

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
generation and distribution of
electric, and for other relief.

Case No. U-17087

Volume 4

CROSS-EXAMINATION

Proceedings held in the above-entitled
matter before Mark E. Cummins, Administrative Law Judge
with MAHS, at the Michigan Public Service Commission,
4300 West Saginaw, Hearing Room One, Lansing,
Michigan, on Monday, March 25, at 10:35 .m.

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1 MS. UITVLUGT: Good morning, your Honor.
2 Anne Uitvlugt, Lauren Donofrio, and Amit Singh on behalf
3 of Michigan Public Service Commission Staff.

4 MR. KESKEY: Good morning, your Honor.
5 Don Keskey appearing on behalf of the Michigan Community
6 Action Agency Association.

7 MR. WHITFIELD: Good morning, your Honor.
8 David Whitfield on behalf of the Midland Cogeneration
9 Venture Limited Partnership.

10 JUDGE CUMMINS: Let's start from left to
11 right here. Anyone else having appearances today? (No
12 response.)

13 Very well. Based on our schedule, the
14 purpose of today's proceeding is to handle any motions to
15 strike, of which we have two, and to take any testimony
16 and receive any exhibits from witnesses. The hearing
17 will go today and Thursday, the 28th, and then we'll at
18 least be available to go all of next week as well. I
19 know we have a late start today because of a timing issue
20 with the room. Thursday's hearing will begin at 9:00 and
21 we'll hopefully go through just close to 5:00. We have
22 to vacate this building apparently before 5:00, so about
23 quarter to we'll have to wind things down each of the
24 days that we do have hearings. Next week Monday through
25 Friday, it should be a 9:00 to 5:00 or 9:00 to 4:45

1 schedule.

2 At this point, as I indicated we have two
3 motions to strike. I have heard prior to going on the
4 record that there has been at least a partial resolution
5 of one of the motions. I have also had indicated to me
6 through e-mail that the other motion is to be decided
7 simply on the filings that have been submitted so far.

8 Why don't we go ahead and begin with the
9 Attorney General's motion to strike. And this is with
10 regard to testimony -- actually I think four portions of
11 testimony that they would like to have stricken. Mr.
12 Moody, I heard there was an agreement between the
13 Applicant and the Attorney General on this. Could you
14 please state that for the record?

15 MR. MOODY: Yes. Anyway, it's the
16 Company's, I think, motion to strike.

17 JUDGE CUMMINS: Oh, I'm sorry.

18 MR. MOODY: That's O.K. And we did a
19 response, but we have come to an agreement, and I'll just
20 state that I'm filing revised testimony in accordance
21 with that agreement, essentially striking portions that
22 we have agreed upon, and the sections on the ones that
23 I've struck already, and taken some of the ones that the
24 Company has suggested before the hearing. So I'll file
25 revised testimony that conforms to our agreement --

1 JUDGE CUMMINS: O.K.

2 MR. MOODY: -- and bind that in next week
3 when we our witness is available.

4 JUDGE CUMMINS: Will you be able to do
5 that let's say tomorrow or so, so the other parties have
6 a copy of it. What I don't want is one of the other
7 parties to say, "Oh, my gosh. This came in?" If you
8 could do that as soon as you can, Mr. Moody, that would
9 be helpful.

10 MR. MOODY: O.K.

11 JUDGE CUMMINS: That way the parties will
12 all have an opportunity to review it before it would go
13 in. You will be binding in this testimony on the 2nd?

14 MR. MOODY: Yes, I think that's the right
15 date. I know it's next week.

16 JUDGE CUMMINS: All right. Well, if you
17 can do that by tomorrow, that would be very helpful, I
18 think, for all the parties concerned. Very well. I
19 can't get overruled on that.

20 We have the Staff's and the Company's
21 issue to deal with, and this is the Staff's motion to
22 strike testimony with regard to Mr. Rao. It was
23 indicated to me through e-mail, and we have confirmed
24 that today prior to going on the record, that this is to
25 be decided simply on the filings that were submitted,

1 which would be the Staff's motion, the Company's response
2 to that.

3 Based on my review of the filings as well
4 as a review multiple times of Mr. Rao's testimony, and
5 the area we're dealing with is his testimony on pages 9,
6 line 24, through page 10, line 13. My feeling is that it
7 doesn't matter whether or not Consumers was actually a
8 party, a signatory to the settlement agreement in
9 question. The terms of the settlement specifically state
10 that the Commission can not use the settlement or
11 anything attached to the settlement to decide issues in
12 any other case in the future.

13 That being the situation, because the
14 Commission's hands are effectively tied, I find that
15 there truly is no relevance then to that testimony. And
16 this again is at page 9, line 24, through page 10, line
17 13. So I'm going to grant the Staff's motion in its
18 entirety. I will ask that the Company redact that
19 portion of Mr. Rao's testimony. Obviously this is not --
20 it does not limit the Company in any way from making
21 legal arguments with regard to that, the issue in
22 question.

23 Obviously, Mr. Chambers, the Company will
24 not be able to cite to the settlement, but they can make
25 arguments along that line if they would like to. That's

1 my ruling with regard to the Staff's motion to strike.

2 Any questions with regard to that? All
3 right. Any other motions to strike? Those are the only
4 two that I saw so far. Very well.

5 That being the case, we're teed up to
6 actually present witnesses and their testimony today.
7 The indication was that there were at least four of the
8 Applicant's witnesses for which no cross-examination was
9 going to be required. Unless there is an objection by
10 any of the parties, what I would like to do is go ahead
11 and bind that testimony in and receive those exhibits at
12 this time.

13 Hearing no objections, Mr. Chambers, you
14 have the floor.

15 MR. CHAMBERS: Thank you, your Honor.
16 Consumers Energy moves to bind in the direct testimony of
17 Ronn J. Rasmussen, consisting of a cover page and 18
18 pages of questions and answers. Mr. Rasmussen did not
19 sponsor any exhibits.

20 JUDGE CUMMINS: Very well. Based on the
21 agreement of the parties, and unless I hear otherwise, I
22 will bind in Mr. Rasmussen's testimony. There are no
23 exhibits to be received at this time.

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25

STATE OF MICHIGAN

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In the Matter of the application of)
CONSUMERS ENERGY COMPANY)
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Case No. U-17087

DIRECT TESTIMONY

OF

RONN J. RASMUSSEN

ON BEHALF OF

CONSUMERS ENERGY COMPANY

RONN J. RASMUSSEN
DIRECT TESTIMONY

1 Q. Please state your name and business address.

2 A. My name is Ronn J. Rasmussen and my business address is One Energy Plaza, Jackson,
3 Michigan 49201.

4 Q. By whom are you employed and what is your present position?

5 A. I am employed by Consumers Energy Company ("Consumers Energy" or
6 "the Company") as Vice President Rates and Regulation.

7 Q. Please review your educational and business experience.

8 A. I was graduated from Ferris State College in May of 1978 with a Bachelor of Science
9 Degree in Accounting. Since joining Consumers Energy in June 1978 I've held various
10 positions in our Accounting, Gas Supply, Business Support, and Rates and Regulation
11 departments.

12 Q. What are your responsibilities as Vice President Rates and Regulation?

13 A. I am responsible for Consumers Energy's rate and regulatory activities which include
14 revenue requirements, cost allocation, rate design, tariff administration and regulatory
15 affairs. I am also responsible for coordinating the Company's planning and budgeting
16 and strategic policy development and integration functions.

17 Q. Have you previously testified before this Commission?

18 A. Yes, on a number of occasions. Most recently, I served as the Company's policy witness
19 in several general rate cases, including Consumers Energy's electric general rate cases:
20 Case Nos. U-16191 and U-16794; and gas general rate proceedings: Case Nos. U-15986,
21 U-16418 and U-16855.

22 Q. What is the purpose of your testimony in this proceeding?

23 A. The purpose of my testimony is to provide an overview of the Company's electric rate
24 application, including a summary of the key drivers, and a brief discussion of our recent

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1 performance and the current business environment. I will address how the filing
2 complies with the Commission's recent Order in Case No. U-16794. I will summarize
3 the customer value and benefits related to our proposals presented in this application.
4 Finally, I will address, from a policy perspective, certain issues detailed in the testimony
5 and exhibits of several other Company witnesses.

6 Q. Please provide a general description of the key financial and operational items that drive
7 the amount of rate relief requested in this filing.

8 A. The \$148 million in rate relief requested in this filing is driven primarily by the
9 Company's continued investment in Michigan. Consumers Energy continues to make
10 significant investments in the infrastructure necessary to provide safe and reliable service
11 to our customers and comply with federal and state environmental requirements.
12 Approximately \$126 million, or 85% of this request, is related to the new investment.
13 Capital investments in Michigan were also the primary driver of Consumers Energy's
14 most recent electric rate applications Case Nos. U-16191 and U-16794, where 60% and
15 77% respectively were related to new investment. This on-going investment is part of
16 Consumers Energy's plan to invest more than \$6 billion in Michigan over the next five
17 years to maintain and improve utility infrastructure, significantly increase the amount of
18 energy generated from renewable resources, and ensure that our customers receive the
19 quality of service that they expect from the Company. These investments make
20 Consumers Energy one of the largest investors in the State of Michigan at a time when
21 investment in improved basic infrastructure is needed. Our ongoing investments generate
22 economic benefits including a significant number of Michigan jobs. Consistent with our
23 support of economic growth in Michigan and attracting new jobs, we are proposing
24 additional emphasis on the use of system demands in allocation of production and

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1 transmission costs and seeking approval to offer new rate designs that will lower the cost
2 of doing business for our large business customers.

3 The new investments can be segregated into three main categories:
4 environmental compliance; generation and distribution system reliability; and enhanced
5 technology, primarily associated with the Smart Grid project. The customer benefits
6 derived from the investments are described in the testimony of witnesses Anderson,
7 Kehoe, Popa, Varvatos, and Youngdahl.

8 Another significant driver of the requested rate relief is a \$46 million increase in
9 O&M expense from current rate levels. A significant portion of this increase directly
10 affects and improves system reliability and reduces outages for our customers, as
11 described by witness Anderson. In addition, a portion of this increase reflects the
12 inclusion of incentive compensation plan costs the Company incurs to attract and retain
13 employees. Consumers Energy's overall compensation plan emphasizes pay that is not
14 more than competitive and then places a portion "at risk" with ties to improving
15 performance. I should also mention that we've not included in this request any incentive
16 compensation for our top six executives. This plan has been designed to assure that it
17 results in a net benefit to our customers.

18 A \$15 million reduction in our projected financing costs, primarily related to
19 lower interest rates helps offset increases related to new investments and operating
20 expenses. We also expect a slight increase of about \$9 million in certain revenues versus
21 previous rate levels which will offset some of the cost increases.

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1 Q. How have the Company's capital expenditures affected recent electric system
2 performance?

3 A. Over the past few summer months of 2012, our electric distribution system has been
4 tested by the hot weather and it performed extremely well given the extreme conditions.
5 We set a record peak for the month of June and broke the all-time record on July 17, with
6 a new system peak of 9,006 MW, exceeding the July 2011 record peak by almost 1% and
7 the prior record peak in August 2006 by 1.4%.

8 While an average summer would have 10 days with temperatures of 90 degrees or more,
9 so far this year we experienced 32 days over 90 degrees and 2 days over 100 degrees. In
10 spite of these conditions our customers have seen a reduction in the number of heat
11 related interruptions of nearly 63% versus the previous peak days. The continued capital
12 investments that the Company has made over the last several years have translated into
13 improved system reliability for a system that has been increasingly taxed. To meet future
14 peak loads and system demands it is imperative that the Company makes continued
15 investments to increase capacity and reliability as our system load grows and the
16 Michigan economy continues to improve.

17 Q. Please discuss the Company's ongoing efforts to minimize the O&M component of
18 customer rates.

19 A. There are many examples of the Company's effort in this area. We focus our capital
20 investments in areas that improve customer service and reliability and reduce fuel and
21 O&M expenses. Capital investments in our generating plants have allowed us to greatly
22 increase the utilization of less expensive western coal, resulting in a decrease in fuel costs
23 of more than \$2 billion. Implementation of SAP technologies result in improved
24 productivity across corporate and operating functions and build the platform for far

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1 greater improvement in future years. We have implemented three voluntary workforce
2 reduction programs that allow us to better align the amount of ongoing work with the
3 level of our workforce and have revised our labor agreements to ensure maximum
4 productivity of the workforce. Productivity across the Company has increased by nearly
5 40% in the past six years. We have one of the most aggressive health care cost sharing
6 mechanisms in the utility industry. Complementing the reductions noted above are the
7 benefits arising from a 69% improvement in the Company's safety performance since
8 2006, a 4% reduction in average annual customer outage minutes since 2006, and a 51%
9 improvement in generation reliability since 2006. The Company's focus on controlling
10 O&M expenses is evidenced by the fact that we continue to benchmark versus our peers
11 in the first quartile for O&M expenses per customer, operating O&M as a percent of
12 revenue, and corporate O&M as a percent of revenue. These results are driven by the fact
13 that the Company's non-fuel O&M expense is at the same level in 2011 as it was in 2006.

14 This filing does include a request to increase the amount of spending related to
15 distribution reliability improvements of \$22 million. A portion of that reliability
16 spending would be devoted to reducing the Company's tree trimming cycle from the
17 current 14-year average to a cycle averaging 8 years, which moves us closer to the
18 industry average of a 4-year cycle. Additional details of the plan and the resulting
19 customer benefit are described in the testimony of witness Anderson.

20 Q. Has the Company proposed any reconciliation mechanisms in this case?

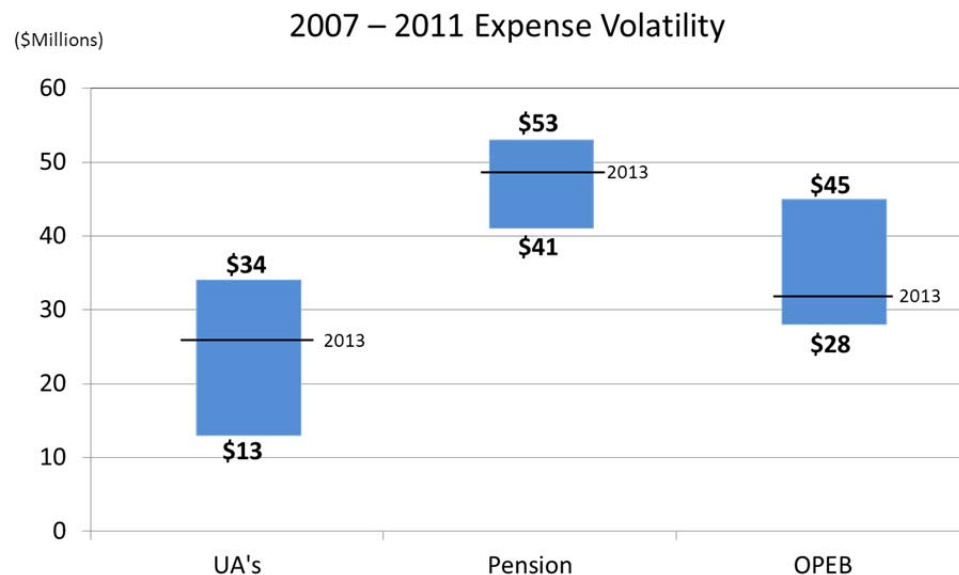
21 A. Yes, the Company has proposed four reconciliation mechanisms including the following:
22 a Revenue Adjustment Mechanism ("RAM") supported by Company witness Stubleski,
23 an Uncollectible Accounts Equalization Mechanism ("UETM") supported by Company
24 witnesses Jones and Stubleski, Pension and OPEB equalization mechanisms ("PEM" and

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1 “OEM”) supported by Company witnesses Kops and Stubleski, and an Investment
2 Recovery Mechanism (“IRM”) presented by Company witnesses Ross and Stubleski.
3 These witnesses discuss the mechanics and need for these reconciliation mechanisms in
4 their respective testimonies.

5 Q. From a policy perspective, why are the reconciliation mechanisms appropriate at this
6 time?

7 A. Uncollectible accounts expense and pension and retiree health care (OPEB) expenses are
8 significant dollar items, volatile, difficult to forecast and largely driven by the economy
9 and financial markets forces such as interest rates, discount rates and market returns that
10 are beyond the control of the Company. Evidence of this volatility can be seen when
11 comparing the lowest expense for each of these items over the past five years with the
12 highest expense:



13 The purpose of the UETM, PEM and OEM are to provide for the recovery of actual
14 expense, no more and no less, by putting in place a process to reconcile actual costs to
15 rate case levels.

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1 Q. Does file and implement ratemaking with the use of a projected test year as provided for
2 in 2008 PA 286 eliminate the need for adjustment mechanisms like the UETM, PEM and
3 OEM?

4 A. No. The file and implement and projected test years provided for in 2008 PA 286
5 address regulatory lag - but don't improve anyone's ability to predict or control items
6 such as uncollectible accounts, pension or retiree health care expenses. To the extent
7 actual costs deviate materially from the levels used to set rates, the Company does have
8 the option of filing a new rate case, but going through the rate case process is a resource
9 intensive exercise for the Company, the Commission and other parties. Adoption of
10 reconciliation ratemaking mechanisms for highly volatile and hard-to-predict cost items
11 would tend to extend the period between rate case applications, to the benefit of all
12 parties.

13 Q. Why should the Revenue Adjustment Mechanism be adopted by the Commission?

14 A. The Revenue Adjustment Mechanism allows the Company to recover the level of
15 revenue (non-fuel margin) authorized and necessary to cover what are for the most part
16 the fixed costs related to investment and expenses approved by the Commission.

17 Q. Why might actual revenues differ from Commission-approved rate levels and what are
18 the impacts of significant differences?

19 A. There are a variety of reasons that revenues might differ from Commission-approved rate
20 levels. These reasons include impacts of weather, the economy, energy efficiency
21 programs, customer migration between rate schedules and other variances in actual sales
22 versus forecast assumptions. It is extremely difficult for the Company to properly
23 balance customer service efforts when revenues are subject to unexpected change
24 (increases or decreases) for the items noted above. The Revenue Adjustment

RONN J. RASMUSSEN
DIRECT TESTIMONY

1 Mechanism will provide for increased certainty that the Company will have stability
2 around its revenue assumptions and can therefore, implement O&M and customer service
3 plans that maximize customer value.

4 Q. Why is it appropriate to implement an Investment Recovery Mechanism in this
5 proceeding?

6 A. The Investment Recovery Mechanism will allow the Commission to review and approve
7 capital expenditures planned for 2014, with the assurance that the investments will either
8 be made, or the associated revenue requirement returned to customers. As I indicated
9 earlier, new investment is the primary driver of the need for the revenue increase
10 addressed in this application. That is also expected to be the case in 2014 and for the
11 balance of our 5-year capital investment plan. The approval of the Investment Recovery
12 Mechanism will allow for review and approval in this proceeding of the 2014 spending
13 plans for projects and programs, most of which are continuations of projects and
14 programs in place in 2012 and 2013. Therefore, the Investment Recovery Mechanism
15 may eliminate the need for a general rate proceeding in 2014 by allowing for an early
16 review of the second year of our capital investment plan. Furthermore, the reconciliation
17 process will provide customers with the certainty that they are only paying for the actual
18 costs of 2014 projects and programs.

19 Q. Please quantify the average customer rate impact if the Commission authorizes the rate
20 relief requested by the Company.

21 A. The average overall rate increase would be approximately 3.9%. Residential customers
22 will experience the majority of the increase under our proposed cost allocation and rate
23 design. To put it in perspective, the typical residential service customer on Rate RS
24 currently pays on average about \$2.71 per day for electric service. Under our proposals,

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1 the typical residential Rate RS customer will pay on average \$2.97 per day for the electric
2 service that provides light, powers furnaces, fans, air conditioning, kitchen and laundry
3 appliances, televisions, computers, entertainment systems, cellular phones, tools,
4 toothbrushes and hair dryers, and for some, automobiles. The Company is aware that
5 Michigan's economy is still recovering and that this increase will challenge some
6 customers more than others. Included in this rate case are a number of items that assist
7 customers who may continue to be more impacted as the economy lags. Examples of
8 these items include low income assistance rates, senior citizen assistance rates, and a
9 variety of programs designed to assist customers with the management of their energy
10 use and bills. In addition to these provisions and programs, the Company and its
11 employees are generous contributors to community based groups including the United
12 Way, the Salvation Army, and a multitude of local community service organizations.

13 I would also reiterate that the Company has a positive influence on the Michigan
14 economy through our investments in Michigan, the jobs directly and indirectly created by
15 that investment, and through the almost \$200 million in property and income taxes paid
16 to the State of Michigan and to nearly 1,400 taxing authorities.

17 The Company strives to keep its requested increase to the lowest level it believes
18 is reasonable while balancing the need for improved reliability and customer service.

19 Q. The Commission's Order in Case No. U-16794 directed the Company to use the criteria
20 from Case No. U-16191 and submit "stronger evidence that will demonstrate its
21 commitment to major capital projects and O&M expenses." Please describe the
22 Company's compliance with that requirement.

23 A. The Company continually evaluates and adjusts its long-term financial plan for a variety
24 of factors that would include: sales and revenue expectations and results; Customer

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1 Choice participation levels; capital investments and the cost of capital; O&M expense
2 expectations and results; and, the impact of a variety of unusual items that occur
3 throughout time (changes in environmental laws and requirements, Commission orders,
4 unusual weather events, customer demands, commodity prices, financing costs, changes
5 in economic expectations, etc.). In any one period of time the Company's capital
6 investments and its O&M expenses may vary from what was expected in a prior period.
7 Indeed, it would not be prudent management to fail to continue to take current and
8 changing conditions into account in incurring expenses and making investments. While
9 the Company understands this ever changing environment, Company witnesses have
10 provided highly detailed and thorough support for both capital expenditures and O&M
11 expenses per the Commission's request.

12 The individual witnesses addressing capital and O&M expenditures in this case
13 address the reasons for these expenditures, and these expenditure levels undergo rigorous
14 management review before they are submitted. While the Company must retain the
15 flexibility to react to changing conditions, the proposed expenditure levels included in
16 this case reflect the Company's commitment to meet its legal responsibilities and
17 improve service reliability and quality. Further evidence of the Company's commitment
18 to make the investments necessary to improve service would be the improvements in the
19 customer service metrics noted throughout the testimony and exhibits filed in this case.

20 More specifically, several Company witnesses have provided detailed analysis to
21 alleviate the Commission's concern with evidentiary support. Witness Anderson
22 provides highly detailed analysis for electric distribution capital expenditures and O&M
23 expense; witnesses Kehoe and Popa provide extensive testimony and analysis regarding
24 generation and environmental capital expenditures; and witness Youngdahl provides a

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DIRECT TESTIMONY

1 substantial amount of analysis in her testimony for Phase 2 of the Company's Smart Grid
2 project.

3 Q. Has the Company provided more detailed evidence and reasoning for its environmental
4 capital expenditures as desired by the Commission?

5 A. Yes, witness Popa has provided extensive analysis and justification which underlies the
6 basis for the Company's capital spending to comply with numerous generation
7 regulations. Witness Popa talks about each of these regulations in detail while providing
8 the Company's plan and reasoning to how overall compliance will occur. In addition,
9 witnesses Popa and Ronk discuss the reasoning behind the Company's decision to
10 "mothball" several of the Company's smaller generating units as it is the most
11 economical choice at this time and allows the Company to defer their compliance plan to
12 a future period when that plan can be better optimized. At that time a decision will be
13 made to either retire these plants or retro-fit them with pollution controls.

14 Q. The Commission's Order in Case No. U-16794 required that the Company provide
15 evidence to demonstrate the improved performance of its distribution system and to show
16 how spending accrues to the benefit of customers. Please indicate how the Company has
17 complied with this requirement.

18 A. Witness Anderson's testimony and exhibits provides significant detail regarding the
19 Company's spending and distribution performance and how the combination of the
20 spending and performance accrues to the benefit of the customer. Witness Anderson also
21 demonstrates how the increased spending in capital expenditures and O&M expense will
22 benefit into future years with extensive analysis to support the Company's position.

RONN J. RASMUSSEN
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1 Q. Has the Company complied with the requirements of PA 286 in preparing this rate case?

2 A. Yes, the cost of service and rate design adheres to the provisions of PA 286. Specifically,
3 the cost of service uses the prescribed production and transmission allocations and the
4 rate design continues to phase out the residential subsidy as prescribed by law. The
5 elimination of the residential subsidy reduces the cost burden that has been borne by
6 business and other nonresidential customers for many years. The specifics of the cost
7 study are found in the testimony of Company witness Keaton while the rate design is
8 covered by witness Stubleski.

9 Q. Has the Company undertaken any initiatives to help businesses within the state to help
10 encourage growth in the Michigan economy?

11 A. Yes, the Company has taken up a couple of initiatives that are clearly “pro-Michigan
12 businesses.” The Company has awarded \$272 million in multi-year contracts to 126
13 Michigan companies in the past year. The Company has also pledged to increase
14 payments of its Michigan-based capital spending by \$100 million per year for five years
15 which is in addition to the already \$2 billion the Company currently spends annually.
16 This initiative partners with Michigan businesses across the State and keeps dollars inside
17 Michigan thus boosting our economy through the use of quality products that are cost
18 competitive.

19 The second initiative is in the rate design proposals included in the testimony of
20 Company witness Stubleski. The 2008 energy law requires the phase-out of the
21 residential subsidy paid by businesses and requires all rates to be based on cost-of-service
22 by October 2013. The rates proposed in this application achieve this statutory
23 requirement. The Company also proposes to update the formula which allocates costs for
24 transmission and also reallocate power supply costs to better reflect peak usage of

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1 residential customers which in turn will reduce business rates. And lastly, the Company
2 proposes to relax the upfront deposit rules so that business customers can pay to upgrade
3 or expand electric distribution facilities dedicated solely to them over time which frees up
4 their investment capital for other uses. The Company believes these initiatives will have
5 a very strong positive impact on Michigan businesses which in turn supports our state's
6 economic recovery.

7 Q. Has the Company included a pilot metal melting tariff as directed by the Commission in
8 the Company's previous electric rate case order?

9 A. Yes. The testimony and exhibits of witness Stubleski describe the proposal in detail.

10 Q. Why is the Company seeking recovery of at-risk incentive compensation costs in this
11 filing?

12 A. Company witness Amy Conrad discusses the incentive compensation issue at great
13 length. In that discussion she makes it very clear that the Company first determines a fair
14 amount of compensation for employees. After that determination, the Company then
15 determines how much of that compensation is put at risk in the form of incentive
16 compensation. She also emphasizes how the customers and Company benefit from this
17 widely accepted and used business practice. The Company's incentive plan encourages
18 employees to provide quality service at a competitive price while also recognizing the
19 importance of the financial health of the Company. The incentive plan is designed to
20 encourage attention to issues that directly relate to customer benefits. To the extent the
21 plan retains an element that relates to the financial health of the Company, this leads to
22 reduced costs of capital through favorable borrowing rates which in turn also directly
23 benefits our customers.

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1 Q. How has the Commission historically addressed the inclusion of incentive compensation
2 in customers' rates?

3 A. Based on my research, the issue of recovery in rates of incentive compensation expenses
4 was first raised in MichCon's rate case, Case No. U-10150, in which the utility requested
5 recovery of 100% of incentive compensation paid to company executives. The
6 Commission's Order in this case stated that "Executive bonuses have often been viewed
7 as an appropriate cost of operating a utility. This is particularly true when the bonus plan
8 is structured in a way that produces significant benefits for the utility's ratepayers." The
9 Commission adopted the Staff's position of a 50/50 sharing between ratepayers and
10 shareholders of these costs, noting that in future filings, MichCon's recovery of incentive
11 compensation would require a showing by the utility that customer benefits are
12 commensurate with the costs.

13 The Commission subsequently further modified the ratemaking that it had been
14 following with respect to incentive compensation plans. In a subsequent general rate
15 case, an electric proceeding, Case No. U-14347, the Company requested 100% recovery
16 of the costs associated with its incentive compensation programs. In a December 22,
17 2005 Order in Case U-14347 the Commission stated: "In Case Nos. U-10149 and U-
18 10150, the Commission determined that executive bonus and employee incentive plans
19 require a showing that the plan will not result in excess rates and that the benefits to
20 ratepayers from the bonus and incentive plans will, at a minimum, be commensurate with
21 the programs' costs." The Commission disallowed 100% of the Company's request
22 related to recovery of incentive compensation expenses. For several rate cases after Case
23 No. U-14347, the Company continued to request either full or partial recovery of the
24 costs associated with its incentive compensation plans. In spite of the Company's

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1 continual efforts to align our incentive compensation programs with the standard
2 expressed by the Commission regarding the demonstration of benefits to our customers in
3 excess of the costs, the Commission continued to deny recovery of these costs. While the
4 Company has demonstrated a direct tie between the design of the incentive plans and
5 desirable benefits for customers, the Commission in prior cases has declined to permit
6 recovery of these costs.

7 Q. Do you support use of the Case U-14347 standard for incentive compensation in this
8 case?

9 A. No. The criterion that is used in evaluating utility expenses is whether the expenses are
10 reasonable. Similarly, from a ratemaking perspective, the test for evaluating
11 compensation expense should be whether the overall level of compensation expense,
12 including both base salary and incentive compensation, is reasonable. On April 27, 2011
13 the Indiana Utility Regulatory Commission issued an order in a case involving Southern
14 Indiana Gas and Electric Company (doing business as Vectren Energy), that recognized
15 the value of incentive compensation plans as part of an overall compensation package to
16 attract and retain qualified personnel. The Indiana Commission did not require a
17 quantification of customer benefits specifically related to the metrics. The Indiana
18 Commission required there be a combination of operating and financial metrics and a
19 demonstration that there is no resultant excess compensation. In this current case,
20 Company witness Ms. Conrad discusses how the incentive plans in place at Consumers
21 Energy meet these requirements.

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1 Q. Did the Indiana Commission include a requirement that there be a sharing of costs with
2 shareholders?

3 A. Yes. While I question the reasonableness of this aspect of the Indiana criteria, I will note
4 that the recommendation of Consumers Energy in this case does involve a sharing of
5 costs. The Company is not seeking recovery of any incentive compensation costs for the
6 top six officers as defined under Securities and Exchange proxy rules. In addition, the
7 Company's proposal in this case would result in shareholders absorbing costs if incentive
8 payments are larger than the target level.

9 Q. Do you believe that benefits to customers from the incentive plans will, at a minimum, be
10 commensurate with the programs' costs?

11 A. Yes. Therefore, I believe that the Company fully satisfies the Case U-14347 standard in
12 this case, and recovery of incentive compensation expenses should be allowed even if the
13 Commission chooses to use that standard in this case. Ms. Conrad discusses various
14 benefits to customers from the design of the Company's incentive compensation plan. In
15 addition, there are quantitative benefits. The design of the EICP plan clearly leads to
16 lower costs and improved service which benefit our customers.

17 Q. Has the Company quantified customer benefits that are tied to its incentive compensation
18 program?

19 A. Yes. Although specific quantification of the costs of the program and the benefits is not
20 easy to perform for every metric included in the program, the Company has looked at
21 several key metrics of the program and has concluded that there is substantial benefit that
22 accrues to the customer. The first of those metrics is employee safety. As previously
23 noted, employee safety statistics have improved by 69% since 2006. The resulting
24 reduction in lost work days and medical expenses approximates \$3.5 million that accrues

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1 to the benefit of the customer. A second metric that can be translated to cost avoidance
2 for our customers is in the area of distribution reliability. Using cost per outage minute
3 estimates from Berkeley Labs, the 11 minute reduction in average outage minutes since
4 2006 results in annual savings to our business customers in excess of \$30 million. The
5 third quantifiable metric is generation reliability. Our improvement in this area from an
6 annual forced outage rate of 9.0% to an annual rate of 4.43% reduces fuel expenses by
7 more than \$5 million per year. Finally, the productivity improvement of approximately
8 40% over the past six years is one of the main reasons that the Company's O&M
9 expenses are in the 1st quartile versus our utility peers. Simply translating superior O&M
10 performance (O&M per customer times number of customers) yields an annual customer
11 benefit versus peers of more than \$50 million.

12 Q. Aren't these benefits things that the Company should be pursuing independent of the
13 incentive compensation plan?

14 A. Yes. The incentive plan takes this into consideration. As discussed by Ms. Conrad,
15 incentive mechanisms help communicate priorities, engage employees in business
16 success, reward valued skills and behaviors, and create business understanding for
17 employees. The incentive plan is structured in a way that helps to highlight certain
18 important elements of utility service, and to emphasize to employees that they should pay
19 particular attention to achieving these targets. Making it clear to employees that a portion
20 of their total compensation depends upon their collective ability to meet these targets
21 communicates clearly to employees the importance of serving customers and encourages
22 them to deliver their best performance. Because the incentive compensation plan has
23 been designed so that the incentive payments simply bring employee compensation to a

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1 competitive level, I think a better way to describe this program is that employees are
2 penalized if the targets are not achieved.

3 Q. Do you believe that the incentive plan is the reason that the above benefits have been
4 realized?

5 A. I believe that the design of the incentive plan is intended to, and does, make it more likely
6 that these customer benefits will be achieved. As mentioned above, it is not easy to
7 quantify exact savings directly attributable to any one incentive compensation plan
8 category. However, even if one were to take an extremely conservative approach to that
9 quantification, and apply it only to the four metrics discussed above, then it would remain
10 evident that customers receive significant benefits from improvement in the performance
11 areas included in the Company's incentive compensation plan. That benefit far exceeds
12 the \$9.0 million of incentive compensation expense that the Company has included in this
13 filing.

14 Q. What is the Company's position related to the potential that the at-risk compensation
15 included in this filing might not be paid out due to the performance based aspects of the
16 plan?

17 A. In that event, the Company would not be opposed to refunding the amount collected in
18 rates.

19 Q. Does this conclude your testimony in this proceeding?

20 A. Yes.

1 MR. CHAMBERS: Your Honor, Consumers
2 Energy moves to bind in the testimony and the rebuttal
3 testimony of Herbert B. Kops. The direct testimony
4 consists of a cover page followed by 46 pages of
5 questions and answers. The rebuttal testimony consists
6 of a cover page followed by three pages of questions and
7 answers. Mr. Kops, in connection with his testimony,
8 sponsored Exhibit A-31. Consumers Energy moves to admit
9 Exhibit A-31.

10 JUDGE CUMMINS: Very well. Any objection
11 to binding in Mr. Kops' testimony? Hearing none, Mr.
12 Kops' testimony will be bound in the record.

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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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

DIRECT TESTIMONY

OF

HERBERT B. KOPS

ON BEHALF OF

CONSUMERS ENERGY COMPANY

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1 Q. Please state your name and business address.

2 A. Herbert B. Kops, One Energy Plaza, Jackson, Michigan.

3 Q. By whom are you employed?

4 A. Consumers Energy Company.

5 Q. What is your current position with Consumers Energy?

6 A. I am currently the Director of Employee Benefits.

7 Q. What are your responsibilities as Director of Employee Benefits?

8 A. I am responsible for design, implementation and administration of the Company's retirement
9 benefit and insurance benefit plans for employees and retirees. I also have responsibility for
10 administration of the Company's self-insured workers compensation program and the
11 educational assistance program.

12 In the retirement benefits area, the Company contributes to the cost of the Pension
13 Plan, the Defined Company Contribution Plan (DCCP) and the 401(k) Savings Plan. The
14 Company also contributes to the Defined Benefit and Defined Contribution Supplemental
15 Executive Retirement Plans for certain higher pay employees. My responsibilities for these
16 benefit plans include the design and implementation of competitive, cost-effective, quality
17 plans that will attract and retain qualified employees to serve customers. These plans are
18 designed to provide a portion of an employee's retirement income along with the employee's
19 social security benefits and personal savings.

20 In the insurance benefits area, the Company contributes to the cost of these insurance
21 benefits plans - health care (medical/prescription drug/dental including health care flexible
22 spending accounts (HCFSA)), life insurance, and long-term disability (LTD) insurance. Like
23 the retirement plans, my responsibilities for these health care and insurance benefit plans
24 include the design and implementation of competitive, cost-effective, quality plans for
25 employees and retirees of the Company that help attract and retain qualified employees to

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1 serve customers. In addition to these plans, I have responsibility for several additional
2 benefit plans offered to employees by the Company at group discounted rates, which require
3 the employee to pay the full cost of the coverage elected. These voluntary plans include
4 24-hour accident insurance, health care and dependent care flexible spending accounts, vision
5 insurance, dependents term life insurance and long-term care insurance. These insurance
6 benefit plans also help attract and retain qualified employees to serve customers as these
7 plans help protect employees and their families from significant financial loss in a number of
8 areas.

9 Q. What is your formal educational experience?

10 A. I graduated from the University of Michigan in Ann Arbor in 1977 with a Bachelor of
11 Business Administration Degree. In 1987, I graduated from the University of Michigan -
12 Flint, earning a Master of Business Administration Degree with High Distinction. Since
13 joining Consumers Energy's insurance benefits area in 1989, I have successfully completed a
14 number of benefits certification courses through World at Work (formerly American
15 Compensation Association) and obtained a Certificate in Benefits Administration.

16 Q. Would you please describe your previous work experience?

17 A. On May 23, 1977, I began my career at Consumers Power Company as a Human Resources
18 Advisor in the Grand Rapids Service Center. In 1979, I accepted additional responsibility as
19 the Human Resources Administrator in the Company's Cadillac District. This was a
20 generalist Human Resources role, offering independent work responsibility for
21 150 employees in the Cadillac, Prudenville, Clare and Big Rapids energy distribution
22 headquarters.

23 In 1982, I became the Human Resources Supervisor in the Company's Saginaw
24 office of the Central Region. I supervised the Saginaw office operation staff in this generalist
25 role and provided leadership and support to other Central Region offices as needed. My

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1 responsibility in Saginaw covered human resources responsibilities for over 600 employees
2 in the Region.

3 I became the Insurance Benefits Supervisor for the Company in 1989 and moved to
4 the corporate office in Jackson. In 1994, I became the Director of Insurance Benefits with
5 responsibility for health care, other insurance programs and the relocation plan of the
6 Company for all active and retired employees. In June of 2003, I became the Director of
7 Employee Benefits for the Company and assumed responsibility for the retirement benefits
8 plans (pension, defined company contribution and savings plans) and the workers
9 compensation program.

10 Q. Are you a member of any professional societies or trade associations?

11 A. Yes, I am a member of World at Work. World at Work is an international professional
12 association dedicated to knowledge leadership in compensation, benefits and total rewards. I
13 am also a member of the International Foundation for Employee Benefits.

14 I am a current member of the Michigan Chamber of Commerce Health and Human
15 Resources Committee, having chaired this committee for a two-year period during my
16 membership. This Committee deals with health and human resources policy and legislation
17 in the State from a business perspective. I am also currently on the Board of Directors for the
18 Michigan Purchasers Health Alliance (MichPHA). This Alliance is an association of
19 employers in southeast Michigan that collaborate to improve health care quality and control
20 health care cost among member companies.

21 I serve on the Blue Cross Blue Shield Employer Advisory Board, providing input and
22 advice to the Blues concerning present and future health care related programs and
23 opportunities. In addition, I am the Senior Benefits Representative for our Company in the
24 HR Policy Association. The HR Policy Association is a group of over 330 chief human
25 resources (HR) officers from the largest corporations in the US employing over 20 million

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1 individuals and whose focus is on HR policy and practices including employee benefits. I
2 also represent our Company as a member of the National Business Group on Health
3 (NBGH), an association of over 340 mostly large employers who provide health coverage to
4 over 50 million individuals. NBGH represents the national voice of large employers
5 dedicated to finding innovative and forward-thinking solutions to the nation's most important
6 health care issues.

7 Q. What is the purpose of your testimony?

8 A. The purpose of my testimony is to provide support for the Company's costs related to the
9 electric business portion of pension, defined company contribution, supplemental executive
10 retirement, savings, health care, life insurance and long-term disability insurance (LTD)
11 plans provided to its active employees and retirees. In Part I of my testimony I will address
12 the retirement benefits plans. In Part II of my testimony I will address health care, life
13 insurance, and long-term disability plans. In Part III of my testimony I will discuss the
14 Company's request in this case for a pension equalization mechanism and an OPEB
15 equalization mechanism.

16 Q. Are you sponsoring any exhibits?

17 A. Yes, I am sponsoring Exhibit A-31 (HBK-1) - Summary of Benefits O&M Expense for the
18 Years 2011-2013 - Electric Portion.

19 Q. Was this exhibit prepared by you or under your supervision?

20 A. Yes.

21 Q. Please describe Exhibit A-31 (HBK-1) - Summary of Benefits O&M Expense for the Years
22 2011-2013 - Electric Portion.

23 A. Exhibit A-31 (HBK-1) summarizes 2011 through 2013 electric operating and maintenance
24 (O&M) expenses for the Company's retirement and insurance benefit plans offered to
25 employees and retirees. On this Exhibit, column (a) provides a program description of the

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1 O&M expense category. Column (b) provides the 2011 actual expense for each plan.
2 Column (c) provides the projected expense in 2012 for each plan. Column (d) provides the
3 projected expense for 2013 for each plan. Column (e) provides a source reference for the
4 expense.

5 **I. RETIREMENT BENEFITS PLANS**

6 Q. Which retirement benefits are you addressing in this section of your testimony?

7 A. I am addressing the Pension Plan, Defined Benefit Supplemental Executive Retirement Plan
8 (DB SERP), Defined Company Contribution Plan (DCCP), Defined Contribution
9 Supplemental Executive Retirement Plan (DC SERP), and 401(k) Employees' Savings Plan
10 (ESP). These expenses are shown on Lines 1, 2, 3, 4 and 5 of Exhibit A-31 (HBK-1) -
11 Summary of Benefits O&M Expense for the Years 2011-2013 - Electric Portion. I am
12 addressing active health care/life insurance/long term disability and retiree health care and
13 life insurance later in my testimony.

14 Q. How are the Pension Plan, DB SERP, DCCP, DC SERP and ESP expenses that are common
15 to electric and gas operations allocated to the electric portion of the business?

16 A. Expenses common to both the electric and gas operations associated with the Pension Plan,
17 DB SERP, DCCP, DC SERP and ESP are allocated on the basis of the relationship of
18 employee labor dollars charged to electric operations compared to the labor dollars charged
19 in both electric and gas operations. These allocations are made by the Accounting
20 Department. The electric portion of the O&M expense for these plans is shown on Exhibit
21 A-31 (HBK-1) - Summary of Benefits O&M Expense for the Years 2011-2013 - Electric
22 Portion.

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1 **Pension Plan**

2 Q. Would you please explain line 1 of your Exhibit A-31 (HBK-1) - Summary of Benefits O&M
3 Expense for the Years 2011-2013 - Electric Portion, which begins with \$40,657,000 in 2011?

4 A. Exhibit A-31 (HBK-1) shows the actual 2011 O&M pension expense for the Pension Plan
5 and the projected pension expenses for 2012 and 2013 attributable to the electric portion of
6 the utility operations. These expenses are shown before any Pension Equalization
7 Mechanism (or pension tracker) adjustments are made.

8 Q. How does the Company determine its expense for the Pension Plan?

9 A. The Pension Plan expense is determined using actuarial analysis that is performed in
10 accordance with Accounting Standards Codification (ASC) 715, formerly known as
11 Statement of Financial Accounting Standards (FAS) 87. Consumers Energy follows
12 Generally Accepted Accounting Principles (GAAP) for its financial statements. Under the
13 provisions of GAAP, ASC 715 describes the methodology and assumptions required to
14 properly calculate and account for pension expense. The calculations required by the
15 accounting standards are performed annually by Consumers Energy's actuary, Aon Hewitt,
16 using information specific to the Company's Pension Plan. In addition, the actuarial
17 assumptions are reviewed by the Company's auditors to insure consistency with GAAP.

18 ASC 715 requires an annual determination of pension expense. Expense is
19 determined based on actuarially reviewed employee census data, the plan provisions, plan
20 assets and certain other actuarial assumptions. Year-end disclosure information is also
21 produced, based on these accounting standards, to show a reconciliation of plan assets and
22 liabilities at the end of the Company's fiscal year.

23 Q. What are the components of the annual pension expense under ASC 715?

24 A. There are four components of the expense: (1) service cost; (2) interest cost; (3) expected
25 return on plan assets; and (4) amortization of gains or losses, prior service cost and any

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1 transitional amounts. The plan's service cost represents the value of the benefits earned
2 during the year. This is determined individually for each participant based on his/her specific
3 employee demographics. The interest cost represents interest on the plan's liabilities due to
4 the passage of time. All future benefits are discounted back to the valuation date based on a
5 discount (interest) rate assumption. The discount rate used reflects the interest rate
6 coincident with economic conditions at the time the expense is being determined. There is
7 also an assumption made for the expected earnings or return on plan assets. The expected
8 return on plan assets each year reduces the plan's annual expense. The expected return
9 assumption is reviewed periodically by the plan's actuary and the Company and is intended
10 to be a long-term assumption based on the best estimate of the long term expected investment
11 earnings of the plan assets. The last component of plan expense is amortization of various
12 plan experiences that were not anticipated by the plan's actuarial assumptions. For example,
13 plan experience gains or losses and any plan design changes would be amortized and
14 included as a part of this component of plan expense. The amortization can be either positive
15 or negative.

16 In order to calculate the plan's total pension benefit obligation and annual ASC 715
17 expense, the actuary uses a number of assumptions including a discount rate, mortality table,
18 salary change, expected return on plan assets and expected future contributions needed to
19 avoid at risk status under the Pension Protection Act (PPA). The assumptions used by the
20 actuary are determined by the Company each year and reviewed by the Company's auditors.

21 Q. Please describe the development of the Pension Plan expense shown on line 1 of Exhibit
22 A-31 (HBK-1), which begins with \$40,657,000 for 2011.

23 A. Each of the annual pension expense levels shown on line 1 for the electric utility is based
24 upon Aon Hewitt's actuarial determination of the plan's total expense for that year in
25 accordance with ASC 715 and also includes plan administration fees. The Consumers

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1 Energy pension expense determined by Aon Hewitt plus administration fees and Pension
2 Benefit Guarantee Corporation (PBGC) premiums are allocated to the electric and gas
3 portions of the utility using the accounting department methodology described earlier. This
4 allocation resulted in the actual electric utility O&M expense for pensions of \$40,657,000 in
5 2011. For 2012 and 2013, Aon Hewitt has projected the Company's ASC 715 pension
6 expense based upon a series of specific assumptions for each year. The electric utility
7 portions of the ASC 715 O&M pension expense plus projected administration fees and
8 PBGC premiums for 2012 and 2013 are included on line 1. For 2012, the electric utility's
9 projected O&M pension expense is \$40,219,000. For 2013, the electric utility's portion of
10 the projected O&M pension expense is \$47,362,000.

11 Q. Did the Company make any cash contributions to the Pension Plan in 2011?

12 A. The Company made cash contributions to the Pension Plan totaling \$250 million in 2011.
13 These contributions were made to ensure the Plan's funding percentage level continues to
14 increase as required under the PPA and to avoid benefit restrictions from at-risk status being
15 placed on the Plan because the Plan's funded percentage status has fallen below an 80%
16 funded level. In addition, these cash contributions start to earn returns as soon as they are
17 placed in the Pension Plan and this helps to reduce the Plan's prospective ASC 715 pension
18 expenses. This, in turn, helps provide a lower cost for this Plan to customers of the
19 Company.

20 Q. Does the Company intend to make any cash contributions to the Pension Plan during 2012
21 and 2013?

22 A. Due to the large dollar contributions made to the Pension Plan in 2010 (\$375 million) and
23 2011 (\$250 million), no contributions to the Pension Plan are required or expected for 2012
24 or 2013. However, the actual amount of contributions in 2012 and 2013 will depend upon
25 future decisions of the Company regarding funding policy; the PPA interest rate approach

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1 used; the future value of plan assets and liabilities; and any potential legislative guidance or
2 changes.

3 Q. Why is the pension expense declining slightly in 2012?

4 A. There are a number of things occurring in 2012 that impact the pension expense, both
5 positively and negatively, but when combined result in a small reduction to net pension
6 expense. The annual expense for the Pension Plan as projected by Aon Hewitt actually
7 decreases in 2012 due primarily to the large contributions the Company made to the Pension
8 Plan in 2010 (\$375 million) and 2011 (\$250 million) and the anticipated earnings these large
9 contributions provide to the Plan, which reduces the projected pension expense. In addition,
10 the salary change assumption used to calculate pension expense was reduced to 3.5% from
11 4.0% beginning in 2012, which further reduces the pension expense projection for 2012.

12 On the other hand, there are several offsetting factors to this decrease in 2012 pension
13 expense. The discount rate used for 2012 projected pension expense estimate is reduced to
14 4.9% from the 5.4% discount rate used for 2011. This change increases the pension expense
15 projection. In addition, the three-tier corporate yield curve interest rate segments used to
16 calculate single sum payments under the Pension Plan also continue to move lower, adding to
17 pension expense. Finally, the expected return on assets assumption was reduced to 7.75%
18 (from 8%) to calculate 2012 projected pension expense which also increases this expense.
19 However, in spite of these components working to increase pension expense in 2012, the
20 large pension contributions and reduced salary change assumption offset these increases,
21 resulting in the projected pension expense declining slightly in 2012.

22 Q. Why does pension expense increase for 2013?

23 A. The 2013 pension expense increase is primarily due to the reduction in the discount rate
24 assumption from 4.9% in 2012 to 4.25% in 2013 based upon the market conditions present at
25 the time the expense was projected. In addition, legislated funding and lump sum interest

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1 rates used by the plan also continue to fall along with projected pension plan returns, both
2 increasing 2013 projected pension expense.

3 It is noteworthy that no benefit changes have been made to the Pension Plan since
4 September 1, 2005, when the Pension Plan was closed to new hires and the Defined
5 Company Contribution Plan (DCCP) was implemented for new hires. The increases in
6 pension expense created by the assumption changes are moderated by the closure of the
7 Pension Plan to new hires as of September 1, 2005. In addition, pension liabilities and
8 expenses are moderating overall as many participants are retiring or leaving and commencing
9 their benefits, which reduces the liability and associated expense over time. Liability and
10 expense will continue to diminish (presuming no change in the market assumptions) until
11 there are no longer any employees or retirees covered by the defined benefit Pension Plan.
12 The changes in the projected pension expense estimates in 2012 and 2013 are primarily the
13 result of economic conditions (asset returns and interest rates) external to the Pension Plan
14 over which the Company has no control.

15 **Defined Benefit Supplemental Executive Retirement Plan (DB SERP)**

16 Q. Would you please explain line 2 of your Exhibit A-31 (HBK-1) - Summary of Benefits O&M
17 Expense for the Years 2011-2013 - Electric Portion, which begins with \$3,327,000 in 2011?

18 A. Exhibit A-31 (HBK-1) shows the actual 2011 O&M expense for the DB SERP and the
19 projected DB SERP expenses for 2012 and 2013 attributable to the electric portion of the
20 utility operations. Of the top six officers identified by the Securities and Exchange
21 Commission proxy rules, four officers are covered by this DB SERP. Their DB SERP
22 expenses are excluded from the DB SERP expenses shown on line 2.

23 Q. Please provide a general description of the DB SERP.

24 A. The DB SERP provides an amount substantially equal to the difference between the amount
25 that would have been payable under the Pension Plan in the absence of legislation limiting

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1 pension benefits and earnings that may be considered in calculating pension benefits, and the
2 amount actually payable under the Pension Plan. Additionally, officers are provided with an
3 additional year of preference service credit for each year of actual service to a combined total
4 of 20 years of service for determining available preference service. The combined maximum
5 years of preference and actual service allowed for calculating DB SERP benefits is 35 years.
6 The 35-year accredited service maximum is the same as the accredited service maximum
7 used for calculating the non-SERP defined benefit Pension Plan benefits. Earnings used in
8 calculating DB SERP benefits include any Employee Incentive Compensation Plan (EICP)
9 awards (annual incentive payments). Any benefit calculated under the Pension Plan is
10 subtracted from the benefit calculated under the DB SERP. DB SERP participants have an
11 unsecured contractual commitment from the Company to receive the annuity due from the
12 DB SERP. This benefit is payable at the later of age 55 or separation from service. Any
13 employees hired or promoted to an eligible position on or after April 1, 2006, are not eligible
14 to participate in the DB SERP. As of that date the DB SERP was replaced by the DC SERP.
15 I discuss the DC SERP later in my testimony.

16 Q. Who is eligible for the DB SERP?

17 A. Officers and certain director level employees hired before April 1, 2006, are eligible for
18 DB SERP. These types of benefits are reasonable and customary in the utility industry for
19 officers and director level employees covered by defined benefit Pension Plans and are
20 consistent with best practices for providing employee benefits. Offering supplemental
21 retirement benefits to officers and director level employees is necessary in order to have
22 competitive benefits that will attract and retain qualified personnel.

23 Q. How does the DB SERP benefit customers?

24 A. The DB SERP is a competitive executive benefit designed to attract, retain and motivate
25 qualified, key management personnel for the Company. It is in the interest of the Company

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1 and its customers to have competitive benefits. This benefit is structured in a way that covers
2 the executive's competitively based compensation above the legislated limits for the defined
3 benefit Pension Plan and provides a defined benefit for these earnings just like the qualified
4 Pension Plan does for all employees it covers. DB SERP also adds earnings coverage for the
5 executive's annual incentive payment, an "at risk" component. This "at-risk" benefit
6 motivates and supports decisions that are in the short-term and long-term best interest of
7 customers. This benefit rewards executives who focus on a number of areas important to the
8 customer including safety, system reliability, improved productivity, competitive pricing,
9 quality customer service, and financial health of the Company.

10 Q. How does the Company determine its expense for the DB SERP?

11 A. The DB SERP expense is determined in essentially the same manner described earlier for the
12 Pension Plan expense. To determine the expense, actuarial analysis is performed annually in
13 accordance with Accounting Standards Codification (ASC) 715 by Consumers Energy's
14 actuary, Aon Hewitt, using information specific to the Company's DB SERP. The expense is
15 comprised of service cost, interest cost and amortization of unrecognized amounts.

16 In order to calculate the DB SERP obligation and annual ASC 715 expense, the
17 actuary uses a number of assumptions including a discount rate and mortality table that are
18 the same as used for the Pension Plan. A salary increase assumption is also used to reflect
19 expected pay and incentive compensation increases. Because the DB SERP is a non-
20 qualified plan, it is not considered funded so no expected return on assets assumption is used.
21 The assumptions used by the actuary are determined by the Company each year and reviewed
22 by the Company's auditors.

HERBERT B. KOPS
DIRECT TESTIMONY

1 Q. Please describe the development of the DB SERP expense shown on line 2 of Exhibit A-31
2 (HBK-1), which begins with \$3,327,000 for 2011.

3 A. Each of the annual DB SERP expense levels shown on line 2 for the electric utility is based
4 upon Aon Hewitt's actuarial determination of the plan's total expense for that year in
5 accordance with ASC 715 and also includes plan administration fees. The Consumers
6 Energy DB SERP expense determined by Aon Hewitt plus administration fees are allocated
7 to the electric and gas portions of the utility using the accounting department methodology
8 previously described. This allocation resulted in the actual electric utility O&M expense for
9 DB SERP of \$3,327,000 in 2011. For 2012 and 2013, Aon Hewitt has projected the
10 Company's ASC 715 DB SERP expense based upon a series of specific assumptions for each
11 year. The electric utility portions of the ASC 715 O&M DB SERP expense plus projected
12 administration fees for 2012 and 2013 are included on line 2. For 2012, the electric utility's
13 projected O&M DB SERP expense is \$3,820,000. For 2013, the electric utility's portion of
14 the projected O&M DB SERP expense is \$4,056,000. DB SERP expenses for the top four
15 officers covered by DB SERP are excluded from the expenses shown on line 2.

16 Similar to the Pension Plan closure to new hires on September 1, 2005, the DB SERP
17 was closed to new participants hired or promoted on or after April 1, 2006, when a defined
18 contribution SERP (DC SERP) was put in place. No benefit changes have been made to the
19 DB SERP since the closure date. The increases in DB SERP expense created from the
20 assumption changes (e.g. discount rate decrease) are moderated by the fact that the Company
21 stopped adding new participants to the DB SERP effective April 1, 2006. In addition, DB
22 SERP liabilities and expenses are expected to moderate overall as participants retire or leave
23 and commence their benefit, which reduces the liability and associated expense over time.
24 Liability and expense will continue to diminish (presuming no change in the market
25 assumptions) until there are no longer any employees or retirees covered by the DB SERP.

HERBERT B. KOPS
DIRECT TESTIMONY

1 The increases in the DB SERP expense calculation in 2012 and 2013 are primarily the result
2 of economic conditions (interest rates) external to the DB SERP over which the Company
3 has no control.

4 **Defined Company Contribution Plan (DCCP)**

5 Q. Does the Company provide an alternative qualified benefit plan to the closed Pension Plan
6 for employees hired on and after September 1, 2005?

7 A. Yes. In order to remain competitive in the area of a benefits package that attracts and retains
8 qualified and talented employees for the benefit of the customer, the Company replaced the
9 Final Average Pay and Cash Balance versions of the qualified defined benefit Pension Plan
10 with the qualified Defined Company Contribution Plan (DCCP) for all newly hired
11 employees on and after September 1, 2005.

12 Q. Please provide a general description of the DCCP.

13 A. The DCCP provides an employer funded cash contribution of six percent of the employee's
14 base pay to the Employees' Savings Plan (ESP). No employee contribution is required to
15 receive the employer contribution. All employees hired on and after September 1, 2005
16 participate in the DCCP as part of their retirement benefit package.

17 Q. Are there any employees included in the DCCP that were hired before September 1, 2005?

18 A. Yes. Those employees who were hired between July 1, 2003, and August 31, 2005, and were
19 provided coverage under the Cash Balance version of the defined benefit Pension Plan
20 became participants in the DCCP as of September 1, 2005. As of September 1, 2005, for this
21 specific group of employees, additional pay credits under the Cash Balance version of the
22 defined benefit Pension Plan were discontinued.

HERBERT B. KOPS
DIRECT TESTIMONY

1 Q. Will the Cash Balance version of the defined benefit Pension Plan accept any new employees
2 as participants?

3 A. No. As with the Final Average Pay defined benefit Pension Plan, the Cash Balance version
4 of the defined benefit Pension Plan now has a finite group of participants that, over time, will
5 diminish until there are no longer any employees or retirees covered under this Plan.

6 Q. Would you please explain line 3 of your Exhibit A-31 (HBK-1) - Summary of Benefits O&M
7 Expense for the Years 2011-2013 - Electric Portion for the DCCP, which begins with
8 \$2,691,000?

9 A. Line 3 represents the electric operations O&M expense related to the DCCP. The actual
10 electric operations expense for this Plan in 2011 was \$2,691,000 as shown in column (b).
11 Column (c) shows the projected 2012 electric DCCP expense of \$3,225,000. Then,
12 column (d) shows the projected electric DCCP expense of \$3,841,000 for 2013. Projected
13 expenses for 2012 and 2013 are based upon the Company continuing to hire employees at a
14 higher than usual rate due to a larger number of expected retirements.

15 Currently, all new hires begin receiving a 6% of base wage Company contribution to
16 the DCCP after 90 days of employment instead of participating in the more costly defined
17 benefit Pension Plan. The DCCP expense will continue to grow based upon the expectation
18 that all newly hired employees participate in this DCCP Plan and not the Pension Plan.
19 Offsetting this increase in DCCP expense is a declining defined benefit Pension Plan expense
20 as the group covered by the Pension Plan is now finite in size and will reduce in numbers
21 with the passage of time.

HERBERT B. KOPS
DIRECT TESTIMONY

1 Q. As a result of the revised eligibility requirements for participation in the Final Average Pay
2 defined benefit Pension Plan or the Cash Balance version of the defined benefit Pension Plan,
3 is it correct to say that all new hire employees starting with September 1, 2005, and after will
4 receive their retirement benefits through plans that are referred to as defined contribution
5 type plans?

6 A. Yes. The primary plans that will provide monetary benefits to this group of employees upon
7 retirement are the DCCP and the Employees' Savings Plan (ESP).

8 Q. Why is the Company's projected DCCP expense increasing in 2012 and 2013?

9 A. This expense is increasing primarily because every new hire into the Company is now
10 covered by the DCCP at a 6% of base wage contribution (rather than the more expensive
11 defined benefit Pension Plan) and also due to the fact that the Company continues to hire
12 employees at a higher than usual rate to replace current and future retirements.

13 **Defined Contribution Supplemental Executive Retirement Plan (DC SERP)**

14 Q. You stated earlier in your testimony that the DB SERP was replaced by the DC SERP for
15 employees hired or promoted to an eligible position on and after April 1, 2006. Why was
16 this change made?

17 A. In order to remain competitive in the area of an executive benefits package that attracts and
18 retains qualified and talented employees for the benefit of the customer, the Company
19 replaced the DB SERP with a DC SERP for officers and eligible director level positions for
20 all hires and promotions made on or after April 1, 2006. This change from DB SERP to
21 DC SERP was made to coordinate with the qualified plan change to the DCCP from the
22 defined benefit Pension Plan. This change now provides all defined contribution retirement
23 plans for eligible officers and certain director level employees going forward as no additional
24 employees will be added to the DB SERP.

HERBERT B. KOPS
DIRECT TESTIMONY

1 Q. Please provide a general description of the DC SERP.

2 A. The DC SERP was established by the Company as of April 1, 2006, replacing the DB SERP.
3 Under the DC SERP the Company provides an amount equal to 5%, 10% or 15% (depending
4 upon the employee's salary grade) of the eligible employee's earnings which exceed the
5 legislated earnings limit plus any award under the EICP (annual incentive payments).
6 DC SERP contributions are transferred to an external record keeping vendor at the time the
7 Company makes a contribution. The contributions are invested in a family of mutual funds
8 available to the DC SERP at the direction of the participant. Earnings or losses are based on
9 the rate of return of the mutual fund(s) selected by the participant. Although the DC SERP is
10 funded, the participants have an unsecured contractual commitment from the Company to
11 receive the amount due under the plan. The assets of the DC SERP are owned by the
12 Company. Full vesting under the DC SERP occurs at age 62 with a required minimum of
13 five years of service. Vesting is on a pro-rata basis for years prior to age 62.

14 Q. How does the DC SERP benefit customers?

15 A. Like the DB SERP, the DC SERP is a competitive executive benefit aimed to attract, retain
16 and motivate qualified, key management personnel for the Company. This benefit is
17 structured in a way that covers the executive's competitively based compensation above the
18 legislated limits for the DCCP and provides a benefit for this compensation like the qualified
19 DCCP does for all employees it covers. DC SERP also adds earnings coverage for the
20 executive's annual incentive payment, an "at risk" component. This "at-risk" benefit
21 motivates and supports decisions that are in the short-term and long-term best interest of
22 customers. This benefit rewards executives who focus on a number of important areas
23 important to the customer including safety, system reliability, improved productivity,
24 competitive pricing, quality customer service and financial health of the Company.

HERBERT B. KOPS
DIRECT TESTIMONY

1 Q. Would you please explain line 4 of your Exhibit A-31 (HBK-1) - Summary of Benefits
2 O&M Expense for the Years 2011-2013 - Electric Portion for the DC SERP, which begins
3 with \$91,000?

4 A. Line 4 represents the electric operations O&M expense related to the DC SERP. The actual
5 electric operations expense for this Plan in 2011 was \$91,000 as shown in column (b).
6 Column (c) shows the projected 2012 electric DC SERP expense of \$103,000. Then,
7 column (d) shows the projected electric DC SERP expense of \$134,000 for 2013. Of the top
8 six officers identified by the Securities and Exchange Commission proxy rules, two officers
9 are covered by this DC SERP. Their DC SERP expenses are excluded from the DC SERP
10 expenses shown on line 4.

11 Q. Is it correct to say that all newly hired officers and SERP eligible directors since April 1,
12 2006, will receive retirement benefits through plans that are referred to as defined
13 contribution type plans?

14 A. Yes. The primary plans that will provide retirement benefits to this group of employees upon
15 retirement are the DCCP, DC SERP and the Employees' Savings Plan (ESP).

16 **401(k) Employees' Savings Plan (ESP)**

17 Q. Please explain briefly how the 401(k) Employees' Savings Plan (ESP) works.

18 A. The ESP is a 401(k) type retirement savings program funded by employee and employer
19 contributions. A portion of employee contributions are matched by Consumers Energy
20 Company. The Company matches 60% of the first 6% of employee contributions.
21 Employee contributions beyond 6% are not matched by the Company. Consumers' expense
22 includes the Company matching contribution and the payments made to Fidelity for
23 administration of the program.

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DIRECT TESTIMONY

1 Q. Would you please explain line 5 of your Exhibit A-31 (HBK-1) - Summary of Benefits
2 O&M Expense for the Years 2011-2013 - Electric Portion for the ESP which begins with
3 \$6,418,000?

4 A. Line 5 represents the Company's electric operations expense related to the 401(k)
5 Employees' Savings Plan (ESP). In 2011, the actual electric utility O&M expense for the
6 ESP was \$6,418,000. For 2012, the O&M expense is projected to be \$6,632,000. For 2013,
7 the electric utility O&M expense projected for the ESP is \$6,814,000.

8 Q. Why does the ESP expense increase in 2012 and 2013?

9 A. Other than the ESP increasing because wages (and matching dollars) increase, the
10 primary reason for the increases for 2012 and 2013 in the ESP is related to a change in
11 the OM&C and VCC union contracts negotiated concerning access-only retiree health
12 care and a new Company contribution to these employees' ESP. All new OM&C and
13 VCC hired by the Company beginning September 1, 2010, may become eligible for
14 access-only retiree health care requiring 100% premium contribution from the retiree and
15 no Company subsidy. To encourage and assist these new OM&C and VCC employees to
16 save for retiree health care expenses, the Company is contributing \$20/week and a one-
17 time \$1,200 contribution after one year of service to each new union employee's 'retiree
18 health care account', established in the ESP beginning January 2011. Restrictions on use
19 of these funds are placed upon the account so the money can accumulate in the account over
20 the employee's career. These funds become available to the employee during retirement for
21 health care expenses. While this retiree health care account expense in the ESP will continue
22 to grow as new union employees are hired, the Company's retiree health care liability and
23 expense is \$0 for these new hires. The Company's liability and expense will decrease over
24 time because the employee group covered by Company-subsidized retiree health care plans is

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1 now finite in size and will decrease with the passage of time. There is no liability that
2 requires expensing as in the case of a defined benefit plan. The only expense related to these
3 retiree health care accounts in the ESP is the matching contribution provided by the
4 Company.

