

STATE OF MICHIGAN

BEFORE THE PUBLIC SERVICE COMMISSION

**In the matter of the Application of)
The Detroit Edison Company)
To Unbundle its Retail Electric Rates)
_____)**

MPSC Case No. U-13286

INITIAL BRIEF OF THE NATIONAL ENERGY MARKETERS ASSOCIATION

Dated: September 20, 2002

I. Introduction

This Initial Brief is submitted by The National Energy Marketers Association (“NEM”) in the above-referenced proceeding. NEM is a national, non-profit trade association representing wholesale and retail marketers of energy, telecom and financial-related products, services, information and related technologies throughout the United States, Canada and the U.K. NEM's Membership includes wholesale and retail suppliers of electricity and natural gas, independent power producers, suppliers of distributed generation, energy brokers, power traders, and electronic trading exchanges, advanced metering and load management firms, billing and information technology providers, credit, risk management and financial services firms, software developers, clean coal technology firms as well as energy-related telecom, broadband and internet companies.

This regionally diverse, broad-based coalition of energy, financial services and technology firms has come together under NEM's auspices to forge consensus and to help resolve as many issues as possible that would delay competition. NEM members urge lawmakers and regulators to implement:

- Laws and regulations that open markets for natural gas, electricity and related products, services, information and technology in a competitively neutral fashion;
- Rates, tariffs, taxes and operating procedures that unbundle competitive services from monopoly services and encourage true competition on the basis of price, quality of service and provision of value-added services;
- Competitively neutral standards of conduct that protect all market participants;
- Accounting and disclosure standards to promote the proper valuation of energy assets, equity securities and forward energy contracts, including derivatives; and

- Policies that encourage investments in new technologies, including the integration of energy, telecommunications and Internet services to lower the cost of energy and related services.

NEM asserts that Detroit Edison's (DTE's) unbundling application should be rejected because it fails to satisfy statutory unbundling requirements. NEM also urges the Michigan Public Service Commission ("MPSC" or "Commission") to require DTE to implement fully allocated embedded cost-based unbundled rates. The instant case is the proper forum to examine unbundling of DTE's rates beyond the basic elements of distribution, transmission and generation. For these reasons, NEM urges that DTE's proposed alternative to unbundled billing should be rejected and that the Commission must ensure that any Transmission System Charge is implemented in a competitively neutral manner.

II. Summary of Detroit Edison's Application

Detroit Edison submitted an Application to Unbundle its Electric Rates dated February 4, 2002. The Application was submitted pursuant to Commission Order dated December 20, 2001, issued in Case No. U-12966 ("Order"), in which the Commission rejected DTE's previous application to unbundle its rates. The Commission's Order found that DTE's previous proposal to provide a bill message in lieu of unbundling rates, "fails to conform with either the letter or the spirit of Section 10b(2), which clearly requires Detroit Edison and all other electric utilities in this state to unbundle their 'existing commercial and industrial electric rate schedules and separately identify and charge for their discrete services.'" (Order at page 5).

In its current application, DTE represents that it "unbundles its metered residential, commercial and industrial retail electric rate schedules into their separate

distribution, transmission and generation components based on a 2000 functional revenue requirement analysis. (Application at page 2). However, DTE, "is not proposing to include in its schedule of rates, nor bill customers the unbundled rates proposed in this application." (Application at page 3). DTE argues that, "[t]his is fully consistent with the statute which only requires the unbundling of 'existing' rate schedules." (Id.). NEM disagrees, and for the following reasons submits that the DTE Application should be rejected.

III. Summary of Testimony of Phil O'Connor for the National Energy Marketers Association

Dr. Philip O'Connor testified on behalf of NEM urging:

the Commission to evaluate and modify as necessary the application filed by Edison in this proceeding in order to promote the development of a robust competitive retail electric market in Michigan. I also urge the Commission to direct Edison to make available fully allocated embedded cost information to all customers as a step toward effective, pro-competitive unbundling of various electric services.

