

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of )  
**PENINSULAR GAS COMPANY** for )  
reconciliation of environmental assessment )  
and remediation costs with amounts recovered )  
from customers through surcharge. )  
\_\_\_\_\_ )

Case No. U-10630-R

At the June 2, 1998 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. John G. Strand, Chairman  
Hon. John C. Shea, Commissioner  
Hon. David A. Svanda, Commissioner

**OPINION AND ORDER**

In Case No. U-10630, Peninsular Gas Company (Peninsular) sought approval of a surcharge to recover the estimated costs associated with the assessment and remediation of environmental contamination emanating from a manufactured gas plant that had operated on a site owned by Peninsular. The Commission's April 13, 1995 order in Case No. U-10630 authorized Peninsular to implement a surcharge for a period of 24 months in an amount estimated to be sufficient to recover 50% of the projected costs associated with the environmental assessment and remedial investigation. Determinations concerning additional recovery of costs associated with this environmental contamination would await a general rate case, which the Commission ordered Peninsular to file. The Commission's order also required that, at the conclusion of the 24-month surcharge period,

Peninsular was to file a reconciliation case during which the reasonableness and prudence of its expenditures would be examined.

On June 30, 1997, Peninsular Gas Company (Peninsular) filed an application seeking reconciliation of costs associated with environmental assessment and remediation with revenues collected pursuant to the environmental surcharge authorized by the April 13, 1995 order. On July 31, 1997, the Commission issued the final order in Case No. U-11127, the general rate case filed pursuant to the requirements of the April 13, 1995 order. In the July 31, 1997 order, the Commission concluded that Peninsular should be allowed the option to employ a surcharge to recover 75% of the reasonable and prudent costs of assessment and remediation of the environmental contamination.<sup>1</sup> On August 21, 1997, Peninsular amended its application in this case to reflect the cost allocation provided as part of the surcharge option offered by the July 31, 1997 order.

Pursuant to due notice, a prehearing conference was held on August 22, 1997 before Administrative Law Judge George Schankler (ALJ). At that time, the ALJ granted the petition to intervene filed by the Township of Calumet (Calumet). The Commission Staff (Staff) also participated.

An evidentiary hearing was held on January 21, 1998. The record consists of 74 pages of transcript and 19 exhibits.

The Staff proposed certain modifications to Peninsular's proposed cost recovery and recommended that the Commission require Peninsular to file annual reports detailing its environmental clean-up expenditures and interest expense, surcharge revenues, and any significant changes in

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<sup>1</sup>The other option was to recover these costs in the same manner that all other Michigan utilities have recovered costs associated with environmental assessment and remediation of contamination from manufactured gas plant sites. That method provides for the deferral and amortization of the costs. Costs are not included in rates until the Commission has reviewed their reasonableness and prudence.

Peninsular's remediation efforts during the period. In addition, the Staff recommended that the Commission require Peninsular to inform the Staff of any significant company decisions or changes to national or state environmental policy that might affect expense levels, milestones, or events in the remediation project. Finally, the Staff recommended that the Commission should instruct Peninsular to maintain an adequate internal review process for paying invoices related to the remediation project. Peninsular agreed to all of the Staff's proposed adjustments and other recommendations.

Calumet took the position that the Commission had established in Case No. U-10630 that Peninsular was to absorb 50% of the costs associated with the assessment and remedial investigation of the environmental contamination. It argued that the Commission's July 31, 1997 order did not entitle Peninsular to increase its recovery to 75% of those costs. Further, Calumet contended that Peninsular should not be allowed to recover through the surcharge legal and consulting costs incurred in litigating Case No. U-10630 and Case No. U-11127.

The parties filed briefs and reply briefs on February 11 and 28, 1998, respectively. On March 27, 1998, the ALJ issued his Proposal for Decision (PFD) in which he rejected Calumet's arguments and concluded that Peninsular should be allowed to recover 75% of the costs associated with the environmental assessment and remediation, including certain legal fees.<sup>2</sup>

On April 10, 1998, Calumet filed exceptions. On April 17, 1998, Peninsular filed replies to exceptions.

