

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter, on the Commission's own motion,
to investigate the appropriateness of instituting a
surcharge to assist in the funding of the
Gas Technology Institute

Case No. U-14561

REPLY BRIEF OF THE GAS TECHNOLOGY INSTITUTE

DATED: June 22, 2006

FRASER TREBILCOCK DAVIS & DUNLAP, P.C.
BY: Robert B. Nelson (P23644)
Business Address:
124 W. Allegan, Ste 1000
Lansing, MI 48933
Telephone: (517) 377-0854

The Gas Technology Institute (GTI) herewith submits the following in response to the briefs filed by various parties in this case on June 22, 2006.

RESPONSE TO ABATE

In its initial brief , the Association of Businesses Advocating Tariff Equity (ABATE) has made three assertions, each of which is inaccurate. ABATE once again contends that GTI has breached a 1998 FERC settlement agreement, that only voluntary payments by customers would comply with previous FERC orders, and that GTI has sought mandatory funding of research and development (R&D). This reply brief will respond to each of these contentions.

ABATE's initial brief repeats both its unsuccessful challenge to GTI's right to participate in this proceeding and its previously rejected advice that by allowing this proceeding to go forward the Commission risks becoming "complicit" in GTI's alleged attempt to breach a settlement agreement approved by the Federal Energy Regulatory Commission (FERC) in 1998 relating to the funding of GTI's predecessor agency, the Gas Research Institute (GRI).

The simple fact is that GTI has not breached the 1998 settlement agreement by participating in the instant proceeding. That agreement is entirely silent as to such participation and GTI is legitimately participating here as a party in a proceeding initiated by the Commission.

Furthermore, a decision by this Commission approving R&D funding through rates and charges subject to its jurisdiction would in no way constitute a breach of the 1998 settlement agreement. As demonstrated earlier in this proceeding, and as will be demonstrated again here, the merits of ABATE's argument as to the relevance of the 1998 settlement agreement to this proceeding depend upon whether the FERC should be seen as precluding collaborative RD&D funding after 2004 through interstate pipeline rates and charges subject to its jurisdiction, except that which is purely voluntary, or whether the FERC can be credited with precluding such

RD&D funding through rates and charges, regardless of jurisdictional considerations, except purely voluntary funding.

As ABATE's initial brief makes clear, it relies very heavily on the faulty premise that, in approving the 1998 settlement agreement, the FERC intended to preclude collaborative RD&D funding through rates and charges for LDC services subject to state commission jurisdiction. Indeed it is the prospect of such funding that according to ABATE would make the Commission complicit with GTI in breaching the 1998 settlement agreement and legally binding obligations there under. (ABATE's Initial Brief at 4).

ABATE's initial brief does mention the fact that this Commission has already held that that ABATE's reliance on the 1998 settlement agreement for this purpose is misplaced and that LDCs may make a request to impose a state-wide funding mechanism for R&D. (ABATE's Initial Brief at 1). The Commission unequivocally rejected ABATE's arguments in this regard in its October 18, 2005 ruling in this proceeding. Nevertheless ABATE persists in repeating and slightly expanding upon such misplaced reliance throughout the leading argument of its initial brief. Clearly, ABATE's continued reliance on the 1998 settlement agreement adds nothing of substance to its position.

Absolutely nothing contained in the 1998 settlement agreement itself and nothing written by the FERC about the 1998 settlement agreement comes close to justifying ABATE's position. Of course the FERC pays attention to information brought to its attention by a wide variety of gas industry stakeholders. But in the end the FERC is legally bound to take action through means within its jurisdiction, in this case interstate pipeline rates and charges. It is in that context, and no other, that the FERC has approved an agreement that limits GRI, and its successor GTI, to purely voluntary funding after 2004.

According to ABATE's simple logic, it and its members are not interested in making voluntary contributions to GTI, and GTI is not entitled to anything but such voluntary contributions because GTI, as GRI's successor, is bound by the 1998 settlement agreement. (e.g., ABATE's Initial Brief at 1 and 3-5). It is clear from this and other aspects of its argument that ABATE is attempting to convince the Commission that the FERC-approved settlement has somehow precluded all GTI funding through distribution and transportation rates and charges except that which is volunteered by gas consumers. ABATE is simply wrong.

When all is said and done, the 1998 settlement agreement remains one that makes interstate pipeline participation in R&D funding voluntary, not one, as ABATE would have it, that precludes distribution or transportation rates that must be paid for gas service that include increments to cover RD&D contributions.

