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January 12, 2004

Ms. Mary Jo Kunkle  
Michigan Public Service Commission  
6545 Mercantile Way  
P.O. Box 30221  
Lansing, MI 48909

Re: Case No. U- 13989

Dear Ms. Kunkle:

Enclosed for filing in the above captioned matter please find the original and four copies of Qualification and Testimony of Richard A. Polich on behalf of Energy Michigan. Also enclosed is the original Proof of Service indicating service on counsel.

Please date stamp one copy of the above entitled document for my records and return it in the self-addressed stamped envelope provided.

Thank you for your assistance in this matter.

Very truly yours,

VARNUM, RIDDERING, SCHMIDT & HOWLETTLLP

Eric J. Schneidewind

EJS/mrr

cc: ALJ  
parties

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of )  
CONSUMERS ENERGY COMPANY )  
For ex parte approval of a special contract )  
For electric service with the State of )  
Michigan, the Board of Trustees of )  
Western Michigan University, the Board )  
Of Trustees of Michigan State University, )  
And the Regents of the University of )  
Michigan on behalf of the University of )  
Michigan-Flint )  
\_\_\_\_\_ )

Case No. U-13989

**QUALIFICATIONS AND TESTIMONY OF RICHARD A. POLICH**

**ON BEHALF OF ENERGY MICHIGAN**

- 1 Q. Please state your name and business address.
- 2 A. My name is Richard A. Polich. My business address is PO Box 3522, Ann Arbor,  
3 Michigan
- 4 Q. By whom are you employed and what is your present position?
- 5 A. I am currently working as an independent consultant in a firm called Energy Options &  
6 Solutions.
- 7 Q. Please state your educational background.
- 8 A. I graduated from the University of Michigan in Ann Arbor in August of 1979 with a  
9 Bachelor of Science Engineering Degree in Nuclear Engineering and a Bachelor of  
10 Science Engineering Degree in Mechanical Engineering. In May 1990, I received a  
11 Masters of Business Administration from the University of Michigan in Ann Arbor.
- 12 Q. Please describe your work experience.

1 A. In May of 1978 I joined Commonwealth Associates as a Graduate Engineer and worked  
2 on several plant modification and new plant construction projects. In May 1979 I joined  
3 Consumers Power Company as an Associate Engineer in the Plant Engineering Services  
4 Department. In April of 1980 I transferred to the Midland Nuclear Project and  
5 progressed through various job classifications to Senior Engineer. I participated in the  
6 initial design evaluation of the Midland Cogeneration Plant. In July 1987 I transferred to  
7 the Market Services Department as a Senior Engineer and reached the level of Senior  
8 Market Representative. While in this department I analyzed the economic and  
9 engineering feasibility of customer cogeneration projects. In July of 1992 I transferred to  
10 the Rates and Regulatory Affairs Department of Consumers Energy as a Principal Rate  
11 Analyst. In that capacity I performed studies relating to all facets of development and  
12 design of the Consumers' gas, retail, electric and electric wholesale rates. During this  
13 period, I was heavily involved in the development of Consumers Direct Access program  
14 and in the development of Retail Open Access program. I also participated in the  
15 development of the Consumers' revenue forecast.

16 In March 1998, I joined Nordic Electric as Vice President in charge of marketing  
17 and sales. My responsibilities included all aspects of obtaining new customers and  
18 enabling Nordic to supply electricity to those customers. In May 2000, my  
19 responsibilities shifted to Operations and Regulatory Affairs. My responsibilities include  
20 management of supply purchases; transmission services, and development of new power  
21 projects. Regulatory Affairs responsibilities include over seeing regulatory and  
22 legislation issues.

23 In March of 2003, I started my own energy consulting business, Energy Options  
24 & Solutions. The primary focus of the business will be to help energy users develop  
25 solutions to energy problems.

26 Q. Are you a registered Professional Engineer in the State of Michigan?

27 A. Yes I am.

28 Q. Have you previously testified before this Commission?

1 A. Yes. I presented testimony on five occasions on behalf of Consumers Energy. In the  
2 remand phase of retail wheeling Case U-10143/U-10176 presenting the Consumers'  
3 method for design of future retail wheeling rates, the Consumers proposed Special  
4 Contract Rate Case U-10625 presenting methods to identify and qualify customers. I  
5 presented testimony in the Consumers' Electric Rate Case proceeding U-10335. I  
6 presented testimony in the initial phase of retail wheeling Case U-10143/U-10176 on the  
7 proposed cost and rate of retail wheeling and in Case U-10685 the Consumers Energy  
8 Electric Rate Case in November 1994. I presented testimony for Energy Michigan in  
9 Cases U-11915 (Supplier Licensing) and U-11956 (Edison True Up Case), U-12478 and  
10 U-12505 (Edison and Consumers Energy Securitization Cases), U-12639 (Stranded Cost  
11 Methodology Case), U-13380 (Consumers Energy Determination of Stranded Costs), U-  
12 13350 (Detroit Edison Stranded Cost Case), U-13715 (Consumers Energy Securitization  
13 of Certain of its Stranded Costs), U-13808 (Detroit Edison General Rate Case) and U-  
14 13933 (Detroit Edison Low-Income Energy Assistance Credit for Residential Electric  
15 Customers).

