



Partners in Business Meeting 2008 Attachment O

Lansing Center

October 3, 2007

Agenda

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|--------------------------------|--------------|
| ■ Opening Remarks | Tom Wrenbeck |
| ■ Introduction to Attachment O | Purvi Patel |
| ■ Details of the Inputs | Nisha Chopra |
| ■ Q & A | |

Meeting Purpose

- METC's billing rate starting on January 1, 2008 is based on the 2008 projected net revenue requirement and load
- The purpose of today's meeting is to review with you the formula rate input projections and cost details

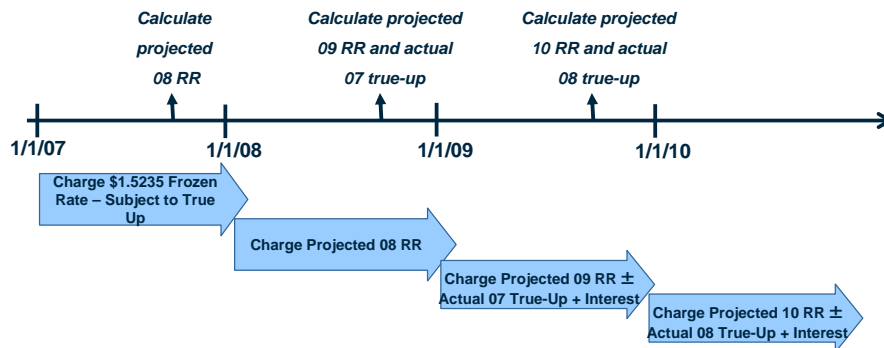
METC Attachment O Filing

- On October 30, 2006, METC and the Midwest ISO jointly filed proposed tariff sheet revisions to allow METC to recover its revenue requirement on a current basis under its Attachment O formula rate with a true-up mechanism
 - The components and calculation of rates under forward looking Attachment O have not changed other than conforming changes to implement a projected revenue requirement with a true-up mechanism
 - Under historical Attachment O, the rates that went into effect June 1st were based on the prior year's net revenue requirement and load
 - Under forward looking Attachment O, rates will go into effect on a calendar year basis (January – December) and will reflect the projected net revenue requirement and load for that year
 - A true-up calculation comparing actual billed revenues to actual net revenue requirement will be completed for each calendar year
 - The true-up, along with interest, will be included in the rate that goes into effect two years later (e.g. the 2008 true-up amount and associated interest accrued will be included in the rate that goes into effect in 2010)
- FERC conditionally accepted the filing on December 21, 2006
 - A Compliance Filing was made on January 22, 2007 and March 23, 2007 and accepted by FERC on May 30, 2007
- The 2008 Attachment O was posted on the MISO OASIS on August 31, 2007

Forward Looking Attachment O

■ Forward Looking Attachment O Timeline (2008 Example)

- **August 2007**
 - Calculate 2008 billing rate based on projected 2008 Net Revenue Requirement ("RR")
- **August 31, 2007**
 - Post rate on OASIS
- **January 2008 – December 2008**
 - Apply 2008 billing rate to monthly peak load
- **August 2009**
 - Calculate 2010 billing rate based on projected 2010 net RR and actual 2008 true-up with interest (comparing actual 2008 billed revenues to actual 2008 net RR)
- **January 2010 – December 2010**
 - Apply 2010 billing rate based on projected 2010 net RR +/- 2008 true-up with interest

