Clark Hill

Stephen A. Campbell
T (313) 309-4274
F (313) 309-6882
Email:SCampbell@ClarkHill.com

Clark Hill
500 Woodward Avenue, Suite 3500
Detroit, MI 48226
T 313.965.8300
F 313.965.8252

July 31, 2024

VIA ELECTRONIC CASE FILING

Executive Secretary
Michigan Public Service Commission
7109 W. Saginaw Highway
Lansing, Michigan 48917

Re: Case No. U-21291 – In the matter of the application of DTE Gas Company for authority to increase its rates, amend its rate schedules and rules governing the distribution and supply of natural gas, and for miscellaneous accounting authority.

Dear Executive Secretary:

Enclosed for filing please find the ***Association of Businesses Advocating Tariff Equity's Reply Brief*** and ***Proof of Service*** in the above referenced proceeding.

Sincerely,

CLARK HILL PLC

Stephen Campbell

Digitally signed by: Stephen Campbell
DN: CN = Stephen Campbell email = scampbell@clarkhill.com C = US O = Clark Hill PLC
Date: 2024.07.31 12:20:05 -04'00'

Stephen A. Campbell

SAC/lkd
cc: Parties of Record

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

*** * * * ***

In the matter of the application of **DTE GAS COMPANY** for authority to increase its rates, amend its rate schedules and rules governing the distribution and supply of natural gas, and for miscellaneous accounting authority	)	Case No. U-21291 ALJ Jonathan F. Thoits

REPLY BRIEF OF THE ASSOCIATION OF BUSINESSES ADVOCATING TARIFF EQUITY

The Association of Businesses Advocating Tariff Equity ("ABATE"), by its attorneys, CLARK HILL PLC, files its Reply Brief in this proceeding initiated by DTE Gas Company ("DTE" or the "Company") before the Michigan Public Service Commission ("Commission") in accordance with the schedule established by the presiding Administrative Law Judge ("ALJ").

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I. INTRODUCTION

The Commission may authorize a Michigan utility to collect rates and charges that are just and reasonable considering the utility's reasonable cost of doing business. In requesting Commission approval, the applicant utility bears the burden of demonstrating that its proposed costs and rates are reasonable and prudent. Despite this requirement, DTE put forth several proposals in this proceeding which would result in rates that do not meet this standard and should be rejected or modified.

These proposals include the Company's use of a projected test year, which inflates DTE's revenue requirement using costs which are conjectural. Indeed, numerous capital expenditure proposals are not adequately supported such that cost recovery is unreasonable at this time. In addition, the Company's projected operations and maintenance ("O&M") costs are inflated and its requested return on equity ("ROE") and equity ratio are excessive and unnecessary. The Company's recommended class cost-of-service study ("CCOSS"), cost allocation, and rate design are also unreasonable and would not best align costs with their causation.

Accordingly, to ensure just and reasonable rates the Commission should adopt the recommendations set out below. These proposals will ensure DTE's rates are reasonable and prudent and that the Company's costs are allocated to customers consistent with the manner in which they are caused by those customers.

II. ARGUMENT

A. The Company's projected test year is unreasonable and would result in further overearning at ratepayer expense.

The Company claimed "that its projected costs are real" and thus its projected test year should be adopted. (DTE Initial Br at 15-16.) As explained in ABATE' Initial Brief, the costs' projected nature definitionally prevents them from being considered "real;" they are hypothetical

and merely potential costs. (ABATE Initial Br at 4-8.) For the reasons set forth in ABATE's Initial Brief the Company's projected test year is deficient and will result in the Company once again receiving revenue far in excess of its costs, as it has in the Company's last several rate cases. As such the Commission should reject the Company's proposal to set its revenue requirement based on projected test year expenses in this case.

B. The Company's requested revenue requirement included projected capital expenditures which are unnecessary or speculative.

1. The Company's proposed investment in its Main Replacement Program is unnecessary at this time.

The Company argued that ABATE's proposed "reduction in expenditures fails to take into account the increased costs associated with more complex grids selected using the results of the Company's Probabilistic Risk Assessment." (DTE Initial Br at 61.) As this objection misunderstands ABATE's proposal it should be rejected.

ABATE recommended the Company limit its main replacement investment to simply meet the 18-year pace approved in Case No. U-18999, which is less than the 206 miles being proposed by the Company. (ABATE Initial Br at 9-11.) In other words, ABATE's proposed cost reduction was associated with less main replacement. The Company's response noted that the main replacement at issue here is more complicated, and that it "needs the flexibility to replace as few as 190 miles annually without a reduction in expenditures." (DTE Initial Br at 61.) This is effectively an acknowledgement that DTE's projected cost is unreliable. The Company has requested an elevated amount of revenue for an excessive main replacement effort, while also claiming it requires the flexibility of using that amount of revenue for replacing less mains. This is not an argument in favor of cost recovery, it is an argument against the reasonableness of DTE's projected cost.

The Commission should at the very least hold the Company to its cost estimates and only approve cost recovery actually associated with the main replacement investment necessary meet the 18-year pace approved in Case No. U-18999. Approving higher amounts to afford the Company "flexibility" is not reasonable or adequately supported on the record. As such the Commission should reject the Company's proposal and adopt the recommendation set out in ABATE's Initial Brief. (ABATE Initial Br at 9-11.)

