

MICHIGAN CONSOLIDATED GAS COMPANY

Unaudited Financial Statements as of and for the Quarter and Nine Months ended
September 30, 2007

MICHIGAN CONSOLIDATED GAS COMPANY

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MICHIGAN CONSOLIDATED GAS COMPANY
CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

| (in Millions) | Three Months Ended September 30 | | Nine Months Ended September 30 | |
|--|------------------------------------|---------------|-----------------------------------|-----------------|
| | 2007 | 2006 | 2007 | 2006 |
| | Operating Revenues | \$ 169 | \$ 167 | \$ 1,335 |
| Operating Expenses | | | | |
| Cost of gas | 56 | 56 | 827 | 768 |
| Operation and maintenance | 104 | 91 | 324 | 320 |
| Depreciation and amortization | 25 | 24 | 70 | 71 |
| Taxes other than income | 13 | 13 | 42 | 41 |
| Asset (gains) and losses, net | (1) | (3) | 2 | - |
| | 197 | 181 | 1,265 | 1,200 |
| Operating Income (Loss) | (28) | (14) | 70 | 59 |
| Other (Income) and Deductions | | | | |
| Interest expense | 16 | 17 | 43 | 49 |
| Interest income | (5) | (2) | (12) | (6) |
| Other income | (2) | (2) | (7) | (6) |
| Other expenses | 1 | - | 3 | 1 |
| | 10 | 13 | 27 | 38 |
| Income (Loss) Before Income Taxes | (38) | (27) | 43 | 21 |
| Income Tax Provision (Benefit) | (10) | (8) | 11 | 3 |
| Net Income (Loss) | \$ (28) | \$ (19) | \$ 32 | \$ 18 |

See Notes to Consolidated Financial Statements (Unaudited)

MICHIGAN CONSOLIDATED GAS COMPANY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

| (in Millions) | <u>September 30</u> <u>2007</u> | <u>December 31</u> <u>2006</u> |
|--|------------------------------------|-----------------------------------|
| ASSETS | | |
| Current Assets | | |
| Cash and cash equivalents..... | \$ 10 | \$ 1 |
| Accounts Receivable (less allowance for doubtful accounts of \$90 and \$96, respectively) | | |
| Customer | 180 | 364 |
| Affiliates | 49 | 82 |
| Other | 28 | 19 |
| Inventories | | |
| Gas | 127 | 77 |
| Material and supplies | 19 | 17 |
| Gas customer choice deferred asset | 94 | 101 |
| Other | 40 | 37 |
| | <u>547</u> | <u>698</u> |
| Investments | <u>97</u> | <u>94</u> |
| Property | | |
| Property, Plant and Equipment | 3,533 | 3,391 |
| Less accumulated depreciation | <u>(1,593)</u> | <u>(1,539)</u> |
| | <u>1,940</u> | <u>1,852</u> |
| Other Assets | | |
| Regulatory assets..... | 417 | 362 |
| Notes receivable..... | 77 | 79 |
| Prepaid benefit costs and due from affiliate..... | 394 | 365 |
| Other | 9 | 20 |
| | <u>897</u> | <u>826</u> |
| Total Assets | <u>\$ 3,481</u> | <u>\$ 3,470</u> |

See Notes to Consolidated Financial Statements (Unaudited)

MICHIGAN CONSOLIDATED GAS COMPANY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

| (in Millions, Except Shares) | <u>September 30 2007</u> | <u>December 31 2006</u> |
|---|------------------------------|-----------------------------|
| LIABILITIES AND SHAREHOLDER'S EQUITY | | |
| Current Liabilities | | |
| Accounts payable | | |
| Affiliates..... | \$ 129 | \$ 13 |
| Other..... | 111 | 198 |
| Dividends payable | 13 | 13 |
| Short-term borrowings | 318 | 342 |
| Current portion of long-term debt | 275 | 30 |
| Federal income, property and other taxes payable | 10 | 14 |
| Accrued gas cost recovery refund | 44 | 81 |
| Other | 56 | 74 |
| | <u>956</u> | <u>765</u> |
| Long-Term debt, (net of current portion)..... | <u>440</u> | <u>715</u> |
| Other Liabilities | | |
| Deferred income taxes..... | 213 | 181 |
| Regulatory liabilities | 580 | 510 |
| Accrued postretirement benefit costs | 348 | 347 |
| Other | 189 | 196 |
| | <u>1,330</u> | <u>1,234</u> |
| Commitments and Contingencies (Notes 4 and 7) | | |
| Shareholder's Equity | | |
| Common stock, \$1 par value, 15,100,000 shares authorized, 10,300,000 shares issued and outstanding..... | 10 | 10 |
| Additional paid in capital | 437 | 432 |
| Retained earnings | 309 | 315 |
| Accumulated other comprehensive loss | (1) | (1) |
| | <u>755</u> | <u>756</u> |
| Total Liabilities and Shareholder's Equity..... | <u>\$ 3,481</u> | <u>\$ 3,470</u> |

