replies to exceptions, pp. 19-23. The Sierra Club also disputes I&M's claimed violations of the Takings Clause arguing that I&M's argument runs afoul of U.S. Supreme Court precedent holding that if the overall impact of the rate order is not confiscatory, a takings claim will fail. *Id.*, pp. 23-24 (citing *Duquesne Light Co v Barasch*, 488 US 299, 307; 109 S Ct 609; 102 L Ed 2d 646 (1989)). The Sierra Club points out that: (1) I&M fails to argue that the overall PSCR plan or factors are confiscatory, (2) the company does not acknowledge its own risk that the Commission may disallow costs associated with the ICPA, (3) past cost recovery does not create a right to ongoing recovery, (4) I&M's statements regarding its financial health are unsupported, and (5) I&M's claim that a disallowance would impair the company's ability to use the ICPA is wrong. *Id.*, pp. 24-27. Thus, per the Sierra Club, "I&M's piecemeal application of the Takings Clause, coupled with such an emphasis on vague economic impact and unreasonable expectations, do not establish a Takings violation[.]" *Id.*, p. 27.

In response to I&M's argument that a disallowance interferes with FERC's jurisdiction over wholesale rates or violates the filed-rate doctrine, the Sierra Club explains that the Commission has addressed and rejected this argument on three occasions pointing to I&M's 2020 PSCR plan case in Case No. U-20529, 2019 PSCR reconciliation case in Case No. U-20224, and 2021 PSCR plan case in Case No. U-20804. Sierra Club's replies to exceptions, pp. 27-28. Further, the Sierra Club contends that the Commission has exclusive jurisdiction over retail rates and can address the reasonableness of the costs of FERC-approved rates on retail customers' rates as the Commission has demonstrated by finding in two of I&M's PSCR proceedings. *Id*., pp. 28-31 (citing *Ky W Va Gas Co v Pa Pub Utility Comm*, 837 F2d 600, 609 (CA 3, 1988); May 13 order, p. 21; and June 23 order). Noting that I&M cited to an order in Case No. U-18361 to argue that the Code of Conduct does not apply to federally regulated wholesale services, the Sierra Club clarifies:

> I&M is wrong. The order cited by I&M clarified in response to a comment from a power supply cooperative that the Code of Conduct does not apply to "federally regulated wholesale services." Thus, the Order cited by I&M relates to the types of entities subject to the Code of Conduct, and not the types of contracts subject to the Code of Conduct. It is uncontested [in the instant proceeding] that I&M is an electric utility regulated by the Commission and subject to the Code of Conduct under the first clause in the definition of "utility."

Sierra Club's replies to exceptions, p. 31.

In its replies to exceptions, the Staff clarifies that while it agrees with I&M that a Section 7 warning and a finding that the company violated the Code of Conduct with the ICPA are not warranted, the Staff reached these conclusions based on different reasoning from I&M. Specifically, the Staff does not agree with I&M that the Code of Conduct does not apply to the ICPA. The Staff explains that I&M has previously made this argument and that the Commission "has for numerous years held that the Code of Conduct does apply to the ICPA." Staff's replies to exceptions, p. 2. The Staff then points to the June 23 order where the Commission recited the history on I&M's Code of Conduct issue and cited the May 13 order that clearly stated that the Code of Conduct applies to the OVEC ICPA. Staff's replies to exceptions, pp. 2-3. Pointing to the ALJ's citation to several Commission orders on page 24 of the PFD that contained findings by the Commission that the Code of Conduct applies to the ICPA, the Staff describes the issue as settled. Staff's replies to exceptions, p. 4.

c. Rockport

The ALJ recounted that the Sierra Club's analysis in Case No. U-20530 (I&M's most recent PSCR reconciliation proceeding) suggested that the company does not economically commit

