

July 20, 2007

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Via E-Docket

Mary Jo Kunkle
Executive Secretary
Michigan Public Service Commission
6545 Mercantile Way
Lansing, MI 48911

**Re: In the matter of the application of Consumers Energy Company for authority to increase its rates for the distribution of natural gas and for other relief.
MPSC Case No. U-15190**

Dear Ms. Kunkle:

Enclosed for filing in the above-referenced case is the *Direct Testimony of Timothy Ray on Behalf of National Energy Marketers Association* and *Proof of Service*.

If you should have any questions, please contact me.

Very truly yours,

Jennifer L. Frye

JLF:jkt
Enclosure

LANSING 34563-1 388833v3

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for authority to increase its rates for the)
distribution of natural gas and for other relief)
_____)

Case No. U-15190

DIRECT TESTIMONY OF

TIMOTHY RAY

ON BEHALF OF THE NATIONAL ENERGY MARKETERS ASSOCIATION

DATED: July 20, 2007

1 **Q1. Please state your name, business title and business address.**

2 A1. My name is Timothy Ray, and I am the Vice President of Energy Management for Direct
3 Energy Services, LLC, a licensed competitive retail natural gas and electricity supplier in
4 Michigan and 7 other states serving residential, commercial and industrial customers.
5 My business address is: 12 Greenway Plaza, Houston, Texas.

6
7 **Q2. On whose behalf are you offering direct testimony?**

8 A2. I am testifying on behalf of the National Energy Marketers Association ("NEM"). Direct
9 Energy is a member of NEM's Executive Committee. NEM is a national, non-profit
10 trade association representing wholesale and retail marketers of natural gas, electricity, as
11 well as energy and financial related products, services, information and advanced
12 technologies throughout the United States, Canada and the European Union. NEM's
13 membership includes independent power producers, suppliers of distributed generation,
14 energy brokers, power traders, electronic trading exchanges and price reporting services,
15 advanced metering, demand side management and load management firms, billing, back
16 office, customer service and related information technology providers. NEM members
17 also include retail energy consumers as well as inventors, patent holders, systems
18 integrators, and developers of solar thin film building integrated Photovoltaics, fuel cells,
19 and advanced Broadband over Power Line (BPL), Power Line Communications (PLC)
20 technologies as well as Smart Electricity.TM

21

1 **Q3. Would you please summarize your education and energy industry work experience?**

2 A3. I graduated from West Virginia University with a Bachelor of Science degree in Business
3 Administration with a major in Accounting. I have worked in the natural gas industry my
4 entire career, starting in 1985 as an accountant and Supervisor of Natural Gas Accounting
5 for Columbus Gas Transmission Corp., an interstate pipeline company. I passed the
6 Certified Public Accountancy Examination in West Virginia in 1989 while employed
7 with Columbia Gas. In 1990, I joined Access Energy, the largest independent marketer
8 of natural gas in the United States at the time, as Manager of Natural Gas Analysis and
9 Manager of Financial Accounting. When Enron Corporation acquired Access and I
10 moved into energy supply management as Manager of Gas Supply for the western United
11 States and in 1998 was promoted to Director of Gas Supply Management where I
12 managed US retail supply operations behind 100 different local distribution companies.
13 Prior to joining Direct Energy in 2002, I was the Vice President of the Energy
14 Management Group for New Power, responsible for both national power and gas
15 operations. Currently, I am the Vice President of Energy Management, responsible for
16 gas supply for all markets served within the continental United States.

17

18 **Q4. What is the purpose of your testimony?**

19 A4. The purpose of my testimony is to urge the parties and the Commission to adopt
20 amendments to Consumers' Gas Customer Choice ("Choice") tariff aimed at improving
21 the program and mitigating the negative impact of the current reconciliation process to
22 customers and suppliers that participate in the gas Choice program. NEM raised these

1 issues in Consumers Energy's previous rate case, Case No. U-14547 and proposed the
2 concept of reconciling price pools in the aggregate instead of each pool individually. At
3 that time, NEM presented tariff language to enact the concept which could have been
4 more fully developed with the input of all stakeholders upon approval. The Michigan
5 Public Service Commission ("Commission") declined to accept the proposal at that time
6 but invited NEM to provide a more detailed proposal in a subsequent case. Accordingly,
7 in conformance with the Commission's Order in U-14547, I will be presenting a multi-
8 faceted proposal to improve the Consumers Gas Customer Choice program by (1)
9 reconciling all pools collectively instead of individually, (2) reducing annual
10 overdeliveries by scheduling deliveries to normal, instead of colder-than-normal, weather
11 with the flexibility to adjust to actual conditions to ensuring system reliability, (3)
12 replacing the current annual volumetric true-up matrix mechanism with a uniform,
13 market-based cash-out mechanism that will provide for a more equitable result, and (4)
14 provide an opportunity for participating suppliers to trade off-setting imbalances among
15 themselves prior to the cash-out. I believe that with these fairly simple but fundamental
16 changes the overall program will be enhanced by treating GCR and Choice customers in
17 a more equitable manner while protecting the integrity of the utility system. Individual
18 elements of the proposal, particularly moving to an aggregated reconciliation rather than
19 pool-by-pool, will be an improvement to the program. However, NEM urges adoption of
20 all elements of the proposal because the positive impact will be significantly greater
21 collectively than is possible individually.

