

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of CONSUMERS)	
ENERGY COMPANY for accounting and ratemaking)	Case No. U-12999
approval of depreciation rates for gas utility plant.)	
_____)	

At the October 14, 2004 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. J. Peter Lark, Chair
Hon. Robert B. Nelson, Commissioner
Hon. Laura Chappelle, Commissioner

OPINION AND ORDER

On June 29, 2001, Consumers Energy Company (Consumers) filed its application for accounting and ratemaking approval of revised depreciation rates for its gas utility plant. Hearings began before Administrative Law Judge Daniel E. Nickerson, Jr. (ALJ), on August 16, 2001. At that hearing, the ALJ granted the interventions of Attorney General Michael A. Cox (Attorney General)¹ and the Association of Businesses Advocating Tariff Equity (ABATE). The Commission Staff (Staff) also participated in the proceedings. Hearings continued on November 6 and December 7, 2001.

At the December 7, 2001 hearing, the parties agreed to an indefinite suspension of the case to no later than October 2003 and moved for the ALJ to accept their agreement. During the period of suspension, the parties agreed to review cost-of-removal issues, to update filings as necessary, and

¹Mr. Cox assumed the office of Attorney General on January 1, 2003, and was substituted for former Attorney General Jennifer M. Granholm; MCR 2.202 (C).

to utilize the existing rates for purposes of revenue requirement calculations within Consumers' then-pending rate proceeding, Case No. U-13000. The parties also agreed that after revised depreciation rates were established, those rates would be synchronized with the company's retail rates for gas utility service. The ALJ accepted the parties' agreement and suspended the proceeding.

The ALJ reconvened the proceeding on October 14, 2003. The parties presented updated testimony and exhibits at a hearing on March 10, 2004. Briefs and reply briefs were filed by the parties, and the ALJ issued his Proposal for Decision (PFD) on June 28, 2004. Consumers, the Staff, the Attorney General, and ABATE filed exceptions and replies to exceptions. Consumers' depreciation rates were last completely reviewed in, and then formally established by, the December 7, 1998 order in Case No. U-11509.

The Proposal for Decision

In his PFD, the ALJ reviewed the various positions of the parties. He noted that the major controversies between the parties centered on the appropriate procedure to be used for determining an asset group's service life and the computation and recovery of net-salvage values. Consumers presented two primary positions, one using the equal life group (ELG) procedure and the other using the average life group (ALG) procedure. In both instances, the proposed depreciation rates continued past practices regarding computing net-salvage values. The ALG procedure was used in Consumers' last depreciation case to establish present rates; a shift to the ELG procedure increases the initial level of depreciation expense when compared to a continuation of the ALG procedure, which maintains approximately the same level of depreciation expense as that obtained from the last depreciation case. Consumers based its net-salvage values on a review of ten years of past

experience (if available) or a projection of net-salvage values when the company determined that use of past data would not be appropriate, such as for gas storage wells and related items.

The Staff would continue use of the ALG procedure, but would then base its net-salvage values on a five-year average of the company's recent net-salvage experience. This reduces the level of depreciation expense below that produced by the depreciation rates authorized in Consumers' last depreciation case.

ABATE and the Attorney General would continue use of the ALG procedure, and each proposed a revised method of recovering net-salvage cost. While similar in effect, the procedures are different. ABATE removes net-salvage cost from the depreciation calculation, and then recovers that cost as a separate expense item. ABATE bases that expense item on a five-year average of the company's recent net-salvage experience. The Attorney General continues to recover net salvage through the depreciation calculation, but separates net salvage from depreciation, calculates a net-salvage amount based on recent company experience, and then collects that amount through the depreciation accounts. The Attorney General provides net-salvage ratios based on his theory, which he then uses to compute depreciation rates. Using either ABATE's proposal or the Attorney General's proposal would reduce the level of depreciation expense significantly below that produced by the rates authorized in Consumers' last depreciation case.