Rockport units 1 and 2 and that the two units are projected to incur $483 million in excess costs relative to the market value of energy and capacity based on unit cost data over the next five years. PFD, pp. 31-32 (citing 3 Tr 289). I&M countered that the Sierra Club did not account for the company's operational decisions and that reliance on I&M's operations during the COVID-19 pandemic is unreasonable. I&M argued that for its generational forecast, it uses a model that commits units in PJM based on variable energy costs and that does not dispatch the Rockport units uneconomically. The company further stated that it has an obligation to run units in its customers' best interests and that a PSCR reconciliation proceeding is the best forum to address the reasonableness and prudence of unit commitments. The Staff agreed with I&M that a Section 7 warning was not necessary for the Rockport units and that a reconciliation proceeding was the appropriate proceeding to evaluate operational decisions. PFD, pp. 32-33.

The ALJ agreed with I&M and the Staff and did not find a Section 7 warning for the costs associated with the Rockport units to be warranted. The ALJ also noted that:

> the Commission previously directed I&M to document the reasons for its decision to designate a generating unit as "must run" when such a decision would cause the marginal cost of operating the unit to exceed the revenue generated from its operation. As such, this [ALJ] does not find it appropriate to assume before the fact that I&M will necessarily make imprudent commitment decisions going forward contrary to the forecasted economical dispatch from the Rockport units.

Id., p. 32 (footnote omitted).

In exceptions, I&M does not dispute the ALJ's recommendation regarding Rockport but asks that the Commission reject the ALJ's commentary regarding the application of the Code of Conduct to the Rockport unit power agreement. I&M's exceptions, p. 4. The Staff and the Sierra Club do not address the Rockport issue in their respective replies to exceptions.

Discussion

A PSCR proceeding concerns the recovery of a utility's power supply costs on an annual basis. A PSCR clause is:

> a clause in the electric rates or rate schedule of an electric utility that permits the monthly adjustment of rates for power supply to allow the utility to recover the booked costs . . . of fuel burned by the utility for electric generation and the booked costs of purchased and net interchanged power transactions by the utility incurred under reasonable and prudent policies and practices.

MCL 460.6j(1)(b). A PSCR factor is "that element of the rates to be charged for electric service to reflect power supply costs incurred by an electric utility and made pursuant to a power supply cost recovery clause incorporated into the rates or rate schedule of an electric utility." MCL 460.6j(1)(c). Subsection 6j(3) of Act 304 requires a utility with a PSCR clause to annually file a PSCR plan describing the expected sources of electric power supply and changes in the cost of power supply anticipated over the 12-month period following the filing of the plan. The PSCR plan must also describe all major contracts and power supply agreements for the 12-month period.

A utility must contemporaneously file "a 5-year forecast of the power supply requirements of its customers, its anticipated sources of supply, and projections of power supply costs, in light of its existing sources of electrical generation and sources of electrical generation under construction." MCL 460.6j(4). Subsection 6j(5) of Act 304 provides that, after a utility files its PSCR plan and five-year forecast, the Commission shall conduct a proceeding to evaluate the reasonableness and prudence of the PSCR plan and to establish PSCR factors for the period covered by the plan. In its final order in a PSCR plan case, the Commission must "evaluate the reasonableness and prudence of the decisions underlying the [PSCR] plan" and must "approve, disapprove, or amend the plan accordingly." MCL 460.6j(6).

In evaluating the decisions underlying the PSCR plan, Subsection 6j(6) of Act 304 states that "the commission shall consider the cost and availability of the electrical generation available to the utility; the cost of short-term firm purchases available to the utility; the availability of interruptible service; . . . whether the utility has taken all appropriate actions to minimize the cost of fuel; and other relevant factors." This subsection also requires the Commission to approve, reject, or amend the 12 monthly PSCR factors requested by the utility in its PSCR plan. The finalized PSCR factors shall not reflect items the Commission could reasonably anticipate would be disallowed in a PSCR reconciliation proceeding. MCL 460.6j(6). In its final order, the Commission shall also evaluate the decisions underlying the five-year forecast filed by a utility and may indicate any cost items in the five-year forecast that the Commission would be unlikely to permit the utility to recover from its customers in rates, rate schedules, or PSCR factors established in the future. MCL 460.6j(7). This is known as a Section 7 warning.

