

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of the application of)	
MICHIGAN CONSOLIDATED GAS COMPANY)	Case No. U-13898
for authority to increase its rates and for other relief.)	
_____)	

In the matter of the application of)	
MICHIGAN CONSOLIDATED GAS COMPANY)	Case No. U-13899
for approval of depreciation accrual rates and other)	
related matters.)	
_____)	

At the April 28, 2005 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. J. Peter Lark, Chairman
Hon. Robert B. Nelson, Commissioner
Hon. Laura Chappelle, Commissioner

OPINION AND ORDER GRANTING RATE RELIEF

On September 30, 2003, Michigan Consolidated Gas Company (Mich Con) filed an application and supporting testimony and exhibits seeking a general rate increase in the annual amount of approximately \$193.6 million, based upon a projected test year ending December 31, 2005, Case No. U-13898. Mich Con also filed an application and supporting testimony and exhibits for approval of revised depreciation accrual rates, Case No. U-13899. Concurrently with its general rate case filing, Mich Con filed a motion for partial and immediate rate relief requesting

approximately \$153.7 million¹ based upon a projected test year ending December 31, 2004. Mich Con's rates were last adjusted by the October 28, 1993 order in Cases Nos. U-10149 and U-10150, which granted the utility a \$15.7 million annual increase in rates.

On December 10, 2003, a prehearing conference was held before Administrative Law Judge Mark E. Cummins (ALJ) in both cases. In Case No. U-13898 (the rate case), the ALJ granted the petitions to intervene filed by the Association of Businesses Advocating Tariff Equity (ABATE), Attorney General Michael A. Cox (Attorney General), the National Energy Marketers Association, Dominion Midwest Energy, Inc., and Dominion Reserves, Inc., Utility Workers Union of America, AFL-CIO, Local No. 223 Social and Welfare Association, and Lakeshore Energy Services, L.L.C. (Lakeshore). The ALJ denied the petitions to intervene filed by The Muskegon Development Company, Ward Lake Drilling, Inc., and Quicksilver Resources Inc. The ALJ also granted the petitions to intervene filed by ABATE and the Attorney General in Case No. U-13899 (the depreciation case). Although the ALJ consolidated Cases Nos. U-13898 and U-13899, the interveners' participation was limited to the proceedings in which they sought intervention. The Commission Staff (Staff) participated in both proceedings.

Evidentiary hearings were held on May 18 and 24, and August 23, 2004. The record consists of 1,524 pages of transcript and 110 exhibits. On September 21, 2004, the Commission granted partial and immediate rate relief in the annual amount of \$35,311,000. The ALJ issued his proposal for decision (PFD) on December 10, 2004 recommending that Mich Con be allowed to increase its rates for gas service in the annual amount of \$60,328,000, which is approximately \$25 million above the interim amount.

¹This number was later adjusted to \$155.6 million.

Exceptions to the PFD were filed on December 29, 2004 by Mich Con, ABATE, Lakeshore, the Attorney General, and the Staff. Replies to exceptions were filed on January 7, 2005 by Lakeshore, and on January 10, 2005 by Mich Con, ABATE, the Attorney General, and the Staff.

I.

DESCRIPTION OF APPLICANT

Mich Con, a subsidiary of DTE Energy Company (DTE), is a Michigan corporation with its principal offices located at 2000 Second Avenue, Detroit, Michigan 48226. Mich Con is a public utility subject to the jurisdiction of the Commission and it is engaged in the acquisition, storage, transportation, distribution, and sale of natural gas and other related services to approximately 1.2 million residential, commercial, and industrial customers within the state of Michigan. The company's service territory includes the metropolitan areas of Detroit, Grand Rapids, and Ann Arbor, as well as communities in the central and northern sections of the lower peninsula and the central and eastern sections of the upper peninsula. Mich Con currently provides service to its retail natural gas transportation, storage, and distribution customers under rates, terms, and conditions established in the Commission's October 28, 1993 order in Cases Nos. U-10149 and U-10150, which Mich Con implemented on January 1, 1994.

II.

TEST YEAR

A test year is the starting point for establishing just and reasonable rates for both the regulated utility and its customers. In its December 7, 1989 order in Cases Nos. U-8678, U-8924, and U-9197, the Commission discussed the importance and the objective of an appropriate test year. In that order, the Commission noted that a test year is a necessary device employed by the

Commission to establish representative levels of revenues, expenses, rate base, and capital structure for use in the rate-setting formula. Because Michigan has no statutory mandate to utilize a particular type of test year, the selection of an appropriate test year is within the Commission's broad ratemaking power and expertise. The Commission is free to select any reasonable methodology that is consistent with the objective of determining: 1) the level of investment on which the shareholders of the utility are entitled the opportunity to earn a fair rate of return, and 2) the level of expenditures that the utility is entitled the opportunity to recover.

In judging the validity of the test-year data, the question to be asked is whether the methodology and the result are reasonable, not whether a more accurate or complex method can be created. The overall objective is fairness, rather than devotion to a particular methodology. However, the Commission has often cautioned that a reliance on projections can adversely influence rates if those projections prove to be erroneous, and that judicious use of historical data provides a clear view of the utility's cost of providing service and of its expected revenues in the chosen future period. To judge the validity of the test-year data presented in any record, the question to be asked is whether the methodology and the result are reasonable. The economic judgments required in a rate proceeding are complex and rest on the soundness of the underlying data, the Commission's confidence in that data, and the probability of projected future events; those judgments do not point to a single correct answer.

A test year may be supported by historical, future, or a combination of historical and future data. A complete historical test year uses actual audited operating data that are generally adjusted for known and measurable changes. A future test year (frequently referred to as a projected test year) uses projections to determine the levels of revenue, expenses, rate base, and capital structure for a future period. In this proceeding, the parties used differing methodologies to achieve the

2005 test year. Mich Con proposed a fully projected 2005 test year, based upon significant amounts of projected data, proposed budgets, and possible future events. The Staff, however, utilized Mich Con's audited historical year 2002 results, adjusted for known and measurable changes, to arrive at the Staff's 2005 test year. However, as to certain test-year data, the Staff proposed additional adjustments to accommodate unusual events that have a high probability of occurring. The Attorney General opposed Mich Con's use of a fully projected test year. The ALJ determined that the Staff's proposal was more appropriate, lacking the uncertainties that use of fully projected data injects into the ratemaking process.

Mich Con excepts to the ALJ's recommendation. In the company's view, its projected data provide the best evidence of the costs that the company will incur during the period in which the requested rates will be in effect—only its evidence provides the most accurate reflection of future events. Mich Con argues that the company's witnesses provided competent and reliable evidence regarding the projected capital expenditures and operation and maintenance (O&M) expenses needed to provide utility services in the future. In the company's view, the Staff's historical forecasting approach will not create a proper test year, because that approach used only mechanical adjustments to the historical base year.

The Staff supports its proposed historically based test year. In the Staff's view, its case relies on actual and verifiable information from a known starting point—the company's audited 2002 historical year. From that base, the Staff states that it made adjustments for expected inflation and other known and measurable changes. Moreover, the Staff states, it made additional adjustments to accommodate unusual events that have a very high degree of probability. The Staff argues that its test year is far more objective than Mich Con's projected case, which is based primarily upon budgets that are subject to change at the caprice of the utility's management. Thus, the Staff

argues, its test year provides a more prudent and careful base for the Commission's regulatory determinations.

In his brief to the ALJ, the Attorney General argues that the deciding factor regarding Mich Con's projected test-year data is whether the company's evidence has persuaded the Commission of its usefulness and accuracy—whether Mich Con has met its burden of proof based upon the whole record and the nature of that record. The Attorney General notes that the projected data depends primarily upon speculative increases in presently authorized expenses, or upon the costs of projected capital assets/projects that are not currently in-service and have yet to be constructed.

The Attorney General states that under MCL 462.25, Mich Con's current Commission-approved gas rates, classifications, regulations, practices, and services are *prima facie* lawful and reasonable. The Attorney General continues, stating that Mich Con bears the burden of going forward with evidence and the burden of persuasion regarding any proposed changes in those existing rates, classifications, regulations, practices, and services. He argues that because Mich Con's projected test year lacks a historical starting point, and because the company's proposed adjustments are not linked to known and measurable changes to a historical base, the company's projected evidence fails to prove by a preponderance of the evidence that the proposed increases in rate base and expenses are just and reasonable.

ABATE supports the Staff's historically based test year. ABATE states that the Staff's approach was not mechanical as argued by Mich Con. Rather, ABATE argues that the Staff looked at all of the available data and then recommended additional increases for items that were substantial, reasonably likely to occur, and largely beyond the control of the utility. In ABATE's view, the Staff's approach represents the Commission's preferred precedent; it uses historically based data adjusted for known and measurable changes.

The Commission is persuaded that the Staff's use of a historical base year, adjusted for known and measurable changes together with the specific additional adjustments made by the Staff for unusual events, provides an appropriate means to establish rates for Mich Con in this proceeding. The Commission has not overlooked Mich Con's testimony. Rather, the Commission simply is not persuaded of the accuracy of a substantial number of the projections and the proposed future events contained within that testimony and its supporting documentation. Substantial forecasted O&M increases in all business areas, as well as significant projected increases in capital expenditures for the company's related business areas, are contained within Mich Con's testimony and exhibits. However, the company provides little firm support that those increases and expenditures will actually occur as forecasted. In the Commission's view, while projecting considerable increases in O&M and capital expenses, the company provides insubstantial assurance that the planned expenditures actually will occur. The historical approach presented by the Staff provides a firm, prudent, and appropriate base to establish just and reasonable rates for the test period. The Commission will use it.

The Commission again takes this opportunity to state its preference for a historically based test year adjusted for known and measurable changes. A properly adjusted historical test year provides a firm, prudent, and practical basis for setting appropriate rates for the future period. Moreover, as was done with the Staff's approach in this case, the historically based test year may include, when shown to be appropriate, adjustments for items that are substantial, reasonably likely to occur, and largely beyond the control of the utility. By separately setting forth such adjustments (with full justification and explanation), their appropriateness can be evaluated by the Commission on a case-by-case basis. In the Commission's view, these additional adjustments must be unusual, and should only occur infrequently.

III.

RATE BASE

A utility's rate base consists of the capital invested in used and useful plant, less accumulated depreciation, plus the utility's working capital requirements. The ALJ separated the Staff's adjusted rate base proposal of \$1,885,450,000² into net utility plant and working capital.

Net Utility Plant

The ALJ began his analysis of the proper net utility plant for the 2005 test year from the Staff's position. The Staff utilized the company's audited December 31, 2002 balances of utility plant-in-service less all accumulated depreciation. The Staff then adjusted the December 31, 2002 figure to remove part or all of four plant assets: 1) the Wet Header system,³ 2) the Guardian Building, Mich Con's former corporate headquarters, 3) the Customer Information System (CIS), Mich Con's prior customer billing and information system, and 4) approximately \$5.8 million of computer equipment. The ALJ found these net utility plant adjustments to be appropriate; he recommended their adoption.

Mich Con views as appropriate the exclusion of the Wet Header system, which the company transferred to an affiliated company after the 2002 historical base period. Because that asset has been transferred to an affiliate and is no longer within the utility's asset base, it is appropriate to remove the system and its effects from the test year. The Commission finds that the Staff's Wet Header adjustment should be adopted.

²Staff Reply Brief, Attachment A, p. 2.

³The Wet Header system is a pipeline transportation and gathering system in the northern lower peninsula of Michigan. The system has been included in previous Mich Con rate cases. However, Mich Con recently transferred the system to its affiliate, Mich Con Lateral Company. *See*, the February 24, 2005 order in Case No. U-14189.

While agreeing with the Wet Header adjustment, Mich Con excepts to the ALJ's recommendation regarding the Guardian Building, the CIS, and the \$5.8 million in computer equipment. ABATE supports the ALJ's recommendation, as does the Staff.

The Guardian Building

The Guardian Building is a 39-floor landmark office tower, located at 500 Griswold Street, Detroit, MI 48226.⁴ Prior to the merger of MCN Energy Group, Inc. (MCN), and DTE, the Guardian Building was the corporate headquarters for MCN and also for its principal subsidiary, Mich Con. It was almost exclusively occupied by Mich Con's executive, administrative, and centrally located operating personnel. After the merger of MCN and DTE in 2001, the Guardian Building became redundant, and Mich Con moved its headquarters and related personnel to the DTE complex located at 2000 Second Avenue, Detroit, MI 48226.

In the Staff's view, at the time that MCN and DTE determined to merge (and the incidental costs for that merger were evaluated by the companies), two corporate headquarters buildings would have been seen as unnecessary. The consolidation of executive, administrative, and central staff personnel was a result of, and caused by, the merger. The Staff argued, and the ALJ agreed, that as of the 2001 merger, the Guardian Building was no longer used and useful in providing utility service and should be removed from the 2002 historical year base. In the Staff's case, the Guardian Building asset and its related depreciation were removed from the 2002 historical year base that was used to establish the 2005 test year. Consequently, that asset and its accumulated depreciation do not appear in the rate base or the revenue requirement calculations for the Staff's test year. ABATE supports the ALJ's determination.

⁴The discussion of the Guardian Building and the related matters includes the First Street Parking Deck, which was available to those employees working at the Guardian Building.

Mich Con excepts to the ALJ's determination regarding the Guardian Building. In the company's view, the change in use of the Guardian Building was no different than the sale of any other utility asset. The company argues that its initial purchase and later use of the building were prudent actions, and the Commission should not now deny it recovery of all costs related to the building's premature retirement and eventual sale. The company acknowledges that its use of the building was substantially reduced after the merger as Mich Con consolidated its operations during 2002 and 2003 with those of The Detroit Edison Company (Detroit Edison); the building was eventually sold in late 2003.

Instead of removing the redundant asset from the company's net utility plant as of the date of the merger, in June 2003, Mich Con retired approximately \$35.9 million of the Guardian Building's asset and depreciation account balances.⁵ Five months later the building was actually sold for \$5 million. Utilizing the Guardian Building's remaining asset and depreciation account balances, Mich Con calculated that the November 2003 sale resulted in a loss of \$17.3 million. Mich Con proposed to defer and to amortize this loss over the remaining period that the Guardian Building would have been depreciated.

Mich Con's proposal effectively removes the Guardian Building asset from net utility plant, albeit with a different depreciation account balance result than the Staff's position. Mich Con's proposal also places the un-amortized loss-on-sale balance within the working capital calculation allowing the company to earn a return on that balance; the yearly amortization of that loss appears

⁵4A Tr. 1487.

as an O&M expense (in lieu of Guardian Building depreciation expense) when calculating the 2005 test year revenue requirement.⁶

Mich Con argues that the Commission's past practice always has been to allow a utility to defer and to amortize any extraordinary gain or loss on the sale of a utility asset.⁷ Mich Con does not agree with the Staff's position that, rather than a utility asset sale, the redundancy of a second corporate headquarters was a foreseeable product of, and thus a cost associated with, the merger of MCN and DTE. Mich Con argues that, to adopt the Staff's and the ALJ's positions, precludes the company from recovery of its prudent investment in the now-unnecessary corporate headquarters. Accordingly, Mich Con would place a \$17.1 million loss-amortization balance within working capital for the test year and a \$543,000 amortization expense in the test-year revenue requirement calculation.

The Commission has reviewed both the Staff's position and Mich Con's position. The Commission, like the ALJ, is persuaded that the redundancy of the Guardian Building was a product of the merger—the usefulness of one of the two corporate headquarters would be impaired by the merger and that fact was apparent and must have formed part of the basis for the price paid by DTE for MCN. Thus, the redundant corporate headquarters became an asset that was not used and useful for utility service and it must be removed from the company's utility plant. The Commission has reviewed the Staff's proposed method to remove the Guardian Building and its related depreciation from the 2002 historical year, as well as the company's two-step method during 2003 that created the loss that Mich Con desires to defer and to amortize. The Commission

⁶Granted, the depreciation and amortization amounts are not the same—but the ratemaking effect is similar. The redundant corporate headquarters continues to be felt in rates.

⁷Citing the November 6, 1979 order in Case No. U-5955; the January 27, 1987 order in Case No. U-8406; and the November 16, 1999 order in Case No. U-11636.

finds the Staff's method more appropriate; it more accurately reflects the nature of the event—the asset ceased to be used and useful for providing utility service because of the 2001 merger and its costs were inappropriate to continue as part of the company's rate base.

Additionally, Mich Con argues that it must be allowed to defer and to amortize the loss on its later sale of the Guardian Building because of past Commission precedent regarding the sale of utility assets. However, the situation before the Commission is unlike those prior cases cited by Mich Con where utility assets were sold at either a profit or a loss. Here, an asset *ceased* to be used and useful for utility purposes because of the merger of two companies. Well after that asset was no longer used and useful in utility service (and should have been properly excluded from rate base), the asset was sold at a loss. Now the company seeks rate recovery of that loss. In the Commission's view, the loss on sale of an asset that was not used and useful for utility service because of the merger is inappropriate for rate recovery—it is a cost generated by and assignable to the merger itself. Accordingly, the Commission finds appropriate the Staff's proposed treatment of the removal of the Guardian Building from rate base and the later loss on sale of that asset. Consequently, that asset and its related depreciation/amortization figures should not appear in the 2005 test year net utility plant, working capital, or expense calculations.

Customer Information System

Prior to the 2001 merger with DTE, Mich Con implemented its CIS to provide improved customer information and billing capabilities.⁸ That system was installed because the prior system had insufficient capabilities to meet many requirements, such as Y2K compliance and customer choice possibilities. However, one of the major results of the 2001 merger was the integration of

⁸The CIS is a client server-based computer system designed to integrate all customer service business functions through use of a Windows™-based information management system tied to all customer accounts by customer name. See, the June 2, 1998 order in Case No. U-11669.

Detroit Edison's and Mich Con's customer billing and information needs into the Detroit Edison Customer Information System. The movement of Mich Con's customer billing and information activities into the Detroit Edison system has substantially reduced the use of Mich Con's CIS.⁹ However, the CIS continues to be accessed for archived information such as: date of service initiation, billing complaints, usage history data, landlord and tenant disputes, and other complaints.¹⁰

Because the major portion of the CIS was not used and useful for utility service after the 2001 merger and migration to the Detroit Edison system, the Staff placed 10% of the CIS account balance into the net utility component of its 2005 test year rate base calculation. In the Staff's view, only 10% of the CIS remains used and useful in providing utility service. In similar manner, the Staff placed 10% of the CIS amortization amount as an amortization expense in calculating the revenue requirement for the 2005 test year. In the Staff's view, the CIS became unnecessary as a customer information and billing system upon the 2001 merger, and it was known at the time of the merger that the combination of Detroit Edison's and Mich Con's customer billing systems would occur. Thus, the Staff states that the redundancy of the major portion of the CIS is properly a cost of the merger; it is not an asset that is used and useful for utility service and appropriate for inclusion within rate base. The Staff does recognize Mich Con's statement that although the CIS is not used for active customer billing, it is accessed for historical customer and account information. Consequently, the Staff uses the 10% figures in its case to account for the CIS portion that still may be used and useful by Mich Con when providing utility service. ABATE supports the Staff.

⁹4 Tr. 968, 969.

¹⁰4 Tr. 986.

The ALJ recommended adoption of the Staff's position, stating that the redundancy of the CIS was a cost of the 2001 merger and that the Staff's 10% figure is an appropriate approximation of the portion of the CIS that remains used and useful for utility service.

Mich Con excepts to the ALJ's recommendation. The company states that the accounting order allowing deferral and amortization of the CIS cost established a 15-year amortization period.¹¹ In the company's view, the accounting procedures regarding the CIS may not be altered, and, therefore, Mich Con must be allowed recovery in its rates of all CIS-related costs. Moreover, the company states, although the useful scope of the CIS was diminished by the merger, the system was a proper investment at the time it was made and the system is still accessed for historical information. Accordingly, the CIS investment remains appropriate for rate recovery. In the company's view, the CIS was a pre-existing utility investment; its redundancy was not a cost related to the merger of DTE and MCN.

The Commission has reviewed Mich Con's arguments and the record. The Commission is not revising the accounting procedures authorized in Case No. U-11669. Rather, the Commission must determine if the CIS asset is used and useful for utility service, and, consequently, is appropriate for inclusion in the test-year rate base. The Commission is persuaded by the Staff's argument that the redundancy of the CIS customer billing system occurred because of the merger of DTE and MCN; the existence of the two customer billing systems was known by the two companies at the time of the merger and was one of the economies that DTE considered when it purchased MCN. Consequently, the redundancy of the CIS is a cost of the merger, and the total cost of the CIS is not properly an item to be recovered in Mich Con's rates because the substantial majority of the asset is not used and useful in providing utility service.

¹¹See, the June 2, order in Case No. U-11669.

The CIS is a complete customer service business system although it is now used mainly to retrieve historical customer information. In the Commission's view, it is that portion of the system that remains used and useful when providing utility service; a portion that is appropriately part of rate base and depreciation expense for the test year. The Commission finds that the Staff's 10% allowance is an appropriate approximation of the portion of the CIS that remains used and useful in providing utility service to Mich Con's customers.

Miscellaneous Computer Equipment

The Staff excluded approximately \$5.8 million in computer equipment and related depreciation from the historical 2002 base year plant in service. In response to the Staff's data request, Mich Con initially stated that this computer equipment had been retired from service because it could not be located. In responding to further inquiries from the Staff, the company revised its response—the computer equipment had been retired because it could not be “relocated” from the Guardian Building following the merger of MCN and DTE and the subsequent consolidation of Mich Con's headquarters from the Guardian Building into the DTE complex on Second Avenue in Detroit.¹² In the Staff's view, the computer equipment was retired substantially in advance of the end of its useful life and that forced retirement occurred because of the merger—the equipment could not be moved from the Guardian Building to be used at a different location. Moreover, the Staff argues, the company should not be rewarded for its tardy response to the Staff's request for clarification regarding the company's apparent misplacement of the equipment; the timing of the company's response did not allow the Staff to further investigate treatment of this particular asset. ABATE supports the Staff's position.

¹²4A Tr. 1167.

The ALJ was persuaded that the premature retirement of this computer equipment was caused by, and a cost of, the merger of DTE and MCN. Moreover, the ALJ was unpersuaded by the company's argument that the accounting treatment afforded the computer equipment pre-determined its rate treatment.¹³ The ALJ recommended use of the Staff's position regarding this computer equipment.

Mich Con excepts to the ALJ's recommendation. In the company's view, the Commission-authorized accounting treatment for this equipment allowed its amortization; therefore, the cost must be allowed for ratemaking purposes. Moreover, it asserts that the purchase of the equipment was appropriate at the time it occurred; and while the equipment became unnecessary after the merger, the cost of the premature retirement of the equipment cannot properly be attributed to the merger.

The Commission has reviewed the company's arguments and the related evidence. The Commission is persuaded by the Staff's argument that the computer equipment became unnecessary because of the merger, and that the cost of the premature retirement of that equipment must be attributed to the merger; it is not a proper cost for inclusion within the test year. Again, the Commission is not revising the company's prior accounting treatment, rather the Commission has determined that this asset is not used and useful in providing utility service and should not be included within test-year calculations.

Beyond this, the Commission is concerned regarding the company's tardy response to the Staff's request for information. The Staff is a necessary point of information for the Commission; its input is vital if the Commission is to discharge its statutory duty to establish just and reasonable rates for those entities under its jurisdiction. Jurisdictional entities have access to significant

¹³See, the June 2, 1998 order in Case No. U-11669.

resources and vast amounts of company-specific information. Without a rapid and open response to Staff inquiries, the Commission is deprived of an informed viewpoint from the Staff.

Accordingly, Mich Con should not be encouraged to obstruct the Staff's review.

For the preceding reasons, the Commission finds that the appropriate net utility plant for the 2005 test year is: \$1,269,920,000.¹⁴

Working Capital

In addition to net utility plant, the 2005 test year rate base also includes a working capital calculation. Working capital is the amount of funds required to bridge the gap between the time of payment of a utility's expenses and the receipt of revenues from its customers. The Commission extensively reviewed the issue in its June 11, 1985 order in Case No. U-7350, in which the Commission determined that the balance sheet method should be used for ratemaking purposes.

The ALJ began his analysis with the Staff's proposed working capital figure. He then discussed five adjustments that Mich Con would make to that figure: 1) amortization of the loss on sale of the Guardian Building, 2) addition of certain inter-company receivables, 3) addition of amounts related to executive bonus and employee incentive plans, 4) a revision to the injuries and damages balance, and 5) revision of manufactured gas plant (MGP) expenses.

The ALJ adopted only one of Mich Con's adjustments—MGP expenses; he rejected the other four. Mich Con excepts to the ALJ's rejection of the company's remaining four adjustments. The Staff excepts to the ALJ's inclusion of Mich Con's MGP adjustment. ABATE supports the Staff's position regarding all of the adjustments. In addition, ABATE excepts to the inclusion of the pre-paid pension expense balance within the Staff's proposed working capital figure; ABATE would remove that amount. If the pre-paid pension amount is not removed from the working capital

¹⁴The Staff's Reply Brief, Attachment A, page 2.

calculation, ABATE would include a negative net pension expense within the revenue deficiency calculation.

Guardian Building

As previously discussed, the loss on sale of the Guardian Building is not appropriate for inclusion within the working capital calculation for the test year. Thus, the Staff's position is correct.

Inter-company Receivables

The Staff excluded approximately \$3.5 million related to non-utility activities from working capital. This amount represents receivables due to Mich Con from affiliates for expenses incurred by Mich Con on behalf of the affiliates.¹⁵ Mich Con argues that the Staff's adjustment is one-sided, removing only half of the accounting amounts that are related to these non-utility activities, and misrepresenting the company's true working capital needs. Mich Con states that offsets to the \$3.5 million of inter-company receivables exist in multiple accounts throughout its accounting system, many of which are payables accounts. In Mich Con's view, to separate each of these offsets would be time-consuming and burdensome. Rather than identify the offsetting amounts and properly account for them, the company states that it is simply easier to include the entire amount related to non-utility activities thereby assuring that no offset would be missed. In Mich Con's view, the Commission cannot have intended for utilities to analyze and to allocate the detail in individual accounts when it authorized the balance sheet working capital calculation method in Case No. U-7350. Therefore, the company states, it is not necessary for it to analyze the offsetting accounts and the Commission must increase its working capital allowance accordingly.

¹⁵4A Tr. 1251, 1252.

The Staff replies that if the company's position is not supported by proper documentation, making it unverifiable, then a disallowance is reasonable and appropriate.

In adopting the balance sheet method in Case No. U-7350, the Commission understood that the balance sheet method would increase the allocations that would be required to be made. However, given the significant resources employed by a utility when preparing and prosecuting a rate case, those additional allocations were determined to be reasonable and appropriate. As stated earlier regarding Mich Con's tardy response to the Staff's information request concerning "lost" computer equipment, the Staff provides an important function in any proceeding before the Commission. The Staff must be provided the information necessary for it to be able to present an informed position. The information necessary to perform the offset calculation regarding these inter-company receivables was appropriate for submission to the Commission and it is lacking in this record. The ALJ cautioned the company regarding these inter-company receivables, that when filing a rate case, a utility must expect to be audited by the Staff, and that when the audit raises concerns, the utility should be more than willing to provide all information necessary to remove those concerns. That did not occur here. The Commission is equally unpersuaded by Mich Con's argument that because the company chose not to present evidence to allow a proper computation of the offsets to the Staff's adjustment, then the Commission has no choice but to include all of the non-utility related amounts because it is simply easier to include the entire amount. Accordingly, the Commission finds the Staff's adjustment proper.