1 **Q5. Are you familiar with Consumers Customer Choice Program?**

2 A5. Yes, I have been managing gas supplies to customers in Consumers Energy and
3 MichCon's service territories for approximately 9 years on behalf of 3 companies. I am
4 currently responsible for all gas supply management provided by Direct Energy to
5 customers in Consumers' program so I'm familiar with the rules and how their
6 implementation affects the price and types of offers suppliers can make to customers.

7

8 **Q6. Can you describe generally how Consumers' program works?**

9 A6. It is a "buy/sell" program with the utility serving as program administrator between the
10 customer and the supplier. Suppliers deliver a relatively flat volume of gas each month
11 of the year to the utility as the graph in Exhibit TR-1 (____) depicts. The utility
12 continues to perform its monopoly function of delivering gas to customers as it is
13 consumed. The difference between volumes of gas consumed by Choice customers and
14 what the supplier delivered to the system is either injected or withdrawn from storage
15 seasonally to variations in customer demand. The utility pays the supplier monthly for
16 volumes delivered but caps the price paid at 110% of the GCR. It is the utility alone that
17 directs the daily deliveries by suppliers to its city gate established on a monthly basis and
18 plans the deliveries to colder-than-normal weather forecasts.

19

20 The utility bills the customer for consumption at the rate established between the
21 customer and the supplier and continues to perform collection activities and processing of
22 bad debt as it has always done. Each supplier has a set number of rate codes available

1 and each rate code or price point represents a “pool” of customers who are paying that
2 rate. After the close of the program year, March 31, the utility reconciles the volumetric
3 differences between what was delivered and what was consumed and the financial
4 differences which include any amounts over the 110% of GCR cap and the average rate
5 billed to customers against the average delivered rate paid to the supplier. The
6 reconciliation is typically completed several months after the program year close. Details
7 of the reconciliation process are described later in this testimony.

8
9 **Q7. Do the volumes of gas delivered match the volumes consumed?**

10 A7. No, it is virtually impossible to predict with precision how much customers will consume
11 in a given year, or for that matter on a daily or monthly basis (since daily metering is not
12 available for residential customers). Per program rules, Consumers provides each
13 Supplier with a monthly schedule of quantities for delivery of gas into the Company’s
14 system on behalf of the Supplier’s customers. The initial schedule will indicate quantities
15 that the Supplier is required to deliver each day under each Supplier-designated pricing
16 category (as such term is defined in the tariff). The tariff states that daily deliveries will
17 not normally vary by more than +(-) 10% from 1/365th of the estimated annual customer
18 load to be served by the Supplier. The additional flexibility is permitted in the tariff
19 because of the realization that due to changes in pool composition over the year, weather,
20 changes in consumption patterns and a variety of other items, customer actual
21 consumption will vary from anticipated customer consumption. To mitigate the
22 differences between anticipated use and actual usage due to these factors, the additional

1 flexibility is permitted in the tariff so that adjustments can be made from time to time so
2 as to realign as much as possible delivered volumes with actual consumption.

3
4 **Q8. How do the variances between the delivered and consumed volumes get reconciled**
5 **under the current program?**

6 A8. The reconciliation rules essentially fit into four different categories as shown in Exhibit
7 TR-2 (_____) depending on whether the supplier is under or over delivered and whether
8 the suppliers' average sales price to its customers is more or less than the weighted
9 average GCR rate for the year. Paragraph M of Consumers' Tariff Second Revised Sheet
10 No. H-3.00 states, in pertinent part:

11 In those instances where both (i) the price per Mcf billed to customers
12 over the course of the program year on Supplier's behalf is higher than the
13 cost of gas billed to sales customer by the Company pursuant to the
14 Company's Rule B10, and (ii) the MMBtu delivered by the supplier
15 converted to the Mcf exceeds the billed customer consumption for the year
16 being reconciled, then the following procedure will be used. In such
17 instances (i) within 60 working days after the end of the March billing
18 cycle, * * * the Company will reconcile the amount billed to customers on
19 the Supplier's behalf with the Company's remittance to the Supplier for
20 the gas delivered, and any difference will be reflected in an adjustment on
21 the next monthly remittance to the Supplier, and (ii) gas delivered by the
22 Supplier in excess of the actual consumption will be returned to the
23 Supplier in kind unless the Company and the Supplier mutually agree on a
24 price for the Company to purchase the excess gas.

25
26 * * *

27 (Q) The * * * annual reconciliation shall apply separately to each
28 Supplier-designated pricing category and each of the two customer groups
29 within that category, i.e. those enrolled as of April 1, and those enrolled
30 after April 1 each program year.