5 OM&C and VCC union employees hired prior to September 1, 2010,
6 Steelworker's union employees and nonunion employees do not receive this retiree
7 health care account contribution.

8 Q. How is the ESP expense that is common to electric and gas operations allocated to the
9 electric portion of the business?

10 A. The ESP expense is allocated in the same way as discussed previously for the Pension Plan
11 and DCCP expenses using employee labor dollars.

12 Q. Is the ESP employer matching program important to attracting and retaining employees?

13 A. Yes.

14 Q. Please explain why the ESP employer matching program is important to attract and retain
15 employees.

16 A. The ESP employer match for Consumers Energy employees serves a number of important
17 purposes. The ESP is a defined contribution plan. The match helps provide a competitive
18 benefits package that enables the Company to attract and retain qualified and talented
19 employees, which directly and indirectly serve and benefit the customer. Defined
20 contribution savings plans with employer matching provisions are offered by the vast
21 majority of Fortune 500 companies located across the country, including Consumers Energy
22 in Michigan. These plans have become a core benefit offering that greatly helps attract and
23 retain qualified employees. In fact, a Fidelity Investments survey of 1,000 working and
24 retired defined contribution plan participants conducted in February 2011 indicated that 90%

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DIRECT TESTIMONY

1 of current workers surveyed said defined contribution plans influence their choice of
2 employer. The survey article went on to indicate that the most common reason given by
3 current workers for their enrollment in their defined contribution plan was the employer
4 match, of which 83% of the workers indicated they received some type of employer match
5 when they enrolled. Not offering a savings plan with an employer match feature would be a
6 competitive disadvantage for the Company as it needs to attract a continual flow of qualified
7 new talent to replace retiring workers. The Company also needs to retain current talented
8 workers to avoid expensive turnover costs.

9 While many current employees are covered by the Company's defined benefit
10 Pension Plan and all new hires since September 1, 2005, are covered by only the DCCP, the
11 Pension Plan or DCCP by itself is not designed to fully meet the employees' retirement
12 income needs. The Pension Plan or DCCP is only part of an overall competitive employee
13 retirement package that includes the Pension Plan or DCCP and the contributory ESP with an
14 employer matching contribution - but only for those employees who contribute to their own
15 future retirement benefit through the ESP. The combination of these plans provide a
16 meaningful incentive for employees to do well in their jobs to the benefit of customers
17 because doing so will benefit them with a more financially secure retirement, supplemented
18 by their own personal savings and social security benefits.

19 The ESP employer match also reflects a prudent business practice because it incents
20 employees to create savings for their retirement. The employer match encourages employees
21 to save more when their contributions are matched. Matching contributions offer an
22 immediate, tangible return that employees contributing to the plan can see and appreciate.
23 New employees are automatically enrolled in the ESP due to the importance of starting to
24 save early as a secure retirement will depend significantly on how much the employee
25 contributes to their ESP account. Employer matching contributions and automatic

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1 enrollment in the ESP are important features that help create savings. These features are
2 important because most retirement studies show that employees, including Consumers
3 Energy employees, do not save enough and need to save more for their retirement than they
4 currently do as costs in retirement continue to increase. Longer life expectancies are leading
5 to longer retirements which require more savings. Additionally, other costs such as health
6 care are expected to continue to increase for retirees. The employer match encourages
7 employees to plan and save for retirement. The ESP provides an excellent vehicle to help
8 employees achieve a more self-sufficient and independent retirement.

9 The bottom line is that savings plans with a match are very much available from
10 Michigan employers as well as from other utility company employers that Consumers
11 Energy competes with for employee talent. It is necessary to continue providing this highly
12 visible, competitive benefit to employees of Consumers Energy in order to continue
13 attracting and retaining competent employees needed by the Company, particularly in light
14 of the large number of retirement eligible employees at the Company. Attracting qualified
15 employees and retaining this talent maximizes the efficiency of the Company's labor force
16 and reduces costly turnover. Retaining trained, experienced and motivated employees works
17 very much to the customers' benefit.

18 Q. Is the ESP employer match "discretionary"?

19 A. It is not discretionary for union employees. A provision in the Working Agreement ratified
20 in 2005 with OM&C and VCC union employees assured these employees that the match
21 would not be suspended during their five-year contract. This provision was renewed in the
22 2010 contracts as part of the final union agreements for these union groups and it is also part
23 of the new Steelworker's union contract effective January 1, 2011. This was an important
24 issue during the last two labor negotiations for these employee contracts, all of which were
25 finally resolved through arms-length bargaining.

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1 With respect to nonunion employees, there is not a similar contractual prohibition
2 against suspension. However, the ESP employer match is part of an overall competitive
3 benefit package and employees depend upon its continuation so they can accumulate savings
4 for retirement. The Company's competitors continue to offer a savings plan match and the
5 Company plans to continue offering the match to compete for new talent and retain current
6 talent for the benefit of the customer. As noted above, it is a benefit that helps the Company
7 attract and retain qualified and talented employees. From a practical standpoint, the
8 Company views the employer match as non-discretionary.

9 Q. Were any changes made to the ESP employer match contribution percentage as a result of
10 the recent 2010 OM&C, VCC or Steelworker's union employee contracts?

11 A. No changes were made to the ESP employer match in the most recent negotiated union
12 contract with OM&C, VCC or Steelworker's employees as this benefit remains competitive
13 with the market. In addition, no changes have been made to the nonunion ESP match for the
14 same competitive reasons.

15 **II. HEALTH CARE, LIFE INSURANCE, AND LONG-TERM DISABILITY**
16 **PLANS**

17 Q. Which insurance benefits are you addressing?

18 A. I am addressing active employee health care (including health care flexible spending
19 accounts (HCFAs)), life insurance, and long-term disability (LTD) plans as well as retiree
20 health care and life insurance plans. These expenses are shown on lines 6 and 7 of Exhibit
21 A-31 (HBK-1) - Summary of Benefits O&M Expense for the Years 2011-2013 - Electric
22 Portion.

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1 Q. Are the expenses for active employee health care (including HCFSAs), life insurance and
2 LTD benefits determined in the same way as expenses for retiree health care and life
3 insurance benefits?

4 A. No. The expenses for active employees are based upon the actual costs for these benefits that
5 have been incurred or are expected to be incurred. The expenses for retirees are determined
6 using actuarial analysis, which is performed by the Company's actuary, in accordance with
7 Accounting Standards Codification (ASC) 715, formerly known as Statement of Financial
8 Accounting Standard (FAS) 106.

9 Q. How were the portions of active employee and retiree health care (including HCFSAs), life
10 insurance and LTD costs allocated to electric operating and maintenance expense
11 determined?

12 A. The portion of the Company's total program expenses attributable to the electric utility have
13 been allocated to the gas and electric utility based upon an annual study by the accounting
14 department of the relationship of the number of employees in the electric utility to the total
15 number of employees in both the electric and gas utility. The amount allocated to the electric
16 utility is allocated between operating and maintenance (O&M) expense and capital expense
17 based upon the accounting department's formula.

18 **Active Health Care (including HCFSAs), Life Insurance and Long-Term Disability**
19 **(LTD)**

20 Q. Please describe the development of the active health care (including HCFSAs), life
21 insurance, and LTD insurance expense levels that are shown on line 6 of Exhibit A-31
22 (HBK-1) - Summary of Benefits O&M Expense for the Years 2011-2013 - Electric Portion,
23 which begins with \$28,500,000 in 2011.

24 A. Line 6 contains electric operations O&M expenses for the Company-subsidized benefit plans
25 for active employees' health care (including HCFSAs), life insurance and LTD insurance.

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1 The primary component of this expense is health care. Life insurance and LTD expense
2 make up a much smaller portion of the expense. In 2011, the Company incurred a combined
3 expense of \$28,500,000 for health care, life insurance and LTD for electric operations. The
4 projected expense for these benefits in 2012 is \$29,509,000 and the projected expense for
5 2013 is \$32,219,000.

6 Q. What factors did you consider in projecting the Company's 2012 and 2013 health care, life
7 insurance and LTD expenses?

8 A. In projecting expected health care cost increases, a number of factors were considered.
9 Primary factors considered included review of national health cost trends survey information,
10 the Company's health carrier's health cost trend expectations and claims experience for the
11 Company, the ages of the Company's workforce, the implementation of the Company's
12 healthy living initiative for employees and retirees, the recent OM&C and VCC union
13 employee contract changes, the reduced headcounts from the voluntary separation programs
14 and layoffs and the impacts of national health care reform.

15 Q. Please explain how these factors were used to determine the Company's health care cost
16 increase?

17 A. To help determine the projected health care cost increases in 2012 and 2013, the Company
18 reviewed health care and consulting firms' market survey information released periodically
19 which projects expected health care cost increases across the country in 2012. National
20 health care cost trends are expected to increase in 2012 over 2011. Recent 2012 health cost
21 surveys by various consulting firms like Aon Hewitt, Segal, Towers Watson,
22 PricewaterhouseCoopers, Buck Consultants and Mercer indicate expected 2012 health care
23 cost increases ranging from 6% to 11%. These 2012 health care cost trends are expected to
24 continue into 2013.

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1 The Company also reviewed its own health care experience with a broad spectrum of
2 experts managing the health plans offered to its employees and retirees. Discussions and
3 analysis occur throughout each year with the Company's health plans (Aetna, Blue
4 Cross/Blue Shield of Michigan, Medco, Priority Health, and Blue Care Network) about
5 expected health care cost increases for Consumers Energy over the next one to two years.
6 Recent discussions and analysis with these health plans indicates a probable increase in
7 health care costs for the Company that will fall within a range of 7% to 10% for both 2012
8 and 2013.

9 While health care trends have moderated somewhat nationally, the Company's health
10 plans indicate that the Company's workforce is older than the average in their plans, and, as a
11 result, has a higher utilization rate of services that is associated with an older covered
12 population. Of the Company's current workforce on December 31, 2011, 62% of employees
13 are over age 45; 47% are over age 50; and 27% are over age 55. The Company understands
14 this aging trend increases its health care costs and has implemented a number of plan changes
15 and programs discussed below to manage and control its rising health care costs. These
16 changes include sharing health care cost increases with employees and retirees, plan design
17 changes which require more cost sharing with participants, education regarding the prudent
18 and informed use of health care benefits as well as the promotion of preventive services and
19 the new healthy living plan designs providing preferred coverage to participants that take
20 steps toward healthier lifestyles to lower overall health costs.

21 The Company also considered the specific changes to the union employees health
22 care plan expenses as a result of the new union agreements and benefit changes that become
23 effective in 2011 and 2012, which are described later in this testimony. While there are very
24 tangible savings in health costs to the Company and its customers as a result of the 2010
25 union agreements, the Company believes a large portion of these savings will be offset by

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1 increased Company costs in 2012 and 2013 from national health care reform requirements,
2 primarily the eligibility expansion for adult children to age 26, payment of cost effectiveness
3 fees, various government reporting requirements and the requirement to provide an
4 increasing number of preventive benefits each year under the health plans but without cost
5 sharing by the participant. In addition, the State of Michigan mandated health benefits for
6 autism and the Michigan Health Insurance Claims Assessment (HICA) will both increase
7 projected costs in 2012 and 2013. However, these added health costs from national health
8 care reform and the State of Michigan mandated changes are expected to be mitigated in the
9 short term by monies the Company has been able to recover under the national health care
10 reform's Early Retiree Reinsurance Program (ERRP). ERRP provides recovery of 80% of
11 claims costs for an early retiree that exceeds \$15,000 in claims, up to \$90,000. ERRP
12 requires that any monies received under this program be returned to the plan for the benefit
13 of all plan participants and the Company. The Company has received monies under this
14 program, and, because the ERRP has stopped making payments as it has reached the
15 \$5 billion fund allocated to the program, the Company plans to use these funds in 2012 or
16 2013 to help control its health cost increase.

17 While national health cost increase survey averages are expected to be in the 6% to
18 11% range for 2012, the Company has also considered the cost impact of its aging, highly
19 skilled workforce and its claims experience on its health care costs. In conclusion, with
20 (1) the annual plan design changes and premium contribution increases for 2012 described
21 later in this document; (2) the new union contracts with added cost sharing in 2012 and 2013;
22 (3) a reduced headcount; (4) the fact that employees and retirees are now participating in an
23 ever expanding health improvement program through benefit design; (5) the promotion of
24 informed consumerism and a healthy lifestyle approach to health that will help to control
25 future health cost increases; (6) the addition of national health care reform requirements; and

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1 (7) ERRP credits, the Company believes it can hold its health care cost increase to about 6%
2 for 2012 and 8% for 2013.

3 Q. What are some of the reasons that health care costs are increasing at a level higher than
4 general inflation?

5 A. There are a number of factors causing a much higher rate of health care inflation than are
6 reflected in the general Consumer Price Indexes (CPIs). Health care costs are expected to
7 continue rising during the next several years due to an aging population living longer,
8 additional utilization of services, price increases for services, new medical technology, cost
9 shifts from government plans, mandated benefits coverage, rising provider malpractice
10 premiums, new taxes on health claims and rapidly escalating prescription drug prices
11 including high prices for new, expensive specialty drugs. In addition, recently enacted
12 national health care reform will increase company health care costs in the near term as a
13 result of eligibility expansions (e.g. adult children to age 26), mandated benefits, removal of
14 annual limits, additional taxes and penalties and more government shifting of costs through
15 Medicaid expansion. These factors are all outside the control of Consumers Energy. Even
16 with all the employee and retiree health plan design and premium contribution changes made
17 annually by the Company over a number of years including the move to healthy living plan
18 designs, health care costs for the Company are still expected to continue increasing annually
19 at a rate two to three times that of general CPI inflation. The assumption that health care
20 costs will only increase at the general rate of inflation has not been the actual experience for
21 many years and is not expected in the foreseeable future. In addition, national health care
22 reform adds a significant number of new benefit mandates, fees, penalties and
23 compliance/reporting requirements in its early years, which will add to health care cost
24 projections.

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1 Based on consideration of these factors, active employee health care cost increases
2 are expected to increase about 6% in 2012 and 8% for 2013. Using a lower general inflation
3 rate for health care costs would significantly understate projected active employee health care
4 costs and is inappropriate.

5 Q. Are large increases in health care costs being experienced both locally and nationally?

6 A. Yes. Both local and national health care costs continue to increase at rates much greater than
7 general CPI inflation as previously noted.

8 Q. Are the significant increases in health care costs limited to active employees?

9 A. No. Health care costs are also increasing at a rate higher than the general CPI inflation for
10 retirees for the same reasons cited earlier. In fact, retiree expenses are generally increasing at
11 higher rates because of retirees older ages and the resulting increases in utilization. The
12 projected increases for active employee health care, like projected increases for retiree health
13 care, are substantial, reasonably expected to occur, and largely beyond the control of the
14 Company.

15 Q. Please describe the development of the expense levels for active employee life insurance and
16 long-term disability costs included in line 6 of Exhibit A-31 (HBK-1).

17 A. A 4% increase in cost was used to develop the projected expenses for life insurance and long-
18 term disability insurance for 2013. In other words, 2013's projected expense for these
19 benefits to the Company will be 4% greater than the projected expense for these benefits in
20 2012 (not including any experience refund paid from 2012). The 4% increase in these
21 expense estimates is reasonable as both life insurance and long-term disability premium costs
22 are based on wage and salary levels and changes to this coverage throughout the year. The
23 4% annual increase represents the normal, expected merit increase in salaries/wages, salary
24 adjustments made for job changes and promotions. It also accounts for the increases in
25 coverage employees elect in life insurance and long-term disability coverage from year to

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1 year during the annual enrollment process as well as overall life and/or LTD plan premium
2 rate increases received from the insurance company due to the actual experience within the
3 plan.

4 For 2012, the new OM&C and Zeeland Plant Steelworker's union employee contracts
5 provide a Company-paid long-term disability (LTD) benefit plan to cover 50% of base wage
6 with an employee buy-up option to purchase 60% of base wage coverage. The Company
7 believes the additional cost for this LTD benefit program, included in the projected 2012
8 LTD expense, will be offset by the reduced cost of eliminating the self-insured short-term
9 disability payments made by the second sick leave bank contained in the previous OM&C
10 union contract. This is expected to result in no additional overall Company expense due to
11 the introduction of the LTD benefit for these union employees.

12 In addition, nonunion employees and VCC union employees were provided a 60%
13 Company-paid LTD benefit program beginning in 2012. The new program design and its
14 coverage for all these employees reduced premium rates significantly and kept Company
15 costs for LTD coverage essentially unchanged.

16 Q. What has the Company done to control the increase in active employee and retiree health
17 care, life insurance and long-term disability expenses?

18 A. The Company has aggressively managed these benefit costs over the last decade. Significant
19 changes have been made to all health, life and LTD plans since the introduction of the
20 Benefit by Choice program first implemented in 2002, which offered employees and retirees
21 different levels of health, life and LTD coverage. A summary of various changes made to
22 manage the cost of the Company's health care plans offered to employees and retirees from
23 2002 through 2010 follows:

- 24 • Increased employee/retiree premium contribution levels annually

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- 1 • Increased employee/retiree plan design cost sharing provisions including
2 medical/dental deductibles, coinsurance limits, office copays, urgent care
3 copays and emergency room copays
- 4 • Reduced plan benefit coverage levels from 90% to 85% and 70%
- 5 • Switched to Maintenance of Benefits (MOB) coordination
- 6 • Required covered spouse to have own employer coverage primary
- 7 • Implemented Preferred Provider Organization (PPO) plans, providing
8 discounted networks to all participants
- 9 • Negotiated administrative fees and insured plan premium rates annually and
10 bid the health plan market to improve pricing
- 11 • Increased employee/retiree prescription drug benefit cost sharing through
12 higher prescription drug copays, three-tier plan designs and network use for
13 specialty drugs
- 14 • Implemented prescription drug management programs including coverage
15 management programs, mandatory use of mail order, safety/efficiency
16 provisions and regular market bids for pricing
- 17 • Implemented health and disease management programs and added case
18 management
- 19 • Implemented a Company defined dollar contribution plan management
20 approach
- 21 • Eliminated high cost health plan offerings
- 22 • Introduced informed consumerism, cost information and credible health
23 sources

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- 1 • Used enhanced technology for more timely determination of plan eligibility
2 and coverage
- 3 • Implemented access only retiree health care benefits for new hires (no
4 Company subsidy)
- 5 • Implemented Healthy Living Plan designs, which require completion of
6 annual health monitoring and improvement steps to maintain preferred
7 benefit coverage levels. Employees/retirees that do not participate are moved
8 to a lower standard benefit coverage level.

9 Q. What changes were made to the union employee health care plan for 2011 as a result of the
10 new OM&C and VCC union employee collective bargaining agreements?

11 A. The newly ratified contracts with OM&C and VCC union employees provide a significant
12 number of health plan changes which generally all started in 2011 and included introduction
13 of the Healthy Living plan designs for all union PPO plans, added cost sharing through
14 various plan design provisions, increased employee premium contributions, introduced the
15 MOB coordination provision and the significant change to new hire access-only retiree health
16 care.

17 The new union contracts make significant changes to union employee health care
18 coverage over the next five years from 2011 through 2015. The 85% PPO plan currently
19 offered and the new 70% PPO plan added for union employees became Healthy Living plans,
20 offering preferred coverage for those employees and covered spouses who both complete the
21 required healthy living steps to improve their health. Those employees and covered spouses
22 that do not complete all the healthy living steps move to a lower level - standard coverage -
23 with more out-of-pocket costs that are about 20% higher than those in the preferred coverage
24 level. All plans offered to all employees and pre-Medicare retirees in 2011, including HMO

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1 plans, contain these Healthy Living requirements - taking a health risk appraisal (HRA) and
2 setting a health improvement plan with their physician - to earn preferred coverage or be
3 moved to the lower standard coverage level. The Company continues to promote the Healthy
4 Living initiative through the health care benefits provided in order to engage a larger
5 percentage of employees, retirees and their family members in healthier lifestyles now and
6 continuing into the future. This initiative is expected to result in productivity and attendance
7 improvements as well as better control of health care costs over the next three to five years.

8 The 85% PPO plan for union employees also includes higher deductibles and
9 coinsurance limits in 2011 and additional increases in 2014. Care provider office copays,
10 urgent care copays and emergency room visit copays all increased. Certain preventive
11 benefits are covered without cost sharing to promote prevention and comply with national
12 health care reform. Eligibility for adult children to age 26 was added as required by national
13 health care reform. A three-tier, incentive prescription drug plan was introduced with higher
14 copays and coinsurance requirements for preferred and non-preferred brand name drugs.
15 Additional prescription drug coverage management programs were introduced. Dental
16 deductibles were increased and annual limits and lifetime orthodontic limits were increased
17 modestly. A new 70% PPO plan with higher deductibles and coinsurance limits was also
18 introduced.

19 In addition to the plan design changes, premium contributions are now required from
20 all union employees covered by the 85% PPO plan or any of the HMO plans. Premium
21 contributions started in 2011 at about \$17 weekly for family coverage and increase each year
22 through 2015 when family coverage will cost a union employee about \$48 weekly or about
23 \$2,500 annually. The levels of employee premium contributions and plan design employee
24 out-of-pocket cost sharing in the plans are expected to continue to keep these plans

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1 competitive with the market and help to cover expected increasing costs over the terms of the
2 union agreements.

3 The MOB provision for union employees was also introduced in 2011. The MOB
4 provision limits reimbursement of claims when other coverage pays first. Under this new
5 method of coordinating benefits, the Company's plan limits the total reimbursement from the
6 Company plan to what would have been paid had the Company plan been the sole payer,
7 inclusive of what any other plan(s) coverage has already paid.

8 In addition, union employees who contribute at least \$100 annually to their HCFSA
9 for use in covering their eligible out-of-pocket medical costs receive a matching \$100
10 Company contribution to encourage them to use this tax-advantaged benefit to cover their
11 higher out-of-pocket costs in the 2011 plan.

12 Finally, all new union employees hired on or after September 1, 2010, who
13 eventually meet retiree health care eligibility requirements at retirement, will be offered
14 access-only retiree health care. The Company will not contribute to the cost of their retiree
15 health care coverage during their retirement.

16 The Company will provide a weekly \$20 and one-time \$1,200 defined contribution
17 after one year of service to a 'retiree health care account' in the ESP for each eligible new
18 union employee hired during the terms of the current contracts for the purpose of helping
19 these employees begin to save money to help cover their future retiree health care expenses.
20 This union new hire access-only retiree health care provision eliminates all ASC 715
21 (formerly known as FAS 106) retiree health care liability and expense for the Company for
22 these individuals.

23 The new contracts also provide for the opportunity to reopen health care discussions
24 with the unions to address national health care reform provisions that would change the cost
25 sharing arrangement and economics contemplated under the union agreements.

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1 These changes to union health care are designed to keep the Company's health and
2 insurance benefits competitive, cost-effective and quality based. These benefits continue to
3 be very important in attracting quality employees, keeping them healthy and productive, and
4 on the job to serve customers.

5 Q. What changes were made to nonunion health benefits for 2011?

6 A. Nonunion employee and pre-Medicare retiree health plans all contain the same two healthy
7 living steps requirement outlined previously in order to earn preferred coverage levels.
8 Urgent care copays, emergency room copays, coverage for preventive benefits, eligibility for
9 adult children to age 26 and some coinsurance limits were aligned with the union plans. The
10 same three-tier, incentive prescription drug plan negotiated with the union was introduced in
11 the nonunion PPO plans and the same coverage management programs were added. The
12 same dental changes outlined above for the union employees were made to the nonunion
13 dental benefits. Nonunion employees also picked up 50% of their expected 2011 cost
14 increase in premium contributions.

15 Q. Briefly describe what benefits the union and nonunion Zeeland Plant employees received in
16 2011?

17 A. Steelworker union employees are being covered under the same benefit plans in 2011 (and
18 through 2015) that cover the OM&C and VCC union employees as detailed previously. This
19 includes all the health and welfare plans as well as the ESP and DCCP. The Steelworker
20 union employees are covered by an access-only retiree health care provision (as in their
21 previous employer's agreement), but do not receive the weekly \$20 DCCP contribution
22 previously described or the \$100 matching contribution to the HCFSA.

23 Nonunion Zeeland Plant employees joining the Company in 2011 are covered by the
24 same benefit plans covering nonunion employees at the Company.

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1 Q. Were other measures taken Company-wide in 2011 to control future health care costs?

2 A. Yes. During 2011, a successful dependent verification program was administered by the
3 Company to eliminate any ineligible dependents covered by the health care plan. In addition,
4 all 2012 administrative fees with all medical and dental plans were renegotiated to provide
5 services at improved cost to the Company for 2012 and 2013.

6 Q. What changes were made to the health care plans for 2012?

7 A. There were a number of changes made to the health care plans for 2012. The Healthy Living
8 plans all added a third required Healthy Living step. Employees/retirees and or covered
9 spouses with weight and/or tobacco use health issues were required to contact a health plan
10 coach to address their health issue(s) in order to maintain preferred benefit coverage. In
11 addition, duplicative and more costly plan offerings were removed which eliminated two
12 PPO and two HMO plans from 2012 availability. The two remaining HMO plans were
13 redesigned to include a deductible, 90% coverage (down from 100%) and coinsurance limits.
14 A High Deductible Health Plan (HDHP) with a Health Savings Account (HSA) was added to
15 the offering for all employees and PreMedicare retirees. Additional prescription coverage
16 management programs were implemented for all employees and retirees. All Medicare
17 retirees were moved to an incentive-based, three-tier prescription drug plan with increased
18 copays for their prescription coverage. Premium contributions for union and nonunion
19 employees and PreMedicare retirees were increased for 2012.

20 In addition, the health care plan was separated into: (1) an employee medical plan,
21 (2) a retiree only medical plan, and (3) a dental plan for employees/retirees beginning in
22 2012. This was done to control future costs as retiree only medical plans and dental plans are
23 not subject to many of the expensive benefit, administrative and reporting requirements of
24 the national health care reform legislation.

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1 **Retiree Health Care and Life Insurance**

2 Q. Would you please explain line 7 of your Exhibit A-31 (HBK-1) - Summary of Benefits O&M
3 Expense for the Years 2011-2013 - Electric Portion for retiree health care and life insurance,
4 which begins with \$29,505,000 in 2011?

5 A. Exhibit A-31 (HBK-1) - Summary of Benefits O&M Expense for the Years 2011-2013 -
6 Electric Portion shows the actual 2011 retiree health care and life insurance expense under
7 ASC 715 (formerly known as FAS 106 expense) as well as the projected retiree health care
8 and life insurance expense for 2012 and 2013. These expenses are shown before any retiree
9 health care and life insurance (also referred to as Other Post-Employment Benefits or
10 “OPEB”) Equalization Mechanism (or OPEB tracker) adjustments are made. Line 7
11 represents the O&M expense associated with the Company’s retiree health care and life
12 insurance plans attributable to the electric portion of the utility operations.

13 Each of the annual expense levels shown on line 7 is the total of three separate items
14 which make up the total expense. Each year’s expense contains: (1) an ASC 715 expense
15 calculation, (2) an amortized ASC 715 transition obligation expense (which ended after
16 2011), and (3) an actuarial services expense.

17 Q. How does the Company determine its ASC 715 expense for retiree health care and life
18 insurance?

19 A. The expense is determined using actuarial analysis that is performed in accordance with
20 ASC 715. Consumers Energy follows GAAP for its financial statements. Under the
21 provisions of GAAP, ASC 715 describes the methodologies and assumptions required to
22 properly calculate and account for retiree health care and life insurance expense. The
23 calculations required by the accounting standards are performed annually by the plan’s
24 actuary, Aon Hewitt. In addition, the actuarial assumptions are reviewed by the Company
25 and the Company’s auditors to insure consistency with GAAP.

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1 ASC 715 requires an annual determination of retiree health care and life insurance
2 expense (OPEB expense or FAS 106 expense). The expense is determined based on
3 actuarially reviewed employee census data, the plan provisions, plan assets and certain other
4 actuarial assumptions. Year-end disclosure information is also produced, based on these
5 accounting standards, to provide a reconciliation of plan assets and liabilities at the end of the
6 Company's fiscal year.

7 Q. What are the components of the annual ASC 715 retiree health care and life insurance
8 expense?

9 A. There are four components of the annual ASC 715 expense: (1) service cost, (2) interest
10 cost, (3) expected earnings on plan assets, and (4) amortization of gains and losses, prior
11 service costs, and any transitional amounts. Service cost represents one-year's expected
12 benefits earned by active covered employees. Interest cost represents interest on the plan's
13 benefit obligation (its liabilities) due to the passage of time. All future benefits are
14 discounted back to the valuation date based upon a discount (interest) rate assumption. The
15 discount rate used reflects the interest rate conditions in the domestic economy at the time the
16 expense is being determined. There is also an assumption made for the expected rate of
17 return on plan assets. This rate of return assumption is intended to be a long-term
18 assumption based upon the best estimate of long-term expected investment earnings of the
19 plan assets. The last component represents amortization of various plan experiences that
20 were not anticipated by the actuarial assumptions.

21 In order to calculate the plan's total benefit obligation and annual ASC 715 expense,
22 the actuary uses a number of assumptions including health care inflation trend rates, a current
23 mortality table, the rate of employee retirements from the Company, the actual retiree health
24 care and life insurance claims of the Company, a discounting rate and the expected

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1 contributions to the plan. The assumptions used by the actuary are determined by the
2 Company each year and reviewed by the Company's auditors.

3 Q. What is the amortized ASC 715 transition obligation expense?

4 A. The amortized transition obligation expense component is a portion of the retiree health care
5 and life insurance expense that was determined at the time FAS 106 (now ASC 715) was first
6 implemented and remains unchanged from year to year. By the end of 2011, the transition
7 obligation was fully amortized and is no longer a portion of the ASC 715 expense in 2012
8 and beyond.

9 This transition obligation expense was first established when FAS 106 (now
10 ASC 715) became effective in 1992 when the Company had to establish its retiree health
11 care/life insurance benefit obligation (liability) under the new accounting standard.
12 Consumers Energy adopted FAS 106 effective January 1, 1992. The transition obligation
13 produced a retiree health care and life insurance expense, which represented benefits already
14 earned as of the date the FAS 106 standard was adopted. This liability was then amortized as
15 an expense on a straight-line basis over the average remaining service period of active plan
16 participants. The MPSC has previously approved recovery of this expense component,
17 which generally did not change from year to year during its amortization period through
18 2011.

19 Q. Are actuarial services expenses included in line 7 of Exhibit A-31 (HBK-1)?

20 A. Yes. An annual expense for the actuarial services provided for the retiree health care and life
21 insurance plans is included in line 7 of the exhibit.

22 Q. What changes were made to retiree health care coverage for 2011 and beyond?

23 A. The same changes described previously for union and nonunion employees were made to the
24 pre-Medicare retiree plans for these groups for 2011 and 2012. These changes included the
25 three-step Healthy Living plan requirements with preferred and standard coverage, increases

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1 in plan deductibles, copays and coinsurance limits, various plan eliminations, increased
2 premium contribution requirements and the implementation of the MOB coordination
3 provision.

4 In addition, as described earlier in the ESP section above, all new union hires since
5 September 1, 2010, may qualify for an access-only retiree health care plan at retirement
6 which requires 100% retiree premium contribution for coverage at retirement and provides
7 for no Company contribution or subsidy and results in no Company ASC 715 liability or
8 expense.

9 In addition, there were changes made to both union and nonunion Medicare retiree
10 health plans starting in 2011 and 2012. These changes included scheduled deductible and
11 coinsurance limit increases in 2011 and 2014, an incentive-based, three-tier prescription drug
12 copay plan in 2012, and the addition of the MOB provision for all union retirees turning age
13 65 or becoming Medicare-eligible on or after January 1, 2011. These changes to the retiree
14 plans were significant enough to create the need for the Company to remeasure its ASC 715
15 retiree health and life insurance liability and expense mid-year in 2010. Because of all the
16 retiree health plan changes, the Company's ASC 715 expense for these benefits is
17 significantly reduced for 2010 through 2013.

18 Q. Do the calculations for the retiree health care and life insurance expense follow the
19 prescribed methodology of ASC 715?

20 A. Yes. The amounts are projected based on ASC 715 using information specific to the
21 Company's retiree health care and life insurance plans, including the remeasurement of
22 ASC 715 for retiree health care and life insurance during 2010.

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1 Q. Please describe the development of the retiree health care and life insurance expense levels
2 that are shown on line 7 of Exhibit A-31 (HBK-1), which begins with \$29,505,000 in 2011.

3 A. Each of the O&M retiree health care and life insurance expense levels shown on line 7 for
4 the electric utility is based upon Aon Hewitt's actuarial determination of the plan's expense
5 for that period in accordance with ASC 715 and includes the amortized ASC 715 transition
6 obligation through 2011 plus the cost for actuarial services related to these plans. The actual
7 2011 O&M retiree health care and life insurance expense for the electric utility was
8 \$29,505,000. The O&M expense for retiree health care and life insurance for the electric
9 utility is projected to be \$29,335,000 in 2012 and \$30,505,000 in 2013.

10 To determine the annual ASC 715 expense for Consumers Energy for 2013, key
11 actuarial assumptions are used by the actuary in developing the expense projection. These
12 assumptions include a specific discount rate, expected rate of return on plan assets, pre-
13 Medicare and Medicare retiree health care cost trends, annual trust contributions, use of the
14 year 2000 mortality table, and the acceptance by the Company of the government subsidy
15 available under the Medicare prescription drug legislation. Using these assumptions, the
16 actuary projected the ASC 715 expense for retiree health care and life insurance to be
17 \$78,000,000 in 2013 for Consumers Energy. Using the headcount allocation methodology
18 mentioned previously, the electric utility O&M portion of this total ASC 715 projected
19 expense for 2013 is \$30,420,000.

20 The annual transition obligation expense for the Company is zero in 2013 as this
21 portion of the expense was completely amortized in 2011.

22 The third piece of the electric utility O&M cost for retiree health care and life
23 insurance for 2013 is \$85,000 for actuarial services related to maintenance of the plan and
24 preparation of required actuarial reports.

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1 These three retiree health care and life insurance O&M expense components result in
2 a total electric utility O&M expense projection of \$30,505,000 for 2013.

3 Q. Why is the retiree health care and life insurance expense for 2012 about the same as 2011 if
4 the transition obligation expense was removed during 2012 and beyond?

5 A. The ASC 715 expense did decrease significantly in 2011 as a result of the 2011 retiree health
6 plan changes outlined above and improved prescription drug unit pricing. The 2012 expense
7 was expected to decrease significantly as well due to the removal of the transition obligation
8 beginning in 2012. However, a number of assumption changes had to be made for 2012 due
9 to current economic conditions at the time the 2012 expense was projected. The discount
10 rate for 2012 was set at 5.1%, reduced from 5.6% which was used to calculate the 2011
11 expense. The expected retirement age assumption also had to be lowered to reflect the more
12 recent actual retirement ages, leading to an increase in the 2012 expense. Finally, the
13 expected rate of return on plan assets was reduced to 7.25% for the 2012 projected expense
14 from 7.5% used to calculate the 2011 expense. These three assumption changes resulted in
15 an increase to 2012 projected expense. When netted against the removal of the transition
16 obligation which ended in 2011 and the expense reduction generated by the lower assumed
17 health care inflation trends for 2012, only a slight reduction to 2012 projected OPEB expense
18 resulted.

19 Q. Why is the retiree health care and life insurance expense higher in 2013 than in 2012?

20 A. To reflect current economic conditions at the time this expense was projected for 2013, the
21 discount rate had to be reduced to 4.45% from the 5.1% used for 2012 expense projection.
22 While this change increases expense, it is offset somewhat by the lower assumed health care
23 inflation trends for 2013, leaving the expected retiree health care and life insurance expense
24 slightly higher in 2013 than 2012.

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1 **III. PENSION EQUALIZATION MECHANISM AND OPEB EQUALIZATION**
2 **MECHANISM**

3 Q. Is the Company requesting that a Pension Equalization Mechanism (PEM) or pension tracker
4 and an OPEB Equalization Mechanism (OEM) or OPEB Tracker be approved in this rate
5 case?

6 A. Yes. Consumers Energy is proposing that equalization mechanisms/trackers be approved in
7 this case for both pension expense and OPEB expense. Consumers Energy believes that
8 approving these equalization mechanisms in this case is a reasonable means of protecting
9 both customers and the utility from the volatility inherent in these expenses, and is a
10 satisfactory way to ensure that the utility's actual pension and OPEB expenses are recognized
11 in rates and that customers pay the correct amounts for these expenses.

12 Q. Please explain.

13 A. A PEM and an OEM are necessary to assure recovery of the correct pension expenses and
14 OPEB expenses and to make sure customers are charged the correct pension expenses and
15 OPEB expenses. These annual expenses are generated in large part based upon actuarial
16 assumptions that reflect current economic conditions and interest rates over which the
17 Company has no control. Trackers would properly account for these market driven
18 fluctuations in expense and also allow Company-managed benefit changes and contributions
19 to be captured in a tracked expense, which would primarily benefit customers via a reduced
20 expense.

21 Q. Can you provide examples of how the trackers would work?

22 A. Several examples illustrate the circumstances of various changes to these expenses and how
23 trackers would result in accurate and appropriate charges to customers for these pension and
24 OPEB expenses. The significant downturn in security values in the 2008 financial markets
25 reduced pension plan assets and OPEB assets significantly as of the 12/31/2008 ASC 715

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1 measurement date. These lower asset values were then used as a basis to establish 2009's
2 ASC 715 pension and OPEB expense. This change in pension plan asset values alone
3 contributed to a \$12 million increase in total 2009 ASC 715 pension expense. Fortunately,
4 during this same year, this pension expense increase was offset by a similar reduction in this
5 expense primarily due to the sale of the Palisades Plant and the resulting pension benefits
6 liability and asset transfer related to transfer of the plant's employees to the new owner of the
7 plant. However, the reduction in OPEB plan asset values contributed to a \$39 million
8 increase in total 2009 ASC 715 OPEB expense as the reduced value of OPEB plan assets had
9 to be immediately recognized in the OPEB expense. In addition, the health care inflation
10 assumption change required to properly reflect retiree health care inflation trends created an
11 additional \$14 million increase in ASC 715 OPEB expense in 2009.

12 Continued volatility in investment performance and/or interest rates in a financial
13 market over which the Company has no control result in increases or decreases to ASC 715
14 pension and OPEB expense. Such was the case for 2010 when interest rates declined further,
15 resulting in higher pension expense in 2010 from 2009. Fortunately, financial markets
16 continued to improve during 2010 and, because the Company made large contributions to its
17 Pension Plan in 2010, the 2011 pension expense actually declined. If a pension tracker were
18 in place for 2011, customers would have benefited from this reduction in the Company's
19 actual pension expense.

20 With regard to OPEB, improving investment performance in 2010 financial markets
21 helped provide a reduction to OPEB expense. At the same time, however, discount (interest)
22 rates continued to fall, offsetting the expense savings generated from improved investment
23 returns in the OPEB plan trust accounts. In addition, the Company negotiated favorable
24 terms in its union contract regarding future retiree health care and current retiree health care
25 plan design which helped to reduce the total 2010 OPEB expenses during the remeasurement

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1 in the middle of 2010 as well as for 2011 and beyond. If an OPEB tracker were in place for
2 2010 and 2011, customers would have favorably benefited as net OPEB expenses actually
3 declined for these reasons.

4 As described above, there are many factors that determine the Company's pension
5 and OPEB expenses from one year to the next. All of these economic factors are beyond the
6 Company's control. The economy dictates interest/discount rates, investment return on plan
7 assets and health inflation trends. In addition, legislation like the Pension Protection Act, the
8 Affordable Care Act (national health care reform) and the State of Michigan's Health
9 Insurance Claims Assessment Act all significantly impact the expenses of these benefits.

10 Q. Will having trackers in place reduce the Company's proactive management of these costs?

11 A. No. The Company has aggressively controlled its pension and OPEB expenses as outlined
12 previously in this testimony - moving to defined contribution retirement plans; making
13 significant Pension Plan contributions; eliminating subsidies for retiree health care; and
14 actively managing both union and nonunion employee and retiree health care expenses
15 through a variety of methods. Having Pension and OPEB trackers in place will recognize the
16 economic factors beyond the Company's control and supports continued aggressive and
17 proactive cost management of these expenses by the Company. The Company will continue
18 to proactively manage these expenses for both the benefit of its customers and the
19 Company's financial viability because it is a prudent business practice - whether or not
20 trackers are in place.

21 Q. Hasn't the new energy law removed the need for trackers?

22 A. No. While the new energy law has removed some of the lag in the recovery of these costs,
23 the energy law does not assure that customers are paying the correct amount for these
24 expenses. This is primarily due to a number of factors resulting from timing - (i.e. when an
25 electric or gas rate case is filed; whether a year-end passes after the filing when all actuarial

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1 assumptions used to set expense for the upcoming year are determined; when the Company
2 makes changes to its benefit plans such as cost sharing changes in the fall of each year; and
3 other significant factors that may influence pension or OPEB expense mid-year such as union
4 contract changes).

5 The bottom line is that a pension and an OPEB tracker would assure that all these
6 variables would be properly accounted for and that customers would be charged no more or
7 no less than the actual costs for these pension and OPEB expenses. As both pension expense
8 and OPEB expense are heavily influenced by multiple economic factors beyond the
9 Company's control, a PEM (pension tracker) and an OEM (OPEB tracker) are appropriate to
10 assure proper recovery by the Company of pension and OPEB expenses from customers.

11 Q. Does this conclude your direct testimony?

12 A. Yes.

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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

REBUTTAL TESTIMONY

OF

HERBERT B. KOPS

ON BEHALF OF

CONSUMERS ENERGY COMPANY

March 2013

HERBERT B. KOPS
REBUTTAL TESTIMONY

1 Q. Please state your name and business address.

2 A. My name is Herbert B. Kops, and my business address is One Energy Plaza, Jackson,
3 Michigan.

4 Q. Are you the same Herbert B. Kops who previously submitted direct testimony in this
5 case?

6 A. Yes.

7 Q. What is the purpose of your rebuttal testimony?

8 A. The purpose of my rebuttal testimony is to rebut recommendations in Brian A. Welke's
9 direct testimony submitted on behalf of the Michigan Public Service Commission Staff
10 and Sebastian Coppola's direct testimony submitted on behalf of the Attorney General,
11 which recommend DB and DC SERP expenses not be allowed recovery in rates.

12 Q. At pages 8-9 of his testimony Mr. Welke recommends that DB SERP and DC SERP
13 expenses be excluded from Consumers Energy Company's ("Consumers Energy" or the
14 "Company") revenue requirement. What concerns does the Company have with
15 Mr. Welke's recommendation to not allow recovery of DB and DC SERP expenses?

16 A. DB and DC SERP benefits are necessary to attract, retain, and motivate a core set of
17 highly skilled executives whose goal is to provide excellent service to customers
18 (ratepayers) while optimizing the Company's resources to meet present day demands and
19 future needs of the business and its customers. The premise expressed by Mr. Welke that
20 the costs for these executive plans are not commensurate with the benefits to customers is
21 an invalid conclusion. Customers benefit from having a competent, highly motivated
22 workforce. It is reasonable and appropriate to pay executives competitive benefits.

HERBERT B. KOPS
REBUTTAL TESTIMONY

1 Q. Mr. Welke states that Staff is recommending exclusion of these costs because they have
2 not been included in prior rate cases. Does this provide a valid reason to exclude these
3 costs in the current case in your opinion?

4 A. No. The fact that the Commission may have concluded in a prior case that the benefits of
5 these plans accrued to investors in the form of higher share prices and dividends (to)
6 ratepayers only tangentially should not be viewed as prohibiting recovery in the current
7 case. SERP benefits are a reasonable, customary, and indeed necessary, utility operating
8 expense. Recovery of the DB SERP and DC SERP expense in rates in the current case is
9 appropriate based on the reality of Michigan's modern day economy and the
10 compensation and benefit requirements needed to procure and retain the necessary
11 executive talent to meet the demands and requirements of managing an electric utility
12 business for the benefit of ratepayers. Executives covered by these DB and DC SERP
13 plans are directly responsible for the day to day operation of the utility and meeting the
14 diverse and demanding needs of ratepayers. Retaining competent and motivated senior
15 executives benefits customers.

16 Q. Please continue.

17 A. The DB and DC SERP plans include a restoration of benefit component to provide
18 retirement benefits for the portion of the executive's competitively based compensation
19 above the legislated Internal Revenue Code limits. This provides a competitive benefit
20 for executives who focus on a number of operational areas important to the customer
21 including safety, system reliability, improved productivity, competitive pricing, quality
22 customer service, and financial health of the Company.

HERBERT B. KOPS
REBUTTAL TESTIMONY

1 Counter to the position presented in Staff testimony, ratepayers are benefited by
2 incentives tied to the financial health of the Company. Demonstrated financial strength
3 and the ability to attract capital is an essential requirement for providing competitive
4 energy and services to the customers of the business. Both are requirements needed for a
5 business to continue to serve its customers. The financial metrics of these long-term
6 SERP plans provide executives with the continuing incentives to motivate maximum
7 performance and serve customers well. These plans are a competitive and reasonable
8 cost of business that should be recoverable in rates.

9 Q. What concerns does the Company have with Mr. Coppola's recommendation to not allow
10 recovery of DB and DC SERP expenses?

11 A. Mr. Coppola's reasons for disallowing recovery of SERP costs include the prior
12 Commission disallowance policy, the lack of benefits to customers, and the Internal
13 Revenue Code limitations on funding additional benefits within a qualified plan. The
14 previous Commission policy and lack of customer benefits arguments have been
15 addressed above. The value of these plans as a restoration of benefits truncated by
16 IRS-imposed limits and as an individual incentive to the executive to maximize personal
17 performance has proven worth across many industries, including the utility industry.

18 These SERP plans are competitive in the industry and necessary to attract, retain,
19 and motivate executives to meet the needs of its customers. Reimbursement of the DB
20 and DC SERP executive benefit plan costs by ratepayers is a reasonable and appropriate
21 request that should be recoverable in rates.

22 Q. Does this complete your rebuttal testimony?

23 A. Yes, it does.

1 JUDGE CUMMINS: With regard to Exhibit
2 A-31, is there any objection to the receipt of this
3 exhibit? Hearing none, Exhibit A-31 is received into
4 evidence.

5 MR. CHAMBERS: Consumers Energy moves to
6 bind in the direct testimony of Ryan J. VanBlarcum. Mr.
7 VanBlarcum's testimony consists of a cover page plus four
8 pages of questions and answers. Mr. VanBlarcum sponsored
9 Exhibit A-63 in connection with his testimony. Consumers
10 Energy moves for the admission of Exhibit A-63.

11 JUDGE CUMMINS: Very well. Any objection
12 to binding in Mr. VanBlarcum's testimony? The testimony
13 will be bound in the record.

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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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

DIRECT TESTIMONY
OF
BRIAN J. VANBLARCUM
ON BEHALF OF
CONSUMERS ENERGY COMPANY

September 2012

BRIAN J. VANBLARCUM
DIRECT TESTIMONY

1 Q. Please state your name and business address.

2 A. Brian J. VanBlarcum, One Energy Plaza, Jackson, Michigan 49201.

3 Q. By whom are you employed?

4 A. I am employed by Consumers Energy Company (“Company” or “Consumers Energy”).

5 Q. What is your position with Consumers Energy?

6 A. I am a Senior Tax Analyst I.

7 Q. Please briefly describe your educational background.

8 A. I am a graduate of Western Michigan University where I earned a Bachelors of Business
9 Administration in Finance.

10 Q. Please describe your business experience.

11 A. I started with the Company in 2004 as a General Accounting Analyst with the Company’s
12 property accounting team. In 2006, I was appointed to my current position as a Senior
13 Tax Analyst I with the Company’s corporate tax department.

14 Q. Are you a certified assessor?

15 A. I am a Level 2 assessor certified by the State of Michigan’s State Tax Commission and a
16 member of the Michigan Assessors Association.

17 Q. What are your responsibilities as a Senior Tax Analyst I?

18 A. I am primarily responsible for the administration of the Company’s real and personal
19 property taxes. This includes managing the Company’s self-declaration of personal
20 property located within the State of Michigan, overseeing property tax matters
21 concerning the Company’s land, generating sites and other real property and supervising
22 tax payments to approximately 1,500 taxing authorities. I am also responsible for
23 budgeting and forecasting current and future year’s property tax payments and expense.

BRIAN J. VANBLARCUM
DIRECT TESTIMONY

1 Q. Have you previously testified before the Michigan Public Service Commission?

2 A. Yes, I sponsored testimony in the following cases:

3 Gas Rate Case (U-15506)

4 Electric Rate Case (U-15645)

5 Electric Rate Case (U-16191)

6 Gas Rate Case (U-16418)

7 Q. What is the purpose of your testimony in this proceeding?

8 A. My testimony identifies the Property Tax Rate for the 2013 test year, and explains how
9 the rate was derived.

10 Q. Have you prepared any exhibits to accompany your testimony?

11 A. Yes. I am sponsoring Exhibit A-63 (BJV-1) Development of the Property Tax Rate for
12 2013.

13 Q. Was this exhibit prepared by you or under your supervision?

14 A. Yes.

15 Q. What is the Property Tax Rate for the 2013 test year?

16 A. As indicated on line 13 of Exhibit A-63 (BJV-1, Page 1), the Property Tax Rate for the
17 2013 test year is 0.012698529.

18 Q. How did you calculate the Property Tax Rate for the 2013 test year?

19 A. The Property Tax Rate for the electric business was calculated using the Company's 2013
20 Estimated Electric Property Tax Expense (line 7, Exhibit A-63 (BJV-1, Page 1) divided
21 by the total of the estimated 2012 year-end plant-in-service (line 8, Exhibit A-63 (BJV-1,
22 Page 1) plus one-half of the estimated Construction Work in Progress (line 11, Exhibit
23 A-63 (BJV-1, Page 1).

BRIAN J. VANBLARCUM
DIRECT TESTIMONY

1 Q. What is included in the Electric Property Taxes Paid - 2012 Estimate on line 1?

2 A. The Consumers Energy 2012 taxes paid of \$135.5 million on behalf of the electric
3 portion of the business represents estimated property taxes to be paid in 2012.

4 Q. What is included in the Estimated Electric Property Taxes on 2012 Plant Investment on
5 line 2?

6 A. The \$5.7 million increase is the estimated property taxes on the 2012 estimated net
7 additions that will be included in the 2013 property tax liability. This is calculated by
8 taking the capital additions less retirements times the first year State Tax Commission
9 multiplier table value to recognize a depreciation allowance, which is then multiplied by
10 the statutory reduction of 50% of true cash value to get the assessed value, then
11 multiplied by Consumers' composite millage rate of 47.0661 to obtain the estimated tax
12 amount. This calculation is shown on page 2 of Exhibit A-63 (BJV-1).

13 Q. What is included in the Estimated Electric Property Taxes on Real Property Taxable
14 Value Increases - Inflation on line 3?

15 A. The \$1.6 million increase for the Real Property Taxable Value relates to Article IX,
16 Section 3, of the Michigan Constitution of 1963 allowing local assessors to raise real
17 property taxable values by the lesser of 5% or the Consumer Price Index ("CPI"). For
18 2013, our property tax model assumes a CPI rate of 2.8%. This calculation is shown on
19 page 3 of Exhibit A-63 (BJV-1).

BRIAN J. VANBLARCUM
DIRECT TESTIMONY

- 1 Q. What result does including the Estimated Electric Property Taxes on Real Property
2 Taxable Value Increase and Estimated Electric Property Taxes on 2012 Plant Investment
3 have on the estimated 2013 property tax amount paid by the electric business?
- 4 A. The result of including these additional items is an estimated 2013 property tax amount to
5 be paid for the electric business of \$142.8 million as shown on line 4.
- 6 Q. Does the amount on line 4 include property tax payments for pollution control equipment
7 or computer software, such as SAP?
- 8 A. No, as pollution control equipment and computer software are exempt under
9 MCL 324.5904(1) and 211.9d, the estimate of 2013 property tax to be paid on line 4 does
10 not include property taxes associated with these items.
- 11 Q. How is this paid amount converted to an expense amount?
- 12 A. Since the Company expenses property taxes based on the fiscal year of the taxing
13 authorities, 50.0% of the 2012 estimated electric property tax payments for Consumers
14 Energy is added to the 2013 estimated electric payments since that amount will be
15 expensed in 2013, while subtracting 50.0% of the 2013 estimated electric payments that
16 will be expensed in 2014, arriving at a total 2013 property tax expense of \$139.2 million
17 as shown on line 7.
- 18 Q. What is the next step in calculating the tax rate?
- 19 A. The estimated Property Tax Expense for the test year is divided by the 2012-estimated
20 year-end plant in service amount plus one-half of construction work in progress to arrive
21 at an average tax rate of 0.012698529.
- 22 Q. Does this conclude your testimony?
- 23 A. Yes.

1 JUDGE CUMMINS: Is there any objection to
2 the receipt of Exhibit A-63? Hearing none, Exhibit A-63
3 is received into evidence.

4 MR. CHAMBERS: Consumers Energy moves to
5 bind the direct testimony and rebuttal testimony of Mr.
6 Warriner into the record. Mr. Warriner's direct
7 testimony consists of a cover page followed by 20 pages
8 of questions and answers. Mr. Warriner's rebuttal
9 testimony consists of a cover page followed by four pages
10 of questions and answers.

11 In connection with his testimony, Mr.
12 Warriner sponsored the portions of Exhibit A-10 which are
13 also labeled LDW-1 consisting of two pages, LDW-2
14 consisting of five pages, LDW-3 consisting of three
15 pages, LDW-4 consisting of two pages, LDW-5 consisting of
16 one page, and LDW-6 consisting of two pages. We move for
17 the admission of these exhibits as Exhibit A-10 sponsored
18 by Mr. Warriner.

19 JUDGE CUMMINS: Any objection to binding
20 in either the direct or the rebuttal testimony of Mr.
21 Warriner? Hearing none, Mr. Warriner's direct testimony
22 and his rebuttal testimony will be bound into the record.

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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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

DIRECT TESTIMONY
OF
LINCOLN D. WARRINER
ON BEHALF OF
CONSUMERS ENERGY COMPANY

September 2012

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 Q. Please state your name and business address.

2 A. My name is Lincoln D. Warriner, and my business address is One Energy Plaza, Jackson,
3 Michigan.

4 Q. By whom are you employed?

5 A. Consumers Energy Company (hereinafter, "Consumers Energy" or the "Company").

6 Q. What is your position with the Company?

7 A. I am a Senior Business Support Consultant - Lead in the Rates and Business Support
8 Department.

9 Q. Please describe your educational background.

10 A. I received a Bachelor of Science Degree in Business Administration, major in
11 Accounting, from Central Michigan University in 1987. In 1994, I received a Master of
12 Science in Administration Degree from Central Michigan University.

13 Q. What is your business experience?

14 A. I began working for the Company in June 1987 as a region accountant at the Grand
15 Rapids Service Center. While there, I performed various reviews of internal accounting
16 control procedures and workflow processes. In 1989, I transferred to a similar position at
17 the Lansing Service Center. In 1991, I took a position as a Management Systems and
18 Planning Analyst in the Southern Region Administration and Planning Department. My
19 primary responsibility in this position was to provide analytical support to region
20 management on issues concerning operating, maintenance and construction budgets and
21 other performance measurements. In February 1994, I took a position as an
22 Administrative Supervisor responsible for the supervision of several administrative
23 functions including region accounts payable, miscellaneous accounts receivable, cash

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 receipts and disbursements, payroll, records center, and mail room operations. In
2 February 1995, I transferred to the Electric SBU Planning Department, which since has
3 been consolidated within the Rates and Business Support Department. In this
4 department, I have been responsible for coordinating the development of financial plans,
5 budgets, analysis, and forecasts for the Electric SBU. Since 1997, my responsibilities
6 have included the electric deliveries forecast, and completing various financial and
7 economic studies for the electric business unit. During 2007 I accepted additional
8 supervisory responsibility for the Company's gas deliveries forecasts and electric revenue
9 forecasts.

10 Q. Have you testified in other cases before the Michigan Public Service Commission (the
11 "Commission")?

12 A. Yes. I have recently provided testimony in the following cases:

13 a. U-16191 – January 2010 electric rate case. I presented adjustments to
14 2008 historical actual sales and revenues for the purpose of developing the
15 projected test year sales and revenue. I also presented the Company's
16 forecast of electric deliveries, generation requirements, and peak demand
17 for the years 2009-2013.

18 b. U-16412 – September 2010 Energy Optimization Plan amendment. I
19 explained the historical and forecasted sales and revenue data that the
20 Company used in developing its amended Energy Optimization Plan.

21 c. U-16418 – August 2010 gas rate case. I adopted the testimony of Linda J.
22 Clark regarding the Company's forecast of gas deliveries and provided

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 rebuttal testimony concerning adjustments to the Company's forecast that
2 were proposed by interveners in that case.

3 d. U-16432 – September 2010 power supply cost recovery (“PSCR”) plan
4 case. I presented the Company's official forecasts of electric deliveries,
5 generation requirements, and peak demand forecasts for 2011-2015.

6 e. U-16543 – February 2011 renewable energy plan amendment. I explained
7 the historical and forecasted sales and revenue data that the Company used
8 in developing its amended renewable energy plan.

9 f. U-16794 – June 2011 electric rate case. I presented adjustments to 2010
10 historical actual sales and revenues for the purpose of developing the
11 projected test year sales and revenue. I also presented the Company's
12 forecast of electric deliveries, generation requirements, and peak demand
13 for the years 2011-2015.

14 g. U-16670 – August 2011 Energy Optimization Plan amendment. I
15 explained the historical and forecasted sales and revenue data that the
16 Company used in developing its amended Energy Optimization Plan.

17 h. U-16890 – September 2011 and February 2012 power supply cost
18 recovery plan case. I presented the Company's official forecasts of
19 electric deliveries, generation requirements, and peak demand forecasts for
20 2012-2016.

21 i. U-16924 – December 2011 gas cost recovery plan case. I presented the
22 Company's official forecasts of natural gas sales and natural gas
23 transportation for 2012-2016.

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 Q. What is the purpose of your testimony in this proceeding?

2 A. The purpose of my testimony is to present the Company's analysis of historical electric
3 operating revenue and projected test year electric operating revenue under current tariff
4 rates for use in this rate proceeding.

5 In Part 1 of my testimony, I will discuss the adjustments to 2011 historical actual
6 sales and revenues that I am recommending for the purpose of developing the projected
7 January 2013 to December 2013 test year sales and revenues.

8 In Part 2 of my testimony, I will present the Company's official forecasts of
9 electric deliveries, generation requirements, and peak demand for the years 2012-2017.

10 Q. Are you sponsoring any exhibits?

11 A. Yes. I am sponsoring the following exhibits:

12 **PART 1: TEST YEAR REVENUE ANALYSIS:**

13 Exhibit A-10 (LDW-1) Test Year Total Electric Revenue Analysis

14 **PART 2: PROJECTED SALES AND REVENUES:**

15 **HISTORICAL AND TEST YEAR SALES DETAIL:**

16 Exhibit A-10 (LDW-2) Test Year and Historical Summary Matrix
17 by Rate and Customer Class

18 **FORECAST OF TOTAL ELECTRIC DELIVERIES:**

19 Exhibit A-10 (LDW-3) Sales by Major Customer Classes and
20 System Output

21 Exhibit A-10 (LDW-4) System Output, Maximum Demands, and
22 Load Factors

23 **FORECAST OF ENERGY OPTIMIZATION SALES REDUCTIONS**

24 Exhibit A-10 (LDW-5) Annual Energy Optimization Incremental
25 Sales Reductions

LINCOLN D. WARRINER
DIRECT TESTIMONY

ECONOMIC OUTLOOK

Exhibit A-10 (LDW-6) Summary of Economic Outlook

Q. Were these exhibits prepared by you or under your direction and supervision?

A. Yes.

PART 1: TEST YEAR REVENUE ANALYSIS

Q. Please describe Exhibit A-10 (LDW-1).

A. Exhibit A-10 (LDW-1) is a two page exhibit that summarizes the development of the projected test year revenues. In this case, the projected test year includes the time period of January 2013 to December 2013. Page 1 summarizes the changes from 2011 actual to the projected test year electric operating revenue in total, including nonjurisdictional sales and revenue. Page 2 summarizes the changes from 2011 actual to the test year electric operating revenue for jurisdictional sales and revenue only.

Q. Please describe your approach to adjusting 2011 sales and revenue to develop the projected test year revenue estimates.

A. As indicated in Column B on page 1 of Exhibit A-10 (LDW-1), total electric operating revenue for 2011 was \$3,897.7 million. This amount was adjusted up to \$3,898.8 million after including the margin from various job work activities that are not reported as electric operating revenues. As shown on Page 2 of this exhibit, jurisdictional revenues for 2011 were \$3,875.1 million. The jurisdictional revenues were also adjusted up to \$3,876.2 million to include the margin from job work activities. The first step in analyzing the test year revenue was to identify the specific components of the historical 2011 electric operating revenue. This resulted in estimations of 2011 revenues for the following categories as identified in Exhibit A-10 (LDW-1):

1. Base Tariff Billed Revenue;

LINCOLN D. WARRINER
DIRECT TESTIMONY

- 1 2. GSG Power Supply Charges;
- 2 3. Base PSCR Billed Revenue;
- 3 4. PSCR Factor Billed Revenue;
- 4 5. Energy Optimization Surcharge Revenue;
- 5 6. Electric Customer Choice Implementation Surcharge Revenue;
- 6 7. Security Recovery Factor Surcharge Revenue;
- 7 8. Regulatory Asset Recovery Factor Surcharge Revenue;
- 8 9. Securitization and Securitization Tax Surcharge Revenues;
- 9 10. Pension/OPEB Equalization Mechanism Revenue;
- 10 11. Renewable Energy Plan Charges;
- 11 12. Stranded Cost Surcharges;
- 12 13. Uncollectible Surcharges;
- 13 14. Electric Choice Incentive Mechanism Surcharges;
- 14 15. Unbilled Tariff Revenues;
- 15 16. Unbilled Base PSCR Revenues;
- 16 17. Unbilled PSCR Factor Revenues;
- 17 18. PSCR Over/Under Recovery Revenues;
- 18 19. Miscellaneous Revenues; and
- 19 20. Intersystem Sales Revenues.

20 The 2011 actual revenues for each of these items were adjusted for numerous
21 reasons which will be described in the remainder of my Part 1 testimony. The end result
22 of this analysis is the Company's proposed level of jurisdictional sales and revenues for
23 the projected test year.

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 Q. Please describe the adjustments you made to develop the Company's proposed test year
2 sales and revenues?

3 A. The following adjustments are included in my proposed test year revenues:

- 4 1. Margin on job work activity (equal to job work revenues less job work
5 expenses) was added as an adjustment to total revenues. These services
6 are appropriately reported as other income in annual reports filed with the
7 Commission. The adjustment to revenue was made to be consistent with
8 similar adjustments adopted in our previous five rate cases, U-14347,
9 U-15245, U-15645, U-16191, and U-16794. This adjustment increased
10 historical year revenues by approximately \$1.0 million. This adjustment
11 appears on lines 24 and 25, in column (b), on page 1 of Exhibit A-10
12 (LDW-1).
- 13 2. Surcharges, unbilled revenues, and other revenue adjustments totaling
14 \$196.2 million were eliminated from test year revenues in column (c) on
15 page 1 of Exhibit A-10 (LDW-1) in order to simplify the rate case revenue
16 analysis. Offsetting amortization costs are also eliminated from this case
17 by the Company's Revenue Requirements witness. The Company is not
18 proposing that regulatory asset surcharges should be changed from current
19 practice. It is simply ignoring them for general ratemaking purposes.
20 2011 PSCR factor and PSCR over/under recovery revenues are also
21 eliminated in column (c), but are re-estimated for test year sales volumes
22 and cost levels in column (j). Megawatt-hour delivery and revenue
23 (\$90.7 million) values for Intersystem Sales are also removed from the

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 analysis in column (c). Miscellaneous revenues from purchased power
2 administrative fees (\$1.0 million) are also removed in this step because
3 those revenues are treated as a credit to the recovery of power supply
4 costs.

5 3. Weather conditions during 2011 were warmer than normal. In a normal
6 weather year, defined as the 15-year average from 1997 to 2011,
7 residential and commercial customer usage would decline from 2011
8 actual experience. Normalizing usage resulted in a decrease of
9 449.9 GWH from 2011. This normalization adjustment decreases total
10 revenue in column (d) on page 1 of Exhibit A-10 (LDW-1) by
11 \$53.1 million. The base PSCR share of this decline is \$23.8 million, and
12 the base tariff share of this adjustment is \$29.3 million.

13 4. During 2010, the Company provided job work services to a variety of
14 customers. In prior cases, the Company has proposed adjustments to
15 historical results to reflect changes in business conditions for these
16 services. At this time the Company is not proposing any adjustments to
17 this recent historical experience for this case.

18 5. General Motors, Delphi, and Nexteer Saginaw Steering are large industrial
19 customers that historically have implemented operational changes to align
20 production with customer demand. These changes have resulted in
21 reductions in electric usage averaging 102.6 GWH per year for the 20-year
22 period ending 2011. Indicators of employment in the Michigan
23 Transportation Equipment sector are consistent with these historical usage

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 reductions. The Company's sales forecast relies on these employment
2 projections to estimate the test year usage for General Motors, Delphi, and
3 Nexteer Saginaw Steering. It appears that operating conditions have
4 stabilized, and some recovery in electric use for these large customers is
5 expected. As a result, column (f) does not reflect any adjustments for
6 industrial plant closings.