Executive Bonus and Non-Executive Employee Incentive Plans

The Staff's 2005 test year did not contain any amounts related to Mich Con's executive bonus plan and only 50% of the amount related to Mich Con's non-executive employee incentive plan. (Inclusion of these bonus and incentive plans within the 2005 test year would increase the working

capital component of the rate-base calculation and would also increase O&M expense.) In the Staff's view, these plans do not provide significant value to ratepayers inasmuch as the plans are designed to foster shareholder—not ratepayer—interests. The Staff states that in Mich Con's last rate case, Cases Nos. U-10149 and U-10150, the Commission determined that executive bonus and employee incentive plans require a showing that the plan will not result in excessive rates and that the benefits to ratepayers from the bonus and incentive plans, at a minimum, will be commensurate with the programs' cost. The Staff argues that the executive bonus plan, and the non-executive employee incentive plan to a lesser degree, are primarily designed to enhance shareholder value, not to create benefits to ratepayers. Consequently, the Staff excludes all of the executive bonus amounts and 50% of the non-executive incentive amounts.

The Attorney General supports the Staff, but would go farther; he would exclude all of the non-executive employee incentive amounts. The Attorney General argues that the evidence presented by Mich Con does not show that the company's ratepayers will receive adequate benefits from those programs to justify including the costs of those programs within the 2005 test year calculations.

The ALJ agreed with the Staff's position. Mich Con excepts. The Attorney General supports the ALJ's recommendation, but continues his request to exclude all of the non-executive employee incentive amounts.

In Mich Con's view, its executive bonus and non-executive employee incentive plans are market competitive and provide benefits to ratepayers. Mich Con argues that the company's levels of executive and non-executive compensation are reasonable, and the Commission must include all of the company's proposed bonus and incentive plans within the 2005 test year calculations. The company stresses that its incentive plans are designed to increase earnings per share, cash

flow, customer satisfaction, and diversity placement, and that all of these goals greatly benefit ratepayers. Thus, the company argues, it has met any rational and reasonable standard necessary for the recovery of all costs of these programs.

The Attorney General reiterates his argument that Mich Con has not shown that the costs of either the executive bonus or the non-executive employee incentive plans are commensurate with any benefit that could flow to ratepayers. The Attorney General renews his request to eliminate the remaining 50% of the non-executive employee incentive plan amount.

The Commission has reviewed the arguments and testimony related to Mich Con's executive bonus and non-executive employee incentive programs. A fair reading of the evidence demonstrates that both of these programs seek to drive employee performance behaviors by rewarding actions and behaviors that closely align the employees' interests with growth in shareholder value.¹⁶ While it is true that increased shareholder value may in some minor respect benefit ratepayers, the Commission is not persuaded that the costs of each of these programs are commensurate with the level of any benefits from the programs that may accrue to the company's ratepayers. For example, the weightings given to components of one of the plans were skewed at least 70% to behaviors or actions related directly to shareholder value: 50% earnings per share growth, 20% increased cash flow. Only a small portion of the program would reward behaviors or actions that could fairly be said are directly related to ratepayer or societal interests: 10% safety, 10% diversity placements, and 10% ratepayer satisfaction.¹⁷ Contrary to Mich Con's statements, the evidence presented by the company does not meet the standard set forth in Cases

¹⁶2 Tr. 268 - 270.

¹⁷2 Tr. 271.

Nos. U-10149 and U-10150. The Commission finds that any purported ratepayer benefits of the executive bonus program are not commensurate with the program's cost.

In keeping with the Attorney General's suggestion, the Commission is not persuaded that the benefits of the non-executive employee incentive plan have been demonstrated. Accordingly, the Commission finds that the executive bonus and the non-executive employee incentive plans should not be included within the test-year calculations.

Injuries and Damages Balance

The Staff's working capital calculation includes an amount for an injuries and damages (I&D) reserve balance. The Staff's 2005 test year O&M expenses contain an O&M expense that is based upon a five-year average of cash I&D expenses net of insurance recoveries. In Mich Con's view, the working capital I&D reserve balance can only represent an amount that is additional to yearly cash expenses—an excess comprising all accumulated provisions for I&D less all cash outlays. Inasmuch as the Staff's position regarding the appropriate O&M expense for I&D does not take into account any such accrued expenses, Mich Con states that any I&D reserve balance must therefore be funded only by shareholders and thus is excludable from the working capital calculation as a non-utility item. The ALJ reviewed prior Commission precedent and determined that the Staff's position was appropriate. ABATE supports the ALJ's recommendation.

Mich Con excepts to the ALJ's inclusion of the I&D reserve balance in the working capital calculation. Mich Con reiterates that because the Staff's O&M expense for I&D is based on a five-year average of actual cash I&D expenses, any I&D reserve can only represent an amount that is non-utility in nature—it is funded by shareholders.

The Commission has reviewed Mich Con's arguments and the related evidence. The Commission is persuaded that the Staff's position is correct. In Mich Con's view, the test-year

O&M expense levels dictate the working capital calculation. That is not correct; the two are related, but not inseparable—they need not run in lock-step. The test-year O&M expense level is an exercise to arrive at a reasonable approximation of the expenses that are appropriate and that the utility will incur in the test year. The test-year working capital calculation is an exercise to arrive at a reasonable approximation of the level of funds needed to bridge the time period between the utility’s payment of expenses and its receipt of funds—the amount of funds needed to run the day-to-day business of the utility.

Thus, the Staff’s use of a five-year cash average for I&D O&M expense replicates what the average expense has been; it is a proper approximation of the reasonable test-year expense level. Equally so, the historically based I&D reserve balance reasonably replicates what the utility usually has on hand; it is a proper approximation of the reasonable level of working capital that the company will need to run the day-to-day business of the utility. They need not be twins, for each performs a different function. For these reasons, the Commission finds the Staff’s position reasonable and proper.

Manufactured Gas Plant Remediation Expenses

The issue of Mich Con’s MGP environmental remediation costs, recoveries, and expenses has not been reviewed by the Commission since 1993 during the company’s last rate case, Cases Nos. U-10149 and U-10150. Rate recovery of MGP environmental remediation costs did not occur in those cases, although the outline for such rate recovery was established. During the last decade, much has occurred related to that issue and Mich Con’s treatment of it, with little guidance sought by the company for such an extremely unusual category of O&M expense, its apportionment, and its eventual rate recovery. Thus, this is the Commission’s first opportunity to determine

whether the company has carried out the Commission's directives and policy regarding recovery and apportionment of this unusual item.

The starting point for this review is the Commission's long-standing determination that these unusual environmental expenses should be fairly apportioned between a utility's shareholders and its ratepayers. The Commission has followed this policy in its treatment of MGP remediation costs for all Commission-jurisdictional entities.¹⁸ MGP remediation costs arose because of the method of manufacture of gas in prior years—which was neither illegal nor improper. Residues from that manufacture of gas are now recognized as environmentally hazardous requiring proper remediation. While the Commission could have reasonably determined that these legacy costs were a shareholder responsibility, it did not. Equally so, the Commission determined that present ratepayers should not bear all of the cost related to long-past energy production.

To provide an equitable and fair resolution of this complex historical environmental problem, the Commission has permitted deferral and amortization of the MGP remediation costs, which allows an O&M expense item and a working capital component to appear in a rate proceeding when the utility's revenue requirement is determined and its general rates are established. The O&M expense portion of cost recovery primarily falls on the company's ratepayers. However, the amounts so deferred and amortized do not earn a return as a working capital component (nor is the amount amortized recovered) until the costs are reviewed by the Commission and determined to be appropriate. This inability to earn on the deferred amount (or to recover amortized MGP costs prior to the Staff's review) falls on the utility's shareholders and also acts as an incentive for the utility to aggressively minimize all deferred amounts.

¹⁸See, the April 13, 1995 order in Case No. U-10630 (*Peninsular Gas Co*); the March 11, 1996 order in Case No. U-10755 (*Consumers Power Co*); the March 27, 1997 order in Case No. U-10960 (*Aquila, Inc. d/b/a Michigan Gas Utilities*).

Beyond this future recovery philosophy to share responsibility between ratepayer and shareholder, in Mich Con's particular situation the initial remediation expense was to be borne by Mich Con's shareholders alone. This treatment of the initial cost was reasonable and appropriate because the utility had already embarked upon that course well before asking the Commission for its opinion. Approximately \$11.7 million in environmental remediation costs had been expensed by the company in 1984, with no direction or policy determination sought by the company. However, Mich Con endeavored to reverse its expense treatment years later when it discovered in 1987 that retroactive deferral and amortization would create an O&M expense item in its rate case revenue requirement calculation. The Commission found Mich Con's request for retroactive revision inappropriate and declined to accommodate Mich Con for its prior action;¹⁹ but later allowed the company the above-described recovery mechanism for its future incremental MGP costs.²⁰

In the hearings leading to the company's last rate order in 1993, the Staff set forth procedures to deal with the MGP deferral and amortization—including any possible recovery from third parties, either other potentially responsible parties, insurance carriers that may have provided coverage, or others. Because those procedures had not yet been implemented and such third-party recoveries had not yet occurred, the prudence of the company's minimization of its cost exposure and any action taken to recover costs from third parties would need to be reviewed prior to rate recovery.²¹ This proceeding is the first opportunity the Commission has had to do so.

¹⁹See, the December 22, 1988 order in Cases Nos. U-8635, U-8812, and U-8854, pp. 32 - 34.

²⁰See, the October 28, 1993 order in Cases Nos. U-10149 and U-10150, pp. 140 - 148.

²¹*Id.*, and Cases Nos. U-10149 and U-10150, 17 Tr. 3449 - 3453.

Since the 1993 rate case, Mich Con has been able to settle environmental claims with its various insurance carriers. While the pursuit of the insurers began because of the MGP situation, the eventual recoveries primarily relate to a complete settlement of all of the company's environmental claims against the insurer.²² In short, Mich Con is precluded from recovering on any future environmental claim at any site. Inasmuch as the recovery amount relates to all of Mich Con's sites and claims, that amount must be apportioned. The Staff and Mich Con differ as to how to apportion the recoveries as well as the related legal costs.

Much of the deferral and amortization of the MGP costs (including the third-party recoveries) has already occurred. In its pleadings, Mich Con appears to argue that the Commission may not revise any of the company's prior MGP-related accounting entries—although that is precisely what the company requested of the Commission in Cases Nos. U-8635, U-8812, and U-8854 for its initial \$11.7 million expenditure. But, in any event, the Commission is not revising Mich Con's prior accounting entries. Rather, the Commission must establish a just, appropriate, and reasonable level of MGP O&M expense and working capital reserve for the test-year calculation—nothing more. And it will do so, keeping in mind the Commission's evenhanded cost-sharing policy for these legacy costs.

The total insurance recovery proceeds received by Mich Con from various insurers during the period of 1996 through 2004 is \$21,021,296. The Staff calculated this amount, which includes an

²²One recovery relates only to MGP; one other relates only to the Kalkaska Inlet Facility, which is a gas processing facility at Kalkaska, Michigan and a terminus of the Wet Header system; 4A Tr. 1210. The Staff's and Mich Con's exhibits and testimony treat these amounts distinctly; the discussion that follows deals with the general insurance recovery, although the exhibits correctly treat these as distinct for allocation purposes.

updated schedule of insurance recoveries provided by Mich Con.²³ The insurance recoveries relate not only to MGP sites, but also to the Wet Header system's Kalkaska Inlet Facility (KIF), the ANR/Loreed storage facilities, Citizens Gas Fuel MGP costs, and other non-MGP environmental claims. Once the total insurance recovery was allocated, both Mich Con and the Staff subtracted legal expenses from each distinct amount. Mich Con states that MGP was the prime mover for the insurance recoveries and the settlement of all other claims was merely injected by the insurance carriers during final negotiations to settle any and all remaining items. Thus, Mich Con allocates almost all of the legal expense costs to MGP and a very small amount to non-MGP areas. The Staff, however, takes a contrary position. In the Staff's view, the legal expenses relate to all of the areas and should be allocated proportionally. The Staff argues that the total settlement would not have occurred but for the legal work done to initiate the MGP recovery requests; thus, the late-injected total settlement concept is equally responsible for the initial legal work that created it.

The Commission is persuaded by the Staff's position and finds that its allocation of the legal costs is more equitable and appropriate than that proposed by Mich Con. Had Mich Con not begun the MGP recovery, then the insurance carriers would not have had a vehicle to offer the total settlement. Thus, it is inappropriate for the MGP area to bear all legal costs. In equal measure, the Commission agrees with the Staff's position regarding the minor amounts Mich Con included within legal costs that relate, not to outside legal assistance, but rather to in-house legal work. Those in-house employees are not incremental to Mich Con, and are an appropriate part of the company's general in-house legal expenses, which are recovered elsewhere in Mich Con's rates.

²³The updated schedule included an additional \$371,296 not included within Mich Con's Exhibit A-9, Schedule C-2-6.

Mich Con includes as part of its MGP expenses costs related to two employees that manage consulting/contracting firms that perform MGP-related work. The Staff excludes these costs, arguing that the deferral and amortization of MGP expenses relates only to incremental costs. In the Staff's view, full-time employees of the utility are not incremental costs; those costs are more appropriately recovered elsewhere in Mich Con's rates. In Mich Con's view, the company hired additional full-time central staff project management employees and because those corporate employees perform work related to MGP sites, their employment costs are incremental and thus eligible for deferral and amortization. As with Mich Con's use of in-house legal counsel in relation to the insurance recoveries, the Commission finds that use of in-house employees is not an "incremental" MGP cost that is eligible for the unusual and extraordinary treatment that the Commission has permitted for MGP costs. The deferral and amortization was designed to assist Mich Con in these environmental expenditures, not to afford the company another method of recovering costs related to its full-time central staff employees. Such expenses are more appropriately recovered elsewhere in Mich Con's rates.

Mich Con apportioned part of the MGP insurance recoveries to the \$11.7 million of MGP-related expenses that the company had expensed in 1984—the same expense that the Commission had declined to allow Mich Con to transform into a deferral in 1988. That amount was formally expensed by the company substantially before it approached the Commission regarding recovery of MGP costs, and before the deferral and amortization mechanism was proposed or authorized. The Commission did not intend for that amount to become part of the recovery proposal authorized simply because it had already been expended and could not form part of the proposal before the Commission. Each proposal placed before the Commission since 1988 has always involved how MGP costs would be treated on a "going-forward" basis. And, the Commission has

consistently stated that the costs would be apportioned fairly between shareholder and ratepayer. Accordingly, the Commission finds that the insurance recoveries (which occurred after authorization and implementation of the deferral methodology) could only have been used as an offset to MGP costs that were eligible for that deferral methodology under any fair reading of the Commission's orders. Thus, the Staff's position is appropriate.

Moreover, the MGP deferral and amortization proposals placed before the Commission always contemplated that third-party recoveries might occur; however, the timing of any recovery was not known. The accounting procedure treated the two—MGP incremental cost and third-party recovery—similarly, but the plain reasoning behind the third-party recovery always was for it to be an offset to MGP incremental amortization expense. However, the issue has not been extensively reviewed prior to this proceeding because it was never brought before the Commission. Mich Con determined to seek what third-party recoveries it could obtain. And, the timing of that recovery as well as the timing of the actual MGP remediation expenses was always within the company's control.

Thus, when the unusual situation arose where the company's accounting practices would allow such third-party recoveries to effectively evaporate as an offset to MGP remediation expenditures, the company did so—never seeking input from the Commission in any manner although the result was plainly contrary to the Commission's stated policy regarding recovery of MGP expenses.

As stated earlier, the Commission is not revising Mich Con's accounts. Rather, the Commission must establish an equitable, reasonable, and appropriate MGP O&M expense and working capital allowance so that appropriate rates may be established for the test year. The Commission finds inappropriate the company's one-sided interpretation of the stated MGP policy,

especially when it could easily have sought guidance on such an important and unusual issue for which it had never before sought rate recovery. The Commission is persuaded that the Staff's position regarding the appropriate test-year MGP O&M expense figure and the MGP reserve balance figure for the working capital calculation serves as a proper proxy to set just and reasonable rates for the test year. The Commission will utilize those figures in this rate case. Moreover, the amortization and deferral procedure authorized for Mich Con is modified such that third-party recoveries shall now offset MGP costs, and when such an offset cannot occur, then the amortization period for the third-party recoveries is suspended.

Pre-paid Pension Expense Balance

Present accounting procedures require Mich Con to evaluate the yearly costs of pensions that will be provided to its employees. The procedures are designed to produce an appropriate pension expense for an accounting period, but are greatly dependent upon the investment return from pension assets, actuarial projections, plan expenses, *etc.* Each of these may have a substantial effect on the yearly pension expense to be recorded by the company. For a number of years, this accounting calculation has actually resulted in a negative expense. The recording of the negative expense creates an asset that is the sum of the various negative amounts—future positive expense amounts would reduce that asset. Mich Con's existing pre-paid pension expense asset has grown quite large—\$376.3 million, and it forms part of the working capital calculation for the test year. The amount is a non-interest earning utility asset and is appropriately part of working capital.

However, in developing the test-year expenses, it became apparent to the Staff and to Mich Con that the test-year pension expense would be large and would be negative. Such a negative expense when placed within test-year O&M reduces a revenue deficiency, but does not provide any offsetting cash flow from rates to accommodate the creation and support of the pre-paid

pension expense asset. Rather than continue to see the increased growth of the pre-paid pension expense asset, with its increased working capital requirement, the Staff and Mich Con both proposed that Mich Con's pension-expense level be established at zero for purposes of setting rates within this proceeding. The Staff and Mich Con also proposed that the Commission authorize Mich Con to record a regulatory liability in its financial statements for any negative pension costs as determined under generally accepted accounting principles. Thus, any future growth in the prepaid pension asset would be offset by the regulatory liability, eliminating any further growth in the working capital requirement.

While that approach accommodates test-year and future pension expense, the large pre-paid pension expense asset balance still exists and still forms part of necessary working capital. Thus, both the Staff and Mich Con include the pre-paid pension expense asset when calculating the test-year working capital. The ALJ recommended adoption of the Staff's and Mich Con's position as a reasonable resolution of the negative pension-expense puzzle. Inclusion of the pre-paid pension expense asset balance within the working capital calculation allows the company to earn a return on the asset that it has funded through the recognition of negative O&M pension expense.

ABATE excepts to the ALJ's recommendation, primarily regarding use of the pre-paid pension expense asset balance within working capital. To a lesser extent, ABATE would recognize the negative pension expense when calculating the test-year revenue requirement. In ABATE's view, the negative nature of the pension expense effectively lowers Mich Con's revenue deficiency. If that negative expense is not to be recognized within O&M expenses, thus benefiting ratepayers, then those same ratepayers should not be required to provide Mich Con with a return on any negative pension expense asset balance as part of the working-capital calculation. ABATE argues that it is improper to ask that ratepayers forgo the benefit of negative pension expense when

calculating test-year expense levels, but at the same time suffer increased cost when calculating working-capital requirements for that test year. ABATE views the two as cognates; what happens to one must happen to the other.

The Commission finds that ABATE's argument is not accurate. The pre-paid pension-expense asset represents a non-interest producing utility asset comprising the cumulative negative pension expenses that the company has encountered. The Staff's and Mich Con's position provides an approximation of a reasonable level of that asset, which must be accounted for as part of the test-year working-capital calculation. The pre-paid pension expense asset exists, it is appropriate, and it should be included within the working capital calculation. And, under the Staff's proposal, that asset will not continue to grow.

As regards utilization of a zero level for an appropriate O&M pension expense for the test year, the Commission finds the Staff's and Mich Con's proposal reasonable and appropriate. Setting the O&M pension expense level at zero for ratemaking purposes will provide Mich Con necessary and reasonable cash flow, it will stop the continued growth of the pre-paid pension expense asset, and the accounting for negative pension expense requested by Mich Con will prevent further growth in the working capital requirement, thus providing benefits to future ratepayers.

For the preceding reasons, the Commission finds that \$620,004,000 is an appropriate amount of working capital for the 2005 test year.

Based on the Commission's findings regarding net utility plant and working capital as explained above, the Commission finds that \$1,889,924,000 is the appropriate rate base for the 2005 test year.

IV.

RATE OF RETURN

To calculate the 2005 test year revenue requirement, a rate of return must be applied to the established rate base. In his PFD, the ALJ reviewed Mich Con's capital structure and the cost of each source of capital. He examined the testimony presented regarding the proper capital structure for Mich Con, the appropriate level of common equity, the various levels of debt, and the costs associated with common equity, long-term debt, and short-term debt; he made recommendations regarding each issue. Only one exception was filed to the ALJ's recommendations; it involves Mich Con's objection to the elimination of Other Interest Bearing Debts (OIB Debts).

The Commission has reviewed the ALJ's recommendations and the supporting testimony and exhibits of the company's and the Staff's rate-of-return witnesses. The Commission finds that a permanent capital structure of 50% common equity and 50% long-term debt for Mich Con is a reasonable proxy for use when establishing rates for the test year; thus, Mich Con's permanent capital is \$860,937,000 in common equity and an equal amount of long-term debt. The Commission finds appropriate a short-term debt level of \$112,704,000, a customer deposit level of \$9,567,000, an Other Interest Bearing Credits (OIB Credits) level of \$25,349,000, a deferred investment tax credits (ITC) level of \$657,000, a deferred federal income tax (FIT) level of \$301,447,000, and a job development income tax credits (JDITC) level of \$18,682,000. The Commission finds that for purposes of calculating rates for the test year, the following cost of capital rates are appropriate: a cost of common equity rate of 11%; a long-term debt rate of 6.57%; a short-term debt rate of 3.10%; a customer deposits rate of 8.79%; and an OIB Credits rate of 1.15%. Further, the Commission finds that the cost of JDITC should be equal to the

weighted cost of permanent capital (maintaining the proposed 50/50 debt/equity ratio), and both deferred ITC and deferred FIT should be cost free.

Only one item of Mich Con's rate of return remains contested, OIB Debits. The ALJ recommended that OIB Debits be excluded from the capital structure. Mich Con excepts. The Staff and ABATE support the ALJ's recommendation.

Other interest bearing items are either assets that have an associated return or liabilities that have an associated cost. Typically, these items consist of inter-company note receivables (OIB Debits) or inter-company payables (OIB Credits).²⁴ In Mich Con's view, these items are related to the same inter-company loan policy and should be treated exactly the same. If one is included within the capital-structure calculation, then the other must also be included. The Staff included OIB Credits within its calculations, but excluded OIB Debits. Mich Con argues that, although the inter-company receivables loans increase the company's cost of capital—thus increasing costs to ratepayers, it is not proper to exclude them while including inter-company payables loans, which decrease the company's cost of capital. Mich Con states that separating the other interest bearing items for ratemaking purposes is contrary to the Commission's rate case filing requirements and should not be permitted.²⁵

The Staff's position regarding other interest bearing items is rather straight forward. The Staff included OIB Credits in its calculations because this particular component represents another source of capital, similar to a bank loan. Mich Con has an inter-company loan agreement and can use capital from inter-company subsidiaries in the form of credit facilities at rates that are similar to use of the company's bank credit facilities. However, the same cannot be said of OIB Debits,

²⁴4 Tr. 770.

²⁵See, the June 11, 1985 order in Case No. U-7350.

and the Staff did not include those receivables in its calculations. A portion of the OIB Debit amount proffered by Mich Con is a receivable due to Gas Cost Recovery (GCR) under-collections; the Staff does not foresee or anticipate GCR under- or overcollections—the separate GCR process governs these amounts, and the Staff believes that it is imprudent to include such an item within Mich Con’s capital structure. Another component of Mich Con’s OIB Debit amount was approximately \$90 million of inter-company loans to Mich Con’s parent, DTE—loans that increase Mich Con’s overall cost of capital.²⁶ In the Staff’s view, an appropriate inter-company loan policy should not harm ratepayers by increasing the company’s cost of capital. Thus, the Staff states, OIB Debits are not properly included when establishing the 2005 test year calculations.

The Commission has reviewed the ALJ’s recommendation, and the related testimony and exhibits. The Commission is persuaded that the Staff’s position is appropriate and that OIB Debits should not be included within the capital calculations for the 2005 test year. A prudent inter-company loan policy would not increase the cost of capital to be borne by the company’s ratepayers, nor is inclusion of a GCR undercollection amount appropriate. Thus, it is not reasonable to include the OIB Debit amount proffered by Mich Con within the test-year calculations. The OIB Credit amount is appropriately included precisely because terms supporting the various inter-company payables are reasonable. As to Mich Con’s argument regarding the filing requirements of Case No. U-7350, that case only established the use of the balance sheet method for calculating working capital within a rate case. The Commission separately determines what is reasonable, appropriate, and proper as part of the test-year capital structure. Here, the Commission is persuaded that in this fact situation, it is not reasonable to include OIB Debits in the cost-of-capital

²⁶4A Tr. 1194 - 1196.

calculation for the 2005 test year. Accordingly, the Commission finds that the ALJ's recommended rate-of-return calculations as described above should be adopted.

For the foregoing reasons, the Commission finds that Mich Con's overall rate of return for the 2005 test year is 7.19%.

V.

THROUGHPUT

An important element of the test-year calculations, throughput, represents the total gas sales and transportation volumes delivered to end-use customers during the test period. This number is then used to compute test-year revenues. And, combined with customer numbers in each rate class, throughput is heavily involved in rate-design issues.

Mich Con and the Staff each provided test-year throughput proposals. As with its entire case, Mich Con relied heavily on projections when it developed its proposed throughput numbers and customer count figures. Mich Con's two market witnesses, Kevin M. J. McCrackin, Director, Market Services & Gas Supply, and George H. Chapel, Manager, Market Forecasting, supported test-year projections of 1,249,272 sales customers, 737 end-use transportation customers, 182 billion cubic feet (Bcf) of sales volumes, and 128 Bcf of transportation volumes. The company based much of its presentation on computer-generated trend analyses to forecast the number of customers and expected annual gas consumption. The company's case uses 10-year weather-normalization.

The Staff's proposed throughput numbers and customer counts were primarily based upon the historical 2002 base year levels, adjusted for known and measurable changes. In the Staff's view, only known and measurable trends should be used to reduce customer count and throughput amounts. Moreover, the Staff (consistent with past Commission practice) utilized a 30-year

weather-normalization to adjust the historical 2002 throughput volumes before beginning its remaining adjustments. Based on the testimony of its witness, Michael L. Collins, Manager, Rates & Tariffs Section, Regulated Energy Division, the Staff supported test-year projections of 1,231,119 sales customers, 758 end-use transportation customers, sales volumes of 195.5 Bcf, and transportation volumes of 138.7 Bcf.

The ALJ recommended use of the Staff's projections. ABATE supports the ALJ's recommendation. Mich Con excepts. The company argues three main points regarding weather normalization, demolitions, and the loss of transportation volumes.

Weather Normalization

Mich Con argues that its use of 10-year weather-normalization provides a more accurate view of what may likely happen during the test year. The company argues that the 10-year weather-normalization technique provides the lowest variability over time and is superior to any other method, as verified by the company through the Root Mean Square Error test. In the company's view, its 10-year weather-normalization technique more accurately minimizes the effect of abnormally hot or cold weather from the test year; no other method is appropriate.

The Staff supports its use of the 30-year weather-normalization technique. In the Staff's view, weather-normalization is a technique used to eliminate the variability in consumption due to the effects of weather that occurred during the historical base year; weather-normalization is not properly used to predict consumption during the future test year. The Staff argues that the Commission has continually used a rolling 30-year average for weather normalization. The Staff acknowledges Mich Con's argument that the company's 10-year averaging technique may produce accurate results. However, the Staff notes that such may not always be the case inasmuch as in 11 of the 22 years listed on Mich Con's Exhibit A-11, Schedule F-2-1, the 30-year technique

produced a more accurate result than did the 10-year technique. In the Staff's view, inadequate evidence has been presented to cause the Commission to shift from its preferred normalization technique.

The Commission has reviewed the arguments, testimony, and exhibits. The Commission, like the ALJ and the Staff, is not persuaded that it should revise its practices and now begin utilization of the 10-year weather-normalization technique. While that technique may at times provide more accurate results, the Commission finds particularly telling Exhibit A-11, in which the 10-year technique provided a more accurate result in only 11 of 22 instances. The 30-year technique provided a more accurate result in the remaining 11 instances. Each technique provided a more accurate result in only 50% of the instances. That record hardly supports abandoning the existing technique for a new one. Thus, the Commission finds reasonable and appropriate the Staff's use of a 30-year technique to normalize the weather of the 2002 historical base year. In the Commission's view, the Staff is correct: weather normalization is used to eliminate the variability in throughput due to the effects of weather that occurred during the historical base year, not to predict weather during the future test year.