31
32 In essence, the way the process works is that if excess gas was delivered by a supplier
33 and the supplier's pool contract price with its customers was less than Consumers'

1 weighted GCR, *i.e.* at a price less than that charged by the utility throughout the program
2 year, then the utility is going to keep the excess gas at the supplier's lower price. If the
3 supplier's pool contract price with its customers is higher than the price of the GCR, that
4 gas is returned to the supplier in the summer after the reconciliation has been performed
5 unless the utility and supplier agree otherwise.

6
7 On the other hand, if the amount of a supplier's deliveries to a single pool of customers is
8 less than the actual consumption of those customers, then the utility will do one of two
9 things depending on the price charged to the customer (keeping in mind that the utility
10 has complete control over the supplier's delivery requirements). If the supplier's average
11 price is higher than the GCR price, the utility will provide the needed gas and retain the
12 supplier's revenues at the higher amount. If the sales price was less than the GCR, the
13 utility will provide the needed gas and collect the difference from the supplier in the form
14 of a Supplier Equalization Charge ("SEC") to make the utility whole. The SEC is applied
15 to all B category customer pools ("B pools") that used more gas than was delivered by
16 the supplier.

17
18 There are two different types of pools managed by Consumers called "A" and "B" pools.
19 A pools are customers that were in the rate code at the start of the program year (April 1).
20 B pool are customers that are added to the pool after the start of the program year. This
21 distinction is important because only in A pools where the suppliers' contract price with
22 the customer is lower than the GCR and the pool is under-delivered are the rules not

1 favorable to the utility. However, the utility directs the gas deliveries of all the marketer
2 pools and as a matter of practice targets volume deliveries in excess of each pool's
3 expected weather normal usage. Therefore, there is a remote chance that this outcome
4 would ever come to fruition.

5
6 Because of the language in Section Q of the tariff, Consumers is compelled to look at
7 each pool individually to determine whether gas will be returned or retained – instead of
8 first looking at all the gas that has been delivered by a competitive natural gas provider to
9 the utility system to see whether the gas delivered by the supplier, in aggregate, met,
10 exceeded or fell short of the its customers' annual consumption. In fact, it is possible for
11 a utility to take multiple actions with regard to one single supplier during the annual
12 reconciliation; that is, keeping lower cost gas, returning higher cost gas, selling gas to and
13 retaining revenues from sales to customers with rates exceeding its weighted average cost
14 of gas ("WACOG"), even if the aggregate gas physically delivered into the utility system
15 balances to all customer requirements. Further, even deliveries that are made to
16 Consumers for existing customers may not be credited to the customer at time of
17 reconciliation, if the customers are moved from one pool to another, which can create a
18 long position in the initial pool and a short position in the later pool, simply because the
19 customers pool has changed.

20

1 **Q9. What is the result of the current reconciliation process?**

2 A9. It essentially results in a “heads I win, tails you lose” scenario in favor of the utility. As
3 stated above, each price point or “pool” is reconciled individually without regard to
4 imbalances in other pools. There is only one of four outcomes within the process that
5 could result in an unfavorable outcome for the utility and it is entirely within its control to
6 mitigate. Suppliers are subject to the utilities’ forecasting and delivery decisions in a
7 program that results in a literally all of the price risk being borne by them and their
8 customers. In contrast, the utility experiences a neutral to positive outcome in all but one
9 scenario. Moreover, due to the limitations of the flat delivery profile approach, the
10 ultimate treatment of the annual imbalance has no connection to the actual time period
11 when it occurred.

12
13 Further, because the forecasting is done using a scenario of colder than normal weather,
14 which occurs throughout the summer injection season, “A” pools are almost guaranteed
15 to be overdelivered. The result of overdeliveries, as described above, is either lower than
16 GCR cost gas retained by the utility for GCR customers, effectively reducing the cost of
17 the GCR to the detriment of Choice, or higher than GCR cost gas returned to the supplier
18 in the summer months when the cost of gas is often at its lowest, also a potential
19 detriment to Choice because there is great risk for a loss on gas sold into the market.

20
21 More importantly, a marketer could theoretically have two or more pools with offsetting
22 imbalances leaving a net zero imbalance on the utility system, yet the current

1 reconciliation rules could result in a punitive result in both pools. The uncertainty and
2 detrimental rules for reconciliation create significant risk and adversely affect the types of
3 products and pricing suppliers can offer to customers and can impact the ability of
4 suppliers to make offers throughout the year.

5
6 **Q10. How does Consumers Energy's program compare to those in other states where you**
7 **manage gas?**

8 A10. Consumers program has limitations. The flat deliveries each month skew the market
9 realities and adjustments throughout the year that hinder the development of the retail
10 market because favorable developments cannot be capitalized on. Though the
11 amendments I'm suggesting in this testimony would greatly improve the program, there
12 are elements of programs in other states that put suppliers on a much more level playing
13 field with the utility such as; equal access to transportation and storage assets,
14 management of daily supply requirements, market-based utility rates and monthly,
15 market-based cash out mechanisms. I would like to see Consumers move to a more
16 mature market structure that contains some or all of these elements but recognize such
17 changes would require a complete restructuring of the program. Therefore, at this time I
18 urge adoption of the specific changes contained in this testimony, which are not drastic
19 but have a significantly positive impact for Choice customers and the program generally,
20 without negatively impacting the GCR.

