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DTE

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October 20, 2023

Ms. Lisa Felice
Executive Secretary
Michigan Public Service Commission
7109 West Saginaw Highway
Lansing, MI 48917

RE: In the matter, on the Commission's own motion, to open a docket to establish a workgroup to review and consider issues related to the creation of financial incentives and penalties involving outages and distribution performance.
MPSC Case No. U-21400

Dear Ms. Felice:

Attached for electronic filing in the above-captioned matter are the Reply Comments of DTE Electric Company in Response to the Commission's August 30, 2023, Order in Case No. U-21400.

Very truly yours,

Andrea E. Hayden

Digitally signed by Andrea E. Hayden
Date: 2023.10.20 13:39:12 -04'00'

Andrea E. Hayden

AEH/cdm
Attachment

Reply Comments of DTE Electric Company in Case No. U-21400
October 20, 2023

DTE Electric Company ("Company" or "DTE") appreciates the perspectives provided by the parties in their initial comments as well as those shared at the October 10, 2023 workgroup meeting. Both forums illustrated the key issues under discussion as the Commission, utilities, and stakeholders work towards an initial performance-based ratemaking (PBR) framework for Michigan. This document has two sections: The first section includes overarching comments, and the second sections offers brief feedback in response to the initial comments filed by parties in the docket on September 22, 2023. The absence of a direct response to any specific stakeholder comment does not constitute agreement with the comment on the part of the Company.

Section 1: Overarching Comments on the Application of PBR

Incentive design and structure should drive balance

Symmetric incentive design is appropriate. As highlighted by the Company's initial comments, symmetry is an important feature of incentive design. Symmetry helps ensure a balanced plan when considering all metrics in all forums. The Company is currently subject to penalty-only standards in the Service Quality and Reliability Standards (SQRS) and symmetry among the metrics being considered in this proceeding will begin to shift the full context back towards balance. The Commission recognized the role of symmetry in its 2018 report, which said "[w]ell designed PBR provides incentives and disincentives based on utility performance" and "[p]rudent PBR design…has recognized the need for a symmetric mix of incentives, both positive and negative…".[1]

Symmetric incentives are allowable under all circumstances. A question was raised at the workgroup discussion on October 10, 2023 as to whether the Service Quality and Reliability Standards precluded incentives under certain circumstances. The focus of these comments was R 460.741 ("Rule 41"), which says in part "(1)The commission may authorize an electric utility or cooperative to receive a financial incentive if it exceeds all of the service quality and reliability standards adopted by these rules". Commenters suggested that Rule 41 precludes the Commission from authorizing symmetric or upside PBR incentives unless all of the standard contained in the SQRS are met. The Company disagrees. Rule 41 allows the company to apply for an incentive if it has exceeded all of the service quality and reliability standards adopted within the rules and it authorizes the commission to approve that incentive. The rule does not prevent the Commission from authorizing a symmetric incentive program for a combination of performance metrics that may include some SQRS. The Company believes that to the extent the Commission believes Rule 41 precludes symmetric or upside incentives, the Commission can waive the rule in whole or in part consistent with its statutory authority. A temporary waiver would be appropriate if the Commission sees the rule as an impediment to the implementation of a robust and fair PBR mechanism.

[1] Commission Report on the Study of Performance-Based Regulation, April 20, 2018

Maximum incentive/penalty must consider SQRS credits. The maximum incentive/penalty in a PBR implementation should be meaningful without being excessive. It should also consider any existing incentives/penalties currently available or applied to the Company for related performance. In the context of reliability, the Company is already subject to SQRS credits, and estimates that ~$9M will be paid to customers in 2023. Any maximum penalty considered in this proceeding is in addition to the credits, and even assuming symmetrical design PBR, will yield substantial net financial risk to the Company.

Benchmarking can help inform PBR in Michigan

Early PBR implementations suggest opportunities for both penalties and incentives. A review of three states indicates that overall PBR should have balance, including both downside risk and upside opportunity for utilities. While each has downside reliability metrics (as does Michigan today as part of the SQRS), those metrics exist within a broader context in all cases.

