STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of
UPPER MICHIGAN ENERGY RESOURCES CORPORATION for approval of a Certificate of Necessity pursuant to MCL 460.6s for Two Reciprocating Internal Combustion Engine Electric Generation Facilities located in the Upper Peninsula of Michigan, approval of Certificate(s) of Public Convenience and Necessity, approval of a Special Contract with Tilden Mining Company L.C. and related accounting and ratemaking authorizations.
_____/

Case No. **U-18224**
(**e-file paperless**)

THE MICHIGAN PUBLIC SERVICE COMMISSION STAFF'S
REPLIES TO EXCEPTIONS

***** PUBLIC VERSION *****

MICHIGAN PUBLIC SERVICE COMMISSION STAFF

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I. Introduction

Several intervening parties have opposed the Upper Michigan Energy Resources Corporation's (UMERC's) application for a Certificate of Necessity (CON) to build two Reciprocating Internal Combustion Engine (RICE) facilities. The opposition concentrates on fringe issues—like Revenue Sufficiency Guarantee (RSG) charges—that should not determine whether or not the Commission approves the application; the opposition does not deny the facilities' core benefits that are at the heart of this case. No one, for instance, disputes that the RICE facilities, which will replace the Presque Isle Power Plant (Presque Isle or PIPP) if approved, will be cleaner, less expensive, and more efficient than the coal plant they are replacing. Neither is it disputed that the RICE facilities will anchor power supply in the Upper Peninsula when WEPCo retires Presque Isle, while leaving room to reduce waste and develop more solar and wind resources in the future.

Since the RICE facilities will benefit UMERC's customers, and since UMERC's CON application meets all of the statutory requirements, the Commission should reject the opposition's arguments against the RICE facilities and approve the CON.

II. The Regulatory Framework for UMERC's CON Request

In this proceeding, UMERC seeks to take advantage of a provision in Act 286 of 2008, as amended by Act 341 of 2016, which allows UMERC to request a CON preapproving its plan to build electric generation facilities. See MCL 460.6s(1). UMERC asks the Commission to grant it a CON to construct ten Reciprocating

Internal Combustion Engine (RICE) electric generation units at two different sites in the Upper Peninsula capable of generating 183 MW. UMERC estimates that these two facilities will cost approximately $277 million. Through this proceeding, the Commission will decide how much of this $277 million, if any, it will preapprove for the construction of these facilities. Acts 286 and 341 provide parameters for the Commission to follow as it makes this decision.

Under Act 341, the CON process is reserved for projects that cost $100 million or more. The Commission must grant a utility a CON preapproving its estimated project costs if the utility meets five statutory requirements. MCL 460.6s(4). The criteria may be paraphrased as follows:

1. The power must be needed. MCL 460.6s(4)(a).
2. The proposed facility must comply with state and federal environmental laws. MCL 460.6s(4)(b).
3. The estimated costs must be reasonable. MCL 460.6s(4)(c).
4. When compared to other power sources, the proposed facility must be the most reasonable and prudent means of meeting demand. MCL 460.6s(4)(d).
5. If feasible, the utility should use Michigan residents to complete the construction. MCL 460.6s(4)(e).

If the Commission grants a CON, it has discretion to decide the amount it will preapprove. See *In re Indiana Mich Power* Co, MPSC Case No. U-17026, 1/28/13 Order, pp 30–31 ("[T]he Commission is permitted, indeed is required, to limit a CON to reasonable and prudent costs if the record shows that costs are excessive."). Besides the cost information that a utility files, the Commission may

consider other project costs that come to its attention, as well as the costs of alternatives raised by intervening parties. MCL 460.6s(5).

If the Commission grants UMERC a CON in this case and preapproves costs for UMERC's proposed facilities, its decision will meaningfully affect future ratemaking proceedings. MCL 460.6s(9). Once UMERC begins operating the RICE units (i.e., once they are used and useful) and UMERC files a rate case to recover its costs, UMERC's rates will be adjusted to reflect the project costs preapproved in this case. See MCL 460.6s(9). At that time, the Commission may not prevent UMERC from recovering costs that it "incurs in constructing . . . an electric generation facility . . . for which a certificate of need has been granted, if the costs do not exceed the costs approved by the commission in the certificate."[1] *Id.*

A decision approving a CON for UMERC will also meaningfully affect future ratemaking proceedings by allowing UMERC to defer certain financing interest expenses. MCL 460.6s(12) provides, "The commission shall allow financing interest cost recovery in an electric utility's base rates on construction work in progress for capital improvements approved under this section prior to the assets being considered used and useful." UMERC may also "recognize, accrue, and defer the allowance for funds used during construction related to equity capital." *Id.*

Acts 286 and 341 also require the Commission to adopt standard application filing forms and instructions for CON applications. In Case No. U-15896, the

[1] Cost overruns, however, are "presumed to have been incurred due to a lack of prudence." MCL 460.6s(9).

Commission fulfilled its obligation under the statute by adopting Public Convenience and Necessity Application Instructions. *In re the Commission's Own Motion to Implement MCL 460.6s(10) and (11)*, MPSC Case No. U-15896, 12/23/2008 & 5/11/2017 Orders.