Beginning on page 4 and continuing onto page 6 of its initial brief, ABATE focuses on language in the FERC's order approving the 1998 settlement agreement that discusses the topic of voluntary funding addressed in Section 1.7 of that agreement, quoting the FERC's discussion extensively. Immediately after the quoted language, ABATE states that "GTI agreed that on and after January 1, 2005, all GTI funding will be on a voluntary basis for all "shippers". This is simply inaccurate and logically unsupportable.

In fact, interstate pipeline shippers are not exempted from paying a share, like it or not, of RD&D costs after 2004 according to two portions of the language quoted by ABATE. First, the 1998 settlement agreement, in referring to "Voluntary Funding" (Section 1.7), describes a process whereby individual interstate pipelines, after 2004, would voluntarily contribute to particular RD&D projects and, subject to challenge, such contributions would be "recoverable in rates." ABATE has previously acknowledged that this type of funding qualifies as voluntary

(Appeal, p. 9), despite the fact that any such funding approved by the FERC would result in rate increments that pipeline customers would have to pay for gas service.¹

Additionally, according to the 1998 settlement agreement, after 2004, interstate pipeline shippers, which of course include LDCs, may "specify the level of contribution" they are willing to support pursuant to a "check the box" mechanism with interstate pipelines serving as collection agents. The FERC and the affected parties clearly contemplated in 1998 a system in which LDCs could "voluntarily contribute" to RD&D as evidenced by the fact that the "check the box" approach is still operational.

Rather, ABATE makes heavy use of the term "voluntary" in an attempt to distinguish the "check the box" mechanism from any that might result from this proceeding and to obscure the fact that if "check the box" amounts are approved by state commissions for pass-through, they then would be reflected in rates and charges for distribution service that would have to be paid by gas consumers. And as indicated above, ABATE also attempts to use its members' status as interstate pipeline shippers and its participation in the 1998 settlement process in aid of its position.

In this vein, ABATE attempts to leave the impression that it helped draft the 1998 settlement agreement and therefore it knows that the use of the word "shippers" in the fourth sentence of the FERC's discussion of Section 1.7 of the agreement precludes any shipper from having to bear any post-2004 RD&D cost unless the shipper agrees to pay. In light of the foregoing, however, it should be clear that under certain circumstances contemplated by Section 1.7 of the 1998 settlement agreement such shippers would have to pay.

¹ See *Gas Technology Institute*, 109 FERC ¶61,162 (2004) at slip op. 23-24, where the FERC clearly indicates that rate recovery of such individual pipeline contributions would qualify for consideration subject to Section 4 of the Natural Gas Act. Any resulting rate recovery mechanism would become part of what the customers of such pipelines would have to pay for gas service.

ABATE's allegations to the contrary rest on an inaccurate reading of the 1998 settlement agreement and faulty logic. The most ABATE can demonstrate concretely is that some interstate pipeline shippers may not have to pay post-2004 RD&D costs, unless they volunteer to do so. Indeed shippers not subject to having such costs passed through to them by way of FERC-approved "voluntary subscriptions by interstate pipelines for particular research and development projects benefiting consumers," "check the box" costs approved by state or local regulatory bodies, or RD&D costs associated with independent state or local regulatory action, would be in a position to avoid paying gas industry RD&D costs. None of these circumstances are relevant here however. Given this, it is clear that ABATE's alleged expertise arising from participation drafting the 1998 settlement agreement, its opinion as to what "voluntary" means, and its argument that all "shippers" are exempt from paying post-2004 RD&D cost unless they agree, are all unavailing.

From the foregoing it is clear that ABATE has effectively conceded an LDC's right to directly apply to the Commission for rate recovery of costs associated with contributions toward GTI-sponsored RD&D activities, and that the FERC has provided two "purely voluntary" means of interstate pipeline participation in post-2004 GTI funding, one that would assure pass-through of the costs involved at the retail level, and another that would make such pass-through discretionary with state and local regulators. There is ample precedent for holding that such pass-through decisions are within the exclusive purview of this Commission. See *Panhandle Eastern Pipeline Company*, 887 F 2d 1295, 1300 (6th Cir 1989).

