

STATE OF MICHIGAN
MICHIGAN OFFICE OF ADMINISTRATIVE HEARINGS AND RULES
FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of Saginaw Bay Pipeline)	
Company's Application Requesting <i>ex parte</i>)	
Approval of New Rates for Transportation on)	Case No. U-20993
The Saginaw Bay Pipeline.)	
_____)	

NOTICE OF PROPOSAL FOR DECISION

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on March 8, 2023.

Exceptions, if any, must be filed with the Michigan Public Service Commission, 7109 West Saginaw, Lansing, Michigan 48917, and served on all other parties of record on or before March 29, 2023, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before April 12, 2023.

At the expiration of the period for filing exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for Decision is reviewed by action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before the date they are due.

MICHIGAN OFFICE OF ADMINISTRATIVE
HEARINGS AND RULES
For the Michigan Public Service Commission

**Katherine E.
Talbot**

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Date: 2023.03.08 10:57:03 -05'00'

March 8, 2023
Lansing, Michigan

Katherine E. Talbot
Administrative Law Judge

STATE OF MICHIGAN
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PROPOSAL FOR DECISION

I.

PROCEDURAL HISTORY

On March 17, 2021, Saginaw Bay Pipeline Company (Saginaw Bay or the Company) filed an application requesting *ex parte* approval “for new gas transportation rates reflected in a 20-year firm service agreement (Agreement), dated February 10, 2021,”¹ between Saginaw Bay and DTE Gas Company (DTE Gas). At the time of this filing, Saginaw Bay was a subsidiary DTE Energy Company, and an affiliate, of DTE Gas.² In July 2021 the affiliate relationship ended when DT Midstream, including Saginaw Bay, separated from DTE Energy Company and became a publicly traded company.³

A Prehearing Conference was conducted on November 30, 2021 at which time Staff appeared and the Attorney General intervened. A second Prehearing Conference

¹ Saginaw Bay Application dated March 17, 2021, p 1.

² Id. DTE Gas is also a subsidiary of DTE Energy Company. 3 Tr 27.

³ 3 Tr 26-27.

was held on January 4, 2022, and a schedule was established by consensus of the parties.⁴

On March 15, 2022, Saginaw Bay filed updated testimony and exhibits of one witness. On June 10, 2022, the Attorney General filed the testimony and exhibits of one witness, and Staff filed the testimony and exhibits of two witnesses. The Company filed the rebuttal testimony and exhibits of one witness on July 11, 2022.

An evidentiary hearing was held on August 5, 2022 where the pre-filed direct and rebuttal testimony of all witnesses was bound into the record, and all proposed exhibits were admitted into the record.

On August 26, 2022 briefs were filed by the Company, Staff, and the Attorney General. On September 9, 2022 the same parties filed reply briefs.

II.

OVERVIEW OF THE RECORD

The evidentiary record is contained in 139 transcript pages, in three volumes, and 25 exhibits.

A. Saginaw Bay Pipeline Company

The Company presented the direct and rebuttal testimony of Steven M. Richman, the Director, Gas Storage and Pipelines, for DT Midstream, Inc (DTM).⁵ He testified to support the reasonableness the revenue requirements for the firm transportation service, in the February 10, 2021 agreement between Saginaw Bay and DTE Gas on the Company's pipeline, including the negotiated rate, to show that the rate agreed to

⁴ The schedule was extended on April 19, 2022, based on agreement of the parties.

⁵ Mr. Richman's direct and rebuttal testimony are transcribed at 3 Tr 23-46. He sponsored Exhibits A-1 to Confidential Exhibit A-3.

consists of the Company's fully embedded costs plus a return of 10%, and to show that approval of this contract will not impact the rates of any other customer of Saginaw Bay.⁶

Mr. Richman testified the Saginaw Bay Pipeline is a 16-inch pipeline, transporting natural gas, which extends from the DTE Gas Kalkaska facility to a location near West Branch, Michigan. He stated the Company and DTE Gas have entered into a contract where Saginaw Bay will provide firm transportation services to DTE Gas for a maximum daily quantity of 50,000 Mcf per day over a 20-year period.⁷

Mr. Richman explained that at the time the contract was negotiated, Saginaw Bay and DTE Gas were affiliates under DTE Energy Company. He stated, on July 1, 2021 Saginaw Bay, along with its parent company DTM, separated from DTE Energy, and the two entities were no longer affiliated. He testified that the affiliate relationship limited the transportation rate agreed to by the parties due to Michigan Public Service Commission requirements, which provides for recovery of the fully embedded costs plus 10%.⁸

Mr. Richman testified the Company calculated a levelized 20-year rate in the contract comprised of a daily Demand Charge of \$0.0957/Dth for firm transportation of 50,000 Mcf per day on the pipeline. He stated this equates to a levelized Monthly Demand Charge for this service of \$145,544 and levelized annual Demand Charge of \$1,746,525.⁹

⁶ 3 Tr 26.

⁷ 3 Tr 26-27. See Exhibit A-2, a copy of the transportation agreement.

⁸ 3 Tr 27.

⁹ 3 Tr 29.

Mr. Richman explained that Saginaw Bay calculated the revenue requirements using:

(1) the estimated O&M required to operate and maintain the Saginaw Bay pipeline, (2) O&M deferred costs and costs for required seven year repeating ILI analysis over the 20-year transportation agreement to serve DTE Gas (2028, 2035 and 2042), (3) depreciation of the remaining book value of Saginaw Bay assets over the 20 year term, and (4) property and income taxes.¹⁰

Pointing to Exhibit A-1, he testified to the assumptions used to estimate the revenue requirements. Mr. Richman stated he used the currently projected 2023 O&M costs totaling \$1,364,998 and then escalated the costs by 3 percent for each subsequent year. He asserted the 3% annual escalation is to account for inflation and “the general expected increase in cost to provide the service.”¹¹ Mr. Richman also included In-Line Inspections (ILI) costs which the Company expects to recur every seven years, stating these were “estimated using the most recent actual costs for ILI, which are considered the base year for each segment and escalated by 3% annually, to account for the increase in costs to perform the service and forecasted for the year they are schedule to recur.”¹² He also testified the digs are recommended to verify the material and coating of the pipeline system, and other digs performed based on the results of the ILI work which have been deferred over the 20-year contract.¹³

Next, Mr. Richman testified that the transportation rate in the contract “was based on an infrastructure and organization that is no longer in place” after DTM and Saginaw Bay separated from DTE Energy, because DTM has a different management and

¹⁰ 3 Tr 28.

¹¹ Id.

¹² Id. Mr. Richman testified the 7-year schedule was recommended by DTM's Pipeline Integrity team. Id.

¹³ 3 Tr 28.

operating structures for the pipeline assets.¹⁴ He stated “based on the updated costs using the same modeling assumptions” the transportation rate would be \$0.101/Mcf when using DTM’s projected costs. Mr. Richman stated the contract does not recover the fully embedded estimated costs of Saginaw Bay based on the updated model. However, the Company did not alter rates in the agreement submitted in this case. Mr. Richman also stated the contracted capacity in the transportation agreement will not impact other existing transportation contracts.¹⁵

B. Staff

Staff presented the testimony of two witnesses. Robert Nichols II, CPA, the manager of the Revenue Requirements Section of the Regulated Energy Division of the Regulated Energy Division of the Michigan Public Service Commission (MPSC)¹⁶, and Kevin P. Spence, a Public Utilities Engineering Specialist in the Gas Operation Section of the Energy Operations Division of the MPSC.¹⁷

Mr. Nichols presented Staff’s “position on the discount rate, the cost of capital, deferred taxes, and [supported] Staff’s calculation of a reasonable transportation rate for Saginaw Bay Pipeline Company[.]”¹⁸ He testified that Saginaw Bay used its projected after-tax cost of capital as the discount rate whereas Staff recommend use of the pre-tax cost of capital as the discount rate and stated it is “typical for the discount rate to

¹⁴ 3 Tr 27.

¹⁵ 3 Tr 29.

¹⁶ Mr. Nichols’ direct testimony is transcribed at 3 Tr 49-58. He sponsored Confidential Exhibits S-1 through S-3.

¹⁷ Mr. Spence’s direct testimony is transcribed at 3 Tr 59-81. He sponsored Exhibits S-4 through Confidential Exhibit S-7.

¹⁸ 3 Tr 54.

equal the rate applied for the required rate of return on investment in the model.”¹⁹ He stated use of an after-tax cost of capital discount rate with the pre-tax cost of capital return on investment “provides an apples and oranges situation, which is not appropriate for this analysis.”²⁰

Mr. Nichols disputed the cost of capital calculations use by Saginaw Bay to calculate the transportation rate of \$0.0957 Dth. Mr. Nichols used inputs from Case No. U-20940, DTE Gas’ most recent rate case, for the basis of his calculations. Using these inputs, Mr. Nichols recommended:

[A] permanent capital structure which includes 50% debt at a 3.97% cost rate and 50% equity at a 9.9% cost rate. The 3.97% debt cost rate and 9.9% equity cost rate match those that are currently approved for DTE Gas, which is appropriate because this case was initially filed as an ex-parte affiliate transaction application. These inputs result in Staff’s calculation of 6.4% after-tax cost of capital and 8.7% on a pre-tax basis.²¹

Mr. Nichols testified the Company did not provide support for the rates used in its model and “[a]bsent support, it is not reasonable to rely on the Company’s cost rates for debt and equity.”²²

Mr. Nichols criticized how Saginaw Bay calculated the impact of deferred taxes on the proposed transportation rate. He testified:

The Company did not include deferred taxes as a zero-cost capital in the capital structure or subtract deferred taxes from rate base when calculating a required return on rate base. Typically, when calculating a revenue requirement, deferred taxes are either included in the capital structure as zero-cost capital or subtracted from the rate base that earns a return. For purposes of the Staff calculation, I have assumed 100%

¹⁹ Id.

²⁰ Id.

²¹ 3 Tr 55. Mr. Nichols provided a table summarizing the inputs used to calculate the after-tax cost of capital of 5.41% based on the rates approved in MPSC Case No. U-20940. Id.

²² 3 Tr 55-56.

expensing for tax purposes and unwound the deferred taxes over the life of the asset, which is twenty years.²³

Mr. Nichols testified Staff applied deferred taxes as a reduction to rate base to calculate the return on investment.²⁴

Incorporating the above adjustments, and those recommended by Mr. Spence, Mr. Nichols calculated the appropriate transportation rate to be \$0.0703/Dth. Pointing to Confidential Exhibit S-2, Mr. Nichols detailed Staff's adjustments to the rate proposed by Saginaw Bay.²⁵

Kevin P. Spence provided testimony regarding Staff's recommended adjustments to Saginaw Bay's proposed expense for ILI and O&M, and he detailed Staff's concerns regarding some of the terms in the Transportation Agreement. These adjustments are reflected in Staff's cost of service and supported by Mr. Nichols.²⁶

Referring to Confidential Exhibit S-2, Mr. Spence testified Staff reduced the total of 2021 ILI Deferred expense to \$1,493,367 from the Company's proposed amount of \$2,454,000.²⁷ He testified, based on Exhibit S-5, the Company planned seven anomaly digs at a cost of \$165,000 per dig. However, based on information provided to Staff, Saginaw Bay previously performed one dig and cut-out to remove a stuck cleaning pig at a cost of \$75,000.²⁸ Based on these actual costs Staff reduced the Company's projected cost for the seven anomaly digs from \$1,155,000 ($7 * \$165,000$) to \$525,000 ($7 * \$75,000$). Mr. Spence testified the Company also proposed that \$850,000 for ILI

²³ 3 Tr 56.

²⁴ 3 Tr 58. See Confidential Exhibit S-1.

²⁵ 3 Tr 57-58.

²⁶ 3 Tr 71, 73. See Confidential Exhibit S-1.

²⁷ 3 Tr 70. See Confidential Exhibit S-1.

²⁸ 3 Tr 71. See Exhibit S-5.