- *Hawaii*. Hawaii has a far more extensive PBR framework and implementation than what is being considered in Michigan. Among the suite of PBR elements, Hawaii offers upside opportunities to reward its utilities for exceptional performance in certain areas (e.g. AMI utilization, interconnection timelines). At the time of the 2021 Order in the Hawaii PBR docket, Hawaii PUC Commissioner Jennie Potter noted "Hawaiian Electric has the opportunity to financially benefit from taking on some challenging areas and delivering excellent service"[2] . Thus, while the Hawaii framework includes downside risk to its utilities, the PUC has explicitly recognized the role upside incentives can play.
- *Illinois*. Illinois was an early adopter of PBR concepts and has reviewed and updated its approach over time. Importantly, the performance metrics initially implemented in Illinois, which were narrowly downside only, were companion to two other elements. The first was a broader statutory requirement to make certain distribution investments were made at certain levels; the second was a level of recovery assurance through formula rates. While this arrangement is not necessarily transportable to Michigan, it does highlight the acknowledgement that achieving certain reliability targets must be supported by a certain level of investment, and that these investments should be recoverable – downside metrics should exist within a more holistic context. Absent assured recoverability of investments, it is not apparent that Illinois would have instituted downside only reliability metrics. The Commission's PBR report in 2018 recognized the role of grid investments, noting "PBR should not be viewed as a mechanism to avoid increases in utility rates, since the expected level of new capital investment, even with the deployment of new technologies, will be significant over the coming years."
- *North Carolina*. Following the passage of legislation, Duke Energy Carolinas (DEC) filed a proposed PBR plan in early 2023. DEC proposed upside and downside PIMs, with reliability and affordability as downside PIMs and peak load reduction and renewables integration as upside PIMs. The overall upside opportunity and downside opportunity is the equal in DEC's proposal. To simply highlight that reliability metrics only have penalties associated with them leaves out the important context and the overall symmetry of the North Carolina model.

[2] Hawaii PUC Press Release, June 1, 2021.

Section 2: Response to Select Stakeholder Comments

Consumers Energy (Consumers). The Company broadly supports the comments of Consumers and specifically highlights three areas of concurrence:

- *Deliberate development*. Consumers described the importance of the Commission adequately considering stakeholder input. The Company additionally notes that it recently filed its Distribution Grid Plan filed in Case No. U-20147, and the Company's approach to distribution investments should inform metrics and targets.
- *Reasonable incentives*. Consumers described that the scope of incentives should be reasonable and that any design should be symmetrical. As described above, the Company strongly supports a symmetric approach to incentive design. Further, Consumers indicated that any PBR implementation should account for the existing bill credits included in the Service Quality and Reliability Standards. As the Company noted in its initial comments, it expects to pay approximately $9M in 2023 related to the SQRS bill credits and strongly recommends that the Commission's PBR proposal consider this existing, penalty-only mechanism.
- *Reasonable targets*. Targets must (1) reflect actual Company performance, (2) offer reasonable interim targets, and (3) be consistent with reliability investments as outlined in the distribution planning process *and* approved in general rate cases. The Company fully supports this perspective.

Attorney General (AG). The AG offered various comments regarding metrics, links between investments, and review of PBR performance. The Company highlights four areas for comment:

- *Simplicity is key for initial PBR implementation.* In their comments, the AG noted that simplicity is important for an initial application of PBR. The Company supports this approach of keeping PBR simple, especially initially. The company believes that limiting the number of metrics is important in the design of PBR, and that these should be kept to as few as possible (e.g., 6 if all focused on reliability).
- *The proposed incentive design is complex.* The AG's proposed "APRR Base" is not a financial measure that is regularly calculated and reported by the Company. Even with the protections proposed by the AG that would prevent an excessive penalty or reward being assessed during the initial application of the SIIM (i.e., the maximum penalty or reward set at $10 million per year), defining a baseline of something substantially greater potentially sets a precedent that could result in excessively punitive or overly rewarding payments in the future. A simpler structure may be more effective. For example, one such structure could have the maximum penalty or reward set at a given amount and the Company's overall performance be directly assessed against that maximum penalty or reward (e.g., $1 million per metric as observed for certain service quality standards in Minnesota – PBR metrics do not have associated incentives and penalties at this time). This would eliminate the need to calculate a separate APRR Base and accomplish the same objectives.

- *Staff is the appropriate auditor of any PBR implementation*. The AG proposes an audit of utility PBR performance data to be conducted by "an outside firm with expertise in utility operations"[3]. While the Company agrees that an audit of its data and reporting process is appropriate, it believes that Staff is well-equipped to perform this function. The Staff is already responsible for overseeing the Company's reliability filings, which contain substantially similar information as the Company would expect to include in a review of PBR performance.
- *Metrics should minimize overlap.* The AG's proposal has several adjacent and overlapping metrics. For example, a customer experiencing a 72-hour outage during a CAT storm event would impact four of the ten targeted metrics – all three of the CAT storm restoration metrics as well as the "Outages of 5 hours plus" metric. In some cases, the same data would feed into the calculation of multiple metrics. When taken together, the proposed SIIM may be introducing unintended incentives and/or disincentives given this overlap.

