

Chapter 2 – The Origins of MPPA

Pancaking Rates

Wholesale electric power rate increases for Michigan's municipal utilities came so fast and furious during the 1970s that public power utility managers had a term for the phenomenon. They called it "pancaking" rates. One rate case decision would still be pending at Federal Energy Regulatory Commission (FERC) while a new case would be filed. Thus, the rate cases were stacked up like pancakes.

The private companies who sold wholesale power to Michigan's municipal utilities were regulated at the wholesale level by FERC. The investor-owned utilities (IOUs) filed for rate increases with FERC, and normally they immediately became effective subject to refund after hearing. Hearings would often drag on for two to three years.

Meanwhile, the municipal utility not only had to pay the higher wholesale rate because the increase became effective – following a 30-day suspension – when filed, it also had to hire lawyers and consultants to represent the municipal utility owners by its citizen consumers before FERC in Washington, D.C. The legal and consulting costs in and of themselves were a significant expense for a small municipality. Therefore, the rate increase frequently delivered a double whammy on cost.

Before the case was decided at the FERC, the private utility often tacked on a second or third wholesale rate increase. This became known as pancaking. The IOU supplier would file a new rate which was higher

The quarter-century following World War II was an almost idyllic era for the nation's electric utilities. Technological advances made possible the construction of huge, new steam-turbines that were far more efficient and economical than their pre-war predecessors. Utilities could purchase baseload generation fuel cheaply from both domestic and foreign sources. Utilities on both coasts fired their generating station boilers with inexpensive crude oil from the Middle East and South America, while utilities in Michigan and the Midwest relied upon abundant resources of coal from Appalachia and the Illinois Basin. The size of new generating units more than tripled from 250 megawatts in 1953 to nearly 800 megawatts by 1970.

Transmission voltages increased and then increased again, allowing utilities to move massive blocks of electric power from generating stations to load centers and end-use customers. Research and development on extra high voltage (EHV) lines accelerated during the 1960s and 1970s. The first 500,000-volt lines in the United States began appearing in the mid-1960s.

In 1966, American Electric Power (AEP) announced that it would build a 1,000-mile-long backbone transmission system rated at 765,000 volts across its five-state service territory, including Michigan.¹ It took six years to complete the first stage of what AEP called its Ultra High Voltage (UHV) project.

Residential and commercial kilowatt-hour demand surged during the 1950s and 1960s. Fueled by pent-up demand for homes and appliances, electric power sales mushroomed during the postwar era. Kilowatt-hour growth averaged 8 percent a year from 1947 to 1973, essentially doubling every nine years during the period.²

Michigan's municipal utilities shared in the growth of the postwar period. Hillsdale installed new diesel generating units throughout the 1950s and 1960s to keep up with the growth of kilowatt-hour demand.³ In 1956, Zeeland's municipal utility announced a 44 percent expansion of its electric generating capacity, installing a diesel engine that was double the size of the last diesel added just after the end of the war in 1945.⁴ Traverse City placed in service at least one boiler, steam-turbine and substation in each decade between 1940 and 1970.⁵ In the late 1950s and again in the 1960s, Hart Hydro-Electric installed new, more powerful diesel engines at its plant.⁶ Charlevoix also added new diesel generators in the 1950s and 1960s to keep pace with surging kilowatt-hour demand.⁷

By the early 1960s, demand was outstripping supply for most of Michigan's municipal utilities. The state's major investor-owned utilities – Consumers Power, Detroit Edison and the Indiana & Michigan Power subsidiary of New York-based American Electric Power Corporation – were at the time in the midst of frenetic construction activity, building big new generating units and high-voltage transmission lines to serve swelling kilowatt-hour demand on their systems. In decades past, the investor-owned utilities (IOUs) had viewed Michigan's municipal utilities as competitors. Now they saw the public power entities as wholesale customers.

Beginning about 1960, the IOUs began offering their municipal utility neighbors attractive wholesale power contracts. The concept seemed to be a win-win arrangement for everybody.

The municipal utilities purchased low-cost power from the IOUs that they then slightly marked up to cover distribution and administrative costs and sold to their customers. Expensive diesel engines could consequently be idled or used as peaking units. The IOUs added bulk generation customers who could help pay for their new baseload power stations.

The situation might have continued indefinitely to the benefit of all had not economics and energy politics intervened after 1970. The wholesale contracts negotiated in the early 1960s set the stage for a transformation of the municipal utility business in the Wolverine State.

White Hats, Black Hats



The energy environment in the United States began to dramatically change in the late 1960s and early 1970s. Within a five-year period between 1968 and 1973, the nation's electric power industry underwent a series of unprecedented challenges.

