July 8, 2015

Ms. Mary Jo Kunkle  
Executive Secretary  
Michigan Public Service Commission  
7109 W. Saginaw Hwy  
Lansing, MI  48917

Dear Ms. Kunkle:

**RE: MPSC Case No. U-17690**

Enclosed for filing in the above-captioned case please find the *Attorney General's Initial Brief* together with a proof of service. This filing is being submitted electronically pursuant to the Commission's Paperless Electronic Filings Program.

Sincerely,

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MEM/wjc  
Enclosures  
c: All Parties
PROOF OF SERVICE - U-17690

The undersigned certifies that a copy of the Attorney General's Initial Brief was served upon the parties listed below by e-mailing the same to them at their respective e-mail addresses on the 8th day of July, 2015.

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In the matter of the application of
MICHIGAN GAS UTILITIES CORPORATION for authority to
implement a Gas Cost Recovery Plan
and Factors for the 12-Month period from
April 2015 through March 2016 and
for related approvals

ATTORNEY GENERAL'S INITIAL BRIEF
I. ARGUMENT

A. The Commission should adopt the Attorney General’s recommendation to amend the revised 2015-2016 GCR plan GCR and GCC sales forecast.

In its revised GCR plan, MGUC included a GCR sales volume forecast of 16,620,243 Mcf and GCC sales volume forecast of 2,791,768 Mcf. Attorney General expert witness Sebastian Coppola examined MGUC’s gas sale forecasting techniques and found that the Company’s 2015-2016 forecasts for GCC customers are significantly underestimated. (Tr 177-179.) Mr. Coppola explained that for GCR customers the average usage per customer forecasted by the Company for the various customer classes tracked relatively well with historical weather normalized usage for the year 2014. (Tr 178.) For GCC customers, however, there is a significant difference in gas usage between the Company’s forecast and recent 2014 actual weather-normalized usage. (Tr 178.)

Mr. Coppola explained the difference as follows:

Exhibit AG-1 show significant differences in gas usage between the Company’s forecast and recent 2014 actual weather-normalized usage. The Company is forecasting usage of 84.59 Mcf per customer for Residential customers when the weather-normalized usage in 2014 was 97.91 Mcf. This is a significant decline of 13.22 Mcf or nearly 14% from 2014. In the same vein, Multi-Family and Small Commercial GCC customers’ average usage in the Company’s 2015-2016 forecast is significantly lower than the weather-normalized gas usage in 2014. These large unexplained variances indicate a faulty forecast of GCC sales volumes. [Tr 178.]

The Company did not provide an explanation in its testimony for such a large decline in GCC sales for the 2015-2016 forecasted year compared to the
recent 2014 numbers. In rebuttal, MGUC did not provide an explanation for such a large decline in GCC sales. Instead, MGUC argued that its forecasting methodology was better and that it can take into account trends. (Tr 98-104.) In fact, MGUC argued that Mr. Coppola should have recommended a lower GCR forecast based on his forecast methodology, again without addressing the significance of Mr. Coppola’s testimony. (Tr 99.)

MGUC’s rebuttal completely ignored Mr. Coppola’s concern regarding the 2015-2016 forecast. Mr. Coppola demonstrated that his forecast methodology using the historical weather-normalized usage for 2014 followed the Company’s GCR usage forecast but that the variance between the 2014 GCC numbers and the Company’s 2015-2016 GCC forecast was nearly 14% or more than double any variance in the GCR forecast. Mr. Coppola’s recommendation is that the Commission should adjust the GCC forecast because a 14% variance with no explanation demonstrates a problem with the Company’s forecasting methodology. The Company’s argument that its forecast methodology takes into account other things does not provide any concrete explanation for the 14% variance from 2014 numbers. The Company should be required to explain why its forecast is reasonable in light of the large variance from a prior year and not just rely upon general arguments about how its forecast takes into account trends. The Company needs to identify the trends or the other factors that led to the variance in order to
demonstrate that its forecast is reasonable and should be relied upon by the Commission.

