

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)	
SEMCO ENERGY GAS COMPANY for amortization)	Case No. U-15679
treatment of certain deferred pension and other)	
post-retirement benefit costs.)	
_____)	

At the August 11, 2009 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. Orjiakor N. Isiogu, Chairman
Hon. Monica Martinez, Commissioner
Hon. Steven A. Transeth, Commissioner

ORDER APPROVING SETTLEMENT AGREEMENT

On September 18, 2008, SEMCO Energy Gas Company (SEMCO) filed an application seeking approval of accounting authority to amortize certain costs associated with pension and other post-retirement benefits (OPEB) obligations.

In its application, SEMCO states that pursuant to a share exchange, SEMCO Holding Corporation, a wholly-owned subsidiary of Cap Rock Holding Corporation, acquired all of the outstanding stock of SEMCO Energy, Inc. (Share Exchange) on November 9, 2007 (Acquisition Date). Before the Acquisition Date, SEMCO had used smoothing mechanisms to partially defer certain costs of its pension and OPEB obligations. SEMCO states that in accordance with the Statement of Financial Accounting Standards (SFAS) Nos. 87 and 106, the sponsors of pension and OPEB plans are required to defer and then gradually reflect amortization of previously unrecognized prior service costs over an expected service life, experience (actuarial) losses, and

transition costs as a normal part of the plans' future periodic costs. These unrecognized deferred costs were recorded as regulatory assets with the adoption of SFAS No. 158 in December 31, 2006. During the period between December 31, 2006, and the Acquisition Date, the regulatory assets were reduced by the amount of amortization reflected in the plans' periodic costs under SFAS Nos. 87 and 106.

In the application, SEMCO further states that under the purchase accounting provisions of SFAS Nos. 87 (paragraph 74) and 106 (paragraphs 86-88), when a business acquisition such as the Share Exchange occurs, the remaining unrecognized costs associated with the plans of the acquired business are excluded from the calculation for the plans' periodic costs for periods after the acquisition. Thus, as of the Acquisition Date, these costs were no longer amortized as part of SEMCO's periodic pension and OPEB costs.

SEMCO states that it seeks to amortize its unrecognized costs by continuing an amortization period based on the expected service life beginning on the Acquisition Date. These unrecognized costs represent the costs SEMCO experienced before the Share Exchange and were deferred under the requirements of SFAS Nos. 87, 106, and 158, including experience losses, prior service costs, and transition costs.

SEMCO also states that the amortization period, based on the expected service life, will closely align with the costs that SEMCO would have recognized in expense if the Share Exchange had not occurred and the company had continued to expense these same costs for SFAS Nos. 87 and 106 purposes.

On October 1, 2008, Attorney General Michael A. Cox (Attorney General) filed a petition to intervene, and on December 10, 2008, SEMCO filed its response. On February 12, 2009, a

prehearing conference was held before Administrative Law Judge Mark D. Eyster. SEMCO, the Commission Staff, and the Attorney General participated in the proceeding.

Subsequently, the parties filed a settlement agreement resolving all issues in the case. According to the terms of the settlement agreement, attached as Exhibit A, the parties agree that SEMCO's application should be approved, and that SEMCO's request for amortization treatment for the pension and OPEB costs as described in the application, and set forth in Attachment A to the settlement agreement, should be approved effective November 9, 2007. The parties further agree that granting the requested approval is for accounting treatment purposes only and has no ratemaking effect. The parties agree that the reasonableness of the recovery through rates of the pension and OPEB costs will be fully considered in SEMCO's next general rate case. Finally, SEMCO agrees that the post-Acquisition Date pension and OPEB costs that have been amortized up to the historic period of the next general rate case filing will not be included for recovery purposes in the company's next general rate case.

The Commission finds that the settlement agreement is reasonable, in the public interest, and should be approved.

THEREFORE, IT IS ORDERED that:

A. The settlement agreement, attached as Exhibit A, is approved.

B. SEMCO Energy Gas Company is authorized beginning November 9, 2007, to amortize the pension and other post employment benefits costs as described in the settlement agreement and set forth in Attachment A to the settlement agreement.

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, under MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

Orjiakor N. Isiogu, Chairman

Monica Martinez, Commissioner

Steven A. Transeth, Commissioner

By its action of August 11, 2009.