See Notes to Consolidated Financial Statements (Unaudited)

MICHIGAN CONSOLIDATED GAS COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

| (in Millions) | Nine Months Ended September 30 | |
|---|-----------------------------------|-------------|
| | 2007 | 2006 |
| Operating Activities | | |
| Net income | \$ 32 | \$ 18 |
| Adjustments to reconcile net income to net cash from operating activities: | | |
| Depreciation and amortization..... | 70 | 71 |
| Deferred income taxes and investment tax credit, net ... | 21 | (24) |
| Asset (gains) and losses, net | 2 | - |
| Changes in assets and liabilities: | | |
| Accounts receivable, net..... | 208 | 362 |
| Inventories | (52) | (78) |
| Postretirement obligation..... | 1 | (3) |
| Prepaid benefit costs and due from affiliate | (29) | (16) |
| Accrued gas cost recovery | (37) | 149 |
| Accounts payable..... | (10) | (108) |
| Federal income, property and other taxes payable..... | (4) | 14 |
| Other assets..... | (35) | (51) |
| Other liabilities | 39 | 10 |
| Net cash from operating activities | 206 | 344 |
| Investing Activities | | |
| Plant and equipment expenditures | (152) | (95) |
| Proceeds from sale of assets | 2 | 3 |
| Acquisitions, net of cash acquired | - | (1) |
| Other..... | 1 | 1 |
| Net cash used for investing activities..... | (149) | (92) |
| Financing Activities | | |
| Redemption of long-term debt..... | (30) | (40) |
| Short-term borrowings, net..... | 19 | (180) |
| Dividends on common stock | (37) | (38) |
| Net cash used for financing activities | (48) | (258) |
| Net Increase (Decrease) in Cash and Cash Equivalents | 9 | (6) |
| Cash and Cash Equivalents at Beginning of Period | 1 | 7 |
| Cash and Cash Equivalents at End of Period | \$ 10 | \$ 1 |
| Supplementary Cash Flow Information | | |
| Interest paid (excluding interest capitalized)..... | \$ 49 | \$ 53 |
| Income taxes paid | 20 | - |

See Notes to Consolidated Financial Statements (Unaudited)

MICHIGAN CONSOLIDATED GAS COMPANY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY
AND COMPREHENSIVE INCOME (UNAUDITED)

| (Dollars in Millions, Shares in Thousands) | Common Stock | | Additional Paid in Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Total |
|---|---------------------|---------------|---|------------------------------|---|---------------|
| | Shares | Amount | | | | |
| Balance, December 31, 2006 | 10,300 | \$ 10 | \$ 432 | \$ 315 | \$ (1) | \$ 756 |
| Net income | - | - | - | 32 | - | 32 |
| Capital contribution..... | - | - | 5 | - | - | 5 |
| Dividends declared on common stock | - | - | - | (38) | - | (38) |
| Balance, September 30, 2007 | 10,300 | \$ 10 | \$ 437 | \$ 309 | \$ (1) | \$ 755 |

The following table displays other comprehensive income for the nine-month periods ended September 30:

| (in Millions) | <u>2007</u> | <u>2006</u> |
|----------------------------|--------------|--------------|
| Net income | <u>\$ 32</u> | <u>\$ 18</u> |
| Comprehensive income | <u>\$ 32</u> | <u>\$ 18</u> |

See Notes to Consolidated Financial Statements (Unaudited)

MICHIGAN CONSOLIDATED GAS COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1 - GENERAL

These Consolidated Financial Statements should be read in conjunction with the Notes to Consolidated Financial Statements included in the 2006 Annual Report on Form 10-K.

The accompanying Consolidated Financial Statements are prepared using accounting principles generally accepted in the United States of America. These accounting principles require us to use estimates and assumptions that impact reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual results may differ from our estimates.