(O'Connor Testimony at pages 4-5). Dr. O'Connor explained the importance of rate unbundling as a means of providing price signals to consumers and educating consumers about competitive options. (O'Connor Testimony at pages 7- 8). Dr. O'Connor further noted that since DTE does not propose to present unbundled rate information in consumer bills or tariffs that "the development of a competitive retail electric market will impeded rather than promoted by what is essentially Edison's non-unbundling application." (O'Connor Testimony at page 8).

Dr. O'Connor also testified that inasmuch as DTE's application is limited to unbundling rates for generation, distribution and transmission, "that the scope of the application is too narrow because it fails to provide information that will assist the Commission, customers, alternative suppliers, and utilities in beginning to unbundle distribution services into all manner of competitive products, services, information and technology." (O'Connor Testimony at page 10). He noted that further unbundling of rates would send price signals to consumers and educate consumers about competitive offerings, and therefore, "would further facilitate customer choice and competition." (O'Connor Testimony at page 10). Dr. O'Connor discussed the kinds of services to consider in further unbundling including, "metering services, billing information services, collections services, and customer enrollment and care services." (O'Connor Testimony at page 11). Examples of such services are contained in an appendix to Dr. O'Connor's testimony.

Dr. O'Connor further testified that DTE's unbundled rates should be based on DTE's fully allocated embedded costs. (O'Connor Testimony at page 13). He presented a number of rationales for embedded cost-based rate unbundling, including: 1) the rates customers currently and historically have been charged are based on embedded costs; 2) the utilities embedded costs have been determined to be "just and reasonable" and therefore unbundled rates based on the same costs must also be "just and reasonable"; 3) unbundling rates based on other methodologies (such as marginal costs) would result in artificially low, subsidized rates; 4) unbundling rates based on less than fully allocated embedded costs could result in increased stranded costs that are incurred over a longer time frame; and 5) unbundling rates based on less than fully allocated embedded costs

could result in customers paying twice for the same services, once to the competitive supplier rendering the service and once to the utility. (O'Connor Testimony at pages 13-14). Finally, Dr. O'Connor in his testimony discussed the importance of "ensuring that the unbundled generation component accurately reflects all costs related to generation, and is not artificially lowered in the unbundling process." (O'Connor Testimony at page 16). The unbundled generation rate must not be set artificially low or it will create a competitive disadvantage for competitive suppliers and harm the development of the market. (O'Connor Testimony at page 17). O'Connor also noted his concerns with DTE's proposed transmission rate. (O'Connor Testimony at page 18).

IV. DTE's Revised Application Should Be Rejected for Failure to Satisfy Statutory Unbundling Requirements

DTE's revised unbundling application should be rejected for failure to satisfy MCL 460.10b(2), which requires that,

No later than 1 year from the effective date of the amendatory act that added this section, each electric utility shall file an application with the commission to unbundle its existing commercial and industrial rate schedules and separately identify and charge for their discrete services. No earlier than 1 year from the effective date of the amendatory act that added this section, the commission may order the electric utility to file an application to unbundle existing residential rate schedules.

Also of note is the requirement set forth in Section 460.10d(1) which provides that,

Unless otherwise reduced by the commission under subsection (4), the commission shall establish the residential rates for each electric utility with 1,000,000 or more retail customers in this state as of May 1, 2002 that will result in a 5% rate reduction from the rates that were authorized or in effect on May 1, 2000. Notwithstanding any other provision of law or commission order, rates for each electric utility with 1,000,000 or more retail customers established under this subsection become effective on the effective date of the amendatory act that added this section and remain in effect until December 31, 2003, and all other electric retail rates of an electric utility with 1,000,000 or more retail customers authorized or in

effect as of May 1, 2000 shall remain in effect until December 31, 2003, unless otherwise reduced by the commission under subsection (4).

DTE has devised a methodology to unbundle its rates necessitated by its tortured reading of the rate freeze requirements of Section 10d(1). DTE reads the rate freeze requirement as imposing a "bill neutrality" constraint for all customers. (See Musial Testimony at page 19). In doing so, DTE confuses the concept of a rate freeze, which holds the utility's underlying rates constant, with a bill freeze, which would entail keeping customers overall bills constant.¹ DTE self-imposed the requirement to "unbundle existing rate schedules into their broad functional components in such a way that the new unbundled rates, when applied to the customer's billing determinants, will yield the exact, same total charge for full requirements service as did the application of our current bundled rates." (Musial Testimony at page 8). This "bill neutrality" constraint is created and imposed by DTE, not the Legislature, and it should not be permitted to obfuscate the process of unbundling DTE's rates.

