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September 17, 2004

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

Re: Case No. U-14098

Dear Ms. Kunkle:

Enclosed for filing in the above captioned matter please find the original and four copies of Energy Michigan's Reply Brief. 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

In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for determination of net stranded costs)
for the year 2003 and approval of net)
stranded cost recovery charges.)
_____)

Case No. U-14098

ENERGY MICHIGAN, INC. REPLY BRIEF

September 17, 2004

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TABLE OF CONTENTS

I. Introduction and Summary of Position 1

 A. Introduction: What is the Problem? 1

 B. Summary of Position: Consumers Has Ignored Methods Of Recovering
 QF Payments and Increased Production Plant Which Would Spread
 These Costs Over All Customers 2

II. Energy Michigan Replies Regarding Specific Categories of Stranded Costs 3

 A. Incremental Seasonal Power Purchases 3

 B. Qualifying Facility Costs Above Levels Collected By The Frozen PSCR 8

 C. Post-2000 Capital Costs 15

 D. Clean Air Act Costs 18

 E. Special Contract Revenues 19

 F. Termination of Securitization Offsets 21

 G. Proposal to Adopt the "Illinois Plan" of Calculating Stranded Costs 23

III. Calculation of Consumers' Stranded Costs 24

IV. Conclusion and Prayer for Relief 25

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ENERGY MICHIGAN, INC. REPLY BRIEF

This Reply Brief is filed on behalf of Energy Michigan, Inc. ("Energy Michigan") by Varnum Riddering Schmidt & Howlett LLP in response to Briefs filed by Consumers Energy Company ("Consumers" or "Consumers Energy"), the Michigan Public Service Commission Staff ("MPSC Staff" or "Staff"), Ada Cogeneration Limited Partnership and Michigan Power Limited Partnership (the "QFs"), the Midland Cogeneration Venture ("MCV") and Constellation NewEnergy ("Constellation").

I. Introduction and Summary of Position

A. Introduction: What is the Problem?

In 1999, the MPSC approved Retail Open Access Service Standards, voluntarily submitted by Consumers Energy, which provided that up to 750 MW or 10-11% of Consumers' total demand at that time could migrate to Open Access Service. This level of competition was perfectly acceptable to Consumers in light of the benefits received from the Commission. U-11290, et al, March 8, 1999. (See attached ROA Tariff Section F2.)

Fast forward to July 2004. Consumers witness Torrey testified that current (July 2004) ROA demand was about 838 MW or about 9% of Consumers total 8,800 MW peak load.¹ 2 Tr 49.

¹ Consumers retail peak is approximately 8,064 MW for the summer period (Case U-14005) and per Mr. Torrey ROA load is expected to be about 838 MW for a total peak of 8902 MW.

Thus, five years after Consumers stated it could live with about 10% of their peak load on competition, ROA load in percentage terms has still not exceeded projected 1999 market penetration.

However, Consumers is aware, and the Commission should be aware as well, that any significant transition charge will destroy competition in the current era of high market prices.

This is not the end of the world. This is predictable, moderate competition. The Commission should not be frightened into approval of transition charges by Consumers' wild projections that ROA load is going to suddenly run out of control and grow by 50% in 2005². This is a time to continue the policies which have benefited customers and competitors while avoiding harm to Consumers.

B. Summary of Position: Consumers Has Ignored Methods Of Recovering QF Payments and Increased Production Plant Which Would Spread These Costs Over All Customers

There are three issues in this case which will decide the fate of competition on the Consumers system: treatment of 1) increased production plant above depreciation levels, 2) incremental seasonal power purchases; and 3) incremental purchases of QF capacity which were bought for the benefit of retail customers yet were excluded from the frozen 2003 rates paid by these same customers. Consumers' proposals to charge the entire amount of these incremental costs to ROA customers as stranded costs (over \$40 million of new production plant above depreciation, \$30 million of seasonal power costs and \$61 million of incremental QF costs) impose financial burdens of a magnitude that would clearly destroy competition.

It isn't as though Consumers has no other choice. While PA 141 § 10d(1) prevents Consumers from collecting these incremental costs from retail customers, other options exist. PA 141 § 10d(4) allows Consumers to accrue and defer annual return of and on capital expenditures in excess of depreciation levels...and expenses incurred as a result of "federal governmental actions". After notice and hearing the Commission is allowed to determine the amount of

² See Exhibit A-5.

reasonable and prudent costs to be recovered under Sec. 10d(4) and allow recovery over a period that shall not exceed five years. Also, PA 142 might allow securitization of incremental QF costs.

Why didn't Consumers make application to recover incremental QF costs under Sec. 10d(4) or PA 142?

Why didn't Consumers make application under Sec. 10d(4) to recover what it clearly admits are \$40 million of production plant capital expenditures in excess of depreciation?

If Consumers wants to be made whole for the "incremental" QF cost that are its largest category of unrecovered costs it needs to step forward and pursue a course of action which is likely to achieve success but does not result in the destruction of competition. To date, however, Consumers prefers to threaten the ROA program rather than collect its costs of doing business.

This case gives the Commission an opportunity to make PA 141 work reasonably for Consumers and its competitors. The Commission can achieve this balance by directing Consumers to appropriately use PA 141 § 10d(4) or PA 142 to recover Clean Air Act investments, generating plant investment above depreciation levels and incremental QF costs. However, recovery must be accomplished through a rate case filing which allows the Commission to determine the amount of reasonable and prudent costs in those categories and order recovery from all customers, not just from ROA customers. Attempting to burden the ROA program with 100% of these incremental costs which were incurred exclusively to serve retail customers is not a fair or reasonable outcome.

II. Energy Michigan Replies Regarding Specific Categories of Stranded Costs

A. Incremental Seasonal Power Purchases

1. Consumers' position.

Consumers proposes to recover, as stranded costs, over \$30 million of summer and winter seasonal capacity costs attributable to purchases of power which were not recovered through the frozen PSCR clause during 2003. Consumers claims that these costs are stranded by arguing that:

a. These resources are needed to provide reliable service and are purchased as part of normal Consumers Energy practices to serve its customers. Consumers Brief, p. 5.

b. In response to Staff recommendations that single year purchases be disallowed because they are avoidable, Consumers claims that single year purchases are not avoidable upon short notice because they are committed years ahead of time and that early commitments for power are necessary to achieve economies. Id, p. 5-6.

c. Consumers also claims that if costs of incremental seasonal purchases are excluded from the stranded cost of calculation, revenue from the sale of excess seasonal power should not be used as an offset to stranded costs. Id.

Staff Takes No Position

MPSC Staff do not take a position regarding exclusion of seasonal power purchases but do recommend various levels of stranded cost recovery based upon three alternatives: all summer options included, multiyear summer options included and all options excluded. See Exhibit S-21. However, Staff's position regarding exclusion of all options still allows of over \$11.5 million of transmission and peak management costs associated with Consumers' unrecovered 2003 seasonal power supplies. See Exhibit S-21, line 9 (column: 2003 "Staff All Options Excluded").