The Consolidated Financial Statements are unaudited, but in our opinion include all adjustments necessary for a fair presentation of such financial statements. All adjustments are of a normal recurring nature, except as otherwise disclosed in these Consolidated Financial Statements and Notes to Consolidated Financial Statements. Financial results for this interim period are not necessarily indicative of results that may be expected for any other interim period or for the fiscal year ending December 31, 2007.

References in this report to “we,” “us,” “our,” MichCon or “Company” are to Michigan Consolidated Gas Company and its subsidiaries, collectively.

Asset Retirement Obligations

We have conditional asset retirement obligations for gas pipeline retirement costs. To a lesser extent, we have conditional asset retirement obligations at certain service centers and compressor and gate stations. We recognize such obligations as liabilities at fair market value at the time the associated assets are placed in service. Fair value is measured using expected cash outflows discounted at our credit-adjusted risk-free rate.

Timing differences arise in the expense recognition of legal asset retirement costs that we are currently recovering in rates. We defer such differences under SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*.

A reconciliation of the asset retirement obligations for the 2007 nine-month period follows:

| | |
|---|--------|
| (in Millions) | |
| Asset retirement obligations at January 1, 2007 | \$ 103 |
| Accretion | 5 |
| Liabilities settled..... | (1) |
| Asset retirement obligations at September 30, 2007..... | \$ 107 |

Retirement Benefits and Trusteed Assets

MichCon sponsors a defined benefit retirement plan for eligible MichCon represented employees. MichCon also participates in a defined benefit retirement plan sponsored by Detroit Edison for its nonrepresented employees, which is treated as a plan covering employees of various affiliates of DTE Energy from the affiliates’ perspective. We are allocated income or an expense each year as a result of our participation in the DTE Energy Company Retirement Plan. Income was approximately \$7 million and \$4 million for the three months ended September 30, 2007 and 2006, respectively, and was approximately \$23 million and \$16 million for the nine months ended September 30, 2007 and 2006, respectively, and is not reflected in the following tables. We recognized pension expense of \$3 million for

MICHIGAN CONSOLIDATED GAS COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

the three months ended September 30, 2006 and \$1 million and \$4 million, respectively, for the nine months ended September 30, 2007 and 2006 in association with our Performance Excellence Process which is not reflected in the following tables. We recognized no pension expense for the three months ended September 30, 2007 in relation to our Performance Excellence Process.

In its April 2005 final rate order, the MPSC approved the deferral of the non-capitalized portion of our negative pension expense. The regulatory liability associated with the non-capitalized negative pension expense was \$65 million at September 30, 2007.

The components of net periodic benefit costs (credit) for pension benefits and other postretirement benefits follow:

| (in Millions) Three Months Ended September 30 | Pension Benefits | | Other Postretirement Benefits | |
|---|-------------------------|-------------|--------------------------------------|--------------|
| | <u>2007</u> | <u>2006</u> | <u>2007</u> | <u>2006</u> |
| Service cost | \$ 1 | \$ 2 | \$ 4 | \$ 3 |
| Interest cost | 4 | 4 | 7 | 7 |
| Expected return on plan assets | (7) | (7) | (3) | (4) |
| Amortization of | | | | |
| Net loss | - | 1 | 2 | 2 |
| Net transition liability | - | - | 1 | 2 |
| Special termination benefits | - | 2 | - | 1 |
| Net periodic benefit cost (credit) | <u>\$ (2)</u> | <u>\$ 2</u> | <u>\$ 11</u> | <u>\$ 11</u> |

| (in Millions) Nine Months Ended September 30 | Pension Benefits | | Other Postretirement Benefits | |
|--|-------------------------|---------------|--------------------------------------|--------------|
| | <u>2007</u> | <u>2006</u> | <u>2007</u> | <u>2006</u> |
| Service cost | \$ 5 | \$ 5 | \$ 11 | \$ 10 |
| Interest cost | 12 | 12 | 21 | 20 |
| Expected return on plan assets | (23) | (22) | (10) | (9) |
| Amortization of | | | | |
| Net loss | 1 | 1 | 7 | 7 |
| Prior service cost | 1 | 1 | 1 | 1 |
| Net transition liability | - | - | 4 | 4 |
| Special termination benefits | - | 2 | - | 1 |
| Net periodic benefit cost (credit) | <u>\$ (4)</u> | <u>\$ (1)</u> | <u>\$ 34</u> | <u>\$ 34</u> |

Special termination benefits in the above tables represent cost associated with our Performance Excellence Process.