Accordingly, the Commission should amend the revised 2015-2016 GCR plan filed by the Company to include the additional GCC sales volumes of 737,835 Mcf, identified in Exhibit AG-1. Furthermore, the Commission should adopt the revised total sales volumes of 20,149,846 Mcf in calculating MGUC’s Reservation Charge for the 2015-2016 period.

B. The Commission should require MGUC to evaluate the cost-effectiveness of continuing to operate the Partello-Anderson storage reservoir and to explore other alternatives.

Attorney General witness Sebastian Coppola testified that the company’s use of the Partello-Anderson storage reservoir may no longer be the best alternative for the company because of a number of changes in the Company’s ability to withdraw natural gas from the reservoir. (Tr 180-183.) Based on the testimony of the Company’s witness and responses to discovery, the Partello-Anderson storage withdrawal has declined from total withdrawal capabilities in 2014 of 340,000 Mcf to only 137,000 Mcf for 2015-2016 and going forward. (Tr 180-181.) In addition, 919,000 Mcf can no longer be cycled and will likely need to be retained in the filed as base gas. (Tr. 180-181.)

Because of the limited ability to withdraw gas and the 919,000 Mcf that can now only be used as base gas and must remain in the reservoir, Mr. Coppola recommended that the Company should examine whether it makes
sense to withdraw all recoverable gas from the Partello-Anderson storage and purchase the needed storage deliverability from a third party. (Tr 182.) Based on the current price of $3 per Mcf, Mr. Coppola calculated that there is in excess of $6.6 million worth of natural gas that can be withdrawn for the benefit of MGUC’s customers.

In rebuttal, MGUC witness Sarah Mead claims that 2.92 Bcf can be cycled during the winter season and that maintaining the Partello-Anderson storage is less costly than purchasing ANR storage. (Tr 72.) The problem with MGUC’s rebuttal is that it is completely contrary to its discovery response and not responsive to Mr. Coppola’s recommendation in this case. First, in response to the Attorney General’s request to confirm that only 137,000 Mcf is usable for cycling working gas inventory in the Partello-Anderson storage field, Ms. Mead explained “Of the 1.056 Bcf that MGUC was carrying as working gas in the fields, about 137,000 Mcf can be safely withdrawn.” This is consistent with Mr. Mead’s direct testimony at page 11 of her direct testimony but contrary to her rebuttal testimony at page 2. (Tr 34, 72.) Second, the discovery request asked whether it was cost effective to operate the fields with only such a small volume of cyclable gas, but Ms. Mead only provided one sentence about the cost of a comparable alternative and never explained whether it was cost effective to operate the field with such a small amount of gas cyclable.
Because of the reduced withdrawal ability from the Partello-Anderson storage field and the large amount of gas that must be kept as base gas, the Attorney General recommends that the Commission direct the Company to evaluate the cost-effectiveness of continuing to operate the Partello-Anderson storage reservoir and to explore other alternatives, including abandoning the reservoir, replacing its current storage withdrawal capacity with third party storage services and removing all recoverable gas from the reservoir for the benefit of its customers. The Commission should require that this analysis be performed no later than 90 days from the date of an order in this case and the conclusions implemented no later than in the 2016-2017 GCR period.

C. The Commission should adopt the Attorney General’s recommendations regarding MGUC’s gas supply and basis hedging.

MGUC is re-evaluating its gas supply portfolio during the summer of 2015 and is looking into different purchase locations as well as hedging options. (Tr 183-184.) The Attorney General’s first concern with MGUC’s plan to re-evaluate is its failure to provide any significant details regarding its intentions and its failure to provide a detailed 5-year plan of supply arrangements the Company expects to enter into with pipeline suppliers as required by MCL 460.6h(4). (Tr 184.) Attorney General recommends that the Commission direct MGUC to be more forth coming and transparent in presenting its 5-year gas supply plan in future GCR plan filings. (Tr 190.)
Second, the Attorney General expressed concern that 28% of the Company’s peak demand will be supplied by call and swing supply not yet contracted. (Tr 186.) This reliance on call and swing supply which will be priced at spot market prices at a time of peak demand represents a significant price risk and perhaps also somewhat of a supply risk if short term pipeline capacity is not available. (Tr 186.) Accordingly, the Attorney General recommends that MGUC include in its planned analysis of the supply portfolio a review of the appropriate exposure to call and swing supply with the objective of diminishing its reliance on this source of supply. (Tr 186.)

