

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
MICHIGAN CONSOLIDATED GAS COMPANY)
for a gas cost recovery reconciliation proceeding)
for the 12-month period ended December 31, 1998.)
_____)

Case No. U-11455-R

At the July 6, 2000 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. John G. Strand, Chairman
Hon. David A. Svanda, Commissioner
Hon. Robert B. Nelson, Commissioner

OPINION AND ORDER

I.

HISTORY OF PROCEEDINGS

On February 26, 1999, Michigan Consolidated Gas Company (Mich Con) filed an application seeking a reconciliation of its gas cost recovery (GCR) revenues and expenses for the 12-month period ended December 31, 1998, and a determination concerning the appropriate refund required pursuant to the company's 90/10 refund mechanism. According to the application, Mich Con's 1998 GCR revenues exceeded its recoverable gas supply costs by \$18 million, including interest through December 31, 1998.

Pursuant to due notice, a prehearing conference was conducted on April 1, 1999 before Administrative Law Judge Daniel E. Nickerson, Jr., (ALJ). At that time, the ALJ granted

intervention to Attorney General Jennifer M. Granholm (Attorney General), the Association of Businesses Advocating Tariff Equity (ABATE), and the Residential Ratepayer Consortium (RRC). The Commission Staff (Staff) also participated in this case.

Evidentiary hearings were held on September 21 and 24, 1999. The record consists of 384 pages of transcript and 46 exhibits that were admitted into evidence.

On October 15, 1999, Mich Con, the Staff, the Attorney General, the RRC, and ABATE filed briefs. By November 5, 1999, reply briefs had been filed by all parties except ABATE.

On January 21, 2000, the ALJ issued his Proposal for Decision (PFD) in which he recommended that the Commission approve Mich Con's proposed accounting treatment of its gas parking service and exchange gas, adopt the Staff's recommendations to reduce GCR costs by \$14,698 for compression payments made after the contracts terminated in 1998 and \$178,509 to reflect the actual rather than the estimated annual average cost of exchange gas, reduce the cost of gas by \$46,263 to exclude the transfer of the Norwich Pipeline in partial satisfaction of a gas contract buyout, and find that Mich Con's decisions regarding its gas storage injections in May and July of 1998 were reasonable and prudent.

On February 18, 2000, Mich Con, the Staff, the Attorney General, and the RRC filed exceptions to the PFD. On March 10, 2000, Mich Con, the Staff, and the Attorney General filed replies to exceptions.

Uncontested Cost of Gas Adjustments

The Staff proposed adjustments to the cost of gas to exclude \$14,698 for compression payments made after the contracts expired and \$201,262 to reflect a preliminary-to-final cost

adjustment.¹ These adjustments were not contested by the parties and are supported by the record. The Commission therefore, adopts these proposed adjustments.

Asset Transfer

The Staff recommended a \$46,263 reduction in the cost of gas to exclude the transfer of the Norwich Pipeline to Samson Hydrocarbons. The Staff asserted that plant asset transfers do not qualify as a booked cost of gas under Mich Con's GCR clause, Rule B-46.00. The Staff took the position that Mich Con could have structured the agreement with its supplier in a manner that might have allowed cost recovery in this GCR case. However, Mich Con's failure to do so should not be disregarded.

In response, Mich Con explained that it transferred the pipeline to its supplier as part of a deal to reduce Mich Con's obligation to purchase gas at above-market prices. It asserted that the asset was transferred at book value in lieu of paying additional cash to the supplier, which the supplier would then have returned to Mich Con to purchase the pipeline. Mich Con argued that the Staff's position unreasonably looked only to the form of the transaction rather than recognizing its substance.

The ALJ agreed with the Staff that the transfer of plant assets is not a recoverable cost of gas sold and that nothing in Rule B-46.00 permits cost recovery in this case. He found that although Mich Con may recover the cost of this transfer, it must do so outside of the GCR process. The ALJ concluded that expecting Mich Con to be aware of and follow the dictates of its Rule B-46.00 does not impermissibly elevate form over substance.

