STATE OF MICHIGAN

IN THE SUPREME COURT

APPEAL FROM THE MICHIGAN COURT OF APPEALS
Judges Patrick M. Meter, Michael J. Talbot and Stephen L. Borrello

CONSUMERS ENERGY COMPANY,

Appellant,

vs

MICHIGAN PUBLIC SERVICE COMMISSION,
Appellee.
_____/

Supreme Court No. 125955

Court of Appeals No. 237874

MPSC Case No. U-12134

REPLY BRIEF ON APPEAL – APPELLANT CONSUMERS ENERGY COMPANY

ORAL ARGUMENT REQUESTED

CONSUMERS ENERGY COMPANY – Appellant

Attorneys for Consumers Energy Company

Jon R. Robinson, Esq. (P27953)
John C. Shea, Esq. (P36854)
One Energy Plaza
Jackson, MI 49201
(517) 788-0698

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Consumers Energy Company ("Consumers Energy") files this Reply Brief in response to the briefs of the Michigan Public Service Commission ("MPSC") and the Michigan Alliance for Fair Competition ("MAFC"). Consumers Energy relies upon its initial brief and concurs in the arguments made by The Detroit Edison Company ("DECO") and the Michigan Electric Cooperative Association ("MECA"), and has therefore attempted to avoid repetitive arguments.

1. The MPSC's discussion of the appropriate standard of review at pages 6-10 of its brief inaccurately characterizes Michigan law. Questions of statutory interpretation, such as that at issue in this appeal, are subject to de novo review. In re MCI Telecommunications Complaint, 460 Mich 396, 413; 596 NW2d 164 (1999). Application of a standard of de novo review is wholly inconsistent with a claim that "deference" must be given to the MPSC's decision. The two concepts are irreconcilable. See Consumers Energy initial Brief, p. 10.

The MPSC's reliance upon a claim that its construction of a statute that it has been legislatively chosen to enforce should be given deference is also misplaced. This appeal concerns the construction of the Michigan Administrative Procedures Act. MCL 24.201 et seq ("APA"). The APA is not an act that the Commission enforces; it is a statute that imposes procedural limitations on the actions taken by the MPSC and by other administrative agencies. It makes little sense to argue that the Commission has some special knowledge or expertise that entitles its decisions concerning such a statute to be given judicial deference.

2. At pages 10-11 of its brief, the Commission vastly overstates the discretion that federal courts have afforded federal agencies to act via rulemaking or order. The Commission cites Securities and Exchange Commission v Chenery, 332 US 194;

67 SCt 1575; 91 LEd 1995 (1947) and National Labor Relations Board v Bell Aerospace Co, 416 US 267; 94 SCt 1757; 40 LEd2d 134 (1974) in support of its claim that it was not obligated to follow rulemaking procedures in adopting the code of conduct.

In the first place, federal law on this subject does not apply to the interpretation of the Michigan Administrative Procedures Act. The federal court decisions in this area are interpreting a different act—the federal Administrative Procedures Act—and those decisions are simply inapplicable to the instant appeal. In addition, however, none of those federal decisions support the MPSC's claim that, in adopting the detailed six page, single spaced code of conduct, it was merely establishing a new principle or a new policy through the adjudication of a specific set of facts.

In SEC v Chenery, supra, company insiders purchased certain securities of a public utility holding company undergoing reorganization. They then sought to convert those securities into common stock pursuant to the ultimately adopted reorganization plan. The SEC ruled that the conversion would not be permitted, and that the insiders would be permitted to receive only their purchase price plus interest. The SEC's decision was based upon its interpretation of the requirements of specific sections of the Public Utility Holding Company Act of 1935, 15 USC Section 79a, the statute under which it was operating. See SEC v Chenery, 91 LEd at 2003. The appellants argued that the SEC had, via this interpretation of PUHCA, adopted a new policy or standard that could only lawfully be done by adoption of a rule that would have prospective effect only. The Supreme Court rejected this contention, and ruled that, even though the SEC had applied its authority under the relevant act to a set of facts that had not previously been addressed in either a specific rule or a specific prior decision, it was entitled to do so through an individually adjudicated case,

rather than through the adoption of a rule. The Court did not, however, adopt the kind of expansive theory that the MPSC is now advocating in this appeal:

> "Since the Commission [SEC], unlike a court, does have the ability to make new law prospectively through the exercise of its rule-making powers, it has less reason to rely upon ad hoc adjudication to formulate new standards of conduct within the framework of the Holding Company Act. The function of filling in the interstices of the Act should be performed, as much as possible, through this quasi-legislative promulgation of rules to be applied in the future. But any rigid requirement to that effect would make the administrative process inflexible and incapable of dealing with many of the specialized problems which arise. [citation omitted] Not every principle essential to the effective administration of a statute can or should be cast immediately into the mold of a general rule. Some principles must await their own development, while others must be adjusted to meet particular, unforeseeable situations. In performing its important functions in these respects, therefore, an administrative agency must be equipped to act either by general rule or by individual order. To insist upon one form of action to the exclusion of the other is to exalt form over necessity.
>
> "In other words, problems may arise in a case which the administrative agency could not reasonably foresee, problems which must be solved despite the absence of a relevant general rule. Or the agency may not have had sufficient experience with a particular problem to warrant rigidifying its tentative judgment into a hard and fast rule. Or the problem may be so specialized and varying in nature as to be impossible of capture within the boundaries of a general rule. In those situations, the agency must retain power to deal with the problems on a case-by-case basis if the administrative process is to be effective. There is thus a very definite place for the case-by-case evolution of statutory standards. And the choice made between proceeding by general rule or by individual, ad hoc litigation is one that lies primarily in the informed discretion of the administrative agency." 91 LEd 2002. Emphasis added.

Thus, the Supreme Court was merely recognizing the difference between (i) the adoption of rules that have prospective effect only and (ii) the need to apply existing law retroactively in the adjudication of actual factual situations that are brought before the agency. This is exactly

the same distinction that is recognized in the Michigan APA, when it distinguishes between the rulemaking process and decisions in "contested cases."

The distinction is further illustrated in NLRB v Bell Aerospace Co, supra, also cited by the MPSC. In that case, the NLRB was asked to rule on the scope of the term "managerial employees" in the context of a specific dispute between an employer and a union seeking certification as a bargaining representative. The Supreme Court held that the NLRB was "not precluded from announcing new principles in an adjudicative proceeding," although it also specifically warned that there "may be situations where the Board's reliance on adjudication would amount to an abuse of discretion." 40 LEd2d 154. Again, this decision offers no support for the MSPC's position in this appeal. It merely illustrates that the essential principle adopted by the federal courts regarding the ability of an agency to act via rulemaking or individual, ad hoc decisions is consistent with that set forth in the Michigan APA. Where an administrative agency is asked to apply existing law retrospectively to a specific factual situation, it is not necessarily precluded from adopting new principles, interpretations, or policies to resolve those cases. This is the essence of the "contested case" exception in the Michigan APA. Where an administrative agency is adopting new rules of "general applicability" that are intended to only have prospective application in the future, however, that is plainly an exercise of more general rulemaking authority, and must be accomplished pursuant to the rulemaking procedures set forth in the Michigan APA. The MPSC does not, and could not, cite any federal cases that support its apparent claim that federal administrative agencies can simply announce an intent to hold some type of hybrid, adjudicative-style proceeding for the purpose of adopting a new set of industry-wide rules to be applied prospectively. Any attempt to do so would undoubtedly be viewed as an abuse of

discretion by the federal courts, as noted by the Supreme Court in the NLRB v Bell Aerospace Co decision.

3. The same distinction discussed above demonstrates why the MPSC's reliance on a series of Michigan Court of Appeals decisions is misplaced. Northern Michigan Exploration Co v PSC, 153 Mich App 635; 396 NW2d 487 (1986) was discussed in Consumers Energy's Appellant's brief at page 18, and that discussion will not be repeated. The important point is that the MPSC was adjudicating a specific factual dispute in that case, and simply applied existing law to that dispute. Similarly, American Way Life Ins v Insurance Commissioner, 131 Mich App 1; 345 NW2d 634 (1983) also involved a dispute concerning the amount of a premium for a new type of credit insurance that had been proposed by the insurance company. This is again the adjudication of a specific factual situation, and an example of a contested case of the "ratemaking" variety.

