

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of	)	
CONSUMERS ENERGY COMPANY for authority	)	
to increase its rates for the distribution of natural	)	Case No. U-13000
gas and for other relief.	)	
_____	)	

At the November 7, 2002 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. Laura Chappelle, Chairman
Hon. David A. Svanda, Commissioner
Hon. Robert B. Nelson, Commissioner

OPINION AND ORDER

I.

HISTORY OF PROCEEDINGS

Consumers Energy Company (Consumers) is a public utility engaged in purchasing, producing, storing, transporting, distributing, and selling natural gas. It serves more than 1.6 million customers in Michigan. Prior to the commencement of this proceeding, Consumers' rates were last reviewed by the Commission in the March 11 and June 5, 1996 orders in Case No. U-10755, which reduced rates by \$11.7 million.

On June 29, 2001, Consumers filed an application seeking authority to increase rates for the transportation, storage, and distribution of natural gas in the annual amount of not less than \$140,011,000. At the same time, Consumers submitted a motion pursuant to MCL 460.6a for

partial and immediate rate relief in the annual amount of not less than \$34,465,000, which it proposed to collect through interim surcharges on all customer classes.

A prehearing conference was conducted by Administrative Law Judge Daniel E. Nickerson, Jr., (ALJ) on August 16, 2001. Petitions for leave to intervene filed by the Association of Businesses Advocating Tariff Equity (ABATE), Attorney General Jennifer M. Granholm (Attorney General), the Midland Cogeneration Venture Limited Partnership (MCV), Metro Bureau Group Services, Inc., (MBGS), the National Energy Marketers Association (NEMA), and Thomas C. DeWard were granted. In addition, the Commission Staff (Staff) participated in the proceedings. The ALJ also established a schedule.

On December 20, 2001, the Commission issued an order granting Consumers interim relief in the annual amount of \$15,380,000. On January 18, 2002, Mr. DeWard filed a petition for reconsideration of the December 20, 2001 order, which was denied by an order issued May 16, 2002.

With regard to Consumers' request for final rate relief, cross-examination of Consumers' witnesses commenced on November 15, 2001 and concluded November 28, 2001. On December 14, 2001, ABATE, the Attorney General, the MBGS, Mr. DeWard, and the Staff filed testimony and exhibits. On January 4, 2002, Consumers, ABATE, and the Attorney General filed rebuttal testimony and exhibits. In its rebuttal filing, Consumers reduced its request for rate relief to \$133.2 million. Cross-examination of these witnesses commenced January 28, 2002 and concluded January 31, 2002, at which time the record was closed. The record consists of 2,361 pages of testimony and argument in 13 volumes of transcript and 189 exhibits.

Briefs and reply briefs were filed by Consumers, the Staff, the MBGS, ABATE, the Attorney General, and Mr. DeWard. The NEMA filed a brief, but not a reply brief. Due to various

adjustments and concessions, by the close of the briefing process Consumers' request for final rate relief had been reduced to \$104.7 million.

On June 3, 2002, the ALJ issued his Proposal for Decision (PFD), which recommended that the Commission grant Consumers a rate increase in the annual amount of \$31,629,000, or \$16,249,000 in excess of the amount granted as interim relief.

On June 24, 2002, exceptions to the PFD were filed by Consumers, the Staff, the MBGS, ABATE, the Attorney General, and Mr. DeWard. Claiming lack of notice of issuance of the PFD, NEMA submitted its exceptions on June 25, 2002, one day late. On June 26, 2002, the MBGS filed a supplement to its exceptions.

Timely replies to exceptions were filed by Consumers, ABATE, and the Staff on July 8, 2002. Mr. DeWard's reply to exceptions was filed July 9, 2002, one day late. The Attorney General filed her reply to exceptions on July 15, 2002 in accordance with an extension of time that was granted by the ALJ.

II.

TEST YEAR

In each rate case, a test year must be selected. A test year is a device employed to determine representative levels of revenues, expenses, rate base, and capital structure for use in the rate-setting formula. A test year may be historical, future, or a combination of historical and future data. A historical test year employs actual operating data that is ordinarily adjusted for known and measurable changes. A future test year uses projections to determine the levels of revenues, expenses, rate base, and capital structure for a future period of time.

In this proceeding, Consumers proposed using calendar year 2002 as its test year. Although the other parties raised a variety of objections regarding Consumers' use of budgeted 2002 test year projections, generally they did not object to 2002 as the test year. Only Mr. DeWard expressed any dissatisfaction with this proposal and his concern seems to be limited to Consumers' failure to finalize its 2002 budget in a timely fashion. Therefore, the Commission finds that 2002 should be used as the test year.

III.

RATE BASE

A utility's rate base is the investment upon which the utility is given an opportunity to earn the authorized rate of return. It is equal to the capital invested in plant, less accumulated depreciation, plus working capital. Consumers and the Staff were the only parties to conduct a comprehensive analysis of Consumers' rate base. Consumers' determination of its rate base appears on Exhibit A-7. The Staff's calculations appear on Exhibits S-121 and S-129. The Attorney General and Mr. DeWard also addressed certain aspects of Consumers' rate base.

Net Utility Plant

Total utility plant is made up of plant-in-service, plant held for future use, and construction work in progress (CWIP). To determine net utility plant, the total utility plant amount is reduced by the amount of accumulated depreciation, moneys retained from contractors, and customer advances.

Most of the controversy in this proceeding centers on a determination of the appropriate level of working capital and on Consumers' proposed capital additions during 2001 and 2002, which are reflected in plant-in-service and CWIP. The other elements that comprise

Consumers' rate base, including such matters as plant held for future use and accumulated depreciation, are not controversial.

With regard to accumulated depreciation, the parties note that Consumers simultaneously filed a depreciation rate case, which was docketed as Case No. U-12999. The parties to that case stipulated on December 7, 2001 that they would rely upon Consumers' existing gas depreciation rates for the revenue requirement calculations in Case No. U-13000. As shown in Appendix A attached to Consumers' brief, Consumers' requested relief reflects an appropriate adjustment to implement the Case No. U-12999 stipulation.

Consumers' proposal to reflect a significant change in the status of Michigan Gas Storage Company (MGS), which is a wholly owned subsidiary of Consumers, is also not controversial. In the past, MGS provided storage and transmission services primarily to Consumers, subject to rates and tariffs approved by the Federal Energy Regulatory Commission (FERC). However, on August 8, 2001, Consumers and MGS filed an application asking the Commission to indicate that it would exercise jurisdiction over MGS to the extent that the FERC granted MGS an exemption from Section 1(c) of the Natural Gas Act (NGA), 15 USC 717(c). In an order issued on August 16, 2001 in Case No. U-13052, the Commission granted that request. On November 9, 2001, MGS asked the FERC to find that MGS is exempt from the provisions of the NGA. That request remained pending before the FERC at the time that the record closed.¹

In anticipation that the FERC would grant an exemption from the NGA, Consumers' case reflects the MGS rate base, capital investments, and operation and maintenance (O&M) expenses

¹ Subsequently, in an order issued on February 28, 2002 in Docket No. CP02-22-000, the FERC declared that MGS's facilities and services would be exempt from the FERC's regulation under Section 1(c) of the NGA effective on the date that the Commission issues an order establishing rates for Consumers that reflect the inclusion of MGS's facilities in Consumers' system. See, 98 FERC ¶ 61,223.

in the same manner as for Consumers. Consumers also proposed retail distribution rates that include MGS's costs.

The Attorney General and the Staff supported Consumers' request in this regard. Mr. DeWard did not oppose the roll-in, but he removed the revenue requirement associated with the roll-in because he believed that the roll-in should be revenue neutral.

The ALJ recommended that Consumers' request to roll MGS's assets into its rate base should be granted. No one objected to the ALJ's recommendation. Therefore, the Commission is persuaded that the rates established in this proceeding should reflect the roll-in of MGS into Consumers' rate base as proposed by Consumers.

1. Capital Additions

As previously noted, Consumers and the Staff approached their projections for net utility plant from different perspectives, which accounts for most of the difference between their positions. Consumers' methodology started with 2000 actual data to which it added budgetary projections for capital expenditures on a project-by-project basis for 2001 and 2002. Consumers' evidence was presented by four witnesses. Collectively, Consumers' witnesses described capital projects costing a total of \$225,970,000 during 2001 and 2002.

Paul N. Preketes, Consumers' Senior Vice President of Gas Operations, described his company's proposed expenditures for a variety of programs, including material condition, pipeline integrity, corrosion control, damage prevention, succession planning, appliance service plan, engineering, operator qualification, uncollectibles, meter technology, accounting changes, and civic improvement. According to Mr. Preketes, these programs are integral to the gas operations of both Consumers and MGS and are designed to provide safe and reliable service to customers and to meet new regulatory requirements. Capital spending on the programs described by

Mr. Preketes would add \$142,287,000 to Consumers' rate base for 2001 and 2002. See, Exhibits A-67 and A-68. Mr. Preketes also adopted the testimony of Kenneth C. Emery, formerly Consumers' Senior Vice President for Information Technology, which indicated that Consumers would make capital expenditures of \$17,630,000 for a variety of information technology programs during 2001 and 2002. See, Exhibits A-94 and A-100.

Rufus D. Gladney, Consumers' Manager of Business Services, presented testimony supporting Consumers' level of capital investments for business services to support the gas utility for 2001 and 2002. He stated that Consumers would spend \$24,177,000 on a variety of projects, including a central office building, the realignment of out-state work facilities, fleet equipment, and infrastructure improvements. See, Exhibit A-83.

Dennis DaPra, Senior Vice President of Accounting and Regulatory Affairs for Consumers, sponsored capital investments that totaled \$1,814,000 in 2001 and \$5,364,000 in 2002. See, Exhibit A-57. He explained that these investments are for computer systems and office equipment to replace the company's 20 year old corporate accounting computer system that uses an outdated data base technology and is becoming increasingly expensive to maintain.

Finally, Benedict C. Sosinski, Manager of Gas Transmission and Storage for Consumers and General Manager of MGS, testified that construction expenditures related to compression, transmission, and storage functions of Consumers and MGS during 2001 and 2002 would add a total of \$34,697,000 to Consumers' rate base. See, Exhibits A-71 and A-73.

Combining Consumers' projections for its 2001 and 2002 capital additions with the other less controversial aspects of rate base, Consumers' originally calculated an average net plant amount of \$1,076,788,000. However, in its brief, Consumers increased its proposal for net utility plant to

\$1,085,875,000 to reflect an adjustment proposed by the Staff related to MGS base gas. See, Exhibit S-129.

The Staff presented its position on Consumers' net utility plant through the testimony of two witnesses. Susan J. Sims and Robert C. Mogis, auditors in the Commission's Gas Division, testified regarding Consumers and MGS, respectively. Collectively, Ms. Sims and Mr. Mogis supported capital expenditures of \$149,767,000 during 2001 and 2002. Therefore, the difference between Consumers' approach and the Staff's approach regarding the amount of capital expenditures for 2001 and 2002 is \$76,203,000. Combined with the other rate base elements, the Staff supported a net plant of \$1,037,777,000.

Ms. Sims stated that Consumers' 2000 historical plant balances were used as the 2001 beginning balances for both Consumers' gas plant and common plant balances. Adjustments were made for CWIP and plant retirements by using average balances for the five-year period from 1996 to 2000 and through the application of ratios to determine 2001 and 2002 year-end balances. Average expenditures for 1996-2000 were increased by the 2001 Consumer Price Index (CPI) of 2.7%, yielding capital expenditures for 2001. Then, 2001 capital expenditures were increased by the 2002 CPI of 2.4%, yielding capital expenditures for 2002.

Ms. Sims testified that her determination of Consumers' 2002 average depreciation balance of \$1,485,973,428 represents the sum of the average depreciation reserve balance of \$1,384,227,398 for gas plant in service and \$101,746,030 for common plant in service allocated to gas utility operations. The calculation of these amounts is shown on Exhibit S-121. The amounts used by the Staff for customer advances and money obtained from contractors mirrored Consumers' figures. Combining all of these factors, Ms. Sims determined that Consumers' test year net utility plant balance would be \$971,443,000.

Mr. Mogis followed a similar methodology to determine MGS's net utility plant. He testified that he used the historical five-year average for 1996-2000 as the basis for determining the plant in service projections for 2001 and 2002 and that he applied the appropriate inflation factors to additions but not to retirements. He also examined the relationship between capital expenditures for 2000 to CWIP at December 31, 2000 and determined that this was 80%, which he applied to his projected capital expenditures for 2001 and 2002, respectively, to determine the projected CWIP for these same years. According to Mr. Mogis, MGS's net utility plant is \$66,334,000 for the test year.

Consumers and the Staff were not the only parties to address net utility plant issues. The Attorney General's position was presented by Charles W. King, a consultant knowledgeable in regulatory matters. Mr. King stated that many of the test year adjustments proposed by Consumers should be rejected or modified. According to Mr. King, gas utilities have been able to offset increasing costs through productivity gains during the past decade. For this reason, Mr. King believed that the Commission should apply the "known and measurable" standard rigidly. Among the capital projects opposed by Mr. King for being associated with unrecognized offsetting productive gains are the \$17,630,000 expenditure for corporate services (Exhibits A-94 and A-100), the \$14,000,000 for enhanced engineering, planning, and scheduling systems (Exhibit A-67), and the \$7,800,000 for meter technology and management (Exhibit A-67). Mr. King also criticized Consumers for proposing to spend a total of \$34.68 million in 2001 and 2002 on gas compression, transmission, and storage facilities. According to Mr. King, Consumers' ability to absorb such expenditures without a rate increase for 17 years indicates that transmission and storage improvements pay for themselves.

Mr. DeWard's testimony addresses several net utility plant issues. On Exhibit I-166, Schedules 2 and 17, Mr. DeWard proposed to reduce Consumers' net utility plant balance by \$6.4 million to remove deferred federal income taxes associated with certain contributions in aid of construction. He also recommended removal of \$4.2 million from net utility plant to adjust for Consumers' profits on the sale of real property in previous years. Finally, he stated that the Commission should deduct deferred income taxes from rate base to adhere to his concept of the correct methodology for determining a utility's capital structure.

The ALJ's recommendations regarding the amount of Consumers' net utility plant balance are based strictly on the Staff's positions. He recommended a total net utility plant balance of \$1,037,777,000, as proposed by the Staff. In so doing, the ALJ implicitly rejected all of the adjustments proposed by Consumers, the Attorney General, and Mr. DeWard. In commenting on the difference in the approaches followed by the parties, the ALJ found that the Staff's approach to projecting test year expenses was more consistent with existing Commission precedent than was Consumers' approach. According to the ALJ, Consumers did not bear its burden of proving that its methodology produced test year projections that were known and measurable or fair and reasonable.

In its exceptions, Consumers argues that the Staff's approach to estimating test year revenues and expenses renders it impossible for Consumers to perform the work necessary to provide safe and reliable service or to earn a just and reasonable return. Consumers contends that the Staff's methodology, which features use of historical data that has been increased by the expected rate of inflation, is simply too conservative. According to Consumers, the fallacy of the Staff's position is proven by the fact that the Staff's proposed level of spending for 2002 is less than Consumers' actual 2001 expenditures.

Moreover, Consumers contends that its witnesses presented detailed evidence describing the capital investments that must be made in 2001 and 2002 to continue providing safe and reliable service to the public. Consumers insists that the record is bereft of evidence that its 2001 and 2002 investments are either unreasonable or imprudent. Consumers also maintains that the record lacks support for a finding that such expenditures are excessive. In short, Consumers contends that there is no justification for concluding that its 2001 and 2002 capital additions should be excluded from its test year rate base.

Consumers also argues that the Staff's methodology is flawed because it fails to properly account for inflation. According to Consumers, for many rate base items, the Staff used a five-year average from the period 1996 to 2000 without escalating the numeric values for the years 1996, 1997, 1998, or 1999 before applying escalation factors for 2001 and 2002. Consumers insists that the Staff's failure to escalate data from 1996, 1997, 1998, and 1999 caused the Staff to understate Consumers' rate base by \$6,015,000 and its required revenue by \$948,000.

The Staff maintains that its case is based upon Consumers' own actions and decisions. According to the Staff, it presented a complete and thorough analysis of the costs Consumers incurs to provide safe and reliable natural gas service. The Staff insists that Consumers seeks to inflate its costs far beyond what it spent on its gas operations during 2000. Indeed, the Staff suggests that Consumers has been spending less on other O&M expenses than provided for in the Company's gas and electric rates. Finally, the Staff contends that Consumers has offered absolutely no assurance that once it is provided recovery of unprecedented levels of expenditures in its gas rates, it will actually spend the money on such programs.

Citing Commission precedent, the Attorney General contends that the evaluation of a utility's rate base, capital costs, revenues, and expenses should begin with booked amounts for a historical

year, which are then adjusted for known and measurable changes that are reasonably expected to occur prior to and during the projected test year. The Attorney General insists that the Commission's existing policy determinations in this regard apply to all regulated gas companies and should not be changed in this proceeding.

The Commission finds that the ALJ did not err when he rejected Consumers' methodology for test year projections. The United States Supreme Court has observed in Duquesne Light Co v Barasch, 488 US 299, 314; 109 S Ct 609; 102 L Ed 2d 646 (1989), that "the economic judgments required in rate proceedings are often hopelessly complex and do not admit of a single correct result." As with many of the other aspects of rate proceedings, the selection of a test year has no single correct answer. Michigan does not have a statute that requires the use of any particular form of test year. Rather, the selection of a test year is within the Commission's broad rate-making power and expertise. Consumers Power Co v Public Service Comm, 181 Mich App 261; 448 NW2d 806 (1989). The Commission is free to select any reasonable methodology that is consistent with the objective of determining the level of investment on which the shareholders of the utility are entitled to the opportunity to earn a fair rate of return and the levels of expenditures that the utility is entitled to the opportunity to recover.

In recent years, the Commission has repeatedly expressed a preference for use of historical test year data to determine rates. It is undisputed that Consumers developed its test year rate base primarily through use of budgetary projections for 2001 and 2002 of capital expenditures, whereas the approach recommended by the Staff and the Attorney General more closely follows Consumers' historical data, deviating only to account for a limited number of known and measurable changes expected to affect the test year.

In setting rates, the Commission must balance the interests of the utility and its shareholders with the interests of the ratepayers in light of the existing regulatory framework. The use of historical test year data supplemented by known and measurable changes has a great deal of merit as it simplifies the rate case proceeding and relies upon data that is more readily verifiable. Further, it lessens the reliance on projections, which, if erroneous, may adversely influence rates. A danger in adopting budgetary projections of test year capital expenditures and other O&M expense levels is the possibility that some portion of the funds provided by the Commission to support such increased expenditures could be diverted to other uses. Therefore, the Commission is persuaded that the Staff's methodology, which more conservatively estimates Consumers' expenditures, generally provides a reasonable assessment of Consumers' financial situation during the test year.

Moreover, it is apparent that Consumers' understanding of the phrase "known and measurable changes" does not correspond with the meaning intended by the Commission in Consumers' previous gas rate cases. Indeed, in his rebuttal testimony, Francis S. Ernst, Jr., Consumers' Executive Director of Rates and Electric Strategic Business Unit Planning, urged the Commission to abandon its traditional adherence to historical test year data updated for known and measurable changes. Mr. Ernst suggested that the Commission either should use a fully projected test year or adopt Consumers' more progressive view of known and measurable changes, which seems better described by the phrase "conceivable and estimable." The Commission declines to do so.

The Legislature recognized that the methodology followed by the Staff in this proceeding could result in financial hardships for a utility in the event that its expenditures exceed the inflation-adjusted historical spending levels approved by the Commission. Therefore, the Legislature provided the Commission with authority in MCL 460.6a to review requests for partial

and immediate rate relief filed by a utility at the commencement of a rate proceeding to address such concerns. Indeed, Consumers availed itself of this provision in the current proceeding. However, it is important to note that the Legislature has not extended similar protective relief towards ratepayers. Because ratepayers cannot obtain partial and immediate relief from paying excessive rates and because the Staff's approach constitutes a reasonable and time-tested methodology for setting rates, the Commission is persuaded that the Staff's position with regard to the amount of Consumer's net utility plant should be used to develop the company's new rates.

Moreover, the Commission finds that neither the complexity of Consumers' budgetary analysis nor its ability to nitpick the Staff's methodology justifies rejection of the Staff's proposal. The Constitution requires only that rates must be reasonable. A reasonable methodology for setting rates is not rendered unreasonable merely because the methodology could be tweaked to produce a more favorable result or because a more complex alternative methodology exists.

2. Net Utility Plant Summary

Based on these determinations, the Commission finds that it should use the Staff's net utility plant amount of \$1,037,777,000 in determining Consumers' new gas rates.

Working Capital

Working capital is commonly defined as current assets less current liabilities. Current assets include cash, accounts receivable, and gas inventory in storage, among other things. Current liabilities include accounts payable, dividends payable, accrued taxes, and accrued interest. For ratemaking purposes, deferred debits and credits are also reflected in working capital.

Initially, Consumers proposed a working capital requirement of \$439,996,000 for Consumers and a negative \$2,154,000 for MGS, for a total working capital requirement of \$437,842,000 for the test year. The Staff proposed a working capital requirement of

\$346,052,000, which included \$347,235,000 for Consumers and a negative \$1,183,000 for MGS. In its brief, Consumers stated that it would accept the Staff's working capital requirement.

The Attorney General and Mr. DeWard urged the ALJ to make several changes to the working capital requirement developed by the Staff. The Attorney General maintained that Consumers' working capital requirement should be subject to a disallowance associated with the rate base effects of the Commission's October 24, 2000 order in Case No. U-12679, which authorized Consumers to reclassify 74.6 billion cubic feet (Bcf) of recoverable base gas from Account 358 to Account 164.1 and to transfer the cost of that gas on the company's books and records to Account 164.1. Consumers made these adjustments on October 25, 2000.

William A. Peloquin, a certified public accountant employed by the Attorney General, testified that equity requires that the effect of the base gas adjustment be shared according to the benefits actually received by the company and the ratepayers. Mr. Peloquin calculated that the reclassification increased Consumers' working capital requirements associated with gas stored underground by \$248,466,000, but reduced Consumers' utility plant for base gas by \$36,502,000, producing a net increase in Consumers' rate base of \$211,964,100. He suggested that half of the net increase in rate base, or \$105,982,000, should be removed from Consumers' average rate base in this case to allocate the increased working capital cost in proportion to their sharing of the corresponding cost reduction benefits. Mr. DeWard agreed with the Attorney General on this issue.

Additionally, Mr. DeWard expressed concern over the use of a projection for the cost of gas in underground storage. Because he believed that Consumers had significantly overstated the cost of gas in storage, he proposed a \$76,687,000 reduction associated with Consumers' August 2001 data

and another \$50,000,000 reduction due to the current downward trend in energy costs. He also stated that Consumers' rates should not depend on a price projection for gas in underground storage that could be significantly overstated when there is a simple solution. As an alternative, Mr. DeWard suggested that the cost of gas in underground storage could be subject to an annual true-up mechanism, which could be considered in the context of Consumers' annual GCR reconciliation cases.

Mr. DeWard also removed from working capital \$8,939,369 associated with customer attachment receivables that accrue interest because Consumers conceded that it was improperly included. In addition, Mr. DeWard recommended working capital reductions of \$26,327,992 and \$15,676,150 to account for an accounts payable offset and the removal of prepaid property tax effects resulting from a change in recording such expenses. Finally, as shown on Exhibit I-166, Schedule 2, Mr. DeWard deleted \$190,120,000 associated with gas stored underground from working capital to be consistent with his belief that such gas should logically be financed with short-term debt rather than long-term debt.