¹The latter adjustment reflects an adjustment for 1998 costs that were booked in 1999. It is necessary to include it here because Mich Con's GCR clause was suspended for 1999.

Mich Con excepts and argues that it should be permitted to recover the booked cost of the pipeline as a GCR cost of gas. Mich Con asserts that, since 1996, it has been actively engaged in various efforts to minimize gas costs, including agreements to buy out or otherwise reduce the cost of certain high priced gas purchase contracts. The agreement with Samson Hydrocarbons, says Mich Con, terminated pending litigation between the parties for payment of \$325,000 and the transfer of the pipeline. To simplify the agreement, the parties eliminated the need for a separate transaction for the pipeline purchase. Mich Con states that the transfer occurred at book cost, with no loss or gain realized.

Mich Con complains that the ALJ's finding that the value of the transfer is not a recoverable cost of gas sold is an "overly mechanical application of form without regard to the substance of the transaction." Mich Con's exceptions, p. 3. It asserts that no challenge was brought against the reasonableness and prudence of the contract buyout to reduce GCR prices; only the form of the transaction was at issue. Mich Con argues that the Commission should reverse the ALJ's conclusion on this issue.

The Staff responds that the ALJ correctly determined that the value of the asset transfer is simply not a recoverable cost of gas under Mich Con's Rule B-46.00. Further, the Staff states, Mich Con's accounting related to this transaction does not comply with the Uniform System of Accounts. The Staff urges the Commission not to reverse the ALJ's determination and thereby set an inappropriate precedent that might encourage utilities to seek to recover through the GCR process various costs that are not contemplated in the company's GCR clause.

The Commission finds that the ALJ properly excluded the recovery of plant from this GCR reconciliation. Act 304 created the GCR process to allow gas utilities to recover a rather narrowly defined booked cost of gas sold. The booked cost of plant is not within that narrow definition, and

is therefore not recoverable through the GCR process. This, however, does not mean that Mich Con will be precluded from recovering the cost of the transferred pipeline. Rather, cost recovery must occur through the company's base rates. As the Staff points out, Mich Con had the opportunity to structure the agreement in a manner that might have brought the costs within the ambit of Act 304 recovery. It should not now be permitted to ignore the structure of that agreement in order to alter the cost recovery process.

Gas Parking Service

During the 1998 GCR period, Mich Con initiated a gas parking service, pursuant to which it received gas from customers that was held for later redelivery. Mich Con characterizes the service as generally involving short-term transactions under its transportation tariff, rather than the longer terms associated with contract storage. However, the parking agreement with Washington 10 Storage Corporation (Washington 10), which involved about six billion cubic feet (Bcf) of gas, lasted about one year. The gas in that transaction was delivered into the system in July and August of the plan year and was expected to be returned the following summer. Mich Con recorded \$1,233,260 in revenues related to 1998 parking services.

Certain challenges arose concerning Mich Con's parking services, addressed below.

A. 90/10 Sharing Mechanism

The Staff took the position that the gas parking service is actually a storage service, the revenues from which must be included when calculating whether a refund is due ratepayers

pursuant to Mich Con's 90/10 sharing mechanism.² The Staff further argued that this short-term storage should have been offered under the company's contract storage tariffs rather than the off-system transportation tariff that the company employed. The Staff reasoned that the gas parking service did not involve movement of gas through Mich Con's system, as required by the off-system transportation tariffs. Rather, the gas was stored on Mich Con's system for later delivery. It pointed out that Mich Con's own witness acknowledged that parking services resulted in the use of Mich Con's storage facilities. Therefore, the Staff argued, the revenues received from these services should be treated as storage revenues subject to the 90/10 sharing mechanism. The Staff's position, if adopted, would result in a refund obligation of \$879,448.

The Attorney General and the RRC agreed with the Staff that parking revenues should be shared with ratepayers. The Attorney General argued that the fees received for all but the Washington 10 transaction should be included as storage revenues in the 90/10 sharing mechanism. In her view, the Washington 10 transaction should not be characterized as storage because it was used to serve GCR customers' needs before ever reaching storage. The Attorney General's position, if adopted would result in a refund obligation of \$819,644.