2. Energy Michigan reply.

ABATE and the Attorney General have all opposed Consumers' request to recover incremental winter and summer power costs. ABATE Brief, p. 7-8; Attorney General Brief, p. 18.

The Energy Michigan Brief set forth the detailed reasons for opposing Consumers' request. Energy Michigan Brief, p. 12-17. These reasons may be summarized as follows:

a. The referenced seasonal costs were incurred exclusively for the benefit of retail customers and were incurred after Consumers Energy knew or should have known that ROA would reduce its summer peak demand. Energy Michigan Brief, p. 13.

b. Consumers has introduced no proof whatsoever allowing the Commission to determine any offset for seasonal capacity costs already included in the bundled rates and PSCR charges. It is impossible to accurately gauge if any of these "seasonal" costs displace contracts which were included in the frozen PSCR but were terminated before or during 2003. *Id.*, p. 13; Polich, 2 Tr 117-18.

c. Little of the purchased capacity was ever reviewed or approved by the Commission for reasonableness and prudence. Energy Michigan Brief, Tab B. Consumers Discovery Response 14098EM-CE-14.

d. There are significant questions regarding the reasonableness and prudence of these purchases. The appropriate format for consideration of these prudence questions would have been a regulatory proceeding rather than a stranded cost proceeding. 2 Tr 119-20; Energy Michigan Brief, p. 13.

e. For the reasons (a)-(d) stated above, the seasonal power costs are not recoverable under regulation and thus do not meet the test set forth in U-12639 requiring recoverability as a condition of being found to be stranded costs. U-12639, December 20, 2001, p. 10.

f. The seasonal power costs were not shown by Consumers to be unrecoverable in a competitive market. This is a requirement of recoverability as a stranded cost under the U-12639 standards. *Id.*, p. 10. Consumers has made no such showing.

g. Consumers' seasonal power costs were incurred in the year 2003, a period in which the PA 141 § 10d(1) rate freeze was in effect. It was this rate freeze which prevented Consumers from collecting incremental power costs from its retail customers since these costs were not included in the frozen rate levels in existence as of June 2000. By relabeling these expenses as stranded costs, Consumers hopes to evade the prohibitions of PA 141 § 10d(1). This is illegal unless the referenced expenses fall under one of the two broad exceptions described in Section 10d(4) of PA 141. Since seasonal power costs do not qualify under the 10d(4) exceptions such cost may not be recovered "notwithstanding any other provision of law or Commission order". PA 141 § 10d(1).

Consumers' arguments that these purchases were a part of its normal practices to provide reliable service and that the purchases were not avoidable are not persuasive answers in the face of the broad prohibitions of Section 10d(1) and Consumers' own failure to obtain regulatory approvals through proceedings which would establish the reasonableness and prudence of these purchases.

Given Consumers' failure to prove that over \$30 million of incremental seasonal power costs qualify for the exemptions under Sec. 10d(4) all of these costs must be excluded as recoverable items for many of the reasons stated by the ALJ James

Rigas in his PFD in Case U-13935 regarding the applicability of the PA 141 rate freeze to costs above frozen levels. U-13935, July 29, 2004, p. 10-12.

h. Consumers' request that revenue from sales of excess seasonal power be excluded as an offset if all seasonal costs excluded, has been incorporated into the Energy Michigan calculation of Consumers net stranded costs. See Tab C, p. 1 and 2, line 9. In both alternatives, (p. 1 with all post-2000 capital additions and p. 2 without post-2000 capital additions) the subtraction for seasonal power is net of income from sales.

Reply to Staff: Staff Has Incorrectly Calculated Consumers'
Allowable Seasonal Cost Of Capacity

The Staff recommended that Consumers' stranded costs include over \$11,523,000 of "net costs of summer capacity" even with all options excluded. See Exhibit S-21, line 9; and Staff Brief, p. 8.

Attached Tab A is Exhibit I-20 containing MPSC Staff workpapers that demonstrate the derivation of the Staff's recommendation for recovery of over \$11.5 million of costs related to Consumers' purchase of seasonal capacity related costs. Exhibit I-20, p. 5-8 shows that Consumers witness Kurzynowski supplied Staff with a calculation of her seasonal capacity recommendation minus single year and multiyear purchases. An examination of these exhibits including Ms. Kurzynowski's initial attached recommendation Exhibit JMK-1 (A-15) Tab A, p. 4 makes it clear that Staff developed their estimate of Consumers' seasonal capacity costs "Without Options" by subtracting the \$19 million cost of options but leaving over \$4.3 million of forward capacity over \$739 thousand of peak load management and over \$7 million of associated transmission to be calculated as a stranded cost. Tab A, p. 3.

The Staff calculation of costs "Without Options" merely commenced with Ms. Kurzynowski's recommendation for \$30.7 million of seasonal costs and after subtracting only \$19 million for External Options and Michigan Capacity was left with a value of \$11.523 million for "All Options Excluded" See Tab A, p. 3. This \$11.523 million corresponds exactly to the price paid by Consumers for transmission capacity (\$7.258 million) external capacity (\$4.317 million) and peak load management costs (\$730.7 thousand) minus \$694 million revenue from the sale of excess transmission capacity. Tab A, p. 1-4 and Exhibit I-20.

In other words, the MPSC Staff recommendation really allows Consumers to be compensated for over \$11.5 million of external capacity, transmission and peak load management costs despite the fact that the recommendation states that this calculation excludes all costs of options. No reason is given for these calculations. This result is illogical because it pays a portion of some Consumers' summer purchases and not a portion of others and it is illegal because it violates the Sec. 10d(1) prohibitions of PA 141 discussed above. The Staff calculation also fails to comply with the criteria of U-12639 because purchases of transmission capacity and peak load management were never approved as reasonable and prudent, nor were they demonstrated to involve costs which could not be recovered in the marketplace.

Impact on Staff Calculation of Stranded Cost

For these reasons, Staff's calculation of stranded costs "Excluding All Summer Options" should be reduced by \$11.5 million from \$35.5 million to \$24 million. See Staff Brief, p. 8.

B. Qualifying Facility Costs Above Levels Collected By The Frozen PSCR

1. Introduction.

The treatment of Qualifying Facility costs above levels collected by the frozen PSCR is the most important issue in this case or, for that matter, in any Consumers Energy case before the Commission. In deciding this issue, the Commission should consider three things:

First, the outcome of this issue will decide the fate of competition. In Case U-13720 (calculation of Consumers' 2002 stranded costs), exclusion of \$13.7 million of incremental QF costs makes the difference between a Staff recommendation of \$10.5 million of stranded costs and a finding of over \$3 million of stranded benefits if all other elements of the Staff case (Special Contract revenue imputation but inclusion of all seasonal costs) are adopted. Energy Michigan Reply Brief U-13720, Tab A, column (4). In this case, exclusion of over \$60 million of QF costs would turn virtually all of the Staff's alternative recommendations (ranging from \$35 million to \$54 million of stranded costs) from positive stranded costs to stranded benefits. See Staff Brief, p. 8.

