

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
MICHIGAN CONSOLIDATED GAS COMPANY)
for approval of an experimental pilot program for)
expanded gas customer choice, including an expanded)
gas transportation program, a transportation aggregation)
tariff, an earnings sharing mechanism, a suspension)
of its gas cost recovery clause, a moratorium on)
non-GCR rate adjustments, and related relief.)
_____)

Case No. U-11682

At the April 28, 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

ORDER APPROVING APPLICATION

On April 21, 1998, Michigan Consolidated Gas Company (Mich Con) filed an application for approval of a voluntary experimental pilot program intended to enhance customer choice. Mich Con's proposed program, referred to in the application as Mich Con Select, would expand its current gas transportation program, adopt transportation standards of conduct, suspend its gas cost recovery (GCR) clause, freeze its gas commodity charge at \$2.95 per thousand cubic feet (Mcf), freeze its distribution service rates at current levels, establish a revenue sharing mechanism, and implement a transportation aggregation tariff.

Mich Con states that the proposed program will provide more complete and comprehensive information concerning customer choice than the pilot transportation program approved in Case No. U-11273 and contained in Mich Con's existing Rate PTS. As proposed, the Mich Con Select program would supersede the Case No. U-11273 pilot program and would be effective for the three-year period beginning April 1, 1999.

Mich Con states that under the Mich Con Select program (i) up to 225,000 customers from throughout Mich Con's service territory will be able to choose their gas supplier, (ii) competing gas marketers and brokers will be allowed to market natural gas to a large number of retail customers in direct competition with Mich Con, and (iii) competing suppliers will be allowed to independently determine the interstate pipeline capacity necessary to deliver gas to Mich Con's system and obtain that capacity from any source and in any manner they deem appropriate.

Mich Con states that participation will be strictly voluntary and that participating customers will be selected on a first-come, first-served basis, up to a maximum of 75,000 customers for the enrollment period occurring during early 1999, 150,000 customers for the enrollment period occurring during early 2000, and 225,000 customers for the enrollment period occurring during early 2001. Nonresidential customer participation is limited to 10 billion cubic feet (Bcf) in the initial year, 20 Bcf in the second year, and 30 Bcf in the third year. Mich Con states that rates for transportation service under Mich Con Select tariff Rate EPTS will be the same as those approved in Case No. U-11273.

As a part of its tariff, Mich Con proposes including transportation standards of conduct that it states are intended to promote fair competition and a level playing field among all customers and gas suppliers involved in transportation within Mich Con's service territory. Mich Con states that it will conduct its business in conformance with the proposed standards and agrees to establish a

complaint procedure that gives marketers and brokers a forum to address any complaints related to those standards.

Mich Con further states that it will continue offering a fully bundled service to all customers who desire such service. It states that to protect customers (nonparticipants as well as participants) from distribution service cost increases or cost shifts during the term of the program, and to maximize the incentive for Mich Con to control its costs and make efficient business decisions, the company will, with two exceptions, freeze its distribution service rates for all retail gas customers. Mich Con therefore requests that, during the term of the program, the Commission (i) suspend Mich Con's GCR clause, (ii) establish a gas commodity charge at \$2.95 per Mcf for customers who remain full service customers or return to Mich Con as full service customers, and (iii) freeze distribution rates at currently authorized levels. In conjunction with this proposal, Mich Con contends that its fixed and automatic gas purchase program and its 90/10 and McLouth Steel revenue sharing mechanisms should be suspended.

Under Mich Con's proposal, the January 1998 through December 1998 GCR period would be subject to reconciliation in the normal fashion. However, to dispose of any 1998 GCR over- or undercollections in a timely manner, Mich Con proposes implementing a 1998 GCR surcharge rate. No GCR plan or reconciliation would be conducted for the period January 1, 1999 through December 31, 2001.