The Attorney General’s third recommendation involves MGUC’s proposal to hedge a portion of its basis price exposure. (Tr 186.) The Attorney General supports the Company’s proposal but recommends that the Company provide a cost/benefit analysis to support the conclusion that hedging the basis price would be beneficial to customers. (Tr 186-187.) In addition, Attorney General expert witness Sebastian Coppola suggested that the Company expand its gas purchasing practices to include gas purchases priced off of the NYMEX month-end index. (Tr 187.) Mr. Coppola explained that this additional price mechanism would further diversify gas supply price risk. (Tr 187.) In rebuttal, MGUC does not object to performing a cost/benefit analysis as recommended and plans on acquiring the necessary information to conduct such an analysis. (Tr 136.) In addition, MGUC stated that it is
examining this gas purchasing practice and the hedging that the Company is considering does include purchases made at NYMEX price. (Tr 136-137.)

Accordingly, the Attorney General recommends that the Commission direct the Company to be thorough in its scope and include of review of its needs for interstate transportation, intrastate transportation, gas storage capacity owned and leased, diminished reliance on call/swing gas supply, access to new gas supply basins, and the use of NYMEX month-end settlement price purchases in the mix of its monthly gas purchases. (Tr 190.) Although it appears from rebuttal that MGUC is already looking into many of these recommendations, the Attorney General requests that the Commission confirm that such an analysis by the Company is reasonable and prudent and should be performed.

D. The Commission should adopt the Attorney General’s revised GCR factor and reservation charge.

In exhibit AG-9, Attorney General expert witness Sebastian Coppola demonstrates how he calculated a revised Commodity GCR factor of $3.0101 per Mcf and a capacity Reservation Charge of $0.5932 for the 2015-2016

1 In her rebuttal, Ms. Mead argues that Mr. Coppola’s statement that there is a clear case where field price indices escalated much higher than NYMEX prices is unsupported in this direct testimony at page 20 lines 12-14. (Tr 73.) The problem with Ms. Mead’s criticism is that she fails to acknowledge pages 21-23 of Mr. Coppola’s direct testimony providing support for his statement. (Tr 187-190.)
period. (Exhibit AG-9; Tr 194.) As explained by Mr. Coppola, the only changes made to MGUC’s filed exhibits are as follows:

1. On line 4, I revised the price hedging costs the Company had included in its Exhibit A-17. The Company’s number of $1,157,175 is not support by the information provided in response to Data Request 1-AG-15. The information supports only an amount of $175,554. Exhibit AG-8 shows the attachment to DR 1-AG-15 and how this revised amount was calculated.

2. On line 9 and 10, I excluded both the prior year Reservation Charge and GCR over-recovery amounts.

3. On line 14, I included the additional GCC sales calculated in Exhibit AG-1. (Tr 195.)

The above changes would result in 2015-2016 GCR expense totaling $61,981,545, including capacity reservation costs, instead of the total of $62,955,405 forecasted by MGUC before the offset of prior year over-recoveries. (Tr 195.)

In comparing his recommended GCR commodity factor and reservation charge with the Company’s requests in its revised filing, Mr. Coppola explained:

As stated above, I recommend that the Commission approve a revised GCR Commodity factor of $3.0101 per Mcf. My factor is based upon recovering the projected revised gas supply commodity costs of $61,981,545 for the 2015-2016 period and dividing that cost by the projected volume of sales for the GCR year. Similarly, I recommend
that the Commission approve a Reservation Charge of $0.5932 per Mcf. This charge is based on dividing the projected capacity reservation costs of $11,952,070 by the combined GCR and GCC sales volumes of 20,149,846 Mcf.

In its February 2015 revised filing, the Company proposed a GCR Commodity factor of $3.0005 and Reservation Charge of $0.5268. The basic difference between my factors and the Company’s proposal relates to the adjustment of hedging losses, my proposal to increase forecasted GCC sales volumes, and my proposal to exclude the Company’s forecasted 2014-2015 GCR Commodity and Reservation Charge over-recovery amounts from the calculation of 2015-2016 GCR Commodity factor and Reservation Charge. [Tr 195-196.]

