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July 28, 2016

Ms. Kavita Kale
Michigan Public Service Commission
7109 W. Saginaw Highway
P.O. Box 30221
Lansing, Michigan 48909

Re: MPSC Case No. U-17990

Dear Ms. Kale:

Attached for electronic filing in the above-referenced matter, please find the Corrected Direct Testimony and Exhibits of Alexander J. Zakem and Proof of Service filed on behalf Energy Michigan, Inc. The Testimony was corrected in one place, on Page 13, line 5, to substitute the word "greater" for the word "less." The rest of the Testimony and all Exhibits remain unchanged.

Thank you for your assistance in this matter.

Sincerely yours,

VARNUM

Timothy J. Lundgren

TJL/kc

c. ALJ
Parties

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STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for authority to increase its rates, for)
the generation and distribution of)
electricity and for other relief)
_____)

Case No. U-17990

CORRECTED DIRECT TESTIMONY
OF
ALEXANDER J. ZAKEM
ON BEHALF OF
ENERGY MICHIGAN, INC.

1 **Q. Please state your name and business address.**

2 A. My name is Alexander J. Zakem and my business address is 46180 Concord,
3 Plymouth, Michigan 48170.

4
5 **Q. On whose behalf are you testifying in this proceeding?**

6 A. I am testifying on behalf of Energy Michigan, Inc. (“Energy Michigan”).
7

8 **Q. Please state your professional experience.**

9 A. Since January of 2004 I have been an independent consultant providing services
10 to various clients, including members of Energy Michigan.

11
12 From March 2002 to December 2003, I was Vice President of Operations for
13 Quest Energy, an alternative energy supplier in Michigan. My responsibilities
14 included the overall direction and management of Quest’s power supply to its
15 retail customers. This included power supply planning, development of
16 customized products, negotiation with suppliers, planning and acquiring
17 transmission rights, and scheduling and delivery of power. It also included
18 managing risk with respect to market price movements and variation of customer
19 loads.

20
21 Prior to joining Quest, I was employed Detroit Edison in 2001, where from 1998
22 to 2001, I was the Director of Power Sourcing and Reliability, responsible for
23 purchases and sales of power for mid-term and long-term periods, planning for

1 generation capacity and purchase power needs, strategy for and acquisition of
2 transmission rights, and related support for regulatory proceedings.

3
4 Additional experience, qualifications, and publications are provided in Exhibit
5 EM-1 (AJZ-1).

6

7 **Q. Have you testified as an expert witness in prior proceedings?**

8 A. Yes. I have testified as an expert witness in several proceedings before the
9 Michigan Public Service Commission (“Commission”), on topics such as standby
10 rates, retail rates and regulations, recovery and allocation of costs and revenues,
11 and the effects of rate restructuring. I have also testified before the Federal
12 Energy Regulatory Commission. Case citations are provided in Exhibit EM-1
13 (AJZ-1).

14

15 **Q. Are you sponsoring any exhibits?**

16 A. Yes. I am sponsoring the following exhibits:

17 Exhibit EM-1 (AJZ-1) Qualifications

18 Exhibit EM-2 (AJZ-2) 2016 OMS MISO Survey Results

19 Exhibit EM-3 (AJZ-3) Improvement in MISO Assessments
20 of Zone 7 Capacity Deficit
21

22

1 **Q. What is the purpose of your testimony?**

2 A. Consumers Energy (“CE”) functions as both an electric distribution company
3 (“EDC”) and a load serving entity (“LSE”). It provides distribution service to all
4 retail customers in its service area, both Full Service customers and Retail Open
5 Access (“ROA”) customers in the Electric Choice (“EC”) program, and it
6 provides power supply service to Full Service customers. As an EDC, it should
7 treat all customers – both Full Service customers and ROA customers equally and
8 fairly regarding rules, distribution services, and charges affecting EC customers.

9
10 The purpose of my testimony is to identify and assess the Consumers Energy
11 proposals affecting ROA customers and, if needed, to recommend changes that
12 make the proposals more equitable.

13
14 **Q. What proposals and rules are you going to address?**

15 A. I will address the following:

16 1. *Employee Incentive Compensation Plan* – Consumers Energy is again
17 proposing that portions of its incentive compensation program should be
18 paid for by customers. If the Commission approves the utility’s proposal,
19 the share borne by ROA customers should be commensurate with the
20 benefits they receive.

21
22 2. *Michigan Capacity* – A “Michigan-first” capacity concept is not
23 economically viable in the Midcontinent ISO (“MISO”) region. Additional

1 and more recent data from MISO will give a more complete perspective on
2 capacity available to the Lower Peninsula Zone 7.

3
4 3. *Plug-In Electric Vehicle Program* – The proposed program primarily
5 promotes increased use of electricity, and as such the costs should be
6 allocated to power supply.