DAIIE v Commissioner of Insurance, 119 Mich App 113; 326 NW2d 444 (1982), and Michigan Life Insurance Co v Insurance Commissioner, 120 Mich App 552; 328 NW2d 82 (1982) are also similar decisions. In both cases, the agency was asked to apply existing law retrospectively to a specific set of facts. In both cases, the agency concluded that the insurance company had committed an unfair trade practice. In both cases, the insurance company argued that the agency was effectively adopting a new standard that should have been promulgated as a rule. In both cases, the Court of Appeals properly held that, in the adjudication of a specific factual dispute, the agency could, based upon its interpretation of existing law, adopt principles not previously specified in rules or prior decisions.

None of these decisions support the type of broad ruling that the MPSC is asking the Court to make in this appeal. The instant appeal concerns a case where the

Commission initiated a proceeding for the sole purpose of adopting rules of general applicability to the electric utility industry that would have only prospective effect. The proceeding was not an adjudication of a historical set of facts; the proceeding was not a "contested case" as that term is used in the Michigan APA. The MPSC is asking the Court to adopt an interpretation of the "contested case" exception in the Michigan APA that would effectively swallow up the general rule; i.e., an agency would never need to follow the rulemaking procedures specified in the APA if all it has to do is commence a proceeding that it labels a "contested case." Plainly, however, the legislature never intended for contested cases to be an alternative means of adopting rules; rather, the contested case exception was intended to allow for the case-by-case development of principles as discussed in SEC v Chenery, supra, in the context of the adjudication of specific factual disputes.[1]

4. The MPSC repeatedly argues that the fact that MCL 460.10a(4) does not specifically direct the Commission to follow the rulemaking procedure in adopting a code of conduct means that it was free to do so by commencing a proceeding it labeled a contested case. In support of this contention, it notes that other sections of 2000 PA 141 specifically state that the Commission "shall issue orders" to implement various features of the act. MPSC Brief, p. 14. But the "default option" in instances where the Legislature does not specifically direct the agency to act by rule or by order is not to allow the agency to invent its own procedure. The only lawful choice for the agency in such situations is to comply with the Michigan APA. Compliance with the rulemaking procedures specified in the APA is the

[1] In other contexts under 2000 PA 141, the MPSC has recognized the need to proceed by rulemaking. See January 29, 2004 Order Approving Administrative Rules in MPSC Case No. U-12270 (concerning Service Quality and Reliability Standards for electric distribution Systems) R 460.701 et seq; September 11, 2003 Order Denying Rehearing and Adopting Rules in MPSC Case No. U-13745 (Electric Interconnection Standards) R 460.481 et seq.

only lawful choice available unless the Legislature has specifically authorized the agency to act pursuant to some different procedure.

5. The MPSC cites a series of cases in support of its claim that the adoption of the code of conduct was the exercise of a "permissive statutory power" and therefore exempt from the definition of a rule in the APA pursuant to MCL 24.207(j). This rationale was briefly identified, but never adopted by the Court of Appeals. See Detroit Edison v Public Service Commission No. 1, 261 Mich App 1, 12; 680 NW2d 512, lv gtd, 688 NW2d 510 (2004). In any event, none of the cases cited by the MPSC support its position in this case.

MCL 24.207(j) exempts the following actions from the definition of a rule:

> "(j) A decision by an agency to exercise or not to exercise a permissive statutory power, although private rights or interests are affected."

Similar to its argument concerning the "contested case" exception, the MPSC asks the Court to interpret MCL 24.207(j) so broadly that it would effectively render the APA rulemaking requirements null and void. The MPSC basically argues that, as long as it has the statutory authority to adopt a code of conduct, MCL 24.207(j) allows it to do so in any manner that it chooses. The MPSC's argument would essentially eliminate any requirement to ever follow the APA rulemaking requirements, since an agency can obviously not take any action in the absence of statutory authority.

Plainly, MCL 24.207(j) was never intended to be interpreted so broadly. A more plausible interpretation would limit it to merely the threshold decision by an agency to "exercise or not to exercise" some permissive power. An example of this is Spear v Michigan Rehabilitation Services, 202 Mich App 1; 507 NW2d 761 (1993), which was discussed in Consumers Energy's Appellant's Brief at page 20. In that case, the threshold decision was

whether or not to adopt a "needs' test for determining eligibility for certain benefits. The Court held that the decision to adopt a needs test was the exercise of a permissive statutory power since it was not required to adopt such a test. That threshold decision itself was therefore not subject to APA rulemaking requirements. Once the decision had been made to adopt such a test, however, the specific needs test adopted was a rule, and the agency was required to follow the rulemaking procedures.