Second, there is no dispute that all the party QFs to this case (MCV, Ada Cogeneration and Michigan Power Limited Partnership) were paid every penny of the capacity payments due under their contracts with Consumers. Torrey, 2 Tr 45. In Case U-13720 the same is true. No proof was introduced that QFs were not paid all contract sums. Thus, the ability of Consumers to exercise the "regulatory out" regarding 2003 QF payments has long since passed. Use of the "regulatory out" issue provision in QF contracts has been waived by Consumers' payment of the funds to the QFs.

Third, Consumers Energy has made no effort whatsoever to explore the use of alternative mechanisms such as PA 141 § 10d(4) or PA 142 securitization as a means of collecting what it claims are federally mandated capacity payments. Rather, Consumers has attempted to burden competition with 100% of these incremental QF costs which were incurred solely for the benefit of retail customers. While this course of action ensures the destruction of competition, it will also result in the inability to collect these sums since ROA service would cease to exist as an avenue for collection. Thus, Consumers' request is self-defeating.

2. Position of Consumers Energy and Party QFs regarding collection of incremental QF costs.

Consumers Energy claims that the QF costs above levels contained in the frozen PSCR should be collectible as stranded costs since they were approved by the Commission as prudent. Consumers also says that exclusion of these costs would expose the Company and potentially QFs to disallowance under regulatory out provisions of each power purchase agreement. Consumers Brief, p. 19-20.

The QFs claim that the Commission should allow Consumers to recover all capacity payments to them. QFs, p. 2; MCV, p. 9-10. While the QFs presented no testimony or evidence in this case, they do not necessarily support Consumers' designation of incremental QF costs as stranded costs but do argue that the Commission must allow Consumers to recover monies paid under contracted QF "one way or another". QF Brief, p. 2-7; MCV Brief, p. 1-2.

The QFs and MCV also make the following arguments:

- a. State law PA 141 § 10a and § 10a (12) and (15) and MCL 460.6j(13a)(b) ("PA 181") and federal law 16 USC § 2601 (PURPA) mandate that Consumers be allowed to recover all QF payments (including the \$61 million of incremental payments presented by Consumers in this case) as stranded costs. QF, p. 2-4, 5-7; MCV, p. 3.
- b. The Commission orders issued prior to PA 141 show intent to allow recovery of incremental QF costs. MCV, p. 3-5; QFs, p. 4-5.
- c. PA 141 § 10a(12) and (15) show an intent to allow recovery of payments despite the Sec. 10d(1) rate freeze. QF, p. 4.

d. The QFs and MCV claim that the proposed decision issued in U-13720 while admitting that the PA 141 rate freeze prevented recovery of incremental QF payments recommended a finding that the amounts were not necessarily disallowed for recovery. QFs, p. 7-10; MCV, p. 9-10.

3. Energy Michigan reply.

a. Consumers cannot invoke regulatory out clauses since QFs have been paid all 2003 capacity payments..

Consumers has admitted that QFs have been paid all sums owing to them in 2003 under their contracts. Torrey, 2 Tr 45. Given this fact, the QF's PURPA rights to payment of their contract amounts have been satisfied, voluntarily, by Consumers. Thus, there is no danger now that Consumers can invoke a regulatory out clause as a basis for refusing 2003 payments on the grounds that the Commission has disallowed the amounts for recovery. This fact alone should render the position of the QFs and MCV in this case moot.

b. Consumers has ignored the obvious mechanisms to achieve recovery of expenses incurred as a result of federal actions: PA 141 § 10d(4) and PA 142.

If Consumers believes that it is compelled to make payments to QFs under PURPA and that this obligation preempts state laws such as PA 141 and specifically the PA 141 rate freeze, Consumers should apply to the Commission for recovery of incremental QF costs under PA 141 § 10d(4). That section provides that Consumers can accrue "...expenses incurred as a result of ...State or federal governmental actions....during [the rate freeze] and then apply to PA 141 § 10d(4) the Commission which must, "after notice and hearing...determine the amount of reasonable and prudent costs, if any, to be recovered and the recovery period which shall not exceed five years...". PA 141 § 10d(4). However, Consumers has failed to take this obvious step which seems a clear response to

the request of the QFs that "one way or another" Consumers be allowed to recover its costs. QFs, p. 2; MCV, p. 9-10.

PA 142 offers another means of dealing with QF costs through securitization. It seems obvious that if Consumers believes that QF payments are a stranded cost which has been approved for recovery Consumers should have attempted to declare these costs to be regulatory assets and hence eligible for securitization. See PA 142, § 10h(g).

Consumers has not pursued either of these remedies which would spread QF costs over all customers, not just ROA customers.

c. The PA 141 rate freeze does not allow Consumers to recover incremental QF costs through the stranded cost mechanisms.

It is not disputed that the \$61 million of 2003 incremental QF costs were not included in the rates frozen with the passage of PA 141. It is also not contested that the Commission repeatedly rejected Consumers' claims to include such costs in the PSCR. See Case U-11180R dated March 14, 2000 and July 11, 2001, as well as U-12366 dated June 19, 2000.

The Commission decisions in these matters held that the PA 141 rate freeze prevented inclusion of the increased costs in the Consumers PSCR clause subsequent to June 2000. Neither Consumers nor party QFs appealed either of these orders.

The basis of the Commission's rejection of Consumers request to add QF costs to their PSCR after passage of PA 141 was simple: The PA 141 § 10d(1) rate freeze took effect "notwithstanding any other provision of law or Commission order." That language supercedes or takes precedence over all Michigan laws or MPSC cases cited by the QFs or MCV. These laws include PA 141 § 10a(12) and (15).

Even if Consumers of the MCV had a federal PURPA right to recover QF costs despite the PA 141 rate freeze, they waived that right when they failed to appeal orders U-11180R and U-12366 which rejected collection of these incremental costs during the PA 141 rate freeze. The QFs and MCV lost any PURPA rights when they were paid by Consumers for all contracted 2003 amounts. Thus, their rights have not been affected by this situation.

d. The QF payments were not recoverable under regulation.

Case U-12639 requires among other things that stranded costs, to be recoverable, must be both recoverable under regulation. U-12639, December 20, p. 10. However, the Commission has ruled twice in Cases U-11180R and U-12366 that Consumers could not recover QF costs in the PSCR process due to the PA 141 rate freeze.