The ALJ recommended a working capital requirement of \$346,052,000 for Consumers and MGS, as proposed by the Staff. In so doing, the ALJ explicitly ruled against the Attorney General's disallowance that was associated with the October 25, 2000 base gas reclassification on the strength of the Commission's interim order in this proceeding. According to the ALJ, the Attorney General's presentation on this issue provided no reason to further scrutinize the Commission's December 20, 2001 determination that the reclassification was not controversial and that Consumers' ratepayers had benefited significantly from it.

The Attorney General filed an exception to the ALJ's recommendation. She argues that no one has questioned the accuracy of Mr. Peloquin's calculations regarding the effects of the

reclassification. According to the Attorney General, because the Commission is required to establish just and reasonable rates and must balance the interests of Consumers and its customers, the Commission should not impose upon customers all of the increased working capital requirements resulting from Consumers' base gas reclassification. Rather, she insists that the \$105,982,000 disallowance supported by Mr. Peloquin should be adopted. Absent such action, the Attorney General believes that the PFD's recommendation is unfair to ratepayers.

The Commission finds that the working capital amount proposed by the Staff, agreed to by Consumers, and approved by the ALJ should be adopted. In so doing, the Commission concludes that the disallowance proposed by the Attorney General and supported by Mr. DeWard is not warranted. It is undisputed that the base gas adjustment reduced Consumers' plant in service balance, increased its working capital requirement balance, and reduced Consumers' GCR cost of gas. The Commission remains convinced that the base gas adjustment should be fully recognized for ratemaking purposes due to the substantial benefits already realized by Consumers' ratepayers.

Unamortized Manufactured Gas Plant Expenditures

The final component of Consumers' rate base may be traced to the earliest days of the gas industry. Before the construction of interstate pipelines, local gas distribution companies would utilize natural gas only if it was produced at nearby wells. Manufactured gas, a mixture of carbon monoxide and hydrogen produced from coal, coke, or oil, was the primary gaseous fuel. The record indicates that Consumers or its corporate predecessors had an ownership interest in 23 sites that formerly housed manufactured gas plants. Such sites present significant environmental concerns and are the subject of statutory environmental cleanup requirements. See, MCL 324.20101 et seq.

The Commission has previously held that prudently incurred manufactured gas plant environmental response costs are recoverable. In its March 11, 1996 order in Case No. U-10755, the Commission held that Consumers' manufactured gas plant environmental response costs should be recorded in a deferred account for each vintage year and amortized over a ten-year period, with rate recovery beginning after a prudence review of the costs. The Commission also concluded that it would be appropriate to include the five-year historical average cost in base rates for future manufactured gas plant environmental expenses, with expenditures in excess of that amount subject to deferral and amortization. In Case No. U-10755, the amount that was approved for inclusion in Consumers' base rates was \$853,000. The Commission also held that to the extent Consumers was successful in obtaining insurance recovery for manufactured gas plant remediation, that recovery, net of expenses, should be amortized over 10 years using the same methodology as for expenses. In addition, the Commission found that, after a prudence review had occurred, carrying costs should be allowed on unamortized environmental expenditures through inclusion of the unamortized balances in rate base.

Consumers originally requested that the Commission find all costs for the period 1999-2002 to be prudently incurred, authorize recovery of amortization expense in the amount of \$2,303,000 (an increase of \$1,450,000 above the \$853,000 currently included in base rates), and include the deferred unamortized balance in the amount of \$18,408,000 in rate base, which represented an \$13,948,000 increase over Consumers' 2000 historical amount of \$4,460,000.

At the hearing, Consumers submitted supplemental testimony indicating that several adjustments to its original position were appropriate. According to Consumers, its environmental response expenditures for 2001 should be increased from \$7,049,938 to \$7,589,807. In addition, Consumers indicated that it anticipated the receipt of \$17.7 million of insurance proceeds near the

end of 2001, which would reduce the amount of the deferred unamortized balance in rate base from \$18,408,000 to \$4,680,000.

The Staff insisted that Consumers' treatment of its manufactured gas plant environmental response costs was inconsistent with the March 11, 1996 order in Case No. U-10755. According to the Staff, Consumers' inclusion of costs from November and December 2001, which the Staff did not have a chance to audit, and its use of projected costs for 2002 are flawed because such expenses must be determined to be prudently incurred before they are eligible for inclusion in the cost recovery mechanism adopted in the March 11 order. Moreover, the Staff contended that it properly considered the effect of the November 2001 insurance proceeds in determining the amount of the deferred unamortized balance to be included in Consumers' rate base. Accordingly, the Staff recommended that Consumers' proposed rate base should be reduced by \$5,534,000 based on the Staff's estimate of Consumers' deferred unamortized manufactured gas plant balance.

Mr. DeWard believed that Consumers' sale of real property for a profit should be linked with Consumers' manufactured gas plant environmental response costs. According to Mr. DeWard, the Commission should order Consumers to apply all future gains, net of losses, on the sale of properties as an offset to accumulated manufactured gas plant environmental response costs.

The ALJ found that Consumers' position was inconsistent with the March 11, 1996 order in Case No. U-10755. He concluded that the Staff's ability to review Consumers' budgeted expenditures for November and December of 2001 and for 2002 was not the type of inquiry contemplated by the Commission's order. For these reasons, the ALJ recommended adoption of the Staff's position.

In its exceptions, Consumers argues that the three areas of disagreement with the Staff involve "timing issues" that should be resolved in its favor. According to Consumers, the November and

December 2001 manufactured gas plant expenditures occurred prior to the test year and prior to the close of the record in this proceeding. Consumers insists that the prudence of such costs was described in the testimony of Gary L. Kelterborn, its Director of Remediation Management, Environmental, and Technical Services. Consumers also contends that the Staff did not determine that any of the November and December 2001 manufactured gas plant expenditures were imprudent in any respect. Finally, Consumers insists that the actual expenditures for this period are consistent with the company's proposed expenditures.

Likewise, Consumers insists that if the November and December 2001 manufactured gas plant expenditures are not included in determining its rates, it would be unfair to include the insurance proceeds, which were not received until November 21, 2001. Indeed, citing Michigan Consolidated Gas Co v Public Service Comm, 389 Mich 624; 640; 209 NW 2d 210 (1973), and General Telephone Co v Public Service Comm, 78 Mich App 528, 539-540; 260 NW 2d 874 (1977), Consumers contends that if the Commission considers anticipated reductions in costs, then anticipated increases in costs for the corresponding period must also be considered.

Finally, although conceding that its request to include the 2002 manufactured gas plant expenditures at this time is not appropriate under the March 11, 1996 order in Case No. U-10755, Consumers requests that the Commission modify the recovery mechanism established by that order to allow such costs to be considered in this proceeding.

The Commission finds that Consumers' exceptions should be rejected. The cost recovery mechanism established in the March 11, 1996 order in Case No. U-10755, which mirrors similar recovery mechanisms applicable to other utilities, has been properly applied by the Staff and the Commission is not persuaded that the recovery mechanism should be altered on a piecemeal basis in this proceeding. Moreover, the record indicates that the Staff's audit concluded with the review

of Consumers' October 2001 manufactured gas plant cost data and therefore could not have included Consumers' environmental response costs for November and December 2001 or for any of 2002. The record also establishes that the insurance arbitration determination awarding Consumers \$17.7 million for environmental response costs was rendered on July 2, 2001. Indeed, on the basis of that determination, Consumers' witness DaPra incorporated such proceeds into Consumers' case in the same manner proposed by the Staff and Consumers' allegation of unfair treatment is misplaced.

Rate Base Summary

Based on the above findings, the Commission concludes that Consumers' test year rate base should be calculated as follows:

Net Utility Plant	\$1,037,777,000
Working Capital	\$346,052,000
Manufactured Gas Plant deferred unamortized amount	<u>(\$5,534,000)</u>
Total Rate Base	<u>\$1,378,295,000</u>

IV.

RATE OF RETURN

Capital Structure

An overall rate of return must be established. To do so requires a review of each element of the company's capital structure. Consumers proposed a capital structure based on its 2000 13-month average capital structure, subject to five adjustments, including a trust preferred securities issuance that occurred in May 2001, a \$150 million equity infusion from its parent company, CMS, planned for the second half of 2001, the issuance of \$350 million of senior notes in

September 2001, the announcement in October 2001 that Consumers is taking a write-off due to losses related to the MCV power purchase agreement, and an additional \$150 million equity infusion from CMS that was planned for mid-year 2002, but that actually occurred on January 3, 2002. Consumers' proposed capital structure is set forth on Exhibit A-10.

The Staff's proposed capital structure appears as Exhibit S-117. The Staff recommended use of Consumers' September 30, 2001 capital balances for long-term debt, preferred stock, and common equity. The Staff also relied upon the 13-month average amounts for 2000 for short-term debt, customer deposits, deferred investment tax credits, accumulated deferred income taxes, and job development investment tax credits (JDITC). According to the Staff, it was necessary to mix data from different periods to ensure consideration of known and measurable changes to Consumers' historical data that would appropriately represent the 2002 test year. By utilizing the more recent data, the Staff included certain known events, including the May 2001 trust preferred securities issuance, the \$350 million senior debt issuance, the 2001 equity infusion by CMS, the after-tax write-off of \$80.471 million for losses related to the MCV, and nine months of 2001 earnings. However, the Staff did not include Consumers' 2002 equity infusion because of doubt as to how the announced equity infusion would benefit Consumers. The Attorney General supported the Staff's recommendations on this issue.

Although ABATE did not sponsor a witness with regard to Consumers' capital structure, in its brief ABATE urged the Commission to accept the Staff's position that the January 3, 2002 equity infusion should not be recognized for ratemaking purposes. Further, ABATE argued that the capital structure used by the Commission should include the effects of the securitization bonds that were issued by Consumers in November 2001 pursuant to Public Act 142 of 2000.

Mr. DeWard approached Consumers' capital structure from an entirely different perspective. Whereas Consumers and the Staff focused on Consumers' combined gas and electric capital structure, Mr. DeWard insisted that the capital structure must be "synchronized" with rate base and reflective of only Consumers' gas operations. Mr. DeWard stated that it is totally inappropriate to use Consumers' combined capital structure because it results in excessive return requirements. Mr. DeWard argued that deferred taxes, customer deposits, and JDITC attributable to electric operations have no place in the gas capital structure. Further, he insisted that the issuance of securitization bonds on November 8, 2001 should have no effect on the capital structure in Consumers' gas rate case. He also maintained that gas stored underground is logically supported by short-term debt, not long-term capital.

The ALJ adopted the Staff's proposed capital structure with one exception. He determined that the January 3, 2002 equity infusion should be incorporated into Consumers' overall rate of return. According to the ALJ, because the purpose of the equity infusion was to maintain and increase Consumers' credit rating by improving its equity ratio, it was unlikely that CMS would attempt to return the equity to itself because such action would harm Consumers' credit rating. Further, the ALJ stated that there was no evidence that CMS would withdraw the equity infusion. While conceding that the timing of the equity infusion could cause some concern, he indicated that there was no proof that the equity infusion was merely an attempt to increase Consumers' capital structure and revenue requirements. Rather, the ALJ was convinced that the Commission should include the equity infusion in Consumers' capital structure to provide CMS's shareholders an opportunity to earn a fair return on their investment.

The Staff and the Attorney General argue in their exceptions that the \$150 million equity infusion should not be considered by the Commission in setting Consumers' rates. According to

them, the last minute equity infusion is merely a ploy to gain a higher overall rate of return with no discernible benefit to Consumers' ratepayers.

The Commission finds that the capital structure proposed by the ALJ should be adopted, with one exception. At the outset, the Commission notes that it is not persuaded by Mr. DeWard's contention that Consumers' capital structure must be synchronized to its rate base in the manner that he has proposed. The selection of a capital structure is not mandated by law. Rather, the Commission has considerable discretion in this regard. For example, in Case No. U-8924, the capital structure used to set Consumers' gas rates was the capital structure of Michigan Consolidated Gas Company (Mich Con). The Commission used Mich Con's capital structure because all parties agreed that Consumers' actual capital structure was so skewed by major write-offs and debt restructuring efforts that it could not serve as the basis for setting a fair rate of return. Finally, adoption of Mr. DeWard's recommendation would require abandonment of past precedent and is not necessary to the establishment of just and reasonable rates. Therefore, the Commission finds that Mr. DeWard's proposed capital structure and all of its related ratemaking adjustments should be rejected.

Additionally, the Commission is persuaded that it should recognize the January 3, 2002 equity infusion for ratemaking purposes. A review of previous rate cases indicates that the Commission has exercised considerable latitude in such determinations. In two of Consumers' recent rate cases, Cases Nos. U-10335 and U-10755, the Commission excluded \$100 million of equity attributable to Consumers' revaluation of an asset by that amount. The Commission reasoned that ratepayers were not benefited by the revaluation. Rather, the Commission found that recognition of the revaluation in the company's capital structure could await receipt of an actual benefit by the ratepayers. However, the March 11, 1996 order in Case No. U-10755 and the February 5, 1996

order in Case No. U-10685 also indicate a willingness on the part of the Commission to recognize significant equity infusions under certain circumstances.

Here, Consumers' January 3, 2002 equity infusion was meant to boost its credit rating by maintaining or increasing its common equity ratio, which is a legitimate purpose. Therefore, the Commission concludes that the January 3, 2002 equity infusion should be considered for the purpose of determining Consumers' capital structure in this proceeding.

The Commission also finds that it would be reasonable to include \$39 million in the capital structure associated with other interest bearing items that were on the books during Consumers' historical test year. The Staff excluded these items because they involved a mixture of other interest bearing items including over-recovered gas costs, supplier deposits, interstate pipeline refunds, and an electric regulatory contingency amount, which might not exist in the future. The ALJ found that this item should be left out of Consumers' capital structure on the strength of the Commission's determination of a similar issue in Consumers' last rate case. Consumers points out that the Commission's filing requirements list other interest bearing items as a category to be included in the company's capital structure. In addition, it is undisputed that Consumers incurs interest expense on this asset category. Further, there is no evidence that inclusion of such assets would skew Consumers' capital structure in a way that would produce unreasonable rates. Therefore, the Commission finds that Consumers' proposal to include \$39,060,000 in its capital structure at 9.83% for other interest bearing items is reasonable and should be adopted.

Return on Common Equity

Consumers offered two witnesses with expertise in rate of return issues. Nicholas A. Vlisides, Director of Financial Risk Management for CMS Enterprises Corporation (CMS), testified that he applied the Discounted Cash Flow (DCF) and the Capital Asset Pricing Model (CAPM)

methodologies to two proxy groups of utility companies to determine a return on equity for Consumers. Citing Bluefield Waterworks & Improvement Co v PSC of West Virginia, 262 US 679; 43 S Ct 675; 67 L Ed 1176 (1923) and Federal Power Comm v Hope Natural Gas Co, 320 US 591; 64 S Ct 281; 88 L Ed 333 (1944), Mr. Vlisides maintained that equity investors are entitled to a return commensurate with investments of comparable risk. He also maintained that the earnings of a regulated company must be sufficient to assure its financial soundness and permit the utility to raise required capital. Mr. Vlisides contended that deregulation and recent gas price volatility were causing increased business risk in the gas utility industry. He reported that Consumers' bond ratings reflect low investment grade ratings from two major rating agencies.

Exhibit A-48 describes Mr. Vlisides' two groups of proxy companies and provides comparative data. He insisted that both groups were less risky than Consumers, which would cause the proxy companies to have lower overall returns on equity than expected for Consumers. Mr. Vlisides' DCF and CAPM analyses were presented on Exhibits A-49 and A-50, respectively. However, he discounted the importance of his CAPM analysis because various academic resources have questioned the validity of CAPM. In so doing, Mr. Vlisides indicated that his DCF analysis supported a rate of return on common equity for Consumers of no less than 12.25%.

John E. Olson, Senior Vice President and Director of Research at an investment banking and securities firm in Houston, Texas, offered testimony regarding his view of the investment community's perspective of appropriate rates of return on investments. Because gas distribution utilities must compete with all privately owned companies for capital, Mr. Olson reasoned that a comparable earnings analysis was more in tune with investor concerns than the various formulistic, mathematical models derived from academic theory. According to Mr. Olson, current returns on equity experienced by the companies that comprise the Standard & Poors 400

Industrials Index (S&P 400) constitute an objective standard for a typical investor's required return on equity. Using this approach, Mr. Olson stated that Consumers' return on equity should be set between 17% to 22%. In so doing, he suggested that the relatively mediocre performance of gas distribution company stocks in recent years is directly attributable to inadequate returns on equity approved by regulators. He also stated that the returns experienced by gas distribution company investors are more comparable to the returns experienced by owners of bonds, which fail to compensate equity investors for market risk. Mr. Olson argued that the business of gas distribution companies has become riskier and that investors have many more investment choices due to globalization and privatization. Because these factors have combined to lessen investor interest in gas distribution companies, Mr. Olson contended that the trend could only be reversed if the Commission abandons traditional models derived from academic theory in favor of a comparative earnings approach. As an equity analyst, Mr. Olson urged adoption of a return on equity based on the most recent five-year average of the S&P 400, which would result in a 22.22% return on equity for Consumers. In any event, Mr. Olson contended that his analysis supported Mr. Vlides' testimony that Consumers' return on equity should be no less than 12.25%.

The Staff presented the testimony of Brian L. Ballinger, Senior Economist in the Commission's Financial Analysis Section of the Licensing and Enforcement Division. Mr. Ballinger testified that he relied upon the DCF and CAPM methodologies in determining a range of reasonable rates for Consumers' rate of return on common equity. Further, Mr. Ballinger stated that Consumers' and CMS's financial data should not be used to determine the financial condition of Consumers' gas operations because the operations of CMS, CMS's unregulated affiliate, CMS Enterprises, and Consumers' electric division, and are far more risky than Consumers' gas division.

Mr. Ballinger used two groups of proxy companies to approximate Consumers' return on equity. One group was made up of selected utilities having gas only operations. The other group was comprised of utilities having both electric and gas operations. Other criteria included the amount of net plant and the bond ratings. Each of Mr. Ballinger's two groups had nine companies, as shown on Exhibit S-117, Schedule D-5. According to Mr. Ballinger, the two groups of utilities were of comparable risk to Consumers and were suitable for estimating Consumers' cost of common equity. For 2001, Mr. Ballinger's gas company group had an average return on equity of 10.44% and the combination group had a return of 13.21%. Given that Consumers' gas division experienced an actual return of 11.77% through June 2001 and the total company earned 15.2% on its average common equity, Mr. Ballinger believed that Consumers' current returns appear to be higher than necessary to satisfy investors.

Using the DCF methodology, Mr. Ballinger calculated dividend yields of 4.77% and 5.11% for his gas and combination groups, respectively. These dividend yields were calculated by using the average of the high and low prices for each month from August to October 2001. The dividend yields were then adjusted by annualizing each company's latest quarterly dividend rate. The results were combined with Mr. Ballinger's projected growth rates for both groups of companies to derive a DCF equity cost of 11.01% for the gas only group and 11.38% for the combination group.

Mr. Ballinger explained that his CAPM analysis focused on data since 1958 for estimation of the risk premium of a security. According to Mr. Ballinger, the risk premium for the time span from 1958 to 2000 was 6.98%, whereas the risk premium for the time span between 1926 to 2000, which formed the basis of Mr. Vlisides' CAPM analysis, was 7.8%. The risk-free rate used by

Mr. Ballinger was 5.7%, which he estimated after considering the forecasted yield of 30-year U.S. Treasury securities and Consumers' recent sale of securitization bonds. Mr. Ballinger's CAPM results, shown on page 15 of Schedule D-5 of Exhibit S-117, reflect a cost of equity of 10.06% using the data from 1958 to 2000 and 11.08% if data from the entire period of 1926 to 2000 were to be used.

Mr. Ballinger believed that it would be inappropriate to include flotation cost expenses in Consumers' cost of equity because Consumers will not be issuing any new shares and because its parent company, CMS, has no plans to do so either.

Based on his studies, Mr. Ballinger recommended that Consumers' return on equity be set at 11%, which is the midpoint of the range of 10.75% to 11.25%.

The Attorney General supported the Staff's position because Consumers' position, which reflects an increase over its prior authorized rate of return, lacks credibility in light of the numerous interest rate cuts made during the past year by the Board of Governors of the Federal Reserve System (Federal Reserve Board).

Although ABATE did not sponsor a witness with regard to any cost rate issues, in its brief ABATE urged the Commission to adopt 10.75%, which is the low end of Mr. Ballinger's range of reasonable rates, for Consumers' return on equity. According to ABATE, lower interest rates and returns experienced by other sectors of the economy make a 10.75% return more than generous for Consumers.

Mr. DeWard testified that the proposal by Mr. Vlissides to set Consumers' rate of return on common equity at 12.25% is out of step with the current condition of the economy. According to Mr. DeWard, Consumers should not be permitted to earn a pretax rate of return of 18.85% when the current returns on savings accounts and money market funds are only 1% to 3%. He was also

concerned that Consumers' current rates are based on a rate of return of 11.6% despite 11 reductions of interest rates during 2001 by the Federal Reserve Board.

Mr. DeWard urged the Commission to set Consumers' rate of return on common equity at 8.1%. He reasoned that many categories of interest rates have declined by roughly 3% since Consumers' rate of return was established at 11.6% in 1996. Therefore, he suggested a 300 basis point reduction associated with the general decline in interest rates and another 50 basis point reduction due to increased risk attributable to failure of Consumers' Midland nuclear plant.

The ALJ agreed with Consumers that an investor could reasonably perceive that the advent of gas customer choice could increase risk associated with Consumers' gas operations due to uncertainty regarding several factors such as the number of customers that will opt into the new program, the number of alternative suppliers that will compete for such customers, and the number of alternative suppliers that will contractually live up to supply obligations. However, the ALJ noted that Consumers did not quantify the increased risk presented by these factors. Accordingly, he stated that he could not determine with any degree of certainty how such factors might affect Consumers' ability to attract capital.

The ALJ also found that Consumers' case was flawed due to its failure to update its testimony and analysis in light of the slowing economy, the numerous interest rate cuts during 2001, and the terrorist attacks on September 11, 2001. The ALJ stated that these matters were highly significant external forces on the equity market that should not have been ignored. The ALJ also indicated that the inclusion of flotation costs by Consumers was not appropriate because Consumers, as a wholly-owned subsidiary of CMS, would never be in position to sell stock to the public. According to the ALJ, the Staff's position is superior to Consumers' position because the Staff's analysis is more current and factored these considerations into its analysis.

Finally, the ALJ found Mr. Olson's testimony to be incredible. According to the ALJ, Mr. Olson's recommendations to his clients that CMS was a "strong buy" in 2001 cannot be squared with his testimony that Consumers needs a return of 22% to attract capital.

Consumers filed exceptions to the ALJ's findings. According to Consumers, the ALJ's recommendation should be rejected for a number of reasons. First, Consumers contends that Mr. Ballinger's analysis contains a number of miscalculations that should be corrected. Citing Mr. Ballinger's concessions that (1) the dividend yield calculation in his DCF analysis contained flaws that were identified in Mr. Vlisides' rebuttal testimony and (2) that there was an error in the growth rate for one of his proxy companies, Consumers insists that the resulting corrections push the Staff's return on equity value above the high end of the range recommended by Mr. Ballinger.

Next, Consumers argues that although the ALJ recognized that Consumers is facing increased risks, he failed to adjust the return on equity recommendation upward to account for the increased risk because he could not quantify the appropriate level of risk to assign. Citing the February 5, 1996 order in Case No. U-10685, Consumers states that the absence of a precise quantification of such risks does not preclude increasing the return to reflect a higher level of risk.

Moreover, Consumers maintains that the range of bond ratings shown on Exhibit S-117 demonstrate that the companies contained in Mr. Ballinger's two proxy groups have higher ratings than Consumers, which means that Consumers has more risk, which should be reflected in a higher rate of return.