2. The Company should not recover costs for large capital projects which will not be completed, used, or useful within the test year.

The Company claimed that the Commission should not disallow cost recovery for projects not expected to go into service until the last six months of the test year. (DTE Initial Br at 45-46.) As the Company acknowledged the potential for delays the Commission should not approve cost recovery for these projects here.

Despite claiming that ABATE's justification for not approving this cost recovery is extrapolated from "DTE Gas's intentional decision to postpone the construction of phase three of the Traverse City Reinforcement project from 2021 to 2022," the Company acknowledged that the "potential for delays is inherent in any capital project and already accounted for in cost and schedule contingency." (*Id*.) In other words the Company asserted that its capital project cost projections are already inflated to account for delays, and that potential delays are inherent in any capital project. This is precisely the issue with approving cost recovery for projects with such extended completion dates. As explained in ABATE's Initial Brief, unforeseen delays due to permitting, labor shortages, material delays, or unforeseen site conditions would make it unlikely that the requested capital investment for these projects will be realized prior to the end of the projected test year. (ABATE Initial Br at 11-13.) The Company has acknowledged these delays are inherent in its capital projects.

The Commission should therefore reduce the proposed capital expenditures in the future test year period to ensure customers will not pay for work that is not completed. (*Id.*) A reasonable approach would be to remove the last six months of the Company's proposed capital investment for the projects described in ABATE's Initial Brief. If these costs are incurred the Company can seek recovery in its next rate case.

C. The Company's proposed O&M expense is inflated and includes costs which should not be collected from customers.

1. The inflation factor used in the Company's analysis is unreasonable.

The Company argued that it's inflation rates should be adopted, claiming alternatives "fail[] to account for updated labor rates" as DTE "has provided the updated inflation factors using updated labor rates, which reflect the Company's actual 2024 annual pay adjustment of 3.5%." (DTE Initial Br at 93-94.) As these figures do not support the Company's request it should be rejected.

The Company claimed that ABATE "fails to account for the direct evidence of the Company's obligations under existing collective bargaining agreements." (*Id.*) As explained in ABATE's Initial Brief this observation does not provide a transparent justification supporting the Company's figures. (ABATE Initial Br at 13-15.) While the Company provided historical annual pay increases over the period 2019-2023, this analysis included executive pay and incentive compensation, which is not reflective of the average salary of the Company's larger workforce. (Cooper 4 Tr 2690; Exhibit AB-20 at 4.) In addition, the historical annual employee pay analysis did not take into account changes in the number of employees throughout the calendar year. If instead the Company looked at the year-over-year change in average salary, the Company's own workpapers would have shown an average pay increase of 1.1% in 2020, 2.7% in 2021, 1.8% in 2022, and 0.6% in 2023, for an average increase of 1.5%. (See Exhibit AB-20 at 1-3.)

The lack of evidentiary support demonstrates the unreasonableness of this figure. If the Company is experiencing increased labor cost it should have supported the 3.0% wage inflation rate with workpapers or some other evidence. The absence of that evidence demonstrates the 3.0% wage inflation rate should not be relied on to escalate O&M expense.

2. The Company's proposed incentive compensation recovery is unreasonable and should be rejected.

The Company argued that the proposed disallowances for incentive compensation recovery "fails to assess the overall reasonableness of the Company's total compensation practices" and the "mere fact that a small portion of the variable compensation is based on multiple measures, including financial, should not alone be determinative of whether these costs are appropriately included in DTE Gas's projected revenue requirement." (DTE Initial Br at 119-21.) As this claim runs counter to the Commission's numerous prior holdings on this issue the Company's incentive compensation proposal should be rejected.

The Company claimed that the intervenors' recommendations "ignore[] the multiple customer benefits related to the maintenance of DTE's current debt ratings, avoided increased interest costs, and the operating and capital cost savings enabled by an organizational emphasis on operating efficiencies that produce improved earnings and cash flow," and overlook "the advantage of DTE's ready access to capital markets." (*Id*.) As set out in ABATE's Initial Brief the Commission has rejected these arguments multiple times. See *In the Matter of the Application of Consumers Energy Co*, order of the Public Service Commission, entered December 22, 2021 (Case No. U-20963), pp 297-98 ("The contention that ratepayers receive benefits from a financially healthy utility is insufficient to demonstrate that incentive compensation tied to financial performance does not primarily benefit shareholders or that benefits to ratepayers are commensurate with the proposed expense for the incentive compensation program"). Specifically,

the Commission has stated that it has "unequivocally and consistently disallowed incentive compensation costs tied to financial measures." *In the Matter of the Application of DTE Electric Co*, order of the Public Service Commission, entered May 8, 2020 (Case No. U-20561), pp 17-19. Thus, "financial-based incentive compensation costs—regardless of when and how they were incurred, the accounting treatment utilized, or whether they were classified as capital expenses or O&M—should not be included in the rates approved." (*Id*.) The Company here did not demonstrate that customers benefit from incentive compensation tied to financial performance metrics. Specifically, as shown on DTE's Exhibit A-19, Schedule I-5, the costs associated with financial performance outweigh the benefits to customers in five out of six metrics.