The ALJ was persuaded that Consumers should continue use of the ALG procedure. He also recommended that the Commission move to the method of computing and recovering net-salvage value recommended by the Attorney General. The Staff, ABATE, and Consumers except to his recommendations.

The Equal Life Group Procedure

Consumers proposed a change from its current ALG procedure to the ELG procedure; each procedure is a methodology to establish the service lives of the assets within an asset group. The remaining parties advocated continued use of the ALG procedure. In its exhibits, Consumers separately paired these procedures with the remaining life technique to establish proposed depreciation rates. The company presently uses the remaining life technique to set its depreciation rates, and the parties did not propose a change from that technique. As regards the evidence in this proceeding, the use of the ELG procedure increases the initial depreciation expense levels for the various vintages of Consumers' gas utility plant when compared to use of the ALG procedure.

The ALJ was persuaded by the arguments of the Staff, the Attorney General, and ABATE that use of the ALG procedure should be continued. He dismissed Consumers' argument for a change to the ELG procedure, directing that Consumers continue use of the ALG procedure coupled with the remaining life technique. In its exceptions, Consumers withdrew its request to utilize the ELG procedure. Accordingly, the Commission finds that Consumers should continue to utilize the ALG procedure coupled with the remaining life technique when establishing its depreciation rates.

Remaining Issues

As part of the record, Consumers submitted a depreciation study. That study is based on December 31, 2002 gas utility plant balances; it also includes the consolidation of the assets of Consumers' Michigan Gas Storage Company subsidiary into the parent utility. The study involved four steps: (1) life analysis, (2) salvage and cost-of-removal analyses, (3) evaluation of the analyses' results and determination of mortality characteristics, and (4) calculation of applicable depreciation rates. Items Nos. 1, 2, and 3 are independent reviews, which are then used within Item No. 4 to calculate depreciation rates.

Life analysis concerns the determination of average service life and retirement dispersion, as identified by standard Iowa-curve type patterns. These curves are a series of frequency distributions used to describe the mortality of physical property. The ALJ noted that the parties did not dispute the average service lives and dispersion curves used in the depreciation study. The parties did not file exceptions to the ALJ's review, and the Commission finds appropriate the average service lives and dispersion curves used by Consumers within its study. (As noted above, Consumers' request to use the ELG procedure has been withdrawn.)

Salvage and cost-of-removal analyses concern the reviews of appropriate net-salvage values to be used when calculating depreciation rates. The analyses produce net-salvage factors. A depreciation accounting system distributes the cost of a tangible asset over that asset's estimated useful life. The cost of the asset is reduced (or increased) by its end-of-life salvage value, which is estimated at the time that the asset is placed into service; that salvage value includes any cost to eventually remove the asset from service. In many instances, the cost to remove the asset exceeds its actual salvage value. In such instances, the asset's net-salvage value is a negative number. Under current regulatory depreciation accounting, the negative net-salvage value is combined with the asset's acquisition cost, and it increases the amount to be depreciated over the asset's useful life.

The ALJ noted that the net-salvage factors used by Consumers have a significant effect upon the company's yearly depreciation expense level. This expense is, of course, one component used when setting Consumers' rates for its gas utility services. If depreciation rates are set artificially low, thereby shifting costs out to future generations that should be paid by current customers, then intergenerational equities will be affected—later generations of customers will pay expenses that earlier generations should have borne.

The Attorney General states that the critical variables identified in Consumers' depreciation study are: (1) the average service life of each gas utility plant account, (2) the retirements dispersion curve, (3) the expected salvage value of the plant, and (4) the expected cost of removal of the plant. He continues that these four variables, along with the record of accrued depreciation reserve in the separate functional categories of gas utility plant (gas storage, transmission, distribution, and general), determine each of the appropriate depreciation rates. The Attorney General notes that the company estimated the average service lives and retirement curves for most of its gas utility plant accounts from actuarial analyses of the aged retirements of plant during recent years. He states that the salvage and cost-of-removal parameters were developed using two methods: (a) for two of the gas storage accounts the company provided estimates of removal costs per gas well based on recent experience and expected removal costs, and (b) for the remainder of the accounts, the company developed net-salvage ratios (salvage less cost of removal) by comparing recent salvage and removal cost experience in each account with the original cost of the plant retired from that account.