21

1 **Q11. How can the problems enumerated above be remedied?**

2 A11. There are four fairly simple changes that would result in great improvement to the
3 program. They are (1) implement an aggregate reconciliation so that all pools are
4 considered together to capture the physical realities of gas delivered to the utility system,
5 (2) change utility forecasts to plan to normal weather instead of colder-than-normal
6 weather, (3) add a time-related market-based component to the cash-out mechanism to
7 capture actual costs at the time they occur, and (4) provide the opportunity for suppliers
8 to trade offsetting imbalances between themselves prior to cash-out. The aggregate
9 reconciliation is the main element but the others are imperative to a truly balanced
10 program.

11

12 **Q12. Can you explain how your aggregate reconciliation proposal works?**

13 A12. Generally, the aggregate reconciliation allows the utility to look at all gas delivered by a
14 supplier during the program year (April 1 – March 31) as a single pool for the purposes
15 of determining the imbalance between deliveries and the amount of gas consumed by its
16 customers. The aggregate reconciliation proposal itself does not in any way change the
17 way utilities calculate delivery requirements or suppliers' duty to comply with those
18 delivery requirements, nor do the rules for how imbalances are settled change. However,
19 it may have the additional benefit of reducing the likelihood that the utility will require
20 over or under deliveries in a specific pool based upon how that pool price compares to the
21 GCR or market price of gas. Instead of each different price point being reconciled
22 individually, the average weighted price of all of a supplier's pools is used to determine

1 which of the four broad reconciliation rules (see Exhibit TR-2 (____)) will be applied to
2 the single imbalance. Adoption of the aggregate reconciliation proposal would eliminate
3 the need for A and B pool distinctions as part of the reconciliation process as well though
4 they would continue to be applied to the other aspects of the program as they do today.

5
6 The aggregate reconciliation proposal alone, without consideration of the other aspects of
7 my proposal which are explained in more detail below, can be achieved with only minor
8 revisions to Consumers' tariff Section H1.Q. as follows:

9 The annual load requirements, delivery schedules, ~~Supply Equalization Charges,~~
10 **and** delivery shortfall Failure Fees, ~~and annual reconciliation~~ shall apply
11 separately to each Supplier-designated pricing category. **The annual load**
12 **requirements, delivery schedules, and delivery shortfall Failure Fees shall**
13 **also apply separately to,** ~~and~~ each of the two customer groups within that
14 category, i.e. those enrolled as of April 1, and those enrolled after April 1 in each
15 program year.

16
17 Exhibit TR-3 (____) provides detailed examples of the aggregate reconciliation proposal
18 in each type of imbalance scenario. I will explain each of them under both the current
19 reconciliation process and under the proposed aggregate reconciliation process to
20 highlight the differences. For the sake of simplified discussion, the assumption in the
21 examples provided is that a supplier has only 2 pools in each example. In practice,
22 suppliers typically have multiple pools and both A and B pools.

23
24 Example 1 of Exhibit TR-3 (____) is the most basic example that shows the result if a
25 supplier's under and over deliveries offset each other exactly (which would not likely
26 happen in reality) purely for illustrative purposes to explain the general concept of the

1 aggregate reconciliation. Two pools are shown; one at \$5 and another at \$6.10 with a
2 GCR price of \$6. At the end of the program year, Pool 1 was under delivered by 100
3 Mcf and Pool 2 was over delivered by 100 Mcf. Under the current reconciliation process,
4 the 100 Mcf under delivered in Pool 1 would be provided by the utility to the customer
5 and either the supplier would pay a supplier equalization charge (SEC) of \$1 per Mcf to
6 be made whole (“B” pool) or the utility would have to provide the gas at its cost (“A”
7 pool). The 100 Mcf of excess gas in pool 2 would be returned to the supplier in the
8 summer months because the price is higher than the GCR. Thus, though the full amount
9 needed to supply the choice customers was provided to the utility, the current
10 reconciliation process results in the supplier potentially having to pay \$100 ($\1×100) to
11 the utility and assume the risk of movement in the market price throughout the year by
12 having the gas returned in the summer when prices are most likely to be depressed.

13
14 Using an aggregate reconciliation, the volume differences would cancel each other out so
15 no volumetric true up would be necessary. Only a billing rate reconciliation between the
16 weighted average price paid to the supplier by the utility and the average weighted price
17 of the volume billed to customers would be necessary. Therefore, \$.366 (avg. sales price
18 v. avg. delivered price difference) is multiplied by 300 (total volume) for a total payment
19 from the supplier to the utility of \$110 but without the risk of gas returned in the summer.