Consumers also contends that the evidence presented by Mr. Vlisides and Mr. Olson supports the conclusion that earnings growth rates provide the best proxy in this case for investor expectations of growth. According to Consumers, Mr. Vlisides used earnings growth rates in his DCF analyses. In contrast, Mr. Ballinger used dividend growth rates and book value growth rates

in addition to earnings growth rates, which Consumers maintains skewed Mr. Ballinger's calculations downward from where they would be if only earnings growth rates had been used.

It is Consumers' position that the mathematical result of using Mr. Ballinger's data (as appropriately corrected) for the earnings growth rates identified by Mr. Ballinger for his proxy companies causes the average growth of the companies in both of his proxy groups to increase to the point that, when combined with the corrected dividend yields, the return for his gas group increases to 12.35% and the return for the combination group increases to 12.30% and that using Mr. Ballinger's earnings growth rates for the growth rate component increases the results from the DCF analyses for both of his proxy groups above the 12.25% return requested by Consumers in this case.

Consumers also attacks the ALJ's reasons for rejecting Mr. Vlisides' DCF and CAPM analyses. In particular, Consumers stresses that Mr. Vlisides' failure to update his analyses in light of numerous short-term interest rate cuts by the Federal Reserve Board is not surprising because equity investments are long-term investments that are not driven by short-term interest rates. In any event, Consumers insists that an 11.0% return on equity is inadequate to attract investors. Citing Mr. Olsen's comparative earnings analysis, Consumers maintains, "it would be completely inadequate to set the return on equity below 12.25%." 5 Tr. 406.

Finally, Consumers contends that the ALJ erred by ignoring flotation costs in determining Consumers' return on equity. According to Consumers, flotation costs are embedded issuance costs that should be included in this case in calculating the authorized return on equity. Indeed, Consumers insists that the recoverability of such issuance costs in the return on equity was upheld in Attorney General v Public Service Comm, 136 Mich App 515, 521; 338 NW 2d 351 (1984).

Therefore, Consumers argues that the Commission should determine its return on equity through use of a 3% flotation cost rate.

In response, the Staff argues that Mr. Olsen's testimony has been discredited by the recent collapses of WorldCom and Enron. According to the Staff, investors in those companies have learned that high returns are accompanied by high risks. The Staff also argues that an 11.00% return is sufficient to assure investor confidence and attract capital. Citing current information regarding long-term treasury bills and utility bond yields, the Staff contends that an 11.0% return for Consumers is adequate to assure its ability to raise new funds. Finally, the Staff contends that the recommended return on equity of 11.0% is reasonable because Consumers has not demonstrated that such a return would adversely affect its current bond ratings.

The Attorney General contends that Consumers' position lacks credibility. Citing Consumers' current return on equity of 11.6% and numerous interest rate cuts by the Federal Reserve Board, the Attorney General insists that the Staff's position of 11.0% is consistent with external trends in capital markets. According to the Attorney General, there is no credible evidence that a return of 11.0% will render Consumers unable to attract capital in the future.

ABATE also supports the recommendation in the PFD. According to ABATE, Mr. Ballinger dispelled Consumers' contention that the corrections suggested by Consumers should result in any changes to his original position. Indeed, ABATE maintains that there is ample evidence to support a finding that 11.0% is a generous return on equity in the current low-interest rate environment. Further, ABATE insists that Consumers' risk-related concerns are self-made problems associated with questionable financial activities.

The United States Supreme Court has detailed the conceptual standards to be followed in establishing rates to meet the constitutional requirements. The leading cases are Bluefield, supra, and Hope, supra. In the Bluefield decision, the Supreme Court stated as follows:

What annual rate will constitute just compensation depends upon many circumstances and must be determined by the exercise of a fair and enlightened judgment, having regard to all relevant facts. A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time, and become too high or too low by changes affecting opportunities for investment, the money market, and business conditions generally.

Bluefield, supra, at 262 US 692-693.

In the Hope decision, the Supreme Court stated:

The rate-making process under the Act, i.e., the fixing of “just and reasonable” rates, involves a balancing of the investor and the consumer interests. Thus we stated in the Natural Gas Pipeline Co. Case that “regulation does not insure that the business shall produce net revenues.” [Citation omitted.] But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view, it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. [Citation omitted.] By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

Hope, supra, at 302 US 603.

Applying these principles to this case, the Commission finds that neither the position of Consumers nor the position of the Staff should be adopted. Compared to Mr. Ballinger’s data, the

data underlying Mr. Vlisides' testimony were stale because of the passage of time and due to intervening events that are not reflected in the data. Mr. Vlisides' DCF analysis uses price information and growth rates projection made in the first quarter of 2001. Subsequent events, including numerous interest rates reductions, the entry of the United States economy into a recession in March 2001, and the tragic terrorist attacks on September 11, 2001, are not factored into Mr. Vlisides' analysis. Mr. Vlisides had a chance to update his DCF, but failed to do so.

Mr. Vlisides' CAPM analysis is also suspect for several reasons. He used a risk-free rate of 6.7% based on May 2001 data as shown on Exhibit A-50. When questioned about his use of that May 2001 data, Mr. Vlisides conceded that "[f]rom the events that have occurred from September 11th, everything has changed. Everything is inappropriate." 7 Tr. 990. Mr. Ballinger's testimony, which was prepared and filed after September 11, 2001, relied on a risk-free rate of 5.7% that was based on the rate of 30-year treasury securities and Consumers' issuance of AAA-rated securitization bonds at an average rate of 5.305%. The Commission finds that Mr. Ballinger's risk-free rate of 5.7% is far more reasonable than Mr. Vlisides' risk-free rate, which calls into question the validity of Mr. Vlisides' results.

Additionally, Mr. Vlisides' recommended 12.25% return on equity was based on the inclusion of flotation costs of 3%. Such costs are associated with the issuance of stock. As a wholly-owned subsidiary of CMS, Consumers does not issue stock. Further, Mr. Vlisides knew of no plans by CMS to issue stock. For this reason, there is considerable doubt whether Mr. Vlisides' inclusion of flotation costs is appropriate.

The Commission finds Mr. Olson's testimony is not consistent with the principles of Bluefield and Hope, and was properly rejected by the ALJ. Mr. Olson would have the Commission set Consumers' return on equity at a rate equivalent to the rate of return expected by investors

in a wide variety of unregulated companies in non-utility industries, which ignores the fact that the Constitution only entitles a utility to earn a return on its rate base equal to that earned on similar investments attended by corresponding risks and uncertainties. A regulated utility is entitled to a return sufficient to assure confidence in the financial integrity of its enterprise so as to maintain its credit and to attract capital. It is not entitled to returns associated with companies involved in riskier enterprises.

However, while the Commission finds that it cannot adopt the recommended return on equity of 12.25% proposed by Mr. Vlisides, it also acknowledges that Consumers has raised some concerns regarding Mr. Ballinger's proposed rate of return of 11.0%.

With regard to Mr. Ballinger's DCF analysis, it appears that the methodology described in his testimony was not followed to calculate dividend yields for his proxy groups. The DCF dividend yield methodology correction proposed by Consumers results in an average return on equity of 11.02% for the gas utilities and 11.38% for the combination utilities, which averages out to 11.2%. A second correction proposed by Consumers concerns the growth rate of one of Mr. Ballinger's combination utility proxy companies, which increases the average return on equity of 11.38% for the combination utilities to 11.58%. Thus, the corrections result in an average return on equity of 11.02% for the gas utilities and 11.58% for the combination utilities, which average out to 11.3%.

While the Staff insists that Consumers' corrections would not change Mr. Ballinger's ultimate opinion regarding Consumers' return on equity, the Commission concludes that some adjustment to Mr. Ballinger's range of reasonable rates is appropriate. Accordingly, the Commission is persuaded that Consumers' return on equity should be set at 11.40%, which is slightly above the range of reasonable rates supported by Mr. Ballinger. In so doing, the Commission provides for a slight upward increase in the return on equity proposed by Mr. Ballinger to address Consumers'

concern over Mr. Ballinger's arithmetical errors. However, the Commission does not agree with Consumers that the test year return on equity should be increased due to any perceived increased risk recognized, but not provided for, at page 34 of the PFD. On this record, the Commission is not persuaded that the advent of customer choice has increased the risk of the gas distribution business conducted by Consumers.

Finally, in determining that the authorized return on common equity should be 11.40%, the Commission need not make a finding regarding the flotation cost adjustment proposed by Consumers. Because the process of setting the rate of return is one of judgment, ignoring the flotation adjustment will not have a material effect on the Commission's finding, which is based on record evidence. Moreover, nothing in Attorney General v Public Service Comm, *supra*, cited by Consumers indicates that the Commission's broad discretion to determine a reasonable rate of return is limited by a rote application of economic models or financial formulas.

Long-term Debt Cost

Consumers proposed a long-term debt cost of 7.13%. Based on more recent data, the Staff calculated a long-term debt cost of 6.42%.

The ALJ recommended adoption of the Staff's position. In so doing, the ALJ rejected Consumers' arguments that the Staff's recommendation needed to be adjusted from 6.42% to 6.51% due to several alleged flaws.

Consumers' exception is devoted to describing the four corrections that it deems appropriate. The Staff's reply to exceptions does not contest the validity of the corrections, but insists that a long-term debt rate of 6.42% remains reasonable in light of interest rate reductions that occurred subsequent to the close of the record.

The Commission agrees with Consumers that the corrections described in its brief and exceptions should be made, which increase the cost of long-term debt calculated by the Staff from 6.42% to 6.51%. The Commission recognizes that based on present conditions, the Staff's long-term debt cost rate might remain reasonable. However, the argument that appears in the Staff's reply to exceptions on this issue is based on information that is not contained in the record. The Commission is limited to record evidence, which supports Consumers' exception.

Short-term Debt Cost

Consumers urged the Commission to use a short-term debt cost rate of 7.20% on Exhibit A-10. Based on more recent data, the Staff proposed a short-term debt cost rate of 3.11%, as calculated on Exhibit S-117, Schedule D-3.

The ALJ recommended adoption of the Staff's proposed rate. He reasoned that the Staff used more current short-term interest rate data, which more accurately represented current market conditions. Further, the ALJ stated that the Staff's rationale for the use of the more current data was sound and that Consumers had not offered a sufficient explanation why the more current data should not be used.

In its exceptions, Consumers insists that its May 2001 data are a better basis for determining short-term interest rates during the test year than the Staff's use of data from October 2001. According to Consumers, the Staff's data is skewed due to its proximity to September 11, 2001 and due to the presence of hedges in some of the Staff's rates.

The Commission finds that the ALJ's recommendation should be adopted. Consumers' arguments present no valid reasons for ignoring the more recent data regarding short-term interest rates that was presented by the Staff. Indeed, adoption of Consumers' position would require the Commission to ignore several short-term interest rate cuts that occurred subsequent to May 2001.

Other Debt Cost Rates

All parties agreed that the cost rates for Consumers' preferred stock and customer deposits should be set at 4.46% and 9%, respectively. The Commission finds that these values should be adopted. Further, the disagreement between Consumers and the Staff regarding whether there should be a category and a cost rate for other interest bearing items was resolved in Consumers' favor in the determination of the proxy capital structure.

Summary

Based on the Commission's findings, Consumers' overall cost of capital should be set at 7.45%, which is calculated as follows:

<u>Description</u>	<u>Amount</u>	<u>Ratio</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Long Term Debt	\$2,987,817	47.94%	6.51%	3.12%
Customer Deposits	\$14,501	0.23%	9.00%	0.02%
Short Term Debt	\$279,268	4.48%	3.11%	0.14%
Preferred Stock	\$44,160	0.71%	4.46%	0.03%
Common Equity	\$2,156,237	34.59%	11.40%	3.94%
Deferred ITC	\$1,709	0.03%	0.00%	0.00%
Deferred FIT	\$610,715	9.80%	0.00%	0.00%
Other Interest Bearing Accts. JDITC	\$39,000	0.63%	9.83%	0.06%
Def JDITC – Long Term Debt	\$56,478	0.91%	6.51%	0.06%
Def JDITC – Preferred Stock	\$844	0.01%	4.46%	0.00%
Def JDITC – Common Equity	<u>\$42,147</u>	<u>0.68%</u>	11.40%	<u>0.08%</u>
Total JDITC	<u>\$99,469</u>	<u>1.60%</u>		<u>0.14%</u>
TOTAL	<u>\$6,232,876</u>	<u>100.00%</u>		<u>7.45%</u>

Multiplying Consumers' test year rate base of \$1,378,295,000 by the overall cost of capital of 7.45% produces Consumers' test year required income amount of \$102,683,000.

V.

THROUGHPUT

Throughput is the total sales and transportation volumes delivered to end-users. It is calculated in a gas rate case as a prerequisite to projecting test year revenues and is also used in determining rate design issues.

The starting point for estimating Consumers' test year throughput is its 2000 historical sales and transportation volumes of 334,571,633 Mcf, as shown on Exhibit A-11, Schedule F-2. The parties agree that the historical data should be weather normalized² and adjusted for a slight increase in the heat content of the gas.³ The other three adjustments proposed by Consumers were rejected by the ALJ. Consumers did not file exceptions to the ALJ's recommendations on those issues.

Therefore, the Commission finds that Consumers' throughput for the test year is 336,969,795 Mcf, as proposed on Exhibit S-145.

VI.

ADJUSTED NET OPERATING INCOME AND REVENUE REQUIREMENT

To determine whether there is a revenue deficiency or sufficiency, it is necessary to project Consumers' net operating income for the test year. The utility's net operating income is equal to its operating revenues less allowable expenses, taxes, and depreciation.

² Consumers accepted the Staff's proposed weather-normalization modification, which added 4,363,000 Mcf of throughput. In so doing, Consumers abandoned its contention that the Commission should adopt a leap year adjustment.

³ The heat content adjustment decreased throughput by 1,964,838 Mcf.

Consumers' revenues are derived from three main sources -- sales, transportation, and miscellaneous. As filed, Consumers' projected test year total revenues, including those of MGS, were \$1,189,050,000. Of that amount, Consumers projected \$1,087,785,000 for sales, \$47,829,000 for transportation, and \$53,436,000 for miscellaneous. Consumers adjusted its sales revenues upward by \$2,457,000 due to its acceptance of the Staff's weather normalization adjustment. Consumers' transportation revenues were adjusted upward by \$221,000 for the same reason. Consumers did not adjust its miscellaneous revenues.

During the course of the proceeding, Consumers conceded a number of issues regarding expense items, including the Staff's positions on true-up adjustments to federal income tax (FIT) expense and Michigan single business tax (SBT) expense, Commission assessment expense, executive incentive compensation program expenses, save and share expenses, weather normalization, executive bonuses, a life insurance refund, advertising, American Gas Association dues, economic development, natural gas vehicles, and Y2K expenses. In its brief, Consumers subtracted the cost of gas (\$681,079,000), company use gas (\$7,729,000), other O&M expenses (\$275,437,000), book depreciation (\$125,871,000), and several categories of taxes (\$50,579,000) from Consumers' total adjusted test year revenues of \$1,191,728,000. Subtracting these expenses, which collectively totaled \$1,140,695,000, from Consumers' test year revenues results in net operating income, adjusted for AFUDC, of \$52,122,000.

Consumers' projections for its test year revenues and expenses deviated significantly from its 2000 historical year data. The other parties raised numerous objections to Consumers' adjustments that were ruled upon in the PFD. The Staff maintained that Consumers' test year net operating income should be set at \$80,270,000. The Attorney General concurred with the Staff's analysis and calculations. On Exhibit I-166, Mr. DeWard proposed 12 operating revenue and

expense adjustments that collectively would reduce Consumers' proposed revenue requirements by \$105,267,307 from the amount requested in Consumers' rebuttal filing.

In arriving at his determination of Consumers' test year net operating income, the ALJ first addressed Consumers' proposed other O&M expenses. In so doing, he found that Consumers' approach to projecting its test year other O&M expenses was flawed. According to the ALJ, Consumers failed to explain how it arrived at its projected expenditures. He stated that "[t]here are just too many unknowns." PFD, p. 43. Additionally, the ALJ rejected Consumers' contention that its management could not change anticipated expenditures at its discretion. Citing the testimony of Mr. English and Mr. Preketes, the ALJ remarked that there was no guarantee that Consumers would spend at the levels proposed in this proceeding.

The ALJ expressed a preference for the Staff's approach, which primarily relied on 2000 historical year data escalated for inflation. The PFD indicates that the Staff's use of inflation adjusted 2000 historical year data was accepted as appropriate for many of Consumers' programs and activities, including those involving material condition; corrosion control; damage prevention; succession planning; appliance service and repair; engineering, planning, and scheduling; operator qualification; uncollectibles⁴ and customer billing; metering technology and management systems; purchasing, technology, and customer contact services; compression, transmission, and storage; and general office and field facilities.

Consumers' pipeline integrity program presented a different situation. Consumers included \$3,036,000 in its 2002 test year for other O&M spending to respond to various federal safety initiatives that arose subsequent to its 2000 historical year. Consequently, the Staff's approach of

⁴ At the hearing and in its brief, the Staff conceded that it had understated Consumers' uncollectibles expense. Accordingly, the Staff adjusted its revenue deficiency to correct for the error, which increased the amount of the rate increase supported by the Staff from \$28.5 million to \$29.9 million.

escalating 2000 spending levels made no provision for test year 2002 expenditures for the pipeline integrity program because that program was not part of the other O&M expenses for 2000.

Notwithstanding his finding that Mr. Preketes' testimony was "convincing that there is an apparent need" for the program and that there was a "strong possibility" that Congress will mandate the other O&M spending by all gas utilities, the ALJ rejected Consumers' proposal because it was not sufficiently substantiated by Consumers' proofs.

With regard to certain employee-related expenses, the ALJ stated that Consumers had revised its request to dollar levels generally acceptable to the Staff. He indicated that Consumers' recommendations were summarized in Appendix C of Consumers' brief and included employee pensions, health care, and life insurance for retirees; health care and life insurance for active employees; and the employee savings plan.

The ALJ also agreed with Consumers' contention that its other O&M expenses should reflect \$3,935,000 associated with a realignment of costs from capital spending to other O&M spending, which was not represented in the company's 2000 historical data.

Another area in which the ALJ agreed with Consumers involved application of the Massachusetts formula, which governs how administrative and general expenses associated with Consumers' parent, CMS, are apportioned among Consumers and its affiliates.

Revisions Related to PFD Corrections

The starting point for analyzing Consumers' revenue deficiency ordinarily would be the ALJ's net operating income in the PFD. However, most of the parties agree that the net operating income amount of \$79,758,000 set forth on page 65 of the PFD needs to be adjusted. They suggest that the amount intended by the ALJ as Consumers' net operating income is \$79,862,000.

After examining their documentation, the Commission agrees. It appears that the difference involved use of a misread number from Exhibit S-124.

Another obvious correction suggested by some of the parties, involves a \$1.4 million upward adjustment to the revenue deficiency due to increased uncollectibles expense that the Staff conceded in its brief should be made. Again, because there is little controversy about this adjustment and because it is readily verifiable, the Commission finds that the \$1.4 million adjustment should be made.

Likewise, two adjustments recommended by the ALJ on page 94 of the PFD involving a \$151,000 cost decrease for SBT expense and \$4,000 increase for sales and use taxes, which were not reflected in the ALJ's calculations, need to be incorporated.

Major Disputed Expense Issues

1. Massachusetts Formula

The Staff opposed Consumers' use of the Massachusetts formula in this proceeding because its parent, CMS, includes net investment in affiliates that it does not operate and, as a result, the corresponding revenue and wage components are lacking from the Massachusetts formula, which causes Consumers to absorb a higher percentage of the costs. Accordingly, the Staff proposed a \$253,000 reduction in Consumers' expenses.

The ALJ rejected the Staff's proposed reduction. He found that the Staff had not justified abandonment of the long-standing use of the Massachusetts formula by Consumers.

In its exceptions, the Staff maintains that it is not urging abandonment of the Massachusetts formula for book accounting purposes. Rather, the Staff insists that the adjustment should be limited to ratemaking purposes to remedy Consumers' accounting for costs in a manner that is

unfair to its ratepayers. According to the Staff, its proposed disallowance represents a more reasonable approach than that produced by rote application of the Massachusetts formula.

Consumers responds that the Massachusetts formula uses a consistent, straightforward approach for cost allocation that has been accepted in the past by the Commission, as well as by the FERC. According to Consumers, the Massachusetts formula was originally conceived as a method for allocating state tax expense and was subsequently adopted for allocating administrative and general expense in diversified corporations. Consumers states that it has used this formula since 1987 and that the Staff has reviewed the use of the Massachusetts formula on several occasions, including in Cases Nos. U-9709 and U-10335.

The Commission finds that the Staff's exception should be granted. In the July 11, 2001 order in Case No. U-12342, the Commission rejected a utility's contention that its reliance upon the Massachusetts formula justifies its proposed cost allocation practices absent an explanation as to how the formula works and evidence that it produces a reasonable allocation of costs. Here, Staff witness Mogis gave a rationale for the Commission to determine that the Massachusetts Formula, as used by Consumers, does not result in a reasonable allocation of parent company indirect overhead costs to ratepayers. Mr. Mogis stated that a majority of the costs that are allocated under the Massachusetts formula are Board of Directors fees and expenses and stockholder relations expenditures, a major component of which is the printing and distribution of the CMS Annual Report to its stockholders. Therefore, the Commission is persuaded that the Staff's alternative method for cost allocation is more reasonable and should be adopted.

2. Accounting for Workload Realignment

Mr. Preketes testified that, due to changes in the way that certain costs are apportioned between capital and other O&M expenses during the test year, Consumers will eliminate

\$3,935,000 in capital expenditures and record a corresponding \$3,935,000 increase in its annual other O&M expenditures as the result of a “true-up” of accounting practices carried over from prior years.

The Staff objected to the company’s treatment of this accounting change and its effects on rate base and other O&M expenditures. The Staff insisted that if this change were appropriate, it should have occurred in 1996-1997. The Staff stated that by waiting until 2002 to implement the change, Consumers has optimized its position in this proceeding at the expense of its ratepayers. The Staff also complained that Consumers’ adjustment was not supported by adequate evidence. Rather, the Staff maintained that its position more appropriately accounted for Consumers’ capital and other O&M expenditures.

The ALJ’s ruling on this issue is confusing. He did not address the issue when he discussed Consumers’ proposed capital spending wherein he adopted all of the Staff’s positions. However, in discussing Consumers’ other O&M expenditures, the ALJ adopted Consumers’ position because he “was not able to find any opposition to this proposal by Staff or other party.” PFD, p. 54. However, despite this statement, the ALJ failed to add \$3,935,000 to his determination of Consumers’ other O&M expenditures.

In its exceptions, the Staff maintains that, contrary to the ALJ’s finding, it actively opposed Consumers’ position on this issue. In so doing, the Staff contends that Consumers’ ratepayers are being treated unfairly because Consumers did not adjust 2000 historic plant balances for the support costs that were not properly reflective of its employees’ responsibilities subsequent to the workload realignment that should have occurred in 1996-1997. Further, the Staff argues that there is no guarantee that Consumers will actually change its accounting for workload realignment in

2002. Finally, the Staff insists that Consumers' projection of the amount of the adjustment is not supported by the evidence.

In reply, Consumers contends that the Staff has not challenged the propriety of the accounting change, only its timing. According to Consumers, the timing of the adjustment is not a reason to ignore it for the purposes of establishing just and reasonable rates. Consumers also insists that the Staff position is internally inconsistent. Consumers maintains that the Staff asserts that Consumers should account for its operations correctly, but then objects when Consumers proposes an adjustment to do so.