The RRC took the position that the Commission should establish in this case a sharing mechanism related to gas parking service. In its view, ratepayers should be allowed to share in the profit realized by the company's use of the system that is charged to ratepayers.

Mich Con responded that its parking service is akin to (and the reverse of) the gas loan service offered by Consumers Energy Company (Consumers), the revenues from which the Commission

²Pursuant to the Commission's October 28, 1993 order in Case No. U-10150, Mich Con's most recent rate case, the company may retain 10% of revenues received from storage services that exceed the \$8.4 million threshold. The remaining 90% is to be refunded to ratepayers in the GCR proceeding. This provision is often referred to as the 90/10 sharing mechanism.

found need not be included in calculating Consumers' refund liability under its 90/10 sharing mechanism for storage service. See August 27, 1997 order in Case No. U-10750-R. Mich Con further argued that the Staff overestimated the role of storage in the gas parking service. The company asserted that its parking transactions did not affect either GCR purchases or GCR-related storage operations. Moreover, Mich Con stated, its parking service was provided for the most part without the use of storage facilities. It pointed to the testimony of its witness, Dawn M. Sherman, who stated that parking transactions often occur simultaneously with a comparable gas loan transaction, thus resulting in no net increase in storage or on-system volumes. At other times, Mich Con stated, it was able to use the gas rather than purchase additional volumes. Mich Con stated that the movement of gas without use of physical facilities is common in today's natural gas marketplace.

Mich Con admitted that there are times when storage is used to provide exchange gas services such as parking and lending. However, Mich Con argued, incidental use of storage does not transform parking service into storage service under its C-1 tariff. It also argued that parking services were not contemplated at the time of Mich Con's latest rate case where the storage revenue threshold was set. Further, it argued that, unlike parking services, traditional storage involves a third party's contractual right to inject gas into Mich Con's storage facilities during the summer injection cycle for redelivery during the following winter heating season. On the other hand, Mich Con stated, parking service is provided on a short-term basis, with restrictions on the scheduling of gas redeliveries. In Mich Con's view, parking service is merely a new service that enhances revenues through use of Mich Con's entire system.

The ALJ concluded that parking service is not equivalent to storage service and thus parking service revenues should not be treated as storage revenues. He reasoned that the language of the

Commission's order in Case No. U-10750-R led to the conclusion that the Commission desired to encourage utility efforts to create revenue enhancing programs that entail creative use of the company's system, and that revenues from such creative efforts should be addressed in general rate cases, not GCR proceedings.

Further, the ALJ found that the gas parking service primarily depends on operational factors rather than available storage to determine whether the system is able to accommodate a particular parking request. In most cases, the ALJ found, the parked gas never reaches storage, and any use of Mich Con's storage system was merely ancillary. He further found that Mich Con's parking did not adversely affect GCR customers.

The Staff excepts and argues that the ALJ failed to fully consider that Mich Con accounts for parked gas through its storage accounts. The Staff further argues that there is no dispute that parked gas will be physically injected into storage in those months when displacement with gas from storage withdrawals cannot be accomplished. Moreover, the Staff argues, Mich Con's own witnesses acknowledged the use of storage facilities needed to provide its parking services. The Staff points out that Mich Con's witness Ms. Sherman testified that only a portion of the parked gas may flow directly into storage, because of offsetting storage withdrawals for gas loans and GCR customer requirements, and concluded that parking service is therefore not storage service. However, the Staff notes, Daniel W. Lehane, Mich Con's Director of Transmission and Storage Operations, testified that parked gas has to be accounted for as storage because it is gas that resides in storage facilities. 3 Tr. 206. The Staff concludes that parking services depend upon gas storage operations and are in fact storage services.