DTE's flawed "bill neutral" unbundling methodology has had the result that, "some of the rate components are set at levels which appear to be peculiar." (Musial Testimony at page 19). As a result, DTE proposes:

not to bill customers based on these unbundled rates. Since we are not proposing to bill customers on these rates, there is no purpose in creating tariff sheets. We can only bill the rates authorized by the Commission and those rates are portrayed on the tariff sheets. If we billed on current rates and our tariff sheets reflect the unbundled rates, customers would not be able to compare rates charged versus those contained in the tariff sheet.

¹ See Case U-12966, Attorney General's Replies to Exceptions, dated September 24, 2001, at page 2, maintaining that, "Section 10d(1) does not conflict with the unbundling mandate found in Section 10b(2), and Section 10d(1) does not prohibit incorrect price signals." The Attorney General noted that Section 10d(1), "freezes rates, not customer bills."

(Musial Testimony at page 18). DTE itself admits that, "if the Company were to unbundle its rates from scratch at the conclusion of the rate freeze, that peculiarity would be addressed." (Musial Testimony at page 19). DTE should have properly unbundled its rates in the instant case to avoid the peculiarity about which it complains.

The Commission should reject DTE's application in the instant case on the same basis that it rejected DTE's earlier filing - failure to comport with Section 10b(2). Section 10b(2) requires unbundling of existing rate schedules into discrete services. DTE has failed to comply with this requirement. DTE has not unbundled existing rates but rather created new rates in the guise of complying with the Section 10d rate freeze. Because of DTE's self-imposed "bill neutrality" constraint it has unnecessarily created a conflict between Section 10b(2) and 10d. The Commission should not permit DTE to avoid its responsibility to unbundle its rates by virtue of this unnecessary and DTE-created problem.

Furthermore, DTE's Application does not comply with Section 10b(2) because DTE does not propose to, "separately identify and charge for [] discrete services." (emphasis added). As noted above, DTE does not propose to bill customers with the unbundled rates set forth in the application. Accordingly, the DTE application quite clearly fails to satisfy the requirements of Section 10b(2) and should be rejected.

V. DTE Should Be Required to Implement Fully Allocated Embedded Cost-Based Unbundled Rates

NEM urges the Commission to require DTE to implement fully allocated embedded cost-based rates. As noted by NEM Witness Dr. O'Connor, embedded cost-based rate unbundling is superior to other methodologies such as marginal cost-based rate

unbundling for a number of reasons. (O'Connor Testimony at pages 13-16). NEM asserts that the proper unbundled rates for contestable services are DTE's embedded costs because the rates which customers currently and historically have been charged are based on embedded costs. Utility revenue requirements are currently established based on fully allocated embedded costs that have been determined by the Commission to be just and reasonable. These just and reasonable rates include embedded costs associated with competitive, workably competitive and potentially workably competitive products, services information and technologies. Accordingly, institution of rates based on or guided by marginal, avoided or long run incremental costs will not reflect accurately the true prices that consumers actually pay for competitive services provided by utilities and will therefore undermine the goal of providing accurate price signals to customers.

Furthermore, instituting rates based on any measure other than the DTE's fully embedded costs will cause DTE to incur much higher stranded costs. If DTE's rates reflect and its customers pay less than fully embedded costs, its customers will be paying an artificially low, subsidized price for competitively available services. If DTE's unbundled rates reflect and its customers pay less than fully embedded costs, its customers end up paying twice for these services, once to the competitive supplier currently rendering the service and once to DTE. In conjunction, these two effects will slow customer migration and DTE will continue to incur costs for competitive services that may ultimately become stranded. In contrast, unbundled utility rates based on fully embedded costs will allow utilities to both quantify and, if properly mitigated, recover stranded costs within a reasonable time frame. It will also provide customers and

competitors with true, accurate price signals that will permit meaningful price competition in the shortest possible time.