Demolitions

Mich Con argues that the Staff's position does not account for volume reductions that occurred because of housing unit demolitions, nor does it account for on-going conservation by existing customers. Mich Con states that on average its Wayne and Washtenaw counties service territories experience 4,654 demolitions per year. The company argues that these demolitions translate into approximately 580,000 thousand cubic feet (Mcf) of throughput loss—a loss that the Staff's position does not recognize. Moreover, the company argues, existing customers are conserving, using less gas. Mich Con states that it projects conservation throughput loss of

approximately 3,600,000 Mcf. In the company's view, the Staff's position ignores these demolition and conservation losses and must be adjusted to recognize both of these throughput losses.

The Staff states that demolitions within Wayne and Washtenaw counties are offset by the growth in other areas of the company's service territories—the evidence shows a consistent net gain of customers in spite of any demolitions. Essentially, customers are relocating within the Mich Con service territories; load has not been lost, it has been relocated. Moreover, the Staff argues that Mich Con has not shown that gas volumes actually were delivered to the demolished housing units during the 2002 historical base year—if volumes were not flowing to those housing units during 2002 then that loss is already contained within the Staff's throughput figures. Simply put, a demolished home that sat vacant during the test year already has been excluded from the historical base year volumes, to adjust for demolitions would double count for the volume loss. The Staff states that its test year does not ignore conservation trends. On the contrary, the Staff argues, the historical 2002 base year captures ten years of historical conservation that have occurred since Mich Con's last rate case in 1993. In the Staff's view, the record does not support Mich Con's projected continued increase in the level of conservation losses.

The Commission is persuaded that the Staff's view regarding demolitions and conservation is the more appropriate. The Commission has cautioned that, unless it can be demonstrated that a demolished housing unit received service during the historical base year, then to adjust for the throughput loss may well improperly double count that loss. The record does not contain evidence that the demolished housing units actually did receive service during the historical base year. Moreover, the record demonstrates that overall the number of housing units receiving service from Mich Con is increasing, lending considerable support to the Staff's argument that Mich Con's load

has not been lost, it has relocated. The Commission is equally persuaded that the Staff's position reasonably and properly accounts for conservation—the Staff's historical base year includes all trends relevant to that issue that have occurred over the last decade. To make Mich Con's adjustment may well double count known and measurable conservation losses.

End-Use Transportation

Mich Con argues that the Staff's position does not properly account for the recent trending of end-use transportation (EUT) loss. In Mich Con's view, EUT has been on a downward trend since 2000 and will continue to trend downward. Mich Con argues that a permanent transportation market loss has occurred—EUT customer numbers have decreased and will not increase; and because of plant closings and manufacturing load reductions, an improved economy will not see increased EUT throughput in Mich Con's service territories.

The Staff argues that Mich Con paints an overly pessimistic view of EUT throughput. The Staff argues that while EUT volumes dropped from 2002 through 2004, a statistically valid trend has not been established. The Staff points out that during the period of 1996 through 2003, Mich Con's transportation volumes decreased during 1997 and 1998, substantially increased during 1999 and 2000, decreased during 2001, increased during 2002, and decreased during 2003. In the Staff's view, the historical volatility of the company's EUT throughput makes the extreme reductions predicted by Mich Con unlikely to occur. The Staff argues that its proposal properly sets a level for EUT transportation that is reasonably likely to occur.

The Commission has reviewed the arguments and the evidence regarding the downward trend in EUT throughput. Quite simply, because of the historical volatility of the EUT volumes over the recent past, the Commission finds that the Staff's position provides a more appropriate and probable picture of what may likely occur. Mich Con's reductions are substantial and are based on

the premise that all of the EUT volumes that have been lost will never be recovered. Given the dramatic fluctuations in EUT volumes over the last decade, it is much too premature to adopt Mich Con's discouraging view of the future based only on the trend of the last three years. Thus, the Commission finds that the Staff's position regarding EUT throughput is a reasonable and appropriate EUT throughput level for use in the test-year calculations.

For the foregoing reasons, the Commission finds that the Staff's test-year projections of 1,231,119 sales customers, 758 EUT customers, sales volumes of 195.5 Bcf, and transportation volumes of 138.7 Bcf are appropriate and should be utilized for 2005 test year purposes.

VI.

DEPRECIATION

Mich Con's depreciation rates were last reviewed and established by the Commission in its December 19, 1997 order in Case No. U-11222. Inasmuch as the depreciation rates authorized for a utility have a significant effect upon the rates charged by that utility, the Commission has been moving toward reviewing the utility's depreciation accrual rates in tandem with the utility's general rates. Hence, Mich Con filed Case No. U-13899, its depreciation accrual case, along with Case No. U-13898, this rate case. While both cases were heard by the ALJ in a common record, only the company, the Staff, the Attorney General, and ABATE were admitted into, filed testimony in, and briefed the depreciation case, Case No. U-13898. This section of the opinion and order concerns and decides that case.

In its application in Case No. U-13898, Mich Con proposed that: 1) the company continue use of the unit-of-production method for calculating depreciation on its natural gas production and gathering plant; 2) the company continue its amortization accounting policies for general plant items with a unit cost of less than \$10,000 or for miscellaneous intangible plant, and 3) the

company reduce the number of depreciation accounts and implement the revised depreciation accrual rates contained within the company's Exhibit A-108.

Parties to the depreciation case did not contest continued use of the unit-of-production method for calculating depreciation on natural gas production and gathering plant. Mich Con's accounts for these assets are not large. The Commission finds that Mich Con should continue use of the existing unit-of-production method for these assets.

Parties did not contest continued use of Mich Con's amortization accounting policies for general plant items with a unit cost of less than \$10,000 and also for miscellaneous intangible plant. The Commission finds that Mich Con should continue use of these existing accounting policies.

The major portion of the depreciation case concerns Mich Con's depreciation accrual rates for its remaining utility plant. The contested areas of the case involve net salvage and various survivor curves used in the depreciation calculations. Thus, significant portions of Mich Con's depreciation practices are not contested.

Mich Con's depreciation system comprises the straight-line method, broad group procedure, remaining life technique. As part of its filing, Mich Con included a depreciation analysis which incorporated current plant balances, adjusted depreciation reserve ratios, and updated remaining lives. The depreciation analysis is primarily an updating of the comprehensive depreciation study done for Case No. U-11222, the company's last depreciation case. Mich Con testified that no significant changes in life characteristics or net-salvage estimates have occurred since the last study to warrant more than an updating of that prior study. The company requests a reduction in the number of depreciation rates from 96 to 42; the company has combined a number of accounts to simplify its depreciation system.

The remaining life technique, which is part of Mich Con's depreciation system, computes the depreciation rate by dividing the unrecovered net investment by the estimated remaining years of the life of the asset (or group of assets). The technique effectively ensures that any past under- or over-accruals of depreciation are recovered during the remaining life of the asset.²⁷ Thus, how the remaining asset life is calculated causes a difference in the final depreciation rates. The Attorney General, supported by ABATE, disputes many of Mich Con's assumptions regarding the remaining service life of certain assets.

The remaining life of the plant assets can be calculated in a variety of ways. Included as part of any of the various calculation methods are "Iowa Curves." These statistical curves were developed at Iowa State University over 60 years ago, and are a series of frequency distributions used to describe the mortality of physical property. The curves describe how closely asset retirements cluster around the average service life and whether those asset retirements tend to occur most rapidly before, after, or coincident with the average service life.²⁸ From an appropriate curve, the remaining life of each asset group is calculated. Mich Con's calculation method, the Simulated Plant Record (SPR) Balances method, attempts to pick the appropriate Iowa Curve for an account through iterations designed to determine a curve's ability to simulate the annual number of asset "survivors" for the account that are close to the actual survivor numbers achieved for selected test years. The Attorney General supports a differing method, one that he argues is substantially more accurate.

Charles W. King, President, Snively, King, Majoros, O'Connor & Lee, Inc., presented the Attorney General's position. Mr. King described Mich Con's SPR Balances method as a semi-

²⁷4A Tr. 1404.

²⁸*Id.*

actuarial method. In Mr. King's view, the method to determine service lives he proposes is much more accurate; his retirement rate approach relates aged retirement data to the amount of plant actually retired during historical age intervals, which is then used to calculate retirement ratios. These retirement ratios are used to calculate an observed life table. The observed life table is a series of percentages of plant surviving by age, which demonstrates the actual retirement experience recorded in a band of mortality data. The statistical technique, least-squares analysis, smoothes and extends this data to fit a family of 31 pre-defined Iowa Curves using various life assumptions. Mr. King continues the process until a best fit curve is found for the data and an appropriate service life determined. Mr. King acknowledged that numerous interactive calculations are required for such a retirement rate analysis.

In Mr. King's view, 18 of the 42 life and survivor curves proposed by Mich Con are incorrect and should be revised. This has the effect of reducing the depreciation amounts requested by Mich Con. Moreover, if the Commission does not accept his revised Iowa Curves, then Mr. King suggests that Mich Con switch from the remaining-life technique to the whole-life technique. In his view, such a switch would reduce the amount of depreciation expense recorded by Mich Con.

The ALJ recommended that Mich Con's proposed life and survivor curves be adopted. The Attorney General excepts. Mich Con supports the ALJ's position.

The Attorney General restates his argument that the Iowa Curves proposed by his witness better fit the data available, and that Mr. King's technique is more appropriate. In the Attorney General's view, Mr. King's actuarial analysis was properly verified by his use of the geometric mean turnover method to analyze the average life of plant property as a check on his actuarial analysis.

Dr. Ronald E. White, Executive Vice President and Senior Consultant, Foster Associates, Mich Con's depreciation witness, testified that the Attorney General's retirement-rate method is not a statistical life analysis technique. In Dr. White's view, the method employed by the Attorney General is, basically, a visual-type Iowa Curve-fitting technique that was used before the advent of computer analysis. Dr. White stated that due to the effect of abnormal retirements, fitting an Iowa Curve only to the observed portion of utility plant that survives may not produce an accurate description of the underlying forces that drive plant retirements. Dr. White prefers the method utilized by Mich Con in its presentation. Moreover, Mich Con argues, the geometric mean turnover method, used by the Attorney General to verify and to support his analysis, assumes a stabilized plant category in which the age distribution of the surviving plant conforms to the survivorship function as described by the underlying mortality forces. The company states that the plant categories maintained by Mich Con do not show any such stability. Therefore, the company states, its life and survivor Iowa Curve choices are appropriate and should be utilized.

The Commission has reviewed the arguments of Mich Con and of the Attorney General regarding the appropriate Iowa Curves to be used as life and survivor curves. The Commission is persuaded by Dr. White's testimony that the Attorney General's proposed Iowa Curves do not more reasonably project the eventual retirements that will occur within Mich Con's plant accounts. Accordingly, the Commission finds that Mich Con's proposed life and survivor curves should be utilized.

Similarly, the Commission is not persuaded that Mich Con should switch from the remaining-life technique to the whole-life technique. The Attorney General's argument is simply not well supported. The Commission will not make a significant change in Mich Con's existing depreci-

ation technique without a detailed record. The switch in depreciation techniques, in the Commission's view, was not significantly explored and commented upon within this record.

Net-Salvage Values

The remaining contested matters within the depreciation case, Case No. U-13899, concern salvage value and cost-of-removal, and the proper accounting treatment for those items. Salvage value and cost-of-removal analyses concern the reviews of appropriate net-salvage values to be used when calculating depreciation rates. The analyses produce net-salvage factors. A system of depreciation accounting distributes the cost of a tangible asset over that asset's estimated useful life. The cost of the asset is reduced (or increased) by its end-of-life salvage value, which is estimated at the time that the asset is placed into service; that salvage value includes any cost to eventually remove the asset from service. In many instances, the cost to remove the asset exceeds its actual salvage value. In such instances, the asset's net-salvage value is a negative number. Under current regulatory depreciation accounting, the negative net-salvage value is combined with the asset's acquisition cost, and it increases the amount to be depreciated over the asset's useful life.

The net-salvage factors used by Mich Con have a significant effect upon the company's yearly depreciation expense level. This expense is, of course, one component used when setting Mich Con's rates for its gas utility services. If depreciation rates are set artificially low, thereby shifting costs out to future generations that should be paid by current customers, then intergenerational equities will be affected—later generations of customers will pay expenses that earlier generations should have borne. Substantial disagreement exists as to what costs of removal are appropriate and how those costs should be accounted for.

The Attorney General notes that the accounting procedures authorized by the Federal Energy Regulatory Commission's (FERC's) Order No. 631²⁹ separate depreciation from recovery of removal costs for FERC-jurisdictional entities. Order No. 631 relates to accounting, financial reporting, and rate-filing requirements for asset retirement obligations; the order deals mainly with Statement of Financial Accounting Standards (FAS) No. 143, which prescribes the treatment of future costs associated with legal obligations to retire assets. The order does not apply FAS No. 143 standards to all retirement obligations, but it does require FERC-jurisdictional entities to maintain separate records for the cost of removal for non-legal obligations where allowances for these costs could be identified.

The Attorney General states that Mich Con has implemented FAS No. 143 with respect to the retirement costs of its New Haven storage field. The Attorney General notes that the company has not implemented FAS No. 143 accounting procedures for the removal costs of transmission and distribution mains and services because Mich Con could not measure those costs. The Attorney General states that Mich Con has transferred the net removal cost accruals for its transmission and distribution mains and services from the company's depreciation reserves.

The Attorney General would change the method of recovery of net-salvage costs. He would maintain separate subsidiary cost-of-removal records and then identify additions and deletions from this account each year. The Attorney General recognizes that this is a major change from the previous treatment of removal costs, but he argues that it is an appropriate change because under existing practices it is difficult to identify what portion of the company's annual depreciation

²⁹FERC Order No. 631, *Accounting, Financial Reporting, and Rate Filing Requirements for Asset Retirement Obligations*, order issued April 9, 2003 in Docket No. RM02-7-000; 69 FR 19610.

expense recovered past capital expenditures and what portion of that expense was accrued to offset future removal costs.

The Attorney General would separate Mich Con's proposed depreciation rates and accruals into their two constituent parts: depreciation and cost-of-removal allowances. He would base his cost-of-removal allowances on the company's most recent five-years' experience. Utilizing a variant of the type of accounting required by FAS No. 143 for financial reporting of legal asset retirement obligations, the Attorney General proposes that the company book a liability for an asset's projected retirement cost, discounted at a risk-free interest rate to arrive at the appropriate present value. Then, the Attorney General continues, each year the company would show two items of expense: (1) the amortization of the booked retirement liability, and (2) the annual accretion in the present value of that liability. In the Attorney General's view, this FAS No. 143-derived procedure recognizes the present value of future removal costs in a much more appropriate and precise manner than would the company's proposed net-salvage ratios; moreover, it eliminates the unfairness of charging present ratepayers a substantial dollar cost that the company will not incur until many years from now.

Because Mich Con has transferred the net removal cost accruals for its transmission and distribution mains and services from the company's depreciation reserves, the Attorney General recommends that regardless of the Commission's determination with respect to depreciation parameters and the calculation of net-salvage allowances, the Commission direct Mich Con to separate depreciation accounting from removal cost accounting so that there are separate depreciation and removal cost rates, charges, and reserves on the company's books.

In ABATE's view, net salvage should be excluded from the development of Mich Con's depreciation rates. ABATE proposes to include net salvage associated with ongoing retirements as

a separate operating expense when calculating Mich Con's revenue requirement. This new operating expense category would be based on Mich Con's current levels of net salvage for its various classes of gas utility plant; ABATE recommends a five-year average of actual net-salvage experience, as adjusted for inflation. The net-salvage operating expense amount would then be added to the accumulated depreciation reserve that would either grow or be reduced, depending upon whether that net amount was positive or negative. In effect, all depreciation expense—except the net-salvage value—would be treated as it has in the past; net-salvage value would be removed from the normal depreciation expense and then incorporated as a separate operating expense.

The Staff states that Mich Con's estimate of negative net-salvage costs is too high; that the company's proposed depreciation accrual rates frontload the costs to the detriment of current customers. The Staff proposes using a five-year average of the company's actual negative net-salvage costs divided by the book cost of retired plant to determine the proper negative net-salvage to be included in calculation of the depreciation accrual rates. Moreover, the Staff states, it believes that Mich Con takes a much too narrow view of the applicability of FAS No. 143 to the company's non-legal removal obligations. In the Staff's view, Mich Con accrues for non-legal removal obligations—future costs of removal for which a legal obligation does not exist. The Staff believes that the Commission should re-examine its policy regarding the recovery of removal costs.

The ALJ reviewed the arguments of the parties regarding these issues. He noted that in Case No. U-14292 the Commission had instituted a generic proceeding to review FAS No. 143, FERC Order No. 631, and their accounting and ratemaking issues. The ALJ stated that in Consumers Energy Company's (Consumers) recent depreciation case proceeding, Case No. U-12999, the

Attorney General, ABATE, and the Staff had raised similar arguments regarding the negative net-salvage issue. In that proceeding, the ALJ noted that the Commission held that an abrupt shift in the method and the manner of cost of removal recovery as proposed by either ABATE or the Attorney General was ill-advised without further industry-wide comment, discussion, and review; the Commission then established the generic proceeding, Case No. U-14292. Because of this, the ALJ recommended that the question of separating depreciation accounting from net-salvage accounting should await the result of the generic proceeding. However, the ALJ agreed with the assertions by the Staff, the Attorney General, and ABATE that Mich Con's proposed level of negative net salvage value is inordinately high when compared to historical figures. The ALJ was persuaded by the Staff's argument that use of a five-year actual average to create the negative net-salvage ratio was appropriate for the near-term and should be used within the rate case, Case No. U-13898. Thus, the ALJ recommended adoption of the Staff's depreciation accrual rates.³⁰ He also recommended that consideration of the various other proposed net-salvage value calculation methods be deferred until the conclusion of the Commission generic review of these issues in Case No. U-14292.

The Attorney General excepts, restating his prior arguments. He would not await the outcome of the generic proceeding, believing that the Commission may make an informed decision regarding appropriate depreciation accrual rates and completely revised net-salvage values for Mich Con using the testimony and arguments provided in this record. ABATE supports the ALJ's recommendation, arguing that while a fundamental change should occur in the treatment of depreciation rates and the computation of net-salvage values, those issues will be fully explored in the generic proceeding, Case No U-12492. Thus, ABATE supports the Staff's position as a near-

³⁰Exhibit S-50, column 13.

term solution to the question of the absolute size of Mich Con's negative net-salvage values. The Staff would support the ALJ's various depreciation recommendations.

Mich Con excepts to the ALJ's recommendation. The company argues that the Commission's determinations in the generic proceeding, Case No. U-14292, are nearly certain to have a direct effect upon Mich Con's future depreciation accrual rates. Mich Con states that the generic proceeding was instituted by the Commission after the presentation in Consumers' most-recent depreciation case of positions directly analogous or identical to the positions taken in this case by the Staff, the Attorney General, and ABATE. Mich Con argues that changes in its existing depreciation rates should await the completion of Case No. U-14292, and the ALJ's recommended change in the company's depreciation accrual rates is premature. Mich Con argues that it should continue implementation of the company's existing depreciation accrual rates established in Case No. U-11222. In Mich Con's view, the Commission has already determined that no revision in depreciation rates may be made for Mich Con and for all other utilities within Michigan until the generic proceeding has concluded.

The Commission has reviewed the testimony and the exhibits regarding calculation of net salvage for Mich Con and Mich Con's statements regarding the preclusive effect of Case No. U-14292, the generic proceeding. Initially, the Commission must address Mich Con's argument that the order establishing the Case No. U-14292 proceeding foreclosed any change in a jurisdictional entity's depreciation accrual rates until conclusion of that case; it did not. As regards Consumers in Case No. U-12999, the positions of the Attorney General and of ABATE provided for significant changes in the method by which net salvage would be calculated and recovered—those positions needed to be more fully explored. However, as recognized by Consumers, the absolute size of the company's negative-net salvage and the calculation of that net salvage were

also prominent issues. After issuance of the October 14, 2004 order in Case No. U-12999 (which reinstated Consumers' prior rates as an interim measure until conclusion of the generic proceeding), Consumers recognized that its existing negative net-salvage values were substantial, and requested that the company be allowed to implement depreciation accrual rates that are similar to the Staff's position in this case. The Commission allowed Consumers to implement those reduced rates.³¹ Thus, Mich Con's statement that its depreciation accrual rates may not be revised until conclusion of the generic proceeding based on the precedent set in Case No. U-12999 is incorrect.

The absolute size of Mich Con's negative net-salvage accounts concerns the Commission, as does the inordinately high level of negative net salvage when compared to the company's actual historical experience as noted by the ALJ. Moreover, the Commission agrees with the ALJ that the issue of separating net salvage accounting from depreciation accounting should be deferred until the generic proceeding is concluded. While the Commission continues to believe that the Attorney General's proposals and those of ABATE must be thoroughly reviewed within the generic proceeding (as should any other proposals of interested parties), like the ALJ, the Commission is persuaded that the Staff's proposal provides a workable solution for the near-term and it reflects the company's actual recent experience. The Commission finds that the Staff's proposal should be implemented along with the general gas service rates established in this order. And, use of the Staff's proposal for the near-term places the depreciation accrual rates of the state's two largest gas distribution utilities on a level field.

In any event, the Commission finds that after the generic proceeding, Mich Con's rates should be revised to reflect any new practices or procedures that are adopted. Thus, within 90 days after

³¹See, the December 2, 2004 order in Case No. U-12999.

the issuance of the Commission’s order in Case No. U-14292, Mich Con should file a case to revise its depreciation accrual rates, including a mechanism to incorporate any revised depreciation accrual rates within the company’s general gas service rates, as determined to be appropriate by the Commission within that later proceeding.

VII.

ADJUSTED NET OPERATING INCOME

In the PFD, the ALJ recommended an adjusted net operating income for the 2005 test year of \$97,921,000. He arrived at that figure from the Staff’s adjusted net operating income figure of \$87,289,000. That base Staff figure was adjusted to remove revenues related to load-balancing charges and unauthorized gas usage charges, the net amount of these charges is \$1,900,000. The Staff agreed that these adjustments to its initial figure were appropriate. The ALJ then adjusted the Staff’s figure to remove Mich Con’s control premium-related expense of \$12,709,000 and to add the company’s MGP-related expense of \$231,000. The ALJ also adjusted the figure to add interest implicit in the test-year capital structure of \$51,000, and interest synchronization of \$3,000. The ALJ’s figure is computed as follows:

	<u>Gross (\$000)</u>	<u>Net (\$000)</u>
Staff’s Adjusted Net Operating Income		87,289
Other Operating Revenue Adjustments:		
Load Balancing Charge Revenue	(1,200)	(760)
Unauthorized Gas Usage Revenue	(1,800)	(1,140)
Control Premium Adjustment	20,071	12,709
MGP Amortization Expense	(365)	(231)
Interest Implicit in Capital Structure	51	51
Interest Synchronization	3	<u>3</u>
Final Adjusted ALJ Net Operating Income:		<u>97,921</u>

Mich Con, the Staff, and ABATE except to certain of the ALJ's recommendations regarding calculation of the company's adjusted net operating income for the test year. The exceptions involve various expenses or adjustments that each party would make to the ALJ's recommended figure. The exceptions are discussed below.

Transportation Discounts

Mich Con provides transportation service at discounted rates in two instances: discounts provided under special transportation contracts, and discounts provided under tariffed rate schedules. Currently, approximately 50 customers receive discounted transportation service. These customers are primarily served under the company's Rate Schedule LT-2, which allows the company to negotiate a distinct rate with each customer within a Commission-established minimum and maximum rate; a pre-set collar of rates inside of which Mich Con is free to negotiate based upon its review of relevant criteria. Mich Con argues that but for these discounted rates, those transportation customers would have left the Mich Con system requiring remaining customers to bear any fixed costs related to those former customers. Mich Con argues that each discount is justified based upon the cost of service to the customers receiving the discount and the benefits remaining customers receive from the incremental recovery of corporate overhead costs that would otherwise be allocated to those remaining customers. In Mich Con's view, the use of a discounted rate was appropriate in each instance and the Commission must allow the revenue lost to the company because of the discounted rate to be recovered from Mich Con's remaining ratepayers.

The Staff does not include the revenue lost from the discounts when calculating its level of sales and transportation revenue for the 2005 test year. The Staff does not dispute Mich Con's evidence; rather, the Staff argues that it is insufficient. The Staff states that Mich Con's support

for recovery of the discounts does not comply with the Commission's directives in prior orders; thus, the discounts should not be considered.

The ALJ recommended adoption of the Staff's position. ABATE supports the ALJ, arguing that the rates of other customers should not be increased to recover discounts received by a few select customers. In ABATE's view, Mich Con failed to meet the criteria established by the Commission for recovery of the discounts listed in the company's testimony.

Mich Con excepts to the ALJ's recommendation. The company argues that each of the discounts meets the Commission's criteria, is based on the cost of service to the customer receiving the discount, and is appropriate for rate recovery. The company states that it provided an exhaustive summary detailing each transportation discount, specifically identifying how each discount was determined and how each discount benefited all other customers.³² Moreover, Mich Con argues, the Commission allowed the recovery of rate discounts in the company's last rate case, Cases Nos. U-10149 and U-10150; it cannot disallow similar discounts in this proceeding.

The Commission has reviewed Mich Con's testimony and arguments. Mich Con refers to the Commission's allowance of the company's coal displacement customer discounts in Mich Con's last rate case, Cases Nos. U-10149 and U-10150; the company argues that this prior treatment of a discounted rate effectively limits the Commission's action within this case. The Commission does not agree.

In the decade since that last rate order, the Commission has continually provided additional guidance on the appropriate recovery of discounts. The Commission has consistently stated with regard to transportation customer discounts that should Mich Con seek rate recovery of those discounts—thus shifting to other customers the cost of discounts given to favored customers—the

³²2 Tr. 367 - 387; Exhibit A-12.

company would bear a substantial evidentiary burden. The Commission has explicitly and repeatedly stated that when rate recovery was sought, at a minimum Mich Con would need to present a clear, convincing, and unequivocal demonstration that either: 1) the rate and service terms provided are justified on the basis of the cost of service, or 2) the benefits to other ratepayers are substantial and have a value that outweighs the costs that are not recovered from the discounted rate customer. In either showing, Mich Con is *required* to provide a cost-of-service study that identifies and quantifies all costs for the particular discounted customer.³³ That required cost-of-service study to support each discounted rate customer is simply lacking in the record.³⁴ Accordingly, Mich Con has not met the criteria for recovery of the discounts and the Staff's position is appropriate.

Control Premium

When DTE merged with MCN in 2001, the price paid by DTE for all of the stock of MCN was above the market value of the MCN shares at that time. The amount paid over the market value represents a cost that DTE incurred to gain control of MCN—it has been variously denominated an acquisition premium or a control premium. In either event, it is an amount that Mich Con seeks to recover from its ratepayers in this proceeding. In Mich Con's view, the acquisition of MCN by DTE created many synergies for the combined operation of Mich Con and Detroit Edison. After the merger, the two utilities (and the one remaining corporate head office) could work together cooperatively providing economies and benefits from their joint action. Mich

³³See, the March 23, 1995 order in Case No. U-10646; the March 11, 1996 order in Case No. U-10755; and the July 16, 1999 order in Case No. U-11998.

³⁴Mich Con must have this customer-specific cost-of-service information—at least for a few customers. Testimony indicated that the cost of service for discounted Customer S in Exhibit A-12 is less than the forecasted revenues related to that customer, 2 Tr. 384; however, the necessary customer-specific cost-of-service study was not provided for the Commission's review.