### 16 **PURPOSE OF TESTIMONY**

17 Q. What is the purpose of your testimony in this proceeding?

18 A. I will present to the Michigan Public Service Commission ("MPSC") testimony regarding  
19 the dangers and implications of Paragraph 5(d) ("The Paragraph") of proposed special  
20 contract between Consumers Energy and the State of Michigan, Michigan State  
21 University, Western Michigan University, and University of Michigan-Flint ("Michigan  
22 Special Contract"). In addition, I will be addressing the testimony of Consumers  
23 Energy's witness, Mr. Scott B. Brocket and the State of Michigan's witness, Mr. Mitch  
24 Irwin. Specifically, I will be addressing Mr. Brocket's discussion of the following  
25 Section of The Paragraph, which in part states as follows:

26 "Critical to such approval is the specific acknowledgement by the MPSC that it will  
27 not, in any proceeding affecting the utility rates charged by Consumers, adopt any  
28 ratemaking adjustment that imputes the amount of the revenue discount provided

1 under this agreement, or adopt any ratemaking adjustment that, in Consumers sole  
2 judgment, has a similar effect.”

3 The portion of Mr. Irwin’s testimony I will be addressing concerns his discussion of  
4 power supply risk and the price protection or certainty, supposedly the Michigan Special  
5 Contract contains.

6 Q. Does the Michigan Special Contract Contain the price certainty/stability discussed by Mr.  
7 Irwin on page 3 of his testimony, greater then could be attained with an Alternative  
8 Electric Supplier (“AES”)?

9 A. No. The Paragraph contains a condition in which the State of Michigan would be forced  
10 to repay all discounts received under the contract back to Consumers Energy if the  
11 contract is canceled by Consumers Energy prior to December 31, 2005. Under the terms  
12 of this provision, the discounts are subject to refund until December 31, 2005, in the  
13 event a MPSC decision is deemed under Consumers Energy’s “sole judgment” to violate  
14 the conditions in The Paragraph. This places the State of Michigan at more risk then  
15 would exist under the Open Access program with service from an AES because any  
16 stranded cost changes are likely to only cause a modest lost to the State of Michigan in  
17 their amount of discount, not a total loss. The condition contained in The Paragraph  
18 contains much greater price risk then would occur under service by an AES under the  
19 Open Access program.

20 Q. Are the risks/discount levels contained in the contract as reasonable when compared to an  
21 AES contract under Open Access as discussed by Mr. Irwin on page 3 of his testimony?

22 A. No. First, the risk associated with service by an AES is no different then would occur  
23 with service under Consumers Energy, provided proper contract provisions are in place.  
24 If the risk of loss of service were a major issue, then the current levels of Open Access  
25 service would be considerably less and many of those entities with AES contracts would  
26 be returning to utility service. There are many public and state agencies which are or  
27 have received service under the Open Access program. Currently many of the  
28 Michigan’s public schools are enjoying millions of dollars of lower electric bills due to

1 Open Access service at discount levels greater than those contained in the Michigan  
2 Special Contract. The cost of electricity is a small portion of manufacturing costs and the  
3 amount of discount would not pay for the loss of production were to occur due to failure  
4 of an AES to supply electricity. If those public and private entities were truly concerned  
5 with the certainty of electric supply from an AES or had their electric service interrupted  
6 due to failure of delivery by an AES, they would not be participating in the Open Access  
7 program.

8 Q. What is the position of Mr. Brocket concerning the impact of The Paragraph on other  
9 customers?

10 A. For Consumers Energy's full service tariffs, Mr. Brocket states on page 4, lines 8 & 9 and  
11 also lines 13-16 that it expects the Michigan Public Service Commission ("MPSC") will  
12 not have an occasion, in which its decisions on full service tariffs could invoke the  
13 provisions of The Paragraph. Mr. Brocket does go on to say on page 5 of his testimony,  
14 in the paragraph starting on line 15, that the contract reduces stranded costs and resulting  
15 in a net positive benefit.