Other Commissions that have examined the issue have concluded that unbundled rates should be based on embedded costs. For instance, the Illinois Commerce Commission recently noted that, "[t]he use of embedded costs has been applied uniformly by this Commission to all DST providers in Illinois . . . [and] the embedded cost approach advances concerns of economic efficiency as well as sending economically-correct price signals that are pivotal to the proper development of the market." (Docket 01-0423, Interim Order, issued April 1, 2002, at page 124). Similarly, the New York PSC also ordered embedded cost-based rate unbundling. (Case 00-M-0504, Order Directing Filing of Embedded Cost Studies, issued November 9, 2001, at pages 15-16). The NY PSC noted that, "as to the appropriateness of using ECOS [embedded cost of service] studies as the basis for establishing competitive rates, it should suffice to observe that we have, on a number of occasions, found it appropriate to use embedded costs as the basis for setting competitive rates." (Case 00-M-0504, Order on Rehearing Petitions and Motions, issued January 24, 2002, at page 6). Accordingly, NEM urges this Commission to follow the lead taken by other states and require DTE to implement fully allocated, embedded cost-based unbundled rates.

VI. The Instant Case is the Proper and Necessary Forum for Consideration of Further Unbundling of Services

A. The Instant Case Should Not Be Limited to Consideration of Basic Unbundling

MEGA's witness, Mr. Ault, argues in his testimony that, "unbundling of services beyond the basic elements of generation, transmission and distribution should not be addressed in this case." (Ault Testimony at page 3). NEM asserts that this statement is erroneous and that the instant case is the appropriate forum for consideration of the expansion of the unbundling of services beyond the basic elements of generation, transmission and distribution to other discrete services such as metering, billing and customer care. (See O'Connor Testimony at pages 10-11). Section 10b(2) requires rate unbundling for "discrete services." The statute does not define "discrete services," and certainly does not limit the scope of unbundling to generation, transmission and distribution. However, the Commission gave guidance as to what "discrete services" are to encompass in the gas unbundling order in which it ordered the gas utilities to, "provide detailed and comprehensive studies on its costs to provide the following services, by customer class: (1) metering services, (2) billing information services, (3) transmission services, (4) balancing services, (5) storage services, (6) backup and peaking services, and (7) customer turn-on and turn-off services." (Case U-12550, Opinion and Order, issued July 11, 2001, at page 2). This list indicates that the Commission itself has a more expansive view of discrete services that can and should be unbundled. Therefore, the restrictions on the scope of this case that Ault seeks to have imposed, but are not set forth in the statute itself, should be rejected.

B. It is Proper to Consider Expansion of Unbundling in Utility-Specific Proceedings

MEGA's Witness, Mr. Ault, argues that the issue of further unbundling should be decided in a generic unbundling case and that this case was intended to address, "completion of basic unbundling into generation, transmission and distribution elements for Detroit Edison." (Ault Testimony at page 3). With respect to Mr. Ault's argument that the issue of unbundling should be dealt with in a generic case, NEM submits that the statute provides guidance as to the appropriate forum for handling unbundling issues. Section 10b(2) required each electric utility to file an application to unbundle its rates into discrete services. Apparently, the Legislature intended that unbundling issues be handled on a utility-specific basis. It is disingenuous to assert that other parties or potential parties could not have contemplated a discussion of unbundling beyond the elements of generation, distribution and transmission in this case. The statute does not limit unbundling to these elements, and the Commission itself has taken a more expansive view of unbundling for the gas utilities. (Case U-12550, Opinion and Order, issued July 11, 2001) NEM also notes that in the Consumers Energy C&I unbundling application rates were unbundled into generation, transmission, distribution, a customer charge and a regulatory adjustment charge. (Case U-12970, Opinion and Order, issued May 16, 2002). Certainly, DTE and others should also have been aware of the more expansive approach that was taken in that case.