Finding the ALJ's recommendation regarding the non-contested issues in this matter to be well-reasoned and based on substantial evidence on the record and noting that no party filed exceptions to the issues listed as uncontested by the ALJ on page 5 of the PFD, the Commission adopts the ALJ's recommendation and accepts those undisputed elements into I&M's 2022 PSCR plan and factor. The Commission now addresses each of the contested issues identified by the ALJ.

a. Inter-Company Power Agreement

The Commission has reviewed the record in this matter and finds the ALJ's findings and conclusions to be well-reasoned and consistent with substantial evidence on the whole record. *See*, PFD, pp. 15-24. The Commission agrees that a Section 7 warning is appropriate for uneconomic power supply costs associated with the ICPA without good faith efforts by I&M to minimize costs or to renegotiate the contract to achieve positive value for its ratepayers.

The issue of the economics of the ICPA has been repeatedly raised in I&M's PSCR plan and reconciliation proceedings and the Commission has expressed its concerns multiple times that the cost of the ICPA exceeds its value to customers. *See*, *e.g.*, May 13, pp. 13-15, 18-19; June 23 order, p. 12; and February 2 order, pp. 12-13. In the November 18 order, citing the third-party analyses that showed the projected losses for the ICPA relative to market alternatives, the Commission found a Section 7 warning was warranted. November 18 order, p. 20. The independent analyses admitted into evidence in this case (the admission of which I&M failed to object to) again show the ICPA to be uneconomic. *See*, 3 Tr 266-267; Exhibits SC-16 and SC-17.

Additionally, Sierra Club presented multiple long-term supply alternatives with which to compare the cost of the ICPA, and the Commission agrees with the ALJ that these comparisons sufficiently demonstrate that the ICPA costs are excessive. While all of the benchmarks may not be perfect apples-to-apples comparisons, as it is difficult to produce comparisons that are identical to the OVEC units, the Commission finds it reasonable to judge the costs of the ICPA based on long-term alternatives such as the Consumers-MCV PPA costs of $56.65 per megawatt-hour (MWh). *See*, 3 Tr 275. Further, although I&M disputed the Sierra Club's $65.41 per MWh cost for the ICPA, I&M's own calculation of $63.91 per MWh was still the highest figure among the benchmarks provided on the record by the Sierra Club. *See*, 3 Tr 156.

The Commission notes its previous directives to I&M to uphold its obligation to assess its existing contracts as market conditions or other factors change over time and to pursue amendments or new contractual agreements that may include taking meaningful steps to renegotiate provisions of the ICPA. May 13 order, p. 15 (quoting December 9, 2020 order in Case No. U-20203, p. 26). Despite evidence in this case and previous cases that the ICPA costs continue to exceed the ICPA's value, by I&M's own admission, the company is "evaluating options related to OVEC" and "potential action [is] under consideration with regard to renegotiation[.]" 3 Tr 137. Finding that potential action does not equate to meaningful steps to take action to minimize costs, the Commission agrees with the ALJ that, absent meaningful steps to renegotiate the contract, a Section 7 warning is appropriate in this case.

Therefore, the Commission adopts the ALJ's recommendation and issues a Section 7 warning that the Commission may not authorize I&M's future recovery of the ICPA costs in excess of market value without good faith efforts at renegotiation.

b. Code of Conduct

The Code of Conduct reads, in relevant parts, that "[a] utility shall not discriminate in favor of or against any person, including its affiliates[,]" and that:

> If an affiliate or other entity within the corporate structure provides services or products to a utility, and the cost of the service or product is not governed by section 10ee(8) of 2016 PA 341, MCL 460.10ee(8), compensation is at the lower of market price or 10% over fully allocated embedded cost.