20
21 Example 2 of Exhibit TR-3 (_____) depicts an over delivery when the GCR is lower than
22 the supplier rate with a \$9 GCR. There are two pools; one at \$13 and the other at \$8.50.

1 Both pools are over delivered by 100 Mcf each. Note that the supplier is only paid 110%
2 of the GCR or \$9.90 for gas delivered into Pool 1. Under the current process, the 100
3 Mcf over delivered in Pool 1 will be returned to the supplier because the price is higher
4 than the GCR. At reconciliation, the difference between the 110% cap and the rate of
5 \$13 will be settled and the supplier will be paid \$3.10 for only the 200 Mcf customers
6 used. In Pool 2, the excess 100 Mcf will be kept by the utility since the GCR is at a rate
7 \$.50 above the supplier delivered price.

8
9 Under the aggregate reconciliation process, there is a single imbalance of 200 Mcf over
10 delivered and a single price point of comparison, the supplier's average delivered sales
11 price, which is \$9.20. Therefore, both a volumetric and billing rate true up is needed.
12 The same rule applies as above for reconciliation of over deliveries at a price higher than
13 the GCR. Thus, the 200 Mcf will be returned to the supplier in the summer months. The
14 supplier will refund the utility for the 200 Mcf paid to it by the utility at the average
15 delivered sales price of \$9.20 for a total payment of \$1,840. In turn, in the billing rate
16 true up, the utility will credit the supplier for the difference in the average billed price of
17 \$10.75 less the average delivered price of \$9.20 times the 400 Mcf actually consumed by
18 the customers, or \$620 for a net payment by the supplier to the utility of \$1,220.

19
20 Example 3 of Exhibit TR-3 (_____) shows a situation where the supplier is over
21 delivered and the GCR is higher than the supplier delivered price. There are two pools;
22 one at \$11 and the other at \$7 and a GCR of \$10. Pool 1 at \$11 is over delivered by 50

1 Mcf and Pool 2 at \$7 is over delivered by 100 Mcf. Under the current process, the 50
2 Mcf of gas in Pool 1 will be returned to the supplier in the summer because it is priced
3 higher than the GCR. The 100 Mcf of excess gas in Pool 2 however will be retained by
4 the utility at \$7, \$3 below the utility gas cost.

5
6 Using the aggregate reconciliation, there is the single 150 Mcf imbalance and a single
7 price point for comparison to the GCR. In this case, the supplier's average delivered
8 price is \$8.33, lower than the \$10 GCR, so the reconciliation rules result in the over
9 delivered 150 Mcf being retained by the utility. Note, even in the aggregate
10 reconciliation, the utility still purchases gas below its GCR at the sole benefit to its
11 customers.

12
13 Example 4 of Exhibit TR-3 (_____) illustrates a situation where the supplier is under
14 delivered and the utility WACOG (the appropriate comparison in accordance with
15 Section H1.E. in the tariff) is lower than the average billed price in Pool 1 (\$13) and
16 higher than the average billed price in Pool 2 (\$8.50). Both pools are under delivered by
17 100 Mcf each and the utility WACOG is \$9. Applying the current reconciliation process,
18 the utility would provide the 100 Mcf under delivered for Pool 1 at its cost of \$9 and then
19 collect the \$13 price from the supplier's customers, a \$4 per Mcf bonus for the utility.
20 The price paid to the supplier on delivery is capped at 110% of the GCR so the marketer
21 is being paid \$9.90. In Pool 2, because the price is lower than the utility WACOG, the
22 utility will provide the additional 100 Mcf needed and either apply an SEC charge to the

1 supplier for the \$.50 difference between the supplier price and utility WACOG or, if this
2 is an “A” pool (exists at on April 1 at the start of the program year), the utility would
3 have to provide the gas at its WACOG but only collect the supplier amount from the
4 customer. As stated earlier, the delivery requirements are wholly set by the utility so
5 ample opportunity should be available to avoid such an outcome. The utility would pay
6 the difference in the average billed price of \$13 for pool 1 and the capped delivered price
7 of \$9.90 times the 200 Mcf delivered to the supplier, or \$620.

8
9 Under the aggregate reconciliation, the sales revenue on the additional 200 Mcf not
10 provided by the supplier is retained by the utility. Since the average billed price is \$1.75
11 greater than the utility WACOG, the GCR customers benefit from the incremental gas
12 consumed by choice customers. The utility remits the difference between the average
13 billed price of \$10.75 and the average delivered price of \$9.20 times the 400 Mcf
14 (volume delivered by supplier) to the supplier, or \$620.

