

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for accounting and ratemaking approval)
of depreciation rates for gas utility plant.)
_____)

Case No. U-12999

NOTICE OF PROPOSAL FOR DECISION

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on June 28, 2004.

Exceptions, if any, must be filed with the Michigan Public Service Commission, P.O. Box 30221, 6545 Mercantile Way, Lansing, Michigan 48909, and served on all other parties of record on or before July 12, 2004, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before July 26, 2004. **An original and four paper copies and an electronic copy in the portable document format (PDF) of either document are necessary to meet proper filing requirements, as well as proof of service on all other parties of record.**

At the expiration of the period for filing of exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for

Decision is reviewed by action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before they are due.

MICHIGAN PUBLIC SERVICE COMMISSION

Daniel E.
Nickerson, Jr.

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Daniel E. Nickerson, Jr.
Administrative Law Judge

June 28, 2004
Lansing, Michigan
dp

STATE OF MICHIGAN
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HISTORY OF PROCEEDINGS

I.

HISTORY OF PROCEEDINGS

On June 29, 2001 Consumers Energy Company (Consumers Energy) filed an application with the Michigan Public Service Commission (Commission) seeking approval for accounting and ratemaking depreciation rates for gas utility plant. Based upon an updated filing, the request is for an increase in annual depreciation expense in the amount of \$11.9 million.

The Commission issued a notice of hearing on July 13, 2001. On August 16, 2001 a prehearing conference was held before Administrative Law Judge Daniel E. Nickerson, Jr. (ALJ). Consumers Energy was represented by attorneys Richard Chambers, Jon Robinson and John Shea. The Attorney General (AG) was represented by Assistant Attorney General Donald E. Erickson. The Association of Businesses Advocating Tariff Equity (ABATE) was represented by attorney Robert A. W. Strong. The Commission Staff (Staff) was represented by Assistant Attorneys General Larry G.

Watterworth and Steven Hughey. Petitions to intervene filed by ABATE and the Attorney General were granted.

On November 6, 2001 a hearing was held. The parties agreed to waive cross-examination and the testimony of Consumers Energy's witness Donald S. Roff was bound into the record and exhibits A-1, A-2 and I-3 were admitted into evidence. On November 30, 2001 Staff filed two motions; one of the motions requested a suspension of the proceedings. On December 7, 2001 a motion hearing was held. Staff agreed to withdraw its two motions and the parties agreed to an indefinite suspension of the proceedings with the understanding that any party could seek resumption of the proceedings for good cause and that the case schedule would resume not later than October 2003. The parties also agree that depreciation rates could be synchronized with retail rates with proposals from the parties concerning the method of synchronizing the rates for revenue requirement purposes.

Almost two years later, on October 14, 2003 a second prehearing conference was held. A schedule for resuming the proceedings was adopted. Consumers Energy filed updated testimony and exhibits based on December 31, 2002 plant balances plus an additional two years of historical data including the consolidation of Michigan Gas Storage Company.

On March 10, 2004 a hearing was held. The parties agreed to waive cross-examination of all witnesses. The testimony of all witnesses was bound into the record and all the proposed exhibits were admitted into evidence.

The record consists of five volumes of transcripts totaling 209 pages and 33 exhibits admitted into evidence. Briefs and reply briefs were timely filed by Consumers Energy, Staff, the AG and ABATE.

II.

DISCUSSION

Consumers Energy's depreciation study, as filed with the application, had been conducted using data as of December 31, 2000. An updated depreciation study was conducted by the accounting firm of Deloitte & Touche LLP using data as of December 31, 2002 for Consumers Energy's gas utility plant. It also reflects the consolidation of Michigan Gas Storage Company into Consumers Energy Company. Consumers Energy explains that its depreciation study involved four steps using data, analysis, evaluation and calculations. The four steps of analysis involved:

1. Life Analysis;
2. Salvage and Cost of Removal Analysis;
3. Evaluation of Analysis Results and Determination of Mortality Characteristics; and;
4. Calculation of Applicable Depreciation Rates.