The Staff further argues that a fair reading of the Commission's order concerning Consumers' gas loan program in Case No. U-10750-R leads to the conclusion that gas parking is a storage

service. The Staff concedes that the Commission stated that use of storage facilities to provide the gas loan program did not transform that program into a gas storage service. However, the Staff states, the Commission based its decision on the fact that gas loan recipients have no right to use Consumers' storage facilities, and gas loans free up storage capacity rather than use it. The Staff argues that, unlike Consumers' gas loan program, gas parking service does not remove gas from storage. Rather, the Staff argues, gas is injected into storage either directly or indirectly through displacement.

The Staff further argues that Mich Con has inappropriately charged for parking services pursuant to its off-system transportation tariff to avoid its refund obligation. The Staff asserts that parking cannot be considered off-system transportation because the gas does not "move through" Mich Con's system as required by the off-system transportation tariff. Rather, the Staff argues, the company admits that the gas is held for later redelivery.

Mich Con responds that the Staff's arguments lack record support, and should be rejected. It argues that although there are instances in which the provision of gas parking and lending services required the use of storage, e.g., when the netting of gas parks and gas loans resulted in a positive park balance, such storage use was incidental to those services. For the most part, Mich Con asserts, gas parking services do not require use of storage facilities. It again points to the testimony of Ms. Sherman, who stated that gas parking transactions on Mich Con's system often occur simultaneously with gas loan transactions, resulting in the netting of parked and loaned volumes and, consequently, no use of storage. At other times, Mich Con claims, it was able to use parked gas volumes to serve system demand and retain gas in storage. Mich Con asserts that it moved gas without the use of storage or any other physical facilities through displacement.

Mich Con claims that the Staff has erroneously relied on the testimony of an accounting witness for Mich Con. Mich Con states that the witness cautioned that she could only respond concerning the accounting treatment, not the physical facility use, of exchange gas. Also, Mich Con argues, Mr. Lehane stated that exchange gas may be accounted for as a source of supply, but did not say that gas parking and storage service were identical.

Mich Con further argues that the Staff's charge that gas parking should be provided under the storage service tariff rather than the off-system transportation tariff was unfairly raised in briefs after the record was closed. It argues that because the Staff failed to support that argument with testimony, the company could not refute it on the record. In any event, Mich Con argues, the Staff's argument misses the mark. Mich Con asserts that gas parking service is a new service developed in response to customer demand. The service relies on the operational flexibility afforded by the totality of Mich Con's physical facilities, including its storage facilities.

In the August 25, 1997 order in Case No. U-10750-R, the Commission faced a similar dispute concerning Consumers Energy Company's (Consumers) gas loan program. The Staff argued in that case that Consumers' loan service should be treated as storage service, because the injection/removal cycle was the same and storage facilities were indispensable to the program. Generally, the gas was purchased by Consumers, held in storage, and then loaned during the winter months and returned to storage in the summer months. The Commission disagreed with the Staff's position that this was merely storage that Consumers disguised in an effort to avoid the 90/10 sharing mechanism. Therefore, the Commission held that revenues from the gas loan program need not be included in Consumers' 90/10 sharing mechanism. Rather, the Commission found that the appropriate treatment of those revenues should be determined in a general rate case.

However, in this case, the Commission is not persuaded that gas parking services are sufficiently distinguishable from gas storage services to require that the resulting revenues be excluded from the 90/10 sharing mechanism. There is an important distinction between the gas loans considered in Case No. U-10750-R and the gas parking service that is involved in the present dispute. For parking, gas is injected into Mich Con's system for later redelivery, whereas gas loans were effected by removal of storage gas that was later replaced. In fact, Mich Con has described its parking service as the reverse of gas loans. As noted by the Staff, the Commission reasoned in Case No. U-10750-R that gas loans were not storage service, but rather the opposite of storage service, in reaching its ultimate conclusion that the associated revenues should be excluded from the 90/10 sharing mechanism.