Con states that the cost savings flowing from these synergies more than offset the expense represented by the acquisition premium paid by DTE above market price to acquire MCN. Because these cost savings exceed its share of the acquisition premium, Mich Con seeks to recover its allocated share of the control premium from its customers.

DTE apportioned responsibility for the control premium as follows: Mich Con, 28%; Detroit Edison, 66%; and other DTE operating units, 6%.³⁵ Mich Con's position is, basically, to annuitize its allocated share, and then to amortize that total amount over a 40-year period. This method places an amortization expense within the test year. Mich Con states that its 28% share of the control premium is \$250 million, which when annuitized at 9.78%³⁶ and then amortized over a 40-year period, results in a \$25.4 million amortization expense for the 2005 test year.

Initially, the Commission must address Mich Con's argument that the Commission already has implicitly and unconditionally approved the merger. As will be demonstrated, the Commission did not approve the merger. Mich Con states that by the Commission's authorization of the special transportation and storage contract with Exelon Energy Company,³⁷ the Commission implicitly approved the merger because the Commission could have stopped the merger merely by withholding its authorization of that special transportation contract. Moreover, Mich Con asserts, the Commission did not file objections to the merger with the United States Securities and Exchange Commission (SEC), which it could have. In Mich Con's view, if the Commission had not approved of the merger, it should have objected to the SEC.

³⁵2 Tr. 279.

³⁶This is the Staff's pre-tax cost of capital, 4 Tr. 962.

³⁷See, the February 14, 2001 order in Case No. U-12825.

These arguments are plainly contrary to the facts as they exist. The Commission's jurisdiction did not extend to the approval of or the authorization of the merger of DTE and MCN. The Commission's actions properly conformed with that jurisdiction. The Commission exercised its statutory duties when it reviewed the Exelon Energy contract in Case No. U-12825, to suggest that the Commission would have utilized its adjudicatory power within that case to achieve a result beyond its jurisdiction—the derailment of the DTE/MCN merger—is impertinent.³⁸ The Commission did not approve or disapprove the merger. And, that is not the question presented within this proceeding. The Commission must determine whether the control premium amortization amount sought by Mich Con is an appropriate expense item to be recovered in the 2005 test year, nothing more.

All parties begin their arguments from the Commission's June 29, 1990 order in Case No. U-9323. Among other things, that proceeding concerned an acquisition adjustment sought by Michigan Gas Company regarding the purchase of the gas assets of Michigan Power Company by Southern Michigan Gas Enterprises; those gas assets became Michigan Gas. Specifically, Michigan Gas sought to amortize approximately \$7.4 million over a 30-year period and to include the un-amortized balance in its rate base. The Commission did not allow the acquisition adjustment. The Commission reviewed the lengthy listing of benefits alleged by Michigan Gas to have been created by the acquisition. The Commission was not persuaded that the net benefits provided to ratepayers by the acquisition outweighed the acquisition costs that Michigan Gas sought to recover from those same ratepayers. The Commission determined that rate recovery of an acquisition adjustment (control premium) should only occur where ratepayers receive a net benefit from the change in ownership of the utility.

³⁸Mich Con well knows that the Commission did not approve the merger, 2 Tr. 29; Mich Con's exceptions, footnote 18, p. 40.

Mich Con argues that it has met this standard—the benefits of the DTE/MCN merger that have accrued (and will accrue) to Mich Con’s ratepayers far outweigh the yearly control premium amortization cost that those ratepayers will bear over the 40 years of its amortization. The remaining parties argue the opposite. The ALJ was not persuaded by Mich Con’s evidence and recommended that the control premium not be included when calculating the company’s rates. Mich Con excepts. The Staff and ABATE support the ALJ’s recommendation.

In Mich Con’s view, the yearly control premium amount to be included in customer rates is substantially less than the cost-saving synergies that Mich Con’s ratepayers enjoy because of the merger. All of these purported savings are based upon Mich Con’s subjective valuations of related costs and the company’s projections of future events. Mich Con’s witness, Daniel G. Brudzynski, its Vice President and Controller, testified regarding the ratepayer benefits that flow from the merger. He testified that upon the merger, the combined companies immediately achieved operating synergies through economies of scale and scope, the combination of its corporate headquarters and staff, and the leveraging of its contiguous and overlapping service territories; these synergies improved customer satisfaction and increased efficiencies of the combined companies’ workforce. Much of these purported synergies were achieved through a “shared services” approach and the overwhelming majority of this value was created by centralizing staff and combining the two separate, yet overlapping, electric and gas staff functions. This staff combination was achieved through an early retirement option and a voluntary resignation offer, resulting in a net reduction of 811 employees. Moreover, Mr. Brudzynski testified, the combined companies achieved lower information technology costs and combined supply chain operations.

Based on the company’s projections and assumed costs, Mich Con states that it achieved at least \$18.6 million in labor and benefit cost savings during 2002, and the company projects that

these labor and benefit cost savings will increase to at least \$24.8 million by the 2005 test year. Exhibit A-13, Schedule H-1 contains an extensive listing of Mich Con's projected O&M cost savings for the test year and the four years preceding the test year. Mich Con argues that the projected level of O&M cost savings for the test year—\$24.8 million—is above its proposed \$24.4 million control premium expense; thus, benefits to ratepayers substantially exceed costs to ratepayers and the Commission must allow the company to recover the control premium.

ABATE argues that Mich Con's ratepayers are not receiving net benefits from the merger. ABATE does not separately quantify each changed O&M expense. Rather, ABATE argues that even considering the possible merger synergies, Mich Con's net O&M expense from the 2002 historical base year to the 2005 test year is escalating at 2.15% per year, which is above the projected rate of inflation.³⁹ ABATE states that the merger does not provide Mich Con's ratepayers with benefits that one would reasonably expect; controllable O&M expense should be declining, not increasing at a rate in excess of inflation. Given this state of affairs, ABATE argues that it is unreasonable to include the control premium when calculating Mich Con's test-year rates. The Attorney General supports ABATE's position.

In its brief and reply brief, the Staff argued that the control premium, itself, should be lower than that proposed by Mich Con. In the Staff's view, approximately \$160 million in MCN tax losses utilized by DTE during the period of 2001 through 2003 should be treated as a reduction in the price paid by DTE for MCN. This has the effect of lowering the control premium allocated to Mich Con, and lowering the amount of control premium expense that would appear in the test year to approximately \$11 million, net of taxes. The Staff would not amortize the balance over 40 years as proposed by Mich Con, arguing that this type of amortization is not consistent with

³⁹Exhibit I-91; 4A Tr. 1356 - 1358.

FAS No. 142. The Staff noted that substantial customer confusion and dissatisfaction occurred as a result of the combination of the Mich Con and Detroit Edison customer billings system and that the Commission opened an investigation into allegations of poor customer service quality by both Mich Con and Detroit Edison.⁴⁰ The Staff noted that the net reduction of the number of employees produced many of the purported central staff synergies; however, after the initial reduction in employees, the companies' employee count has increased. In the Staff's view, because of employee productivity losses, Mich Con's projected merger-related savings are overstated for 2004 and beyond. The Staff would allow its reduced control premium level to be recovered from ratepayers.

The ALJ did not adopt the Staff's position. Rather, he determined that overall the net benefits purported to flow to ratepayers from the merger did not eclipse the costs asked to be borne by them. In its exceptions, the Staff supports the ALJ's elimination of the control premium expense from the test year.

The Commission has reviewed Mich Con's valuation of the initial cost saving from the merger, as well as its projections of the cost savings that may occur during the 2005 test year and then on into the future. The Commission has also reviewed the Staff's arguments concerning the MCN tax losses as a necessary and proper reduction in the absolute amount of any proposed control premium. The Commission finds that the Staff's position is well-taken. The MCN tax losses have been utilized and those losses reduced DTE's tax liability thereby affording a return to DTE of value expended to acquire MCN. It would be inappropriate to permit that same amount to again be recovered through a control premium expense, and the Staff's reduced control premium

⁴⁰2 Tr. 315 through 322, and the record in Case No. U-13287.

calculation is an appropriate starting point for the Commission’s analysis of any control premium recovery.

After review of the testimony, exhibits, and arguments, the Commission is simply not persuaded that the alleged benefits flowing to Mich Con’s ratepayers outweigh the costs that Mich Con seeks to recover through the test-year control premium amortization expense—even at the Staff’s reduced level. Mich Con’s exhibits and testimony attempt to solidify the projected cost savings related to the “synergies” flowing from the combined and reduced staffs and operations of the two utilities. However, the Commission finds that the projected numbers depend upon assumptions of employee counts, labor and benefit expenses, and continued gains in employee productivity that may or may not happen. Telling is the company’s admission that much of the initial “synergy” savings was created by staff early retirements and voluntary resignations—the company states that it right-sized itself into a lean, cost-efficient utility.⁴¹ However, the employee count soon needed to increase—and in the Commission’s view, it is doubtful that the alleged cost savings will continue at the rate projected by the company. Mich Con testified that the labor force in the companies’ centralized customer service departments is higher now than it was for the total of the two companies before the merger.⁴² The Commission finds speculative the quantitative data and cost data underlying Mich Con’s projections of merger-related synergy savings.

The Commission also finds persuasive ABATE’s argument that regardless of the synergies alleged by Mich Con, the company’s controllable O&M expenses have grown in excess of the rate of inflation, which is counterintuitive to any conclusion that the merger results in net benefits to Mich Con’s ratepayers. Additionally, ratepayer benefits are not only measured in cost savings,

⁴¹2 Tr. 280.

⁴²2 Tr. 215.

they are measured in customer service quality as well. It cannot be properly argued that the transition to combined billing went smoothly; Case No. U-13287 was begun due to the deluge of complaints received by the Commission from Mich Con and Detroit Edison customers. For all of these reasons, the Commission finds that the benefits projected by Mich Con to flow to its rate-payers due to the merger of DTE and MCN do not outweigh the cost of the acquisition premium expense requested to be recovered by Mich Con in the 2005 test year. Accordingly, the Commission finds that the test year should not include such an expense.

Trufant Agreement

Mich Con's service territory extends throughout Michigan. In the lower peninsula, much of the company's market area is integrated—the service area can be served from all of Mich Con's storage, transmission, and distribution system. The Grand Rapids area is a notable exception; it is distinct from the remaining portions of Mich Con's lower peninsula service territories. Thus, that service area does not have direct access to all of the interconnections with storage fields and inter- and intrastate pipelines within the remaining Mich Con lower peninsula service area; it only interconnects with ANR Pipeline Company (ANR). Over the years, Mich Con has sought to integrate the Grand Rapids market area with the rest of the company's system.

Prior to 1990 and the significant changes to the interstate pipeline industry caused by the FERC's Order 636, Mich Con served the Grand Rapids area with natural gas that was both purchased from and delivered by ANR. Due to the lack of system integration, Mich Con had no alternative but to contract with ANR for sufficient pipeline capacity to serve the Grand Rapids area's entire design day load. However, around 1990, Mich Con determined to reduce the company's dependence on ANR (and to serve much of the Grand Rapids area load from its own northern Michigan storage fields) by integrating its Grand Rapids market with its transmission and

storage facilities located elsewhere in Michigan. This would allow Mich Con to save millions of dollars per year by reducing its high-priced daily service entitlements for gas purchased from ANR.

Mich Con's storage facilities are north of Grand Rapids, near the company's Woolfolk compressor/city gate station in Mecosta County. ANR's pipeline facilities also interconnect at that location. Mich Con's three large high-pressure transmission lines, the A, B, and C lines, run southeast from the Woolfolk station across the state's lower peninsula to the Milford compressor/city gate station in Oakland County in the Detroit metropolitan area. Those major transmission lines basically integrate Mich Con's southeast Michigan market area with much of the company's storage capabilities, and many of the company's inter- and intrastate pipeline interconnections. Mich Con noted that a new company-built transmission pipeline connecting its Grand Rapids area distribution system with the existing cross-state A, B, and C high-pressure transmission lines would achieve the system integration that the company sought. If that proposed connecting pipeline would have been built, it would have run near the Village of Trufant in Montcalm County.⁴³

However, after presenting its potential construction plan to ANR, Mich Con negotiated a firm transportation agreement with ANR to move up to 400 million cubic feet per day of the company's own gas from the Woolfolk compressor/city gate station to the Grand Rapids market area entry points. This firm transportation contract, which served as a substitute for the potential connecting pipeline because of its favorable pricing provisions, is now commonly referred to as the "paper pipeline" or the "Trufant Agreement." Pursuant to the September 25, 1991 order in Case No. U-9638, the Commission granted Mich Con's request to treat this paper pipeline in the same

⁴³The system was to be called the Grand Rapids and Sparta Pipeline, Case No. U-9497.

manner for ratemaking purposes as any utility-owned transmission pipeline. Specifically, the Commission authorized Mich Con to include the annual \$3.5 million cost of the ANR firm transportation agreement as part of the utility's base rates. The Commission's decision to treat the Trufant Agreement as if it was an actual pipeline was based on the inclusion of all present and future surcharges within the agreement's price, as well as Mich Con's ability to extend the agreement for two successive 20-year periods beyond the agreement's initial 20-year term.

Mich Con now argues that the Trufant Agreement's costs are more properly recovered within the company's annual GCR proceedings conducted pursuant to 1982 PA 304, as amended (Act 304), MCL 460.6h *et seq.* In Mich Con's view, the company ships diverse sources of gas supply under the Trufant Agreement, and the agreement is not a pipeline asset of the company subject to depreciation allowances and return on investment; thus, it does not serve a distribution function and must be recovered through the company's GCR proceedings as a gas supply-related cost.

The Staff would continue recovering the Trufant Agreement's \$3.5 million annual cost within base rates as previously authorized by the Commission. The Staff argues that the Trufant Agreement serves a purpose identical to that of the pipeline that would otherwise have been built. However, the Staff argues that any costs for short-term transportation contracts between Mich Con and ANR for the Grand Rapids market should be recovered through Mich Con's annual GCR process where those costs would be reviewed for reasonableness and prudence. In the Staff's view, a distribution-integration function is served by the Trufant Agreement; however, most, if not all, incremental load in the Grand Rapids market area is a function of increased GCR-related services⁴⁴ and recovery of those costs is proper within Mich Con's annual GCR proceedings.

⁴⁴4A Tr. 1244.

The Attorney General would continue recovering the costs of the Trufant Agreement within Mich Con's base rates. He disputes Mich Con's claim that the agreement does not perform a distribution function. In the Attorney General's view, in 1991 the Trufant Agreement was presented to the Commission as a system integration project which linked the company's then-Interstate Storage Division gas supplies with the Grand Rapids market area. Thus, the company should be kept to its prior statements and actions. Moreover, in the Attorney General's opinion, many end-use transportation customers use the Trufant Agreement capacity, not only GCR-related services, making recovery within base rates the appropriate treatment.

Additionally, the Attorney General argues that costs such as the Trufant Agreement and the incremental agreements for the Grand Rapids area discussed by the Staff cannot be recovered within Act 304 proceedings. The Attorney General argues that the Trufant Agreement, and similar such agreements, cannot qualify as gas supply activities that obtain gas as those terms are used within Section 6h(3) of Act 304, MCL 460.6h(3).

The ALJ was not persuaded by Mich Con's re-evaluation of the Trufant Agreement's function. He recommended that the agreement's cost continue to be recovered in base rates and that any incremental agreements, as described by the Staff, be included within, and reviewed within, the company's annual GCR proceedings. The Staff, the Attorney General, and ABATE support the ALJ's recommendation. Mich Con excepts.

Mich Con argues that a sound basis does not exist to deny the company's request to shift the cost recovery of the Trufant Agreement from base rates to the GCR process. In the company's view, the Trufant Agreement serves a gas supply function and as such it should properly be included within the GCR proceedings. Mich Con notes the ALJ's recommendation that incremental agreements, as described by the Staff, should be reviewed within the company's

annual GCR proceedings. The company argues that the ALJ's recommendation is too narrow; current negotiations exist to modify the Trufant Agreement and any such changes in the Trufant Agreement's costs and services should also be reviewed within the annual GCR proceedings.

The Commission is not persuaded that it should shift the cost recovery of the Trufant Agreement from base rates to Mich Con's GCR proceedings. In Case No. U-9638, the company (and ANR) contended that, rather than construct the Grand Rapids and Sparta Pipeline to integrate its system, the Trufant Agreement would provide the same system integration at a lower and stable cost.⁴⁵ Thus, in the Commission's view, Mich Con's initial request to recover the cost of the paper pipeline characterized it as a distribution integration function. Mich Con's prior characterization is proper and the Commission finds it reasonable and appropriate that the Trufant Agreement's costs should continue to be recovered in the company's base rates.

However, the Commission has reviewed the Staff's position and testimony that incremental transportation agreements to serve the Grand Rapids market will serve GCR-related load. The Commission finds the Staff's argument persuasive, and agrees with the ALJ's recommendation that incremental transportation agreements such as those characterized by the Staff are appropriately part of, reviewed in, and recovered through the GCR process. The Commission notes that the Attorney General did not except to the ALJ's recommendation regarding review of those incremental transportation agreement costs within Mich Con's GCR proceedings; however, in his brief the Attorney General argued that such costs are not appropriately part of an Act 304 proceeding. The Commission is not persuaded that such incremental transportation costs as described by the Staff do not, and cannot, form gas supply costs as those costs are understood under Act 304.

⁴⁵ See, the September 25, 1991 order in Case No. U-9638, pp. 10 - 11, and 24 - 28.

Thus, the Commission directs that those costs be included within future Mich Con GCR proceedings.

In equal measure, the Commission notes Mich Con's testimony and the statement in its exceptions that the company may modify the Trufant Agreement and then seek recovery of any changes in that agreement's costs and services through the company's GCR proceedings. In Case No. U-9638, where Mich Con sought and received recovery of the paper pipeline's costs, the Commission cautioned Mich Con that the company should remain cognizant that the Commission's rejection of the Attorney General's request to certify construction of the Grand Rapids and Sparta Pipeline was based, in great part, upon Mich Con's repeated assurances (and those of ANR) that the paper pipeline will only cost \$3.5 million per year. The Commission stressed that, in light of the company's cost assurances, it would be very difficult for Mich Con to argue for any future rate increase to recoup higher costs relating to that paper pipeline.⁴⁶ The Commission reminds Mich Con of its past assurances and of the Commission's statements regarding increased costs relating to the Trufant Agreement.

MGP and Pension Expenses

The Staff excepts to the ALJ's recommendation regarding MGP expense and ABATE excepts to the ALJ's recommendation regarding setting pension expense at zero for purposes of the 2005 test year. The Commission discussed these issues during its discussion of the appropriate working capital calculation for the test year. The Commission finds the Staff's position regarding MGP-related matters to be appropriate. The Commission finds the ALJ's recommendation regarding pension expense to be appropriate.

⁴⁶*Id.*, at p. 28.

Active Employee Health-care Costs

Mich Con argued that it incurs substantial costs for the provision of medical-related benefits for its active employees. The company included an escalation factor of 13% per year when forecasting its Other Employee Benefits Expense (OEBE) figure. The Staff's proposal combined health-care costs with other O&M expenses and then used an average inflation rate of 2.4% to escalate those costs for forecasting purposes. The ALJ recommended using the Staff's approach. He agreed with the Staff that some O&M expenses will increase at a rate higher than the 2.4% inflation factor and some O&M expenses will increase at a lower rate (or even decrease in total); thus, overall the Staff's proposal should prove appropriate. Mich Con excepts. The Staff and ABATE support the ALJ's recommendation.

Mich Con states that, in essence, the Staff projects that the company's active employee health-care costs should only increase at the overall inflation rate of 2.4%. Mich Con believes that the Staff's assumption is inaccurate. Mich Con argues that its active employee health-care costs are rapidly escalating in excess of 13% annually, and that these significant cost increases have occurred despite substantial efforts by the company to reduce health-care costs and revise its health-care programs. Mich Con states that in Consumers' recent rate case, the October 14, 2004 order in Case No. U-13730, the Commission recognized the dramatic increase in health-care costs over the recent past. The company requests that the Staff's OEBE figure be increased to account for these substantial employee health-care cost increases.

The Staff argues against a specific recognition of a higher level of active employee health-care costs. In the Staff's view, its overall O&M inflation adjustment provides ample leeway for variations in expense levels; some O&M areas will increase at a rate above the average, some at a

rate below the average, and some may decrease overall. Moreover, the Staff argues, the company will continue to achieve productivity gains that will also factor into the overall O&M equation.

The Commission understands the Staff's argument regarding the variety of items that are included in its O&M proposal. Overall, the Commission is persuaded that the Staff's view is correct—some expense areas will increase at rates above the inflation average, while some areas will increase at rates below that average, or even decrease overall. However, at the present juncture, health-care expenses do not appear to adhere to past patterns; rather, those expenses appear to be increasing at an unusual rate. The Commission has reviewed Mich Con's testimony regarding the measures that the company has taken to reign in its escalating employee medical expenses: substantial increases in employee cost-sharing and significant medical plan design changes.⁴⁷ The Commission has also reviewed the company's testimony that prescription drug coverage costs are projected to increase at 18%, medical service costs at 13%, and dental services at 5%. The Commission is persuaded that Mich Con's request to add \$3.3 million to its test-year O&M expenses for OEBE is appropriate and should be granted.⁴⁸ While the Commission is mindful that the company has done much to reduce these costs, Mich Con should continue to do all that it can to reduce or to contain increases to these costs.

Uncollectibles Expense

The ALJ recommended adoption of Mich Con's Uncollectible Expense True-up Mechanism (UETM), as modified by the Staff. Under the Staff's O&M proposal, Mich Con's uncollectibles expense level for the 2005 test year would be set at \$37.3 million, and actual uncollectibles

⁴⁷2 Tr. 264 - 265.

⁴⁸The initial increase in the Staff's proposal is \$5.6 million, which is then reduced by \$2.3 million, which is the appropriate level of employee benefits costs capitalized and transferred, resulting in a net increase in OEBE of \$3.3 million. Mich Con's Reply Brief, p. 31.

expenses would be tracked yearly by the UETM. No exception was filed to the ALJ's recommendation. The Commission finds that Mich Con's uncollectibles expense level should be set at the Staff's recommended level.

Many factors affect uncollectibles expense, including the state's economy, the price of natural gas, the absolute total amount of customer billings, and the amount of state and federal aid that is available for heating assistance. Of these factors, the single largest influence on uncollectibles expense is the cost of natural gas, which has been increasing significantly during the immediate past. The high price of natural gas, when coupled with reductions in government funding available to Mich Con's low-income customers and the significant unemployment level in Mich Con's service territories, has resulted in a large increase in uncollectible accounts. These factors are largely beyond Mich Con's control.

Because of the uncertain nature of the uncollectibles expense level, Mich Con proposed that the rates in this proceeding be set based upon the Staff's most recent projection of \$37.3 million. However, Mich Con's tariff would include the UETM to adjust for the actual level of uncollectibles expense in a given time period. On or before March 31 of each year, Mich Con would file an application as a continuation of this docket. The annual application will compare Mich Con's actual uncollectibles expense for the preceding calendar year with the base level of uncollectibles expense contained within the company's rates. Ninety percent of the difference between those amounts would be collected from, or refunded to, Mich Con's customers through a temporary surcharge or credit over the subsequent 12-month period. The surcharge or credit would be implemented by Commission order after an opportunity for hearing on the annual application.

Mich Con would remain at risk for 10% of its uncollectibles expense to provide an incentive to minimize its actual expense level. The surcharges or credits for each rate class would be calculated based upon the percentage of uncollectibles expense allocated to the rate class in the cost-of-service study utilized in the final rate design in this proceeding. (Those percentages are attached to this order as Attachment B.) The UETM would remain in effect until the Commission issues a final order in Mich Con's next general rate case.⁴⁹ The Staff supported the company's UETM, with three clarifications. Each March 31 filing must fully describe the methods used to calculate the uncollectibles expense for the preceding year, detailing any changes in methodology from the previous year, and fully explaining the reasons for any changes of methodology. The annual filing must provide in detail the calculations for the uncollectibles expense for the preceding year, along with support for all assumptions made in the uncollectibles expense calculations. Because the initial period of the UETM may be less than a full calendar year, the Staff requested that the Commission describe the method to be used to prorate the first period's over- or undercollection; the Staff would compare sales and transportation revenue for the part of the calendar year that the UETM is effective to the total sales and transportation revenue for that same calendar year. The Staff states that this method would provide a simple and fair proration for the initial less-than-calendar-year period.

Mich Con's present and likely-to-occur projected uncollectibles expense level is uncharacteristic as regards the known and measurable change standard, and highly unusual. Thus, it is appropriate to consider an increased cost level for purposes of this proceeding only. The Commission is persuaded that the UETM, as clarified by the Staff, should be implemented. The UETM should remain in effect until a final order is issued in Mich Con's next rate case. Many factors

⁴⁹4 Tr. 953 - 957.

influencing uncollectibles expense are largely beyond Mich Con's control, and the 10% factor contained within the UETM should provide an incentive to the company to contain, as much as possible, its uncollectibles expense. Because the initial March 31 UETM application will contain less than a calendar year, although it will be filed based upon a calendar year, the Commission finds appropriate the Staff's request that the Commission establish a proration method for this initial period. The Staff's proposed method is simple and straightforward; it should be adopted. Accordingly, the Commission finds that sales and transportation revenue, for the part of the calendar year that the UETM is effective, should be compared to the total sales and transportation revenue for that same calendar year, and that ratio should be used for proration of the UETM for the initial period.

In its testimony regarding uncollectibles expense, Mich Con stressed that state and federal heating assistance aid have been reduced, which has significantly increased the company's uncollectible accounts. Mich Con states that in 1993 its customers received approximately \$42 million in energy-cost assistance; but that by 2002 that figure had dropped to \$3 million due to legislative revisions in assistance programs, and this funding would be eliminated as of 2003. The company also testified that during 2002 its service territory contained 50% of the state's low-income population but that Mich Con's customers were allocated only 28% of the state's available home heating credits, which further increases pressure on the company's uncollectible accounts.⁵⁰ This testimony provides a sound basis for the UETM, but the testimony also points to a more fundamental need—a method to fund low-income energy needs, which in no small measure should assist Mich Con in its efforts to reduce the company's uncollectible accounts.

⁵⁰2 Tr. 230 - 235.

Accordingly (and inasmuch as the UETM is only authorized until the company's next general rate case), in its next general rate case filing Mich Con should propose a low-income energy efficiency funding program, the costs of which would be recovered as part of its base rate structure. While Mich Con's sister company, Detroit Edison, already has a Low-Income Energy Efficiency Fund (LIEEF) program and funding mechanism, Mich Con should propose its own program to meet the needs of the utility, which might limit the program to its service area (keeping in mind the existing LIEEF program). During Mich Con's next general rate case, the company's low-income energy efficiency proposal can be reviewed along with its then-current level of uncollectibles expense and an appropriate solution created.

Safety and Training-related O&M Expenses

While not extensively treated by the parties, safety and training-related O&M expenses comprised one area where the Staff proposed adjustments beyond those normally involved with the use of a historically based test year. The Staff projected safety and training-related O&M expenses of \$17,805,000. However, the Staff acknowledged that Mich Con had presented testimony that potential cost increases in these areas might occur that were uncharacteristic in terms of the known and measurable change standard; but, that because of the extraordinary nature of the expenses, they could be included as expenses for purposes of this case only under certain conditions. Accordingly, the Staff recommended that the Commission include an additional \$6,914,000 beyond the historically based test-year projections, and that any such additional amount be subject to refund if not expended by the utility on the safety and training-related areas.⁵¹ In his revenue calculations, the ALJ utilized the increased amount—recommending

⁵¹4A Tr. 1159 – 1161 and Exhibit S-63.

adoption of the Staff's calculations. Parties did not file exceptions to the use of the Staff's increased figure.