16 Q. What is your primary concern regarding Mr. Brocket's interpretation of The Paragraph?

17 A. Mr. Brocket fails to discuss several key implications of The Paragraph. First, The  
18 Paragraph makes the MPSC a party of the agreement by binding its hands on all MPSC  
19 decisions concerning Consumers Energy, not only rate related decisions. Second, The  
20 Paragraph states that it is Consumers Energy's "sole judgment" regarding whether a  
21 MPSC decision results in adjustments which imputes revenue discounts associated with  
22 the Michigan Special Contract. Third, Mr. Brocket's assessment of the impact on  
23 stranded costs is misleading because the discussion does not specify how Consumers  
24 energy will treat the discounts under this contract in future stranded cost cases.

25 Q. Is Mr. Brocket's testimony clear on the impacts of The Paragraph on full service rates?

26 A. No. First, Mr. Brocket states that "at this, time, the Company doesn't anticipate a change  
27 in its base electric rates prior to January 1, 2006". This statement does not commit  
28 Consumers Energy to delay the filing of any case which effects rates, until a time in

1 which an MPSC decision would occur after January 1, 2006. Second, The Paragraph also  
2 has the same impact upon MPSC decisions in cases the MPSC would initiate and could  
3 effectively prevent the MPSC from performing its proper oversight of utility operations,  
4 revenues and rates of return. Third, The Paragraph is very broad in that it would apply to  
5 "...any proceeding..." which involves a MPSC decision. The Paragraph leaves the  
6 decision on the determination of the impact of an MPSC decision on ratemaking with  
7 Consumers Energy. The Paragraph requires the MPSC to commit in the order approving  
8 this contract, to ensure that any decision between now and December 31, 2005, not  
9 impute any revenues or have any ratemaking impact that can be attributed to the  
10 discounts associated with this contract..

11 Q. Why does The Paragraph make the MPSC a party of the contract?

12 A. The statement, "Critical to such approval is the specific acknowledgement by the MPSC  
13 that it will not, in any proceeding...", implies the MPSC must agree in its order in this  
14 case to acknowledge and agree to base all ratemaking decisions on the conditions of The  
15 Paragraph. Mr. Brocket fails to address this issue in his discussion of the impacts of the  
16 contract. In order for The Paragraph to be placed into effect, the MPSC must include in  
17 the order approving the Michigan Special Contract, specific acknowledgement of  
18 agreement to base all decisions, not just ratemaking decisions, on the conditions  
19 contained in The Paragraph. This will have significant implications on any MPSC  
20 decisions in Consumers Energy cases until December 31, 2005. This will hold the MPSC  
21 hostage to this contract because any decision that in Consumers Energy "sole judgment"  
22 is felt to violate The Paragraph will result in the repayment of the discounts by the  
23 contracting parties to Consumers Energy. This could result in millions of dollars of  
24 repaid discounts.

25 Q. Why is Mr. Brocket's assessment of the stranded cost impacts of this contract  
26 misleading?

27 A. Mr. Brocket's testimony on stranded cost impacts is misleading for several reasons.  
28 First, contrary to Mr. Brocket's statement on page 5, line 17 & 18, it is highly unlikely

1 that all of the load included in the Michigan Special Contract would switch to open  
2 access. Mr. Brocket failed to provide any support that 100% of the load included in the  
3 Michigan Special Contract would move to open access. The loads of Michigan State  
4 University and Western Michigan University are highly variable and unpredictable due to  
5 their use of cogeneration. This increases the difficulty of an AES to serve these entities.  
6 Mr. Mitch Irwin states on page 3 of his testimony that the stranded cost uncertainty, use  
7 of out of state supplies, added risk, multi-year agreement and the source of third party  
8 supply created concerns for the State of Michigan regarding third party (AES) power  
9 supply. Second, The Paragraph would force the MPSC to transfer the cost responsibility  
10 of the discounts to open access customers as stranded costs. Third by transfer the  
11 discount to stranded costs, The Paragraph would insulate Consumers Energy from any  
12 impacts of the discounts. Mr. Brocket fails to discuss these impacts in his testimony.  
13 The result of the conditions contained in The Paragraph, assuming the 18.3 million on  
14 line 16 of page 5 of Mr. Brocket's testimony represents roughly 94.2% of the electric  
15 costs without discount, transfers over one million in discounts to stranded costs to be paid  
16 by open access customers. This means that Open Access customers will become  
17 responsible for funding the \$2.25 million (two years at approximately \$1.125 million per  
18 year) discount provided under the Michigan Special Contract through stranded costs, not  
19 Consumers Energy.

20 Q. Why would the approximately \$2.25 million of discount instead of just 29.1% of the  
21 discount, as discussed on line 16 of page 5 of Mr. Brocket's testimony, be transferred to  
22 stranded costs?