Consumers also argues that the Staff failed to present any evidence on this issue. Consumers insists that if the Staff believed that Consumers was not in compliance with generally accepted accounting principles (GAAP) in the past, it should have presented some evidence to support that contention. Rather, Consumers states that the accusations made by the Staff are baseless and irrelevant to a resolution of this issue. In any event, Consumers points out that the Staff never argued that the accounting changes implemented by Consumers are inappropriate.

The Commission concludes that the full amount of the \$3,935,000 other O&M increase sought by Consumers should be approved. The Commission is not persuaded that adoption of Consumers' proposal will be unfair to ratepayers. The Staff does not dispute the reasonableness of the costs being accounted for or the appropriateness of the proposed accounting change. Only the timing of the accounting change is at issue.

The Commission finds that Consumers' delay in implementing the accounting change did not have a significant adverse effect on its ratepayers. In the future, Consumers would be well advised to consult with the Staff in regard to such accounting revisions to ensure that the timing of an otherwise reasonable accounting change does not become the basis for a disallowance.

3. Health Care and Employee Benefits

At page 57 of the PFD, the ALJ summarized Consumers' position on the four types of expenses covered by this broad category. In so doing, he seems to have agreed with Consumers' positions on the basis that the Staff found Consumers' requests to be generally acceptable.

In its exceptions, the Staff insists that it did not concede the appropriateness of Consumers' positions on these issues. Rather, the Staff contends that differences between its positions and those of Consumers, which are shown on the table below, are significant.

<u>Expense type</u>	<u>Amount of difference</u>
Employee Pension	\$284,000
Health Care/Life Ins.-Post Retirement	\$3,559,000
Health Care/Life Ins.-Active Employees	\$99,000
Employees Savings Plan	<u>\$627,000</u>
Combined Difference	<u>\$4,569,000</u>

The Staff states that it adjusted Consumers' historical benefits expense amounts only for known and measurable changes. The employee savings plan and active employee health care and insurance costs were adjusted for inflation for 2001 and 2002. Pension costs and post-retirement health care and insurance costs were adjusted for inflation and other known and measurable amounts that were supported by evidence presented in this case. Citing the ALJ's general acceptance of most of its other O&M costs, the Staff contends that his findings on those matters should be applicable to the company's employee benefit expenses. Finally, the Staff insists that the Commission should not increase expenses by the \$4,569,000 difference in benefit costs because the Staff's calculations are more reasonable than Consumers' and are based on sound ratemaking principles.

Consumers responds by arguing that it provided detailed testimony concerning how its pension and health care expenses were projected. According to Consumers, it relied upon its actuary for the proper level of 2002 expenses. Consumers criticizes the Staff's approach for determining test year pension expense. The Staff used a 2001 figure, made one adjustment to reflect a transition obligation amortization, and then simply adjusted the resulting amount for inflation. Consumers contends that the Staff's approach is inconsistent with GAAP and Financial Accounting Standards (FAS) 87 and 106. With regard to health care benefits, Consumers insists that the Staff's approach of escalating 2001 expenses for inflation at 2.4% is inconsistent with FAS 106 and ignores well-documented trends in health care costs, which predict double-digit increases.

The Commission finds that the ALJ's recommendation in this area should be adopted with one modification. The Commission is persuaded that Consumers carried its burden of proof with regard to employee pensions, post-retirement health care/life insurance, and active employee healthcare/life insurance. However, because Consumers' costs for its employee savings plan are primarily tied to wage increases, the Commission is persuaded that the Staff's approach of adjusting the historical amount for inflation more accurately provides for this expense.

4. Safety Related Other O&M Issues

Included in this broad category of expenses are a number of topics addressed by Consumers' witness Preketes, including material condition, pipeline integrity, corrosion control, damage prevention, and operator qualification. In each case, the ALJ determined that the Staff's expense amount, which was determined primarily through use of an inflation adjustment to the historical year expenditure level, should be adopted.

In its exceptions, Consumers maintains that Mr. Preketes' testimony demonstrates the company's need to spend more on these programs than proposed by the Staff. Further, Consumers insists that Mr. Preketes' descriptions are more than sufficient to meet the "known and measurable" standard. A review of Mr. Preketes' testimony indicates that Consumers planned to spend \$12,382,000 during 2002 for the material condition program. He explained that the purpose of that program is to address the replacement of pipelines, regulation, and metering facilities, additions to gas facilities due to obsolescence and deterioration, and the addition of new facilities to upgrade equipment and instrumentation. According to him, the safety and reliability of Consumers' gas system requires that Consumers update and replace these facilities.

Consumers originally planned to spend a total of \$3.04 million on other O&M costs for its pipeline integrity program, which was revised downward by \$2.2 million. However, Mr. Preketes stated that those savings would be offset by increased other O&M expenditures for increased security of \$0.736 million and use of temporary rather than permanent pipeline inspection equipment of \$1.464 million.

Mr. Preketes stated that Consumers recently completed the seventh year of a ten-year remediation plan to repair or replace all non-compliant underground and above ground pipe as part of an agreement with the Commission's Gas Safety Division. The plan includes mileage goals for each year, and during the first few years, the longest sectors were restored. Because Consumers is now working on the shorter sectors, there are a greater number of sectors involved in reaching the mileage goals in the plan. Regardless of its length, each sector requires similar diagnosis and repair time. Therefore, the total cost in 2001, 2002, and 2003 is greater than that in the first few years of the 10-year program. He also stated that atmospheric corrosion expenditures for Consumers and MGS would be more expensive because the paint used until the early 90's for

atmospheric corrosion protection contained lead, which was subsequently prohibited. Therefore today, more expensive special procedures and equipment must be used to deal with the loose and flaking lead base paint.

Mr. Preketes testified that the increase in underground cathodic protection in 2002 over 2000 would be \$934,000. He also stated that atmospheric corrosion work on distribution, transmission, storage equipment, meter stands, pipeline, and regulation equipment in year 2002 for Consumers is planned to be \$2,390,000 higher than in year 2000. For MGS's storage wellheads and structures, the increase would be \$603,000 for 2002. Finally, he indicated that, at the completion of the current 10-year remediation program, Consumers would continue to incur a similar level of expenses for continuing corrosion control efforts.

Mr. Preketes described Consumers' damage prevention program as the process by which the utility prevents excavation dig-ins to underground facilities. It includes elements such as planning, effective use of one-call systems, accurate location and marking of underground facilities, adherence to safe digging practices, proper placements of facilities, and strong public education and awareness. As shown on Exhibit A-66, Consumers planned to increase other O&M expenditures by \$2,443,000, including inflation, for damage prevention in 2002, which is \$2,179,000 higher than the Staff's inflation adjustment.

Mr. Preketes also explained his company's needs with regard to operator qualification activities. According to Mr. Preketes, Consumers' operator qualification program was established due to a federal mandate designed to ensure that pipeline operators develop, maintain, and execute a qualification program for individuals performing certain tasks on pipeline facilities. Consumers maintains that it will be required to spend \$6,563,000, or \$2,255,000 more than the Staff's case allotted for these activities.

The Commission finds that Mr. Preketes' testimony adequately describes Consumers' need to increase its spending in these areas to ensure the safety and reliability of its gas system. The Commission strongly supports gas safety programs and finds that such expenditures are in the public interest. Therefore, the Commission finds that Consumers' 2002 other O&M expenditures should be increased to include the additional spending proposed by Consumers for these programs.

The Commission recognizes that some of the other O&M expense categories for which additional spending levels supported by Consumers are being approved by this order may correspond to rate base issues wherein Consumers' positions have been rejected. The Commission does not consider these results to be incongruous. As previously noted, the Staff's position regarding Consumers' test year rate base included almost \$150 million of capital expenditures during 2001 and 2002, which undoubtedly would contribute to some additional O&M expenditures. Further, it is reasonable to assume that Consumers will have less flexibility to curtail spending on safety-related projects, which makes increased spending on safety-related other O&M expenditures more likely.

Rejected Expense Issues

The Commission finds that Consumers' positions on the remaining disputed other O&M expense issues, which include succession planning, appliance repair plan/appliance repair, engineering/planning/scheduling, compression, transmission, and storage expenditures, field facility expenditures, uncollectibles/customer billing, metering technology/management systems, purchasing, technology/customer services, general office facilities, and customer uncollectibles reserve, should be rejected. In so doing, the Commission observes that the Staff's approach, which relies on historical expenditures escalated for inflation, should provide Consumers with adequate funds to pay for these costs. This is particularly true of several of the cost items that

have associated capital expenditures. It is the Commission's experience that capital expenditures frequently are made to obtain reductions in other O&M costs. For example, the installation of new equipment to replace obsolete equipment should lower repair costs.

For other items, such as succession planning, the Commission finds Consumers' arguments unpersuasive. Simply because its workforce is aging, does not mean that Consumers' succession planning costs will outpace inflation to the degree projected by the company. The same is true of Consumers' appliance repair plan/appliance repair programs. Consumers offered no explanation for why its costs for these programs would be expected to increase by more than the inflation rate.

Other Cost Determinations

1. Lost and Unaccounted for Gas Costs

The ALJ determined that the Staff's proposal regarding lost and unaccounted for gas costs applicable to sales volumes, which is based on five-year historical data, should be adopted by the Commission. The amount proposed by the Staff for this expense is \$5,936,000, which is adopted due to the agreement between the parties on this issue. Because transportation customers contribute gas-in-kind to cover Consumers' expenses for lost and unaccounted for gas, the discussion of their contribution to this category of costs appears in the portion of the order dealing with tariff provisions.

2. Manufactured Gas Plant Expenses

Given the Commission's determinations on the manufactured gas plant issues related to rate base, which adopted the Staff's position on those issues, consistency requires the Commission to adopt the Staff's position with regard to the proper treatment of such 2002 test year expenses.

3. Taxes

With regard to FIT expenses, the ALJ found that Mr. DeWard's position, which supported a \$12.389 million reduction in Consumers' FIT expense, should be rejected. Mr. DeWard had maintained that Consumers' proposed FIT amount was sustainable only if the company could show that flow-through accounting was appropriate in the past and that ratepayers benefited from the accounting. Mr. DeWard insisted that the flow-through amounts must appear in years of rate cases and not just in non-rate case years. In reaching his determination, the ALJ relied on the testimony and the arguments of Consumers and the Staff. They explained that the February 8, 1993 order in Case No. U-10083 provided that full normalization of all book/tax depreciation differences was required for all property placed into service after December 31, 1992. Further, because full normalization was not required for property placed into service before December 31, 1992, Consumers and the Staff insisted that the flow back of such items would increase tax expense in the historical test period.

Although Mr. DeWard's exceptions express broad dissatisfaction with the PFD and the Commission's December 20, 2001 order on partial and immediate relief, he has not specifically objected to the ALJ's ruling regarding his income tax argument. Therefore, the Commission finds that the ALJ's ruling should be adopted. In any event, the PFD contained a number of specific recommendations regarding appropriate tax expenses to be considered in the ratemaking process. No exceptions were filed with regard to those recommendations. The following are the amounts approved by the Commission:

Property Taxes	\$35,516,000
Other General Taxes	\$10,804,000
MSBT	\$6,560,000
FIT	\$23,276,000

4. Depreciation

The PFD relied on the Staff's calculation of depreciation for the test year. Having selected the Staff's rate base for use in setting rates, the Commission finds that it would be more appropriate to use the Staff's test year level of depreciation, which is \$122,288,000.

5. Job Development Investment Tax Credit (JDITC)

There were no differences in methodology between Consumers and the Staff over the calculation of JDITC. The numerical difference is the result of the different positions the parties have taken on other issues that offset the calculation.

The ALJ found that the Staff's calculation should be adjusted to include the \$150 million infusion of equity. As the Commission has adopted the January 3, 2002 equity infusion for ratemaking purposes, use of the ALJ's methodology is appropriate, as adjusted to reflect adoption of 6.51% as the cost rate for long-term debt.

Consumers' historical net operating income of \$65,008,000 and the adjustments made by the Staff, which totaled \$15,262,000, are set forth on Exhibits S-124 and S-130. The additional adjustments to net operating income made by this order reduce net operating income by a total of \$13,121,000 on a net basis and are set forth in the following table:

Category	Adjustments-net of taxes
Uncollectibles	\$892,000
MSBT rate change	(\$98,000)
Sales and use taxes	\$3,000
Interest synchronization	\$4,000
Pro forma tax savings	(\$4,000)
Other O&M adjustments:	
Material condition	\$140,000
Pipeline integrity	\$1,936,000
Corrosion control	\$2,398,000
Damage prevention	\$1,389,000
Operator qualification	\$1,438,000
Employee pension	\$181,000
Post-retirement health care	\$2,269,000
Health care - active	\$63,000
Accounting for workload realignment	\$2,509,000
Total other O&M adjustments	\$12,324,000
Total adjustments	\$13,121,000

Summary and Calculation of Revenue Deficiency

Historical Net Operating Income	\$65,008,000
Staff Adjustments	\$15,262,000
Commission Adjustments	<u>(\$13,121,000)</u>
Adjusted Net Operating Income	<u>\$67,149,000</u>

Based on the above findings, the Commission finds that Consumers' revenue deficiency is \$55,728,000 calculated as follows:

Income Required	\$102,683,000
Adjusted Net Operating Income	<u>\$67,149,000</u>
Income Deficiency	\$35,534,000
Revenue Multiplier	<u>1.5683</u>
Revenue Deficiency	<u>\$55,728,000</u>

VII.

ALLOCATION

Cost Allocation

Having established Consumers' revenue deficiency, the Commission must now allocate costs and design rates in a way that both eliminates the revenue deficiency and establishes just and reasonable rates for all customer classes. Consumers, the Staff, and ABATE each presented a cost of service study. The differences between Consumers' study and the Staff's study were so minor that Consumers accepted the Staff's cost study with one exception, which concerns calculation of the residential customer charge.

ABATE's positions on cost allocation were presented by Nicholas Phillips, Jr., a consultant in the field of public utility regulation. Mr. Phillips maintained that Consumers' transportation customer rates result in an overcharge of \$15-\$16 million annually and that Consumers' current rates are not cost-based. Mr. Phillips believed that the rates of each customer class should be increased or decreased in this proceeding to produce revenues that are equal to the cost-of-service. He also stated that it is inequitable for transportation customers to subsidize the other rate classes.

Mr. Phillips contended that the "peak and average" allocation technique used by Consumers is flawed. According to him, investment in mains is more appropriately allocated on peak day demand instead of peak month demand. He also insisted that transportation customers should not be allocated any costs related to promotional and uncollectibles expenses.

Calculation of the Residential Customer Charge

Consumers proposed to apportion the residential class overall rate increase between the customer charge and the distribution charge. Scott B. Brockett, Consumers' Supervisor of Pricing and Revenue Forecasting, supported an increase in the residential monthly customer charge from

\$6.50 to \$8.00. Consumers presented a fully allocated cost study to use as a basis for setting the residential customer charge. According to Consumers, a conservative estimate of customer costs would justify a residential customer charge of \$10.37 per month.

Charles F. Belknap, Jr., Consumers' Supervisor of Planning and Financial Analysis, testified that labor overheads, including pensions and benefits, payroll taxes allocated to customer accounting, and customer services functions, supervision, and engineering O&M expenses, should be included in the calculation. Consumers' formula includes labor overheads to calculate customer-related costs, whereas the Staff's approach does not. Consumers argued that the Staff takes too narrow an interpretation of customer-related costs in this regard. Consumers recalculated the Staff's calculation, inserting customer-related labor overheads, but maintaining the exclusion of customer-related O&M supervision and engineering expenses, which produced a customer charge of \$8.40 per month. Consumers also determined that using its approach and the Staff's revenue requirement would yield a residential customer charge of \$9.64 per month.

The Staff's position, which was presented by William G. Aldrich, a Gas Cost of Service Specialist in the Commission's Gas Division, contended that Consumers was attempting to recover costs that are inappropriate for inclusion in the residential customer charge. He indicated that the Commission had previously rejected such an attempt in its March 11, 1996 order in Case No. U-10755. Accordingly, Mr. Aldrich urged rejection of Consumers' present bid to include labor overheads. Nevertheless, Mr. Aldrich supported increasing Consumers' customer charge to \$7.50 per month.

The ALJ found that the March 11, 1996 order in Case No. U-10755 controlled the outcome of this issue and he recommended approval of the \$7.50 per month customer charge supported by the Staff.

Contrary to the ALJ's recommendation, Consumers asserts that its proposal is supported by the controlling legal authority, the weight of the evidence, and by interpretation of the Staff's position in Case No. U-10755. Moreover, Consumers insists that the Staff's approach is inconsistent. Citing the Staff's overall cost of service study, Consumers stresses that Mr. Aldrich allocated employee pensions and benefits and payroll taxes to such functions as customer accounting and customer service. Because the costs associated with these functions are classified as customer-related and are included in the Staff's formula for calculation of customer-related costs allocated to various rate classes, Consumers maintains that the portion of labor overheads allocated to these functions should be classified as customer-related and included in the calculation of all customer-related costs. Consumers also contends that the Staff's use of labor overheads in Exhibit A-147 supplements previous Commission directives regarding labor overheads and customer charges. Accordingly, Consumers urges the Commission to approve a residential monthly customer charge of at least \$7.74, if it is not willing to approve the full \$8.00 customer charge supported by the company.

The Staff responds that Consumers' position is inconsistent with past practice dating to the January 18, 1974 order in Case No. U-4331 and was most recently rejected by the Commission in the March 11, 1996 order in Case No. U-10755. Accordingly, the Staff urges the Commission to uphold the ALJ's decision on this issue.

The Commission finds that Consumers' exception should be rejected and a \$7.50 per month customer charge should be approved. The precise issue that Consumers has attempted to litigate was clearly rejected in the March 11, 1996 order in Case No. U-10755. The Commission is not persuaded that the issue should be revisited in this proceeding.

Subsidies

The ALJ rejected ABATE's proposed cost of service study. In so doing, he found that ABATE had not shown the existence of the overcharge or subsidy it alleges.

ABATE argues that the ALJ engaged in nonsensical reasoning in rejecting its proposed cost of service study. According to ABATE, the transportation rates set in Case No. U-10755 clearly included a substantial subsidy. In any event, ABATE maintains that the Commission should clarify that the rates that are placed into effect as a result of this order will eliminate all interclass subsidies.

The Attorney General maintains that the complete elimination of interclass subsidies produces an untenable result. According to the Attorney General, the principle of gradualism should be invoked to avoid rate decreases for some customers in conjunction with rate increases for other customers.

The Commission agrees that the rates established by this order should not contain any interclass subsidies. Moreover, the Commission finds that the attached rate schedules achieve that goal.

Allocation of Promotional and Uncollectibles Expenses to Transportation Customers

In his testimony, Mr. Phillips stated that the Commission should not allocate any of the costs associated with promotional and uncollectibles expenses to transportation customers.

In its exceptions, ABATE contends that although the ALJ acknowledged that ABATE's cost of service study and methodology removed promotional and uncollectibles expenses from costs allocated to the transportation classes, he failed to indicate why it is reasonable to continue the practice of charging such costs to transportation customers despite the clear evidence presented by Mr. Phillips. For this reason, ABATE asserts that there is no reasoned decision making to support

a continuation of this practice, and it requests the Commission to approve a change in this proceeding.

The Commission finds that ABATE's exception should be rejected. It is long-standing Commission policy to allocate uncollectibles expense to all rate classes based on total cost of service. Customers who pay uncollectibles costs are not the customers who cause such expenses to occur. Accordingly, uncollectibles expenses must be viewed as part of Consumers' overall cost of doing business. Accordingly, the Commission finds that this category of expense should be apportioned among the various rate classes on a total cost-of-service basis, including the cost of gas for sales customers.

With regard to promotional expenses, the Commission finds that such expenses relate to Consumers' efforts to promote or retain the use of utility services by present and prospective customers of any kind. More specifically, there is no indication in the record that Consumers' promotional activities will be exclusively aimed at promoting and maintaining sales customer load as opposed to transportation customer load. Rather, such activities appear to affect all customers. Instead, it appears that the cost of all customer load retention and load growth activities are included in this account.

Therefore, the Commission concludes that ABATE's proposed change in the allocation of sales promotion expenses should be rejected.

Peak and Average Allocation Methodology

ABATE also complains that the ALJ approved continuation of the peak and average allocation methodology used by Consumers and the Staff for allocating the cost of transmission and distribution mains merely because it was approved by the Commission in a prior case and because it was consistent with a load study used by Consumers. According to ABATE, the record supports

a finding that there was no such load study either in the prior case or in this case to support Consumers' methodology. Rather, citing Mr. Phillips' testimony at 11 Tr. 1873, ABATE insists that Consumers' methodology did not identify customer demand, but simply made an estimate of that demand by taking an average of an average. In summary, ABATE argues that its modifications to Consumers' cost of service study are reasonable and should be adopted by the Commission to establish final rates in this case. ABATE also argues that Exhibit I-142 accurately and correctly sets forth the appropriate cost of service methodology that should be adopted.

Mr. Phillips' position ignores the results of a load study that was performed by Consumers for its last rate case, Case No. U-10755. A brief explanation of the company's finding is set forth on Exhibit S-160, which indicates that the peak month usage of its customer classes is a good proxy for their usage on a peak day. Therefore, the premise underlying ABATE's position is not correct because the peak demand allocator is not diluted by using peak month as a proxy for peak day demand. For that reason, the Commission finds that ABATE's exception should be rejected.

VIII.

RATE DESIGN AND TARIFF ISSUES

Pages 70 to 91 of the PFD contain rulings by the ALJ on rate design and tariff issues, such as the creation of a new extra large transportation class, the consolidation of sales tariffs B and C, remote meter charges, transportation discounts, and changes in various charges and tariff provisions, that are not the subject of exceptions. Therefore, the Commission finds that the ALJ's rulings on these issues should be adopted without further discussion.

Company Use and Lost and Unaccounted for Gas

The current allowance for company use and lost and unaccounted for gas included in Consumers' rates is 1.03%. Consumers recovers these costs from sales customers through inclusion of a dollar amount as an expense item. Transportation customers compensate Consumers through a gas-in-kind contribution pursuant to Rule F4.1.D.

Originally, based on data from May 2000 to April 2001, Consumers proposed to increase the gas-in-kind contribution of transportation customers to 1.72%.

The Staff calculated a percentage for company use and lost and unaccounted for gas of 0.82% for both sales and transportation customers on historical five-year data as shown on Exhibits S-143 and S-144.

In its brief, Consumers agreed with the Staff's position for purposes of Consumers' sales service. However, Consumers did not agree that use of the Staff's percentage would be appropriate for Consumers' transportation service. Rather, Consumers insisted that the Commission should increase the percentage to 1.72% for gas-in-kind contributions by transportation customers due to use of more gas associated with additional gas withdrawals from storage and due to the presence of additional natural gas liquids passing through storage field gas meters.

ABATE argued that there was insufficient evidence to support Consumers' contention that it had permanently changed its method of operating its storage fields. According to ABATE, a reasonable approach would be to leave the current 1.03% rate unchanged for the present time.

As previously noted, the ALJ adopted the Staff's position with regard to company use and lost and unaccounted for gas expenses of sales customers. However, the ALJ's ruling with regard to transportation volumes, which are addressed in Consumers' tariff provisions, is unclear. At

pages 63-64 of the PFD, the ALJ appeared to agree with the Staff's position because he expressly rejected the position proffered by Consumers, which urged a significant percentage increase in the gas-in-kind contribution of its transportation customers. At pages 86-87 of the PFD, the ALJ adopted Consumers' position. In so doing, the ALJ expressly stated that Consumers' position was convincingly supported by the evidence.

In its exceptions, Consumers insists that the ALJ's latter determination should be controlling because it involved a more thorough analysis of the evidence.