Moreover, Case U-12639 requires that so-called stranded costs not be recoverable in a competitive market. *Id.* Consumers has not proven in this case that QF costs are unrecoverable in a competitive market.

e. There is a way to reconcile federal law, State law and Public Service Commission decisions regarding recovery of QF costs.

Consumers Energy has deliberately ignored obvious solutions to the difficulty of reconciling the body of federal and State statutory law as well as MPSC administrative decisions which impact recovery of QF capacity payments. The PA 141 rate freeze is designed to prevent recovery of cost increases during the rate freeze period established in Sec. 10d(1). The Proposed Decision of Administrative Law Judge James Rigas in Case U-13935 emphasizes that this broad exclusion is subject to two specifically enumerated exceptions. July 29, 2004, p. 10-12. The first exception relates to power plant capital costs and is not applicable. The second exception relates to expenses incurred as a result of

governmental actions. If Consumers believes that the federal law mandates payment of PURPA capacity costs and collection of these costs from its customers, Sec. 10d(4) offers the obvious solution: Demonstrate the reasonableness and prudence of the purchases and request a Commission order authorizing collection of these costs from all customers, not just ROA customers, commencing January 1, 2006.

As noted above, PA 142 may offer another solution in the form of securitization of what Consumers alleges to be stranded costs. This option entails satisfaction of several financial conditions but would seem to be an available avenue for collection of stranded QF costs which Consumers, QFs and MCV believes have been ruled prudent and collectible under regulation.

That Consumers has chosen neither of these avenues but rather has attempted to collect well over \$60 million of costs incurred for the benefit of retail customers only from competitive ROA service is a testimony to its desire to limit or destroy competition rather than its true desire to collect legitimate costs.

Use of PA 141 § 10d(4) or PA 142 is entirely consistent with the findings of the Administrative Law Judge in U-13720 in which she stated, "The fact that Consumers was precluded from billing those [QF] charges after imposition of the Act 141 rate freeze does not mean that the Commission has "disallowed" those charges." PFD, p. 10. Collection through Sec. 10d(4) or PA 142 would therefore be consistent with the Judge's proposal that QF payment costs be deemed collectible.

Conclusion

There are means available to Consumers to collect incremental QF costs without the destruction of the ROA program. The Commission should forcefully direct Consumers to either use these available options or drop the issue once and for all.

C. Post-2000 Capital Costs

1. Consumers and Staff position.

Consumers opposes Energy Michigan's recommendation that increased revenue requirements relating to generating plant investment greater than the levels in effect at passage of PA 141 be excluded from the Production Fixed Costs used to calculate overall stranded costs under the Staff Method. Consumers claims that previous MPSC cases have only excluded Clean Air Act investment and that an attempt by Energy Michigan to exclude non-Clean Air Act production plant increases was unsuccessful (Case U-13808). Consumers Brief, p. 16. Consumers also denies that it was put on notice that increased investment would not be recoverable (Id, p. 15-16), and that Energy Michigan simply wants to exclude consideration of all new Consumers production plant investment. Id. P. 17. Finally, Consumers claims that Energy Michigan calculations were wrong in that it did spend more on plant investment than the amounts in its depreciation rates. Id., p. 17-18.

Staff also opposes the Energy Michigan position on post-2000 production plant costs as inconsistent with the "Staff Method". Staff Brief, p. 5-6.

2. Energy Michigan reply.

Consumers has, in effect, taken the position that, other than Clean Air Act expenditures, it should be able to increase its rate base by over \$200 million above pre-Act 141 levels and bill the cost of those increases to ROA customers whether or not the costs are eligible for collection under PA 141 § 10d(4)

In other words, Consumers urges that the rate base increases below depreciation levels which are not collectible other than in frozen rates and the rate base expenses above

depreciation levels which could be collected under Sec. 10d(4) should all be factored into the stranded cost calculation and the shortfall be billed to ROA customers.

Lest there be any doubt, the following quote from Consumers' own Brief demonstrates what is at stake with this issue: "Contrary to Energy Michigan's conclusion, Mr. Torrey explains that Consumers Energy's 'production related capital expenditures exceeded the depreciation expense booked and collected through frozen rates." 2 Tr 74. Consumers Brief, p. 18. (Emphasis supplied).

Like Clean Air Act expenditures, Sec. 10d(4) of PA 141 provides Consumers with the ability to collect "...annual return of and on capital expenditures in excess of depreciation levels incurred during and before the time period described in [the PA 141 rate freeze]." Mr. Torrey has admitted above that Consumers in fact did expend monies (about \$40 million) for rate base production plant improvements that exceeded depreciation levels. Torrey, 2 Tr 73-74. Yet, Consumers has not attempted to collect these amounts through Sec. 10d(4) and rather includes 100% of the amounts in its calculation of stranded costs

As fully described in the Energy Michigan Initial Brief at pages 27-28, Consumers did not follow the specific mandatory procedures for recovery of these above production plant depreciation costs. Both the standards enunciated in U-12639 (as discussed below) and PA 141 § 10d(4) require that Consumers provide notice of the hearing to its customers and come forth with proof of the reasonableness and prudence of the expenditures. Moreover, a Commission order to this effect must be secured before collection may commence. Consumers has not complied with any of these requirements in the current case and therefore the sums are not collectible but may be collected in future proceedings if Consumers chooses to comply with the law. As to amounts expended below depreciation levels, Sec. 10d(1) of PA 141 prevents Consumers from passing on rate increases to customers for increased costs during the rate freeze period. See PFD of James Rigas, U-13935, July 29, 2004.

Failure to Comply With MPSC Case Standards

Consumers' application to recover costs of rate base increases does not even comply with MPSC case law standards set forth in U-12639. P. 10. Expenditures must be shown to be recoverable under regulation before they can successfully be recovered as stranded costs. *Id.* Yet in this case, Consumers presented no proof whatsoever regarding the reasonableness and prudence of increased rate base investments, both above and below depreciation levels. Given this situation, the Commission can scarcely make a finding that the costs would have been recoverable under regulation since it has no idea whether the costs were reasonable or prudent.

U-12639 also set forth as a criterion that costs be shown to be unrecoverable in a competitive market. In this case, Energy Michigan witness Polich testified that the cost of Consumers' generation plant are competitive in the marketplace. Polich, 2 Tr 121. Given this fact, Consumers has failed to make a showing that the increased production plant costs have made the output of Consumers' power plants unrecoverable in a competitive market. According to Mr. Polich, just the opposite is true. The output of Consumers' generating plants is competitive and attractive in the marketplace and thus all of Consumers' production plant cost increases could be recovered without payment by ROA customers.

Conclusion

There are really two issues contained in the heading "Post-2000 Capital Costs": Investments above depreciation and investments below depreciation.