As things stand, there are at least three instances in which ABATE's "voluntary" funding argument clearly falls down and ABATE has failed to make a compelling case here as well. Indeed, inclusion of the "check the box" mechanism in the 1998 settlement agreement indicates that state and local regulators were intended to have opportunities to participate in post-2004 GTI

R&D funding. The instant proceeding accomplishes this purpose and in no way constitutes an attempt by GTI to breach its obligations.

In light of the foregoing, it is clear that the term “voluntary” funding as pertains to the 1998 settlement agreement does not mean that gas consumers may choose whether to pay approved rate increments intended to cover GTI R&D costs. Nevertheless, one might wonder what it does mean. As suggested above, GTI submits that the term “voluntary” as used within the context of the 1998 settlement agreement refers to interstate pipeline rate matters within the jurisdiction of the FERC and not, as ABATE would have it, to distribution rate matters within the jurisdiction of this Commission. In approving the 1998 settlement agreement, the FERC limited interstate pipeline participation in post-2004 GTI funding to the two means discussed at length above, thus making the participation of FERC jurisdictional pipelines voluntary.

The fact is that for years the FERC used the term “voluntary” to characterize approved GRI R&D funding, despite the fact that rate increments to cover the cost of that funding were not discretionary to consumers. In one of the three proceedings resolved by the 1998 settlement agreement, the FERC set out the background for its proposal to impose a gas industry R&D funding system that all pipelines would participate in.

There, the FERC characterized an R&D funding mechanism put in place in 1993 as one that was voluntary in the sense that it for the first time permitted pipelines to discount without having to absorb GRI costs. As a basis for its proposed rule, the FERC stated as follows:

“The Commission shares the concerns of those who believe that continuation of voluntary funding threatens the RD&D efforts of GRI. The limits of voluntary funding for GRI, in the more than three years that the temporary voluntary funding mechanism has been in place, have been explored.” *Research, Development, and Demonstration Funding*, 62 Fed. Reg.24,853 (May 7, 1997), FERC Stats. & Regs. ¶ 32,524 (1997).

It is clear from this that the FERC has long characterized R&D funding mechanisms subject to its jurisdiction as voluntary so long as they afford interstate pipelines some measure of discretion. And given that the two means left open to interstate pipeline participation in post-2004 GTI funding afford pipelines even greater discretion than previous voluntary funding mechanisms, it is perhaps not surprising that the FERC has deemed such funding “completely” or “purely” voluntary.

Given the FERC’s focus on whether R&D funding participation by FERC jurisdictional interstate pipelines is voluntary or not, and the limitations of the FERC’s jurisdiction, GTI submits that it is not credible to attribute to the FERC in approving the 1998 settlement agreement an intent to preclude this Commission, Michigan LDCs or GTI from pursuing means of funding R&D through state regulatory means that do not involve pipelines at all. At the very least, such a departure from the FERC norm would have been addressed at some length and detail in the extensive procedures leading to the 1998 settlement agreement or in the FERC orders pertaining thereto.

And yet ABATE has cited nothing in the 1998 settlement agreement or related FERC documents that speaks directly to an intention to limit the discretion of state and local regulators that may contemplate extending rate coverage to costs associated with GTI-sponsored RD&D. The same is true with regard to restricting anyone from approaching such regulators for the purpose of providing for GTI funding. Indeed, ABATE might have noticed the explicit statement at page 3 of the settlement agreement indicating that it is intended to resolve only the specific issues pending in the three captioned proceedings in which it was filed, none of which address limiting GTI to funding avenues that remain at the federal level and those that are voluntary from a consumer’s perspective.

Nothing, however, in the 1998 settlement agreement or related FERC pronouncements indicates that costs associated with voluntary pipeline RD&D contributions no longer may be passed through to consumers nor that state and local regulators may not, in accordance with applicable law, approve rate increments to cover RD&D costs regardless of whether such increments are associated with the “check the box” mechanism or an approach totally unrelated to interstate pipeline involvement. Neither ABATE’s participation in the proceeding leading to the 1998 settlement agreement, nor its status as a shipper can overcome the fact that the 1998 settlement agreement and related documents simply do not support ABATE’s position in this proceeding.

In fact in its latest order dealing with RD&D funding, the FERC noted that GTI had raised some \$17 million from LDCs and, instead of objecting, the FERC went on to point out that individual pipelines were free to apply to the FERC for similar funding. *See Gas Technology Institute*, 109 FERC ¶61,162 (2004) at slip op. 23-24. That neither state nor federal regulators are behaving in a manner that supports ABATE’s position in this proceeding is yet another reason to doubt that it is well grounded.