Using straight line depreciation, Consumers Energy calculated its required annual accrual using the following formula found in Exhibit A-5, p 9:

$$\text{Annual Accrual} = \frac{\text{Plant Balance} \times (100\% - \text{Net Salvage } (\%)) - \text{Book Reserve}}{\text{Average Remaining Life (Years)}}$$

$$\text{Rate } (\%) = \frac{\text{Annual Accrual} \times 100\%}{\text{Plant Balance}}$$

Including Consumers Energy's proposed depreciation expense, the parties have presented a wide range of recommended depreciation expense. The current

depreciation expense¹ of \$107,995,903 is calculated based upon plant balance at December 31, 2002 of \$2,408,904,231. Exhibit A-11. The following is a summary of the recommended range of depreciation expense taken from Exhibit A-6 and Appendix B (Consumers Energy Initial Brief):

<u>Party</u>	<u>Depreciation Expense (millions)</u>	<u>Percentage Change²</u>
Detroit Edison	\$119.944	+11%
Attorney General	\$55.9	-48.2%
Staff	\$70.5	-34.7%
ABATE	\$35.3	-67.3%

Essentially, there is no dispute regarding determinations of average life and retirement dispersion curves. The main areas of disagreement among the parties involve whether to continue to use the Average Life Group procedure or switch to the Equal Life Group procedure in setting depreciation rates and the proper method for the determination of net salvage value.

Average Life Group v Equal Life Group

Consumers Energy proposes to switch to the Equal Life Group (ELG) procedure for use in setting depreciation rates. Staff, the AG and ABATE oppose the proposed change to ELG and recommend continuing use of the Average Life Group (ALG) procedure. The significant difference between the two procedures is the treatment of the depreciable assets within a designated group. Under ELG, assets within a group have different service lives and the different service lives are taken into account when depreciation rates are developed. Under ALG, all assets within a designated group are assumed to have the same average service life.

¹ The current depreciation expenses were approved by the Commission in MPSC Case No. U-11590, dated December 7, 1998.

² The percentage change is calculated from the current annual depreciation expense of \$107,995,903.

Consumers Energy believes that ELG method coupled with the remaining life technique provides for full recording and cost allocation over the remaining life of depreciable property and improves the match between actual property consumption and booked depreciation. Consumers Energy relies on its witness Donald S. Roff to explain several key aspects of ELG and remaining life technique. Mr. Roff testified concerning the remaining life technique which is not in dispute but is nonetheless a critical component in calculating depreciation expenses:

The remaining life technique compensates for any past over- or under-accruals of depreciation and plant and reserves transactions different from those anticipated by the mortality characteristics used to calculate the existing rates. The remaining life technique also limits depreciation to the utility's investment, net of expected salvage and cost of removal – no more and no less. 5 Tr 77.

Mr. Roff describes ELG as providing the correct depreciation rates equivalent to what the combination of depreciation rates would be if each asset were to be depreciated separately. Mr. Roff denies that ELG is a form of accelerated depreciation. He states, "There is no acceleration of depreciation. ELG is, in my opinion, a superior procedure." 5 Tr 71. He further explains that ELG better matches expenses with the consumption of assets or revenues produced by the assets. The term used to describe this matching of expenses and assets used by Mr. Roff is intergenerational customer equity. He explains:

Intergenerational equity means the costs are borne by the generation of customers that caused them to be incurred and not by some earlier or later generation. This matching is required to ensure that charges to customers reflect the actual cost of providing service. 5 Tr 73.

Mr. Roff also presented a table illustrating an example of the comparison of ELG and ALG. 5 Tr 70.³ The table shows a comparison of ELG and ALG based on a hypothetical of two assets both installed in the same year each costing \$10.00. Asset A is assumed to have a life of two years and asset B is assumed to have a life of eight years. Under ALG, the average life of the two assets is 10 years which then determines the annual accrual amount. Under ELG, each asset retains its own expected use life which then determines the annual accrual. According to Mr. Roff, this table, comparing the two methods, shows that ELG maintains the useful life characteristic of the asset thus there is no average life. While both procedures provide for the full recovery of the initial \$20.00 investment, Consumers Energy believes its comparison shows ALG results in an actual deferral of recovery when compared with ELG.