7 6. Actual calendar year 2011 retail open access ("ROA") sales were
8 3,900.6 GWH. The Company's forecast reflects an expectation that the
9 ROA cap will continue to be filled with existing customer choice
10 enrollments. Approximately 792 MW of noncoincident customer load is
11 currently active, and is expected to continue at a similar level through the
12 test year period. The annual energy sales of active ROA load are expected
13 to be 3,934.6 GWH. Because the Company's forecast of test year ROA
14 sales is similar to 2011 historical usage, no adjustments for load shifting
15 between bundled service and ROA service are being presented in column
16 (g) of this exhibit.

17 7. Column (h) on page 1 of Exhibit A-10 (LDW-1) is labeled "Other
18 Miscellaneous Adjustments." The adjustment in column (h) adjusts
19 Miscellaneous Revenues by -\$2.0 million from 2011 actual results for
20 various miscellaneous revenue changes, primarily reductions in property
21 rental revenues (-\$1.7 million) and forfeited discounts (-\$0.3 million).

22 8. Revised rates were approved by the Commission in its June 7, 2012, Order
23 in case U-16794. The Company's forecast of revenue under current tariff

LINCOLN D. WARRINER
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1 rates for the test year period reflects the prices approved by the
2 Commission in that case. Updated estimates of the number of residential
3 customers that qualify for the Residential Income Assistance provision
4 have also been considered in determining the projected Base Tariff
5 Revenue. Projected sales levels are expected to increase from 2011 as a
6 result of improving economic conditions within the State of Michigan.
7 Column (i) on page 1 of Exhibit A-10 (LDW-1) reflects a sales increase of
8 593.7 GWH from weather adjusted 2011. This adjustment includes
9 reductions attributable to the Company's Energy Optimization Plan.
10 Specific economic factors considered in this forecast include Global
11 Insight's projections of Michigan population and household levels as well
12 as indicators of manufacturing and service sector employment. In order to
13 appropriately reflect underlying economic conditions in the Company's
14 test year revenue analysis, an adjustment was made to bring the test year
15 sales and revenues in line with the Company's current forecasts. The
16 analysis of sales and rate design changes result in an expected increase of
17 \$214.3 million of Base Tariff Revenues as shown in column (i) on page 1
18 of Exhibit A-10 (LDW-1).

- 19 9. Power costs discussed by Company witness David Ronk are expected to
20 be about \$2.1 billion dollars during the test year period. In order to make
21 sure that the Company's proposed rate increase in this case is not
22 influenced by the expectations for changes in power supply costs, column
23 (j) on page 1 of Exhibit A-10 (LDW-1) includes estimates of

LINCOLN D. WARRINER
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1 \$124.4 million of PSCR factor revenues and recognition of \$51.6 million
2 of projected intersystem sales revenue. These adjustments balance the
3 jurisdictional power costs with jurisdictional PSCR base and PSCR factor
4 revenues.

5 Q. Please summarize the impact these adjustments have on the projected test year sales and
6 revenues.

7 A. The Company's proposed test year jurisdictional revenues are \$3,923.5 million as shown
8 on line 26, column (k) of page 2 in my Exhibit A-10 (LDW-1).

9 Total Company electric deliveries are projected to increase about 154.9 GWH
10 between actual 2011 and the projected test year period (or 604.8 GWH over weather
11 normalized 2011). Weather increased usage in 2011 about 449.9 GWH above normal
12 weather conditions. Production capacity of semiconductor and solar energy components
13 within our service territory continues to increase, and electric service under the
14 Company's economic development rate E-1 is expected to be 184.4 GWH higher during
15 the test year than in 2011. In addition, improving economic conditions will result in
16 usage growth of 420.4 GWH, after accounting for savings from the Company's Energy
17 Optimization Plan.

18 In addition to changes in customer usage from 2011, the Company's revenue
19 outlook is influenced by the rates approved by the Commission in its Order in case
20 U-16794.

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 **PART 2: PROJECTED SALES AND REVENUES**

2 **HISTORICAL AND TEST YEAR SALES DETAIL**

3 Q. Please describe Exhibit A-10 (LDW-2).

4 A. Exhibit A-10 (LDW-2) is a five-page exhibit that summarizes by rate, and customer
5 class, sales and customer values for the historical year as well as the projected test year.
6 Pages 1 through 3 present the historical sales and average customer values for 2011. The
7 rows (Line 1 through 15) on this exhibit represent tariff rate categories, while the
8 columns (Column (c) through (k)) represent customer class categories. It is important to
9 note that on Pages 1, 2, and 3 of this exhibit the historical values for Interdepartmental,
10 Wholesale, and Intersystem sales are identified on line 14, which is titled "Other." The
11 Intersystem sales are included in the historical analysis because they are reported as part
12 of "Sales for Resale" within the Company's annual report to the Commission. On pages
13 4 and 5, which represent the test year forecast, only the Wholesale class is represented on
14 the "Other" line. For purposes of the forecast, Interdepartmental sales are split into
15 individual rate categories, and Intersystem sales are specifically excluded from the
16 forecast of electric deliveries. It is also important to note that historical actual sales on
17 page 1 include unbilled sales, which are quantified at the customer class level.

18 Q. Please describe how the weather normalized electric deliveries were estimated on page 2
19 of Exhibit A-10 (LDW-2).

20 A. Weather normalization coefficients were estimated using historical calendar deliveries
21 for the residential and commercial classes, and historical heating degree day and cooling
22 degree day indicators, for the 2003 to 2011 time period. Regression analysis was used to
23 estimate the value of the weather normalization coefficient for each class. The variation

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 in actual heating degree day and cooling degree day indicators from a 15-year average of
2 those indicators (based on 1997 through 2011) was multiplied by the corresponding
3 coefficient to determine the amount of weather normalization for each class. The
4 weather normalized sales for each class were then allocated to each rate code in relative
5 proportion to the actual sales volumes.

6 **FORECAST OF TOTAL ELECTRIC DELIVERIES**

7 Q. Please comment on the Company's current outlook for electric deliveries.

8 A. Improving economic conditions in the Michigan manufacturing sector, expectations for
9 increasing electric service under the Company's economic development rate E-1, and
10 consideration of average weather conditions are major factors in the Company's
11 expectation that test year electric deliveries will increase about 0.4% from 2011 actual
12 results. The forecast also reflects expected impacts related to the Company's Energy
13 Optimization Plan.

14 The forecast of electric deliveries includes projections of usage by bundled (or
15 full service) customers as well as ROA customers. The overall outlook for electric
16 deliveries is quantified on page 1 of Exhibit A-10 (LDW-3). Page 2 of this exhibit
17 reflects the outlook for full service sales, and page 3 of this exhibit quantifies the outlook
18 for ROA deliveries.

19 Q. Please describe the data contained in Exhibit A-10 (LDW-3).

20 A. Exhibit A-10 (LDW-3) documents the forecast of electric service area sales. Historical
21 values for 2004 through 2011 are also provided for reference. Page 1 summarizes the
22 forecast of total service area sales into four major categories: residential, commercial,
23 industrial, and other. Total system output is also reflected in column (i) of this exhibit.

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 Total system output is defined as the amount of energy that must be generated or
2 purchased to support the volume of electric service area sales as well as provide for
3 losses of energy over the transmission and distribution system. Page 2 summarizes the
4 bundled sales forecast. The Company provides both power supply and distribution
5 services to bundled customers. Page 3 documents the customer choice sales forecast.
6 The Company provides distribution services to customers who elect to participate in retail
7 open access, power supply services are provided to these customers by alternate energy
8 suppliers. The forecast of electric service area sales includes both jurisdictional and
9 non-jurisdictional sales.

10 Q. How were the residential forecasts developed?

11 A. The residential class forecasts were developed from forecasts of customer growth and
12 average use per customer.

13 1. Customer statistics were analyzed using a regression model to estimate
14 changes in residential customers based on projected changes in household
15 indicators for the State of Michigan. These Michigan level indicators
16 were further refined to quantify the historical and projected trends for the
17 geographic area of Michigan served by Consumers Energy. Household
18 indicators support the Company's expectation that residential customers
19 will increase slightly (by about 0.3%) from 2011 to 2013.

20 2. Average use forecasts were developed from regression models that
21 quantify the influence of billing cycle duration, weather conditions, and
22 seasonal factors on the average monthly usage of the residential class.
23 Economic factors such as the average household size, average household

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 income, and electricity price trends are also included. For purposes of this
2 forecast, future weather conditions are assumed to be equal to a 15-year
3 average of historical weather conditions from 1997 to 2011. Reductions in
4 the average use for the residential class reflect differences in weather
5 conditions between the normal weather test year and the warmer than
6 normal weather experienced during 2011.

- 7 3. The forecasts of monthly average use were then multiplied by the
8 forecasts of monthly customers to project the total residential deliveries.
9 The result of this calculation was then adjusted for the anticipated
10 reductions associated with energy efficiency programs and appliance and
11 lighting efficiency improvements (-332.9 GWH in the test year period).
12 Additional loads for plug-in hybrid vehicles (+15.8 GWH in the test year
13 period) are also considered in the forecast.

14 Q. How was the commercial class forecast developed?

15 A. The commercial forecast was estimated using regression analysis that quantifies the
16 influence of weather conditions, economic conditions, and seasonal factors on monthly
17 commercial class usage. Economic conditions are quantified by electric service area
18 indicators of service sector employment. For purposes of this forecast, future weather
19 conditions are assumed to be equal to a 15-year average of historical weather conditions
20 from 1997 to 2011. Adjustments to the forecast for energy efficiency programs
21 (-255.3 GWH during the test year time period) were also made as part of this forecast.

LINCOLN D. WARRINER
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1 Q. How was the industrial class forecast developed?

2 A. The industrial class forecasts were developed from forecasts of General Motors, Delphi,
3 and Nexteer customer usage and other industrial customer usage.

4 1. The General Motors, Delphi, and Nexteer usage forecast was developed
5 using regression analysis that quantifies the influence of Michigan
6 Transportation Equipment sector employment, and seasonal factors on
7 monthly usage of General Motors and Delphi accounts.

8 2. The industrial other usage forecast was analyzed in two subsets of
9 customer usage. The largest subset utilizes regression analysis to estimate
10 the influence of electric service area manufacturing employment trends,
11 combined with increasing trends in labor productivity on the monthly
12 usage of industrial customers other than General Motors, Delphi, Nexteer,
13 and a large producer of polycrystalline silicon. The industrial other
14 forecast also includes anticipated industrial class energy efficiency
15 program reductions (-235.6 GWH in the test year). The second subset of
16 the industrial other forecast includes a large producer of semiconductor
17 and solar energy components, which is included in the industrial other
18 category, but is analyzed individually based on expected monthly
19 maximum billing demands, billing days, hours per day, and load factor
20 considerations. The results of this approach were reconciled with
21 customer developed usage projections provided to the Company.

22 Q. How was the other class forecast developed?

23 A. The other class has three forecast components:

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 1. Street lighting usage was forecast using the August 2011 light inventory
2 levels for various types of lighting fixtures. Energy consumption is
3 estimated by multiplying the number of each type of fixture by its
4 associated wattage and the number of operating hours in each billing
5 month.

6 2. Interdepartmental usage was forecast using actual monthly usage results
7 for the 12-month time period ending August 2011.

8 3. Wholesale usage was estimated based on the 2012 PSCR application of
9 Alpena Power Company in MPSC Case number U-16880.

10 Q. Do these forecasts include adjustments for energy efficiency programs?

11 A. Yes.

12 Q. What method was used to adjust the forecast for energy efficiency programs?

13 A. Adjustments for energy efficiency were derived from the Company's Amended Energy
14 Optimization Plan, Case U-16670, which was filed with the Commission in August 2011.

15 Q. Please describe Exhibit A-10 (LDW-4).

16 A. Exhibit A-10 (LDW-4) identifies the forecast of annual system output (or generation
17 requirements), maximum demands, and annual load factor.

18 Q. How are the generation requirements estimated?

19 A. Generation requirements are estimated by dividing the calendar deliveries for each time
20 period by the Company's system efficiency factor of 92.76%. In other words, the level of
21 line loss is projected to be 7.24% of generation requirements. This estimate was based on
22 the 3-year average system efficiency for the period ending April 2007.

LINCOLN D. WARRINER
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1 Q. Please describe how the maximum demands that are shown in Exhibit A-10 (LDW-4)
2 were developed.

3 A. The summer peak forecast was developed as part of a monthly regression analysis that
4 quantifies the influence of base loads, cooling loads, and heating loads. The monthly
5 peak forecast was developed utilizing regression models that quantify the influence of
6 overall changes in energy usage, household growth, and high and low daily temperatures
7 on the day of the system peak. For purposes of this forecast, future weather conditions
8 are assumed to be equal to a 15-year average of historical peak day temperatures from
9 1997 to 2011. A rank and average method was used to estimate peak day weather
10 conditions for each month.

11 Q. Please describe how the summer peak demand forecast is adjusted to incorporate the
12 effect of energy efficiency programs?

13 A. The peak demand adjustments for energy efficiency are derived directly from the
14 Company's Amended Energy Optimization Plan that was filed with the Commission in
15 August 2011.

16 Q. Are any other adjustments included in the summer peak demand forecast?

17 A. Yes, there are two programs under development that are expected to reduce load at peak
18 demand times. The first program, direct load management is projected to impact the
19 Company's peak demand starting in 2013. The other program under development is the
20 Company's dynamic peak pricing (or demand response) program. The forecast includes
21 adjustments for dynamic peak pricing starting in 2015.

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 Q. How is the load factor in column J of Exhibit A-10 (LDW-4) calculated?

2 A. The system load factor is a function of the annual Generation Requirements and the
3 Summer Peak. Generation Requirements are first divided by the number of hours in a
4 year, then divided again by the Summer Peak.

5 **FORECAST OF ENERGY OPTIMIZATION SALES REDUCTIONS**

6 Q. Please describe Exhibits A-10 (LDW-5).

7 A. Exhibit A-10 (LDW-5) summarizes the planned impacts of the Company's Amended
8 Energy Optimization Plan, which was filed with the Commission in August of 2011.
9 These impacts are derived directly from summary tables contained within that filing.

10 **ECONOMIC OUTLOOK**

11 Q. Please describe Exhibit A-10 (LDW-6).

12 A. Exhibit A-10 (LDW-6) is a two page exhibit that identifies the economic outlook that was
13 used as one of the inputs into the Company's projections of future electric deliveries.
14 The Michigan indicators included on page 1 in these exhibits were taken directly from
15 economic forecasts provided by Global Insight in January of 2012. These indicators are a
16 starting point in the analysis of economic trends for the Consumers Energy service area.
17 The service area indicators included on page 2 were estimated by applying annual service
18 area shares estimated from county level forecasts provided by Global Insight in
19 September of 2011 to the January 2012 Michigan forecast update.

20 Q. Why are service area indicators being estimated from indicators for the State of
21 Michigan?

22 A. I have analyzed long-range trends of various indicators at a county level, and have
23 concluded that over time, the geographic area served by Consumers Energy electric

LINCOLN D. WARRINER
DIRECT TESTIMONY

1 service has gradually developed into a larger portion of the total Michigan economy. The
2 approach of applying service area shares to the Michigan forecast allows the Company to
3 use the most current outlook for the state in its forecasts, since county level forecasts are
4 updated twice a year, while state level economic forecasts are updated each month.

5 Q. Does this complete your direct testimony?

6 A. Yes.

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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

REBUTTAL TESTIMONY

OF

LINCOLN D. WARRINER

ON BEHALF OF

CONSUMERS ENERGY COMPANY

March 2013

LINCOLN D. WARRINER
REBUTTAL TESTIMONY

1 Q. Please state your name and business address.

2 A. My name is Lincoln D. Warriner, and my business address is One Energy Plaza, Jackson,
3 Michigan.

4 Q. Are you the same Lincoln D. Warriner who presented direct testimony in this case
5 regarding Consumers Energy Company's ("Consumers Energy" or the "Company")
6 analysis of historical and projected test year electric operating revenue under current
7 tariff rates for use in this rate proceeding?

8 A. Yes.

9 Q. What is the purpose of your rebuttal testimony in this proceeding?

10 A. The purpose of my testimony is to rebut the Michigan Public Service Commission Staff's
11 ("Staff") projection of \$54.2 million for miscellaneous revenue. The Staff's projection is
12 described in the direct testimony and exhibits of Ms. Poornima Jayasheela. Staff's
13 projection is \$4.0 million higher than the Company's test year projections, and should be
14 rejected for three primary reasons, which will be discussed in the remainder of my
15 rebuttal testimony.

16 Q. How did Ms. Jayasheela describe the analysis Staff used to project miscellaneous
17 revenues?

18 A. On page 4 of her testimony, Ms. Jayasheela indicates that Staff developed test year
19 miscellaneous revenues using a three-year historical average. The historical time period
20 of 2009 to 2011 was used for the purpose of making this calculation.

21 Q. Did Staff exclude any historical revenue from this three-year average?

22 A. Yes. Staff excluded \$9 million of transmission service related miscellaneous revenue,
23 which represented an accounting reversal of a reserve for a potential refund from a prior

LINCOLN D. WARRINER
REBUTTAL TESTIMONY

1 period. I agree that this revenue item should be excluded when comparing the
2 Company's estimate of test year miscellaneous revenue to historical values.

3 Q. Are there any other miscellaneous revenue items that should be excluded from the rate
4 case test year?

5 A. Yes. Staff's use of a three-year historical average includes revenue from purchased
6 power administrative fees. However, as identified on page 8 of my original direct
7 testimony in this case, the Company reduced historical miscellaneous revenues for
8 purchased power administrative fees because those revenues are treated as a credit to the
9 recovery of power supply costs in the Company's PSCR litigation conducted under
10 1980 PA 304. For example, in the Company's 2011 PSCR Plan Reconciliation Case No.
11 U-16432-R, Company witness David Ronk, Jr. identified the \$998,616 credit to
12 purchased power costs from administration fees in column (d) of his Exhibit A-20
13 (DFR-1). Since these revenues are used to offset power supply costs in PSCR
14 reconciliations, it would constitute double counting to count them as an offset to tariff
15 revenue requirements in general rate cases. Use of a three-year average of purchase
16 power administrative fees overstates the Staff's miscellaneous revenue projection by
17 \$1,006,810.

18 Q. Are there any other miscellaneous revenue items that are overstated by Staff's use of a
19 three-year average?

20 A. Yes. Pole attachment revenues are overstated by Staff's use of a three-year average. An
21 order by the Federal Communications Commission ("FCC") on April 7, 2011, required
22 electric utility companies to reduce the rates charged to telecommunications service
23 providers in an effort to minimize the difference in rental rates paid for attachments that

LINCOLN D. WARRINER
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1 are used to provide voice, data, and video services. The intent of the FCC in reducing
2 these rates was to encourage competition, affordability, and availability of advanced
3 communications services, including broadband. Since these lower rates went into effect
4 during 2011, use of any historical revenues prior to the full implementation of these rates
5 overstates expected test year revenues. Staff's use of a three-year average for pole
6 attachment revenues results in an overstatement of test year revenues of \$2,821,902. The
7 Company's test year forecast reflects a reduction from 2011 of \$1.7 million in property
8 rental revenues as described on page 9 of my original direct testimony in this case.

9 Q. Do you have any concerns about the Staff's three-year average approach to estimating
10 job work revenue for the test year?

11 A. Yes. Staff witness Brian A. Welke adopted the Company's estimate for job work
12 expense in his analysis of Projected Other Operations and Maintenance Expense (Exhibit
13 No. S-3, Schedule No. C5, line 12). Staff's calculation of a three-year average for job
14 work revenue has the effect of overstating the amount of margin from job work activities
15 included in the Staff's analysis of revenues and expenses. It is unreasonable for Staff to
16 expect the Company to increase its revenue from job work activities by \$756,595 without
17 incurring additional expenses to perform the work.

18 Q. Please summarize your analysis of the Staff's revenue projection.

19 A. Staff made two adjustments to the Company's test year revenue projection that included a
20 \$0.3 million increase in wholesale revenue and a \$4.0 million increase in miscellaneous
21 revenues. My analysis of the three-year average approach suggested by Staff identified
22 three corrections to the Staff's estimate that would reduce test year revenues by
23 approximately \$4.6 million. These corrections include a \$1 million correction to remove

LINCOLN D. WARRINER
REBUTTAL TESTIMONY

1 purchased power administration fee revenues, a \$2.8 million correction to align pole
2 attachment revenues with rates currently allowed by the FCC, and a \$0.8 million
3 correction to align the Staff's job work revenue projection with Staff's job work expense
4 projection. Because these corrections more than offset the adjustments made by Staff to
5 the Company's projection of test year revenue, it is my recommendation that the
6 Commission adopt the Company's originally filed projection of revenues for the 2013
7 test year.

8 Q. Does this complete your rebuttal testimony?

9 A. Yes.

1 JUDGE CUMMINS: With regard to the
2 portions of Exhibit A-10 described by Mr. Chambers, is
3 there any objection to the receipt of these exhibits?
4 Very well, that being the case, Exhibit A-10, limited to
5 at this point in time LDW-1 through LDW-6 are received
6 into evidence.

7 MR. CHAMBERS: Your Honor, I believe that
8 completes the witnesses that are scheduled for today that
9 other parties have indicated they do not have cross for.

10 At this time Consumers Energy calls Amy
11 Conrad to the witness stand.

12 - - -

13 A M Y M. C O N R A D

14 was called as a witness on behalf of Consumers Energy
15 Company and, having been duly sworn to testify the truth,
16 was examined and testified as follows:

17 DIRECT EXAMINATION

18 BY MR. CHAMBERS:

19 Q Would you state your name and business address for the
20 record, please.

21 A Amy M. Conrad, One Energy Plaza, Jackson, Michigan.

22 Q Ms. Conrad, did you prepare or cause to be prepared for
23 purposes of this case testimony consisting of a cover
24 page labeled Direct Testimony of Amy M. Conrad, followed
25 by 42 pages of questions and answers?

1 A I did.

2 (Christopher Bzdok entered the hearing room.)

3 Q Did you also, in connection with this case, prepare or
4 cause to be prepared rebuttal testimony consisting of a
5 cover page labeled Rebuttal Testimony of Amy M. Conrad,
6 followed by 14 pages of questions and answers?

7 A I did.

8 Q In connection with your direct testimony, did you prepare
9 or cause to be prepared Revised pages 1 and 14,
10 identifying revisions on page 1, line 4, page 1, line 19,
11 and page 14, line 8?

12 A I did.

13 Q Is it your intention to adopt those changes today as part
14 of your testimony?

15 A Yes.

16 Q If I were to ask you the questions contained in your
17 direct testimony and in your rebuttal testimony, would
18 you give me the answers that are indicated in the
19 prefiled testimony subject to the revisions?

20 A Yes.

21 Q In connection with your direct testimony did you prepare
22 or cause to be prepared three exhibits which have been
23 marked for identification as Exhibits A-16, A-17, and
24 A-18?

25 A Yes.

1 Q Do you have any additions, corrections, or modifications
2 that you would like to make to any of those exhibits at
3 this time?

4 A No.

5 MR. CHAMBERS: Your Honor, at this time I
6 move to bind the direct testimony and the rebuttal
7 testimony of Amy Conrad into the record. In addition, I
8 move for the admission of Exhibits A-16, A-17, and A-18,
9 and tender Ms. Conrad for cross-examination.

10 JUDGE CUMMINS: Thank you, Mr. Chambers.
11 Any objection to binding in the direct and rebuttal
12 testimony with the revisions indicated of Ms. Conrad?
13 Hearing none, the direct and rebuttal testimony of
14 Ms. Conrad will be bound into the record.

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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 generation and distribution of)
electricity and for other relief.)
_____)

Case No. U-17087

DIRECT TESTIMONY

OF

AMY M. CONRAD

ON BEHALF OF

CONSUMERS ENERGY COMPANY

September 2012

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. Please state your name and business address.

2 A. Amy M. Conrad, One Energy Plaza, Jackson Michigan.

3 Q. In what capacity are you employed?

4 A. I am employed as ~~Principal Compensation Analyst~~ ^{Director of Compensation} for Consumers Energy Company
5 (“Consumers Energy” or the “Company”).

6 Q. What is your educational background?

7 A. I graduated from Central Michigan University in 1999 with a Bachelor of Science degree
8 in Business Administration with a major in Accounting. In addition, I am designated a
9 Certified Compensation Professional and Certified Executive Compensation Professional
10 by World at Work and a Certified Public Accountant by the Michigan Association of
11 Certified Public Accountants. World at Work is an international professional
12 organization focused on human resources issues, including compensation, benefits, work
13 life, and integrated total rewards to attract, motivate, and retain a talented work force.

14 Q. What have your job responsibilities entailed with Consumers Energy?

15 A. In February 2002, I joined Consumers Energy as Financial Reporting and Technical
16 Accounting Analyst. My duties included accounting and reporting of equity based
17 compensation, technical accounting standard research, and preparation of quarterly and
18 annual Securities and Exchange Commission (“SEC”) filings. After eight years of
19 progressing responsibilities in this role, I transferred to my ~~current~~ position as Principal
20 Human Resource Consultant. I currently have responsibility for administering
21 Consumers Energy’s compensation function. This includes administration for all
22 non-union employee compensation, including developing compensation programs
23 designed to attract and retain a qualified workforce for the Company. My duties include

AMY M. CONRAD
DIRECT TESTIMONY

1 gathering of comparable wage and salary data in order to determine how Consumers
2 Energy's pay level compares to the labor market and developing compensation programs
3 that are competitive and deliver pay to employees that is fair and equitable and that
4 motivates employees to perform at their full potential.

5 My responsibilities also consist of assisting with preparation of materials for the
6 Compensation Committees of the Consumers Energy and CMS Energy Boards of
7 Directors, including the Compensation Discussion & Analysis section of the annual
8 Proxy statement for the top six officers.

9 Q. What is the purpose of your testimony?

10 A. The purpose of my testimony is to provide support for Consumers Energy's request for
11 rate recovery for costs of annual Employee Incentive Compensation Plan ("EICP")
12 incentives and the long-term incentive plan (sometimes referred to as the "restricted
13 stock" plan) at target levels.

14 First, I will discuss Consumers Energy's overall compensation philosophy. In
15 this section of my testimony, I will discuss the importance of paying employees a
16 competitive level of compensation and the reasonableness of the overall compensation
17 levels that the Company is requesting in this case. In addition, I will discuss: (i) the fact
18 that EICP compensation is part of an employee's overall compensation and not in
19 addition to it and (ii) why Consumers Energy has included incentive plans as part of
20 overall compensation.

21 Second, I will discuss the EICP incentives and provide support for the Company's
22 request for rate recovery in this case related to Consumers Energy's non-officer and
23 officer EICP. In my testimony I will discuss the design of the EICP. As I will discuss

AMY M. CONRAD
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1 later, the Company's incentive compensation plans have safety metrics, reliability
2 metrics, customer value metrics, and financial metrics. In addition, I will discuss the
3 long-term incentive plan and provide support for the Company's request for rate recovery
4 in this case related to Consumers Energy's long-term incentive plan.

5 Third, I will discuss customer-related benefits that result from use of the incentive
6 plans and how customers are best served when Consumers Energy can attract, retain, and
7 motivate a talented work force with compensation packages that are competitive and fair.

8 Q. Please summarize your conclusions.

9 A. My conclusions include the following: (i) use of incentive compensation by utility
10 companies is an accepted, common, and reasonable practice; (ii) Consumers Energy's
11 decision to make a portion of compensation subject to incentives is reasonable; (iii) the
12 amount of overall compensation included by Consumers Energy in this case is reasonable
13 and is reasonably necessary to attracting and retaining a talented workforce; (iv) incentive
14 compensation is part of the reasonable level of compensation and not in addition to it;
15 (v) recovering costs of Consumers Energy's employee incentive plans will not result in
16 excess rates; (vi) Consumers Energy's EICP operational and performance goals and
17 thresholds provide customer-related benefits; and (vii) the EICP goals provide
18 customer-related benefits at no incremental cost to the customers.

19 Q. How is the remainder of your testimony organized?

20 A. The remainder of my testimony is organized as follows:

AMY M. CONRAD
DIRECT TESTIMONY

1 **I. OVERVIEW**

2 **II. EMPLOYEE COMPENSATION PHILOSOPHY**

3 **III. INCENTIVE COMPENSATION PLANS**

4 **i. DESCRIPTION OF INCENTIVE PLANS**

5 **ii. ASSESSMENT OF CUSTOMER BENEFITS OF THE INCENTIVE**
6 **COMPENSATION PLANS**

7 **IV. CONCLUSION**

8 Q. Are you sponsoring any exhibits?

9 A. Yes. I am sponsoring the following exhibits:

10 Exhibit A-16 (AMC-1) EICP Performance Measures

11 Exhibit A-17 (AMC-2) Growing Forward Goals

12 Exhibit A-18 (AMC-3) Summary of Requested Expenses

13 Q. Were these exhibits prepared by you or under your supervision?

14 A. Yes.

15 **I. OVERVIEW**

16 Q. How does Consumers Energy structure non-officer compensation for its salaried
17 employees?

18 A. Consumers Energy first determines what a competitive level of pay is for salaried
19 non-officer employees. It does so using various market surveys. Consumers Energy then
20 structures the compensation by allocating this market-based wage between base salary
21 and incentive compensation. The incentive compensation is part of the overall
22 competitive level. It is not in addition to it. Total compensation is targeted at
23 approximately the market median (50th percentile).

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. How does Consumers Energy structure officer compensation?

2 A. Officer compensation levels are determined by the Compensation Committees of the
3 Boards of Directors of Consumers Energy and CMS Energy. The Company creates a
4 compensation package for officers that deliver base salary, annual incentive
5 compensation, and long-term incentive compensation targeted at the median or
6 50th percentile of the competitive market. In determining individual officer compensation
7 levels, the Compensation Committees are advised by an independent consultant, and take
8 into consideration market research, experience levels, and individual contributions.

9 Q. What is the difference between short-term incentive pay and long-term incentive pay?

10 A. Short-term incentive pay is designed to focus and reward performance over periods of
11 approximately one year or less. Long-term incentive pay is designed to focus and reward
12 performance over a period of longer than one year. Long-term incentive pay is also
13 designed to reward good long-term decisions for the Company and for customers. The
14 EICP plans are a form of short-term incentives. Restricted stock is a form of a long-term
15 incentive.

16 Q. In this proceeding, is the Company requesting recovery in rates of all electric expenses
17 related to incentive compensation plans?

18 A. No. While the Company believes that both officer and non-officer incentive
19 compensation expenses are reasonable, the Company in this case is excluding the costs of
20 incentive compensation for the top six officers as identified by the SEC proxy rules from
21 its request.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. Why is the Company requesting recovery in rates of incentive compensation expenses?

2 A. Consumers Energy uses market data to determine an overall competitive level of
3 compensation. The overall compensation levels, including the officer and non-officer
4 incentive compensation, are reasonable compared to the market. Compensation levels
5 without the incentive payments would be below market competitive levels. Paying
6 non-competitive pay levels of compensation would result in a lower qualified workforce.
7 In order to hire and retain qualified personnel it is necessary to either pay a competitive
8 incentive or increase base salaries. The incentive compensation costs are reasonable
9 costs of doing business.

10 Use of incentive mechanisms is a recognized management technique for
11 companies, including utility companies. As I discuss later in my testimony, incentive pay
12 is the number one design used to influence short- to mid-term business results. Incentive
13 mechanisms help communicate priorities, engage the employees in business success,
14 reward valued skills and behaviors, and create business understanding for employees.
15 Consumers Energy's incentive programs are structured in a way that is designed to help
16 keep non-officers and officers focused on such areas as safety, reliability, and customer
17 value. The incentive compensation program encourages employees to deliver their best
18 performance for the Company's customers.

19 Q. Who is eligible for the EICP incentives?

20 A. All non-union employees are eligible for EICP. Both non-officers and officers
21 participate in an annual EICP incentive plan.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. How are the EICP incentives structured?

2 A. The EICP incentive structure incorporates: (i) safety; (ii) reliability; (iii) customer value;
3 and (iv) financial incentive measures. The Company believes that performance in these
4 areas is critical for the Company's success in its electric and gas public utility business.

5 The non-officer EICP equally weights the operational and performance measures
6 of safety, reliability, and customer value with the financial measures:

- 7 - Half (50 percent) of employee's 2013 incentive will be based on
8 achievement of 11 operational and performance measures for safety,
9 reliability, and customer value.
- 10 - Half (50 percent) of employee's 2013 incentive will be based on the
11 achievement of two financial measures, earnings per share ("EPS") and
12 operating cash flow. Consumers Energy is a vital part of the Michigan
13 economy and it is important that the utility remain financially strong so
14 that it can provide the utility service that customers expect and deserve.
15 Financial health also leads to reduced costs of capital.

16 The goals are the same for the officer EICP incentive plan, but the weightings are
17 different. For the officer plan, the safety, reliability, and customer value goals are a plus
18 or minus modifier to the financial goals. I will discuss this difference in weightings later
19 in my testimony.

20 Q. How is the long-term incentive plan structured?

21 A. The long-term incentive award is an equity-based plan that involves issuance of restricted
22 stock with a three-year cycle period. The long-term incentive plan has two components -
23 a performance component (75 percent) and tenure component (25 percent).

24 The long-term incentive plan performance component - relative total shareholder
25 return ("relative TSR"), compares the shareholder returns of CMS Energy to the
26 shareholder returns of other specified utility companies (utilities in the S&P 400 Midcap
27 and in the S&P 500 indices). The Company's long-term incentive program is based

AMY M. CONRAD
DIRECT TESTIMONY

1 primarily on relative TSR because it offers a head-to-head comparison of how well the
2 management team performed compared to other management teams in the utility
3 industry.

4 The Company also awards a portion of long-term incentive compensation on the
5 basis of continued employment (referred to as “tenure” or “tenure-based”). The
6 employee will receive stock upon remaining employed over a three-year performance
7 period. The tenure-based restricted stock helps build executive share ownership,
8 alignment with shareholder and customer interests, and serves as a retention mechanism.

9 Q. Are officers the only eligible participants in the long-term incentive plan?

10 A. No. Performance-based and tenure-based restricted stock is also awarded to non-officer
11 directors as part of their annual compensation and helps to retain, motivate, and reward
12 key salaried employees for their significant contributions to the success of Consumers
13 Energy.

14 **II. EMPLOYEE COMPENSATION PHILOSOPHY**

15 Q. What is Consumer Energy’s philosophy about the overall level of compensation?

16 A. The Company’s management believes Consumers Energy should pay a fair and
17 reasonable salary, comparable to the market that is equitable to employees, consistent
18 with Company values and strategies, and that supports the highest level of customer
19 service at a reasonable cost.

20 Q. What are the components of Consumers Energy’s compensation for salaried employees?

21 A. There are two parts of overall compensation for salaried employees of Consumers
22 Energy. The first part is base pay. The second part for salaried employees is annual
23 employee incentive compensation.

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1 Q. What are the components of Consumers Energy's compensation for officers?

2 A. There are three parts of overall compensation for officers of Consumers Energy. The
3 first two parts are cash compensation through base pay and annual incentive
4 compensation. The third part is equity based long-term incentive. For officers,
5 compensation is viewed as a three-legged stool: (1) base salary; (2) short-term incentive;
6 and (3) long-term incentive. Should any one component be eliminated, one or both of the
7 other components would need to be increased to remain competitive.

8 Q. Why does the Company make a portion of compensation subject to incentives?

9 A. A wide body of research supports the view that variable pay works. One researcher
10 states, "theory and research show that incentive pay can substantially increase individual
11 and organizational performance, and can represent a powerful tool for establishing a
12 competitive advantage within an industry," (Dow Scott, "Incentive Pay: Creating a
13 Competitive Advantage - World-at-Work Press, 2007). I agree with this assessment.
14 When properly selected and implemented, incentives motivate employees, focus
15 employees on a company's goals, and increase both individual work performance and
16 team performance. When goals are challenging yet achievable, employees are motivated
17 to increase productivity. In addition, incentives increase a company's ability to attract,
18 hire, and retain qualified and motivated individuals. A study by the International Society
19 of Performance Improvement showed that incentive pay programs increase performance
20 by an average of 22 percent. (International Society of Performance Improvement,
21 "Incentives Motivation and Workplace Performance Research and Best Practices" Spring
22 2002). As stated by the Society of Human Resource Management:

23 "Research has demonstrated that some human resource programs
24 and initiatives produce a significant impact on performance in

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1 organizations (as measured by factors such as quality, productivity,
2 speed, customer satisfaction and unwanted turnover). The two
3 initiatives that consistently showed statistically significant positive
4 results were linking pay to performance and using variable pay.
5 Research has established the potential of variable pay to produce
6 the desired business results.” (Robert Greene, Variable Pay: How
7 to Manage it Effectively, Society of Human Resource
8 Management, April 2003).

9
10 As I discuss in my testimony, Consumers Energy has adopted incentives that are
11 designed to emphasize operational and performance criteria in four areas that are critical
12 to the Company’s utility business. Focusing employees on these goals provides both
13 qualitative and quantitative benefits for Consumers Energy’s utility customers.

14 Q. Are the overall compensation levels for employees subject to the non-officer EICP
15 reasonable?

16 A. Yes. Overall compensation levels for employees subject to the non-officer EICP and
17 management’s decision of how to allocate the overall compensation between base salary
18 and EICP are reasonable.

19 Q. How does Consumers Energy determine what level of overall compensation for
20 non-officers is reasonable?

21 A. First, Consumers Energy’s management targets overall compensation to the market
22 median. Second, Consumers Energy’s management actively reviews compensation
23 levels so that employees are neither overpaid nor underpaid relative to market. Third, the
24 Company uses a rigorous survey process which uses valid and reliable data from multiple
25 sources to determine median levels of compensation. Fourth, the Company’s overall
26 compensation, including both the base pay and the incentive compensation, is at
27 approximately the market median. The fact that a portion of the compensation is in the

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1 form of an incentive payment does not mean that employees are paid in excess of market
2 rates when they receive that incentive payment.

3 Q. Would it be reasonable for Consumers Energy to pay employees below market level on
4 an ongoing basis?

5 A. No.

6 Q. Why would it be unreasonable for Consumers Energy to pay below market level?

7 A. Consumers Energy has a responsibility to customers to employ a competent workforce
8 that is ready, willing, and able to provide service for our customers. Paying competitive
9 wages and salaries is necessary in order to fulfill that commitment. It would not be
10 reasonable or fair to the Company, customers, or employees for the Commission to set
11 rates at a level that did not include reasonable levels of overall compensation.

12 The level of service our customers deserve requires a qualified, experienced, and
13 motivated workforce. The Company is able to attract, retain, and motivate talented
14 employees when its overall compensation is competitive with market levels. A decision
15 to compensate employees below market levels would detract from the Company's ability
16 to assemble the committed workforce our customers deserve. Over time, this would be
17 detrimental to customers, as well as being unfair to our diligent, hardworking employees.
18 Compensating employees below market levels will eventually result in them leaving for
19 jobs that are paying at market levels. Over time, the workforce would tend to be less
20 qualified, less experienced, or less capable (as the most capable would, in general, tend to
21 go to employers paying at competitive levels). This in turn could lead to less efficiency
22 and could result in a need to hire more employees to produce the same service to
23 customers, thus increasing costs to our customers.

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1 Q. How does the Company determine the level of overall compensation for salaried
2 non-officer employees?

3 A. For salaried non-officer employees the Company uses salary survey data from utility and
4 energy companies. Using this survey data, a benchmarking analysis of total
5 compensation (base pay and incentive pay) is made between the Company's jobs and
6 comparable survey jobs. Benchmarking analysis is a comparison of jobs commonly
7 found in the labor marketplace and/or a job that is highly relevant/populated within a
8 company. This comparison indicates where the Company's pay stands relative to the
9 market. The Company's goal is to target overall pay levels within plus or minus
10 5 percent of the market median. While pay for individuals inevitably varies from the
11 survey market levels due to differences in experience levels, education, job performance,
12 longevity, position responsibilities, etc., the survey data indicate that the Company's
13 overall non-officer compensation levels, assuming the EICP payment at the target level,
14 are on average within target pay level of plus or minus 5 percent of market median.
15 Paying compensation that approximates the market median is particularly important
16 given that Consumers Energy will have a particular need over the next few years to hire
17 engineers to staff various projects as Consumers Energy and the State move forward, as
18 well as due to significant attrition. In competing for engineering, as well as other
19 personnel, it will be important to have a reputation for paying a competitive level of
20 overall compensation. Excluding the incentive targets results in the Company's
21 competitive pay levels being approximately 5 percent to 10 percent below market level.

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1 Q. How do you know the market data that the Company is using are appropriate and are not
2 inflating salary levels?

3 A. The Company uses a number of survey sources to compare to the non-officer salaried
4 workforce. The Company participates in two industry surveys that are conducted
5 annually on behalf of the Edison Electric Institute (“EEI”) and on behalf of the American
6 Gas Association (“AGA”). Both of these surveys are conducted by independent survey
7 firms which report data on an anonymous basis. The data from EEI and AGA are our
8 primary sources of compensation information. The Company also participates and uses
9 EAP Data Information Solutions, LLC, an independent survey firm serving the energy
10 industry, for non-officer hourly workforce market data. To supplement this data, the
11 Company uses a reputable national on-line survey resource (CompAnalyst) which has
12 survey data from a wide variety of independent sources. In every instance when using
13 the survey data the Company looks at the median total compensation (base pay and
14 incentive) reported for highly populated jobs for which there is a comparable match. In
15 this way, the Company is matching the relevant market, not trying to lead the market and
16 thus not inflating our overall compensation above prevailing market levels. The
17 Company also looks at data only from companies who are in the utility and energy
18 industry, not data from high paying technology companies or pharmaceutical companies.
19 By looking at three survey sources we can determine if any one source is varying
20 significantly from another.

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1 Q. Can you give an example of the relationship between the Company's pay levels and the
2 market's pay levels?

3 A. Yes. For the Company's Administrative Assistant III (150 employees) job, the
4 Company's average salary plus incentive target (overall compensation target) is
5 7.6 percent below the market overall compensation median. For Administrative
6 Specialist II (160 employees) the Company's level is 0.4 percent above the market. For
7 Technical Specialist II (117 employees) the Company's level is 7.7 percent below the
8 market. For Senior Technician (81 employees) the Company's level is ~~2.7~~^{4.0} percent below
9 the market. For Senior Engineer II (131 employees) the Company's level is 8.8 percent
10 below the market. For Gas Field Leader (91 employees) the Company's level is
11 10.5 percent below the market. For BTS Technical Lead/Specialist I (90 employees) the
12 Company's level is 14.9 percent below the market. For Senior Engineering Technical
13 Analyst II (43 employees) the Company's level is 3.9 percent above the market. These
14 eight jobs are among the most highly populated of our salaried workforce. There are
15 863 employees in these eight jobs which represent approximately 19 percent of the
16 salaried workforce.

17 Q. Are incentive plans common in the utility industry?

18 A. Yes, incentive plans are quite common. Annual incentive programs are a critical and
19 highly integral part of competitive compensation packages for many organizations.
20 Research from Towers Watson 2011 General Industry Salary Budget Survey Report
21 indicates that approximately 80 percent of companies offer annual incentive (bonus
22 and/or variable pay) programs. That number is slightly higher at 81.2 percent for those
23 companies within the utility industry sector. An analysis of the utility industry sector

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1 survey respondents was performed to determine what percentage of their business related
2 to electric regulated revenue. Where data was available, electric regulated revenue
3 averaged 63 percent. The survey data support the conclusions that including incentive
4 pay as part of a competitive pay package is a standard industry practice, and is required to
5 attract and retain good employees.

6 A 2012 Mercer study of more than 1,200 organizations reveals that actual
7 company spending on variable pay for salaried exempt employees as a percentage of pay
8 is 12.0 percent and salaried/hourly non-exempt employees as a percentage of pay of
9 6.0 to 7.0 percent for energy companies. The survey also indicates that 80 to 82 percent
10 salaried/hourly non-exempt employees in the energy sector are eligible for annual
11 incentive compensation and this number increases to 85 percent for salaried
12 professionals. A 2009 Hewitt Associates study of more than 1,100 organizations further
13 reports that companies were budgeting variable pay for salaried exempt employees at
14 11.8 percent and 5.5 percent to 6.1 percent for salaried/hourly non-exempt employees for
15 2010. Ken Abosch, leader of Hewitt's North American Broad-Based Compensation
16 Consulting business, added:

17 "Over the past decade, we've seen companies steadily shift from a
18 fixed pay model to one that emphasizes true performance based
19 awards, and we expect this trend will continue."

20 Consumers Energy's practice of making a portion of overall employee
21 compensation subject to incentives is consistent with best practices for compensation.

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1 Q. Why is the use of incentive pay such a widespread practice?

2 A. Incentive pay is the number one design used to influence short- to mid-term business
3 results. Coupled with clear strategy, solid leadership and good, safe working conditions,
4 variable pay incentive designs:

- 5 - Increase employee understanding of what is important to the Company;
- 6 - Increase employees identification with the Company's success and the
7 factors by which it is measured;
- 8 - Reward valued skills and behaviors; and
- 9 - Enhance employee engagement by educating them on how and why their
10 contributions will benefit them, the Company, and our customers.

11 Dividing overall compensation between base salary and incentive compensation is
12 an approach that is common and effective in business today.

13 Q. How many employees does the Company have that will be eligible for the non-officer
14 EICP payout?

15 A. Consumers Energy has approximately 4,300 employees (total utility) that are eligible to
16 receive an incentive if and when the requirements for a payout are met. The risk of no
17 payout is the same for all of these eligible employees. Either every eligible employee
18 receives a payout or no one receives any incentive compensation.

19 Q. How did the Company determine the level of compensation that would be provided as
20 incentive compensation for these eligible employees?

21 A. The EICP target level for each pay grade was established by measuring the difference
22 between the Company's base salary target and the market's overall compensation level.
23 The EICP compensation is part of the overall competitive level of compensation, not in
24 addition to it.

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1 Q. Is there an alternative to providing incentive pay for salaried employees?

2 A. The alternative would be to increase the base compensation to a level that approximates
3 the overall competitive level of compensation. Prior to 2003, employees below salary
4 grade 19 were not eligible for incentive awards and their full compensation was in base
5 pay, which was recovered in rates. As a result, base pay was targeted at the market's
6 overall compensation. The Company needed to target base pay at this higher level in
7 order to attract and retain employees. Absent the higher base pay, Consumers Energy's
8 compensation offering would not have been competitive with the labor market. For
9 example, if our base target was \$50,000 for a hypothetical job and market base average
10 pay was \$50,000 plus a \$2,000 incentive award, then the Company would need to offer
11 \$52,000 to match the market's current pay. So the alternative to having an incentive
12 component of overall compensation would be to raise base pay to the market's overall
13 compensation. Eliminating incentive pay would result in the same costs, but the loss of
14 incentives that help focus employees on safety, reliability, and customer value goals.

15 The Company's overall compensation needs to be comparable to the market for
16 salaried employees regardless of whether it is composed of only base pay or composed of
17 base pay plus the target incentive award amount. The Company has maintained overall
18 compensation at competitive levels through the incentive plan. But for the incentive
19 plan, the Company's non-officer base salaries for 2012 would be less than overall
20 competitive compensation levels.

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1 Q. Would elimination of incentive pay be in the best interests of customers?

2 A. No. With incentive compensation, the employees and the Company as a whole must
3 re-earn the at-risk compensation each year. If high levels of performance are not met
4 each year, incentive pay can be reduced or eliminated. The elimination of variable
5 “at-risk” pay would create a situation where all compensation is guaranteed and would
6 remove an important incentive to improve service. This result would be counter to
7 customer interests.

8 Q. How does the Company determine the level of overall compensation for officers?

9 A. A utility must maintain a competitive total compensation package in order to attract and
10 retain executive talent. As discussed in the Overview section of my testimony,
11 Consumers Energy creates a compensation package for officers that deliver base salary,
12 annual incentives, and long-term incentives targeted at the 50th percentile of the market,
13 as defined by a Compensation Peer Group approved by the Compensation Committees of
14 the Boards of Directors. The Compensation Peer Group consists of energy companies
15 comparable in business focus and size to CMS Energy with which the Company might
16 compete for executive talent. The Compensation Peer Group currently includes
17 15 companies.

18 Q. How do you know the market data that you are using for officer compensation is
19 appropriate and are not inflating salary levels?

20 A. Annually, the Compensation Committees engages an independent consultant to provide
21 advice and information regarding compensation practices of the Compensation Peer
22 Group as well as additional information from published surveys of compensation in the
23 public utility sector and general industry. During the Compensation Committees’ review

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1 of officers' compensation levels, the Compensation Committees considers the advice and
2 information received from the Compensation Committees' independent compensation
3 consultant; however, the Compensation Committees are ultimately responsible for
4 determining the form and amount of the compensation programs.

5 Where available by position, Compensation Peer Group data serve as the primary
6 reference point for pay comparisons, and broader survey data and published proxy data
7 are also provided by the compensation consultant as a point of reference. Where
8 available by position, the independent compensation consultant gathers compensation
9 data from Towers Watson's Energy Services Executive Database (over
10 60 investor-owned utilities) and Towers Watson's General Industry Executive Database
11 (approximately 400 participating companies), which it regresses based on CMS Energy's
12 revenues to provide additional market context to the Compensation Peer Group. In
13 selecting members of the Compensation Peer Group, financial and operational
14 characteristics are considered. The criteria for selection of the Compensation Peer Group
15 included comparable revenue, approximately \$2.5 billion to \$12.9 billion (ranging from
16 approximately one-half to two times that of CMS Energy), relevant utility industry group,
17 similar business mix (revenue mix between regulated and non-regulated operations) and
18 availability of compensation and financial performance data.

19 In addition, annually proxy advisor services Glass Lewis & Co. and Institutional
20 Shareholders Services assist institutional investors in their advisory vote on the
21 reasonableness of compensation pay and practices (referred to as "Say-on-Pay") of the
22 proxy named executive officers by providing a vote recommendation. The incentive pay
23 practices for the proxy named executive officers are the same as for the remaining officer

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1 group. In 2012 both proxy advisory service firms recommended a vote “for” the proxy
2 named executive officer compensation pay and practices.

3 Q. Does the independent consultant provide other services for CMS Energy or Consumers
4 Energy that could result in a conflict of interest?

5 A. No. The independent consultant is required to obtain approval of the Compensation
6 Committees of the Boards of Directors before undertaking any activity on behalf of the
7 management of CMS Energy or Consumers Energy. During the time the consultant has
8 been engaged as the compensation consultant for the Boards of Directors, it has not
9 performed any services on behalf of the management of CMS Energy or Consumers
10 Energy.

11 Q. Are surveys the only determining measure used in setting officer compensation levels?

12 A. No. Additionally the Compensation Committees consider experience levels and
13 individual contributions.

14 Q. Are incentive plans common in the utility industry or in other industries for officers?

15 A. Yes, incentive plans are prevalent. Research from Mercer LLC, US Compensation
16 Planning 2011/2012 survey indicates that approximately 89 percent of companies and
17 90 percent of energy companies offer annual incentive (bonus and/or variable pay)
18 programs for officers. The survey data support the conclusions that including incentive
19 pay as part of a competitive pay package is a standard practice, and is required to attract
20 and retain qualified officers.

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1 **III. INCENTIVE COMPENSATION PLANS**

2 **i. DESCRIPTION OF INCENTIVE PLANS**

3 Q. Please describe the EICP that will be in place for 2012 and 2013.

4 A. The EICP plan for 2012 is based on achieving breakthrough goals related to the four
5 critical areas of the Company's operations: (i) safety; (ii) reliability; (iii) customer value;
6 and (iv) being financially healthy.

7 The Plan seeks to remind employees that in order to provide quality service to
8 customers at a competitive price, the Company must be healthy overall in these four
9 critical areas of Company operations. The EICP uses a multi-year horizon for purposes
10 of developing goals. It is designed to align with the Company's "Growing Forward"
11 strategy that will help position the Company to serve customers and contribute to
12 Michigan's energy future.

13 The EICP goals seek to encourage employees to provide reliable energy, customer
14 value, and responsive service to our customers, and to do so safely. Each year, the
15 Company establishes utility specific performance criteria within each of these four areas
16 of safety, reliability, customer value, and being financially healthy. With this as the
17 foundation, 13 specific plan goals were established for 2012. There are four individual
18 performance criteria, or measures, for safety, three for reliability, four for customer value,
19 and two for financial performance. The Company anticipates essentially the same plan
20 goals will be in effect for 2013. The EICP Performance Measures are summarized on
21 Exhibit A-16 (AMC-1).

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1 Q. Please describe Exhibit A-16 (AMC-1).

2 A. Exhibit A-16 (AMC-1) identifies the four critical areas that the EICP focuses on and
3 identifies the specific measures that have been adopted for each of these areas. In the last
4 column the year-end target is identified. As I indicated earlier, 50 percent of the
5 non-officer incentive compensation is based on the safety, reliability, and customer value
6 measures and the remaining 50 percent is based on the financial measures.

7 Q. Please describe the process for establishing a framework for the EICP.

8 A. The overall process of establishing a framework for the EICP has been divided into a
9 number of steps. The initial steps can be summarized as follows:

- 10 1. Identify a vision and purpose.
- 11 2. Determine a strategy to achieve the vision and purpose.
- 12 3. Determine “breakthrough goals” consistent with the vision, purpose, and
13 strategy.
- 14 4. Develop targets and plans.

15 In addition, there will be ongoing monitoring and assessment of results and
16 benchmarks.

17 Q. Please describe the vision and purpose.

18 A. Management began by identifying an overall vision and purpose. Management has a
19 vision of Consumers Energy being best in class, best in value, with employees that are
20 “proud to wear the colors.” The EICP seeks to both: (i) help instill this vision into
21 employees and (ii) keep at the forefront before employees that the Company has, as an
22 overall purpose, the providing of reliable energy and responsive service to our customers,
23 safely for both customers and employees. In order to provide quality service to
24 customers at a quality price, the Company must be successful overall, including being

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1 financially healthy. In order to raise capital, which is becoming increasingly important,
2 at the best available rates, Consumers Energy needs to be financially healthy.

3 Q. Please discuss the strategy for the EICP.

4 A. As I indicated, the EICP program is designed to align with Consumers Energy's
5 "Growing Forward" strategy. The overall strategy is based on management's view that,
6 in order to achieve the vision and purpose, the Company should focus on five key areas:

- 7 (i) safe, excellent operations;
8 (ii) providing customer value;
9 (iii) effectively investing in utility assets for the benefit of customers;
10 (iv) positioning the Company to achieve fair and timely regulatory treatment;
11 and
12 (v) being financially healthy.

13 The strategic Growing Forward Goals are summarized on Exhibit A-17 (AMC-2).

14 The EICP structure is designed to help emphasize that this strategy is ongoing.
15 For example, providing safe, excellent operations for customers is at the foundation to the
16 Company's strategy and the EICP goals help serve as a reminder that employees are part
17 of this foundation of safe, excellent operations. Employees have a responsibility to
18 ensure each other's safety and that of the public, while at the same time pursuing
19 operational excellence.

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1 Q. Why is providing safe, excellent operations the foundation of the Company's strategy?

2 A. It is in the interests of Consumers Energy and its customers for Consumers Energy to
3 provide safe and excellent operations. The foundation of the strategy triangle of "Safe,
4 Excellent Operations" and the EICP categories of safety, reliability, and customer value
5 help reinforce to employees that the Company's strategy and goals are based on a
6 foundation of safe, excellent operations. On this foundation is built customer value and
7 utility investment.

8 Q. Why is "Consistent Financial Performance" at the peak of the strategy triangle?

9 A. This illustrates that the utility's consistent financial performance is built on the other
10 parts of the triangle. It does not drive the strategy, but is a result of Safe, Excellent
11 Operations, Customer Value, Utility Investment, and Fair and Timely Regulation.
12 Consistent financial performance is critical to healthy utility operations and having a
13 healthy utility benefits customers. It is at the top of the strategy triangle because it is the
14 result of everything else that happens elsewhere in the triangle.

15 Q. How are the targets for the EICP measures determined?

16 A. The metrics and data for each goal, and action plans to achieve the goal's target are based
17 on making progress each year toward the multi-year objectives. Target levels and action
18 plans are developed to help ensure customers receive the reliability of service and the
19 quality of service that Consumers Energy's customers deserve. For example, for 2012:
20 (i) the utility's safety goal will require maintaining first quartile employee safety
21 performance and meeting gas leak response time and downed wire response time targets;
22 (ii) the customer reliability goal will include both an improvement in the System
23 Average Interruption Duration Index ("SAIDI") (which is average number of minutes

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1 interrupted divided by total customer base), a reduction in customer outage minutes, and
2 a reduction in the percentage of customers experiencing repetitive outages; and (iii) the
3 customer value goal will require, among other things, that the Company attain residential
4 customer satisfaction ranking at or above the comparison sample mean and productivity
5 improvement.

6 Q. Why are you including both gas and electric performance measures in this plan as this is
7 an electric rate case?

8 A. For purposes of efficiency and improved service, the Company has combined operations
9 as one organization. For that reason the plan contains both gas and electric measures.

10 Q. Are the two financial performance goals that are included in the EICP measures
11 consistent with the Company's responsibilities to its customers?

12 A. Yes. As I mentioned earlier, consistent financial performance is the result of everything
13 else that happens. It is in the customers' interests to have a financially healthy utility.
14 This allows the utility to better meet customer needs at the best price. The two financial
15 goals are balanced with other operational and performance criteria. Having a financially
16 healthy utility is important to customers and to the State of Michigan. Financial goals
17 help focus employees on achieving superior results in a cost-effective manner. By
18 focusing employees' attention on goals that encourage improved performance and greater
19 efficiencies, customers are benefited. The incentive compensation goals are designed to
20 help motivate employees to perform at their full potential and exercise discretionary
21 effort to help move the Company forward.

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1 Q. How are the targets for the annual officer EICP incentives measures determined?

2 A. As mentioned earlier, the goals are the same for the officer and non-officer EICP
3 incentive plans, but the weightings are different.

4 Q. Why is the weighting different for the officer plan?

5 A. Officer annual incentive awards will be based on the achievement of EPS and operating
6 cash flow goals. These two metrics are good indicators of strategy execution. The
7 Officer annual incentive award will be reduced if there is no award earned under the
8 safety, reliability, and customer value measures portion of the EICP and the award will be
9 increased (but in no event shall the award exceed the maximum of the target annual
10 incentive) if the maximum award payout is achieved under the safety, reliability, and
11 customer value measures portion of the EICP. This potential adjustment provides linkage
12 of executive compensation with the goals related to safety, reliability, and customer
13 value.

14 Q. How are the EPS and operating cash flow components determined?

15 A. EPS means EPS as determined in accordance with generally accepted accounting
16 practices, excluding asset sales, changes in accounting principles from those used in the
17 budget, large restructuring and severance expenses greater than \$5 million, legal and
18 settlement costs or gains related to previously sold assets, and regulatory recovery for
19 prior year changes. Cash flow means generally accepted accounting principles operating
20 cash flow with adjustments to include changes in power supply cost recovery from
21 budget (disallowances excluded), changes in pension contribution, and gas-price changes
22 (favorable or unfavorable) related to gas cost recovery in January and February of the

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1 following performance year. The Compensation Committees review management's
2 preliminary recommendations and establish final goals.

3 Q. How are the target amounts for the annual officer incentives determined?

4 A. The Compensation Committees determine the target amounts of the annual officer
5 incentives. In determining the amount of target incentives, the Compensation
6 Committees consider the following factors:

- 7 • the target incentive level, and actual incentives paid, in recent years;
- 8 • the relative importance, in any given year, of each performance goal
9 established; and
- 10 • the advice of the Compensation Committees' compensation consultant as
11 to compensation practices at other companies in the Compensation Peer
12 Group and the utility industry.

13 Q. How are the targets for the officer long-term incentive measures determined?

14 A. In determining the amount of equity incentive compensation that is provided to each
15 officer in a given year the Compensation Committees considers factors such as
16 performance, retention and incentive practices and the relative percentages of cash and
17 equity paid by the Compensation Peer Group and other market data.

18 Q. Why has the Company's management chosen to design the EICP incentive plan with
19 broad goals and objectives rather than individual goals and objectives?

20 A. It is necessary and appropriate for a large organization, such as Consumers Energy, to
21 establish broad goals and objectives that are communicated to all employees as matters
22 that are important to the success of the organization. Some employees will be in a better
23 position to influence whether particular goals and objectives are met, but having every
24 employee linked to a set of common customer focused objectives is an effective method
25 for emphasizing the importance of customer value and service. Having common goals

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1 and objectives: (i) provides clear communication of Company goals; (ii) encourages
2 employees to support each other and work together for common goals; and (iii) provides
3 a scorecard with a focus on corporate-wide goals that benefit customers.

4 Consumers Energy incorporates individual goals through the annual performance
5 feedback process, which includes the creation and review of individual goals and
6 objectives for each salaried employee and the opportunity to recognize and reward
7 individual performance. The existence of a common set of customer objectives enables
8 supervisors and employees to establish individual goals and objectives which are
9 supportive of and in alignment with the corporate goals reflected in the EICP.

10 ii. **ASSESSMENT OF CUSTOMER BENEFITS OF THE INCENTIVE**
11 **COMPENSATION PLANS**

12 Q. What level of expenses for Consumers Energy's incentive plans have been included in
13 the test year revenue requirement?

14 A. The Company is requesting recovery of electric expenses related to incentive
15 compensation plans at target levels. The level of expense is \$9.0 million as illustrated in
16 Exhibit A-18 (AMC-3). This includes \$5.0 million for EICP incentive compensation and
17 \$4.0 million for long-term incentive (restricted stock) compensation. Incentive
18 compensation for the top six officers is not included in these amounts.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. How are the 2013 electric expenses of \$9.0 million related to incentive compensation
2 calculated?

3 A. The \$5.0 million for EICP incentive compensation is based on the following:

- 4 • For officers: The 2013 expense amount is based on 2012 salaries
5 (excluding the top six officers) multiplied by the approved target incentive
6 percentage of salary from the 2012 Compensation & Human Resources
7 Committee of the Board of Directors. Factors that impact the incentive
8 expense year-over-year are retirements of officers and successors being at
9 lower incentive amounts (decrease expense) and forecasted salary
10 increases (increase expense).
- 11 • For non-officers: The 2013 expense amount is based on an estimate of the
12 number of employees in each salary grade multiplied by the plan
13 prescribed incentive target amount. Progression to higher salary grades as
14 employees gain additional work experience will increase the amount of
15 incentive expense year-over-year and headcount reductions will decrease
16 the amount of incentive expense year-over-year.

17 The \$4.0 million restricted stock expense for 2013 is based on 2012 expense amounts.
18 Restricted stock expense is based on two factors: (1) granted share level, and (2) fair
19 value of the award. The expense is then determined by multiplying the projected shares
20 times the fair value. This resulting expense is recognized over the three-year cycle
21 period. As such the 2013 expense amount included a portion of 2010, 2011, 2012, and
22 2013 restricted stock grants.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. How were granted shares and value determined?

2 A. Granted shares are based on percentage of base salary for officers. As discussed above in
3 my testimony, the level of the officer awards are determined by the Compensation
4 Committees considering the practices of the Compensation Peer. Director awards are
5 determined on a similar basis by the Governance Committees of the Board of the
6 Directors. The 2012 granted share levels for officers and directors were then inflated by
7 projected salary increases of 3.0 percent to arrive at the 2013 projected granted shares
8 level. A 2012 Mercer survey and 2012 World-at-Work survey both indicated that pay
9 increases are expected to be 3.0 percent. Non-officer grant levels were based on internal
10 grant targets to move grant levels to align with market levels.

11 The fair value of tenure-based restricted stock is based on the CMS Energy stock
12 price on the date of grant. The fair value of performance-based restricted stock for 2012
13 is based on a third party valuation. This valuation process considers such factors as stock
14 price volatility (including a three-year look back at historical volatility) and expected
15 dividends for CMS Energy and the long-term incentive peer group. The 2012 amount
16 was used to calculate a 2013 amount.

17 As previously mentioned, the \$9.0 million expense reflects the adjustment to
18 eliminate incentive compensation for the top six executives.

19 Q. How was the electric portion of the incentive compensation expense determined?

20 A. The allocation percentages were supplied by the Accounting Department.

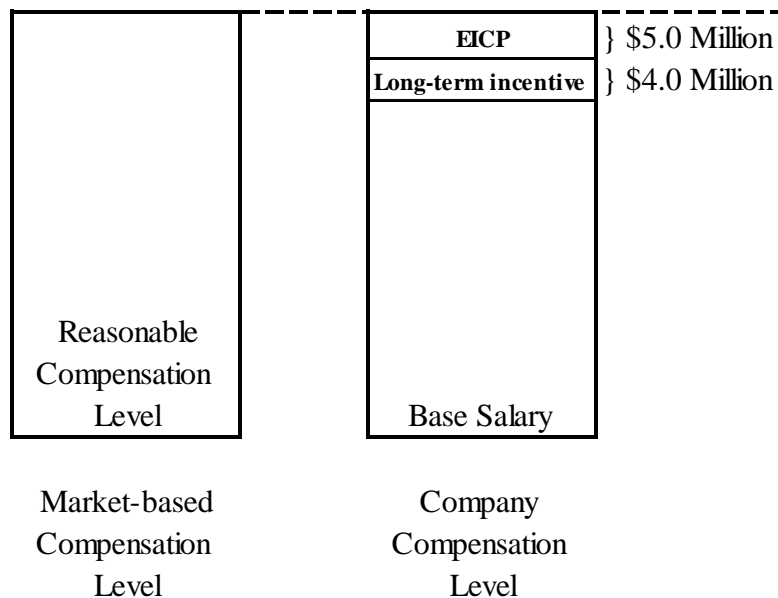
AMY M. CONRAD
DIRECT TESTIMONY

1 Q. Do Consumers Energy's electric customers benefit from making a portion of employee
2 compensation subject to incentives?