23 A. The full \$2.25 million of discount would be transferred to stranded costs because in the  
24 next stranded cost case Consumers Energy would determine that the discount was only  
25 on fixed generation costs. Using the logic that the contract was entered into for the  
26 purposes of competition with open access, and that customer charges, transmission costs  
27 and distribution costs are the same for all customers and not subjected to discounts.  
28 Thus, the discounts must be on generation related costs. The application of the



1 percentage of revenues dedicated to recovery of fixed generation costs of 29.1048%  
2 would be determined to not be applicable to the discount. Instead unlike the discussion  
3 on page 5, line 16 of Mr. Brocket's testimony, Consumers is likely to apply calculate the  
4 contribution to fixed generation revenue for those facilities served under the Michigan  
5 Special Contract using full service rates, reduce that amount by the \$1.125 million (1  
6 year) discount and then use the result for the portion of Michigan Special Contract  
7 revenues that contribute to fixed generation costs under the contract in a stranded cost  
8 calculation. Any other method of calculation would impute additional revenues to cover  
9 fixed generation costs.

10 This method of accounting for the discounts would assign the full level of the  
11 discount to stranded costs and include the funding of the discounts in the transition  
12 Charge. As a result, the Open Access customer would repay Consumers Energy the  
13 discount amounts, thus subsidizing bundled discounted bundled service. Consumers  
14 Energy is made whole, does not see any impacts of competition, open Access customers  
15 subsidize rate discounts and the competitive market is truly not competitive because  
16 Consumers Energy has no risk.

17 Any decision to the contrary by the MPSC would be seen by Consumers Energy  
18 in their "sole judgment" to adopt a ratemaking adjustment, invoke The Paragraph, thus  
19 terminating the agreement and forcing State institutions to repay any discounts. Mr.  
20 Brocket's testimony avoids any discussion of this issue and the real impacts on stranded  
21 costs by only discussing the revenue contribution from the discounted rates toward  
22 generation fixed costs.

23 Q. Will the MPSC approval of the Michigan Special Contract with The Paragraph impact  
24 the competitive market?

25 A. Yes. Any competitive situation in which the utility is absolved of risk to its revenues or  
26 its economic performance due to a discounted rate, provides the utility a free ride in the  
27 competitive marketplace. The Paragraph is requiring the MPSC to provide such an  
28 opportunity to Consumers Energy. Acceptance by the MPSC of The Paragraph terms,

1 “...adopt any ratemaking adjustment that imputes the amount of the revenue discount  
2 provided under this agreement...”, will allow Consumers Energy to use the competitive  
3 market to subsidize its discounts. Consumers Energy did not provide any cost of service  
4 justification for these discounts nor did they provide any justification that eh discounts  
5 are prudent. The MPSC is being asked to sign on to this agreement without any evidence  
6 being provided by the utility to justify the discounts. This will encourage other  
7 customers to negotiate similar contracts, knowing the MPSC will approve the contract  
8 and transfer the discounts to stranded costs. Under such market conditions, AES’s will  
9 discontinue providing competitive options and the Retail Open Access program will  
10 come to an end.

11 Q. Did Mr. Brocket address the reason for the benefit of the MPSC approving the Michigan  
12 Special Contract, including the provisions include in The Paragraph?

13 A. Yes. On page 4, Mr. Brocket’s testimony implies there will be no detrimental impacts of  
14 the contract on bundled customers and only incremental benefits on open access  
15 customers. His testimony implies the provisions contained in The Paragraph constitute  
16 good public policy the MPSC should adopt. In fact, this is totally contrary to the truth  
17 because any single contract between a utility and a customer which; A) Holds the MPSC  
18 hostage and effects every order associated with that utility for two years, B) Insulates the  
19 utility from the discounts in the contract by transferring the funding of those discounts to  
20 other customer class (Open Access Customers), C) Allows the utility engage in  
21 competition without facing the same economic impacts of market forces and price  
22 discounts, is bad public policy.

23 Q. Does this conclude your testimony?

24 A. Yes, it does.

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the Application of )  
 CONSUMERS ENERGY COMPANY )  
 For Ex Parte Approval of a Special Contract )  
 For Electric Service with the State of Michigan, )  
 The Board of Trustees of Western Michigan )  
 University, The Board of Trustees of Michigan )  
 State University, and the Regents of the )  
 University of Michigan on behalf of )  
 The University of Michigan – Flint, and the )  
 Board of Trustees on Michigan State University, )  
 A Michigan Constitutional Corporation. )  
 \_\_\_\_\_ )

Case No. U-13989

PROOF OF SERVICE

Monica Robinson, duly sworn, deposes and says that on this 12th day of January, 2004 she served a copy of Qualifications and Testimony of Richard A. Polich on behalf of Energy Michigan upon those individuals named on the attached service list.

\_\_\_\_\_  
 Monica Robinson

Subscribed and sworn to before me  
this 12th day of January, 2004.

\_\_\_\_\_  
 Eric J. Schneidewind, Notary Public  
 Eaton County, Michigan  
 Acting in Ingham County, Michigan  
 My Commission Expires: April 24, 2006

## SERVICE LIST

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