The Staff, the Attorney General, and ABATE disagree. The Staff and the Attorney General maintain that the Commission should adopt the ALJ's initial determination. According to them, it makes no sense to have a company use and lost and unaccounted for gas percentage for transportation customers that is more than twice as large as the percentage used to calculate the expense for sales customers.

ABATE urges retention of the present 1.03% for transportation customers because of the lack of convincing evidence to support Consumers' position.

The Commission finds that Consumers' exception is not well taken. The Commission agrees that there is inadequate justification for charging sales customers for company use and lost and unaccounted for gas at a rate that is less than half the rate proposed for transportation customers. In addition, the Commission finds that Consumers' reliance on fewer data points, including information from September 2000 that was extremely out of step with information from other months, most probably skewed Consumers' results. Therefore, the Commission finds that the Staff's position should be adopted and Rule F4.1.D should be amended accordingly.

2. Unbundling

In its brief, NEMA maintained that competition in the retail gas market will be furthered by requiring Consumers to implement fully allocated embedded cost-based unbundled rates as soon as practical. Citing the July 11, 2001 order in Case No. U-12550, NEMA contended that Consumers filed an unbundled cost of service allocation study in its rate case, which would permit determination of either fully allocated embedded cost-based unbundled rates or backout rates for a variety of services, including metering, billing, transmission, balancing, storage, backup, peaking, and turn-on or turn-off services. According to NEMA, the implementation of such rates is necessary to establish efficient, competitive markets for utility services that could be provided by third parties.

Consumers responded by arguing that the unbundling of gas commodity sales from delivery services is far more significant to customers than is the type of unbundling proposed by NEMA. Consumers contended that any further unbundling would produce negligible benefits and could raise significant concerns regarding safety, stranded costs, and allocative efficiency. Moreover, Consumers maintained that NEMA's arguments are not supported by any evidence and its economic theories are flawed. According to Consumers, the unbundling program promoted by NEMA would require that the utility be limited to one price while competitors would be free to price their products and services at any price they deem necessary to maximize their net income or market share. Finally, Consumers stated that it would be contrary to the public interest to allow third parties to own and maintain gas meters, which could present serious safety issues without realizing any significant economic benefits.

The Staff contended that the problem with NEMA's position is that there is no basis for determining backout credits without a description of the alternative service that would be

provided. According to the Staff, NEMA put the cart before the horse by asking the Commission to price out services that have not even been described yet, let alone meet the requirements not to adversely affect the integrity, reliability, safety, or cost-effective operation of Consumers' system. For this reason, the Staff argued that NEMA's request for fully unbundled rates in this case should be denied.

The Attorney General also opposed NEMA's proposal. According to the Attorney General, customer choice is in the public interest only if the features adopted as a result of that policy create net benefits for all of Consumers' customers. She cautioned that it would not be just or reasonable to set any unbundled rate at a level that will increase overhead costs for customers not electing an alternative supplier. Further, she insisted that unless the entrance of new suppliers creates net benefits for all customers, it should be treated as discriminatory cream skimming.

The ALJ found that NEMA failed to provide a specific description of the services to which it proposed to apply the backout charges. According to the ALJ, NEMA attempted to require unbundling in the abstract. He stated that the Commission's prior order requires more specificity. He also stated that NEMA's request to unbundle metering raises serious questions concerning the safety of such a proposal in light of the legislative mandate regarding electric utility metering.

In its exceptions, NEMA argues that the express purpose of the unbundled cost of service study required by the July 11, 2001 order in Case No. U-12550 was "for use by parties who wish to advocate or oppose unbundling." Order, p. 2. NEMA insists that it clearly satisfied that requirement in this proceeding. According to NEMA, its brief supported implementation of fully allocated embedded cost-based unbundled rates for each of the products, services, information, and technologies listed in the July 11 order. Therefore, NEMA urges that the Commission require

Consumers to implement fully allocated embedded cost-based unbundled rates for all of the services delineated in the July 11 order.

The Commission finds that NEMA's proposals should not be adopted at this time. As pointed out by Consumers and the Staff, it makes little sense to establish a rate for a service before the details of the service are known. To do so is to inform potential alternative suppliers of contested services of the price to beat before they design the services to be offered to customers. The Commission finds that cream skimming would be the likely result, with no assurance of any real benefit to the public.

3. MBGS

The MBGS urged the Commission to accommodate the special needs and circumstances of Michigan's schools, which the MBGS maintained are in dire financial straits, by allowing schools to take service under their own transportation tariff provision or affording them relief from certain of the requirements currently applicable to them as transportation customers. Specifically, the MBGS maintained that schools should have lessened notice requirements for switching between transportation and sales service, lessened restrictions on the injection and withdrawal of gas from storage, and uniform transportation rates determined by the throughput of a school district's largest building or the lowest throughput charge under a market-based tariff. In addition, the MBGS contended that schools should not be required to contribute to recovery of Consumers' uncollectibles expenses because school districts are creditworthy customers that must remain in operation and are not a risk to relocate to another state. For these reasons, the MBGS argued that it would be unlawful to include any costs associated with uncollectibles or bad debt in a tariff that is applicable to a school district.

In the alternative, the MBGS suggested that the Commission should at least order Consumers to involve the MBGS and others in a short-term study of the schools' concerns and indicate that this proceeding will be reopened upon application to deal with the results of the study.

In any event, the MBGS insisted that there are no legal impediments to treating school districts differently from other customers. Indeed, the MBGS cited various Commission orders issued in Case No. U-7479 as precedent for its position that school districts should have their own transportation tariff.

Mr. DeWard supported the MBGS's proposal to further study the creation of a special tariff for school districts. However, Mr. DeWard urged expansion of the study to include the feasibility of creating special rates for other governmental entities and non-profit organizations.

Consumers, the Staff, ABATE, and the Attorney General insisted that there is inadequate record support for the MBGS's proposal. They also agreed that the MBGS's proposal should be denied because it constitutes a preference that is not justified under the circumstances.

The ALJ found that MBGS failed to show that the cost of service for schools is any less than for any other class of customers. He indicated that MBGS had not presented a separate class cost of service study to buttress its case. Further, he concluded that MBGS's position lacked substantive evidence in support of the claims made. In so doing, he stressed that uncollectibles expenses are collected from customers that do not cause the expense to occur and are not directly related to good paying customers. Rather, he stated that uncollectibles expenses are simply part of the cost of doing business that must be paid by all of the utility's customers.

The ALJ also rejected the public interest argument raised by MBGS. The ALJ agreed with the assessment of Consumers, ABATE, and the Staff that a rate case proceeding is not the proper forum for MBGS to seek such relief. Further, he noted that there were other public interest service

customers of Consumers that could make similar claims. According to the ALJ, without verifiable evidence that schools pay rates that overcollect the cost to serve them, granting MBGS's request would simply shift a portion such cost to another class of customers.

MBGS's exceptions contain nine related arguments. Among other things, MBGS insists that the schools cannot afford to fund a cost of service study to support its contention that they are entitled to preferential rate treatment. Therefore, MBGS contends that the Commission should order Consumers to prepare such a study at its expense. Further, MBGS believes that it has established that schools should be excused from contributing to Consumers' uncollectibles expenses. According to MBGS, schools comprise a unique class of customers because their revenues are capped by law and they are not a risk to depart from the state or to default on their payments. For these reasons, MBGS argues that the ALJ should have recommended one of the forms of relief described in its testimony and briefs.

The Commission finds that the relief requested by the MBGS should not be granted. The Commission is not persuaded that MBGS's clients should be afforded any of the types of preferential treatment described in its testimony and briefs or that Consumers should be required to bear the expense of producing a cost study. Schools are not unique in their budgetary concerns. Unlike many of Consumers' other customers, schools have a revenue stream that is provided for by the taxpayers of this state. Albeit their source of funds is not unlimited, schools are arguably in better position than many customers who must depend on commerce, not taxes, to pay their bills. Also, the Commission agrees with the ALJ that schools are not entitled to be relieved of contributing to Consumers' uncollectibles expenses. As previously noted, any attempt to assign uncollectibles expenses only to customers who do not pay their bills and to relieve all creditworthy customers from this category of expenses would result in Consumers being unable to recover its

uncollectibles expenses. Accordingly, the Commission remains committed to allowing Consumers to recover this cost of doing business from all of its customers. For these reasons, the Commission finds that MBGS's exceptions should be rejected.

4. Daily Gas Supply

Consumers maintains that the ALJ failed to address an important language addition to its transportation rate schedules, which provides as follows:

In the months of January, February and March the customer's daily gas supply to the Company shall be not less than that customer's gas consumption in that same month in the prior year reduced by 3% of that customer's ACQ, then divided by the number of days in that month. Failure to supply this minimum daily quantity will result in the application of the Unauthorized Gas Usage Charge to any daily supply shortfall.

Exhibit A-108.

According to Consumers, over the last 15 years, the annual volume of transportation service has tripled and the business of gas supply has emerged as a commodity business for the suppliers who use sophisticated methods to arbitrage gas supply. Because greater fluctuations in daily supplied gas volumes have the potential to put undue burden on the company's storage withdrawal capabilities during the peak winter months, Consumers proposes to limit the minimum daily supply requirement to reduce the risks of excess storage withdrawals without imposing a daily balancing requirement on all end-users. Consumers states that daily balancing could be very expensive to implement and would put pressure on the end-users to precisely anticipate their daily gas supply requirements. Consumers also states that this concept is consistent with rules regarding daily delivery obligations for the gas customer choice program.

The rule change is opposed by ABATE for several reasons. First, ABATE insists that the rule change is premised on speculation that gas transportation customers will try to arbitrage their gas

positions, which in turn leads to the further speculation that such conduct could put undue pressure on Consumers' system. ABATE maintains that Consumers' speculation in this regard is not supported by any evidence. Second, ABATE contends that most transportation is done for industrial customers having very little temperature-sensitive load. Third, ABATE states that the Commission should not put restrictions on the use of private property unless it is absolutely required. In this instance, ABATE maintains that there is no showing that would justify any such limitations. Fourth, ABATE argues that the proposed rule change is flawed on its face. According to ABATE, the proposed rule contains a formula that ignores reality. For example, ABATE states that a customer could reduce its gas usage by a percentage in excess of 3% of what it used in the prior January, February, or March for a variety of reasons, including conservation or production changes. Nevertheless, ABATE believes that this proposed revision would require the customer to acquire 97% of the gas that it had delivered into Consumers' system in the prior January, February, and March even though the customers did not need that gas, which ABATE contends would be a ludicrous result.

The Commission finds that Consumers' proposal should not be adopted in its current form. In reaching this determination, the Commission finds that ABATE's opposition is based primarily on a misunderstanding of Consumers' proposal. The rules change sought by Consumers would limit a customer to reducing its *monthly* deliveries by up to 3% of the customer's *annual*, not monthly, contract requirement, which allows far greater deviation than contemplated by ABATE. Nevertheless, because the justification offered by Consumers in support of this proposal is the need to discourage arbitrage, the Commission concludes that Consumers' proposal is too broad. As pointed out by ABATE, Consumers' proposal would apply to a customer that reduces its consumption for a reason other than arbitrage. The Commission is persuaded that the proposal

should not be adopted until Consumers includes language that would exempt customers that have a legitimate reason for reduced deliveries from application of the unauthorized gas usage charge.

IX.

OTHER ISSUES

Severance Payments to Former CMS Executives

In August 2002, CMS disclosed that it had agreed to provide severance payments totaling \$7.65 million to three former executives, including William McCormick (\$4.0 million), Tamela Pallas (\$2.0 million), and Alan Wright (\$1.65 million). These payments were widely reported by the media and the financial press.

Out of concern that Consumers' ratepayers should not be required to bear the burden of the severance payments to these former executives, the Commission conducted an investigation to ensure that the rates to be established pursuant to this order would not include any amount associated with the severance payments. In so doing, the Commission reviewed the record in this proceeding and also examined the employment termination agreements and releases, which were submitted by CMS to the Securities and Exchange Commission as exhibits to its August 14, 2002 Form 10-Q filing for the quarterly period ended June 30, 2002. The review of the record indicates that Consumers' 2002 test year expenses do not include any amounts associated with the severance payments. Moreover, nothing in the employment termination agreements and releases suggests a contrary conclusion.

Nevertheless, the Commission deems it appropriate to place Consumers on notice that the Commission intends to continue to closely scrutinize all current and future Consumers' gas and

electric rate case proceedings to ensure that amounts associated with these severance payments are never included in Consumers' retail rates.

Administrative Notice

The Staff attached a variety of documents to its pleadings that were not introduced into evidence and requested that they be considered by the ALJ and the Commission. The ALJ found that all such documents were improperly submitted.

In its exceptions, the Staff maintains that two of the Commission's Rules of Practice and Procedure, R 460.17325 and R 460.17327 support its position.

The Commission finds that the Staff's argument for consideration of the materials is moot because the Commission has chosen not to consider any of them in reaching its determinations in this proceeding.

The Commission FINDS that:

- a. Jurisdiction is pursuant to 1909 PA 300, as amended, MCL 462.2 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACCS, R 460.17101 et seq.
- b. Consumers is experiencing a revenue deficiency of \$55,728,000 on an annual basis in test year 2002.
- c. Consumers' rate base is \$1,378,295,000. It should be authorized to earn a rate of return on common equity of 11.40%, and its overall rate of return should be set at 7.45%.

THEREFORE, IT IS ORDERED that:

A. Consumers Energy Company is authorized to increase its annual gas revenues by \$55,728,000 as provided for in the tariff sheets attached to this order as Exhibit A, for service rendered on and after November 8, 2002.

B. Within 30 days, Consumers Energy Company shall file revised rate schedules reflecting the rates, terms, and conditions of service approved in this order and set forth on Exhibit A.

C. All contentions of the parties inconsistent with this order and not specifically determined are rejected.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, pursuant to MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ Laura Chappelle
Chairman, concurring.

(S E A L)

/s/ David A. Svanda
Commissioner

/s/ Robert B. Nelson
Commissioner, concurring and dissenting in part.

By its action of November 7, 2002.

/s/ Dorothy Wideman
Its Executive Secretary

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MICHIGAN PUBLIC SERVICE COMMISSION

Chairman, concurring.

Commissioner

Commissioner, concurring and dissenting in part.

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Its Executive Secretary

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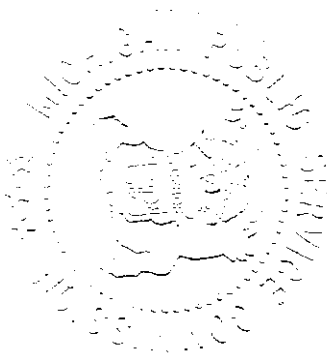
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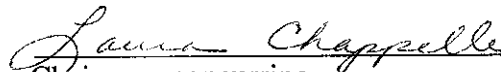
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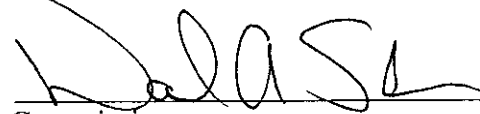
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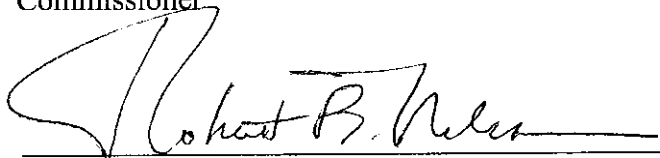
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MICHIGAN PUBLIC SERVICE COMMISSION




Chairman, concurring.


Commissioner


Commissioner, concurring and dissenting in part.

By its action of November 7, 2002.

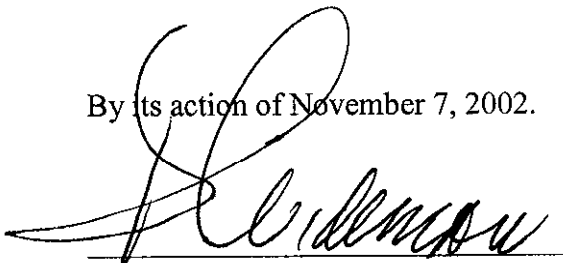

Its Executive Secretary

Exhibit A

Case No. U-13000

Consumer Energy Company

Summary of Rates
And
Tariff Sheets

Consumers Energy Company
Case No. U-13000

Summary of Ordered Gas Rate Increase (Decrease)

Line	Description	Current Revenue	Ordered Revenue	Increase (Decrease)	Percent Change	Cost Of Service Allocation
		(A)	(B)	(C)	(D)	(E)
1	Residential - Rate A	\$319,971,026	\$372,324,130	\$52,353,104	16.4%	
2	Multifamily Dwelling - Rate A-1	\$11,008,246	\$12,821,774	\$1,813,528	16.5%	
3						
4	Subtotal - Residential Sales	\$330,979,272	\$385,145,904	\$54,166,632	16.4%	\$385,148,939
5						
6	General Service - Rate GS-1	\$24,253,773	\$20,294,188	(\$3,959,585)	-16.3%	\$90,737,390
7	General Service - Rate GS-2	\$58,589,260	\$67,443,221	\$8,853,961	15.1%	
8	General Service - Rate GS-3	\$13,488,986	\$14,546,948	\$1,057,962	7.8%	\$11,547,523
9	Outdoor Lighting - Rate GL	\$7,596	\$10,224	\$2,628	34.6%	\$10,224
10						
11	Subtotal - General Service Sales	\$96,339,614	\$102,294,581	\$5,954,966	6.2%	\$102,295,137
12						
13	Total Sales Service	\$427,318,886	\$487,440,485	\$60,121,598	14.1%	\$487,444,076
14						
15	Transportation Service Rate ST	\$14,691,155	\$14,148,732	(\$542,423)	-3.7%	\$14,148,771
16	Transportation Service Rate LT	\$18,439,567	\$18,267,978	(\$171,588)	-0.9%	\$18,268,239
17	Transportation Service Rate XLT	\$14,820,573	\$11,134,188	(\$3,686,385)	-24.9%	\$11,134,918
18						
19	Subtotal Transportation Service	\$47,951,294	\$43,550,898	(\$4,400,396)	-9.2%	\$43,551,928
20						
21						
22	Total Sales & Transportation	\$475,270,180	\$530,991,383	\$55,721,203	11.7%	\$530,996,004

Consumers Energy Company

Case No. U-13000

Comparison of Current and Ordered Rates

Line	Description	Current Rates		Ordered Rates	
		(A)		(B)	
1	SALES SERVICE:				
2	Residential - Rate A				
3	Customer Charge	\$6.50	per month	\$7.50	per month
4	Distribution Charge	\$1.2008	per Mcf	\$1.4038	per Mcf
5	MultiFamily Dwelling - Rate A-1				
6	Customer Charge	\$6.50	per month	\$7.50	per month
7	Excess Demand Charge	\$0.0366	per Mcf	\$0.0366	per Mcf
8	Distribution Charge	\$1.2008	per Mcf	\$1.4038	per Mcf
9	General Service - Rate GS-1				
10	Customer Charge	\$15.00	per month	\$7.50	per month
11	Distribution Charge	\$1.0558	per Mcf	\$1.4030	per Mcf
12	General Service - Rate GS-2				
13	Customer Charge	\$15.00	per month	\$11.60	per month
14	Distribution Charge	\$1.0558	per Mcf	\$1.2624	per Mcf
15	General Service - Rate GS-3				
16	Customer Charge	\$210.00	per month	\$360.00	per month
17	Distribution Charge	\$0.7073	per Mcf	\$0.6431	per Mcf
18	Interruptible Service - Rate F				
19	Customer Charge	\$1,000.00	per month	Canceled	
20	Distribution Charge	\$0.6644	per Mcf	Canceled	
21	Outdoor Lighting - Rate GL:				
22	UP TO 2.5 CCF per hour	\$9.00	per month	\$12.00	per month
23	2.6 TO 4.5 CCF per hour	\$11.00	per month	\$15.00	per month
24					
25	TRANSPORTATION SERVICE:				
26	Rate ST (Less than 100,000 Mcf)				
27	Customer Charge	\$750.00	per month	\$450.00	per month
28	Transportation Rates				
29	Cost Based	\$0.5293	per Mcf	\$0.5891	per Mcf
30	Optional Maximum Rate	\$0.8286	per Mcf	\$0.9482	per Mcf
31	Optional Minimum Rate	\$0.2300	per Mcf	\$0.2300	per Mcf
32	Rate LT (100,000 to 500,000 Mcf)				
33	Customer Charge	\$1,300.00	per month	\$2,000.00	per month
34	Transportation Rates				
35	Cost Based Rate	\$0.4633	per Mcf	\$0.4016	per Mcf
36	Optional Maximum Rate	\$0.6966	per Mcf	\$0.5732	per Mcf
37	Optional Minimum Rate	\$0.2300	per Mcf	\$0.2300	per Mcf
38	Rate XLT (500,000 Mcf or more)				
39	Customer Charge	\$1,300.00	per month	\$5,550.00	per month
40	Remote Meter Charge	N/A		\$70.00	
41	Transportation Rates				
42	Cost Based	\$0.4633	per Mcf	\$0.3148	per Mcf
43	Optional Maximum Rate	\$0.6966	per Mcf	\$0.4796	per Mcf
44	Optional Minimum Rate	\$0.2300	per Mcf	\$0.1500	per Mcf
45	Other Transportation Charges:				
46	AUTHORIZED GAS USAGE		see tariff provision		
47	UNAUTHORIZED GAS USAGE		see tariff provision		
48	LOAD BALANCING		see tariff provision		

SECTION B - PART II
GENERAL RULES AND REGULATIONS
(FOR ALL CUSTOMERS)

INTENT OF SECTION B - PART II

These General Rules and Regulations for all customers are not to supersede but are in addition to Rule B1, Technical Standards for Gas Service, Rules C1-C7, Consumer Standards and Billing Practices for Residential Customers, and Rule D1, Commercial and Industrial Billing Practices.

B2. CHARACTERISTICS OF SERVICE

B2.1 Character of Service

The Company shall endeavor, but does not guarantee, to furnish a continuous supply of gas and to maintain pressure in its lines within reasonable limits.

The Company shall not be liable for interruptions in the service, variations in the pressure, or variations in the service characteristics, or for any loss or damage of any kind or character occasioned thereby, due to causes or conditions beyond the Company's reasonable control, and such causes or conditions shall be deemed to specifically include, but not be limited to the following: acts or omissions of customers or third parties; operation of safety devices except when such operation is caused by the negligence of the Company; absence of an alternate supply of service; failure, malfunction, breakage, necessary repairs or inspection of machinery, facilities or equipment when the Company has carried on a program of maintenance consistent with the general standards prevailing in the industry; act of God; war; action of the elements; storm or flood; fire; riot; labor dispute or disturbances; or the exercise of authority or regulation by governmental or military authorities.

Regardless of contracts in force, the Company shall have the right (a) to institute and maintain curtailments of gas service in accordance with the provisions of Rule B4, Curtailment of Gas Service, of this rate schedule, and (b) in the event of an emergency causing a short-term shortage of gas supply, to grant preference to that service, which in the Company's judgment, is most essential to the public health, safety and welfare.

Before purchasing equipment or installing piping, the customer shall secure from the Company information regarding whether new or additional gas loads are being accepted and the characteristics of the service available.

No ownership rights in facilities provided by the Company shall pass to any person as a result of any deposit or contribution made under these rules. Deposits or contributions made by customers shall not be refundable unless expressly provided in these rules.

The Company will make a leakage test prior to the establishment of gas service. The Company shall not be liable for the installation, maintenance or use of fuel lines, piping or appliances owned by the consumer or installed beyond the Company's meter nor shall the Company be liable for any continuing duty of inspection of such equipment or facilities.

B2.2 Hours of Service

Gas shall be supplied 24 hours per day except as provided elsewhere in the Company's Gas Rate Schedule.

