STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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

At the October 3, 2002 meeting of the Michigan Public Service Commission in Lansing, Michigan.

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

OPINION AND ORDER

On December 4, 2000, the Commission issued an order adopting a code of conduct, as required by Section 10a(4) of the Customer Choice and Electricity Reliability Act:

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

MCL 460.10a(4). Among other things, the order required the filing of compliance plans and permitted the filing of requests for waivers.

On January 23, 2001, the Commission issued an order amending the code of conduct to require the filing of compliance plans within 60 days after the issuance of an order on rehearing of the December 4, 2000 order. On October 29, 2001, the Commission issued the rehearing order, and adopted a revised code of conduct.

Cherryland Electric Cooperative (Cherryland), Cloverland Electric Cooperative (Cloverland), Great Lakes Energy Cooperative (Great Lakes), HomeWorks Tri-County Electric Cooperative (HomeWorks), Midwest Energy Cooperative (Midwest), and Thumb Electric Cooperative (Thumb) filed similar compliance plans and requests for waivers. Alger Delta Cooperative Electric Association (Alger Delta) and The Ontonagon County Rural Electrification Association (Ontonagon) filed compliance plans, but did not request waivers. Presque Isle Electric & Gas Co-op (Presque Isle) filed a compliance plan, but did not request waivers.

Waiver Requests

Cherryland, Midwest, and Thumb request waivers of section II.A to permit office and field employees to market propane service. Great Lakes and Tri-County (HomeWorks) request waivers of section II.A to permit office and field employees to market unregulated services.

On February 21, 2002, the Michigan Propane Gas Association (MPGA) filed a petition for leave to intervene for the purpose of filing an objection to the requests for waivers of the restrictions on marketing propane and other unregulated services. It says that it is in a position to provide the Commission with evidence regarding whether the requested waivers will inhibit the development or functioning of the competitive market. It says that its position is that the cooperatives "cannot possibly meet" the burden of showing that the waivers will not inhibit competition. Petition, p. 3. MPGA requests that if the Commission does not reject the request for waivers, it conduct contested case proceedings on whether the requested waivers will inhibit the development or functioning of the competitive market.

On March 7, 2002, the five cooperatives filed a letter in response. Among other things, they point out that the Commission rejected the MPGA's application for leave to appeal the ALJ's denial of their petition to intervene and that they did not appeal that order or file for rehearing within 30 days. With respect to the objection, the cooperatives state that the Commission did not provide for the filing of objections, much less a filing by a nonparty whose prior attempts to participate in the case have been rejected.

The Commission denies the MPGA's renewed request to participate in this case. In the December 4, 2000 order, the Commission considered and rejected the MPGA's late request to be permitted to participate in this case. The Commission remains persuaded that it correctly denied the MPGA's request to participate, and finds no reason to reach another conclusion at this time. The MPGA simply disagrees with the Commission's conclusion that the Act does not require it to bar the cooperatives from participating in unregulated markets, but rather permits their participation under the reasonable terms set out in the code of conduct.

The Commission will require that the cooperatives must adhere to full functional separation for their propane operations. Further, the cooperatives must maintain separate books and accounts, properly and fully allocate all costs between regulated and unregulated services, provide comparable information to propane competitors on a contemporaneous basis, provide a list of propane competitors to their customers, and maintain separate facilities for the delivery of propane service. The Commission will grant the waivers for Cherryland, Midwest, and Thumb with the understanding that the waivers apply only to propane service and only for the joint use of personnel for marketing purposes.

The Commission will not grant waivers for Great Lakes or HomeWorks at this time because the requests are unduly broad. Great Lakes does not specify the services to which the waiver would apply. HomeWorks indicates at one point that it seeks a waiver for unregulated services, which is unduly broad, and at another point, requests a waiver for only propane service. The Commission may grant the waivers in a later order, with appropriate safeguards, following the filing of a proper application with a list of the services to which the waiver is intended to apply.

Cloverland requests waivers to permit an employee to be shared between Lighthouse Computers (an affiliate) and Cloverland. It also requests waivers to permit joint marketing and advertising in order to provide combined direct mailing. The cooperative has not identified which waivers it is seeking for these services. The Commission will consider waivers for these purposes once Cloverland fully identifies the sections for which it is seeking waivers.

Cherryland, Cloverland, Great Lakes, HomeWorks, Midwest, and Thumb request waivers of section II.F to permit the cooperatives to finance or cosign loans for their affiliates.