III. The Burden of Proof

"[I]n matters before the Commission where statutory law is silent regarding the correct quantum of proof needed to review a utility's costs, the Commission assesses those costs using the preponderance of the evidence standard adopted in civil cases." *In re Detroit Edison Co on Remand*, MPSC Case No. U-15768, 10/17/2013 Order, p 16, citing *Residential Ratepayer Consortium v Public Service Comm*, 198 Mich App 144, 149 (1993). And the Commission has held that "Section 6s did not alter the burden of proof in an administrative proceeding before the Commission." *In re Indiana Michigan Power Company's Application for a Certificate of Necessity*, MPSC Case No. U-17026, 1/28/2013 Order, p 33. UMERC, therefore, has the burden of proving its case by a preponderance of the evidence.

Preponderance of the evidence means "such evidence as, when weighed with that opposed to it, has more convincing force and the greater probability of truth." *People v Pugh*, 48 Mich App 242, 245 (1973). According to the Michigan Supreme Court, preponderance of the evidence "is not satisfied by proof creating an equipoise, but it does not require proof beyond a reasonable doubt. No essential issue may be left to surmise, guess, or conjecture . . . ." [*Dillon v. Lapeer State Home & Training Sch*, 364 Mich 1, 8 (1961) (quotation marks and citation omitted).]

If UMERC proves its case by a preponderance of the evidence, other parties may still challenge that evidence, but at that point the burden of proof shifts to the other parties. In *In re Detroit Edison Co's Application to Increase Rates*, MPSC Case No. U-15768, 1/11/2010 Opinion and Order, pp 35–38, the Commission held that once a utility has satisfied its initial burden of proof, another party "may challenge that evidence and present evidence of unreasonableness." *Id.* at 38. But at that point, the other party "has the burden to demonstrate its position is correct." *Id.*

IV. Background

Events leading to this case began when WEPCo announced its plans to retire the aging Presque Isle Coal Plant, which was no longer needed to serve the Mines (Tilden Mining Company L.C. and Empire Iron Mining Partnership) after they left WEPCo for a choice provider. (3 TR 230.) In other areas of Michigan, retiring a 344 MW power plant may not have presented an insurmountable obstacle, but the Upper Peninsula is an isolated energy load pocket that depends on Presque Isle's power. So the Midcontinent Independent System Operator (MISO) intervened and refused to let WEPCo retire Presque Isle. See *In re Midcontinent Indep Sys Operator, Inc*, FERC Docket No ER14-2860-000, Application for Approval of Replacement SSR Agreement, September 12, 2014, pp 2–3. MISO notified Wisconsin Electric that the facilities qualified to become System Support Resource (SSR) Units and entered into two controversial SSR agreements with Wisconsin Electric that were challenged at FERC. *Id.*

Events spiraled from FERC back to the Midwest where the Integrys Energy Group, Inc. (then Wisconsin Public Service Corporation's parent Company) proposed to merge with the Wisconsin Energy Corporation. The merger was subject to review in several jurisdictions, including Michigan where Wisconsin Energy, the Mines, and other parties to the case agreed to place conditions on the merger. *In re Wisconsin Energy Corp and Integrys Energy Group, Inc*, MPSC Case No. U-17682, 4/23/2015 Order Approving Amended and Restated Settlement Agreement, Attachment 1, pp 3–7. The conditions required Wisconsin Energy and the Mines, along with a possible third party, to take steps to resolve the Upper Peninsula's projected long-term capacity shortfall. *Id*.

As part of the agreement, Wisconsin Energy and the other applicants agreed not to seek another SSR designation for Presque Isle so long as the Mines remained full-requirements customers. *Id*. at 3, ¶6.a. This commitment was to last until the earlier of December 31, 2019 or until a new clean power plant begins operating in the Upper Peninsula. *Id*. In accordance with the agreement (referred to as the Amended and Restated Settlement Agreement or ARSA), Wisconsin Energy created, and the Commission approved, a Michigan-only jurisdictional utility (the Upper Michigan Energy Resources Corporation or UMERC). *In re Upper Michigan Energy Resources Corporation*, MPSC Case No. U-18061, 12/9/2016 Order, p 32. While that case was ongoing, Wisconsin Energy and UMERC entered into a contract with the Mines on August 12, 2016, referred to as the Tilden Special Contract, to meet the Mines' supply requirements.

Through the Special Contract, the Mines' committed to UMERC's proposed generation solution—RICE generating units at then undisclosed locations—and to pay their share of the facilities' costs: all of the operating expenses and half of the capital costs. (3 TR 88–90.) The Mines also committed to purchase power from the facilities for the next 20 years, (3 TR 404), facilitating UMERC's efforts to obtain financing for the project. Although these agreements marked significant progress toward a generation solution, they did not predetermine the result. All of these commitments were conditioned on the Commission approving a CON for the facilities in this proceeding. E.g., *In re Wisconsin Energy Corp and Integrys Energy Group, Inc*, MPSC Case No. U-17682, 4/23/2015 Order Approving Amended and Restated Settlement Agreement, Attachment 1, p 6.

If UMERC's CON is not approved, then all of the progress made to date will be lost. If UMERC's RICE project is not constructed, MISO may identify Presque Isle as a System Support Resource (SSR) once again, which could burden ratepayers across the UP footprint. Fortunately, UMERC has requested a CON that meets Act 286's requirements, as the evidence shows. Through the CON, UMERC has proposed a viable solution to the forecasted capacity shortfall in the Upper Peninsula—a solution that anchors the electric grid in the Upper Peninsula and allows WEPCo to retire PIPP while leaving room to build more renewable energy in the future and further reduce energy waste.'