The Commission has reviewed the testimony regarding these uncharacteristic, increased safety and training-related O&M expenses. Steven E. Kurmas, Senior Vice President, Distribution Operations, DTE, testified regarding a number of these safety and training-related areas. He stated that the company is performing more leak repairs due to the age of Mich Con's infrastructure.⁵² Mr. Kurmas stated that training expenses had substantially increased because of the need to handle operator qualification training by Mich Con's Codes and Standards Group, an area of the company that ensures that Mich Con complies with the rules and regulations mandated by state, federal, and other regulatory authorities.⁵³ In Mich Con's view, much of this increased expense involved the federal Pipeline Safety Improvement Act of 2002, Pub. L. 107-355; 116 Stat. 2985 *et seq.*; 49 USC 60109, and the new federal Operator Qualification Rule,⁵⁴ both of which will require extensive review of the company's pipeline system and substantial training and testing of the company's personnel.

The Commission is concerned that Mich Con have the financial ability to meet these new safety and training-related costs. However, the Commission is also concerned that these amounts, which are above the known and measurable change standard, are utilized as requested by the company. Accordingly, the Commission finds that the increased safety and training-related expenses included on Exhibit S-63 are appropriate for inclusion when calculating the 2005 test year revenue requirement; and that, as proposed by the Staff, any amount not expended by the company on the safety and training-related expenses contained within the company's testimony be

⁵²2 Tr. 136 – 137.

⁵³2 Tr. 187 – 194.

⁵⁴49 CFR, Part 192, Subpart N.

refunded to the company's ratepayers. Along with its March 31 filing for the UETM, the company should file an annual report for the preceding year (or period) on the status of the various program expenditures as they relate to the level of cost recovery provided for in this order. The report should state, with particularity, the safety and training-related expenditures of the company for the appropriate time period. As part of the yearly UETM review, the Commission will review the company's safety and training-related expense filing. Should that filing indicate that a refund is due to Mich Con's ratepayers, then the Commission may order an appropriate refund at that time.

Net Operating Income Conclusion

Based upon the foregoing discussion, the Commission finds that Mich Con's adjusted net operating income for the 2005 test year is \$97,461,000. This figure is computed as follows:

	<u>Gross (\$000)</u>	<u>Net (\$000)</u>
Staff's Adjusted Net Operating Income		87,289
Other Operating Revenue Adjustments:		
Load Balancing Charge Revenue	(1,200)	(760)
Unauthorized Gas Usage Revenue	(1,800)	(1,140)
Control Premium Adjustment	20,071	12,709
Employee Incentive Program Adjustment	2,266	1,463
Health Care Adjustment	(3,322)	(2,144)
<i>Pro Forma</i> Tax Savings Adjustment	44	<u>44</u>
Adjusted Net Operating Income		<u>\$97,461</u>

VIII.

REVENUE DEFICIENCY

Having determined Mich Con's 2005 test year rate base, overall rate of return, and adjusted net operating income, the Commission finds that the company has a revenue deficiency of \$60,756,000 for the 2005 test year. This revenue deficiency is calculated as follows:

Rate Base	\$1,889,924,000
Overall Rate of Return	<u>7.19%</u>
Income Required	\$ 135,931,000
Less: Adjusted Net Operating Income	<u>(97,461,000)</u>
Income Deficiency	\$ 38,470,000
Revenue Multiplier	<u>1.5793</u>
Revenue Deficiency	\$ <u>60,756,000</u>

IX.

RATE DESIGN AND TARIFF REVISIONS

The ALJ recommended that the Staff's proposed cost allocation, as set forth on the Staff's Exhibit S-54, should be utilized to allocate the test-year revenue requirement to the various rate classes, with two revisions. First, the ALJ recommended adopting Mich Con's proposed method of allocating costs relating to intangible plant and revenues arising from contract home services. Second, final costs should be allocated in such a way that Rate 10 customers' rates will not be changed. Parties did not file exceptions to the ALJ's cost allocation recommendation, and the Commission finds that it should be adopted.

Beyond cost allocation, the ALJ recommended adoption of many uncontested tariff revisions, as well as the Staff's proposed changes to the company's tariff to bring it more in line with the format used by Consumers. Mich Con, Lakeshore, and ABATE filed exceptions to certain of the ALJ's tariff recommendations that primarily concern transportation matters. All of these are discussed below.

Miscellaneous Tariff Revisions

Kenneth L. Slater, Manager, Case Litigation, Regulatory Affairs, Mich Con, proposed certain miscellaneous changes to the company's tariff. The Staff also proposed miscellaneous changes to

the company's tariff regarding combining certain rate classes and reformatting the tariff. Those changes were not opposed by any party, and the ALJ recommended that the revisions be authorized. The Commission finds that the following tariff changes should be authorized.

- 1) Elimination of Rate Schedule 3, Senior Citizen Rate. Customers currently under this rate would be transferred to Rate Schedule 3A, Low Income Senior Citizen Spaceheating Rate.
- 2) Elimination of Rate Schedule 8, Alternate Fuel Displacement Rate. There are no customers currently taking service under this rate.
- 3) Revisions to Rate Schedule 3A lowering the age requirement.
- 4) Rate Schedules 1 and 6 will be offered under the General Service Rate Schedule, which will be designated as Rate GS-1 and Rate GS-2, respectively.
- 5) Elimination of the "Conservation of Natural Gas – Insulation" section of the sales rate tariffs. (In the company's view, such standards are now governed by the state building code and local ordinances.)
- 6) The sales tariffs will be reformatted and revised to make them more consistent with the tariff style approved for Consumers in Case No. U-13000.
- 7) The transportation tariffs would be reformatted into a single section with three price categories—ST, LT, and XLT.
- 8) The revision to the non-sufficient funds (NSF) charge in Section B6.3., increasing it from \$5 to \$15.
- 9) The revision to the reconnect charge under Section B6.7 to support the proposed test-year revenue, to revise various cut-and-cap and restoration-of-service charges, and to include an on-premise bill collection charge.
- 10) The revision to the gas service turn-on charge, Section B6.7(D).
- 11) The revision to Section B12 "Customer Attachment Program" to reflect the specific carrying cost rate of 9.46% and the discount rate of 8.79% approved in this proceeding.
- 12) The elimination of the filing requirement for the paper copy of the monthly rate summary.
- 13) The various miscellaneous or minor changes to the tariff contained on Exhibit A-11, Schedule F-7, which are intended to update and enhance the tariff for clarity, efficiency, and ease of administration for customers, marketers, Mich Con, and the Staff.

The company also proposed changes to off-system transportation and contract storage tariffs, which would, among other things, provide for separate TOS-F, TOS-I, CS-F, and CS-I tariffs, distinguish service by length of time, eliminate an administrative fee, and revise notice language. The Commission has reviewed those revisions and additions, and finds them appropriate.

The ALJ recommended discontinuance of Mich Con's 90/10 refund mechanism. Pursuant to that mechanism, Mich Con has refunded to its GCR customers 90% of its annual storage revenues that are in excess of the level included within its present rate structure. Because of changes in the off-system storage market, Mich Con stated that the program was no longer useful; the Staff agreed. Parties did not file exceptions to the ALJ's recommendation. After review of the testimony and arguments, the Commission agrees with the ALJ, and the 90/10 mechanism should be discontinued.

Aggregated Accounts Gas-In-Kind (GIK) Charge

A GIK charge is assessed to an end-use transportation agreement as part of the transportation rate structure. The charge is expressed as a percentage of the gas volume delivered for transportation that will be retained by Mich Con to reimburse the company for lost-and-unaccounted-for (L&U) gas and for company-use gas (compressor fuel, facility heating, *etc.*). The ALJ recommended that the GIK charge be set at 1.42% as proposed by the Staff. No party excepted to that recommendation, and the Commission finds that the GIK charge should be set at the Staff's recommended 1.42% level.

Mich Con's tariffs allow the aggregation of a number of accounts for billing purposes. The aggregation of accounts works well for Mich Con's ratepayers—a single bill, pooling of storage injection and withdrawal entitlements, *etc.* The aggregation tariff has been in effect for some time. However, Lakeshore pointed to one anomaly that occurs when a gas sales account is aggregated

with a master transportation account. Lakeshore explains that the standard transportation GIK charge is assessed against all of the volumes on the aggregated statement although the sales distribution charge (which is also assessed against the aggregated gas sales volumes) already includes an allowance for L&U gas and for company-use gas. Therefore, Lakeshore argues, the aggregated gas sales volumes are effectively charged twice for L&U and company-use gas. Lakeshore would remove the GIK charge for any sales volumes that are aggregated with a master end-use transportation account.

The ALJ noted that allowing the GIK charge to be assessed to aggregated gas sales volumes basically assesses responsibility twice for L&U gas and company-use gas. He recommended adoption of Lakeshore's position. The Staff, Lakeshore, and ABATE support the ALJ's recommendation. Mich Con excepts.

Mich Con argues that the imposition of the GIK charge on aggregated sales volumes is appropriate because of the many benefits that aggregation provides to the master account holder. In Mich Con's view, if the additional cost represented by the sales volume GIK charge outweighs the aggregation benefits the account holder receives, then the account holder does not have to aggregate sales volumes. Mich Con states that it cannot remove the GIK charge from sales volumes aggregated in a master account and maintain the benefits of non-contiguous account aggregation. Mich Con states that the GIK charge is applied to all gas receipts delivered to Mich Con for a transportation account; to remove the GIK charge would require each subsidiary account to be nominated and controlled separately thereby eliminating the convenience that aggregation provides.

The Commission is concerned that sales volumes should not twice bear L&U gas and company-use gas costs. Accordingly, the Commission finds that the GIK charge should not be

assessed against sales volumes that are aggregated under a master transportation account. While the Commission understands Mich Con's argument that its present system does not easily permit non-application of the GIK charge to aggregated sales volumes, the problem is one that Mich Con is aware of and has had to adjust for. George H. Chapel, Mich Con's Manager, Market Forecasting, testified that in order to establish proper sales volume levels for the 2002 historical base year, he had to separate aggregated sales volumes from their associated transportation contracts and then reclassify those volumes as gas sales where revenues attributable to those volumes should have been included.⁵⁵ Thus, this anomaly is one that will continually plague Mich Con's sales volume record keeping, and it should be remedied. Such a remedy will eliminate a recurring (and automatic) error in sales volume records and will also eliminate the unreasonable double-collecting of L&U gas and company-use gas responsibility from sales volumes aggregated with master transportation accounts.

One other matter concerns the GIK charge. Mich Con's tariff contains a load balancing storage rate. Basically, this rate is a penalty to deter storage in excess of authorized levels. The charge is 25¢ per Mcf, plus fuel for injection (the GIK charge), for the storage of any month-end balance of gas that exceeds 10% of the customer's annual contract quantity. Lakeshore argues that the 25¢-per-Mcf charge may be appropriate, but that the imposition of another injection fuel charge (the GIK charge) is improper given that Mich Con is not actually injecting more gas into storage (and thus using compressor fuel), the utility is merely keeping in storage that which was already injected. ABATE supports Lakeshore.

Mich Con responds that the load balancing storage rate is not designed as a revenue producing product. Rather, it is a penalty to deter certain behavior, the unauthorized storage of gas in excess

⁵⁵2 Tr. 50.

of authorized levels. Consequently, the company argues, the rate should be set at the maximum price Mich Con has available to charge for contract storage, which includes the GIK charge. To charge a differing rate may not deter the improper behavior.

The Commission is persuaded that the load balancing storage rate should remain as proposed by Mich Con. The rate is not designed as a product; rather, it is designed to deter unauthorized storage of gas. In the Commission's view, EUT customers must manage their gas receipts and deliveries; this is part of an EUT customer's responsibility, and the EUT tariff already includes significant storage to allow that EUT customer substantial flexibility. Penalties may be avoided by proper management of gas transportation, and those penalties should be set at a high enough level to deter improper activity. Accordingly, Mich Con's proposal should be authorized.

Monthly Administrative Fee for Aggregated Accounts

Mich Con proposed adding a \$105 monthly fee to cover costs associated with the administration of the company's Rule D3.3 (B) Master Account, which provides for the aggregation of transportation customers' accounts. The ALJ agreed with Lakeshore's opposition to the new charge, stating that an insufficient basis had been presented to impose the additional \$105 monthly administrative fee.⁵⁶ The Commission agrees with the ALJ, and finds that the monthly customer charges established in this proceeding furnish adequate revenue to defray Mich Con's total cost of providing EUT service, including costs associated with administering the aggregation of accounts. This is not a new service; thus, the costs are embedded and are part of those costs already included within transportation customers' rates.

⁵⁶PFD, p. 97.

Annual Contract Quantity and Maximum Daily Quantity Calculations

Mich Con proposed revisions in the method by which an EUT customer's annual contract quantity (ACQ) and maximum daily quantity (MDQ) calculations are performed. The ACQ and the MDQ relate to the various volumes—daily and annual—that may flow under a transportation contract. The establishment of the precise level for the ACQ and the MDQ is very important for the EUT customer. Lakeshore presented its own proposals regarding the ACQ and MDQ tariff provisions, and ABATE supported Lakeshore.

The ALJ reviewed the proposals and recommended that, overall, Mich Con's proposed method of calculating an EUT customer's ACQ and MDQ is preferable to that suggested by Lakeshore. However, the ALJ was persuaded by Lakeshore's argument that allowing Mich Con to set the ACQ and MDQ levels in the company's sole discretion was unwise. In the ALJ's view, while Mich Con's testimony discussed the factors that the company would consider when setting the ACQ and MDQ levels, the lack of such objective criteria within the tariff itself would permit the company to act in a capricious manner, if it so chose. The ALJ recommended adoption of Lakeshore's proposed tariff language, under which Mich Con would use its best efforts to ensure that a customer's ACQ and MDQ are reflective of that customer's annual consumption and maximum daily consumption. In the ALJ's view, this would provide a standard by which Mich Con's actions could be reviewed. Mich Con excepts to the ALJ's recommendation. Lakeshore and ABATE support the recommendation.

Mich Con argues that, because it is the system operator, the company must maintain "sole discretion" to establish just and reasonable service terms with all customers to ensure safe, reliable, and cost-effective gas procurement opportunities. Mich Con states that when using its sole discretion to establish the ACQ and MDQ levels, the company works with customers to

establish an appropriate figure, that the company understands that it must create reasonable figures, and that the company does not arbitrarily pick and choose—it must have some reason for its action.

Lakeshore argues that the ALJ's recommendation simply places within the tariff that which Mich Con has stated is the company's existing practice. Lakeshore states that Mich Con's proposed tariff, when taken at face value, allows the company to adjust an ACQ or an MDQ to any level the company desires for any reason, while the company's testimony explains that it will do so only for good reasons. Lakeshore states that the language it proposed, and the ALJ recommended, eliminates any ambiguity regarding Mich Con's use of its discretion in setting an ACQ or an MDQ. Lakeshore states that its proposal only requires that Mich Con use its "best efforts" and provide EUT customers "reasonable opportunities," which simply provides a standard by which Mich Con's action can be reviewed. ABATE supports Lakeshore, arguing that the revised language provides Mich Con with discretion, but in a suitable context to review that company's actions when establishing an ACQ or an MDQ.

The Commission finds that Lakeshore's proposed language should be adopted. Mich Con testified that when exercising its discretion, it does so only for valid reasons. The language proposed by Lakeshore and recommended by the ALJ provides a standard by which Mich Con's actions when setting an ACQ or an MDQ may be evaluated. Moreover, as pointed out by Lakeshore, the language merely memorializes Mich Con's existing practice as explained in its testimony.

As part of his recommendation regarding the MDQ definition, the ALJ accepted Mich Con's language, which restricts the MDQ of EUT customers during the months of September and October. According to Mich Con's witness, Mr. McCrackin, the months of September and

October are critical to procuring and storing gas for the company's GCR customers; the limitation on MDQ for those two months provides Mich Con the necessary flexibility regarding storage injections during that period. Lakeshore excepts to the ALJ's acceptance of the two-month limitation. ABATE supports Lakeshore.

Lakeshore argues that EUT customers must have the same flexibility to use the Mich Con system as do GCR customers. In Lakeshore's view, EUT customers and GCR customers pay equally for use of the system and, thus, EUT customers must have exactly the same service. Additionally, Lakeshore argues that Mich Con did not present financial studies to support its storage injection-related argument.

Mich Con responds that EUT customers and GCR customers do not pay equally for use of the company's system. Rather, EUT customers are allocated storage costs in accordance with their peak day requirement, which is lower than the GCR customers' peak day requirement. GCR customers pay for much more storage within their distribution rate than do EUT customers. Moreover, the company argues, Mich Con has storage injection operational characteristics during September and October that are critical to procuring and storing gas for the company's GCR customers. Because of this, the company states, the ALJ's recommendation is appropriate.

The Staff supports Mich Con's argument. The Staff states that EUT customers and GCR customers are distinct and separate customer classes, each with its own allocation of services and costs through separate cost-of-service studies. In the Staff's view, GCR customers do not have flexibility in how much gas is delivered to Mich Con for injection into storage—they must depend upon Mich Con to plan for their peak day needs. EUT customers, however, regulate their own purchases and needs. In the Staff's view, the September and October MDQ limitations are appropriate and reasonable as a means for Mich Con to plan and to control its system needs.

The Commission is persuaded that Mich Con's proposed MDQ limitation for the months of September and October is appropriate. GCR customers have little, if any, control over gas purchasing for their peak needs. And, the GCR customers have been allocated significant costs related to storage—much higher than EUT customers. Mich Con must be given the necessary tools to serve this distinct customer class. Accordingly, the tariff should contain Mich Con's proposed MDQ limitation for the months of September and October.

Economic Break-even Points for Transportation Rates

In his PFD, the ALJ recommended adoption of the Staff's position regarding Mich Con's EUT tariff structure. Under the structure, the three forms of EUT available on Mich Con's system, ST, LT, and XLT, would be combined into a single transportation tariff. Then, economic break-even points would be used to separate customers into each class under the single tariff. While each class would have a cost-based rate established for it, an optional rate for each class would allow for negotiated rates within a Commission-approved range of rates. Accordingly, ST-1 would be the cost-based rate, ST-2 would be the optional negotiated rate, LT-1 would be the cost-based rate, and so forth. Each of the various rates was designed using all of the cost-data for the 2005 test year. Thus, the lower revenue level caused by the creation of Rate XLT is accounted for by the Staff's cost-of-service calculations. The Commission finds appropriate the ALJ's recommendation to utilize the Staff's single tariff structure with various classes under that tariff.

Exceptions have been raised about specific language to be utilized within the EUT tariff. However, one effect of the creation of the single tariff and the addition of Rate XLT is the establishment of various transportation rates defined only by economic break-even points, which of necessity would require that customers be given notice of this substantial shift so that they can migrate to the appropriate new rate category that best suits their pattern of gas consumption. The

ALJ recommended that Mich Con provide each EUT customer with notice of the new economic break-even points of the revised and changed tariff. The ALJ also recommended that Mich Con notify each customer that the customer could then move to the appropriate rate within 30 days of notification. Mich Con excepts. Lakeshore supports Mich Con. The Staff supports the ALJ. ABATE supports the ALJ and the Staff.

Mich Con states that it generally agrees with the ALJ's suggestion. However, the company argues that the ability to migrate to a different rate category should only be made available to existing customers paying standard rates, Rate Schedules 1, 6, 10, ST-1, and LT-2. The company states that negotiated rate, discounted customers should be kept to the rates and terms of their discounted service agreements. In the company's view, the discounted service agreements were negotiated under certain economic assumptions and conditions, such as to recover facility investment costs; those customers should be held to their commitments. Lakeshore supports Mich Con, arguing that Mich Con's request is a recognition that the negotiated discounted rates incorporate factors unique to their respective contracts.

The Staff argues that all EUT customers must be allowed to choose the new rate that is in their economic best interest. In the Staff's view, the rate design it proposed (and the ALJ adopted) accounts for all revenues and costs for the 2005 test year. That rate design considers all customers, costs, and projected revenues. If certain existing customers are not allowed to migrate to the appropriate new rate (and will, therefore, pay higher rates than they would have under the revised rate design), Mich Con effectively will receive additional rate relief above that provided for in the test-year rate design and that test year's revenue calculations. ABATE supports the Staff's position.

The Commission is persuaded that the ALJ's recommendation is appropriate and should be implemented. While the Commission understands Mich Con's argument that facility costs may have driven discounted rate negotiations, all appropriate utility plant has now been included in the test-year rate base. And, as argued by the Staff, the number of customers, volumes related to each class, and associated revenues have been established such that the 2005 test year rate design provides Mich Con a reasonable opportunity to achieve the projected revenue results. To permit rates to exist that are different than those assumed for the test year is not proper and reasonable. Thus, Mich Con should notify each of its EUT customers of the economic break-even points of the new and revised transportation rates. Then within 30 days of that notification, those customers may migrate to the appropriate rate.

Rate XLT Remote Metering

Remote metering permits Mich Con and EUT customers to monitor metered consumption on a daily basis—more frequently if Mich Con desires. Mich Con acknowledged that some of its EUT accounts do have remote metering—those customers had requested the service and Mich Con made arrangements to provide the requested service. As part of the creation of the new Rate XLT, which covers volumes of 700,000 Mcf per year and above, the Staff proposed that each of the Rate XLT accounts have remote metering. The ALJ recommended that the Staff's position be adopted. Mich Con excepts, supported by ABATE. The Staff supports the ALJ's recommendation.

Mich Con states that it would support a voluntary remote meter policy that would be available to all non-residential rate schedules. Under Mich Con's proposal, customers choosing voluntary electronic metering would: 1) reimburse Mich Con for its actual costs for equipment and installation through an up-front reimbursement payment; 2) provide a telecommunications line and

service to Mich Con at the customer's expense; 3) pay a monthly service fee of \$25 per meter; and 4) sign a service contract. In return, Mich Con will provide meter consumption data on a daily basis.⁵⁷ Mich Con does not support a mandatory remote metering program for Rate XLT customers. The company argues that many of those customers have meters aggregated into the main account; to remotely monitor all of these smaller meters will be burdensome and very expensive for the customers. ABATE supports Mich Con's voluntary program, and does not support the mandatory use of remote metering for Rate XLT customers.

The Staff responds that Mich Con's testimony indicates that there are, at most, 20 Rate XLT customers. The Staff notes that some large aggregated master accounts may have dozens of smaller subsidiary accounts. However, the Staff states, its proposal for remote metering covers only the meter subject to the Rate XLT monthly customer charge—\$11,350, as proposed by the Staff. Therefore, the Staff argues, Mich Con's concern regarding the need to remotely meter significant numbers of small meters is not well-founded. In the Staff's view, the remote metering of approximately 20 Rate XLT accounts is a pilot program that can be easily adjusted from time-to-time to accommodate the experience achieved from the program. Because of the absolute size of the monthly charge and monthly volumes associated with Rate XLT customers, the Staff does not believe that its \$100-per-month charge is economically burdensome for Rate XLT customers.

The Commission is persuaded that the Staff's proposal to remotely meter those accounts to which the monthly Rate XLT charge applies is a proper first step as a pilot program. Because this remote electronic metering will attach only to those meters to which the monthly Rate XLT charge applies, Mich Con's concern that hundreds of subsidiary accounts will be involved is eliminated. Accordingly, the Staff's proposal regarding Rate XLT accounts should be implemented. While

⁵⁷4 Tr. 793 - 794.

Mich Con has proposed certain conditions for its voluntary program (including the provision of telecommunications lines and service contracts), the Commission is not persuaded that those terms should apply to the Rate XLT pilot program. Thus, Mich Con should provide all necessary remote metering facilities for the \$100-per-month charge.

After reviewing Mich Con's proposal for a voluntary remote metering program, the Commission is persuaded that it should also be implemented. That voluntary program will apply to all non-residential rate schedules, other than Rate XLT. It may well be that after the Rate XLT pilot program becomes operational, other customers (or other subsidiary meter accounts) may desire the benefits of remote metering. However, Mich Con has indicated that some customers have already implemented remote metering under agreements with Mich Con. The Commission is persuaded that those existing relationships should be maintained, and that those existing remote metering arrangements should be grandfathered under the new programs.

EUT Annual Volume Commitment

As part of the company's proposed negotiated Rate XLT tariff, Mich Con included a volume commitment provision under which the EUT customer guaranteed that it would move a minimum annual quantity of natural gas under its transportation contract. If the minimum annual volume was not transported, then Mich Con would bill the EUT customer for the balance—the minimum annual amount less the actual volumes billed to and paid by the EUT customer. Consequently, each Rate XLT agreement would automatically have a minimum annual volume commitment.

The Staff removed the requirement, and then included Rate XLT as part of its combined EUT tariff; Rate XLT is now one of the various levels of the general EUT tariff. In the Staff's view, the language of the EUT tariff provides sufficient flexibility for Mich Con to negotiate terms and conditions of service in exchange for rate discounts. The Staff argues that its proposed unified

tariff and its language allow Mich Con to tailor service provisions to an individual customer's needs and situation. The Staff states that should a customer need more than standard load balancing, then Mich Con can negotiate to increase that service, or should a customer desire a lower rate and be willing to accept a reduction in services or minimum volumetric levels, then the company may negotiate for that. The only caveat, the Staff states, is that the final rate charged cannot exceed the maximum allowed under the tariff. ABATE supports the Staff's position, arguing that the minimum annual volume commitment would virtually guarantee all Rate XLT revenue to the company.

The ALJ agreed with the Staff and with ABATE regarding the tariff language; he recommended that a minimum annual volume commitment not be automatically included within each transportation contract. Mich Con excepts. The Staff and ABATE support the ALJ.

Mich Con argues that without the minimum volume language, the company's incentive to offer a discounted rate to a customer will be severely limited, if not eliminated. In the company's view, Mich Con has historically used minimum volume commitments to insure recovery of large investments in facilities. Rather than make a large, up-front payment for those facilities, many customers have chosen to make annual volume commitments. Mich Con argues that without a minimum annual volume commitment, it will require all facilities to be paid for up-front, and will not accommodate requests from customers for reimbursement over multi-year, fixed-rate contracts.

The Staff responds that an annual volume commitment can be an element of the service agreement between Mich Con and the EUT customer—it just must be a product of negotiation between those parties. The Staff argues that its proposed tariff and language allows Mich Con to negotiate on a customer-by-customer basis for a rate and for various service provisions. If a

customer chooses to pay for facilities by way of a long-term volume commitment rather than by an up-front fee, then nothing in the tariff prohibits that negotiated arrangement. ABATE argues that Mich Con's proposed minimum annual volume commitment may make gas transportation more costly and should not be allowed.

The Commission has reviewed Mich Con's proposed tariff language and that proposed by the Staff. The Commission finds the Staff's tariff and its language preferable. In the Commission's view, the Staff's proposal allows a minimum annual volume commitment, albeit a negotiated one rather than a mandatory one. Thus, Mich Con can accomplish all that it seeks through reasonable negotiations under the Staff's proposed tariff. The Commission is concerned with Mich Con's statement that without a mandatory requirement for minimum guaranteed volumes the company will refuse to negotiate concerning facility reimbursement situations.⁵⁸ The Commission believes that Mich Con is concerned that the company may not employ a minimum annual volume commitment without explicit tariff language stating so. As explained by the Staff, its proposed language allows the company to negotiate the terms and services of its discounted EUT agreements—such as minimum volume commitments in exchange for facility enhancements, as long as the final rate charged does not exceed the maximum allowed under the tariff. Accordingly, Mich Con can achieve its minimum annual volume goal through the negotiation process, and any failure to negotiate in a reasonable, good-faith manner may be reviewed in the Commission's complaint process. The Commission finds that the Staff's proposed EUT tariff language should be adopted.

⁵⁸Mich Con's exceptions, p. 53.