3 A. Yes. Paying a competitive level of compensation is an essential prerequisite to being
4 able to attract, retain, and motivate qualified employees. Consumers Energy has
5 determined a reasonable level of compensation and then made a portion of that
6 compensation at-risk. Customers receive both qualitative and quantitative benefits at no
7 additional cost.

8 Q. Why do you say there is no additional cost?

9 A. The officer and non-officer incentive plans are designed so that the total base salary plus
10 incentive payments will be equivalent to the market-based compensation level. The
11 EICP and long-term incentive compensation is part of the overall reasonable level of
12 compensation. It is not in addition to it. This is illustrated in the following diagram:



AMY M. CONRAD
DIRECT TESTIMONY

1 Q. Are you aware of what criteria the Commission identified for review of employee
2 incentive plan costs in its December 22, 2005, Order in Consumers Energy's electric rate
3 case No. U-14347?

4 A. Yes. In its Order in that case the Commission stated: "In Case Nos. U-10149 and
5 U-10150, the Commission determined that executive bonus and employee incentive plans
6 require a showing that the plan will not result in excess rates and that the benefits to
7 ratepayers from the bonus and incentive plans will, at a minimum, be commensurate with
8 the programs' costs."

9 Q. Do you believe this standard should be used for evaluating the incentive compensation
10 for purposes of ratemaking in the current case?

11 A. No.

12 Q. Why do you believe that the Case U-14347 standard should not be used?

13 A. Making a portion of compensation subject to incentives is a recognized, well-established,
14 common, practice in the utility industry and is reasonable and appropriate. The
15 appropriate standard from a business perspective in evaluating whether the level of
16 compensation is reasonable is whether the overall level of compensation, including both
17 base salary and incentive compensation, is reasonable. Using this standard would also be
18 appropriate for ratemaking purposes. Looking at whether the overall level of
19 compensation is reasonable will provide a better indication of whether the incentive plan
20 results in excess rates than attempting to examine the cost allocable to the incentive
21 compensation compared to benefits to customers. The overall level of compensation that
22 Consumers Energy has included in its request in this case is reasonable.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. Are you aware of what criteria the Indiana Utility Regulatory Commission has used in
2 reviewing whether incentive compensation is recoverable in rates?

3 A. Yes. Consumers Energy's witness Ronn Rasmussen discusses the Indiana Utility
4 Regulatory Commission criteria from a ratemaking standpoint. In a 2011 Order issued by
5 the Indiana Utility Regulatory Commission ("IURC") regarding Southern Indiana Gas
6 and Electric Company (doing business as Vectren Energy), the IURC stated:

7 "The Commission recognizes the value of incentive compensation
8 plans as part of an overall compensation package to attract and
9 retain qualified personnel. The criteria for the recovery of
10 incentive compensation plan costs are well established. We will
11 allow recovery in rates when: (1) the incentive compensation plan
12 is not a pure profit-sharing plan, but rather incorporates operational
13 as well as financial performance goals; (2) the incentive
14 compensation plan does not result in excessive pay levels beyond
15 what is reasonably necessary to attract a talented workforce; and
16 (3) shareholders are allocated part of the cost of the incentive
17 compensation programs." (Case No. 43839, April 27, 2011, p. 50)

18 In that case the IURC allowed recovery of incentive compensation costs by the utility.

19 Q. How do the IURC criteria differ from criteria applied by the MPSC in Case U-14347?

20 A. The IURC recognized the value of incentive compensation plans as part of an overall
21 compensation package to attract and retain qualified personnel. Instead of requiring a
22 quantification of customer benefits specifically related to the metrics, which can be
23 extremely difficult for measures that support undeniably desirable achievements
24 (e.g., improved customer satisfaction and safety), Indiana's criteria require there be a
25 combination of operating and financial metrics and a demonstration that there is no
26 resultant excess compensation. These requirements, as applied by the IURC in its 2011
27 Order, provide a reasonable approach. The plans in place at Consumers Energy meet
28 these requirements.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. The IURC criteria also require that shareholders be allocated part of the cost of incentive
2 compensation programs. Do you agree with that portion of the IURC criteria?

3 A. No. If overall compensation levels are reasonable, then those costs should be recoverable
4 through utility rates. I will note, however, that the Company's incentive compensation
5 proposals in this case do result in shareholders bearing a portion of these costs. The plans
6 in place at Consumers Energy meet this requirement.

7 Q. Please discuss the first standard under the IURC criteria.

8 A. The first standard requires that the incentive compensation plan "incorporates operational
9 as well as financial performance goals." At page 50 of its April 2011 Order the IURC
10 stated that the annual incentive compensation plan under review incorporated
11 non-financial measures such as safety, customer satisfaction, and unit availability in
12 addition to financial performance measures. It appropriately rejected the argument that
13 incentive plan costs should be disallowed to the extent they relate to financial measures.
14 As discussed above, the Consumers Energy EICP includes non-financial operational and
15 performance goals in addition to financial goals. The Company's EICP meets the first
16 standard of the criteria.

17 Q. Please discuss the second standard under the IURC criteria.

18 A. The second standard involves whether the incentive compensation results in "pay levels
19 beyond what is reasonably necessary to attract a talented workforce." In applying this
20 standard, the IURC stated that the evidence showed the utility's Human Resources
21 Department evaluated the competitiveness of its compensation package and a
22 compensation package was developed that was market competitive. This is also true for
23 Consumers Energy's compensation. The IURC said the evidence indicated that base pay

AMY M. CONRAD
DIRECT TESTIMONY

1 plus annual incentives and that base pay plus annual and long-term incentives were
2 within the market competitive range as established by peer companies and a broader
3 national sample. The IURC concluded that therefore the incentive compensation plan did
4 not result in excessive pay beyond what is reasonable to attract a talented workforce. The
5 same conclusion applies to Consumers Energy's non-officer and officer incentive
6 compensation plans.

7 Q. Please discuss the third standard under the IURC criteria.

8 A. In applying the third standard, the IURC noted that the utility was only seeking funding
9 for its incentive compensation plan up to the approved target level. It stated that the
10 evidence showed that the shareholders would bear the expense of incentive compensation
11 in excess of the target level. The IURC found that shareholders were, therefore, allocated
12 part of the utility's compensation costs. Consumers Energy's incentive plans meet this
13 standard, as applied by the IURC.

14 Q. How does the Company's proposal for recovery of incentive compensation costs result in
15 a sharing of costs with the Company's shareholders?

16 A. The Company's proposal to include incentive compensation costs at target levels will
17 result in the Company absorbing the incentive compensation costs in those years when
18 the actual payouts are greater than target level. Thus shareholders will absorb any
19 resulting increase in costs arising from above target performance. If actual payouts in
20 future years are less than target levels due to inadequate financial performance, then the
21 Company's shareholders will absorb the consequence of inadequate financial results.

22 In addition, the Company is allocating to shareholders 100 percent of the costs of
23 incentive compensation for the top six officers as identified by the SEC proxy rules.

AMY M. CONRAD
DIRECT TESTIMONY

1 Further, cash payments under the EICP reduce earnings and grants of equity
2 shares under the long-term incentive increase outstanding shares. As a result, both are
3 dilutive to shareholders. This is accepted since the EICP and long-term incentive are
4 components of market compensation package that is required to attract, retain, and
5 motivate a talented workforce.

6 Q. Is the payment of incentive compensation reasonable given the “tough economic”
7 conditions facing the Company’s customers?

8 A. Yes. The incentive compensation costs are reasonable costs of doing business. The
9 market median of survey data reflects current economic conditions and current pay
10 practices. The Company maintains an annual practice of surveying the external market.
11 Any trends in compensation - increases/decreases - would be reflected in the market
12 survey results. Paying a reasonable level of compensation is reasonable and is in the
13 interests of the Company’s customers. Incentive compensation does not result in
14 excessive compensation and is reasonably necessary to attract, retain, and motivate a
15 talented workforce. Further, gaps between the skills that employers require and those
16 available in the labor market are growing. Paying a reasonable level of compensation,
17 which includes incentive compensation is necessary to attract, retain, and motivate a
18 talented workforce

19 Q. What are some of the ways the EICP incentives benefit customers?

20 A. Customers benefit by having a portion of compensation shifted to the EICP program
21 since the goals of the program are in the interests of customers. Customer benefits are
22 achieved without any additional cost to customers since this program has been structured
23 as a “carve out” of the employee’s base salary. If the EICP costs had not been allocated

AMY M. CONRAD
DIRECT TESTIMONY

1 to incentive compensation, those costs would need to be recovered as base compensation
2 in order for Consumers Energy to have a reasonable competitive level of compensation.

3 Also, customers are best served when Consumers Energy can attract, retain, and
4 motivate talented salaried employees and executives with compensation packages that are
5 competitive and fair. Performance-based incentives (like Consumers Energy's) permit
6 the Company to provide an incentive to accomplish specific annual goals that represent
7 performance priorities for Consumers Energy and its customers. With variable pay, the
8 employee and the Company as a whole must re-earn the incentive award every year. If
9 performance goals are not achieved, cash compensation is reduced or eliminated.
10 Variable pay creates a performance culture rather than an entitlement culture.

11 In addition, an incentive program structured to focus on safety, reliability, and
12 customer value results in the following customer benefits:

- 13 • Safety measures result in reduced number of lost days (less absenteeism)
14 and reduced medical costs;
- 15 • Reliability measures result in reduced interruption costs; and
- 16 • Customer value measures result in reduced operating and maintenance
17 costs from increased productivity.

18 A quantitative analysis of the benefits received by the customer is discussed by
19 Consumers Energy's witness Ronn Rasmussen in his testimony in this case.

20 Further, customers are best served when Consumers Energy can raise capital at
21 the best available rates. The use of earnings and cash flow measures in the EICP and
22 officer annual incentive recognizes that Consumers Energy's financial health is
23 important. Financial health leads to reduced costs of capital, thus resulting in savings to
24 the customer.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. How does the long-term incentive benefit customers?

2 A. Customers benefit from the Company having a compensation package that provides
3 competitive compensation. The Company is better able to attract, retain, and motivate
4 officers when its overall compensation is competitive with market levels. Customers also
5 benefit by having a portion of compensation in the form of equity based long-term
6 incentive because there is no cash outflow as a result of providing equity based long-term
7 incentive. Equity based long-term incentive also results in tax savings, as stock grants
8 result in a tax deductions on the corporate return. The Company has maintained overall
9 compensation at competitive levels through the use of the incentive plans (both short- and
10 long-term). But for the incentive plan, the Company's officer total compensation (base
11 salary plus incentives) for 2013 would be less than overall competitive compensation
12 levels. The absence of a long-term incentive plan would require additional cash outflows
13 in the form of base salaries in order to pay at competitive levels. This would result in
14 fewer available funds for utility investment, thus directly impacting the Company's
15 ability to provide customer value and reliability.

16 Further, the long-term incentive performance metric is TSR relative to a peer
17 group. Long-term incentive participants are only rewarded if good long-term decisions
18 are made. Strong stock performance in comparison to peers takes out irrelevant market
19 factors and provides a measure of a well-run, high performing utility. Strong stock
20 performance helps provide access to capital which the Company uses to invest in plant
21 that supports safe and reliable electric distribution, thus providing a benefit to customers.

22 In addition, the long-term incentive helps assure that officers are looking at
23 longer-term impacts of decisions and not just short-term impacts.

AMY M. CONRAD
DIRECT TESTIMONY

1 Q. Has Consumers Energy assessed whether benefits to customers of this program equal or
2 exceed costs?

3 A. Yes. The benefits to customers of the Company's EICP program outweigh the costs of
4 the program. The costs of the EICP and officer incentive programs are projected at
5 \$9.0 million for 2013. Since this amount is part of the overall level of reasonable
6 compensation, rather than being in addition to it, all benefits to customers are achieved at
7 zero additional cost to customers. Achievement of the Company's non-officer EICP
8 goals and objectives result in pay that is competitive with the labor market, not above the
9 market. The EICP costs are not in addition to the reasonable level of compensation, they
10 are part of reasonable level of compensation. If these amounts are not paid, then overall
11 compensation would be at a level which is below the market level. Similarly, the
12 long-term incentive costs are part of the reasonable level of compensation and if not paid
13 would result in compensation below the competitive market level. Thus, all of these
14 costs could reasonably and properly be included as part of base pay. There is no valid
15 basis to eliminate incentive costs from the cost of service recovered in rates because they
16 are a part of an incentive plan rather than including these costs as part of base pay. As
17 stated before, overall levels of compensation are at levels that are not excessive. Rate
18 recovery of 100 percent should be allowed.

19 Q. Would rate recovery of incentive costs be appropriate if the Commission were to apply
20 the criteria that the Commission identified for review of employee incentive plan costs in
21 its 2005 Order in Case No. U-14347?

22 A. Yes. The incentive plans do not result in excessive costs and provide benefits to
23 customers. The measures used for the incentive plans are financial performance,

AMY M. CONRAD
DIRECT TESTIMONY

1 customer value, safety, and reliability. The incentive programs have both a qualitative
2 (as described in my above testimony) and quantitative benefit to customers. As I have
3 stated above, the benefits that are provided to customers are provided at no additional
4 cost. However, in addition, there are quantitative benefits that offset the incremental
5 portion of compensation that is incentive-based. As I stated above, a quantitative
6 analysis of the benefits received by the customer is discussed by Consumers Energy's
7 witness Ronn Rasmussen in his testimony in this case.

8 Q. Why does the Company provide both annual incentives and long-term incentives for the
9 officers?

10 A. The inclusion of both annual and long-term incentives for officers helps reinforce that
11 overall policy and operational decisions should be made keeping in mind both the
12 short-term and long-term interests of the Company and its customers. As I discussed in
13 my above testimony, customers also benefit by having a portion of compensation in the
14 form of equity based long-term incentive because there is no cash outflow as a result of
15 providing equity based long-term incentive. This results in greater available funds for
16 utility investment, thus directly impacting the Company's ability to provide customer
17 value and reliability. In addition, if the Company is financially healthy it will be easier to
18 raise funds for needed capital investments on reasonable terms and conditions.

19 **IV. CONCLUSION**

20 Q. Is the Company's overall compensation program, including the customer-focused
21 incentive reasonable?

22 A. Yes. The approach used by the Company is a reasonable approach, is consistent with
23 industry standards, and represents well-established best practices for creating customer

AMY M. CONRAD
DIRECT TESTIMONY

1 focus through compensation design, and it does so without any additional customer cost.
2 The overall compensation levels, including the incentive costs, are reasonable. All these
3 incentive costs should therefore be included in the cost of service recovered from
4 customers. These are legitimate and reasonable costs of doing business. Rates
5 established in this rate case should include \$9.0 million for incentive compensation
6 expense.

7 Q. Please summarize reasons why full recovery of incentive compensation costs should be
8 allowed in this case.

9 A. Reasons that full recovery of compensation costs should be allowed include the
10 following:

- 11 i) Employee compensation is a reasonable cost of doing business, has been
12 set at a reasonable level, and has been determined using a reasonable
13 methodology;
- 14 ii) The amount of compensation that is subject to incentive measurements is
15 part of the market-based compensation level, not in addition to it;
- 16 iii) The incentive compensation plan does not result in excessive pay levels
17 beyond what is reasonably necessary to attract a talented workforce;
- 18 iv) Making a portion of compensation subject to incentives is a recognized,
19 well-established, common, industry practice and is neither irrational nor
20 unreasonable;
- 21 v) The decision of Consumers Energy to allocate a portion of overall
22 compensation that would otherwise have been in base pay so that it is
23 subject to incentives does not provide a valid basis to disallow these
24 expenses;
- 25 vi) The Plan incorporates operational as well as financial performance goals;
- 26 vii) Benefits of having a portion of compensation subject to incentives occur at
27 no additional cost to customers given the compensation structure adopted;
- 28 viii) Shareholders bear the expense of incentive compensation in excess of the
29 target levels; and

AMY M. CONRAD
DIRECT TESTIMONY

1 ix) The focus should be on whether the overall level of compensation is
2 reasonable, not on the precise structure of the compensation program.

3 It is reasonable for Consumers Energy to pay its employees competitive levels of
4 compensation. Paying employees at competitive market levels is reasonable and prudent.
5 Those costs are reasonable costs of doing business and are recoverable from customers.
6 Since the total level of compensation - including both base pay and incentive pay - is
7 reasonable, that justifies the expense. There is no additional compensation expense
8 resulting from the approach used by Consumers Energy. Customers do not pay more
9 than the reasonable level of compensation.

10 Q. Does this conclude your testimony?

11 A. Yes.

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 generation and distribution of)
electricity and for other relief.)
_____)

Case No. U-17087

REBUTTAL TESTIMONY

OF

AMY M. CONRAD

ON BEHALF OF

CONSUMERS ENERGY COMPANY

March 2013

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. Please state your name and business address.

2 A. Amy M. Conrad, One Energy Plaza, Jackson Michigan.

3 Q. Are you the same Amy Conrad who previously submitted testimony in this case?

4 A. Yes.

5 Q. What is the purpose of your rebuttal testimony?

6 A. The purpose of my rebuttal testimony is to provide rebuttal to testimony and exhibits
7 presented by witnesses for the Staff, the Attorney General, and Energy Michigan
8 regarding Consumers Energy Company's ("Consumers Energy" or the "Company")
9 incentive compensation plan and to recommendations to exclude incentive compensation
10 costs from the revenue requirement in this case. For reasons discussed in my original
11 testimony and in this rebuttal testimony, the Commission should find that the incentive
12 compensation costs that Consumers Energy is seeking to recover in this case are
13 reasonable costs of doing business and should be included in rates. Consumers Energy
14 has acted reasonably in paying its employees at market levels and is entitled to have that
15 expense recovered in rates.

16 Q. How is your rebuttal testimony organized?

17 A. In Section I of my rebuttal, I address testimony and exhibits presented by Staff's witness
18 Brian Welke. In Section II of my rebuttal, I address testimony and exhibits presented by
19 the Attorney General's witness Sebastian Coppola. In Section III of my rebuttal, I
20 address testimony and exhibits presented by Energy Michigan's witness
21 Alexander Zakem.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 **I. Rebuttal to Staff Witness Welke**

2 Q. At pages 7-8 of his testimony, Mr. Welke states: “Staff recommends 100% exclusion of
3 incentive plan costs from the revenue requirement because the Company has not
4 adequately addressed any of the Commission’s prior reasons for excluding incentive
5 compensation.” Do you agree with this recommendation?

6 A. No. I disagree both with Staff’s recommendation and Staff’s stated reasons for reaching
7 this recommendation. Employee compensation is a reasonable cost of doing business and
8 Consumers Energy’s overall employee compensation costs, including incentive
9 compensation, have been set at a reasonable level. Adopting Staff’s recommendation
10 would result in a level of compensation that is below a reasonable and competitive level.
11 The variable, or at risk, pay is a component of total compensation. It is not in addition to
12 competitive levels of compensation.

13 Q. At page 6 of his testimony, Mr. Welke states that the Company’s incentive plans “are
14 biased toward the achievement of financial performance.” Do you agree?

15 A. No. The non-officer incentive plan includes both operational (non-financial) goals and
16 financial goals. Both provide benefits to customers and are equally important. Thus the
17 weighting is split 50%/50%. Customer benefits include:

18 Safety measures – reduced number of lost days and reduction in medical expense;

19 Reliability measures – reduced interruption costs/increased reliability;

20 Customer value measures – improved customer satisfaction and reduced operation
21 and maintenance costs from increased productivity; and

22 Financial health – reduced cost of capital, thus resulting in savings to customers.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. At page 7 of his testimony, Mr. Welke states: “Without a 2013 plan, the Company has
2 failed to offer evidence with detailed supporting explanations and underlying
3 assumptions necessary for Staff to make an adequate review or the Commission to make
4 an informed decision.” Is this statement correct?

5 A. No. Consumers Energy has provided sufficient explanations and underlying assumptions
6 to allow the Staff to make an adequate review and the Commission to make an informed
7 decision. I have presented evidence that the overall level of compensation is reasonable,
8 that the use of incentive compensation is a well-established management technique, that
9 the incentive criteria used by Consumers Energy are reasonably related to goals that
10 benefit customers, and that the overall employee compensation levels would be
11 unreasonably low if incentive compensation were not included.

12 Q. Please explain.

13 A. In my direct testimony I present evidence regarding how the Company structures the
14 overall compensation levels for its non-officer salaried employees and for its officers. I
15 present evidence that the overall compensation levels are reasonable relative to the
16 market, are determined in a reasonable manner, and are a reasonable cost of doing
17 business. In addition, I present evidence that paying competitive wages and salaries is
18 necessary in order to maintain a competent workforce, compensation levels without
19 incentive compensation included would be below market competitive levels, that paying
20 less than the reasonable level of compensation would result in a lower qualified
21 workforce and would not be in the interests of the Company or its customers.

22 In addition, I present evidence in my direct testimony regarding the Company’s
23 compensation philosophy, I discuss the difference between short-term and long-term

AMY M. CONRAD
REBUTTAL TESTIMONY

1 incentive pay and the purpose for each, I present evidence that incentive pay is
2 recognized as the number one design to influence short- to mid-term results, and I show
3 that use of incentive compensation encourages employees to deliver their best
4 performance for the Company's customers.

5 I also present evidence in my direct testimony describing the structure of
6 Consumers Energy's incentive compensation plans, how the incentive criteria is designed
7 to help communicate priorities important to customers, help keep employees focused on
8 such areas as safety, reliability, customer value, and encourage employees to deliver their
9 best performance for the Company's customers. I present evidence describing the
10 process for establishing the framework for the EICP, including the vision and purpose,
11 the strategy, and how the goals are consistent with the vision and purpose.

12 Q. How do you respond to Mr. Welke's statement that there is insufficient information to
13 review the 2013 plan because it had not yet been completed?

14 A. Initially, I would note that customers are receiving benefits at no additional cost since the
15 incentive compensation program has been structured as a "carve out" from the
16 employees' base salary and not as an incremental addition to it. Second, while
17 refinements occur each year, the four critical areas of safety, reliability, customer value,
18 and being financially healthy remain unchanged, and as I have shown in my direct
19 testimony, these provide benefits to customers. Third, in my direct testimony I testified
20 that the Company anticipated essentially the same plan goals will be in effect for 2013 as
21 for 2012. The incentive compensation goals reflect a multi-year strategy. The supporting
22 explanations and underlying assumptions for the 2012 plan are also applicable for the
23 2013 plan.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. Are the 2013 plan goals essentially the same as for 2012?

2 A. Yes. Both the 2012 and 2013 incentive plans include: (i) employee safety, gas leak
3 response, and downed wire response measures in the safety category; (ii) repetitive
4 electric outages, distribution reliability, and generation reliability measures in the
5 reliability category; and (iii) competitive price, customer satisfaction surveys, call center
6 response, and productivity improvement measures in the customer value category. Both
7 the 2012 and 2013 incentive plans, in addition, recognize the importance to the
8 Company's ability to serve its customers of having a financially healthy utility.

9 **II. Rebuttal to the Attorney General Witness Coppola**

10 Q. At pages 27-37 of his testimony, Mr. Coppola discusses various reasons that he disagrees
11 with the Company's request to recover incentive compensation costs in rates. Do the
12 concerns and issues he has identified in his direct testimony provide a valid basis to not
13 allow any recovery of incentive compensation costs in rates?

14 A. No. I disagree with his analysis and his conclusions. Mr. Coppola's conclusion that
15 Consumers Energy's incentive compensation plans do not benefit customers is not
16 correct. A wide body of research supports the view that, when properly selected and
17 implemented, as has been done with the Company's plans, incentives motivate
18 employees, focus employees on a company's goals, and increase both individual work
19 performance and team performance. The overall compensation levels are reasonable.
20 The incentive compensation is part of the overall reasonable level, not in addition to it.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. At page 28 of his testimony, Mr. Coppola states: “Generally, the Company’s short term
2 incentive plans are too heavily weighted toward financial measures that mostly benefit
3 shareholders and not customers.” He makes a similar statement at page 36. Do you
4 agree?

5 A. No. As evidenced in my testimony, it is important that the utility remain financially
6 strong so that it can provide the utility service that customers expect and deserve. It is in
7 the customers’ interests to have a financially healthy utility. This allows the utility to
8 better meet customer needs at the best price. The two financial goals are balanced with
9 other operational and performance criteria. Having a financially healthy utility is
10 important to customers and to the State of Michigan. Financial goals help focus
11 employees on achieving superior results in a cost-effective manner. By focusing
12 employees’ attention on goals that encourage improved performance and greater
13 efficiencies, customers are benefited. The incentive compensation goals are designed to
14 help motivate employees to perform at their full potential and exercise discretionary
15 effort to help move the Company forward.

16 Mr. Rasmussen states in his testimony that Consumers Energy’s planned
17 investments in Michigan over the next five years to maintain and improve utility
18 infrastructure, increase energy generated from renewable resources, and ensure customers
19 receive the quality of service they expect from the Company which is one of the largest
20 investors in the state of Michigan. In addition to direct benefits to customers, these
21 investments will generate economic benefits within Michigan.

22 As I state in my testimony, financial health leads to lower costs of capital. For
23 evidence of this one can look to the Utility bond spread or difference in yield (rate of

AMY M. CONRAD
REBUTTAL TESTIMONY

1 return) between different securities, due to different credit quality. It indicates that a
2 financially healthy company with higher credit ratings will generally have lower credit
3 spreads and a lower overall cost of capital. This is why for instance an A-rated company
4 has lower cost of capital than a B-rated company.

5 Q. At page 29 of his testimony, Mr. Coppola states: "I see considerable duplication in many
6 of the measures. . . Given that the payout is based on achieving a certain number of
7 performance measures, the duplication makes it more likely that the target level will be
8 achieved." Do you agree?

9 A. No. Overall the package of goals is designed to help employees remain focused on a
10 portfolio of factors that will help Consumers Energy deliver value to its customers, while
11 continuing to be attractive to investors in order to be able to complete needed
12 investments. Evaluating progress being made in more than one way can help focus
13 employee attention on the desired goals.

14 Q. Please provide some examples.

15 A. Employee Safety – The Company's employee safety performance for 2012 was measured
16 two ways to emphasize the importance of employee safety to the Company and to ensure
17 we are looking at performance compared with other utilities for improvement
18 opportunities. The metrics are related, but not duplicative. One measure is relative to
19 how other utilities are doing and the other was absolute. The relative measure
20 (1st quartile performance) can be impacted both by the Company's own performance and
21 by the performance of peer companies. By using both measures, the Company set an
22 aggressive target for year over year results that can be monitored throughout the year.
23 Consumers Energy has a vision of being a best in class utility in the area of safety. With

AMY M. CONRAD
REBUTTAL TESTIMONY

1 the relative metric, the Company keeps an eye on the marketplace to ensure its safety
2 performance is keeping up with the best performing companies. The discipline of
3 achieving safety targets is an important foundation for other performance results as well,
4 as illustrated in my Exhibit A-17 (AMC-2) Growing Forward Goals. In order to help
5 maintain the emphasis on employee safety, for 2013 employee safety target is expressed
6 in terms of achieving a reduced number of incidents below the level experienced in 2012.

7 Customer Satisfaction – While the call center response is a factor in customers’
8 view of Consumers Energy, it is not the only driver of the satisfaction results. In fact, in
9 2012, the Company met the average speed of answer metric but did not achieve the four
10 of five customer satisfaction surveys. Again, these measures are related but not
11 duplicative. Keeping focus on customer satisfaction directly relates to delivering value
12 for customers.

13 Productivity – The Company has taken on a major effort to improve productivity
14 by becoming more efficient, improving customer satisfaction and increasing output. The
15 focus on measurement of activities is designed to identify measurable items that impact
16 efficiency, satisfaction, or output. More work is being completed with fewer employees,
17 which delivers a bottom line value to customers. In addition to safety and customer
18 satisfaction, a Company-wide focus on productivity which is aggressively measured and
19 monitored will deliver value to customers.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. At page 29 of his testimony, Mr. Coppola states: “In the financial measures, the
2 operating cash flow is directly linked to earnings. So if earnings per share go up, it is
3 most likely that operating cash flow will also go up.” Do you agree?

4 A. No. While earnings and cash flow are related, they are not the same. Earnings per share
5 is a measure of the profit generated by a company’s daily operations. This figure
6 includes revenues and expenses. Some of the expenses used to calculate earnings are
7 considered “non-cash” items, such as depreciation and amortization, and do not impact
8 cash flow. The incentive operating cash flow is a measure of the cash generated from
9 operations and what is needed to make investments in the utility.

10 Q. At page 29 and continued on page 30 of his testimony, Mr. Coppola states: “Another
11 concern is the low threshold to achieve a payout under the EICP. This is a very generous
12 incentive plan that is not directly connected with achieving superior customer benefits
13 before making threshold incentive payouts.” Do you agree?

14 A. No. When setting payout levels, threshold is set at a level of achievement that can
15 typically be reached eight or nine times out of every ten years. Maximum payout is for
16 exceptional performance (one to two times out of every ten years). These levels are to
17 engage the participants in meeting the goals. Employees, as a whole, must re-earn the
18 incentive/at risk portion of compensation each year. If the threshold to achieve a payout
19 was set at a level viewed as not achievable, it would be difficult to maintain employee
20 motivation and would result in less customer benefits. Overall compensation levels
21 including the EICP at target (100%) level that Consumers Energy seeks is not excessive.
22 It is reasonable for Consumers Energy to pay its employees competitive levels of
23 compensation.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. Do you have any additional response regarding Mr. Coppola's statement that the
2 incentive plan is not directly connected with achieving superior customer benefits?

3 A. Yes. Customers directly benefit from having a qualified, talented, and motivated
4 workforce that is focused on areas such as safety, reliability, and customer value. The
5 incentive compensation program encourages employees to deliver their best performance
6 for customers. This is illustrated in the area of safety. The number of safety incidents in
7 2006 was at 495. In 2007 the number of incidents increased to 558. Each year since then
8 incidents have decreased: 355 in 2008, 258 in 2009, 207 in 2010, 149 in 2011, and
9 119 in 2012. This decrease from 2006 to 2012 of approximately 75% can be attributed to
10 the significant emphasis Consumers Energy has placed on safety during this period. The
11 safety components of the EICP performance measures have been an important part of
12 keeping an employee focused on safety.

13 Q. At page 30 of his testimony, Mr. Coppola states: "Still another concern is with
14 employees receiving a payout under the EICP even though their performance is less than
15 par." Do you agree?

16 A. No. As evidenced in my testimony, it is necessary and appropriate for a large
17 organization, such as Consumers Energy, to establish broad goals and objectives that are
18 communicated to all employees as matters that are important to the success of the
19 organization. Some employees will be in a better position to influence whether particular
20 goals and objectives are met, but having every employee linked to a set of common
21 customer focused objectives is an effective method for emphasizing the importance of
22 customer value and service. Having common goals and objectives: (i) provides clear
23 communication of Company goals; (ii) encourages employees to support each other and

AMY M. CONRAD
REBUTTAL TESTIMONY

1 work together for common goals; and (iii) provides a scorecard with a focus on
2 corporate-wide goals that benefit customers. Consumers Energy incorporates individual
3 goals through the annual performance feedback process, which includes the creation and
4 review of individual goals and objectives for each salaried employee and the opportunity
5 to recognize and reward individual performance. The existence of a common set of
6 customer objectives enables supervisors and employees to establish individual goals and
7 objectives which are supportive of and in alignment with the corporate goals reflected in
8 the EICP. The approach used is valid and reasonable management tool.

9 Q. At page 30 of his testimony, Mr. Coppola states: “In response to a discovery question the
10 Company reported that it has granted merit/salary increases in each year from 2006 to
11 2012 and has included such an increase also in the test year O&M expenses for all
12 employee labor costs. . . Such significant increases in compensation are difficult to
13 justify. . .” Do you agree?

14 A. No. Salary structures and trends are reviewed annually. I present evidence in my
15 testimony that the overall compensation levels are reasonable relative to the market, are
16 determined in a reasonable manner, and are a reasonable cost of doing business. The
17 Company's merit increases have aligned with market data. As indicated in my testimony,
18 a 2012 Mercer survey and 2012 World at Work survey both indicated that pay increases
19 are expected to be 3.0 percent. This increase correlates to historic and projected merit
20 budgets. Customers are best served when Consumers Energy can attract, retain, and
21 motivate a talented work force with compensation packages that are competitive and fair.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. At page 32 of his testimony, Mr. Coppola states: “It is very clear from the design of the
2 LTIP that the intent of this incentive plan is to reward officer, directors and other
3 management employees for increasing shareholder value. There is no customer service or
4 operating efficiency measures that directly tie the cost of this plan to utility customers.”
5 Do you agree?

6 A. No. Long-term incentive pay is designed to reward good long-term decisions for the
7 Company and for customers. The Company's long-term incentive plan does not duplicate
8 the measures of the short-term incentive plan thus opening up the recipient to being
9 rewarded twice for the achievement of a single performance measure. The tenure based
10 restricted stock helps build executive share ownership, alignment with Company and
11 customer interests, and serves as a retention mechanism.

12 Q. At page 30 of his testimony, Mr. Coppola states: “. . . the fact that the performance
13 measures use CMS Energy financial information and comingle electric and gas business
14 measures is a concern.” Do you agree?

15 A. No. As evidenced in my testimony, for purposes of efficiency and improved service, the
16 Company has combined operations as one organization. For that reason the plan contains
17 both gas and electric measures.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 **III. Rebuttal to Energy Michigan Witness Zakem**

2 Q. At page 5 of his testimony, Mr. Zakem states: “There is nothing inherently good or bad
3 with inclusion of ‘incentive compensation’ in rates for utility service.” Does this
4 statement reflect an appropriate focus insofar as it relates to the incentive compensation
5 costs that Consumers Energy is seeking in this case?

6 A. No. The focus of Mr. Zakem’s statement is incorrect. A more appropriate focus is
7 whether there is anything inherently good or bad about including a competitive level of
8 compensation in rates. For reasons I discuss in my direct testimony, it should be apparent
9 that it is reasonable and necessary to pay employees a competitive level of compensation
10 and this is an reasonable cost of business that should be recoverable from customers.

11 Q. At page 6 of his testimony, Mr. Zakem states: “For any rate-paying customer to pay an
12 additional bonus to a utility for increasing earnings per share is illogical.” Do you agree?

13 A. No. The EICP is not a bonus or profit sharing plan. A bonus is a discretionary payment
14 given without predetermined goals or objectives and a profit sharing plan entitles
15 employees to a share of the profits of the company. Consumers Energy offers incentive
16 compensation, which is based-on predetermined goals and objectives and award levels.
17 Incentive compensation is part of an employee’s overall compensation and not in addition
18 to it like a bonus or profit sharing plan. The fact that a portion of compensation is in the
19 form of an incentive payment does not mean that employees are paid in excess of market
20 rates when they receive their incentive payment. Employee compensation is a reasonable
21 cost of doing business. If overall compensation levels are reasonable, then those costs
22 should be recoverable through utility rates.

AMY M. CONRAD
REBUTTAL TESTIMONY

1 Q. At page 7 of his testimony, Mr. Zakem states: "I would recommend that the electric
2 measures be in electric rates, and the gas measures be in gas rates." Do you agree?

3 A. No. The incentive structure incorporates: (i) safety; (ii) reliability; (iii) customer value;
4 and (iv) financial incentive measures. Performance in these areas is critical for the
5 Company's success in its electric public utility business. For purposes of efficiency and
6 improved service, the Company has combined operations as one organization.

7 Q. Does this conclude your rebuttal testimony?

8 A. Yes.

1 JUDGE CUMMINS: With regard to Exhibits
2 A-16, A-17, and A-18, I'll withhold ruling on those until
3 the end of cross-examination. Which parties have
4 cross-examination for Ms. Conrad?

5 MR. MOODY: Attorney General.

6 JUDGE CUMMINS: The Attorney General,
7 very well. Please proceed, Mr. Moody.

8 MR. MOODY: Thank you, your Honor.

9 JUDGE CUMMINS: Actually, let me take a
10 second. We did appearances earlier, Mr. Bzdok. Why
11 don't you give us your appearance for today.

12 MR. BZDOK: Thank you, Judge.
13 Christopher Bzdok on behalf of the Michigan Environmental
14 Council and the Natural Resources Defense Council. I
15 apologize, I had a couple mishaps on my trip down this
16 morning.

17 JUDGE CUMMINS: That's -- hopefully
18 you're still intact.

19 MR. BZDOK: Very fine.

20 JUDGE CUMMINS: You didn't come in on
21 crutches; that's always a good sign.

22 Mr. Moody, with that, please proceed.

23 CROSS-EXAMINATION

24 BY MR. MOODY:

25 Q Good morning, Ms. Conrad.

1 A Good morning.

2 Q Let's start off with a hypothetical assumption here.

3 Assume that the State of Michigan has high unemployment
4 and many of the non-utility businesses are cutting
5 salaries and laying off workers. With that assumption in
6 mind, would you still make the same recommendations that
7 you have made in your direct testimony and rebuttal in
8 this case?

9 A Yes. Overall compensation levels are reasonable relative
10 to the market, are determined in a reasonable manner, and
11 are a reasonable cost of doing business.

12 Q All right. In preparing your testimony for this case, do
13 you take into account the state or national economy?
14 Does that affect your analysis in any way?

15 A Again, overall compensation levels are reasonable
16 relative to the market and are a reasonable cost of doing
17 business.

18 Q I know that they are reasonable in that regard, but do
19 you take into account the state of the economy in any of
20 your factors in deciding what would be a reasonable
21 compensation level for the Company?

22 A We set our compensation levels at market. I mean, we do
23 a market survey, and that would incorporate looking at
24 pay of other utilities.

25 Q And do you look outside of the utilities for your market

1 survey?

2 A No.

3 Q So if the state of the economy is poor for all the
4 non-utility companies, that's not a factor then,
5 obviously, in your analysis for this case, right?

6 A We focus our studies on utility companies. That is where
7 we would look to attract talent from.

8 Q Do you know whether Consumers Energy management and
9 employees have taken any pay cuts to reduce the amount of
10 rate increase needed for the Company?

11 A I am not aware.

12 Q All right. Are you aware of any cuts in benefits along
13 that line?

14 A I'm also not aware.

15 MR. MOODY: Your Honor, may I approach
16 the witness?

17 JUDGE CUMMINS: Certainly.

18 (Document shown to Mr. Chambers and handed to the
19 witness.)

20 Q (By Mr. Moody): Ms. Conrad, I am handing you what's been
21 marked Attorney General Exhibit 7. It's in Sebastian
22 Coppola's testimony.

23 When you were preparing your testimony in
24 this case did you review the direct testimony and
25 exhibits of Mr. Coppola?

1 A Yes, I did review them.

2 Q Do you recall reviewing Attorney General Exhibit 7
3 dealing with salaries and wage increases?

4 A I do not recall at this time.

5 Q Let me ask you this question. Do you agree with the
6 statement that annual salaries for Consumers Energy
7 employees have increased 2.5 percent to 3 percent each
8 year?

9 A Yes, I do agree with that statement.

10 Q Actually that's all I needed out of that one exhibit. I
11 can take it from you.

12 (Document returned to Mr. Moody.)

13 Do you agree with the statement that --
14 Well, I guess turn first to page 30 of your direct
15 testimony. I'm sorry, I'm looking at the wrong one. Do
16 you have Sebastian Coppola's testimony in front of you,
17 direct testimony?

18 A I do not, no.

19 MR. MOODY: Your Honor, may I approach
20 the witness again?

21 JUDGE CUMMINS: Certainly, Mr. Moody.

22 Q (By Mr. Moody): Ms. Conrad, I'm handing you a copy of
23 Sebastian Coppola's direct testimony and exhibits filed
24 in this case.

25 A O.K.

1 MR. CHAMBERS: Mr. Moody, is there a
2 particular page you want her to look at?

3 MR. MOODY: Yes, page 30, if you could.
4 Thank you.

5 Q (By Mr. Moody): At the bottom of page 30 of Mr.
6 Coppola's direct testimony he talked about salary
7 increases over the eight-year period equaled to about a
8 28 percent increase. Do you see that statement?

9 A Yes, I do.

10 Q Do you have any reason to disagree with that?

11 A Salary increase has averaged between two and a half and
12 three percent per year. I agree with that statement.

13 Q And the sentence after that, the salary increases over
14 the eight-year period translate into 28 percent compound
15 growth. Do you disagree with that or have reason to
16 disagree?

17 A I just would like to state that we review structures and
18 trends of salary on an annual basis and adjust our pay
19 accordingly to keep up with the market.

20 Q And is that then -- Do you disagree then with that
21 statement on the bottom of page 30?

22 A I have not re-computated the math in order to agree or
23 disagree with the statement.

24 Q When you reviewed Mr. Sebastian Coppola's testimony, did
25 you rebut that sentence in your rebuttal anywhere?

1 MR. CHAMBERS: Your Honor, could we
2 clarify which sentence Mr. Moody is referring to?

3 MR. MOODY: I'm sorry.

4 Q (By Mr. Moody): Again looking at the bottom of page 30,
5 starting with the salary increases, going into
6 subsequently page 31, ending with 2010. Or ending with
7 employees; I'm sorry. Looking at that sentence there,
8 when you reviewed Mr. Sebastian's testimony and prepared
9 your rebuttal, did you address that sentence anywhere, or
10 rebut it?

11 A On page 11 of my rebuttal I went through and responded to
12 those various.

13 Q Thank you. In your direct testimony in this case you're
14 proposing that the Commission should authorize recovery
15 of 9 million of the incentive compensation for Consumers
16 Energy; is that correct?

17 A Yes.

18 Q If I could turn your attention to Exhibit A-16 of your
19 direct testimony.

20 A O.K.

21 Q Is it true that -- I'm sorry. Are you at Exhibit A-16?

22 A Yes.

23 Q Is it true that 50 percent of short term incentive
24 compensation explained here is driven by financial
25 measures EPS and cash flow?

1 A Yes, that is true.

2 Q And EPS is earnings per share; is that correct?

3 A That is correct.

4 Q And isn't it true that the EPS numbers are CMS Energy
5 earnings per share and not Consumers Energy?

6 A That is correct.

7 Q Isn't it true that some of the safety measures discussed
8 here are related to both the gas and electric business
9 for Consumers Energy?

10 A Yes. For efficiency and improved service we have
11 combined the operations, and for those reasons they
12 include both gas and electric.

13 Q And that's the same with the customer value measures too?

14 A Yes, for the competitive price.

15 Q And looking at this exhibit, isn't it true that the
16 Company only needs to achieve 8 out of the 11 operating
17 measures to get a hundred percent payout under that
18 component?

19 A Yes, that is true. We set the levels so that they're
20 challenging but achievable to help motivate employees.

21 Q Isn't it true that the Company can only achieve six of
22 eleven measures, which is less than 60 percent, and still
23 get a 50 percent payout under the operating component?

24 A Under the operating component, yes.

25 Q Turning to page 7 of your direct testimony.

1 A O.K.

2 Q Looking at the bottom half there talking about long-term
3 incentive plans, can you describe how the long-term
4 incentive plan works?

5 A Yes. The long-term incentive plan is based on relative
6 total shareholder return for the portion that is
7 performance based, and then there also are awards that
8 can be based on tenure, which would be service.

9 Q All right. So what triggers a payout and what form of
10 payout is given to the employee?

11 A What triggers a payout? It would be, on the performance
12 base it would be looking at Consumers Energy's total
13 shareholder return and how that compares to a peer group.
14 At the end of a three-year period, if it's tenure based
15 it would be just waiting for a three-year service
16 requirement. And at the end of that time the individuals
17 receive stock. It's called restricted stock so at that
18 time the ability to transfer the stock would be lifted so
19 that they receive stock.

20 Q Isn't it true that the measures that trigger payouts are
21 primarily related to CMS Energy's stock performance
22 relative to other utilities in the peer group and a
23 portion is related to tenure or years of employment with
24 the Company?

25 A Yes, generally that's true.

1 Q I think you just said that. And isn't it true that the
2 triggers that result in granting the shares of stock are
3 not directly based on customer service levels or
4 operating performance of Consumers Energy?

5 A Financial health also benefits the customers, so having a
6 well performing stock price would provide benefits to
7 customers of Consumers. So there is some.

8 Q So your answer is yes, that the triggers that result in
9 granting these shares are not directly based on customer
10 service or operating performance of Consumers Energy?

11 A If you look at Exhibit A-17, which is the strategy
12 triangle, Consistent Financial Performance is the peak,
13 which is the results of all the operating measures at
14 Consumers. So the stock price which would be a financial
15 measure, would be a result of and provide benefits to the
16 customer, so the safe and excellent operations consider
17 the operational goals that are mentioned in Exhibit A-16.

18 Q Thank you. Under your analysis, here on that Exhibit
19 A-17 and in your testimony about the goals regarding
20 long-term incentive plans, could customers be totally
21 dissatisfied with service they are getting from the
22 Company -- I'm sorry. Could the companies be totally
23 dissatisfied with the service they are getting from the
24 Company, yet management still get a grant of shares of
25 stock?

1 MR. CHAMBERS: Your Honor, could I have
2 the question re-read?

3 JUDGE CUMMINS: Could you please re-read
4 or restate it?

5 MR. MOODY: Yes, I can.

6 Q (By Mr. Moody): Again, talking about the long-term --
7 the long-term incentive plan, looking at that analysis
8 that we're talking about.

9 A O.K.

10 Q And your testimony and exhibits around that point. Isn't
11 it true that customers could be totally dissatisfied with
12 the service they're getting from the Company, Consumers
13 Energy, and yet the management of Consumers Energy could
14 still get a grant of shares of stock underneath this
15 long-term incentive plan?

16 A Yes. Customer satisfaction is only one of the
17 operational measures, so it would be possible.

18 Q And in your testimony are you proposing that customers
19 pay approximately four million in expense relating to
20 these stock grants?

21 A Yes, that's correct.

22 Q Turning to your rebuttal testimony at page 8.

23 A All right.

24 Q At page 8 you talk about or you disagree with Sebastian
25 Coppola's testimony about cash flow increases with

1 earnings. Do you see that testimony?

2 A It's at the bottom of page 8, is my response to Coppola's
3 question.

4 Q Could you explain how the cash flow number is determined
5 and what the components are?

6 A I do not have the details of that information with me.

7 Q O.K. Can you give me generally -- Let me give you a
8 scenario or an example or a simple example and tell me if
9 this makes sense. Does the calculation start with
10 earnings after taxes, plus -- I'm sorry. Stop there.
11 Does the calculation start with earnings after taxes,
12 plus depreciation, plus interest expense, as well as some
13 other adjustments?

14 A It starts with the Generally Accepted Accounting
15 Principles, operating cash flow from the 10K.

16 Q And what are those? What are those generally -- what are
17 those points that you're talking about? Or can you
18 restate that?

19 A I don't have the details with me, but the operating cash
20 flow starts with operating cash flow from the SEC filing,
21 the 10K, which is under Generally Accepted Accounting
22 Principles.

23 Q Then do you look at -- Your operating cash flow, is that
24 the same as your earnings after taxes or is that
25 different?

1 A There are various accounting adjustments and I did not
2 bring all the details with me.

3 Q I understand that. I don't have to have an exact, you
4 know, all of the different components that you take to
5 determine this cash flow number. But do you have --

6 A It starts with earnings of the Company.

7 Q O.K. So when you say it starts with earnings, is that
8 earnings after taxes?

9 A I don't recall at this time. I'd have to look.

10 Q Do you take into account depreciation in that, in cash
11 flow?

12 A It's a noncash, you don't do depreciation.

13 Q Does interest expense, is that included anywhere in your
14 cash flow?

15 A It is included in the cash flow statement. It is not an
16 operating activity.

17 Q O.K. In your direct testimony do you discuss the cash
18 flow number or is that -- Is it the analysis you do
19 outside of the direct testimony?

20 A It's not discussed in direct testimony.

21 Q In responding to Sebastian Coppola's analysis on cash
22 flow, do you provide any analysis then on how you prepare
23 your cash flow analysis in the rebuttal?

24 A In the rebuttal or the direct testimony, no.

25 Q Let me ask you this: Isn't it true that if earnings of

1 Consumers Energy go up and down, does that mean the cash
2 flow amounts would also go up and down, assuming other
3 components stay the same?

4 A Not necessarily because the earnings can include noncash
5 items.

6 Q What kind of --

7 A Depreciation amortization would be examples of a noncash
8 item.

9 MR. MOODY: O.K. That's all the
10 questions, your Honor. Thank you.

11 JUDGE CUMMINS: Ms. Conrad, before we
12 check with anyone else, I just had two basic questions.
13 These will show what a neophyte I am in these areas.

14 With regard to the peer group that the
15 Company tends to use in assessing what compensation
16 levels are adequate to retain personnel that are desired,
17 is there a reason that the Company does not go beyond
18 utilities? It seems to be it's utility-based. Is there
19 a reason for not going beyond utilities-based in looking
20 at corporations of the same size, whether regional or
21 national?

22 A For the primary employees we use the utilities as our
23 primary source of data when we are determining market
24 mediums or where to set our levels of pay. If no
25 information were available, we do have access to

1 non-utility data. But when we are setting our
2 structures, we base it off on who we compete with for
3 talent, which would be other utility companies.

4 JUDGE CUMMINS: Is that regional or
5 national, do you know?

6 A Depending on the survey provider and what data is
7 available, we look at a geographic or a revenue base
8 scoping.

9 JUDGE CUMMINS: O.K. So if it was one
10 where, let's say it's a starting engineer, it's easier to
11 find something that's regional versus national; is that
12 correct?

13 A The information we have available is regional
14 information, so we do have that available.

15 JUDGE CUMMINS: The second question I had
16 was: Do you have any idea, have you looked at or do you
17 have any idea with regard to what the increase in pay
18 levels have been in similar size companies? Or haven't
19 you looked at that, whether regional or national, over
20 the last eight years that Mr. Moody was referring to?

21 A I don't have information over the last eight years that
22 would have various studies that look at the trends of
23 where salaries have been going. And they have been
24 averaging around 3 percent increases on an annual basis.

25 JUDGE CUMMINS: O.K. Thank you, Ms.

1 Conrad. Did any of the other parties have questions of
2 this witness?

3 Hearing none, we have before us three
4 exhibits, these are A-16, A-17, and A-18. Is there an
5 objection to the receipt of these three exhibits?

6 MR. MOODY: No, your Honor.

7 JUDGE CUMMINS: Very well. Exhibits
8 A-16, A-17, A-18 are received. You may step down, Ms.
9 Conrad. Thank you.

10 THE WITNESS: Thank you.

11 (The witness was excused.)

12 MR. CHAMBERS: Your Honor, could we go
13 off the record a moment?

14 JUDGE CUMMINS: Certainly.

15 (Brief in-place recess was taken.)

16 - - -

17 CHRISTOPHER J. VARVATOS

18 was called as a witness on behalf of Consumers Energy
19 Company and, having been duly sworn to testify the truth,
20 was examined and testified as follows:

21 JUDGE CUMMINS: Very well. Mr.
22 McQuillan, please proceed.

23 MR. McQUILLAN: Thank you, your Honor.

24 - - -

DIRECT EXAMINATION

BY MR. McQUILLAN:

Q Good morning, Mr. Varvatos.

A Good morning.

Q Could you state your name and business address for the record, please.

A Christopher J. Varvatos, One Energy Plaza, Jackson, Michigan 49201.

Q Mr. Varvatos, did you cause to be prepared in this case direct testimony consisting of a cover page and 19 pages of questions and answers?

A I did.

Q Do you have a copy of that with you today?

A Yes.

Q If I were to ask you the questions contained in the direct testimony today, would your answers be the same?

A Yes.

Q Do you adopt that as your sworn direct testimony in this cause?

A Yes.

Q In conjunction with your direct testimony did you cause to be prepared exhibits which have been marked for the Court Reporter as A-64, A-65, A-66, A-67, and A-68?

A Yes.

Q Do you have a copy of your exhibits with you today?

1 A Yes.

2 Q Do you have any corrections or changes to those exhibits?

3 A No.

4 Q And those are the exhibits that are referenced in your
5 direct testimony?

6 A Yes.

7 Q Mr. Varvatos, did you also cause to be prepared rebuttal
8 testimony consisting of a cover page and 12 pages of
9 questions and answers?

10 A Yes.

11 Q Do you have a copy of that with you today?

12 A Yes.

13 Q If I were to ask you those questions would your answers
14 be the same?

15 A Yes.

16 Q And do you adopt that as your sworn rebuttal testimony in
17 this cause?

18 A Yes.

19 Q In conjunction with your rebuttal testimony did you cause
20 an exhibit to be prepared which has been marked as
21 Exhibit A-82?

22 A Yes.

23 Q Do you have a copy of that with you today?

24 A Yes.

25 Q Do you have any corrections, changes, or modifications to

1 that exhibit?

2 A No.

3 Q Is that the exhibit that is referenced in your rebuttal
4 testimony?

5 A Yes.

6 Q Thank you, Mr. Varvatos.

7 MR. McQUILLAN: Your Honor, I would move
8 the admission of the direct testimony consisting of a
9 cover page and 19 pages of questions and answers, the
10 rebuttal testimony consisting of a cover page and 12
11 pages of questions and answers, and the exhibits as
12 identified, A-64 through A-65 [sic] and A-82 into the
13 record and would then tender the witness for
14 cross-examination.

15 JUDGE CUMMINS: By way of clarification,
16 I believe, Mr. McQuillan, you're looking for exhibits in
17 the direct of A-64 through A-68; is that correct?

18 MR. McQUILLAN: I'm sorry. Yes, sir.

19 JUDGE CUMMINS: Then we have A-82 which
20 is part of the rebuttal?

21 MR. McQUILLAN: That is correct.

22 JUDGE CUMMINS: Any objection to binding
23 in Mr. Varvatos' direct or rebuttal testimony? Hearing
24 none, Mr. Varvatos' direct and rebuttal testimony will
25 bound into the record.

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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

DIRECT TESTIMONY
OF
CHRISTOPHER J. VARVATOS
ON BEHALF OF
CONSUMERS ENERGY COMPANY

CHRISTOPHER J. VARVATOS
DIRECT TESTIMONY

1 Q. Please state your name and business address.

2 A. Christopher J. Varvatos, One Energy Plaza, Jackson, Michigan.

3 Q. How long have you worked for Consumers Energy Company (“Consumers Energy” or
4 the “Company”) and what positions have you held?

5 A. I have been with Consumers Energy for over 19 years, having worked all of that time in
6 the Information Technology (“IT”) department. I joined the Company as a Systems
7 Analyst, and have held a number of increasingly responsible positions, including team
8 leader, large project manager, manager of application development and director. I am
9 currently the Director of Business Relationship Management for Distribution and
10 Customer Operations. In this capacity I serve as the primary liaison between the IT
11 department and the gas and electric energy distribution departments.

12 Q. Would you please state your educational background?

13 A. I earned a Bachelor of Science degree in Industrial and Systems Engineering from the
14 University of Michigan – Dearborn in May of 1985.

15 Q. Have you ever testified in any other proceedings before this Commission?

16 A. Yes, I filed rebuttal testimony in MPSC Case No. U-16855.

17 Q. What is the purpose of your testimony in this proceeding?

18 A. The purpose of my testimony is to describe the Business Technology Solutions (“BTS”) department, and then identify and support the BTS department’s: 1) Operation and
19 Maintenance (“O&M”) expense and 2) Capital Expenditures. I will discuss the hardware
20 and software application projects and maintenance costs. I will also describe the Asset
21 Management capital expenditures and Major Computing Infrastructure projects.
22

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1 Q. What exhibits are you sponsoring in this proceeding?

2 A. I am sponsoring the following exhibits:

3 Exhibit A-64 (CJV-1) Employee and Contractor Counts

4 Exhibit A-65 (CJV-2) Summary of Projected Electric & Common O&M
5 Expense for the Years 2011 - 2013

6 Exhibit A-66 (CJV-3) Summary of Projected Electric & Common Capital
7 Expenditures for the Years 2011 - 2014

8 Exhibit A-67 (CJV-4) Software Applications Capital

9 Exhibit A-68 (CJV-5) Asset Management Capital

10 Q. Were these exhibits prepared by you or under your supervision?

11 A. Yes, they were.

12 **DESCRIPTION OF THE BTS DEPARTMENT**

13 Q. Please describe the BTS department.

14 A. The BTS department is the IT department for Consumers Energy. It is staffed by a mix
15 of Company employees and contractors, as shown in Exhibit A-64 (CJV-1) Employee
16 and Contractor Counts. While the number of Company employees has been relatively
17 stable over the years, the number of contractors can vary widely depending on the
18 workload within the department in any given year.

19 Q. What is the purpose of the BTS department?

20 A. The purpose of the BTS department is to provide and maintain reliable and secure IT
21 solutions and services that support the Company's business objectives.

22 Q. Please describe the functions that the BTS department performs.

23 A. The BTS department provides IT solutions and services including the identification,
24 implementation, operational support and maintenance of software solutions, computing
25 and communications infrastructure. BTS also provides the day-to-day operational

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1 support for each individual user of technology, whether that technology is a desktop,
2 laptop, or mobile device, which includes ruggedized field devices, tablet computers, cell
3 phones, smart phones or other handheld devices.

4 Q. What is meant by the phrase “software solutions”?

5 A. Software solutions are business applications that automate and support business functions
6 such as customer service and billing, work and asset management, outage management,
7 payroll, supply chain, electronic mail, and document creation and management. The BTS
8 department operates and maintains a full range of tools and computing infrastructure for
9 the software applications utilized by the Consumers Energy work force.

10 Q. Please describe the Company’s computing infrastructure.

11 A. Consumers Energy’s computing infrastructure consists of hardware and communications
12 networks which are utilized by virtually all aspects of Company operations. Hardware
13 includes servers and data storage devices, bill processing equipment, workstations,
14 printers, and mobile devices. Communications networks for telephone and radio systems
15 enable voice, data and wireless communications across the Company.

16 Q. How do software solutions and computing infrastructure provided by the BTS department
17 support the Company and benefit its customers?

18 A. The IT that is supplied and supported by BTS facilitates virtually every work process in
19 the Company and helps the business run more efficiently. Software applications, and the
20 computing infrastructure they run on: (i) support the work force in the customer call
21 centers to respond to customer requirements; (ii) support the distribution-field operations
22 and generating plants to schedule and track work; (iii) support the supply chain functions
23 to procure, distribute and assign material to the worksites; and (iv) support the “back

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1 office” to perform the business functions of accounting, accounts receivable including
2 customer billing, and accounts payable. “Back office” refers to the internal functions of
3 an organization, which are not “customer facing” functions. Customer facing functions
4 are collectively known as “front office” functions.

5 In addition, the communications infrastructure provides voice and data
6 communications flow between customers and the Company; between dispatchers and
7 work crews; between Company personnel at any location; between the Company and its
8 vendors and other relevant stakeholders. The reliability and functionality of the software
9 applications and the computing infrastructure is operationally critical to public and
10 workforce efficiency and safety.

11 **BTS DEPARTMENT’S O&M EXPENSES**

12 Q. Please describe Exhibit A-65 (CJV-2) Summary of Projected Electric & Common O&M
13 Expense for the Years 2011 - 2013.

14 A. Exhibit A-65 (CJV-2) Summary of Projected Electric & Common O&M Expense for the
15 Years 2011 - 2013 summarizes the Electric allocation of actual and projected BTS
16 department’s O&M expenditures. Specifically:

- 17 • Column (a) provides the O&M expense category
- 18 • Column (b) identifies the 2011 actual O&M expense as \$32,687,000
- 19 • Column (c) identifies the 2012 projected O&M expense as \$35,489,000
- 20 • Column (d) identifies the 2013 projected O&M expense as \$36,238,000
- 21 • Column (e) identifies the source reference

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1 Q. Please explain how the 2011 BTS department's O&M expenses were calculated.

2 A. The 2011 BTS department's O&M expenses were taken from the Company's records for
3 the period January through December 2011. These costs include internal and external
4 labor costs associated with operating and maintaining the Company's business software
5 systems and the computing infrastructure. Licensing of software systems and
6 maintenance contracts for computing infrastructure and communications networks are
7 also operating expenses included in the BTS department costs.

8 Q. In the electric rate case, MPSC Case No. U-16191 the MPSC approved BTS O&M for
9 the 12 months ending June 30, 2011, of \$33,669,000. In MPSC Case No. U-16794, the
10 Company requested BTS O&M in the amount of \$32,766,000 for 2011. How much
11 O&M did BTS actually spend in 2011?

12 A. In 2011, BTS spent \$32,687,000 in O&M, as shown in Exhibit A-64 (CJV-1) Summary
13 of Projected Electric & Common O&M Expense for the Years 2011 - 2013. This is
14 \$79,000 or two tenths of a percent less than what was requested.

15 Q. Please explain the increase requested in this docket in O&M expense between 2011 and
16 2012.

17 A. The 2012 O&M is 8.6% higher than 2011. This mainly reflects increases in the costs of
18 hardware and software maintenance agreements, and increases in the costs of circuits
19 used by the Company's voice and data networks. New software applications typically
20 have maintenance agreements with the software provider to ensure continued
21 performance of the software. New software applications quite often also require
22 additional computer hardware such as servers and storage devices, and maintenance
23 agreements with third party providers are used to ensure the continued performance of

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1 the hardware. Hardware and software maintenance costs are increasing from 2011 to
2 2012 as new software applications such as the Customer Relationship Module 7
3 (“CRM 7”) and Device Lifecycle Management (“DLM”) and other, smaller systems are
4 placed into service.

5 The new software applications, including Microsoft Outlook, the Company’s
6 email system, Microsoft Communicator (an instant messaging system), and Sharepoint (a
7 system to facilitate document storage and retrieval), collectively will enhance employee
8 productivity and collaboration while contributing to the growth in data traffic on the
9 Company’s network. In addition, the increased use of video conferencing, video
10 presentations, and wireless Local Area Networks also drive up the bandwidth
11 requirements for the network. Additional circuits have been obtained for 2012 and 2013
12 to satisfy these bandwidth requirements. The Company’s Dark Fiber East Expansion
13 project will help to offset the growth in these costs. This project is discussed in the Asset
14 Management portion of my testimony.

15 2012 also reflects the increased costs associated with the Company’s investments
16 in cyber security. Recently the Company adopted an industry standard framework for
17 computer (or cyber) security. This framework has served as a guide to the Company’s
18 computer security program, which has resulted in new investments in cyber security.
19 Many of these new investments have resulted in ongoing maintenance and support costs,
20 and those costs are included in this case. 2012 includes \$1.3M of additional O&M
21 expense over 2011 for cyber security.

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1 Q. Please describe the CRM 7 software application.

2 A. CRM 7 is an application that will both improve service to customers and support
3 Automated Metering Infrastructure (“AMI”) enablement. As described in the Company’s
4 filing in MPSC Case No. U-16794, the initial phase of the CRM 7 project comprises the
5 replacement of existing Windows based Customer Service functions with a Web based
6 version. These enhanced functions will provide Consumers Energy employees with
7 simplified system views including enhanced search capabilities for account identification,
8 improved continuity of customer information through Interaction Record history, and
9 streamlined system navigation. This improved navigation will allow Consumers Energy
10 employees to answer all customer questions with increased efficiency, optimizing
11 processing times for employees, leading to improved customer satisfaction.

12 Q. What are some of the benefits of CRM 7?

13 A. Some of the benefits of implementing CRM 7 include: a reduction in the time it takes to
14 handle certain customer transactions, resulting in long term reductions in average call
15 handling time; reduction in the manual steps needed to review a customer’s debit/credit
16 transactions; improvements in processing of rate comparisons for the customer; a more
17 intuitive look and feel for the screens used by the customer service representatives;
18 simplified navigation for all search capabilities; a reduction in the amount of training
19 time required for new employees, and improved productivity for new employees upon
20 completion of training. BTS implemented this module in March of 2012.

21 Q. What are the benefits of CRM 7 for automated metering infrastructure and Smart Grid?

22 A. In addition to significant system navigation improvements, CRM 7 is also a foundational
23 improvement on which many of the advanced metering processes will be built. This will

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1 allow Consumers Energy to begin utilizing Smart Grid related functionality such as the
2 ability to trigger remote meter connection and reconnection, view customer interval data
3 and obtain on demand customer meter reads.

4 Q. Please describe the DLM system.

5 A. The objective of the DLM project is to implement an integrated enterprise software
6 solution to support the new meter device processes introduced by Smart Grid. The first
7 phase, which was implemented in March 2012, will support goods procurement, device
8 tracking, audit management, vendor evaluation and basic smart meter testing.
9 Replacement of the Meter Equipment Database and Meter Information and Records
10 Automation ("MED/MIRA") system also occurred in the first phase. Subsequent project
11 releases planned for 2012 will include the capability for MPSC reporting from the SAP
12 system, Supply Chain reporting to monitor devices installed, true-up activities for AMI
13 metering previously installed, and the ability to switch customers from manual to
14 automated meter reads.

15 Q. Please explain the difference in expense between 2012 and 2013.

16 A. 2013 is 2.1% higher than 2012, and mainly reflects increases in the costs of hardware and
17 software maintenance agreements, and increases in the costs of circuits, offset by
18 reductions in employee labor and staff augmentation.