The Attorney General notes that the accounting procedures authorized by the Federal Energy Regulatory Commission's (FERC's) Order No. 631² separate depreciation from recovery of removal costs for FERC-jurisdictional entities. Order No. 631 relates to accounting, financial reporting, and rate-filing requirements for asset retirement obligations; the order deals mainly with Statement of Financial Accounting Standards (FAS) No. 143, which prescribes the treatment of future costs associated with legal obligations to retire assets. The order does not apply FAS No. 143 standards to all retirement obligations, but it does require FERC-jurisdictional entities to

²FERC Order No. 631, Accounting, Financial Reporting, and Rate Filing Requirements for Asset Retirement Obligations, order issued April 9, 2003 in Docket No. RM02-7-000; 69 FR 19610.

maintain separate records for the cost of removal for non-legal obligations where allowances for these costs could be identified.

In the Attorney General's view, depreciation and cost of removal are separate procedures, each with its own set of accrual rates, annual accruals, and accumulated reserves. The Attorney General does not challenge any of the life or survivor curve parameters proposed by the company. However, the Attorney General would change the method of recovery of net-salvage costs. He would maintain separate subsidiary cost-of-removal records and then identify additions and deletions from this account each year. The Attorney General recognizes that this is a major change from the previous treatment of removal costs, but he argues that it is an appropriate change because under existing practices it is difficult to identify what portion of the company's annual depreciation expense recovered past capital expenditures and what portion of that expense was accrued to offset future removal costs.

The Attorney General separates the company's proposed depreciation rates and accruals into their two constituent parts: depreciation and cost-of-removal allowances. He would base his cost-of-removal allowances on the company's most recent five-years' experience. Utilizing a variant of the type of accounting required by FAS No. 143 for financial reporting of legal asset retirement obligations, the Attorney General proposes that the company book a liability for an asset's projected retirement cost, discounted at a risk-free interest rate to arrive at the appropriate present value. Then, the Attorney General continues, each year the company would show two items of expense: (1) the amortization of the booked retirement liability, and (2) the annual accretion in the present value of that liability. In the Attorney General's view, this FAS No. 143-derived procedure recognizes the present value of future removal costs in a much more appropriate and precise manner than would the company's proposed net-salvage ratios; moreover, it eliminates the

unfairness of charging present ratepayers a substantial dollar cost that the company will not incur until many years from now.

The Attorney General's proposed cost-of-removal allowances are listed on Exhibit I-25. The Attorney General's Exhibit I-26 converts those cost-of-removal allowances into net-salvage ratios to be used in a traditional depreciation expense calculation, if the Commission chooses to continue that approach rather than adopt the Attorney General's preferred approach. The exhibits substantially reduce the net-salvage amount to be recovered by Consumers; the Attorney General's Exhibit I-25 creates an annual net-salvage recovery of approximately \$8 million, with a corresponding approximate \$52 million reduction in Consumers' annual depreciation expense level.

In ABATE's view, net salvage should be excluded from the development of Consumers' depreciation rates. ABATE proposes to include net salvage associated with ongoing retirements as a separate operating expense when calculating Consumers' revenue requirement. This new operating expense category would be based on Consumers' current levels of net salvage for its various classes of gas utility plant; ABATE recommends a five-year average of actual net-salvage experience. The net-salvage operating expense amount would then be added to the accumulated depreciation reserve and any negative net-salvage cost incurred would reduce that reserve. In effect, all depreciation expense – except the net-salvage value – would be treated as it has in the past; net-salvage value would be removed from the normal depreciation expense and then incorporated as a separate operating expense. ABATE removes all net-salvage expense from Consumers' depreciation rates and replaces it with an operating expense increase of \$8.17 million – which causes a decrease of over \$50 million in Consumers' annual depreciation expense.