The Commission will grant conditional waivers only for the cooperatives that requested them. The Commission is concerned about the amount of debt issued by the cooperatives to finance unregulated ventures, especially because some of these ventures may be difficult to finance on their own. Affiliate transaction audits and rate case audits conducted by the Staff have identified large debt service requirements, poor or even non-existent earnings, and potential cross-subsidization issues associated with many of these ventures. If these ventures require large enough amounts of debt and fail to be profitable, the financial well-being of the regulated utility services of the cooperatives could be affected. This could result in a cooperative subsidizing its affiliate to the detriment of its own customers. Therefore, the Commission will permit a cooperative to cosign or help finance unregulated ventures and affiliates so long as the cooperative's margin (or equity) ratio is at least 40% and remains above that level (computed as total margin divided by the sum of margin and debt, i.e., equivalent to the equity ratio of an investor-owned utility). In granting these conditional waivers, the Commission does not seek to undo prior transactions, and therefore the conditional waivers apply prospectively only. Furthermore, the Commission will grant these waivers only so long as costs are appropriately allocated between regulated and unregulated services or affiliates.

Cherryland, Cloverland, Great Lakes, HomeWorks, Midwest, and Thumb request waivers of sections II.K and II.L to allow the joint use of the cooperatives' logos. Cloverland and Thumb request waivers only until their current inventory of promotional material has been used. Cherryland, Great Lakes, HomeWorks, and Midwest do not limit their requests to existing inventories.

The Commission will grant these waivers so long as costs are fully and appropriately allocated between regulated and unregulated services or affiliates and so long as the promotional material does not include mass marketing material such as newspaper or magazine advertisements, bill boards, etc.

Cherryland, Cloverland, Great Lakes, HomeWorks, and Midwest request waivers of section IV to allow the disclosure of certain information for their telecommunication ventures.

The Commission will grant these waivers so long as the use of the information is for the cooperatives' telecommunications ventures only and costs are appropriately allocated. The Commission will not permit the information to be used for any other purpose.

Presque Isle did not request any waivers, but its compliance plan rests on the assumption that its natural gas operations are regulated for purposes of the code.

Presque Isle's assumption is incorrect because the Commission does not regulate the rates of its natural gas operations. The Commission's authority to set rates for both electric and gas services, and thus the ability to control the extent to which, if any, one service subsidizes another, is the primary justification for not applying the code to two regulated services. While it is true that the Commission has safety jurisdiction over Presque Isle's gas operations, jurisdiction to issue certificates of public convenience and necessity, and jurisdiction to review books and records, and it is true that the gas rates are set by a municipality and that the cooperative is non-profit, none of those are a reason to exempt the cooperative from the code of conduct. Therefore, Presque Isle must comply with the code of conduct or request appropriate waivers related to its gas operations. Because Presque Isle has not requested any waivers, violations of the code from this date forward will be dealt with accordingly.

All of the waivers granted by this order apply narrowly to the programs described in the cooperative's compliance plans. Any new programs or modifications to the programs described in the cooperatives' December 28, 2001 compliance plans will require new waiver applications.

An overly restrictive code of conduct is not in the interests of the cooperatives, their customers, or the Commission. Therefore, the Commission has allowed flexibility in its code of conduct by permitting each utility to seek waivers. This additional flexibility requires the Commission and its Staff to be diligent in preventing cross-subsidization between utilities and their non-regulated operations and affiliates. One of the Commission's paramount goals in adopting this code of conduct is to assure that the cooperatives do not subsidize their unregulated ventures or affiliates with revenues from regulated operations, which is required by Act 141. To assure that this does not take place, while facilitating the granting of waivers from the code's requirements, the Commission will require those cooperatives that are granted one or more waivers to adhere to the following conditions.

(1) The utility shall ensure that the Commission has access to books and records of any holding company owning the utility and each of the holding company's affiliates and their joint ventures. Any objections to providing access as requested under this requirement must be raised before the Commission, and the burden of showing that the request is unreasonable or

unrelated to the Commission's responsibilities is on the party seeking to deny or withhold access.

(2) Consolidated 10k reports and shareholders' reports of the consolidated utility and/or its parent holding company on an annual basis.

(3) Annual balance sheet and income statements of the non-regulated subsidiaries of the utility and/or the non-consolidated subsidiaries of the holding company.

(4) Reports of internal audits conducted regarding transactions between the utility and its nonutility affiliates. Such reports will be submitted every three years beginning with a report for the year 2003. The audit report shall address transactions occurring since the last audit report and shall describe whether appropriate cost allocation procedures and transfer pricing methodologies were followed and whether the utility and its affiliates are maintaining records that are adequate to facilitate an effective audit of the transactions. The Commission Staff may require more frequent reports or additional audits when appropriate.