B5.3 Application of Residential Usage and Nonresidential Usage (Contd)**C. Combined Residential and Nonresidential Usage and Rate Application**

When the gas supplied to a customer is used for both residential and nonresidential purposes, the piping may be so arranged that the residential and nonresidential usage is metered separately. Each type of usage shall be billed on the appropriate rate. If the usage is not separately metered, the combined usage shall be billed on the appropriate General Service Rate.

B5.4 Resale

No customer shall resell gas service to others. The renting of premises with the cost of gas service included in the rental as an incident of tenancy, the sale of gas to transient tenants or supplying gas under the terms of Rates CC, ST, LT, and XLT are not considered to be a resale of such service.

B5.5 Mobile Home Park - Individually Served

For purposes of this rule, the definition of a mobile home park is a parcel or tract of land under the control of a person upon which three or more mobile homes are located on a continual basis and which is offered to the public for that purpose regardless of whether a charge is made therefore, together with any building, structure, enclosure, street, equipment, or facility used or intended for use incident to the occupancy of a mobile home.

Service to separately metered mobile homes shall be billed on Residential Service Rate A.

The mobile home park shall be of a permanent nature with improved streets and with individual water and sewer connections to each lot. Ordinarily, gas service to a mobile home shall be in the name of the occupant. However, service to lots designated for occasional or short-term occupancy shall be in the name of the owner of the park or an authorized representative.

At the request of the owner of the mobile home park or an authorized representative, the Company shall install gas distribution mains in accordance with Rule B11, Customer Attachment Policy, for any mobile home park qualifying hereunder.

The owner of the park or an authorized representative shall provide the Company with the necessary easement for construction, operation, maintenance and replacement of the Company's facilities on the park property. The owner of the mobile home park or an authorized representative shall provide, own, install and maintain, in accordance with Company specifications, suitable meter and regulator pedestals of a design subject to approval of the Company. The owner of the park or an authorized representative shall provide, own, install and maintain the facilities from the outlet side of the meter and regulator to each mobile home.

B6.2 Bills and Payments (Contd)**B. Meter Reads and Estimated Bills**

The Company shall schedule meters to be read on approximately a monthly basis and will attempt to read meters in accordance with such schedule.

When the Company is unable to obtain an actual meter reading, the bill shall be estimated on the basis of past service records, adjusted, as may be appropriate. Where past service records are not available or suitable for use, such billing shall be based upon whatever other service data are available. Each such account shall be adjusted as necessary each time an actual meter reading is obtained.

C. Customer Meter Reads

Bills rendered for gas service for periods for which readings were not obtained shall have the same force and effect as those based upon actual meter readings. Any customer may read his/her own meter and send the readings to the Company on appropriate forms which shall be provided by the Company.

D. Responsibility for Payment

The customer is responsible for the payment of bills until service is ordered shut off or terminated and the Company has had reasonable time to secure a final meter reading.

E. Due Date

The Company shall allow each residential customer a period of not less than 17 calendar days, and a nonresidential customer a period of not less than 21 calendar days, from the date the bill was transmitted to pay in full.

If a bill remains unpaid and not in dispute five days after its due date, the Company shall then have the right to issue to the customer a notice of intent to shut off service ten days or more after issuance of the notice.

F. Late Payment Charge

The Company shall assess a late payment charge as authorized by the Company's Gas Rate Schedule.

G. Returned Checks

A check remitted as a bill payment and returned or an authorized prepayment not honored by the bank or financial institution against which it is drawn shall be rebilled to the customer's account. A \$25.00 charge shall be assessed to the customer for processing a check or an authorized prepayment returned by a bank or other financial institution for reason of insufficient funds, account closed, no account and similar situations, excluding bank or financial institution errors.

B6.2 Bills and Payments (Contd)**(2) Undercharge**

If a customer has been undercharged as a result of a meter error or nonregistering meter, the amount of the undercharge may be billed to the customer in accordance with Rule B1.6 of the Technical Standards for Gas Service.

J. Energy Theft, Stolen Meter and Switched Meter

In cases where metered or unmetered energy theft, stolen meter or switched meter are involved, refunds and backbillings are for the determined duration of the period. Where the duration cannot be reasonably established or estimated, the Company shall adjust the billing for the past three years on the basis of actual monthly consumption determined from the most recent 36 months of consumption data.

Metered or unmetered energy theft includes but is not limited to tampering, unauthorized use, diversion and interference. For purposes of this rule, a stolen meter is classified as any meter not specifically assigned to that service location by the Company. For purposes of this rule, a switched meter is classified as a meter incorrectly assigned to a customer resulting in the customer being billed for another customer's consumption.

The Company reserves the right to recover all unbilled service revenue and costs associated with the theft of energy, stolen meter or switched meter. The offending customer who intentionally stole a meter, switched a meter or who was intentionally involved in energy theft shall pay all associated costs including costs for discovery, investigation and rewards for discovery. The customer who did not intentionally steal a meter, switch a meter or who did not intentionally become involved in energy theft shall pay for their energy usage according to Section H of this rule.

The owner of a multiple-metered building shall be responsible for accurately tracing all fuel lines and for tagging such fuel lines with Company-provided tags to assure individual units are properly metered. The Company shall not set the meters until the fuel lines are identified. The owner of a multiple-metered building could be held responsible for any underrecovery of revenues resulting from improperly tagged meters. Any future expense of tracing fuel lines due to instances of switched meters related to errors in tracing and tagging of such fuel lines shall be the responsibility of the current owner of the multiple-metered building.

B6.3 Restoration of Service

Restoration charges and meter relocation charges shall be made by the Company to partially cover the cost of shutting off, terminating and restoring service.

Where service has been shut off for reasons as outlined in Rule B2.3, Use of Service, a restoration charge of \$35.00, for restorations done during regular working hours, shall be collected from the customer whose service was shut off if service was shut off at the customer's meter or at the curb valve. If the customer specifically requests restoration of service after regular working hours and the customer is advised of the increased charge, a restoration charge of \$45 shall be collected. If an excavation was necessary to shut off service, a restoration charge of \$300 shall be collected from the customer whose service was shut off.

B6.3 Restoration of Service (Contd)

Where service has been shut off for reasons as outlined in Rule B2.3, Use of Service, a meter relocation charge, if applicable, and assessed in accordance with Rule C5.55, Charges for Meter Relocation, shall be collected from the customer whose service was shut off. The Company shall charge the customer for relocating the meter, based on the Company's current cost.

The restoration charge and meter relocation charge, if applicable, shall be billed to the customer and shall be paid before service is restored.

If the customer about to be shut off for nonpayment elects to pay the energy arrears in full at the time of the disconnection, the Company employee shall be authorized to accept the payment. In addition to full payment of arrears, a \$20.00 charge shall be paid by the customer for sending the employee to the customer's premises.

In the case of shutoff of service, the Company shall restore service only after the customer has paid all applicable charges authorized by its Gas Rate Schedule, subject to the customer's right to dispute such charges as set forth in Rules C1-C7, Consumer Standards and Billing Practices for Residential Customers, and Rule D1, Commercial and Industrial Billing Practices.

A customer who orders a termination and a restoration of service at the same premises within a 12-month period shall be billed a "turnon" charge of \$45.

B7. MAIN EXTENSIONS

Rule B7 has been superseded by Rule B11, however, customers taking service under main and/or service line extension projects initiated pursuant to Rules B7 and/or B8 will pay the charges applicable under those rules.

B7.1 Extension Policy**A. General**

When the Company is reasonably assured of the permanence of service, and application is made for gas service which requires the extension of the Company's existing distribution mains within its service area, the Company shall make such extensions under the terms of Paragraph B below. This main extension policy is subject to Rule B2.4, Unusual Facility Requirements.

Each distribution main extension financed in part by customers shall be a separate, distinct unit and any further extension thereof shall have no effect upon the agreements under which such extension is constructed. The unrefunded portion of the deposit at the end of five years shall accrue to the Company. The amounts, if any, to be refunded shall be determined in accordance with the provisions of this rule.

B10. GAS COST RECOVERY CLAUSE AND STANDARD REFUND PROCEDURES**B10.1 Gas Cost Recovery Clause****A. Applicability of Clause**

All rates for gas service, unless otherwise provided in the applicable rate schedule, shall include a Gas Cost Recovery Factor to allow the Company to recover the booked costs of gas sold by the Company if incurred under reasonable and prudent policies and practices.

B. Booked Cost of Gas Sold

- (1) Booked cost of gas sold as used in this rule includes the following as expensed on the books of the Company:
 - (a) Interstate Purchases: Cost for gas service.
 - (b) Intrastate Purchases: Costs for gas service incurred pursuant to all contracts on file with the Michigan Public Service Commission.
 - (c) Company-Produced Natural Gas: Costs which vary with volume produced.
 - (d) Company-Produced Substitute Natural Gas: Costs for feedstock used to produce substitute natural gas.
 - (e) Liquefied Petroleum Gas-Air Mixture: Costs for propane used to produce a propane-gas-air mixture.
 - (f) Storage Gas: Net costs of gas injected and withdrawn from underground storage facilities.
 - (g) Purchases From Other Michigan Utilities: Costs for gas service pursuant to contracts approved by the appropriate regulatory body.
 - (h) Supplier Refunds and Credits: Refunds and credits from suppliers in the period realized.
- (2) Booked cost of gas sold as used in this rule specifically excludes the following items:
 - (a) Gas used by the Company, at the annual average booked cost of gas sold.
 - (b) Lost and unaccounted for gas, at the annual average booked cost of gas sold.
 - (c) Gas sold at a price which does not include a Gas Cost Recovery Factor, at the incremental cost from the Company's suppliers.
 - (d) Contract, tariff and other penalties, unless the customers of the Company benefit as a result of payment of such penalties.

B10.1 GAS COST RECOVERY CLAUSE (Cont'd)**C. Billing**

- (1) In applying the Gas Cost Recovery Factor, per Mcf or dekatherm, any fraction of 0.01 cent shall be rounded to the nearest 0.01 cent.
- (2) Each month the Company shall include in its rates a Gas Cost Recovery Factor up to the maximum authorized by the Commission as shown on Sheet No. E-3.00. For months in which the Michigan Public Service Commission has not approved a specific Gas Cost Recovery Factor, the Company may include an appropriate Gas Cost Recovery Factor in its rates if authorized by law to do so.
- (3) The Gas Cost Recovery Factor shall be the same per Mcf or Ccf for each billed customer. The factor shall be placed into effect in the first billing cycle of each monthly billing period and shall continue in effect throughout all cycles in each monthly billing period.
- (4) The Gas Cost Recovery Factor shall appear on all customer bills.

D. General Conditions

- (1) At least 15 days prior to a billing month for which the GCR factor to be billed is to differ from that currently in effect, the Company shall notify the Public Service Commission Staff as to the actual factor to be billed to its customers in the subsequent month.
- (2) This Gas Cost Recovery Clause is authorized by the provisions of 1982 PA 304. A copy of that act is available for public inspection at each business office of the Company. The Company shall provide a copy of the act to any customer upon request.

B10.2 Standard Refund Procedures for Gas Cost Recovery and Other Supplier Refunds**A. Receipt of Refunds by the Company****(1) Supplier Refunds**

By April 15 of each year, the Company shall notify the Michigan Public Service Commission Staff of any pipeline or other supplier refunds (other than a routine billing adjustment) received during the prior twelve months ended March 31. The notification shall be in the form of a letter, and include:

- (a) The amount of each refund, including interest.
- (b) The date each refund was received.
- (c) The source and reason for each refund.
- (d) The period covered by each refund (historical refund period).

Additionally, if any portion of any pipeline or other supplier refund is property allocable to non-GCR customers, this amount, along with any calculations of deductions wherefrom for Company Use and Lost and Unaccounted-For Gas, shall also be included in the written notification.

Failure of the Company to report a refund to the Michigan Public Service Commission Staff by the April 15 deadline shall result in an interest penalty of 50% over the normal authorized rate of return on common equity for the period of time that the utility fails to comply with the refund notification requirement.

B10.2 Standard Refund Procedures for Gas Cost Recovery and Other Supplier Refunds (Contd)

A. Receipt of Refunds by the Company (Contd)

(2) Gas Cost Recovery (GCR) Plan Reconciliation

Over/(under)-recovery amounts arising from the annual GCR Reconciliation shall be reported in accordance with the provisions of 1982 PA 304.

(3) Proportional Refunds

The monthly refund liabilities incurred from proportional refund provisions shall be reported annually.

B. Refund Allocation

(1) Supplier Refunds

Gas supplier refunds shall normally be allocated in their entirety to GCR sales customers. Where appropriate, supplier refunds shall be allocated between GCR and Non-GCR customers on the basis of actual consumption during the historical refund period.

Deductions for Company Use and Lost and Unaccounted-For volumes may be made from the portion of the refund allocable to transportation customers based upon the actual percentages for Company Use and Lost and Unaccounted-For during the historical refund period.

(2) Proportional Refunds

The monthly refund liability incurred under these refund provisions shall be allocated between GCR and Rate T-1 Non-GCR customers on the basis of throughput Mcf Volumes (excluding Rate T-2 volumes) for the period GCR year, weighted for the class average revenue requirements per Mcf established in the last general rate case.

C. Refund Pass-Through

(1) To GCR Customers [Roll-in Methodology]

All supplier refunds allocable to GCR customers shall be reflected as adjustments to the GCR Cost of Gas Supply in the month received and should be included in "Purchased and Produced." Adjustments to prior year's GCR under- or over-recoveries and any Commission-ordered disallowances associated with a prior GCR period, along with all other refund liabilities will be reflected separately below the cost of gas sold line for the month of effect, in order that they may be included in the month-to-month rolling over/(under)-recovery balance for purposes of interest calculation, but without their affecting the costing of Company-Use and Lost & Unaccounted-for Gas.

The Company shall maintain records as to the source amount, and timing of each roll-in component.

Interest shall be accrued on the month-to-month rolling over/(under)-recovery balance at the rates specified in 1982 PA 304.

B10.2 Standard Refund Procedures for Gas Cost Recovery and Other Supplier Refunds (Contd)

C. Refund Pass-Through (Contd)

(2) To Non-GCR Customers [Traditional Methodology]

All Non-GCR customer refund liabilities shall be credited to a refund liability account to accrue interest until such time as these monies are authorized to be refunded. The interest rate for pipeline refunds, proportional refunds, and unrefunded balances shall be Consumers' authorized rate of return on common equity.

Application for distribution of Non-GCR customer refund liabilities shall be included in Consumers' annual GCR reconciliation filing.

(3) Distribution of Non-GCR Customer Refunds in General

(a) Data Retention

Consumers shall maintain individual customer consumption data for a minimum period of four years. In addition, the last known address of each customer who has left Consumers' system shall be maintained for the same time period.

(b) Refund Distribution Period

The refund distribution period shall correspond to the period used to allocate the refund liability except when the allocation period exceeds the 48-month retention period for individual customer consumption data.

In the event that the refund allocation period covers time periods beyond the 48-month data retention period, a more current period for which data is available may be used as the refund distribution period.

When multiple refunds are being considered in the same refund proceeding, refund liability amounts allocated to each respective rate class may be aggregated and the sum distributed using the most logical refund distribution period.

(c) Current Customers

Refunds shall be made to current customers based upon their consumption at any location in the Company's service territory during the refund distribution period. Bill credits shall appear as a separate line item on the bill and be identified as a refund. Rights to any portion of a refund shall not vest until a refund amount has been credited to a customer's bill or a refund check to a past customer is negotiated.

B10.2 Standard Refund Procedures for Gas Cost Recovery and Other Supplier Refunds (Contd)

C. Refund Pass-Through (Contd)

(3) Distribution of Non-GCR Customer Refunds in General (Contd)

(d) Past Customers

All past customers who had consumption during the refund distribution period shall be issued a refund check to their last known address, except that the utility is not required to issue refund checks to past customers who would receive \$2.00 or less, those in arrears with the utility, or to customers whose checks were returned as undeliverable from previous refunds. Rights to any portion of a refund shall not vest until a refund amount has been credited to a customer's bill or a refund check to a past customer is negotiated. After 180 days, any returned or uncashed check shall be transferred to the refund liability account to be refunded with interest in the next refund.

(e) Customers in Arrears

Refunds made pursuant to these procedures will be applied against any past due amounts owing to Consumers. The amount, if any, in excess of the amount owed will be refunded in accordance with these procedures.

(f) Refund Completion Reports

Six months after the completion of a refund distribution, Consumers shall submit a completion report to the Commission Staff showing the amount actually refunded as compared to the authorized refund amount and the date the refund was completed.

(g) Unrefunded Balances

Any undistributed amounts remaining shall be rolled back into the refund liability account to accrue interest at Consumers' authorized rate of return on common equity until refunded to customers in the next refund distribution.

B11. CUSTOMER ATTACHMENT PROGRAM**A. Purpose**

The Company proposes to make extension of its gas mains and/or service lines from time to time, at its own cost, to serve applicants whose requirements will not disturb or impair the service to prior users or will not require an expenditure out of proportion to the revenue obtainable therefrom.

The Company reserves the right to delay or deny a request for service under this rule, if fulfilling such a request could, in the Company's opinion, create conditions potentially adverse to the Company or its customers. Such conditions may include, but are not limited to, safety issues, system operating requirements or capital constraints. The provisions under this Rule are in addition to the existing rules and tariffs for customer gas service.

When relocation or modification of Company facilities is requested or made necessary by the customer, all costs for the relocation or modification shall be charged to the requesting party.

B. Customer Contribution

A customer contribution shall be required prior to construction equal to the following components: Connection Fee plus any applicable Fixed Monthly Surcharge or lump sum payment plus any Excessive Service Line Fee plus any Direct Charges. Direct Charges include, but are not limited to, any specific license fees, inspection fees, or rights of way fees charged by any political subdivision for any construction provided under this rule, and are to be paid the Company.

Any written communication from the Company regarding construction activity and its associated contribution due from the customer, unless specified otherwise in the document, shall have an expiration date of 60 days from the date issued. If either the customer or the Company takes no action by that time, the Company shall have the right to withdraw the proposal or modify the conditions under which it was made.

C. Payment of Customer Contribution

The Connection Fee, Direct Charges and the Excessive Service Line Fee are payable in lump sum at the time the service agreement is executed by the customer. The Connection Fee is non-refundable. The Direct Charges and Excessive Service Line Fee are refundable if the service line has not been installed. If the service line has been installed, the Direct Charges and Excessive Service Line Fees are non-refundable.

B11. CUSTOMER ATTACHMENT PROGRAM (Contd)

C. Payment of Customer Contribution (Contd)

Unless otherwise stated by the Company, the customer shall pay any remaining charges resulting from a Revenue Deficiency in a lump sum in advance of the facility expansion. Customers deemed by the Company to require significant investment for unpredictable operations may enter into a contract with the Company to have all or a portion of the revenue deficiency designated as a deposit subject to refund, at the option of the Company. Refunds shall not exceed the amount of the deposit, and shall be based solely on any incremental increase in consumption and accompanying revenues above that recognized in the Model to calculate the customer contribution.

For land developers, builders, mobile home park developments, or rental units, the customer contribution shall be required in a lump sum in advance of the facility expansion; they are not eligible for the Fixed Monthly Surcharge, and may not be considered as an unpredictable operation eligible for terms of a contract subject to refund.

The Company may offer the Fixed Monthly Surcharge as an alternative payment method. The Fixed Monthly Surcharge shall be payable monthly throughout the surcharge period. Billing of the Fixed Monthly Surcharge shall commence within six months following completion of construction of the main and initial service lines. The customer may at any time elect to pay off the remaining Fixed Monthly Surcharge balance with a lump sum payment equal to the present value of the remaining monthly payments. If the present value of the Fixed Monthly Surcharge is less than \$200.00, the Company may require the customer to make a lump sum payment. The Fixed Monthly Surcharge is assessed to the property served such that any subsequent customer requesting gas service at the property address, once notified by the Company of the amount and duration of such surcharge, shall be liable for the Fixed Monthly Surcharge. Such notification may be verbal, written or in the form of a bill which includes the Fixed Monthly Surcharge. Failure of sellers, agents, lessors or other non-company parties to notify a customer of the Fixed Monthly Surcharge shall not relieve the customer's obligation to pay the Fixed Monthly Surcharge. Failure by the customer to timely pay the Fixed Monthly Surcharge shall result in the discontinuation, termination or denial of natural gas service.

B11. CUSTOMER ATTACHMENT PROGRAM (Contd)**D. Connection Fee**

The Connection Fee is equal to \$200.00 per meter. The Connection Fee for a multiple metered installation on a single structure that is served from a single service line is equal to \$100.00 per meter.

E. Excessive Service Line Fee

The Excessive Service Line Fee will be assessed to a customer whose service line requirement is in excess of the Service Line Limit. The Excessive Service Line Fee will be calculated annually to be effective March 1st. The Service Line Limit for an individual service line shall be equal to the point at which the cost of the customer's service requirements are greater than the allowance based on the Cost of Service Model. The Company reserves the right to use a different Service Line Limit for different categories of customers. The Service Line Limit will be calculated annually to be effective March 1st. In calculating the average service line length for a project containing more than one customer, the maximum length of each service line to be included in the calculation is the Service Line Limit for a primary residential home.

F. Fixed Monthly Surcharge

A Fixed Monthly Surcharge (Surcharge) will be calculated for each Customer Attachment Project (Project). The Surcharge will recover the Revenue Deficiency anticipated from the proposed Project. The Surcharge is calculated such that the present value of the anticipated Surcharges collected from the Project will equal the net present value Revenue Deficiency. The Surcharge will be recoverable over a predetermined time period, not to exceed ten years. The Company will be responsible for determining the appropriate Surcharge time period. The Surcharge will be a fixed dollar amount for all customers within the Project and will expire on the same date for all customers within the Project, regardless of when the surcharge was initially assessed to the customer. The Surcharge will not be subject to adjustment, reconciliation or refund. A customer who attaches to a Project after the surcharge period has expired or a customer whose proposed attachment was beyond the scope of the original Project, will be treated as a separate Project.

The Company will supply, upon request by the party responsible for payment of the Surcharge, the following information for an account subject to a Surcharge: the current present value of the Surcharge balance, a report of monies paid either (a) to date for an account or (b) for a twelve-month period for an account provided the request is made within 90 days of the end of the time period requested, and the expiration date of the project. This information will be supplied at no charge to the customer once within a calendar year.

G. Customer Attachment Project

A Project may consist of a single customer, requiring only the installation of a service line and meter, or may consist of numerous customers requiring the installation of mains, service lines and meters. A Project will generally be defined as a customer or group of customers that may be served from the contiguous expansion of new distribution facilities.

H. Revenue Deficiency

A discounted Cost of Service Model (Model) will be used to calculate the Net Present Value (NPV) Revenue Deficiency anticipated from a Project. The Model will use the expected incremental revenues and incremental costs associated with the Project for each year of a twenty year period. From this information an annual net revenue excess or deficiency will be calculated. The annual net revenue excess or deficiency will be discounted and summed to determine the NPV revenue deficiency of the Project. If the NPV revenue deficiency is negative, the discounted revenues exceed the discounted costs, then an NPV revenue deficiency of zero will be used.

RESIDENTIAL SERVICE RATE A**Availability**

Subject to any restrictions, this rate is available to any customer desiring gas service for any usual residential use in private family dwellings; tourist homes, rooming houses, dormitories, nursing homes and other similarly occupied buildings containing sleeping accommodations for up to six persons; or multifamily dwellings containing two households served through a single meter.

This rate is not available for resale service, multifamily dwellings containing more than two living units served through a single meter or for tourist homes, rooming houses, dormitories, nursing homes and similarly occupied buildings containing sleeping accommodations for more than six persons or for any other nonresidential usage.

Residences in conjunction with commercial or industrial enterprises and mobile home parks may take service on this rate only under the terms and conditions contained in the Company's Gas Rate Schedule.