If the Commission determines to continue present practice and include net salvage within the calculation of depreciation rates, ABATE argues that the Commission should use Consumers'

recent actual experience rather than the company's proposed ten-year average or forecasted costs. ABATE states that the net-salvage component of Consumers' proposed depreciation rates produces an annual net-salvage cost of \$58.4 million, while Consumers' average annual net-salvage expense over the last five years has been approximately \$8.2 million. In ABATE's view, the company's depreciation rates contain a cost seven magnitudes above Consumers' present actual experience.

The Staff believes that the methodologies employed by ABATE and by the Attorney General to address salvage values are essentially the same. In the Staff's view, either approach results in the recovery of approximately the same amount for negative net-salvage costs, only the form of the cost recovery differs—ABATE's approach recovers negative net-salvage costs as a line-item adjustment in the company's rate case, whereas the Attorney General's approach continues to collect the negative net-salvage costs as a separate component of depreciation expense. Thus, the Staff argues, either ABATE's approach or the Attorney General's approach would negate the intergenerational principle. The Staff favors its approach, using a five-year average of net-salvage costs. This is a single net-salvage ratio that is derived from all of the actual net removal costs incurred by the company during the past five years compared to the original cost of all of the gas utility plant retired during that same five-year period. The Staff notes that Consumers' negative net-salvage values are substantially in excess of those utilized for other Commission-jurisdictional natural gas utilities. The Staff requests that Consumers undertake a study of its net-salvage values and how those values differ from other Michigan natural gas utilities.

Consumers argues that its depreciation study uses the present Commission-authorized format and procedures for calculating net-salvage values. While the negative net-salvage values may appear high in relation to other Michigan regulated natural gas utilities, those net-salvage values

represent a reasonable and appropriate approximation of the future costs that the company will incur to retire or to remove its assets. In Consumers' view, the company's approach recovers any cost relating to negative net-salvage amounts over the useful life of the asset; consequently, those customers that benefit from an asset will bear the expense of that asset. The company argues that to change to a method that recovers only present expenses shifts large amounts of removal cost forward to future customers—customers that have never benefited from an asset, but will bear its removal cost. In the company's view, any alteration in the presently approved method of the recovery of net-salvage value must be thoroughly explored and reviewed prior to its implementation. Consumers' proposed depreciation rates result in an annual depreciation expense of \$101 million, which is approximately \$7 million less than that produced using the depreciation rates approved within Consumers' last depreciation case.

Consumers states that it based the company's net-salvage values on a study of its actual annual salvage and cost of removal for the ten-year period of 1993 through 2002. Consumers notes that the Staff proposes to establish the cost of removal using a five-year average of actual annual salvage and cost of removal. The company argues that the Staff's more simplified, company-wide average does not examine the disparities that may exist within and between functional classes of gas utility plant; that simplified average can mask items such as an unusual \$11 million retirement of risers within the services account during 2000. Moreover, the company states, the Staff's proposal ignores adjustments that are necessary to include appropriate projections for the costs of removal of storage well construction and related equipment. If a five-year average is used, Consumers argues that a five-year average of net salvage by functional class of gas utility plant should be used. In that event, Consumers' proposed depreciation rates produce an annual

depreciation expense of \$86.1 million, an approximate \$21 million reduction in annual depreciation expense from the rates authorized within Consumers' last depreciation case.

Consumers states that what ABATE and the Attorney General actually propose for net-salvage cost is to substitute a present-expense approach in place of a depreciation approach. Consumers argues that this is a significant change from the traditional methodology used to compute depreciation rates and that the approach is not based on depreciation theory. In Consumers' view, the change will shift costs that should be borne by current customers to later customers.

Consumers argues that the ABATE proposal and the Attorney General proposal each use today's salvage and removal cost, not the cost to be expected when the actual depreciated asset is removed from service. Accordingly, Consumers reasons that present rates will not include appropriate costs for the removal of assets that are used to provide today's service; rather, future ratepayers will bear whatever costs are necessary to retire those assets, and this is contrary to asset depreciation theory.