The Commission should therefore again reject DTE's proposal to recover $12.0 million of incentive compensation expense associated with financial performance. These expenditures do not benefit customers and should not be paid by ratepayers.

D. The Company's proposed capital structure and ROE are excessive and unreasonable.

1. The Company's proposed equity ratio is contrary to Commission direction and a reasonable proxy group.

The Company argued it requires a higher equity ratio. (See DTE Initial Br at 65-66.) As this claim is inconsistent with recent Commission holdings and a reasonable proxy group the Commission should reject the DTE's proposal.

The Company argued that intervenors' "equity capital structure recommendations of 51% and 50%, respectively, are lower than (ii) the average equity percentage allowed natural gas utilities in 2023 to 2024, and (iii) the Company's reasonable request," and that "[g]iven the increase in interest rates and increase in exposure to decarbonization initiatives, it is not reasonable to decrease the equity percentage in DTE Gas's capital structure lower than DTE Gas's currently approved equity percentage" (DTE Initial Br at 65-66.) As explained in its Initial Brief, the

Company proposed a 51.5% equity ratio which is higher than its current equity ratio, counter to the Commission's former directives, and inconsistent with industry trends. (See Walters 4 Tr 1358-61 (internal citations omitted)). The Commission should therefore reduce the Company's equity ratio to avoid unnecessarily increasing customer rates. (*Id*.)

The Company's proposed equity ratio is diametrically contrary to the Commission's previous Order in U-20940, where it authorized an equity ratio of 51.0% and, in rejecting the Company's proposed 51.9% equity ratio, stated such a request "does not reflect an effort to move to a more balanced capital structure." *In the Matter of the Application of DTE Gas Co*, order of the Public Service Commission, entered December 9, 2021 (Case No. U-20490), pp 76-78. Further, contrary to DTE's claims, it significantly exceeds the equity ratio for the proxy group the Company used to support its ROE recommendation. (See Walters 4 Tr 1358-61; Exhibit AB-5.) While ABATE's proxy group in this case had an average common equity ratio of 44.4% (including short-term debt) and 50.0% (excluding short-term debt) as calculated by S&P Global Market Intelligence and *Value Line*, respectively, DTE's proposed ratemaking equity ratio of 51.50% (excluding short-term debt) exceeds that of the proxy group's equity ratio and is not reasonable for ratemaking purposes. (*Id*.)

The Company's 51.5% proposed equity ratio therefore significantly exceeds the equity ratios of the proxy group and directly contradicts the Commission's prior direction for DTE to maintain a more balanced capital structure. As such the Commission should, consistent with its prior Orders, approve a permanent equity ratio for DTE of 50.0%.

2. The concept of financial leverage does not support a higher equity ratio or ROE.

The Company claimed that intervenors "fail to consider financial leverage in their evaluations of the cost of equity," which purportedly "creates non-trivial downward bias on

proposed ROE recommendations," while if "adjusted for financial risk, the capital structure recommendations of [intervenors] would be consistent with and supportive of DTE Gas's 10.25% ROE at 51.5% equity." (DTE Initial Br at 66.) As this claim is inaccurate the Company's proposal should be rejected.

The Company claimed that if the Commission adopted intervenor "capital structure recommendations, the cost of equity would increase due to the higher amount of leverage in the capital structure." (*Id*.) As explained in ABATE's Initial Brief, this claim is belied by the Company's additional arguments. For instance, while the Company claimed that "the authorized common equity ratio approved by the state commissions for the peer group gas operating companies is 53.8% and consistent with the Company's request for an authorized equity ratio of 51.5%," these dockets demonstrate this peer group gas operating companies have much lower ROES. (See Lepczyk 4 Tr 2209; ABATE Initial Br at 26 n 16.) Specifically, the average authorized ROE for the same group is 9.58% and ranges from 9.10% to 10.25%. Of the 20 reported authorized ROEs from the set of rate cases provided by DTE, 10 are 9.50% or lower, 18 of them are below the Company's currently authorized ROE of 9.90%, and the remaining two ROE decisions are 10.0% and 10.25%. (*Id*.)

The Company's analysis is therefore incomplete and its claim regarding financial leverage ignores the much lower ROEs for peer companies. As such the Company's claim should be rejected and its equity ratio should be set at 50%.

3. The utility industry's access to capital and the context of the current economic environment indicate the Company's ROE should be reduced.

The Company claimed that ROEs have increased after 2021 and adopting a lower ROE would be unlikely to attract equity investors. (DTE Initial Br at 73-74.) As these claims are overstated and misleading the Commission should reject the Company's objection.