Monthly Rate**Customer Charge**

\$7.50 per customer per month, plus

Distribution Charge

\$1.4038 per Mcf for all Mcf purchased.

Gas Cost Recovery Charge

The gas cost recovery factors are shown on Sheet No. E-2.00.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. E-1.00 and surcharges shown on Sheet No. E-2.00.

Minimum Charge

The minimum charge shall be the customer charge included in the rate.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 17 days from the date of transmittal. A late payment charge of 2%, not compounded, of the portion of the bill, net of taxes, shall be assessed to any bill that is delinquent. A customer who participates in the Winter Protection Plan or who is 65 years of age or older and who has notified the Company the customer is 65 years of age or older, shall be exempt from a late payment charge as described in Rule C6.74.

Term and Form of Contract

Service under this rate shall not require a written contract.

MULTIFAMILY DWELLING SERVICE RATE A-1

Availability

Subject to any restrictions, this rate is available to any multifamily dwelling installation containing more than two households served through a single meter and where, in the Company's opinion, it is impractical to provide gas service to each household through an individual meter.

This rate is not available for multifamily dwellings containing two households served through a single meter.

Monthly Rate

Customer Charge

The charge per customer per month shall be the sum of the following charges:

\$7.50 per month, plus
\$0.0366 per Mcf of excess peak demand, plus

Distribution Charge

\$1.4038 per Mcf for all Mcf purchased.

Gas Cost Recovery Charge

The gas cost recovery factors are shown on Sheet No. E-2.00.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. E-1.00 and surcharges shown on Sheet No. E-2.00.

Minimum Charge

The minimum charge shall be the customer charge included in the rate.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

M.P.S.C. No. 1 - Gas
 Consumers Energy Company
 (To Replace Rate Schedules B & C)

Sheet No. E-7.00

General Service Rate **(Rates GS-1, GS-2, and GS-3)**

Availability

Subject to any restrictions, this rate is available to any customer desiring gas service for any nonresidential usage which includes tourist homes, rooming houses, dormitories, nursing homes and similarly occupied buildings containing sleeping accommodations for more than six persons. Gas shall not be purchased under any other rate for any equipment or process which uses gas under this rate.

This rate is not available for residential usage or for resale purposes.

All customers requesting service under this rate shall make written application for such service on a form provided by the Company.

Rates and Charges

<u>Service Category</u>	<u>Customer Charge per Month</u>	<u>Distribution Charge</u>
<u>GS-1</u>	<u>\$ 7.50 per meter</u>	<u>\$1.4030 per Mcf</u>
<u>GS-2</u>	<u>\$ 11.60 per meter</u>	<u>\$1.2624 per Mcf</u>
<u>GS-3</u>	<u>\$360.00 per meter</u>	<u>\$0.6431 per Mcf</u>

Customers may choose the Service Category under which they take service, consistent with the provisions of Rules B5.1 and B5.2. When the Customer is selecting its initial Service Category, the Company must advise them that the economic break even point between GS-1 and GS-2 is approximately 350 Mcf per year and the economic break even point between GS-2 and GS-3 is approximately 6,750 Mcf per year. After the initial selection is made, then it is the customers responsibility to determine when it is appropriate to switch Service Categories, as permitted by Rule B5.2.

Gas Cost Recovery Charge

The gas cost recovery factors are shown on Sheet No. E-2.00.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. E-1.00 and surcharges shown on Sheet No. E-2.00.

Minimum Charge

The minimum charge shall be the customer charge included in the rate.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

Term and Form of Contract

Service under this rate shall not require a written contract.

M.P.S.C. No. 1 - Gas
Consumers Energy Company
(To Cancel Rate C)

Sheet No. E-9.00

This sheet has been cancelled.

M.P.S.C. No. 1 - Gas
Consumers Energy Company
(To Cancel Rate F)

Sheet No. E-10.00

This sheet has been cancelled.

M.P.S.C. No. 1 - Gas
Consumers Energy Company
(To Cancel Rate F)

Sheet No. E-11.00

This sheet has been cancelled.

M.P.S.C. No. 1 -
Consumers Energy Company

Gas Sheet No. E-12.00

GENERAL SERVICE OUTDOOR LIGHTING RATE GL

This Rate Is Not Open to New Business

Availability

Subject to any restrictions, this rate is available to any commercial or industrial customer for streetlighting or outdoor area lighting service for any system consisting of two or more gas luminaires where the Company has an existing gas distribution system.

Nature of Service

The customer shall furnish the necessary posts, luminaires and fixtures. The Company shall install this equipment and make all connections to its gas distribution system. The Company shall supply the gas, renew the mantles, clean the luminaires and paint all metal parts as needed; all other renewals and maintenance shall be paid for by the customer.

Monthly Rate

\$12.00 per luminaire having a rated consumption of 2.5 cubic feet or less per hour.

\$15.00 per luminaire having a rated consumption of more than 2.5 cubic feet but not more than 4.5 cubic feet per hour.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

Term and Form of Contract

Minimum term of three years on written contract and year to year thereafter until terminated by mutual consent or upon three months' written notice given by either party.

Special Terms and Conditions

The Company reserves the right to make special contractual arrangements as to term or duration of contract, termination charges, contributions in aid of construction, monthly charges or other special consideration when the customer requests service, equipment or facilities not normally provided under this rate.

SECTION F
TRANSPORTATION SERVICE
GAS TRANSPORTATION STANDARDS AND BILLING PRACTICES

F1. GENERAL PROVISIONS AND DEFINITIONS

F1.1 Definitions.

As used in this section:

- (a) "Account" shall mean customer's facilities and operations directly connected with the individual facilities identified in the transportation contract between the Company and the customer. The gas for each account being measured by a single Company meter.
- (b) "Allowance for Use and Loss" is defined in Rule F4.1.D. in this Section F.
- (c) "Annual Contract Quantity" (ACQ) means the greatest quantity of gas the Company shall accept for transportation on the customer's behalf for any given year as specified in the contract. The contracted ACQ shall be adjusted based on the customer's highest consecutive 12-month usage determined from the latest 24 months of data except that the ACQ may be adjusted for known or expected changes.
- (d) "Authorized Tolerance Level" means 6.5%, 7.5%, 8.5%, 9.5%, or 10.5% of the customer's ACQ
- (e) "Cubic Foot of Gas" means the volume of gas, which occupies one cubic foot when such gas is at a temperature of sixty degrees (60°) Fahrenheit and at a pressure base of fourteen and sixty-five hundredths (14.65) psia dry.
- (f) "Day" means a period of 24 consecutive hours (23 hours when changing from Standard to Daylight Time and 25 hours when changing back to Standard Time) beginning at 10:00 AM Eastern Clock Time or at such other time as may be mutually agreed.
- (g) "Designated Sales Rate" means the rate under which the customer would take service if purchasing system-sales service.
- (h) "Gas" means natural gas, manufactured gas or a combination of the two, which meets the "quality" standards as specified in Rule F3, Gas Quality, in this Section F.
- (i) "Gas Rate Schedule" means the Schedule of Rates Governing the Sale of Natural Gas Service as approved by the Michigan Public Service Commission.
- (j) "Load Balancing Charge" is defined on the Transportation Service Rate schedules.
- (k) "Maximum Daily Quantity" (MDQ) means the greatest quantity of gas that the Company shall accept for transportation on the customer's behalf on any day. The MDQ shall not exceed the customer's peak monthly usage in the last 24 months of such service divided by 30 except that the MDQ may be adjusted for known or expected changes.
- (l) "MMBtu" means one million Btu.
- (m) "Month," except as provided with respect to billing, means a period beginning at 10:00 AM Eastern Clock Time on the first day of a calendar month and ending at 10:00 AM Eastern Clock Time on the first day of the following calendar month or at such other time as may be mutually agreed.

F1.1 Definitions. (Contd)

- (n) "Nominations" means the process by which the customer or the customer's agent notifies the Company of expected transportation quantities.
- (o) "Total Heating Value Per Cubic Foot" means the number of Btu produced by the combustion, at constant pressure, of one cubic foot of gas, with air of the same pressure and temperature as the gas, when the products of combustion are cooled to the initial temperature of the gas and air, and when the water formed by the combustion is condensed to the liquid state. This definition applies regardless of the equipment used to determine the total heating value per cubic foot.
- (p) "Unauthorized Gas Usage Charge" is defined on the Transportation Service Rate Schedule.

F1.2 Application of Rules.

Unless otherwise provided for within this Section F or under their contracted Transportation Service Rate, transportation rate customers are subject to the Company's Gas Rate Schedule. Customers taking transportation service shall be considered utility service customers of the Company.

F1.3 Possession of Gas.**A. Responsibility for Gas**

The Company and the customer shall each be responsible for its own equipment, facilities and gas on its own side of a delivery point. The customer shall have good title or good right to make delivery and, further, shall warrant for itself, its successors and assigns that such gas shall be free and clear of all liens, encumbrances, and claims whatsoever. With respect to any such adverse claim that may arise to said gas or to royalties, taxes, license fees or charges thereon, the customer shall indemnify and save the Company harmless from all suits, actions, debts, accounts, damages, costs, losses, and expenses arising from or out of same.

B. Indemnification of the Company

In the absence of negligence, recklessness or willful misconduct on the part of the Company or of the Company's officers, employees or agents, the customer waives any and all claims against the Company, its officers, employees or agents, arising out of or in any way connected with (1) the quality, use or condition of the gas after delivery from the Company's line for the account of such customer; (2) any losses or shrinkage of gas during or resulting from transportation and (3) all other claims and demands arising out of the performance of the duties of the Company, its officers, employees, or agents.

F2. RECORDS, ACCOUNTING AND CONTROL**F2.1 Mailing of Notices, Bills, and Payments.**

All notices, bills, and payments required or permitted to be given in connection with this service shall be sent to the address specified in the customer's contract, shall be in writing and shall be valid and sufficient if delivered in person, dispatched by first class mail, Western Union, telex, or facsimile.

F2.2 Nominations, Accounting, and Control.

- A. If the customer designates some other party as agent for purposes of nominating, and of giving and receiving notices, the customer shall provide the Company with written notice of such designation. Any such designation shall be effective until revoked in writing by the customer.
- B. All nominations shall be submitted by facsimile, e-mail or an available electronic nomination system.
- C. **Daily:** The customer or the customer's authorized representative shall notify the Company's Gas Transportation Services Department of the daily quantity of gas (in MMBtu) that the customer is nominating for delivery to the Company on behalf of the customer. Such nominations shall be submitted by 12:30 PM Eastern Clock Time prior to the effective day of the proposed delivery. Nominations made after the 12:30 PM deadline shall be accepted at the sole discretion of the Company. Customers are required to have a nomination on file for each day of the month. A single nomination shall be assumed to apply for each subsequent day of the month, unless otherwise indicated.
- D. The customer or the customer's authorized representative may transfer a portion of their account balance to another customer. The customer from whom the gas is transferred shall be charged a \$25 fee. Such transactions are prospective and may not be used to avoid penalties once charged.

F3. GAS QUALITY**F3.1 Quality.**

The gas delivered to the Company shall meet the following requirements:

- A. Gas shall not contain more than 0.005 percent (50 ppm) oxygen by volume;
- B. Gas shall be commercially free from objectionable odors, solid or liquid matter, bacteria, dust, gum or gum-forming constituents which might interfere with its merchantability or cause injury to or interference with proper operation of the lines, regulators, meters or other appliances through which it flows;
- C. Gas shall not contain more than 0.25 grain of hydrogen sulphide nor more than 0.5 grain of mercaptan sulfur per 100 cubic feet;
- D. Gas shall not contain more than 5.0 grains of total sulfur (including hydrogen sulphide and mercaptan sulfur) per 100 cubic feet;
- E. Gas shall not at any time have a carbon dioxide content in excess of two percent by volume;
- F. Gas shall not contain an amount of moisture, which at any time exceeds seven pounds per million cubic feet;
- G. Gas shall be fully "interchangeable" in accordance with the provisions of AGA Research Bulletin No. 36.
- H. The temperature of the gas shall not exceed 100° F;
- I. The hydrocarbon dew point of the gas shall not exceed 30° F at 500 pounds per square inch.

F3.2 Heating Value.

The gas transported shall have a total heating value per cubic foot of not less than 965 Btu nor more than 1,110 Btu. Unless otherwise agreed, differences in the thermal value of the gas transported shall be determined by the Company based on the assumption that the gas delivered to the customer has a Btu content per Mcf that is the same as the Company's then-current system average Btu content per Mcf which shall be redetermined monthly.

F4. SERVICE REQUIREMENTS**F4.1 Quantities.**

- A. The customer may deliver, or cause to be delivered, and the Company shall, subject to other provisions in the Company's Gas Rate Schedule, accept quantities of gas up to the MDQ specified in the transportation contract. If deliveries to the Company exceed the agreed upon quantities, the Company may terminate the contract upon 30 days' written notice to the customer.
- B. Deliveries to the Company may be made by or on behalf of the customer at existing interconnections between the gas transmission facilities of the Company and other pipeline systems. These points of receipt shall be those that are agreed to from time to time by the customer and the Company.
- C. The Company shall endeavor to deliver gas to the customer, and the customer shall endeavor to take a quantity of gas that is thermally equivalent to the gas that it delivers or causes to be delivered. Such delivery on the part of the Company and take on the part of the customer is to be made at the outlet of the Company gas meter(s) identified in the transportation contract.
- D. The Company shall retain 0.82 percent of all gas received at the points of receipt to compensate it for the Company's use and lost and unaccounted for gas on the Company's system ("Allowance for Use and Loss"). This volume shall not be included in the quantity available for delivery to the customer.
- E. If, in any month, the quantity of gas received by the Company at the points of receipt, less the Allowance for Use and Loss, is more than the quantity of gas taken by the customer at the points of delivery, then the difference shall be retained by the Company and delivered to the customer in those succeeding months when the quantity of gas received by the Company is less than the customer's requirements. Such subsequent deliveries to the customer shall be subject to the withdrawal limitations identified on the Transportation Service Rate Schedule. Should the aggregate quantity of gas, less the Allowance for Use and Loss, retained by the Company at any month-end exceed the authorized tolerance level, then the Company shall have the right: (1) to refuse to receive any additional quantity of gas for that customer until the Company has satisfied itself that the quantity of gas retained for the customer is less than the authorized tolerance level and (2) to assess the customer a Load Balancing Charge for any month-end balance that exceeds the authorized tolerance level. The customer shall withdraw or transfer any gas retained by the Company within 60 days of the termination of the contract.
- F. Nothing herein shall prevent the Company and the customer from entering into a separate storage agreement.

F4.2 Delivery Pressure.

All deliveries of gas by the customer and the Company shall be made at a pressure sufficient to effect same, provided that neither party shall directly or indirectly cause the other to make such deliveries at a pressure in excess of that which would be a reasonably expected maximum.

F4.3 Shutoff of Service.

The Company shall not be required to perform service under a transportation contract on behalf of any customer failing to comply with any and all terms of the customer's contract, and the Company's Gas Rate Schedule.

F5. BILLING

On or before the 20th of each calendar month, the Company shall endeavor to render a statement to the customer for service during the prior calendar month, such statement to show a separate billing for each of the customer's accounts. The Company and the customer shall have the right at all reasonable times to examine the books, records and charts of the other party, to the extent necessary to verify the accuracy of any statement, charge or computation made under or pursuant to any provisions of this service.

F6. AUTHORIZED GAS USAGE CHARGE

A customer may apply to obtain access to the Company's system supply for gas requirements in excess of the cumulative quantity delivered to the Company (less gas used by the customer and less the Allowance for Use and Loss) on behalf of that customer. To obtain access, the customer shall make a prior written application to the Company specifying the quantity required and the time period requested (not to exceed 90 days). The Company, at its sole discretion, may grant the request if it has sufficient quantity to do so without jeopardizing service to other customers. If the Company is unable to grant the request, in whole or in part, it shall notify the customer of the quantity available (if any), and shall maintain the application on file. If multiple customers request access, service shall be made available on a first-requested, first-served basis. Priorities will be established based on the time of receipt of the application by the Company. Existing unserved applications shall have priority over any new application.

F7. UNAUTHORIZED GAS USAGE CHARGE

A customer who has not obtained authorized access to the Company's system supply shall be subject to an unauthorized gas usage charge as designated on the Transportation Service Rate.

F8. TRANSPORTATION RATE RESTORATION CHARGE

A turn-on charge of the sum of the intervening months' Customer Charges since the service was shut off, shall be made to any transportation rate customer who orders a shutoff and a restoration of service at the same premises within a period of 12 months.

F9. AGGREGATION OF ACCOUNTS

Customer may qualify for aggregation of accounts under option *A* or *B* below.

Option A: Contiguous Facilities.

When an industrial or commercial customer purchasing gas under the General Service Rate Schedule (GS-1, GS-2, or GS-3), or a commercial and/or industrial transportation customer transporting gas under the Transportation Service Rate Schedule (ST, LT, XLT) occupies a group of buildings or parts of buildings which are exclusively used by such customer as a unitary enterprise under a common ownership or leasehold, the quantities of gas supplied to such buildings or parts of buildings under the same rate schedule will be added for the purpose of determining the amount of the bill which such customer shall receive for service, provided:

- (i) The buildings or parts of buildings are situated upon the same parcel or contiguous parcels of land and are exclusively occupied and used by the customer as a unitary enterprise at one location and under one management; or
- (ii) The buildings or parts of buildings, separated by a public street or alley (but not including a limited-access highway), are situated upon parcels of land which occupy wholly or in part immediately opposite street frontages on the same street or alley and are exclusively occupied and used by the customer as a unitary enterprise at one location and under one management.

Option B: Master Account

A customer receiving gas service at multiple facilities under a common ownership may elect to aggregate the quantities of gas supplied to such facilities if the following conditions are met:

- (i) The customer must designate one of the facilities as the master account. The master account must be a transportation account under Rate ST, LT, or XLT.
- (ii) Only subsidiary accounts will be eligible for aggregation with the master account. To qualify as a subsidiary account a facility must be served under a sales service rate schedule (Rate A, A-1, or GS). The customer must specify which of the other facilities will be designated as a subsidiary account.
- (iii) The facility designated as the master account shall be subject to and billed under the provisions of its transportation tariff. Facilities designated as subsidiary accounts shall be subject to all the terms and conditions of the master account tariff, except that the subsidiary accounts will pay the customer charge and distribution charge in effect for their designated sales rates rather than the customer charge and transportation charge in effect for the master account.

F10. ELECTRONIC BULLETIN BOARD

The Company shall make available, maintain and update, an electronic bulletin board (EBB) accessible to shippers and the public via the Internet with respect to the following eight (8) interconnections at which gas can be received by the Company's gas transmission system (receipt points) from pipelines other than the Bluewater Pipeline and pipelines in Michigan owned by Panhandle Eastern Pipe Line Company, Trunkline Gas Company, and the Jackson Pipeline Company:

1. Stag Lake in White Pigeon Township, St Joseph County, Michigan,
2. Otisville in Forest Township, Genesee County, Michigan,
3. Overisel in Overisel Township, Allegan County, Michigan,
4. Chippewa in Chippewa Township, Isabella County, Michigan,
5. Birch Run in Birch Run Township, Saginaw County, Michigan,
6. Blue Lake "36" in Blue Lake Township, Kalkaska County, Michigan,
7. Goose Creek in Blue Lake Township, Kalkaska County, Michigan,
8. Northville in Northville Township, Wayne County, Michigan.

The EBB shall:

- (a) List the name of each pipeline or other transportation facilities to which the Company is connected at each of the 8 receipt points,
- (b) Contain for each receipt point for each month of the calendar year the daily volume of gas the interconnection is designated to accept for transfer from shippers into the Company's gas transmission system (the Designated Capacity) and the volume of gas the Company is ready, willing and able to accept at each receipt point (the Available Interconnection Capacity) if different from the Designated Capacity,
- (c) Provide a schedule for each receipt point of the average daily volume of gas from shippers recorded by the Company's Supervisory Control and Data Acquisition system at the interconnection during the previous month (the Recorded Throughput),
- (d) Provide shippers at least 48 hours notice in advance of the Company's scheduled maintenance for a receipt point whenever such maintenance would reduce transfer capacity at the receipt point, including a posting of the reduced transfer capacity for the receipt point (the Adjusted Designated Capacity) to reflect the amount of any expected or potential reduction in the Designated Capacity, the planned date the reduction is expected to end and include in the Adjusted Designated Capacity the volumetric impact of a force majeure event, once that event and impact becomes known,
- (e) Identify for shippers as soon as reasonably possible, but in no case later than 24 hours after its occurrence, the amount of any unscheduled reduction in the transfer capacity of any receipt point by reason of force majeure or otherwise, including the reason for the reduction and an estimate of the time when the transfer capacity would be restored to its previously scheduled amount,
- (f) No later than the second business day of each month, a listing for the month of the volumes of gas that shippers propose to deliver to each receipt point (the Amount Nominated) and a schedule for each receipt point matching the Amount Nominated to the volumes to be received by the corresponding recipients (the Amount Confirmed), and
- (g) List the telephone number and fax number of the Michigan Public Service Commission Gas Staff and the telephone number of the Federal Energy Regulatory Commission Enforcement Task Force Hotline where any complaints about the Company's operation of the receipt points may be lodged.

Transportation Service Rate
(Rates ST, LT, and XLT)**Availability**

Subject to any restrictions, service under this rate schedule is available to any customer that could otherwise purchase gas under another Company Rate Schedule. A customer selecting transportation service is not eligible to receive gas under any of the Company's firm gas sales rates for a minimum period of one year from the date the customer commenced taking transportation service.

Under this rate schedule, the Company shall transport gas for the customer to the interconnections between the Company's facilities and those of the customer (points of delivery), from the interconnections between the Company's facilities and those of a third party that delivers gas to the Company for redelivery to the customer (points of receipt).

A producer or a broker may contract for service on this rate schedule for the transportation of gas from a wellhead through the Company's system to another pipeline, for the transportation of gas from one pipeline to another pipeline or for the transportation of gas from a specified interconnection between the Company's facilities and those of a third party for delivery to a specific customer within the Company's integrated distribution system, provided that all gas transported for a producer or broker pursuant to this rate schedule is consumed in and never leaves the State of Michigan after entering the Company's system.

All customers requesting transportation service under this rate schedule shall make written application for such service on a form provided by the Company.

Rates and Charges

	<u>Service Category</u>		
	<u>ST</u>	<u>LT</u>	<u>XLT</u>
<u>Monthly Charges</u>			
<u>Customer Charge</u>	<u>\$450.00 per meter</u>	<u>\$2,000.00 per meter</u>	<u>\$5,550.00 per meter</u>
<u>Remote Meter Charge</u>	<u>N/A</u>	<u>N/A</u>	<u>\$ 70.00 per meter</u>
<u>Transportation Rates</u>			
<u>Cost Based Rate</u>	<u>\$0.5891 per Mcf</u>	<u>\$0.4016 per Mcf</u>	<u>\$0.3148 per Mcf</u>
<u>Optional Rates:</u>			
<u>Maximum Rate</u>	<u>\$0.9482 per Mcf</u>	<u>\$0.5732 per Mcf</u>	<u>\$0.4796 per Mcf</u>
<u>Minimum Rate</u>	<u>\$0.2300 per Mcf</u>	<u>\$0.2300 per Mcf</u>	<u>\$0.1500 per Mcf</u>

Selection of Service Category and Rates:

A Customer may choose the Service Category under which they take service, consistent with the provisions of Rules B5.1 and B5.2. When the Customer is selecting its initial Service Category, the Company must advise them that the economic break even point between ST and LT is 100,000 Mcf per year and the economic break even point between LT and XLT is 500,000 Mcf per year. After the initial selection is made, then it is the customer's responsibility to determine when it is appropriate to switch Service Categories, as permitted by Rule B5.2.