Rerun be included in the ILI deferred expense; however, Saginaw Bay provided information, as part of an audit request, that the Company utilized a contractor to complete the inspection at a cost of \$519,267. Staff reduced the proposed amount to the actual amount paid for the contract services.²⁹

Mr. Spence testified the Company projected 2023 ILI ongoing expenses which included \$37,000 for CIS/DCVG Survey and \$45,00 for A/C Mitigation.³⁰ He stated Staff reduced this expense to zero, testifying there is no regulatory requirement requiring the work and the Company has not supported a need for the projects.³¹ This reduced the Company's proposed total 2023 Additional Costs by \$82,000 for a total of \$140,000.³² Then, Mr. Spence testified Staff removed one-time costs from the ILI ongoing expense which included 2020 costs of \$200,000 for cleaning and \$22,500 related to disposal, and \$75,500 for removal of a stuck pig cleaning tool. He testified:

These costs are not typical and were required because first, the ILI tool got stuck in the pipeline and second, the previous service of the pipeline was gathering and there is a greater propensity for debris to be present. With the pipeline being converted to dry transmission service, there will not be the likelihood of a stuck ILI tool or the need for chemical cleaning.³³

Mr. Spence testified this resulted in a reduction to the 2019 ILI ongoing expense to \$1,202,500 from Company's projection of \$1,500,000.³⁴

Next, Mr. Spence testified that Staff disagree with the method used by the company to project the O&M expenses. Saginaw Bay projected O&M expenses based on actual expenses incurred in 2019. Mr. Spence testified that Staff recommend the

²⁹ 3 Tr 72. See Exhibits S-5 and S-6.

³⁰ Id.

³¹ Id. See Exhibits S-4 and S-5.

³² Id.

³³ 3 Tr 73.

³⁴ Id. See Exhibit S-6.

O&M expenses be based on the five-year average of O&M expenses for the years 2017 to 2021. Mr. Spence testified the O&M costs for 2019 and 2021 were significantly higher due to cost associated with the ILI inspections, removal of the stuck pig, cleaning, and material verification.³⁵ He testified:

ILI inspections are only required every seven years and material verification will not be an ongoing expense. Because all these costs are not reoccurring every year, it is not reasonable to assume that the O&M costs will be at the 2019 spending level into the future. Staff's five-year average is a reasonable approach to estimating future O&M expenses.³⁶

Based on this average, Staff recommended the O&M expenses be adjusted from the Company's projection of \$416,784 to [REDACTED]³⁷

Mr. Spence also detailed Staff's concerns with the terms of the Transportation Agreement proposed by Saginaw Bay in this matter. First, he explained that Staff have concerns regarding Article VI, Term and Termination, Section 6.2 of the Agreement.³⁸ Mr. Spence testified the language in this section seems to allow a third party to present a bona fide offer to Saginaw Bay prior to the end of the 20-year term of the Agreement which could result in displacement of DTE Gas's contracted capacity or require the payment of higher costs.³⁹ He testified that Staff recommend that Section 6.2 be revised to clarify that it only applies after the initial 20-year term of the contract.⁴⁰

Mr. Spence also testified that Staff recommend the Transportation Agreement include clear language allowing DTE Gas to extend it after the initial 20-year term and language that provides for a 50/50 sharing of third-party revenue between Saginaw Bay

³⁵ 3 Tr 74-75.

³⁶ 3 Tr 75.

³⁷ 3 Tr 74. See Confidential Exhibit S-7.

³⁸ See Exhibit A-2.

³⁹ 3 Tr 76-77.

⁴⁰ 3 Tr 77.

and DTE Gas.⁴¹ He refers to a Transportation Agreement between DTE Gas and DTE Michigan Lateral Company (DML)⁴² and points to the provision in that agreement which provides:

Shipper shall have the right and DML shall have the obligation to extend the term of this Agreement (in accordance with the notice provisions herein) with up to six (6) five-year extension terms (each an "Extension Term") exercisable by Shipper . . .⁴³

He also points to Article X, Price Section 10.5 of that Agreement, which provides:

During the Primary Term and any Extension Term of this Agreement, and DML proceeds to contract with such Additional Shippers, DML will notify Shipper of any such Additional Shippers and SML will credit to Shipper the incremental value, based on incremental demand charge payments, exclusive of any capital recovery, actually received from such Additional Shippers on a 50/50 basis . . .⁴⁴

Mr. Spence testified that Staff recommend the Transportation Agreement between Saginaw Bay and DTE Gas should contain similar provisions providing for up to six extensions and a sharing of third-party revenue on a 50/50 basis.⁴⁵

C. Attorney General

The Attorney General presented the direct testimony of Sebastian Coppola, an Independent Business Consultant.⁴⁶ He provided a brief description and history of the Saginaw Bay Pipeline and opined it has been underutilized in the past.⁴⁷ Pointing to Exhibit AG-1, Mr. Coppola stated Saginaw Bay will receive approximately \$1.1 million in revenue in 2022; primarily from a contract with Consumers Energy which could expire in

⁴¹ 3 Tr 79, 81.

⁴² See Exhibit S-8. DML and DTE Gas were affiliates at the time the Transportation Agreement was signed, but the affiliate relationship ended when DML was transferred to DT Midstream on July 1, 2021.

⁴³ 3 Tr 78-79. See Exhibit S-8, Article VI, Term and Termination, Section 6.2.

⁴⁴ 3 Tr 79. See Exhibit S-8, Article X, Price, Section 10.5.

⁴⁵ 3 Tr 80-81.

⁴⁶ Mr. Coppola's direct testimony is transcribed at 3 Tr 84-136. He sponsored Exhibits AG-1 to AG-10.

⁴⁷ 3 Tr 93-94.

February of 2023. He testified if that contract is not renewed, projected revenue is approximately \$177,000 in 2023.⁴⁸ Mr. Coppola also noted the Saginaw Bay Pipeline was recently converted to “transport only pipeline quality dry gas.”⁴⁹

Mr. Coppola testified that DTE Gas proposed, in prior rate cases,⁵⁰ to provide gas supply redundancy to the Traverse City and Alpena service areas with the Traverse City/Alpena Reinforcement Project (TCARP) which included the use of transportation services from the Saginaw Bay Pipeline assets.⁵¹ Mr. Coppola stated that “[i]n conjunction with the TCARP project, DTE Gas and DTE Gathering signed a Precedent Agreement on February 10, 2021, identifying the key facilities and services to be provided by subsidiaries of DTE Gathering, including Saginaw Bay[.]”⁵² He stated the original agreement also included utilization of pipeline assets owned by another affiliate of DTE Gathering, DTE Michigan Lateral Company (DMLC), and he noted a transportation agreement between DTE Gas and DMLC was reviewed by the Commission.⁵³

Mr. Coppola recommended that the Commission should not approve Saginaw Bay’s proposed transportation rate of \$0.0957 per Dth.⁵⁴ He outlined eight primary concerns: (1) the data included in the model used by Saginaw Bay is outdated and does not reflect the most current information available, (2) the Company did not use a traditional cost of service model to obtain its proposed rate and monthly demand charge

⁴⁸ 3 Tr 94. See Exhibit AG-1.

⁴⁹ 3 Tr 93.

⁵⁰ See MPSC Case No. U-20642 and MPSC Case No. U-20940.

⁵¹ 3 Tr 94-95.

⁵² 3 Tr 95. See also Confidential Exhibit AG-4.

⁵³ Id.

⁵⁴ 3 Tr 96.

in the Transportation Agreement, (3) the Company used an outdated net plant book value for the Saginaw Bay Pipeline, (4) the O&M expenses used by Saginaw Bay are based on the actual costs from 2019 and do not represent more recent actual costs, (5) the Company deferred costs for recovery through the transportation rate to be charged DTE Gas for ILI that were outdated and later lowered by the Company, (6) Saginaw Bay improperly estimated on-going ILI costs in its modelling, (7) the Company improperly included a 10 percent margin on O&M and pipeline integrity costs forecasted over the 20-year term of the Transportation Agreement, (8) the Company used cost of capital rates that are excessive, with no evidence to support the rates.⁵⁵

Mr. Coppola asserted that MCL 483.110 is applicable to the calculation of an appropriate transportation rate to be charged in this case, and stated use of the methodology “the Commission typically uses to establish rates for utilities is required.”⁵⁶ He testified the language should be interpreted to require use of a traditional cost of service model.⁵⁷

Mr. Coppola testified he calculated the levelized transportation rate, for 50,000 Dth/day of firm service for the 20-year contract period, to be \$0.0780 per Dth/day, or a fixed monthly demand charge of \$118,633.⁵⁸ Mr. Coppola stated he used the traditional cost of service model, explaining:

This approach starts with determining the average plant investment, net of accumulated depreciation and deferred taxes, using the Company's net plant book value of \$3,060,787 at December 31, 2021. This information is presented on lines 3 through 10 of Exhibit AG-8. The cost-of-service model applies an overall rate of return to the net rate base to calculate the

⁵⁵ 3 Tr 99-100.

⁵⁶ 3 Tr 102.

⁵⁷ 3 Tr 103.

⁵⁸ Id. See Exhibit AG-8.

return on investment. The model also includes the annual depreciation expense, O&M expense, property taxes, and other costs to arrive at the total annual cost of service. In this case, due to the fact that we need to establish a fixed 20-year demand charge, the annual cost of service amounts over that 20-year term were discounted to present value using the overall rate of return. That present value was divided by the present value of capacity contracted over the 20-year period to arrive at the levelized transportation demand rate.⁵⁹

Mr. Coppola testified he depreciated the net plant book value of \$3,060,787, reported to the Commission in Saginaw Bay's 2021 report, evenly over the 20-year term and then deferred taxes were calculated based on the difference in depreciation expense between book and tax values. He used an overall pre-tax rate of return of 9.23%, consisting of a 5% debt interest rate and a pre-tax ROE of 13.47%, or 10% after tax, and assumed a 50/50 capital structure. He testified Saginaw Bay's parent company recently issued long-term debt at 4.3% and noted the Company's own model indicates new investments in the pipeline are unlikely, and therefore the 5% debt rate is appropriate.⁶⁰ Observing that the 10.00% after tax ROE that he proposed is higher than the ROE approved in DTE Gas's last rate case, Mr. Coppola testified his proposed ROE and overall rate of return of 9.23% for the 20-year agreement with a fixed rate demand charge, guarantees a fixed revenue stream and "more than adequately compensated Saginaw Bay for its investment in the pipeline and in providing the contracted transportation service."⁶¹

For O&M expense, Mr. Coppola testified he used the amount of \$420,000 beginning in 2022 and escalated it by an annual inflation factor of 3 percent. He stated: "To arrive at the \$420,000 amount, I started with the actual O&M expense of \$279,719

⁵⁹ 3 Tr 104.

⁶⁰ 3 Tr 104-105.

⁶¹ 3 Tr 105.

reported by the Company for 2021, rounded it up to \$280,000, and added an additional 50% for unexpected future increases in operation and maintenance costs.”⁶²

Mr. Coppola testified he used a total amount of \$2,872,273 for deferred ILI costs, which included updated spending amounts in 2021 and 2022 provided by Saginaw Bay in Exhibit AG-7, and the deferred amount from 2020. And Mr. Coppola used a base amount of \$1.4 million for recurring major ILI work costs; he removed a small amount of 2020 costs from the Company’s projection, which he concluded were not likely to recur in later years.⁶³ Mr. Coppola used the amount for property taxes that was forecasted by Saginaw Bay and also used the company’s forecasted inflation rate of 3%.⁶⁴

Mr. Coppola testified the Transportation Agreement should provide a lower rate for interruptible transportation service services. He testified the firm transportation rate for 50,000 Dth/day incorporates recovery of all fixed and variable costs, plus a 10% after tax return. He stated approving the same rate for transportation services above the firm 50,000 Dth/day will create a “windfall” by charging for costs which are not incurred. Mr. Coppola testified the Commission should approve an interruptible service rate that reflects only “incremental variable costs that would likely be incurred” in the transportation of gas volume above the firm 50,000 Dth/day plus a profit margin.⁶⁵ He asserted these costs could include O&M and ILI costs resulting from the additional volume. Using Exhibit AG-9 Mr. Coppola testified he calculated the interruptible transportation rate to be \$0.0172 per Dth.⁶⁶

⁶² 3 Tr 105.

⁶³ 3 Tr 106.

⁶⁴ 3 Tr 104-106.

⁶⁵ 3 Tr 107.

⁶⁶ 3 Tr 107-108.