15
16 Finally, Example 5 of Exhibit TR-3 (____) shows an under delivery scenario when the
17 utility WACOG is higher than the average billed price. Similar to the previous example,
18 one pool is at \$13 and the other at \$8.50. The only difference is the price of the utility
19 WACOG is \$11 and the average delivered price for pool 1 is subject to the 110% cap, or
20 \$12.10. Therefore, the utility will provide the 100 Mcf to each pool at its WACOG and
21 collect the average billed price from the customer. Since the average billed price of pool
22 1 exceeds the utility WACOG, the GCR customers benefit from this additional

1 consumption by transportation customers. However, since the average billed price for
2 Pool 2 is less than the utility WACOG, the utility GCR customers absorb this price risk if
3 Pool 2 is an A pool. If pool 2 is a B pool, then the utility may collect a Supplier
4 Equalization Charge on the 100 Mcf shortfall times the difference between the utility
5 WACOG and the average delivered price of \$8.50. It is again important to reiterate that
6 this outcome is remote for an A pool as the utility has full control over the volume
7 delivered to its citygate.

8
9 In contrast, under the aggregate reconciliation, the sales revenue on the additional 200
10 Mcf not provided by the supplier is retained by the utility. Since the average billed price
11 is \$.25 less than the utility WACOG, the GCR customers bear this price risk from the
12 incremental gas consumed by transportation customers. Under the aggregate
13 reconciliation, the utility may collect a Supplier Equalization Charge on the difference
14 between the average billed price and the utility WACOG regardless of the pool type. The
15 utility remits the difference between the average billed price of \$10.75 and the average
16 delivered price of \$9.20 times the 400 Mcf (volume delivered by supplier) to the supplier,
17 or \$620.

18
19 In summary, the following is a high level overview of the proposed aggregate
20 reconciliation methodology:

21 **Step 1:** Calculate the total volume consumed by the supplier's customers, in the aggregate
22 adding all volumes for all of the supplier's pools together to arrive at one number;

1 **Step 2:** Calculate the total volume delivered by the supplier, in the aggregate, adding all
2 deliveries for all of the supplier's pools to arrive at one number;

3 **Step 3:** Calculate the supplier's weighted average sales price for all sales made to its
4 customers;

5 **Step 4:** At the point where supplier's deliveries meet supplier's customers' consumption,
6 reconcile the price (because at this point the volumes will match, regardless of whether
7 there is an over or under deliver of volumes);

8 • multiply the sales by the weighted average sales price, multiply the
9 delivered volumes by the weighted average delivered price and the difference flows to
10 the party that was underpaid.

11 **Step 5:** address the over or under deliveries as compared to the sales. If in the aggregate
12 there were over deliveries, compare the over deliveries to the GCR and take appropriate
13 action. If in the aggregate there were under deliveries, compare the weighted average
14 sales price to the utilities WACOG, and take the appropriate action.

15
16 As the examples show, the current reconciliation process not only advantages the utility
17 in almost every situation, but also fails to recognize the costs associated with the
18 imbalance during the period it is incurred. The aggregate reconciliation provides a more
19 realistic and fair approach to the annual true up. The examples do not include the
20 additional suggestions below to add a market-based cash-out mechanism that recognizes
21 the realities of when gas is actually injected and withdrawn from storage or to allow
22 suppliers to trade imbalances among themselves prior to settlement. My attempt in this

1 section is to keep the proposal simple for the parties to consider but I urge the
2 consideration of that additional element to any future discussions on program
3 improvements.

4
5 **Q13. Why is forecasting to normal instead of colder-than-normal important?**

6 A13. On Consumers system, suppliers are scheduled to colder-than-normal from November to
7 March so the forecast is increased by 10 percent (See Curtis Testimony, U-14574,
8 transcript volume 4, page 499, lines 23-24 and page 505, lines 9-13). From a system
9 integrity standpoint, having excess gas in storage does not enable a supplier to deliver
10 more gas to a customer on any particular day. It is the peak day deliverability of assets
11 that is most critical in serving customers' needs in the winter. In addition, since there is
12 no empirical way of determining whether a given winter has a greater probability of
13 being colder or warmer than normal, having suppliers deliver more gas than customers
14 are expected to use is not a risk mitigating action. On the contrary, since suppliers are in
15 essence delivering a speculative gas position to the utility, they are incurring significant
16 price risk on this gas. A regulated utility, under the gas cost recovery mechanism, can
17 ultimately recoup these types of costs from its customers. However, Choice suppliers do
18 not have this opportunity in a competitive environment.

19
20 It has been my experience in other states that planning to normal weather while allowing
21 for day-to-day adjustments to bring in the appropriate amount of gas to meet demand and
22 maintain system integrity has resulted in the most accurate, effective, and efficient

1 planning and system management. In these markets, the most critical issue for winter
2 planning is the daily deliverability of assets not the level of gas in storage.

3
4 **Q14. Will you explain your proposal for a market-based component to the cash-out
5 process?**

6 A14. Coupled with the aggregate reconciliation proposal, the addition of a market-based cash-
7 out mechanism that seeks to match costs as closely as possible to the imbalances when
8 they occur will mitigate the impact of the reconciliation rules that heavily favor the utility

9
10 The approach would be to use an average of historical prices that prevailed during the
11 contract term in which the imbalances were created. This approach better matches cost to
12 the time the imbalance was created but still will not exactly reflect the true cost of the
13 imbalance. Unfortunately, since the flat deliveries made by the suppliers to the utility do
14 not match the gas being consumed by the customers, there is no way to precisely
15 determine the actual cost of the imbalance at year end.

