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June 6, 2005

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

Re: Case No. U-14274

Dear Ms. Kunkle:

Attached for electronic filing is Energy Michigan's Replies to Exceptions in the above captioned matter. Also attached is the original Proof of Service indicating service upon counsel.

Thank you for your assistance in this matter.

Very truly yours,

VARNUM, RIDDERING, SCHMIDT & HOWLETT LLP

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 approval of a power supply cost)	
recovery plan and for authorization)	Case U-14274
of monthly power supply cost recovery)	
factors for calendar year 2005.)	
_____)	

ENERGY MICHIGAN, INC. REPLIES TO EXCEPTIONS OF CONSUMERS ENERGY AND THE ATTORNEY GENERAL

I. Introduction and Summary of Position

A. Introduction

These Replies to Exceptions to the Proposal for Decision (the "PFD") issued by Administrative Law Judge Mark Cummins ("ALJ") on May 12, 2005 are filed by Varnum Riddering Schmidt & Howlett LLP on behalf of Energy Michigan, Inc. ("Energy Michigan"). These Replies address Exceptions filed by Consumers Energy and Attorney General Michael Cox (the "Attorney General"). Failure to respond to other Exceptions should not be taken as agreement with those Exceptions.

Energy Michigan recognizes that the PFD issued on May 12, 2005 denied the Application of Energy Michigan for late intervention in this matter as well as the request of Energy Michigan that it be permitted to file Exceptions and Replies to the PFD. However, on May 17, 2005, Energy Michigan filed an Application for Leave to Appeal ("Application for Leave") the ruling of the ALJ and renewed its request for admission as an Intervenor in this matter with full rights to file Exceptions and Replies.

Given the issuance of the PFD in this matter on May 12, 2005, it was unlikely that the Commission would rule on the Energy Michigan Application for Leave before the May 26, 2005

due date for Exceptions. Therefore, Energy Michigan filed Exceptions in the nature of an Offer Of Proof under Rule 337(3) which may become a part of this record in the event that the Commission does grant the Energy Michigan Application for Leave.

This course of action was necessary because, if the Commission ultimately grants the Energy Michigan Application for Leave, there would be a delay in the proceeding or potential prejudice to other parties because Energy Michigan would have to file its Exceptions and Replies after the May 26 and June 6 dates established by the ALJ for Exceptions and Replies respectively. Since the Commission did not rule upon the Energy Michigan Application for Leave prior to the June 6, 2005 due date for Replies, Energy Michigan has filed Replies to Exceptions under the same theory.

B. Summary of Replies to Exceptions.

1. Attorney General Exception #4 correctly states that the PFD (Staff's) proposal to allocate third party sales revenue violates Order U-12639 requirements.

In his Exception #4, the Attorney General correctly states that the Staff methodology for allocating third party sales revenues adopted in the PFD has not established a connection between the amount of money allocated to mitigate stranded costs on the one hand and the amount of power that has been freed up by ROA service on the other hand. Therefore the proposal fails to meet the criteria established in Case U-12639 for mitigation. Moreover, it is quite likely that the Staff allocation proposal which assumes ROA sales are 17.2% of total Consumers deliveries yet allocates only 5.2% of third sales party revenue for stranded cost mitigation is flawed precisely because it does not link allocation of third party sales revenues to the amount of power actually made available for sale by ROA migration.

2. The Consumers Exception is correct that the third party sales allocation issue should not be decided in a vacuum as proposed in the PFD.

In its only Exception, Consumers Energy has correctly observed that the PFD attempts to address third party sales issues in a vacuum without considering the implications that recommendations regarding allocation of third party sales revenue will have on stranded cost calculation in other cases.

Energy Michigan has stated that the precedent created in this case would affect at least four other cases: the 2004 PSCR reconciliation case (U-13917-R), the 2004 stranded cost case which is yet to be filed, the yet to be filed 2005 PSCR reconciliation and the 2005 stranded cost case. In truth, since allocation of third party sales revenue has a direct impact on calculation of stranded cost, these issues should be decided in combined cases such as filed by Edison in Case U-13808-R where credits given for third party sales in 2004 are equally applicable to reconciliation of the 2004 PSCR revenue and expense and calculation of 2004 stranded costs.

II. Reply to Attorney General Exception #4

A. Attorney General Exception #4.

The Attorney General states that Staff's proposal to allocate third party sales revenue did not comply with the mandates of MPSC Order U-12639 as it applies to calculation of stranded costs. Attorney General Exception #4, p. 19.

B. Energy Michigan Reply.

The "MPSC Staff Methodology" for calculating stranded costs adopted in Case U-12639 requires that "...energy that [is] freed up when customers choose alternative electric suppliers be used as a mitigation method to offset calculated stranded costs..." U-12639, December 20, 2001, p. 10 (emphasis supplied). Therefore, under the Commission stranded cost methodology, the Staff should base its method for allocating third party sales revenue to offset stranded costs on actual ROA sales volumes. In the alternative, Staff should have proved that its calculation or allocation method accurately linked its proposed allocation of third party sales revenue to pay stranded costs with the amount of power freed up by ROA migration. The Staff method did neither.

