STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of Michigan Consolidated Gas Company to terminate the suspension of its Gas Cost Recovery Clause and establish a cash-out mechanism.	)))))	Case No. U-12762

INITIAL BRIEF OF ASSOCIATION OF BUSINESSES ADVOCATING TARIFF EQUITY

The Association of Businesses Advocating Tariff Equity ("ABATE"), by its attorneys, Clark Hill P.L.C., submits its Initial Brief pursuant to the abbreviated schedule established for this case.

I

INTRODUCTION

This is a case about budgets and the allocation of risk between shareholders and customers. The budget aspect is evidenced by the Rule 207 Statement by Mr. Larry Ladomer of Blue Circle, Inc. There is a concrete example of how at least this corporation built a budget based upon an understanding that the cost of natural gas during 2001 would be $2.95 per Mcf. In fact, all of the available information leads one to the inexorable conclusion that there was a price guarantee through the end of this year. Statements found in MichCon's Application in Case No. U-11682, the statements in the Michigan Public Service Commission's ("Commission" or "MPSC") order approving the program outlined in the Application and even the Commission's Web site which flatly states that the price of natural gas will be $2.95 per Mcf until the end of 2001 (http://cis.state.mi.us/mpsc/gas/choicemc.htm) support there was a guarantee that the price of gas was fixed for 2001.

MichCon would like to get out of this guarantee and terminate its program nine months early and implement a GCR factor of $5.17 per Mcf as offset by certain credits. If approved, the evidence shows that the price of natural gas would exceed $2.95 per Mcf during 2001. MichCon's position is supported by one marketer who claims higher prices are needed in order to spur "competition".

On the other side of the issue are the customer groups and MPSC Staff which unanimously take the position that the cost of gas should be $2.95 per Mcf for 2001 regardless of whether the Application is rejected or, in the case of the Staff, it is approved with modifications. It is ABATE's position that MichCon's proposed termination of the suspension of its GCR clause should not be approved and that MichCon be required to maintain this suspension through December 31, 2001 as it had originally proposed. It is obvious that during the early part of the suspension period, MichCon made approximately $70 million by having its GCR factor frozen and now that the suspension has turned unfavorable, MichCon seeks to lift it.

ABATE also opposes, MichCon's proposal to sell its below market gas contracts. It is incumbent upon gas utilities, such as MichCon, to manage their gas costs and risks associated with service to bundled customers. Most of MichCon's bundled service customers are not in the position to manage their gas costs or hedge their risks and, by a necessity, this function must remain with MichCon. The existence of retail open access does not affect this fundamental utility responsibility. If this responsibility is allowed to change, then ABATE requests the Commission to require MichCon to file a rate case to examine the appropriate level of MichCon's rate of return on common equity.

As will be set forth below, the great weight of the evidence requires the MPSC to either dismiss the Application or approve the Application with the price guarantees proposed by Staff. Of the two alternatives available to the Commission, ABATE urges the Commission to dismiss the Application because this is consistent with MichCon's initial proposal approved by the MPSC and it eliminates the time and effort that would be needed to monitor the price guarantee proposal. Dismissal of the Application will preserve the price of natural gas that customers were counting on. Finally, the sale of the contracts, even with the price guarantee, would suggest that the MPSC is allowing MichCon to eliminate its responsibility to manage gas costs for its customers. The MPSC should empathically reject this approach.

II

ARGUMENT

A. THE COMMISSION SHOULD REJECT MICHCON'S APPLICATION.

1. MPSC Staff.

Staff witness Aldrich testified that he would support MichCon's Application but only if the refund calculation is modified to include the additional gas cost paid by GCC customers and if MichCon is required to guarantee all of its GCR and GCC customers would pay no more than $2.95 per Mcf for April-December, 2001, billed sales, as adjusted for credits received during the period April 2001 through March 2002. 3 TR 203. ABATE certainly agrees with the result of this proposal, however, it appears to be overly complicated and the same result could be accomplished if the Commission simply were to reject MichCon's Application. In addition, ABATE has read the Residential Ratepayers Consortium's ("RRC") Motion and Brief in Support related to the dismissal of the case because Act 304 requires a 12 month GCR period, not the nine months as set forth in

MichCon's Application and the Commission can avoid this additional legal issue simply by rejecting the Application as opposed to adopting the Staff's adjustments. Finally, there is one small cash flow problem with the Staff approach which is that customers may not be made whole until March 2002 or thereafter. This problem can be avoided by simply rejecting the Application.