The main difference between Company’s numbers and the Attorney General’s numbers is the exclusion of the Company’s forecasted 2014-2015 GCR Commodity and Reservation Charge over-recovery amounts from the calculation of 2015-2016 GCR Commodity factor and Reservation Charge. (Tr 196.)

Mr. Coppola provided a detailed explanation as to why the Commission’s policy should be to exclude such a roll-in and require such over and under recoveries to be treated as a separate line item on customers’ bills aside from the GCR Commodity factor and Reservation charge for current deliveries:

Q. WHY DID YOU EXCLUDE THE PRIOR YEAR GCR AND RESERVATION CHARGE OVER-RECOVERY
AMOUNTS FROM YOUR CALCULATION OF THESE FACTORS FOR 2015-2016?

A. Any 2014-2015 GCR over-recovery amounts are related to consumption of natural gas during that period. Furthermore, 2014-2015 GCR expenses and capacity costs are unrelated to consumption of natural gas during April 2015 through March 2016. In my opinion, the 2015-2016 GCR factor should be calculated by projecting only GCR expenses and capacity costs incurred by MGUC to deliver natural gas to GCR customers and capacity reservation services from April 2015 through March 2016.

Thus, the 2015-2016 GCR Commodity factor should be calculated by dividing total projected GCR expenses for gas to be delivered from April 2015 through March 2016 by the projected volume of GCR deliveries for the same period. Similarly, the capacity Reservation Charge should be calculated by dividing the capacity reservation costs to be incurred during the 2015-2016 period by the total GCR and GCC sales forecasted to be delivered during the same time period.

Q. WHY SHOULD OTHER COSTS BE EXCLUDED FROM GCR AND RESERVATION FACTORS?

A. The GCR Commodity factor is multiplied times the amount of gas each customer buys during each month in the GCR year; therefore, adding or subtracting any costs to the costs which MGUC will incur to deliver natural gas to customers during the GCR year will send a misleading and inaccurate price signal to each customer. Adding under-recoveries or over-recoveries from another year
will result in a factor that is either higher or lower than MGUC’s booked costs of gas sold for the volumes being billed to the customer that year. Customers cannot accurately compare the price for the gas they are currently buying from MGUC with the price they might pay to alternative gas suppliers or for alternative fuels.

Adding under-recoveries or over-recoveries to the booked costs of gas sold means that customers in the prior period will either pay below the actual costs or more than the actual cost for the natural gas they use. For customers billed during the subsequent year, the opposite results will happen. In addition, an annual under-recovery or over-recovery represents the cumulative annual impact of paying too little or too much.

The same arguments also hold for the capacity Reservation Charge billed to both GCR and GCC customers.

Q. IS THERE RECENT EVIDENCE THAT THE WRONG CUSTOMERS ARE PAYING FOR OR BENEFITTING FROM PRIOR YEARS’ UNDER-RECOVERIES AND OVER-RECOVERIES?

A. Yes. In his testimony Mr. Wallin has stated that during 2014-2015 GCR period a significant number of customers migrated from the Gas Choice program back to GCR service and that further migration is expected during the 2015-2016 period.

Information obtained from the Company through data requests shows that the

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2 Aaron Wallin Supplemental Direct Testimony at page 6.
number of GCC customers has declined from 30,202 at the end of March 2014 to a level of 23,087 at the end of March 2015 and is expected to decline further to 20,484 by the end of March 2016.  

In my Direct Testimony filed in Case No. U-17331, I had predicted that the roll-in of the 2013-2014 GCR under-recovery into the 2014-2015 GCR factor would result in a misallocation of prior year costs to the wrong customers. The evidence from the concluded 2014-2015 plan year indicates that 7,115 GCC customers, who migrated from the Gas Choice program to GCR service during 2014-2015, paid for a portion of the $6.6 million in gas costs under-recovered in the prior year when they were not GCR customers. Similarly, with the Company now proposing to roll-in $1.1 million of over-recoveries from the 2014-2015 GCR period, the 2,500 GCC customers who will likely move from the Gas Choice program to GCR service during the 2015-2016 period will benefit from the roll-in of the over-recovery when again they were not GCR customers in that prior year.