Consumers argues that the Attorney General's approach requires extensive review of data in the record of this proceeding to determine how that data was split, adjusted, and then recombined to establish the Attorney General's recommended net-salvage values. In the company's view, the Attorney General's proposal ignores historical relationships of utility plant and net-salvage experience, is cumbersome to compute, and has not been utilized by Michigan utilities before.

Consumers argues that a change to a present-expense method to recover net-salvage costs is inconsistent with fundamental principles of depreciation theory.

Consumers also notes that neither FAS No. 143 nor FERC Order No. 631 require the company to adopt a present-expense approach to net-salvage costs. Initially, Consumers states that Order No. 631 is not applicable to the company because the FERC does not have accounting jurisdiction over Consumers—it is a Commission-jurisdictional entity. Moreover, the company states, while

Order No. 631 requires that FERC-jurisdictional entities maintain various subsidiary accounting records, the FERC did not change the fundamental accounting procedure for cost of removal within depreciation rates and expense. The company notes that FAS No. 143 is a financial reporting requirement that deals with the identification, measurement, and recording of legal liabilities and offsetting costs associated with asset retirement. In the company's view, FAS No. 143 is a financial reporting requirement not a regulatory/ratemaking requirement, and in many instances these forms of accounting differ; the Commission is not obligated to adhere to these financial reporting requirements for ratemaking purposes.

Appropriate Net-Salvage Ratios

The positions presented by the parties vary widely in the amount of annual depreciation expense produced by the proposed rates—the differences are caused by the methods of calculation and recovery of net-salvage values. Consumers would continue the traditional approach to calculating and recovering net salvage; that approach maintains the *status quo* but does not address the singular issue raised by the remaining parties regarding the absolute size of the negative net-salvage values proposed by Consumers and the formidable present net-salvage level within the company's books. The Staff's position reduces net-salvage values through the use of a five-year rather than a ten-year average of recent experience, but (as pointed out by Consumers) does so through use of a simplified company-wide average rather than on a functional plant group basis. Such an approach can mask anomalies that may exist within specific classes of gas utility plant. ABATE advocates utilization of a completely revised approach—net-salvage cost would become an expense item separate from depreciation and collected as such in Consumers' rates. The Attorney General would also separate net salvage from depreciation, but would recover that cost through depreciation expense, albeit with a similar current-cost result as ABATE. This

“separation” concept has not been adopted in Michigan before, although other state commissions have considered it.

The gulf between the positions of the various parties is approximately \$50 million in the amount of annual depreciation expense that is appropriate for recovery, or approximately one-half of the amount that the Commission has previously found appropriate as a depreciation expense for Consumers. The effect of such a considerable shift in cost recovery on both customer rates and quality of service could similarly be large, and it should not be undertaken lightly. The Commission is persuaded that the abrupt shift in the method and the manner of cost of removal recovery as proposed either by ABATE or the Attorney General is ill-advised at this juncture without further industry-wide comment, discussion, and review. The Commission provides for this in a companion order issued today in Case No. U-14292.

The Commission is equally not persuaded that a shift to a simplified five-year company-wide average as proposed by the Staff should be implemented. However, the Commission is concerned that the large negative net-salvage values that result from Consumers’ analysis of ten years of data (or the projected costs for storage wells and related matters) do not provide an accurate illustration of the costs that Consumers will bear to retire its assets in the future. The large variance between Consumers’ incurred removal costs and its projected costs has been amply pointed out by the Attorney General and by ABATE. Thus, Consumers’ proffered rates will not alleviate this concern of the remaining parties.

Consumers’ existing depreciation rates (and the concomitant net-salvage values, retirement dispersion curves, and the ALG procedure, remaining life technique) were found just and reasonable in the Commission’s final order in Case No. U-11509; under MCL 462.25 these existing rates are *prima facie* lawful and reasonable until changed or modified by the Commission.