16
17 To be precise, the best and most accurate approach in my opinion is using prior contract
18 year average first of month utility citygate posting indexes for all imbalances regardless
19 of direction of imbalance. This approach better matches the prevailing prices over the
20 entire period where imbalances were created which will provide increased incentive for
21 reduced imbalances and a fair mechanism to capture the actual price of the delivered gas.

22

1 **Q15. How would allowing imbalance trading among participating suppliers enhance the**
2 **program?**

3 A15. Since the goal at the end of the program year should be to match supplier delivered gas to
4 customer consumption as closely as possible, another suggestion to help achieve the goal
5 is to allow suppliers to trade among themselves. A set period of time (two to four weeks
6 would work) after the imbalances are identified but before the reconciliation is settled,
7 suppliers should be afforded the opportunity to negotiate terms for the exchange of gas
8 between themselves to reduce imbalances. So, if supplier A has 100 Mcf of over delivery
9 and supplier B has 100 Mcf of under delivery, they can negotiate terms to swap and thus
10 eliminate the need for the volumetric reconciliation. Any necessary billing rate
11 reconciliation would still take place.

12
13 **Q16. What relief is NEM requesting in this case?**

14 A16. First, NEM is requesting that the Commission consider the testimony and other evidence
15 submitted on the proposed improvements to the Consumers Natural Gas Customer
16 Choice Program, including aggregate reconciliation, scheduling to normal weather,
17 market-based cash-out mechanism, and imbalance trading among suppliers, and adopt the
18 proposed amended tariff language to effectuate said changes to create a more equitable
19 program for all customers. Though these elements do not necessarily have to be adopted
20 together, each piece in addition to the aggregate reconciliation add a commensurate
21 incremental improvement to Consumers' program.

22

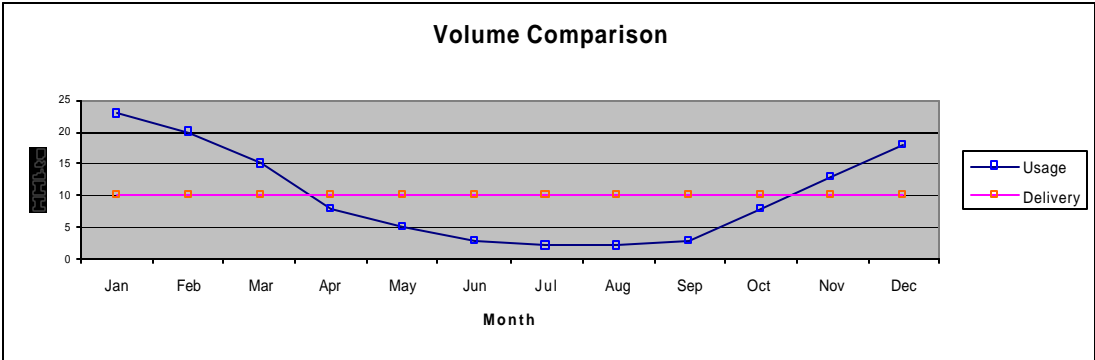
1 **Q17. Does this conclude your testimony?**

2 A17. Yes, it does.

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Michigan Natural Gas Choice Program Annual Reconciliation Matrix

		Suppliers Price > GCR	Suppliers Price < GCR
Billed Volumes > Delivered Volumes (under-delivery)	SCENARIO 1 Consumption exceeds delivered volumes and supplier's price is higher than GCR Result: Utility provides the gas and collects the supplier's higher rate from the customer <i>Utility benefit</i>	SCENARIO 2 Consumption exceeds delivered volumes and supplier's price is lower than GCR Result: Utility provides the gas and collects the supplier's rate from the customer Supplier pays SEC charge to make utility whole ("B") <i>No utility risk</i> or Utility provides and absorbs difference ("A") <i>Only potential for utility risk; entirely utility controlled</i>	
	SCENARIO 3 Delivered volumes exceed consumption and supplier's price is higher than GCR Result: Excess gas returned to supplier in summer (utility borrows gas during the winter and repays in summer) <i>No utility risk / Supplier risk of loss</i>	SCENARIO 4 Delivered volumes exceed consumption and supplier's price is less than GCR Result: Excess low-cost gas retained by the utility at a price below the GCR <i>Utility benefit</i>	
Billed Volumes < Delivered Volumes (over-delivery)			