Applied to the instant appeal, the Commission is claiming not only that the threshold decision to proceed by order rather than by rulemaking was exempt under MCL 24.207(j), but in addition that the multitude of specific prohibitions and restrictions detailed in the six page, single-spaced code of conduct (see Appellant's Appendix, pp. 108a-113a) are also exempt from the definition of a rule pursuant to this subsection. Such a claim, if accepted, would render the rulemaking procedures of the APA null and void.

6. The Commission briefly and half-heartedly attempts to distinguish the decision in In Re Public Service Commission Guidelines for Transactions Between Affiliates, 252 Mich App 254; 652 NW2d 1 (2002) from the instant appeal. The Commission argues that, unlike the affiliate guidelines case, the Commission was under a statutory mandate to adopt a code of conduct.[2] The Commission never explains why this is a justification for the Court of Appeals' failure to follow the precedent established in the affiliates guidelines case. The Commission also argues that MCL 460.10a(4) required it to adopt a code of conduct "within 180 days" of the effective date of 2000 PA 141, and that such a requirement would have been impossible to meet had the Commission followed the rulemaking process. There is nothing in the APA rulemaking provisions, however, that dictates how long an agency must

[2] The Commission fails to note the conflict with its claim that the adoption of a code of conduct was the exercise of a permissive statutory power.

deliberate concerning a proposed rule. It is not at all obvious that following those provisions would inevitably take longer than 180 days. Further, as conceded by the Commission in its statement of facts, it was off to a head start in this case, having already conducted lengthy hearings at the time 2000 PA 141 was enacted and became effective. In any event, the claim that it might have been burdensome to comply with the rulemaking provisions of the APA hardly constitutes a lawful excuse to ignore their applicability.

7. The MPSC argues that addressing the issues presented in this appeal is unnecessary, because the Legislature "ratified" the Commission's actions in adopting the code of conduct when it passed 2004 PA 88. 2004 PA 88 is an amendment to 2000 PA 141 that added subsections (5) through (11) to Section 10a. See MCL 460.10a(5)-(11).[3] The second sentence of subsection (5) states that, "[e]xcept as otherwise provided by this section the utility shall comply with the code of conduct established by the commission under subsection (4)." The MPSC argues that this represents a legislative blessing of the procedure used by the MPSC in adopting the code of conduct, as well as of the substance of the code. This is an ambitious argument, to say the least, and there are multiple defects in the Commission's position. First, the cases cited by the MPSC all concern the effect of a re-enactment of statutory language that has previously been the subject of judicial interpretation. In this instance, however, the process of judicial review was still underway at the time 2004 PA 88 was enacted (and indeed, is still underway). Thus, there has been no judicial interpretation by a "court of last resort" as is discussed in the cases cited by the MPSC that could be said to have been ratified by the legislature. See Smith v Smith, 433 Mich 606, at

[3] The only changes to Subsection (4) were to change the phrase "[w]ithin 180 days after the effective date of the amendatory act that added this section," to "[n]o later than December 2, 2000," and to change a reference to "sections 10b through 10bb" to "sections 10b through 10cc."

637; 447 NW2d 715 (1989). Second, the legality of MCL 460.10a(4) is not at issue in this appeal. What is under challenge is the Commission's failure to follow the dictates of the Michigan APA. A re-enactment of MCL 460.10a(4) cannot reasonably be interpreted as a ratification of the procedure followed by the Commission in adopting the code. A more reasonable interpretation of the second sentence of new subsection (5) is merely that utilities are obligated to follow a code of conduct that is lawfully established under subsection (4). Third, the re-enactment rule relied upon by the MPSC is a limited tool of statutory interpretation that, in some circumstances, may be useful in determining legislative intent where statutory language is ambiguous. See Jones v Dept of Corrections, 468 Mich 646, 657-658; 664 NW2d 717 (2003). The MPSC's claim that this tool is helpful in interpreting the APA because 2000 PA 141 was amended is not consistent with even the most expansive applications of this rule. See People v Hawkins, 468 Mich 488, 508-509; 668 NW2d 602 (2003).

Respectfully submitted,

CONSUMERS ENERGY COMPANY

Dated: February 28, 2005

By: _____

Jon R. Robinson, Esq. (P27953)
John C. Shea, Esq. (P36854)
Attorneys for Consumers Energy Company
One Energy Plaza
Jackson, MI 49201
(517) 788-0698