ABATE has alleged, in its initial brief that the “reason behind GTI’s efforts to impose a mandatory surcharge upon Michigan gas consumers is that mandatory funding which GTI and its predecessor, the Gas Research Institute (“GRI”), received pursuant to FERC surcharges expired at the end of 2004.” (ABATE initial brief, p. 3). In fact, GTI has not sought mandatory funding in this proceeding. The testimony of Mr. Edelstein and the initial brief filed by GTI make it clear that GTI supports “voluntary” funding of its projects by Michigan LDCs. Nowhere in Mr. Edelstein’s testimony or rebuttal testimony is there any mention of a mandatory surcharge or other form of mandatory funding. In fact, Mr. Edelstein specifically stated, in response to a question about mandatory funding:

“Q. Would an LDC be required to apply for recovery of R&D in accordance with the above criteria?

A. It would be up to the individual LDC to apply for recovery of R&D expenses.” (Tr 83)

As noted above, voluntary funding does not include the right of a customer, whether a shipper or otherwise, to elect to fund R&D. Rather, each LDC would have the right to request R&D funding and, if certain criteria are met, secure cost recovery. In the same way that FERC approved voluntary funding for entities under its jurisdiction, i.e. pipelines, the Commission should approve voluntary funding of R&D for entities under its jurisdiction. The Commission has broad discretionary ratemaking authority to regulate all public utilities within its jurisdiction, specifically natural gas utilities. Cf *Attorney General v PSC*, 118 Mich App.311, 315 (1982). This would even include the authority to approve surcharges for specified purposes and at the very least, the authority to decide which expenses of a gas utility should be recoverable in rates. See *Consumers Power v ABATE*, 205 Mich App. 571 (1994), appeal denied 448 Mich 872 (1995).

RESPONSE TO THE ATTORNEY GENERAL

The Attorney General (AG) has, like ABATE, asserted that the Commission has no authority to impose a mandatory surcharge on Michigan’s gas utilities to fund GTI’s R&D. As noted above, GTI has not requested a mandatory surcharge. Instead, GTI has supported a voluntary funding mechanism for each gas utility that seeks to recover R&D funding in rates.

The AG has also asserted that the Commission should not adopt: “any type of requirement” that a gas utility use GTI to conduct R&D. (AG brief, p.7) GTI has never indicated that R&D should only be performed by GTI to be eligible for recovery in utility rates. In fact, in setting forth criteria that would need to be met in order for a utility to avail itself of a rebuttable presumption for cost recovery, GTI did not intend to preclude a utility who seeks to

recover R&D expenses separate from GTI from utilizing the criteria to avail itself of this presumption.

In this regard, the AG , in summarizing the testimony of the Staff, indicated that Staff witness Devon did not support a “rebuttal presumption’ as proposed by Mr. Edelstein with regard to the recovery of R&D expenses. (AG brief, p. 3) In fact, Ms. Devon did testify that the criteria set forth in Mr. Edelstein’s testimony “could be used by the Commission and gas utilities in determining” whether R&D expenses are recoverable from ratepayers. (Tr. 171) Although Ms. Devon testified that it was incumbent on each utility to provide support for R&D funding decisions in future rate case proceedings, such support could be accomplished by filing testimony that demonstrated that the criteria had been met. It is imperative that the Commission find in this proceeding that there be a rebuttable presumption of recovery for meeting specified criteria. Otherwise, the Commission would have accomplished nothing by conducting this proceeding.

The case law cited by the AG is inapposite to the current proceeding. GTI is not proposing that utilities be required to use GTI in order to recover R&D expenses, as suggested by the AG, and thus there is no contravention of *Union Carbide v PSC*, 431 Mich 135 (1988).

RESPONSE TO CONSUMERS ENERGY

Consumers Energy (Consumers), like ABATE and the AG, has contended that there should not be any “mandatory funding for GTI.” (Consumers brief, p.3) As noted above, GTI has not requested mandatory funding. Consumers appears to be under the impression that GTI’s proposed funding mechanism would somehow limit its discretion in decisions surrounding the funding of R&D. As noted above, GTI does not oppose the application of its criteria to other research and development efforts. Consumers can choose to fund its own R&D and if it meets the established criteria, recover the expenses in a general rate proceeding.