ELG is preferred by Consumers Energy because it contends that ELG: “(i) provides a proper matching between asset consumption and depreciation; (ii) depreciates each asset correctly over its expected life and (iii) results in lower total life revenue requirements.” Consumers Energy criticizes ALG because it: “(i) results in a deferral of recovery for short-lived assets and (ii) requires an over-accrual of depreciation for long-lived assets to make up for under accrual of short-lived assets.”

Staff disputes Consumers Energy claims regarding the advantages of ELG versus ALG. According to Staff, the ELG is not appropriate for Michigan and excess depreciation would result from adopting ELG. Staff seeks to show this excess depreciation through the same comparison presented by Consumers Energy witness Mr. Roff. Staff observes that the comparison submitted by Consumers Energy shows a cumulative depreciation expense which exceeds the cost of plant. Staff contends that

³ Consumers Energy also presented a slight variation of the table in its reply brief at page 11.

the problem with ELG is that there is no mechanism for reducing the depreciation rate after the first two years. Staff prepared a table (in its brief) showing its point. According to Staff, the cumulative depreciation expense results in an overrecovery of plant costs over the eight year period while at the same time ALG works perfectly recovering the exact cost of plant.

The AG recommends the continuing use of ALG over that of the ELG. The AG notes ELG accelerates the depreciation on short-lived assets while deferring the depreciation on long-lived assets. However, the AG is concerned because ELG groups are not tracked separately as sub accounts and no record of actual retirements are maintained for each group. The AG points out that not all vintage of plant throughout the history of the depreciable plant contain the same amount of investment which tends to make the ALG and the ELG offset depreciation expense of short-lived and long-lived assets. However, utility systems grow and inflation causes recent vintages to contain more investment than older vintages thus skewing ELG toward accelerated depreciation and overrecovery when compared with ALG.

Also, Consumers Energy structures and improvements accounts do not retire continuously i.e. Consumers Energy's transmission mains account 367 shows no even pattern over time \$1,800 for retirements in 1999; \$29,195 in 2000; \$216,119 in 2001; \$216,119 in 2001 and \$0 in 2002. The AG further notes the accelerated aspect of the ELG procedure. According to the AG, the depreciation rates decline for each vintage every year so the following years' depreciation rate is higher than the depreciation rate for that vintage year for the year following.

ABATE also opposes the adoption of ELG. ABATE concurs with Staff's observations concerning the overrecovery flaw in ELG. ABATE expounds that since depreciation rates are not changed annually ELG results in overrecovery of depreciation expense. ABATE also criticizes ELG because it lacks flexibility should assumptions deviate from forecasts. ABATE asserts forecasts regarding consumption or use of plant become increasingly inaccurate as the service life of an asset increases. ELG is unrealistic in its attempt to precisely allocate consumption of assets over time. ABATE is concerned that the use of ELG is administratively more cumbersome requiring the Commission to spend more time examining depreciation expense than it now does. ABATE calculates that ELG results in depreciation expense being \$16.618 million higher than the ALG calculation due to the accelerated nature of the accounting of depreciation expense of ELG.

The ALJ finds that Consumers Energy has not been persuasive in its presentation of ELG as a more appropriate procedure than the currently in use ALG for the use in depreciation of gas plant. While ELG and ALG are both designed for complete recovery of the asset, the ALJ finds ELG is front-loaded in terms of the amount of the recovery. Consumers Energy's position that ALG is a deferred method and therefore ELG only corrects the deferral aspect of ALG is unconvincing. A review of the comparison of ELG and ALG shows this front-loading in actual operation. Other than Consumers Energy's presentation of Mr. Roff's testimony there is no further substantiation for Consumers Energy's claims.