Accordingly, the Commission finds that the existing depreciation rates established in Consumers' last depreciation case, Case No. U-11509, should continue.³ After the generic proceeding discussed later in the order, the Commission will be in a better position to consider revised depreciation rates and to accommodate any changes in ratemaking that any revised depreciation rates or practices may engender. Additionally, the Commission also will have available the Staff's proposed review of Consumers' substantial negative net-salvage values, as provided for below. Such additional information can only serve to assist the Commission in its review of this important issue.

Order No. 631, FAS No. 143, and Commission-jurisdictional Natural Gas and Electric Entities

The Staff notes that while through Order No. 631 the FERC approved an accounting methodology for FAS No. 143 purposes, it also indicated that ratemaking issues related to FAS No. 143 would be treated by the FERC in future rate cases before that agency. Thus, the FERC's final position regarding appropriate ratemaking to deal with the effect of FAS No. 143 is uncertain. In the Staff's view, the procedures proposed by ABATE, and to a lesser extent the Attorney General, represent a strict interpretation of FAS No. 143 by expensing costs of removal as those costs occur. For these reasons, the Staff advocates a generic proceeding for both electric and natural gas Commission-jurisdictional entities that would review the issues of the ratemaking effect of FAS No. 143 and the appropriate accounting for the effects of FAS No. 143. In its replies to exceptions, Consumers notes that these issues are of industry-wide concern. Consumers argues that if a generic proceeding is initiated, then all Commission-jurisdictional electric and natural gas utilities should be involved.

³This concludes Consumers' present voluntary reduction in its depreciation rates, in which the Commission acquiesced by its December 18, 2003 order in Case No. U-13730.

The Commission is persuaded that such a generic proceeding should be instituted. The procedures proposed by ABATE and by the Attorney General, which would separate cost of removal to permit that item to be more extensively reviewed and recovered in a different manner, while inappropriate for immediate implementation, should be thoroughly reviewed and subjected to comment from all of the involved parties. Moreover, although FERC Order No. 631 is not applicable to Commission-jurisdictional services and FAS No. 143 is a financial (not regulatory) reporting requirement, the procedures, concepts, research, and experience under these accounting pronouncements can assist the Commission in its review of these issues. Accordingly, the Commission will commence by its companion order issued today a generic review of the possible ratemaking effect of FAS No. 143, the appropriate accounting for the effects of FAS No. 143, and matters related to those issues.

Study of Negative Net-Salvage Cost Recovery

ABATE and the Attorney General presented testimony regarding the large negative net-salvage amounts contained within Consumers' depreciation rates. The parties to this proceeding also presented testimony regarding the vastly different negative net-salvage levels between Consumers and the remaining natural gas utilities regulated by the Commission. The Staff proposed that Consumers conduct a study to determine why the company's negative net-salvage costs are substantially in excess of those of other regulated Michigan natural gas utilities. The ALJ recommended that Consumers conduct that study. Consumers excepts, arguing that much of the comparison data is maintained by other utilities and that each company's asset inventory and service territories are so substantially different that any comparison will not be meaningful. Consumers states that it would work informally with the Staff to review its net-salvage costs.

The testimony presented demonstrates that the level of negative net salvage proposed by Consumers is substantially in excess of that of other Commission-regulated natural gas utilities. Granted that each company's assets and service territories vary, but the construction-related cost of removal for pipe, meters, and risers should bear some relation to cost-of-construction rates within a given geographic area. Moreover, the existence of such a large variance within Michigan natural gas utility companies requires a prudent management to investigate and to review all available information to determine if that variance is appropriate for a particular company. For these reasons, the Commission directs Consumers to undertake the study as proposed by the Staff. The Commission also directs the Staff to assist Consumers in its dealings with other Michigan natural gas utilities to ensure that the appropriate data is provided to Consumers such that the study's results are meaningful and accurate. The company shall file its report with the Staff on or before December 31, 2005.