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<sup>2</sup>The Staff had objected to the inclusion of \$5,606 in legal fees associated with Peninsular's filing of Case No. U-11088, a general rate case, because the case was later dismissed for failure to comply with the Commission's order in Case No. U-10630 and because rate case expenses are already included in base rates, which were set in Case No. U-11127. As noted, Peninsular agreed with the Staff's proposed adjustments. Peninsular represents that no legal fees associated with Case No. U-11127 are included in this reconciliation.

## Cost Apportionment

In its first two exceptions, Calumet argues that the Commission should reverse the ALJ's determination that Peninsular is entitled to recover 75% of the costs at issue in this case. Calumet argues that the ALJ's determination is based on a misinterpretation of the Commission's orders in Case No. U-10630 and Case No. U-11127 and violates the prohibition against retroactive ratemaking.

Calumet argues that the Commission's order in Case No. U-10630 made a distinction between costs associated with the environmental assessment and remedial investigation and costs associated with cleaning up the contaminated site. Calumet further argues that the order expressly allocated responsibility for the assessment and remedial investigation costs equally between Peninsular's shareholder and its ratepayers. That finding, Calumet insists, was not altered by the Commission's July 31, 1997 order. To support its argument, Calumet points to the language in the ordering section of that order that permitted Peninsular to implement a surcharge for "service rendered no earlier than the date of this order." *Id.* p. 35. Because Peninsular incurred the costs at issue here prior to July 31, 1997, Calumet insists that those costs cannot be subject to the provisions of the order in Case No. U-11127.

Calumet further contends that increasing ratepayers' share of these costs would violate the prohibitions against retroactive ratemaking. According to Calumet's analysis, the April 13, 1995 order in Case No. U-10630 provided for 50% recovery of costs incurred prior to the conclusion of a general rate case. Because Case No. U-10630 was not a rate case, for which partial and immediate relief may be granted, Calumet argues, increasing Peninsular's rate of recovery would retroactively alter rates for the time period at issue in this case.

Peninsular responds that the ALJ properly found that the Commission's April 13, 1995 order in Case No. U-10630 was intended to provide Peninsular with interim relief, as reflected in the position the Commission took before the Michigan Court of Appeals to defend that order. Peninsular argues that, in Case No. U-10630, the Commission fashioned a temporary remedy because of its reluctance to authorize full recovery through a surcharge before completion of a general rate case. It further argues that the Court of Appeals held that there had been no final disallowance of these costs in Case No. U-10630, finding in part: "Any errors in the allocation may be corrected in the general rate case." Peninsular Gas Company v PSC, Docket No. 185681, unpublished Court of Appeals decision issued October 29, 1996.

Peninsular argues that Calumet misreads the portion of the Commission's July 31, 1997 order in Case No. U-11127 in which the Commission stated:

If Peninsular Gas Company chooses the surcharge method, it shall, for service rendered no earlier than the date of this order, implement surcharges listed on Exhibit B attached to this order to recover 75% of the reasonable and prudent costs associated with the assessment and remediation of the environmental contamination at the [manufactured gas plant site]. Id. p. 38.

Peninsular argues that the phrase "for service rendered no earlier than the date of this order" modifies the verb "shall implement" rather than the phrase "to recover 75% of the reasonable and prudent costs." Thus, Peninsular asserts, the quoted portion of the order permits the surcharge to commence for service rendered after the date of the order and permits the surcharge to recover 75% of the environmental costs, without reference to the date those costs were incurred.

Moreover, Peninsular argues, altering the recovery percentage did not violate the prohibition against retroactive ratemaking. In Peninsular's view, the ALJ correctly found that implementation of a temporary measure with an explicit reservation of final judgment is not retroactive ratemaking.