The ALJ disagrees with Consumers Energy's assessment that ALG is a form of deferred depreciation; there is nothing in the record to support such an assertion. A

comparison of the annual accrual of ELG and ALG is also unpersuasive inasmuch as the difference can be explained, as argued by the parties in opposition, that ELG may be appropriately termed a form of accelerated depreciation.

ELG has been adopted by the Federal Communications Commission (FCC) in telecommunications cases⁴, there has been no credible showing here that it is suitable for application in depreciation of gas utility plant. In adopting ELG the FCC has required a triennial represcription study every three years to maintain integrity of ELG by reflecting changed parameters and declining plant depreciation rates. A similar represcription review has not been proposed in this case. In fact, the next depreciation case filing as proposed by Consumers Energy would be 2010, over five years from now. Also, the ALJ believes telecommunications assets are subject to faster obsolescence due to more rapid technological development which is inherently different than assets used in gas plant service where technological obsolescence is not as great a concern.

The ALJ further agrees that the adoption of ELG would administratively prove more cumbersome. ABATE's point regarding forecasts becoming increasingly inaccurate as the service life increases is well taken. Consumers Energy in this case has four functional accounts. In each of those four functional accounts there are numerous sub accounts. Of course, the distribution account is the largest by far dollar wise. However, the other functional accounts have just as many sub accounts. The Commission has finite resources. Regulatory review of ELG would require more resources for review than does ALG. While the ALJ believes this alone is insufficient basis for rejecting the switch, there should arguably be some commensurate amount of increased benefit. The ALJ finds an insufficient basis to reach such a conclusion. The

⁴ Report and Order, FCC Docket No. 20188, December 5, 1981.

gain in supposed accuracy has not been shown while the experience of satisfactory results with ALG which appears to meet the concerns of intergenerational equity without the increased administrative burden has been shown.

Net Salvage Costs

Consumers Energy observes that the appropriateness of including net salvage in the calculation of depreciation expense has long been recognized and is not contested by the parties. Consumers Energy disagrees with the suggestion by ABATE that cost of removal be treated as a part of base rates rather than depreciation expense. According to Consumers Energy, this would violate the fundamental principle of depreciation accounting.

Consumers Energy proposes what it refers to as a traditional approach for determining salvage costs and costs of removal. Mr. Roff examined 10 years of experience with annual salvage costs and cost of removal. He believes that analyzing data for 10 years rather than five years minimized timing mismatches and smoothes the results.

Consumers Energy prepared and presented exhibits which show depreciation rates and expenses when using ELG and when using ALG. Exhibits A-5 and A-7. Consumers Energy states that salvage costs properly allocable for depreciation expense is the net salvage value at the time of the asset's retirement. Doing so, asserts Consumers Energy ensures that the cost of salvage will be incurred among the generations of customers that benefit from the asset. Consumers Energy did not adjust the current net salvage percentages to reflect anticipated inflation.

The five-year averaging approach as used by Staff, the AG and ABATE, is viewed askance by Consumers Energy. It claims that the parties using the five-year average did not evaluate the data by function but rather conducted only a summary level approach. This summary level approach without investigating functional disparities could skew results states Consumers Energy. Using a five-year average, Mr. Simonsen performed analysis using functional class of plant. Exhibits A-8 through A-11⁵. Consumers Energy asserts that the problems with Staff, the AG and ABATE's five-year average approach is to inappropriately lower the assumed net salvage cost which in turn keeps the depreciation rates artificially low and shifts costs of deprecation out to future generations of customers which, according to current regulatory practice, should be paid by current customers.

The four functional categories used by Consumers Energy in its functional approach involve (i) Underground Storage Plant, (ii) Transmission Plant, (iii) Distribution Plant and (iv) General Plant. Consumers Energy is persuaded that the five-year average presented by Mr. Simonsen is more appropriate for numerous reasons cited in its brief at page 15. Consumers Energy distinguishes the Commissions acceptance of a simplified five-year approach involving SEMCO and Aquila as methods adopted through settlement and compromise thus lacking in precedential value in this case.