Mary Jo Kunkle, Executive Secretary

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)	
SEMCO ENERGY GAS COMPANY)	Case No. U-15679
for amortization treatment of certain deferred)	
<u>pension and other post-retirement benefit costs.</u>)	

SETTLEMENT AGREEMENT

As provided in Section 78 of the Administrative Procedures Act of 1969 (“APA”), as amended, MCL 24.278, and the Commission’s Rules of Practice and Procedure, Rule 333, 1999 AC R 460.17333, SEMCO Energy Gas Company (“SEMCO Gas” or the “Company”), the Michigan Public Service Commission Staff (“Staff”) and the Attorney General (“AG”) have resolved through settlement discussions the contested issues regarding this proceeding and hereby agree as follows:

1. On September 18, 2008, SEMCO Gas filed its application with the Michigan Public Service Commission (“MPSC” or the “Commission”) seeking approval of accounting authority to amortize certain costs associated with pension and other post-retirement benefit costs. As represented in the application, pursuant to a share exchange, SEMCO Holding Corporation, a direct wholly-owned subsidiary of Cap Rock Holding Corporation, acquired all of the outstanding stock of SEMCO Energy, Inc., (“Share Exchange”), on November 9, 2007 (“Acquisition Date”). Prior to the Acquisition Date,

SEMCO Gas had used smoothing mechanisms to partially defer certain costs, e.g. prior service costs, transition costs, actuarial losses, etc., of its pension and other post-employment benefit (“OPEB”) obligations. SEMCO Gas represents that in accordance with, and as prescribed by, the Statements of Financial Accounting Standards (“SFAS” or “Standards”) Nos. 87 and 106, the sponsors of pension and OPEB plans are required to defer and then gradually reflect amortization of previously unrecognized prior service costs over an expected service life, experience (actuarial) losses, and transition costs as a normal part of the plans’ future periodic costs. These unrecognized deferred costs were recorded as regulatory assets with the adoption of SFAS No. 158 in December 31, 2006. During the period between December 31, 2006, and the Acquisition Date, the regulatory assets were reduced by the amount of amortization reflected in the plans’ periodic costs under SFAS Nos. 87 and 106.

As further represented in the application, under the purchase accounting provisions of SFAS Nos. 87 (paragraph 74) and 106 (paragraphs 86-88), when a business acquisition occurs such as the Share Exchange, the remaining unrecognized costs associated with the plans of the acquired business are excluded from the calculation for the plans’ periodic costs for periods after the acquisition. Thus, as of the Acquisition Date, these costs are no longer amortized as part of SEMCO Gas’s periodic pension and OPEB costs.

SEMCO Gas states in the application that it seeks to amortize its unrecognized costs by continuing an amortization period based on the expected service life beginning

on the Acquisition Date. The unrecognized costs, set forth in Attachment A hereto, at the Acquisition Date represent the costs SEMCO Gas experienced prior to the Share Exchange and were deferred under the requirements of SFAS Nos. 87, 106 and 158, including experience losses, prior service costs and transition costs.

SEMCO Gas represents that the amortization period, based on the expected service life, will closely align with the costs that SEMCO Gas would have recognized in expense if the Share Exchange had not occurred and the Company had continued to expense these same costs for SFAS 87 and SFAS 106 purposes.

2. On October 1, 2008, the AG filed his notice of intervention and request for a contested hearing, and on December 10, 2008, SEMCO Gas filed its response to the AG's intervention and request for hearing.

3. On January 21, 2009, the Commission's Executive Secretary issued a Notice of Hearing directing SEMCO Gas to mail a copy of the Notice of Hearing to all cities, incorporated villages, townships and counties in its Michigan service area. Further, SEMCO Gas was directed to publish the Notice of Hearing in daily newspapers of general circulation throughout its Michigan service area.

4. On February 12, 2009, a prehearing conference was held. Administrative Law Judge Mark D. Eyster presided over the proceeding. SEMCO Gas electronically submitted the requisite Affidavit of Mailing and Affidavit of Publication prior to the conference. SEMCO Gas, Staff, and the AG participated in the proceeding.

5. On April 1, 2009, SEMCO Gas filed the direct testimony and exhibit of Steven W. Warsinske in support of its application.

6. Subsequent to the prehearing conference, the parties engaged in settlement discussions and have agreed that SEMCO Gas's application should be approved, and that SEMCO Gas request for amortization treatment for the pension and OPEB costs as described in the application and set forth in Attachment A hereto should be approved effective November 9, 2007. The parties further agree that granting the requested approval is for accounting treatment purposes only and has no ratemaking effect. Therefore, because it is agreed that this approval is for accounting treatment only, it is understood that the reasonableness of the recovery through rates of the pension and OPEB costs will be fully considered in SEMCO Gas's next general rate case. Finally, SEMCO Gas agrees the post-Acquisition Date pension and OPEB costs that have been amortized up to the historic period of the next general rate case filing, will not be included for recovery purposes in the Company's next general rate case.