The distribution rate freeze proposed by Mich Con is subject to two exceptions. They are that (i) Mich Con agrees to credit customers' bills pursuant to an income sharing mechanism if earnings exceed certain levels, and (ii) Mich Con or other interested parties may seek a limited issue rate case to adjust rates to reflect the effect of legislative action or new authoritative accounting pronouncements promulgated by the Financial Accounting Standards Board or the Securities and

Exchange Commission that affect Mich Con's annual revenue requirement by more than \$5 million.

Under the utility's income sharing proposal, if Mich Con's return on equity for its natural gas utility business (currently authorized at 11.5%) exceeds 13.50%, amounts equal to 50% of the earnings between 13.51% and 17.50%, plus amounts equal to 75% of the shareable earnings over 17.50%, would be refunded to customers. The methodology for determining the amount subject to refund is described in Mich Con's application.

Mich Con goes on to state that it will gather information to determine performance measurements that reflect the importance of maintaining quality customer service, reliability, and safety. These performance measurements would be used to adjust the sharing threshold percentage under the income sharing mechanism. Mich Con states that, within six months of Commission approval of those proposals, Mich Con will file an application requesting implementation of specific performance criteria to be used in conjunction with the proposed income sharing mechanism.

Mich Con states that further expansion of customer choice will occur through the implementation of a new transportation aggregation tariff. Subject to certain conditions, the new tariff will allow customers receiving gas service at multiple, noncontiguous facilities under the common ownership of a customer to aggregate the quantities of gas supplied to such facilities for purposes of nomination and storage. Mich Con states that it will make the new transportation aggregation tariff available immediately upon Commission approval.

Mich Con states that its proposed experimental customer choice program will provide substantial information and experience concerning (i) the degree to which retail gas customers desire the opportunity to select alternative gas suppliers, (ii) the various ways customers respond to having gas supply choices, (iii) the extent and nature of alternative gas supply and pricing options made

available to customers by alternative suppliers, (iv) the means by which alternative gas suppliers obtain the gas supplies and interstate transportation necessary to satisfy customer demands in a competitive environment, as well as the reliability of those means, (v) the extent to which incentive-based regulation is an appropriate long-term substitute for rate of return regulation of local distribution companies, and (vi) the continued need for mechanisms like those provided by 1982 PA 304 (Act 304), MCL 460.6h et seq.; MSA 22.13(6h) et seq., in an environment where customers have the ability to purchase gas from multiple suppliers.

On April 27, 1998, the Residential Ratepayer Consortium filed a response and petition for leave to intervene.

Discussion

The Commission has been active in investigating and promoting ways to introduce more competition into the industries it regulates. Mich Con's proposed experimental customer choice program provides a valuable opportunity to gain information regarding whether and how gas transportation service should be extended to all customers.

The proposed Mich Con Select program is larger and more comprehensive than the pilot program approved in Case No. U-11273. Specifically, although that pilot program provided opportunities for up to 50,000 sales customers in a limited geographic area to choose an alternative gas supplier, the Mich Con Select program will provide up to 225,000 sales customers (approximately 20% of Mich Con's sales customers) located throughout Mich Con's service territory the opportunity to purchase gas from other suppliers. Thus, the Mich Con Select program will likely serve as a better source of information than the pilot program approved in Case No. U-11273.

Mich Con proposes to establish transportation standards of conduct that will ensure fair competition between gas suppliers and Mich Con's affiliated gas supplier. This proposal also establishes definitive steps that gas suppliers can take to report alleged inconsistencies with the standards of conduct. Mich Con indicates that it will implement these new standards of conduct upon Commission approval.

The proposed program would freeze existing noncommodity rates and the gas commodity charge for three years. A fixed distribution rate and gas commodity charge would insulate customers from potential cost increases that, under traditional regulation, would be recoverable through increased rates. Moreover, the Commission has previously approved several suspensions of power supply cost recovery clauses and at least one suspension of a GCR clause. See the Commission's September 21 and December 20, 1995 orders in Case No. U-10923, its December 15, 1995 order in Case No. U-10994, its September 12, 1996 order in Case No. U-11166, and its December 19, 1997 Order in Case No. U-11599. The relevant provisions of Act 304 are the same for both electric and gas service.