V. The Proposal for Decision

The ALJ recommended that the Commission grant UMERC a CON confirming the following:

1. The power to be supplied from UMERC's proposed generating facilities is needed, MCL 460.6s(3)(a);

2. The facilities' size, fuel type, and design characteristics are the most reasonable and prudent means of meeting that need, MCL 460.6s(3); and

3. UMERC may recover the facilities' estimated capital and financing costs from its customers. MCL 460.6s(3)(d).

UMERC showed that it needs the power from its proposed generating facilities to meet demand and that its proposed RICE generating facilities are the best way to meet that need—better than the alternatives. UMERC considered continuing to operate the Presque Isle Power Plant, building a combined-cycle power plant, building renewable energy and distributed generation, managing load and reducing energy waste, and adding transmission. The ALJ agreed that none of these alternatives measured up to UMERC's proposal (in terms of costs and benefits). He recommended that UMERC be allowed to recover the facilities' estimated capital and financing costs from its customers, but cost-allocation issues should be decided later.

The ALJ also found that UMERC had satisfied all of the other statutory criteria, including the IRP requirements. After discussing the statutory IRP requirements, UMERC's IRP, and testimony on the subject, the ALJ concluded that UMERC's IRP met the statutory requirements. He noted, however, that the IRP

addressed the unique circumstances facing UMERC's Upper Peninsula customer base and was intended to meet ARSA's objectives:

> Staff witnesses Simpson, Baldwin, and Walker reviewed UMERC's IRP and, for the reasons set forth in the preceding sections, concluded the IRP meets all § 6s (11) requirements. Staff also concluded UMERC's IRP conforms to the Commission's IRP Filing Guidelines, Attachment B to the Commission's Order in U-15896. I agree with Staff's conclusion. I find the evidence presented shows that UMERC's IRP meets the requirements of § 6s (11) and the Commission's IRP filing Guidelines.
>
> I also agree with Staff that the Commission should note that UMERC's IRP is designed to address the unique circumstances associated with UMERC's Upper Peninsula customer base and to meet the objectives Amended and Restated Settlement Agreement (ARSA) approved in. U-17682. [PFD, p 133.]

The ALJ was not persuaded by the ELPC's argument that the IRP did not evaluate resources that could partially displace the proposed RICE generating facilities. He also rejected GlidePath's argument that UMERC's IRP was flawed because it did not include GlidePath's alleged unsolicited proposal. The ALJ was further not convinced by UPPCo's argument that building at two sites instead of one would increase UPPCo's RSG costs or by its arguments that he should reverse his earlier decision granting Staff's motion to strike UPPCo witness Aaron Wallin's testimony. The ALJ rejected Cloverland's arguments as well.

The ALJ recommended that the Commission grant UMERC the CON it requested. He also recommended that the Commission approve the Certificates of Public Convenience and Necessity that UMERC requested, subject to conditions, and that the Commission approved the Tilden Special Contract. He rejected CARE's argument that the Commission could not approve the Tilden Special

Contract in this proceeding, but he agreed with Staff, CARE, and Fibrek that the Commission should not approve the cost allocation in the Tilden Special Contract because UMERC had not satisfied the requirements in Case No. U-10646.

VI. Response to the Environmental Law and Policy Center (ELPC)

In its testimony and initial brief, UMERC considered whether renewable resources could partially displace the proposed RICE generating facilities. The ELPC and some other parties argue that UMERC did not evaluate resources that could partially displace the Company's proposed facilities: "The IRP, inconsistent with MCL § 460.6s(11)(f), *contained no analysis of whether renewable or storage could partially displace* the proposed project and *contained no cost estimates* for renewable or storage alternatives . . . ." (ELPC's Exceptions, p 3.) But UMERC and Staff have already explained that if UMERC attempts to use renewable-energy resources, even in part, to meet its capacity shortfall, it still would need 183 MW of baseload generation to anchor supply in the Upper Peninsula. (Staff's Initial Br, p 53, citing 3 TR 232–233[2]; accord Exhibit A-19, IRP, pp 7–8.) The ALJ agreed. (PFD, p 139.)

During cross examination, UMERC witness Jeffrey Knitter appeared to concede that the IRP did not consider resources that could partially displace the proposed RICE generating facilities:

[2] Staff's Initial Brief contained a typographical error, citing 2 TR 232–233 instead of 3 TR 232–233.

Q And when you evaluated solar in the IRP study, it was evaluated as to whether it could meet 100 percent of the resource requirement?

A Yes.

Q So you did not analyze in the IRP whether solar generation could partially displace the RISE unit generation, did you?

A No.

Q And you didn't analyze whether solar generation plus storage could partially displace the RICE generation?

A I did not.

Q And you did not analyze whether wind generation could partially displace the RICE generation; is that correct?

A That's correct. [3 TR 308–309.]

Mr. Knitter's comments should be considered in context—context that includes Mr. Knitter's statement that "[i]f wind or solar generation were used to supply a significant portion [not all of it] of the 183 MW UP Gen Project, the UP Gen Project would still be needed, in its entirety, to meet the reliability requirements of the UP." (3 TR 232–233.) This is a qualitative analysis in its own right and speaks to "the availability [and feasibility] . . . of other electric resources that could . . . partially displace the proposed generation facility." MCL 460.6s(11)(f). In short, wind and solar cannot partially displace UMERC's proposed project because even if the Company built wind and solar, it would still need 183 MW from the RICE generating facilities.