Association of Businesses Advocating Tariff Equity (ABATE). ABATE offered comments focused primarily on incentive design and applicability, including two that are addressed below.

- *PBR should utilize one set of targets*. ABATE proposes that should a utility fail to achieve any of the six standards provided in Rule 460.722 (Rule 22) of the SQRS, there should be no opportunity for an incentive.

  The Commission's straw proposal, and the Company's initial comments in this docket, propose pathways to achieve second quartile or better performance with interim targets based on actual Company performance. Said differently, the Company has proposed to meet median industry performance, which includes dozens of utilities with newer systems and more favorable weather. ABATE also states "incentives should only be awarded for superior performance" and then notes "the straw proposal long term targets…appear to be in line with this principle" – on this point the Company concurs. However, ABATE instead proposes that not only should the Company be judged on the performance of the PBR metrics, but it should then again be judged on the SQRS, which were contemplated outside of the PBR framework. The Company disagrees.

- ABATE explains that incentives should be linked to authorized return on equity (ROE) as applied to distribution plant. Specifically, ABATE indicates that total earned ROE should not exceed either the "upper range of reasonableness" or "50 basis points above the authorized ROE". It then says "no additional compensation should be paid to the extent the utility is already earning in excess of its authorized ROE including the incentive"[4]. There are two issues with this approach:
  - *PBR incentives should not be linked to ROE.* Practically, both authorized and earned ROE are considered in the context of general rate cases. An annual determination of performance relative to PBR metrics and targets is not the appropriate venue to consider ROE related matters.

[3] Sept 22, 2023 comments of the Attorney General in Case No. U-21400, Pg 10
[4] Sept 22, 2023 comments of ABATE in Case No. U-21400, Pp 3-4

- *A two-step threshold for incentive payments is inappropriate.* ABATE proposes first to limit incentives based on distribution ROE, and then again based on overall ROE. The Company disagrees with both approaches and maintains that (1) tying performance to ROE is inappropriate, and (2) there should be no second threshold for incentives beyond achieving metric-level performance sufficient to earn an incentive.

Michigan Energy Innovation Business Council and Advanced Energy United (MEIBC/U). MEIBC/U offered comments regarding the applicability of incentives/penalties and perspectives on metric choice. The Company offers the following feedback:

- *Reliability is the appropriate focus for an initial PBR implementation.* MEIBC/U suggests that additional metrics beyond reliability could be appropriate to include. The Company refers to its initial comments that the Commission's current reliability focus is appropriate at this time given the Commission's previous guidance, the overall simplicity of one primary topic within an initial PBR implementation, and the acknowledgement that there is opportunity for improvement.

ELPC, Ecology Center, Vote Solar, and Union of Concerned Scientists (CEO). The CEO offered comments regarding process, incentive design, metric choice, and the role of this docket in the broader regulatory context. The Company offers the following feedback:

- *Measured implementation is appropriate*. In their comments, the CEO said they "urge the Commission to…be measured in adopting penalties for poor performance and cautious in adopting incentives"[5]. The Company agrees with this perspective and the possible risk of unintended consequences of a less measured implementation. This view is illustrated as well by the experience in Minnesota, which has included intentional stakeholder engagement and metrics without associated incentives.
- *PBR incentives should not be linked to ROE***.** The CEO indicates that any upside incentives should come with (presumably downward) adjustments to ROE that "reflect the upside that the utility can earn through performance". As stated previously, the Company disagrees that PBR should be linked to ROE. Any penalty incurred by the Company will already effectively reduce earned ROE, and any incentive awarded would increase earned ROE – this dynamic is already a feature of symmetric PBR in which the Company and its shareholders bear the financial risk associated with poor performance. For example, credits paid under the SQRS ultimately reduce earned ROE. Reducing *authorized* ROE, which as previously mentioned should not occur within a PBR plan but in a general rate case, would very likely result in double penalties considering both the reduction in the ROE itself (and therefore the Company's revenue requirement and rates), and any penalty incurred within the PBR context would be additional.

[5] Sept 22, 2023 comments of CEO in Case No. U-21400, Pg 5