During the three-year program, there is no mechanism in Mich Con's proposal to increase charges for system supply gas even if gas commodity prices increase. However, there are two exceptions to the freeze on noncommodity rates: one is the potential implementation of the income sharing mechanism, and the other is rate revisions arising in response to unanticipated legislative or accounting actions. The income sharing mechanism provides for a portion of earnings to be returned to customers if earnings on common equity exceed certain levels. Mich Con states that it would credit customers' bills for the customers' allocable share of the excess. No rate increases can result from the operation of this mechanism even if Mich Con's gas utility business earned return on equity falls below its authorized level. The amount to be credited to customers' bills will

be determined in accordance with the specified formula set forth in Mich Con's application. These potential credits will benefit customers. Moreover, this type of sharing mechanism was approved by the Commission in its December 19, 1991 order in Case No. U-10037, and its legality was affirmed by the Court of Appeals in Attorney General v Public Service Comm, 206 Mich App 290; 520 NW2d 636 (1994).

Mich Con also proposes to file exhibits similar to those contained in Attachment D to its application, along with any necessary work papers supporting its calculation, not later than March 31, 2000, 2001, and 2002, identifying the amount, if any, to be credited to customers under the sharing mechanism. It proposes that parties be given 30 days to request a hearing regarding the calculations and that the scope of any hearing be limited to the filing's accuracy and conformance to Attachment D. It further proposes that, if no hearing is requested, it be allowed to promptly implement any applicable credit.

The second exception to the noncommodity rate freeze addresses unanticipated legislative action or new authoritative accounting pronouncements promulgated by the Financial Accounting Standards Board or the Securities and Exchange Commission that affect Mich Con's annual revenue requirement by more than \$5 million. If such changes occur, Mich Con or other interested persons would have a right to seek a limited issue rate case to adjust rates to reflect the effect of such changes. This provision does not establish that a change will occur. Rather it gives parties a right to seek such a change, if necessary. Any change would be subject to all applicable procedural and statutory requirements, including any applicable requirements for notice and opportunity for hearing.

Furthermore, Mich Con's proposed transportation aggregation service would make gas transportation services available to a broader range of customers, thus providing expanded and more flexible gas supply choices to customers within Mich Con's service territory.

After a review of the application, the Commission finds that Mich Con's proposals are reasonable and in the public interest, and should be approved. This finding reflects the Commission's belief that experimentation with alternative, more flexible regulatory mechanisms is appropriate in view of the changing nature of the natural gas utility industry. Further, the Commission is persuaded that approval of the proposed experimental program is appropriate because, among other things, it provides incentives to the utility to operate in an efficient manner and should enhance the utility's ability to respond to market demands. Mich Con's experimental program should also provide valuable information to assist the Commission in future decisions that may address whether it is in the public interest to permanently extend or approve transportation tariffs for small commercial and residential customers. This information should quantify customer benefits or disadvantages associated with customers' choosing to participate in the Mich Con Select program. Finally, implementation of the Mich Con Select program should coincide with the termination of Mich Con's current transportation pilot program.

Approval of Mich Con's application will not increase the rates and charges of any customer. Therefore, the Commission may approve the experimental program without providing notice or an opportunity for a hearing, pursuant to MCL 460.6a; MSA 22.13(6a).

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.; 1982 PA 304, as amended, MCL 460.6h et seq.; MSA 22.13(6h) 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. Mich Con's application for authority to implement an expanded experimental pilot program for increased customer choice, including an expanded gas transportation program, adoption of transportation standards of conduct, suspension of its GCR clause, a moratorium on gas commodity and nongas commodity rate adjustments, a revenue sharing mechanism, and a transportation aggregation tariff, should be approved.

c. Adoption of the Mich Con Select program, as reflected in the tariff sheets and the standard authorized gas supplier contract attached to this order as Attachments A and B, respectively, is reasonable and in the public interest, and should be approved.