19 Q. Are Consumers Energy's O&M expenses in the BTS department reasonable?

20 A. Yes. The levels of O&M expenses in the BTS department for 2012 and 2013 are
21 reasonable and appropriate in order to provide IT solutions and services for Consumers
22 Energy's electric business, including the operational support and maintenance of software
23 solutions and computing infrastructure, in a reliable and efficient manner. Benchmarking

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1 information supports the conclusion that O&M expenses in the BTS department are
2 reasonable, as the BTS financial performance is consistently better than the industry
3 average. For 2011, the Company's IT Spend as a Percent of Revenue was 2.1%, and this
4 was 17% less than the Gartner's utility average of 2.5% for Utilities with between \$1B
5 and \$10B in revenue.¹

6 In addition, the Company's IT Spend as a Percent of Operational Expense was
7 2.5%, which was 20% lower than the Gartner's utility average of 3.1% for Utilities with
8 between \$1B and \$10B in revenue.²

9 Finally, the Company's IT Spend per Employee was \$17,476, which was 5%
10 lower than the Gartner's utility average of \$18,325 for Utilities with between \$1B and
11 \$10B in revenue.³

12 Gartner was founded in 1979 and is the world's leading IT research and advisory
13 company. 80% of the Fortune 500 companies use Gartner for their key technology
14 initiatives, and each year Gartner delivers over 5,500 IT cost and performance
15 benchmarks.⁴

16 Q. What does BTS do to control costs in order to ensure customer value?

17 A. Contracts for non-specialized goods and services are competitively bid to maximize
18 business value. Projects are prioritized within BTS and across the Company to ensure
19 that the most critical needs of the customers and business are met. In addition, BTS uses

¹ Taken from the "IT Key Metrics Data 2012: Key Industry Measures: Utilities Analysis: Current Year, page 11, IT Spend as a Percent of Revenue section, Table 1.

² Taken from the "IT Key Metrics Data 2012: Key Industry Measures: Utilities Analysis: Current Year, page 12, IT Spend as a Percent of Operational Expense section, Table 2.

³ Taken from the "IT Key Metrics Data 2012: Key Industry Measures: Utilities Analysis: Current Year, page 14, IT Spend per Employee section, Table 3.

⁴ Taken from Gartner, Inc. website

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1 benchmarking information to determine whether its costs are in line with other IT
2 departments in the utility industry.

3 Q. What else is BTS doing to control costs?

4 A. Consumers Energy is also using its Employee Development and Sourcing Initiative
5 (“EDSI”) as another means of controlling costs. In our technology-driven world there is
6 an ever-increasing demand for IT solutions to business problems. Over the years
7 Consumers Energy has increasingly used contractors to assist with IT project design and
8 build. With the EDSI project, Consumers Energy will be moving employees from system
9 maintenance roles into roles that are focused on project design and build. The system
10 maintenance roles that had been traditionally performed by Company employees within
11 BTS will now be performed by contractors. This shift in workload will take place in
12 2012, and over time is expected to increase capacity to meet current and future demand.
13 Business value will be added by lowering the overall cost of maintenance for existing
14 technologies, which would support the incremental maintenance costs associated with
15 additional technology investments. Some of the projects that employees will be working
16 on in the test year, such as the Customer Value Initiative, are described in the section
17 entitled Software Application Projects.

18 Q. How does the Company decide which projects will be implemented?

19 A. Potential projects from departments across the Company are evaluated to determine
20 which projects are most needed by the business. This evaluation process begins with the
21 project sponsor or subject matter expert collaborating with a BTS Business Relationship
22 Manager to prepare a business case and a financial analysis for the project. Projects are

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1 presented to the officers for scoring and prioritization. The officers evaluate the benefits
2 and costs of each project and rank the projects.

3 Q. Is there a standard approach to evaluating the costs and benefits of the Company's
4 technology projects?

5 A. Yes. The project sponsors and Business Relationship Managers must document the
6 business case and financial costs and benefits using a standard format in order for the
7 project to be considered.

8 Q. Who decides which projects will be funded each year?

9 A. Technology projects are ranked along with other capital projects at the Corporate
10 Portfolio Management meetings. These meetings evaluate and prioritize all Company
11 projects, and the projects with the highest scores are approved to be funded.

12 Q. How are customer benefits included in project scoring?

13 A. Customer benefits are included in project scoring in three ways. The Customer Value
14 category is given a 70% weighting in the overall scoring of a project, and this is
15 comprised of the project's cost benefit ratio and the JD Power impact ratio. This
16 weighting favors projects that have strong financials in that they provide a good value for
17 the customer. It also favors projects that are designed with specific customer benefits.

18 The second way in which customer benefits are included in project scoring is
19 related to whether a project supports the long-term goals of the utility. Utility Goals
20 alignment is given a 15% weighting in project scoring, and three of these goals are
21 directly related to customer benefits. Those goals are Maintain Customer Safety,
22 Increase Customer Reliability, and Attain 1st Quartile Customer Satisfaction.

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1 The third way in which customer benefits are included in project scoring is related
2 to whether a project supports the Performance Measures of the Company. Performance
3 Measures alignment is also given a 15% weighting in project scoring, and a number of
4 performance measures are directly associated with customer benefits. These include Call
5 Center Response, Customer Satisfaction Surveys, Repetitive Electric Outages, Downed
6 Wire Response, Electric Competitive Price, Distribution Reliability Minutes, Gas Leak
7 Response and Gas Competitive Price.

8 **CAPITAL EXPENDITURES**

9 Q. What is the nature of the capital expenditures incurred by the BTS department?

10 A. The capital expenditures for the BTS department fall into three categories: 1) Software
11 Application projects; 2) Asset Management; and 3) Major Computing Infrastructure
12 projects.

13 Q. Please describe the capital expenditures shown on Exhibit A-66 (CJV-3) Summary of
14 Projected Electric & Common Capital Expenditures for the Years 2011-2014.

15 A. Exhibit A-66 (CJV-3) Summary of Projected Electric & Common Capital Expenditures
16 for the Years 2011-2014 identifies the Electric allocation of projected capital
17 expenditures to procure, install, and implement the software and infrastructure identified
18 earlier in this testimony to meet business requirements. Specifically:

- 19 • Column (a) provides the description of the capital expenditures
- 20 • Column (b) identifies the 2011 actual capital expenditures as \$46,073,000
- 21 • Column (c) identifies the 2012 projected capital expenditures as
22 \$51,511,000
- 23 • Column (d) identifies the 2013 projected capital expenditures as
24 \$46,028,000

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- 1 • Column (e) identifies the 2014 projected capital expenditures as
- 2 \$39,096,000
- 3 • Column (f) identifies the source reference for each category listed

4 Q. In the electric rate case MPSC Case No. U-16191, the Commission authorized BTS
5 capital of \$19,176,000 for the first six months of 2011. In MPSC Case No. U-16794, the
6 Company requested BTS capital in the amount of \$45,009,000 for 2011. Did BTS spend
7 the capital that was requested for 2011?

8 A. Yes. As stated above, actual capital expenditures for 2011 were \$46,073,000, which is
9 \$1,064,000 greater than the funding requested.

10 Q. How was the additional funding used?

11 A. The additional funding was used for new project development work, such as Information
12 Management & Reporting (“IMR”) projects. These projects included providing critical
13 work order, customer billing, call center and related data to our operational departments
14 for reporting and analysis of work completion metrics.

15 **SOFTWARE APPLICATIONS PROJECTS**

16 Q. Please describe some of the Software Application projects the Company plans to fund in
17 2012 through the end of the test year.

18 A. A number of projects are being developed as part of the Customer Value initiative, which
19 aims to improve our customers’ experience when they are dealing with the Company. A
20 summary of Software Applications costs from 2011 through 2014 is included as Exhibit
21 A-67 (CJV-4) Software Applications Capital. These include 2-Way Customer
22 Communications, which will give the Company the ability to communicate and conduct
23 its business in a way that better serves our customers’ needs, including enhanced
24 communications regarding outages and restoration times, and billing and payment

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1 notifications. Customer Analytics Reporting, which would help the Company to better
2 understand why customers call us and how they perceive our customer service, in order
3 to address customers' concerns and improve service to the customer through first call
4 resolution; Campaign Management, which would allow the Company to develop and
5 administer its own outbound customer surveys and call campaigns, rather than relying on
6 customer survey information provided by third parties; and eService and Mobile web site,
7 which in addition to improving the usability, functionality and performance of the
8 Company's eServices website, would allow customers to access a number of different
9 features of this website from their mobile devices. This will include features such as
10 Outage Reporting, Outage Maps and Status Updates, Emergency Alerts and
11 Notifications, Account Access and Edit Information, View/Pay Bill and Payment History,
12 Submit Meter Readings, Start/Cancel Service, and Find Payment Agents and Payment
13 Centers.

14 Other projects include Enterprise Compliance Solution, which would provide a
15 framework for compliance oversight and efficiency by automating the management,
16 measurement, remediation and reporting of regulatory and policy compliance activities;
17 and Master Data Management, which would leverage our prior investment in the SAP
18 Master Data Management module and Business Objects data service tools to implement a
19 master data management process that ensures data quality and data governance.

20 The Field Mobility Program integrates several individual projects in order to
21 maximize productivity for the Company and value for its customers. The Mission
22 Critical Voice Sustainment project will focus on maintaining the highly reliable voice
23 communication capabilities of the Company's aging 800 MHz system by replacing its

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1 most at-risk components, while working on transitioning data communications to public
2 carriers over the next several years. This “life-extension” project of the Company’s Land
3 Mobile Radio (“LMR”) system anticipates that over time, as the Public Cellular Carriers
4 (“PCC”s) continue to mature they will provide more complete coverage of our service
5 territory and may be an option to replace the Company’s LMR system. Alternatively, in
6 time it may become feasible to work with the State of Michigan and other “first
7 responder” organizations in utilizing a 700 MHz system. The 700 MHz frequency band
8 has been discussed at the federal level for establishment of a nationwide public safety
9 broadband network. Such a network would conceivably allow Consumers to join with
10 other utilities and governmental entities in a common network.

11 Q. Please describe the function of the Company’s LMR system.

12 A. The LMR system is the primary means of communication for field employees for both
13 day to day and emergency communications of both voice and data. While the LMR
14 system is augmented by the Company’s use of PCCs, it is designed to provide coverage
15 to any location within the Company’s service territory, and is maintained to a very high
16 degree of reliability (over 99.9%) to ensure communications for customer service and
17 during outage restoration.

18 Since 1948, Consumers Energy’s radio system has been a vital part of the
19 Company’s ability to provide safe and reliable energy to Michigan’s businesses and
20 residents. The system has matured from one fixed transmitter and a handful of mobile
21 radios to a homogeneous system covering 31,000 square miles, supporting 4,000
22 subscribers and nearly 70 million transmissions annually. Consumers Energy also

CHRISTOPHER J. VARVATOS
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1 utilizes public communications technologies such as cellular telephony and global
2 positioning systems in its generation, distribution, and administrative processes.

3 Q. Why is the Mission Critical Voice Sustainment project needed?

4 A. This project is needed to address physical equipment obsolescence of the aging
5 electronics in the LMR system. These electronics are now at least 18 years old, and
6 replacement parts are becoming increasingly difficult to obtain. The options facing the
7 Company are that either the electronics for the LMR system must be replaced with the
8 current generation of communications hardware, or the LMR system needs to be replaced
9 by the use of PCCs, or some combination thereof.

10 Q. Are there more projects in the Field Mobility program?

11 A. Yes. The Field Connectivity project will provide the technology, processes and training
12 to allow field personnel to be able to work wirelessly; the Field Mobile Applications
13 project will supplement the outdated Order Management and Routing (“OMAR”) system
14 with mobile applications which will speed up work order processing, reduce the number
15 of field trips and reduce field employees’ “wait” or unproductive time; the Field Devices
16 and Hardware project provides for replacement of field devices on a predetermined
17 schedule to avoid downtime from older, unreliable hardware, reduce hardware
18 maintenance costs that increase over time, minimize total cost of ownership and provide
19 the capacity to run newer, more resource-intensive applications.

20 Q. Please describe some of the other Software Application projects the Company plans to
21 fund in 2012 through the end of the test year.

22 A. Other projects include the Call Center Infrastructure Refresh project, which entails a
23 comprehensive replacement of the key components of the Company’s five call centers.

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1 The equipment to be replaced will be at the end of its expected life in 2014, and over the
2 years it has become technologically obsolete. Completing this project will ensure that the
3 Company's call centers continue to be available to take customers' calls on a day-to-day
4 basis, and are able to accept and respond to the significant call volume increases during
5 storms and emergency situations.

6 A project that will aid overall employee productivity is Sharepoint Document
7 Management, which will provide employees with the tools to more easily manage, and
8 more rapidly locate and access documents throughout their lifecycle. This will provide
9 employees with a common repository for documents, which will facilitate collaboration
10 and enhance efficiency.

11 **ASSET MANAGEMENT**

12 Q. Please describe the Asset Management capital expenditures.

13 A. Asset Management capital expenditures include the annual capital investments required
14 to provide the Company with secure and reliable computing infrastructure. A summary
15 of Asset Management costs from 2011 through 2014 is included as Exhibit A-68 (CJV-5)
16 Asset Management Capital. To ensure the operation, availability, reliability, and
17 functionality of the computing infrastructure for business continuity, the BTS department
18 conducts asset management programs for voice, data and wireless networks, servers,
19 multi-function printers, desktop computers, laptop computers, and field devices. The
20 programs are designed to minimize costs by replacing assets that are at the end of their
21 useful life before significant repair costs or business impacting outages of technology
22 systems are incurred. The reliability and functionality of this equipment is critical to the

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1 Company's work force in completing day-to-day responsibilities and in responding to
2 emergency situations.

3 Q. Are any projects funded under Asset Management?

4 A. Yes. One of the larger projects is the Dark Fiber East Expansion project. This is a
5 project that will build a fiber optic ring to provide improved bandwidth and reliability to
6 the east side of the Consumers Energy service territory. Recently a fiber optic ring was
7 placed into service on the west side of the State, and this ring included two of the
8 Company's five Customer Call Centers. The Dark Fiber Expansion project will connect
9 the final three Customer Call Centers at Flint, Saginaw, and Royal Oak, and will also
10 bring in the Karn/Weadock plant along with the service centers at Flint and Livonia. This
11 project is expected to provide all the bandwidth needed for the foreseeable future, while
12 greatly improving video conferencing and security camera transmission capabilities from
13 these sites.

14 **MAJOR COMPUTING INFRASTRUCTURE PROJECTS**

15 Q. Why are capital expenditures shown for the 800 MHz project in 2011, while no capital
16 expenditures are shown for this project in the years 2012 and 2013?

17 A. In 2011 the 800 MHz project was still classified as a Major Computing Infrastructure
18 project. A lower level of capital expenditures is forecast for the 800 MHz project in
19 2012, 2013, and 2014, and as such it no longer qualifies as a Major Computing
20 Infrastructure project. In addition, the 800 MHz project has been renamed as the Mission
21 Critical Voice Sustainment project

22 Q. Why has the forecast for this project been reduced?

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1 A. The reason that capital expenditures will be lower in 2012, 2013, and 2014 is that the
2 Company plans to pilot the use of PCCs for field data communications. The original plan
3 for this project had been to replace the aging electronics used in this system to ensure
4 continued reliability and performance into the future. In recent years the PCC industry
5 has begun to address the reliability and performance issues it had experienced in the past,
6 potentially making the PCCs a viable alternative to our current LMR system for data
7 communications.

8 Q. Does this conclude your testimony?

9 A. Yes, it does.

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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

REBUTTAL TESTIMONY

OF

CHRISTOPHER J. VARVATOS

ON BEHALF OF

CONSUMERS ENERGY COMPANY

March 2013

CHRISTOPHER J. VARVATOS
REBUTTAL TESTIMONY

1 Q. Please state your name and business address.

2 A. Christopher J. Varvatos, One Energy Plaza, Jackson, Michigan.

3 Q. Are you the same Christopher J. Varvatos that provided direct testimony in this
4 proceeding?

5 A. I am.

6 Q. What is the purpose of your rebuttal testimony?

7 A. I will respond to the testimony and exhibits submitted by the Attorney General in this case
8 concerning Business Technology Solutions (“BTS”) operation and maintenance (“O&M”)
9 expense and capital expenditures. Specifically, I will address Attorney General witness
10 Sebastian Coppola’s proposed reductions in BTS O&M and capital expenditures for the
11 test year.

12 Q. Are you sponsoring any exhibits with your testimony?

13 A. Yes, I am sponsoring the following exhibit:

14 Exhibit A-82 (CJV-6) Website Log-Ins and eBill Customers

15 Q. Was this exhibit prepared by you or under your direction?

16 A. Yes, it was.

17 Q. By what amount is Mr. Coppola proposing to reduce BTS O&M in the test year?

18 A. Mr. Coppola recommends reducing BTS O&M by \$2,400,000 in the test year on page 22
19 of his testimony. Mr. Coppola based his recommendation on his conclusion “that the
20 Company will realize at least a 10% cost efficiency in 2013” over 2011 in labor and
21 contracted services costs.

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1 Q. Do you agree?

2 A. No. In my testimony I explained that there were certain benefits we expected from
3 transitioning our operations and support costs to a managed services contractor, but an
4 immediate reduction in our labor costs was not one of them. On page 10 of my testimony
5 I explained how Consumers Energy Company (“Consumers Energy” or the “Company”)
6 is using its Employee Development and Sourcing Initiative as a method for controlling
7 costs. With this project Consumers Energy will be moving employees from system
8 maintenance roles into roles that are focused on project design and build. The system
9 maintenance work that had been traditionally performed by Company employees within
10 BTS will now be performed by contractors. This shift in workload will begin in 2012, and
11 over time is expected to increase capacity to meet current and future demand. Business
12 value will be added by lowering the overall cost of maintenance for existing technologies,
13 which would support the incremental maintenance costs associated with additional
14 technology investments.

15 Q. Were costs expected to increase as a result of the transition of operations and support work
16 to a managed services contractor?

17 A. Yes. During this transition, costs will be higher as Company employees work with the
18 contractors to prepare them for the operational support work and as they develop skills to
19 perform their new responsibilities. In time the Company does expect efficiencies from the
20 use of HCL Technologies (“HCL”) to perform operations and support work, while
21 Company employees focus on new project development work. However, as new projects
22 are implemented, BTS will incur additional labor costs to support the new applications.

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1 These additional labor costs will offset some of the efficiencies gained by employing
2 HCL.

3 Q. Is there any other reason why BTS O&M should not be reduced?

4 A. Yes. On pages 8 and 9 of my testimony I explained that the BTS department uses
5 benchmarking information to compare its costs to industry averages to ensure its O&M
6 expenses are reasonable. I reported that a number of the measures reported by Gartner,
7 Inc. in its IT Key Metrics Data 2012 indicate that BTS's costs are lower than Gartner's
8 utility average.

9 Q. What is your conclusion regarding the BTS O&M reduction Mr. Coppola has proposed?

10 A. My conclusion is that the transition of operations and support work over to the managed
11 services contractor HCL will in time bring efficiencies which will help offset the cost of
12 supporting new initiatives. However, the transition to managed services, which began in
13 February of 2012 for some services and in May of 2012 for other services, has not yet
14 reached the point at which HCL's costs will begin to decline. Analysis of the base
15 contracts with HCL suggest their costs will begin to decline for the current technology
16 supported in 2014. However, new change requests are being approved with HCL and
17 these changes will add new costs that will offset reductions to the base contract. In
18 addition, benchmarking information indicates that BTS's O&M expenses are lower than
19 their utility averages. Accordingly, my conclusion is that funding for BTS O&M should
20 be approved at the requested levels.

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1 Q. Mr. Coppola states on page 49 of his testimony that the eService and Mobile Website
2 project “is of marginal value and in fact has a negative Net Present Value.” Mr. Coppola
3 then recommends the Commission remove the \$1.4M of capital for this project from the
4 Company’s proposed 2013 rate base amount. Do you agree with Mr. Coppola’s
5 recommendation?

6 A. No. The eService and Mobile website will make significant improvements to the
7 Company’s website, and provide our customers with a new and more convenient method
8 for communicating with the Company. As I stated in my testimony on page 14, the
9 eService and Mobile web site will improve the usability, functionality, and performance of
10 the Company’s eServices website, and will permit customers to access a number of
11 different features of this website from their mobile devices. This will include features
12 such as Outage Reporting, Outage Maps and Status Updates, Emergency Alerts and
13 Notifications, Account Access and Edit Information, View/Pay Bill and Payment History,
14 Submit Meter Readings, Start/Cancel Service, and Find Payment Agents and Payment
15 Centers. Although the Company has performed no specific estimates on how many
16 customers will use the system in each of the first five years after implementation, it has
17 kept records of log-ins to its website and of the number of customers using eBill by year.
18 This information is presented Exhibit A-82 (CJV-6). This exhibit illustrates the steady
19 growth in the number of customers participating in eBill, as well as the more than 50%
20 increase in the average number of log-ins to the Company’s website over the last
21 two years. The Company justified this project based upon its analysis of its JD Power
22 results regarding where it was falling short of “best in class” utilities in providing this type
23 of functionality.

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1 Q. What is your conclusion regarding the eService and Mobile Website project?

2 A. The eService and Mobile Website is a valuable project that will improve the functionality
3 and usability of the Company's website, making it easier for customers to complete
4 transactions with the Company online. It will also provide our customers access from
5 their mobile devices to a number of transactions that are important to our customers. The
6 information we have gathered from JD Power tells us our customers' expectations of us as
7 a Company are changing and this project will address a number of those expectations.
8 Funding for this project should be allowed at the level requested.

9 Q. Mr. Coppola notes five separate projects with negative Net Present Value ("NPV") on
10 pages 49 through 50 of his testimony. Mr. Coppola recommends that \$2.9 million and
11 \$8.5 million for 2012 and 2013, respectively, be removed from the calculation of the 2013
12 proposed rate base amount. The projects listed were Campaign Management, Enterprise
13 Compliance Solution, Mission Critical Voice Sustainment, Field Connectivity project, and
14 Field Device and Hardware project. Do you agree with Mr. Coppola's recommendation?

15 A. No I do not. NPV is only one of the scores Consumers Energy uses to evaluate projects,
16 and project scores are only one of the ways projects are evaluated. On pages 10 through
17 12 of my testimony I explained the process by which the Company decides which projects
18 will be implemented. Financial analysis is only part of the process by which potential
19 projects are evaluated.

20 Q. Does the Campaign Management project currently have a negative NPV?

21 A. No. While the information previously provided to Mr. Coppola did indicate a negative
22 NPV for the Campaign Management project at that time, a more recent analysis shows a
23 positive NPV for this project. The current NPV analysis is based on a lower overall cost

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1 of the project. It also includes project benefits, such as a reduction in bad debt expense
2 from being able to send targeted messages through the dunning process.

3 Q. What is your conclusion regarding the Campaign Management project?

4 A. Campaign Management will help the Company manage customer interactions, marketing
5 campaigns, and the dunning process for residential and business customers. It will help
6 the Company communicate the right message to the right customer at the right time, and
7 help support achievement of the JD Power customer satisfaction breakthrough goals. It
8 has a positive NPV with a strong focus on improving customer satisfaction with the
9 Company. Funding for this project should be approved at the requested level. Campaign
10 Management is an example of why NPV is not the only factor determining whether we
11 move forward with a project.

12 Q. Is Mr. Coppola correct in recommending that the Enterprise Compliance Solution project
13 funding should not be approved?

14 A. No. The current analysis for the Enterprise Compliance Solution project shows an
15 improved NPV figure, however, the NPV figure is still negative. The Company's ability
16 to sustain healthy compliance programs is challenged due to the increased volume and
17 complexity of compliance requirements, coupled with antiquated systems and manual
18 processes with minimal integration across the enterprise for managing compliance
19 responsibilities. The Company, particularly in the areas of physical security and electric
20 reliability, has seen significant growth in the volume and complexity of requirements over
21 the past five years. The Company anticipates additional growth over the next five to
22 ten years, particularly in the areas of cyber security, electric reliability, gas code, and
23 environmental. By implementing the Enterprise Compliance Solution within the project

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1 timeline the Company expects to reduce the risks and impacts associated with
2 noncompliance with the continued goal of ensuring safe and reliable service to our
3 customer base.

4 Q. What is your conclusion regarding the Enterprise Compliance Solution project?

5 A. My conclusion is that this is a project that will help the Company manage and meet its
6 compliance requirements now and well into the future, and funding for this project should
7 be approved at the requested amount.

8 Q. Is Mr. Coppola correct in recommending disallowance of the funding for the Mission
9 Critical Voice Sustainment project?

10 A. No. The current NPV analysis for the Mission Critical Voice Sustainment project now
11 shows a positive NPV, whereas the NPV provided earlier to Mr. Coppola indicated a
12 negative NPV. The original NPV analysis had been to refresh or replace the Company's
13 800 MHz Land Mobile Radio ("LMR") system at a significant capital investment cost.
14 This project has been re-scoped to focus on sustainment of the Company's mission critical
15 voice capabilities of the 800 MHz system through methodical investments in
16 functionally-equivalent equipment over the next several years. The capital investment
17 needed for the re-scoped project is much lower than the original project, and that is why
18 this project now has a positive NPV.

19 Q. What is your conclusion regarding the Mission Critical Voice Sustainment project?

20 A. As I stated in my testimony, this project is needed to address physical equipment
21 obsolescence of the aging electronics in the LMR system. These electronics are now at
22 least 18 years old and replacement parts are becoming increasingly difficult to obtain. The
23 LMR system is the primary means of communication for field employees for both

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1 day-to-day and emergency communications of both voice and data. The Mission Critical
2 Voice Sustainment project provides a cost-effective solution to the problem of the aging
3 electronics that are the foundation of the 800MHz or LMR system. My recommendation
4 is that funding for this project should be approved.

5 Q. Is Mr. Coppola correct in recommending that the Field Connectivity project funding
6 should not be approved?

7 A. No. The current NPV analysis for the Field Connectivity project now shows a positive
8 NPV. The current NPV analysis includes the benefits of this project, while the previous
9 NPV analysis did not.

10 Q. Why is it important for the Company to proceed with this project at this time?

11 A. This project provides the foundation for a mobile workforce by provisioning the field
12 workers to work wirelessly. This project improves productivity and customer satisfaction
13 by providing field employees faster and better ways to effectively communicate, quicker
14 access to safety and work method information, reduction in travel time and expenses, and
15 reliable transmission of data utilizing a public carrier network which frees up bandwidth
16 for voice communication on our private LMR system. This project is necessary to enable
17 the benefits of the Mission Critical Voice Sustainment project, and to deliver the
18 foundation on which the Field Mobile Applications and Field Devices and Hardware
19 projects will build.

20 Q. What is your conclusion regarding the Field Connectivity project?

21 A. This project is key to providing wireless capability to the field workforce and will enable
22 the full range of benefits of the Mission Critical Voice Sustainment, Field Mobile

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1 Applications and Field Devices and Hardware projects to be achieved. Funding for this
2 project should be approved at the requested level.

3 Q. Is Mr. Coppola correct in recommending that funding for the Field Devices and Hardware
4 project be disallowed?

5 A. No. The Field Devices and Hardware project provides for replacement of field devices on
6 a predetermined schedule to avoid downtime from older, unreliable hardware, reduce
7 hardware maintenance costs that increase over time, minimize total cost of ownership and
8 provide the capacity to run newer, more resource-intensive applications. This project
9 works in conjunction with the Field Mobile Applications project to ensure that the field
10 devices are optimized to work with the new solutions. To deliver full value to customer
11 service and to efficiency efforts, the field devices need to be replaced along with the
12 applications that they support.

13 Q. What is your conclusion regarding this project?

14 A. The Field Devices and Hardware project is critical to ensuring the reliability and
15 improving the functionality of the field devices used by the Company's field workforce.
16 Funding for this project should be approved at the requested level. This is another
17 example of why NPV is not the only determinant of whether we move forward with a
18 project.

19 Q. Mr. Coppola describes the Strategic Initiatives category of projects on page 50 of his
20 testimony and recommends that funding for these initiatives be removed from the 2013
21 forecasted rate base. Do you agree with Mr. Coppola's recommendation?

22 A. No I do not. The Strategic Initiative projects consist of technology investments that
23 provide the foundation for future business capabilities resulting in customer value,

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1 employee productivity, safety and security, and other operational benefits. The projects
2 include base, enterprise-level technology platform, hardware and software investments
3 that will be used across multiple projects and business areas. Examples of such projects
4 include the base investments in Windows configuration management software and high
5 performance analytics tools. It is important that the Company continually make strategic
6 investments in its technology platforms to leverage the capabilities and avoid technical
7 obsolescence.

8 Q. Can you cite an example of a project in this category?

9 A. Yes. I will cite three examples. First, this category includes such projects as the SAP
10 HANA project, which is the next generation in memory computing appliance that creates
11 a real-time database platform that will support real-time applications and analytics. This
12 is the future state for SAP Analytics, Reporting, and Data Management. The purpose of
13 the SAP HANA (High Performance Analytics) project is to address the growing volume
14 of data, and the increasing time that it takes to query and analyze customer, financial, and
15 work management data. It will provide the technology platform to increase the
16 availability and response of the Company's reporting systems, used for driving business
17 decisions, Company performance and productivity.

18 A second project included in this category is the Windows 7 project. The
19 Company currently uses Windows XP, which is the primary operating system used on PC
20 workstations, laptops, and field devices across the Company. Windows XP is scheduled
21 to go out of service support in April 2014. The Windows 7 project will replace Windows
22 XP with Windows 7 and will address the hardware and software related issues associated
23 with a change in operating systems.

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1 Q. Why is this project necessary?

2 A. This project is needed to avoid technology obsolescence of the software used by
3 employees of the Company. Software applications are continually being revised, updated
4 and improved, and as new operating systems are developed, software designers code their
5 applications specifically to run under the new operating systems. To minimize the
6 problems experienced by employees who use these software packages, as well as the
7 associated support costs, and to ensure a smoother transition from one operating system to
8 the next, the Company has chosen to replace the Windows XP operating system with the
9 next generation of Windows operating systems.

10 My third example is the project called High Availability Environment for SAP.
11 The High Availability Environment for SAP project will define mid-to-long term efforts
12 needed to reduce SAP production outages and improve system reliability. It will address
13 the identification, prioritization, and implementation of corrective actions. Potential
14 outcomes could include the deployment of technical monitoring tools, SAP enhancement
15 redesign and revised processes to manage changes to SAP resulting in an SAP
16 environment that is more stable, reliable, and available.

17 Q. What is your conclusion regarding the Strategic Initiative projects?

18 A. The Strategic Initiative projects provide the foundation that supports the computing
19 technology of the Company. These are projects that will lead the Company from its
20 present state of technology into the future and help it avoid technical obsolescence.
21 Funding for these projects should be approved.

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1 Q. Mr. Coppola notes on page 51, of his testimony that “Company witness
2 Lauren Youngdahl stated that subsequent to filing this rate case, the Company decided to
3 extend the delivery of the initial smart meter billing release from December 2012 to the
4 second quarter of 2013. It appears that this delay will also affect the timeline of some of
5 the other BTS software systems under development. As such, the capital expenditures
6 planned for 2012 for Smart Grid Enablement also will likely be delayed into 2013.
7 Therefore, I would estimate that at least half, or \$2.4 million of the 2012 expenditures will
8 be pushed into 2014, past the test year period.” Do you agree with Mr. Coppola?

9 A. No I do not. There is no basis for Mr. Coppola's estimation that half of 2012's
10 expenditures would be delayed into 2014. The actual expenditures for Smart Grid
11 Enablement in 2012 were \$7.8 million in total, \$4.9M for electric, and the entire amount
12 expended should be allowed into the rate base. Furthermore, any delays in release dates in
13 Smart Grid do not affect the BTS Smart Grid Enablement projects. Smart Grid
14 Enablement projects must be completed and be available for use before Smart Grid is able
15 schedule delivery of a new service.

16 Q. Does this conclude your rebuttal testimony?

17 A. Yes, it does.

1 JUDGE CUMMINS: As usual, I will withhold
2 ruling on the six proposed exhibits until the completion
3 of cross-examination.

4 Mr. Moody, you indicated have you some
5 questions for this witness.

6 MR. MOODY: Thank you, your Honor.

7 CROSS-EXAMINATION

8 BY MR. MOODY:

9 Q Good morning, Mr. Varvatos.

10 A Good morning.

11 Q Looking at your rebuttal testimony, starting at page 1
12 and looking in to page 2 and 3, in those pages you
13 respond to Sebastian Coppola's testimony about reducing
14 O&M expenses by 2.4 million. Do you see that testimony?

15 A Yes.

16 Q In that testimony you state that the contract with -- I
17 think it's HCL, which is I guess HCL Technologies, you
18 state that that contract that started in -- is that 2012;
19 is that correct? Or 2010? I'm sorry. Let me get that
20 right. The contract with HCL started in 2002; is that
21 correct?

22 A I'm sorry, did you ask 2002?

23 Q Yes.

24 A No.

25 Q When was that contract started?

1 A I don't have the exact date of the contract, but it's
2 been within the last two years.

3 Q And you said the efficiencies from -- or maybe you can
4 explain a little bit again: What is the Company
5 intending to accomplish with the contract with HCL?

6 A The contract with HCL is as a managed services provider,
7 which makes them responsible for the operational support
8 of our business applications and our infrastructure.

9 Q All right. Now, I think in your testimony you state that
10 the efficiencies from this HCL contract won't start until
11 2014; is that correct?

12 A That's when we believe the efficiencies will begin with
13 the current contract applications and infrastructure.

14 Q Even though the contract was started two years prior, why
15 would you not see any efficiencies until 2014?

16 A The earlier years, 2012 is a transitional year, so we
17 have employees who are actually working with HCL to
18 transition their knowledge into the specifics of our
19 application, so we have increased labor during this
20 transitional period. And as HCL supports those
21 applications, we expect they will gain efficiencies by
22 2014 in the amount of labor to support.

23 Q Is that a -- how do you come up with the 12-month
24 transition? Is that a set number or could it be six
25 months?

1 A We believe it's a minimum of 12 months. It's normal for
2 these types of contracts with managed services providers
3 to have a transitional period with increased costs.

4 Q Now, if the contract was put together two years ago, then
5 is there another year missing there? Why wouldn't the
6 efficiencies be in 2013?

7 A I stated that I didn't have the exact contract date. But
8 we transitioned our applications beginning in 2012.

9 Q O.K. What is your 12-month transition analysis based on?
10 History or past practice?

11 A It's based on industry experience for managed services
12 providers, and also our projection that there would be a
13 transitional period knowing that there was specific
14 knowledge that needed to be transferred by employees to
15 our provider.

16 Q That can't be accomplished in less than 12 months?

17 A With the complexity of our technology environment, we
18 projected 12 months.

19 Q Have you done managed contracts before in this, similar
20 to this, with Consumers Energy?

21 A Not on this scale. We have had other contracts to
22 support other technologies with other vendors in the
23 past, but not for a large set of applications within a
24 structure like we do with HCL.

25 Q Now, the people that HCL are bringing in, are these

1 professional people that know the area for this managed
2 services?

3 A Yes. HCL brought professionals who understand the base
4 technologies that we support in our Company, such as the
5 SAP systems and our infrastructures that we support.

6 Q So are they that different than the systems that
7 Consumers Energy is using, are they so far different than
8 the other ones that are out there that these people need
9 12 months to transition to it?

10 A There are always complexities that are unique to our
11 industry and our sets of applications that require a
12 transitional period for the knowledge transfer.

13 Q Is there a -- Did you guys consider any other managed
14 service contract, you know, professionals, that could do
15 it in a shorter timeframe, this transition, or was HCL
16 the only one that you worked with?

17 A The contract was a result of a bid process, of following
18 standard bid procedures, and we would expect this level
19 of transition with any new provider or managed services
20 in our Company.

21 Q So when you bid for this, sent out the proposals or
22 request for proposals, is that a question that you put in
23 there, what the transition timeframe might be when they
24 provide a bid to you, or to Consumers Energy?

25 A I don't have the request for proposal or bid documents

1 with me to answer that.

2 Q Do you know what, or do you have an idea what the
3 efficiencies or savings might be in 2014 as a result of
4 this HCL contract?

5 A We don't have an exact projection of the efficiencies and
6 savings.

7 Q Looking at your rebuttal testimony page 3, near the
8 bottom you state that -- I think it's the third sentence
9 up, starting with however. Are there going to be
10 additional costs that are going to offset the benefits in
11 2014 as a result of this HCL contract?

12 A Yes. We expect there will be, in that timeframe there
13 will we will be installing new infrastructure and new
14 software applications that will also require maintenance
15 labor and will add to the contract with HCL. So while we
16 expect the efficiency with the existing application and
17 infrastructure, we will be adding new applications and
18 infrastructure which will have increased costs that
19 offset that.

20 Q So as a total, there really isn't any benefit then to the
21 contract with HCL until the future, is that the summary
22 of that?

23 A No, I would not say that. Regardless of the provider
24 supporting our system, we would have increased costs for
25 software and technology and infrastructure with new

1 applications and technology, regardless of the provider.

2 Q Looking at page 4 of the rebuttal, when you talk about
3 the eService and Mobile website, can you explain what
4 these computer applications do?

5 A The eServices and website applications for Consumers
6 Energy allow customers to access features for, related to
7 billing and payments, meter readings, outage reporting,
8 and status updates. The Mobile website would enable some
9 of these applications on mobile platforms, and the
10 eServices portion would improve our eServices system for
11 our customers by adding additional functionality.

12 Q So there already is some services out there for the
13 customers to do billing and check on reporting an outage
14 and stuff; is that correct?

15 A There is some applications on the website, but there are
16 no mobile applications for billing support today for our
17 customers.

18 Q So Mobile application, that means like your phone or --

19 A Smart phones, tablets, yes.

20 Q All right. But you can do it on a laptop computer then
21 right now?

22 A If you access our regular website and eServices.

23 Q Isn't it true that the Company doesn't know how many
24 customers will actually use these new applications?

25 A Well, I'm glad you asked that because Mr. Coppola in his

1 testimony stated that the Company stated we had no idea.
2 And that is not the case. We have some idea based on our
3 current usage of our website and eServices on-line bill
4 payment.

5 Q Now, your on-line bill payment, is that the same as the
6 eService?

7 A On-line bill payment is part of our eServices
8 functionality. And we've had a 23 percent increase over
9 the last two years in our eBill customer usage.

10 Q So is your on-line, I think that's your Exhibit A-82, is
11 that correct, where you talk about that?

12 A Yes.

13 Q This is Website Log-Ins and eBill Customers, is that the
14 heading of that exhibit?

15 A Yes.

16 Q So now this log-in to the eService website, that's not
17 the Mobile website; is that correct?

18 A Since we don't have the Mobile website ready for services
19 billing and payment, it would not be mobile.

20 Q So you wouldn't know then as to, I guess the Mobile
21 website, the Company doesn't know how many customers
22 would use this application; is that correct?

23 A Specifically mobile, we have had experience with our
24 outage reporting capability that we do have mobile, and
25 also on our website. And when we implemented the mobile

1 version of that, we had a high usage rate and movement
2 toward the mobile capability. So we would expect that
3 with the billing functions, we would have the same
4 migration to the mobile platform as well as the use of
5 our on-line website.

6 Q So where do you have the mobile applications right now?

7 A We have a mobile application for outage reporting and
8 estimated restoration times, which I do have metrics for
9 here.

10 Q So you didn't include any of that analysis in your
11 rebuttal?

12 A No, because the question was specifically related to
13 eServices and our website in general.

14 Q So in response to Sebastian Coppola's testimony regarding
15 the mobile website and the fact that you should maybe cut
16 the funding to that, you didn't provide any of that
17 analysis about other mobile applications in your rebuttal
18 testimony. Am I correct?

19 A Not the mobile, correct.

20 Q So you do have some studies regarding the mobile
21 applications in the Company, the usage?

22 A We keep statistics of usage of our websites, including
23 the functions that we do have enabled mobilely.

24 Q Again none of that, you don't have a reference to any of
25 those analyses of any studies in this testimony anywhere,

1 do you?

2 A I do not.

3 Q So in this analysis, say on 82 where you have numbers
4 about how many customers will use this website log-in,
5 the numbers that are presented here in A-82 are customers
6 have used the Company's log-in eBill services; is that
7 correct?

8 A The number of log-ins per month in eServices and the
9 number of eBill customers, yes.

10 Q And do you have any -- I guess you wouldn't know then if
11 the people that use this service are the same people that
12 would use the mobile website?

13 A We would only predict that based on the way we have seen
14 our customers adopt the mobile functions that we have in
15 other applications like the outage recording. We believe
16 these statistics are an indicator of demand that
17 customers have for transacting on-line business with our
18 company.

19 Q So if you didn't spend the money on the eService and
20 Mobile website, customers would still have access to what
21 you talked about here on A-82?

22 A They would have access to our current eServices
23 functions.

24 Q Turning to page 5 of your rebuttal testimony, and looking
25 at the bottom there, you talk about the Campaign

1 Management Project. Are you there?

2 A Yes.

3 Q You state there that Sebastian Coppola's testimony
4 indicated a negative NPV and now you're stating that a
5 more recent analysis shows positive NPV for this project;
6 is that correct?

7 A Yes.

8 Q Do you provide that analysis here in the rebuttal
9 testimony?

10 A No, it is not in the rebuttal.

11 Q Did you provide a copy of the updated NPV calculation to
12 the Attorney General in response to discovery or
13 anything?

14 A We provided the current or the original business case
15 submission with the analyses with discovery.

16 Q But not the updated?

17 A But not the updated.

18 JUDGE CUMMINS: So Mr. Varvatos, what has
19 been disclosed was the negative one but not the positive
20 one; is that correct?

21 A Yes.

22 JUDGE CUMMINS: Thank you.

23 Q (By Mr. Moody): Similarly on page 6 of your rebuttal
24 testimony, talking about the Enterprise Compliance
25 Solution, do you see that testimony?

1 A Yes.

2 Q You talk about that the Enterprise Compliance Solution
3 project shows an improved NPV figure, but it's still
4 negative. Do you see that testimony here in the middle?

5 A Yes.

6 Q When you say improved NPV figure, is there an analysis
7 provided in the rebuttal to support the analysis of
8 improved NPV figure?

9 A A specific analysis is not included with the rebuttal.

10 Q Since the Attorney General filed their direct testimony
11 in February of this year stating that there was a -- you
12 have done a subsequent analysis that shows an improved
13 NPV figure, this Enterprise Compliance Solution?

14 A I'm sorry. Can you say it again?

15 Q Yes, I'm trying to get the timeframe. So since the
16 filing of the Attorney General's direct testimony in this
17 case, which I think is in February of this year, the
18 Company or you have done additional analysis on the
19 Enterprise Compliance Solution and have shown an improved
20 NPV figure; is that correct?

21 A I don't have the exact timing of the revised analysis.
22 But it is a normal part of our process as we develop the
23 business cases and the financial analysis and other
24 considerations in the planning phase, later on in the
25 project we will recalculate that based on what we learn

1 in the design and re-analysis of benefits and costs for
2 the improvement project. So at some point that was
3 revised. I don't have the exact date of when that was
4 revised.

5 Q It was after obviously your direct testimony, correct,
6 the improved analysis?

7 A It is after the analyses that correspond with the
8 planning numbers that we supplied with the project.

9 Q In your direct testimony? Just to make sure I got this
10 right.

11 A The financial analysis was provided as part of the
12 discovery request and not with the direct testimony.

13 Q So let's look at page 9 of your rebuttal testimony.
14 Actually, I'm sorry. Let me turn back again to page 7 of
15 your rebuttal. At page 7 of your rebuttal you talk about
16 Mission Critical Voice Sustainment project. Do you see
17 that?

18 A Yes.

19 Q Again you have a statement that the project now shows a
20 positive NPV. Is that analysis provided in rebuttal
21 testimony?

22 A The analysis is not included with rebuttal.

23 Q And again looking at page 8 of your rebuttal testimony,
24 dealing with the Field Connectivity project funding, do
25 you see that?

1 A Yes.

2 Q And similarly is the new positive NPV that you talk about
3 there, is that analysis in your rebuttal testimony?

4 A It was not included with the rebuttal.

5 Q At page 9 of your testimony, near the end there, I think
6 it's the second question and answer, you talk about there
7 at the bottom of that answer, this is another example why
8 NPV is not the only determinant of whether we move
9 forward with a project. Do you see that?

10 A Yes.

11 Q If it's -- if NPV is not the most important determinant,
12 why even do the analysis?

13 A I believe we say NPV is not the only determinant. And we
14 base our analyses on a number of factors in addition to
15 NPV. We use the NPV in the scoring, but management also
16 takes into account other factors such as the customer
17 requirements and other business requirements at that
18 time.

19 Q If the -- I guess if the project has a negative NPV, that
20 doesn't mean -- you're saying -- let me get that
21 statement, the question better to you.

22 So if the project had a negative NPV,
23 Consumers Energy might still do the project. Is that
24 what you're saying?

25 A Yes. There may be other factors that would require

1 Consumers Energy to undertake the project.

2 Q At page, turning back to page 7 of your rebuttal, you
3 state that at one point dealing with I think the Mission
4 Critical Voice Sustainment project, that the NPV is
5 better because the project requires less capital
6 investment. Do you see that?

7 A Yes.

8 Q Can you quantify how much less in capital investment
9 these projects add up to, or this project?

10 A I don't have the exact numbers with me, but it is
11 significant in that the original project involved a scope
12 of replacing our full 800 megahertz radio system. And
13 the Mission Critical Voice Sustainment project, it's
14 replacing critical components that would allow us to
15 sustain the voice capability for a five to ten year
16 period.

17 Q You don't provide those numbers of how much less capital
18 investment in your rebuttal?

19 A They're not included with the rebuttal.

20 Q I think with some of the other ones you talk about there
21 are less capital investments for some of these projects.
22 The numbers for that aren't in the rebuttal, are they?

23 A Specific numbers for the projects noted are not included
24 with the rebuttal.

25 MR. MOODY: O.K. That's all, your Honor.

1 JUDGE CUMMINS: Very well. Do any other
2 parties have questions of this witness? Any redirect,
3 Mr. McQuillan?

4 MR. McQUILLAN: May I have just a moment,
5 your Honor?

6 JUDGE CUMMINS: Sure. Let's go off the
7 record for a second.

8 (Brief in-place recess was taken.)

9 JUDGE CUMMINS: Let's go back on the
10 record. Any redirect for this witness, Mr. McQuillan?

11 MR. McQUILLAN: Yes, your Honor. Thank
12 you.

13 REDIRECT EXAMINATION

14 BY MR. McQUILLAN:

15 Q Mr. Varvatos, do you recall that the Attorney General
16 asked you some questions concerning rebuttal testimony
17 about various projects where you indicated there was a
18 continuing view of the present value in some of the
19 projects that improved?

20 A Yes, I recall.

21 Q Do you recall he asked whether you provided the details
22 and analysis of the present value analysis of those
23 projects with your rebuttal testimony?

24 A Yes, I recall.

25 Q I believe your answer was you had not provided it with

1 your rebuttal testimony?

2 A Correct.

3 Q Did you provide that level of detail and analysis for all
4 of these projects in your direct testimony?

5 A No, I did not.

6 Q How is that information provided to a party if they want
7 it?

8 A It's typically provided through discovery requests.

9 Q So when he says it wasn't provided with rebuttal, it also
10 wasn't provided with direct?

11 A Correct.

12 MR. McQUILLAN: That's the only questions
13 I have. Thank you.

14 JUDGE CUMMINS: Mr. Moody, does that
15 raise any questions for you?

16 MR. MOODY: No, actually. Thank you,
17 your Honor.

18 JUDGE CUMMINS: We have before us
19 Exhibits A-64, A-65, A-66, A-67, A-68, and A-82. Is
20 there any objection to the receipt of those exhibits?

21 Hearing none, those exhibits are received
22 into evidence. Mr. Varvatos, you may step down.

23 THE WITNESS: Thank you.

24 (The witness was excused.)

25 JUDGE CUMMINS: As I discussed just

1 briefly with a few of the parties off the record, it's
2 now quarter to 12:00. We have two witnesses left and it
3 appears that the Attorney General -- well, we may have
4 more after that, I'm not sure if we're binding in
5 testimony, but we have two witnesses that will be
6 cross-examined starting after lunch. My suggestion is we
7 go ahead and take our lunch break now. We would
8 reconvene at 1:00 o'clock. We have a relatively short
9 day because we weren't allowed to start before 10:30. So
10 if you could be back here at 1:00 o'clock, we'll
11 reconvene at that point in time.

12 Mr. McQuillan?

13 MR. McQUILLAN: Your Honor, just because
14 I don't know the logistics of restaurants in Ann Arbor
15 [sic] that well, could we go 1:15 maybe?

16 JUDGE CUMMINS: Let's do that. I'll give
17 you an hour and a half. We'll do 1:15 back here. I'm
18 assuming we're going to begin with Mr. Anderson; is that
19 correct?

20 MR. McQUILLAN: That is correct.

21 JUDGE CUMMINS: Very well. We're
22 adjourned until 1:15, at which time we will take up Mr.
23 Anderson.

24 Mr. Keskey?

25 MR. KESKEY: Your Honor, since I do not

1 have cross on the witnesses this afternoon, I am asking
2 to be excused for this afternoon.

3 JUDGE CUMMINS: That's fine with me. As
4 long as you're not having more fun than we're having, Mr.
5 Keskey, you're free to go.

6 MR. KESKEY: Thank you.

7 JUDGE CUMMINS: That being the case,
8 we're adjourned until quarter after 1:00. Thank you.

9 (At 11:45 a.m., the hearing recessed for lunch.)

10 - - -

1 pages of questions and answers?

2 A Yes.

3 Q Do you have a copy of that with you today?

4 A Yes, I do.

5 Q Do you have any corrections, changes, or modifications to
6 those answers?

7 A No, I do not.

8 Q If I were to ask you those questions today, would your
9 answers be the same?

10 A Yes.

11 Q Do you adopt that as your sworn direct testimony in this
12 cause?

13 A Yes, I do.

14 Q Did you cause in conjunction with your direct testimony
15 to be prepared exhibits which have been labeled for the
16 Court Reporter as A-12, A-13, A-14, and A-15?

17 A Yes.

18 Q Do you have a copy of those with you today?

19 A Yes.

20 Q Do you have any corrections, changes, or modifications to
21 any of the exhibits?

22 A No, I do not.

23 Q Are those the exhibits that are referenced in your direct
24 testimony?

25 A Yes, they are.

1 Q Did you also cause to be prepared rebuttal testimony
2 consisting of a cover page and 28 pages of questions and
3 answers?

4 A Yes.

5 Q Do you have a copy of that with you today?

6 A Yes.

7 Q Do you have any corrections, modifications, or changes to
8 the answers to those questions?

9 A No.

10 Q If I asked you those questions today would your answers
11 be the same?

12 A Yes.

13 Q Do you adopt that as your rebuttal testimony in this
14 cause?

15 A Yes.

16 Q In conjunction with your rebuttal testimony did you cause
17 to be prepared three exhibits which have been labeled for
18 the Court Reporter as A-73, A-74, and A-75?

19 A Yes.

20 Q Do you have a copy of those with you this afternoon?

21 A Yes.

22 Q Do you have any corrections, modifications, or changes to
23 those exhibits?

24 A No.

25 Q Are those exhibits that are referenced in your rebuttal

1 testimony?

2 A Yes.

3 MR. McQUILLAN: Thank you. Your Honor,
4 at this time we would request that the direct testimony
5 and rebuttal testimony of James Anderson be bound into
6 the record, the direct testimony consisting of a cover
7 page and 46 pages of questions and answers, the rebuttal
8 testimony consisting of a cover page and 28 pages of
9 question the answers. We move the admission of Exhibits
10 A-12, 13, 14, 15, and Exhibits A-73, A-74, and A-75, and
11 tender the witness for cross-examination.

12 JUDGE CUMMINS: Thank you, Mr. McQuillan.
13 Any objection to binding in the direct and rebuttal
14 testimony submitted by Mr. Anderson? Hearing none, the
15 testimony, both the direct and rebuttal, will be bound
16 into the record.

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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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

DIRECT TESTIMONY
OF
JAMES R. ANDERSON
ON BEHALF OF
CONSUMERS ENERGY COMPANY

September 2012

JAMES R. ANDERSON
DIRECT TESTIMONY

1 Q. Please state your name and business address.

2 A. James R. Anderson, 1945 W. Parnall Road, Jackson, Michigan.

3 Q. By who are you employed?

4 A. I am employed by Consumers Energy Company ("Consumers Energy" or the
5 "Company").

6 Q. What is your position with Consumers Energy?

7 A. I am the Executive Manager of Electric Asset Management for Consumers Energy. I
8 have previously held the following positions: Manager of Distribution Engineering and
9 Regulatory Services, Manager of Electric Network Services, Executive Manager of
10 Business Services, Manager of Electric System Control and Optimization and Electric
11 Field Manager. I have also held various other positions since joining Consumers Energy
12 in 1987.

13 Q. What are your responsibilities as Executive Manager of Electric Asset Management?

14 A. I am responsible for system planning, engineering, design and standards of the
15 Company's high voltage and low voltage electric distribution lines and substations.
16 Additionally, I am responsible for reliability, interconnection agreements, North
17 American Electric Reliability Corporation ("NERC") compliance, forestry/line clearing
18 operations and system control of the electric distribution system.

19 Q. Are you a member of any professional societies or trade associations?

20 A. I currently serve on the Power Delivery Committee of the Association of Edison
21 Illuminating Companies.

JAMES R. ANDERSON
DIRECT TESTIMONY

1 Q. What is your formal educational experience?

2 A. I graduated from Michigan Technological University with a Bachelor of Science degree
3 in Electrical Engineering in 1986.

4 Q. Have you previously testified before the Michigan Public Service Commission (“MPSC”
5 or the “Commission”)?

6 A. Yes, I previously testified in MPSC Case Nos. U-14347, U-16191 and U-16794.

7 Q. What is the purpose of your testimony?

8 A. The purpose of my testimony is to discuss electric distribution system performance and
9 the impact and benefit to customer service of improving its performance. In the section
10 entitled “ELECTRIC DISTRIBUTION PERFORMANCE DISCUSSION” which starts
11 on page 3, I discuss how customer satisfaction is impacted by service reliability,
12 identifying the major causes of customer outages and how outages affect common
13 industry metrics such as System Average Interruption Duration Index (“SAIDI”), System
14 Average Interruption Frequency Index (“SAIFI”), and Customer Average Interruption
15 Duration Index (“CAIDI”), which in turn directly impact several of the MPSC Service
16 Quality and Reliability Standards. Also, included in this section is a discussion of our
17 Business Plan Deployment. Additionally, in the sections entitled “ELECTRIC
18 DISTRIBUTION O&M EXPENSES” (starting on page 16) and “CAPITAL
19 EXPENDITURES” (starting on page 34), I will identify and support Electric
20 Distribution’s: 1) Operation and Maintenance (“O&M”) Expense; and 2) Capital
21 Expenditures necessary to meet an improved level of performance in these standards.
22 Finally, in the section entitled “CONCLUSION,” (starting on page 43) I summarize the

JAMES R. ANDERSON
DIRECT TESTIMONY

1 expected improvement results in the Service Quality and Reliability Standards and in
2 average customer outage minutes (SAIDI) that the requested funding should achieve.

3 Q. Are you sponsoring any exhibits?

4 A. Yes. I am sponsoring the following exhibits:

- 5 ▪ Exhibit A-12 (JRA-1) – Summary of Projected Electric & Common O&M
6 Expenses for the years 2011, 2012 and 2013
- 7 ▪ Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common
8 Capital Expenditures for the years 2011, 2012, 2013 and 2014
- 9 ▪ Exhibit A-14 (JRA-3) – Distribution Performance Standards Results for
10 Years 2007-2011
- 11 ▪ Exhibit A-15 (JRA-4) – Comparison of Electric Utility Distribution and
12 Customer Accounts/Service (excluding Uncollectables) O&M Cost per
13 Customer for Year 2010

14 Q. Were these exhibits prepared by you or under your supervision?

15 A. Yes.

16 **ELECTRIC DISTRIBUTION PERFORMANCE DISCUSSION**

17 Q. Does the level of spending on Electric Distribution that you will testify about provide a
18 benefit to customers?

19 A. Yes. There is a direct and measurable relationship between the level of investment made
20 and the reliability and quality of service experienced by customers. The purpose of any
21 distribution system is to safely deliver electrical energy from generators to end use
22 customers. The reliability of that distribution system is one of the more important factors
23 in determining the customers' satisfaction with electric service. The results of customer
24 satisfaction surveys the Company has done to measure customer attitudes/opinions, as
25 well as complaint data, support this conclusion. Based on customer survey data, there is

JAMES R. ANDERSON
DIRECT TESTIMONY

1 a drop-off in customer satisfaction when they have experienced three or more outages
2 with declining satisfaction for each additional outage beyond three outages.

3 The O&M and capital spending on the electric distribution system discussed in
4 my testimony addresses the principal factors determining the reliability of the electric
5 service experienced by customers such as frequency and length of outages, and the load
6 serving capacity of the system. The Company manages its overall level of capital
7 investments and O&M expenses across the utility portfolio which can result in potential
8 spending fluctuations from year to year in the programs represented in my testimony.
9 For example, service restoration expenses are extremely difficult to predict, other than
10 very short term, as the level of expense is predominately driven from weather (i.e., storm
11 and heat) activities. Typically when the Company encounters service restoration
12 expenses which are higher or lower than expected for a point in time during the year,
13 adjustments are considered and sometimes made in other expense programs. While the
14 impact of changing capital investments and O&M expenses on reliability and system
15 capacity is not always immediate, greater or lesser program expenditures will inevitably
16 lead to greater or lesser service quality, with respect to reliability experienced by
17 customers. The amount of O&M funding requested as shown in Exhibit A-12 (JRA-1)
18 line 3 and the capital expenditure levels requested as shown in Exhibit A-13 (JRA-2)
19 line 8 reflect a level of spending that is projected to maintain electric distribution
20 reliability and provides a reasonable expectation of meeting the Commission's Service
21 Quality and Reliability standards.

JAMES R. ANDERSON
DIRECT TESTIMONY

1 Q. What are the top three causes of interruptions to Consumers Energy's electric customers?

2 A. Interruption statistics during 2007 through 2011 show that trees (22%), lightning/weather
3 (20%), and equipment failures (18%) are the top three causes of customer interruptions.

4 The most effective way to improve system performance to the benefit of customers is to
5 perform maintenance and upgrade the distribution infrastructure. The expenditures
6 discussed in my testimony will address the three most recurring interruption causes by
7 improving system conditions and configuration leading to a reduction in the number of
8 interruptions.

9 Q. What methodology are you using to project the level of capital expenditures and O&M
10 expenses required to improve reliability?

11 A. Consumers Energy uses its Decision Analysis Reliability Evaluation ("DARE") model to
12 predict system reliability performance and allocate funding for various electric
13 distribution reliability programs. The model includes 28 various reliability programs
14 such as line clearing, replacement of obsolete insulators and upgrading lightning
15 protection. These programs use historical outage frequency and duration, equipment
16 deterioration rates, repair costs, customer impact along with several other parameters to
17 model the life cycle of each program and predict its relationship to system reliability.

18 Given the unpredictable nature of weather and other challenges facing the
19 delivery of electric power, no computer model can predict future system reliability
20 performance with one hundred percent certainty; however, the DARE model has proven
21 to be an effective tool to predict system performance through an unbiased evaluation of
22 reliability programs and allocation of funding for our O&M and capital programs.

JAMES R. ANDERSON
DIRECT TESTIMONY

1 Q. How has the DARE model been used in the past to predict system performance?

2 A. In the early 1990s the Company set a goal to improve system reliability. The objective
3 was to reduce the SAIDI excluding storms to a targeted level. The DARE model was
4 developed as a result of this mission and became the Company's primary electric
5 distribution reliability analysis tool. Through utilization of the DARE model the
6 Company was successful in achieving the SAIDI target in 1995-1998 and is why it
7 considers the DARE model to be an effective tool. In its final rate Order of November 4,
8 2010, in MPSC Case No. U-16191 (pages 32-33), the Commission recognized that
9 consistent use of the DARE model provides results that reflect trends over time.

10 Q. How is system reliability measured by the Company?

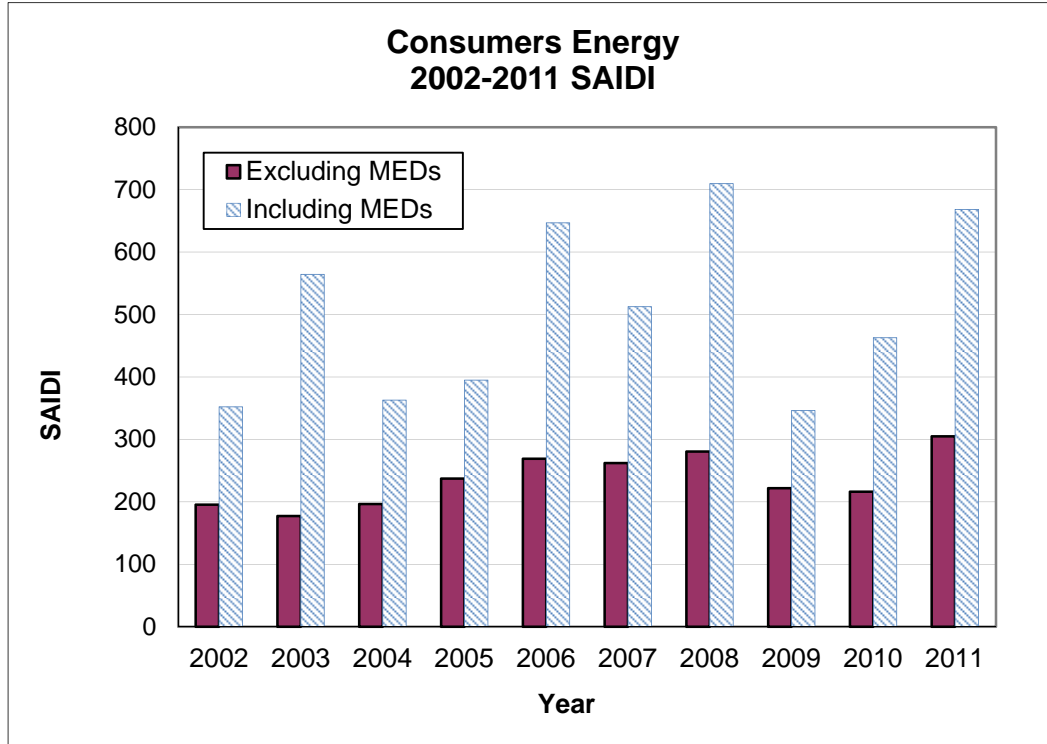
11 A. A primary measurement of system reliability used by Consumers Energy (and other
12 utilities) to evaluate system reliability is SAIDI. SAIDI is a measurement of the average
13 duration of outages experienced by all customers per year. Additionally, the Company
14 monitors its system reliability performance through utilization of the Commission's
15 Service Quality and Reliability Standards established in MPSC Case No. U-12270.

16 Q. What has been the reliability performance of the Consumers Energy distribution system?

17 A. Chart 1 shows Consumers Energy's SAIDI results, excluding "Major Event Day"
18 ("MED") storms, of 305 minutes in 2011, with a slightly increasing trend between 2007
19 and 2011. In 2011 there were a number of significant weather challenges that did not rise
20 to the level of MEDs which affected the 2011 results. The methodology of determining
21 the level of storm activity to exclude in developing this chart is based on the Institute of
22 Electrical and Electronics Engineers ("IEEE") Guide for Electric Power Distribution
23 Reliability Indices (1366-2003).

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DIRECT TESTIMONY

CHART 1 – SAIDI PERFORMANCE (2002-2011)



1 Q. What are the components of the SAIDI metric?

2 A. The SAIDI performance metric is comprised of 2 components – it is the mathematical
3 product of frequency of outages measured by the SAIFI driven by system condition,
4 system configuration, and system challenges (i.e., weather); and duration (restoration
5 time) measured by the CAIDI. Duration is driven by system condition, the number of
6 interruptions, resource availability, and restoration management practices.

$$7 \quad \text{SAIDI} = \text{SAIFI} * \text{CAIDI}$$

8 Q. Is there a correlation between SAIDI performance and the Commission's Service Quality
9 and Reliability Standards for Electric Distribution Systems?

10 A. Yes there is. The 2 components of SAIDI (SAIFI and CAIDI) have a strong correlation
11 with 2 of the Commission's key Service Quality and Reliability Standards that were
12 adopted in MPSC Case No. U-12270 and influence customer satisfaction. These

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1 2 standards are the Repetitive Outage performance standard (less than 5% of customers
2 experiencing 5 or more interruptions in a year) which by definition includes storms, and
3 the Normal Conditions restoration performance standard (more than 90% of customers
4 restored in 8 hours during normal conditions) as defined by the Commission in those
5 standards.

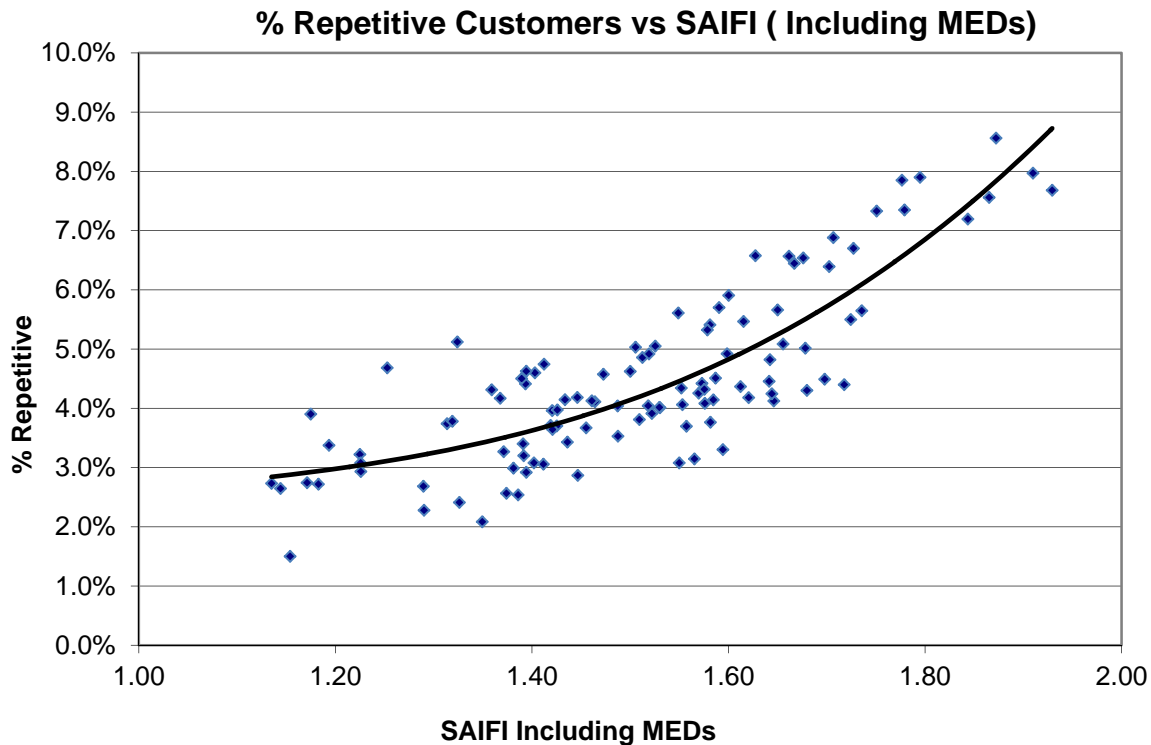
6 Q. What Commission performance standard is impacted by SAIFI?