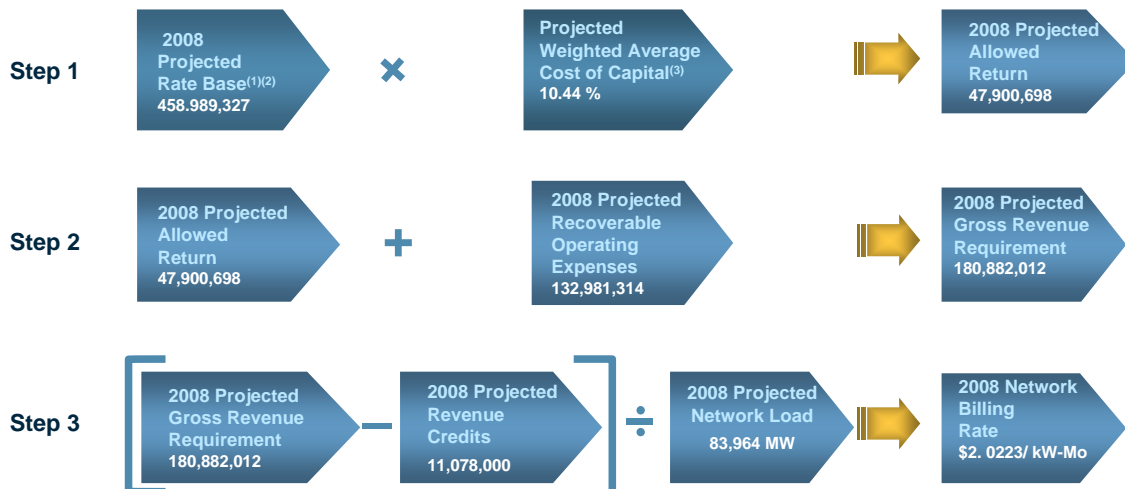


5



Forward Looking Attachment O

Using Attachment O to Derive the 2008 Billing Rate



(1) Includes new in-service property, plant and equipment additions in rate base
 (2) Includes the Regulatory Assets in rate base
 (3) Weighted average cost of capital based in part on FERC accepted return on equity

6



Step 1A – Establish Rate Base

Rate Base Item	2008 Projected Amount	2005 Cost Year Amount	Increase/ (Decrease)	Explanation
Gross Plant in Service	\$ 677,815,000	\$ 572,028,392	\$ 105,786,608	Additions to plant
Less Accumulated Depreciation	293,912,000	265,042,508	28,869,492	Higher depreciable asset base
Net Plant in Service	383,903,000	306,985,884	76,917,116	
Deferred Taxes	(54,423,000)	(43,246,430)	(11,176,570)	Higher net deferred tax liability attributable to MACRS and property additions
Regulatory Amortizations	110,136,000	121,093,935	(10,957,935)	Reflects settlement amounts
Materials & Supplies	8,082,575	5,142,089	2,940,486	Higher inventory balances due to higher capital levels
Land Held for Future Use	-	-	-	
Prepayments	1,411,000	909,095	501,905	Higher insurance premiums
Change in Working Capital	9,879,752	5,247,998	4,631,754	Attachment O calculation (1/8 of recoverable O&M)
Total Rate Base	<u>\$ 458,989,327</u>	<u>\$ 396,132,571</u>	<u>\$ 62,856,756</u>	

2008 Capital Additions

	Forecasted Start Date	Forecasted In-Service Date	Forecasted Plant Additions *
Reliability-System Capacity Improvements			
138kV Capacitors at Croton and Bard Rd.	Jan '08	May '08	\$3,163,127
Tallmadge Station Transformer #3 Addition Phase II	Jan '08	Dec '08	9,146,907
Reliability-Infrastructure Improvements			
Replace Ludington Reactor	Jan '08	May '08	\$3,030,488
Terminal Equipment Upgrade Program	Mar '07	Nov '08	562,886
138kV Sag Clearance	Feb '08	Dec '08	2,720,431
Goss Station-Replace 345kV Bus & Breakers (GIS)	Jan '07	Dec '08	8,788,129
METC Communication and Relaying Upgrade	Jan '08	Dec '08	14,781,645
Transformer Monitoring Program	Jan '08	Dec '08	1,834,368
Power Plant Control Relocation	July '08	Dec '08	216,997
Relay NERC/8A Compliance	May '08	Dec '08	5,414,160
Breaker Replacement Program		Ongoing	5,365,719
Relay Betterment/NERC Compliance		Ongoing	447,695
Wood Pole Replacement Program		Ongoing	235,362
Misc. NRUC/ERUC		Ongoing	483,298
Customer Connections			
Riggsville-Mod Bus Protection	Sept '08	Oct '08	\$182,559
Hile Road	Sept '08	Oct '08	313,221
Facilities			
General Facilities		Ongoing	\$1,367,559
General Plant			
Vehicles, Tools & Equipment		Ongoing	\$5,470,235
Information Technology		Ongoing	820,535

* Includes previous years' expenditures for multi-year projects

Step 1B – Establish Rate of Return & Allowed Return

	Ratio	Cost	2008 Projected WACC	2005 Cost Year WACC	Increase/ (Decrease)	Explanation
Equity	60%	13.38%	8.03%	7.20%	0.83%	40/60 debt to capitalization structure
Debt	40%	6.01%	2.40%	2.75%	-0.34%	Renegotiated interest rates on revolving credit
Rate of Return			10.44%	9.95%	0.49%	