Mich Con's attempts to distinguish gas parking from gas storage are not persuasive. Its contention that parking service is more temporary in nature is contradicted by the fact that the Washington 10 transaction ran about a year, which is not a shorter period than the typical storage service cycle. Mich Con's argument that parked gas did not go into storage facilities, except when displacement, line pack, or a corresponding volume of loaned gas was not feasible, is similarly not persuasive. Whether the actual gas molecules added to the system by a parking customer were placed in storage or displaced other gas left in storage is of little or no value in determining whether the service is storage service or something else. Generally, no effort is expended to trace particular gas molecules added to the system to determine whether those molecules are placed in storage or to ensure that volumes used to serve customers are discrete from those placed in storage. Rather, injections and removal from storage are accounted for as if the volumes injected into the system are those that were injected or removed from storage, notwithstanding the actual physical

events. Although movement of gas is kept to a minimum for efficiency's sake, storage facilities are used and needed for gas parking service.

The Commission finds that to hold otherwise creates an incentive for the utility to determine that volumes injected into the system for later redelivery are pursuant to a parking service, rather than gas storage service to which the 90/10 refund mechanism applies. In the Commission's view, there is little if anything to distinguish parking service from storage service, and certainly nothing sufficient to warrant treating the revenue differently for sharing purposes. Therefore, the Commission adopts the Staff's proposal to increase the amount subject to refund by \$1,233,260. According to the Staff, that results in a refund liability of \$879,448. Exhibit S-1, line 31.³

Further, the Commission agrees with the Staff that Mich Con's use of its off-system transportation tariff for gas parking was inappropriate. It is undisputed that parked gas does not "move through" Mich Con's system as the off-system transportation tariff contemplates, but is held for later redelivery to the parking customer. This is a storage service, however short term. Contrary to Mich Con's arguments, this issue was properly raised in the Staff's testimony. 2 Tr. 98-100.

B. Exchange Gas Accounting

Mich Con accounted for all of its parks and loans as exchange gas. All parties agree that the nature of exchange gas means that neither the party giving nor the party receiving pays for the gas. Therefore, the company must account for the gas by establishing a reasonable price. Mich Con priced the Washington 10 volumes (6 Bcf) at the incremental cost of purchasing gas during the months that Mich Con received the gas. Mich Con explained that it priced these volumes in that manner because they displaced gas purchases that would have been made to serve GCR customers

³Given the result reached here, there is no need to address the RRC's final exception concerning establishing a sharing mechanism for these revenues.

had the exchange gas not been used for that purpose. Mich Con took the position that no other exchange gas displaced purchases that would have been made in its absence. Mich Con priced all other exchange gas received in 1998 at its estimated annual average cost of gas, consistent with its past practice for exchange gas volumes. Mich Con stated that it reprices the gas from year to year as it obtains a new estimated annual average cost of gas. It maintained that it had used this method consistently over the years and that its method was appropriate for ensuring that GCR customers would be unaffected by exchange gas.

Mich Con's witness Ms. Schmidt testified that Mich Con adjusts the value of exchange gas activity each year to reflect the estimated annual average gas purchase rate for the current year. The repricing of the exchange volumes carried from one year into the next, she said, permits the removal of these exchange gas volumes from Mich Con's books at a price reflecting the current market value of gas. Mich Con claims that its method results in an ultimate match between the unit price of all volumes booked to the exchange gas account with all exchange gas volumes eliminated from that account, thus leaving no effect on the GCR cost of gas.

The Attorney General took the position that Mich Con improperly accounted for and priced the non-Washington 10 exchange gas volumes. The Attorney General's witness, Ralph E. Miller, explained that, in his view, exchange gas that is flowed through the GCR cost of gas should be priced as if it were from whichever operational activity it displaced. He stated that generally there are only two sources of GCR gas, purchases and storage. According to Mr. Miller, Mich Con appropriately priced the 6 Bcf of exchange gas related to the Washington 10 park at the incremental cost that it would have incurred by purchasing the gas at the time it was received. In his view, that treatment was consistent with the company's position that the Washington 10 gas displaced purchases that otherwise would have been made in July and August of 1998. Mr. Miller took the

position that the remaining 5.3 Bcf of exchange gas did not displace purchases, it must have displaced storage (either injections or withdrawals), and should have been priced at the LIFO⁴ rate appropriate for the volumes so displaced, rather than the estimated annual average cost of gas. If adopted, the Attorney General's proposal would reduce the 1998 cost of gas by approximately \$1.5 million.