This anticipated customer migration clearly shows the inequities created by rolling in prior year over- and under-recoveries into the current year GCR factor.

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3 MGUC responses to data request 1-AG-6 and Exhibit A-8.

Q. SHOULDN'T UTILITIES RECOVER UNDER-
RECOVERIES OR CREDIT CUSTOMERS FOR OVER-
RECOVERIES?

A. Yes. However, charges or credits should be treated as a separate line item on customers’ bills aside from the GCR Commodity factor and Reservation Charge for current deliveries. The under- and over-recovery amounts should be allocated to the customers who bought the gas related to any under- or over-recovery. Even if the total is relatively small, the charge or credit should still be treated as a separate line item in customers’ bills.

Q. HAS THE COMPANY MADE A PERSUASIVE CASE THAT THE ADMINISTRATIVE COSTS OF RETURNING TO A SEPARATE BILL SURCHARGE OR CREDIT MECHANISM FAR OUTWEIGH THE BENEFITS OF ACCURACY?

A. No. I have seen no quantitative analysis showing what the administrative costs would be of implementing such a computerized process. The Commission should not accept vague claims of excessive administrative costs. The Company bears the burden of proving what the real administrative costs are so that the Commission can make an informed decision based on solid evidence and can properly weigh the benefits of billing accuracy versus the cost of achieving that desired level of accuracy.

Q. DO YOU HAVE A RECOMMENDATION TO AVOID OVER-RECOVERY OF CAPACITY RESERVATION COSTS?
A. Yes. During the 2014-2015 GCR period, the Company continued to charge GCR and GCC customers the approved maximum Reservation Charge of $0.5933 per Mcf for the first three months and $0.4691 per Mcf for the remaining 9 months.\(^5\) The Company continued to charge these maximum rates despite the fact that it was experiencing an over-recovery throughout the year. The same problem, and to a greater extent, occurred during the 2013-2014 GCR period due to higher sales and the fact that nearly all of the reservation costs are fixed costs that do not vary with increased sales volumes. The result is that for the 2013-2014 period the Company over-recovered in excess of $3.2 million and for the 2014-2015 period it forecasts to over-recover approximately $1.7 million.

In my opinion, such large over-recoveries should be prevented. From its response to a data request, the Company does not believe it has the authority to reduce the Reservation Charge when increased sales volumes indicate a large cumulative over-recovery is likely to occur for the GCR year\(^6\). The Company should have the authority to minimize over-recovery of capacity reservation costs.

Therefore, the Commission should clarify in its order in this case that the approved Reservation Charge is a maximum rate that the Company can charge and the

\(^5\) Exhibit A-16, page 2.

\(^6\) MGUC response to Attorney General discovery request U-17331 3-AG-22.
Company can reduce that rate if in its best judgment believes it necessary in order to minimize over-recovery of capacity reservation costs.

[Tr 196-200.]

In rebuttal, MGUC does not dispute the argument that a proper price signal is important but claims that the Attorney General is exaggerating the price signal attributable to the roll-in methodology and admits that the its roll-in methodology is not designed to guarantee that costs be attributed to the same customers that incurred those costs. (Tr 157, 161.) MGUC also argues that the separate line item would be too complicated for a customer to understand. (Tr 163.)

The Attorney General believes that providing customers with more transparency regarding their gas usage is not only helpful to any customer who seeks to determine actual charges for service in comparing competitive options, but also it is reasonable and prudent to only charge customers for the gas they used instead of simply charging all customers higher charges for sake of expediency and ease of operation. Accordingly, the Commission should adopt the Attorney General's recommendations regarding the treatment of over and under recoveries.
II. RELIEF REQUESTED

For the reasons stated above, the Attorney General respectfully requests that the Commission adopt the recommendations provided in his direct testimony and exhibits and presented in this Initial Brief.

Respectfully submitted,

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Attorney General

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