2. Attorney General.

The Attorney General's witness, Mr. Miller, recommended that the Commission simply reject MichCon's Application. He found that MichCon's proposal had two principal defects which justified the Commission rejecting MichCon's Application:

> "First, if MichCon's proposal is adopted, then it is likely that customers will pay many millions of dollars more than the promised price of $2.95 per Mcf for gas purchased from MichCon in the last nine months of 2001. Customers will end up paying more than $2.95 because it is likely that the combination of MichCon's proposed cash-out credits and the additional 'reconciliation' refund of gross margins will together be less than the difference between the GCR rate for the last nine months of 2001 and the promised $2.95 price. . . .
>
> The second defect in MichCon's proposal is the timing of the effective gas commodity rate changes that would result if it is implemented. There would be an immediate rate increase of $1.31 per Mcf in April 2001 under MichCon's own base case assumptions, and a larger increase with more realistic NYMEX prices. This immediate rate increase would provide an over-collection of much more than $100 million above the promised gas price of $2.95 for the last nine months of 2001. Then, in January 2002, the gas commodity price paid by MichCon's customers would decrease if - as appears likely - MichCon's gas supply costs are less in 2002 than for the last nine months of 2001. This lower rate would continue at least until the cash-out credits are exhausted in March of 2002, and it would continue even longer if there is a 'reconciliation' refund. If the reconciliation refund is large enough to achieve the promised gas price of $2.95 for the last months of 2001, then it would be likely to have to run through most of the summer of 2002 under MichCon's pricing plan. At that time, when the last of the refunds was

> completed, the effective gas commodity price would again increase." 3 TR 156-7.

Mr. Miller also addressed the arguments made by MichCon and Energy America that the reimposition of the GCR clause and factor as proposed by MichCon would lead to increased competition and was in the public interest. Mr. Miller testified that termination of MichCon's GCR suspension will not lead to increased competition:

> "(2) Early termination of the GCR suspension will not promote gas supply competition in Michigan. It will not lead to increase gas supply competition during the last nine months of 2001, except perhaps at the expense of MichCon's customers who would be forced to pay more than $2.95 per Mcf for their gas purchases during this period. Also, moving the termination date of the GCR suspension up from December 2001 to March 2001 will not provide any benefits for competition in 2002 and beyond." 3 TR 139.

According to Mr. Miller:

> "Competition does not benefit consumers unless it is expected to lead to lower prices or improved products and services." 3 TR 171.

In his opinion, MichCon's proposal for an early termination would have exactly an opposite effect because it would force GCR sales customers to pay prices which were higher than the $2.95 price established for the remainder of the year. Id. Moreover, competition beginning April 1 through the end of the year, would not provide any economic benefits, just economic losses, because of the higher prices customers would be forced to pay. Id.

Mr. Miller also testified that an early termination of the suspension of the GCR factor would not result in uniformity of the gas pricing practices of MichCon and Consumers Energy for a variety of reasons including Consumers proposed use of a $1.00 per Mcf volatility factor, the difference in the total GCR factor, different gas purchasing strategies and different methods for accounting for storage. Consequently, there is no justification for the early termination of the suspension based upon achieving uniformity of pricing.

3. **Residential Ratepayer Consortium**.

Mr. Hollewa testified on behalf of the Residential Ratepayer Consortium and his testimony added weight to the outcome that MichCon's Application should be rejected. He said it was self serving for MichCon and marketers to claim that the $2.95 fixed price is a deterrent to choice, that irreparable damage may be done to the GCC program because no new customers are participating and that the suspension of the GCR clause should be terminated to coincide with the reinstatement of Consumers Energy Company's GCR on April 1, 2001. 3 TR 109. He further testified that customers would be much better off by retaining the $2.95 fixed price than adopting MichCon's proposal:

> "MichCon's sales customers are currently in a position where most of them (especially commercial) did not or could not avail themselves of the incremental savings achieved by choice customers in 1999 and 2000 because of enrollment limits in the GCC program. However, they are now in a position where the selection of a supplier (choice) is far less important than the continuation of a fixed price that is extremely advantageous and beneficial to them. Can any logical person believe that a survey of customers would be necessary to determine whether choice at $5.00 per Mcf is preferable to a fixed price of $2.95 from MichCon? Why would anyone want choice simply for the sake of choice?" Id.

Mr. Hollewa gave absolutely no credence to MichCon's argument that the termination of the suspension was necessary in order to jump start MichCon's GCC program because, in his opinion, the move to customer choice would take years, not months to accomplish. Id.

Mr. Hollewa criticized MichCon's cash-out proposal because it would provide benefits to all customers and not just GCR customers. He suggested that the GCC participants were already benefitting from lower prices and should not receive any cash-out payments should they be approved by the Commission. 3 TR 110. He also criticized MichCon's cash-out mechanism which would not make funds available to customers until April, 2002. If that is the case, customers during 2001 must necessarily pay a unit cost of gas which is higher than the fixed price of $2.95. Another problem that Mr. Hollewa had was that the NYMEX prices quoted by MichCon had a undetermined origin which made MichCon's analysis suspect. 3 TR 113.

In summary, Mr. Hollewa did not believe MichCon's assertion that there was a strong probability that MichCon customers would pay $2.95 or less:

> "[Mr. Stanczak] is incorrect when he states that there is a high probability that customers will not pay more than $2.95 per Mcf rate during the last nine months of 2001 (P. DMS-13, lines 10-14)." 3 TR 115.