As provided in ABATE's Initial Brief, authorized ROEs have been reasonably stable below 10.0% for roughly the last nine years (specifically the majority of authorized ROEs since 2016 have been below 9.7%, with many being below 9.5%). (Walters 4 Tr 1337-54.) During that time the utility industry's common equity ratios have also not deviated too much from the range of 50.0% to 52.0%. (*Id*.) Since 2009 industry credit ratings have also continued to improve[1] while capital expenditures for electric and natural gas utilities have increased and utilities have been able to readily access external capital. (*Id*.) Indeed, capital expenditures for the regulated electric and natural gas delivery utilities have increased considerably over the period 2023 into 2024, and the forecasted capital expenditures remain elevated through the end of 2025. (*Id*.) Capital investments are therefore enhancing utility shareholder value and attracting both debt and equity capital to the utility industry.

The claim that recently increased ROEs suggest a higher ROE for DTE is reasonable ignores the extent to which DTE's current ROE already far exceeds national trends. Given DTE's current relatively elevated and excessive ROE a reduction is warranted to align the Company's ROE with national trends.

4. Reasonable empirical models demonstrate a reasonable ROE for the Company is 9.45%.

a. The Company's objections to ABATE's DCF analyses are unreasonable and should be rejected.

The Company claimed that ABATE's DCF analyses involve the application of "odd and unsupported timeframes for key inputs like stock price" and are based on "limited sources that

[1] The Company's claims that "[c]redit ratings speak only to credit quality, but do not indicate investment merit or measure asset value" are inaccurate. (DTE Initial Br at 76-77.) A company with a higher credit rating will have more access to capital at better terms and prices than another company with a lower credit rating, all else equal. To suggest that credit ratings have no impact on the cost of equity is completely unfounded.

indicate [the] model is inconsistent and should be ignored." (DTE Initial Br at 72-73.) As these claims are inaccurate the Company's objection should be rejected.

As provided in ABATE's Initial Brief, in developing a reasonable ROE for the Company ABATE witness Chris Walters applied, among other analyses, a constant growth Discounted Cash Flow ("DCF") model using the consensus of analysts' growth rate projections, a constant growth DCF using sustainable growth rate estimates, and a multi-stage DCF model. (ABATE Initial Br at 27-30.) These analyses used standard inputs and provided a comprehensive and contextual view of a reasonable ROE. An explanation of these methods and a response to DTE's misplaced objections is provided in ABATE's Initial Brief and, for the sake of brevity, will not be restated here. (*Id*.) For the reasons explained therein the Company's objection and its ROE recommendation should be rejected.

b. The Company's risk premium model is unreasonable and should be rejected.

The Company claimed the intervenors' "risk premium models fail to consider the inverse relationship between utilities' equity premium and interest rates." (DTE Initial Br at 73-74.) As provided in ABATE's Initial Brief its risk premium model is a straightforward application of the analyses. (ABATE Initial Brief at 30.) Contrarily, DTE's regression-derived risk premium estimate of 6.26% for gas utilities is significantly higher than the equity risk premiums realized in 2023 and the Company's regression analysis estimated an equity risk premium that is nearly a full percentage point higher than what was realized in 2023. (Walters 4 Tr 1403-05.) This is inconsistent with expectations for 2024. As Regulatory Research Associates explained in a recent report, the equity risk premium is expected to narrow in 2024 relative to 2023 for several reasons as "regulators navigate the ongoing energy transition and potential affordability challenges posed by higher interest rates and rising costs." (*Id*. (internal citation omitted).)

The Company's claim that a regression approach "takes into account the relationship between the risk premium and interest rates" is therefore irrelevant; DTE's risk premium is significantly askew from the actual evidence of recent risk premiums. (Villadsen 4 Tr 2542, 2581.) As such the Company's risk premium analysis is unreliable and the recommended ROE based thereon should be rejected.

c. The Company's objections to ABATE's CAPM model are unreasonable and should be rejected.

The Company claimed that intervenors' CAPM analyses supported DTE's recommended ROE, while it also disagreed with the method. (DTE Initial Br at 71.) As neither of these claims is accurate or reasonable they should be rejected.

As explained in ABATE's Initial Brief, its CAPM method supports a far lower ROE than proposed by DTE.[2] (ABATE Initial Br at 31-33.) The Company further claimed that ABATE's CAPM analysis was deficient "by relying on a long-term average of historic betas, which fail to incorporate current economic and financial conditions and over value the data during the arbitrary timeframe selected." (DTE Initial Br at 71.) As explained in ABATE's Initial Brief, historical betas provide context for the significant extent to which current betas are anomalous and were required to provide a more normalized estimated beta component for the CAPM analysis. (ABATE Initial Br at 31-33; Walters 4 Tr 1380-90.) The Company's disregard of historic averages skews its ROE analysis in favor of betas influenced by more recent anomalous occurrences unlikely to be repeated in the test year. As such the Company's analysis should be rejected.

[2] The Company's similar claim that its requested ROE "is supported by the analyses proffered by Staff and Intervenors" is, for the reasons set out in ABATE's Initial Brief, similarly inaccurate. (See DTE Initial Br at 69; ABATE Initial Br at 22-33.)

As shown in Exhibit AB-18, the results of nine different applications of the CAPM range from 9.15% to 10.80%. (*Id.*) Because current beta estimates are based on the most recent five years of historical stock returns and volatility, however, they are still heavily impacted by the market fallout in early 2020. (*Id.*) As such, it is appropriate to give primary consideration to the results of a CAPM analyses using long-term average *Value Line* betas. The Company's objection and recommendation is therefore unreasonable and should be rejected.

d. The Company's CAPM and ECAPM analyses are overstated.

