STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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| In the matter of the application of<br>**CONSUMERS ENERGY COMPANY** for approval<br>of an experimental pilot program for expanded<br>gas customer choice, including an expanded gas<br>transportation program, a suspension of its gas<br>cost recovery clause, a moratorium on non-GCR<br>rate adjustments, an earnings sharing mechanism,<br>and related relief.<br>_________________________________ | )<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>) | Case No. U-11599 |

At the December 19, 1997 meeting of the Michigan Public Service Commission in Lansing, Michigan.

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

## ORDER APPROVING APPLICATION

On December 9, 1997, Consumers Energy Company (Consumers) filed an application for approval of a voluntary experimental pilot program for expanded gas customer choice (EGCC program). As part of its EGCC program, Consumers proposes to expand its gas transportation program, eliminate Rate SC-T and replace it with Rate CC, suspend its gas cost recovery (GCR) clause, freeze its gas commodity charge at the currently authorized GCR factor, freeze its distribution service rates at current levels, and establish a revenue sharing mechanism.

Consumers states that the proposed program should provide more complete and comprehensive information concerning customer choice than the program approved in Case No. U-11249 and contained in Rate SC-T, which was a pilot program limited to customers in Bay County. As proposed, the EGCC program would supersede the Case No. U-11249 pilot program, which would no longer be available for service effective with the commencement of service under the EGCC program. Consumers proposes that the EGCC program have a term of three years, commencing April 1, 1998.

Consumers states that the EGCC program will (i) allow 300,000 residential, commercial, and industrial retail gas sales customers to choose their gas supplier, (ii) allow competing gas suppliers, including gas marketers and brokers, to market natural gas to a large number of retail customers in direct competition with Consumers, (iii) be available to customers throughout the company's gas service territory, (iv) be available to customers in all sales classes, (v) allow suppliers to independently determine their needs for pipeline capacity necessary to deliver gas to Consumers' system and obtain that capacity in whatever manner and from whatever source they deem appropriate, and (vi) allow customers to choose to participate at any time during the course of the year, rather than being restricted to a limited sign-up period.

Consumers states that participation will be strictly voluntary and that participating customers will be selected, on a first come, first served basis, up to a maximum of 100,000 customers commencing April 1, 1998, 200,000 customers commencing April 1, 1999, and 300,000 customers commencing April 1, 2000. Consumers states that rates for transportation service under Rate CC will be the same as those approved in Case No. U-11249.

In conjunction with the EGCC program, Consumers included in its proposed tariff sheets transportation standards of conduct that it states are intended to promote fair competition and a level playing field among all participants involved in transportation within Consumers' service territory. Consumers states that it will conduct its business in conformance with the proposed standards and agrees to establish a complaint procedure that gives marketers and brokers a forum to address any complaints related to those standards.

Consumers further states that it will continue offering a fully bundled service to all customers who desire such service. It also states that to protect customers (nonparticipants as well as participants) from distribution service cost increases or cost shifts during the term of the program, and to maximize the incentive for Consumers to control its costs and make efficient business decisions, the company would, with two exceptions, freeze its distribution service rates for all retail gas customers. Consumers therefore requests that, during the term of the program, the Commission (i) suspend Consumers' GCR clause, (ii) establish a gas commodity charge at the currently authorized GCR charge of $2.8364 per thousand cubic feet (Mcf) for customers who remain full service customers, and (iii) freeze distribution rates at currently authorized levels. According to Consumers, the 90/10 revenue sharing mechanisms that have been administered through the GCR process should also be suspended for the term of the EGCC program.

Under Consumers' proposal, the April 1997 through March 1998 GCR period would be subject to reconciliation in the normal fashion. However, no plan or reconciliation would be conducted for the period beginning April 1, 1998 and thereafter for the term of the EGCC program.

The distribution rate freeze proposed by Consumers is subject to two exceptions. They are that (i) Consumers agrees to make refunds pursuant to a revenue sharing mechanism if earnings exceed certain levels, and (ii) Consumers or other interested parties may seek a limited issue rate case to adjust rates to reflect the effect of significant changes in laws, regulations, accounting requirements, or taxes that impact Consumers' annual revenue requirement by more than $5 million. Under the utility’s proposal, if Consumers' return on equity for its gas business (currently authorized at 11.6%) exceeds 13.50%, amounts equal to 50% of the earnings between 13.51% and 17.50%, plus amounts equal to 75% of the earnings over 17.50%, would be refunded to customers. The methodology for determining the amounts subject to refund is described in Consumers' application.