Where net salvage is negative (i.e. costs of removal is greater than the salvage value) the recoverable depreciation is increased to collect the excess of cost. In this case, Consumers Energy's calculation of its net negative salvage costs is an issue

⁵ Exhibit A-9 shows the application of ALG with a five-year average by functions. Exhibit A-8 shows the application of ELG with a five-year average by functions.

because the amount calculated exceeds by a significant amount calculations of other approved cases before the Commission involving Michigan utility companies.

Staff believes that Consumers Energy's cost of removal as used in calculating its depreciation rates is overstated. Staff supports setting negative net salvage cost recovery of 69% of depreciable plant. Staff calculates the 69% rate as a five-year average of negative net salvage costs divided by the cost of retired plant. Staff avers that this is the approach it used in the cases of Aquila and SEMCO⁶. Staff has a concern that Consumers Energy's net salvage costs are too high when compared with other recent Commission approved depreciation cases.⁷ The adjustment proposed by Staff would reduce annual depreciation expense to \$70.5 million. Exhibit S-27. Staff explains that Consumers Energy's proposed depreciation rate would include \$2.2 billion of negative net salvage recovery or an additional 92% of the cost of Consumers Energy's \$2.4 billion of negative net salvage. To the Staff, the 92% appears excessive when compared with other gas distribution companies in the state.⁸

The AG urges the Commission to flatly reject Consumers Energy's approach which he describes as fraught with erroneous assumptions leading to a system which increases Consumers Energy's depreciation expense and costs of service recovery. The AG's opposition is focused in major part on Consumers Energy's calculation of costs for depreciable plant and the projections for future costs. The use of historical ratios do not accurately predict the future costs and it limits the present value difference

⁶ SEMCO and Aquila's net salvage cost recovery was approved by the Commission in MPSC Case Nos. U-13496, dated May 2, 2003 and U-13393, dated March 12, 2003 both cases were settled by the parties prior to submission to the Commission for its approval. Exhibit A-31.

⁷ Staff's proposal concerning Consumers Energy performing a study to determine its negative net salvage value is presented later in this PFD.

⁸ For ready comparison, a table showing the comparison, its presented later in this PFD under the heading "Study of Consumers Energy's Negative Salvage Cost Recovery."

between today's payments and future costs. Also, the historical ratio of retired plants cost to actual costs is not accurate. The AG applies a method which, it argues, more closely tracks the actual historical costs of net salvage value.

ABATE states that the problem is that Consumers Energy seeks to recover about \$58 million in negative net salvage expense compared with only about \$8 million incurred, historically, when the last five years are averaged together. ABATE's witness James T. Selecky describes that the calculation of future net salvage is fraught with uncertainty and could result in future customers benefiting substantially by current customers paying more of the costs of negative net salvage. ABATE proposes a method based on the Statement of Position (SOP) by the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants on Accounting for Certain Costs and Activities Related to Property, Plant and Equity. SOP requires that the cost of removal be expensed as incurred. 5 Tr 113. ABATE's proposal removes the negative net salvage cost from depreciation rates and replaces it with an increase in operating expenses in the amount of \$8 million. Mr. Selecky sponsored Exhibit I-17 which sets forth its proposed depreciation rates at a \$58 million reduction from the level proposed by Consumers Energy in Exhibit A-9.

First, to address the issue raised by ABATE concerning removing the negative net salvage cost from depreciation rates and replace it with an increase in operating expenses. The ALJ finds this approach negates the principle of intergenerational equity. For example, if there should be a large retirement project in year 2005, the ratepayers for the year 2005 would bear the expense of the retirement. The plant to be

retired could have been in service for many years yet those customers served for those many years do not bear the cost but only those customers that are customers in 2005.

The same holds true for depreciation expenses that are not major. There is no consideration for the concept of intergenerational equity matching the depreciation expense with the class of customers benefiting from investment which in turn produced the expense.