The Company argued that "the ECAPM adjustment is not duplicative – it is complementary to the Blume adjusted values inherent in the Value Line data used." (DTE Initial Br at 71-72.) As explained in ABATE's Initial Brief this claim is inconsistent with prior regulatory determinations in front of the Commission and should again be rejected. (See ABATE Initial Br at 37-39.)

E. The Company and Staff's recommended CCOS is unreasonable and should be rejected.

1. Staff's recommended A&P cost allocation does not reflect cost causation and should be rejected.

Staff recommended the Commission approve a cost allocation based on the A&P method. (See Staff Initial Br at 71-72.) Because this approach does not reflect how customers cause DTE to incur costs the Commission should instead approve a Design Day method cost allocation.

Staff reiterated its argument that "the A&P method best reflects the way costs are caused by customer classes' use of the system," while also contrarily acknowledging that the "A&P method is described as 'tempering' costs and as a compromise between high- and low-load factor classes." (*Id.*) The fact that the A&P method tempers cost allocation and compromises the allocation between classes effectively prevents it from accurately reflecting DTE's actual cost of service. (ABATE Initial Br at 39-56.) As explained in ABATE's Initial Brief, "tempering" and endeavoring to "compromise" between the costs allocated to different classes is inconsistent with

the manner in which DTE designs its systems and the way its customer cause its costs. (*Id.*) Thus, despite Staff's claim that the A&P method does not reflect "artificiality or the introduction of rate design concerns," it does precisely that. (Staff Initial Br at 71-72.) Despite the straightforward application of cost causation principles, the A&P method instead serves to skew and shift costs amongst rate classes as a "compromise" to "temper" rate increases. (ABATE Initial Br at 39-56.) This inconsistency with cost causation should not be approved.

Thus, Staff's claim that "the customer classes who stand to benefit from either method could argue that their preferred method is the only correct way to allocate costs without basing those arguments on the outcome" completely misses the reality of how DTE designs its system and incurs costs. (Staff Initial Br at 71-72.) As explained in ABATE's Initial Brief, the system's main capacity is designed and built to serve the system's Peak Day, or Design Day Demand. (ABATE Initial Br at 39-47.) Stated differently, the Company's costs are incurred to and based on its ability to serve its Peak Day demand. Measures of utilization (e.g., Average Demand, or annual throughput) predominant in the A&P method therefore have no bearing on how DTE incurs delivery capacity cost. (*Id.*) While Staff argued that the A&P method recognizes both sides of the way the system is used, it does not reflect the manner in which the Company incurs costs and thus it is inconsistent with cost causation and cost-of-service principles. (*Id.*; see Staff Initial Br at 71-72.) The Peak Day method recommended by ABATE is not "aim[ed]" at a particular outcome; it reflects the manner in which customers cause DTE to incur costs and, as such, best reflects cost causation.[3] (*Id.*) Further, there is no "assum[tion]" that the Peak Day method accurately reflects

[3] While DTE stated that it disagreed with ABATE's recommendation, it did so based only its assertion that the Commission has historically approved the use of the A&P method, not because it reflects cost of service. (DTE Initial Br at 133.) The Company's disagreement is therefore not substantive and should be given little weight.

cost causation, the Company's own admissions explicitly describe how it designs its system capacity to meet the Design Day and Design Hour Demands of its customers, that "[f]rom a cost of service perspective, it is assumed that the system is designed to provide service at design peak day volumes," that "the cost to construct distribution mains is not related to annual volume delivered," and "the cost to construct transmission mains is not related to annual volume delivered." (See ABATE Initial Br at 45-48.) While Staff's argument is based on its philosophical perspective regarding how to best temper and compromise between customer class rate increases, the Peak Day method reflects the way DTE has acknowledged it incurs costs.

Also, while DTE affirmed that distribution main cost is not related to volume, Staff inaccurately alleged that the A&P allocator does not "primarily" allocate costs on volume and instead "allocates 64.236% of any cost it is applied to on peak day demand, and thus primarily allocates on peak day demand." (Staff Initial Br at 73.) This claim entirely ignores the actual cost allocation for the transportation classes and is indicative of how Staff's proposal favors compromising and tempering rate increases amongst classes rather than following cost causation. (ABATE Initial Br at 42 n 30, 44-45.) Specifically, as explained in ABATE's Initial Brief, Staff's reference to 64.236% represents the weight that each class's peak day demand gets in the calculation of the composition P&A allocator. In other words, that is 1-system load factor. Staff is ignoring the fact that average demand comprises 86% of the peak day allocator for XXLT, and 76% of the peak day allocator for XLT. Mathematically the average demand represents about 91% of the composite P&A allocator for XXLT, and 84% for XLT. (*Id.*) As regards the transportation customers, therefore, Staff's claim is demonstrably incorrect and should be rejected.