Rule 8(1) and (4), respectively.

I&M makes similar arguments in this case as in previous proceedings that the Code of Conduct does not apply to the ICPA and that the Code of Conduct cannot be read in harmony with Act 304. As it has done before, the Commission rejects these arguments. Finding this issue to be well-settled, the Commission will not rehash its legal analysis explaining the application of the Code of Conduct. Rather, the Commission incorporates by reference the discussions in its previous orders,[6] and, finding the ALJ's analysis in the instant proceeding at pages 24-31 of the PFD to be well-reasoned and aligned with the Commission's previous decisions on this issue, adopts the PFD.

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[6] May 13 order, pp. 15-21; June 23 order, pp. 7-13; and November 18 order, pp. 13-17.

I&M does not assert that facts or circumstances have changed with respect to the company's relationship with OVEC or the nature of the ICPA such that the Code of Conduct and its affiliate pricing provisions would no longer be applicable. Therefore, the Commission finds that the Code of Conduct applies to the ICPA as an affiliate contract and that the Code of Conduct does not interfere with the requirements under Act 304. As such, the ICPA is an affiliate contract and is subject to the market price cap set out in Rule 8(4) of the Code of Conduct.

Under Rule 8(4), if an affiliate provides services or products to a utility, compensation is limited to the lower of the market price or 10% over fully allocated embedded cost. Thus, the Commission finds that an appropriate proxy must be used to calculate a potential disallowance and I&M's compensation. In the November 18 order, the Commission noted that, among other comparisons, the Rockport sale capacity value and net CONE may be appropriate proxies and added that "[t]here may also be legitimacy in valuing the attributes of price stability, supply certainty, and resilience afforded by a utility's Fixed Resource Requirement (FRR) alternatives to the PJM capacity market." November 18 order, p. 22. In that case, the Commission deferred a determination on an appropriate proxy to I&M's IRP (Case No. U-21189) and PSCR reconciliation proceeding (Case No. U-20805) where additional evidence on the issue would be available. *Id*. The Commission notes that I&M's IRP was resolved by a settlement agreement that did not include a proxy and Case No. U-20805 is currently pending before the Commission; therefore, an appropriate proxy has not been determined in either of those cases.

In the February 2 order addressing I&M's 2020 PSCR reconciliation, the Commission stated that cost comparisons to prior power transaction costs are the fairest benchmarks for calculating disallowances of PSCR costs. In that case, the Commission adopted the ALJ's disallowance of ICPA costs based on the difference between the ICPA costs and the "average ($52.02 per MWh) of the MPPA [Michigan Public Power Agency]-DTE [Energy Company] Belle River transaction cost ($55.16 per MWh) and the Consumers-MCV transaction cost ($48.49)[.]" February 2 order, p. 8 (quoting the PFD in Case No. U-20530, p. 62). This amount was then multiplied by I&M's 721,476 MWh of electricity billed in 2020, reduced for Michigan's 13.9% share of the costs. February 2 order, p. 8 (citing the PFD in Case No. U-20530, p. 62). In the instant case, the ALJ found that the comparison of the ICPA to Consumers-MCV PPA was "particularly relevant" given the Commission's comments in the February 2 order regarding past power transactions being fair benchmarks.