MICHIGAN CONSOLIDATED GAS COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Income Taxes

Uncertain Tax Positions

We adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48)* on January 1, 2007. This interpretation prescribes a recognition threshold and a measurement attribute for the financial statement reporting of tax positions taken or expected to be taken on a tax return. As a result of the implementation of FIN 48, we recognized a \$0.2 million increase in liabilities which was accounted for as a reduction to the January 1, 2007 balance of retained earnings. The total amount of unrecognized tax benefits amounted to \$0.2 million at January 1, 2007, all of which would favorably impact our effective tax rate if recognized. These unrecognized tax benefits related entirely to federal income taxes. We had no unrecognized tax benefits pertaining to federal income taxes at September 30, 2007. The decline in unrecognized federal tax benefits during the nine months ended September 30, 2007 was attributable to settlements with the Internal Revenue Service (IRS) for the 2002 and 2003 tax years.

We recognize interest and penalties pertaining to income taxes in Interest expense and Other expenses, respectively, on our Consolidated Statements of Operations. We had no accrued interest and no accrued penalties pertaining to income taxes at January 1, 2007 and September 30, 2007. We had no interest expense in relation to income tax for the three and nine months ended September 30, 2007 and 2006.

Our U.S. federal income tax returns for years 2004 and subsequent years remain subject to examination by the IRS.

Michigan Business Tax

On July 12, 2007, the Michigan Business Tax (MBT) was enacted by the State of Michigan to replace the Michigan Single Business Tax (MSBT) effective January 1, 2008.

The MBT is comprised of the following:

- An apportioned modified gross receipts tax of 0.8 percent; and
- An apportioned business income tax of 4.95 percent.

The MBT provides credits for Michigan business investment, compensation, and research and development.

Effective with the enactment of the MBT in the third quarter of 2007, a state deferred tax liability of \$45 million was recognized by the Company for cumulative differences between book and tax assets and liabilities. Effective September 30, 2007, legislation was adopted by the State of Michigan creating a deduction for businesses that realize an increase in their deferred tax liability due to the enactment of the MBT. Therefore, a deferred tax asset of \$45 million was established related to the future deduction. The deduction will be claimed during the period of 2015 through 2029. The recognition of the enactment did not have an impact on our income tax provision for the three and nine months ended September 30, 2007.

The \$45 million of deferred tax liabilities and assets recognized were offset by corresponding regulatory assets and liabilities in accordance with SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*, as the impacts of the deferred tax liabilities and assets recognized upon enactment and amendment of the MBT will be reflected in our rates.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Stock-Based Compensation

Effective January 1, 2006, our parent company DTE Energy adopted SFAS No. 123(R), *Share-Based Payment (SFAS 123(R))*, using the modified prospective transition method. We receive an allocation of costs associated with stock compensation and the related impact of cumulative accounting adjustments. Our allocation for the three months ended September 30, 2007 and 2006 for stock-based compensation expense was approximately \$2 million and \$1 million, respectively, while such allocation was \$3 million and \$2 million, respectively, for the nine months ended September 30, 2007 and 2006. The cumulative effect of the adoption of SFAS No. 123(R) was immaterial.

Asset (gains) and losses, net

Asset losses of \$2 million in the nine months ended September 30, 2007 included a \$3 million disallowance of certain costs related to the acquisition of pipeline assets partially offset by a land sale during the three months ended September 30, 2007.

NOTE 2 – NEW ACCOUNTING PRONOUNCEMENTS

Fair Value Accounting

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. It emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Fair value measurement should be determined based on the assumptions that market participants would use in pricing an asset or liability. SFAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are currently assessing the effects of this statement, and have not yet determined its impact on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115*. This standard permits an entity to choose to measure many financial instruments and certain other items at fair value. The fair value option established by SFAS 159 permits all entities to choose to measure eligible items at fair value at specified election dates. An entity will report in earnings unrealized gains and losses on items, for which the fair value option has been elected, at each subsequent reporting date. The fair value option: (a) may be applied instrument by instrument, with a few exceptions, such as investments otherwise accounted for by the equity method; (b) is irrevocable (unless a new election date occurs); and (c) is applied only to entire instruments and not to portions of instruments. SFAS 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. We are currently assessing the effects of this statement, and have not yet determined its impact on our consolidated financial statements.