(5) A notification to the Commission 30 days prior to any transfer to non-utility affiliates of any utility assets or property exceeding a fair market value of $100,000. At the time notice is provided, the utility shall make available to the Commission information that demonstrates how the transfer price was determined.

(6) In its annual report, each utility shall provide information on any arrangement that allows an affiliate to obtain credit in a manner that permits a creditor, upon default, to have recourse to or in any way encumber the utility's assets.

(7) The cooperatives must submit additional schedules in their annual reports detailing affiliate transactions. The Staff will supply the additional schedules that are required to be filed by December 1, 2002 for the calendar year 2001, and annually, thereafter, with their annual reports.

(8) The cooperatives must fully disclose all affiliate books and records to the Commission Staff as requested by the Staff and in a manner that the Staff will prescribe to protect the confidentiality of those records.

Compliance Plan Wording

The compliance statements filed by each of the cooperatives could be viewed as changing the meaning and undermining the purposes of the Commission's approved wording of the code of conduct. For example, the cooperatives' wording for section III.F would permit them to steer their member-customers away from alternative electric suppliers, which is expressly prohibited by the code. As another example, Cherryland, HomeWorks, Midwest, and Thumb word section II.H to permit them to jointly market and sell regulated and unregulated services, which the code expressly prohibits without a waiver.

The cooperatives' compliance statements also fail to include other corporate entities (entities other than affiliates) within code provisions such as sections II.G, III.B, and III.C. For example, the responses of Cherryland, Cloverland, Great Lakes, and Alger Delta to section III.B would seem to permit them to offer a discount to an unregulated division without offering the same discount to customers of other alternative electric suppliers. For section II.A, the cooperatives seek to exempt unregulated operations providing less than $10,000 a month from separations requirements without seeking a waiver. They do so without even identifying the $10,000 as a gross or net figure. This amount may be more than all their unregulated affiliates earn on a net basis. The Commission will not permit wording in a compliance statement to exempt a cooperative from the requirements of the code.

The cooperatives also state that they will adhere to the code beginning 30 days after the Commission's approval of their compliance plans. They also seek to exempt themselves from the separation requirements of the code, such as sections II.D, II.E, and II.M. Further, they state that portions of the code do not apply to them because they do not have affiliates that are alternative electric suppliers at this time.

The Commission will require each of the cooperatives to adhere to the wording and intent of the code of conduct, and will not allow them to modify the code through compliance statements.

The Commission will also not authorize blanket separation waivers, but will consider each request for a waiver on a case-by-case basis. Finally, the code takes effect immediately.

The Commission FINDS that:

a. Jurisdiction is pursuant to 1909 PA 106, as amended, MCL 460.551 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACS, R 460.17101 et seq.

b. The compliance filings should be accepted, subject to the discussion above.

c. The requests for waivers should be granted in part and denied in part, as discussed above.

THEREFORE, IT IS ORDERED that:

A. The compliance filings of Alger Delta Cooperative Electric Association, Cherryland Electric Cooperative, Cloverland Electric Cooperative, Great Lakes Energy Cooperative, HomeWorks Tri-County Electric Cooperative, Midwest Energy Cooperative, The Ontonagon County Rural Electrification Association, Presque Isle Electric & Gas Co-op, and Thumb Electric Cooperative are accepted, subject to the discussion above.

B. The requests of Cherryland Electric Cooperative, Cloverland Electric Cooperative, Great Lakes Energy Cooperative, HomeWorks Tri-County Electric Cooperative, Midwest Energy Cooperative, and Thumb Electric Cooperative for waivers are granted in part and denied in part, as discussed above.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, pursuant to MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ Laura Chappelle
Chairman

(S E A L)

/s/ David A. Svanda
Commissioner

/s/ Robert B. Nelson
Commissioner

By its action of October 3, 2002.

/s/ Dorothy Wideman
Its Executive Secretary

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

Laura Chappelle
Chairman

Commissioner

Commissioner

By its action of October 3, 2002.

Its Executive Secretary

PROOF OF SERVICE

STATE OF MICHIGAN)

Case No. U-12134
(Co-ops waivers)

County of Ingham)

Gloria P. Jones being duly sworn, deposes and says that on October 3, 2002, A.D. she served a copy of the attached Order by mailing copies thereof by first class mail, postage prepaid, or by inter-departmental mail, to the persons as shown on the attached service list.

Gloria P. Jones

Subscribed and sworn to before me
this 3rd day of October 2002

Sharon Allen
Notary Public, Ingham, County, Michigan
My Commission expires August 16, 2004

SERVICE LIST FOR DOCKET # U - 12134- CASE #
DATE OF PREPARATION: 10/04/2002

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