The Staff generally accepted Mich Con's accounting as consistent with past practice, but recommended that an adjustment of \$178,509 be made to the 1998 cost of exchange gas to reflect the actual annual average cost of gas rather than the estimated average, in recognition that there would not be another GCR proceeding in the near future in which GCR customers would be compensated. However, the Staff indicated its agreement with the Attorney General that Mich Con's accounting does affect GCR customers to some extent. Therefore, the Staff indicated that it would be reevaluating its position in any future GCR cases. Mich Con agreed that the Staff's one-time adjustment for 1998 should be adopted.

The ALJ rejected the Attorney General's arguments on this issue and found that Mich Con's accounting method, with the adjustment proposed by the Staff, should be adopted. He noted that all parties agreed that the appropriate accounting method should leave GCR customers unaffected; the disagreement surrounded how to achieve that goal. He reasoned that the method proposed by the Attorney General would necessarily affect GCR customers from year to year, sometimes to their benefit and sometimes to their detriment. He further found that the exchange gas at issue did not displace any other operational activity. Therefore, he concluded, there is no associated price to attach to the exchange volumes.

⁴“LIFO” refers to last in first out, an accounting method used to account for the value storage gas as it is removed and replaced.

The Attorney General excepts and argues that the ALJ's analysis was seriously flawed and should be rejected. She argues that if the ALJ is correct that the exchange volumes do not displace any operational activity, then there is no justification for the volumes to be included in GCR costs. She notes that \$28.9 million of the \$467.9 million total cost of gas purchased and produced is for 11.3 Bcf of exchange gas, the disputed portion of which is 5.3 Bcf (valued at \$15,525,687). The Attorney General argues that, unlike the Washington 10 volumes for which Mich Con provided a reasoned pricing scheme, no rational explanation was provided for the additional exchange gas volumes. Moreover, the Attorney General argues, Mich Con's position that its accounting process has been in place for years without objection ignores the sudden and tremendous increase in exchange gas volumes because the company chose to account for its parks and loans in this category.

Mich Con responds that the ALJ correctly analyzed the arguments of the parties and determined that there was no negative effect on GCR customers. It states that the method it used to account for its exchange gas is consistent with the accounting method used over the years in GCR proceedings. It argues that there is no need to alter what has historically been an approved method of accounting for these volumes.

The Commission finds that in instances in which Mich Con uses parked gas for meeting GCR customers' demand, the company should impute a cost for the gas that would have been incurred had the parked gas not been available for use. Price risks associated with changes in the cost of gas between GCR periods related to parking and loan activities should be borne by Mich Con, not GCR customers. As noted by the Attorney General in her reply brief and by Mr. Miller in his rebuttal testimony, repricing the park and loan volumes between periods as recommended by the Staff does not accomplish this goal. But neither does the Attorney General's proposed repricing

based on the LIFO layers in storage, because it assumes that the storage inventory will be depleted rather than replaced in the normal course of business. To appropriately place the risk of price changes on Mich Con, the company should have imputed a cost for the gas that would have been incurred had the parked gas not been available for use. Mich Con properly did this for the Washington 10 volumes. The remaining park and loan activities for 1998 should be priced at the 1998 annual average cost of gas, without the repricing between periods proposed by Mich Con and supported by the Staff. The Attorney General's witness calculated that this would result in an adjustment of approximately \$1.3 million to the Staff's proposed cost of exchange gas. 2 Tr. 135-136.

Reasonableness and Prudence of Storage Operations

The RRC took the position that Mich Con unreasonably and imprudently deviated from the monthly storage levels that were approved in the plan case, which resulted in excess GCR costs. In its view, Mich Con failed to capitalize on the warmer than normal conditions to minimize the cost of injected storage volumes. In particular, the RRC criticized Mich Con for spot market purchases made in May and July that were injected into storage. The RRC's witness, Frank J. Hollewa, an independent energy consultant, testified that had Mich Con followed its GCR storage plan, it could have saved ratepayers \$5 million. He asserted that Mich Con's failure to do so was in part related to its park and loan services, and that the Washington 10 park caused over \$2.2 million of the \$5 million excess costs.