Consumers goes on to state that information will be gathered to determine potential benchmarks for evaluating system safety, reliability, and distribution service to its customers. It states that it will submit an application on or before June 1, 1998 for implementation of performance criteria to be effective during the second year of the EGCC program.

Consumers states that the EGCC program should provide substantial information and experience concerning (i) the degree to which retail gas customers desire the opportunity to select alternative gas suppliers, (ii) the various ways customers respond to having additional gas supply choices, (iii) the extent and nature of alternative gas supply and pricing options made available to customers by alternative suppliers, (iv) the means by which alternative gas suppliers obtain the gas supplies and interstate transportation necessary to satisfy customer demands in a competitive environment, as well as the reliability of those means, (v) the extent to which incentive-based regulation is an appropriate long-term substitute for rate of return regulation of local distribution companies, and (vi) the continued need for GCR mechanisms like those provided by 1982 PA 304 (Act 304), MCL 460.6h et seq.; MSA 22.13(6h) et seq., in an environment where customers have the ability to purchase gas from multiple suppliers.

On December 11, 1997, the Association of Businesses Advocating Tariff Equity (ABATE) filed an objection to Consumers' application, a demand for hearing, and petition for leave to intervene; Attorney General Frank J. Kelley filed a motion for a hearing and a petition for leave to intervene; and the Residential Ratepayer Consortium filed a request for hearing and petition for leave to intervene. On December 18, 1997, ABATE filed a supplement to its objection, and Enron Energy Services Corp. filed a motion for a contested case hearing and petition for leave to intervene.

Discussion

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

The proposed EGCC program is larger and more comprehensive than the pilot program approved in Case No. U-11249. Specifically, although that pilot program provided opportunities for up to 40,000 sales customers in a limited geographic area to choose an alternative gas supplier, the EGCC program will provide up to 300,000 sales customers (approximately 20 percent of Consumers' sales customers) located throughout Consumers' service territory the opportunity to purchase gas from other suppliers. Thus, the EGCC program would likely serve as a better source of information than the pilot program approved in Case No. U-11249.

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

There is no mechanism in Consumers’ proposal to increase charges for system supply gas during the EGCC program even if gas commodity prices increase. However, there are two exceptions to the freeze on noncommodity rates. The first is a revenue sharing mechanism, which provides for a portion of earnings to be returned to customers if earnings on common equity exceed certain levels. Consumers states that if its proposed program is approved, it would make the refunds equivalent to a portion of the excess. No rate increases can result from the operation of this mechanism, even if Consumers’ gas utility business earned return on equity falls below its authorized level. The amount to be refunded will be determined in accordance with a specified formula set forth in Consumers' application. This type of revenue sharing mechanism was approved by the Commission in its December 19, 1991 order in Case No. U-10037, and its legality was affirmed by the Court of Appeals in Attorney General v Public Service Comm, 206 Mich App 290; 520 NW2d 636 (1994). These potential refunds benefit customers.

Consumers also proposes to file an exhibit similar to Attachment F to its application, along with any necessary workpapers supporting its calculation, not later than July 1 of 1999, 2000, and 2001, respectively, identifying the amount, if any, to be refunded to customers under the revenue sharing mechanism. It proposes that parties be given 30 days to request a hearing regarding the calculations and that the scope of any hearing be limited to the filing's accuracy and conformance to Attachment F. It further proposes that, if no hearing is requested, it be allowed to promptly implement any applicable refund.

The second exception to the noncommodity rate freeze is if there are changes in laws, regulations, accounting requirements, or taxes that impact Consumers' annual revenue requirement by more than $5 million. If such changes occur, Consumers or other interested persons would have a right to seek a limited issue rate case to adjust rates to reflect the impact of such changes. This provision does not establish that a change will occur. Rather it gives parties a right to seek such a change. Any change would be subject to all applicable procedural and statutory requirements, including any applicable requirements for notice and opportunity for hearing.

After review of the application, the Commission finds that Consumers' proposals are reasonable and in the public interest, and should be approved. This finding reflects the Commission's belief that experimentation with alternative, more flexible regulatory mechanisms is appropriate in view of the changing nature of the gas utility industry. Further, the Commission is persuaded that approval of the proposed experimental program is appropriate because, among other things, it provides incentives to the utility to operate in an efficient manner and should enhance the utility's ability to respond to market demands.