The record clearly demonstrates that Design Day Demand drives DTE's costs. Allocating those costs accordingly would therefore produce the most accurate measure of the Company's cost

of providing service to each class. The Commission should therefore reject Staff's objections and approve a cost allocation consistent with Design Day Demand and the manner in which DTE's incurs costs to serve its various customer classes.

2. The A&E method more accurately aligns costs with causation than the A&P method.

Staff also objected to ABATE's alternative proposal that, if the Commission declines to adopt the Design Day Demand or Peak Day method, it should direct that costs be allocated according to the A&E method. (Staff Initial Br at 73-74, 77.) As Staff's objections are unreasonable they should be rejected.

Staff claimed that the A&E method "breaks the link between system load factor, peak, and usage that the A&P method relies on" and "fails to recognize how classes use the system." (*Id.*) As explained above and in ABATE's Initial Brief the A&E method more accurately reflects cost causation than the P&A method. (ABATE Initial Br at 49-51.) It identifies the base amount of capacity that would be needed if all customers used gas at a constant rate (i.e. 100% load factor), and allocates that capacity on average demand, which is the same approach as the P&A method recommended by Staff. (*Id.*) The A&E method then identifies the amount of capacity needed to meet each class's peak demand in excess of the base (i.e. Average) demand. This portion is allocated in proportion to the difference between each class's non-coincident peak demand[4] and average demand. (*Id.*) Contrasted with the P&A method, this method assigns a greater amount of

[4] Regarding Staff's assertion that "the use of NCP should be rejected as speculative and unsupported," if Staff's position is that average demand impacts the cost of transmission and distribution ("T&D") main capacity, and the objective of cost allocation is to reflect the impact of average demand on T&D main capacity costs, then it would be a mistake to allocate the excess demand with a coincident peak allocation factor, because doing so would produce allocation factors that are identical to those derived using a coincident peak demand method. (Staff Initial Br at 73-74; see ABATE Initial Br at 40-52.) This is discussed in the 1989 NARUC Electricity Cost Allocation Manual, although the same logic and math applies to natural gas T&D main capacity.

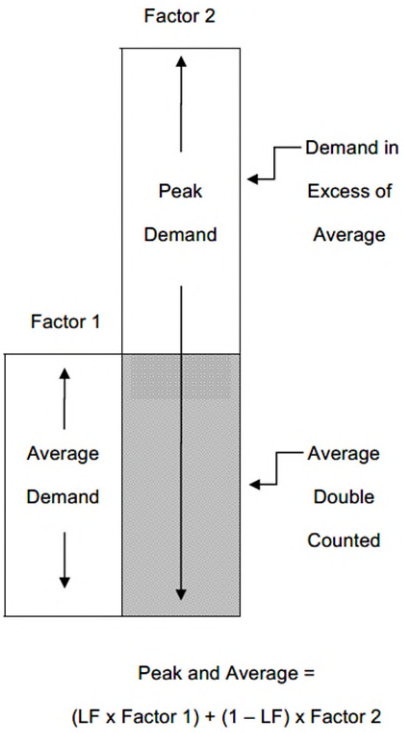
capacity cost to weather sensitive customer classes whose peak demand demonstrates the greatest variability relative to average demand.[5] This is appropriate because the excess capacity that exists on the system on a non-peak day is held in reserve to meet the peak day demand of weather sensitive customers. In other words, those customers cause those costs and cost-of-service rates should allocate those costs to those customers. Further, regarding Staff's claim as to the "link between system load factor, peak and usage that the A&P method relies on," as noted above measures of utilization like load factor and average demand are not linked to cost causation. (*Id.;* Staff Initial Br at 73-74, 77.)

In addition, Staff's response to the double-counting of average demand inappropriately inherent in the P&A method misstates the problem. Staff claimed that the "argument regarding double-counting also fails to reflect the reality that the average amount of usage has different costs on the peak day than an average day and does not recognize that average usage represents throughput in the allocation equation," and "even if the double counting did exist it would be on a single day out of an entire year's worth of throughput, rendering it immaterial." (*Id.;* Staff Initial Br at 73-74, 77.) As explained in ABATE's Initial Brief, these assertions appear to be based on a claim that the average considered in the A&E methodology is somehow different from that in the A&P methodology. This is incorrect. As explained above, these components are mathematically identical; that is, they are both based on average annual throughput and weighted using the system load factor. (ABATE Initial Br at 51; York 4 Tr 1270-92.) Thus, any differences (although Staff does not explain what they are) between the costs to deliver an "average" amount of gas on a peak

[5] For this reason Staff's claim that the A&E method continues "to use the system load factor to weight between the two factors in the allocator when one of the factors (contribution to peak day usage) is no longer used in its calculation, severing the link between the aspects of the A&E allocator calculated by the Company" is also incorrect. (See Staff Initial Br at 73-74, 77.)

day as compared to the costs on an average day are irrelevant. Indeed, transmission and distribution mains costs are fixed, meaning these costs do not change on days when demand is less than that on a peak day. (See *Id*.) As explained by DTE, main capacity is designed and built (i.e., costs are incurred) to meet Peak Day demand, although the Company varies the main pressure and amount of gas to meet the demands of all rate classes, and the system, every day of the year. (*Id*.) In other words, the fixed cost of main capacity designed to meet the system peak demand remains the same every day of the year, irrespective of operating pressure and capacity utilization of the mains. (*Id*.) Furthermore, the average usage incorporated in the A&E method by definition incorporates annual throughput. If Staff sees this as a flaw in the A&E method, this same flaw also exists in the A&P method Staff recommended.