Mr. Coppola expressed three areas of concern regarding the Transportation Agreement.⁶⁷ First he addressed Section 6.2 of the agreement and asserted it could result in DTE Gas paying higher transportation costs. He stated the language in this section could allow a third party to offer a higher transportation rate than provided in the agreement, potentially resulting in a loss of the gas supply to DTE Gas or requiring payment of the higher rate offered by the third-party.⁶⁸ Mr. Coppola noted the Company stated this would only occur after the 20-year term ends, but he asserted the language is ambiguous and argued the Commission should order language to clarify that it is only applicable after the expiration of the 20-year term in the Transportation Agreement.⁶⁹

Next Mr. Coppola testified the Transportation Agreement between Saginaw Bay and DTE Gas should provide a right of extension to DTE Gas. He pointed to the Transportation Agreement between DTE Gas and DMLC where, under section 6.2, DTE Gas has the right to extend it up to six times after the end of the 20-year term. He also noted that section 6.3 of the agreement between DTE Gas and DMLC codifies that DTE Gas has the right of first refusal to match any bona fide offers from a third party after the end of the final extension.⁷⁰ Mr. Coppola stated that the Transportation Agreement in this case is part of the larger TCARP project and the “disparate terms of paragraphs 6.2 and 6.3 of the Saginaw Bay and DMLC transportation agreements create a disconnect that puts the entire TCARP project at risk of disintegrating after the initial 20-year term of the agreement and perhaps sooner.”⁷¹ Mr. Coppola recommended that the

⁶⁷ See Exhibit A-2.

⁶⁸ 3 Tr 109.

⁶⁹ 3 Tr 110.

⁷⁰ Id. See Exhibit AG-10.

⁷¹ 3 Tr 111.

Commission direct Saginaw Bay to modify the Transportation Agreement to conform to sections 6.2 and 6.3 of the transportation agreement that was approved between DTE Gas and DMLC.⁷²

Finally, Mr. Coppola recommended the Transportation Agreement in this case should provide for 50/50 sharing of revenues with DTE Gas that are received from other shippers using the Saginaw Bay Pipeline.⁷³ He again points to the agreement between DTE Gas and DMLC noting Section 10.5 of that agreement provides a “credit DTE Gas for 50% of any incremental revenue received from additional shippers after consideration of a 10% after-tax return on incremental capital costs and after any incremental O&M expense related to providing service to the additional shippers.”⁷⁴ He stated failure to include such a provision in the agreement between Saginaw Bay and DTE Gas will allow Saginaw Bay to receive 100 percent of the additional revenue while DTE Gas pays the fixed and variable operation costs. Mr. Coppola recommended the Commission direct Saginaw Bay to modify the Transportation Agreement to conform to section 10.5 of the transportation agreement that was approved between DTE Gas and DMLC.⁷⁵

D. Rebuttal

Mr. Richman responded to issues raised by the Attorney General and Staff witnesses. Addressing the proposed transportation rate, Mr. Richman asserted the other parties had misinterpreted “a discovery response including both the original basis for the filed rate as well as the current forecasted analysis showing a higher rate would

⁷² 3 Tr 111.

⁷³ 3 Tr 112.

⁷⁴ Id. See Exhibit AG-10.

⁷⁵ Id.

be justifiable.”⁷⁶ Mr. Richman defended the Company’s rate design and addressed several specific issues, raised by the Attorney General and Staff, to support the proposed transportation rate. And he responded to issues raised by both the Attorney General and Staff, related to the terms of the Transportation Agreement. Mr. Richman again asserted there was “some apparent confusion involved in the term for the contract . . . associated rights of first refusal . . . sharing of revenues and suggested changes or modifications to the extension of rights.”⁷⁷

Mr. Richman testified “this is a transmission pipeline matter and not a general utility rate case. The traditional utility cost of service model does not apply.”⁷⁸ He testified the Company used a “cost-of-service type” model to calculate the transportation rate.⁷⁹ In support, Mr. Richman presented testimony and Confidential Exhibit A-3 to explain the Company’s rate design and the derivation between the rate in the Transportation Agreement for which the Company seeks approval (\$0.0957/Dth) and the rate produced by Confidential Exhibit A-3 (\$0.101/Dth).⁸⁰ He testified the information in Confidential Exhibit A-3 is based on updated information which occurred between the time the Application was originally filed in February 2021 and the time his direct testimony was filed on March 15, 2022. He testified the updated rate reflects several modifications, including updated O&M numbers and amounts for ongoing and follow up ILI work.⁸¹ Noting that the updated transportation rate is higher, Mr. Richman testified that the Company proposes to proceed with the rate in the Transportation

⁷⁶ 3 Tr 31.

⁷⁷ 3 Tr 31-32.

⁷⁸ 3 Tr 39.

⁷⁹ 3 Tr 39-40.

⁸⁰ 3 Tr 32. See Exhibit A-2 and Confidential Exhibit A-3.

⁸¹ Id.

Agreement. He asserted the Company is accepting additional risk, “but Saginaw Bay is willing to accept the lower rate in order to keep the project proceeding in a timely manner without a need to renegotiate with the customer, DTE Gas”⁸²

Mr. Richman disagreed with adjustments to O&M made by the Attorney General and Staff witness and asserted they did not take into account the updates, including projected O&M changes. Mr. Richman testified the Company correctly projected O&M costs to be \$550,505.⁸³ He disagreed with the base rate proposed by the Attorney General of \$420,000, which used the projected O&M amount from 2022, and disagreed with the rate calculated by Staff using an average of the O&M amounts in the years 2017 to 2021. He asserted:

First in 2017 the line was in gathering service, which is not subject to as many O&M related requirements as a transmission system. In 2018, the line was converted, but not for the full year, to transmission service. Staff indicated that 2019 was significantly higher because of ILI related costs, however, because ILI related costs were deferred and are not included as part of the rate design in the present case, it is reflective of operating costs in that year. The costs for O&M in 2020 were significantly lower due to pandemic protocols limiting availability of personnel and equipment.⁸⁴

And he asserted while the amount reported for 2021 may be an estimate, it was also adversely affected by pandemic protocols and does not necessarily reflect a normal operational year.⁸⁵ Mr. Richman testified it was appropriate to use the O&M amount for 2019 as a base which when updated “would result in a number similar to \$550,505 used by Saginaw Bay in its updated rate design.”⁸⁶

⁸² Id.

⁸³ Id.

⁸⁴ 3 Tr 34.

⁸⁵ Id.

⁸⁶ 3 Tr 35.

Mr. Richman testified future ILI costs were originally proposed to be approximately \$1.5 million, but costs identified by Staff and the Attorney General lowered the base costs to approximately \$1.2 million. He asserted, however, neither party included costs for up to four validation digs which would increase the amount to approximately \$1.5 million.⁸⁷ Mr. Richman also testified that the updated estimated of the cost per dig is now \$85,000 and argued this amount is more reasonable than the amount of \$75,000 used by Staff.

Mr. Richman criticized Staff's exclusion of costs for the proposed CIS/DCVG and AC mitigation work. He asserted that Staff did not use the most current cost data, which was updated.⁸⁸ Mr. Richman disagreed with Staff's argument that the work is not required by regulation, stating, "Saginaw Bay views the regulations require the work to prudently understand the effectiveness of its installed cathodic protection system."⁸⁹ He testified it is prudent for Saginaw Bay to perform the work and Staff's exclusion is not appropriate.⁹⁰

Mr. Richman testified that Staff did not use the correct updated information to calculate the costs for rerun of the ILI which should reflect an actual cost of \$272,430, not the higher number used by Staff. And, he testified, based on updated information, Saginaw Bay is using the correct net book value, and noted it is the same as starting number used by the Attorney General witness. Mr. Richman testified that the Company calculated the total deferred costs to be approximately \$2.962 million using the updated information in Conf Exhibit A-3. Noting that Staff used \$2.993 million, and the Attorney

⁸⁷ Id.

⁸⁸ 3 Tr 36.

⁸⁹ Id.

⁹⁰ Id.

General used \$2.872 million, Mr. Richman recommended use of the Company's number.⁹¹

Mr. Richman asserted that a 10% return on O&M costs is reasonable in this case, disagreeing with Mr. Coppola. Mr. Richman asserted the Company could recover less than the full amount of its costs when proceeding under the assumption of an affiliated transaction, which existed at the time the Transportation agreement was negotiated. Noting the termination of the affiliate relationship, Mr. Richman testified:

As non-affiliated parties, Saginaw Bay could simply file the contract and proceed with services when facilities are ready. Instead, Saginaw Bay is treating the case as originally filed and so it is appropriate to apply the affiliated transaction pricing rule which applies 10% to all costs.⁹²

Mr. Richman also disagreed with the capital structures used by Staff and the Attorney General witnesses. He stated Staff used 3.97% debt cost rate and 9.9% equity cost rate approved for DTE Gas in its last rate case. Mr. Richman testified this structure is unreasonable for Saginaw Bay as "DTE Gas has a large asset base with large numbers of customers and its cost of debt is based on a portfolio of debt issuances over a long period of time with many in the past five-year period. However, Saginaw Bay has a single asset tied to a contract rate for a full 20 year term period."⁹³ Noting that the Attorney General suggested a 5% debt cost and 13.47% equity costs, Mr. Richman testified that Saginaw Bay will not be able to attract sufficient capital with either proposed structure, and opined that the Company would not be able to issue debt

⁹¹ 3 Tr 37.

⁹² 3 Tr 37-38.

⁹³ 3 Tr 38.

at a rate of less than 6% in the current market. He stated the structure proposed by Saginaw Bay is reasonable.⁹⁴

Mr. Richman disagreed with the changes to the treatment of deferred taxes proposed by Staff and Attorney General. He asserted accelerated tax advantage was realized over the first fifteen years of operation and asserted the book value is “effectively 0” so an accelerated depreciation has no advantage. Mr. Richman testified deferred taxes should likely be removed from the models. And Mr. Richman disagreed with Staff’s use of the pretax figure for the calculation of the discount rate and argued it is reasonable to use the after-tax discount rate.⁹⁵

Mr. Richman also disagreed with use of an interruptible rate that differs from the firm rate as proposed by the Attorney General witness. He stated interruptible shippers without a firm agreement pay \$0.50/Mcf per day for service and he states Saginaw Bay’s agreement with another firm shipper, Consumers Energy, incorporates the same rate for firm and interruptible service. He testified it is reasonable to use the same rate for firm and interruptible service.⁹⁶

Finally, Mr. Richman addressed the changes to the contractual terms of the transportation agreement proposed by both Staff and the Attorney General. First, he testified that Article Vi, Term and Termination, Section 6.2 of the agreement was negotiated “to cover an extraordinary case, which is not really expected to be a likely outcome.”⁹⁷ Mr. Richman testified the provision only applies at the conclusion of the 20-year term. He stated it provides for a third party to make an offer for capacity that

⁹⁴ 3 Tr 38.

⁹⁵ 3 Tr 39.

⁹⁶ 3 Tr 40.

⁹⁷ Id.

includes the 50 Dth/d allocated to DTE Gas – in order to retain the capacity DTE Gas would have the option to match the offer. Mr. Richman also testified there is a provision for extension of the agreement by DTE Gas if there is no third-party offer.⁹⁸

Mr. Richman challenged the inclusion of a provision that would allow DTE Gas to extend the agreement for up to six five-year terms that was suggested by both Attorney General and Staff witness. He testified there is nothing to stop the parties from agreeing to the same terms after expiration of the initial 20-year period. Mr. Richman asserted the current agreement is flexible and should not be modified.⁹⁹ And Mr. Richman disagreed with the suggestion that Saginaw Bay should share additional transportation revenue on a 50/50 basis with DTE Gas as proposed by the Attorney General and Staff. He stated the agreement involving DMCL and the Precedent Agreement were based on different circumstances and needs. Mr. Richman asserted Saginaw Bay can receive and deliver gas to locations other than the DTE Gas facilities and the Company is exposed to additional risks as a result. He asserted the revenue sharing agreement would make Saginaw Bay vulnerable to other shippers requesting the same treatment.¹⁰⁰

III.

DISCUSSION

Saginaw Bay requests the Commission find the transportation agreement between the Company and DTE Gas is reasonable, prudent, and satisfies the

⁹⁸ 3 Tr 41.

⁹⁹ Id.