Even Consumers has admitted that its production related capital expenditures actually exceeded depreciation expense by \$40 million in 2003. Torrey Rebuttal, 2 Tr 73-74. Given this situation, PA 141 § 10d(4) allows Consumers to demonstrate the reasonableness and prudence of these expenditures and recover them from its retail customers in less than five years if it chooses to do so. Energy Michigan has no doubt

that if recovery is denied here, Consumers will add this issue to a future rate case application. Commission precedent from U-13380 strongly indicates that Consumers should be ordered to take this approach rather than attempting to cover 100% of these expenditures which were made for the benefit of retail customers from ROA customers as stranded costs.

Consumers' rate base increases below depreciation levels should be disallowed for recovery under the restrictions of Sec. 10d(1) which literally prevents Consumers from passing along rate increases incurred during the rate freeze to its customers. In any event, the Commission cannot and should not allow such costs to be collected without the demonstration of reasonableness and prudence that is the unquestioned precondition to cost recovery. That showing has not been made in this case.

D. Clean Air Act Costs

1. Consumers position.

While Consumers admits that Clean Air Act costs can be recovered from retail customers through securitization or use of PA 141 § 10d(4), Consumers persists in its arguments that these costs be included in its calculation of stranded cost payable by ROA customers. Consumers Brief, p. 2-3. Consumers concludes with the statement, "If these Clean Air Act costs are not recovered through securitization (or in some other manner), then they need to be included in the stranded cost calculation." Consumers Brief, p. 3.

2. Energy Michigan reply.

The Commission should put this matter behind us once and for all. In Case U-13380 the Commission clearly ruled that cost recovery of Clean Air Act investment was appropriate through means other than stranded cost cases. U-13380, December 20, 2002. Even Consumers admits that PA 142 provides one option. There is no doubt that PA 141 § 10d(4) offers another avenue of recovery.

However, both PA 141 § 10d(4) and any other avenue of recovery would require a demonstration of reasonableness and prudence (e.g. recoverability under regulation) prior to recovery. There is no question whatsoever that Consumers has not attempted to prove the reasonableness and prudence of Clean Air Act investments in this case. Therefore, the investments are not recoverable under regulation and could not be treated as stranded cost under either the U-12639 format or under Sec. 10d(4).

Given all these factors, and the pendency of Case U-13715 (regarding securitization of other Consumers Clean Air Act costs) Consumers application should be rejected as recommended by all parties to this matter except the QFs.

E. Special Contract Revenue

1. Consumers position.

Consumers opposes the Commission's long standing practice of revenue imputation (treating Special Contract revenue as though it were collected at retail rates rather than discounted rates). Consumers claims that it has met three tests posed by the Commission as a condition of abandoning revenue imputation. Specifically, Consumers claims that it has shown that 1) its Special Contracts are offered at rates which cover full cost of service once the impact of "skewing" is ignored; 2) That Special Contract benefits exceed Special Contract costs; and 3) That its Special Contracts do not impede competition. Consumers Brief, p. 11-14.

2. Energy Michigan reply.

The long case history supporting the Commission's decision to treat Special Contract revenue as though it were at retail rates rather than discounted rates is discussed in the Energy Michigan Initial Brief. See p. 30-31. Behind this long list of case law lies one simple and reasonable premise: Calculation of stranded costs using discounted revenues

will tend to increase stranded costs by reducing the revenue available to pay Production Fixed Costs. The bigger the discount granted to Special Contract customers, the larger the stranded costs that will result. If you did not impute Special Contract revenue at retail rates, you would be asking open access customers to literally pay for the cost of the discounts which are being used to compete against open access service. Under these circumstances competition would not survive.

Consumers' three arguments in defense of Special Contract discounts are easily answered.

1) The Consumers Special Contract rates do not cover the cost of service. Energy Michigan witness Polich testified that Consumers reached the conclusion that Special Contract revenue exceeds costs of service by simply ignoring significant portions of the Special Contract revenue requirement by labeling these amounts "skewing" and claiming that the remaining "non-skewed" portion of the rate was equal to or less than the revenue produced by the Special Contract. Mr. Polich pointed out that this analysis fails to account, however, for the fact that the "skewing" amount ignored is a revenue requirement which must be recovered from some customer class. If this revenue requirement is ignored for Special Contract customers, the requirement would be transferred to other non-Special Contract customers thereby raising their rates. Either Special Contracts do not cover the full cost of service or, if the "skewing" component is transferred to another class, those classes are significantly disadvantaged thus causing Consumers to fail in its attempts to meet the test that decrees that benefits to non-participants must exceed costs. Mr. Polich also demonstrated that the allocation factor used by Consumers is inappropriate for this class of customers. Polich Direct, 2 Tr 122-24.

2) Consumers has not demonstrated that Special Contract benefits exceed costs. As noted above, Consumers' cost of service analysis would require transfer of significant costs to non-participating classes thereby depriving them of all or most of the alleged benefits which they receive from Special Contracts. Energy Michigan witness

Polich testified that Consumers has not demonstrated benefits to other classes. 2 Tr 125. For the reasons discussed above that the current practice of imputing Special Contract revenue at retail rates benefits the Special Contract customers, retail customers who do not pay subsidies and ROA customers whose stranded costs are not inflated. The only disadvantaged class is Consumers' shareholders whose loss of return is offset by the increased revenue which they receive due to customer retention through use of Special Contracts.

3) Consumers has not shown that Special Contracts have not impeded competition just because the Rate DA and ROA programs are healthy.

Consumers statements merely prove that Special Contracts with revenue imputation do not impede competition. If SMC revenues were not imputed at retail rates it is undeniable that stranded costs would increase significantly and undoubtedly have an adverse effect on competition. Consumers has merely proved that the existing system of imputation works not that a changed system would work.

F. Termination of Securitization Offsets

1. Consumers position.

It is difficult to describe Consumers' position on this issue.

In Case U-13720 Consumers filed Exceptions which claimed to accept the recommendation of the ALJ to develop an estimate of the amount of securitization offset which could be provided with projected levels of ROA participation and potentially reduced sources of funding. Consumers Exceptions, U-13720, p. 17, August 13, 2004.

However, in this case, Consumers seems to be backtracking to their original U-13720 position: if 50% of excess securitization savings were not sufficient to fully offset ROA securitization payments, the entire offset should be terminated and 100% of the excess

savings accruing in the 2005 timeframe should be given to both ROA and retail commercial and industrial customers in the form of reduced distribution rates. Consumers Brief, p. 22-23.

For purposes of this Reply, Energy Michigan will assume that the position stated in Consumers' Initial U-14098 Brief (termination of the offset) is the current Consumers position on this issue.