Deferred Accounting for FAS No. 143

Consumers requested authority to establish deferred accounting for timing differences that could result from implementation of FAS No. 143. Consumers has requested authority for two specific items: (1) the commitment to remove inside gas meters, regulators, and risers pursuant to Case No. U-13156, and (2) the commitment to the Michigan Department of Environmental Quality to seal wells at the company's to-be-abandoned Northville Trenton storage field. The Attorney General opposes that authorization inasmuch as the company has not presented exactly what amounts will be deferred. No other party opposed the request. This issue is also being reviewed within Consumers' rate case, Case No. U-13730. While the Commission understands the Attorney General's desire to see the precise amounts that will be deferred, the Commission believes that it is sufficient to authorize the deferred accounting treatment for these two known

items. An eventual audit will determine whether the entries were appropriate, as occurs with all of the company's other accounts. The Commission finds that Consumers should be authorized to utilize deferred accounting for the two items requested.

Consumers noted that the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants had issued a statement of position (SOP) regarding accounting for certain costs and activities related to property, plant, and equipment. That SOP would require component depreciation for each asset and expensing of the cost of removal as incurred. Consumers noted that if the Financial Accounting Standards Board (FASB) approved the SOP, then the company would need to set up regulatory assets and regulatory liabilities to account for any timing differences that occurred; the company requested authority to do so. The Attorney General notes that the SOP has not been adopted by the FASB and that Consumers has not explained what accounts would be established and what would be placed into those accounts. Unlike FAS No. 143, the SOP has not been adopted by the FASB and the timing differences that may occur have not been fully explored. Consumers recognizes that any grant of accounting authority would need to be conditioned on approval of the SOP, and that any such grant would be unnecessary if the FASB does not approve the SOP.

The Commission is not persuaded that contingent accounting authorization should be granted for proposals that may not be adopted by the FASB. After the FASB has acted on the SOP proposal, Consumers should request any necessary authority, not before.

Next Depreciation Filing

Consumers proposes that an application for new depreciation accrual rates for natural gas utility plant be filed not later than October 1, 2010, with a depreciation study using natural gas utility plant balances as of December 31, 2009. The Attorney General prefers an earlier date,

September 1, 2007. He prefers that date because possible changes in depreciation accounting and related regulations may warrant a filing earlier than 2010. The Staff favors the later date proposed by Consumers.

Because the Commission has continued Consumers' prior depreciation rates, the filing dates proposed by the parties are inapplicable. Recently, the Commission has attempted to coordinate the revision of depreciation rates with the establishment of general rates, which allows the depreciation rates to be synchronized with those general rates. The parties to this proceeding requested similar treatment. Accordingly, Consumers shall file an application for new depreciation accrual rates for its natural gas utility plant on, or no earlier than a date three months prior to, the date that the company files its next natural gas general rate case; the company shall use its natural gas utility plant balances as of December 31 of the calendar year immediately preceding the filing date. If a different date becomes appropriate because of the Commission's generic proceeding in Case No. U-14292, then the Commission may direct another filing date.

Additionally, Consumers requested approval of page 2 of its Exhibit A-4, Administration of Depreciation, which provides directives for the calculation of annual depreciation expense, the handling of fully accrued accounts, the date for the next depreciation study, and other similar matters. The parties did not object to this administration procedure (other than the date), and the Commission finds that the procedure should be authorized, as revised for the differing filing date of the next depreciation study.

Synchronization with rates

All parties to this proceeding agreed that any revision of the company's depreciation rates adopted in this proceeding would be synchronized with Consumers' retail rates for natural gas utility service within Consumers' present rate case, Case No. U-13730. Because this order

continues the existing depreciation rates authorized by Case No. U-11509, action within Case No. U-13730 is not necessary.

The Commission FINDS that:

- a. Jurisdiction is pursuant to 1909 PA 300, as amended, MCL 462.2 et seq.; 1919 PA 419, as amended, MCL 460.51 et seq.; 1939 PA 3, as amended, MCL 460.1 et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1999 AC, R 460.17101 et seq.
- b. Consumers should continue the depreciation rates authorized by the December 7, 1998 order in Case No. U-11509.
- c. Consumers should undertake the study of the company's net-salvage values as proposed by the Staff. The company should file its report with the Staff on or before December 31, 2005.
- d. The deferred accounting requested for the Case No. U-13156 removals and the Northville Trenton storage field well closures should be authorized.
- e. Consumers' proposed administration of depreciation, Exhibit A-4, page 2, should be authorized as revised by this order. Consumers shall file an application for new depreciation accrual rates for its natural gas utility plant on, or no earlier than a date three months prior to, the date that the company files its next natural gas general rate case; Consumers shall use its natural gas utility plant balances as of December 31 of the calendar year immediately preceding the filing date.