Next, concerning the calculation of net salvage costs and depreciable expenses. The ALJ finds the testimony and exhibits sponsored by Charles W. King, the witness for the AG, clear, concise and credible. Mr. King, first, describes the requirements of Order No. 631 of the Federal Energy Regulatory Commission (FERC Order No. 631). FERC Order No. 631 requires utilities to separate depreciation from recovery of removal costs. Mr. King states that he therefore treats the two procedures as totally separate procedures with respective sets of accrual rates, annual accruals and accumulated reserves. He testified that Consumers Energy has not yet implemented FERC Order No. 631.

Mr. King challenges Consumers Energy's net salvage factors. At a minimum he would adjust those factors to eliminate the high effects of inflation during the 1970s and 1980s. When using adjusted figures, ". . . Mr. Roff's net salvage factors drops from \$67.8 million to \$34.4 million. The same adjustment to Mr. Simonsen's removal cost factors reduces the annual allowance from \$44 million to \$18.6 million." 5 Tr 158.

While Mr. King does not recommend the application of SFAS 143 because it requires projections of removal costs many years into the future, he nonetheless performed the calculated removal cost factors using SFAS 143. Mr. King recommends,

instead, basing net salvage factors on the ratios of the most recent five years of actual salvage experience to plant-in-service. Mr. King lists as advantages to this method as it is consistent with SOP; it eliminates the permanent and continuously growing loan from ratepayers for future removal costs; and it is based on known data not estimates, judgment or speculation.

The ALJ finds particularly illuminating in exposing the deficiencies of Consumers Energy's proposed net salvage costs methodology the historical five-year average experiences for net salvage costs of Consumers Energy. This figure should not be ignored but rather shows, the ALJ believes, a definitive relevant consideration as far as future projections of the net salvage costs to be included in depreciation costs. While historical costs are certainly no guarantee of future costs the relevancy cannot be reasonably disputed. Particularly, in this case, the historical costs represent a five-year average which tends to smooth the highs and lows for the five-year period. Consumers Energy's net salvage cost for 1998-2002 is \$8,321,174.62 or \$7,983,170. Exhibits A-10 & I-20. Consumer Energy's calculation of \$8,321,174.62 is the five-year historical average by function. Exhibit A-10. The AG's calculation of \$7,983,170 is the five-year historical average from its workpapers. Exhibit I-20. There is no stated objections against the use of the functional approach as proposed by Consumers Energy for the purpose of calculating the five-year average.

Consumers Energy's proposal is significantly incongruous with its historical net salvage cost of removal. The costs proposed by Consumers Energy significantly exceeds its actual historical net salvage costs. For example, this significant disparity may be seen by examining Consumers Energy's proposed net salvage cost for its

distribution plant, its largest dollar amount of the functional accounts, with its historical net salvage costs. Consumers Energy proposes approximately \$67.8 million⁹ in net salvage costs for the functional account of distribution plant. Consumers Energy's historical experience with the same distribution account is approximately \$8.3 million. Exhibit A-10. This huge disparity effectively increases expenses today which lower the costs tomorrow. This represents a form of accelerated depreciation while at the same time violating the fundamental principle of intergenerational equity.

Consumers Energy is using the plant balance for December 31, 2002 and its proposed net salvage percentages shows total net salvage at \$2,808,189,028. Exhibit A-8, p 4. This figure actually exceeds the total gas utility plant amount of \$2,409,904,226. Exhibit A-8, p. 4. Consumers Energy argues that the proposed methodology should not be rejected because its net salvage value exceeds the total gas utility plant. The ALJ agrees that that reason alone is insufficient basis to reject Consumers Energy's proposal. However, the ALJ recommends the rejection of Consumers Energy's proposal for the reasons stated above and for the reasonableness of the AG's proposal.