Economies of scale in the industry had plateaued in the late 1960s. President Lyndon Johnson was trying to fight a war in Vietnam against the backdrop of a peacetime economy, and inflation began a steady rise in 1967 that wouldn't abate until the 1980s.

Landmark environmental legislation that sharply increased the cost of power plant and transmission line construction was passed by Congress in the early 1970s. Electric power costs to consumers increased an average of 80 percent between 1969 and 1977; in New York City, the rise was 171 percent for the same period.⁸ Kilowatt-hour costs began an upward spiral that would bedevil consumers through the present day.

The energy crises of 1973 and 1979 put upward pressure on the prices of coal, gas and oil burned in fossil fuel plants. Utilities with nuclear construction programs watched helplessly as project costs doubled and tripled in the late 1970s and early 1980s.

Interest and inflation rate increases, environmental costs, and rises in the price of fuel resulted in sharply higher electricity rates for America's consumers. For the first time since the end of World War II, Americans started using less electric power. Kilowatt-hour consumption kept increasing, but at an average annual rate well below previous years. By 1980, kilowatt-hour demand was growing at an average annual rate of 2.5 percent, a third of the rate of increase during the 1960s.⁹

Utility managers went from wearing white hats to black hats as rate increases came one after the other in the late 1960s and early 1970s. For Michigan's municipal utilities, the rate increases were particularly painful. Wholesale power rates in the state jumped by more than 40 percent between 1969 and 1973. The municipals were held hostage to rising fuel costs, general inflation, upward-moving interest rates and construction cost overruns at the power plants being built by the state's IOUs.

than the prior rate, the rate that was already being contested and liti-gated through regulatory hearings. The new rate, however, was effective subject to refund while the earlier increase was still being decided.

More often than not, the FERC commissioners ruled that the original rate was not completely justified. The municipal utility would receive a refund from the power supplier when FERC finally ruled on the case. In the meantime, the municipal utility was contesting the new case that was higher than the first unjustified rate increase.

The result was that Michigan's municipal utilities during the 1970s constantly experienced wholesale rate increases that were inevitably ruled unjustified and unreasonable as filed, although the system kept them in effect.¹ Pancaking also was a major reason that Michigan's municipal utilities made a concentrated effort in 1976 to secure joint action agency legislation from the Michigan statehouse. They were interested in fixing their cost by becoming an owner of generating plant and transmission systems. The experience was similar to leasing an apartment in which the landlord regularly raises the rent. The lessee, by taking out a mortgage and buying the house, ends up with a constant, known mortgage payment that is not going to increase over time.

Endnote

1. Gary Zimmerman Interview, p.9

Dave Naberhuis, MPPA's financial manager, first heard about the squeeze affecting the state's municipal utilities in the 1970s from his uncle, Marty Hieftje, longtime electric department superintendent at Zeeland. Hieftje told Naberhuis that the 1970s were a difficult time for municipal utility managers. Naberhuis recalled his uncle telling him that "inflation was driving everyone's cost through the ceiling and everyone was trying to cover costs. Things didn't get easy after that point in time."¹⁰



In the late 1960s, Consumers Power announced plans to build a mammoth nuclear power plant near Midland. Midland Unit No. 1 was rated at 533 megawatts and was scheduled to go into commercial production in 1974. Unit No. 2, which would follow the next year, was rated at 792 megawatts.¹¹ The Midland nuclear project would turn out to be the costliest utility gamble in the state's history, but at the time, nuclear power had the reputation of being an almost inexhaustible, inexpensive way to generate electricity.

In the 1960s, then Atomic Energy Commission (AEC) Chairman Glenn Seaborg predicted that nuclear energy would be "too cheap to meter." By 1970, the prediction seemed to be coming true.¹² More than 55 nuclear power plants were in operation or under construction, and an additional 60 plants were planned or had applied for construction permits from the AEC.¹³

In 1971, Marty Hieftje of Zeeland accompanied utility managers from Coldwater, Grand Haven, Traverse City and Holland to Jackson to discuss a potential ownership investment in the Midland nuclear project. The five municipal utility managers, as well as representatives of the state's two Lower Peninsula Generation and Transmission (G&T) cooperatives, Northern Michigan Electric Cooperative and Wolverine Electric Cooperative, reasoned that Consumers Power would welcome participation in the project, which was already estimated to cost upward of \$1 billion.

Consumers Power was not interested in having municipal utilities or G&T cooperatives participate in Midland. The attitude was that the municipals and the G&Ts could buy wholesale power from Consumers – at ever-increasing prices – but the customers should have no say in how those rates were set. Part of the problem was Consumers' lengthy history of adversarial relations with the G&T cooperatives, but the power company's outright refusal angered the municipal utility managers.