EXAMPLE 1 Offsetting Pool Imbalance / Price Difference								
Customer Sales				Supplier Delivery			Reconciliation	
Pool	MCF	Price	Amount	MCF	Price	Amount		
Pool 1	200	\$5.00	\$1,000.00	100	\$5.00	\$500.00	Paid to Supplier	\$1,720
Pool 2	100	\$6.10	\$610.00	200	\$6.10	\$1,220.00	Paid to Utility	\$1,610
Total	300	\$5.367	\$1,610.00	300	\$5.733	\$1,720.00	Under Delivery SEC Charge ***	N/A
GCR	\$ 6.00						Over Delivery Refund	N/A
							Rate Settlement Owed/(Credit)**	\$110
							Returned Gas (MCF)	0

EXAMPLE 2 Over Delivered / GCR is Lower								
Customer Sales				Supplier Delivery			Reconciliation	
Pool	MCF	Price	Amount	MCF	Price	Amount		
Pool 1	200	\$13.00	\$2,600.00	300	\$9.90	\$2,970.00	Paid to Supplier	\$5,520
Pool 2	200	\$8.50	\$1,700.00	300	\$8.50	\$2,550.00	Paid to Utility	\$4,300
Total	400	\$10.75	\$4,300.00	600	\$9.20	\$5,520.00	Under Delivery SEC Charge ***	N/A
GCR	\$ 9.00						Over Delivery Refund	(\$1,840)
							Rate Settlement Owed/(Credit)**	(\$620)
							Returned Gas (MCF)	200

EXAMPLE 3 Over Delivered / CGR is Higher								
Customer Sales				Supplier Delivery			Reconciliation	
Pool	MCF	Price	Amount	MCF	Price	Amount		
Pool 1	100	\$11.00	\$1,100.00	150	\$11.00	\$1,650.00	Paid to Supplier	\$3,750
Pool 2	200	\$7.00	\$1,400.00	300	\$7.00	\$2,100.00	Paid to Utility	\$2,500
Total	300	\$8.33	\$2,500.00	450	\$8.33	\$3,750.00	Under Delivery SEC Charge ***	N/A
GCR	\$ 10.00						Over Delivery Refund	N/A
							Rate Settlement Owed/(Credit)**	\$0
							Returned Gas (MCF)	0

EXAMPLE 4 Under Delivered / WACOG is Lower								
Customer Sales				Supplier Delivery			Reconciliation	
Pool	MCF	Price	Amount	MCF	Price	Amount		
Pool 1	300	\$13.00	\$3,900.00	200	\$9.90	\$1,980.00	Paid to Supplier	\$3,680
Pool 2	300	\$8.50	\$2,550.00	200	\$8.50	\$1,700.00	Paid to Utility	\$6,450
Total	600	\$10.75	\$6,450.00	400	\$9.20	\$3,680.00	Under Delivery SEC Charge ***	N/A
WACOG	\$ 9.00						Over Delivery Refund	N/A
							Rate Settlement Owed/(Credit)**	(\$620)
							Returned Gas (MCF)	0

EXAMPLE 5 Under Delivered / WACOG is Higher								
Customer Sales				Supplier			Reconciliation	
Pool	MCF	Price	Amount	MCF	Price	Amount		
Pool 1	300	\$13.00	\$3,900.00	200	\$12.10	\$2,420.00	Paid to Supplier	\$4,120
Pool 2	300	\$8.50	\$2,550.00	200	\$8.50	\$1,700.00	Paid to Utility	\$6,450
Total	600	\$10.75	\$6,450.00	400	\$10.30	\$4,120.00	Under Delivery SEC Charge ***	\$50
WACOG	\$ 11.00						Over Delivery Refund	N/A
							Rate Settlement Owed/(Credit)**	(\$180)
							Returned Gas (MCF)	0

* Owed=owed by marketer to utility
 ** Credit=credit owed by utility to marketer
 *** Only owed by supplier if pool 2 is a B pool

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for authority to increase its rates for the)
distribution of natural gas and for other relief.)
_____)

Case No. U-15190

PROOF OF SERVICE

STATE OF MICHIGAN)
) SS
COUNTY OF WASHTENAW)

Jacqueline K. Tinney, being first duly sworn, deposes and states she is employed at Dickinson Wright PLLC; and that on July 20, 2007 caused a copy of the *Direct Testimony of Timothy Ray on Behalf of National Energy Marketers Association* to be served upon the parties listed on the following page via email.

Jacqueline K. Tinney

Subscribed and sworn to before me,
a Notary Public in and for said County,
this 20th day of July, 2007.

Elaine M. Masters, Notary Public
Washtenaw County, Michigan
Acting in Washtenaw County, Michigan
My Commission Expires: 9/23/07

Service List – MPSC Case No. U-15190

<p>Administrative Law Judge Hon. Mark D. Eyster eystem@michigan.gov</p>	<p>Consumers Energy Jon R. Robinson H. Richard Chambers John C. Shea Rhonda M. Morris Raymond E. McQuillan jrrobinson@cmsenergy.com hrchambers@cmsenergy.com jcshea@cmsenergy.com rmmorris@cmsenergy.com remcquillan@cmsenergy.com mpscfilings@cmsenergy.com</p>
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