The AG argues that Consumer Energy's approach fails to recognize that future levels of inflation were not likely to match historical levels of inflation and this same argument was rejected by the Commission in its most recent prior depreciation case. MPSC Case No. U-11509, supra. The ALJ does not view this finding by the Commission as fatal to the AG's proposal which seeks to apply salvage factors based

⁹ This amount was calculated from Exhibit A-8, p 2. The calculation was performed by taking each sub account individually and multiplying the plant balance by the net salvage percent then dividing the product by the remaining life and then adding together all of the sub accounts under the distribution functional class.

on historical ratios. Likewise, the ALJ rejects Consumers Energy's argument concerning FERC Order 631 not being applicable to it in this case. FERC Order 631 is not the driving factor in the AG's proposal, it only addresses a component of the AG's methodology which separates for accounting purposes depreciation recovery and removal costs.

Exhibits I-25 and I-26, presented by the AG, show the calculation of depreciation costs and the resulting ratios based on Mr. King's recommendations. These calculations correct the errors found in Consumers Energy's methods while reducing the amount of depreciable expense. The ALJ finds this approach is more appropriate. The AG's approach is straight-forward and based on historical salvage cost ratios rather than some estimate or projection. The ALJ recommends that the Commission adopt the net salvage ratios and recommended removal cost allowances set forth in Exhibits I-25 and I-26.

Study of Consumers Energy's Negative Salvage Cost Recovery

Staff is concerned because Consumers Energy's negative net salvage costs exceeds by a significant percentage those of other Michigan utility companies when compared with the total depreciable plant. For purposes of comparison, Staff cited three recent examples showing the negative net salvage costs as a percent of depreciable plant as follows:

<u>Company</u>	<u>Commission Order</u>	<u>Negative Net Salvage % of Dep. Plant</u>
Aquila	U-13393, 3/12/03	20%
SEMCO Energy	U-13496, 5/2/03	13%
Mich Con	U-13899, pending	32%
Consumers Energy	U-12999, present case	92%

Staff recommends that the Commission order Consumers Energy to conduct a study to determine the reasons its costs are so much more than some other Michigan utility companies. Staff suggests that the report should include findings and recommended remedies. Staff requests that the report be filed within one year from the date of the final order in this case.

The AG supports Staff's recommendation but conditions its support on the Commission not delaying its final decision on the depreciation rates, in this case, on the results of the study.

Consumers Energy opposes the proposal. It asserts that the Staff has not shown that its costs are indeed excessive. It argues that two of the comparisons cited by Staff involve settlements which inherently involve considerations resulting in settlement which are beyond the scope of this proceeding and cannot be reliably used for comparison purposes. Consumers Energy states that the study would require information that it does not have and realistically cannot obtain; for example it believes that such a study would involve books records and practices of other utilities that is not likely to be readily available.

The ALJ concurs with Staff. Even though the data provided in support of Staff's request is at its most rudimentary level it is nonetheless revealing that there is a significant disparity among regulated utilities in the State of Michigan. Consumers Energy's negative net salvage costs, when compared with the above utilities, shows a range of percent difference from 60-79%. Taking the same data and omitting Consumers Energy, the range among the remaining utilities is only 7-19%. The ALJ recognizes the concerns raised by Consumers Energy regarding the availability of data;

however, it appears as though the focus of the study sought by Staff is into Consumers Energy' own books, records and practices. Also with regard to the cases cited above which involve settlements. The ALJ is aware of the nature of compromise inherent in settlements. However, the methodology that the Staff used, negative net salvage as a percent of depreciable plant is a quantitative verifiable measure. When the methodology is applied across the board there is a significant disparity. So even though some of the percentage disparity may be explained through compromises, the ALJ finds the disparity so significant that other factors must be involved other than settlement concerns. Consumers Energy is absolutely correct, there are a wide variety of factors that could explain the disparity. The study should assist in determining which of those factors account for the disparity. The ALJ believes that because the disparity is so significant that the results of the study should inform on the reasons for the disparity.