Storage Service Proposals

Lakeshore presented four proposals regarding storage services for EUT customers. In Lakeshore's opinion, each of these proposals will help EUT customers avoid incurring excess storage charges. Lakeshore proposed: 1) establishing a storage balance transfer program identical to that offered by Consumers; 2) allowing Mich Con the option of purchasing excess stored gas from a customer at a pre-determined market price; 3) establishing a program similar to that of Consumers, with a few differences, under which EUT customers would be able to purchase additional, or sell back unneeded, storage; and 4) reallocating to EUT customers 12 to 15 Bcf of lower-quality storage capacity that Mich Con expects to be available during the winter of 2005-2006. ABATE supported Lakeshore, and the Staff favored adopting a storage transfer program similar to Consumers as well as allowing Mich Con to purchase excess storage gas when the utility determined to do so. Mich Con agreed to implement a storage transfer program similar to Consumers, but stressed that the company should not be compelled to buy gas (or storage) that it might not need and at pre-determined prices. Additionally, Mich Con did not favor assigning the 12 to 15 Bcf of lower-quality storage to EUT customers.

The ALJ recommended adopting Lakeshore's proposals, with two modifications. He found appropriate a storage transfer program similar to Consumers, and he believed that Mich Con should be able to purchase excess storage gas—but under the terms and language proposed by Mich Con. Additionally, the ALJ determined that Mich Con should implement a program, similar to Consumers, under which EUT customers could purchase additional, or sell back unneeded, storage to the utility; and that the 12 to 15 Bcf of lower-quality storage should be assigned to EUT customers as proposed by Lakeshore. Mich Con excepts to the ALJ's recommendation regarding

the 12 to 15 Bcf of lower-quality storage and the buy additional/sell unneeded storage proposals. ABATE supports the ALJ's entire recommendation regarding Lakeshore's proposals.

Mich Con would not reallocate the 12 to 15 Bcf of lower-quality storage to EUT customers, nor would it implement the buy/sell proposal. The company argues that it has agreed to the Consumers-type storage transfer program and that the utility may purchase excess storage gas at its sole discretion at a negotiated price. However, the company argues that it is inappropriate to require the company to repurchase unneeded storage at a predetermined price and that if the 12 to 15 Bcf of storage is reallocated, then the company's test-year revenue requirement must be revised.

The company states that the ALJ's revenue requirement calculation includes an annual revenue amount of \$10.7 million from off-system storage, which represents the revenue to be received from the sale of the 12 to 15 Bcf of excess storage. If that storage is reassigned to EUT customers, then that revenue will not be available to Mich Con and its revenue deficiency must be revised upward to recover this cost. Moreover, the shift of storage capacity and cost responsibility will require a change to Mich Con's cost allocations. Mich Con argues that there is little record support for this shift of \$10.7 million in cost responsibility.

Additionally, the company states, its proposed 18¢ per Mcf rate for the excess storage was based upon a projected revenue of \$5.7 million for the test year, which was discarded by the ALJ when he adopted the \$10.7 million figure. Consequently, the 18¢ per Mcf figure is not correct. In the company's view, EUT customers may always purchase additional storage under the existing tariffs, and it is inappropriate to force the company to repurchase storage that it has already sold.

Lakeshore responds that its proposed programs regarding the sale of unneeded storage and the reallocation of excess storage are appropriate. In Lakeshore's view, the company's discussion of

off-system storage revenues included within the company's revenue requirement and the shifting of cost responsibility are new issues that have been raised in Mich Con's exceptions. Accordingly, the exception should be rejected. Moreover, Lakeshore states, the company's witness, Mr. McCrackin, introduced the 18¢ per Mcf figure as his best estimate of what the company might expect to receive for lower-quality storage. Lakeshore argues that by reallocating the excess lower-quality storage to EUT customers, Mich Con will be relieved of the need (and the related costs) to market the additional storage. ABATE supports Lakeshore.

The Commission has reviewed Lakeshore's proposals and arguments. The Commission is persuaded that the ALJ's first two recommendations are appropriate. Mich Con should implement a storage transfer program similar to that of Consumers. Mich Con should also be able to purchase excess storage gas pursuant to the language that the company has proposed. However, the Commission is not persuaded that the company should be forced to repurchase storage nor that the 12 to 15 Bcf of lower-quality storage is appropriately allocated to EUT customers. Under the company's existing tariffs, EUT customers may purchase additional storage. The reallocation of the 12 to 15 Bcf of lower-quality storage to EUT customers will cause costs for that storage service to be reassigned and necessitate a revision in expected revenues. The Commission does not believe that the present record provides sufficient support for this significant shift in storage responsibility. Accordingly, Lakeshore's third and fourth proposals are rejected.

Conclusion

For the foregoing reasons, the Commission finds that Mich Con should be authorized to increase its annual gas revenues by \$60,756,000 and to revise its tariffs as provided for within this opinion and order. Any exceptions or positions of the parties that have not been specifically

reviewed and discussed within this opinion and order have been fully considered by the Commission and have been rejected.

The Commission FINDS that:

a. Jurisdiction is pursuant to 1909 PA 106, as amended, MCL 460.551 *et seq.*; 1919 PA 419, as amended, MCL 460.51 *et seq.*; 1939 PA 3, as amended, MCL 460.1 *et seq.*; 1969 PA 306, as amended, MCL 24.201 *et seq.*; and the Commission's Rules of Practice and Procedure, as amended, 1999 AC, R 460.17101 *et seq.*

b. Mich Con should be authorized to increase its annual gas revenues by \$60,756,000 for service rendered on and after the day following the issuance of this opinion and order.

c. The September 21, 2004 interim order should be rescinded, and the bond provided by Mich Con in support of that order should be canceled.

d. Mich Con should be granted accounting authority to accrue a regulatory liability for any negative pension costs incurred after the date of this order.

e. For the 2005 test year, Mich Con's net utility plant is \$1,269,920,000, its working capital is \$620,004,000, and its rate base is \$1,889,924,000.

f. The MGP amortization and deferral procedure authorized for Mich Con should be modified such that third-party recoveries should now offset MGP costs, and when such an offset cannot occur, then the amortization period for the third-party recoveries should be suspended.

g. A permanent capital structure of 50% common equity and 50% long-term debt for Mich Con is a reasonable proxy for use when establishing rates for the test year; Mich Con's permanent capital is \$860,937,000 in common equity and an equal amount of long-term debt.

h. For the 2005 test year, Mich Con's appropriate short-term debt level is \$112,704,000; customer deposit level is \$9,567,000; Other Interest Bearing Credits level is \$25,349,000; deferred

investment tax credits level is \$657,000; deferred federal income tax level is \$301,447,000; and job development income tax credits level is \$18,682,000.

i. For the 2005 test year, the following are appropriate for Mich Con: a cost of common equity rate of 11%; a long-term debt rate of 6.57%; a cost of short-term debt rate of 3.10%; a cost of customer deposits rate of 8.79%; a cost of Other Interest Bearing Credits rate of 1.15%; and an overall rate of return of 7.19%.

j. The Staff test-year projections of 1,231,119 sales customers, 758 EUT customers, sales volumes of 195.5 Bcf, and transportation volumes of 138.7 Bcf are appropriate and should be utilized for 2005 test year purposes.

k. The depreciation accrual rates proposed by the Staff and contained within Exhibit S-50, column 13, should be implemented by Mich Con.

l. Within 90 days after the issuance of the Commission's order in Case No. U-14292, Mich Con should file a case to revise its depreciation accrual rates, including a mechanism to incorporate any revised depreciation accrual rates within the company's general gas service rates, as determined to be appropriate by the Commission within that later proceeding.

m. The UETM, as clarified by the Staff, should be implemented, and should remain in effect until a final order is issued in Mich Con's next general rate case; Mich Con should make the necessary UETM filings on or before March 31 of each calendar year. For the initial March 31 UETM application, the sales and transportation revenue, for the part of the calendar year that the UETM is effective, should be compared to the total sales and transportation revenue for that same calendar year, and the resulting ratio should be used to prorate the UETM for the initial period.

n. Mich Con should propose a low-income energy efficiency funding program in its next general rate case filing, the costs of which would be recovered as part of its base rate structure.

o. The increased safety related expenses included on Exhibit S-63 are appropriate, and, as proposed by the Staff, any amount not expended by the company on the safety and training-related expenses contained within the company's testimony should be refunded to the company's ratepayers. Along with its March 31 filing for the UETM, the company should file an annual report for the preceding year (or period) on the status of the various program expenditures as they relate to the level of cost recovery provided for in this opinion and order. The report should state, with particularity, the safety and training-related expenditures of the company for the appropriate time period. As part of the yearly UETM review, the Commission will review the company's safety and training-related expense filing. Should that filing indicate that a refund is due to Mich Con's ratepayers, then the Commission may order an appropriate refund at that time.

p. Mich Con's 90/10 refund mechanism regarding storage revenues should be discontinued.

THEREFORE, IT IS ORDERED that:

A. Michigan Consolidated Gas Company is authorized to increase its annual gas revenues by \$60,756,000 for service rendered on and after the day following issuance of this opinion and order.

B. The September 21, 2004 order in this proceeding granting partial and immediate rate relief in the annual amount of \$35,311,000 is rescinded for service rendered on and after the day following issuance of this order, and the bond provided by Michigan Consolidated Gas Company in support of that order is canceled.

C. Michigan Consolidated Gas Company is granted all necessary accounting authority to record a regulatory liability for any negative pension costs incurred after the date of this order.

D. The manufactured gas plant remediation amortization and deferral procedure authorized for Michigan Consolidated Gas Company is modified such that third-party recoveries shall now

offset manufactured gas plant remediation costs, and when such an offset cannot occur, then the amortization period for the third-party recoveries shall be suspended.

E. The depreciation accrual rates contained within Exhibit S-50, column 13, of this proceeding shall be implemented by Michigan Consolidated Gas Company on and after the day following issuance of this opinion and order.

F. Within 90 days after the issuance of the Commission's order in Case No. U-14292, Michigan Consolidated Gas Company shall file a case to revise its depreciation accrual rates, including a mechanism to incorporate any revised depreciation accrual rates within the company's general gas service rates, as determined to be appropriate by the Commission within that later proceeding.

G. The Uncollectible Expense True-up Mechanism, as clarified by the Commission Staff, shall be implemented, and shall remain in effect until a final order is issued in Michigan Consolidated Gas Company's next general rate case; Michigan Consolidated Gas Company shall make the necessary Uncollectible Expense True-up Mechanism filings on or before March 31 of each calendar year. For the initial March 31 Uncollectible Expense True-up Mechanism application, the sales and transportation revenue, for the part of the calendar year that the mechanism is effective, shall be compared to the total sales and transportation revenue for that same calendar year, and the resulting ratio shall be used to prorate the mechanism for the initial period.

H. Michigan Consolidated Gas Company shall propose a low-income energy efficiency funding program in its next general rate case filing, the costs of which shall be recovered as part of the company's base rate structure.

I. Along with its March 31 filing for the Uncollectible Expense True-up Mechanism, Michigan Consolidated Gas Company shall file an annual report for the preceding year (or period)

regarding the company's expenditures for safety and training-related expenditures as provided for in this opinion and order. That report shall state, with particularity, the safety and training-related expenditures of Michigan Consolidated Gas Company for the appropriate time period and shall reconcile those expenditures to the level of safety and training-related operations and maintenance expenses included within this order. As part of the yearly Uncollectible Expenses True-up Mechanism review, the Commission shall review the company's safety and training-related expense filing. Should that filing indicate that a refund is due to Michigan Consolidated Gas Company's ratepayers, then the Commission may order an appropriate refund at that time.

J. Michigan Consolidated Gas Company's 90/10 refund mechanism regarding storage revenues is discontinued.

K. Within 30 days, Michigan Consolidated Gas Company shall file revised rate schedules and tariffs reflecting the rates and tariffs approved in this order and shown in Attachment A and in Attachment C.

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.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ J. Peter Lark
Chairman

(S E A L)

/s/ Robert B. Nelson
Commissioner

/s/ Laura Chappelle
Commissioner

By its action of April 28, 2005.

/s/ Mary Jo Kunkle
Its Executive Secretary

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.

MICHIGAN PUBLIC SERVICE COMMISSION

Chairman

Commissioner

Commissioner

By its action of April 28, 2005.

Its Executive Secretary

Attachment A

(Continued From Sheet No. B-21.00)

B2. CHARACTERISTICS OF SERVICE

B2.1 Company Liability and Force Majeure:

Company Liability

In any case of stoppage of the flow of gas to Customers, whether caused by accident, repairs or other cause, Company will not be liable for any damage that may arise therefrom. All stoppage of gas or damages of any kind that may be caused by severe cold weather will be considered beyond the control of Company and involving no pecuniary responsibility on its part.

Company shall not be liable for damages that may be incurred by the use of gas or appliances or the presence of Company's property on Customer's premises.

If a judgment is entered against Company as a result of its failure to exercise reasonable care and skill, Company's liability shall be limited to an amount equivalent to three times Customer's non-gas Monthly Customer Charge or one thousand dollars, whichever is less. Neither Company nor Customer shall be liable to the other party for consequential, incidental, exemplary, punitive, or indirect damages, lost profits or other business interruption damages arising out of the performance or non-performance of any obligation under Company's Rate Book or any contract, by statute, in tort or contract, under any indemnity provision or otherwise.

Force Majeure

Neither Customer nor Company shall be liable in damages, or in any other remedy, legal or equitable, to the other for any act, omission, or circumstances occasioned by or in consequence of any acts of God, strikes, lockouts, acts of the public enemy, wars, sabotage, terrorism, blockades, insurrections, riots, epidemics, landslides, lightning, earthquakes, fires, storms, floods, washouts, arrests, and restraints of rulers and peoples, civil disturbances, failure of electronic data, explosions, breakage, or accident to machinery or lines of pipe or the necessity to make repairs, tests, or alteration to machinery or lines of pipe, line freezeups, the binding order of any court or governmental authority which has been resisted in good faith by all reasonable legal means, or any other cause, whether of the kind herein enumerated, or otherwise, and whether caused or occasioned by or happening on the account of the act or omission of one of the parties hereto or some person or concern not a party hereto, not within the control of the party claiming suspension and which by the exercise of due diligence such Party is unable to prevent or overcome. A failure to settle or prevent any strike or other controversy with employees or with anyone purporting or seeking to represent employees shall not be considered a matter within control of the party claiming suspension. Under no circumstances will the following events constitute Force Majeure: (i) Customer's lack of finances, (ii) inadequate or uneconomic markets for Customer's gas, or (iii) insufficiency of Customer's gas supplies.

Such causes or contingencies affecting the performance of any obligations under any rate schedule or agreement by either Customer or Company, shall not relieve it of liability in the event of its concurrent negligence or in the event of its failure to use due diligence to remedy the situation and remove the cause in an adequate manner and with all reasonable dispatch, nor shall such causes or contingencies affecting performance of any obligation relieve Customer from its obligation to make payments of amounts then due, nor shall such causes or contingencies relieve either Customer or Company of liability unless such party shall give notice and full particulars of the same in writing, including by facsimile or electronic communication, to the other party as soon as possible after the occurrence relied on.

(Continued on Sheet No. B-22.01)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. B-22.00)

B2.2 Contracts:

Prospective Customers for residential, small commercial and small industrial consumption are required to sign a form of Contract known as "Application for Gas." This contract is not limited as to time.

Prospective Customers for gas for use in qualifying schools and university buildings are required to sign a form of Contract limited as to time known as "Application for Gas for Use in Schools and Universities." All such contracts must be approved and executed by the President or a Vice President of the Company, or a designated representative, before they shall be binding upon the Company.

Large volume Customers, taking gas under Rate Schedule GS-2, are required to sign (in addition to the Application for Gas) a Contract limited as to time. All such large volume Contracts must be approved and executed by the President or a Vice President of the Company, or a designated representative, before they shall be binding upon the Company.

Customers taking service under Rate Schedules ST, LT, XLT, TOS-F, TOS-I, CS-F or CS-I are required to sign a Contract for service incorporating the General Terms and Conditions contained in Section F. All such Contracts shall have a minimum term of one year unless Company, in its sole discretion, allows a term less than the one-year minimum.

Any Contract to which Company is a party for the provision of services under any Rate Schedule in Company's Rate Book is governed by the laws of the State of Michigan.

(Continued on Sheet No. B-23.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. B-23.00)

B2.6 Meter Readers and Complaints:

Requests for service and complaints may be made at an office of the Company in the District where service is rendered. Meter readers are not authorized to take such requests and complaints.

B2.7 Modification by Agents:

No employee or agent of the Company shall have the power to amend, modify, alter or waive any of the conditions of any gas service contract, except upon the approval of a duly authorized officer of the Company, or to bind the Company by making any promise or representation contrary to or inconsistent with these Rules and Regulations or with the provisions of any contract.

B2.8 Amendments:

Subject to the approval of the Michigan Public Service Commission, the Company may alter or amend its Rules and Regulations from time to time, and add such further and other Rules and Regulations as experience may suggest. Effective upon approval by the Michigan Public Service Commission, all such amendments shall be incorporated in and modify, if applicable, any existing gas service Contract.

B3. Controlled Service

(A) Scope

This Controlled Service Rule provides the Company with the authorization to control the attachment of additional gas sales load and non-system supply load, consistent with changes in gas supply as they occur.

(B) Application

- (1) Upon declaration of a Controlled Service condition, all those customers within the affected priorities requesting gas sales service shall make written application for such service on a form provided by the Company.
- (2) Existing gas sales customers requesting to attach additional gas burning equipment, existing Gas Customer Choice customers or existing transportation customers shall not be given preferential treatment over new customers but shall be considered the same as new customers in accordance with this Controlled Service Rule.

(Continued on Sheet No. B-25.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. B-36.00)

B6.2 Billing Period:

The Company renders bills once each month covering in each case as nearly as is reasonably possible a normal monthly period. The Company makes every reasonable effort to read the customer's meter every month on or about the same day of each month. Whenever, for any reason, the meter is not read at the end of a given monthly period, the Company shall render an estimated interim bill based in general upon the average monthly gas consumption determined by the last previous meter reading. In special cases this interim bill may be based upon the customer's past service record. For space heating customers, interim bills shall be estimated upon a degree day deficiency basis. The consumption determined by a meter reading shall be reduced by the consumption theretofore billed on estimated interim bills rendered since the last previous meter reading and the remainder shall be used as the basis for rendering a regular monthly bill.

Any customer who does not desire to receive an estimated interim bill, will, upon request to the Company, be supplied with forms upon which he may record the reading of his meter or meters. Such readings will, if received in time for normal billing purposes, be used in the computation of the interim bills of such customer.

When a meter fails to register, the Company may render an estimated bill based upon past service records.

B6.3 NSF Charges:

Checks remitted by customers as bill payments and returned because they are not valid are rebilled to the customer's account. A \$15.00 charge will be assessed to customers for handling checks received and returned by banks for reasons of insufficient funds, bank account closed, no account and similar situations.

B6.4 Where Bills Are Payable:

Bills are payable at an office of the Company in the District in which gas service is supplied and at various specified agencies.

B6.5 Prompt Payment Discount:

None.

(Continued on Sheet No. B-38.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. B-37.00)

B6.6 Notice to Turn Off Gas:

A customer will be held responsible for all gas supplied to his premises until forty-eight (48) hours after the receipt by the Company of a written notice to terminate the supply of gas in his name and the Company will bill such customer for all gas supplied in his name until the time designated in such notice for termination of service.

B6.7 Restoration of Service:

(A) Charges to offset the costs of restoring service and costs of meter relocation, if applicable, to customers whose previous service has been discontinued for nonpayment of bills or for any other breach by customers of the Company's Rates, Rules and Regulations, will be collected by the Company as follows:

- (1) Where service has been discontinued as a result of theft, a charge of \$500.00 will be collected if service was terminated by cutting and capping the service line.
- (2) If excavation was necessary to shut off service, a restoration charge of \$300.00 shall be collected from Customer.
- (3) Where service has been shut off and restoration does not require excavation, a restoration charge of \$35.00 for restorations done during regular working hours shall be collected from the customer whose service was shut off. If Customer specifically requests restoration of service after working hours and if the customer is advised of the increased charge, a restoration charge of \$45.00 shall be collected

Refer
[C5.55(D)]

- (4) As provided under Rule 55 (C5.55) of the Consumer Standards and Billing Practices where a meter has been relocated, a charge of \$250.00 will be collected in addition to the applicable service restoration charge payable under this Rule.

All service restoration charges are charges for gas service and are subject to the same payment requirements applicable thereto.

Refer
[C6.62(3)]

- (B) No service restoration charge shall be collected where the customer is receiving state or federal assistance or a state or federal agency determines that the customer is eligible to receive assistance, and the agency agrees to pay all or a satisfactory part of the customer's arrearage in accordance with the standards set forth in Rule C6.62 of these Rules.
- (C) If Customer elects to pay the energy arrears in full at the time of the shut off, Company's employee shall be authorized to accept the payment. In addition to full payment of arrears, an \$8.00 charge shall be paid by Customer for sending Company's employee to Customer's premises.
- (D) For Customers taking service under any of the sales Rate Schedules, turn on of gas service requested within 12 months of a request to turn off gas service by the same customer at the same address shall be performed at a charge of \$35.00 done during regular work hours or \$45.00 done during after working hours.

(Continued on Sheet No. B-39.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. B-51.00)

B12. Customer Attachment Program (Continued)

(I) Model Assumptions

Incremental Revenues:

The incremental revenues will be calculated based on current rates and a forecast of the timing and number of customer attachments as well as the customers' annual consumption levels.

Incremental Costs:

(1) Carrying Cost Rate

The Carrying Cost Rate will be a pre-tax weighted rate of long-term debt and common equity. The cost will be equal to and weighted in proportion to those authorized in the Company's most recent rate order. Based on MichCon's rate order in Case No. U-13898, dated ____ __, 2004, the Carrying Cost Rate is equal to **9.46%**.

(2) Plant in Service

Plant in Service shall reflect the Company's estimated cost to construct distribution mains, customer service lines, meters and pressure regulators or regulating facilities for the Project. The timing of the facility investment, primarily service lines, will correspond with the projected timing of the customer attachments.

The facility investment for an individual customer service line will be limited to the greater of 400 feet or 150% of the average length of all service lines within the Project.

(3) Carrying Costs

The Carrying Costs will be the product of the average of beginning and end-of-year net plant, Plant in Service minus accumulated depreciation minus deferred taxes, multiplied by the Carrying Cost Rate, noted in paragraph (1) above.

(4) Depreciation

Depreciation expense will be the product of Plant in Service multiplied by the appropriate prescribed depreciation rates approved for the Company.

(5) Property Taxes and Other Operating Expenses

Property Taxes will be the product of Plant in Service multiplied by the Company's average property tax rate. All Other Incremental Operating Expenses will be included as identified. Incremental O&M will at a minimum include a proportional cost for monthly meter reading, billing and mailing.

(Continued on Sheet No. B-53.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. B-52.00)

B12. Customer Attachment Program (Continued)

(I) Model Assumptions (Continued)

(6) Discount Rate

The Discount Rate will be a weighted rate of long-term debt and common equity. The cost will be equal to and weighted in proportion to those authorized in the Company's most recent rate order. Based on MichCon's rate order in Case No. U-13898, dated ____ __, 2004, the Discounted Rate is equal to **8.79%**.

(J) Customer Attachment Project Areas

All gas sold in any area specifically listed below is subject to the following Customer Attachment Project (CAP) charges. CAP areas and charges shall be added to or removed from the list from time to time by the Company.

<u>CAP ID</u>	<u>CAP Area</u>	<u>District</u>	<u>CAP Charge Per Month</u>	<u>End Date</u>
970200004	Clark Rd – Harrisville	Alpena	\$19.41	12/31/05
472200001	Cedar Lake Road	Alpena	\$14.58	08/31/06
50300009	112 Bear Point Road	Alpena	\$30.42	06/30/07
452300006	Jesse Road and Jesse Drive	Alpena	\$32.35	09/30/07
330400008	Jasmin Road	Alpena	\$36.30	11/30/08
261400007	3597 3 rd , Carole	Alpena	\$62.63	07/08/09
499300003	Huron Bluffs	Alpena	\$18.98	09/09/09
391200006	Canton Twp.	Ann Arbor	\$15.29	10/31/01
246200005	Joslin Lake Drive	Ann Arbor	\$ 5.13	12/31/01
718300004	Debra Court	Ann Arbor	\$13.84	09/30/03
680200007	Lima Twp Phase I	Ann Arbor	\$25.00	02/28/06
91200000	Huron River/Pineview	Ann Arbor	\$19.51	07/31/06
678100003	Saline Twp.	Ann Arbor	\$15.49	07/31/06
682200009	Ann Arbor Twp	Ann Arbor	\$17.74	08/31/06
44200009	Exeter Twp	Ann Arbor	\$21.91	10/31/06
464200002	Milan Twp I	Ann Arbor	\$16.86	10/31/06
345200002	Stoney Bluff	Ann Arbor	\$22.87	10/31/06
12200009	Martinsville/Sumpter Twp	Ann Arbor	\$15.73	11/30/06
235200003	Holly Lane	Ann Arbor	\$11.38	01/31/07
579200002	Joslin Lake	Ann Arbor	\$48.76	01/31/07
989200003	Martz Road	Ann Arbor	\$19.72	05/31/07
200300002	2675 Fini Drive	Ann Arbor	\$57.04	07/31/07
969200004	Cavallo Farms	Ann Arbor	\$44.65	07/31/07
929200004	Milan Twp II	Ann Arbor	\$16.86	07/31/07
60300006	Clark Wear Haggerty	Ann Arbor	\$17.97	08/31/07

(Continued on Sheet No. B-54.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. D-13.00)

D3.3 Aggregation of Accounts

(A) Contiguous Facilities:

When an industrial or commercial customer purchasing gas under Rate Schedule GS-2, Rate Schedule S (School Rate), or a commercial and/or industrial transportation customer transporting gas under Transportation Rate Schedule Nos. ST, LT, or XLT occupies a group of buildings or parts of buildings which are exclusively used by such customer as a unitary enterprise under a common ownership or leasehold, the quantities of gas supplied to such buildings or parts of buildings under the same rate schedule will be added for the purpose of determining the amount of the bill which such customer shall receive for service, provided:

- (i) The buildings or parts of buildings are situated upon the same parcel or contiguous parcels of land and are exclusively occupied and used by the customer as a unitary enterprise at one location and under one management; or
- (ii) The buildings or parts of buildings, separated by a public street or alley (but not including a limited-access highway), are situated upon parcels of land which occupy wholly or in part immediately opposite street frontages on the same street or alley and are exclusively occupied and used by the customer as a unitary enterprise at one location and under one management.

(B) Master Account:

A customer, receiving gas service at multiple facilities that are under common ownership by the customer, may elect to aggregate the quantities of gas supplied to such facilities, subject to all of the following conditions:

- (i) The customer must designate one of the facilities as the master account. Upon aggregation, the master account must receive service under an End User Transportation Rate Schedule account (ST, LT, or XLT).
- (ii) Only subsidiary accounts will be eligible for aggregation with the master account. To qualify as a subsidiary account, a facility must be served under a Gas Sales Rate Schedule (Rate A, AS, 2A, GS, or S) or Transportation Rate Schedule (ST, LT, or XLT). The customer, or the customer's agent, must specify which of the customer's facilities will be designated as subsidiary account(s). The customer may designate some or all of its facilities as subsidiary accounts.
- (iii) The facility designated as the master account shall be subject to and billed under the provisions of its End User Transportation Rate Schedule. Facilities designated as subsidiary accounts shall be subject to all of the terms and conditions of the master account End User Transportation Rate Schedule, except that the subsidiary accounts will pay the monthly customer service charge and distribution charge in effect for its designated sales or transportation rate rather than the monthly customer service charge and distribution transportation charge in effect for the master account. All other charges applicable to the master account as identified under Rate Schedule Nos. ST, LT, or XLT apply to the subsidiary accounts.

(Continued on Sheet No. D-15.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

**GENERAL SERVICE RATE
(Rates GS-1 and GS-2)**

Availability:

Subject to limitations and restrictions contained in orders of the Michigan Public Service Commission in effect from time to time and in the Rules and Regulations of the Company, service is available under this Rate Schedule to any non-residential customer, for any purpose.