The customer will be charged the Cost Based Rate under its chosen Service Category, unless the customer chooses to negotiate a different rate under the Optional Rate provision. The Company must advise the customer of its right to negotiate rates under the Optional Rate provision, however the Company is under no obligation to offer a rate different than the Cost Based Rate. The Company, at its discretion, may negotiate different transportation rates for individual customers between the maximum and minimum rates under the appropriate Optional Rate provision. The negotiated rate may be applied to the customer's entire load or a portion of its load; however, under no circumstances can the Company charge an average rate per Mcf greater than the maximum rate or less than the minimum rate. The transportation rate is charged for each Mcf of gas delivered to the customer in a given month.

Transportation Service Rate (continued)
(Rates ST, LT, and XLT)

Authorized Gas Usage Charge

A customer may request in advance to purchase authorized gas in accordance with the Company's Gas Rate Schedule. The Company may grant such request if sufficient supplies are available. In such instances, the customer shall be billed for such authorized usage at the customer's Designated Sales Rate, plus \$1.00 per Mcf. The customer shall pay \$.10 per Mcf for any unused volume that the customer received authorization to take. The Customer Charge shall be that as contained on the customers' designated service category.

Unauthorized Gas Usage Charge

A customer who has not obtained authorized access to the Company's system supply for such Account(s) shall pay an Unauthorized Gas Usage Charge for any unauthorized volumes taken. Such charge shall be the highest price reported for Michigan or Chicago LDC's during the applicable month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$10 per Mcf for all gas taken by the customer in excess of the cumulative volume delivered to the Company (less gas used by the customer less the Allowance for Use and Loss) on behalf of the customer.

Monthly withdrawals from the customer's previous month-end balance during November through March will be limited to the customer's Contract Storage Quantity (CSQ), if any, plus 3% of the customer's ACQ. If in any month the quantity of gas received by the Company, less the allowance for gas-in-kind plus 3% of the transportation customer's ACQ and its allowed CSQ is less than the quantity of gas taken by the customer at the points of delivery, then the excess delivery will be treated as unauthorized gas usage and subject to the "Unauthorized Gas Usage Charge".

Load Balancing Charge

A customer shall be charged \$.25 per MMBtu for any month-end balance of gas that exceeds the sum of its Authorized Tolerance Level (ATL) plus its contract storage quantity. In addition, there is a 2.0 percent gas-in-kind for fuel used for injection, for any month-end balance of gas that exceeds the authorized tolerance level and is in excess of the prior month-end balance.

A customer's ATL shall be 8.5% of the Customer's ACQ unless the customer contracts for a different percent in accordance with the following table. The Transportation Charge shall be adjusted as follows:

<u>Authorized</u> <u>As a % of ACQ</u> <u>Tolerance Level</u>	<u>Transportation</u> <u>Charge Adjustment</u>
<u>6.5%</u>	<u>\$(0.0420) Per Mcf</u>
<u>7.5%</u>	<u>\$(0.0210) Per Mcf</u>
<u>8.5%</u>	<u>No Change</u>
<u>9.5%</u>	<u>\$0.0210 Per Mcf</u>
<u>10.5%</u>	<u>\$0.0420 Per Mcf</u>

The monthly injection of gas into the customer's ATL and additional CSQ, if any, shall be at the customer's discretion except in September and October when any monthly injections in excess of the customer's CSQ plus 1.43% of the customer's ACQ, will be charged the Load Balancing Charge.

M.P.S.C. No. 1 - Gas
Consumers Energy Company

Sheet No. F-10.00

Transportation Service Rate (Continued)
(Rates ST, LT, and XLT)

Excess Pipeline Costs Surcharge

This surcharge shall be assessed to the customer.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill that is not paid in full on or before the due date shown thereon.

General Terms and Conditions

This rate is subject to all general terms and conditions shown on Sheet No. E-1.00 of the Company's Gas Rate Schedule.

Term and Form of Contract

All service under this rate shall require a written contract with a minimum term of one year and month-to-month thereafter which must be approved by an officer of the Company or a duly authorized agent before it shall be binding upon the Company. A customer may cancel this contract at the end of any month in order to take service under Small Transportation Service Rate ST-2. A customer eligible to request a return to sales rates must provide a minimum of 12 months written notice of their intent to return to sales rates. For purpose of the notice requirement, notice must be delivered to and received by the Company. The burden is on the customer to establish notice has been given. The Company reserves the right to deny return to sales rates subject to the Company's Controlled Service Rule B3.

M.P.S.C. No. 1 - Gas
Consumers Energy Company
(To cancel Sheet Nos. F-11 Through F-19)

Sheet Nos. F-11 through F-19

Sheet Nos. F-11 through F-19 have been cancelled.

Transportation Rate Schedules ST-1, ST-2, LT-1, and LT-2 have been replaced by
Transportation ServiceRate Schedule (Rates ST, LT, and XLT)

CONTRACT STORAGE SERVICE RATE CS**Availability**

Subject to any restrictions, this rate is available to any transportation customer desiring storage service provided the Company has determined that it has sufficient available and uncommitted storage capacity to perform the service requested.

Delivery of gas into or out of storage may be subject to interruption at the sole discretion of the Company.

A customer requesting service on this rate shall make written application for such service on a form provided by the Company. A storage agreement shall also be required.

Monthly Rate**Administrative Fee**

\$200 per account per month, plus

Storage Charge

\$0.20 per MMBtu to \$1.50 per MMBtu, as negotiated.

Unauthorized Gas Usage Charge

The Company is authorized to charge storage customers for deliveries to, or redeliveries from, storage in excess of the maximum quantities set forth in the storage agreement. The penalty rates shall not exceed the current Unauthorized Gas Usage Charge stated in the applicable Transportation Service Rate Schedule.

Fuel Used for Injection

All gas placed in storage shall be subject to a 2.0 percent gas-in-kind for fuel used for injection.

Due Date and Late Payment Charge

The due date of the customer's bill shall be not more than 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

General Terms and Conditions

This rate is subject to all general terms and conditions shown on Sheet No. E-1.00 of the Company's Gas Rate Schedule.

Term and Form of Contract

All service under this rate shall require a written contract which must be approved by an officer of the Company or a duly authorized agent before it shall be binding upon the Company.

OPTIONAL INTERCONNECTION ASSURANCE SERVICE RATE OIAS**Availability**

This optional service is available to shippers utilizing the eight (8) receipt points, as designated for listing on the electronic bulletin board by Section F11, in connection with Rates CC, ST, LT, and XLT. (See Section F11 for definitions of terms used in this rate.) A shipper can take this service for one or more of the receipt points at the shipper's option. A shipper does not have to take service under this rate in order to utilize the receipt points. However, the only way a shipper can be eligible for the back-up service provided hereunder is to elect this rate.

A shipper may elect this rate in two ways:

- A. By making written application in advance on a form provided by the Company for back-up service (Pre-arranged Back-up Service) under the rate, or
- B. By a verbal request and certification at the time of a Receipt Point Restriction which triggers the need for back-up service under the rate (Short Notice Back-up Service).

Monthly Administrative Fee

- A. \$10 per receipt point per month for the receipt points identified by the shipper in a written contract signed in advance for Pre-arranged Back-up Service under this rate.
- B. A \$100 charge per receipt point for each Receipt Point Restriction for Short Notice Back-up Service under this rate.

Conditions of Pre-arranged and Short Notice Back-up Service at Eight (8) Receipt Points

The provisions of this paragraph apply whenever the Company declines a shipper's nominations of gas for one of the 8 receipt points because the Available Interconnection Capacity at the receipt point is less than the Adjusted Designated Capacity at the receipt point (a Receipt Point Restriction). Whenever there is a Receipt Point Restriction, the Company shall provide to a shipper on this rate two alternatives: first, the Company will offer to accommodate the shipper's gas at another receipt point if the affected shipper is able to move its deliveries to that interconnection without any additional cost to the shipper, or secondly, if the shipper certifies in writing that it is unable to move its deliveries at no additional cost, the Company will provide as back-up service under this rate, from the Company's system supply gas, the volume of gas which could not be transferred through the receipt point because the shipper's Amount Confirmed was less than the shipper's Amount Nominated because of a Receipt Point Restriction. By the end of the calendar month following the month in which a Receipt Point Restriction occurred, a shipper on this rate shall return in kind at any receipt point on the Company's system the volume of gas provided from the Company's system supply gas. An Unauthorized Gas Usage Charge shall be assessed the shipper on any volumes not so returned.

Unauthorized Gas Usage Charge

For failure by a shipper to return gas provided pursuant to the terms of this rate, the Company shall charge a shipper the currently effective gas cost recovery factor (stated on a MMBtu basis) on General Service Rate C plus \$6 per MMBtu for all volumes of gas not returned by the shipper.

Due Date and Late Payment Charge

The due date of the shipper's bill shall not be more than 21 days from the date of billing. A late payment charge of 2% of the unpaid balance, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

H1. GENERAL PROVISIONS (Contd)

- L. The Company shall remit to the Supplier, approximately 21 days from the end of each calendar month, an amount for the cost of gas equal to the MMBtu quantities that the Supplier has delivered onto the Company's system, not in excess of the Suppliers' delivery obligation, multiplied by the lesser of the price per Mcf converted to MMBtu, billed to the Supplier's customers that month or 110% of the cost of gas billed to sales customers pursuant to the Company's Rule B10. The amount to be remitted shall be reduced for any applicable Supply Equalization Charges, Administrative Fees, Billing Fees, Failure Fees, and/or amounts owed pursuant to the annual price reconciliation per Paragraph M.
- M. Except as set forth below, within 60 working days after the end of the March billing cycle, or revocation of a Supplier's Authorized Supplier status, the Company will reconcile the cost per MMBtu remitted to the Supplier per Paragraph L, before reductions for Administrative Fees, Billing Fees, Failure Fees, and Supply Equalization Charges, converted to cost per Mcf using monthly system-average Btu content, with the price per Mcf billed to customers over the course of the program year on the Supplier's behalf. Any difference multiplied by the smaller of the Mcf delivered by the Supplier or the billed customer consumption for the year being reconciled, will be reflected in an adjustment on the next monthly remittance to the Supplier.
- In those instances where both (i) the price per Mcf billed to customers over the course of the program year on the Supplier's behalf is higher than the cost of gas billed to sales customers by the Company pursuant to the Company's Rule B10, and (ii) the MMBtu delivered by the Supplier converted to Mcf exceeds the billed customer consumption for the year being reconciled, then the following procedure will be used. In such instances, (i) within 60 working days after the end of the March billing cycle, or revocation of a Supplier's Authorized Supplier status, the Company will reconcile the amount billed to customers on the Supplier's behalf with the Company's remittance to the Supplier for the gas delivered, and any difference will be reflected in an adjustment on the next monthly remittance to the Supplier, and (ii) gas delivered by the Supplier in excess of the actual customer consumption will be returned to the Supplier in kind unless the Company and the Supplier mutually agree on a price for the Company to purchase the excess gas.
- N. A Supplier that fails to comply with the terms and conditions of the program shall have its Authorized Supplier status suspended and/or terminated and subject to Rule B3, Controlled Service, its customers shall become sales rate customers of the Company.
- O. The Company will convert customer consumption from Mcf to MMBtu using monthly system-average Btu content.
- P. Where used in this rule, the term "month," unless otherwise indicated, means billing month when referring to customer consumption and calendar month when referring to deliveries by Suppliers.
- Q. The annual load requirement, delivery schedules, Supply Equalization Charges, delivery shortfall Failure Fees and annual reconciliation shall apply separately to each Supplier-designated pricing category and each of the two customer groups within that category, i.e. those enrolled as of April 1, and those enrolled after April 1 in each program year.
- R. The Company may disclose, at such times as requested by the Commission or its staff, the gas rates charged to Rate CC customers.

GAS CUSTOMER CHOICE RATE CC

Availability

Subject to any restrictions, this rate is available to any customer desiring gas service where the customer's gas is provided by an Authorized Gas Supplier under Rule H1. A customer will take service under this rate commencing with the customer's first full billing month following enrollment, but not earlier than April 1, 2001. Service is limited to a total of 600,000 customers beginning April 1, 2001, and 900,000 customers beginning April 1, 2002. Beginning April 1, 2003 all customers are eligible. A Rate CC customer may switch Suppliers at the end of any billing month provided the Company receives sufficient notice in a form acceptable to the Company. A customer may change Suppliers one time in any 12-month period beginning April 1 at no cost to the customer. A fee of \$10 will be required for each additional change of Supplier within the same 12-month period. If a Supplier's actions force a Customer to the Company's sales service, the Customer may choose another Supplier within 60 days without a switching fee regardless of the length of time that has elapsed since the Customer left the Company's sales service. Except as set forth in the preceding sentence, a Customer returning to the Company's sales service rates from Rate CC is subject to the Choice of Rates provisions of those sales rates and except as otherwise provided, must remain on the sales rate for 12 months.

Minimum Term

Subject to the following provisions of this paragraph, a customer who has elected to take service under Rate CC shall not be permitted to change from Rate CC to another rate until at least 12 months have elapsed. A customer who has elected to take service under Rate CC may, however, switch Suppliers during the 12-month period. During the 12-month period, a customer may only change from Rate CC to another rate if (i) the customer exercises an unconditional right of cancellation pursuant to Section H with the initial Supplier selected by the customer, (ii) the customer establishes that the customer was enrolled by a Supplier without the customer's knowing consent, (iii) the Supplier's action forces the customer to the Company's sales service, (iv) the Supplier selected by the customer defaults under its Supplier Agreement, or (v) the Supplier selected by the customer has its Authorized Supplier status revoked or terminated.

Nature of Service

The customer will remain a customer of the Company. The Company will read the meter and render a bill to the customer for the monthly customer charge, distribution charge, surcharges, penalties and taxes. The authorized Supplier's cost of gas charges will be billed as part of the Company's bill. Service is subject to all of the Company's "Schedule of Rates Governing the Sale of Natural Gas Service" as approved by the Michigan Public Service Commission. By requesting service on this rate, the customer gives consent to the Company to furnish to the customer's authorized Supplier pertinent customer sales or transportation data.

Monthly Rate**Customer Charge**

As shown on the customer's applicable sales rate schedule.

Distribution Charge

As shown on the customer's applicable sales rate schedule.

Gas Commodity Charge

The customer's cost of gas will be as communicated to the Company each month by the customer's Authorized Supplier. If a participating customer obtains gas supply from Consumers Energy as a result of its chosen Supplier becoming disqualified, or the customer otherwise returns to Company sales supply, the customer is subject to Rule B3, Controlled Service.

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of the application of	)	
CONSUMERS ENERGY COMPANY for authority	)	
to increase its rates for the distribution of natural	)	Case No. U-13000
gas and for other relief.	)	
_____	)	

**CONCURRING OPINION OF
CHAIRMAN LAURA CHAPPELLE**

(Submitted November 7, 2002)

I have signed the majority opinion, which authorizes Consumers to increase its retail rates for the sale of natural gas by \$55,728,000 on an annual basis. In reaching this determination, the Commission relied upon the rate base amount calculated by the Staff on the basis of primarily historical data rather than upon the rate base amount projected by Consumers on the basis of its planned expenditures. I write separately because I could have supported an even greater rate increase if Consumers' request for relief in this proceeding had been coupled with a proposal to collect a portion of its rates under bond, to track its capital and other O&M expenditures to ensure that they actually occurred, and to refund to customers amounts by which its rates were increased above levels of the company's actual expenditures.

At the outset, I believe that it is important to note that Consumers' most recent rate increase occurred on August 17, 1984 in Case No. U-7650, which means that Consumers has not had a rate increase for over 18 years. During that interval, the Commission thrice decreased Consumers' rates by a total of \$63 million. I consider Consumers' ability to provide gas service to its customers in the face of rate decreases and 18 years of inflation as a testament to its ability to

achieve productivity increases and wisely manage its resources. However, Consumers' current application evidences a marked departure from the past. In this proceeding, Consumers sought increases of 26% for 2001 and 64 % for 2002 above its historical 2000 capital expenditures. Additionally, Consumers proposed to spend 28 % above historical levels for other O&M expenditures in 2002. These hefty spending increases after 18 years of declining rates and productivity gains raise suspicion.

Nevertheless, I believe that with added precautions, the Commission could have reasonably granted Consumers a rate increase of up to \$62 million on an annual basis while ensuring reasonable rates to customers. The Commission proposed such an approach in its May 7, 1991 order in Case No. U- 9346, a Consumers electric rate case. In that proceeding, the Commission provided that \$35 million of Consumers' annual rate revenue could be collected under bond and subject to refund in the event that Consumers failed to spend the full amount of the other O&M expenditures authorized by the Commission.¹ Had Consumers proposed such a mechanism in this proceeding or had the Commission provided for such a mechanism and Consumers agreed to it, I believe that it would have been appropriate to base Consumers' rates on its budgetary projections for capital expenditures and most of its projected other O&M expenditures.

MICHIGAN PUBLIC SERVICE COMMISSION

Laura Chappelle, Chairman

¹ Consumers declined to participate in the innovative approach offered by the Commission in Case No. U-9346.

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MICHIGAN PUBLIC SERVICE COMMISSION



Laura Chappelle, Chairman

¹ Consumers declined to participate in the innovative approach offered by the Commission in Case No. U-9346.

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of the application of	)	
CONSUMERS ENERGY COMPANY for authority	)	
to increase its rates for the distribution of natural	)	Case No. U-13000
gas and for other relief.	)	
_____	)	

**CONCURRING AND DISSENTING OPINION OF
COMMISSIONER ROBERT B. NELSON**

(Submitted November 7, 2002)

I support the opinion issued today in this proceeding to the extent that it authorizes an increase in natural gas distribution rates for Consumers Energy Company (Consumers) by \$47.2 million on an annual basis. I believe that Consumers has demonstrated a revenue deficiency in that amount. However, I must dissent from the remainder of the majority opinion inasmuch as it authorizes an increase in natural gas distribution rates which recognizes an equity infusion by CMS Energy Corporation (CMS) in January 2002 in Consumers' capital structure, the inclusion of an inappropriate accounting change and an inflated cost of common equity.

The majority opinion allows Consumers to increase its common equity for purposes of computing its overall cost of capital by including \$150 million in equity that was transferred to Consumers by CMS, Consumers' parent corporation, on January 3, 2002, one day prior to the filing of Consumers' rebuttal testimony in this case. In my view, Consumers has failed to demonstrate that this last minute equity infusion actually produced the result intended- to maintain and increase Consumers' credit rating by improving its equity ratio. Moreover, the record in this case provides no assurance that the equity infusion will remain with Consumers long enough to

produce a benefit to ratepayers proportionate to the benefit that inclusion of the equity in the company's capital structure will have to Consumers. Accordingly, I would agree with Staff and the Attorney General and disallow the recognition of the capital infusion for purposes of this case.

The current financial condition of Consumers and its parent, CMS, are legitimate concerns for this Commission. However, our foremost responsibility is to protect Consumers' ratepayers. Not only does this entail making sure that rates that we authorize are based on competent, material, and substantial evidence, but it also involves the adoption of a capital structure that truly reflects the business risk of a regulated utility. In addition to rejecting the recognition of the capital infusion, I would adopt a cost of common equity for Consumers that is within the range of Staff witness Ballinger's recommendation (10.75-11.25%) and authorized returns recently approved by the Commission (Cf., Wisconsin Electric Power Co., U-12725). I would provide for a slight increase from the midpoint of Mr. Ballinger's range to address Consumers' concern about his arithmetical errors and find that an 11.15% return on common equity is appropriate.

I also take issue with the majority with regard to the recognition of an accounting change designed to "true-up" accounting practices carried over from prior years. In my view, Consumers has not provided adequate record support for its position and it should not be permitted to manipulate the implementation of accounting changes to optimize its rate relief. As Staff has asserted, Consumers was able to capitalize costs that it should have expensed by delaying implementation of the accounting change from the time when the opportunity first arose (1996-7) until 2002. It now seeks to not only have the Commission use an inflated rate base to set rates, but to allow it to recover the full amount of the formerly capitalized expenses as other O&M expenditures.

Had Consumers immediately implemented the accounting change in 1996-7, over-allocated support costs would not be included in 2000 historical year plant balances and both Consumers' and Staff's 2002 test year plant balances would be dramatically different. This Commission must continue to monitor the accounting practices of utilities under our jurisdiction and recognize in rates only those practices that are in compliance with generally accepted accounting principles.

MICHIGAN PUBLIC SERVICE COMMISSION

Robert B. Nelson, Commissioner

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MICHIGAN PUBLIC SERVICE COMMISSION



Robert B. Nelson, Commissioner

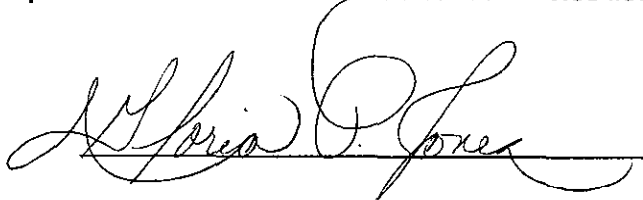
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STATE OF MICHIGAN)

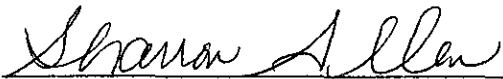
Case No. U-13000

County of Ingham)

Gloria P. Jones being duly sworn, deposes and says that on November 8, 2002, A.D. she served a copy of the attached Order by mailing copies thereof by first class mail, postage prepaid, or by inter-departmental mail, to the persons as shown on the attached service list.

A handwritten signature in cursive script, appearing to read "Gloria P. Jones", written over a horizontal line.

Subscribed and sworn to before me
this 8th day of November 2002

A handwritten signature in cursive script, appearing to read "Sharon Allen", written over a horizontal line.

Notary Public, Ingham, County, Michigan
My Commission expires August 16, 2004

SERVICE LIST FOR DOCKET # U - 13000-
DATE OF PREPARATION: 10/28/2002

CASE #

MR. MICHAEL VAN HEMERT
CONSUMERS ENERGY COMPANY
212 W. MICHIGAN AVENUE
JACKSON MI 49201

MR. THOMAS C. DEWARD
25806 GLOVER COURT
FARMINGTON HILLS MI 48335

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SPECIAL LITIGATION DIVISION
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ID MAIL

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CLARK HILL PLC
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SUITE 301
BIRMINGHAM MI 48009

MR. JON R. ROBINSON
CONSUMERS ENERGY COMPANY
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JACKSON MI 49201

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DICKINSON WRIGHT PLLC
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MR. DANIEL E. NICKERSON, JR.
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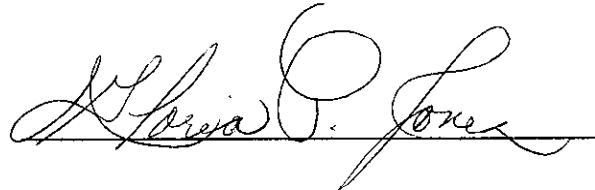
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STATE OF MICHIGAN)

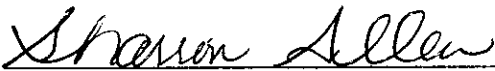
Case No. U-13000

County of Ingham)

Gloria P. Jones being duly sworn, deposes and says that on November 12, 2002, A.D. she served a copy of the attached Order by mailing copies thereof by first class mail, postage prepaid, or by inter-departmental mail, to the persons as shown on the attached service list.

A handwritten signature in cursive script, reading "Gloria P. Jones", written over a horizontal line.

Subscribed and sworn to before me
this 12th day of November 2002

A handwritten signature in cursive script, reading "Sharon Allen", written over a horizontal line.

Notary Public, Ingham, County, Michigan
My Commission expires August 16, 2004

SERVICE LIST FOR DOCKET # U - 13000-
DATE OF PREPARATION: 11/12/2002

CASE #

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