

STATE OF MICHIGAN
DEPARTMENT OF ATTORNEY GENERAL



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June 8, 2006

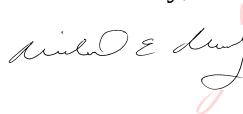
Ms. Mary Jo Kunkle
Executive Secretary
Michigan Public Service Commission
6545 Mercantile Way
Lansing, MI 48911

Dear Ms. Kunkle:

Re: MPSC Case No. U-14701

Enclosed for filing in the above-captioned case please find the **Attorney General's Exceptions to Proposal for Decision**, together with a Proof of Service. This filing is being submitted electronically pursuant to the Commission's Paperless Electronic Filings Program.

Sincerely,

 Michael E. Moody
2006.06.08
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MEM:jas
Enc.
c: All Parties

PROOF OF SERVICE - U-14701

The undersigned certifies that a copy of the **Attorney General's Exceptions to Proposal for Decision** was served upon the parties listed below by mailing the same to them at their respective addresses with first class postage fully prepaid thereon, on the 8th day of June, 2006.

Janet Schafer

Digitally signed by Janet Schafer
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Janet A. Schafer

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STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of
Consumers Energy Company for approval
of a power supply cost recovery plan and
authorization of power supply cost recovery
factors for calendar year 2006.

Case No. U-14701

ATTORNEY GENERAL'S EXCEPTIONS TO PROPOSAL FOR DECISION

I. INTRODUCTION

On May 25, 2006, Administrative Law Judge Mark E. Cummins (ALJ) issued his Proposal for Decision (PFD) in the above captioned case. Pursuant to the schedule provided in the PFD, the Attorney General respectfully submits the following Exceptions to the PFD.

II. STANDARD OF REVIEW

Recently, the Michigan Public Service Commission (MPSC or Commission) summarized the standard of review of an ALJ decision as follows:

[I]n issuing a ruling, an ALJ does not create findings of fact or conclusions of law that bind the Commission. The ALJ's decision is a recommendation, and the Commission is not subject to the constraints imposed by a legal standard of appellate review in deciding whether to accept, reject, or modify the ALJ's assessment of the evidence or legal analysis. See MCL 24.281(3); MSA 3.560(181)(3) ("On appeal from or review of a proposal of decision the agency, except as it may limit the issue upon notice or by rule, shall have all the powers which it would have if it had presided at the hearing.").

In the matter of the complaint of AT&T Communications of Michigan, Inc., MPSC Case No. U-12321 (August 31, 2000), p 13.

In fact, the Commission has held that "it will reverse an administrative law judge's ruling if the Commission finds that a different result is more appropriate." *In the matter of the application of*

the Midland Cogeneration Venture Limited Partnership for approval of capacity charges contained in a power purchase agreement with Consumers Power Company, MPSC Case No. U-8871 (June 28, 1988), p 2.

III. ARGUMENT

A. The ALJ Erred in His Treatment of Futures Contracts/FTRs.

In his PFD, the ALJ found:

[W]ith the change in methodology proposed by the Staff, Consumers' request should be approved. The FTRs in question are directly related to the transmission service provided Consumers by MISO. As such, the Commission's repeated rulings in favor of recovering transmission-related expenses through the PSCR process apply equally to these FTRs. The ALJ therefore recommends that the Commission authorize Consumers to account for FTRs in a manner that ensures that their final, settled value is included as part of the utility's 2006 PSCR costs.

U-14701 PFD, p 22 (footnote omitted).

The ALJ's finding is erroneous because he failed to require Consumers Energy to satisfy its burden of proof regarding this issue; his finding is bad public policy; and his finding is beyond the Commission's statutory authority.

FTRs are derivative instruments that allow Consumers Energy to hedge against future congestion costs on the transmission systems. (5 T 352). As the settlement date approaches, the FTRs value may increase because of the probability of congestion increases or they may lose value because transmission demand declines. (5 T 353). Under current accounting rules, FTR value increases are treated as income and decreases are treated as losses. Neither situation is reflected in the PSCR. Attorney General expert witness Charles King explained that Consumers Energy did not identify the fair value of these FTRs nor has it adequately explained how it will treat FTRs that are allocated or acquired in one calendar year and settled in another calendar year. (5 T 354, 355; AG Initial Brief, p 7). Mr. King noted that the failure of Consumers Energy

to address these concerns in its rebuttal testimony shows that Consumers Energy has not demonstrated the reasonableness and prudence of including these costs in the PSCR. On a more public policy issue but also a reasonableness question is the fact that the more a utility can transfer costs increases into a PSCR (as simply a cost pass through) the more the utility is immune from any risk and the more the utility's incentive decreases to actively attempt to reduce these costs to customers in the PSCR.