Calculation

Rate Base	\$	458,989,327
x Return		10.44%
= Allowed Return	\$	47,900,698

Step 2A – Determine Recoverable Operating Expenses

Expense Item	2008 Projected Amount	2005 Cost Year Amount	Increase/ (Decrease)	Explanation
Operating & Maintenance Expense	\$ 44,903,000	\$ 32,218,853	\$ 12,684,147	Increase in vegetation management, tower painting, steel tower maintenance and inspections
Plus Administrative & General Expense	34,135,016	9,765,132	24,369,884	Increase in staffing and outside services plus backcharge for Novi HQ and Operations Center
Plus Depreciation Expense	15,402,000	14,018,382	1,383,618	Higher depreciable asset base
Plus Regulatory Amortizations	6,155,000	22,380,962	(16,225,962)	Settlement reflects 20 year amortization of regulatory asset
Plus Payroll Taxes	518,000	261,195	256,805	Higher payroll taxes due to higher staffing
Plus Plant Related Taxes	9,030,000	7,521,133	1,508,867	Higher asset base
Plus Income Taxes	22,838,298	15,361,809	7,476,489	Higher income plus addition of state business tax as income tax
Total Recoverable Operating Expenses	<u>\$ 132,981,314</u>	<u>\$ 101,527,466</u>	<u>\$ 31,453,848</u>	

Step 2B – Establish Gross Revenue Requirement

Calculation

Allowed Return	\$	47,900,698
+ Total Recoverable Operating Expenses		132,981,314
= Gross Revenue Requirement	\$	180,882,012

Step 3A – Establish Net Revenue Requirement

Credit Item	2008 Projected Amount	2005 Cost Year Amount	Increase/ (Decrease)	Explanation
Point to Point & Schedule 26	\$ 11,078,000	\$ 10,830,288	\$ 247,712	Schedule 26 revenues from RECB process, offset by lower point-to-point revenues
Total Revenue Credits	<u>\$ 11,078,000</u>	<u>\$ 10,830,288</u>	<u>\$ 247,712</u>	

Calculation

Gross Revenue Requirement	\$	180,882,012
- Revenue Credits		(11,078,000)
= Net Revenue Requirement	\$	169,804,012

Step 3B – Establish Billing Rate

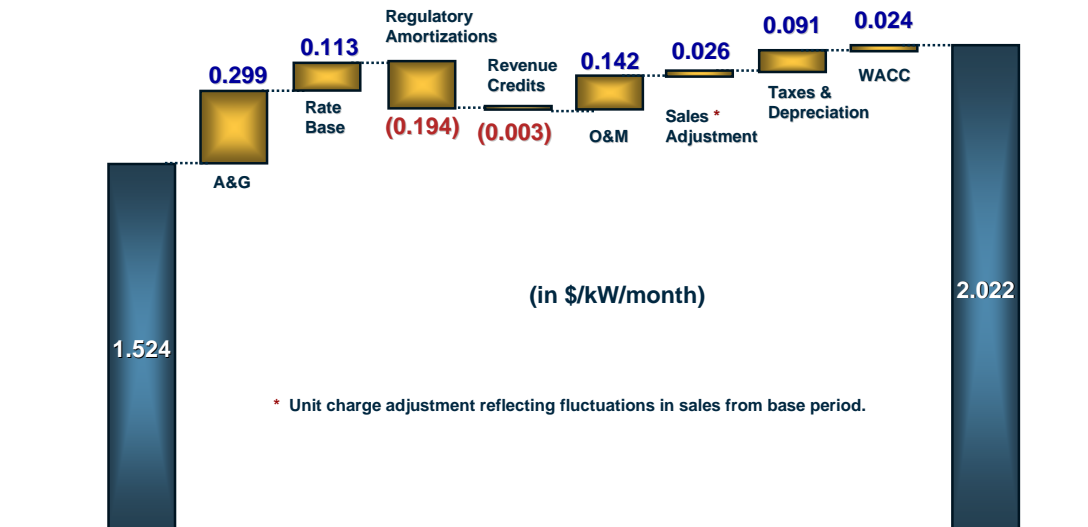
	2008 Projected Load	2005 Cost Year Amount	Increase/ (Decrease)	Explanation
Sum of 2008 Monthly Coincident Network Peak Loads (in kW)	83,964,000	85,398,000	(1,434,000)	- Based on METC short term peak demand forecast model - Econometric model including weather, economic and calendar drivers

Calculation

Net Revenue Requirement	\$	169,804,012
/ Load (kW)		83,964,000
= 2008 Rate (per kW-Mo)	\$	2.0223

Summary

- The \$2.022/kW-Mo rate (effective January 1, 2008 through December 31, 2008) is shown below.



Contact Information

- For additional questions, please contact:

Tom Wrenbeck – Manager, Stakeholder Relations

Email: twrenbeck@itctransco.com

Work phone: (248)374-7243