The Commission's later decision to apply a different allocation of costs did not alter in any way the surcharge authorized by the April 13, 1995 order in Case No. U-10630.

Finally, Peninsular argues that recovery of previously deferred costs does not constitute retroactive ratemaking, citing Detroit Edison v PSC, 221 Mich App 370, 374-376; 462 NW2d 224 (1997). Therefore, Peninsular argues, Calumet's citations to cases in which the respective courts held retroactive ratemaking to be unlawful are inapposite.

The Commission finds that Calumet's first exception should be rejected. Calumet's arguments are based on its assumption that the Commission's April 13, 1995 order in Case No. U-10630 was a final determination of the allocation of these costs between ratepayers and the shareholder. It was not. The order explicitly states that the surcharge approved by the Commission is an interim measure, and all of the provisions of that order should be read in that light. The interim quality of that order was expressly recognized by the Michigan Court of Appeals in its decision affirming the Commission's April 13, 1995 order. Peninsular Gas Co, supra.

Despite the Commission's reluctance to authorize a single issue rate increase, the record in Case No. U-10630 reflected that Peninsular would have difficulty meeting its obligation to pursue cleaning up the contamination without obtaining some immediate relief. In an attempt to ameliorate the situation, the Commission granted partial, interim relief subject to a later reconciliation, but determined that any additional recovery of these costs should await completion of a general rate case.

At the conclusion of the rate case ordered in Case No. U-10630, the Commission found that it would be appropriate to allow Peninsular the option to recover its environmental assessment and remediation costs through a surcharge rather than the manner in which all other utilities recover like costs, if the company agreed to absorb a portion. Therefore, the Commission permitted Peninsular

to implement the same surcharge as authorized in Case No. U-10630 to recover 75% of the reasonable and prudent environmental costs. Peninsular's agreement to absorb 25% of these costs was a prerequisite to its ability to obtain substantial financing from its customers, which would shorten or eliminate any delay in cost recovery and thereby assist the company to obtain needed capital for the project. The Commission intended that Peninsular be allowed to recover 75% of all its reasonable and prudent environmental expenses, including those for the assessment and remedial investigation of the contamination.

The Commission also rejects Calumet's second exception, which charges that allowing Peninsular to recover 75% of the environmental costs for the period encompassed by the initial surcharge violates the prohibition against retroactive ratemaking. The Commission's April 13, 1995 order in Case No. U-10630 authorized Peninsular to implement a surcharge that was calculated to recover 50% of the projected costs. At that time, no one knew what the actual costs or the ultimate method of recovery would be. The amount of the authorized surcharge does not change as a result of the Commission's decision today. Nor has Peninsular requested to rebill customers for service rendered during the surcharge period.

Further, the Commission rejects Calumet's argument that these costs are "past costs" that may not be recovered through rates without violating principles of retroactive ratemaking. Pursuant to the Commission's order in Case No. U-10484, Peninsular was authorized to defer its environmental costs prior to recovery from ratepayers. Recovery of previously deferred costs does not change the rates charged by a utility for its service in violation of the retroactive ratemaking prohibition.

Detroit Edison v PSC, 221 Mich App 370, 374-376; 462 NW2d 224 (1997).

Finally, the language from the July 31, 1997 order in Case No. U-11127 that limited the authorized surcharge to "service rendered no earlier than the date of this order" merely expressed

the prospective nature of the surcharge authorized by that order. The phrase was not intended to, and did not, limit the recoverable environmental costs to those incurred after July 31, 1997.

### Recoverable Costs

Calumet argued that all legal and consulting costs associated with Case No. U-10630 (through the appellate level) and Case No. U-11127 should be excluded from recovery through the surcharge. In Calumet's view, these costs are more properly reviewed and recovered through a general rate case.

The Staff's proposal excluded legal fees related to Case No. U-11127 because Peninsular's base rates already include an amount for legal fees for the general rate case. However, the Staff took the position that the consulting fees and the legal fees for Case No. U-10630 could be legitimately recovered through the surcharge.