RESPONSE TO MICH CON

GTI agrees with Michigan Consolidated Gas Company (Mich Con) that R&D funding decisions should be made by the Commission separate and apart from other rate case decisions and that the only decision to be made by the Commission about R&D in a general rate case proceeding should be the level of funding. (Mich Con brief, p. 5).

CONCLUSION

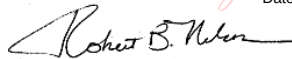
GTI submits that the record in this proceeding demonstrates that voluntary funding of R&D activities, as defined in this reply brief, should be supported by the Commission. To avoid unnecessary litigation in each rate case proceeding, criteria should be established by the Commission in this proceeding that can be used in future rate cases so that the only decision to be made, if the criteria are met, is how much funding should be approved. In this connection, the "cap" on funding proposed by the Staff would be acceptable to GTI.

Respectfully submitted,

FRASER TREBILCOCK DAVIS & DUNLAP, P.C.
Attorneys for Gas Technology Institute

Robert B. Nelson

Digitally signed by Robert B. Nelson
DN: CN = Robert B. Nelson, C = US, O =
Fraser Law Firm
Date: 2006.07.10 14:40:50 -04'00'



Dated: July 10, 2006

By: _____

Robert B. Nelson (P23644)

Business Address:

124 W. Allegan, Ste 1000

Lansing, MI 48933

Telephone: (517) 377-0854

E-mail: rnelson@fraserlawfirm.com

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter, on the Commission's own motion,
to investigate the appropriateness of instituting a
surcharge to assist in the funding of the
Gas Technology Institute

Case No. U-14561
PAPERLESS CASE

CERTIFICATE OF SERVICE

Doreen Bowerman hereby certifies that on the 10th day of July, 2006, she served the
Reply Brief of the Gas Technology Institute in the above docket on the persons identified in
the attached service list by e-mail.

Doreen
Bowerman



Doreen Bowerman

Digitally signed by Doreen
Bowerman
DN: CN = Doreen Bowerman, C =
US, O = Fraser Law Firm
Date: 2006.07.10 14:41:09 -04'00'

U-14561 Service List

Administrative Law Judge

Hon. Mark E. Cummins
Michigan Public Service Commission
6545 Mercantile Way
P.O. Box 30221
Lansing, MI 48911
e-mail: mecummi@michigan.gov

MSPC Staff

Patricia A. Barone
Assistant Attorney General
Public Service Division
6545 Mercantile Way, Ste 15
Lansing, MI 48933
e-mail: baronep@michigan.gov

Consumers Energy Company

John C. Shea
Consumers Energy Company
One Energy Plaza, Room EP11-225
Jackson, MI 49201
e-mail: jcshea@cmsenergy.com

Aquila

Stewart A. Binke
Dykema Gossett PLLC
124 W. Allegan, Ste 800
Lansing, MI 48933
e-mail: sbinke@dykema.com

Citizens Gas Fuel Company

Bruce Maters
Richard P. Middleton
The Detroit Edison Company
2000 Second Avenue, 688 WCB
Detroit, MI 48226
e-mail: matersb@dteenergy.com
middletonr@dteenergy.com
mpscfilings@dteenergy.com

Attorney General

Michael Moody
Assistant Attorney General
Special Litigation Division
525 W. Ottawa, 6th Floor
P.O. Box 30212
Lansing, MI 48909
e-mail: moodyme@michigan.gov

Michigan Consolidated Gas

Bruce Maters
Richard P. Middleton
The Detroit Edison Company
2000 Second Avenue, 688 WCB
Detroit, MI 48226
e-mail: matersb@dteenergy.com
middletonr@dteenergy.com
mpscfilings@dteenergy.com

SEMCO Energy Gas Company

Harvey J. Messing
Sherri A. Wellman
Miller Canfield
One Michigan Avenue, Ste 900
Lansing, MI 48933
e-mail: messing@millercanfield.com
wellmans@millercanfield.com

Wisconsin Public Service Corp

Harvey J. Messing
Sherri A. Wellman
Miller Canfield
One Michigan Avenue, Ste 900
Lansing, MI 48933
e-mail: messing@millercanfield.com
wellmans@millercanfield.com

ABATE

Robert A.W. Strong
Thomas E. Maier
Clark Hill, PLC
255 S. Old Woodward Avenue, 3rd Floor
Birmingham, MI 48009
e-mail: rstrong@clarkhill.com