¹⁰⁰ 3 Tr 42-43.

requirements of the Code of Conduct, and to find the Company's calculation of the transportation rate is reasonable and prudent.

Staff and the Attorney General argue that Saginaw Bay improperly calculated the transportation rate. Both parties disagree with the method used by Saginaw Bay to calculate the rate, and both disputed the reliability of some of the inputs used. Staff and the Attorney General recalculated the transportation rate using a cost-of-service model and based on the data provided by their respective witnesses. These parties also challenged some terms of the transportation agreement.

A. Transportation Rate

1. Commission Authority to Review the Transportation Agreement

Saginaw Bay argues it “does not need Commission approval of the initial rates under Act 9” because the parties are no longer affiliates.¹⁰¹ Citing MCL 483.110, Saginaw Bay contends it is only required to file its rates and contracts with the Commission and is not required to seek Commission approval. Then, the Company states: “Under the Code of Conduct and **not Act 9**, Saginaw Bay requests the Commission approve as reasonable and prudent the contract for services between a regulated utility and its affiliated company. R460.10108.”¹⁰² And, citing to section 4 of that rule, Saginaw Bay notes the “Code of Conduct requires that compensation be at a lower market rate price or 10% over fully allocated embedded costs.”¹⁰³ Then, based on the testimony of Mr. Richman, Saginaw Bay argues “approval of the contractual

¹⁰¹ Saginaw Bay Initial Brief, p 2.

¹⁰² Id. at p 4. Emphasis added.

¹⁰³ Id. at p 5.

terms under the Code of Conduct is no longer required. R460.10108.”¹⁰⁴ And then appears to refute that argument with:

The negotiated rate determined by Saginaw Bay are in fact lower than the requirement stated in the Code of Conduct. Witness Richman explained that the original rate design was intended to recover the projected cost at the time, plus 10%. However, the updated model using currently projected costs after the DTM and DTE Energy split reveals Saginaw Bay will recover less than a full recovery. Accordingly, the negotiated rate is reasonable because it is well within the requirements of the Code of Conduct.¹⁰⁵ [citations omitted]

Finally, in a footnote, the Company states:

The Commission may decline to approve Saginaw Bay’s rates under the Code of Conduct because the issue is moot. If the Commission does decline, Saginaw Bay requests the Commission treat the agreement submitted as initial rates under Act 9.¹⁰⁶

Initially, Staff summarize the Commission’s authority to regulate natural gas pipelines and the authority to “control and regulate corporations, associations and persons engaged, directly or indirectly, in the business of purchasing or selling or transporting natural gas for public use ...”¹⁰⁷

Repeating that the Company, as the petitioner, has the burden of proof and, the Attorney General observes MCL 483.110 sets forth the standards for approval when unaffiliated parties request approval for specific rates and charges in agreements.¹⁰⁸ The Attorney General notes she asked Saginaw Bay to point to a specific rule or citation to support its assertion that, as an unaffiliated entity, the Company did not need Commission approval of the contract, and asserts the Company provided an imprecise

¹⁰⁴ Id. at 9.

¹⁰⁵ Id.

¹⁰⁶ Id. at p 4, footnote 2.

¹⁰⁷ Id. at p 2, citing MCL 483.103.

¹⁰⁸ Attorney General Initial Brief, p 5.

response with “zero further support.”¹⁰⁹ Based on Mr. Coppola’s testimony, the Attorney General concludes the “statute requires the use of a traditional cost of service model, which is typically used in traditional ratemaking for setting rates for gas and electric utilities.”

In response Saginaw Bay reiterates that the cost-of-service models used by Staff and the Attorney General are improper as this is not a general rate case. And the Company argued the negotiated rate should not be scrutinized as if the parties were still affiliates.¹¹⁰ Then, the Company argues that the transportation rates are reasonable and prudent under the Code of Conduct because the negotiated rate is less than full recovery of embedded costs plus 10%, based on updated information.¹¹¹

Citing the definition of affiliate in the Code of Conduct, Staff observe that Saginaw Bay and DTE Gas were affiliates when the contract was negotiated and when this matter was filed.¹¹² Therefore, Staff reply it is reasonable for the Commission to review the contract under the Code of Conduct, which provides:

If a utility provides services or products to any affiliate or other entity within the corporate structure, and the cost of the service or product is not governed by section 10ee(8) of 2016 PA 341, MCL 460.10ee(8), compensation is based upon the higher of fully allocated embedded cost or fair market price. If an affiliate or other entity within the corporate structure provides services or products to a utility, and the cost of the service or product is not governed by section 10ee(8) of 2016 PA 341, MCL 460.10ee(8), compensation is at the lower of market price or 10% over fully allocated embedded cost. Asset transfers from a utility to an affiliate or other entity within the corporate structure for which the cost is not governed by section 10ee(8) of 2016 PA 341, MCL 460.10ee(8), is at the higher of cost or fair market value. Asset transfers from an affiliate or other entity within the corporate structure to a utility for which the cost is

¹⁰⁹ Id. at p 11. See Exhibit AG-14.

¹¹⁰ Saginaw Bay Reply Brief, p 2.

¹¹¹ Id. at p 3. See Confidential Exhibit A-3.

¹¹² Staff Reply Brief, p 2.

not governed by section 10ee(8) of 2016 PA 341, MCL 460.10ee(8) is at the lower of cost or fair market value.¹¹³

Staff do not support conversion of Saginaw Bay's filing in this matter, as suggested by the Company in a footnote in its Initial Brief. Arguing that the Company should have withdrawn this case and refiled under Act 9, Staff assert this matter should be adjudicated as initially filed, as an affiliate transaction case.¹¹⁴ In the alternative, Staff suggest the Commission decline to approve the request in this matter.¹¹⁵

In reply, the Attorney General argues that Saginaw Bay's calls into question what the Company is requesting and the "propriety of proceeding with this case at all."¹¹⁶ The Attorney General asserts that the Company is requesting the Commission approve its transportation rate, find the agreement is reasonable and prudent, and find the agreement complies with the Code of Conduct, but confuses standards and makes points that are contrary to each other such as arguing the Code of Conduct does not apply while requesting the Commission find compliance with the Code, and stating approval of rates is not needed, while requesting the Commission find its rates reasonable and prudent.¹¹⁷ Like Staff, the Attorney General questions if proceeding in this matter is appropriate "given the confusion inherent in the record, and the substantive change in circumstance since the case was originally filed,"¹¹⁸

The Attorney General criticizes Saginaw Bay's assertion that it does not need approval of its rates from the Commission again noting approval of the rates is what the

¹¹³ R460.10108(4).

¹¹⁴ Staff Reply Brief, p 3.

¹¹⁵ Id. at p 4.

¹¹⁶ Attorney General Reply Brief, p 1.

¹¹⁷ Id. at pp 2-3 and p 17.

¹¹⁸ Id. at p 3.

Company requested in this matter.¹¹⁹ The Attorney General also argues the assertions being made by Saginaw Bay in this matter were rejected in Case No. U-20894 where the Commission found it has authority to review the reasonableness and prudence of rates in a firm transportation contract under Act 9.¹²⁰ And the Attorney General points out while arguing for the assertion that it does not need Commission approval of the contract, Saginaw Bay “simply leaves off the portion of MCL 483.110 that contradicts its position[.]”¹²¹

The Attorney General asserts that Saginaw Bay repeatedly makes contradictory statements about the applicability of the Code of Conduct,¹²² and states:

On the one hand, the company is arguing that the Commission must assess the contractual terms through the lens of non-affiliated entities (which the parties are now), while on the other it argues that to find those terms unreasonable would be contrary to the Code of Conduct (which applies to affiliated entities and which Saginaw Bay has just gotten done arguing does not apply any more). The disconnect there is clear – Saginaw Bay is advocating for the Commission to map a Code of Conduct analysis onto non-affiliated entities. It is simply not proper for Saginaw Bay to negotiate an agreement with an affiliate and then argue that the terms cannot be unreasonable, since the parties are no longer affiliated.¹²³

The Attorney General recommends the Commission “hold this clear inconsistency against the Company when making a determination.”¹²⁴

This PFD finds that the Attorney General is correct when she argues that the record in this matter is “befuddled.”¹²⁵ Saginaw Bay makes contradictory arguments

¹¹⁹ Id. at p 4.

¹²⁰ Id. at p 4, footnote 9.

¹²¹ Id. at p 5.

¹²² Id. at p 6-8.

¹²³ Id. at p 9.

¹²⁴ Id. at p 6.

¹²⁵ Id. at p 1.

about the Commission's authority and has intermixed application of the Code of Conduct with the requirements of Act 9.

In Case No. U-20894, the Commission made this unequivocal finding: "[T]he Commission does have the authority to review the rates in the firm transportation contract, to ensure that the same are just and reasonable, under MCL 483.110."¹²⁶ This finding did not make an distinction between its authority under Act 9 or the Code of Conduct, and supports the conclusion that the Commission has authority to review the terms of a firm transportation contract for reasonableness and prudence, whether between affiliates or not.

If the parties are unaffiliated, the Commission has authority under MCL 483.110, which provides:

A common purchaser or common carrier of natural gas, before receiving the gas for transmission or delivery, shall file with the commission a schedule of the rates and price at which the common purchaser or common carrier will receive gas at delivery stations from a well, field, or source of supply, as well as the rates or charges at which the common purchaser or common carrier will deliver gas to connecting carriers or distributing lines or customers, and, if the common purchaser or common carrier is operating as a carrier for hire, the rates and charges which the common purchaser or common carrier will charge for the service to be performed by it. A common purchaser or common carrier operating as a carrier for hire also shall file a copy of each contract for purchasing, receiving, or supplying gas. The price to be paid and the rates and charges shall be stated and set up in the manner and form required by the commission and outlined in the rules of the commission for filing of rates of artificial gas utilities or pursuant to rules and conditions of service adopted by the commission, which the commission may make for the regulation of common purchasers and common carriers of natural gas. Thereafter, a common purchaser or common carrier of natural gas may alter or amend its price paid, rates, charges, and conditions of service by application to and approval by the commission in the same manner and by the same process and under the same legal limitations and like right as

¹²⁶ July 27, 2021 Order, MPSC Case No. U-20894, p 24.
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are now provided by statute for the regulation by the commission of the rates for electricity transmitted in this state and process of appeal provided in section 26 of Act No. 300 of the Public Acts of 1909, being section 462.26 of the Michigan Compiled Laws.

First, the Commission addressed the application of Act 9 in Case No. U-20894. Citing the Michigan Court of Appeals in *Antrim Resources v Public Service Commission*, the Commission stated:

Section 10 [of Act 9] requires that copies of the initial contracts between common purchasers and natural gas producers be filed with the [Commission] along with a schedule of the rates and price at which the common purchaser will receive gas. The statute is silent as to [Commission] approval of the initial price. It provides, however, that these contracts

be stated and set up in the manner and form required by the commission and outlined in its rules and regulations for filing of rates of artificial gas utilities or in accordance with such rules, regulations and conditions of service as may be hereafter adopted by the commission and which it is hereby empowered to make for the regulation of such common purchasers.

Clearly, the statute does not contemplate that producers and [a common purchaser] may enter into initial contracts for the purchase of gas which contain pricing provisions or rate schedules determined at the parties' whim and caprice. The statute mandates that these initial contracts adhere to the rules and regulations of the [Commission].¹²⁷

The Commission further held:

The Court went on to say that “[p]roducers who enter into contracts with common purchasers are charged with the knowledge that they are subject to the jurisdiction of the [Commission] to the extent that the pricing provisions in their contracts with common purchasers and any alterations or amendments in the price are subject to [Commission] approval,” concluding that the Commission, in looking to MCL 460.557, “has

¹²⁷ July 27, 2021 Order, MPSC Case No. U-20894, p 25; citing *Antrim Resources v Pub Serv Comm*, 179 Mich App 603, 610-11; 446 NW2d 515 (1989).

jurisdiction to determine whether the price which [a common purchaser] may pay for natural gas is just and reasonable.”¹²⁸

As noted above, this decision does not disturb the Commission’s long-standing use of the Code of Conduct to review agreements between affiliated parties for reasonable and prudence.