Although Peninsular agreed to the Staff's adjustments, it argued that the remaining legal and consulting fees are a part of the assessment and remediation of the environmental contamination and are properly recovered through the surcharge. Peninsular also pointed out that although these costs were identified in the general rate case, they were not included in base rates.

The ALJ found that the legal and consulting fees requested by Calumet, as adjusted by the Staff, should be authorized for recovery through the surcharge approved in Case No. U-10630. He found that the costs bear a sufficient relationship to the assessment and remediation costs to be recovered through the surcharge. Moreover, he noted that because Peninsular opted to absorb 25% of these costs, the company has an incentive to minimize them. He further found that if the Commission requires Peninsular to recover these costs through base rates, the company will incur additional costs to file another rate case.

Calumet excepts and argues that the ALJ's analysis is flawed. In Calumet's view, the company did not present a budget for these items with a rationale supporting their inclusion in the surcharge in Case No. U-10630, and they bear no relationship to costs that were authorized for recovery in the Commission's April 13, 1995 order in that case. Calumet maintains that the Commission's authorization to recover "costs associated with the assessment and remedial investigation" cannot be stretched to include legal and consulting fees in proceedings before the Commission.

Peninsular responds that the ALJ correctly concluded that the legal and consulting costs are recoverable through the surcharge. It asserts that these fees all relate to the company's attempts to procure a revenue stream that would allow it to perform the assessment and remediation activities required by the Michigan Department of Environmental Quality. Costs incurred to obtain the funds to complete the project are necessarily a part of the cost of the project. Peninsular asserts that these costs have not been included in base rates, because the company included them in the separate accounting for environmental costs to be recovered through the surcharge.

The Commission finds that the legal and consulting fees, as adjusted by the Staff, are properly included in the costs recoverable through the surcharge authorized in Case No. U-10630. Calumet takes too narrow a view of what may be associated with the assessment and remedial investigation of the contamination. Costs to obtain funding may legitimately be considered a part of the project. Thus, these costs are recoverable through the surcharge as long as the charges are reasonably and prudently incurred. There is no suggestion that Peninsular was unreasonable or imprudent in its procurement of the consulting or legal services to which these costs relate.

The Commission FINDS that:

- a. Jurisdiction is pursuant to 1909 PA 300, as amended, MCL 462.2 et seq.; MSA 22.21 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; MSA 22.1 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; MSA 22.13(1) et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; MSA 3.560(101) et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACRS, R 460.17101 et seq.
- b. Peninsular's proposed reconciliation of revenues recorded pursuant to the environmental surcharge authorized in Case No. U-10630 and costs associated with its environmental assessment and remedial investigation, as modified by the Staff, should be approved.
- c. The Staff's proposals concerning reporting and accounting procedures, to which Peninsular agreed, should be adopted.

THEREFORE, IT IS ORDERED that:

- A. Peninsular Gas Company's proposed reconciliation of revenues recorded pursuant to the environmental surcharge authorized in Case No. U-10630 and costs associated with its environmental assessment and remedial investigation, as modified by the Commission Staff, is approved.
- B. The Commission Staff's proposals concerning reporting and accounting requirements, to which Peninsular Gas Company agreed, are adopted.

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; MSA 22.45.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ John G. Strand

Chairman

( S E A L )

/s/ John C. Shea

Commissioner

/s/ David A. Svanda

Commissioner

By its action of June 2, 1998.

/s/ Dorothy Wideman

Its Executive Secretary

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MICHIGAN PUBLIC SERVICE COMMISSION

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Case No. U-10630-R

Suggested Minute:

“Adopt and issue order dated June 2, 1998 reconciling the revenues received through the surcharge approved for Peninsular Gas Company in Case No. U-10630 with the recoverable environmental assessment and remediation costs, as set forth in the order.”