7 A. There is a correlation between SAIFI (including storms) and the Commission's
8 Repetitive Outage performance standard which by definition includes storms. As outage
9 frequency (SAIFI) increases, the number of customers that experience 5 or more outages
10 (repetitive outages) in a given year also increases. While in any given year the
11 relationship between SAIFI and the Commission's Repetitive Outage performance
12 standard can vary, historical data illustrates there is a strong statistical correlation
13 between SAIFI and the Repetitive Outage performance standard. As SAIFI (including
14 MEDs) reaches a level greater than 1.62, it becomes more likely that the Repetitive
15 Outage performance standard (less than 5% of customers experiencing 5 or more
16 interruptions in a year) will not be met. Consumers Energy's 2004-2011 year end SAIFI
17 performance including MEDs has ranged from 1.23 to 1.72 and the Repetitive Outage
18 year end performance has ranged from 3.1% to 6.6%. Chart 2 illustrates the relationship
19 between SAIFI and Repetitive Outage performance at a 50% confidence level. The data
20 in this chart represents SAIFI and Repetitive outage calculated on a rolling 12-month
21 basis for each month from January 2004 through December 2011. A diligent and focused
22 effort on SAIFI performance must be maintained to meet the Commission's Repetitive
23 Outage performance standard which ultimately benefits customers. A deteriorating

JAMES R. ANDERSON
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1 SAIFI will increase the probability that more than 5% of customers would experience
2 5 or more outages per year. As the number of outages increase, customer satisfaction
3 declines.

CHART 2 - % Repetitive vs. SAIFI



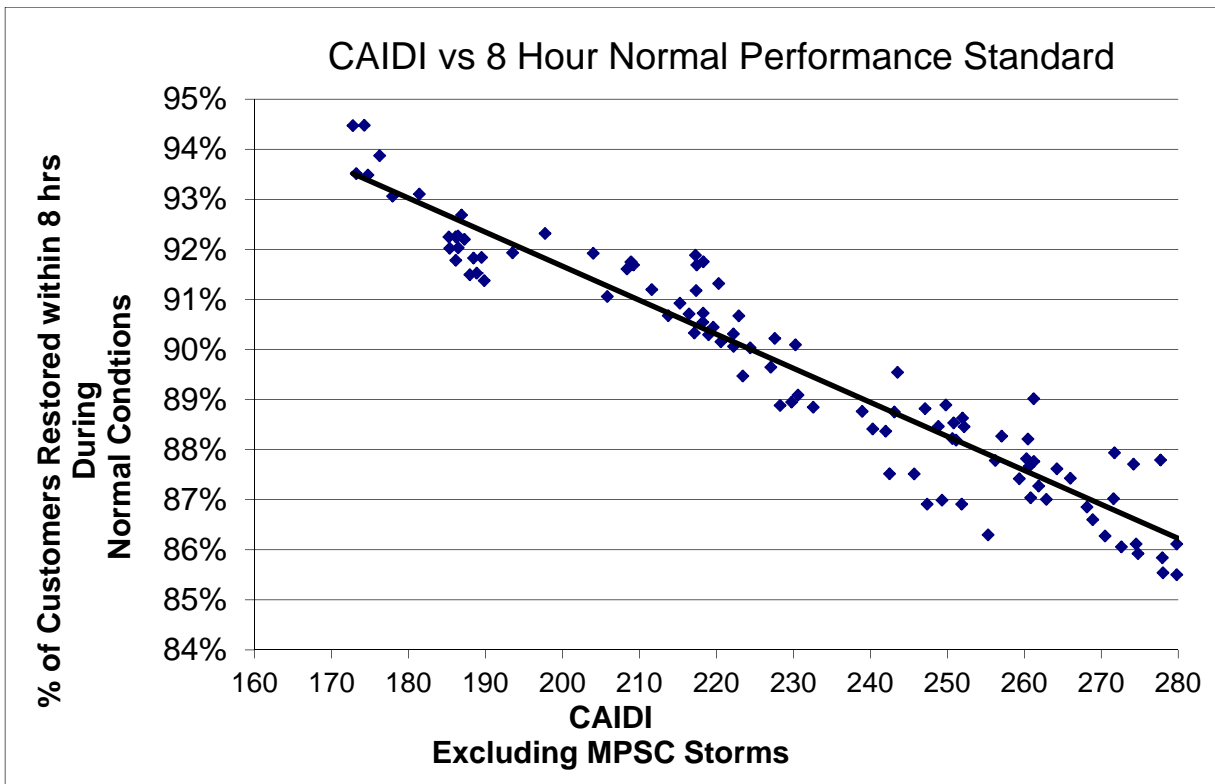
4 Q. What Commission performance standard is impacted by CAIDI?

5 A. There is a strong correlation between CAIDI (for outages as defined as normal based on
6 the Commission's Service Quality and Reliability Standards) and the Commission's
7 Normal Conditions restoration in 8 hours performance standard. While in any given year
8 the relationship between CAIDI and the Commission's Normal Conditions restoration in
9 8 hours performance standard can vary, over time there is a strong statistical correlation
10 between CAIDI and the Commission's Normal Conditions restoration standard. As
11 CAIDI reaches a level of about 225 minutes (excluding Commission's Service Quality
12 and Reliability Standards defined storms), it becomes more likely that the Normal

JAMES R. ANDERSON
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1 Conditions restoration performance standard (greater than 90% restored in 8 hours) will
 2 not be met. Consumers Energy’s 2004-2011 year end CAIDI performance (excluding
 3 Commission’s Service Quality and Reliability Standards defined storms) has ranged from
 4 209 minutes to 283 minutes and the Normal Conditions restoration performance has
 5 ranged from 91.7% to 85.5%. Chart 3 illustrates the relationship between CAIDI and
 6 Normal Conditions restoration showing the relationship at a 50% confidence level. The
 7 data in this chart represents CAIDI and percent of customers restored within 8 hours
 8 during normal conditions calculated on a rolling 12-month basis for each month from
 9 January 2004 through December 2011. A deteriorating CAIDI increases the probability
 10 that less than 90% of customers would be restored within 8 hours during normal
 11 conditions.

CHART 3 - CAIDI vs. % Customers Restored in 8 hours (Normal)



JAMES R. ANDERSON
DIRECT TESTIMONY

1 Q. Please explain why the Company's SAIDI performance was significantly higher in 2011
2 as compared to 2009 and 2010?

3 A. As stated previously, SAIDI is the product of SAIFI and CAIDI. The 2011 SAIFI
4 excluding MED conditions increased by 29.5% and 30.8% when compared to 2009 and
5 2010, respectively. A key variable that drove these SAIFI increases directly correlates to
6 the volume of challenges which our electric distribution system endured in 2011 as
7 opposed to 2009 and 2010. Chart 4 below summarizes the number of severe weather
8 warnings (thunderstorms and tornadoes), icing observation hours, and lightning strikes
9 for the Lower Peninsula of Michigan based on information derived from the National
10 Weather Service and United States Precision Lightning Network data. Simply put, when
11 compared to recent history, 2011 was a year in which our electric distribution system was
12 most significantly challenged.

CHART 4 – Weather Event Summary, MEDs excluded

Weather Event Summary, Major Event Days Excluded					
			Observed Event Count		
			Warnings Issued	Icing Observation Hours	Lightning Strikes
Year					
2009			91	80	309,000
2010			230	68	938,000
2011			324	180	1,094,000
			Percent Increase		
Year	v.	Year	Warnings	Icing	Lightning
2011	v.	2009	256%	165%	254%
2011	v.	2010	41%	125%	17%
2011	v.	Ave(2009,2010)	102%	143%	75%

13 CAIDI (excluding MEDs) also increased in 2011; however, it did not degrade in the same
14 proportion as SAIFI due to significant actions taken by the Company to counteract the

JAMES R. ANDERSON
DIRECT TESTIMONY

1 tremendous increase in customer service restoration workload attributable to SAIFI. In
2 2011, Consumers Energy implemented several tactics designed to improve its response to
3 customer outages. Restoration pre-planning prior to expected weather events and regular
4 weekend pre-planning were instituted to proactively establish response approaches based
5 on anticipated weather impacts. The Company frequently considered and scheduled
6 weekend work assignments to perform necessary work and to have line crews available
7 for outage response during these non-standard work hours. Office and line crew
8 resources were mobilized in some cases prior to weather events in areas expected to be
9 impacted. Mobilization of additional contractor line crews (in state and out of state) was
10 initiated earlier, both during and prior to weather events, to increase resource availability
11 in the initial phase of restoration. These tactics allowed the Company to overcome the
12 large customer service restoration workload (SAIFI) in 2011 relative to 2009 and 2010
13 resulting in a relatively smaller average duration increase (CAIDI) for these same years.
14 Despite these efforts, the overall CAIDI and SAIFI results combined to drive up SAIDI
15 significantly.

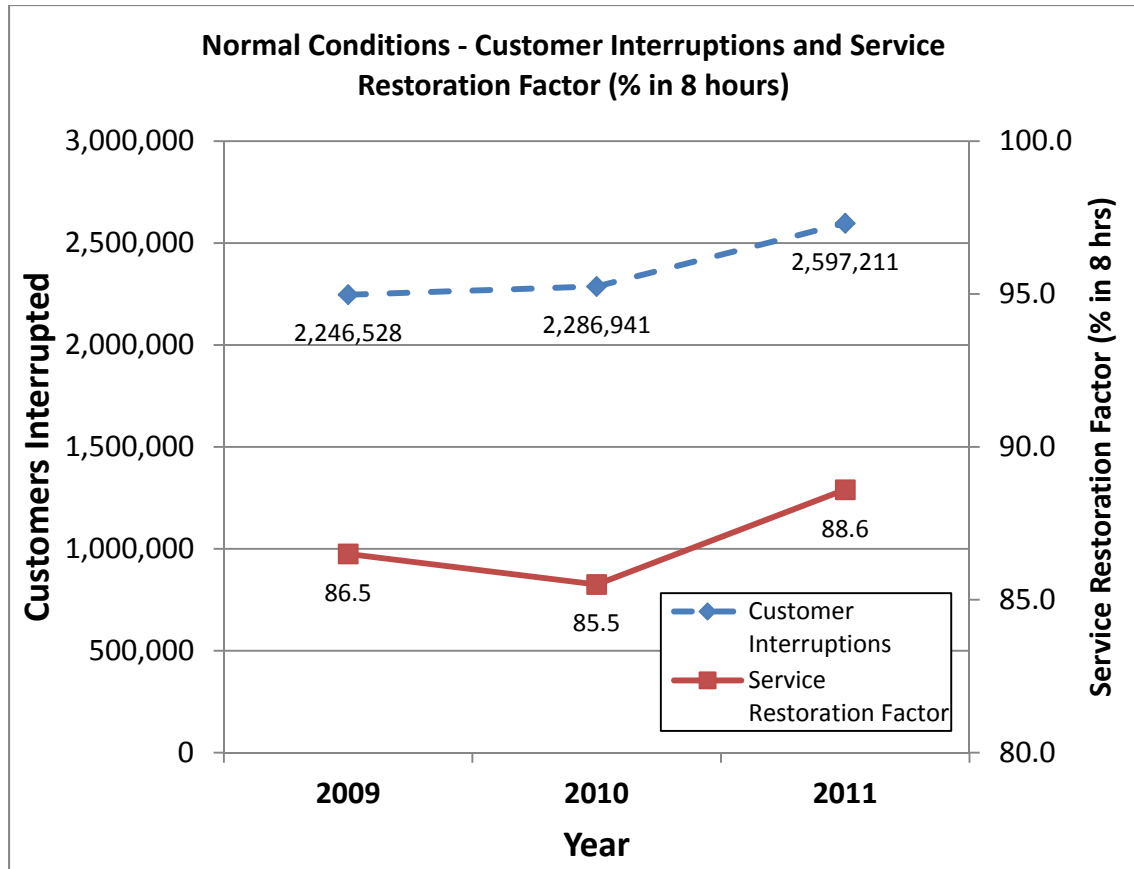
16 Q. How did the tactics stated above impact the Company's performance relative to the
17 Service Quality and Reliability Standards and to the benefit of its customers?

18 A. Chart 5 represents the number of customers that required service restoration in years
19 2009, 2010, and 2011 during Normal Conditions as defined by the Service Quality and
20 Reliability Standards and represented by the dashed line in Chart 5. Clearly, there was an
21 increase in the number of customers requiring service restoration in 2011 as a result of
22 the weather event challenges described earlier. In spite of this increase, the Company
23 posted an overall improvement in its Normal Conditions restoration factor in 2011 as

JAMES R. ANDERSON
DIRECT TESTIMONY

1 represented by the solid line in Chart 5. Restoring more customers sooner is clearly a
2 benefit to customers. The actions the Company took in 2011 relative to pro-active
3 service restoration supports the Company's commitment of continually striving to meet
4 or exceed the Service Quality and Reliability Standards.

CHART 5 – Customer Interruptions and Normal Conditions Service Restoration Factor



5 Q. Are there additional reasons to focus on SAIDI performance?

6 A. Yes. The importance of SAIDI performance was emphasized in a September 1, 2009,
7 report addressed to the Michigan State Legislature submitted on behalf of the MPSC in
8 accordance with Section 10p of 2008 PA 286, MCL 460.10p (Act 286) where it was
9 stated: *“In light of the research Staff conducted, the Commission finds that Consumers*
10 *Energy and Detroit Edison at this time should include SAIDI, SAIFI, and CAIDI*

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1 *reporting (with and without major events) on a rolling five year average in a new docket*
2 *that will be opened by the Commission. These indices have been proven to show the*
3 *reliability of electricity in a utility's power system and are useful to the Commission in*
4 *identifying utility performance trends for each specific utility on a going forward basis.*
5 *The intent of the information is not to benchmark the utilities nationwide or within the*
6 *state, but rather to measure performance levels of each utility against its own historical*
7 *data.”* Additionally, in accordance with the September 15, 2009, Order in MPSC Case
8 No. U-16066, the Company is providing annual performance information related to
9 SAIFI, CAIDI, and SAIDI with and without major events, on a rolling 5-year average
10 basis, using the industry standard IEEE method of calculation.

11 Q. What business process is utilized to maximize customer value through operational
12 performance improvements?

13 A. A key process is Business Plan Deployment (“BPD”) which is a disciplined approach
14 being utilized to support the Company’s vision to be a more customer centric
15 organization and provide a methodology to continuously improve customer service levels
16 and operational performance. BPD is a strategic planning/strategic management
17 methodology that has found broad use in the automotive, manufacturing, as well as
18 service industries. It is a discipline that begins with a focus on the organization’s vision
19 and strategic goals, and aligns the priorities, plans, resources, metrics, accountabilities,
20 and controls to effectively achieve the stated goals. BPD is a management system that
21 recognizes the value of combining a well-articulated strategic intent to deliver customer
22 value with empowered employees. It is a dynamic process where employees engage and
23 make adjustments to plans as necessary to achieve the targeted results.

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1 Q. How did you determine your priorities in delivering customer value?

2 A. Customer value is driven through listening to customers and adapting to their needs.
3 Customer insights were gained from industry wide surveys, targeted research, and direct
4 customer feedback. In general, customers want the Company to: 1) provide safe and
5 dependable service; 2) provide information and offer options in the services provided;
6 and 3) make and meet commitments in performing work for them in a cost effective
7 manner. These have become part of the Company's strategic priorities.

8 Q. How is customer value tied to operational performance in developing the Company's
9 business plans?

10 A. Key service levels and operation performance objectives are developed for the strategic
11 priorities that directly or indirectly tie to customer value. This establishes which
12 improvement priorities need to be targeted to meet the objectives and ultimately deliver
13 on customer value. With full implementation of BPD around a vision and strategy
14 focused on the customer, employees can better understand the translation of that vision
15 and strategic goals into their day-to-day activities and priorities. This will enable a
16 culture of personal ownership for actions and decisions that deliver excellent customer
17 service and support the success of the Company. It will also result in quality customer
18 experiences via seamless, well executed processes that have aligned objectives and goals
19 and across functional organizations.

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1 **ELECTRIC DISTRIBUTION O&M EXPENSES**

2 Q. Please describe Exhibit A-12 (JRA-1) – Summary of Projected Electric & Common
3 O&M Expenses for the years 2011, 2012, and 2013.

4 A. Exhibit A-12 (JRA-1) summarizes the Company's total 2011, 2012, and 2013 electric
5 and common O&M expense for Consumers Energy Electric Distribution. Specifically:

- 6 • Column (a) identifies each O&M expense program description.
- 7 • Column (b) identifies the 2011 Electric Distribution O&M expense as
8 \$265,063,000.
- 9 • Column (c) identifies the 2012 Electric Distribution O&M expense as
10 \$232,545,000.
- 11 • Column (d) identifies the Test Year O&M expense as \$233,661,000 for
12 2013.
- 13 • Column (e) provides the source reference for each category listed above.

14 The Electric Distribution O&M Expenses are shown in 2 program categories.
15 Line 1 of Exhibit A-12 (JRA-1) covers the Electric Division Expenses. The activities and
16 responsibilities of the 3 major organizations included in the Electric Division Expenses
17 are described later in my testimony. Line 2 of Exhibit A-12 (JRA-1) covers the expenses
18 associated with Statutory Low Income Programs for which funding has been eliminated
19 in the test year 2013 as explained later in my testimony.

20 Q. Please explain the source of the 2011 actual O&M expenses for Electric Distribution.

21 A. The 2011 actual O&M expenses for Electric Distribution were taken from Consumers
22 Energy's internal reporting records.

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1 Q. Do the 2011 actual O&M expenses for the Electric Division as shown on line 1 of
2 Exhibit A-12 (JRA-1) – Summary of Projected Electric & Common O&M Expenses for
3 the years 2011, 2012, and 2013 represent continuing functions and activities?

4 A. Yes, we project that the functions and activities represented by the Electric Division
5 expenses for the test year 2013 will be similar and consistent with the functions and
6 activities that were performed in 2011 with a reduction for service restoration activities
7 and with adjustments upward for pole inspections, NERC Standard PRC-005-02
8 expenses, and line clearing.

9 Q. Please explain the derivation of the Electric Division O&M expense requirements as
10 shown on line 1 of Exhibit A-12 (JRA-1) – Summary of Projected Electric & Common
11 O&M Expenses for the years 2011, 2012, and 2013.

12 A. The Company has projected Electric Division Test Year O&M expenses to meet
13 customer service and safety requirements. The 2011 expenses of \$238,526,000 shown in
14 line 1, column (b) are actual expenses. These 2011 O&M expenses reflect a reasonable
15 and appropriate level of expense for these operations. The 2012 O&M expenses of
16 \$219,047,000 shown in line 1, column (c) are the projected amounts. The 2013 O&M
17 expenses of \$233,661,000 shown in line 1, column (d) were derived utilizing 2011
18 expenses as a reference point from which forward looking adjustments were made
19 predominantly for a reduction in service restoration expenses, expanded distribution pole
20 inspection, the expanded NERC PRC-005-2 reliability standard, and expanded line
21 clearing as explained more fully below. Customer service and reliability will be
22 enhanced by the increased spending for distribution pole inspections, the NERC
23 PRC-005-2 reliability standard and line clearing. The net result of all adjustments

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1 discussed above is a \$4,865,000 reduction of projected Electric Division Expenses in
2 2013 compared to 2011.

3 Q. On what basis are Consumers Energy's Electric Division Expenses concluded to be
4 reasonable and appropriate?

5 A. As shown in Exhibit A-15 (JRA-4), using publicly available utility expense and customer
6 data from Federal Energy Regulatory Commission ("FERC") Form 1 and other similar
7 regulatory filings for 2010, which is the most recent data available, the Company ranks
8 near the top of the second quartile on a least O&M cost per customer basis when
9 compared to other utilities; that is, nearly 75% of the other utilities have higher O&M
10 costs per customer. This analysis was performed by dividing the summation of
11 Distribution Operations, Distribution Maintenance, Customer Account (less uncollectible
12 accounts) and Customer Service, and Information Expenses by the summation of
13 residential, commercial, and industrial customers.

14 Q. Please explain the \$4,865,000 reduction between the Company's 2013 Total Electric
15 Division Expenses as compared to 2011 as shown on line 1, Exhibit A-12 (JRA-1) –
16 Summary of Projected Electric & Common O&M Expenses for the years 2011, 2012, and
17 2013?

18 A. The \$4,865,000 reduction shown on line 1, Exhibit A-12 (JRA-1) consists of
19 approximately \$16,000,000 reduction in service restoration activities, offset by an
20 upward adjustment of \$1,500,000 in increased pole inspections, \$2,000,000 in NERC
21 reliability standard PRC-005-2, and \$7,812,000 in line clearing.

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1 Q. How is safety and customer service reliability enhanced by reducing service restoration
2 by \$16,000,000?

3 A. Safety and customer service reliability is our primary focus. This reduction does not
4 reduce our commitment to our customers. It is simply recognition that 2011 was a very
5 challenging weather year which drove service restoration expenses higher than in a
6 typical year as described on page 11 of my testimony. The Company does not anticipate
7 that the 2011 weather experience will be repeated in 2013. Therefore the Company is
8 projecting a lower service restoration expense level in 2013 than what was experienced in
9 2011.

10 Q. How is safety and customer service reliability enhanced by expanding the pole inspection
11 program by \$1,500,000?

12 A. The increased funding for pole inspections allows the Company to move to a 12-year
13 inspection cycle resulting in approximately 140,000 low voltage distribution system
14 ("LVD") and 7,500 high voltage distribution ("HVD") poles being inspected in 2013.
15 The inspection program allows the Company to enhance customer service reliability and
16 safety by identifying poles that could potentially fail and create an outage.

17 Q. Please explain the requirements associated with the NERC PRC-005-2 reliability
18 standard and why additional funding is necessary.

19 A. The NERC PRC-005-2 standard is a proposed protection system maintenance and testing
20 standard that would replace the existing PRC-005-1 standard. The proposed standard is
21 currently working its way through the NERC standards development process and
22 Consumers Energy believes it is likely to go into effect sometime in early 2013. The
23 standard in its current form is dramatically more prescriptive in: 1) its definition of

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1 protection system components that require inspection/testing; 2) what the inspection
2 and/or testing needs to consist of; and 3) the intervals for inspection/testing. The new
3 standard would result in many more components being inspected and/or tested, much
4 more rigorous documentation requirements, and significantly more complex field-testing
5 than the current standard requires. Given the dramatic changes being proposed,
6 Consumers Energy needs to begin its efforts to prepare for the new standard in late 2012
7 ahead of the final adoption of PRC-005-2. Funding is necessary to support the additional
8 technical and field resources needed to implement and sustain the expanded protection
9 system maintenance and testing program that would comply with the new standard.

10 Q. How is safety and customer service reliability enhanced by increasing line clearing by
11 \$7,812,000?

12 A. Trees are the number one cause of customer service interruptions on the Company's
13 electric distribution system. The Company is requesting an additional \$7,812,000 in line
14 clearing expenses bringing the total amount to \$53,000,000 for the line clearing program
15 which supports clearing approximately 7,900 miles. This compares to 6,452 miles at the
16 expense of \$45,188,000 in 2011 and a plan of approximately 5,800 miles at the planned
17 expense of \$40,896,000 in 2012. This requested funding will result in line clearing of
18 approximately 25% of the HVD system, and approximately 12.5% of the primary LVD
19 system annually (or an effective clearing cycle of approximately 8 years).

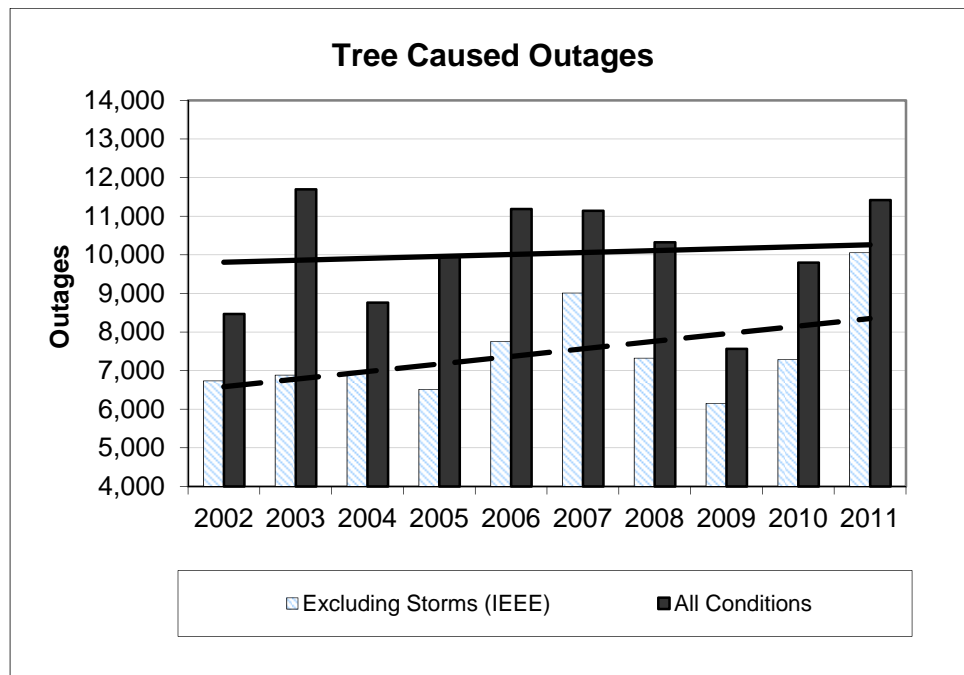
20 Q. Please describe the customer benefits of additional line clearing O&M?

21 A. The Consumers Energy distribution system consists of approximately 54,000 miles of
22 overhead primary LVD lines, 4,500 miles of overhead 46 kV lines, and 425 miles of
23 overhead radial 138 kV lines. The 46 kV and 138 kV radial lines are considered HVD

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1 lines. For the 5-year period 2007-2011, trees on average caused approximately 22% of
2 customer interruptions. The longer term trend in tree caused outages is still increasing.
3 (see Chart 6 below)

CHART 6 – Tree Caused Outages



4 Our Decision Analysis Modeling indicates that the most cost effective way to improve
5 system conditions and reliability is by reducing tree caused interruptions through an
6 increased level of line clearing.

7 Q. What is the basis for the \$53,000,000 requested level of line clearing funding?

8 A. The proposed funding level in this rate case of \$53,000,000 represents the next step of a
9 longer term plan to achieve a level of line clearing spending which optimizes the overall
10 benefit to customers, through improved reliability performance as measured by SAIDI,
11 while maintaining a reasonable unit cost per mile trimmed. Ideally, Consumers Energy
12 needs to eventually achieve an optimal line clearing program of approximately 14%
13 clearing per year for the LVD system (or an effective clearing cycle of approximately

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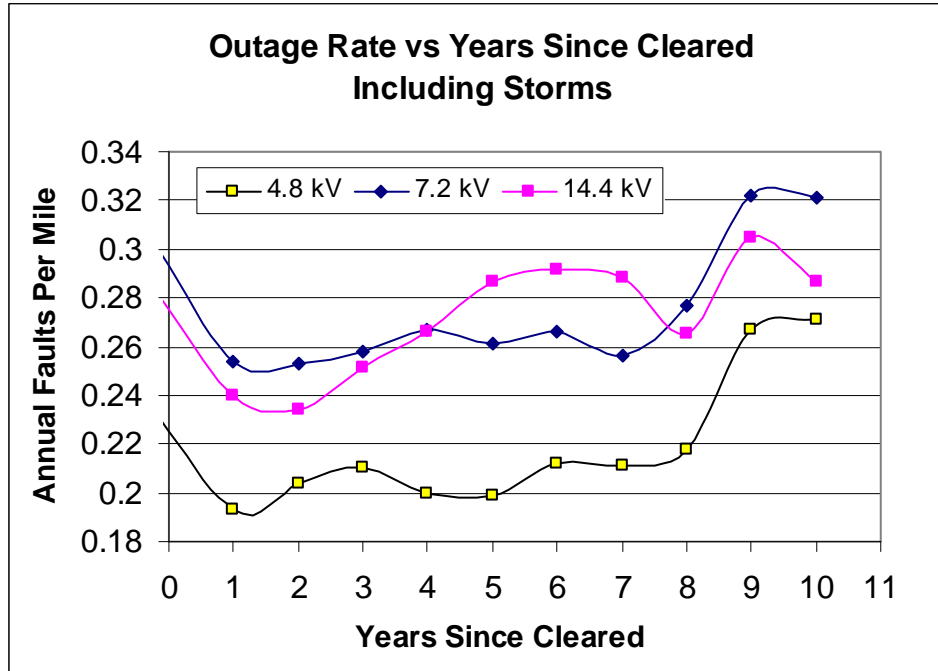
1 7 years) and a 25% clearing per year for the HVD system which would cost
2 approximately \$59,000,000. As part of its plan to achieve that optimal level of line
3 clearing, Consumers Energy would increase the line clearing program in a way that can
4 be effectively managed over the course of time. This approach lessens the immediate
5 cost impact on our customers while providing increasingly better outage performance.

6 Q. Please explain more about a 14% LVD line clearing program.

7 A. The 14% clearing program (approximately 7-year effective cycle) for the LVD system
8 represents the optimal clearing interval for the different system voltages and respective
9 system miles for those voltages. In general, the risk of tree caused outages on LVD
10 circuits increases significantly as the time since last cleared increases, particularly during
11 storms. LVD circuits operating at 14.4 kV begin to show dramatic increases in tree
12 related outages after 3 years since last cleared with 7.2 kV and 4.8 kV circuits showing
13 increases after 7 and 8 years, respectively, since last cleared. Chart 7 shows the historical
14 relationship between outage rates and years since last trimmed for primary voltages of
15 4.8 kV, 7.2 kV, and 14.4 kV.

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CHART 7 -Outage Rates vs. Years Since Cleared



1 The DARE model predicts that a 14% clearing program (approximately 7-year
2 effective cycle) will result in a reduction in system SAIDI minutes of approximately
3 13 minutes when compared to system SAIDI minute results based on continuing a 7%
4 program (the historical 10-year average). The requested 12.5% clearing program
5 (approximately 8-year effective cycle) at the \$53,000,000 funding level would result in a
6 reduction in system SAIDI minutes of approximately 9 minutes when compared to
7 system SAIDI minute results based on continuing a 7% program (the historical 10-year
8 average).

9 Q. Please provide the approximate equivalency of percent LVD clearing program levels with
10 effective clearing cycle time in years.

11 A. See CHART 8 below.

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CHART 8 - % System Cleared vs. Effective Cycle Time	
% LVD System Cleared	Effective Clearing Cycle
25%	4 Year
14%	7 Year
12.5%	8 Year
10%	10 Year
7%	14 Year

1 Q. How does the Company's line clearing program compare to other utilities?

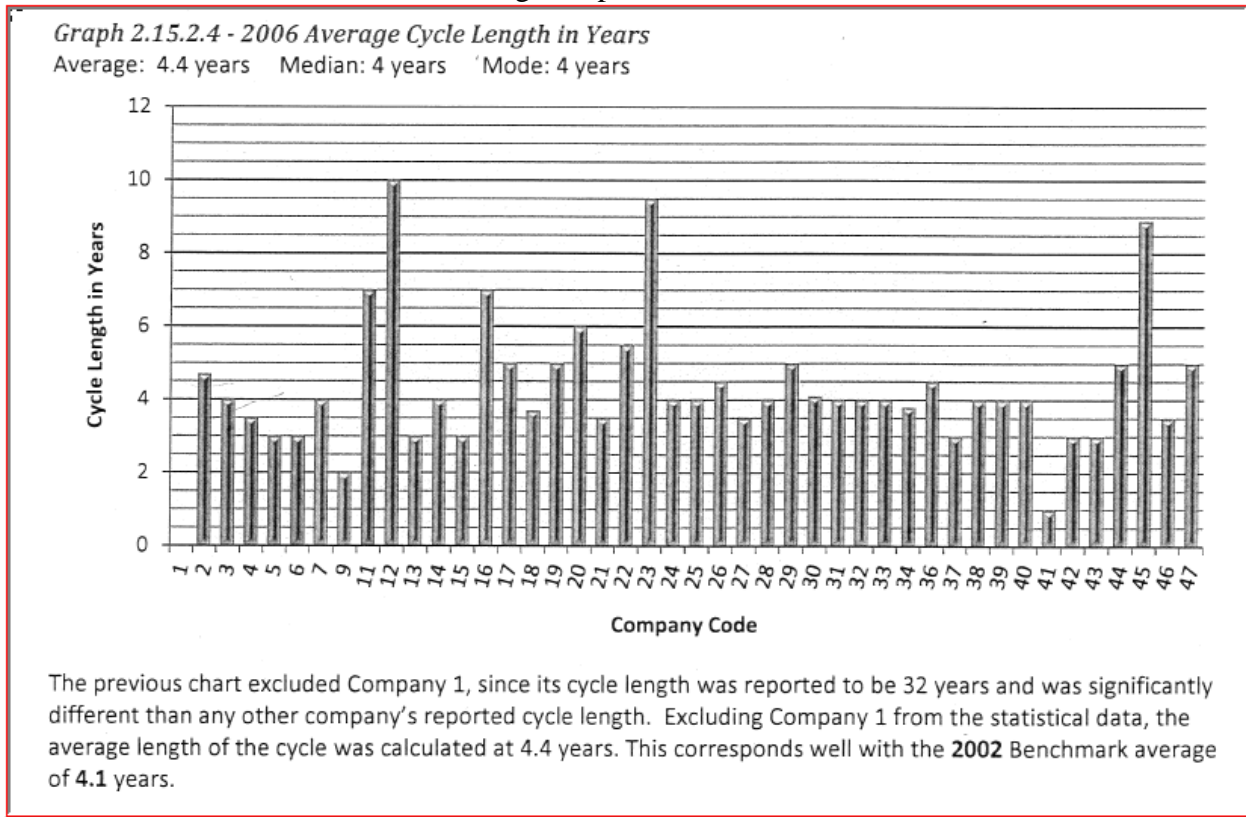
2 A. Consumers Energy's actual annual average LVD miles cleared over the last 10 years
3 (2002-2011) has been approximately 3,700 miles which is about 7% of the system
4 annually or about a 14-year effective clearing cycle. This includes approximately
5 5,400 LVD miles cleared in 2006, 2009, and 2011 which were significant exceptions over
6 this period. This overall clearing rate has allowed vegetation conditions to continually
7 grow at a rate faster than miles cleared annually, resulting in approximately 40% of the
8 LVD system that has not been cleared in 10 or more years. This level of clearing is in
9 contrast to the average 4-year effective clearing cycle utilized by domestic electric
10 utilities. To put the Company's proposed line clearing program recommendation into
11 perspective, benchmark studies (Chart 9) show that the average level of line clearing
12 utilized by North American electric utilities is an approximate 4-year effective clearing
13 cycle or 25% of their system. Additionally, clearing cycle lengths were surveyed for
14 Michigan utilities in the MPSC Staff Report issued December 26, 2007, with results
15 demonstrating that Michigan utilities typically utilize cycle lengths in the 4- to 7-year
16 range. Shorter clearing cycles result in less outage impact due to vegetation, lower line
17 clearing cost per mile, and less dramatic impact on customer's property when line
18 clearing does occur. The Company's recommended level of \$53,000,000 equates to an

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1 approximate 8-year effective clearing cycle or approximately 12.5% clearing of the
2 Company's LVD system. This effective clearing cycle is almost twice as long as the
3 industry average. As can be seen in Chart 9 below (CN Utility Consulting, Utility
4 Vegetation Management Benchmark & Industry Intelligence published in 2010 and most
5 current data available), which is a comparison of North American utility clearing cycle
6 lengths for system voltages up to 59 kV (which includes the Company's LVD and the
7 majority of the Company's HVD system) for the year 2006, the average length of the
8 cycle was calculated at 4.4 years. As noted in the text describing the chart this 2006
9 average clearing cycle length is consistent with benchmark results previously recorded
10 for 2002 of 4.1 years. In Chart 9, Consumers Energy is Company Code 45.
11 Additionally, during the 10-year period of 2001 through 2010, 2006 was Consumers
12 Energy's second shortest recorded combined LVD and HVD effective clearing cycle
13 length of approximately 9 years, for that year. Removing the HVD portion of the system
14 cleared from this statistic results in a LVD effective clearing cycle length of 9.9 years, for
15 just 2006.

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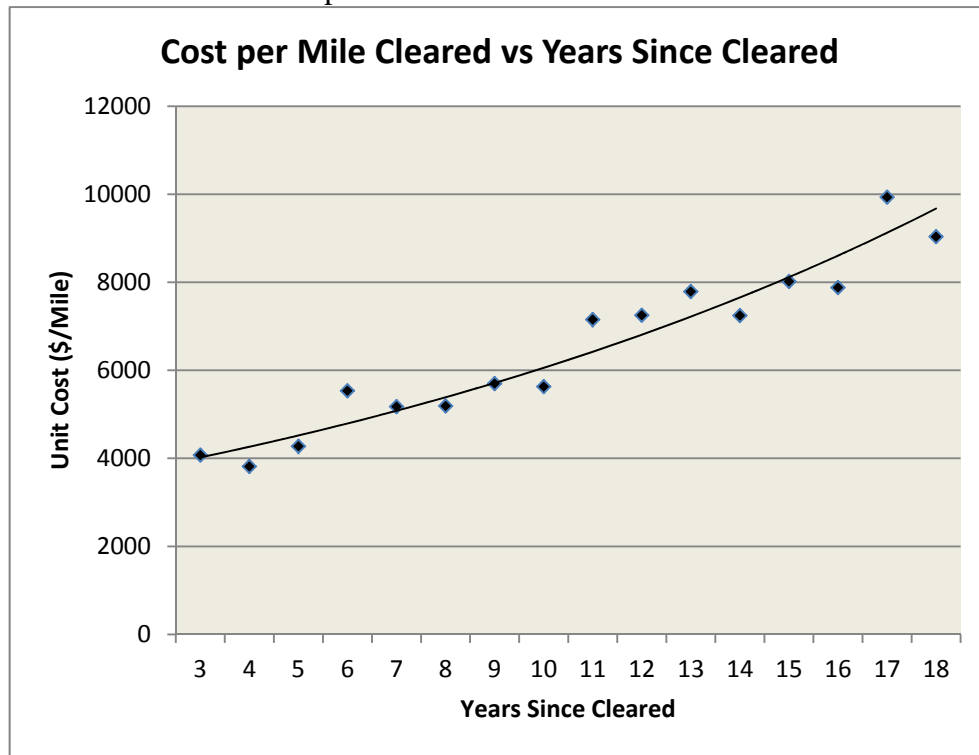
CHART 9 - CN Utility Consulting, Utility Vegetation Management Benchmark & Industry Intelligence published in 2010



- 1 Q. Are there any other advantages to clearing a greater percentage of the electric system
2 other than reducing tree related outages?
3 A. Yes, efficiency. As the time lengthens since a circuit was last cleared, the unit cost to
4 clear a circuit mile increases dramatically due to increased vegetation density. Chart 10
5 illustrates the historical relationship between cost to clear a circuit mile and the time since
6 it was last cleared.

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CHART 10 – Cost per Mile to Clear vs. Years Since Last Cleared



1 Additionally, based on operational experience, as the years since last clearing increases,
 2 the time needed to restore customers also increases due to the severity of and our ability
 3 to assess damage after outage events. Our overall goal is increased customer satisfaction
 4 and benefit through improved reliability while minimizing the long term unit cost per
 5 mile for line clearing.

6 Q. Are there any Employee Incentive Compensation Program (“EICP”) O&M expense
 7 dollars included in your exhibits?

8 A. No there are not. The testimony and exhibits of Company Witness Amy M. Conrad
 9 contain the Electric Division EICP O&M expense dollars.

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1 Q. Please identify the activities and responsibilities for the 3 major organizations which are
2 included in the Electric Division represented by line 1 of Exhibit A-12 (JRA-1) –
3 Summary of Projected Electric & Common O&M Expenses for the years 2011, 2012, and
4 2013.

5 A. The Electric Division O&M expenses represent activities and responsibilities associated
6 with 3 major organizations: 1) Electric Energy Operations; 2) Electric Energy Delivery;
7 and 3) Electric Customer Operations, excluding the Uncollectible write-offs.

8 **Electric Energy Operations**

9 Q. Please describe the activities of the Electric Energy Operations category.

10 A. Electric Energy Operations includes all the field work and administrative support for
11 operating, maintaining, and constructing the electric HVD and LVD lines, substations,
12 metering and other infrastructure involved in receiving electricity from our suppliers and
13 delivering it to our customers in a safe and reliable manner. Included in this category are
14 services relating to field operations for lines, substations, metering and service
15 restoration; new connection design and installation; work scheduling and field
16 dispatching; training and employee development. The Electric Energy Operations
17 category is comprised of the following 5 major sections:

- 18 • **Electric Network Services:** operates and maintains our HVD lines, both
19 overhead and underground, and all substations and other associated
20 equipment. Many routine maintenance and construction activities such as
21 equipment inspections, testing, and maintenance are performed in
22 Network Services to keep the HVD system and substations operating
23 safely, efficiently, and reliably.

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- 1 • **Energy Services:** receives electricity from the electric HVD system for
2 delivery to our residential, commercial, and industrial customers. This
3 section operates and maintains, and constructs our LVD lines, both
4 overhead and underground, metering, and other associated equipment.
5 This section performs maintenance and construction on the LVD system to
6 keep it operating safely, efficiently, and reliably. Additionally, this
7 section responds to customer service calls including storm related
8 customer outages. Meter reading is also included in the Energy Services
9 section.
- 10 • **Operation Services:** provides dispatching services, responds to customer
11 service calls and streetlight repairs, responds to requests from third parties
12 to stake the locations of the Company's underground system, provides
13 comprehensive work planning, and designs most residential new service
14 connection requests.
- 15 • **Employee Development and Skilling:** manages the Company's line
16 worker, substation worker, and other apprentice training programs, and all
17 other field worker development and skills training.
- 18 • **Business Services:** includes operations and maintenance for all Company
19 electric related building and similar facilities including utility costs, real
20 estate services for electric facility projects, and environmental, mail and
21 graphic services for all office locations.

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1 **Electric Energy Delivery**

2 Q. Please describe the activities of the Electric Energy Delivery category.

3 A. Electric Energy Delivery provides the centralized planning, budgeting, engineering,
4 engineering support, design services, and project management for the Electric Division.

5 The Electric Energy Delivery category is comprised of the following 4 major sections:

- 6 • **Electric Asset Management:** provides system operational and capacity
7 planning, LVD and HVD system design engineering, technical design
8 standards, system control and monitoring. Electric Asset Management
9 also performs program management for all of electric distribution's
10 reliability based maintenance and capital programs. In addition this
11 section is responsible for line clearing program management, and NERC
12 regulatory compliance associated with electric distribution.
- 13 • **Work Process and Business Management:** provides budget services
14 and analysis, and Sarbanes Oxley compliance support.
- 15 • **Distribution Strategy:** provides support for long term strategic planning.
- 16 • **Project Management:** provides project management competencies and
17 discipline, for targeted projects that are more complex in nature and
18 require a significant amount of coordination with customers or other
19 external parties.

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1 **Electric Customer Experience and Operations**

2 Q. Please provide a brief summary of the activities (excluding Uncollectible Write-Offs) for
3 the Electric Customer Experience and Operations category.

4 A. Electric Customer Experience and Operations provides for the vast majority of all direct
5 contact between the Company and its electric customers, including customer inquiries,
6 billing and payment, and customer preferences. The portion of Electric Customer
7 Experience and Operations expenses covered in my testimony is comprised of the
8 following 6 major sections:

- 9 • **Small Customer Care:** is composed of the Call Centers, Consumer
10 Affairs, and the Executive Complaints Assistance Center (“ECAC”) and
11 all the supporting areas required for their operation. The Company Call
12 Centers are the first contact point between customers and the Company.
13 The Call Centers handle all inquiries from residential and small
14 commercial/industrial customers. The Consumer Affairs and ECAC areas
15 attempt to resolve informal and formal customer complaints forwarded to
16 the Company by the Commission, Company management or legislators as
17 well as other inquiries generated by customer calls.

- 18 • **Revenue Operations:** includes Credit and Collections, Direct Payment
19 Offices (“DPOs”), Damage Claims and Loss, Theft, and Customer Billing.
20 The Credit and Collections area handles customer accounts that are past
21 due. Employees within this area make field stops to customer premises in
22 an attempt to collect past due money, sign customers up for low income
23 programs or a payment plan where appropriate and/or disconnect service.

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1 Additionally, Credit and Collections manages customer security deposits
2 and collection agency expenses associated with our efforts to reduce
3 uncollectible accounts. This area also works with local/state and federal
4 assistance agencies to collect payments on behalf of the customers to
5 avoid disconnection. The DPOs are walk-in customer payment offices in
6 13 locations around the state. The Damage Claims and loss area
7 investigates and resolves incidents where either damage was caused to
8 Company property/facilities or damage was caused to customer
9 property/facilities. The Theft area investigates incidences of suspected
10 theft on our electric meters. The Customer Billing area manages the
11 exception billing process for Consumers Energy's electric customers.
12 "Exception billing" occurs when a customer bill requires individual
13 analysis in order to resolve unusual billing, meter problems, etc. The
14 exception billing process may include customer contact, billing
15 adjustment, re-reading the meter, or billing as is.

- 16 • **Business Customer Care:** is responsible for meeting the informational
17 and services needs of Consumers Energy's largest and most complex
18 business class customers. This section is composed of Business Customer
19 Management and the Business Customer Operations Center. Business
20 Customer Management includes Corporate Account Managers ("CAM"s)
21 who deal directly with Consumers Energy's larger, more sophisticated
22 business customers on energy issues affecting these customers. The
23 Business Customer Operations Center, a specialized call center, is

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1 available to business customers during routine business hours and with
2 extended hours during times of emergency situations.

- 3 • **Customer Experience Design:** This department's primary role is to
4 improve the customers' overall experience when interacting with the
5 Company's customer-facing processes. This section also provides
6 marketing support to core customer value initiatives such as increasing
7 enrollments in the Budget Plan, customer billing options such as electronic
8 billing, increasing participation in the Company's voluntary Renewable
9 Resource Program, and net metering programs.

- 10 • **Customer Insights & Quality:** This department analyzes the results of
11 utility customer satisfaction surveys and conducts several primary
12 customer research studies that support the Company's Customer Value
13 Initiative. These studies include surveys of various customer segments
14 ranging from residential to large commercial and industrial, which
15 measure customer satisfaction with the products and services they receive
16 for the price that they pay. The group also manages a Voice of the
17 Customer Feedback System that analyzes complaints, transaction data, and
18 other leading indicators of Company performance. All of this information
19 is used as inputs to modify policies, adjust processes, develop better
20 communications efforts, and inform product and service development – all
21 with the goal of improving customer value.

- 22 • **Business Support:** includes funding related to the use of stationery,
23 forms, and service bill postage.

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1 Q. Please explain the O&M expenses for the Statutory Low Income Programs as shown on
2 line 2 of Exhibit A-12 (JRA-1) – Summary of Projected Electric & Common O&M
3 Expenses for the years 2011, 2012, and 2013.

4 A. In 2011, approximately \$26.5 million was included in customer rates to fund the Low
5 Income Energy Efficiency Fund (“LIEEF”) and its successor, the Vulnerable Household
6 Warmth Fund (“VHWF”). This amount is shown on line 2, column (b) of Exhibit A-12
7 (JRA-1). A portion of the 2011 LIEEF amount in rates was refunded to customers in
8 June 2012 as a result of the Commission’s May 1, 2012, Order in MPSC Case No.
9 U-16962. Consumers Energy’s electric business was apportioned approximately
10 \$14.3 million of the VHWF funding. Approximately \$0.9 million of this amount
11 represents amounts in rates from December 20 through December 31, 2011. The
12 \$13.4 million remainder was in customer rates from January to July 2012 and that
13 amount is shown on line 2, in column (c) of Exhibit A-12 (JRA-1). The VHWF achieved
14 the statutory funding required from utilities in July 2012 at which time it was removed
15 from customer rates. The Company does not anticipate the need to include in its general
16 base rates the VHWF or any similar mechanism in 2013 and that is reflected on line 2,
17 column (d) of the afore mentioned exhibit.

18 **CAPITAL EXPENDITURES**

19 Q. Please describe the Company’s projections of capital expenditures for Electric
20 Distribution as shown in Exhibit A-13 (JRA-2) – Summary of Projected Electric &
21 Common Capital Expenditures for the years 2011, 2012, 2013, and 2014.

22 A. As shown in Exhibit A-13 (JRA-2), the total Electric Distribution capital expenditures for
23 which the Company is requesting rates recognition in this case for the years 2011, 2012,

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1 2013, and 2014 time periods are \$323,266,000; \$338,504,000; \$341,870,000; and
2 \$344,129,000, respectively, as set forth in this exhibit on line 8, column (b), line 8,
3 column (c), line 8, column (d) and line 8, column (e), respectively. The 2011 capital
4 expenditures shown in column (b) are based on actual expenditures taken from internal
5 Company records. Columns (c), (d) and (e) were based on future projections of the
6 investment levels necessary within the various programs to meet expected load, maintain
7 the Company's SAIDI to address customer reliability expectations and account for new
8 business. In addition to activity levels, the projections reflect capitalized cost increases
9 such as wage and salary increases and increases associated with purchasing new higher
10 efficiency distribution transformers that meet Department of Energy ("DOE")
11 10 CFR 431.196 efficiency standards which went into effect on January 1, 2010.

12 Q. What are the major programs within the Electric Distribution capital expenditures?

13 A. The 7 major programs, as shown on Exhibit A-13 (JRA-2) lines 1-7 are: 1) New
14 Business; 2) Reliability; 3) Capacity; 4) Demand Failures; 5) Asset Relocations;
15 6) Technology/Production Support; and 7) Electric Business Services.

16 **New Business**

17 Q. Please describe the capital expenditures related to the New Business program as shown
18 on line 1 of Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common Capital
19 Expenditures for the years 2011, 2012, 2013, and 2014.

20 A. The New Business program consists of the capital cost of adding new commercial,
21 industrial, and residential customers. The program costs include the cost of installing
22 poles, conductors, transformers and services, and the cost of meters to service new
23 customers. These costs are partially offset by customer contributions. The Company is
24 projecting total New Business capital expenditures (net of customer contributions) to be

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1 \$34,490,000; \$31,374,000; \$36,685,000;and \$39,033,000 as set forth in this exhibit on
2 line 1, column (b), line 1, column (c), line 1, column (d), and line 1, column (e),
3 respectively.

4 **Reliability**

5 Q. Please describe the capital expenditures related to the Reliability program as shown on
6 line 2 of Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common Capital
7 Expenditures for the years 2011, 2012, 2013, and 2014.

8 A. This category includes asset management programs designed to ensure the long-term safe
9 and reliable operation of the electric HVD and LVD systems. The capital expenditures in
10 this program include investments to install, upgrade, and rehabilitate LVD lines,
11 metropolitan underground systems, the Supervisory Control and Data Acquisition
12 (“SCADA”) systems, protective relay systems, HVD lines, and HVD and LVD
13 substations. Additionally there is funding to begin upgrading existing LVD Substations
14 with Distribution SCADA (“DSCADA”) to the benefit of our customers. The Company
15 is projecting total Reliability capital expenditures to be \$75,098,000; \$101,940,000;
16 \$106,132,000; and \$107,481,000 as set forth in this exhibit on line 2, column (b), line 2,
17 column (c), line 2, column (d), and line 2, column (e), respectively. This funding level of
18 Reliability will provide for necessary line equipment rehabilitation, an expanded pole
19 replacement program and address repetitive outages that our customers experience. The
20 repetitive outage areas are sections of our system where customers experienced more than
21 5 outages in a 12-month period and require investment to upgrade poles, conductor, and
22 other facilities to improve reliability.

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1 Q. What types of fully projected reliability activities are being funded in this time period?

2 A. The Company is planning to fund investment in our electric distribution system in order
3 to upgrade deteriorated equipment, reduce system outages during weather challenges,
4 improve our ability to monitor and restore system outages, and generally strengthen our
5 electric distribution system assets. The capital investments are all directed at preventing
6 outages and/or replacing obsolete equipment, and can be broken down into investments
7 in LVD lines, investments in substations, and investments in HVD lines.

8 Q. What investments in LVD lines are planned?

9 A. The work on the LVD lines will include: 1) upgrading lightning protection; 2) replacing
10 equipment that has reached the end of its useful life such as poles, switches and overhead
11 and underground conductors; 3) addressing areas that have experienced repetitive
12 outages; and 4) sectionalizing. Sectionalizing refers to measures designed to segment the
13 electric distribution system into smaller sections, thereby minimizing the number of
14 customers that are affected by any individual outage. Introduction of more advanced
15 distribution sectionalizing through automated methods are included in this program. This
16 work also includes a project to identify and replace distribution fused switches of a
17 particular vintage which have a notably higher failure rate. The Decision Analysis model
18 is used to analyze the effectiveness of reliability programs at a high level. Work plans
19 are developed taking into account and addressing the poorest reliability and repetitive
20 outage performance issues.

21 Q. What investments in substations are planned?

22 A. The work on the LVD and HVD substations will be directed at: 1) targeted replacement
23 programs for specific equipment, such as obsolete oil circuit breakers, substation

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1 lightning arresters and transformer bushings; 2) complete substation rebuilds;
2 3) protective relay replacements; and 4) DSCADA. Protective relay equipment is the
3 critical means to protect major HVD system assets (transformers, lines etc.) from damage
4 due to faults on the system, and is used to automatically isolate and reconfigure the HVD
5 system after faults, reducing customer outages, and outage duration.

6 Q. What is DSCADA?

7 A. The existing SCADA system at Consumers Energy is almost exclusively in HVD
8 substations. DSCADA is an expansion of the existing SCADA system and capabilities
9 into the LVD substations. The internal substation communications hardware required for
10 DSCADA has been the Company's standard design for new substations since 2007. The
11 external communications hardware is being added to the standard design for all new
12 substations in 2012 and beyond.

13 Q. What is the DSCADA Program?

14 A. The DSCADA Program is a multi-year capital investment program to systematically
15 upgrade Consumers Energy's existing LVD substations to our present LVD substation
16 standard which includes DSCADA. The current plan is to deploy DSCADA during years
17 2012 through 2022.

18 Q. What investments in the DSCADA program are included in your testimony?

19 A. In 2012 the Company projects to spend \$1,500,000; in 2013 the Company is projecting to
20 spend \$3,090,000; and in 2014 the Company is projecting to spend \$5,635,000 for the
21 DSCADA program. These expenditures would result in upgrades to approximately
22 15, 30, and 55 LVD substations, respectively. The investments consist of the DSCADA
23 work in the LVD substations which will include: 1) substation external communications

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1 hardware; 2) substation internal communications hardware and remote terminal unit
2 (“RTU”); and 3) replacement of obsolete circuit recloser and voltage regulator devices
3 and controls.

4 Q. How does DSCADA benefit customers?

5 A. DSCADA provides real-time monitoring and control of key equipment in LVD
6 substations. This functionality improves the Company’s awareness of and ability to
7 respond to system issues and outages that impact customers.

8 Q. What investment in HVD lines is planned?

9 A. The work on the HVD lines will be directed at: 1) complete overhead line rebuilds
10 including conductor, and structure replacements on our worst performing line sections;
11 2) deteriorated underground lines replacement; and 3) installation of motor operated air
12 break devices to again, minimize customer outages and outage duration. The Company
13 needs to aggressively replace obsolete and deteriorated equipment. We estimate that
14 50-70% of our major equipment is over 30 years old and thus approaching the end of its
15 useful life. The Company would upgrade assets to reduce the number of outages due to
16 deterioration and lightning, and to improve our distribution assets’ ability to withstand
17 storm activity. This will complement O&M expenses on line clearing and preventive
18 maintenance.

19 Q. What is the customer benefit that will be obtained by these capital expenditures and
20 O&M expenses?

21 A. Together these capital expenditures and O&M expenses address the leading causes of
22 customer outages on the Company’s electric system, which again are tree related,
23 equipment failures, and lightning/weather. Overall, the reliability program is targeted to

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1 improve system reliability and to enhance customer satisfaction through a reduction of
2 customer outages and improves response when outages occur.

3 **Capacity**

4 Q. Please describe the capital expenditures related to the Capacity program as shown on line
5 3 of Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common Capital
6 Expenditures for the years 2011, 2012, 2013, and 2014.

7 A. This category includes capital investments necessary to: (i) ensure that the HVD electric
8 system is capable of serving forecasted electric peak demand with all HVD facilities
9 in-service; (ii) ensure that single facilities of the HVD system can be taken out of service
10 during non-peak demand periods for maintenance and construction without loading
11 remaining HVD facilities above emergency ratings or serving customers with
12 unacceptable low voltage; and (iii) fix LVD system overloads and low voltage
13 occurrences after they occur. The Consumers Energy customers realized the benefit of a
14 consistently funded Capacity program during the third week of July in 2011 when the
15 Company's all-time gross peak load of 8,930 MW occurred and again on July 17, 2012,
16 when the Company recorded a new all-time gross peak load of approximately 9,000 MW.
17 During these periods there were no significant customer service related issues associated
18 with these system peaks. The Company is projecting total Capacity capital expenditures
19 to be \$58,850,000; \$58,215,000; \$56,128,000; and \$53,508,000 as set forth in this exhibit
20 on line 3, column (b), line 3, column (c), line 3, column (d), and line 3, column (e),
21 respectively.

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1 **Demand Failures**

2 Q. Please describe the capital expenditures related to the Demand Failures program as
3 shown on line 4 of Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common
4 Capital Expenditures for the years 2011, 2012, 2013, and 2014.

5 A. This category includes expenditures incurred in connection with customer outage
6 restoration and the repair or replacement of equipment due to unanticipated or imminent
7 failure. This provides both immediate customer benefit via service restoration and longer
8 term customer benefit associated with having new equipment providing their service.
9 This category also includes expenditures to support the Company's conversion of
10 mercury vapor streetlights which started in 2011. The Company is projecting total
11 Demand Failures capital expenditures to be \$108,788,000; \$91,825,000; \$96,607,000;
12 and \$95,337,000 as set forth in this exhibit on line 4, column (b), line 4, column (c),
13 line 4, column (d), and line 4, column (e), respectively.

14 **Asset Relocations**

15 Q. Please describe the capital expenditures related to the Asset Relocations program as
16 shown on line 5 of Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common
17 Capital Expenditures for the years 2011, 2012, 2013, and 2014.

18 A. This category includes capital investments necessary to relocate electric facilities due to
19 planned road, building, or other third party construction. The cost of relocating lines in
20 road rights-of-way or, in some instances, on private property, is typically the
21 responsibility of Consumers Energy. The fully projected expenditures in this program
22 reflect both past history as well as requirements to meet the level of asset relocations
23 associated with anticipated local and state government spending. The Company is

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1 projecting total Asset Relocation capital expenditures to be \$21,513,000; \$18,660,000;
2 \$16,310,000; and \$18,519,000 as set forth in this exhibit on line 5, column (b), line 5,
3 column (c), line 5, column (d), and line 5, column (e), respectively.

4 **Technology/Production Support**

5 Q. Please describe the capital expenditures related to the Technology/Production Support
6 program as shown on line 6 of Exhibit A-13 (JRA-2) – Summary of Projected Electric &
7 Common Capital Expenditures for the years 2011, 2012, 2013, and 2014.

8 A. This category includes expenses for development, procurement, and implementation of
9 new or enhanced computer hardware and software infrastructure necessary to manage the
10 electric distribution operation. The Company is projecting total Technology/Production
11 Support capital expenditures to be \$1,954,000; \$4,019,000; \$3,444,000; and \$2,659,000
12 as set forth in this exhibit on line 6, column (b), line 6, column (c), line 6, column (d),
13 and line 6, column (e), respectively. These expenditures include items associated with
14 the Outage Management System, the Energy Management System, field device
15 replacements, capital tools, and substation security technologies.

16 **Electric Business Services**

17 Q. Please describe the capital expenditures related to the Electric Business Services program
18 as shown on line 7 of Exhibit A-13 (JRA-2) – Summary of Projected Electric & Common
19 Capital Expenditures for the years 2011, 2012, 2013, and 2014.

20 A. There are a number of areas that are contained in the Electric Business Services
21 program. These primarily include facilities investments and transportation fleet
22 investments. Facilities investments include repairing failed capital components of
23 buildings including yards and ground, building envelope and operating systems,

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1 removing conditions that contribute to potential health and safety hazards, proactively
2 repairing emergency backup systems, those minimal facilities infrastructure investments
3 which mitigate the effects of building depreciation to avoid imminent near term failures
4 and upgrades for health and wellness. It also includes dollars for paving, roofing,
5 elevators, etc. at various building and plant sites. The building of new service centers in
6 Muskegon and West Branch, a training center at the Campbell Plant, and a guardhouse
7 at the Karn Weadock plant are additionally included. Transportation fleet investments
8 include the purchase of vehicles, equipment, and trailers as part of the Company's fleet
9 lifecycle program. Computer and other equipment include the purchase of
10 miscellaneous printers, mechanical equipment, print production equipment, and wellness
11 equipment. The Company is projecting total Electric Business Services capital
12 expenditures to be \$22,574,000; \$32,473,000; \$26,564,000; and \$27,592,000 as set forth
13 in this exhibit on line 7, column (b), line 7, column (c), line 7, column (d), and line 7,
14 column (e), respectively.

15 **CONCLUSION**

16 Q. Will the proposed O&M expenses and capital expenditures levels allow Consumers
17 Energy to meet the Commission's Service Quality and Reliability Standards?

18 A. Yes, in most years. The Commission established a set of performance standards for
19 distribution utilities that became effective on February 9, 2004. As shown in Exhibit
20 A-14 (JRA-3), our actual performance for 2007 met 10 of the 11 standards. The Outage
21 Response Normal Conditions standard was not met for 2007. The Company's actual
22 performance for 2008 met 8 of the 11 standards. The Outage Response Normal
23 Conditions standard was not met in 2008. The Company's actual performance for 2009

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1 met 9 of the 11 standards. The Outage Response Normal Conditions standard was not
2 met in 2009. The Company's actual performance for 2010 met 10 of the 11 standards.
3 The Outage Response Normal Conditions standard was not met in 2010. The Company's
4 actual performance for 2011 met 9 of the 11 standards. The Outage Response Normal
5 Conditions standard and the Repetitive Outage standard were not met in 2011.
6 Consumers Energy's planned O&M and projected capital funding as described
7 throughout my testimony addresses the reliability related standards. The reliability
8 investments previously discussed, along with the O&M levels addressed earlier in my
9 testimony, will help reduce the number of total interruptions as well as the number of
10 customers affected by repetitive outages. The Decision Analysis model has projected
11 that without these levels of spending on preventive maintenance and capital improvement
12 programs our reliability will deteriorate and our ability to meet performance standards for
13 service restoration and repetitive outages will further suffer. Consumers Energy has
14 requested a level of funding that provides a reasonable expectation that it would meet the
15 Commission's Service Quality and Reliability Standards in most years.

16 Q. Please explain the importance to the Company of meeting the Commission's Service
17 Quality and Reliability Standards?

18 A. The Service Quality and Reliability Standards were developed as a means to annually
19 monitor utilities' customer service and success in delivering safe and reliable electric
20 service to its customers. Sound customer service and delivery of electric service in a safe
21 and reliable manner are fundamental goals of Consumers Energy which completely align
22 with the philosophy behind the Service Quality and Reliability Standards.

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1 Q. How has spending on the electric distribution system accrued to the benefit of Consumers
2 Energy's customers?

3 A. Since 2006 the Company has focused funding to improve system reliability and provide
4 its customers with an improved service level. The SAIDI, SAIFI and CAIDI data,
5 excluding MEDs per the IEEE Standard 1366-2003 found in Chart 11 below for the years
6 2007 through 2011, illustrate an improvement in electric distribution system performance
7 through 2010. The 2011 results were adversely affected by the significant increase in
8 weather challenges as compared to 2009 and 2010.