Accordingly, this PFD recommends the Commission find it has authority to review a transportation agreement involving a regulated utility for reasonable and prudence under Act 9 and the Commission reaffirm its authority to review contracts between affiliates under the Code of Conduct.

2. Transportation Rate for Firm Transportation Service

Saginaw Bay requests the Commission find its calculation of the transportation rate in the contract is reasonable.¹²⁹ Based on the testimony of Mr. Richman the Company asserts its revenue requirements to provide firm transportation service to DTE Gas, are reasonable, including the negotiated rate, which consists of fully embedded costs plus a return of 10%.¹³⁰ Saginaw Bay calculated the levelized 20-year rate in the transportation agreement for firm transportation service to be a daily demand charge of \$0.0957 per Dth, or a levelized monthly demand charge of \$145,544 or an annual charge of \$1,746,525.¹³¹ The transportation agreement also provides for 100,000 Dth per day of interruptible service at the same rate.¹³²

¹²⁸ July 27, 2021 Order, MPSC Case No. U-20894, p 26; citing *Antrim Resources v Pub Serv Comm*, 179 Mich App 603, 612-13; 446 NW2d 515 (1989).

¹²⁹ Saginaw Bay Initial Brief, p 17.

¹³⁰ Id. at p 12. See Exhibit A-2.

¹³¹ Id. The ALJ notes the actual Transportation agreement provide for a monthly rated of \$145,643. Exhibit A-2, p 17.

¹³² Id.

Saginaw Bay argues it is appropriate to use a “cost-of-service type” financial model to calculate the revenue requirements and a levelized transportation rate.¹³³ The Company states the revenue requirements were properly projected using estimated O&M operational costs for the pipeline, deferred O&M costs, and costs for a seven-year repeating ILI over the 20-year term, depreciation of the remaining book value of assets over the 20-year term, and property and income taxes.¹³⁴ Mr. Richman used projected the O&M costs of \$1,364,998 and projected ILI costs of approximately \$1.5 million, which were both escalated annually by 3%, to calculate the transportation rate. Saginaw Bay states Mr. Richman “calculated a levelized rate for the service to DTE Gas using a cost-of-service type financial model including these assumptions over the 20 years of the firm contract to achieve a 10% return on the fully allocated embedded costs.”¹³⁵

Next, Saginaw Bay asserts that the most recent information justifies a higher daily demand rate of \$0.101 per Dth and argues this figure includes updated O&M projections and updates to both current and forecasted amounts for ongoing ILI and follow-up integrity work.¹³⁶ However, Saginaw Bay is not requesting the Commission approve the higher rate. The Company states, “[t]his is a significant impact that creates additional risk for Saginaw Bay but Saginaw Bay is willing to accept the lower rate to keep the project proceeding in a timely manner without a need to renegotiate with the customer, DTE Gas.” (3 Tr. 33).¹³⁷

¹³³ Id. at p 13.

¹³⁴ Id. at p 28. See 3 Tr 28.

¹³⁵ Id. at p 13. See 3 Tr 28-29.

¹³⁶ Id. at p 23. See 3 Tr 32.

¹³⁷ Id. at p 13.

Saginaw Bay argues that the rate designs used by Staff and the Attorney General are outdated and should not be used. Relying on Mr. Richman's testimony, Saginaw Bay contests the O&M assumptions used by Staff and the Attorney General. The Company asserts updated information was provided to the parties in discovery, but the data was not used in the calculations by either Staff or the Attorney General.¹³⁸ Noting that Staff used an average of the O&M costs for the years 2017 to 2021, and the Attorney General focused on the years 2020 and 2021, Mr. Richman stated the pipeline was not part of a transmission system in 2017, and costs in 2020 and 2021 were impacted by COVID-19 limitations. He asserted that the only viable year to use in estimating O&M costs is 2019 because the pipeline was fully operational.¹³⁹ Citing Mr. Richman's testimony, Saginaw Bay maintains that the 2019 O&M costs should be "adjusted to reflect the interim, ongoing inflationary rate impacts, and the impacts of the DTM and DTE Energy split, which would result in a similar figure to \$550,505 as used by Saginaw Bay in its rate design."¹⁴⁰ The Company argues this is the most reasonable value for O&M costs.

Saginaw Bay asserts there is "confusion as to the ongoing ILI costs versus historic and ongoing costs related to ILI work."¹⁴¹ The Company maintains Staff and the Attorney General failed to include costs for up to four validation digs to correlate site data when determining future ILI costs which results in a figure of approximately \$1.2 million. The Company states, with inclusion of these costs, the reasonable future ILI

¹³⁸ Id. at p 14.

¹³⁹ Id. See 3 Tr 34.

¹⁴⁰ Id. See 3 Tr 34-35.

¹⁴¹ Id.

costs are approximately \$1.5 million, which is increased by a 3% inflation rate in the Company's model.¹⁴²

The Company criticizes several suggestions made by Staff to reduce the overall rate of transportation, and again argues that Staff did not include updated information in its calculations. The Company states that Staff reduced costs for currently planned verification digs from \$165,000 per dig to \$75,000 but did not recognize that Saginaw Bay reduced this cost in its updated information to \$85,000 per dig, and the Company states Staff reduced the costs associated with a second ILI rerun to \$519,267 but did not see the Company's reduction to a significantly lower amount of \$272,430.¹⁴³ The Company disputes Staff's removal of costs associated with CIS/GCVG and AC mitigation and argues they are necessary to ensure the pipeline is maintained prudently.¹⁴⁴ Saginaw Bay argues that Staff's recommendations are unreasonable and should not be adopted. And, the Company notes the other parties recommend modifying total deferred costs; the Attorney General recommends the amount be \$2.872 million and Staff recommend \$2.993 million. Observing that these amounts are comparable to the Company's projected figure of \$2.962 million, Saginaw Bay argues its total deferred costs are the most reasonable.¹⁴⁵

Saginaw Bay criticizes the capital structures recommended by both Staff and the Attorney General and, based on the testimony of Mr. Richman, argues they are unreasonable given that the Company has a single asset tied to a 20-year contract

¹⁴² Id. at p 15.

¹⁴³ Id.

¹⁴⁴ Id. See 3 Tr 36.

¹⁴⁵ Id. at p 16.

term.¹⁴⁶ Addressing Staff's recommendation that the rate be 3.97% for debt and 9.9% for equity capital, based on rates approved for DTE Gas in its last rate case, Saginaw Bay argues it would be unreasonable to impose a utility-type return in this case because the Company does not have a large base of assets and lacks flexibility to revisit its rates with the Commission. And the Company argues the structure recommended by Mr. Richman, with an after-tax return of 10%, is the cost reasonable and should be adopted.¹⁴⁷

Staff dispute Saginaw Bay's calculations of the revenue requirement, including the discount rate, the cost of capital, deferred taxes, O&M expenses, and ILI expenses.¹⁴⁸ Based on the testimony of Mr. Nichols, and utilizing a traditional cost of service model, Staff originally recommended a transportation rate of \$0.0703/Dth. However, after review of rebuttal testimony, Staff adopted the Company's update for ILI rerun (addressed below) and recalculated its recommended transportation rate to be \$0.0695/Dth.¹⁴⁹

Staff assert that Saginaw Bay improperly applied its projected after-tax cost of capital as the discount rate. Based on Mr. Nichols' testimony, Staff argue the discount rate typically equals the rate applied for the required rate of return on investment; but in its model, Saginaw Bay mixes an after-tax cost of capital discount rate with the pre-tax cost of capital return on investment which is not appropriate.¹⁵⁰ And, Staff disagree with

¹⁴⁶ Id. See 3 Tr 38.

¹⁴⁷ Id.

¹⁴⁸ Staff Initial Brief, p 3. See Confidential Exhibit S-1.

¹⁴⁹ Id. at p 23. See 3 Tr 57. Staff provide a table detailing its recommended adjustments to the transportation rate calculated by Saginaw Bay and Staff's resulting transportation rate. Id. at 24.

¹⁵⁰ Id. at p 3-4. See 3 Tr 54.

the Company's rebuttal argument that changing the rate from after-tax to pre-tax has a small impact on the rate and is therefore unnecessary.¹⁵¹

Staff dispute the capital structure and cost rates proposed by Saginaw Bay and recommend "a permanent capital structure which includes 50% debt at a 3.97% cost rate and 50% equity at a 9.9% cost rate."¹⁵² Staff reiterate that these cost rates equal those approved for DTE Gas in its last rate case and are appropriate in this matter because Saginaw Bay initially filed this matter as an affiliate transaction.¹⁵³ Using its inputs, Staff calculate an after-tax cost of capital of 6.4% or 8.7% on a pre-tax basis.¹⁵⁴ Staff argue that Saginaw Bay did not provide support for its capital structure in rebuttal and failed to do so when asked by the Attorney General to explain why the proposed debt and equity rates were reasonable.¹⁵⁵ Staff assert, absent such support, it not reasonable to rely on Saginaw Bay's cost rates for debt and equity. Staff acknowledge Saginaw Bay's contention that DTM, its parent company, has a corporate secured debt rate of 4.3% and Staff note the Attorney General supports a pre-tax equity cost of 13.47% which equals an after-tax rate of 10%. But Staff continue to recommend "3.97% debt rate and 9.9% after-tax return on equity, or in the alternative no greater than the 4.3% corporate debt rate and the Attorney General's 10% after-tax return on equity."¹⁵⁶

Staff maintain the Company did not properly account for deferred taxes in its model and state "[w]hen calculating cost-based rates, deferred taxes are either

¹⁵¹ Id. at p 4.

¹⁵² Id.

¹⁵³ Id. at p 5. See 3 Tr 55. See also, December 9, 2021 Order, MPSC Case No. U-20940.

¹⁵⁴ Id.

¹⁵⁵ Id. See 3 Tr 100-101.

¹⁵⁶ Id. at p 5-6.

subtracted from the rate base or included in the capital structure at a zero cost.”¹⁵⁷ Staff subtracted the deferred taxes from rate base when calculating the required return on investment.¹⁵⁸ Noting that the Company asserts “[t]he tax basis of the assets on the books is effectively 0 at this point, so an accelerated depreciation would result in no tax advantage regardless[.]” Staff argue this scenario exemplifies the reason deferred taxes are recognized in the modelling.¹⁵⁹ Staff state:

Deferred taxes are calculated based on the difference between book basis (GAAP) and tax basis. When an asset has a tax basis of zero, but a book balance greater than zero due to depreciation, this is referred to as a temporary difference. The difference between book and tax is usually caused because tax basis allows for accelerated depreciation, which increases current depreciation expense and therefore reduces taxable income allowing for paying lower current taxes. However, the reduction in current taxes payable is offset by recording deferred taxes. Deferred taxes are considered a zero-cost loan from the government for ratemaking. [footnotes omitted]¹⁶⁰

Staff contend deferred taxes should be assumed in this matter since the Company did not present any evidence to dispute the existence of a book/tax difference with the pipeline assets.¹⁶¹ Noting that Saginaw Bay’s model indicates a deferred tax impact on the cash flow calculation, but no impact in the rate calculation, Staff argue this results in an inflated rate. And Staff argue if there are no deferred tax impacts, the Company should have explained why it was included in the cash flow model. Staff maintain that its method properly accounts for deferred taxes.¹⁶²

¹⁵⁷ Id. at p 7. See 3 Tr 56.

¹⁵⁸ Id. at p 6. See Confidential Exhibit S-1.

¹⁵⁹ Id.

¹⁶⁰ Id. at p 6-7.

¹⁶¹ Id. at p 7.

¹⁶² Id. at p 8.

Relying on Mr. Spence's testimony, Staff argue that O&M expenses should be adjusted to [REDACTED] from the Company's projected amount of \$416,784. Staff base its figure on the five-year average of the O&M expenses for the years 2017 to 2021.¹⁶³ Staff assert that O&M costs were significantly higher in 2019, the year used by Saginaw Bay as the basis for its O&M cost estimates, and it is not reasonable to assume those costs will continue in future years.¹⁶⁴ After reviewing Mr. Richman's rebuttal testimony, Staff find it unpersuasive and continue to recommend O&M expenses base on the five-year average of the years 2017 to 2021 and maintain that the expenses in 2019 do not represent O&M costs going forward.¹⁶⁵

Based on the testimony of Mr. Spence, Staff recommend reductions to proposed ILI costs. Staff note Saginaw Bay plans seven anomaly digs in the 2021 ILI deferred expenses, however, based on information supplied to Staff in an audit response, the Company completed one dig and cut-out to remove a stuck cleaning tool at a cost of approximately \$75,000.¹⁶⁶ Using the actual amount reported, Staff recommend a reduction from \$1,155,000 to \$630,000 for these digs,¹⁶⁷ which reduces the costs from the Company's ILI deferred expenses from \$2,454,100 to \$1,824,100.¹⁶⁸ Noting that Saginaw Bay provided updated estimates in rebuttal testimony that the projected costs are now \$85,000 per dig, Staff maintain its recommendation that the ILI deferred

¹⁶³ See Confidential Exhibit S-2.