C. Further Unbundling is Necessary for Market Development

Mr. Ault also claims that further unbundling, "should not be addressed until more experience with retail electric competition is obtained." (Ault Testimony at page 3). Mr. Ault's argument that further unbundling should be forestalled pending further development of retail competition should be rejected. Other PSCs that have reviewed the issue of rate unbundling have recognized its value in encouraging the development of the market. For instance, the New York PSC concluded that, "a prerequisite to fostering retail market development is the establishment of unbundled rates for competitive or potentially competitive functions that reflect fully allocated costs." (Case 00-M-0504, Order Directing Filing of Embedded Cost Studies, issued November 9, 2001, at page 1). The NYPSC required that embedded cost studies, and unbundled rates based on these studies, be filed reflecting the following electric functions: supply, including separate identification of the procurement function; supply - non-bypassable; delivery; meter service providers; meter data service providers; meter ownership; billing and payment processing; energy services-competitive; uncollectibles; and customer care. (Case 00-M-0504, Order Directing Filing of Embedded Cost Studies, issued November 9, 2001, pages 11-12 and Attachment A).

Likewise, the Illinois Commerce Commission concluded that, "the unbundling of metering and billing will promote the development of competitive markets for electric energy in Illinois. The evidence indicates that there is customer interest in unbundling these services and that unbundling could result in innovation and greater efficiency. Further, the unbundling of these services allows customer choice for additional services besides generation services." (Case 99-0013, Interim Order, issued April 12, 1999, at

page 11). As noted by NEM Witness Dr. O'Connor, "[i]nnovation and cost savings are the main values that competition brings to consumers, and greater unbundling of discrete services promotes those values." (O'Connor Testimony at page 11). Accordingly, NEM urges this Commission to require the unbundling of additional services as an appropriate and valuable means of fostering the development of the Michigan market.

DTE objects to the scope of unbundling proposed by Dr. O'Connor because, as DTE Witness Mr. Musial states, "Detroit Edison is not offering to make its Regulatory Compliance function competitive, nor is it offering to make any of the other functions listed by Dr. O'Connor at page 15 of his testimony, a competitive market." (Musial Rebuttal Testimony at page 11). NEM submits that DTE's offer or lack thereof to further unbundle its rates for competitive services, products, information and technology is irrelevant. The relevant consideration is whether or not further unbundling of competitive products, services, information and technology will yield positive benefits for the development of the Michigan market. Unbundling yields multiple benefits including sending proper price signals, educating consumers, preventing cross-subsidies in utility rates and stimulating innovation. (O'Connor Testimony at pages 7-8 and 10-11; Wallace Testimony at pages 3 and 6).

D. The Statutes Do Not Bar Further Unbundling

MEGA's Witness, Mr. Ault, argues that the effect of Section 10q(5) must be considered before further unbundling is ordered. Mr. Ault asserts that, "[t]he Commission needs to consider, before proceeding, the extent to which Act 141, Section 10q(5) would prevent expansion of mandatory unbundling to metering and billing

services." (Ault Testimony at page 6). DTE Witness Musial goes so far as to claim that, "Sections 10q(4) and (5) of PA 141 provide that utilities shall be allowed to continue to meter and bill their customers. Metering and billing were specifically excluded from services that are to be offered on a competitive basis." (Musial Rebuttal Testimony at page 11). NEM asserts that Mr. Ault and Mr. Musial have made unduly restrictive interpretations of these statutes.

Section 10q(5) of Act 141 provides that, "[t]he commission shall not prohibit an electric utility from metering and billing its customers for services provided by the electric utility." While Section 10q(5) may bar the Commission from prohibiting the electric utilities from metering and billing for the services they provide, it does not prohibit competitive providers from offering these discrete services. In fact, Edison's current Retail Access Service Tariff provides for separate billing by the utility and the alternative electric supplier. (Retail Access Service Tariff, First Revised Sheet No. EC2, ¶ 16.2). If consumers are to be permitted to evaluate and compare competitive suppliers' and utilities' offerings of discrete services such as metering and billing, it is imperative that they be provided with unbundled rate information to allow them to make fully informed decisions.

Section 10q(4) of Act 141 provides that, "[o]nly investor-owned, cooperative, or municipal electric utilities shall own, construct, or operate electric distribution facilities or electric meter equipment used in the distribution of electricity in this state." An electric utility's "ownership" or "operation" of electric meter equipment used in the distribution of electricity can and should be construed to permit competitive metering. For instance, meter service providers render services including installation, maintenance,

testing and removal of meters. Meter data service providers render services including meter reading, meter data translation, and customer association, validation, editing and estimation. (See NYPSC Case 00-M-0504, Order Directing Filing of Embedded Cost Studies, issued November 9, 2001, Attachment A). These competitive services are not inconsistent with a utility's ownership and operation of an electric meter for distribution-related purposes.