Mr. Hollewa noted that Mich Con's plan for storage injections and resultant storage levels was based on a projected year of normal weather. It assumed a storage balance on April 30, 1998 of 17 Bcf and a full storage balance of 87 Bcf at the end of the injection cycle on October 31, 1998.

Because of a warmer than normal winter, the actual storage balance on April 30, 1998 was 32 Bcf. In Mr. Hollewa's view, this high beginning storage balance should have prompted the company to exercise restraint in purchasing volumes early in the injection cycle to attempt to minimize the cost of gas being injected. Given the normal requirements projected for May, storage would exceed the planned level for the end of May by over 9 Bcf even without injections during that month. Yet the company purchased gas for injection at an average of \$2.42 per Mcf. In contrast, Mr. Hollewa testified, the city gate index price for September was \$1.69 per Mcf. In Mr. Hollewa's opinion, in May 1998, there was every indication that prices lower than \$2.42 per Mcf would be available in the next five months and that May could be warmer than normal.

Mr. Hollewa stated that again in July, Mich Con should have passed up purchasing gas for injection into storage and should have refused the Washington 10 park for July. Had Mich Con done as Mr. Hollewa recommended, he claimed, the company could have purchased 11 Bcf in September for injection into storage at significant savings over the amount included in the 1998 cost of gas.

The RRC argued that Mich Con had no operational constraints that would have required it to purchase volumes for injection into storage so early in the injection season. That position is supported, argued the RRC, by the company's own storage plan included in its 1998 GCR plan. The RRC argued that its proposed injection scheme more closely matches Mich Con's planned storage levels than Mich Con's actual performance. Finally, the RRC argued, deviation from the approved 1998 GCR plan requires Mich Con to meet a higher evidentiary burden to show by clear and convincing evidence that the excess expenses were beyond the utility to control through reasonable and prudent actions.

Mich Con responded that the RRC was attempting to hold it to a standard of omniscience from a position of 20/20 hindsight. Mich Con argued that it met the standard of reasonableness and prudence in its storage decisions, which supports cost recovery pursuant to Act 304. At the time of the challenged purchases, Mich Con argues, the signs did not all point towards declining prices. Rather, it argues that based on the NYMEX screen, prices were expected to rise. Mich Con further argued that, given a warmer than normal year, Mich Con followed its planned storage injections as closely as possible. Mich Con asserts that it followed the least cost purchase pattern consistent with reliability and meeting the goal of full storage at the end of the injection cycle.

The ALJ determined that Mich Con had followed its plan with respect to storage injections for 1998. Therefore, he found, the company need not meet a standard of proof greater than whether its actions were reasonable and prudent. The ALJ further determined that Mich Con's purchases for the months of May and July were reasonable and prudent based on the known and reasonably foreseeable circumstances at the time. He therefore recommended rejecting the RRC's proposed disallowance.

The RRC excepts and argues that the ALJ erred in determining that Mich Con did not deviate from its 1998 GCR plan and thus should not be subject to the higher standard of proof. It further argues that the ALJ erroneously concluded that the RRC's analysis did not consider risk factors that were unknown at the time of purchase. Finally, the RRC charges that in reaching his conclusions, the ALJ ignored the evidence on gas prices presented in the RRC's initial brief and relied on Mich Con's NYMEX screen prices, despite the fact that Mich Con does not make gas purchasing decisions based only on the NYMEX information.