¹⁶⁴ Staff Initial Brief, p 9.

¹⁶⁵ Id. at p 11.

¹⁶⁶ See Exhibit S-6.

¹⁶⁷ Staff Initial Brief, p 12. The difference is calculate based on a reduction of \$90,000 per dig; from \$165,000 to \$75,000. See 3 Tr 71

¹⁶⁸ Staff Initial Brief, p 12. See 3 Tr 71.

expenses be reduced to the actual cost of \$75,000 per dig.¹⁶⁹ And Staff continue to recommend an adjustment to Saginaw Bay's proposed ILI costs related to the ILI rerun included in the 2021 ILI deferred expenses.¹⁷⁰ The Company originally proposed a cost of \$850,000, which Staff recommended be reduced to \$519,267 based on information provide in an audit response.¹⁷¹ However Saginaw Bay provided updated information which show actual costs of \$272,430 in Confidential Exhibit A-3.¹⁷² Acknowledging the Company's update, Staff currently recommend an expense of \$272,430 for the ILI rerun included in the 2021 ILI deferred expenses. This adjustment is reflected in the updated transportation rate of \$0.0695 per Dth recommended by Staff.¹⁷³

Staff adjusted the Company's projected ILI costs related to CIS/DCVG survey and A/C mitigation based on Mr. Spence's testimony, who noted there is no regulatory requirement for the work and the Company has not provide any technical data to support the need for the proposal.¹⁷⁴ Staff reduced the 2023 entire estimated costs for both, totaling \$82,000, from Saginaw Bay's projected ILI expenses for 2023 which reduced ongoing ILI expense from \$222,000 to \$140,000.¹⁷⁵ Noting the Company provide an updated projection for the CIS/DCVG mitigation work and argued the work was necessary to assess its cathodic protection system in rebuttal, Staff maintain its adjustments are appropriate. And Staff removed one-time costs from the 2020 ILI ongoing expenses for cleaning, disposal, and removal of a stuck cleaning tool (aka

¹⁶⁹ Id. at p 12.

¹⁷⁰ Id. at p 13. See 3 Tr 71-72.

¹⁷¹ Id. See also Confidential Exhibit S-1.

¹⁷² 3 Tr 36.

¹⁷³ Staff Initial Brief, p 14, 24.

¹⁷⁴ Id. at p 14-16. See 3 Tr 72-73.

¹⁷⁵ Id. at p 14-16.

“pig”).¹⁷⁶ Staff argue that these costs are not typical and were necessitated by the stuck pig, and because the pipeline is being converted to dry transmission, the likelihood of debris and the need for cleaning is doubtful therefore it is not likely these costs will recur.¹⁷⁷ “The estimated \$1,500,000 for ongoing ILI inspections was adjusted by Staff to \$1,202,500 by removing the \$200,000 for cleaning, \$22,500 for disposal, and \$75,000 for removal of the stuck pig.”¹⁷⁸ Staff acknowledge Saginaw Bay’s argument costs for up to four validation digs, to correlate ILI with site data, were not included in its recommendation. Staff assert that the Company’s analysis is speculative and note Mr. Richman’s testimony that these costs “are yet to be incurred and were not in the base data.”¹⁷⁹ Staff continue to recommend the removal of these one-time costs.

The Attorney General argues, based on the testimony of Mr. Coppola, that the appropriate levelized transportation rate is \$0.780 per Dth or a fixed monthly demand charge of \$118,633 for the firm transportation of 50,000 Dth/day.¹⁸⁰ Mr. Coppola testified he used the traditional cost of service model to calculate this rate. He used the figure reported by Saginaw Bay in December of 2021 for net plant investment of \$3,060,787 which was depreciated evenly over the 20-year contract period, and deferred taxes were calculated using the typical MACRS 15-year schedule.¹⁸¹ Mr. Coppola used an overall pre-tax rate of return of 9.23% which assumed a 50/50 capital structure and consists of a debt rate of 5% and a pre-tax rate of return of 13.47% (or 10% after-tax). Mr. Coppola used the amount of \$420,00 for O&M expense beginning in

¹⁷⁶ Id. at p 16.

¹⁷⁷ Id. at p 17. See 3 Tr 73. See also Exhibit S-6.

¹⁷⁸ Id.

¹⁷⁹ Id. at p 18. See 3 Tr 35.

¹⁸⁰ Attorney General Initial Brief, p 13. See 3 Tr 104-106. See also Exhibit AG-8.

¹⁸¹ 3 Tr 104.

2022 with a 3% annual inflation factor which he estimated based on the Company's actual O&M expense reported for 2021, and added 50% "for unexpected future increases."¹⁸² He used updated spending amounts for ILI and integrity work in 2021 and 2022, and the deferred amount from 2020 for a total of \$2,872,273 for deferred ILI costs, and Mr. Coppola used the Company's updated estimates for ongoing ILI and integrity costs.¹⁸³ And for the 7-year recurring ILI and integrity work, Mr. Coppola used a base amount of \$1.4 million, removing a small amount from Saginaw Bay's projection of \$1.5 million for expenses that are not expected to recur.¹⁸⁴

The Attorney General argues Saginaw Bay calculated a defective and unreasonable rate in the transportation agreement with DTE Gas, which could ultimately be paid by its customers and should be rejected by the Commission.¹⁸⁵ Referring to Mr. Coppola's testimony, the Attorney General asserts Saginaw Bay provides "very limited information on the cost components and assumptions used" to support the transportation rate of \$0.0957 per Dth.¹⁸⁶ Incorporating Mr. Coppola's testimony, the Attorney General argues there are several defects in the Company's modelling and inputs that result in an incorrect rate such as: (1) the data included in the model is outdated and does not reflect the most current information available; (2) the Company did not use a traditional cost of service model for its calculations; (3) the Company used an outdated net plant book value; (4) the O&M expenses used by Saginaw Bay do not represent more recent actual costs; (5) the Company deferred costs for recovery

¹⁸² 3 Tr 105.

¹⁸³ 3 Tr 106. See Confidential Exhibit AG-7.

¹⁸⁴ 3 Tr 106.

¹⁸⁵ Attorney General Initial Brief, p 7.

¹⁸⁶ Id. at p 6-7. See 3 Tr 96-101.

through the transportation rate to be charged DTE Gas for ILI that were outdated; (6) Saginaw Bay improperly estimated on-going ILI costs in its modelling; (7) the Company improperly included a 10 percent margin on O&M and pipeline integrity costs forecasted over the 20-year term of the Transportation Agreement; and (8) the Company used cost of capital rates that are excessive, without evidence for support.¹⁸⁷

The Attorney General maintains that Mr. Richman's rebuttal testimony primarily discusses a higher transportation rate of \$0.101 per Dth for which Saginaw Bay is not seeking approval.¹⁸⁸ Noting, the company did not file supporting information until rebuttal with Confidential Exhibit A-3, the Attorney General argues, the documents in that exhibit provide support for the higher rate and leave the rate requested unsupported.¹⁸⁹ And the Attorney General asserts Mr. Richman's rebuttal testimony focused on justifying the higher rate of \$0.101 per Dth. The Attorney General maintains, Saginaw Bay's attempt to justify a higher rate that it does not wish to implement, and then requesting a lower rate, is not a proper approach to ratemaking, and argued the Commission should reject it.¹⁹⁰

The Attorney General argues Saginaw Bay did not use a traditional cost of service model to calculate its projected transportation rate, as did Mr. Coppola and Mr. Nichols, and instead used a cash flow model that searched for a billing rate to calculate the desired revenue to meet the targeted return on investment.¹⁹¹

¹⁸⁷ Id. at p 6-7.

¹⁸⁸ Id. at p 7.

¹⁸⁹ Id. at p 7-8.

¹⁹⁰ Id. at p 8-9.

¹⁹¹ Id. at p 10. See Exhibit AG-11.

The Attorney General criticizes the Company's estimated O&M expense of \$550,505 for 2023 and asserts no support for this amount has been provided. Noting that the Company stated in a discovery response that the estimates were based on historical data, the Attorney General argues Saginaw Bay did not provide information to link its forecasted amounts to the historical cost data.¹⁹² And the Attorney General disagrees with Mr. Richman's assertion that O&M costs will increase due the separation of DTM from DTE Energy, stating no evidence to support this projected increase was supplied and Saginaw Bay did not justify its inclusion in the transportation rate.¹⁹³

The Attorney General contends that Saginaw Bay did not justify its inclusion of a 10% margin on costs as an affiliate despite the fact that it is no longer affiliated with DTE Energy.¹⁹⁴ And addressing Saginaw Bay's rebuttal concerning capital structure, the Attorney General points out that the Company alleged that DTM, its parent company, issued debt at 4.3% and it was trading for at 6.75% in the secondary market, but did not provide support for this allegation, even after requested in discovery.¹⁹⁵

In reply, Saginaw Bay argues both Staff and the Attorney General improperly used the traditional cost of service model as if this were a traditional utility rate case.¹⁹⁶ Arguing that the negotiated rate in the transportation agreement was inherently a business decision, Saginaw Bay states:

While the model used by Saginaw Bay is a cost of service type model, the objective and determination of reasonableness is different. For affiliated transactions, reasonableness of that negotiated rate is determined by the Code of Conduct, which provides a reasonable rate allows a utility to

¹⁹² Id. at p 9. See Exhibit AG-13.

¹⁹³ Id. at p 9-10.

¹⁹⁴ Id. at p 11.

¹⁹⁵ Id. at p 12. See Exhibit AG-14.

¹⁹⁶ Saginaw Bay Reply Brief, p 3.

receive return on a project that is limited to recovery of the fully embedded costs plus 10%. R.460.10108(4). Saginaw Bay's negotiated rate achieves this objective. (3 Tr. 26). As the record demonstrates, the updated model supports that the negotiated rate will actually result in *less than* a full recovery because of the DTM split from DTE Energy and, of course, increased costs in material, labor, and other costs as a result of general inflationary pressures.¹⁹⁷

The Company repeats that Staff and the Attorney General relied on “outdated” information supplied at the time of filing while ignoring data supplied in discovery and rebuttal. Saginaw Bay asserts the transportation rates recommended by Staff and the Attorney General are unreasonable as the Company has a single asset that will be tied to a 20-year agreement.¹⁹⁸

Noting that the Company was an affiliate with DTE Gas at the time the contract was negotiated, and the time of this filing, Staff argue the transportation agreement at issue here should be assessed under the provisions of the Code of Conduct which requires review under a traditional cost of service model of the embedded costs, and then comparison to the “market price.”¹⁹⁹ Citing to a footnote in Saginaw Bay's Initial brief, Staff note the Company appears to be requesting a conversion from review under the Code of Conduct to review under Act 9, if the Commission does not believe review under the Code of Conduct is appropriate.²⁰⁰ Noting that different rules apply to approval under Act 9, Staff do not support this suggestion. Staff assert the Commission should decline to approve the transportation rate under Act 9 and should approve Staff's updated transportation rate of \$0.0695.²⁰¹

¹⁹⁷ Id.

¹⁹⁸ Id. at p 4.

¹⁹⁹ Staff Reply Brief, p 2, citing R460.10108(4).

²⁰⁰ Id. at p 3, citing to Saginaw Bay Initial Brief, p 4; footnote 2.

²⁰¹ Id. at p 4.