The ALJ failed to address either of these issues dealing with the reasonableness or prudence of Consumers Energy's proposal to move these FTRs into the PSCR proceeding, and thus apparently believes that the burden was on the Attorney General to prove their unreasonableness or imprudence. The Commission has held that "the establishment of a prima facie case by [utility's] witnesses does not shift the burden of proof. The burden of proof is a concept that includes two meanings. The burden of persuasion or risk of non-persuasion is placed on [the utility] by Act 304 and does not shift through the course of the proceeding." MPSC Case No. U-8871 (June 28, 1988), p 2. In fact, the Commission has also stated that "[i]t is the duty of the applicant in a PSCR reconciliation proceeding to prove its case and opposing parties are not obligated to introduce any evidence if the applicant's case falls short of the evidentiary standards established in Section 6j(15) of Act 304, . . ." *In the matter of the application of Upper Peninsula Power Company for authority to reconcile its 2000 supply costs and revenues*, MPSC Case No. U-12126-R (April 16, 2002), p 8. Accordingly, the Commission should find that Consumers Energy failed to sustain its burden of showing that moving the FTRs costs into the PSCR proceeding is reasonable and prudent as required under MCL 460.6j(6).

In addition to Consumers Energy's failure to demonstrate the reasonableness and prudence of moving the FTRs costs into the PSCR proceeding is the lack of statutory authority of

the Commission to even permit the moving of the FTR costs into the PSCR proceedings. As argued in the Initial Brief, "the Attorney General believes that the inclusion of transmission costs, let alone the FTR's value increases or decreases, into the PSCR violates MCL 460.6j(1)(a) since it is not a booked cost of fuel burned by the utility for electric generation or the booked costs of purchased and net interchanged power transactions by the utility incurred under reasonable and prudent policies and practices." (AG Initial Brief, p 7). Thus, whether or not the inclusion of these FTR costs in the PSCR proceeding is wise or practical is not a decision that the Commission can consider when carrying out its legislatively circumscribed powers. As a creature of the Legislature, the Commission possesses only that authority bestowed upon it by statute. *Union Carbide Corp v Public Service Commission*, 431 Mich 135, 147 (1988) (citations omitted). As stated by the Michigan Supreme Court, "our Legislature is free to make policy choices that, especially in controversial matters, some observers will inevitably think unwise. This dispute over the wisdom of a law, however, cannot give warrant to a court to overrule the people's Legislature." *Henry v Dow Chemical Co*, __Mich__ (2005), Docket No. 125205, p 42 n 19. Accordingly, the Attorney General requests that the Commission reject the ALJ's recommendation and find that it lacks the statutory authority to include these FTR costs in a PSCR proceeding.

B. The ALJ Erred in Rejecting the Attorney General's Argument Regarding the High-Cost Peaking Facilities.

In the PFD, the ALJ rejects the Attorney General's argument regarding the dispatch of the Karn 1 plant by MISO but failed to address the Attorney General's argument regarding the high-cost peaking facilities (e.g. the Karns 3&4 Gas & Oil and the Peakers). (U-14701 PFD, 24-26; AG Initial Brief, p 10-12). The Attorney General presented expert witness testimony stating that Consumers Energy failed to demonstrate the reasonableness and prudence of dispatching these

high-cost peaking facilities when Consumers Energy could purchase less expensive on-peak power from the market. (AG Initial Brief, p 10). Mr. King presented a table showing the costs/MWH for different facilities and purchased power from the market and explained that the use of these high-cost peaking facilities was imprudent. (AG Initial Brief, p 10; 5 T 356; Exhibit A-12). Noting that this issue is separate from the MISO dispatch issue, Mr. King stated that these high-cost peaking facilities should be "retired and removed from rate base" and that their capacity, when needed, should be replaced by purchased peaking power at a much lower cost. (AG Initial Brief, pp 11-12).

Because Consumers Energy has the burden of proof of demonstrating that the use of the high-cost peaking facilities in its PSCR plan is reasonable and prudent, the ALJ should have recommended that these facilities be retired since Consumers Energy failed to demonstrate the reasonableness and prudence of using these facilities over the less expensive purchased power. Accordingly, the Commission should reject the ALJ's recommendation on this issue and order Consumers Energy to retire these high-cost peaking facilities and save PSCR customers additional and unreasonable costs in using these facilities over cheaper alternatives.

C. The ALJ Erred in Rejecting the Attorney General's Argument Regarding Nuclear Fuel Costs.

In his PFD, the ALJ states:

The ALJ shares the Attorney General's concerns regarding the near-term spike in Consumers' nuclear fuel expense. As noted on Exhibit AG-9, the costs of purchasing and converting uranium are expected to jump 46.3% and 118.2%, respectively, between Batch V and Batch W. Similarly, the costs of enrichment and fuel assembly fabrication are predicted to rise by approximately 20% over the same period, before moderating noticeably for Batches X through Z.