Accounting for Defined Benefit Pension and Other Postretirement Plans

In September 2006, the FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an Amendment of FASB Statements No. 87, 88, 106, and 132(R)*. SFAS 158 requires companies to (1) recognize the overfunded or underfunded status of defined benefit pension and defined benefit other postretirement plans in its financial statements, (2) recognize as a component of other comprehensive income, net of tax, the actuarial gains or losses and the prior service costs or credits

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

that arise during the period but are not immediately recognized as components of net periodic benefit cost, (3) recognize adjustments to other comprehensive income when the actuarial gains or losses, prior service costs or credits, and transition assets or obligations are recognized as components of net periodic benefit cost, (4) measure postretirement benefit plan assets and plan obligations as of the date of the employer's statement of financial position, and (5) disclose additional information in the notes to financial statements about certain effects on net periodic benefit cost in the upcoming fiscal year that arise from delayed recognition of the actuarial gains and losses and the prior service costs or credits.

We adopted the requirement to recognize the funded status of a defined benefit pension or defined benefit other postretirement plan and the related disclosure requirements on December 31, 2006. We requested and received agreement from the MPSC to record the additional liability amounts on the Statements of Financial Position as a regulatory asset.

The requirement to measure plan assets and benefit obligations as of the date of the employer's fiscal year-end statement of financial position is effective for fiscal years ending after December 15, 2008. The Statement provides two options for the transition to a fiscal year end measurement date. We have not yet determined which of the available transition measurement options we will use.

NOTE 3 - RESTRUCTURING

Performance Excellence Process

In mid-2005, we initiated a company-wide review of our operations called the Performance Excellence Process. We began a series of focused improvement initiatives and expect this process to continue into 2008.

We have incurred costs to achieve (CTA) for employee severance and other costs, consisting primarily of project management and consultant support. We cannot defer CTA costs at this time because a recovery mechanism has not been established. We expect to seek such a recovery mechanism in our next rate case in 2009.

Amounts expensed are recorded in the Operation and maintenance line on the Consolidated Statements of Operations. Expenses incurred for the three months ended September 30, 2007 and 2006 are as follows:

| (in Millions) | Employee Severance Costs | | Other Costs | | Total Cost | |
|-----------------|--------------------------|------|-------------|------|------------|-------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Costs incurred: | \$ 1 | \$ 8 | \$ 1 | \$ 4 | \$ 2 | \$ 12 |

Expenses incurred for the nine months ended September 30, 2007 and 2006 are as follows:

| (in Millions) | Employee Severance Costs | | Other Costs | | Total Cost | |
|-----------------|--------------------------|-------|-------------|------|------------|-------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Costs incurred: | \$ 3 | \$ 10 | \$ 2 | \$ 8 | \$ 5 | \$ 18 |

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

A liability for future CTA associated with the Performance Excellence Process has not been recognized because we have not met the recognition criteria of SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*.

NOTE 4 - REGULATORY MATTERS

Regulation

We are subject to the regulatory jurisdiction of the MPSC, which issues orders pertaining to rates, recovery of certain costs, including the costs of generating facilities and regulatory assets, conditions of service, accounting and operating-related matters.

Regulatory Accounting Treatment for Performance Excellence Process

In May 2006, we filed applications with the MPSC to allow deferral of costs associated with the implementation of the Performance Excellence Process, a company-wide cost-savings and performance improvement program. Implementation costs include project management, consultant support and employee severance expenses. We sought MPSC authorization to defer and amortize Performance Excellence Process implementation costs for accounting purposes to match the expected savings from the Performance Excellence Process program with the related CTA. We anticipate the Performance Excellence Process to continue into 2008. Our CTA is estimated to total between \$55 million and \$60 million. In September 2006, the MPSC issued an order approving a settlement agreement that allows commencing in 2006, to defer the incremental CTA. Further, the order provides for us to amortize the CTA deferrals over a ten-year period beginning with the year subsequent to the year the CTA was deferred. However, we cannot defer CTA costs at this time because a recovery mechanism has not been established. We expect to seek a recovery mechanism in its next rate case in 2009.