UMERC also satisfied the statutory requirement that it analyze the "costs of other electric resources that could . . . partially displace the proposed generation

facilities." MCL 460.6s(11)(f). Resources that could, in theory, partially displace the proposed generation project are the same resources that could defer or completely displace the generation project. The Company evaluated these resources and their costs in its IRP and found that the RICE generating facilities will save "UMERC's non-Tilden customers $161 million in net present value over 30 years compared to the next best alternative." (3 TR 224.) Staff agreed that the Company's proposal is the least-cost plan. (See Staff's Initial Br, pp 15–24, 33–36.)

For all of these reasons, the ALJ was right to reject the ELPC's arguments:

> Contrary to ELPC's belief the evidence shows that wind and solar cannot partially displace UMERC's UP Gen Project because even if UMERC built wind and solar, it would still need 183 MW from the RICE generating facilities. UMERC's IRP evaluated these renewable resources and their costs and concluded that the RICE generating facilities would save "UMERC's non-Tilden customers $161 million in net present value over 30 years compared to the next best alternative." Staff in its Brief agreed that the UMERC's UP Gen Project proposal is the least-cost plan. [PFD, p 139 (citations omitted).]

VII. Response to GlidePath

For the most part, GlidePath parrots the ELPC's argument that UMERC's IRP did not analyze resources that could partially displace the proposed RICE generating facilities—an argument Staff has already addressed. GlidePath goes so far as to argue that "there was *no 'analysis'* performed of other generating resources." (GlidePath's Exceptions, pp 4, 6, emphasis added). But that is exactly why UMERC hired HDR Engineering, Inc.: "to evaluate the most feasible options for UMERC to generate power in the Marquette and Keweenaw Peninsula area to

serve its customers." (3 TR 198–199.) HDR prepared a thorough report dedicated to evaluating resource options. GlidePath does not once mention the report.

In GlidePath's Exceptions, it also mischaracterizes Staff witness Julie Baldwin's testimony. It alleged, "Staff witness Baldwin essentially indicates that compliance with the statute was not necessary 'in this particular situation' in UMERC's application for a CON for the proposed RICE generating facilities because UMERC needed to 'own' some generation to supply its customers." (GlidePath's Exceptions, p 7.) That is not what Ms. Baldwin said. Ms. Baldwin agreed that UMERC's IRP met the guidelines in Case No. U-15896 related to renewable energy and, by extension, the statutory requirements on the same topic. (See Exhibit ELP-8.)

When Ms. Baldwin referred to UMERC's unique situation, her point was that the Company does not own baseload generation to anchor its system, which has an impact on whether or not renewable energy can displace or partially displace the proposed project. So while renewable energy may not be the best resource option at this time, there will be room in UMERC's portfolio to develop renewable energy in the future. She said, "In a future IRP which builds upon and adds to UMERC's generation portfolio, a more robust evaluation of renewable energy alternatives to fulfill various levels of the future generation need should be considered." (4 TR 500.)

According to GlidePath, supporting a more robust evaluation of renewable energy alternatives in the future is akin to admitting that "UMERC's IRP was

deficient." (GlidePath's Exceptions, p 8.) Not so. Ms. Baldwin's statement was a forward-looking acknowledgement that more work could be done in the future to diversify UMERC's portfolio. Ms. Baldwin clarified this in a discovery response that GlidePath ignored:

> UMERC's situation is unique because, as I state in my testimony, UMERC is a utility with no company-owned generation in its supply portfolio. The guidelines in Case No. U-15896 require consideration of renewable alternatives. *UMERC did so*, although UMERC's analysis leaves room for a more robust evaluation of renewable alternatives in the future. *This evaluation should take place in future IRP and REP cases where the Company should thoroughly review alternatives to fulfil various levels of future generation need.* [Exhibit ELP-8, emphasis added.]

Ms. Baldwin also noted that "UMERC is subject to the 15% by 2021 renewable energy standard," and UMERC's "renewable energy plan filed at the Commission in Case No. U-18236 will provide an opportunity to examine how the Company will achieve the standard." (*Id.*) Whatever may be required in the future, however, UMERC's proposed RICE facilities are the right generation solution now. They are specifically tailored for UMERC and its customer base in the Upper Peninsula and are the culmination of years of work to resolve projected capacity shortfalls. GlidePath claims that it offered UMERC better supply-side resource options as an alternative to the RICE facilities, which UMERC allegedly ignored. (GlidePath's Exceptions, p 10.) But this is not clear on the record.

GlidePath witness Chris McKissack wrote a memorandum, which he sponsored as an exhibit, that ostensibly chronicled *informal communications* (phone calls and e-mails) between GlidePath and UMERC about GlidePath's verbal

proposal to provide renewable and distributed energy to UMERC. (Exhibit GP-1.) There is no evidence that GlidePath ever *officially tendered a bid* to provide UMERC with power. Mr. McKissack did not even include the e-mails between the parties with his exhibit.[3]

Even if GlidePath had officially bid to provide Cliff's or UMERC with power, there is not enough information in this case for the Commission to seriously evaluate the bid. If a third party like GlidePath wants the Commission to take an alternative proposal seriously, it should provide enough details on the record to allow the Commission to evaluate it.