Rates and Charges:

<u>Service Category</u>	<u>Customer Charge per Month</u>	<u>Distribution Charge</u>
GS-1	\$20.00 per meter	\$0.19431 per 100 cubic feet
GS-2	\$475.00 per meter	\$0.15533 per 100 cubic feet

Customers may choose the Service Category under which they take service, consistent with the provisions of Rule B5.1 and B5.2. When a Customer is selecting its initial Service Category, the Company must advise them that the economic break even point between GS-1 and GS-2 is approximately **14,000** Mcf per year. After the initial selection is made, then it is the customer's responsibility to determine when it is appropriate to switch Service Categories, as permitted by Rule B5.1.

Applications for this gas service shall be in writing upon application forms to be supplied by the Company.

Gas Cost Recovery Charge:

The gas cost recovery factors are shown on [Sheet No. E-3.00](#). This rate is subject to adjustments for fluctuations in the cost of gas as stated in Rule B10 of the applicable Rules and Regulations of the Company.

General Terms and Surcharges:

This Rate is subject to all General Terms and Conditions shown on [Sheet No. E-1.00](#) and Surcharges shown on [Sheet No. E-2.00](#).

Late Payment Charge and Due Date:

A late payment charge of 2% of the bill, net of taxes, not compounded, may be added to any bill which is not paid on or before 21 calendar days from the date of mailing.

Standby Service:

- (A) Definition: "Standby Service" means that gas service provided by Company whereby gas systems maintained by Company (including, but not limited to, unauthorized gas, pipes, regulation, and metering) are available for immediate no-notice use for the delivery and/or sourcing of natural gas to Customer's energy systems relied upon for: (1) emergency, (2) contingency, (3) supplemental energy, (4) reserve energy, (5) displacing the primary fuel source, or (6) operating a limited number of hours annually.
- (B) Surcharge: A customer taking standby service for a facility or equipment shall pay a monthly charge equal to 25¢/cf or \$250/MMBtu for each cf or MMBtu of nameplate rating of the facility or equipment taking standby service.

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

Section F
**General Terms and Conditions for Transportation and Storage Service and
Rate Schedules for Transportation and Storage Service**

F1. General Provisions & Definitions

F1.1 Definitions

"Annual Contract Quantity" or "ACQ" means an annual quantity of natural gas specified in the Contract between Customer and Company, that can be delivered to Company and is based on Customer's average 12 Month usage (determined from the last 36 Months of data), plus adjustments, approved at Company's sole discretion, for known or expected changes or special operating conditions.

"Business Day" is Monday through Friday, excluding Company holidays.

"Contract" is the agreement between Company and Customers for the provision of transportation or storage services under Company's Rate Schedule. For purposes of clarity, the agreement between Company and Customer may also be referred to as a Transportation Contract or Storage Contract.

"Contract Year" is defined within each Contract.

"Customer" means the individual or business that purchases transportation or storage service from Company.

"Delivery Point(s)" are the point(s) where Company delivers gas to Customer, or for Customer's account.

"Gas Day" is a period of 24 consecutive hours (23 hours when changing from Standard Time to Daylight Savings Time and 25 hours when changing back to Standard Time) beginning at 10:00 a.m. Eastern Clock Time.

"Maximum Daily Quantity" or "MDQ" means a daily quantity of natural gas specified in the Contract between Customer and Company, that can be delivered to Company and is based on Customer's highest historical Month usage (determined from the last 36 Months of data) divided by the number of days during that Month and multiplied by 110%, plus adjustments, approved at Company's sole discretion, for known or expected changes or special operating conditions. Provided, however, during September and October, Customer's MDQ will be based on the daily average of Customer's September and October usage from the previous three years, plus 1.42% of Customer's ACQ divided by 30 days. The Company and customer may agree to use a different MDQ as part of the negotiations for an optional discount from the cost based rates set forth in the tariff. The Company will utilize their best efforts to insure that the customer's MDQ is reflective of the customer's maximum daily consumption and allow the customer all reasonable opportunities to minimize the risk of Unauthorized Gas Usage Charges.

"MMBtu" means one million Btu.

"MMcf" means one million cubic feet of gas at a base temperature of 60° F and a base pressure of 14.65 psia.

"Month" is the period beginning on the first Gas Day of the calendar Month and ending at the same hour on the first Gas Day of the next succeeding calendar Month.

"Nomination" or "Nominating" is a transmittal by Customer, or its designated agent, of request for receipt and/or delivery of gas for Customer's account for each Gas Day that service is desired.

"Operational Flow Order, OFO: See section F4.5.

(Continued on Sheet No. F-2.00)

**ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS**

DETROIT, MICHIGAN

**EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005**

**ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898**

(Continued From Sheet No. F-1.00)

"Rate Schedule" means the schedule of rates governing natural gas service as approved by the Michigan Public Service Commission.

"Receipt Point(s)" are those interconnection(s) between the facilities of Company and third parties that deliver gas to Company, for the account of Customer.

"Standby Service" means that gas service provided by Company whereby gas systems maintained by Company (including, but not limited to, unauthorized gas, pipes, regulation, and metering) are available for immediate no-notice use for the delivery and/or sourcing of natural gas to Customer's energy systems relied upon for: (1) emergency, (2) contingency, (3) supplemental energy, (4) reserve energy, (5) displacing the primary fuel source, or (6) operating a limited number of hours annually.

"Standby Maximum Daily Quantity" or "SMDQ" means the Maximum Daily Quantity of natural gas specified in the Contract between Customer and Company for Standby Service to support the operation of Customer's facility or equipment.

"Tariff" means Company's Rules, Regulations and Rate Schedules for Gas Service, MPSC No. 4 as modified and approved from time to time by the Michigan Public Service Commission.

"Total Heating Value Per Cubic Foot" means the number of Btu produced by the combustion, at constant pressure, of one cubic foot of gas, with air of the same pressure and temperature as the gas, when the products of combustion are cooled to the initial temperature of the gas and air, and when the water formed by the combustion is condensed to the liquid state. This definition applies regardless of the equipment used to determine the total heating value per cubic foot.

"Transportation Rate Restoration Charge: See section F9.

"Unauthorized Gas Usage Charge": See section F8.

F1.2 Application of Rules

If at any time during the term of a Contract any of the parties, by force of any such law, order, decision, rule or regulation are ordered or required to do any act inconsistent with the provisions hereof, then for the period during which the requirements of such law, order, decision, rule or regulation are applicable, such Contract shall be deemed modified to conform with the requirement of such law, order, decision, rule or regulation.

F1.3 Possession of Gas

As between Company and Customer, Customer shall be deemed in exclusive control and possession of the gas transported hereunder and responsible for any loss, damage or injury caused thereby until it is delivered to Company at the Receipt Point(s) and after it is delivered by Company at the Delivery Point(s). Company shall be deemed in exclusive control and possession of said gas and responsible for any loss, damage or injury caused thereby after it is delivered by Customer, or for Customer's account, at the Receipt Point(s) and until it is delivered by Company at the Delivery Point(s).

F1.4 Warranty

Customer warrants, for itself, its successors and assigns, that it will have, at the time of delivery of gas hereunder good and marketable title to the gas delivered and that such gas shall be free and clear of all liens, encumbrances, and claims. Customer warrants that it will indemnify Company and save it harmless from suits, actions, debts, accounts, damages, costs, losses and expenses arising from or out of adverse claims of any and all persons to said gas or to royalties, taxes, license fees or charges thereon.

(Continued on Sheet No. F-3.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-2.00)

F1.5 Non-Waiver of Future Defaults

No waiver by either party of any one or more defaults by the other in the performance of any provisions of Company's Tariff or any Contract will operate or be construed as a waiver of any future default or defaults, whether of a like or of a different character.

F1.6 Incorporation of Rate Schedules and Contract

Unless limited to specifically identified Rate Schedules, the General Terms and Conditions set forth in Sections B, D and F are incorporated in and are a part of any Contract entered into by Company for the provision of service under The Transportation Service Rate Schedule, or Rate Schedules TOS-F, TOS-I, CS-F or CS-I. To the extent there is any inconsistency between terms in these General Terms and Conditions and terms in any Rate Schedule or Contract, the applicable Rate Schedule shall govern.

F1.7 Assignment

Customer may not assign any of its rights or obligations hereunder without the prior written consent of Company.

F1.8 Default

Company reserves the right to suspend transportation and/or storage services, or to terminate any Contract between Customer and Company, at any time in the case of an emergency or as a result of violation of the General Terms and Conditions of the Contract or Company's Tariff.

F2. Records, Accounting & Control

F2.1 Mailing of Notices, Bills & Payments

All notices, bills and payments required or permitted to be given in connection with service shall be sent to the address specified in Customer's Contract shall be in writing and shall be valid and sufficient if delivered in person, dispatched by first class mail, overnight mail or facsimile.

F2.2 Nominations Accounting & Control

- (a) Customer may designate a third party as agent for purposes of Nominating, and for giving and receiving notices related to Nominations. Customer shall provide Company with written notice of such designation. Any such designation shall be effective starting the Month following the receipt of the notice and will remain in effect until revoked in writing by Customer.
- (b) All Nominations shall be submitted through Company's electronic gas nomination system. Specific information to be included in the Nomination is posted on Company's electronic gas nomination system.
- (c) Customer, or its designated agent, shall notify Company's Gas Nominations Department of the daily quantity of gas that Customer is Nominating for delivery to Company on behalf of Customer. Such Nominations shall be submitted by 2:00 p.m. Eastern Clock Time prior to the effective Gas Day. Nominations made after the 2:00 p.m. deadline shall be accepted at the sole discretion of Company. Customer, or its designated agent, shall provide Company with a Nomination for each Gas Day. (If a single nomination is received it shall be assumed to apply for each subsequent day of the month unless otherwise stated.)
- (d) If Customer fails to provide a Nomination for any Month, the daily Nomination is assumed to be zero.

(Continued on Sheet No. F-4.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-3.00)

F3. Gas Quality

F3.1 Quality

- (a) The gas delivered to Company shall meet the following requirements:
- 1) Gas shall not contain more than 0.0005 percent (5 ppm) oxygen by volume;
 - 2) Gas shall be commercially free from objectionable odors, solid or liquid matter, bacteria, dust, gum or gum-forming constituents which might interfere with its merchantability or cause injury to or interference with proper operation of the lines, regulators, meters or other appliances through which it flows;
 - 3) Gas shall not contain more than 0.25 grain of hydrogen sulfide nor more than 0.5 grain of mercaptan sulfur per 100 cubic feet;
 - 4) Gas shall not contain more than 5.0 grains of total sulfur (including hydrogen sulfide and mercaptan sulfur) per 100 cubic feet;
 - 5) Gas shall not at any time have a carbon dioxide content in excess of two percent by volume;
 - 6) Gas shall not contain an amount of moisture that at any time exceeds five pounds per million cubic feet;
 - 7) Gas shall be fully interchangeable in accordance with the provisions of AGA Research Bulletin No. 36 and any subsequent modifications and amendments thereof;
 - 8) The temperature of the gas shall not exceed 100° F;
 - 9) The hydrocarbon dew point of the gas shall not exceed 0° F at 500 pounds per square inch.
- (b) If the gas delivered by Customer at any Receipt Point fails to meet the qualities stipulated in Section F3.1(a), then Company shall notify Customer of such deficiency and thereupon may, at its option, refuse to accept delivery pending correction. Upon demonstration that the gas being tendered meets the gas quality specifications of Section F3.1(a), Company shall resume taking delivery of gas.

F3.2 Heating Value

The gas delivered by Customer shall have a Total Heating Value Per Cubic Foot of not less than 950 Btu nor more than 1,100 Btu.

F4. Service Requirements

F4.1 Quantities

- (a) Customer may deliver, or cause to be delivered, and Company shall, subject to other provisions in Company's Rate Schedule, accept quantities of gas up to the MDQ specified in the Contract. If deliveries to Company exceed agreed upon quantities, Company may refuse deliveries or terminate the Contract upon 30 days' written notice to Customer.
- (b) Deliveries to Company may be made by Customer or on behalf of Customer at existing interconnections between the gas transmission facilities of Company and other pipeline systems. These Receipt Point(s) shall be those specified by Company from time to time on its electronic bulletin board.

(Continued on Sheet No. F-5.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-4.00)

F4.2 Delivery Pressure

All deliveries of gas by Customer and Company shall be made at Company's prevailing pressure.

F4.3 Shutoff of Service

Company is not required to perform service under any Contract on behalf of any Customer failing to comply with any and all terms of Customer's Contract and Company's Tariff.

F4.4 Measurement

- (a) All quantities of gas received at Receipt Point(s) by Company for the account of Customer shall be measured at the Receipt Point(s) by Company or its designee in accordance with, and shall comply with the measurement specifications contained in:
- (1) Transmission Measurement Committee Report #3, Natural Gas Department, American Gas Association, including the Appendix thereto, dated September 1985, ("Gas Measurement Report #3")
 - (2) Transmission Measurement Committee Report #7, Natural Gas Department, American Gas Association, including the Appendix thereto, dated April 1996, ("Gas Measurement Report #7")
 - (3) Transmission Measurement Committee Report #8, Natural Gas Department, American Gas Association, including the Appendix thereto, dated July 1992, ("Gas Measurement Report #8")
 - (4) Transmission Measurement Committee Report #9, Natural Gas Department, American Gas Association, including the Appendix thereto, dated June 2000, ("Gas Measurement Report #9")
 - (5) And any subsequent modifications and amendments thereof.
- (b) All quantities of gas delivered at the Delivery Point(s) by Company to Customer, of for the account of Customer, shall be measured at the Delivery Point(s) by Company, or its designee, in accordance and in compliance with the measurement specifications contained in the Gas Measurement Report #3, Gas Measurement Report #7, Gas Measurement Report #8 and Gas Measurement Report #9.

F4.5 Notice of Operational Flow Order

When there is adequate time during an emergency situation, and if applicable, Company will implement an Operational Flow Order, or OFO. An OFO invokes daily-balancing upon all Customers and allows Company to limit the daily storage withdrawal volumes of Customers with Storage rights specified in Customer's Contract and/or applicable Rate Schedule to that level authorized by Company in the OFO. The payment of Unauthorized Gas Usage penalties does not create the right to exceed the levels established by an OFO. Customers not balancing deliveries to Company, with use, and authorized storage withdrawal volumes, on any Gas Day during an OFO will be subject to a penalty equal to the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$1.00 per 100 cubic feet, plus Customer's contracted transportation Charge, for all gas taken by Customer in excess of the cumulative volume delivered to Company (less the allowance for gas-in-kind) on behalf of Customer.

(Continued on Sheet No. F-6.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-5.00)

If an OFO or curtailment becomes necessary, Company shall provide notice to the Commission and all affected Customers of the nature, probable duration and extent of such OFO or curtailment. Such notice will be given as far in advance as possible.

F5. Billing

Company shall follow the billing practices outlined in Section D of the Tariff.

F6. Creditworthiness

If a customer deposit is required in accordance with the provisions of Rules D1.13 (Customer Deposits) and D1.14 (Discontinuation, Termination or Denial of Service, Customers taking service under Rate Schedules ST, LT, XLT, TOS-F, TOS-I, CS-F and CS-I shall be subject to the following provision:

(a) Customer shall be required to demonstrate creditworthiness. Company is not required to commence service or to continue to provide service if Customer, when requested by Company to demonstrate creditworthiness, fails to do so to Company's satisfaction. Creditworthiness will be based upon (1) a credit rating of investment grade defined as a rating of at least "BBB-" by Standard & Poor's Corporation, a rating of at least "Baa3" by Moody's Investors Service, or a rating of at least BBB- by Fitch Ratings; or (2) if public credit reports are not available, an equivalent rating of investment grade as determined by Company based on the financial rating methodology, criteria and ratings for the industry of Customer as published by the above rating agencies from time to time. For purposes of credit evaluation, Company will consider the following, as applicable:

- (1) audited financial statements;
- (2) annual report;
- (3) most recent filed statements with the Securities and Exchange Commission (or an equivalent authority) or such other publicly available information;
- (4) for public entities, the most recent publicly available interim financial statements, with an attestation by its Chief Financial Officer, Controller or equivalent that such statements constitute a true, correct and fair representation of financial condition prepared in accordance with Generally Accepted Accounting Principles (GAAP) or equivalent;
- (5) publicly available credit reports from credit and bond rating agencies;
- (6) private credit ratings, bank or trade references;
- (7) past payment history to Company;
- (8) whether Customer has filed for bankruptcy protection and/or is operating under any chapter of the bankruptcy laws;
- (9) whether Customer is subject to liquidation or debt reduction procedures such as an assignment for the benefit of creditors or any creditors' committee agreement;
- (10) whether Customer's credit rating has been downgraded by a credit rating agency within the last six Months; or
- (11) such other information as may be mutually agreed to by Company and Customer.

(Continued on Sheet No. F-7.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-6.00)

- (b) If Company determines that Customer is not creditworthy, then within 5 business days of notice from Company, Customer shall provide company with one of the following credit alternatives (1) a corporate guaranty of all Customer obligations from a creditworthy entity; (2) an irrevocable letter of credit in form and from an institution satisfactory to Company; (3) a deposit equal to 25% of Customer's annual bill, or (4) such other security, as reasonably determined by Company, to be of a continuing nature and in an amount equal to such amounts which would be due. Customer's obligation to provide credit assurance shall continue until Customer compiles a record of 12 continuous months of bill payment on or before the due date, as specified in Rules D1.13 and D1.14.
- (1) A guarantor shall be deemed creditworthy provided it has an investment grade rating for its long-term senior unsecured debt from at least two of the recognized rating agencies listed below. The minimum acceptable investment grade rating from each of the indicated rating agencies is:
- | | |
|---------------|------|
| Moody's | Baa3 |
| S&P | BBB- |
| Fitch Ratings | BBB- |
- (2) A guarantor that is considered creditworthy at the time it provided the guaranty but, at a later date, no longer meets the creditworthiness standards of this subsection will be required to provide other security acceptable to Company within five business days of notice from Company that the guarantor fails to meet the creditworthiness standards of this subsection.

F7. Authorized Gas Usage Charge

[This rule has been cancelled.]

F8. Unauthorized Gas Usage Charge

A Customer taking service under Rate Schedules ST, LT, or XLT shall be subject to an unauthorized gas usage charge as more fully set forth in the applicable Rate Schedule.

F9. Transportation Rate Restoration Charge

A turn-on charge equal to the sum of the intervening Months' Monthly Customer Charges since the service was shut off shall be made to any Customer taking service under the Transportation Service Rate Schedule who orders a shutoff and a restoration of service at the same premises within a 12 Month period.

F10. Aggregation of Accounts

Customer as defined in Section D3.3 of the Tariff may qualify for aggregation of accounts as more fully set forth in Section D3.3 of Tariff.

F11. Electronic Bulletin Board

Company shall make available, maintain and update, an electronic bulletin board (EBB) accessible to Customers and their authorized agents who Nominate gas to Company's system.

(Continued on Sheet No. F-8.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-7.00)

F12. Transportation Standards of Conduct

This rule is intended to promote fair competition and a level playing field among all participants involved in transportation within Company's regulated gas service territory. Company will conduct its business to conform to the following transportation Standard of Conduct:

- (a) Company will apply any Tariff provision relating to transportation service in the same manner without discrimination to all similarly situated persons.
- (b) Company will not give its marketing affiliate or customers of its affiliate preference over any other non-affiliated gas marketers or their customers in matters relating to transportation service including, but not limited to, nominating, balancing, metering, billing, storage, standby service, curtailment policy or price discounts.
- (c) Company will not communicate to any Customer, Supplier or third parties that any advantage may accrue to such Customer, Supplier or other third party in the use of Company's services as a result of that Customer, Supplier or other third party dealing with its marketing affiliate and shall refrain from giving any appearance that it speaks on behalf of its affiliate.
- (d) Company will process all similar requests for transportation service in the same manner and within the same period of time.
- (e) Company will not provide leads or provide market sensitive information regarding a current or potential customer or marketer to its marketing affiliate. If a customer requests information about marketers, Company will provide a list of all marketers operating on its system, including its affiliate, but will not promote its affiliate.
- (f) If a Customer makes a request in writing that its historic volumetric sales and transportation data be provided to a particular marketer or marketers in general, that request will be honored by Company until revoked by Customer. To the extent Company provides to its marketing affiliate a discount or information related to the transportation, sales or marketing of natural gas, including but not limited to Company's customer lists, that is not readily available or generally known to any other marketer or Supplier or has not been authorized by a Customer, it will provide details of such discount or provide the information contemporaneously to all potential marketers on its system that have requested such information. A marketer may make a standing request for contemporaneous disclosure of such information.
- (g) Company will not condition or tie its agreement to release interstate pipeline capacity to any agreement by a gas marketer, Customer, Supplier or pipeline transporter relating to any service in which its marketing affiliate is involved.
- (h) Company will process all similar requests for transportation service in the same manner and within the same period of time.
- (i) Company will not provide leads or provide market sensitive information regarding a current or potential customer or marketer to its marketing affiliate. If a customer requests information about marketers, Company will provide a list of all marketers operating on its system, including its affiliate, but will not promote its affiliate.

(Continued on Sheet No. F-9.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-9.00)

F14. Transportation Contract Cancellation

Customers taking service under the Transportation Service Rate Schedule may cancel their Contract during the initial term of the Contract if Customer provides at least 30 days prior written notice to Company that (1) Customer's facility or business has or will permanently close or cease operations, (2) Customer is transferring ownership of the facility or business in whole, or (3) Customer is transferring service to another Rate Schedule provided Customer complies with all rules for transferring service to another Rate Schedule. Upon Contract termination, Customer will be required to pay all outstanding charges owed to Company by the payment due date posted on the final invoice for transportation service.

If Customer taking gas service under the Transportation Service Rate Schedule, and is paying a negotiated transportation rate under the optional provision, terminates their Contract prior to the end of the term as provided above, Customer will be required to pay Company, as liquidated damages and not as a penalty, a settlement payment equal to the sum of the Transportation Charges and Monthly Customer Charges that Company would have received from the time of cancellation to the expiration date of Customer's Contract. In calculating the settlement payment, the Transportation Charge will be applied to Customer's then current ACQ. Any settlement payment will be discounted to present value using the London Interbanking Offer Rate (LIBOR) on the date of Contract cancellation to take into account the period between the date of cancellation and the date on which such amounts would have otherwise been due under the Contract.

F15. Cashout Mechanism

F15.1 Scope

This Cashout Mechanism provides Company with the authorization to Cashout Imbalances with Nominating Agents at Company's Dry Receipt Point(s).

F15.2 Definitions

As used in Section F15:

"Actual Deliveries" means the amount of gas nominated by the Nominating Agents for the Production Month and tendered by Company during the same Month at Dry Receipt Points.

"Actual Receipts" means the amount of gas tendered by Nominating Agent to Company during the Month at Dry Receipt Points.

"Alpena System Dry Points" means those receipt points identified on ConQuest EBB, as may change from time to time, under the heading "Alpena System Dry Points".

"Business Day" means Monday through Friday, excluding Federal Banking Holidays.

"Cashout" means the monetary settlement of Imbalances. Company will purchase and sell gas at Alpena System Dry Points and Non-Alpena System Dry Points to correct Imbalances.

"Cashout Price" means the price determined pursuant to Section F15.4.

"Company" means Michigan Consolidated Gas Company.

"ConQuest Electronic Bulletin Board" or "ConQuest EBB" means Company's electronic communication system, which is available to all Nominating Agents.

(Continued on Sheet No. F-11.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-10.00)

“Deficient Quantities” means the negative volume that is derived by subtracting Actual Deliveries from Actual Receipts.

“Dry Receipt Points” means both the Alpena System Dry Points and the Non-Alpena System Dry Points.

“Excess Quantities” means the positive volume that is derived by subtracting Actual Deliveries from Actual Receipts.

“Imbalance” means the volumetric difference between Actual Receipts and Actual Deliveries as further explained in Section F15.4(A).

“Maximum Nomination Quantity” means a quantity of gas as determined by Company based on the previous twelve Month average Actual Receipts multiplied by 110%, plus adjustments for known or expected changes that are communicated to Company at least five days prior to the effective nomination change.

“Month” means the period beginning on the first day of a calendar Month and ending on the last day of the same calendar Month.

“Monthly Index Price” means the price determined pursuant to Section F15.4(B).

“Nominating Agent” means the party responsible for nominating gas on the ConQuest EBB at the Dry Receipt Points.

“Non-Alpena System Dry Points” means those receipt points identified on ConQuest EBB, as may change from time to time, under the heading “Non-Alpena System Dry Points”.

“Production Month” means the Month during which Nominating Agent receives service under Section F15.

“Title Holder” means the owner of the largest working interest in any well from which gas is nominated into Company’s Dry Receipt Points.

F15.3 Determination and Resolution of Imbalances

- (a) It is the Nominating Agent’s responsibility to provide timely and accurate nominations of quantities proposed to be received and delivered by Company, and to maintain each day, as nearly as practicable, equality between Actual Receipts and Actual Deliveries under Section F15. Company will reject nomination’s exceeding the Maximum Nomination Quantity. Actual Receipts exceeding the Maximum Nomination Quantity will be considered Trespass Gas, as such term is defined on ConQuest EBB.
- (b) If Actual Deliveries exceed Actual Receipts at a Dry Receipt Point by greater than ten percent (10%) on a cumulative daily basis throughout the Month, Company will reject and or modify all nominations received at the Dry Receipt Point. Company will allow nominations to continue when the difference between Actual Deliveries and Actual Receipts at the Dry Receipt Point is equal to or less than ten percent (10%) on a cumulative daily basis for the Month.
- (c) At the end of each Production Month, Company will determine whether Nominating Agent caused an Imbalance to occur. If an Imbalance exists, Nominating Agent and Company shall Cashout the Imbalance volume pursuant to Section F15.4.

(Continued on Sheet No. F-12.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-11.00)

F15.4 Cashout Provision

- (a) Company shall compare Actual Receipts to Actual Deliveries tendered at each Dry Receipt Point utilized by Nominating Agent and calculate an Imbalance no later than the tenth (10th) Business Day following the end of each Production Month. The volumetric difference, after any imbalance trading has occurred pursuant to Section F15.5, will result in Excess Quantities or Deficient Quantities. If the Nominating Agent nominated gas on multiple Dry Receipt Points, Company shall aggregate Excess Quantities and Deficient Quantities for all Alpena System Dry Points separately from Non-Alpena System Dry Points. The separately aggregated Excess Quantities and/or Deficient Quantities shall be divided by the Actual Deliveries separately aggregated for the Alpena System Dry Points and the Non-Alpena System Dry Points respectively, using final Monthly confirmed volumes as posted on Company's ConQuest EBB. This calculation will be used to determine Nominating Agent's Monthly Imbalance percentage on the Alpena System Dry Points and separately for the Non-Alpena System Dry Points. Company shall be authorized to purchase and sell gas at Dry Receipt Points to manage imbalance quantities.
- (b) Each Month, Company shall determine the Monthly Index Price. The Monthly Index Price shall be based on the Daily Price Survey rates for MichCon citygates as reported in Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service. The Monthly Index Price shall be equal to the sum of the daily Mich.-MichCon Midpoint Citygate Price for the applicable Production Month divided by the number of quoted price days in the same Production Month. Company will post the Monthly Index Price on its ConQuest EBB by the 3rd Business Day of the Month.
- (c) In cases where Nominating Agent's Imbalance results in Excess Quantities, Company shall pay Nominating Agent the following based on the Monthly Imbalance percentage:

<u>Imbalance Percentage (Tier)</u>	<u>Cashout Price for the Excess Quantities</u>
Greater of first 100 Mcf	
Or 0% up to 2%	100% of Monthly Index Price
> 2% Up to 5%	80% of Monthly Index Price
> 5%	60% of Monthly Index Price

For purposes of determining the tier at which an Imbalance will be cashed out, the price will apply only to volumes within a tier. For example, if there is a 7% imbalance, Excess Quantities that make up the first 2% of the Imbalance will be priced at 100% of the Monthly Index Price. Excess Quantities making up the next 3% of the Imbalance will be priced at 80% of the Monthly Index Price. Excess Quantities making up the remaining 2% of the Imbalance will be priced at 60% of the Monthly Index Price.