Staff's claim that the A&P method's "double counting could be remedied by removing the peak day from the average calculation with very little change in the allocator itself" is also incorrect and misunderstands the allocation method. (Staff Initial Br at 77.) As explained in ABATE's Initial Brief, the A&E method does not remove the peak day from the average calculation, instead it removes the peak day from the excess element of allocation. (See ABATE Initial Br at 48-49; York 4 Tr 1270-92.) Considered in the context of the figure included in ABATE's Initial Brief and set forth below, Staff's argument is essentially to remove only a tiny sliver from Factor 1. The A&E method, however, is based upon removing the entirety of Factor 1 when determining excess demand to be allocated (Factor 2), as that Factor 1 is already incorporated into the average demand to be allocated. (*Id*.) In other words, the A&E method incorporates Factor 1 once, while the A&P method redundantly incorporates it twice.



Staff's additional claim that regulatory authorities from other jurisdictions "are notable for their reasoning, but not for the outcomes" further demonstrates the reasonableness of the A&E method. (Staff Initial Br at 77.) The other jurisdictions noted by ABATE reasoned that the relevant utility "must rely on design day demand in planning and constructing downstream transmission and distribution facilities" and "the peak and average methodology is not reflective of cost-causation, as [the utility's] system must be sized to meet its Design Day Peak Demand." (See York 4 Tr 1280-82 (citation omitted).) As set out above that is precisely the acknowledgement made here regarding DTE's system, as the Company acknowledged that "[f]rom a cost of service perspective, it is assumed that the system is designed to provide service at design peak day volumes," that "the cost to construct distribution mains is not related to annual volume delivered," and "the cost to construct transmission mains is not related to annual volume delivered." (See ABATE Initial Br at 45-48.) These other jurisdictions also reasoned that there existed "implicit double counting of Average Demand in the P&A methodology" as "the A&E methodology

allocates mains costs based, in part, on Average Demand, and, in part, on the portion of Peak Demand that exceeds Average Demand" while "[a]lternatively, mains costs are allocated under the P&A methodology based, in part, on Average Demand, and, in part, on the total Peak Demand." (See York 4 Tr 1280-82 (citations omitted).) Thus, "Average Demand is included in the Average Demand component and in the Peak Demand component, which includes Average Demand" and "due to residential customers having temperature sensitive demand and corresponding low-load factors, double-counting Average Demand understates the residential cost of service while overstating the cost of service of more efficient gas users." (*Id*.) This reasoning was reiterated in an additional jurisdiction, where the regulatory body explained that the "Peak and Average method . . . initially allocates average costs to each class, but then, instead of allocating just the excess of the peak usage period to the various classes to the cost causing classes, the method reallocates the entire peak usage to the classes that contribute to the peak." (*Id*.) Thus, "the classes that contribute a large amount to the average usage of the system but add little to the peak, have their average usage allocated to them a second time," meaning "the Peak and Average method double counts the average system usage, and for that reason is unreliable." (*Id*.) These are realities at issue here and, as such, the Commission should reject Staff's objection.

Regarding Staff's claim that the Commission has adopted the P&A method in the past, a previous determination which patently does not reflect cost causation should not be maintained simply due to inertia. (Staff Initial Br at 77.) As explained in ABATE's Initial Brief, while the prior Commission Order cited by Staff noted that "peak day load alone is insufficient to pay for the cost of building the plant, and off-peak service alone is not sufficiently desirable to many customers to allow for rates sufficient to recover the costs of building the plant," ABATE's alternative proposal does suggest costs be allocated in this manner. (See ABATE Initial Br at 49.)

As explained above and in ABATE's Initial Brief the average component of the A&E method allocates costs in a manner that reflects that the gas distribution system is required to provide service to customers in every day of the year. (*Id.*; see York 4 Tr 1270-92.) Thus, while that Order claimed that the proposal at issue in that case "would have the Commission allocate the entire cost of the 'plant' to users of the peak day service product, because the whole plant is needed to produce that product," that is not ABATE's alternative proposal here. (See *Id.*) Instead, the proposed A&E method incorporates both average demand and excess demand in a manner which reflects how customer classes cause the Company to incur its related costs better than the P&A method. (*Id.*)

Thus, while the Peak Day method described above best aligns cost with how DTE actually incurs them, the alternative A&E method allocates "some portion of demand-related costs on throughput" which, although it does not best reflect DTE's cost of service, does reflect how the system is used in a more accurate manner than the A&P method. (See Staff Initial Br at 77; ABATE Initial Br at 48-51.) Thus, while the Peak Day method best reflects cost causation, the A&E method reflects how the system is planned to be used every day, even as it may be planned to enable operation on peak days, and aligns costs with causation more accurately than the A&P method.[6] The Commission should therefore reject Staff's objection and, in the event it does not adopt a Peak Day cost allocation method, order the Company follow the A&E method in allocating its costs.