Uncollectible Expense True-Up Mechanism (UETM) and Report of Safety and Training-Related Expenditures

2005 UETM — In March 2006, MichCon filed an application with the MPSC for approval of its uncollectible expense true-up mechanism for 2005. This is the first filing MichCon has made under the uncollectible true-up mechanism, which was approved by the MPSC in April 2005 as part of MichCon's last general rate case. MichCon's 2005 base rates included \$37 million for anticipated uncollectible expenses. Actual 2005 uncollectible expenses totaled \$60 million. The true-up mechanism allows MichCon to recover ninety percent of uncollectibles that exceeded the \$37 million base. Under the formula prescribed by the MPSC, MichCon recorded an under-recovery of approximately \$11 million for uncollectible expenses from May 2005 (when the mechanism took effect) through the end of 2005. In December 2006, the MPSC issued an order authorizing MichCon to implement the UETM monthly surcharge for service rendered on and after January 1, 2007.

As part of the March 2006 application with the MPSC, MichCon filed a review of its 2005 annual safety and training-related expenditures. MichCon reported that actual safety and training-related expenditures for the initial period exceeded the pro-rata amounts included in base rates and based on the under-recovered position, recommended no refund at this time. In the December 2006 order, the MPSC also approved MichCon's 2005 safety and training report.

2006 UETM — In March 2007, MichCon filed an application with the MPSC for approval of its uncollectible expense true-up mechanism for 2006 requesting \$33 million of under-recovery plus applicable carrying costs of \$3 million. The March 2007 application included a report of MichCon's 2006 annual safety and training-related expenditures, which shows a \$2 million over-recovery. In August 2007,

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MichCon filed revised exhibits reflecting an agreement with the MPSC to net the \$2 million over-recovery related to the 2006 safety and training-related expenditures against the 2006 UETM under-recovery. An MPSC order in this case is expected by the end of 2007.

Gas Cost Recovery Proceedings

2005-2006 Plan Year — In December 2004, MichCon filed its 2005-2006 GCR plan case proposing a maximum GCR factor of \$7.99 per Mcf. The plan includes quarterly contingent GCR factors. These contingent factors allow MichCon to increase the maximum GCR factor to compensate for increases in gas market prices, thereby reducing the possibility of a GCR under-recovery. In April 2005, the MPSC issued an order recognizing that Michigan law allows MichCon to self-implement its quarterly contingent factors. MichCon self-implemented quarterly contingent GCR factors of \$8.54 per Mcf in July 2005 and \$10.09 per Mcf in October 2005. In response to market price increases in the fall of 2005, MichCon filed a petition to reopen the record in the case during September 2005. MichCon proposed a revised maximum GCR factor of \$13.10 per Mcf and a revised contingent factor matrix. In October 2005, the MPSC approved an increase in the GCR factor to a cap of \$11.3851 per Mcf for the period November 2005 through March 2006. In June 2006, MichCon filed its GCR reconciliation for the 2005-2006 GCR year. The filing supported a total over-recovery, including interest through March 2006, of \$13 million. MPSC Staff and other interveners filed testimony regarding the reconciliation in December 2006 in which they recommended disallowances related to MichCon's implementation of its dollar cost averaging fixed price program and its use of fixed basis in contracting purchases. In January 2007, MichCon filed testimony rebutting these recommendations. The 2005-2006 GCR reconciliation case is still in the regulatory review and approval process, and the final resolution is uncertain. Based on available information, MichCon is unable to assess the range of a reasonably possible loss related to the proposed disallowances. An MPSC order is expected in 2007.

2006-2007 Plan Year – In June 2007, MichCon filed its GCR reconciliation for the 2006-2007 GCR year. The filing supported a total under-recovery, including interest through March 2007, of \$18 million. An MPSC order in this case is expected in 2008.