VII. DTE's Alternative to Unbundled Billing Should Be Rejected

DTE also proposes an alternative to unbundled billing. DTE Witness Mr. Musial proposes that:

If the Commission were to require Detroit Edison to bill on an unbundled basis as they have ordered Consumers Energy to do, then I would suggest that Detroit Edison be allowed to offer its customers a choice in bill presentation. The customer could be offered the choice of receiving a summary bill with charges rebundled or of receiving a bill with prices functionally unbundled per the Company's proposal in this case.

(Musial Rebuttal Testimony at page 12). As an initial matter, NEM points out that DTE's previous unbundling application which proposed to offer a bill message in lieu of unbundled rates was rejected by the Commission. As such, DTE's proposal to offer a "rebundled" bill appears to be nothing more than an attempt to revive its previous application not to unbundle its rates. As argued by NEM Witness Dr. O'Connor, "[n]egative prophecies that unbundled bills will only serve to confuse and dissatisfy customers should not prevent the advancement of customer education about real opportunities for competition, now or in the future." (O'Connor Testimony at page 12). A rebundled bill will not send price signals to consumers, and as the Commission

previously noted, "[m]eaningful choice will be thwarted if the provisions of Act 141, specifically Section 10b, are ignored." (Case U-12966, Order Dismissing Application and Requiring the Filing of a New Application, issued December 20, 2001, at page 6).

Furthermore, with respect to Consumers Energy's application to unbundle its commercial and industrial rates, it is noteworthy that the Commission rejected the proposal to allow Consumers to only unbundle generation rates on bills and required that all of the functional components in Consumers' application must appear on customer bills. (Case U-12970, Opinion and Order, issued May 16, 2002, at page 5). DTE should not be permitted to comply with a lesser standard than Consumers Energy was held to. For the foregoing reasons, DTE's proposal to offer a rebundled bill option should be rejected.

VIII. Transmission System Charge

Although DTE does not propose to bill customers based on its unbundled rates, DTE has utilized this application as an opportunity to introduce a Transmission System Charge that it fully intends to include in customer bills. In fact, DTE proposes to, "reduce the current energy-based ($\text{\$/kWh}$ -based) charges by an amount equal to [the] proposed $\text{\$/kWh}$ Transmission System Charge." DTE reasons that it, "can introduce this charge while not impacting the total charge on an individual customer's bill." (Musial Testimony at page 21). Yet again, DTE confuses its own "bill neutrality" concept with the rate freeze requirement that is, in fact, required by Section 10d.

Even more incredible is DTE's assertion that the Transmission System Charge, "is one price signal that we can provide customers that should be fairly reflective of the cost

that they will incur through a marketer in the Electric Choice environment." (Musial Testimony at page 21). Inasmuch as DTE refuses to provide unbundled rate information to customers on their bills, it is entirely unclear how customers would be able to see and respond to such a price signal. Furthermore, inasmuch as the charge would artificially lower the energy component of the bill, it would actually serve to distort, not enhance, any purported price signal. As noted by NEM Witness Dr. O'Connor, "[t]he generation component should be the right price to compare because it should be the price that competitive suppliers must compete against (with respect to commodity and other products, services, information and technology) to offer incumbent utility customers savings on their electric supply costs. If the generation component is set too low, then competitive providers are put at an artificial disadvantage and the development of a competitive retail electric market is artificially impeded." (O'Connor Testimony at page 17). Therefore, DTE's proposed reduction of the energy-based charge to accommodate the Transmission System Charge should not be permitted.

IX. Conclusion

For the reasons set forth herein, NEM urges the Commission to: 1) reject DTE's unbundling application for failure to satisfy statutory unbundling requirements; 2) require DTE to implement fully allocated embedded cost-based unbundled rates; 3) unbundle DTE's rates beyond the basic elements of distribution, transmission and generation; 4) reject DTE's proposed alternative to unbundled billing; and 5) and ensure that any Transmission System Charge is implemented in a competitively neutral manner.