[6] Regarding ABATE's alternative recommendation, Staff argued there is "no support for an equal percentage increase by class," or for the Company providing a A&E COS. (Staff Initial Br at 71; see also DTE Initial Br at 134.) Of course, as demonstrated on the record and throughout ABATE's Initial Brief the current COSSs provided by the Company do not reflect cost of service and should be rejected. (ABATE Initial Br at 39-56.) Thus, the purpose of this recommendation is to provide an equitable allocation of any rate increase while a more cost-reflective COSS is developed and provided in the Company's next rate case. Proceeding instead with a CCOS which does not reflect cost causation is not a reasonable or prudent outcome and will prejudice the customers which are inappropriately allocated additional costs which they do not cause.

III. RELIEF REQUESTED

WHEREFORE, ABATE requests the Commission issue an Order adopting ABATE's positions as outlined in its Direct and Rebuttal Testimony, as well as its Initial and Reply Briefs.

Respectfully submitted,

CLARK HILL PLC

By: Stephen Campbell

Digitally signed by: Stephen Campbell
DN: CN = Stephen Campbell email = scampbell@clarkhill.com C = US O = Clark Hill PLC
Date: 2024.07.31 12:20:34 -04'00'

Michael J. Pattwell (P72419)
Stephen A. Campbell (P76684)
Attorneys for the Association of Businesses Advocating Tariff Equity
Clark Hill PLC
500 Woodward, Suite 3500
Detroit, Michigan 48226
313-309-4274
mpattwell@clarkhill.com
scampbell@clarkhill.com

Date: July 31, 2024

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

*** * * * ***

In the matter of the application of **DTE GAS COMPANY** for authority to increase its rates, amend its rate schedules and rules governing the distribution and supply of natural gas, and for miscellaneous accounting authority	)))))))	Case No. U-21291 ALJ Jonathan F. Thoits

PROOF OF SERVICE

STATE OF MICHIGAN)
) ss
COUNTY OF WAYNE)

Stephen A. Campbell, being first duly sworn, deposes and says that on July 31, 2024, he did cause to be served the ***Association of Businesses Advocating Tariff Equity's Reply Brief,*** as well as this ***Proof of Service*** in the above docket, via electronic mail, to the persons identified on the attached service list.

Stephen Campbell

Digitally signed by: Stephen Campbell
DN: CN = Stephen Campbell
email = scampbell@clarkhill.com
C = US O = Clark Hill PLC
Date: 2024.07.31 12:20:49 -04'00'

Stephen A. Campbell

SERVICE LIST
MPSC Case No. U-21291

Administrative Law Judge Hon. Jonathan Thoits Administrative Law Judge Michigan Public Service Commission 7109 W. Saginaw Hwy., 3rd Floor Lansing, Michigan 48917 Email: thoitsj@michigan.gov	**Counsel for Dept. of Attorney General** Joel B. King Aaron Walden Email: kingj38@michigan.gov WaldenA1@michigan.gov ag-enra-spec-lit@michigan.gov
Counsel for DTE Gas Company Paula Johnson-Bacon Carlton D. Watson Andrea Hayden Email: paula.bacon@dteenergy.com carlton.watson@dteenergy.com andrea.hayden@dteenergy.com mpscfilings@dteenergy.com	**Counsel for MPSC Staff** Monica M. Stephens Michael Orris Anna B. Stirling Heather Durian Email: stephensm11@michigan.gov orrism@michigan.gov stirlinga1@michigan.gov durianh@michigan.gov mayabbl@michigan.gov
Counsel for Citizens Utility Board of Michigan (CUB); Michigan Environmental Council; Natural Resources Defense Council (NRDC); Sierra Club Christopher M. Bzdok Holly L. Hillyer Breanna Thomas Nihal Shrinath **Email:** chris@troposphere legal.com holly@troposphere legal.com breanna@troposphere legal.com nihal.shrinath@sierraclub.org	**Counsel for Environmental Law & Policy Center, The Ecology Center, Vote Solar, And Union of Concerned Scientists, Inc.** Nicholas N. Wallace Daniel H.B. Abrams Carolyn Boyce Alondra Estrada Email: nwallace@elpc.org dabrams@elpc.org cboyce@elpc.org aestrada@elpc.org MPSCdocket@elpc.org
Counsel for City of Ann Arbor Valerie J.M. Brader Valerie R. Jackson **Email**: valerie@rivenoaklaw.com vjackson@a2gov.org	**Retail Energy Supply Association** Jennifer Utter Heston **Email:** jheston@fraserlawfirm.com

Counsel for Billerud Americas Corporation Timothy Lundgren Email: tlundgren@potomaclaw.com	**Counsel for Dearborn Industrial Generation, LLC** Sean P, Gallagher Email: sgallagher@fraserlawfirm.com
Counsel for ABATE Michael J. Pattwell Stephen A. Campbell **Email:** mpattwell@clarkhill.com scampbell@clarkhill.com	**Consultants for ABATE** Jim Dauphinais Email: jdauphinais@consultbai.com