7. Pursuant to Rule 333(6) of the Commission's Rules of Practice and Procedure, R 460.17333(6), the parties agree any order approving this settlement agreement shall not establish precedent for future proceedings and shall not be used as such. This settlement agreement is entered into for the sole and express purpose of reaching a compromise among the parties. All offers of settlement and discussions relating to this settlement are considered privileged under MRE 408. If the Commission approves this settlement agreement without modification, neither the parties to the

settlement nor the Commission shall make any reference to, or use this settlement agreement or the order approving it, as a reason, authority, rationale or example for taking any action or position or making any subsequent decision in any other case or proceeding; provided however, such references may be made to enforce or implement the provisions of this settlement agreement and the order approving it.

8. If the Commission approves this settlement agreement, without modification, the undersigned parties agree not to appeal, challenge or otherwise contest the Commission order approving this settlement agreement only. Except as otherwise set forth herein, the parties agree and understand that this settlement agreement does not limit any party's right to take new and/or different positions on similar issues in other administrative proceedings, or appeals related thereto.

9. This settlement agreement is not severable. Each provision of this settlement agreement is dependent upon all other provisions of this settlement agreement. Failure to comply with any provision of this settlement agreement constitutes failure to comply with the entire settlement agreement. If the Commission rejects or modifies this settlement agreement or any provision of this settlement agreement, this settlement agreement shall be deemed to be withdrawn, shall not constitute any part of the record in this proceeding or be used for any other purpose, and shall not operate to prejudice the pre-negotiation positions of any party.

10. The Staff agrees that this settlement agreement is reasonable and in the public interest.

11. The parties agree to waive Section 81 of the Administrative Procedures Act of 1969 (MCL 24.281), as it applies to the issues in this proceeding, if the Commission approves this settlement agreement without modification.

SEMCO ENERGY GAS COMPANY

Dated: July 1, 2009

By: _____
One of Its Attorneys
Sherri A. Wellman (P38989)
Michael C. Rampe (P58189)
Miller, Canfield, Paddock & Stone, P.L.C.
One Michigan Avenue, Suite 900
Lansing, MI 48933

MICHIGAN PUBLIC SERVICE COMMISSION
STAFF

Dated: July 1, 2009

By: _____
One of Its Attorney
Kristin M. Smith (P46323)
Anne M. Uitvlugt (P71641)
Assistant Attorney General
Public Service Division
6545 Mercantile Way, Suite 15
Lansing, MI 48911

ATTORNEY GENERAL

Dated: July 1, 2009

By: _____

Its Attorney

Donald E. Erickson (P13212)

Attorney General's Office

Tobacco & Special Litigation Division

7th Floor G. Mennen Williams Bldg.

525 West Ottawa

Lansing, MI 48911

LALIB:178450.1\129584-00026

ATTACHMENT A

SEMCO Energy, Inc. Pension and Retiree Medical Plans
Estimates of Certain Expense Amortization Components prior to Purchase Accounting Adjustments

As of November 8, 2007

(Figures in \$000s)

<u>SEMCO Plans</u>	Non-Union Pension	Union Pension	Non-Union Retiree Medical	Union Retiree Medical	Total
Projected Benefit Obligation	(40,640)	(25,797)	(20,361)	(15,972)	(102,770)
Fair Value of Assets	37,522	23,320	14,932	17,727	93,501
Funded Status	(3,118)	(2,477)	(5,429)	1,755	(9,269)
Unrecognized (Gain)/Loss	10,497	5,881	4,129	3,152	23,659
Amortization Period	11.83	12.40	13.75	12.84	
Annual Amortization Amount	888	474	300	245	1,907
PSC Amortization Bases:					
(1) Date Established	1/1/1998	12/31/2001	1/1/2004	12/31/2006	
Unrecognized Amount	(183)	(142)	(1,650)	(245)	(2,220)
Remaining Period as of Valuation Date	5.75	8.81	6.51	8.16	
Annual Amortization Amount	(32)	(16)	(253)	(30)	(331)
(2) Date Established	10/1/2000		12/31/2006		
Unrecognized Amount	262		(775)		(513)
Remaining Period as of Valuation Date	8.13		8.68		
Annual Amortization Amount	32		(89)		(57)
Total Unrecognized Amounts	10,576	5,739	1,704	2,907	20,926
Total Current Annual Amortization Amounts	888	458	(42)	215	1,519
Level 13.75 Year Amortization Amounts	769	417	124	211	1,522

The results presented above are based on the data, assumptions and methods outlined in the actuarial valuation report to determine accounting disclosure requirements as of 11/8/2007. Therefore, the descriptions of the data, assumptions, methods and limitations of the valuation and its use should be considered part of the above schedule. This schedule was prepared by consultants of Watson Wyatt Worldwide with actuarial credentials that meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein. There is no relationship between SEMCO and Watson Wyatt Worldwide that impacts our objectivity.