2. Energy Michigan reply.

In Case U-12505 the Commission issued an irrevocable securitization order which specifically required Consumers to use 50% of excess securitization savings to offset ROA securitization charges until a rate base case has been filed. U-12505, October 24, 2000, p. 43-44 and January 4, 2001, p. 6-8. Consumers has not argued that the 50% of excess securitization savings will not be forthcoming. It has only argued that, as presently calculated, 50% of excess savings would be insufficient to offset 100% of ROA securitization charges. In Case U-13720, Energy Michigan responded to Consumers request for input by stating that it preferred Consumers stated alternative #2: "Calculate a uniform securitization offset for the remainder of 2004 and all of 2005. The offset would be calculated by estimating available 2004 and 2005 savings and dividing by estimated 2004 and 2005 ROA load during the same period." Energy Michigan Reply to Exceptions, U-13720, August 23, 2004, p. 11.

There is, however, a qualification to the position of Energy Michigan. In this case, Consumers has presented what can only be characterized as wildly inflated estimates of ROA growth, particularly during the year 2005. According to Consumers, ROA will grow 62% from the 2003 to the 2004 calendar year. See Exhibit A-5. And, improbably, that ROA will grow another 47% from 2004 to 2005. In view of current retail market conditions and the demonstrated fact that as of summer 2004 even Consumers admits that ROA is less than 10% of its total load, it seems impossible that the ROA load will grow to more than 16% of Consumers' load in 2005. See Exhibit A-5 for Consumers'

estimates. More likely, Consumers' estimates of ROA growth are a self-serving attempt to justify high transition charges and in this case a very low/kWh securitization offset.

In order to ensure an estimated offset which is fair to ROA customers and Consumers alike, Energy Michigan recommends that Consumers develop a new ROA offset by dividing the annualized 50% of excess securitization savings by its estimated 2004 ROA load as contained in Exhibit A-5. This factor would be in effect through the balance of 2004. Energy Michigan further recommends that as of January 2005 and July 2005 this estimated factor be revised on the most current actual data available rather than upon Consumers' inflated 2005 estimates.

G. Proposal to Adopt The "Illinois Plan" of Calculating Stranded Costs

1. Constellation position.

Constellation proposes a stranded cost methodology which it claims is based on a model used in Illinois. Constellation Brief, p. 2-6. In describing this same model in Case U-13720, Constellation used the term "lost revenue" several times (e.g. see p. 3 of their Initial Brief) to describe their plan. The Constellation model essentially calculates the margin between the retail market and the ROA market and grants all of that margin minus the market value of "freed up" power as a stranded cost to be collected by the utility except for a small (8-10%) shopping credit which is supposed to give the Alternate Supplier a profit and the customer a savings. Id. The size of the "shopping credit" margin that will determine the success or failure of the ROA market appears to be totally subjective and unrelated to anything other than political judgment.

2. Energy Michigan reply.

The Constellation proposal should be rejected because it is based on the discredited "lost revenue" method. The Commission has repeatedly rejected the "lost revenue" method for calculating stranded costs. See Case U-12639, p. 11; Case U-13350, p. 12. Recently in

the current Detroit Edison rate Case U-13808 the Commission stated that the "lost revenue" approach "...clearly produces excessive transition charges." See U-13808 Interim Order, February 20, 2004, p. 59.

On substantive grounds, the Constellation presentation was not accompanied by a detailed financial analysis or a recommendation of specific stranded costs as was the presentation of Energy Michigan. Thus, the Commission has not been given a factual basis that would support adoption.

III. Calculation of Consumers' Stranded Costs

Given the many different positions in this case and the fact that the Staff presented three different alternatives regarding seasonal purchases, Energy Michigan offers an explanation of the stranded costs which would result from its position.

Exhibit I-18 (attached as Tab C) is the Energy Michigan calculation of Consumers 2003 stranded costs under two different alternatives:

1. A stranded cost calculation which includes all post-2000 rate base additions (position supported by Consumers and MPSC Staff). Stranded benefits equal \$2,902,000. Exhibit I-18 (Tab C), p. 1 of 2; and
2. A stranded cost calculation which removes all post-2000 rate base additions. Exhibit I-18, p. 2 of 2. Stranded benefits equal \$10,138,000.

Other than these rate base alternatives, both Energy Michigan calculations assume the following adjustments to the Consumers position:

1. Special Contract revenue is imputed at retail rates. See Tab C, p. 1 and 2, lines 15 and 16.

2. Clean Air Act investments are removed from rate base. See Tab C, p. 1 and 2, line 12.

3. All \$30.395 million of Consumers seasonal capacity purchases are removed including \$11.5 million left in by MPSC Staff for purchases of transmission and external forward capacity. See Tab C, p. 1 and 2, line 9.

4. PPA capacity charges are reduced from the \$499 million level proposed by Consumers to approximately \$473 million which was in effect as of the PA 141 rate freeze and which excludes incremental QF costs. See Tab C, p.1 and 2, line 7.

If the Commission agrees with the MPSC Staff position except as regards recovery of seasonal capacity and incremental QF capacity, Energy Michigan Exhibit I-18, p. 1 of 2 would be appropriate (\$2,902,000 of stranded benefits). If the Commission agrees that Consumers rate base additions in addition to Clean Air Act investments should be removed, Energy Michigan Exhibit I-18, p. 2 of 2 (\$10,138,000 of stranded benefits) would be appropriate.

IV. Conclusion and Prayer for Relief

WHEREFORE Energy Michigan respectfully requests that the Commission:

1. Reject Consumers claims that \$30.4 million of incremental seasonal capacity costs which were not included in the frozen 2003 PSCR factor paid by retail customers should be recovered only from ROA customers as stranded costs. Adjust the MPSC Staff "All Options Excluded" alternative to remove \$11.5 million of associated transmission costs, peak load management costs and external capacity costs.

2. Reject Consumers' claim that over \$61 million of incremental QF capacity costs which were not included in the 2003 PSCR factor should be recovered from ROA customers as stranded costs.

3. Reject treatment as stranded costs for over \$51 million of Clean Air Act costs which have been ruled by the Commission to be unrecoverable from ROA customers and are recoverable from retail customers in either retail rate increases or securitization bond payments.

4. Reject Consumers request for recovery, as stranded costs, of post-2000 Generating Plant capital improvements to Generating Plants since these improvements were not included in the rates paid by retail customers as of the PA 41 rate freeze which took effect June 2000. At a minimum, reject over \$40 million of costs production plant above depreciation levels which can be recovered under PA 141 § 10d(4).

5. Reject Consumers' request to report Special Contract revenues at discounted rates rather than imputing these revenues at retail levels to prevent requiring ROA customers to subsidize competitive offerings.

6. Find that Consumers experienced \$10.138 million of 2003 stranded benefits (excess of Production Fixed Cost Revenue over Production Fixed Costs) based on issues #1-#5 above if all post-2000 plant additions are deleted. See Tab C, p. 2. Or, \$2.9 million of stranded benefits if post-2000 plant additions are allowed.