7
8 4. *Economic Development Expenses* – CE is proposing an economic
9 development program to help bring more businesses to Michigan. The role
10 of CE as a potential economic development agent of state government
11 deserves scrutiny. The cost allocation effects on ROA customers may not
12 be fair.

13
14 5. *Revenue Adjustment Mechanism (“RAM”)*
15 CE is proposing an RAM to compensate for variation in actual sales
16 compared to projected sales used to set rates. The proposal is premature and
17 has deficiencies.

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1. Employee Incentive Compensation Plan

**If included in revenue requirements, the share borne by
ROA customers should be commensurate
with the benefits they receive.**

**Q. What is your opinion on Consumers Energy’s incentive compensation
proposal?**

A. The application of CE’s incentive compensation proposal (“Employee Incentive
Compensation Plan” or “EICP”) as applied to ROA customers should be
modified. The EICP is shown in Exhibit A-30, and the proposed electric share of
expenses is shown on Exhibit A-32.

The inclusion of incentive compensation in rates – and how much should be
included – is a policy issue for the Commission that has been argued, re-argued,
ordered, and re-ordered for many years.

My perspective is that if incentive compensation is going to be included in rates
and tied to utility performance, then rate recovery should be allowed only in the
rates of customers that are specifically benefitted by specific performance criteria,
and in an amount that reflects a reasonable sharing of the benefits of superior
performance that would not have occurred without the incentive.

**Q. Have you addressed this issue in previous CE cases, and if so are your
recommendations different?**

1 A. CE's EICP proposal in its previous general rate case, Case No. U-17735, was
2 approved by the Commission. That was a policy decision, and I am not revisiting
3 that decision. In this proceeding I am addressing the fair application of that
4 policy to ROA customers, a narrower perspective.

5

6 **Q. Has the Commission already addressed the issues you are raising in this**
7 **proceeding?**

8 A. No, it has not. In its order of November 19, 2015, in Case No. U-17735, the
9 Commission stated: "Finally it should be noted that Energy Michigan did not file
10 exceptions or replies, and therefore the Commission declines to address its
11 proposed changes to Consumers' EICP." Order at p. 78.

12

13 In the September 16, 2015, Proposal For Decision ("PFD") in Case No. U-17735,
14 the Administrative Law Judge recommended exclusion of the entire EICP. PFD
15 at p.127. Consequently, there was nothing in the PFD for Energy Michigan to
16 take exception to related to the proposed EICP. Nevertheless, the Commission
17 did not address the issues raised by Energy Michigan in its Testimony and
18 briefing when the Commission chose to depart from the PFD's recommendations.

19

20 **Q. Do the performance measures in Exhibit A-30 reasonably reflect the sharing**
21 **of benefits of superior performance, if they were to be included in the rates of**
22 **ROA customers for distribution services?**

1 A. No, in several areas they do not. The two main deficiencies are (a) failure to tie
2 financial performance to benefits to customers – which affects all customers, not
3 just ROA customers – and (b) failure to separate distribution service benefits from
4 power supply service benefits that ROA customers do not receive – which affects
5 only ROA customers.

6
7 Regarding the failure to tie financial performance to ROA customer benefits,
8 Exhibit A-30 shows that 50% of the incentive payout is tied to financial goals –
9 earnings per share and operating cash flow. For any rate-paying customer to pay
10 a bonus to a utility for increasing earnings per share is illogical and violates the
11 principle of paying for a shared benefit on a cost-of-service basis. Such a system
12 forces ratepayers to reward the utility for making them pay more, as the earning
13 are earned on the ratepayers’ backs, so to speak. Moreover, “performance”
14 defined as increased earnings per share benefits stockholders, not customers.
15 Therefore, if there is to be a shared benefit, the share due to financial performance
16 should not come out of ROA customers’ distribution rates.

17
18 **Q. What is your recommendation?**

19 A. My recommendation is that if the Commission approves the continuation of the
20 EICP, then the “financial” portion shown on Exhibit A-30 should be excluded
21 from the distribution rates of ROA customers.

22

1 **Q. The other portion of Exhibit A-30 relates to safety, reliability, and customer**
2 **value. How would you assess these parts of the proposal?**

3 A. Consumers Energy has failed to separate distribution service benefits from power
4 supply service benefits. Specifically, regarding “reliability,” there are three
5 measures of reliability in that category on Exhibit A-30. Two of the measures
6 pertain to distribution performance (“Repetitive Electric Outages” and
7 “Distribution Reliability”), and one pertains to the forced outage rate of
8 generation performance (“Generation Reliability (EFOR)”). Full service
9 customers take both power supply service and distribution service, while ROA
10 customers take only distribution service. Full service customers benefit from
11 improved EFOR because (a) when generation is running or can run, the full
12 service customers are better hedged against Midcontinent Independent System
13 Operator (“MISO”) market energy prices including the costs of ancillary services,
14 and (b) the generation has a higher capacity rating when Consumers Energy
15 applies the generation to satisfy the MISO planning resource requirements. But
16 because these are benefits on the power supply side, ROA customers do not
17 receive these benefits because they do not receive power supply service from the
18 utility. Therefore, if there is a reliability component in the approved incentive
19 compensation mechanism, ROA customers should pay only for the performance
20 in distribution reliability.