Mr. Hollewa also took exception to MichCon's analysis regarding decrimenting storage. He said that it was virtually impossible to decrement storage absent the termination of the GCR suspension. Further, decrimenting storage, as MichCon proposed, would act as a deterrent to competition in 2001 or 2002. 3 TR 120.

Mr. Hollewa urged the Commission to reject MichCon's Application:

> "The Michigan Public Service Commission should reject the company's Application and require continuation of the $2.95 gas commodity rate through December 2001. In my opinion, the value of a fixed $2.95 rate for the majority of MichCon's customers out weights the policy concerns underlying the company's proposals for jump starting its gas customer choice program in April 2001 for a minority of its customers." 3 TR 121.

B. **<u>MICHCON'S PROPOSAL IS UNFAIR TO CUSTOMERS</u>**.

Mr. Miller discussed why MichCon's proposal was unfair and why, if the Commission approved the termination of the suspension that modifications should be made. He noted that the MichCon proposal was asymmetrical in that the risk that price of gas over the last nine months of 2001 could exceed $70 million and that customers could actually pay a higher amount than the fixed price of $2.95. On the other hand, if the price of natural gas did not eat up the $70 million, then MichCon would retain the benefits. 3 TR 163.

If the suspension is terminated then ABATE supports the program modifications supported by Mr. Miller beginning at 3 TR 168. ABATE agrees that a general progression of rate increases is preferable to MichCon's proposal which has retail rates going up and down and then up again.

C. **<u>MICHCON'S HIDDEN PROPOSAL TO TERMINATE GCC CONTRACTS EFFECTIVE APRIL 1, 2001 IS OUTRAGEOUS</u>**.

Although there is nothing in MichCon's Application or testimony, it came out through cross-examination that MichCon's plan is to require GCC participants to terminate their contracts with their existing suppliers and re-enroll in the new program effective April 1, 2001. 3 TR 65. This proposal was completely unknown to the parties until cross examination because some of the witnesses even suggested that it was illogical to feedback the credits to GCC customers. Now we understand why MichCon was proposing to do exactly that.

ABATE opposes any attempt by MichCon to deprive existing customers of the benefit of their bargain with their gas suppliers. The Commission should be very careful and not create an event of *force majeure* that would allow suppliers to void their contracts with GCC participants. If these customers wish to terminate their contracts, they should negotiate with their suppliers, but in no event should termination be mandatory.

D. **LEGAL STANDARD**.

If the GCR factor had not been suspended then one of the criteria for reviewing a plan is found in MCL 460.6h(6): "... whether the utility has taken all appropriate legal and regulatory actions to minimize the cost of purchased gas; . . . " ABATE submits that this standard can still be used by an analogy and it is clear from the evidence in this case that the only way to guarantee that customers will pay $2.95 per Mcf during 2001 is to dismiss MichCon's Application.

Another a possible legal standard for judging MichCon's proposal is found in Section 22 of the Railroad Act. This Section states the Commission is authorized to change rates if they are found to be "unreasonable, inadequate or unjustly discriminatory". MCL 462.22(a). Clearly, $2.95 per Mcf fixed price is reasonable for customers in today's gas market.

An argument can also be made that MichCon waived the right to seek further and additional relief from the Commission as a result of the statements made in its Application in Case No. U-11682. MichCon's Application stated:

> "19. Over the last three years, the natural gas market has become increasingly volatile, often experiencing wide fluxuations in market prices with corresponding changes in MichCon's market-sensitive GCR factor. . . .
>
> 20. . . . A stable commodity rate will provide customers who choose MichCon as their natural gas supplier with price certainty, an easy means of comparing alternative gas supply offers, and afford the Company the purchasing and operational flexibility necessary to support customer choice.
>
> 21. In proposing a fixed gas commodity rate of $2.95 per Mcf, MichCon recognizes that it will also assume significant risks.

> Portions of the Company's gas supply contract costs could be unrecoverable." Application, U-11682, pp. 12-13.

Based upon these statements, it is clear that MichCon waived any cause of action deemed to change the price guarantee of $2.95 per Mcf at the end of 2001.

III

RELIEF

WHEREFORE, ABATE requests that the Commission reject MichCon's Application and grant such other relief as is just and reasonable.

Respectfully submitted,

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PROOF OF SERVICE

STATE OF MICHIGAN)
)
COUNTY OF OAKLAND)

Lisa Ann Teets, being first duly sworn, deposes and says that she filed electronically a copy of the attached "Initial Brief of Association of Businesses Advocating Tariff Equity" in the above docket on the persons identified on the attached service list by depositing the same on March 2, 2001, in the United States mail in the City of Birmingham, Michigan with first-class postage thereon fully paid.

Lisa Ann Teets

Lisa Ann Teets

Peggy A Green

Notary Public, Oakland County, Michigan
My Commission Expires 8/18/03

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