The Commission agrees with the ALJ that the Consumers-MCV PPA may represent an appropriate proxy. However, the Commission finds that the corresponding PSCR reconciliation to this proceeding will be the appropriate venue based on the evidence in that case to determine the correct proxy to calculate a potential disallowance. The Commission will consider evidence from the parties in that case as to the appropriate benchmark comparison for determining the affiliate price cap, whether that be the Consumers-MCV PPA, the Rockport capacity value, CONE, or another viable option supported by substantial evidence on the record.

c. Rockport

The Commission finds the ALJ's findings and conclusions with respect to the Rockport units to be well-reasoned and based on substantial evidence on the record. In the June 23 order, the Commission directed I&M to document the basis for its Rockport commitment decisions when the company's forecasts suggest that those decisions to designate a unit as must-run will result in marginal operational costs that exceed the revenue from supplying that power to PJM. June 23 order, pp. 15-16. In this case, I&M testified that it complied with the Commission's directives and began documenting its self-commitment decision in May 2021, prior to the Commission's June 23 order. I&M noted that it also addressed its Rockport commitment decisions in Case Nos. U-20224 (I&M's 2019 PSCR reconciliation case), U-20530 (I&M's 2020 PSCR reconciliation case), and U-20805 (I&M's 2021 PSCR reconciliation case). 3 Tr 162-163.

The ALJ agreed with the Staff and the company that a warning regarding costs related to the Rockport units is not warranted in this case, reasoning that it is not "appropriate to assume before the fact that I&M will necessarily make imprudent commitment decisions going forward contrary to the forecasted economical dispatch from the Rockport units." PFD, p. 33. The ALJ explained that the company's associated reconciliation proceeding is the more appropriate venue for evaluating operational decisions and the Commission agrees. However, the Commission directs I&M to continue to document its commitment decisions for the Rockport units as this information is helpful in the Commission's evaluation of the reasonableness and prudence of must run commitment decisions.

THEREFORE, IT IS ORDERED that:

A. Indiana Michigan Power Company's application for a power supply cost recovery plan for planning year 2022 metered jurisdictional sales of electricity is approved, as set forth in this order.

B. Indiana Michigan Power Company's proposed power supply cost recovery factor of 6.23 mils per kilowatt-hour or $0.0063 per kilowatt-hour and five-year forecast are accepted.

C. The Commission issues a warning under MCL 460.6j(7) and the Commission's Code of Conduct, Mich Admin Code, R 460.10101 *et seq*., that Indiana Michigan Power Company may not be able to recover its full costs under the Ohio Valley Electric Corporation's Inter-Company Power Agreement without evidence demonstrating good faith efforts by Indiana Michigan Power Company to minimize the costs of the Inter-Company Power Agreement, which may include renegotiation of the contract.

D. Indiana Michigan Power Company shall document, and make available to the Commission Staff upon request, the basis for the company's decision to designate a generating unit as must run when the company's forecast demonstrates that the decision to do so will result in excess costs, as described in 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. To comply with the Michigan Rules of Court's requirement to notify the Commission of an appeal, appellants shall send required notices to both the Commission's Executive Secretary and to the Commission's Legal Counsel. Electronic notifications should be sent to the Executive Secretary at mpscedockets@michigan.gov and to the Michigan Department of Attorney General – Public Service Division at pungp1@michigan.gov. In lieu of electronic submissions, paper copies of such notifications may be sent to the Executive Secretary and the Attorney General – Public Service Division at 7109 W. Saginaw Hwy., Lansing, MI 48917.

MICHIGAN PUBLIC SERVICE COMMISSION

Daniel C. Scripps, Chair

Katherine L. Peretick, Commissioner

By its action of June 22, 2023.

Lisa Felice

Lisa Felice, Executive Secretary

P R O O F   O F   S E R V I C E

STATE OF MICHIGAN)

Case No. U-21052

County of Ingham)

Brianna Brown being duly sworn, deposes and says that on June 22, 2023 A.D. she electronically notified the attached list of this **Commission Order via e-mail transmission**, to the persons as shown on the attached service list (Listserv Distribution List).

Brianna J. Brown

Brianna Brown

Subscribed and sworn to before me
this 22nd day of June 2023.

Angela P. Sanderson

Angela P. Sanderson
Notary Public, Shiawassee County, Michigan
As acting in Eaton County
My Commission Expires: May 21, 2024

Service List for Case: **U-21052**

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