In 1972, the five municipal utilities and the two G&T cooperatives filed a federal antitrust suit against Consumers. The seven plaintiffs primarily asked for the right to participate in the Midland project as part owners. But the plaintiffs, the G&T cooperatives in particular, also wanted Consumers Power to join with them in statewide energy planning, including allowing the public power entities to transmit, or "wheel," power across Consumers Power's high-voltage transmission grid.¹⁴

Robert Jablon of the Washington law firm of Spiegel and McDiarmid represented the Michigan municipal utilities in the antitrust suit. Hearings before the AEC's Atomic Safety and Licensing Board consumed much of 1973 and 1974. Donald Potter, the longtime executive vice president of the Michigan Municipal Electric Association (MMEA) in East Lansing, noted in 1978 that the antitrust suit kicked off a series of long, complicated negotiations between the municipal utilities and Consumers Power.¹⁵ MMEA is a trade association that represented most of Michigan's municipal utilities. For much of the 1970s, MMEA was instrumental in providing the administrative leadership for the fight to create joint action agencies in Michigan.



Joint Action

One of those complicated actions involved the lengthy struggle to convince the state of Michigan to allow municipal joint action agencies in Michigan. Joint action agencies were increasingly common by the 1970s. The state of Washington had authorized the nation's first joint action agency in 1957, and in the 1960s, Arizona, California, Iowa and South Dakota approved the formation of joint action agencies.¹⁶

The concept of a joint action agency was simple. Most municipal utilities were too small to build or buy into a large baseload generating plant. But if a number of those municipal utilities could pool their electric loads and their financial resources, then ownership of baseload generating capacity was a distinct possibility. With the antitrust suit against Consumers Power winding its way through the bureaucracy of the AEC, Michigan's municipal utilities began lobbying the Michigan Legislature for passage of joint action agency legislation.

Two of the strongest proponents of the legislation were Joe Wolfe, then general manager of the Traverse City utility and a prime mover in the antitrust suit, and Earl Brush, the crusty general manager of the Lansing Board of Water and Light.¹⁷ In 1972, a prototype joint action agency failed in the Michigan House by one vote. Legislative maneuvers between 1973 and 1975 produced legislation that modified bonding laws to allow municipal utilities to issue revenue bonds for power plant projects. But as the 1976 session of the legislature got underway, there was still no agreement on a joint action agency bill.¹⁸



SB 1539

Leading the charge for the passage of joint action agency legislation in the 1976 session was Don Potter, MMEA's executive vice president. Potter, who would run MMEA from an office in his home from 1961 to 1989, was a fixture at the statehouse. Michigan municipal utility managers still talk about Potter's Rolls-Royce with its fully-stocked bar.¹⁹ Potter knew every legislator in the state, from Eagle Harbor to Ann Arbor, and during the 1976 session, he talked to every legislator he knew.

Assisting Potter in the accelerated effort to get joint action agency legislation passed was Seth Burwell, a distinguished Lansing attorney.²⁰ Potter and Burwell drafted a 50-page law modeled on the recently enacted North Carolina joint action agency legislation. Lobbyists from Consumers Power and Detroit Edison were as fully committed to killing the bill as Potter, Burwell and the MMEA were to passing it.

In October 1976, Senator Anthony A. Derezinski's Committee on Corporations and Economic Development sent Senate Bill 1539 to the full Senate with a recommendation of passage. In one short paragraph, SB 1539 outlined a sea change in how electric power would be generated, transmitted and distributed in Michigan.

SB 1539 was described as "a bill to prescribe the powers and duties of municipalities and governmental units to acquire, finance, maintain, and operate generating, transmission, and distribution facilities of electric power and energy, fuel and energy sources and reserves and all necessary related properties, equipment and facilities; to permit the exercise of those powers