Implementation of the EGCC program should coincide with the April 1998 storage injection cycle. Thus, prompt Commission action is necessary in order to allow a systemwide education effort to inform customers about the program and allow alternative suppliers an opportunity to solicit customers. Further, since the proposal would suspend the GCR process, it would be preferable for the Commission to take action prior to the December 31, 1997 deadline for filing Consumers' next GCR plan case.

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

The Commission FINDS that:

a. Jurisdiction is pursuant to 1909 PA 300, as amended, MCL 462.2 et seq.; MSA 22.21 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; MSA 22.1 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; MSA 22.13(1) et seq.; 1982 PA 304, as amended, MCL 460.6h et seq.; MSA 22.13(6h) et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; MSA 3.560(101) et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACS, R 460.17101 et seq.

b. Consumers' application for authority to implement an expanded experimental pilot program for expanded gas customer choice, including an expanded gas transportation program, a suspension of its GCR clause, a moratorium on gas commodity and nongas commodity adjustments, and a revenue sharing mechanism should be approved.

c. The adoption of the EGCC program, as reflected in the tariff sheets and the standard authorized gas supplier contract attached to this order as Exhibits A and B, respectively, is reasonable and in the public interest, and should be approved.

d. Suspension of the GCR clause for a three-year period beginning April 1, 1998 and establishment of a gas commodity charge at the existing retail sales rate of $2.8364 per Mcf is reasonable and in the public interest, and should be approved as part of the EGCC program.

e. Consumers should not be required to file a GCR plan or reconciliation case for any of the three years beginning April 1998, April 1999, and April 2000. Consumers should be required to file, according to the normal schedule, a GRC reconciliation proceeding for the year April 1997 through March 1998. The gas commodity charge of $2.8364 per Mcf should not be subject to reconciliation with actual gas costs during the three-year experimental program.

f. Approval of a moratorium on noncommodity rate adjustments, subject to the revenue sharing mechanism and the exception for significant changes in noncommodity costs, as more fully described in the order, are reasonable and in the public interest, and should be approved as part of the EGCC program.

g. The proposed EGCC program is reasonable and in the public interest, and is consistent with the policy of the Commission and the State of Michigan to promote competition and customer choice in the gas utility industry.

h. The EGCC program (under Rate CC) will supersede the pilot program approved in Case No. U-11249 and currrently being offered under Rate SC-T.

i. The relief granted will not increase the rates of any customer and the public interest will be adequately protected without the time and expense of a public hearing.

THEREFORE, IT IS ORDERED that:

A. Consumers Energy Company is authorized to implement the experimental program described in its December 9, 1997 application.

B. Rate Schedule CC will take effect April 1, 1998, at which time service will no longer be available under Consumers Energy Company's Rate Schedule SC-T.

C. Consumers Energy Company, with respect to the regulated portion of its gas business, shall adhere to the transportation standards of conduct set forth in the tariff sheets attached as Exhibit A to this order. Moreover, Consumers Energy Company shall establish a complaint procedure as detailed in its application.

D. Consumers Energy Company's gas cost recovery clause is suspended effective April 1, 1998 for a three-year period, during which a gas commodity cost shall be established at a fixed rate of $2.8364 per thousand cubic feet. A reconciliation proceeding shall be conducted for the plan year ending March 31, 1998.

E. Consumers Energy Company shall, within 30 days of issuance of this order, file tariff sheets incorporating all rate schedule and rule changes approved in this order.

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

G. On or before June 1, 1998, Consumers Energy Company shall file an application for implementation of performance criteria.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, pursuant to MCL 462.26; MSA 22.45.

MICHIGAN PUBLIC SERVICE COMMISSION

John G. Strand
Chairman

( S E A L )

John C. Shea
Commissioner

David A. Svanda
Commissioner

By its action of December 19, 1997.

Dorothy Wideman
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; MSA 22.45.

MICHIGAN PUBLIC SERVICE COMMISSION

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By its action of December 19, 1997.

Executive Secretary

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| rate adjustments, an earnings sharing mechanism, | ) | |
| and related relief. | ) | |
| ______________________________________ | ) | |

Suggested Minute:

> "Adopt and issue order dated December 19, 1997 authorizing Consumers Energy Company to implement an expanded gas customer choice program, suspend its gas cost recovery clause, implement a moratorium on nongas cost recovery rate adjustments, and establish a revenue sharing mechanism, as set forth in the order."