Instead, Staff developed a new formula for allocation which purports to compare the fixed costs paid by retail customers with the power supply fixed costs paid by ROA customers. By making the unjustified assumption that ROA customers may constitute 17.2% of total deliveries but should only receive 5.2% of third party sales revenues, Staff virtually guarantees a mismatch between the amount of third party sales revenue used to mitigate stranded costs and the amount of energy freed up when customers migrate to ROA. Ancona, Tr 433.

Nowhere in his testimony does Mr. Ancona provide support for the linkage of his proposed method of allocating third party sales revenue and the actual amount of power freed up by ROA migration as is mandated by the Commission in U-12639. U-12639, December 20, 2001, p. 10. Such a showing is necessary in order to overcome the burden of revising the existing methodology for third party sales allocation adopted in Case U-12639 as referenced above.

As will be seen below, the Attorney General's Exception #4 also emphasizes an extremely important point: Staff's revenue allocation proposal amounts to a substantial revision of the stranded cost methodology adopted in Case U-12639. *Id.*, p. 19. This subject matter was not noticed for this 2005 PSCR Plan case. Potentially interested parties such as Energy Michigan were not informed that the "Staff Method" of calculating stranded costs would be the subject matter of this proceeding.

In conclusion, the Attorney General is correct: By destroying any linkage between the amount of capacity and energy made available because of migration to ROA service on the one hand with the portion of third party revenues that can be used for stranded costs mitigation, on the other hand, Staff's allocation method ensures a mismatch between the results adopted in this 2005 PSCR Plan case and the results that would likely be adopted in a stranded cost case calculation for year 2005.

By treating this Plan case as establishing a temporary factor to be finalized in a later combined 2005 PSCR reconciliation and 2005 stranded cost case the Commission can assure that 1) interested parties are noticed and 2) that the final result is accurate and uniform for both PSCR calculation and stranded cost calculation.

III. Reply to Consumers Energy

A. Consumers Exception.

The Consumers Exception contends that the PFD erroneously asks the Commission to consider treatment of third party sales revenues in a vacuum. Consumers Exception, p. 1.

The Exception of Consumers Energy observes that their own witness Torrey established, "...the close relationship that the Staff proposal in this case will have on stranded cost calculations in other cases...". Consumers goes on to state that these considerations should be incorporated by the Commission in its decision concerning third party sales revenues. Consumers Exceptions, Id.

B. Energy Michigan Reply.

Consumers understates the problem. The third party sales allocation solution recommended by the PFD will impact a pending 2004 PSCR reconciliation case U-13917-R, a 2004 Consumers Energy stranded cost case yet to be filed, a 2005 PSCR reconciliation case yet to be filed and a 2005 stranded cost case yet to be filed. There may also be an impact on the U-14347 Consumers general rate case where several parties including Energy Michigan have filed proposals to establish future stranded costs.

The PFD and MPSC Staff, however, ask the Commission to establish what amounts to a revision of a stranded cost methodology established in Case U-12639 in a 2005 PSCR Plan case where Staff did not even establish what portion of third party sales were made possible by power freed up due to migration to ROA service. The Commission cannot possibly know the answer to that question for 2005 since actual sales data and alleged stranded cost data has not even been established and will not be established until the 2005 Reconciliation case is filed in the spring of 2006. If the Commission proceeds as recommended by Staff it will be blindly be establishing a methodology for 2005 that could lead the absolutely unforeseen results.

The far better approach would be to treat this 2005 plan case as establishing a temporary factor based on Staff's recommendations regarding allocation of third party sales revenue but finalizing both the amount of revenue allocated and the method of allocating that revenue in a combined docket which considers 2004 final PSCR data (U-13917-R) and a yet to be filed 2004 stranded cost case.

To lend urgency to this situation, the Commission should be aware that in the 2004 reconciliation case, Consumers has openly stated that it will have over \$20 million of stranded costs during calendar year 2004 which under U-12639 methods of allocating third party sales revenue would have been fully offset. U-13917-R Application, March 31, 2005; Testimony of David Ronk, p. 25. However, if the Commission revises the third party sales allocation method as urged by Staff, there is no way whatsoever, of knowing how much if any of this \$20 million of stranded cost will be offset.

IV. Conclusion and Prayer for Relief

WHEREFORE, Energy Michigan respectfully requests that the Commission:

- A. Utilize the recommendation of the PFD as a format for the 2005 plan year but reserve final decision on the Staff methodology for allocating third party sales (or any such methodology) until completion of the 2005 Reconciliation Case and stranded cost cases; and
- B. Rule that the Staff methodology contains a fundamental flaw described in Energy Michigan Exception #3 which must be reviewed and corrected in a PSCR Reconciliation proceeding for the year 2005.

Respectfully submitted,

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

June 6, 2005

By: _____

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Case U-14274

PROOF OF SERVICE

Monica Robinson, duly sworn, deposes and says that on this 6th day of June, 2005 she served a copy of Energy Michigan, Inc.'s Replies to Exceptions upon the individuals listed on the attached service list by e-mail only at their last known addresses.

Monica Robinson

Subscribed and sworn to before me
this 6th day of June, 2005.

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

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