Mich Con responds that the RRC's exceptions amount to mere complaints that the ALJ failed to address evidence presented and arguments offered or adopted. It argues that, contrary to the

RRC's complaint, the ALJ carefully considered the evidence and arguments before correctly concluding that the positions espoused by the RRC were without merit. For example, Mich Con states, the ALJ rejected the RRC's contention that the company should be held to a higher burden of proof based on its failure to follow its GCR plan for storage. The ALJ reasoned that although the monthly storage levels were higher because of warmer than normal weather, the company followed the general purchase pattern and injection schedule it had set for itself in the plan. Mich Con states that the ALJ similarly reviewed and rejected the RRC's arguments concerning gas price indicators. According to Mich Con, the ALJ properly relied on Ms. Sherman's testimony concerning the price increases projected on the NYMEX screen. Mich Con asserts that the record amply supports the ALJ's determination that Mich Con was reasonable and prudent in its May and July purchasing decisions.

The Commission finds that the ALJ correctly determined that Mich Con should not be held to a higher standard of proof based on the alleged failure to follow its approved 1998 GCR plan. The company made purchases that are consistent with the plan, although the storage levels were much higher because of warmer than normal weather. Therefore, the standard to be used in judging these purchases is whether the company acted in a reasonable and prudent manner, not whether excess expenses were beyond the utility's ability to control through reasonable and prudent actions. The record reflects that the company could have waited to purchase additional volumes for injection into storage. After all, the plan schedule that the company submitted for 1998 presumably took into consideration all operational constraints and weighed the probability of supply problems. Therefore, the question that must be answered is whether the indications of the then future gas price decline were such as to require the reasonable and prudent purchaser to wait

until September to purchase gas for injection. After a review of the record, the Commission finds the answer to that critical question is no.

Although the NYMEX futures price is not the only thing that Mich Con reviews before making its purchases, it certainly is one factor that reasonable and prudent purchasers look at in making purchasing decisions. The warmer than normal weather certainly was a factor also. Although that factor created the stocked condition of Mich Con's storage, it also was a factor that might induce spiked prices as gas would be required for electricity generation to help customers cope with the heat waves. Moreover, although the plan considered the risk of supply problems and system constraints, there is a certain wisdom in determining that risk faced earlier is less than risk faced later, when there is less time to make up the loss. Given the conflicting indications concerning the likely price of gas and the general circumstances of the utility, the Commission does not find that Mich Con was unreasonable or imprudent in its gas purchases for May and July. It therefore, rejects the RRC's proposed disallowance.

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 1998 total GCR revenues exceeded its GCR costs by \$18,233,781.
- c. Mich Con's refund liability pursuant to its 90/10 sharing mechanism for 1998 is \$879,448.

d. Mich Con should refund to its GCR customers the amounts shown on Exhibit A attached to this order in the next billing cycle following issuance of this order.

e. Mich Con has refunded a part of its overrecovery during January, February, and March 1999. The remaining refund liability with interest through March 1999 is \$2,660,205.

THEREFORE, IT IS ORDERED that Michigan Consolidated Gas Company shall refund to its gas cost recovery customers \$2,660,205, plus interest, as provided on Exhibit A attached to this order, in the next billing cycle following issuance of 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/ David A. Svanda
Commissioner

/s/ Robert B. Nelson
Commissioner

By its action of July 6, 2000.

/s/ Dorothy Wideman
Its Executive Secretary

d. Mich Con should refund to its GCR customers the amounts shown on Exhibit A attached to this order in the next billing cycle following issuance of this order.

e. Mich Con has refunded a part of its overrecovery during January, February, and March 1999. The remaining refund liability with interest through March 1999 is \$2,660,205.

THEREFORE, IT IS ORDERED that Michigan Consolidated Gas Company shall refund to its gas cost recovery customers \$2,660,205, plus interest, as provided on Exhibit A attached to this order, in the next billing cycle following issuance of 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

Chairman

Commissioner

Commissioner

By its action of July 6, 2000.

Its Executive Secretary

In the matter of the application of)
MICHIGAN CONSOLIDATED GAS COMPANY)
for a gas cost recovery reconciliation proceeding)
for the 12-month period ended December 31, 1998.)
_____)

Case No. U-11455-R

Suggested Minute:

“Adopt and issue order dated July 6, 2000 requiring Michigan Consoli-
dated Gas Company to refund to its gas cost recovery customers
\$2,660,205 plus interest, as set forth in the order.”