7. Reject Consumers' proposal to terminate the rate credit for ROA customers funded by excess securitization savings. Instead, the Commission should order Consumers to calculate a revised securitization offset credit which would be calculated by dividing available funds by projected 2004 ROA sales. This calculation should be adjusted for actual ROA sales January 1, 2005 and July 1, 2005.

8. Reject implementation of the "Illinois Method" of calculating stranded costs.

Respectfully submitted,

VARNUM, RIDDERING, SCHMIDT & HOWLETTLLP
Attorneys for Energy Michigan, Inc.

September 17, 2004

By: _____
Eric J. Schneidewind (P20037)
The Victor Center, Suite 810
201 N. Washington Square
Lansing, Michigan 48933
(517) 482-6237

TAB A

**Energy Michigan Reply Brief
Case No. U-14098
September 17, 2004**

Blair, Daniel J (DLEG)

From: Jeanne M Kurzynowski [jmkurzyn@cmsenergy.com]
Sent: Thursday, May 20, 2004 4:36 PM
To: Blair, Daniel J (DLEG); Bak, Lawrence S (DLEG)
cc: Michael A Torrey
Subject: Option Capacity Costs - ST vs. LT



pic05705.jpg

As promised, following is Consumers' calculation of option capacity contracts broken down by single-year and multi-year. (The Michigan option capacity and energy numbers are off from my exhibit by \$1 due to rounding.) Please call me at 517-788-1110 if you have any questions.

Jeanne Kurzynowski

(Embedded image moved to file: pic05705.jpg)

2003 Option Capacity Contracts

	One-Yea	Mult Yea	Total
External Option Capacity Purchases	7,843,200	-	\$ 7,843,200
Michigan Capacity and Energy Purchases	994,800	10,228,999	\$ 11,223,799
	<u>\$ 8,838,000</u>	<u>\$ 10,228,999</u>	<u>\$ 19,066,999</u>

CE U-14098

2003 Option Capacity Contracts

	One-Year	Multi-Year	Total
External Option Capacity Purchases	7,843,200		\$ 7,843,200
Michigan Capacity and Energy Purchases	994,800	10,228,999	\$ 11,223,799
	<u>\$ 8,838,000</u>	<u>\$ 10,228,999</u>	<u>\$ 19,066,999</u>

ALL OPTIONS EXCLUDED

30,709,421 from JMK-1
 - 19,066,999 from 5/20 EMAIL
11,642,422
 X .98975
\$ 11,523,087

ONLY ONE YEAR EXCLUDED

30,709,421
 - 8,838,000
21,871,421
 X .98975
\$ 21,647,238

NET COST OF SEASONAL CAPACITY

Consumers Energy Company
Summary of 2003 Seasonal Capacity and Cost

<u>Line</u>	<u>Capacity Contract</u>	<u>Summer Peak MW</u>	<u>Total cost</u>
1	External Option Capacity	300	\$ 7,843,200
2	External Forward Capacity	100	\$ 4,317,604
3	Michigan Capacity and Energy	301	\$ 11,223,800
4	Peak Load Management	62	\$ 730,694
5	Sub-total Power Capacity	762	\$ 24,115,198 (1)
6	External Transmission Capacity (AEP, Cinergy, NIPSCO)	400	\$ 7,288,337 (2)
7	Transmission Capacity Sales - (MWh)		\$ (694,115) (3)
6	Total Seasonal Capacity Costs	6	\$ 30,709,421
Summer vs. Winter Capacity Costs			
9	Summer Capacity Costs	81.2%	\$ 24,937,793
10	Winter Capacity Costs	18.8%	\$ 5,771,627

- (1) Consumers Energy 2002 Capacity Costs (JMK-WP-1)
(2) Consumers Energy 2002 Transmission Reservations (JMK-W-2)
(3) Consumers Energy 2002 Resale of AEP Transmission (JMK-WP-3)

TAB B

**Energy Michigan Reply Brief
Case No. U-14098
September 17, 2004**

Case No. U-14098
Witness: SCDDevon
Exhibit S-21(SCD-1)
Date: July 23, 2004

CONSUMERS ENERGY
CALCULATION OF 2003 STRANDED COSTS

Line #	DESCRIPTION	2003 CONSUMERS	2003 STAFF ALL OPTIONS INCLUDED	2003 STAFF MULTI YEAR OPTIONS INCLUDED	2003 STAFF ALL OPTIONS EXCLUDED
1	Net Production Plant including CWIP	\$1,528,950	\$1,528,950		
2	Pre tax rate of return	10.63%	10.63%		
3	Return Requirement	162,527	162,527		
4	Depreciation	63,048	63,048		
5	R&PP tax	42,421	42,421		
6	Insurance	3,056	3,056		
7	PPA capacity	499,869	499,869		
8	Rev Req of Fixed Costs of Generation	\$770,921.39	\$770,921.39	\$770,921.39	\$770,921.39
9	Net Cost of Summer Capacity (Options)	30,395	30,395	21,647	11,523
10	TOTAL	<u>\$801,316</u>	<u>\$801,316</u>	<u>\$792,568</u>	<u>\$782,444</u>
11	TOTAL REVENUE REQUIREMENT	\$801,316	\$801,316	\$792,568	\$782,444
12	REMOVE CLEAR AIR ACT REV REQ	51,440	51,440	51,440	51,440
13	TOTAL REVENUE REQUIREMENT	<u>\$749,876</u>	<u>\$749,876</u>	<u>\$741,128</u>	<u>\$731,004</u>
14	TOTAL REVENUE FROM SALES TO ULTIMATE CUST	2,321,440	2,321,440	2,321,440	2,321,440
15	IMPUTED REVENUES		21,626	21,626	21,626
16	TOTAL REVENUE FROM SALES TO ULTIMATE CUST	<u>\$2,321,440</u>	<u>\$2,343,066</u>	<u>\$2,343,066</u>	<u>\$2,343,066</u>
17	GENERATION AS A % OF TOTAL SALES	29.1048%	29.1048%	29.1048%	29.1048%
18	CONTRIBUTION TO FIXED COSTS OF DIRECT GENER	675,650	681,945	681,945	681,945
19	CONTRIBUTION TO FIXED COSTS FROM 3RD PARTY	13,553	13,553	13,553	13,553
20	TOTAL CONTRIB TO FIXED COSTS OF GENERATION	<u>\$689,203</u>	<u>\$695,498</u>	<u>\$695,498</u>	<u>\$695,498</u>
21	TOTAL STRANDED COSTS	60,673	54,379	45,631	35,507
22	ADD:CLEAN AIR ACT REVENUE REQUIREMENT	51,440	0	0	0
23	TOTAL STRANDED COSTS	<u>\$112,113</u>	<u>\$54,379</u>	<u>\$45,631</u>	<u>\$35,507</u>