The Attorney General also argues that this matter should be reviewed under the Code of Conduct and notes Saginaw Bay specifically requests this relief.²⁰² Like Staff, the Attorney General observes this contract was negotiated when Saginaw Bay and DTE Gas were affiliates, and criticizes the Company's assertion that the parties are now separate entities acting in their own best interests, stating: "Simply making statements that 'the terms of the contract are reasonable and mutually [beneficial],' and that the Agreement was 'negotiated in good faith,' does not make them true."²⁰³

Repeating that Saginaw Bay's calculations are "unsubstantiated and unsupported," because no objective data or analysis was provided to support the underlying inputs, the Attorney General argues the capital structure used, and transportation rate calculated, by Mr. Coppola are more reasonable and prudent than the rate projected by the Company.²⁰⁴

First, it is undisputed that the Commission utilizes a traditional cost-of-service method to calculate rates charged to customers by a utility such as DTE Gas. In this case Saginaw Bay requests approval of rates that will eventually be charged to DTE Gas.²⁰⁵ As noted above, the Commission cited with approval the finding in *Antrim Resources* that "[p]roducers who enter into contracts with common purchasers are charged with the knowledge that they are subject to the jurisdiction of the [Commission] to the extent that the pricing provisions in their contracts with common purchasers and

²⁰² Attorney General Reply Brief, p 6, citing to Saginaw Bay Initial Brief, p 4.

²⁰³ Id. at p 8.

²⁰⁴ Id. at p 11.

²⁰⁵ See Exhibit A-2.

any alterations or amendments in the price are subject to [Commission] approval[.]”²⁰⁶ Therefore, the only reasonable interpretation is that the method used to calculate transportation rates must involve a cost-of-service model so that the Commission can properly review the inclusion of any costs associated with transportation in base rates eventually charged to consumers. And, to determine whether the price is “just and reasonable” when the parties to the transportation agreement are affiliates, the Commission looks to the Code of Conduct provisions which were codified to avoid contract terms which result in higher rates for customers. When reviewing under the Code of Conduct, the Commission takes notice of the fact that the parties are under common control, and subject to the terms of R460.10108(4). As Saginaw Bay notes, “the code of conduct requires that compensation be at a lower market rate price or 10% over fully allocated embedded costs.”²⁰⁷ To conduct this review, the Commission uses a cost-of-service methodology in the calculation of the embedded costs.

Therefore, in this case it most appropriate to review the transportation agreement in light of the circumstances that existed when it was negotiated and executed – that is under the Code of Conduct. The Company notes that Mr. Richman testified the parties considered the limitations of affiliate transactions when negotiating the transportation agreement and explained the original rate design was intended to cover projected costs plus 10%.²⁰⁸ Saginaw Bay asserts “[t]he terms of agreement were negotiated in good faith and did not change because of the split of DTM from DTE Energy.”²⁰⁹ Saginaw

²⁰⁶ July 27, 2021, MPSC Case No. Order U-20984, p 26, citing *Antrim Resources v Pub Serv Comm*, 179 Mich App 603, 612-13; 446 NW2d 515 (1989).

²⁰⁷ Saginaw Bay Initial Brief, p 5.

²⁰⁸ Id. at p 9. See 3 Tr 26.

²⁰⁹ Id. See 3 Tr 37, 43.

Bay also argues that updated modelling, using projected costs after the split from DTE Energy, reveals the Company will not recover its fully embedded costs under the current transportation agreement.²¹⁰

Accordingly, this PFD recommends the Commission utilize a cost-of-service methodology to review the transportation rates in the proposed agreement.²¹¹

Because Saginaw Bay's transportation rate and underlying inputs are not based on a cost-of-service model this PFD suggests that the Commission could refuse to approve the transportation agreement. And given the record, this PFD agrees that Staff and the Attorney General correctly question whether the Commission should proceed with this matter. If the Commission chooses to reject Saginaw Bay's filing, there is no need for further review. However, in the interests of completeness this PFD evaluates changes recommended by Staff and the Attorney General.

Staff's adjustment to O&M and ILI expenses are reasonable. As both the Attorney General and Staff observe, many of the inputs used by Saginaw Bay for its calculations are unsubstantiated projections with insufficient data to properly review them for reasonable and prudence. Staff's explanation of how and why its inputs differ, is clear and in conformity with a cost-of-service model. This PFD agrees that deferred taxes were not properly subtracted from rate base or included as zero-cost capital. Staff refute Saginaw Bay's assertion that the deferred taxes are essentially zero and properly question the inclusion of deferred taxes in cash flow calculations when they are not included in the rate calculation. And Staff's adjustments to Saginaw Bay's O&M and

²¹⁰ Id. at p 9-10. See 3 Tr 29.

²¹¹ Exhibit A-2.

ILI expenses are logical and appropriate. Saginaw Bay argues Staff did not use updated data provided in a discovery request and included with rebuttal testimony as Conf Exhibit A-3. However, this PFD notes that it is inappropriate to provide new information with rebuttal and suggests that Staff aptly considered and applied the data, where appropriate, such as discussing why a newly projected rate of \$85,000 per dig for the seven anomaly digs was unsupported and lowering the amount for rerun ILI to an actual amount of \$272,430. Noting that Saginaw Bay and DTE Gas were affiliates when the Transportation agreement was negotiated and signed, Staff have supported the capital structure it proposes. As Staff observe, it is reasonable to use the capital structure approved for DTE Gas in its last rate case. And both the Attorney General and Saginaw Bay based their respective capital structures, at least in part, on data that is speculative and unsupported.

Accordingly, this PFD recommends the Commission adopt the adjustments made by Staff to the transportation rate calculated by Saginaw Bay and approve the transportation rate of \$0.0695 per Dth for service under the agreement.

3. Transportation Rate for Interruptible Service

In addition to firm transportation service for 50,000 Dth per day, the contract also provides for 100,000 Dth per day of interruptible transportation service at the rate of \$0.0957 per Dth.²¹² Saginaw Bay argues this amount is reasonable and prudent.

The Attorney General argues that the interruptible rate should be lower than the firm rate based on the testimony of Mr. Coppola.²¹³ He testified that an interruptible

²¹² Exhibit A-2, p 17.

²¹³ Attorney General Initial Brief, p 13.

transportation rate is more appropriate for this interruptible service than the rate charged for firm service.²¹⁴ Mr. Coppola testified:

The interruptible service rate should reflect only incremental variable costs that would likely be incurred for the transportation of additional gas volumes plus a profit margin. The incremental variable costs would be O&M expense and potentially ILI costs that could increase due to additional flowing volumes on the pipeline. In Exhibit AG-9, I included these variable costs and the return on investment as a profit margin proxy and calculated the interruptible service rate of \$0.0172 per Dth. This is a more appropriate rate for interruptible service than the full firm transportation rate.²¹⁵

The Attorney General asserts that Saginaw Bay was asked in discovery to explain why the firm rate and the interruptible rate should be the same, when the firm rate allows the Company to recover all fixed costs. The Attorney General argues the Company did not provide an answer which “is a clear indication that it cannot justify its proposed interruptible rate.”²¹⁶

Based on the testimony of Mr. Richman, Saginaw Bay disagrees with use of an interruptible rate and argues use of the same rate as the firm rate was reasonable and prudent.²¹⁷ Mr. Richman testified the contract was for 50,000 Dth per day of firm service and opined DTE Gas would likely not need more.²¹⁸ Staff did not address the issue.

This PDF does not recommend that the Commission direct the inclusion of an interruptible rate in this transportation agreement. As noted, before, Saginaw Bay’s assertions are somewhat contradictory, however, Saginaw Bay provided updated

²¹⁴ 3 Tr 108.

²¹⁵ Id.

²¹⁶ Attorney General Initial Brief, p 14. See Exhibit AG-15.

²¹⁷ Saginaw Bay Initial Brief, p 8. 3 Tr 40.

²¹⁸ 3 Tr 40.

calculations based on information gathered after the original filing, and argued the updated data provided for a higher transportation rate and argued the proposed rate does not cover all its embedded costs. If in fact the Company's embedded costs are not covered by the transportation rate, it may be reasonable and prudent to charge the same rate for firm and interruptible service. But, to justify the costs, associated with use of the interruptible service under this contract, for inclusion in rate base, DTE Gas will have to establish the rate for interruptible service under this transportation agreement is reasonable and prudent.

Accordingly, this PFD recommends the Commission reject the interruptible transportation rate proposed by the Attorney General and allow interruptible service to be billed at the same transportation rate for firm service equaling Staff's proposed amount of \$0.0695 per Dth for service under the agreement.

B. Disputed Contract Terms in the Transportation Agreement

As noted above, Saginaw Bay requests that the Commission approve the Transportation Agreement in Exhibit A-1, including all its provisions.²¹⁹ Staff and the Attorney General both take issue with sections of the agreement.

1. Article VI, Term and Termination, Section 6.2

Staff and the Attorney General argue that Section 6.2 should be revised.²²⁰ This provision of the transportation agreement states:

Right of First Refusal for Capacity. Shipper shall have a right of first refusal ("Capacity ROFR") with respect to any bona fide offer received by Saginaw Bay from a third party during the time period that begins on the Sag Bay Term Effective Date and ends on the date that is six (6) months

²¹⁹ Saginaw Bay Initial Brief, p 17.

²²⁰ Staff Initial Brief, p 19 and Attorney General Initial Brief, p 14.

immediately preceding the end date of the Term ("Offer Period") to the extent that the acceptance of such bona fide offer would result in the displacement of any or all of Shipper's transportation capacity hereunder for a term commencing upon the end of the Term ("Bona Fide Offer"). If, during the Offer Period, Saginaw Bay receives a Bona Fide Offer, it shall promptly notify Shipper of such Bona Fide Offer. Within 60 days of receipt of notice of the Bona Fide Offer, Shipper may elect to take capacity on the terms and conditions offered in the Bona Fide Offer or, in any event, under terms that would provide Saginaw Bay with at least the same net present value of such Bona Fide Offer; provided, however, the maximum rate that Shipper must pay shall not exceed the maximum rate that Saginaw Bay can charge for delivery on the Saginaw Bay Pipeline under then-applicable regulations. If Shipper does not respond to Saginaw Bay within 60 days, it shall be deemed to have not elected to exercise the Capacity ROFR and Saginaw Bay shall be free to accept the Bona Fide Offer. In the event that Saginaw Bay does not receive any Bona Fide Offers or rejects any or all Bona Fide Offers during the Offer Period, Saginaw Bay and Shipper may mutually agree upon the terms and conditions under which Shipper shall be entitled to continue to receive service on the Saginaw Bay Pipeline.²²¹

As set forth in Mr. Spencer's testimony, Staff recommend this section be revised to clarify that it only applies at the end of the 20-year term of the agreement.²²² Mr. Spencer testified that the proposed language in this section "seems to allow a third party to present a bona fide offer to Saginaw Bay prior the end of the 20-year term."²²³

The Attorney General also asserts language in Section 6.2 of the transportation agreement is of concern, based on the testimony of Mr. Coppola.²²⁴ Mr. Coppola testified:

As written, Section 6.2 of the transportation agreement could result in DTE Gas paying higher transportation costs than agreed to in the 20-year agreement and DTE Gas could potentially lose its right to transport natural gas on the Saginaw Bay pipeline if a third party were to offer a higher

²²¹ Exhibit A-2.

²²² Staff Initial Brief, p 19. Tr 76-77. See Exhibit A-2.

²²³ 3 Tr 77.

²²⁴ Attorney General Initial Brief, p 15.

transportation rate for the firm capacity contracted by DTE Gas during the term of the agreement.²²⁵

The Attorney General argues Section 6.2 is ambiguous and recommends the Commission direct Saginaw Bay to revise the section to clarify it applies only after the 20-year term.²²⁶

The Attorney General reiterated that the transportation agreement was negotiated when parties were affiliates and argues that the negotiations were not at between independent parties and were not at arm's length. And, the Attorney General argues the Commission should scrutinize the terms of the contract, noting that any costs billed to DTE Gas could negatively impact rate base customers.²²⁷

Saginaw Bay argues the clarification recommended by Staff and the Attorney General is unnecessary and assert it is improper for the Commission to require two, non-affiliated entities to renegotiate a reasonable contract.²²⁸ Relying on Mr. Richman's testimony, the Company responds that "Section 6.2 in no way impacts the capacity during the initial term . . . and is specifically for service after the initial term."²²⁹ Mr. Richmond testified the provision was "negotiated to add a layer of optionality to cover an extraordinary case, which is not really expected to be a likely outcome."²³⁰

Saginaw Bay reiterates that the transportation agreement is between two, non-affiliated entities, and asserts "approval of the contractual terms under the Code of

²²⁵ 3 Tr 109.