VIII. Response to the Upper Peninsula Power Company (UPPCo)

UPPCo takes exception to two of the ALJ's findings:

1. UPPCo argues that building at two sites, instead of one, is more expensive and will increase RSG costs for UPPCo and its customers.

2. UPPCo argues that the ALJ improperly struck portions of Mr. Wallin's testimony and that the Commission should overturn the ruling and rely on his testimony.

Below, Staff explains how UPPCo overlooked key facts that led it to reach flawed conclusions.

[3] UMERC also sponsored a discovery response from Mr. McKissack as an exhibit that described informal communications between GlidePath and Cleveland-Cliffs Iron Company (Cliffs). (Exhibit A-22.) There is no evidence that GlidePath ever officially tendered a bid to provide Cliffs with power.

A. The RICE generating facility at the Baraga site will defer transmission costs and reduce RSG costs.

The RICE generating facility proposed for the Baraga site will defer the need for a $100 million upgrade to the Lakota-Winona transmission line. UPPCo argues that these $100 million in savings are really "phantom savings" because the Lakota-Winona upgrade is allegedly no longer necessary due to an "operating guide" transmission reconfiguration. (UPPCo's Exceptions, p 3, quoting 4 TR 677.) UPPCo is mistaken. The transmission reconfiguration was only intended to be a short-term solution to allow an aging generating unit to retire: "MISO indicated in a presentation to stakeholders on August 9, 2016 (Exhibit A–10 (JH-7)) the reconfiguration plan 'provides short term resolution to allow White Pine Unit 1 to retire.' " (3 TR 338.) The Lakota-Winona project is slated to go forward even after the reconfiguration:

> MISO's determination that the reconfiguration is an "acceptable alternative" to White Pine SSR with the notation that ATC will continue to develop a transmission project with a similar scope of the Lakota – Winona project is evidence that both the Transmission Owner (TO) and Planning Coordinator (PC) see a need for this project. It is the responsibility of MISO (PC) and ATC (TO) to withdraw a project that is no longer necessary, and they have not done so. [3 TR 341–342.]

For this reason, the ALJ properly concluded that "[t]he evidence shows that UMREC's UP Gen Project Baraga site and the elimination of the Lakota-Winona upgrade will result in cost savings for UMERC customers." (PFD, p 145.) And he said that building at the Baraga site will save UPPCo's customers even more than UMERC's customers: "[B]ecause UPPCO's retail load is approximately 15% greater

than the non-Tilden UMERC retail load, it is likely that the savings to UPPCO will exceed the savings for the non-Tilden UMERC customers and provide NPV savings in excess of $1 million with an average benefit of approximately $125,000 per year." (*Id.*)

UPPCo argues, in the alternative, that if UMERC builds at two sites instead of one, UPPCO will incur an additional $200,000 annually in RSG charges. (UPPCo's Exceptions, p 4.) Mr. Wallin, however, did not compare UPPCo's projected RSG charges with its current charges. (*Id.*) Mr. Knitter did. He found that UPPCo's RSG charges will actually decrease compared to current levels, probably by more than 75%, if UMERC goes forward with its proposed project. (3 TR 251.) He reached this conclusion using Mr. Wallin's own exhibit, Exhibit UPP-3, that shows "UPPCO paid $509,057 in RSG Costs in 2016 and that the future two-site UPPCO RSG costs will drop to $325,839, *a savings of over $175,000 per year after the UP Gen Plant is built*." (3 TR 251, emphasis added.)

The $175,000 in savings are based on Mr. Wallin's projections, but even these projections are too high. Mr. Wallin's projections are based on flawed inputs, which when corrected, show that UPPCo will save more than he estimates. According to Mr. Knitter, "Mr. Wallin's assumptions are based on a very high level of reliability dispatch and a very high percentage allocation of the Baraga site costs to UPPCO." (3 TR 252.) When Mr. Knitter substituted these flawed assumptions with more realistic assumptions, UPPCo's projected RSG costs dropped to "$123,000 per year, or less than 40% of the cost calculated by Mr. Wallin for a two-site project as

proposed, *a savings of almost $400,000 per year compared to UPPCO's current RSG costs*." (3 TR 252–253, emphasis added.)

Moreover, after correcting Mr. Wallin's flawed inputs, there is not much difference between building on one site and building on two. Specifically, "The hypothetical single site has about $75,000 per year in lower RSG costs than the two site UP Gen project." (3 TR 253.) Indeed, when also considering UPPCo's energy and transmission costs, UPPCO would be worse off. As Mr. Knitter explained, "Factoring in transmission costs savings of $125,000 per year and energy cost savings of $150,000 per year offsetting these savings with increased VLR/RSG costs of $75,000 per year, *UPPCO's overall costs would be higher by $200,000 (or more)* if, hypothetically, all the RICE units were built at Negaunee." (*Id.*)

Changes to UPPCo's RSG charges are not a good reason to abandon the Baraga plant. UMERC's proposed facilities, when they are both built, will actually reduce UPPCo's costs more than building at one site would. UPPCo should be supporting UMERC's proposed facilities, not opposing them.