Case No. U-14098
Witness: SCDevon
Exhibit S-7 (SCD-1)
Date: July 23, 2004

CONSUMERS ENERGY COMPANY
CALCULATION OF 2003 STRANDED COST SURCHARGE

Line #	DESCRIPTION	2003 CONSUMERS	2003 STAFF ALL OPTIONS INCLUDED	2003 STAFF MULTI YEAR OPTIONS INCLUDED	2003 STAFF ALL OPTIONS EXCLUDED
1	TOTAL STRANDED COSTS	\$60,673	\$54,379	\$45,631	\$35,507
2	CARRYING COSTS @7%	8,792	7,879	6,612	5,145
3	2003 ACTUAL STRANDED COSTS WITH CARRYING	\$69,464	\$62,258	\$52,243	\$40,652
4	2005 ROA SALES FORECAST	6,636,799	6,636,799	6,636,799	6,636,799
5	STRANDED COST CHARGE	\$ 0.010467	\$ 0.009381	\$ 0.007872	\$ 0.006125

TAB C

**Energy Michigan Reply Brief
Case No. U-14098
September 17, 2004**

Consumers Energy
Calculation of 2003 Stranded Cost

Case No: U-14098
Exhibit No.: I-18
Page No.: 1 of 2
Witness: Richard A. Polich
Date: 23-Jul-04

Line No.	Description (a)	Energy Mich with CECO		Source
		Consumers (b)	Prod (c)	
Direct Costs				
1	Net Production Plant	\$1,528,950	\$1,528,950	MA Torrey Exhibit (MAT-1R)
2	Pre-Tax Rate of Return	10.63%	10.63%	MA Torrey Exhibit (MAT-1R)
3	Return Required	\$162,527	\$162,527	MA Torrey Exhibit (MAT-1R)
4	Depreciation	\$63,048	\$63,048	MA Torrey Exhibit (MAT-1R)
5	Property Taxes	\$42,421	\$42,421	MA Torrey Exhibit (MAT-1R)
6	Insurance	\$3,056	\$3,056	MA Torrey Exhibit (MAT-1R)
7	PPA Capacity Charges	\$499,869	\$472,983	2000 PPA Capacity Costs
8	Revenue Required of Fixed Gen.	\$770,921	\$744,035	Sum of Lines 3-7
9	Net Cost of Summer Capacity (Options)	\$30,395	\$0	
10	Total			
11	Total Generation Related Reg Assets	\$801,316	\$744,035	Sum of Lines 8-10
12	Remove Clean Air Act Rev Req	(\$51,440)	(\$51,440)	
13	Total Revenue Requirement	\$749,876	\$692,595	
Fixed Generation Related Revenue				
14	Total Revenue from Sales to Ultimate Customers	\$2,321,440	\$2,321,440	MA Torrey Exhibit (MAT-1R)
15	2003 Special Contract Revenue	\$0	(\$132,394)	MA Torrey Exhibit (MAT-8)
16	2003 Special Contract Revenue under Standard Tariffs	\$0	\$154,019	MA Torrey Exhibit (MAT-8)
17	Tariff Based 2002 Revenue	\$2,321,440	\$2,343,066	Sum of Lines 12-14
18	Generation as Percent of Sales	29.10%	29.10%	MA Torrey Exhibit (MAT-1R)
19	Fixed Generation Related Revenues	\$675,650	\$681,945	Line 12 * Line 13
20	From: Third Party Sales	\$13,553	\$13,553	MA Torrey Exhibit (MAT-1R)
21	Total Contribution to Fixed Generation Costs	\$689,203	\$695,498	Sum of Lines 14 & 15
22	Total Stranded Costs	\$60,673	(\$2,902)	Line 11 minus Line 20
23	ADD: Clean Air Act Revenue Requirement	\$51,440		
24	Final Stranded Costs/(Benefits)	\$112,113		

Case No: U-14098
 Exhibit No: I-18 (RAP-1R)
 Page No: 2 of 2
 Witness: R.A. Polich
 Date: 23-Jul-04

Consumers Energy
Calculation of 2003 Stranded Cost

Line No.	Description (a)	Energy	
		Consumers (b)	Michigan Source (c)
Direct Costs			
1	Net Production Plant	\$1,528,950	\$1,034,060 RAP WP-1
2	Pre-Tax Rate of Return	10.63%	10.63% MA Torrey Exhibit (MAT-1R)
3	Return Required	\$162,527	\$109,921 MA Torrey Exhibit (MAT-1R)
4	Depreciation	\$63,048	\$56,979
5	Property Taxes	\$42,421	\$42,421 MA Torrey Exhibit (MAT-1R)
6	Insurance	\$3,056	\$3,056 MA Torrey Exhibit (MAT-1R)
7	PPA Capacity Charges	\$499,869	\$472,983 2000 PPA Capacity Costs
8	Revenue Required of Fixed Gen.	\$770,921	\$685,360 Sum of Lines 3-7
9	Net Cost of Summer Capacity (Options)	\$30,395	\$0
10	Total	\$801,316	\$685,360 Sum of Lines 8-10
11	Total Generation Related Reg Assets	(\$51,440)	\$0
12	Remove Clean Air Act Rev Req	\$749,876	\$685,360
13	Total Revenue Requirement	\$2,321,440	\$2,321,440 MA Torrey Exhibit (MAT-1R)
Fixed Generation Related Revenue			
14	Total Revenue from Sales to Ultimate Customers	\$0	(\$132,394) MA Torrey Exhibit (MAT-8)
15	2003 Special Contract Revenue	\$0	\$154,019 MA Torrey Exhibit (MAT-8)
16	2003 Special Contract Revenue under Standard Tariffs	\$2,321,440	\$2,343,066 Sum of Lines 12-14
17	Tariff Based 2002 Revenue	29.10%	29.10% MA Torrey Exhibit (MAT-1R)
18	Generation as Percent of Sales	\$675,650	\$681,945 Line 12 * Line 13
19	Fixed Generation Related Revenues	\$13,553	\$13,553 MA Torrey Exhibit (MAT-1R)
20	From: Third Party Sales	\$689,203	\$695,498 Sum of Lines 14 & 15
21	Total Contribution to Fixed Generation Costs	\$60,673	(\$10,138) Line 11 minus Line 20
22	Total Stranded Costs	\$51,440	\$112,113
23	ADD: Clean Air Act Revenue Requirement		
24	Final Stranded Costs/(Benefits)		

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for determination of net stranded costs)
for the year 2003 and approval of net)
stranded cost recovery charges.)
_____)

Case No. U-14098

PROOF OF SERVICE

Monica Robinson, duly sworn, deposes and says that on this 17th day of September, 2004 she served a copy of Energy Michigan, Inc's Reply Brief in the above captioned matter upon those individuals listed on the attached service list by e-mail and regular mail at their last known addresses.

Monica Robinson

Subscribed and sworn to before me
this 17th day of September 2004.

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

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