2007-2008 Plan Year / Base Gas Sale Consolidated – In August 2006, MichCon filed an application with the MPSC requesting permission to sell base gas that would become accessible with storage facilities upgrades. MichCon's estimated sale of this base gas would be worth \$34 million. In December 2006, the administrative law judge in the case approved a motion made by the Residential Ratepayer Consortium to consolidate this case with MichCon's 2007-2008 GCR plan case. In December 2006, MichCon filed its 2007-2008 GCR plan case proposing a maximum GCR factor of \$8.49 per Mcf. In August 2007, a settlement agreement in this proceeding was reached by all intervening parties that provides for a sharing with customers of the proceeds from the sale of base gas. In addition, the agreement provides for a rate case filing moratorium until January 1, 2009, unless certain unanticipated changes occur that impact income by more than \$5 million. The settlement agreement was approved by the MPSC on August 21, 2007. MichCon's gas storage enhancement projects, the main subject of the aforementioned settlement, will enable 17 billion cubic feet (Bcf) of gas to become available for cycling. Under the settlement terms, MichCon will deliver 13.4 Bcf of this gas to its customers at a savings to market-priced supplies of approximately \$54 million. This settlement provides for MichCon to retain the proceeds from the sale of 3.6 Bcf of gas, which MichCon expects to sell in 2008 and 2009. By enabling MichCon to retain the profit from the sale of this gas, the settlement provides MichCon with the opportunity to earn an 11% return on equity with no customer rate increase for a period of five years from 2005 to 2010.

MICHIGAN CONSOLIDATED GAS COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Other

We are unable to predict the outcome of the regulatory matters discussed herein. Resolution of these matters is dependent upon future MPSC orders and appeals, which may materially impact the financial position, results of operations and cash flows of the Company.

NOTE 5 – LONG – TERM DEBT

Debt Retirements and Redemptions

In May 2007, we retired at maturity \$30 million of First Mortgage Bonds bearing 7.21% interest.

NOTE 6 – SHAREHOLDER’S EQUITY

In September 2007, a note receivable in the amount of \$5 million, with our parent company, was converted into a capital contribution.

NOTE 7 – COMMITMENTS AND CONTINGENCIES

Environmental Matters

Prior to the construction of major interstate natural gas pipelines, gas for heating and other uses was manufactured locally from processes involving coal, coke or oil. We own, or previously owned, 14 such former MGP sites. Investigations have revealed contamination related to the by-products of gas manufacturing at each site. In addition to the MGP sites, we are also in the process of cleaning up other contaminated sites. Cleanup activities associated with these sites will be conducted over the next several years.

The MPSC has established a cost deferral and rate recovery mechanism for investigation and remediation costs incurred at former MGP sites. Accordingly, we recognize a liability and a corresponding regulatory asset for estimated investigation and remediation costs at former MGP sites. During 2006, we spent approximately \$2 million investigating and remediating these former MGP sites. In December 2006, we retained multiple environmental consultants to estimate the projected cost to remediate each MGP site. We accrued an additional \$7 million in remediation liabilities, to increase the reserve balance to \$39 million at December 31, 2006, with a corresponding increase in the regulatory asset. The reserve balance was \$37 million at September 30, 2007.

Any significant change in assumptions, such as remediation techniques, nature and extent of contamination and regulatory requirements, could impact the estimate of remedial action costs for the sites and affect the Company’s financial position and cash flows. However, we anticipate the cost deferral and rate recovery mechanism approved by the MPSC will prevent environmental costs from having a material adverse impact on our results of operations.

Labor Contracts

There are several bargaining units for our represented employees. In October 2007, a new three-year agreement was ratified by approximately 950 employees.

MICHIGAN CONSOLIDATED GAS COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Purchase Commitments

As of September 30, 2007, we were party to numerous long-term purchase commitments relating to a variety of goods and services required for our business. These agreements primarily consist of long-term gas purchase and transportation agreements. We estimate that these commitments will be approximately \$1.5 billion from 2007 through 2051. We also estimate that 2007 capital expenditures will be approximately \$215 million. We have made certain commitments in connection with expected capital expenditures.

Bankruptcies

We sell gas and gas transportation and storage services to numerous companies operating in the steel, automotive, energy, retail and other industries. Certain of our customers have filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code. We regularly review contingent matters relating to these customers and our sale contracts and we record provisions for amounts that we can estimate and are considered at risk of probable loss. We believe our previously accrued amounts are adequate for probable losses. The final resolution of these matters is not expected to have a material effect on our financial statements.

Other Contingencies

We are involved in certain legal, regulatory, administrative and environmental proceedings before various courts, arbitration panels and governmental agencies concerning claims arising in the ordinary course of business. These proceedings include certain contract disputes, environmental reviews and investigations, audits, inquiries from various regulators, and pending judicial matters. We cannot predict the final disposition of such proceedings. We regularly review legal matters and record provisions for claims that we can estimate and are considered probable of loss. The resolution of pending proceedings is not expected to have a material effect on our operations or financial statements in the periods they are resolved.

See Note 4 for a discussion of contingencies related to Regulatory Matters.