- (d) In cases where Nominating Agent's Imbalance results in Deficient Quantities, Nominating Agent shall pay Company the following based on the Monthly Imbalance percentage:

<u>Imbalance Percentage (Tier)</u>	<u>Cashout Price for Deficient Quantities</u>
Greater of first 100 Mcf	
Or 0% up to 2%	100% of Monthly Index Price
> 2% Up to 5%	120% of Monthly Index Price
> 5%	140% of Monthly Index Price

(Continued on Sheet No. F-13.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-12.00)

For purposes of determining the tier at which an Imbalance will be cashed out, the price will apply only to volumes within a tier. For example, if there is a 7% imbalance, Deficient Quantities that make up the first 2% of the Imbalance will be priced at 100% of the Monthly Index Price. Deficient Quantities making up the next 3% of the Imbalance will be priced at 120% of the Monthly Index Price. Deficient Quantities making up the remaining 2% of the Imbalance will be priced at 140% of the Monthly Index Price.

- (e) Cashout of volumes relating to prior period adjustments shall be cashed out at 100% of the Monthly Index Price applicable to the Production Month in which the prior period adjustment was created.

F15.5 Imbalance Trading

- (a) Company will allow a Nominating Agent to net Imbalances with other Nominating Agents within the Alpena System Dry Points and within the Non-Alpena System Dry Points, but not between the Alpena System Dry Points and the Non-Alpena System Dry Points. Gas from Alpena System Dry Points must be transported to Company's Woolfolk delivery point, or other points as identified on ConQuest EBB before imbalance trading can occur.
- (b) The information required for imbalance trading must include the identification of both Nominating Agents involved in the trade, production period, and the Monthly volume to be traded. Imbalances must be traded with Imbalances in the opposite direction and must move the Nominating Agent's Imbalance closer to zero.
- (c) Company will enable the imbalance trading process by:
 - (1) Receiving the request for imbalance trade;
 - (2) Receiving the imbalance trade confirmation;
 - (3) Sending the imbalance trade notification;
 - (4) Reflecting the trade on the Nominating Agent's next Monthly imbalance or cashout invoice.
- (d) Imbalance trades can only be withdrawn by the initiating Nominating Agent and only prior to Company sending the imbalance trade notification.
- (e) Company will post on its ConQuest EBB a list of imbalance trading procedures in order to facilitate the Monthly trading of Imbalances.

(Continued on Sheet No. F-14.00)

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-13.00)

F15.6 Billing and Payment

- (a) On or about the 20th calendar day of each Month, Company shall render to Nominating Agent a statement of the Cashout amount for the preceding Production Month.
- (b) In cases where a Deficient Quantity exists, Nominating Agent shall make payments to Company within 10 calendar days of the statement date. Payments shall be remitted to Company as directed on the invoice.
- (c) In cases where an Excess Quantity exists, Company shall make payments to Nominating Agent within 10 calendar days of the statement date. Company shall remit payments to Nominating Agent in the manner directed by Nominating Agent.
- (d) In the event that Nominating Agent fails to pay the amount of any statement rendered by Company within the allowed time, then Nominating Agent will be subject to immediate suspension of service, i.e., nominations will not be accepted, until such amount is paid. By authorizing Nominating Agent to nominate gas, Title Holder is deemed to be the guarantor for payment of any amounts due Company not paid by Nominating Agent. In addition to any other remedies Company may have, without notice or approval, (i) Company may offset any indebtedness it owes under this mechanism or otherwise to Nominating Agent and or Title Holder against any amounts Nominating Agent or Title Holder owes to Company under this mechanism and (ii) Company may take title, at no cost and free and clear of any adverse claims, to Title Holder's gas on Company's system including but not limited to gas in Company's and MichCon Gathering Company's transportation facilities, parked gas and gas in Company's storage facilities as compensation for service in the event Nominating Agent defaults on any of its cashout payment obligations to Company. Company will only take title to an amount of Title Holder's gas necessary to offset the undisputed dollar amount Nominating Agent owes to Company. The monetary value of the gas will be the Monthly Index Price for the Month in which the imbalance occurred.

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

**Transportation Service Rate
(Rates ST, LT, XLT)**

Availability:

Subject to any restrictions, service under this rate schedule is available to any customer who could otherwise purchase gas under any another Company Rate Schedule.

A Customer that selects transportation service under this Rate Schedule must remain on this Rate Schedule for at least 12 Months before the Customer is eligible for sales service and shall continue on this rate Month to Month after the initial term of the Transportation Contract has expired unless otherwise agreed upon between Company and Customer. A Customer eligible to request a return to sales rates must provide a minimum of 12 Months written notice to the Company of its election to return to sales rates.

Company reserves the right to deny a return to sales rates subject to Company's Controlled Service Rule B3.

Under this Rate Schedule, Company will transport gas for Customer from the Receipt Point(s) to the Delivery Point(s).

RATES AND CHARGES

	<u>Service Category</u>		
	<u>ST</u>	<u>LT</u>	<u>XLT</u>
Monthly Charges			
Customer Charge	\$1,300.00	\$3,375.00	\$11,300.00
Remote Meter Charge			\$100.00
Transportation Rates			
Cost Based Rate	\$0.08078 Per Ccf	\$0.05596 Per Ccf	\$0.04219 Per Ccf
Optional Rates:			
Maximum Rate	\$0.13856 Per Ccf	\$0.08892 Per Ccf	\$0.06638 Per Ccf
Minimum Rate	\$0.02300 Per Ccf	\$0.02300 Per Ccf	\$0.01800 Per Ccf

SELECTION OF SERVICE CATEGORY AND RATES

When the customer is selecting its initial service category, Company must advise them that the economic break even point between ST and LT is approximately 100,000 Mcf per year and the economic break even point between LT and XLT is approximately 700,000 Mcf per year (Based on the cost based rate). After the initial selection is made, then it is the customer's responsibility to determine when it is appropriate to switch service categories

Transportation Service

In accordance with Section F2.2 and Company's Nominating procedures, Customer shall advise Company of the volume of gas that Customer will cause to be delivered to Company for transportation during that Month and the Receipt Point(s) where the gas will be delivered to Company.

(Continued on Sheet No. F-16.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-15.00)

If in any Month, the volume of gas received by Company at the Receipt Point(s), less the allowance for company-use and lost-and-unaccounted-for gas, is more than the volume of gas taken by Customer at the Delivery Point(s), then the difference shall be retained by Company and delivered to Customer in those succeeding Months when the volume of gas received by Company is less than Customer's requirements. Should the aggregate volume of gas, less the allowance for company-use and lost-and-unaccounted-for gas, retained by Company at any Month-end exceed 10% of the Annual Contract Quantity, then Company shall have the rights: (1) to refuse to receive any additional volume of gas for that Customer until Company has satisfied itself that the volume of gas retained for Customer is less than 10% of the Annual Contract Quantity, and (2) to charge Customer for the storage of any Month-end balance that exceeds 10% of the Annual Contract Quantity.

If Customer does not withdraw its gas retained by Company within 60 days of the termination of the Contract, then Company shall have the right to purchase the gas from customer at a rate of \$0.10 per 100 cubic feet.

Gas in Kind

Company shall retain **1.42%** of all gas received at the Receipt Point(s) to compensate it for the allowance for company-use and lost-and-unaccounted-for gas on Company's system. This volume shall not be included in the quantity available for delivery to Customer.

Surcharges and Special Taxes

This Rate Schedule is subject to Surcharges shown on Sheet No. E-2.00.

In municipalities which levy special taxes, license fees, or street rentals against the Company, and which levy has been successfully maintained, the standard of rates shall be increased within the limits of such municipalities so as to offset such special charges and thereby prevent the customers in other localities from being compelled to share any portion of such local increase.

Bills shall be increased to offset any new or increased specific tax or excise imposed by any governmental authority upon the Company's production, transmission or sale of gas.

Late Payment Charge and Due Date

A late payment charge of 2% shall be applied to the unpaid balance outstanding if the bill is not paid in full on or before the date on which the bill is due. The due date of the customer's bill shall be 21 days from the date of mailing.

Unauthorized Gas Usage

"Unauthorized Gas Usage" occurs when a Customer uses Company's system supply while taking service under a transportation Rate Schedule.

If a Customer uses Company's system supply, then Customer shall pay Company for Unauthorized Gas Usage at the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$1.00 per 100 cubic feet, plus Customer's contracted Transportation Charge, for all gas taken by Customer in excess of the cumulative volume delivered to Company (less Gas-in-Kind) on behalf of Customer.

(Continued on Sheet No. F-17.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-16.00)

Load Balancing Storage Charge

- (a) Customer shall be charged **\$0.025** per 100 cubic feet per Month plus **1.42%** for fuel for injection, for the storage of any Month-end balance of gas that exceeds 10% of the Annual Contract Quantity. The **1.42%** for fuel for injection shall be paid for by Gas-in-Kind.
- (b) Monthly withdrawals from storage during November through March will be limited to 3% of the Customer's ACQ. Withdrawals in excess of that limit may be authorized but are subject to MichCon's sole judgment and prior approval pursuant to appropriate terms and conditions. Without prior approval, if in any Month the volume of gas received by Company, less Gas-in-Kind plus the 3% of Customer's ACQ is less than the volume of gas taken by Customer at the Delivery Point(s), then the excess delivery will be treated as unauthorized gas usage and will be charged under the Unauthorized Gas Usage provision.
- (c) Injections into storage during September and October will be limited to no more than **1.42%** of ACQ without prior approval from Company. Customer will be charged **\$0.025** per 100 cubic feet of gas, plus **1.42%** retained as fuel, for any gas injected during the September and October period that exceeds the Month-end tolerance level of **1.42%** of ACQ per Month. This charge will be in addition to any charges assessed to Customer for exceeding the Month-end balance of gas that exceeds 10% of the ACQ.

Standby Service

- (a) Charges:

Customer taking Standby Service for a facility or equipment shall pay a Monthly charge equal to Company's election of:
 - (1) \$0.065 per cubic foot, or \$65 per MMBtu, for each cubic foot, or MMBtu, of nameplate rating of the facility or equipment taking Standby Service; or
 - (2) \$0.271 per 100 cubic feet of SMDQ.
- (b) Company may require Customer to pay for facilities (e.g. additional meter(s), electronic remote metering, flow restriction devices, etc.) required to monitor Customers Standby Service contracted election.

Customer Contract

Customer is required to sign a Transportation Contract, limited as to time, which must be approved and executed by the President or a Vice President of the Company, or a designated representative, before it shall be binding upon Company.

ISSUED _____, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
_____, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED _____, 2005
IN CASE NO. U-13898

Rate Schedule TOS-F

Applicable to all Districts

**Transportation Off-System (Firm)
(Rate TOS-F)**

Service Eligibility

Service shall be available to all entities desiring to move gas through Company's system to an Off-System location.

Customer is required to sign a Contract, limited as to time, which must be approved and executed by the President or a Vice President of the Company, or a designated representative, before it shall be binding upon Company.

Definitions:

As used in this Rate Schedule:

"Equivalent Quantities" means the quantity of gas received from Customer, or for the account of Customer, at the Receipt Point(s) less Gas in Kind withheld by Company for loss and use.

"Off System" means gas that is transported from a Receipt Point into Company's system to a Delivery Point that is interconnected to another local gas distribution company or a pipeline not owned by Company.

Defined terms used in this Rate Schedule and not defined above have the same meaning as set forth in Section F1.1 or in Contract.

Type of Service Offered:

Under this Rate Schedule, Company will transport natural gas volumes on a firm basis, for Customer on Company's Dry Gas Transmission System. Company, in its sole judgment, shall have the right to determine if capacity is available for firm transportation under this Rate Schedule.

Transportation Service:

Company shall receive gas from Customer or for the account of Customer at the Receipt Point(s) and redeliver Equivalent Quantities, to Customer or for the account of Customer at the Delivery Point(s).

In accordance with Section F2.2 and Company's Nominating procedures, Customer shall advise Company of the volume of gas that Customer will cause to be delivered to Company for transportation during that Month, and the Receipt Point(s) and Delivery Point(s).

The Receipt Point(s) and Delivery Point(s) shall be mutually agreed upon by Company and Customer and set forth in the Contract.

Any rates, terms and conditions not covered by Tariff shall be as contained in Company's standard Contract for Off-System Service.

(Continued on Sheet No. F-19.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-18.00)

Rate Schedule TOS-F (Continued)

Applicable to all Districts

Imbalance:

Company and Customer shall work to keep the gas flow in balance at all times. If at any time, the volumes of gas received by Company at the Receipt Point(s) are greater or lesser than the gas delivered at the Delivery Point(s), Company may refuse, increase or decrease deliveries to correct the imbalances. If, upon termination of a Contract, Customer has not delivered to Company quantities of gas that are equal to those Customer has taken at the Delivery Point(s), Customer must deliver the deficient volumes to Company, within 60 days of the termination of Contract, at a mutually agreeable rate of delivery. If Customer fails to correct the imbalance within the 60 day period, then Customer shall pay an unauthorized usage charge to Company at a rate of the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$1.00 per 100 cubic feet for all gas taken by Customer in excess of the cumulative volume delivered to Company (less use and loss) on behalf of Customer.

Gas in Kind

Company shall retain 1.42% of all gas received at the Receipt Point(s) to compensate it for the allowance for company-use and lost-and-unaccounted-for gas on Company's system. This volume shall not be included in the quantity available for delivery to Customer. In no event will Customer pay Gas-in-Kind more than once on the same volumes.

Rates:

- (a) For contracts less than 365 days, a rate as mutually agreed to by Customer and Company and set forth in Contract, consisting of a demand portion and/or a commodity portion.
- (b) For contracts equal to or exceeding 365 days, a rate not to exceed \$0.02690 per 100 cubic feet, consisting of a demand portion and/or a commodity portion shall be mutually agreed to by Customer and Company and set forth in Contract.

Late Payment Charge and Due Date

A late payment charge of 2% shall be applied to the unpaid balance outstanding if the bill is not paid in full on or before the date on which the bill is due. The due date of the customer's bill shall be 21 days from the date of mailing.

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

Rate Schedule TOS-I

Applicable to all Districts

**Transportation Off-System (Interruptible)
(Rate TOS-I)**

Service Eligibility

Service shall be available to all entities desiring to move gas through Company's system to an Off-System location.

Customer is required to sign a Contract, limited as to time, which must be approved and executed by the President or a Vice President of the Company, or a designated representative, before it shall be binding upon Company.

Definitions:

As used in this Rate Schedule:

"Equivalent Quantities" means the quantity of gas received from Customer, or for the account of Customer, at the Receipt Point(s) less Gas in Kind withheld by Company for loss and use.

"Off System" means gas that is transported from a Receipt Point into Company's system to a Delivery Point that is interconnected to another local gas distribution company or a pipeline not owned by Company.

Defined terms used in this Rate Schedule and not defined above have the same meaning as set forth in Section F1.1 or in Contract.

Type of Service Offered:

Under this Rate Schedule, Company will transport natural gas volumes on an interruptible basis, for Customer on Company's Dry Gas Transmission System. Company, in its sole judgment, shall have the right to determine, on a day-to-day basis, if capacity is available for interruptible transportation under this Rate Schedule.

Transportation Service:

Company shall receive gas from Customer or for the account of Customer at the Receipt Point(s) and redeliver Equivalent Quantities, to Customer or for the account of Customer at the Delivery Point(s).

In accordance with Section F2.2 and Company's Nominating procedures, Customer shall advise Company of the volume of gas that Customer will cause to be delivered to Company for transportation during that Month, and the Receipt Point(s) and Delivery Point(s).

The Receipt Point(s) and Delivery Point(s) shall be mutually agreed upon by Company and Customer and set forth in the Contract.

Any rates, terms and conditions not covered by Tariff shall be as contained in Company's standard Contract for Off-System Service.

(Continued on Sheet No. F-21.00)

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

(Continued From Sheet No. F-20.00)

Rate Schedule TOS-I (Continued)

Applicable to all Districts

Imbalance:

Company and Customer shall work to keep the gas flow in balance at all times. If at any time, the volumes of gas received by Company at the Receipt Point(s) are greater or lesser than the gas delivered at the Delivery Point(s), Company may refuse, increase or decrease deliveries to correct the imbalances. If, upon termination of a Contract, Customer has not delivered to Company quantities of gas that are equal to those Customer has taken at the Delivery Point(s), Customer must deliver the deficient volumes to Company, within 60 days of the termination of Contract, at a mutually agreeable rate of delivery. If Customer fails to correct the imbalance within the 60 day period, then Customer shall pay an unauthorized usage charge to Company at a rate of the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$1.00 per 100 cubic feet for all gas taken by Customer in excess of the cumulative volume delivered to Company (less use and loss) on behalf of Customer.

Gas in Kind

Company shall retain 1.42% of all gas received at the Receipt Point(s) to compensate it for the allowance for company-use and lost-and-unaccounted-for gas on Company's system. This volume shall not be included in the quantity available for delivery to Customer. In no event will Customer pay Gas-in-Kind more than once on the same volumes.

Rates:

- (a) For contracts less than 365 days, a rate as mutually agreed to by Customer and Company and set forth in Contract, consisting of a demand and/or a commodity portion.
- (b) For contracts equal to or exceeding 365 days, a rate not to exceed \$0.02690 per 100 cubic feet, consisting of a demand and/or a commodity portion shall be mutually agreed to by Customer and Company and set forth in Contract.

Late Payment Charge and Due Date

A late payment charge of 2% shall be applied to the unpaid balance outstanding if the bill is not paid in full on or before the date on which the bill is due. The due date of the customer's bill shall be 21 days from the date of mailing.

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

Rate Schedule CS-F

Applicable to all Districts

Contract Storage Rate-Firm

Availability:

This Rate Schedule is available to all entities desiring firm storage service to the extent that:

- (a) Company has determined that it has sufficient available and uncommitted storage capacity to perform the service requested by the entity; and
- (b) Customer is required to sign a Contract, limited as to time, which must be approved and executed by the President or a Vice President of the Company, or a designated representative, before it shall be binding upon Company.

Characteristics of Service:

Any rates, terms and conditions not covered by the Tariff shall be as contained in the Contract.

Service commitments under any Contract for storage services are limited to a maximum of five years. Contracts which exceed a five-year term must state that service beyond the five-year limitation is on an "as available" basis.

Gas in Kind

Fuel for injection of **1.42%** shall be paid for by Gas-in-Kind.

Rates:

The Storage Charge shall be a rate not to exceed \$0.15 per 100 cubic feet, consisting of a demand portion and a commodity portion, as provided by Contract.

Late Payment Charge and Due Date

A late payment charge of 2% shall be applied to the unpaid balance outstanding if the bill is not paid in full on or before the date on which the bill is due. The due date of the customer's bill shall be 21 days from the date of mailing.

(Continued on Sheet No. F-23.00)

**ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS**

DETROIT, MICHIGAN

**EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005**

**ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898**

(Continued From Sheet No. F-22.00)

Rate Schedule CS-F (Continued)

Applicable to all Districts

Penalty Charges:

Company is authorized to charge storage Customers for deliveries to, or redeliveries from, storage in excess of the maximum volumes set forth in the Contract. The penalty rates shall not exceed the rate of the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$1.00 per 100 cubic feet for all gas taken by Customer in excess of the cumulative volume delivered to Company (less use and loss) on behalf of Customer.)

Customer shall request the withdrawal of all its gas in storage for delivery to the Delivery Point(s) on or before the last Gas Day on the term of the Contract. If, upon termination of the Contract, Customer has not requested the withdrawal of all its gas in storage, then the Customer's remaining volumes shall be deemed sold to Company at a rate of the MichCon City Gate Index as published in Gas Daily less \$0.050 per 100 cubic feet. Payment for the volumes left in storage shall appear as a credit on the last statement rendered by Company. To the extent that the credit exceeds the total charges in that statement, Company shall pay the difference to Customer.

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

Rate Schedule CS-I

Applicable to all Districts

Contract Storage Rate-Interruptible

Availability:

This Rate Schedule is available to all entities desiring interruptible storage service to the extent that:

- (a) Company has determined that it has sufficient available and uncommitted storage capacity to perform the service requested by the entity; and
- (b) Customer is required to sign a Contract, limited as to time, which must be approved and executed by the President or a Vice President of the Company, or a designated representative, before it shall be binding upon Company.

Characteristics of Service:

Any rates, terms and conditions not covered by the Tariff shall be as contained in the Contract.

Service commitments under any Contract for storage services are limited to a maximum of five years. Contracts which exceed a five-year term must state that service beyond the five-year limitation is on an "as available" basis.

On any Gas Day, gas that is nominated to Company for injection or withdrawal is subject to interruption at the sole discretion of Company.

Gas in Kind

Fuel for injection of **1.42%** shall be paid for by Gas-in-Kind.

Rates:

The Storage Charge shall be a rate not to exceed \$0.15 per 100 cubic feet, consisting of a demand portion and a commodity portion, as provided by Contract.

Late Payment Charge and Due Date

A late payment charge of 2% shall be applied to the unpaid balance outstanding if the bill is not paid in full on or before the date on which the bill is due. The due date of the customer's bill shall be 21 days from the date of mailing.

(Continued on Sheet No. F-25.00)

**ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS**

DETROIT, MICHIGAN

**EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005**

**ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898**

(Continued From Sheet No. F-24.00)

Rate Schedule CS-I (Continued)

Applicable to all Districts

Penalty Charges:

Company is authorized to charge storage Customers for deliveries to, or redeliveries from, storage in excess of the maximum volumes set forth in the Contract. The penalty rates shall not exceed the rate of the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus \$1.00 per 100 cubic feet for all gas taken by Customer in excess of the cumulative volume delivered to Company (less use and loss) on behalf of Customer.)

Customer shall request the withdrawal of all its gas in storage for delivery to the Delivery Point(s) on or before the last Gas Day on the term of the Contract. If, upon termination of the Contract, Customer has not requested the withdrawal of all its gas in storage, then the Customer's remaining volumes shall be deemed sold to Company at a rate of the MichCon City Gate Index as published in Gas Daily less \$0.050 per 100 cubic feet. Payment for the volumes left in storage shall appear as a credit on the last statement rendered by Company. To the extent that the credit exceeds the total charges in that statement, Company shall pay the difference to Customer.

ISSUED ____ __, 2005 BY
M. E. CHAMPLEY
SENIOR VICE PRESIDENT
REGULATORY AFFAIRS

DETROIT, MICHIGAN

EFFECTIVE FOR GAS SERVICE
RENDERED ON AND AFTER
____ __, 2005

ISSUED UNDER AUTHORITY OF THE
MICHIGAN PUBLIC SERVICE COMM.
DATED ____ __, 2005
IN CASE NO. U-13898

Attachment B

Michigan Consolidated Gas Company
Case No. U-13898
Allocation of Uncollectibles Expense

<u>Description</u>	<u>Allocation Factor</u>
Rate 1	21.366111%
Rate 2, 3, and 3A	69.373784%
Rate 2A	3.246228%
Rate 10	0.311975%
Small Transportation Rate	1.755019%
Large Transportation Rate	<u>3.946884%</u>
Total Company	<u><u>100.000000%</u></u>

Line	Description	Previously Approved Rates	Newly Approved Rates	Increase (Decrease)
		(a)	(b)	(c)
1	<u>Sales Service</u>			
2	Residential - Rate A (Rate 2)			
3	Customer Charge	\$7.50 per month	\$8.50 per month	\$1.00 per month
4	Distribution Charge	\$1.4488 per Mcf	\$1.7013 per Mcf	\$0.2525 per Mcf
5				
6	Residential - Rate 3 - Senior Citizens			
7	Customer Charge	\$7.50 per month	Transferred to Rate AS	
8	Distribution Charge	\$1.3442 per Mcf	Transferred to Rate AS	
9				
10	Residential - Rate AS (Rate 3A, Senior Citizens)			
11	Customer Charge	\$7.50 per month	\$8.50 per month	\$1.00 per month
12	Winter Discount (December - March)	(\$12.00) per month	(\$12.00) per month	\$0.00 per month
13	Distribution Charge	\$1.4488 per Mcf	\$1.7013 per Mcf	\$0.2525 per Mcf
14				
15	Residential - Rate 2A (Multi-Family)			
16	Customer Charge - Meter Class 1	\$7.50 per month	\$8.50 per month	\$1.00 per month
17	- Meter Class 2	\$15.00 per month	\$20.00 per month	\$5.00 per month
18	Distribution Charge	\$1.4488 per Mcf	\$1.7013 per Mcf	\$0.2525 per Mcf
19				
20	General Service - Rate GS-1 (Rate 1)			
21	Customer Charge	\$15.00 per month	\$20.00 per month	\$5.00 per month
22	Distribution Charge	\$1.8179 per Mcf	\$1.9431 per Mcf	\$0.1252 per Mcf
23				
24	General Service - Rate GS-2 (Rate 6)			
25	Customer Charge	\$600.00 per month	\$475.00 per month	(\$125.00) per month
26	Distribution Charge	\$1.3469 per Mcf	\$1.5533 per Mcf	\$0.2064 per Mcf
27				
28	Non-Residential - Rate 8	Closed	Eliminated	
29				
30	Schools - Rate 10			
31	Customer Charge	\$200.00 per month	\$200.00 per month	\$0.00 per month
32	Distribution Charge	\$1.4841 per Mcf	\$1.4841 per Mcf	\$0.0000 per Mcf
33				
34				
35	<u>Transportation Service</u>			
36	Service Category ST (Rates ST-1 & ST-2)			
37	Customer Charge	\$1,300.00 per month	\$1,300.00 per month	\$0.00 per month
38	Cost Based Rate	\$0.6420 per Mcf	\$0.8078 per Mcf	\$0.1658 per Mcf
39	Optional Maximum Rate	\$0.9630 per Mcf	\$1.3856 per Mcf	\$0.4226 per Mcf
40	Optional Minimum Rate	\$0.2300 per Mcf	\$0.2300 per Mcf	\$0.0000 per Mcf
41				
42	Service Category LT (Rates LT-1 & LT-2)			
43	Customer Charge	\$2,100.00 per month	\$3,375.00 per month	\$1,275.00 per month
44	Cost Based Rate	\$0.5458 per Mcf	\$0.5596 per Mcf	\$0.0138 per Mcf
45	Optional Maximum Rate	\$0.8187 per Mcf	\$0.8892 per Mcf	\$0.0705 per Mcf
46	Optional Minimum Rate	\$0.2300 per Mcf	\$0.2300 per Mcf	\$0.0000 per Mcf
47				
48	Service Category XLT (New)			
49	Customer Charge	\$2,100.00 per month	\$11,300.00 per month	\$9,200.00 per month
50	Remote Meter Charge	\$0.00 per month	\$100.00 per month	\$100.00 per month
51	Cost Based Rate	\$0.5458 per Mcf	\$0.4219 per Mcf	(\$0.1239) per Mcf
52	Optional Maximum Rate	\$0.8187 per Mcf	\$0.6638 per Mcf	(\$0.1549) per Mcf
53	Optional Minimum Rate	\$0.2300 per Mcf	\$0.1800 per Mcf	(\$0.0500) per Mcf
54				
55	Other Transportation Charges			
56	Unauthorized Gas Usage Charge	\$10.00 per Mcf	\$10.00 per Mcf	\$0.00 per Mcf
57	Load Balancing Storage Charge	\$0.2500 per Mcf	\$0.2500 per Mcf	\$0.0000 per Mcf
58	Gas In Kind	1.67%	1.42%	-0.25%

Notes:

Service Category ST is most economical for customers with annual usage less than 100,000 Mcf.
 Service Category LT is most economical for customers with annual usage greater than 100,000 Mcf, but less than 700,000.
 Service Category XLT is most economical for customers with annual usage greater than 700,000 Mcf.