Chapter 2 Endnotes

1. Corbitt, And There Was Light, p.561
2. Growth, <http://www.americanhistory.si.edu/csr/powering/hirsh2/frmain.htm>
3. Taylor, "The Hillsdale Municipal Electric Utility," *MMUA Newsletter*, August 31, 1955, p.4
4. "Zeeland Plans 44% Expansion," *MMUA Newsletter*, April 2, 1956, p.1
5. "Statistics of the Traverse City Electric Plant," *MMUA Newsletter*, October 31, 1955, p.4
6. Passage, "Report on the Hart Hydro-Electric," *MMUA Newsletter*, September 10, 1955, p.8
7. "Charlevoix Expands," *MMUA Newsletter*, February 25, 1956, p.4
8. Richard F. Hirsh, Technology and Transformation in the Electric Utility Industry (Cambridge and New York: Cambridge University Press, 1989) pp.128-129
9. *Ibid.*, p.159
10. Tape-Recorded Oral History Interview with Dave Naberhuis, Lansing, Michigan, December 19, 2002, p.9
11. Raymond Miller, The Force of Energy: A Business History of the Detroit Edison Company (East Lansing: Michigan State University Press, 1971), p.212
12. Beck, PP&L: 75 Years of Powering the Future (Allentown, Pennsylvania: Pennsylvania Power & Light Company, 1995), p.316
13. *Ibid.*, p.386
14. Rodney Bailey, "An Analysis of Northern Michigan and Wolverine Electric Cooperatives and the Circumstances Behind Their Nuclear Power Partnerships with Investor-Owned Utilities in Michigan," in Jack Doyle,

Lines Across the Land: Rural Electric Cooperatives – the Changing Politics of Energy in Rural America (Washington, D.C.: The Rural Land & Energy Project/ Environmental Policy Institute, 1979), p.428

15. News Item, *Michigan Municipal Electric Association Newsletter*, August 1978, p.1; Hereinafter Cited as *MMEA Newsletter*

16. Mark McCain, "Sum of Their Efforts," *Florida Municipal Electric Association Relay*, May-June 2003, p.20

17. "How One Bill Became Law," *MMEA Newsletter*, December 1976, p.1

18. *Ibid.*, p.2

19. Tape-Recorded Oral History Interview with Gary Zimmerman, Lansing, Michigan, December 18, 2003, pp.9-11

20. "How One Bill Became Law," *MMEA Newsletter*, December 1976, p.2

21. News Item, *MMEA Newsletter*, November 1976, p.1

22. *Ibid.*, p.1

23. "How One Bill Became Law," *MMEA Newsletter*, December 1976, p.2

24. *Ibid.*, pp.6-7

in joint venture or joint agency agreements; to provide for the issuance of bonds and notes; to prescribe the powers and duties of the municipal finance commission and certain other state officers and agencies with respect to municipal electric utility financing; to create certain funds and prescribe their operation; and to provide for tax exemptions and other exemptions."²¹

Potter mobilized all 35 members of MMEA to contact their elected representatives in Lansing to urge passage of the landmark energy independence legislation. "Contact anyone who you think can help MMEA in the passage of this vital bill," Potter wrote members in November 1976. "We have worked too hard and come too far to lose this bill now through lack of effort. Time is short."²²

Once in the full Senate, the bill faced stiff opposition from the investor-owned utilities (IOUs). On November 19, 1976, Consumers Power's lobbying firm presented 52 proposed amendments to the bill, all but gutting it of joint agency and finance provisions. Potter and Burwell worked over the weekend and reduced the amendments to 13, keeping the all-important joint agency and bonding sections. Senator James DeSana of Wayne County carried the bill to the floor of the Senate on Tuesday, November 23, and it passed 35-0, with three members absent or not voting.²³

Following a Thanksgiving adjournment, the Michigan House returned in early December to debate the bill. Opponents kept trying to add amendments that would negate the intent of the bill. At a Public Utilities Committee hearing, the state's deputy treasurer urged that the bill be postponed until the 1977 session of the Legislature. Fortunately, Committee Chairman Gerrit "Barney" Hasper ruled that SB 1539 would be voted up or down in the next week to 10 days.

In lengthy meetings, committee members agreed to strike Article 4 of the bill, eliminating the provision for state funding for joint ventures. Potter and the Michigan municipal utility advocates reluctantly agreed to the change, and pressed Hasper to release the bill to the full House.

When he did, opponents made one last ditch attempt to kill the bill. On December 14, House Floor Leader Joe Forbes moved to suspend the rules and take up debate on the legislation. Lansing Representative David Hollister immediately offered an amendment to limit joint ventures to non-nuclear projects. Hollister's amendment was defeated by a 60-25 margin. One other amendment to limit the bill to existing municipal electric utilities was introduced. When it was handily defeated, Forbes moved that the bill go to a vote of the House. Some 30 minutes later, SB 1539 passed 81-11.²⁴

The next day, the House version of SB 1539 crossed the aisle to the Senate, where DeSana moved an immediate vote on the House amendment. The amended legislation passed unanimously and was sent to Governor William G. Milliken, who signed it a few days before Christmas. Now officially called Public Act 448 of 1976, the joint action agency legislation ushered in a new era for Michigan's municipal electric utilities.

Before the next year ended, Michigan's public power community would receive even better news from the Atomic Safety and Licensing Board.