THEREFORE, IT IS ORDERED that:

A. Consumers Energy Company shall continue the depreciation rates authorized by the December 7, 1998 order in Case No. U-11509.

B. Consumers Energy Company shall undertake the study of net-salvage values as proposed by the Commission Staff and shall file its report with the Commission Staff on or before December 31, 2005.

C. The deferred accounting treatment requested by Consumers Energy Company for removals related to Case No. U-13156 and the Northville Trenton storage filed well closures is authorized.

D. Consumers Energy Company's proposed administration of depreciation, Exhibit A-4, page 2, is authorized as revised by this order. Consumers Energy Company shall file an application for new depreciation accrual rates for its natural gas utility plant on, or no earlier than a date three months prior to, the date that Consumers Energy Company files its next natural gas general rate case. Consumers Energy Company shall use its natural gas utility plant balances as of December 31 of the calendar year immediately preceding the filing date.

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

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

MICHIGAN PUBLIC SERVICE COMMISSION

(S E A L)

/s/ J. Peter Lark
Chair

By its action of October 14, 2004.

/s/ Robert B. Nelson
Commissioner

/s/ Mary Jo Kunkle
Its Executive Secretary

/s/ Laura Chappelle
Commissioner

B. Consumers Energy Company shall undertake the study of net-salvage values as proposed by the Commission Staff and shall file its report with the Commission Staff on or before December 31, 2005.

C. The deferred accounting treatment requested by Consumers Energy Company for removals related to Case No. U-13156 and the Northville Trenton storage filed well closures is authorized.

D. Consumers Energy Company's proposed administration of depreciation, Exhibit A-4, page 2, is authorized as revised by this order. Consumers Energy Company shall file an application for new depreciation accrual rates for its natural gas utility plant on, or no earlier than a date three months prior to, the date that Consumers Energy Company files its next natural gas general rate case. Consumers Energy Company shall use its natural gas utility plant balances as of December 31 of the calendar year immediately preceding the filing date.

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

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

MICHIGAN PUBLIC SERVICE COMMISSION

Chair

By its action of October 14, 2004.

Commissioner

Its Executive Secretary

Commissioner

P R O O F O F S E R V I C E

STATE OF MICHIGAN)

Case No. U-12999

County of Ingham)

Patricia A. Fronta being duly sworn, deposes and says that on October 14th 2004, A.D. she served a copy of the attached Commission orders by first class mail, postage prepaid, or by inter-departmental mail, to the persons as shown on the attached service list.

Patricia Fronta

Subscribed and sworn to before me
this 14th day of October 2004

Notary Public, Eaton County, Michigan
Acting in Ingham County
My Commission expires November 22, 2004

SERVICE LIST FOR DOCKET # U - 12999-
DATE OF PREPARATION: 10/19/2004

CASE #

MR. THOMAS MCNISH
CONSUMERS ENERGY COMPANY
212 W. MICHIGAN AVENUE
JACKSON MI 49201

MR. DONALD E. ERICKSON
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6545 MERCANTILE WAY, 2ND FLOOR
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MR. ROBERT A. STRONG
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ONE ENERGY PLAZA
JACKSON MI 49201

MR. DANIEL E. NICKERSON, JR.
PSC ALJ DIVISION
6545 MERCANTILE WAY
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ALL GAS ORDERS

MS. LISA DONFRIED
MICHIGAN CONSOLIDATED GAS COMPANY
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MS. MONICA MARTINEZ
SENATE DEMOCRATIC STAFF
ROMNEY BUILDING
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ID MAIL

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