Chart 11
2007-2011 Interruption Statistics (Excluding IEEE 1366 Major Event Days)

Year	SAIDI	SAIFI	CAIDI
2007	262	1.28	205
2008	281	1.08	260
2009	222	1.05	212
2010	216	1.04	207
2011	305	1.36	224

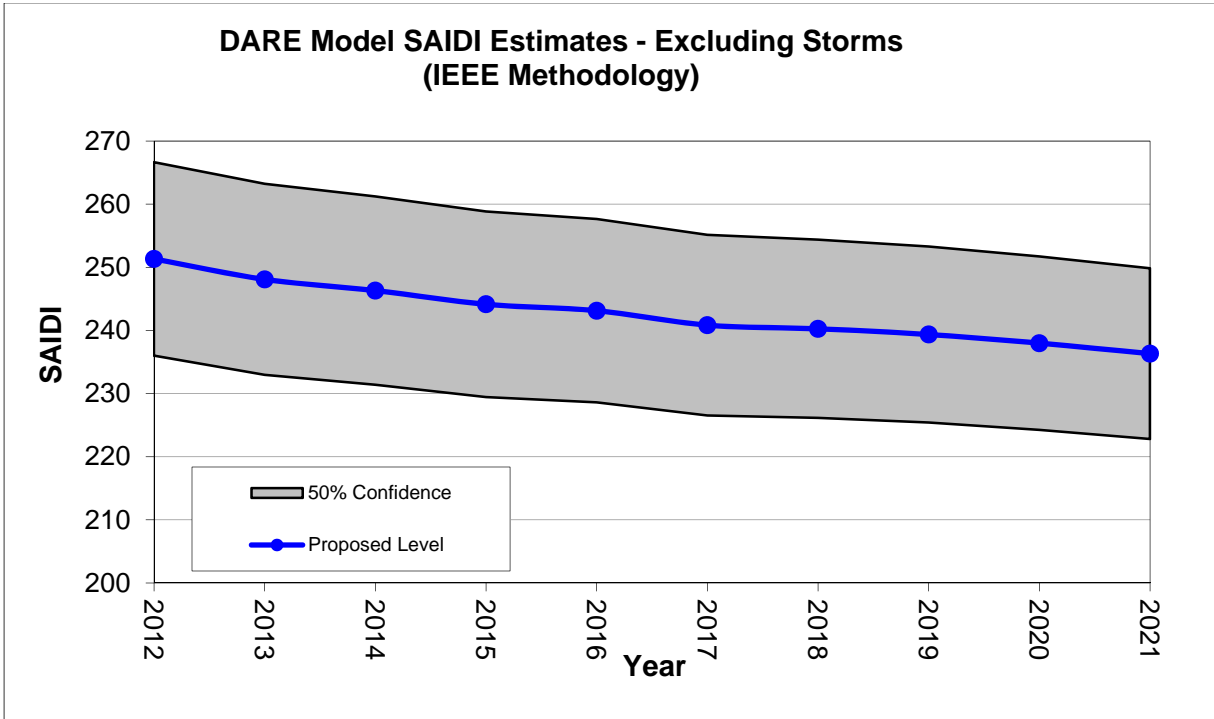
9 Q. What impact do you expect the O&M expenses and Capital expenditures will have on
10 future customer service reliability?

11 A. As shown in Chart 12 below, the DARE model predicts if the projected year levels of
12 O&M and capital funding the Company is requesting are maintained into the future that
13 reliability (SAIDI, excluding major events as defined by IEEE 1366-2003) will improve
14 over time and perform within the range depicted in the chart. This range represents a
15 50% confidence level that the electric system performance will be within this predicted
16 range. For example, the model predicts that the system SAIDI will be between
17 227 minutes and 255 minutes in 2017 which is an improvement over 2013 levels by
18 about 7 minutes. The value of this chart is not to provide a year against year comparison

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1 but rather to demonstrate that over time, the requested funding improves the electric
2 system performance and hence provides increased customer value.

Chart 12 – SAIDI Scenarios



3 Q. Does this conclude your testimony?

4 A. Yes.

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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

REBUTTAL TESTIMONY

OF

JAMES R. ANDERSON

ON BEHALF OF

CONSUMERS ENERGY COMPANY

March 2013

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. Please state your name and business address.

2 A. James R. Anderson, 1945 W. Parnall Road, Jackson, Michigan 49203.

3 Q. Are you the same James R. Anderson who previously presented direct testimony in this
4 case?

5 A. Yes.

6 Q. What is the purpose of your testimony?

7 A. First, I will rebut the direct testimony of MPSC Staff witness Ryan S. Laruwe concerning
8 Consumers Energy Company's ("Consumers Energy" or the "Company") electric
9 distribution reliability performance and his dismissal of the weather impacts on the
10 Company's 2011 reliability indices. I will also rebut the direct testimony of witness
11 Laruwe regarding the level of line clearing, service restoration, and NERC standards
12 implementation O&M spending necessary to improve reliability and customer service
13 and maintain regulatory compliance. I will also rebut the direct testimony of witness
14 Laruwe concerning the meter reading expense level in the test year 2013. I will also
15 rebut the direct testimony of witness Laruwe concerning his claim that historical capital
16 reliability funding has not demonstrated sufficient improvement in reliability
17 performance to justify further spending increases. I will then provide rebuttal testimony
18 concerning Attorney General witness Sebastian Coppola's O&M expense levels.
19 Additionally, I will rebut witness Coppola's direct testimony concerning the business
20 services expenditure reductions as well as rebut his concern about the DARE model
21 confidence level.

22 Q. Have you prepared any exhibits in conjunction with your rebuttal testimony?

23 A. Yes, I am sponsoring three additional exhibits:

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- 1 • Exhibit A-73 (JRA-5) – DP&P Reliability Improvement Report, August
2 2011;
- 3 • Exhibit A-74 (JRA-6) – CN Utility Consulting, Utility Vegetation
4 Management Benchmark & Industry Intelligence published in 2010,
5 Participants in 2006 and 2009; and
- 6 • Exhibit A-75 (JRA-7) – Summary of Actual & Projected Capital
7 Expenditures for the Electric Business Services Program, For the Years
8 2011, 2012, 2013, and 2014.

9 Q. Were these exhibits prepared by you or under your supervision?

10 A. Yes.

11 Q. Please describe Exhibit A-73 (JRA-5).

12 A. Exhibit A-73 (JRA-5) contains a report named DP&P Reliability Improvement Report,
13 August 2011 which analyzes historical costs and system improvement for Low Voltage
14 Distribution (“LVD”) reliability improvement projects completed by the Company in the
15 years 2002-2009. This report provides strong correlation between localized reliability
16 metrics and reliability improvement projects.

17 Q. Please describe Exhibit A-74 (JRA-6).

18 A. Exhibit A-74 (JRA-6) contains a list of the participants in the 2006 and 2009 CN Utility
19 Consulting, Utility Vegetation Management Benchmark & Industry Intelligence survey,
20 which was published in 2010.

21 Q. Please describe Exhibit A-75 (JRA-7).

22 A. Exhibit A-75 (JRA-7) provides a listing of the projects that make up the Company’s
23 electric business services capital program expenditures for 2011 and projected
24 expenditures for the years 2012 through 2014.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

MPSC Staff Witness Ryan S. Laruwe

ELECTRIC DISTRIBUTION PERFORMANCE DISCUSSION

1 Q. Mr. Laruwe asserts on pages 5-6 of his direct testimony that the IEEE 1366-2003 Major
2 Event Days (“MEDs”) exclusion methodology removes large storm anomalies from the
3 reliability data. He says this results in data that shows the utility’s ability to control the
4 frequency and duration of outages on a system wide basis under normal conditions
5 year-to-year. Do you agree?

6 A. No. While the IEEE 1366-2003 methodology removes the worst weather related events
7 from the year-to-year comparison data, it does not remove all abnormal weather days.
8 There are severe weather days that cause more outages than normal but do not rise to the
9 level of a MED. For example, a recent winter storm that hit Michigan on February 27,
10 2013, did not result in a MED. However, it was far from a normal day. Restoration
11 efforts required the mobilization of Company and contractor crews throughout Consumers
12 Energy’s statewide electric service territory to be sent to Michigan’s southern counties
13 where the preponderance of the outages occurred to complete the restoration efforts in a
14 timely manner. Small to medium sized storms like these do not rise to the level of a MED
15 but they still contribute to outages affecting “normalized” System Average Interruption
16 Frequency Index (“SAIFI”), System Average Interruption Duration Index (“SAIDI”), and
17 Customer Average Interruption Duration Index (“CAIDI”). If the weather patterns in a
18 particular year consist of many small to medium sized storms, the reliability statistics for
19 that year will still be skewed even with MEDs excluded.

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REBUTTAL TESTIMONY

1 Q. Mr. Laruwe asserts on page 6 of his direct testimony that the severe weather events that
2 impacted the Company's service territory in 2011 were normalized through the IEEE
3 1366-2003 MED exclusion process. He states that this places the 2010 and 2011
4 reliability results on an equal basis to be compared against each other. Do you agree?

5 A. No. The IEEE 1366-2003 MED exclusion process calculates a daily SAIDI. If the daily
6 SAIDI exceeds a certain threshold called the Tmed value, determined by adding
7 2.5 standard deviations to the average of the natural logarithms of the electric utility's
8 daily SAIDI performance during the most recent five-year period, that day is considered a
9 MED and excluded from ongoing reliability metrics. Typically, a severe weather event is
10 what drives a daily SAIDI to exceed the Tmed value and that day becomes a MED. Chart
11 1 shown below, provides the number of days in 2009, 2010 and 2011 that were
12 categorized as MEDs.

CHART 1 – Number of MEDs by Year

	2009	2010	2011
Number of MEDs	5	7	6

13 However, the IEEE 1366-2003 MED exclusion process does not fully normalize
14 reliability data when a high differential of small to medium sized weather events occurs
15 between years. As provided in my direct testimony, Chart 2 is a weather event summary
16 for 2009, 2010, and 2011 for the days in those years that were not considered MEDs
17 (“non-MEDs”). That is, Chart 2 is the weather event summary for the 360, 358, and 359
18 non-MEDs in 2009, 2010, and 2011, respectively. These are the same days that are
19 included in the calculation of the Company's IEEE 1366-2003 reliability metrics,
20 excluding MEDs.

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CHART 2 – Weather Event Summary, MEDs excluded

Weather Event Summary, Major Event Days Excluded					
		Observed Event Count			
		Warnings Issued	Icing Observation Hours	Lightning Strikes	
Year					
2009		91	80	309,000	
2010		230	68	938,000	
2011		324	180	1,094,000	
		Percent Increase			
Year	v.	Year	Warnings	Icing	Lightning
2011	v.	2009	256%	165%	254%
2011	v.	2010	41%	125%	17%
2011	v.	Ave(2009,2010)	102%	143%	75%

1 As demonstrated by Chart 2, the weather on non-MEDs in 2011 was much worse than
2 2009 and 2010, even though the number of MEDs were approximately the same.

3 Q. What were the Company's IEEE 1366-2003 reliability metrics excluding MEDs for 2009,
4 2010, and 2011?

5 A. The Company's metrics can be found in Chart 3 below.

CHART 3 -
2009-2011 Reliability Statistics (Excluding IEEE 1366 Major Event Days)

Year	SAIDI	SAIFI	CAIDI
2009	222	1.05	212
2010	216	1.04	207
2011	305	1.36	224

6 Q. What conclusion can be drawn when comparing the data and information contained in
7 Charts 2 and 3?

8 A. A key characteristic of Charts 2 and 3 that needs to be clearly understood is that both
9 contain data for the same days, non-MEDs, within the respective years. Knowing that
10 weather events create challenges for an electric distribution system it is a logical

JAMES R. ANDERSON
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1 conclusion that the higher percentage of weather events in 2011 contributed significantly
2 to the Company's 2011 reliability results. While the Company agrees and supports the
3 use of the IEEE 1366-2003 as a methodology for normalizing year-to-year data, it must be
4 recognized that it does not totally eliminate the impact of numerous small to medium
5 weather events (like was experienced in 2011) on year-to-year reliability indicators. In
6 summary, the number of weather challenges in 2011 compared with 2009 and 2010
7 significantly contributed to the higher SAIFI and SAIDI numbers in 2011.

8 Q. Mr. Laruwe used two of the Service Quality and Distribution Reliability standards for
9 analysis in this rate case, namely: 1) "Service Restoration – All Conditions" which
10 requires that 90% of customers experiencing an outage are restored within 36 hours, and
11 2) "Same Circuit Repetitive Interruptions" which requires that no more than 5% of the
12 Company's circuit elements experience more than 5 outages in a 12-month period. This
13 implies that the other 9 standards that are part of the Service Quality and Reliability
14 Standards adopted in MPSC Case No. U-12270, are not significant in this case. Do you
15 agree that these 2 of the 11 Service Quality and Distribution Reliability standards are the
16 only ones that should be used to measure the Company's reliability performance in this
17 docket?

18 A. No. While the Company met the "Service Restoration – All Conditions" standard in
19 2011, the Company endeavors to meet all 11 of the Service Quality and Reliability
20 Standards and meets most of them every year. The Company's actual performance for
21 2011 met 9 of the 11 standards. The "Service Restoration – Normal Conditions" standard
22 and the "Same Circuit Repetitive Interruptions" standard were not met in 2011.

JAMES R. ANDERSON
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1 Q. How did the Company perform in 2012 relative to the Service Quality and Reliability
2 Standards?

3 A. The Company met all 11 of the Service Quality and Reliability Standards in 2012.

4 Q. What are the Company's 2012 IEEE 1366-2003 reliability metric results, excluding
5 MEDs and how do they compare to the 2011 results?

6 A. The Company's 2011 and 2012 reliability metric results can be found in Chart 4 below.

CHART 4 –
2011-2012 Reliability Statistics (Excluding IEEE 1366 Major Event Days)

<u>Year</u>	<u>SAIDI</u>	<u>SAIFI</u>	<u>CAIDI</u>
2011	305	1.36	224
2012	204	1.06	192
% Improvement	33%	22%	14%

7 The Company made a tremendous improvement in 2012 when compared to 2011 to the
8 benefit of its customers. Proactive storm restoration practices and effective capital
9 reliability investments contributed to improved reliability in 2012.

ELECTRIC DISTRIBUTION O&M EXPENSES

10 Q. What amount is Mr. Laruwe proposing for line clearing O&M expenses?

11 A. Mr. Laruwe is proposing a line clearing spending level of \$44,550,000 on page 20,
12 line 14, of his testimony, an amount that is significantly lower than Consumers Energy's
13 projected amount of \$53,000,000.

14 Q. Do you agree with Mr. Laruwe's proposed amount for the line clearing O&M program?

15 A. No. Mr. Laruwe suggests that annual line clearing expenses should be based on what was
16 approved in the Company's last rate case (Case No. U-16794). He indicates the
17 Company's projection for \$53,000,000 to increase miles trimmed and hence reduce cycle
18 length is not prudent until data is provided that supports an increase in system reliability

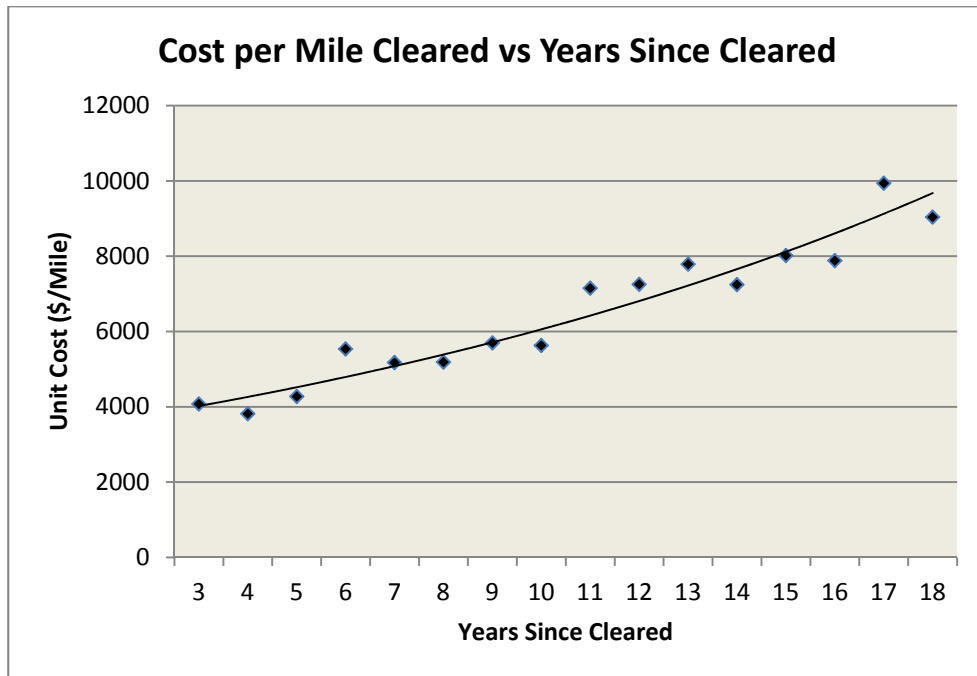
JAMES R. ANDERSON
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1 indices as a result of recent reductions in cycle length. However the Company has
2 provided data demonstrating the basis for the projected amount in my direct testimony on
3 pages 20-27.

4 Q. Staff witness Mr. Laruwe contends on page 20 of his direct testimony that reliability is the
5 proper measure for the “efficiency” of the line clearance program rather than cycle length.
6 Do you agree?

7 A. No. Reliability is a measure of the line clearing program *effectiveness*. The efficiency of
8 the line clearing program is measured by the cost per mile cleared. Efficiency decreases
9 (cost per mile cleared increases) as the program cycle length increases. Cycle length has a
10 dramatic impact on the cost per mile cleared as explained on pages 26-27 of my direct
11 testimony and summarized in Chart 5 below.

CHART 5 – Cost per Mile to Clear vs. Years Since Last Cleared



12 The amount projected by the Company will increase the efficiency of the line clearing
13 program by shortening the cycle length, because the cost per mile of trees cleared will

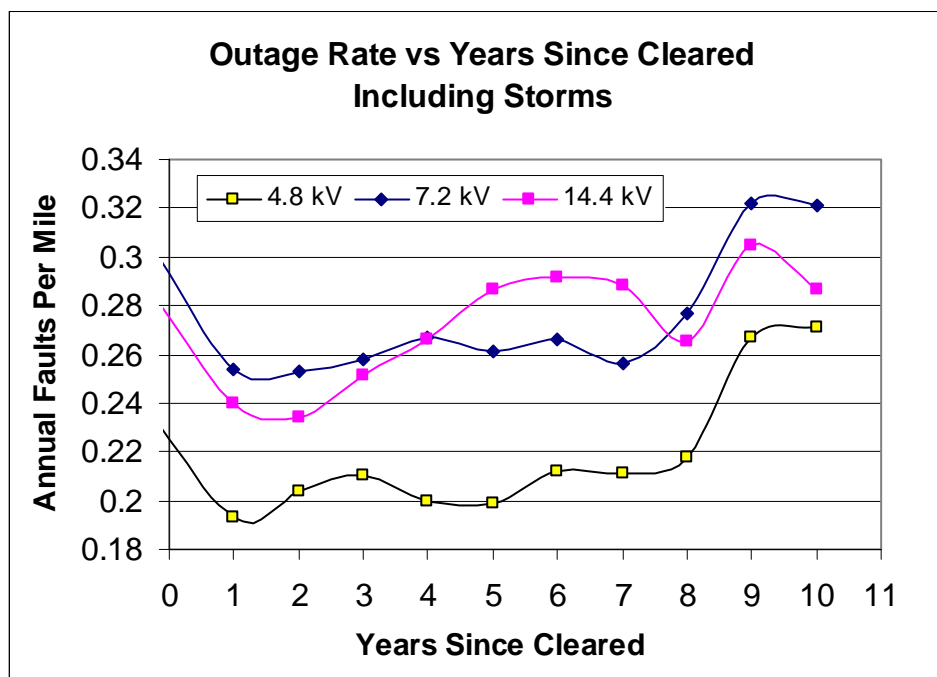
JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 decrease. Staff's suggestion that the Company continue to spend the same amounts does
2 not result in a more efficient line clearing program or improve reliability as sought by the
3 Company.

4 Q. What evidence demonstrates that reduced cycle length results in improved tree related
5 reliability?

6 A. First, Chart 7 on page 23 of my direct testimony, which is shown again as Chart 6, clearly
7 shows that the tree related reliability deteriorates measured on the y-axis as annual faults
8 per mile (more annual faults per mile) as the year since cleared increases on the x-axis.

CHART 6 -Outage Rates vs. Years Since Cleared



9 Simply put, the more often a circuit is cleared, the tree related reliability (annual faults per
10 mile) of the circuit improves. Second, there is a benefit and positive impact of circuit line
11 clearing relative to circuit reliability metrics of SAIDI, CAIDI, and SAIFI on circuits that
12 are trimmed. This is demonstrated in Exhibit A-73 (JRA-5) DP&P Reliability

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1 Improvement Report, August 2011. Chart 7 below is taken from page 44 of the Exhibit
2 and shows the analysis of 684 Consumers Energy distribution circuits that were cleared
3 over a multiple year timeframe and the reliability impact that this work had on the local
4 circuits. It compares the performance of those circuits in the years before the trimming
5 was accomplished with the performance of those circuits after the work was completed.

CHART 7: Full Circuit Tree Trimming Project Data

Full Circuit Trim Data								
Cost per Mile		Circuits Affected each Year of Analysis	Calculated Data Including Storms			Calculated Data Excluding Storms		
No. of Projects	684		Annual SAIDI for Improvement Zones	Annual SAIFI for Improvement Zones	Annual CAIDI for Improvement Zones	Annual SAIDI for Improvement Zones	Annual SAIFI for Improvement Zones	Annual CAIDI for Improvement Zones
Minimum**	\$88							
Average	\$5,522							
Maximum	\$55,278							
5 Yrs Before Project Completion	685	363.5	1.13	320.6	154.1	0.89	173.1	
4 Yrs Before Project Completion	685	417.3	1.22	341.2	167.5	0.89	188.0	
3 Yrs Before Project Completion	685	536.8	1.40	384.0	201.5	0.97	208.7	
2 Yrs Before Project Completion	685	584.4	1.61	362.0	250.4	1.23	203.1	
1 Yr Before Project Completion	685	680.3	1.67	408.0	301.2	1.26	239.7	
Year of Project Completion	685	454.1	1.20	379.6	202.8	0.94	216.2	
1 Yr After Project Completion	685	374.1	1.09	343.9	188.9	0.87	218.2	
2 Yrs After Project Completion	535	319.8	0.99	323.8	164.5	0.80	206.0	
3 Yrs After Project Completion	493	375.9	1.04	360.6	183.4	0.83	221.7	
4 Yrs After Project Completion	456	381.6	1.06	358.8	162.3	0.80	203.1	
5 Yrs After Project Completion	394	422.8	1.07	393.4	192.6	0.80	240.2	
6 Yrs After Project Completion	359	353.0	1.00	352.7	172.3	0.78	221.6	
7 Yrs After Project Completion	347	411.2	1.17	351.0	223.63	0.94	237.28	
3 Year Average Before Project Completion		600.5	1.56	384.7	251.0	1.15	217.2	
3 Year Average After Project Completion		356.6	1.04	342.7	178.9	0.83	215.3	
Improvement		243.9	0.52	41.9	72.1	0.32	1.9	
% Improvement		40.62%	33.37%	10.90%	28.73%	27.88%	0.88%	
Improvement per \$10,000 Spent		441.7 minutes	0.94 outages	75.9 minutes	130.6 minutes	0.58 outages	3.5 minutes	

**Minimum cost data may be inaccurate due to unaccounted for costs during the SWM to SAP conversion.

6 In summary, SAIDI performance, excluding storms, improved 28.7% and SAIFI
7 performance improved 27.9% in the three years after trimming as compared to the
8 previous three years.

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REBUTTAL TESTIMONY

1 Q. Do overall system reliability metrics improve to the same extent as the circuit reliability
2 metrics improve as found in Chart 7?

3 A. No. Overall system reliability results are dependent on the current tree conditions of the
4 *entire* system and the percentage of the entire system that is cleared annually on a
5 continual basis. Historical average level of line clearing spending did not adequately
6 address the overall system tree conditions as stated in my direct testimony on page 24,
7 lines 2 through 8. In order to begin to see improvements in system reliability statistics,
8 the projected level of \$53,000,000 (effective eight-year trim cycle) for line clearing is
9 needed to more than offset outage increases caused by natural tree growth in the areas not
10 cleared in a given year, resulting in an overall improvement in system reliability statistics.
11 In summary, more line clearing (reduced cycle length) provides greater circuit reliability
12 to the benefit of the customers on those circuits. The Company proposes to increase the
13 number of circuit miles cleared to impact overall system reliability.

14 Q. How critical is the line clearing program to the Company's overall electric system
15 reliability?

16 A. Very critical. Trees are the number one cause of outages on the Company's electric
17 distribution system. For the five-year period 2006-2010, trees on average caused
18 approximately 22% of customer interruptions.

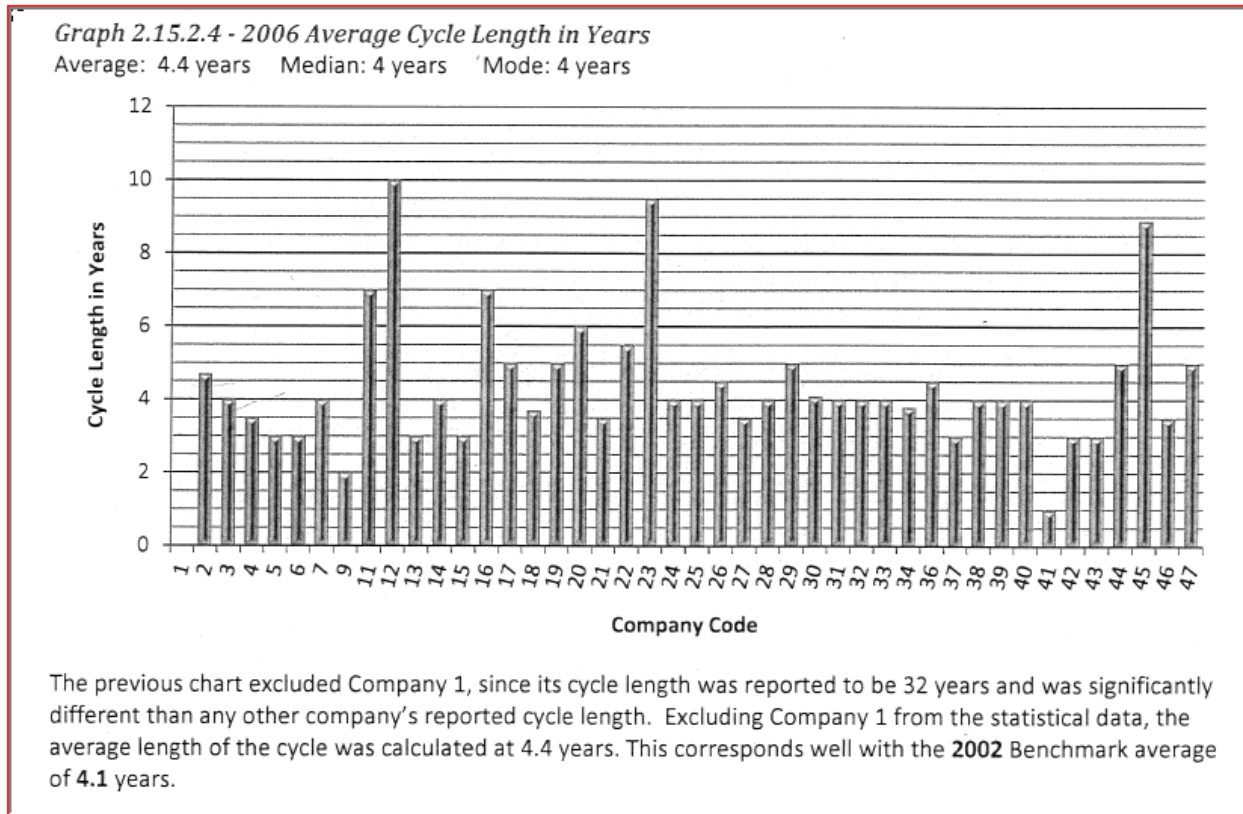
JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. On page 19 of his direct testimony, Mr. Laruwe suggests that the Company's use of utility
2 benchmark data related to line clearing trim cycles was not justification for increased
3 funding due to the anonymous nature of the demographics of the participants in the
4 benchmark study. Do you agree with this assessment?

5 A. No. Out of 43 utilities that responded to the benchmark survey related to cycle time,
6 Consumers Energy has the third highest cycle time of this group. Refer to Chart 8 below
7 which is also shown on page 26 of my direct testimony. The identities of the specific
8 utilities as they relate to the Company Code(s) within the chart are not known other than
9 Consumers Energy which is Company Code 45. However, the utilities that participated in
10 the benchmark study are known. The list of participants include utilities here in the
11 Midwest servicing electric service territories in Michigan, Indiana, Wisconsin, Minnesota,
12 Pennsylvania, and Illinois with similar growing seasons and vegetation types. Many of
13 these are the same states listed on page 7 of Mr. Laruwe's direct testimony to support his
14 use of the 2011 IEEE Benchmark Study data pertaining to system reliability metrics. A
15 list of the participating utilities in the CN Utility Consulting, Utility Vegetation
16 Management Benchmark & Industry Intelligence published in 2010 is included as
17 Exhibit A-74 (JRA-6).

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CHART 8 - CN Utility Consulting, Utility Vegetation Management Benchmark & Industry Intelligence published in 2010



1 It is common for utilities to reference industry data. Staff itself references IEEE industry
 2 data, without identifying each specific participant and their demographics. Staff's
 3 criticism of the anonymous industry data does not negate the fact that the Company's
 4 level of line clearing is the third longest cycle of this utility group.

5 Q. Do you agree with Mr. Laruwe that not knowing the demographics listed on page 19 of
 6 his direct testimony discredits the use of this comparative cycle length data chart?

7 A. No, I do not. Some of the demographics listed by Mr. Laruwe such as overhead vs.
 8 underground lines, percent lines requiring trimming, and size and terrain of service
 9 territory, have little or no bearing on cycle length. The impactful demographics are
 10 growing season and vegetation type. Knowing that utilities serving states here in the

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Midwest are included in the benchmark study provides sufficient correlation to
2 Consumers Energy's growing season and vegetation type to utilize this as a sound data
3 point source. Additionally, Consumers Energy is far outside of the cycle length of all but
4 2 of the 43 utilities contained in the data.

5 Q. Do you have any additional comments related to the Company's line clearing funding
6 projection?

7 A. Yes. It is not reasonable to expect the Company's overall system reliability performance
8 will improve without increasing the most impactful program the Company has to reduce
9 customer interruptions. The Company's projection of \$53,000,000 is necessary to move
10 the program level up to approximately 12.5% per year on the LVD system (an
11 approximate eight-year effective clearing cycle) in order to begin to make more
12 significant and necessary improvements in overall system reliability to the benefit of our
13 customers.

14 Q. Mr. Laruwe is proposing the service restoration O&M expenses be decreased from
15 \$38,180,000 to a four-year average of \$35,400,000 as noted in his direct testimony on
16 page 22. Do you agree?

17 A. No. Mr. Laruwe's assertion that a four-year historical average should be the basis of
18 determining the amounts needed in 2013 does not take into account the increased efforts
19 the Company has implemented to improve response time during outages as explained on
20 pages 11 and 12 of my direct testimony. Mobilization of resources, including increased
21 on-call coverage in advance of forecasted weather (one of the tactics the Company has
22 implemented), costs more than a reactive approach when weather does not develop as
23 predicted and the costs of mobilization are lost. Proactive storm restoration efforts benefit

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 customers because those efforts result in shorter duration outages than would otherwise be
2 achievable if the weather does develop as predicted or forecasted. The Company believes
3 that customers value a planned, prepared, and proactive approach to service restoration.
4 In 2011, Consumers Energy implemented several tactics designed to improve its response
5 to customer outages. Restoration pre-planning prior to expected weather events and
6 regular weekend pre-planning were instituted to proactively establish response approaches
7 based on anticipated weather impacts. The Company frequently considered and scheduled
8 weekend work assignments to perform necessary work and to have line crews available
9 for outage response during these non-standard work hours. Office and line crew resources
10 were mobilized in some cases prior to weather events in areas expected to be impacted.
11 Mobilization of additional contractor line crews (in state and out of state) was initiated
12 earlier, both during and prior to weather events, to increase resource availability in the
13 initial phase of restoration. These tactics allowed the Company to overcome the large
14 customer service restoration workload (SAIFI) in 2011 relative to 2009 and 2010 resulting
15 in a relatively smaller average duration increase (CAIDI) for these same years.

16 Q. Mr. Laruwe is proposing that no NERC PRC-005-2 standard expenses be included in the
17 Company's distribution O&M projection on page 24 of his direct testimony. Do you
18 agree?

19 A. No. The Company's projection of \$2 million is reasonable. The proposed NERC
20 PRC-005-2 standard is a protection system maintenance and testing standard that would
21 replace the existing PRC-005-1 standard. The proposed standard is dramatically more
22 prescriptive in: 1) its definition of protection system components that require
23 inspection/testing, 2) what the inspection and/or testing needs to consist of, and 3) the

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1 intervals for inspection/testing. The new standard would result in many more components
2 being inspected and/or tested, much more rigorous documentation requirements, and
3 significantly more complex field testing than the current standard requires. For example,
4 there is a change in the definition of what relays and protective equipment fall under the
5 new standard that will result in a larger population of equipment affected. There are new
6 testing requirements for voltage and current transformers that supply relays, for which we
7 will now have to verify that current and voltage signals are provided to relays. Also in the
8 future, testing for circuit breaker tripping control circuits will be much more extensive.
9 These changes will likely require more equipment maintenance outages than in the past
10 and will require the preparation and execution of detailed testing procedures that do not
11 exist today. Given the dramatic changes being proposed, Consumers Energy needs to
12 begin its efforts to prepare for the new standard in early 2013 ahead of the final adoption
13 of PRC-005-2. Funding is necessary to support the addition of up to 19 FTE technical and
14 field resources (not counting temporary contractors) needed to implement and sustain the
15 expanded protection system maintenance and testing program that would comply with the
16 new standard.

17 Q. Why does the Company maintain its projected funding for the NERC PRC-005-2 standard
18 in light of the delay in its implementation?

19 A. While it has taken the proposed standard longer than originally anticipated to work its way
20 through the NERC standards approval process, the changes are substantial enough and
21 require so much additional skilled labor that is not readily available, that the Company
22 needs to get started with preparation now. Also, the Company needs to develop new test
23 procedures that require additional time and resources to prepare prior to performing the

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 actual testing in the field. Preparation for the new standard is a prudent and responsible
2 step to ensure the Company maintains the necessary level of NERC compliance once the
3 standard goes into effect. Waiting to prepare for the standard after it goes into effect runs
4 the risk of not being fully compliant when required.

5 Q. On page 25 of his direct testimony, Mr. Laruwe recommends reducing the Company's
6 2013 distribution O&M meter reading expenses by \$1,578,000 to account for the AMI
7 meter deployment benefit of \$1,578,000. Do you agree with this recommendation?

8 A. No, because the \$1,578,000 expense reduction has already been taken by the Company in
9 this filing. Mr. Laruwe demonstrates this reduction in his Exhibit S-12, Schedule G-3, a
10 discovery response provided to the MPSC Staff by Company witness Lauren E.
11 Youngdahl (17087-ST-CE-135). The notation at the bottom of the response from
12 witness Youngdahl shown on Mr. Laruwe's exhibit clearly states that the \$1,578,000 was
13 taken from Line 1 of Exhibit A-70 (LEY-2). Witness Youngdahl is sponsoring the
14 expenses *and* expense reductions resulting from the Smart Energy (AMI) program. Thus
15 Mr. Laruwe is attempting to take this reduction twice in this proceeding, a proposal that
16 should be rejected.

CAPITAL EXPENDITURES

17 Q. On page 16 of his direct testimony, Mr. Laruwe is proposing a reliability capital
18 expenditure level of \$91,836,000 in 2013 and \$103,396,000 in 2014 as compared to the
19 Company's projection for \$106,132,000 in 2013 and \$107,481,000 in 2014. Do you
20 agree?

21 A. No. The Company's reliability capital expenditure program projection in 2013 and 2014
22 reflect additional funding over the 2011 level for deteriorated pole replacements that are

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 identified as a result of a more rigorous pole inspection program, increased line
2 rehabilitation associated with repetitive outages, and metropolitan system improvements
3 all of which will result in improved system reliability to the benefit of our customers.

4 Q. Can you explain the discrepancy between the actual reliability capital expenditures and
5 the authorized capital amounts as discussed by Mr. Laruwe on page 13 of his direct
6 testimony?

7 A. Yes. Overall the Company has spent close to its authorized amount for total distribution
8 capital expenditures in the years 2009 and 2011 as shown on Mr. Laruwe's Exhibit S-12,
9 Schedule G-1, page 3. In addition, the Company's 2012 total distribution capital
10 expenditures were \$336,609,000 versus a projected amount of \$338,504,000. The
11 reliability program expenditures have been less than authorized generally because actual
12 demand failure capital expenditures have exceeded forecasted levels and reductions had to
13 be made in the reliability program to bring overall capital expenditures in line with
14 available funding.

15 Q. Can you explain why the Company would defer reliability capital expenditures and
16 instead use the funding for other capital programs?

17 A. Yes. The reliability capital program is a very important program from a customer service
18 reliability standpoint. However, the Company has limited resources (funding, labor, etc.)
19 and some of the other capital programs require immediate action. For example, demand
20 failures are a function of imminent/emergent customer interruptions that must be
21 immediately rectified. New business requests must be fulfilled based on customer
22 requirements. Asset relocations respond to governmental or customer requests to relocate

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 facilities to accommodate their project requirements. There is much less spending
2 discretion in these programs than in the reliability capital program.

3 Q. Is there a reliability benefit when spending in the other programs is required?

4 A. Yes. When investments are made in many of the other distribution capital programs such
5 as new business, capacity, demand failures, and asset relocations, there is an ancillary
6 positive impact to system reliability. These capital programs, like the reliability capital
7 program, typically result in new infrastructure (poles, conductor, transformers, and other
8 ancillary equipment) being installed on the electric system. Whether this is a replacement
9 of existing infrastructure or added infrastructure on the system, it results in new
10 infrastructure which is inherently more reliable.

11 Q. Do you agree with Mr. Laruwe's assertion on pages 12-13, that the Company did not
12 provide evidence that recent increases in approved distribution capital reliability
13 expenditures are providing customer reliability benefits?

14 A. No. I supplied several examples throughout my direct testimony of how additional
15 funding improves reliability for customers. However, reliability spending increases do not
16 necessarily improve overall system reliability metrics in a direct proportion. Although
17 localized capital expenditures are highly effective at addressing poor performing portions
18 of the system, overall system reliability metrics are also impacted by the size, age,
19 condition, and performance of the portions of the electric distribution system that the
20 Company has not worked on or improved in a given year. Improvements in localized area
21 performance can often be masked in overall system metrics if the size, age, condition, and
22 performance of areas not invested in declines faster than those areas invested in.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. What additional evidence can you provide to address Staff's concern that recent increases
2 in approved distribution capital reliability expenditures are providing customer reliability
3 benefits?

4 A. First, the benefit and positive impact of capital reliability projects can be found throughout
5 the DP&P Reliability Improvement Report, August 2011, Exhibit A-73 (JRA-5). As an
6 example, Chart 9 below shows the analysis of 101 aerial spacer cable projects over a
7 multi-year timeframe and the reliability impact that those projects had on the local area
8 served. It shows a comparison of the performance for those areas in the years before the
9 project was accomplished and a comparison of the performance of those areas after the
10 projects were done. In short, SAIDI performance, excluding storms, improved 47.6% and
11 SAIFI performance improved 61.1% in the three years after the project was completed as
12 compared to the previous three years.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

CHART 9: All Aerial Spacer Cable Project Data

Table II: All Aerial Spacer Cable Projects Combined

All Aerial Spacer Cable Projects Data								
Cost per Mile		LCPIs Affected each Year of Analysis	Calculated Data Including Storms			Calculated Data Excluding Storms		
No. of Projects	101		Annual SAIDI for Improvement Zones	Annual SAIFI for Improvement Zones	Annual CAIDI for Improvement Zones	Annual SAIDI for Improvement Zones	Annual SAIFI for Improvement Zones	Annual CAIDI for Improvement Zones
Minimum**	\$8,090							
Average	\$248,559							
Maximum	\$731,408							
5 Yrs Before Project Completion		126	187.2	0.85	289.9	85.3	0.50	171.7
4 Yrs Before Project Completion		126	126.7	0.57	222.3	68.8	0.41	169.4
3 Yrs Before Project Completion		126	241.7	0.84	286.3	150.5	0.69	217.6
2 Yrs Before Project Completion		126	286.7	0.96	298.3	163.6	0.74	222.2
1 Yr Before Project Completion		126	673.5	1.64	410.6	280.4	1.16	241.4
Year of Project Completion		126	260.5	0.79	329.9	146.1	0.56	262.4
1 Yr After Project Completion		126	273.1	0.48	563.6	109.7	0.35	309.2
2 Yrs After Project Completion		100	154.2	0.43	355.3	98.0	0.34	284.4
3 Yrs After Project Completion		85	142.5	0.36	396.2	104.0	0.31	338.5
4 Yrs After Project Completion		42	285.2	0.51	559.7	146.0	0.41	355.4
5 Yrs After Project Completion		36	211.9	0.35	607.6	42.1	0.19	218.5
6 Yrs After Project Completion		25	51.5	0.18	284.1	5.2	0.04	135.1
7 Yrs After Project Completion		8	183.8	0.23	790.9	5.05	0.01	614.00
3 Year Average Before Project Completion			400.6	1.15	331.7	198.2	0.86	227.0
3 Year Average After Project Completion			189.9	0.43	438.4	103.9	0.34	310.7
Improvement			210.7	0.72	-106.7	94.3	0.53	-83.7
% Improvement			52.59%	62.90%	-32.16%	47.58%	61.14%	-36.85%
Improvement per \$10,000 Spent			8.6 minutes	0.03 outages	-4.3 minutes	3.8 minutes	0.02 outages	-3.4 minutes

**Minimum cost data may be inaccurate due to unaccounted for costs during the SWM to SAP conversion.

1 Second, using the same approach as Mr. Laruwe on page 13 of his direct testimony, Chart
2 10 below contains the Company's 2006 and 2012 IEEE 1366-2003 reliability metrics,
3 excluding MEDs.

CHART 10: IEEE 1366-2003 SAIDI, SAIFI, CAIDI (2006 vs 2012)

<u>Year</u>	<u>SAIDI</u>	<u>SAIFI</u>	<u>CAIDI</u>
2006	269	1.26	213
2012	204	1.06	192
% Improvement	24%	16%	10%

4 Significant improvement in all three reliability metrics has been realized between 2006
5 and 2012. This dispels Staff's conclusion that the Company's increased spending since
6 2006 did not provide customer reliability benefits.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. How critical is the reliability capital program to the Company's overall electric system
2 reliability?

3 A. Very critical. Equipment failures are the number three cause of outages on the
4 Company's electric distribution system behind tree-related and weather/lightning related
5 failures. For the five-year period 2007-2011, equipment failures on average caused
6 approximately 20% of customer interruptions.

7 Q. Do you believe the Company is committed to spending the level of reliability capital
8 expenditures that it is projecting?

9 A. Yes, the Company is committed to the level of reliability capital spending as long as
10 spending for the other capital programs that require immediate action do not exceed the
11 Company projections. The Company has identified reliability capital investments in its
12 distribution infrastructure that will improve service to its customers in areas that are
13 directly impacted. These expenditures are a subset of overall distribution capital
14 expenditures which include other programs such as new business, capacity, reliability,
15 demand failures, asset relocations, etc. that must be balanced against the overall available
16 funding. The overall amount of all distribution capital expenditures projected in 2013 and
17 2014 represents a level that is about 6% higher than what was spent in 2011. This overall
18 increase is within the Company's ability to manage, both from an engineering and
19 construction standpoint.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. Do you have any additional comments related to the Staff's testimony regarding the
2 Company's reliability capital funding projection?

3 A. The Company appreciates the Staff's understanding of the importance of capital
4 investments in an aging infrastructure and their recognition that reliability and quality of
5 service experienced by customers are directly related to the level of investment made.

Michigan Attorney General Witness Sebastian Coppola

ELECTRIC DISTRIBUTION PERFORMANCE DISCUSSION

6 Q. In his direct testimony on page 14, Mr. Coppola suggests that the DARE model's
7 confidence level of 50% is "a rather low level of probability on which to rely when
8 spending tens of millions of dollars." Do you agree with Mr. Coppola's assessment?

9 A. No, I do not. The 50% confidence level represents the expected value of system
10 performance over the long term. In any given year, the actual result will fall above the
11 expected value 50% of the time or below the expected value 50% of the time (thus the
12 reference to 50% confidence level). However, over the long term it is expected that the
13 system performance will trend near the DARE model result. Additionally, to help ensure
14 DARE model accuracy the program managers review the DARE model result and weigh it
15 against experience and actual system performance. Mr. Coppola raised a similar concern
16 about the DARE model's 50% confidence level as an issue in MPSC Case No. U-16191.

17 Q. Has the Commission previously addressed Mr. Coppola's concern about the Company's
18 use of its DARE model?

19 A. Yes, the Commission addressed this concern in its November 4, 2010, Order in MPSC
20 Case No. U-16191, on page 33 in the second paragraph where it stated, "*The Commission*
21 *is not persuaded that it should adopt the Attorney General's position on this issue. The*

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 *criticisms leveled at the DARE model seem to misunderstand the function of the model.*
2 *Consistent use of the DARE model provides results that reflect trends over time.”*

ELECTRIC DISTRIBUTION O&M EXPENSES

3 Q. What amount is Mr. Coppola proposing for line clearing O&M expenses?

4 A. Mr. Coppola is proposing a line clearing spending level of \$44.6 million versus the
5 Company’s projected amount of \$53,000,000.

6 Q. Mr. Coppola suggests that test year line clearing spending levels should be based on the
7 authorized amount approved by the Commission in MPSC Case No. U-16794. His main
8 rationale for recommending this level instead of the Company’s projection of \$53 million
9 is that the Company has been inconsistent in its historical spending pattern for line
10 clearing and that it has never spent \$53 million for line clearing. He also asserts that the
11 proposed improvement in SAIFI does not correspond to the percentage increase in line
12 clearing dollars being spent. Do you agree?

13 A. No. As with MPSC Staff witness Ryan S. Laruwe, Mr. Coppola’s rationale in
14 determining his proposed line clearing spending is not based on what is actually needed
15 and necessary to make significant improvements in reliability over time, but rather he
16 bases it on recent spending. As I noted previously, the Company is projecting to increase
17 its line clearing program to \$53,000,000 to move the program level up to approximately
18 12.5% per year on the LVD system (an eight-year effective clearing cycle) in order to
19 begin to make more significant and necessary improvements in overall system reliability
20 to the benefit of our customers.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. Mr. Coppola suggests that the large percentage change in line clearing spending does not
2 seem to make sense when compared to the rate of decline in SAIDI projected in future
3 years. Can you explain why he is not correct?

4 A. Yes. As explained in my rebuttal to Mr. Laruwe, line clearing expense increases do not
5 necessarily improve overall system reliability metrics in a direct proportion to the
6 expense. Although localized line clearing expenses are highly effective at addressing poor
7 performing portions of the system, overall system reliability metrics are also impacted by
8 the time since last trimmed and performance of the portions of the electric distribution
9 system that are not cleared in a given year. Improvements in localized area performance
10 can often be masked in overall system metrics if the size, age, condition, and performance
11 of non-maintained areas declines faster. This has been especially true in line clearing,
12 where historical spending patterns from 2002-2011 did not support overall improvement
13 in reliability metrics. This is clearly stated in my direct testimony on pages 24-25. The
14 Company's projection to move the program to a 12.5% program (effective eight-year
15 clearing cycle) is a recognition that more needs to be done in order to make significant
16 improvements in the overall system reliability metrics to the benefit of our customers.

17 Q. Does Mr. Coppola's recommended the line clearing program take into account industry
18 benchmarking?

19 A. No it does not. Mr. Coppola's recommended line clearing program is strictly based on
20 what the Commission approved in the last rate case (MPSC Case No. U-16794) and does
21 not reflect what is needed and necessary to improve overall system reliability; nor does it
22 consider industry benchmarks and practices.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. On page 17 of his direct testimony, Mr. Coppola is proposing a NERC PRC-005-2 O&M
2 expense reduction of \$1.0 million from the level projected by the Company due to the
3 delay in the implementation of PRC-005-2. Do you agree with this reduction?

4 A. No, I do not agree with this reduction. Although Mr. Coppola correctly points out that the
5 implementation of the NERC PRC-005-2 standard has been delayed, as I explained in my
6 rebuttal to Mr. Laruwe, the proposed changes are substantial enough and require so much
7 additional skilled labor that is not readily available, that we need to get started with
8 preparation now. Also, the Company needs to develop new test procedures that require
9 additional time and resources to prepare prior to performing the actual testing in the field.
10 Preparation for the new standard is a prudent and responsible step to ensure the Company
11 maintains the necessary level of NERC compliance once the standard goes into effect.

CAPITAL EXPENDITURES

12 Q. On page 48 of his direct testimony, Mr. Coppola is proposing a downward adjustment in
13 the 2012 proposed amount for business service capital expenditures of \$6.4 million from
14 the Company projected amount of \$32.5 million, bringing his proposed amount to
15 \$26.1 million in 2012. He did not request any adjustments to the 2013 and 2014 amounts.
16 Do you agree with witness Coppola's proposed reduction to the capital expenditures in the
17 electric business services program?

18 A. No, I do not. As discussed in my direct testimony beginning on page 42, line 20, there are
19 a number of areas contained in the electric business services program. This program
20 includes some expenditures that are relatively stable and predictable such as those for
21 repairing failed capital components of buildings, grounds and operating systems. The
22 Electric Business Services program also includes major projects wherein the expenditures

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 vary widely from year to year. These major projects are what causes the variability in the
2 expenditures and these projects are discussed in my direct testimony beginning on page
3 43, line 5. This variability was demonstrated in Exhibit A-13 (JRA-2) line 7, but was
4 questioned by Mr. Coppola in his testimony on pages 47-48. His Exhibit AG-13 cites
5 WP-JRA-9 and discovery responses 17087-AG-CE-162 and 17087-ST-CE-286 which
6 were provided by the Company. The Company's initial responses to discovery questions
7 17087-AG-CE-162 and in 17087-ST-CE-286 addressed the significant project year over
8 year variances in funding as compared with 2011, as requested in the questions, but did
9 not list all of the asset preservation and capitalized projects which are part of the business
10 services capital program. The Company also provided in its response to discovery
11 question 17087-AG-CE-363 further detail as to the year these major project expenditures
12 were projected. This information demonstrates which year the expenditures were
13 projected to have been incurred. Additionally, the Company has provided supplemental
14 responses to 17087-AG-CE-162 and in 17087-ST-CE-286 that show all of the specific
15 project line items that make up the funding projection for asset preservation & capitalized
16 projects. I have included the specific project list that was provided in the supplemental
17 responses along with the transportation equipment and computer & other equipment line
18 items that show the details of the business services capital expenditure projection as
19 Exhibit A-75(JRA-7). The amounts projected for the period from 2012-2014 are
20 supported by the project listing shown in Exhibit A-75 (JRA-7) and as supplied to
21 Mr. Coppola in the discovery process. These expenditures are reasonable and
22 Mr. Coppola's proposed reduction should be rejected.

JAMES R. ANDERSON
REBUTTAL TESTIMONY

1 Q. Does this conclude your rebuttal testimony?

2 A. Yes, it does.

1 JUDGE CUMMINS: With regard to questions,
2 there was indication that the Attorney General had
3 questions. Is that correct?

4 MR. MOODY: That is correct, your Honor.

5 JUDGE CUMMINS: Please continue,
6 Mr. Moody.

7 CROSS-EXAMINATION

8 BY MR. MOODY:

9 Q Good afternoon, Mr. Anderson.

10 A Good afternoon.

11 Q If you could turn to page 24 of your rebuttal testimony.
12 If you could?

13 A I'm there.

14 Q In that page there you talk about or rebut Mr. Coppola's
15 proposal that the line clearing expense should reduce
16 from 53 million to 44.6 million. Is that correct?

17 A That is correct.

18 Q Why hasn't or has Consumers Energy spent, or did
19 Consumers Energy spend \$53 million in the prior year on
20 line clearing?

21 A No, it did not.

22 Q O.K. Why hasn't the Company spent the \$53 million for
23 line clearing last year?

24 A The Company does balance its expenses, both O&M and
25 capital, across the utility portfolio. And also the

1 amount that's in rates right now is not at a \$53 million
2 level.

3 Q So has the Company ever spent \$53 million a year in line
4 clearing in the past five years?

5 A Not to my knowledge, no.

6 JUDGE CUMMINS: Actually, Mr. Anderson --
7 I don't mean to interject here, Mr. Moody -- is there a
8 reason why there is a difference for the projected year
9 versus what has historically been spent, that you know
10 of?

11 A Yes. As discussed in both my direct testimony and in my
12 rebuttal testimony, it's for the reliability, the service
13 that we provide to our customers, forestry or the line
14 clearing is an integral part of avoiding outages and
15 having a highly reliable system. So the amount, the
16 53 million as opposed to what's in rates now is what we
17 need to do as a company to trim and clear more miles of
18 our system in order to have a reliable system.

19 JUDGE CUMMINS: And actually that
20 answered my second question, which was whether this was
21 more of a make-up situation, which it seems to be; is
22 that correct?

23 A Based on historic spending, there is some make-up. But
24 we need to get to a cycle length of approximately, an
25 effective clearing cycle of about eight years, which is

1 discussed in my testimony, which will allow us to trim
2 more of our system in order to have a more reliable
3 system.

4 JUDGE CUMMINS: That was the question I
5 had, that went really through your testimony, whether
6 this was actually to make up or catch up, I guess, versus
7 trying to get ahead of the curve. This is actually
8 trying to catch up to where you would like to be at this
9 point?

10 A That's where we need to be going forward as well.

11 JUDGE CUMMINS: O.K. Thank you,
12 Mr. Anderson. Please continue, Mr. Moody.

13 MR. MOODY: Thank you, your Honor.

14 Q (By Mr. Moody): Along that, I guess my questioning, you
15 talk about the DARE model, I believe it's called, in your
16 testimony. Can you explain a little bit what the DARE
17 model is?

18 A The DARE model, which is referenced in my direct
19 testimony, I'd like to find the pages on that. If you
20 reference in my direct testimony on page 5, it discusses
21 what the DARE model is, which is a reliability analysis
22 model that we utilize. It models 28 various reliability
23 programs. And based on the assessment of the status of
24 our electric system and then what we're spending, it
25 predicts the reliability, what the reliability is going

1 to be on a go forward basis.

2 Q Can you, I guess, also give me a definition of what the
3 System Average Interruption Frequency Index is?

4 A Is that SAIFI?

5 Q Yes.

6 A You said system average?

7 Q Yes.

8 A The SAIFI is basically the frequency of outages that
9 appear across Consumers Energy's system, across the
10 entire system. I believe there's an actual definition
11 contained in one of the testimonies, but not in mine. It
12 really deals with the frequency of outages that our
13 customers experience. To put it on kind of a simple
14 term, if the Company has 1.8 million customers, if there
15 were 1.8 million outages, customer outages, it would be a
16 frequency of one.

17 Q All right.

18 A Across the system.

19 Q Now at the top of page 25 -- your rebuttal testimony,
20 sorry.

21 A All right.

22 Q On the top of page 25 you say there is no direct
23 relationship between spending money on line clearing and
24 the System Average Interruption Frequency Index or SAIFI.
25 Do you see that?

1 A On the top of 25?

2 Q That's correct. I think it's the answer to the first
3 question. You say line clearing expenses, or line
4 clearing expense increases do not necessarily improve
5 overall system reliability metrics in direct proportion
6 to the expense. Do you see that?

7 A Uh-huh.

8 Q Is that the same as the SAIFI, saying that?

9 A SAIDI is the System Average Index Duration as opposed to
10 the frequency. But SAIFI is a fundamental part of the
11 SAIDI calculation.

12 Q So if I were to say that there is no direct relationship
13 between spending money on line clearing and SAIFI, is
14 that what you're saying here?

15 A No. There is a direct relationship between spending a
16 sufficient amount of line clearing on a system to
17 positively impact the SAIFI, the frequency, reduce the
18 frequency of outages on the system.

19 Q O.K. So this sentence is just talking about SAIDI,
20 you're saying?

21 A Right.

22 Q So what percent of decrease in -- what percent of
23 decrease in SAIFI will the Company achieve over the next
24 year or two with that 53 million that you're proposing?

25 A As far as a percent decrease, I don't have the percent

1 decrease in frequency with me here.

2 Q All right. Maybe just so I can understand it better, can
3 you explain again the difference between the SAIDI and
4 the SAIFI?

5 A O.K. Let's go to my direct testimony. On the bottom of
6 page 7 of my direct testimony, it's a fairly simple
7 mathematical equation where you take the SAIFI and you
8 multiply it by the CAIDI, which is the Customer Average
9 Induction Duration. So when you take a system frequency
10 and multiply it by a customer duration, the
11 multiplication of those two results in the SAIDI or the
12 System Duration Index.

13 JUDGE CUMMINS: Let's go off the record
14 for just a second.

15 (Brief discussion off the record.)

16 Q (By Mr. Moody): So with the \$53 million that you're
17 proposing to spend in this area of the line clearing,
18 that will then produce a reduction of SAIDI; is that what
19 you're saying?

20 A It'll produce a reduction in SAIDI, but predominately
21 because it's going to influence that SAIFI. And when you
22 lower that, it should lower the SAIFI, it should lower
23 the SAIDI because it's a product.

24 Q So the line, the line clearing will mean less system
25 interruptions I guess you're saying, right?

1 A Right, fewer system interruptions.

2 Q The reason why I just want to make sure I understand
3 again, on that 25, page 25 of rebuttal, I keep making you
4 go back to that.

5 A That's O.K. So again on the top of 25?

6 Q Yes. The answer, I guess I didn't understand your answer
7 that the line clearing expense increases do not
8 necessarily improve overall system reliability metrics.

9 A Which line are you reading?

10 Q I'm sorry. It's the first, actually the first sentence
11 or second sentence of the first answer there.

12 A O.K.

13 JUDGE CUMMINS: For the record, it would
14 be lines 4 through 6 or 7, I believe.

15 MR. MOODY: Thank you, your Honor.

16 A Yes. The nature of that, those two lines there, is
17 explained in my rebuttal. Line clearing expenses don't
18 necessarily improve overall system liability in a direct
19 proportion to the expense, although localized line
20 clearing expenses are highly effective at addressing poor
21 performing areas of the system.

22 I bring your attention down to line 9.
23 Improvements in localized area performance can often be
24 masked in overall system metrics if the size, age,
25 condition and performance of non-maintained areas

1 declines faster.

2 What this response here is stating is
3 that when we do trimming or line clearing in an area, we
4 get very good results in that area. But if the rest of
5 the system we are not addressing in a timely manner, the
6 gains that we have in that localized area aren't
7 recognized across the system because the larger part of
8 the system is degrading faster than what we're doing in
9 the small areas. That's essentially what the discussion
10 was there.

11 Q All right. Then turning back to the DARE model, which
12 you explained earlier, you say that the DARE model only
13 gives a 50 percent probability or confidence level that
14 this SAIFI level will decline if the \$53 million is
15 spent. Is the 50 -- is that true?

16 A Yes. It's a predictive model, and there is a range
17 associated. It's like any model that predicts. It is
18 not precise. There is a range there. But the overall
19 value of the DARE model is to really predict that we are
20 improving our service reliability. That is, is our SAIDI
21 going down? Are our customers being served better? The
22 degree to which it goes down, that's what we're looking
23 for is a trend. It's really about a trend in a
24 predictive improvement.

25 Q So just so I understand, I know you talk a little bit

1 about it in your rebuttal too at page 23, in response to
2 Mr. Coppola's testimony where he criticizes the 50
3 percent.

4 A Sure.

5 Q When you say that in any given year -- I'm trying to get
6 this straight for you.

7 You're spending the \$53 million to get a
8 50 percent confidence level for the DARE model; is that
9 correct?

10 A No. The 53 million is to increase the percentage of our
11 system that we're clearing on an annual basis, and
12 getting to an approximate eight year effective clearing
13 cycle, as opposed to, we're on a much longer cycle right
14 now based on what we have been spending. I don't know --

15 Q O.K. I guess -- I'm sorry, I --

16 A So the 53 million is to ensure that we are having a
17 declining SAIDI or improving our reliability to our
18 customers. But the confidence level isn't really
19 influenced by the \$53 million spent.

20 Q So the confidence level of reaching that goal is
21 50 percent under the DARE model?

22 A Under the DARE model it's basically a 50 percent range
23 that we predict that we will be in. Increasing our tree
24 clearing spending will ensure that we improve reliability
25 for our customers.

1 Q So that's -- I guess that answers that question. So it's
2 a 50 percent probability that by doing the program that
3 you're doing, that you'll, using the DARE model, there's
4 a 50 percent probability that doing what you're doing,
5 that you'll achieve your results of reducing the SAIDI
6 and SAIFI?

7 A The DARE model predicts that we will trend down, but
8 within any given year, whether that is the SAIDI comes in
9 at exactly what the model predicted, what we're saying is
10 it could be 50 percent higher or lower.

11 Q Then --

12 A I think that's explained in my direct somewhere.

13 Q O.K. I just want to make sure. What would -- let's put
14 it this way: In your rebuttal, at page 23, line 12 into
15 13, you say: However, over the long term it is expected
16 that the system performance will trend the DARE model
17 result. I think you might have said this already, but
18 what does that mean?

19 A I'm sorry. It's page what?

20 Q Page 23 of your rebuttal.

21 A Which lines?

22 Q Line 12 and 13, starting with however.

23 A Right. On line 10 there is the explanation similar to
24 what I just stated, in any given year the actual result
25 will fall above the expected value 50 percent of the time

1 or below 50 percent of the time. And it's the next
2 statement that your question is around?

3 Q That's correct.

4 A However, over the long term it is expected that the
5 system performance will trend near the DARE model result.

6 And the trend, what I would ask to draw
7 your attention to really is in page 46 of my direct
8 testimony, which is a prediction. And as I indicated
9 with my hand gesture here (waving hand), which I probably
10 shouldn't do, is that the SAIDI is improving, which is a
11 downward trend. That is, we are, our customers are
12 experiencing fewer outages and/or the duration of them is
13 going down. So that statement there is about the trend
14 that it is headed in the right direction.

15 Q I understand when you criticize Mr. Coppola's testimony
16 on this point, but I didn't understand, it really is,
17 when you say 50 percent probability, it's as if you're
18 flipping a coin. I think 50 percent will be heads, 50
19 percent will be tails that the expected result will come
20 to fruition, right?

21 A The expected result around the 53 million again, what
22 that is about is increasing the number of miles of our
23 system that we would be clearing. And because tree
24 outages are our number one cause of outages,
25 fundamentally clearing more of the system and clearing

1 more of the system in line with the industry, we will
2 improve the reliability to our customers.

3 Q All right. Would you shoot for a higher -- I mean I know
4 you say here the DARE model confidence level is 50
5 percent. Should you be shooting for a DARE model
6 confidence level of 60 or 70 percent?

7 A The confidence level, from my vantage point the
8 confidence level in the DARE model, whether that band
9 is -- if it were a narrower band, that would just say
10 that our confidence model is higher. But independent of
11 the confidence level, it's about the predictive nature,
12 are we improving the reliability of the system and at
13 what rate are we improving it?

14 I guess whether the 50 percent is just
15 that, again on page 46 of my direct testimony, it just
16 says whether we hit that specific data-point in that
17 specific year, we're just saying that we may be 50
18 percent higher or 50 percent lower, because there are so
19 many factors that go into the reliability index,
20 everything from weather and other investments, and
21 whatnot. There's just so many factors. The 50 percent
22 is just the confidence level of hitting that specific
23 value.

24 Q All right. Turning to page 25 of your rebuttal
25 testimony.

1 A O.K.

2 Q At the -- one of your criticisms of Sebastian Coppola's
3 testimony is that he didn't consider industry benchmarks
4 or practices.

5 Is Consumers Energy's expenditures on
6 line clearing, are they consistent with industry
7 benchmarks and practices over the past five years?

8 A Spending levels, I don't have a comparison on spending
9 levels. What we did compare to in benchmarking that is
10 contained both in my direct testimony and in my rebuttal
11 testimony is in regards to the effective clearing cycle
12 for the number of years between, or the number of years
13 that we're out on a circuit and trimming a circuit. So
14 it's more about the frequency that we're going out and
15 performing our work as opposed to benchmarking from a
16 dollar standpoint. Because a dollar, you know, amount
17 standpoint is really influenced by the size of your
18 system and many other things. So it's really about the
19 frequency of being out there, is what we benchmark and
20 reference in here.

21 Q O.K. I guess, maybe this doesn't fit, but is the --
22 going back to that DARE model, is that something that
23 other utilities use too?

24 A The DARE model is a model that we built in-house at
25 Consumers Energy. So they wouldn't be using the DARE

1 model.

2 Q O.K.

3 A I presume they use other predictive models that they
4 either built themselves or purchased.

5 Q Is it common then for a utility to have that same type of
6 50 percent probability of confidence, that the outcome
7 will be --

8 A I don't know. I don't know what others use.

9 Q O.K. In your practice do you go to other utilities to
10 learn how their system clearing, you know, line clearing
11 works?

12 A Yes. We will do benchmarking. In fact, the one study
13 that is referenced in here is a pretty exhaustive study
14 in regards to benchmarking.

15 Q But you don't study how other utilities do their line
16 clearing and what type of models they use?

17 A Well, how they do their line clearing, that is in
18 benchmarking studies.

19 Q O.K.

20 A But the second part of your question is more on what they
21 utilize to predict the impact on overall SAIDI
22 performance. We don't do as much benchmarking on that
23 second piece, no.

24 Q At the top of page 26 of your rebuttal again, you rebut
25 Mr. Coppola's proposal to reduce the expense by a million

1 dollars. Do you see that on the first sentence there?

2 A That is correct.

3 Q Has Consumers Energy hired all the people that it
4 intends -- yes. Has Consumers Energy hired all the
5 people that it anticipates to hire to put this standard
6 in place, this NERC standard?