Nevertheless, the record identifies no less-expensive alternatives to Consumers' proposed actions. The ALJ therefore has no recourse but to recommend that the Commission approve recovery of the utility's projected nuclear fuel costs for 2006, albeit with the directive that Consumers provide (in

the reconciliation phase of this case) a more detailed analysis regarding why those costs rose so dramatically with regard to Batch W.

U-14701 PFD, p 34 (emphasis added)

The problem with the ALJ's recommendation is that he fails to require Consumers Energy to identify that there are no less-expensive alternatives to its proposed actions. Consumers Energy has the burden of demonstrating that its proposed actions regarding the costs of enrichment and fuel assembly fabrication are reasonable and prudent. Consumers Energy cannot simply propose a course of action in its PSCR plan application and require the Staff, intervenors, or the Commission to explain why its course of action is unreasonable and imprudent. Similar to the Commission's ruling in the quoted reconciliation case above, it is the duty of the applicant in a PSCR plan proceeding to prove its case and opposing parties are not obligated to introduce any evidence if the applicant's case falls short of the evidentiary standards established in Section 6j(3). *See, In the matter of the application of Upper Peninsula Power Company for authority to reconcile its 2000 supply costs and revenues*, MPSC Case No. U-12126-R (April 16, 2002), p 8. Section 6j(3) requires the utility to evaluate the "reasonableness and prudence of its decisions to provide power supply in the manner described in the plan, in light of the existing sources of electrical generation, and an explanation of the actions taken by the utility to minimize the cost of fuel to the utility."

Because Consumer failed to demonstrate the reasonableness and prudence of its proposed actions regarding the costs of enrichment and fuel assembly fabrication, the Commission should reject the ALJ's finding and disallow the cost increases that have not been demonstrated to be reasonable and prudent.

D. Attorney General's Arguments on Appeal.

In his PFD, the ALJ notes"

[T]he Attorney General listed five issues, each involving matters in which the Commission ruled against him during Consumers' prior PSCR plan case. Because these issues were raised solely to "preserve them for appellate purposes" while appeals in Case No. U-14274 are pending, they have not been specifically addressed in the present case.

U-14701 PFD, p 10, n 8.

As stated by the ALJ, the Attorney General raises the following legal arguments in order to preserve them for appellate purposes:

1. The Attorney General takes the position that transmission expenses resulting from the sale of Consumers Energy's transmission system should not be incorporated in the expenses for Consumers Energy's PSCR plan and 5-year forecast because transmission expenses fall outside the scope of MCL 460.6j(1) and are partially included in Consumers Energy's MPSC-approved base rates. The Attorney General is aware that the MPSC has rejected this position in Case No. U-14274, but the Attorney General presents this issue to indicate that he is not waiving this objection while appeals concerning U-14274 are pending.
2. The Attorney General takes the position that Consumers Energy's transmission expenses are caused by and directly related to the level of peak demand, and therefore, it would not be just and reasonable to allocate those expenses to customers on an energy-consumed basis via PSCR factors. The Attorney General is aware that the MPSC has rejected this position in Case No. U-14274, but the Attorney General presents this issue to indicate that he is not waiving this objection while appeals concerning U-14274 are pending.
3. The Attorney General takes the position that the MPSC would violate MCL 460.6j(1) if the MPSC permits Consumers Energy to recover the cost of NO_x or similar allowances via Consumers Energy's PSCR factors. The Attorney General is aware that the MPSC has rejected this position in Case No. U-14274, but the Attorney General presents this issue to indicate that he is not waiving this objection while appeals concerning U-14274 are pending.
4. The Attorney General takes the position that the MPSC would violate MCL 460.10d(2) if the MPSC authorizes deferral and future recovery of any PSCR expenses not recovered because of the rate cap imposed by that statute. The Attorney General is aware that the MPSC has rejected this position in Case No. U-14274, but the Attorney General presents this issue to indicate that he is not waiving this objection while appeals concerning U-14274 are pending.
5. The Attorney General takes the position that the MPSC would violate MCL 460.10d(2) if for any reason the MPSC authorizes Consumers Energy to

charge residential customers a PSCR factor during 2006 in excess of the PSCR factor set in Case No. U-14274.

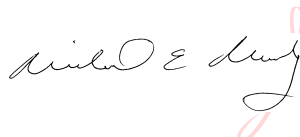
Because the Commission has rejected these arguments in prior cases and because those cases have been appealed by the Attorney General to the Court of Appeals, the Attorney General simply raises these arguments for purposes of preserving them following resolution of Court of Appeals cases.

IV. CONCLUSION

For the reasons stated above, the Attorney General respectfully requests that the Commission reject, in part, the ALJ's recommendations on the above issues and adopt the Attorney General's arguments in this case regarding those issues.

Respectfully submitted,

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