B. The ALJ should reject UPPCo's arguments that he improperly struck testimony from the record.

UPPCo argues that the Commission should overturn the ALJ's ruling granting Staff's Motion to Strike, but UPPCo does not explain why the ALJ was wrong to find that Mr. Wallin speculated about UPPCo's possible future plans. (UPPCo's Exceptions, pp 6–7.) The ALJ's decision should only be overturned if the Commission finds that he abused his discretion and that the result is "so palpably

and grossly violative of fact and logic that it evidences perversity of will, defiance of judgment or the exercise of passion or bias." *In re Consumers Energy Co*, MPSC Case No. U-17317, 5/20/2016 Order, p 5 (citation and quotation marks omitted). UPPCo has not demonstrated that the ALJ abused his discretion.

In his pre-filed direct testimony, Mr. Wallin claimed that the Upper Michigan Energy Resources Corporation (UMERC) proposed Baraga plant would deprive UPPCo of a prime location to build and would monopolize the gas supply in the area. Mr. Wallin's arguments were premised on UPPCo's *possible* plans to "build generation to meet its own customer's exposed energy and capacity needs." (4 TR 683.) Based on this testimony, UPPCo opposed UMERC's proposed CON for the Baraga site because its IRP *might* indicate that it needs additional generation, it *might* decide to meet that need by building a power plant (rather than entering into a power purchase agreement), and it *might* want to use UMERC's proposed Baraga site for its plant. Mr. Wallin's testimony on this subject was too speculative on too many levels to consider in this case.

Mr. Wallin referenced UPPCo's ongoing Integrated Resource Plan (IRP) as support for UPPCo's position, but UPPCo has not yet released its IRP or committed to building additional generation to serve its customers. UPPCo has not complied with the Michigan Rules of Evidence, which require UPPCo to admit evidence to support its position, MRE 702 and 703, and give judges the discretion to strike speculative testimony. See *Phillips v Deihm*, 213 Mich App 389, 401–402 (1995)

("Where such [expert] testimony is purely speculative, it should be excluded or stricken pursuant to MRE 403.").

The ALJ agreed that Mr. Wallin's testimony about the Baraga plant did not satisfy MRE 703:

> In granting Staff's motion with regard witness Wallin's testimony, I agreed that MRE 703 required UPPCO to admit into evidence the facts or data underlying witness Wallin's opinion. UPPCO did not admit the IRP that witness Wallin references in his testimony because no such IRP exists.
>
> I also agreed with Staff that witness Wallin's testimony did not satisfy MRE 703 because it was not based on sufficient facts or data and is not reliable. If UPPCO has an IRP or plan to build new generation at the Up Gen Projects Baraga site, it did not file that IPR or plan in the CON proceeding nor did it file a § 6s(4) alterative proposal for the Commission's review and consideration.

The ALJ also agreed that Mr. Wallin's testimony about the Baraga plant did not satisfy MRE 702:

> According to MRE 702 a qualified expert's testimony is admissible if the:
>
> a) Testimony is based on sufficient facts or data,
>
> b) Testimony is the product of reliable principles and methods, and
>
> c) Witness has applied the principles and methods reliably to the facts of the case.
>
> There is no dispute that witness Wallin is a qualified expert witness. However, his speculative testimony regarding UPPCO's future plans regarding the UP Gent Project's Baraga site is not based on sufficient facts or data to be admissible. Therefore, I recommend the Commission affirm my decision to strike UPPCO witness Wallin's testimony regarding the UP Gen Project Baraga site. [PFD, p 152, citation omitted.]

UPPCo does not appear to disagree with these findings. Not once in its Exceptions does it dispute that Mr. Wallin's testimony was speculative. Instead, UPPCo seems to argue that Mr. Wallin's testimony was so critical to the case that it should be admitted regardless of its evidentiary foundation. (See UPPCo's Exceptions, p 6, "[W]itness Wallin's testimony shows that UMERC's decision to build two generating facilities and position one of those facilities, which Mr. Wallin demonstrated to be unnecessary, at a critical transmission juncture, substantially impacts other Upper Peninsula utilities, which is a principal concern of MCL 460.6s.") This is not a reason to overturn the ALJ's ruling. The ruling may only be overturned if the ALJ abused his discretion, and he did not.

IX. Response to Cloverland

Like UPPCo, Cloverland argues that its RSG charges may increase if UMERC builds its proposed RICE facilities. (Cloverland's Exceptions, pp 3–4.) But unlike UPPCo, Cloverland did not even attempt to admit evidence on this subject. The only evidence on the record about Cloverland's RSG charges is UMERC's testimony that load-serving entities would pay less in RSG charges if UMERC builds its proposed facilities. (3 TR 251.) RSG charges arise when a plant is dispatched because it is needed for reliability, and the Presque Isle Coal Plant (as the primary baseload generation in the Upper Peninsula) drives most of the RSG charges in the region when it runs even though it is uneconomic to do so. (*Id*.) Since Presque Isle "has higher production costs than the UP Gen Project units, RSG

and VLR are expected to go down significantly" when the new RICE facilities are built, probably more than 75% below current levels. (*Id.*)

In any case, Cloverland is a third-party electric provider. UMERC's customers will be the ones who pay for UMERC's proposed project, so the Commission should evaluate the project's cost and rate impact on UMERC's customers. Any ancillary impact on third parties like Cloverland should be given little or no weight.