7 A No, it has not.

8 Q And why is that?

9 A As stated in both my direct and my rebuttal, the timing
10 of that standard when it goes into effect, currently it's
11 sitting with FERC and we anticipate that it will get
12 approved this year, in 2013. We are working, our
13 implementation is in line with our prediction around when
14 that will be finalized.

15 Q When do you expect then to hire all the people you need
16 to implement the NERC, the standard?

17 A Yes, we will hire again based upon a prudent and
18 responsible approach as to when that order, the FERC
19 order, when that becomes final, when the standard becomes
20 final.

21 Q So if it becomes final this year, you'll finish it up
22 this year?

23 A There's typically an implementation period once the
24 standard goes in that then you have a certain period of
25 time, which can vary, as to when you need to be in

1 compliance with the standard. So the timing of hiring
2 the resources that were referenced in there will be based
3 on that.

4 Q And do you know, I mean what do you base your prediction
5 that the NERC standard that we talk about here on page 26
6 will be issued in 2013?

7 A Based on the current status of where it's at in the
8 approval process is basically what's solidifying our
9 confidence that it is going to be this year. But again,
10 it is at -- it is with FERC, and you can't predict with a
11 hundred percent certainty what the timing of that is
12 going to be. But our confidence is high that it's going
13 to be here in 2013.

14 Q How long is the -- what is your expectation of the
15 implementation period for this NERC standard?

16 A I can't say with certainty what that implementation
17 period is going to be.

18 Q Would it be -- is it possible it could be six months or
19 is that too long?

20 A Oh, no. It could be six months, it could be.

21 Q Could it be as long as a year?

22 A I can't say with certainty how long exactly it would be.

23 Q O.K. Looking at your Exhibit 75, A-75.

24 A O.K.

25 Q Can you explain a little bit what this exhibit is

1 presenting or showing?

2 A Yes. This exhibit, A-75, is referenced in accordance
3 with my rebuttal testimony on page 27, which was really
4 to clarify and respond to Mr. Coppola's direct testimony
5 regarding the projects associated with the business
6 services area. The exhibit here that you're referencing
7 is really to clarify in the years '11 through the
8 projected year '14, 2011 through the projected year of
9 2014, the projects that were represented in my original
10 exhibit of my direct testimony. So it was a breakdown to
11 ensure that there was clarity of which years those
12 projects fell in because it appeared that seemed to be
13 the nature of what Mr. Coppola was focussed on.

14 Q Right. For example, if you took the 2014 projected line
15 and start at the top there, the Asset Preservation Non
16 Project, what is the percent probability that you have
17 that these dollars that you quote here will be spent on
18 that particular project, say the Statewide Asset
19 Preservation?

20 A I can't say with certainty what the percent or the
21 probability would be. That line item, Statewide Asset
22 Preservation, is a fairly consistent spend that you can
23 see there, and so is that one? My confidence level would
24 be high that it would be spent because it's consistent
25 changes that are needed across the Company's facility

1 portfolio.

2 Q So if it was -- if the number was closer to the average
3 spend, then you would say you would have a higher
4 confidence level?

5 A Well, that line item is more, you know, an on-going, as
6 opposed to you look in the next group halfway down there,
7 new construction, which those would be specific projects.

8 So back to your question, my confidence
9 level on the Statewide Asset Preservation, that line item
10 is quite high because it's a consistent program as
11 opposed to a specific project in the new construction
12 area.

13 Q So for the new construction, what you were just saying,
14 you have a lower -- Well, what range of probability for
15 example on the Campbell training facility? Or let's go
16 to West Branch, that one is all by itself. For 2013,
17 what would be your kind of range of probability that the
18 6,000 there is about what you spend?

19 A I can't give you a range of probabilities there.

20 Q I mean. 50 percent or do you think it's a hundred
21 percent for sure? Obviously it doesn't sound like it.

22 A That particular project, that six million in 2013, just
23 knowing where we're at on that in our operation, my
24 confidence level would be high. I put it in a high, just
25 kind of high/medium/low, I put it a high category.

1 Q So high would be above 50 percent?

2 A I would say high.

3 MR. MOODY: All right. That's it, your
4 Honor.

5 JUDGE CUMMINS: All right. Any other
6 parties want to cross-examine this witness? Hearing
7 none, any redirect for this witness, Mr. McQuillan?

8 MR. McQUILLAN: No, your Honor. Thank
9 you.

10 JUDGE CUMMINS: O.K. Very well. We have
11 seven exhibits to take up now. These are Exhibits A-12,
12 A-13, A-14, A-15, and also A-73, A-74, and A-75. Any
13 objection to the receipt of these exhibits? Hearing
14 none, those seven exhibits are received into evidence.
15 Mr. Anderson, you may step down.

16 THE WITNESS: Thank you.

17 (The witness was excused.)

18 - - -

19 JUDGE CUMMINS: My understanding is, Mr.
20 McQuillan, you have another witness to call today; is
21 that correct?

22 MR. McQUILLAN: That is correct, your
23 Honor. Are we ready now?

24 JUDGE CUMMINS: Do the parties want to
25 take a quick break and then we'll start in? Does anybody

1 have questions besides Mr. Moody for this witness? This
2 would be Ms. Youngdahl.

3 MR. McQUILLAN: Correct.

4 JUDGE CUMMINS: That being the case, why
5 don't we go ahead and take a ten-minute break, and we'll
6 start in with Ms. Youngdahl and go from there.

7 (At 2:05 p.m., a 10-minute recess was taken.)

8 JUDGE CUMMINS: Back on the record. Mr.
9 McQuillan.

10 MR. McQUILLAN: Thank you, your Honor.
11 Consumers Energy calls Lauren Youngdahl.

12 - - -

13 L A U R E N E . Y O U N G D A H L
14 was called as a witness on behalf of Consumers Energy
15 Company and, having been duly sworn to testify the truth,
16 was examined and testified as follows:

17 JUDGE CUMMINS: Please continue, Mr.
18 McQuillan.

19 DIRECT EXAMINATION

20 Q Good afternoon.

21 A Good afternoon.

22 Q Could you state your name and business address for the
23 record, please.

24 A Lauren E. Youngdahl. And my business address is One
25 Energy Plaza, Jackson, Michigan.

1 Q Did you cause to be prepared in this case direct
2 testimony consisting of a cover page and 22 pages of
3 questions and answers?

4 A Yes.

5 Q Do you have a copy with you today?

6 A I do.

7 Q Do you have any corrections, modifications, or changes to
8 any of the answers to those questions?

9 A No.

10 Q If I were ask you those questions this afternoon, would
11 your answers be the same?

12 A Yes.

13 Q And do you adopt that as your sworn direct testimony in
14 this cause?

15 A I do.

16 Q Did you cause to be prepared Exhibits A-69 and A-70, A-71
17 and A-72 in conjunction with your direct testimony?

18 A Yes.

19 Q And did you cause Exhibits A-69 and A-70 to be revised in
20 conjunction with your rebuttal testimony?

21 A Yes.

22 Q Other than the revisions on those two exhibits, A-69 and
23 A-70 with regards to your rebuttal testimony, do you have
24 a copy of those exhibits with you this afternoon?

25 A I do.

1 Q Do you have any other changes, corrections, or
2 modifications to those exhibits?

3 A No.

4 Q Are those exhibits that correspond to your direct
5 testimony?

6 A Yes.

7 Q Did you also cause to be prepared rebuttal testimony
8 consisting of a cover page and seven pages of questions
9 and answers?

10 A Yes.

11 Q Do you have a copy of that with you this afternoon?

12 A I do.

13 Q Do you have any corrections, modifications, or changes to
14 the answers to those questions?

15 A No.

16 Q If I were to ask you those questions this afternoon would
17 your answers be the same?

18 A Yes.

19 Q Do you adopt that as your sworn rebuttal testimony in
20 this cause?

21 A I do.

22 MR. McQUILLAN: Your Honor, at this time
23 I would move to bind in the direct testimony consisting
24 of a cover page and 22 pages of questions and answers,
25 and rebuttal testimony consisting of a cover page and

1 seven pages of questions and answers, and move the
2 admission of Exhibit A-69 Revised, A-70 Revised, A-71,
3 and A-72, and would tender the witness for
4 cross-examination.

5 JUDGE CUMMINS: Thank you, Mr. McQuillan.
6 Any objection to binding in Ms. Youngdahl's direct and
7 rebuttal testimony? Hearing none, that testimony will be
8 bound into the record.

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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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

DIRECT TESTIMONY
OF
LAUREN E. YOUNGDAHL
ON BEHALF OF
CONSUMERS ENERGY COMPANY

September 2012

LAUREN E. YOUNGDAHL
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1 Q. Please state your name and business address.

2 A. Lauren E. Youngdahl, One Energy Plaza, Jackson, Michigan.

3 Q. By whom are you employed?

4 A. Consumers Energy Company (“Consumers Energy” or the “Company”).

5 Q. In what capacity are you employed?

6 A. I am the Smart Grid Customer Engagement Programs Manager.

7 Q. Please briefly describe your educational background.

8 A. I received a Masters of Business Administration from Michigan State University’ Eli
9 Broad School of Management in 2007; a Bachelors in Marketing from Michigan State
10 University’s Eli Broad School of Business in 2004, and a Bachelors in International
11 Relations from Michigan State University’s James Madison Honors College in 2004.

12 Q. Please describe your business and professional experience.

13 A. I joined Consumers Energy in 2004, working in multiple facets of Energy Distribution
14 and Customer Operations for the next eight years with increasing levels of responsibility.
15 Positions include assignments in Marketing, where I managed the acquisition, retention,
16 and revenue recovery channels for the Appliance Service Plan program. Then I joined
17 the Regulatory Affairs team, managing the relationship between the Company and the
18 Michigan Public Service Commission (“Commission”) on topics related to customer
19 service and operations, Smart Grid, and rate case filings. In 2010, as the Brand Equity
20 Manager, I developed and implemented culture change plans to build brand awareness
21 amongst employees and a communication strategy to create a strong brand externally.
22 This effort led to the development of the Customer Value Initiative. I was the project
23 lead for this initiative that created the foundation for the Company’s strategic direction.

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1 Then, in a supervisory role, I provided oversight to 34 meter readers in the Grand Rapids
2 headquarters, managing the safety culture, labor relations issues, and performance
3 expectations. In March 2012, I assumed responsibility of Smart Grid Customer
4 Engagement Programs.

5 Q. What are your present responsibilities and duties as the Smart Grid Customer
6 Engagement Manager?

7 A. As the Smart Grid Customer Engagement Manager, my responsibilities include
8 developing and implementing programs and services enabled by smart meters, internal
9 and external communications, and employee training.

10 Q. What is the purpose of your testimony?

11 A. The purpose of my testimony is to describe the Company's ongoing Smart
12 Grid/Advanced Metering Infrastructure ("SG/AMI") program. As authorized in the
13 Commission's June 7, 2012, rate Order MPSC Case No. U-16794, the Company is
14 proceeding with Phase 2 smart meter installations. Given that the projected years in this
15 filing are calendar years 2013 and 2014, the Company is requesting:

- 16 • approval of \$60.6 million capital and \$8.1 million in operating and
17 maintenance expenses associated with the Phase 2 installation of 200,000
18 electric meters from January 2013 through December 2013; and
- 19 • approval of \$57.4 million capital expenses associated with the continuance
20 of Phase 2 installations for an additional 200,000 electric smart meters
21 January 2014 through December 2014.

22 My testimony includes the following major components: Program Approach;
23 Discussion of Advanced Metering Infrastructure ("AMI") Installation; Program Costs:
24 Projected Year Capital Expense; Program Costs: Projected Year Operating and
25 Maintenance Expense; Discussion of SG/AMI Program Benefits; Program Business Case

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1 Summary; Discussion of Customer Communications Activities; Customer Smart Meter
2 Opt-Out Proposal; and Summary.

3 Q. Are you sponsoring any exhibits in this case?

4 A. Yes, I am sponsoring the following exhibits:

5 Exhibit A-69 (LEY-1) Summary of Electric and Common Projected
6 Capital For the years 2011-2014

7 Exhibit A-70 (LEY-2) Summary of Projected Electric and Common O&M
8 Expense for the Years 2011-2013

9 Exhibit A-71 (LEY-3) Summary of Business Case Costs and Benefits
10 2007-2032

11 Exhibit A-72 (LEY-4) Smart Meter Opt-Out Proposal - Cost Summary

12 Q. Were these exhibits prepared by you or under your supervision?

13 A. Yes.

14 **Program Approach**

15 Q. Please describe the Company's approach to the SG/AMI Program.

16 A. In 2007, Consumers Energy established a team to better understand AMI and associated
17 Smart Grid technologies and to develop a roadmap of how these technologies could be
18 applied to benefit our customers. The AMI system will include electric smart meters
19 capable of transmitting and receiving summarized energy usage data as well as meter
20 operating "event" data via a two way cellular based communications network. Early on,
21 the team recognized the evolving state of Smart Grid technologies and determined that a
22 methodical and thoughtful approach should be pursued for installation of SG/AMI.

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1 Q. What has Consumers done to collaborate with and apply lessons learned from other
2 utility installations?

3 A. Consumers Energy is constantly monitoring and applying best practices from utilities
4 who have successfully implemented smart meters. Two utilities with strong, national
5 reputations for educating and engaging their customers during the meter installation
6 process are Oklahoma Gas & Electric and San Diego Gas & Electric. Earlier in 2012
7 Consumers Energy met with representatives from these utilities to gain a better
8 understanding of lessons learned that could be refined and applied to customers in our
9 service territory. Key take-aways from these visits include:

- 10 1. Have a vision that employees and customers can understand and unite
11 around.
- 12 2. Establish a 90-day communication/customer touch point plan that
13 includes:
- 14 (a) local outreach in the form of presentations at town councils,
15 businesses, community groups;
- 16 (b) engaging employees as spokespeople at internal and external
17 events;
- 18 (c) sending letters informing customers about the installation process;
- 19 (d) having a dedicated group of call center representatives to handle
20 questions;
- 21 (e) having employees go door-to-door doing quality/customer
22 assurance checks post installation; and
- 23 (f) conducting follow-up surveys to measure awareness and
24 satisfaction of the installation process.
- 25 3. Handle installation issues quickly and apply lessons learned going
26 forward.
- 27 4. Be transparent in all dealings.

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1 **AMI Installation**

2 Q. What is the current status of the Company's SG/AMI program?

3 A. To date, we have completed Phase 1, which focused on validating the technology,
4 confirming customer responses to energy usage programs, and testing the assumptions in
5 the Company's business case. Our primary vendor partners have been chosen through
6 rigorous evaluation and selection activities and performance-based contracts are in place.
7 As authorized by the Commission's June 7, 2012, Order in MPSC Case No. U-16794, we
8 are commencing Phase 2 meter installation including implementing software and IT
9 system changes to provide the system functions required to support the acquisition and
10 installation of smart meters and to accommodate large volumes of meter data and
11 modified business processes. The Company began installing electric smart meters in the
12 Muskegon and greater Grand Rapids area on August 20, 2012. In total, about 1.8 million
13 electric smart meters will be installed during the period of 2012 through 2019. The
14 infrastructure investment of the current SG/AMI program will further enable the
15 modernization of the electric grid, including the addition of distribution system controls
16 and devices.

17 Q. Please describe the Company's plan for SG/AMI installation in 2013 and 2014.

18 A. The Company in 2013 will install 200,000 electric meters, primarily in our Muskegon,
19 Zeeland, and Grand Rapids work headquarter areas at an estimated cost of \$38 million
20 dollars. In 2014, an additional 200,000 smart meters will be installed to complete the
21 smart meter installation in the Grand Rapids area at an estimated cost of another
22 \$38 million. The meter installations will be accomplished using primarily contracted
23 resources supported by the Company employees when necessary. The smart meters

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1 installed, coupled with the systems functions scheduled to be implemented in December
2 of 2012, will allow the Company and our customers to begin realizing the initial benefits
3 of the SG/AMI Program early in 2013. The initial benefits to be realized include:

- 4 1. Reduced meter reading operating expenses, including costs associated
5 with obtaining meter reads, meter reader handheld devices, vehicle
6 mileage reimbursement, supervision, and administrative costs.
- 7 2. Improved meter read accuracy/reduced number of estimated bills. For
8 customers with smart meters installed, satisfaction is improved as
9 estimated meter reads are reduced to 1% or less. This will reduce the
10 number of estimated bill related customer inquiries to the Company's call
11 center. A reduction in "special" field trips to obtain actual meter reads is
12 also anticipated.
- 13 3. Improved theft identification and an overall reduction in energy theft will
14 result through observation as we visit every electric premise to exchange
15 the meter. Later, in 2014, this benefit will increase as we support the
16 capture and processing of meter tamper alarms.
- 17 4. Increased customer access to detailed energy usage web portal/energy
18 efficiency services. In 2013, customers with smart meters will have
19 access to a web portal that provides hourly energy usage information and
20 energy conservation related services.
- 21 5. Customers with smart meters will be able to select their own billing due
22 date when enrolling in the Company's existing e-billing program.

23 In mid-2013 another systems implementation will occur enabling additional
24 operating and customer benefits, including the AMI enabled Direct Load Administration
25 ("DLA") program. The program allows customers to collectively reduce electricity costs
26 by reducing the overall peak demand on the electric grid. Load management saves
27 money for both the Company and its customers by reducing the need for generation
28 capacity and minimizing the amount of energy the Company must purchase on the open
29 market at peak demand periods. Customers who participated in the 2010 pilot DLA

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1 program experienced energy and monetary savings via a reduction in their energy usage
2 cost.

3 An additional systems implementation is scheduled for late 2013 that will enable
4 key operating improvements that will begin to be realized in early 2014, supporting:

- 5 1. Improved outage management and reduction in outage times as AMI
6 meter outage event and restoration data are made available to the
7 Company's outage management systems.
- 8 2. Smart meter enabled remote services will result in a reduced number of
9 field trips which supports reduced operating costs and faster response to
10 customer requests (e.g. remote power reconnects).
- 11 3. Increased theft benefits over those to be realized in early 2013. This
12 system implementation will support the capture of meter tamper alarms
13 contributing additional theft benefits.

14 Systems implementations planned for 2014 will provide customers with programs
15 to choose from that will reduce their overall energy consumption and reduce customer
16 and Company costs. Dynamic Pricing Programs similar to the programs tested and
17 confirmed during the Phase 1 pilot, will be offered to residential, commercial, and
18 industrial customers. Other programs currently being considered are discussed further in
19 this testimony and include:

- 20 • **Home Energy Management** – which utilizes the electric consumption
21 data that is accessible from the smart meter, customers may choose to
22 have the ability to access information on energy usage patterns to be better
23 informed on what influences their energy costs.
- 24 • **Pay As You Go** – through different payment options customers will be
25 able to purchase power ahead of consumption.
- 26 • **Interruptible Load** – targeting customers with sufficient loads available
27 for reduction the addition of smart meter energy consumption data is
28 anticipated to enhance this existing program.
- 29 • **Building Management Systems Integration** – targeting commercial and
30 industrial (“C&I”) customers smart meter data will be integrated into

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1 existing and new energy building management systems to lower energy
2 consumption and cost.

3 Q. Is the Company planning to conduct any pilot programs in 2013 and 2014?

4 A. Yes. Although specific pilot program details are not yet finalized, Consumers Energy is
5 planning to test customer responses and the operational requirements to support:

- 6 • **Residential Customer Pay As You Go (Prepay):** The Company is
7 proposing to contract with a third party provider for a pilot beginning the
8 first quarter of 2014 of energy prepay services to test customer acceptance
9 and satisfaction, operational requirements, and the costs associated with
10 providing all residential smart meter customers with this option later in
11 2014. Pilot design, test and implementation activities will occur in 2013.
12 This pilot will allow customers to purchase blocks of energy, allowing for
13 enhanced self-management of their energy consumption.

- 14 • **Commercial and Industrial Demand Response Programs:** The pilot
15 will be offered to a sub set of our current MV-90 metered customers to test
16 various time of use rates for C&I accounts. Interviews conducted on the
17 Company's behalf by the Boston Consulting Group indicate that 15% of
18 commercial customers and 10% of industrial customers are interested in
19 participating in time of use rate structures. The pilot will confirm
20 customer acceptance and satisfaction, operational requirements and the
21 cost associated with providing smart meter based programs to a larger
22 C&I group beginning in 2014.

23 **Program costs: Projected Year Capital Expense**

24 Q. Please describe Exhibit A-69 (LEY-1), Summary of Electric & Common Projected
25 Capital for the Smart Grid Program For the years 2011-2014.

26 A. This Exhibit presents the electric capital projected expenditures for the Smart Grid
27 Program, totaling \$60.6 million in 2013 and \$57.4 million in 2014. The expenditures are
28 categorized into five cost categories: (1) Field Equipment/Facilities; (2) Meters;
29 (3) Software/Systems Development; (4) Smart Grid Infrastructure and (5) Program
30 Engineering, Design and Management. For each of the activities, the capital expenditure
31 is shown for calendar year 2011 actual, 2012 actual/projected, 2013 projected, and
32 2014 projected.

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1 Q. What do each of the categories listed in this Exhibit represent?

2 A. **Line 1:** Field Equipment/Facilities, refers to the \$6.4 million in funding for 2013 and
3 \$7.0 million in 2014. The largest component of cost in this line item is for the purchase
4 of devices for the Company's AMI enabled direct load administration program. This line
5 item also supports upgrades as needed in our electric meter shop for smart meter testing
6 and new field tools needed by our crews to support and diagnose problems with advanced
7 electric meters.

8 **Line 2:** Meters \$38.1 million, are the costs in 2013 for the purchase and
9 installation of the electric smart meters needed to support the Phase 2 deployment. In
10 2014 our estimated costs for the purchase and installation of electric smart meters is
11 \$38.2 million.

12 **Line 3:** Software/Systems Development refers to the \$8.2 million in funding in
13 2013 and \$4.1 million in 2014. In late 2012, we plan to implement those systems
14 functions required to support the smart electric meter customer billing functions and to
15 reduce the number of estimated bills. Systems implementations planned for 2013 will
16 enable the AMI DLA program and enable key operational benefits based primarily on
17 reductions in "truck rolls." In 2014 planned systems expenditures will support a variety
18 of AMI enabled residential, commercial, and industrial customer programs.

19 **Line 4:** Smart Grid (IT) Infrastructure costs are for the computing and data
20 network communications equipment needed to support AMI installation and operations.
21 The Smart Grid Infrastructure supports Phase 2 activities by providing the needed
22 communication head end equipment, the hardware and installation of the meter data
23 management system, as well as, technical environments that provide for application and

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1 security testing and disaster recovery backup capabilities. The 2013 costs are
2 \$0.6 million with \$1.4 million projected to be spent in 2014, as the majority of the needed
3 computing hardware and communications components have been acquired in prior years.

4 **Line 5:** Program Engineering, Design, and Management are costs associated with
5 advanced meter installation activities and also include general program management
6 costs and are projected to be \$7.3million in 2013 and \$6.6M in 2014.

7 **Program Costs: Projected Year Operating and Maintenance Expense**

8 Q. Please describe Exhibit A-70 (LEY-2), Summary of Projected Electric & Common O&M
9 Expense for the Years 2011-2013.

10 A. This Exhibit presents the O&M expenditures for the Smart Grid Program, totaling
11 \$8.1 million in 2013. The expenditures are categorized in four cost groups: (1) Project
12 Management & Other Common; (2) Deployment & Meter; (3) Operations; and
13 (4) Communications and Customer Programs.

14 For each of the activities, the O&M expenditure is shown for calendar years
15 2011-2013. Page 1 shows total amounts for each of the years listed while page 2 shows
16 total amounts for each of the years listed, plus the year-to-year change in O&M
17 expenditure.

18 Q. What do each of the categories listed in the exhibit represent?

19 A. **Line 1:** Project Management & Other Common includes items such as program staffing,
20 professional services and associated expenses, hardware and software maintenance and
21 employee engagement and training. This expenditure is projected to be \$1.8 million in
22 2013.

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1 **Line 2:** Deployment & Meter is projected to cost \$1.6 million in 2013, includes
2 funding for a portion of the deployment team staffing, professional services, incremental
3 overall maintenance costs and the back haul costs for communication of the data from the
4 electric smart meter to the AMI system.

5 **Line 3:** Operations O&M includes the staffing and ongoing operation of the AMI
6 system. Functions include monitoring to ensure the meter data is received as planned and
7 validated, responding to certain high priority meter events and alarms, monitor and
8 maintain AMI end-to-end security. These activities are projected to be \$0.8 million for
9 2013.

10 **Line 4:** Communications and Customer Programs are projected to total
11 \$4.0 million in 2013. During 2013 these costs support the customer recruitment and
12 management of the direct load administration and customer engagement (web portal)
13 activities. They also support early program design for the dynamic pricing programs to
14 be offered beginning in 2014.

15 **Discussion of SG/AMI Program Benefits**

16 Q. Please identify the categories of benefits associated with SG/AMI Programs in general.

17 A. The Edison Foundation: Institute for Energy Efficiency¹ identifies three major categories
18 of SG/AMI Program benefits:

- 19 • **Customer benefits** arise from engagement in energy management driven
20 by information and/or price signals, which leads to electricity usage
21 reduction or load shifting and the opportunity to lower bills or mitigate
22 cost increases.
- 23 • Operational benefits allow the utility to deliver more reliable service, rapid
24 remote (service) connection, and better outage detection and recovery to
25 its entire customer base at a lower overall cost.

¹ *IEE Whitepaper July 2011*, The Edison Foundation: Institute for Electric Efficiency, prepared by The Brattle Group, http://www.edisonfoundation.net/iee/Documents/IEE_BenefitsofSmartMeters_Final.pdf

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- 1 • Societal benefits arise from demand response and direct load control,
2 enabling reduction of peak generation, thereby applying downward
3 pressure on energy prices in spot markets, offsetting the need for new
4 generation and transmission and distribution (“T&D”) capacity, and
5 potentially lowering carbon emissions through integration of cleaner
6 distributed generation and household usage reduction.

7 Q. Can you describe examples of the types of the new programs that SG/AMI will enable in
8 the future for residential and small commercial customers?

9 A. Based on customer’s wants and needs, industry benchmarking, and the Company’s
10 learnings to date, the following is a potential portfolio of optional programs customers
11 may choose to participate in that are enabled by SG/AMI that may be offered in the
12 future.

- 13 • **Home Energy Management** – Utilizing the electric consumption data
14 that is accessible from the smart meter, customers will have the ability to
15 access information on energy use patterns to be better informed on what
16 drives their energy costs. Based on the data, customers will be able to
17 make informed decisions about their individual energy usage and
18 conservation. Examples of enabling technologies that customers will be
19 able to utilize, based on their preference, include web energy portals, in
20 home displays, programmable communicating thermostats, and mobile
21 applications.

22 Of note, the Smart Grid enabled web portal will expand upon the existing
23 Energy Efficiency Home Energy Reports program. By adding this
24 additional information customers will gain insights through access to
25 hourly interval consumption data. The additional analytics will allow the
26 program to reach additional customers with timely energy efficiency
27 messaging, including AMI-enabled insights, and generate substantial,
28 cost-effective electricity savings.

- 29 • **Direct Load Administration** – This is a program offered by Consumers
30 Energy to smart meter customers who have central air conditioning to
31 qualify for a lower energy rate. The program allows customers to reduce
32 their electricity costs by contributing to reductions in the overall peak
33 demand on the electric grid. By reducing overall peak demand in the
34 summer months, the Company can reduce future capacity requirements
35 and costs which benefit all customers.

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1 A small device (switch) is installed near participant's outdoor
2 central air conditioner. During a limited number of peak demand periods
3 in the summer, the device is activated to adjust the cycling time of the air
4 conditioner's compressor.

- 5 • **Pay As You Go Program** – Through different mediums, customers would
6 have the ability to purchase power ahead of consumption. Customers with
7 smart meters are provided access to their consumption data through the
8 Smart Grid networks to provide near real-time information on total
9 consumption, rate of consumption and predictive tools on current balance.
10 This data provides customers the ability to choose, control, and manage
11 their energy bill. The system employs various technologies (web portal, in
12 home display, etc.) or customer reporting (hard copy, email) that may be
13 leveraged to provide customers access to their balances. The offering is
14 anticipated to use existing rate categories and potential new rates, as they
15 are identified, for improving customer value.
- 16 • **Dynamic Pricing Programs** – Consumers Energy customers with smart
17 meters may enroll in critical peak pricing rates to better manage their
18 energy use by taking advantage of lower rates during off peak and
19 non-critical peak periods. The program provides customers the
20 opportunity to manage their energy costs with new technology, better
21 information, and advanced tools. Customers are notified in advance when
22 a critical peak event is to be declared and are incented via a rebate on their
23 bill to reduce their electricity usage during the event.
- 24 • **Customer Selected Bill Due Date** – Smart meters provide the ability to
25 read customer energy consumption data each day rather than the current
26 monthly read process, customers with smart meters will be able to select
27 their preference for when their energy bill is due. Through the smart
28 meter network, data can be accessed as required to create a customer's bill
29 on the requested date. This option would require enrollment in the
30 utility's existing e-commerce programs for electronic billing.

31 Q. How do C&I customers benefit from the SG/AMI investments?

32 A. All customers benefit in the Company's anticipated SG/AMI enabled operating and cost
33 benefits, as well as the societal benefits. Additionally, several C&I customer programs
34 are being evaluated including:

- 35 • **Direct Load Management** – A rate based program offered by Consumers
36 Energy to its customers with smart meters, receiving for bill credits by
37 allowing Consumers to cycle electric loads (e.g., central air conditioners)
38 during high demand periods. The program provides for customers to

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1 reduce their electricity costs by reducing the overall peak demand on the
2 electric grid. By reducing peak demand, the Company can reduce future
3 capacity costs which benefit all customers.

- 4 • **Dynamic Pricing** – Consumers Energy customers with smart meters may
5 enroll in critical peak pricing rates to better manage their energy use by
6 taking advantage of lower rates during off peak and non-critical peak
7 periods. The program provides customers the opportunity to manage their
8 energy costs with new technology, better information, and advanced tools.
9 Customers are notified in advance when a critical peak event is to be
10 declared and are incented via a rebate on their bill to reduce their
11 electricity usage during the event.
- 12 • **Interruptible Load** – For customers with sufficient loads available for
13 reduction (currently ≥ 1 MW), the Electric Interruption rate is available for
14 customer opportunity to reduce cost. Through Smart Grid, the program
15 can be enhanced to better facilitate the program through providing
16 additional data to the customer and Consumers Energy to manage events.
17 Coupled with building management systems, customer response to events
18 can be automated to the required response time and the amount of load
19 reduction can be acquired more efficiently for customer savings and load
20 reduction impact.
- 21 • **Data Analytics** – Through additional energy consumption data, customers
22 will have the ability to analyze their energy usage against their operations.
23 The new data source will enable predictive billing as defined by the
24 customer, Operational load studies/management (opportunity to be further
25 supported by customers sub-metering), and customer directed account
26 aggregation.
- 27 • **Building Management Systems Integration** – Leveraging standards
28 being developed by the Open ADR Alliance and the University of
29 California-Berkley, Smart Grid data can be integrated into customer
30 energy management systems to control processes to impact customer
31 saving. Many of our C&I customers have systems already in place with
32 only slight upgrades required to leverage the Smart Grid system.

33 **Program Business Case Summary**

- 34 Q. What are the results of the most recent update to the SG/AMI business case and the key
35 benefit categories?
- 36 A. The SG/AMI business case analysis was updated in March of 2012 (Exhibit A-71,
37 LEY-3, Summary of Business Case Costs and Benefits 2007-2032) with the result

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1 indicating a 20 year positive net present value of \$42 million for the overall program.

2 The updated business case includes final vendor pricing for meters, associated
3 components, and vendor services, adjustments for the current Phase 2 meter installation
4 plan and the updated schedule of benefit enabling systems deliverables. Costs for the
5 anticipated IT infrastructure were re-assessed and reduced. We continue to confirm
6 business case benefits and are preparing to include operating department budget
7 reductions in the corporate five-year financial plan as program benefits are realized. Key
8 benefit categories include:

- 9 • **Customer Programs:** Representing 35% of the total benefits, this
10 category summarizes our planned DLA, Dynamic Pricing demand
11 response customer programs, and a moderate reduction in energy usage
12 due to customer energy conservation. Benefits to customers are realized
13 by a lower Power Supply Cost Recovery (“PSCR”) factor enabled by
14 reduced capacity requirements during “critical peak” conditions.
15 Customers may benefit further if they chose to reduce energy usage,
16 lowering their individual energy bill and conserving energy based upon
17 additional and timelier energy usage information.
- 18 • **Energy Theft:** Representing 22% of total benefits, smart meters provide
19 advanced energy theft detection capabilities. The Company and our
20 customers benefit when energy theft is detected and addressed.
- 21 • **Meter Reading:** Reductions in the cost of manual meter reading
22 represent 19% of total benefits. The Company and our customers benefit
23 in reduced operating costs and, with actual meter read rates at 99%+, the
24 near elimination of estimated bills.
- 25 • **Other O&M and Avoided Capital:** Another 17% of identified benefits
26 are tied to remote access to smart meter data and smart meter operational
27 notification functions including low voltage, power loss, and power
28 restoration. The primary O&M benefits in this category are reductions in
29 the number of field visits (“truck rolls”) by operating employees for
30 trouble calls. Customers also will benefit from an anticipated reduction in
31 outage restoration times, based on the utility receiving immediate and
32 more specific outage and service quality notifications. Avoided capital
33 benefits include the elimination of planned capital expenditures for meter
34 reader devices and mechanical meters which will no longer be required.

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- 1 • **Terminal Value:** At 7% of total benefits, this category captures the value
2 of the investment beyond the end date of the business case analysis. Our
3 business case ends in 2032 however meters installed in 2013-2019 with a
4 20-year life accrue benefits beyond 2032.

5 Q. Please describe the business case capital costs as presented in Exhibit A-71 (LEY-3).

6 A. This business case includes key impact cost and benefit categories. Estimated total
7 program capital costs 2007-2019 are \$750 million (page 1, Line 32, column (o)) and
8 include Line 19: Electric Smart Meter Purchases, including Set & Test; Line 20: Field
9 Equipment/Facilities; Line 21: Software/Systems Development; Line 22: Smart Grid
10 Infrastructure (IT), Line 23: Project Prep & Project Management costs.

11 Q. In previous electric rate cases there has been discussion regarding the adequacy of the
12 Program's contingency amount in the business case model. Does the SG/AMI business
13 case contain an amount for total program contingency?

14 A. Yes, previous business cases included amounts for program contingency as does the
15 current business case. Overall program contingency in the most recent business case
16 analysis for modeling purposes is included in Line 19: Electric Meter/Gas Module
17 Purchases.

18 Q. What are the O&M costs for the business case contained in Exhibit A-71 (LEY-3)?

19 A. O&M Program costs (page 3, sum of Lines 77-82, 2007-2019) are expected to be
20 \$150 million and include costs associated with dynamic pricing, load management
21 programs, and project management. This also includes costs associated with meters, gas
22 modules, property taxes, data backhaul charges and other common O&M costs, including
23 software and hardware maintenance and the operational support for installed devices.

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1 Q. What are the business case benefits for avoided Capital and O&M costs contained in
2 Exhibit A-71 (LEY-3)?

3 A. Program benefits include operational and customer benefits, as well as reductions in
4 planned capital expenditures. Benefits associated with avoided capital costs are
5 identified on pages 1 and 2, Line 25 representing the estimated cost avoidance of both
6 conventional meters and meter reader handheld devices.

7 O&M benefits are identified on pages 3 and 4, Lines 64 through 75. Operational
8 benefits include savings in:

- 9 • meter reading;
- 10 • expenses associated with uncollectable accounts;
- 11 • costs associated with theft detection and response;
- 12 • customer program benefits and conservation;
- 13 • property tax savings on existing meters; and
- 14 • other operating benefits which are primarily associated with reductions in
15 the number of required employee field trips.

16 Customer benefits identified as conservation and energy efficiency are related to
17 the availability of near real time usage information (Line 70), participation in the load
18 management program (Line 67) and participation in demand response/time of use pricing
19 programs (Line 68).

20 There is also a benefit for terminal value (Line 75), which represents the value of
21 the investment beyond the end date of the business case (2032).

22 The business case analysis includes benefits as confirmed by the Phase 1 pilot
23 results. Remote metering and meter event capabilities (reading, voltage monitoring,
24 outage identification, service restoration notification, etc.) will facilitate O&M cost

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1 reductions and support efficiency improvements including optimization of customer care,
2 billing, and payment. Business operations will benefit from improved employee safety,
3 reduced operating expenses, and avoided capital. Customer benefits include a reduction
4 in estimated bills, reduced outage restoration times, and enhanced opportunities for
5 energy consumption management.

6 **Customer Communications Activities**

7 Q. What types of communication activities do you have planned to make sure customers
8 know they are getting a smart meter and the benefits that are enabled by smart meters?

9 A. Successful implementation includes building customer awareness around Smart Grid
10 benefits, increasing participation in energy efficiency and value-add offerings, and
11 helping foster positive attitudes and advocacy toward Consumers Energy. Smart Grid
12 Customer Engagement will carry strong brand messages and will rely on three primary
13 communication strategies:

- 14 1) General Consumers Energy brand and Smart Grid awareness for
15 customers statewide: The Company recently completed segmentation
16 work that identifies and categorizes the wants and needs of customers into
17 segments. As a result of this study, eight segments were identified for
18 residential customers and five segments identified for C&I customers.
19 This information will help us provide information and tailor messages
20 based upon customers' preferences. This segmentation work was used for
21 communicating about Smart Grid.
- 22 2) Targeted community campaigns (by segment) prior to and during specific
23 roll-out waves: We are proactively informing, educating and engaging
24 audiences in the Muskegon, Zeeland, Grand Rapids, and Allegan area –
25 well ahead of planned smart meter installations – to generate awareness of
26 the activities and benefits associated with smart meters. The approach is
27 founded in grassroots activities. We have identified neighborhood
28 associations, faith-based organizations, local service organizations,
29 business groups, and local government and are conducting face-to-face
30 presentations to help ensure the community understands our program,
31 address any questions or concerns, and incorporate their insights and
32 feedback into refining our approach. Additionally, to showcase immediate
33 value, we are driving customer understanding of, and traffic to, the

LAUREN E. YOUNGDAHL
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1 OPower utility customer consumption data web portal (expected to be
2 available in 2013) to cultivate the realization of smart meter benefits,
3 including leveraging personalized insights and calls to action to make
4 informed, cost-conscious energy choices.

- 5 3) Strong employee awareness, understanding, and advocacy throughout the
6 state: Employees who live in the Phase 2 installation area will receive
7 smart meters first. It is important that employees experience the benefits
8 that smart meters bring so they can be a resource for their family, friends,
9 and neighbors, and advocates for the program.

10 The customer communications plan includes a 90 day planned series of touch
11 points:

Customer Communications



Pre-Installation	During Installation	Post-Installation
<ul style="list-style-type: none"> • Smart Energy community presentations • Direct mail campaign • Various channels ready (e.g. website, brochures, video, etc.) • Employees aware & ready • Attitude Survey I 	<ul style="list-style-type: none"> • Dedicated Call Center team • Customer quality assurance home visits • Door Hangers upon install 	<ul style="list-style-type: none"> • Attitude Survey II (2 weeks post install) • Focus Group • Attitude Survey III (Q1 2013)

Customer Smart Meter Opt-Out Proposal

12 Q. Does Consumers Energy intend to allow customers to Opt-Out of having a smart meter?

13 A. Yes. The Commission issued an Order on September 11, 2012, in MPSC Case No.
14 U-17000 which directs the Company to make available an Opt-Out option based on
15 cost-of-service principles, for its AMI customers. As discussed in Consumers Energy's
16 response to MPSC Case No. U-17000, to realize the various benefits and opportunities

LAUREN E. YOUNGDAHL
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1 associated with smart meters, the Company encourages all customers to allow the
2 installation of a fully functional smart meter. For customers who decide they do not want
3 a smart meter, the Company proposes to provide them with the option to retain their
4 existing meter equipment subject to a tariff-based maintenance charge to cover the cost of
5 maintaining and testing the existing equipment and obtaining monthly meter readings.
6 Further discussion of the electric tariff is discussed in Company witness Stephen P.
7 Stubleski's testimony.

8 Q. Please discuss the cost-of-service principles for the proposed customer Opt-Out charges.

9 A. As detailed in Exhibit A-72 (LEY-4), Smart Meter Opt-Out Proposal – Cost Summary,
10 the Company anticipates that both additional up-front and on-going operating costs will
11 be incurred when customers retain their existing metering equipment.

- 12 • **Up-front costs:** include the creation and maintenance of a legacy meter
13 inventory, smart meter installation exception processes, and supporting
14 systems modifications, customer support labor, purchase and support of
15 additional meter reader handheld devices and the initial install or
16 reinstallation of the standard smart meter when the customer terminates
17 service at a premise.

18 The timing of when a customer declares their intent to Opt-Out of
19 a smart meter installation will impact the up-front costs. If a smart meter
20 already exists on the customer's premise additional costs will be incurred
21 by the Company to remove the smart meter and replace it with a legacy
22 meter. These additional costs are summarized in the up-front costs
23 section of Exhibit A-72 (LEY-4).

- 24 • **Ongoing costs:** Consumers Energy will incur monthly costs to enable and
25 support the non-standard metering alternative when a customer chooses to
26 retain their existing metering equipment (analog/solid state). Monthly
27 costs include labor to manually read meters and costs to support meter
28 reading, ongoing systems modifications, and the annual meter-testing
29 program for legacy meters.

LAUREN E. YOUNGDAHL
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1 Q. Does an Opt-Out program impact the SG/AMI business case?

2 A. Some expenses that were anticipated to be reduced or eliminated with the installation of
3 smart meters will still exist. However, given the relatively small number of customers
4 projected to Opt-Out (1% - 2%) and assuming approval of an Opt-Out tariff that is cost of
5 service based, the business case is not appreciably impacted.

6 **Summary**

7 Q. Why are customers better off if the Company makes investments in SG/AMI?

8 A. All customers will benefit from reduced utility operational costs as well as overall
9 societal benefits. Additionally, customers will have opportunities to benefit from access
10 to new energy usage information and tools, new billing options, and a variety of new
11 programs they may choose from that are enabled by the investment in SG/AMI. Recently
12 the Company has engaged in activities to better segment and observe our customer base,
13 both residential and business. The purpose is to better understand the important ways in
14 which needs and wants vary, and how the drivers of satisfaction change for each
15 customer segment. Using both quantitative and qualitative research and analysis, the
16 Company will be able to target more precise messages, identify the most effective
17 communications channels, and develop the SG/AMI enabled core service offerings that
18 customers desire.

19 Q. On what basis are these expenses concluded to be reasonable and appropriate?

20 A. We believe that our various collaborations, standards development involvement and
21 measured approach for testing, pilot and advanced meter installation has been the right
22 approach, as it mitigates the risk associated with installation of newer technologies. We
23 are enhancing the functions of core IT systems, testing meters and equipment for

LAUREN E. YOUNGDAHL
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1 functionality, quality, and adherence to the security and interoperability standards, and
2 validating that the system, once installed, will work as designed. The step-by-step
3 implementation, minimizing up-front costs as much as possible while completing robust
4 testing was chosen to ensure that the investment choices will produce customer benefits
5 over a time horizon of twenty years or more. The most recent business case update as
6 discussed indicates a positive net present value for the program going forward. As such,
7 we believe the expenses as presented in this testimony to be reasonable and prudent.

8 Q. Does this conclude your testimony regarding the Smart Grid Program?

9 A. Yes, it does.

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 generation and distribution of)
 electricity and for other relief.)
 _____)

Case No. U-17087

REBUTTAL TESTIMONY

OF

LAUREN E. YOUNGDAHL

ON BEHALF OF

CONSUMERS ENERGY COMPANY

March 2013

LAUREN E. YOUNGDAHL
REBUTTAL TESTIMONY

1 Q. Please state your name and business address.

2 A. My name is Lauren E. Youngdahl, and my business address is One Energy Plaza,
3 Jackson, Michigan.

4 Q. Are you the same Lauren E. Youngdahl who presented direct testimony in this case
5 regarding Consumers Energy Company's ("Consumers Energy" or the "Company")
6 Smart Energy/Advanced Metering Infrastructure Program?

7 A. Yes.

8 Q. What is the purpose of your rebuttal testimony in this proceeding?

9 A. The purpose of my testimony is to respond to the Michigan Public Service Commission
10 ("MPSC") Staff's and the Attorney General's testimony regarding the Company's Smart
11 Energy Program.

12 Q. Are you sponsoring any exhibits?

13 A. Yes. I am sponsoring Exhibit A-69 (LEY-1) Revised, Summary of Electric & Common
14 Projected Capital and Exhibit A-70 (LEY-2) Revised, Summary of Projected Electric &
15 Common O&M Expense.

16 **PROJECTED TEST YEAR CAPITAL INVESTMENTS**

17 Q. On pages 7 and 8 of Staff witness Nicholas Evans' testimony he recommends
18 disallowance of \$2.884 million for the cost of DLA devices. Do you agree?

19 A. As referenced throughout our audit and discovery responses, the Company has extended
20 delivery of the initial smart meter billing release to allow for additional integration testing
21 ensuring billing quality. As a result, this has also extended delivery of customer
22 programs such as Critical Peak Pricing and Direct Load Management which are
23 contingent upon a successful billing release. As such, the Company accepts the

LAUREN E. YOUNGDAHL
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1 disallowance in the associated expenditures within the context of this general rate case
2 proceeding. The Company plans to file for recovery of the deferred costs during the next
3 general electric rate case proceeding based on the Company's actual experience.
4 Exhibit A-69 (LEY-1) has been revised to reflect our agreement with Mr. Evans'
5 proposed disallowance.

6 Q. On pages 7 and 8 of Mr. Evans' testimony he recommends disallowance of
7 \$7.539 million in contingency costs. Do you agree?

8 A. The Company does not agree with this recommendation. As stated above and subsequent
9 to the filing of this case, the Company determined that additional integration testing was
10 necessary resulting in the delay of the smart meter billing release. The smart energy
11 billing release represents the foundational platform upon which all future customer and
12 operational programs and features will be built upon. Given the significance of this
13 billing platform, it was determined that additional integrated testing to ensure billing
14 quality was necessary prior to "go live." Contingency dollars were included in the
15 original Company projections because costs for program systems requirements were not
16 yet available and not incorporated into the original 2013 projected costs as a specific line
17 item. The contingency dollars previously identified as projections have now been
18 identified as known costs associated with the additional integrated testing and quality
19 assurance work. Therefore, we believe these costs to be reasonable and prudent, and will
20 actually be incurred, fitting Mr. Evans' definition of recoverable costs. Exhibit A-69
21 (LEY-1) has been revised to reflect the additional software development costs, offset by
22 reduction in contingency estimates.

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REBUTTAL TESTIMONY

1 Q. Will this updated projection result in an increased total capital investment for the
2 program?

3 A. No, while this updated projection will result in exceeding the contingency funding
4 amount for 2013, it has no impact on the projected lifetime project investment which
5 remains unchanged at \$750MM.

6 Q. How have these updated costs been determined?

7 A. The updated costs represent known costs associated with signed contracts from all
8 vendors working on the delivery of the billing release, including those associated with the
9 Systems Integrator ("SI").

10 Q. Please describe the reasons for these changes and the Company's decision to partner with
11 a SI?

12 A. System functions originally planned to be delivered in December 2012 were delayed and
13 are currently scheduled to be delivered in April 2013 (Billing) and June 2013 (Customer
14 Web Portal), respectively. Through our continuing smart energy best practice research
15 and the recent system enhancement to implement SAP's CRM7 software, we have
16 learned:

- 17 • Increased involvement from business groups in all aspects of systems
18 development lifecycle is necessary to ensure a quality implementation.
- 19 • Comprehensive testing and validation is necessary and can still be
20 accomplished with an aggressive implementation schedule.
- 21 • An increased emphasis on release management and integrated planning –
22 coordinated plans for systems change activities along with business change
23 management readiness and alignment across all Company project.

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REBUTTAL TESTIMONY

1 Those lessons learned led to recognition of the need for a SI to assist with systems
2 delivery. A SI brings experience with implementing advanced metering infrastructure
3 (“AMI”) systems and integrating with existing software applications. A SI also provides
4 expertise in a wide variety of roles and will work with Consumers Energy with the
5 objective of accelerating and optimizing both customer and operational benefits. In
6 summary, the additional systems integration testing and the partnering with the SI will
7 lead to a more effective implementation and a positive customer experience.

8 **OPERATIONS AND MAINTENANCE (“O&M”) EXPENSE SUMMARY**

9 Q. On page 13, Mr. Evans is recommending downward adjustments to 2013 O&M expenses
10 of \$1.163 million. Do you agree?

11 A. Similar to the response above for capital expenditures, the Company does not expect a
12 reduction in O&M expenses from the test year projection. While the Company has
13 extended the timeframe for development of the initial smart meter billing release, it does
14 not expect to reduce its smart meter/advanced metering infrastructure O&M expenses.
15 The Company expects that the need for additional technical resources to support the
16 initial smart meter billing release will exceed the test year estimates by approximately
17 \$1.163 million, offset in part by delays in programs that had been included in the
18 Company’s test year estimate. Exhibit A-70 (LEY-2) has been revised to reflect the shift
19 of expected costs from customer programs to billing release ‘go-live’ system support
20 costs.

LAUREN E. YOUNGDAHL
REBUTTAL TESTIMONY

1 **OPT-OUT TARIFF**

2 Q. On page 5 of Staff witness Poornima Jayasheela’s testimony she recommended a
3 reduction in the ongoing monthly opt-out charge from \$11.12 to \$9.72 per month. Do
4 you agree?

5 A. Yes, the Company accepts the Staff’s recommendation.

6 Q. Exhibit S-6, Schedule F-5, page 1 of 4 of Ms. Jayasheela’s exhibits, she recommends
7 various changes to the AMI opt-out provision, or as proposed by Staff, the
8 non-transmitting meter provision. Do you agree with the changes proposed by Staff?

9 A. The Company has concerns with two modifications proposed by Staff to its AMI opt-out
10 provision. First, Staff removed the Residential Small Farm Secondary Rate (“RF”),
11 Residential Service Space Heating Secondary Rate (“RH”), and General Service
12 Agricultural Secondary Rate (“GSA”) from this proposed provision because Staff does
13 not agree with the Company’s proposal to implement these new rate categories. If the
14 Commission approves these new proposed rate categories, then customers taking service
15 on these rates should be included as eligible for the AMI opt-out provision. The
16 Company also objects to Staff’s removal of the sentence that states “In order for a
17 customer to be eligible to participate in the opt-out program, the customer must have a
18 meter that is accessible to Company employees and the customer shall have zero
19 instances of unauthorized use, theft, fraud and/or threats of violence toward Company
20 employees.” The Company believes this sentence needs to be retained so that the opt-out
21 provision is offered only under reasonable conditions that recognize the Company’s need
22 to obtain accurate reads, while still properly ensuring reasonable credit and collection
23 practices, and maintaining employee safety.

LAUREN E. YOUNGDAHL
REBUTTAL TESTIMONY

1 **TECHNICAL CONFERENCES**

2 Q. On page 5 of his testimony Mr. Wright recommended a technical conference with the
3 Company's technical experts once every two months. Do you accept this
4 recommendation?

5 A. The Company accepts Mr. Wright's recommendation.

6 **RESPONSE TO ATTORNEY GENERAL TESTIMONY**

7 Q. On pages 22 and 23 of his testimony Mr. Coppola recommends that the Commission
8 reduce 2013 O&M expense by \$2 million. Do you agree?

9 A. No, as stated previously, the Company does not expect a reduction in O&M expense from
10 the test year projection. While it is true that the Company has extended the timeframe for
11 development of the initial smart meter billing release, the Company does not expect to
12 reduce its smart meter/advanced metering infrastructure O&M expenses. The Company
13 expects that the need for technical resources to support the initial smart meter billing
14 release will exceed the test year estimates by approximately \$1.163 million, offset in part
15 by delays in programs that had been included in the Company's test year estimate.

16 Q. On page 51, and again on page 59, of his testimony Mr. Coppola recommends that the
17 Commission order the Company to put the smart grid/advanced metering infrastructure
18 on hold, and disallow recovery of \$232.6 million of capital expenditures related to the
19 smart grid/advanced metering infrastructure project, including those already spent and
20 those planned through the test year period, stating that the cost/benefit analysis shows
21 insufficient net value to customers. Do you agree?

22 A. No, the Company does not agree. The benefits of smart grid/advanced metering
23 infrastructure to Michigan, customers and the Company's operations have been

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1 repeatedly recognized and endorsed by federal and state authorities, business
2 associations, Company management, and the Commission.

3 As stated in my direct testimony, the smart grid/advanced metering infrastructure
4 program includes initial benefits of: reduced operating expenses, improved meter read
5 accuracy and reduced number of estimated bills, improved theft detection, and increased
6 customer access to detailed energy usage. Additional programs provided to customers
7 will enable them to reduce their overall energy consumption and reduce customer and
8 Company costs.

9 Q. On page 60 and in Exhibit AG-23 Mr. Copolla proposes changes to the upfront costs and
10 ongoing monthly costs associated with the opt-out proposal. Do you agree with these
11 changes?

12 A. The Company rejects these changes and instead accepts the changes proposed by
13 Ms. Jayasheela in the Staff's testimony.

14 Q. Does this complete your rebuttal testimony?

15 A. Yes.

1 JUDGE CUMMINS: Any cross-examination for
2 this witness?

3 MR. MOODY: Yes, your Honor.

4 JUDGE CUMMINS: Yes, Mr. Moody, please
5 proceed.

6 CROSS-EXAMINATION

7 BY MR. MOODY:

8 Q Good afternoon.

9 A Good afternoon.

10 Q Turning to your rebuttal testimony, it's page 6, if you
11 could go there?

12 A Sure. Yes.

13 Q Looking at lines 12 to 16, you state the Company expects
14 the need for technical resources to support the initial
15 smart meter billing release will exceed the test year
16 estimates by approximately 1.163 million. Do you see
17 that?

18 A I do.

19 Q Is the 1.163 million increase in the communication
20 customer programs area?

21 A This is for O&M expenses.

22 Q And is that -- what particular area is that increase in?

23 A It is not in the communications and customers programs
24 line item. You'll see on my exhibit, the Revised Exhibit
25 A-70, it's an increase in the program management and

1 other to support our billing go-live.

2 Q O.K. And staying on that page 6 of your rebuttal, you
3 talk about an extended timeframe for the development of
4 the initial smart meter billing release. Do you see
5 that?

6 A I'm sorry, which line are you referring to?

7 Q Sure. That's lines 10 and 11?

8 A Yes.

9 Q Why does the delay in implementing the billing module now
10 also create a delay in the start of the communication and
11 customer program?

12 A So the reason that we are delaying is because we have
13 taken a very deliberate approach, based on industry best
14 practices, because we want to get this right for our
15 customers. So that does not delay the communication
16 outreach that we are doing with our customers. In fact,
17 we have been, starting with when we first installed our
18 first meter on August 20th of 2012, there was outreach
19 going on around 90 days before that to ensure customers
20 knew that the smart meters were going to be coming, what
21 the exchange process was like, among many other things,
22 so there were no surprises.

23 Q Staying on that same page, at the bottom of page 6, in
24 rebutting Mr. Coppola's testimony you say the Company
25 disagrees with Mr. Coppola about the benefits of smart

1 grid and the fact that they're widely recognized. Do you
2 see that?

3 A I do.

4 Q Isn't it true that each utility's smart grid/AMI project
5 is different, should be justified on its own merits?

6 A I don't know.

7 Q Well, would you expect then that Consumers Energy's AMI
8 project should be justified based on Duke Energy's study
9 regarding their AMI project?

10 A So -- can you ask the question again, please? I want to
11 make sure I understand what you're asking.

12 Q Sure. So if you were comparing Duke Energy to Consumers
13 Energy on their AMI/smart grid project for example, their
14 presentation about how you should justify expenses and
15 everything else entailed with that, for Duke Energy,
16 would that also apply to Consumers Energy's project?

17 A It could. And that's why we have taken this deliberate
18 and measured approach. So to date there are
19 approximately 36 million smart meters installed across
20 the nation, and annual growth rate of 30 percent. By
21 2015, it's expected to see 65 million smart meters across
22 the nation. So we know, based upon the learnings of
23 others who have gone before us, who have done it right
24 and not right, what we can apply to our implementation.

25 Q But you would think that Consumers Energy's justification

1 for its AMI is based on Consumers Energy's program and
2 plan for its company, correct?

3 A We use, we apply lessons learned from others, what's
4 happening in the industry, and our own internal analysis.

5 Q So if the commission in dealing with Duke rejected their
6 AMI project because it wasn't justified, doesn't have the
7 cost-benefit savings, would you say then that that
8 applies to Consumers Energy?

9 A No.

10 Q Are you aware whether Michigan Public Service Commission
11 has required a cost-benefit analysis to be done to
12 justify the AMI projects smart grid for Consumers?

13 A We have submitted our business case, as you know, in this
14 filing and in previous filings as well. So they have
15 seen our business case.

16 Q Is that the same as a cost-benefit analysis? Is that
17 correct, the business case?

18 A I believe so.

19 Q Looking at page 7 of your rebuttal testimony, and I'm
20 looking starting at line 9 where we talk about the
21 rebuttal to opt-out proposals. Do you see that?

22 A Yes, I do.

23 Q You're familiar obviously with the fees and costs that
24 the Company is proposing with the opt-out proposal,
25 correct?

1 A I do, yes.

2 Q Why is the Company proposing to charge a fee that
3 includes 39.52 to restore a premises standard meter when
4 the current meter is not being removed or replaced?

5 A So the fundamental tenets of our opt-out proposal is it's
6 cost of service based. We anticipate that one and a half
7 percent of customers will want to opt-out of our meter.
8 So with that understanding and with the notion that we do
9 want to offer choices to our customers, because we want
10 to provide customer value and customer service, so we
11 have this option. But customers who opt out -- the
12 customers who have smart meters should not have to
13 subsidize those who want to opt-out. So it's cost of
14 service based.

15 So the way that we have structured the
16 upfront fee is, the standard, our standard meter going
17 forward is the smart meter. So that additional fee is to
18 restore the premise, once the customer leaves, to the
19 standard state smart meter.

20 Q Do you charge a customer right now to remove their
21 current meter to put in the smart meter?

22 A No.

23 Q But you will charge a future customer to put the new
24 smart meter in; is that correct?

25 A I'm sorry. Say that again, please.

1 Q Currently right now Consumers Energy does not charge a
2 customer to take out their old meter and put in a new
3 smart meter, right?

4 A Currently right now when we go a premise, when we are
5 doing the exchange for the first time, we do not charge
6 the customer for the smart meter.

7 Q But if a customer says: I don't want the smart meter
8 now, you will charge that customer a fee because in the
9 future he might switch it? Is that what you're saying?

10 A I'm not sure I'm following your question. There's two
11 different costs for upfront charges. So which are you
12 referring to?

13 Q The 39.52, the one about the restore premises.

14 A Is there --

15 Q I guess maybe there is a charge for when someone opts
16 out, opts out of this smart grid. I think it's 39.52.
17 And if you want to look at Attorney General Exhibit 23,
18 Mr. Coppola sets out some of the different company
19 calculations. That might help.

20 A This is in --

21 Q I have -- Do you have Mr. Coppola's testimony and
22 exhibits available?

23 A I do. One moment.

24 MR. McQUILLAN: Your Honor, just for my
25 reference, are you on line 12 of that exhibit, Mike?

1 MR. MOODY: Yes. Sorry.

2 Q (By Mr. Moody): Looking at Attorney General Exhibit
3 AG-23, do you have that in front of you or do you need a
4 copy?

5 A I do not have that in front of me.

6 Q All right.

7 MR. MOODY: Your Honor, may I approach
8 the witness?

9 JUDGE CUMMINS: Certainly, Mr. Moody.

10 (Document was handed to the witness.)

11 A Thank you.

12 Q (By Mr. Moody): Looking at that AG-23, which is the
13 Attorney General proposed exhibit, if you look at under
14 cost to support opt-out, line 5 there, restore premise to
15 standard metering, 39.52?

16 A Uh-huh.

17 Q Is that the fee that you charge someone who opts out from
18 the smart grid program?

19 A So this is to restore the meter to the current state
20 smart meter when they leave the premise.

21 Q So you charge the person who opts out 39.52 because
22 you'll have to change it later?

23 A Correct.

24 Q That's the --

25 A And also we have accepted Staff's position on this.

1 Q Which is?

2 A They support the upfront costs.

3 Q O.K. Does it make sense though to charge -- let me ask
4 this one more time to make sure I understand it. If I
5 want to change my meter or if I agree to change my meter
6 to the new smart grid/AMI meter, I won't get charged the
7 39.52; is that correct?

8 A If you choose to not opt-out?

9 Q Yes, if I just go with the program.

10 A Correct.

11 Q If I choose to opt-out, I get charged 39.52; is that
12 correct?

13 A Correct, to restore it to the standard state, which is
14 the smart meter, when you leave the premise.

15 Q But currently you're not charging anybody to put that
16 meter; is that correct?

17 A Because they haven't opted out, right. If you do not opt
18 out, correct.

19 Q O.K. Why is there a cost, when is there a 39.52 cost to
20 put the AMI meter in later but not now? Like now being
21 if I agree to the AMI there is no 39.52 cost. If I don't
22 agree to it and you have to do it later, switch it, there
23 is a 39.52 cost.

24 A Correct.

25 Q Why is there a cost later and not now?

1 A It is the cost associated with re-installing or
2 installing this smart meter after you leave the premise.

3 Q O.K.

4 JUDGE CUMMINS: Ms. Youngdahl, this
5 raises a question for me. If I currently do not have a
6 smart meter --

7 A Yes.

8 JUDGE CUMMINS: And I wanted to retain my
9 smart meter, would I have to pay the \$39.52 charge?

10 A If you choose not to opt-out.

11 JUDGE CUMMINS: If I choose not to have
12 it changed, say I've got the old standard meter and I am
13 notified, in whatever form, that my neighborhood at least
14 we're going to be installing smart meters, and I choose
15 to retain my existing old-fashioned meter. Would I then
16 fall into the opt-out class and have to pay the \$39.52
17 charge?

18 A You would pay the upfront cost in addition to a monthly
19 recurring cost.

20 JUDGE CUMMINS: Anyone taking over my
21 residence after the fact then, though, would be held
22 harmless? They wouldn't have to pay? When I left, the
23 smart meter would be installed at no charge to them?

24 A Correct.

25 JUDGE CUMMINS: O.K. Thank you.

1 Anything further, Mr. Moody?

2 MR. MOODY: No, your Honor.

3 JUDGE CUMMINS: Do any of the other
4 parties have questions for this witness? Any redirect?

5 MR. McQUILLAN: No, your Honor. Thank
6 you.

7 JUDGE CUMMINS: Very well. We have
8 before us four exhibits. These are A-69 Revised, A-70
9 Revised, A-71 and A-72. Is there any objection to the
10 receipt of these four exhibits? Hearing none, those four
11 exhibits are received into evidence.

12 Ms. Youngdahl, you may step down.

13 THE WITNESS: All right. Thank you.

14 (The witness was excused.)

15 JUDGE CUMMINS: It's my understanding we
16 have come to the end of the witnesses that were planned
17 to be presented today by the Applicant. Is that correct?

18 MR. McQUILLAN: That is correct, your
19 Honor. Consumers Energy appreciates the cooperation of
20 all the parties in narrowing down the issues, and the
21 availability of the witnesses was designed,
22 optimistically, hoping to get through that many today.
23 We have done very well; we're very pleased.

24 JUDGE CUMMINS: Very well. My
25 understanding also is that I believe it's Wednesday that

1 is set aside for discussions among the parties,
2 independent of me. Is that correct?

3 MR. McQUILLAN: Yes.

4 JUDGE CUMMINS: We will not be having
5 hearings as I sent out in an e-mail. I'm hoping that
6 everyone was apprized of that. The room will not be
7 available for us in the afternoon on Wednesday. So we're
8 going to be adjourned until Thursday morning at 9:00, at
9 which point we'll go hopefully 9:00 until shortly before
10 5:00, trying to get as much of the Company's case in as
11 we can.

12 Let me know if there are, right now I
13 think there may be two potential witnesses that are not
14 of the Company's control, that may have to go on
15 Thursday. But there was a question as to whether folks
16 were willing to stipulate to their testimony. Hopefully
17 we'll know by the end of tomorrow or at least early
18 Thursday where things stand and we can try to juggle
19 things accordingly on Thursday to do what we can.

20 I was talking to Ms. Uitvlugt before we
21 broke and indicating that I know that for the
22 Commission's purposes, it is beneficial if we can segment
23 the testimony into the Company's, the Intervenors, and
24 the Staff's, as congruent as we can make that. If you
25 can strive to do that, that would be helpful for them

1 because it's a time sensitive case.

2 Is there anything else we need to address
3 today? Hearing nothing, we're adjourned until Thursday
4 at 9:00 a.m., at which point we'll continue with
5 cross-examination with the Company's witnesses.

6 MR. McQUILLAN: Thank you, your Honor.

7 JUDGE CUMMINS: Thank you all very much
8 for your patience and assistance.

9 (At 2:45 p.m., the hearing adjourned to March 28,
10 2013, for continuation of cross-examination.)

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C E R T I F I C A T E

I, Marie T. Schroeder (CSR-2183), do hereby certify that I reported in stenotype the proceedings had in the within-entitled matter, that being Case No. U-17087, before Mark E. Cummins, Administrative Law Judge with MAHS, at the Michigan Public Service Commission, Lansing, Michigan, on Monday, March 25, 2013; and do further certify that the foregoing transcript, consisting of Volume 4, Pages 181-572, is a true and correct transcript of my stenotype notes.

Marie T. Schroeder, CSR-2183
33231 Grand River Avenue
Farmington, MI 48336

Dated: March 26, 2013