²²⁶ Attorney General Initial Brief, p 3. See 3 Tr 90.

²²⁷ Id. at p 14.

²²⁸ Saginaw Bay Initial Brief, p 10.

²²⁹ Id. See 3 Tr 41.

²³⁰ 3 Tr 40.

Conduct is no longer required.”²³¹ And Saginaw Bay states Mr. Coppola is “completely off base to be inferring the agreement was not negotiated at arm’s length simply because both companies happen to be subsidiaries of the same parent company.” Responding to Saginaw Bay’s repeatedly references to the fact that the company is no longer affiliated with DTE Gas, the Attorney General responds that the problem with this argument is “that the contract was formulated and negotiated when they were affiliated, and a big portion of this case was conducted under that arrangement.”²³²

This PFD agrees with the Attorney General’s argument that because Saginaw Bay and DTE Gas were affiliates at the time the transportation agreement was negotiated and ratified, the Commission should review the terms based on that relationship. Saginaw Bay acknowledges the Commission utilizes the code of conduct to ensure a regulated utility does not favor an affiliated entity. The fact that the affiliate relationship ended after the transportation agreement was negotiated does not establish the same arm’s length assumptions that would exist between two entities that were never affiliated.

And Saginaw Bay does not dispute that the provisions of Section 6.2 are intended to take effect at the end of the 20-year term. Given this fact, it is reasonable to clarify the agreement to avoid the possible misinterpretation feared by Staff and the Attorney General.

²³¹ Saginaw Bay Reply Brief, p 4.

²³² Id. at p 7.

Accordingly, this PFD recommends the Commission reject the transportation agreement unless Saginaw Bay modifies Section 6.2 to clarify that it only applies after the conclusion of the 20-year term.

2. Inclusion of a Provision for Extensions

Staff and the Attorney General argue that the transportation agreement should include specific provisions for extension of the agreement.²³³ Both refer to an agreement between DTE Michigan Lateral Company (DMLC) and DTE Gas²³⁴ which contains specific language providing for extensions. Article VI, Term and Termination, Section 6.2 of that agreement states:

Extension Term(s) and Rates: Shipper shall have the right and DML shall have the obligation to extend the term of this Agreement (in accordance with the notice provisions herein) with up to six (6) five-year extension terms (each an “Extension Term”) exercisable by Shipper by giving DML at least twelve (12) months prior written notice of its intent to extend the Primary Term or Extension Term currently in effect, provided DML has not given Shipper written notice of its intent to terminate at least thirty-six (36) months prior to the end of the Primary Target or any Extension Term. For any such Extension Term, neither Party may seek to change the MDQ or any other terms or conditions of service except as provided in this Section 6.2. For each Extension Term, the Parties agree that the demand charge will be designed to recover 100% of the actual cost of service, excluding property taxes, of the Converted Assets Pipeline during such period, on a levelized basis, plus actual property taxes assessed. The “cost of service” shall be the lower of (a) fair market value, or (b) % over the fully allocated embedded cost. “Fair market value” as used herein shall be the value which the Converted Assets Pipeline would be expected to command if offered for sale at that time in an open market.²³⁵

Staff and the Attorney General argue the transportation agreement in this case should provide for six, 5-year extension terms like the above provision.²³⁶ The Attorney

²³³ Staff Initial Brief, p 20 and Attorney General Initial Brief, p 14-15.

²³⁴ See Exhibit AG-10.

²³⁵ Id.

²³⁶ Staff Initial Brief, p 20 and Attorney General Initial Brief, p 4.

General argues that the transportation agreement in this case is part of the larger TCARP plan, which also includes the agreement with DMLC. The Attorney General asserts that she asked Saginaw Bay to explain the difference in renewal terms, and no justification was provided.²³⁷ Relying on Mr. Coppola's testimony, the Attorney General posits this could expose DTE Gas, and therefore its customers, to higher costs because it would be at a disadvantage if it attempts to extend the TCARP project.²³⁸

Saginaw Bay argues that inclusion of a specific renewal provision is unnecessary. Based on the testimony of Mr. Richman, the Company argues that Section 6.2 in the current agreement provides for DTE Gas to have a "right of first refusal" if there is not a bona fide offer from another shipper and the parties can mutually agree to extend service. Saginaw Bay also argues that it is unreasonable to require the Company to agree to an additional 30 years of service and asserts the current provisions provide for extensions based on the needs of the parties.²³⁹

Staff acknowledge that after the initial 20-year term, the parties may have different requirements, but continue to argue that that the agreement should provide for extensions.²⁴⁰ The Attorney General agrees.²⁴¹

This PDF agrees with the recommendations of Staff and the Attorney General that inclusion of specific provisions for extension are warranted. As noted above, the parties were affiliates when the contract was negotiated and executed, therefore the provisions should be reviewed under the Code of Conduct. The Company has not

²³⁷ Attorney General Initial Brief, p 16.

²³⁸ Id. See 3 Tr 111.

²³⁹ Saginaw Bay Initial Brief, p 10-11.

²⁴⁰ Staff Initial Brief, p 21.

²⁴¹ Attorney General Initial Brief, p 3-4.

provided any reason for the difference in the language of the agreements involving Saginaw Bay and DMCL. And the transportation agreement in this case is part of the larger TCARP project undertaken by DTE Gas. To ensure the seamless development of that project, DTE Gas should have the same extension rights in both agreements.

Accordingly, this PFD recommends the Commission reject the transportation agreement unless Saginaw Bay modifies includes a provision that provides for up to six, 5-year extension of the transportation agreement.

3. Inclusion of a 50/50 Revenue Sharing Provision.

Staff and the Attorney General argue that the transportation agreement should include specific provisions for sharing of revenue received by Saginaw Bay, from third-party shippers, with DTE Gas.²⁴² Again, both refer to an agreement between DMLC and DTE Gas²⁴³ which contains specific language providing for revenue sharing. Article X, Price, Section 10.5 of that agreement states:

Additional Shippers. The Parties acknowledge that DML may have the opportunity to enter into firm and interruptible Transportation service agreements with additional shipper(s) on the Converted Assets Pipeline ("Additional Shippers"). In the event that DML is presented with such an opportunity during the Primary Term and any Extension Term of this Agreement, and DML proceeds to contract with such Additional Shippers, DML will notify Shipper of any such Additional Shippers and SML will credit to Shipper the incremental value, based on incremental demand charge payments, exclusive of any capital recovery, actually received from such Additional Shippers on a 50/50 basis after consideration of a ten percent (10%) after-tax return on incremental capital costs and after consideration of incremental O & M Costs, if any, that Gathering will incur to provide service to the Additional Shipper ("Additional Shipper Credit"). As used herein, the O & M Costs are those incurred by Gathering solely and directly related to the Converted Assets Pipeline, and such O & M Costs to be considered as noted herein would only be those incrementally

²⁴² Staff Initial Brief, p 22 and Attorney General Initial Brief, p 16.

²⁴³ See Exhibit AG-10.

incurred due to the Additional Shipper. The Additional Shipper Credit will be provided to Shipper in the form of a reduction in the demand charges for the same period as the contract term for any Additional Shipper so long as the contract between DML and the Additional Shipper remains in effect.²⁴⁴

The transportation agreement in this case was designed to cover Saginaw Bay's embedded costs plus 10%. The Attorney General argues that failure to include a revenue sharing provision will result in retention of 100% of any additional revenue "although DTE Gas is paying 100% of the fixed and variable costs of operating the pipeline included in the transportation rate under the 20-year fixed demand contract."²⁴⁵ And the Attorney General notes, unlike DMLC, Saginaw Bay is not making significant additional investments, consequently failure to implement the revenue sharing will result in DTE Gas, and its customers, paying an unreasonable amount.²⁴⁶

Saginaw Bay disagrees with the recommended addition of a 50/50 revenue sharing provision and argues it would be unreasonable to impose against the Company. Arguing that it is committing an existing asset with the capabilities of serving customers from other receipt points, the Company argues additional revenues received from these contracts should be retained by Saginaw Bay. The Company argues DTE Gas is paying for services, not specifically designed assets.²⁴⁷

This PDF agrees with the recommendations of Staff and the Attorney General that inclusion of specific provisions for sharing of additional revenues. Again, the parties were affiliates when the contract was negotiated. As an affiliate transaction, Saginaw Bay is requesting recovery of its embedded costs plus 10%. These embedded

²⁴⁴ See Exhibit AG-10.

²⁴⁵ Attorney General Initial Brief, p 16. 3 Tr 112.

²⁴⁶ Id. at p 16-17.

²⁴⁷ Saginaw Bay Initial Brief, p 11.

costs cover operation of the pipeline and therefore additional revenue paid to Saginaw Bay will be at the expense of DTE Gas and its customers. This is not reasonable and prudent.

Accordingly, this PFD recommends the Commission reject the transportation agreement unless Saginaw Bay modifies it to include a provision that provides for up to revenue sharing between DTE Gas and Saginaw Bay on a 50/50 basis.

C. Code of Conduct

Saginaw Bay request the Commission find “the Agreement between Saginaw Bay Pipeline Company and DTE Gas Company is reasonable, prudent and satisfies the requirement of the Code of Conduct.”²⁴⁸

The problem with this request centers on the language in the applicable provision of the Code of Conduct. It provides:

If an affiliate or other entity within the corporate structure provides services or products to a utility, and the cost of the service or product is not governed by section 10ee(8) of 2016 PA 341, MCL 460.10ee(8), **compensation is at the lower of market price or 10% over fully allocated embedded cost.**²⁴⁹ (Emphasis added)

To comply with this provision, the applicant must establish that the compensation is the lower of “market price” or embedded costs plus 10%. But there is no evidence in this record to establish if a market price exists or the value of market price for the firm delivery services in the transportation agreement. And taken as a whole, the Code of Conduct requires that the regulated utility, not the affiliate, establish compliance if and

²⁴⁸ Id. at p 17.

²⁴⁹ R460.10108(4)

when attempting to include the costs in rates charged to customers. As set forth in the July 27, 2021, Order in Case No. U-20894:

The Commission, however, highlights that approval of the firm transportation contract in this case is not tantamount to approval for inclusion of these costs in DTE Gas's rates; rather, that determination will be made by the Commission when DTE Gas makes such a request.²⁵⁰

Accordingly, based on the record, this PFD recommends that the Commission reject the Company's request to find that the agreement "satisfies the requirement of the Code of Conduct."

IV.

CONCLUSION

This PFD recommends that the Commission adopt the following findings of fact and conclusions of law:

1. The Commission has authority to review the reasonableness and prudence of a transportation agreement under the provisions of Act 9 or the provisions of the Code of Conduct.
2. Implement the adjustments suggested by Staff and approve a transportation rate of \$0.0695 per Dth for the firm transportation of 50,000 Dth per day.
3. Reject the inclusion of an interruptible transportation rate as suggested by the Attorney General.
4. The Commission should require the transportation agreement in this matter be revised to specify that Article VI, Section 6.2 only applies after the initial 20-year

²⁵⁰ July 27, 2021 Order, MPSC Case No. U-20894, p 35.
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term of the transportation agreement. If Saginaw Bay is unwilling to do so, the Commission should reject the transportation agreement in this matter.

5. The Commission should require that the transportation agreement include a provision for up to six, 5-year extensions of the agreement in conformance with Article VI, paragraphs 6.2 and 6.3 of the transportation agreement between DTE Gas and DMLC (see Exhibit AG-10). If Saginaw Bay is unwilling to do so, the Commission should reject the transportation agreement in this matter.
6. The Commission should require that the transportation agreement include a provision for 50/50 sharing of additional revenues, received by Saginaw Bay from additional shippers, which conforms to Article X, paragraph 10.5 of the transportation agreement between DTE Gas and DMLC (see Exhibit AG-10). If Saginaw Bay is unwilling to do so, the Commission should reject the transportation agreement in this matter.

MICHIGAN OFFICE OF ADMINISTRATIVE
HEARINGS AND RULES
For the Michigan Public Service Commission

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Katherine E. Talbot
Administrative Law Judge

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