X. Response to UMERC and the Tilden Mining Company L.C.

Staff agrees with UMERC and Tilden on almost every issue in this case. On one issue, however, Staff disagrees. UMERC and Tilden ask the Commission to allow UMERC to allocate to non-Tilden customers the costs "to construct, own, and operate the RICE electric generation facilities . . . in rates set in future UMERC rate proceedings, consistent with the terms of the Tilden Special Contract." (UMERC's Exceptions, pp 1–2.) But as the ALJ found, UMERC did not adequately support its request to allocate costs this way. (PFD, p 176, "[T]he evidence presented does show that UMERC has not satisfied the U-10646 Order COSS requirement.") This is why the Commission should deny UMERC's and Tilden's request until it is buttressed by a cost-of-service study in a future rate case.

UMERC also asked the Commission to clarify two findings in the PFD. Staff supports this request.

A. UMERC and Tilden did not adequately support their request to allocate costs as agreed upon in the Tilden Special Contract.

UMERC argues that without assurances that it will recover the costs of its proposed project, UMERC will assume substantial risk. (UMERC's Exceptions, pp 30–31.) The Company also argues that the Special Contract so clearly benefits its non-Tilden customers that the Company does not need to back up its request for special ratemaking treatment with a cost-of-service study. (*Id.* at 24–30.) The Company cannot have it both ways. If its evidence about the need for special ratemaking treatment is as compelling as the Company suggests, then there is little to no risk that a cost-of-service study will not confirm it. On the other hand, if the Company is assuming substantial risk, then its evidence cannot be as compelling as the Company suggests.

In Staff's view, UMERC's evidence is compelling, so there is little risk that it will not be allowed to charge its proposed rates or recover its costs. (4 TR 527.) Staff witness Nick Revere explained why:

> While there is some risk to the Company in having to wait for approval of the ratemaking treatment of costs accruing to non-Tilden customers as a result of the Tilden Contract, that risk is minimal. The benefits that accrue to non-Tilden customers based on reasonable assumptions about the current power purchase agreements (PPAs) and the Reciprocating Internal Combustion Engine (RICE) units enabled by the Tilden Contract significantly outweigh the costs (otherwise attributable to Tilden under traditional ratemaking) that non-Tilden customers would bear. Modifying the assumptions to explore different potential outcomes still results in significant benefits for non-Tilden customers. [4 TR 526–527.]

But no matter how compelling the IRP and the supporting testimony is, no utility should be relieved of the duty to file a cost-of-service study to prove that costs

potentially pushed on to other customers by a special contract are justified. As the ALJ said, [I]gnoring the Commission special contract requirements would weaken the strong protections the Commission has put in place for special contract ratemaking and would place non Tilden customers at risk." (PFD, p 173, summarizing Staff's testimony.)

UMERC claims that it met the "compelling showing" required for a utility to "reallocate the costs of serving contract customers to other ratepayer classes." *In re Detroit Edison Co's Application for Special Electric Supply Contracts*, MPSC Case No. U-10646, 3/23/1995 Order, p 21. The order gave utilities two options for satisfying this compelling showing:

> To make a compelling showing for a different treatment, Detroit Edison would bear a substantial burden. This burden would require, at a minimum, a clear, convincing, and unequivocal demonstration either (1)_that the contract prices and terms are justified on the basis of the cost of service, or (2) that the benefits for other (non-participating) ratepayers are substantial and have a value that outweighs the costs that are not recovered from the contract customers. [*Id*.]

UMERC claims that it has satisfied the second option and that no cost-of-service study (COSS) is required to meet the second option. This claim cannot be squared with the language of the order, which says that "[e]ither showing would require support from a cost-of-service study that identifies and quantifies all costs incurred under the contracts." *Id*. Further, under the second option, a utility cannot know whether the benefits outweigh the costs unless they are properly quantified.

The Company also misunderstands the two options, as evidenced by its claim that only a COSS differentiates the two, when both require it. Under the first option, rates must be justified purely on a COSS with that customer as a separate class, while under the second, the benefits of the contract must outweigh the costs identified in a COSS, even if the rates are not justified purely by the COSS results.

UMERC also misconstrues the ARSA approved in Case No. U-17682. The Company argues, "Deferring a determination of UMERC's recovery of its UP Gen project costs would be inequitable and contrary to the clear terms of the ARSA, which contemplate UMERC receiving cost recovery relief in this case." (UMERC's Exceptions, p 31.) While the ARSA envisioned a CON proceeding and even conditioned the ARSA on CON approval, the ARSA did not predetermine the result in this case.

As CARE correctly pointed out in its initial brief, the ARSA reserved all ratemaking questions, (CARE's Initial Br, p 20), saying that UMERC's generation investment "will be fully recovered through Michigan retail rates, *if just and reasonable*." (Exhibit A-3, Attachment 1, pp 6–7, ¶ 6(g), emphasis added.) UMERC needs to provide a cost-of-service study to ensure that the rates it is charging are just and reasonable.

Additionally, the ARSA did not explain how the costs will be recovered (i.e., from which classes or customers), except to say that they will be "fully recovered" if a CON is approved. By drafting a special contract that is not flexible enough to

incorporate a Commission-approved cost allocation, the Company has created this risk that the costs will not be recovered.