d. Suspension of the GCR clause for a three-year period beginning January 1, 1999 and establishment of a gas commodity charge of \$2.95 per Mcf is reasonable and in the public interest, and should be approved. Mich Con should not be required to file a GCR plan or reconciliation case for any of the three years beginning January 1999, January 2000, and January 2001. The gas commodity charge of \$2.95 per Mcf should not be subject to reconciliation with actual gas costs during the three-year experimental program.

e. Mich Con should be required to file, according to the normal schedule, a GCR reconciliation proceeding for the year January through December 1998, including the implementation of its 1998 GCR surcharge rate to account for any GCR over- or undercollections during 1998.

f. Adoption of a fixed gas commodity rate in 1999 supports the elimination of Mich Con's fixed and automatic gas purchase program for all volumes to be purchased in January 1999 and

subsequent months. Adoption of an income sharing mechanism supports the elimination of Mich Con's 90/10 and McLouth Steel refund mechanisms.

g. Approval of a moratorium on noncommodity rate adjustments, subject to the sharing mechanism and the exception for significant changes in noncommodity costs, as more fully described in the order, is reasonable and in the public interest.

h. The proposed experimental pilot program for expanded gas customer choice is reasonable and in the public interest, and is consistent with the policy of the Commission and the State of Michigan to promote competition and customer choice in the gas utility industry.

i. Adoption of the transportation aggregation tariff, the transportation standards of conduct, and the complaint procedures proposed by Mich Con, as also reflected in the tariff sheets attached to this order as Attachment A, are reasonable and in the public interest.

j. The relief granted will not increase the rates of any customer.

THEREFORE, IT IS ORDERED that:

A. Michigan Consolidated Gas Company is authorized to implement the experimental program described in its April 21, 1998 application.

B. Rate Schedule EPTS shall take effect April 1, 1999, at which time service will no longer be available under the existing pilot program.

C. Michigan Consolidated Gas Company shall, with respect to the regulated portion of its gas business, adhere to the transportation standards of conduct and related complaint procedures as set forth in the tariff sheets attached as Attachment A to this order. Michigan Consolidated Gas Company shall file within 10 days tariff sheets incorporating the standards of conduct and associated complaint procedures.

D. Michigan Consolidated Gas Company's gas cost recovery clause is suspended effective January 1, 1999 for a three-year period, during which the gas commodity cost shall be established at a fixed rate of \$2.95 per thousand cubic feet. Michigan Consolidated Gas Company shall file all tariff and rule changes arising from the suspension of the gas cost recovery clause and the establishment of a fixed gas commodity charge, all of which are currently contained in Attachment A, no later than December 1, 1998. A reconciliation proceeding shall be conducted for the plan year ending December 31, 1998, and Michigan Consolidated Gas Company shall file the 1998 gas cost recovery reconciliation according to the normal schedule, including any surcharge rate necessary to minimize any over- or undercollection of 1998 gas cost recovery costs.

E. Michigan Consolidated Gas Company shall file tariff sheets consistent with this order no later than December 1, 1998.

F. A three-year moratorium on noncommodity rate adjustments is approved, subject to the sharing mechanism proposed in the application and the exception for significant changes in noncommodity costs.

G. Within six months following the issuance of this order, Michigan Consolidated Gas Company shall file an application for implementation of performance criteria to be used in conjunction with the income sharing mechanism approved in this order.

H. Michigan Consolidated Gas Company shall file within 10 days tariff sheets incorporating the noncontiguous transportation aggregation tariff approved in this order.

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 April 28, 1998.

/s/ Dorothy Wideman
Its Executive Secretary

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Suggested Minute:

“Adopt and issue order dated April 28, 1998 authorizing Michigan Consolidated Gas Company to implement an experimental program for expanded customer choice, establish a transportation aggregation mechanism, adopt transportation standards of conduct, suspend its gas cost recovery clause, institute a moratorium on non-gas cost rate adjustments, and establish a revenue sharing mechanism, as set forth in the order.”