Deferred Accounting Approval

Consumers Energy seeks approval to implement SFAS 143. Consumers Energy notes that this request was also presented to the Commission in its pending gas rate case.¹⁰ SFAS 143 requires that, "any legal obligation to incur expenditures after the useful life of a long live tangible asset be recorded as a liability, at its present value." 5 Tr 114. Mr. Simonsen identified at a minimum two such obligations: 1) The Meter Move Program, and 2) The sealing of wells that are scheduled to be abandoned in the Northville Trenton Storage Field. 5 Tr 114. Consumers Energy also requests the authority to set up regulatory assets and regulatory liabilities for any timing differences should the Financial Accounting Standards Board approve the Statement of Position on

¹⁰ MPSC Case No. U-13730 filed on March 13, 2003; reply briefs filed on March 29, 2004.

Accounting for Certain Costs and Activities Related to Property, Plant and Equipment.
5 Tr 113.

The AG objects to the approval stating that there is insufficient supporting testimony describing why there is a need or the nature of the differences related to SFAS 143. Also, there is not even a sample accounting entry to show what the Commission is asked to approve.

Consumers Energy replies that its request only addresses the accounting timing differences between required SFAS 143 reporting and the regulatory recovery model. Consumers Energy points out that the AG also opposed its request in MPSC Case No. U-13730, as well, stating that a decision should be deferred to this case. Consumers Energy states that there is no valid reason not to grant the request. The ALJ concurs. The AG's objections appear to avoid the issue of the requirements set forth by SFAS 143 and the accompanying Statement of Position should it be approve. The implementation of SFAS 143 results in no additional recovery should it receive Commission approval.

Synchronization with Revenue Requirements

Consumers Energy requests Commission approval for the provisions of Administration of Depreciation set forth in Exhibit A-4, p 2. Consumers Energy points out that no party presented any evidence in opposition to this request. The ALJ concurs.

Next Depreciation Filing

Consumers Energy proposes that an application for new depreciation accrual rates for gas plant be filed not later than October 1, 2010 with a depreciation study using plant balances as of December 31, 2009. Mr. Roff in setting forth the proposed filing date of the next depreciation case does not specify the reasons for the proposed date. 5 Tr 79.

The AG proposes the next depreciation case filing by Consumers Energy be not later than September 1, 2007. The AG observes that potential changes in depreciation accounting and potential changes in regulation warrant an earlier filing.

The ALJ recommends, in light of the findings above, the later date for filing of the next depreciation case as proposed by Consumers Energy. The ALJ notes that the proposed date is an outside date and that a filing could take place sooner where the concerns raised by the AG come to fruition.

III.

CONCLUSION

The ALJ finds that ELG should not be approved and that continued use of ALG sufficiently serves the depreciation of gas plant. The ALJ finds that the AG's proposed method for determining net salvage expense is reasonable and recommends its approval based on five-year not 10-year historical analysis.

MICHIGAN PUBLIC SERVICE COMMISSION

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Administrative Law Judge

June 24, 2004
Lansing, Michigan
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ISSUED AND SERVED: June 28, 1004

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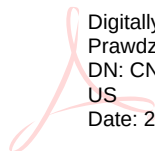
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STATE OF MICHIGAN	)		
	)	SS.	Case No. U-12999
County of Ingham	)		
_____	)		

P R O O F O F S E R V I C E

Dawn M. Prawdzik deposes and says that on the 28th day of June 2004, she served a copy of the attached Proposal for Decision, upon those persons shown on Attachment A, by enclosing same in a sealed envelope addressed as indicated above and delivering the envelope to the Commission's mail courier for (1) postage prepayment and deposit with the United States Postal Service, or (2) delivery through interdepartmental mail (I.D.M.).

Dawn M.
Prawdzik

 Digitally signed by Dawn M.
Prawdzik
DN: CN = Dawn M. Prawdzik, C =
US
Date: 2004.06.24 15:19:11 -04'00'

Subscribed to before me this 28th
day of June, A.D. 2004.

Sharron Allen

 Digitally signed by Sharron Allen
DN: CN = Sharron Allen, C = US, O = MPSC, OU = Case Management
Location: Lansing, Michigan
Date: 2004.06.24 15:31:31 -04'00'

Notary Public, Ingham County, Michigan

My Commission expires 8-16-2004.

ATTACHMENT A

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