[redacted]

B. Staff supports UMERC's request for clarification.

The ALJ recommended that the Commission approve UMERC's CON subject to two conditions:

1. UMERC may not operate the UP Gen Project's Baraga Township electric generation plant until SEMCO receives a Certificate of Public Convenience and Necessity to construct, own and operate the Baraga pipeline as filed in Case No. U-18384.

2. UMERC may not operate the Up Gen Project's Negaunee Township electric generating plant until SEMCO receives a Certificate of Public Convenience and Necessity to construct, own and operate the Negaunee pipeline as filed in Case No. U-18385. [PFD, p 182.]

UMERC accepted these conditions, but it asked that if the Commission adopts them, it do so with one caveat:

> UMERC requests that if the Commission adopts them, the Commission word the conditions in a way that permits UMERC to pursue other options, so that if for some reason the Commission does not approve SEMCO's applications in Case Nos. U-18384 and U-18385 [for lateral pipelines to supply the RICE generating facilities], then UMERC's operation of the new generating units would be subject to the Commission approving CPCNs for laterals constructed by an alternative similar supply source. [UMERC's Exceptions, p 32.]

This is a reasonable request that Staff supports.

XI. Response to CARE

Staff disagrees with CARE that "[n]o legal authority exists to seek approval of a Rule 31 special contract in a CON case." (CARE's Exceptions, p 10.) Rule 31 requires a utility to file an application; it does not specify the type of proceeding in which an application may be filed. It says, "When a utility enters into a special contract to provide service in a manner or at a rate not specifically covered by its filed rate schedules or rules and regulations, the utility shall file an application for approval of the special contract with the commission." Mich Admin Code, R 460.2031. Rule 31 should be interpreted like a statute. *In re Complaint of Consumers Energy Co*, 255 Mich App 496, 503–04 (2002) ("[C]ourts apply principles of statutory construction in construing administrative rules.").

Rule 31's silence about where and when an application should be filed is evidence that the Commission retains discretion to decide this question. In *In re Detroit Edison Co Application*, 296 Mich App 101, 118 (2012), the Court of Appeals held that "the Legislature intended the specificity where it was specific and the silence where it was silent," and where the Legislature was silent, the Commission retains discretion. Here the rule is silent, meaning that the Commission has

discretion to decide where and when a utility may file an application to approve a special contract.

This conclusion makes sense given that if UMERC had filed separate applications, the Commission could have, consistent with its statutory authority, consolidated the two cases. See Mich Admin Code, R 792.10415 ("The commission . . . may order proceedings consolidated for hearing on any or all matters at issue in the proceeding . . . ."). If the Commission could have consolidated separate applications and approved them jointly, there is no reason why it could not also accept and approve a single application requesting the same relief.

CARE argues that MCL 460.6s "includes a detailed list of approvals that the Commission may grant with respect to the construction or purchase of a generating facility," which does not include approval of a special contract. As a result, CARE argues, special contracts may not be approved in a CON case. CARE also says that "[t]he wording of [Rule 31] plainly contemplates a special-purpose case," (CARE's Exceptions, p 10), but in reality the rule never uses the words "special-purpose case." By CARE's reasoning, therefore, this would mean that a utility cannot file a special-purpose case to approve a special contract since it is not specifically spelled out in the statute. Obviously, this is not the case.

CARE also disputes the ALJ's finding that there is no evidence of cost shifting. It points to testimony that Tilden will consume about 70% of UMERC's load but only pay 50% of the capital costs. (CARE's Exceptions, p 5.) But consuming 70% of UMERC's load does not necessarily equate to being responsible

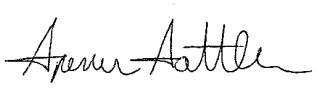
for 70% of UMERC's costs. Further, although Tilden will pay 50% of the capital costs, there are other costs to consider as well. Tilden, for example, has agreed to pay all of the new plant's operations and maintenance expenses. (3 TR 88–89.)

XII. Conclusion

For the reasons set forth in Staff's testimony, exhibits, and filings, the Commission should grant UMERC a CON for its proposed RICE generating facilities. The Commission should also approve the Tilden Special Contract and UMERC's requested Certificates of Public Convenience and Necessity subject to the conditions that Staff has proposed.

Respectfully submitted,

MICHIGAN PUBLIC SERVICE COMMISSION STAFF



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DATED: September 25, 2017
18224/Replies to Exceptions

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of
UPPER MICHIGAN ENERGY RESOURCES CORPORATION for approval of a Certificate of Necessity pursuant to MCL 460.6s for Two Reciprocating Internal Combustion Engine Electric Generation Facilities located in the Upper Peninsula of Michigan, approval of Certificate(s) of Public Convenience and Necessity, approval of a Special Contract with Tilden Mining Company L.C. and related accounting and ratemaking authorizations.
_____/

Case No. **U-18224**
(e-file paperless)

PROOF OF SERVICE

STATE OF MICHIGAN)
) ss
COUNTY OF EATON)

TINA L. BIBBS, being first duly sworn, deposes and says that on **September 25, 2017,** she served a true copy of **THE MICHIGAN PUBLIC SERVICE COMMISSION STAFF'S REPLIES TO EXCEPTIONS (Public Version)** upon the following parties **via e-mail only:**

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Subscribed and sworn to before me
this **25th** day of **September, 2017.**

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State of Michigan, County of Clinton
Acting in the County of Eaton
My Commission Expires: 5-7-2018