21
22 **Q. What is your recommendation?**

1 A. My recommendation is that if the Commission approves the continuation of the
2 EICP, then the “Generation Reliability (EFOR)” portion shown on Exhibit A-30
3 should be excluded from the distribution rates of ROA customers.
4

5
6 **2. Demand Response and Michigan Capacity**

7 **a. MISO Demand Response Cannot be “Michigan First”**
8

9 **Q. CE testimony describes the proposed demand response program as a**
10 **“Michigan-first” energy resource that helps to manage “the capacity**
11 **shortage.” What is a “Michigan-first” energy resource, and is there a**
12 **capacity shortage in Michigan?**

13 A. CE witness Mr. Julio H. Morales calls the demand response program a
14 “Michigan-first, flexible commercial and industrial energy resource that can help
15 meet capacity needs.” J.Morales direct testimony, page 7, lines 6-7. He also
16 states, “Additionally, customers can feel proud, knowing they are contributing to
17 a sustainable and Michigan-first energy resource that benefits the communities
18 they live and work in.” J.Morales direct testimony, page 9, lines 10-13.
19

20 At the same time, he also states, “Proper management of the portfolio of
21 customers, in terms of diversity and event management, ensures a resource that
22 delivers predictable capacity as a Load Modifying Resource in the MISO market.”
23

1 MISO uses all resources to serve all load, subject to transmission constraints. A
2 Load Modifying Resource (“LMR”) that is offered to MISO to satisfy capacity
3 requirements can be used by MISO for any region, zone, or state within MISO.
4 The use of a demand response resource made up of customers in the CE service
5 area is not limited to the CE service area or even to Michigan. For example, the
6 CE demand response resource could be dispatched by MISO, subject to MISO
7 procedures, to benefit a reliability event in Indiana. There is no “first” for
8 Michigan in the use of this resource.

9
10 Nevertheless, a demand response resource can be a useful and economic capacity
11 resource, if designed and managed well. I am not objecting to Mr. Morales’s
12 assessment of the merits of the proposed demand response program. I am
13 correcting the misleading impression that somehow the people of Michigan will
14 have greater electric supply/demand reliability compared to other states in MISO
15 as a result of the CE demand response program.

16
17 **Q. Could a so-called “Michigan-first” energy policy actually be harmful to**
18 **electric customers in the state?**

19 A. Yes. What CE is calling a “Michigan-first” energy policy could be economically
20 harmful to electric customers in the state. The reason is that if Michigan desires
21 to satisfy all its electric capacity needs through capacity resources within the state,
22 then it will need significantly more capacity resource than it requires now when it
23 is sharing all of MISO resources via the transmission capacity in and out of

1 Michigan. A so-called “Michigan-first” policy foregoes the value of sharing a
2 greater diversity of supply over a greater diversity of load, within MISO.

3 Reducing capacity requirements *for all* is one of the great values that MISO, as a
4 Regional Transmission Organization “(RTO)”, brings for CE’s and other
5 Michigan utilities’ membership in MISO.

6
7 **Q. Can you give an example of the capacity value gained by Michigan being a**
8 **part of MISO and sharing all resources?**

9 A. Yes. MISO provides this information. It can be found in MISO’s report
10 “2016/2017 Planning Resource Auction Results,” May 4, 2016 (“PRA Report”),¹
11 which displays information for all of MISO zones, including Zone 7 Lower
12 Michigan.

13
14 First, consider how much capacity Lower Michigan would need if it were
15 independent – that is, if it made no use of the transmission system to share other
16 resources in MISO. MISO calls this the Local Reliability Requirement (“LRR”),
17 and displays it on page 17 of the PRA Report as 24,372 MW.

18
19 Next, consider how much capacity Lower Michigan actually needs as part of
20 MISO. Page 17 of the PRA Report also displays the Planning Reserve Margin

¹ “2016/2017 Planning Resource Auction Results, Resource Adequacy Subcommittee, May 4, 2016,” page 17.
https://www.misoenergy.org/Library/Repository/Meeting%20Material/Stakeholder/RASC/2016/20160504/20160504%20RASC%20Item%2003a%202016-17_PRA_Summary.pdf

1 Requirement (“PRMR”) for Zone 7 as 22,406 MW. This is the amount of
2 capacity that Zone 7 actually is required to have considering all the resources in
3 MISO and the transmission interconnection among the various zones.

4
5 The actual required PRMR is ~~greater~~ less than the “self-sufficient” PRMR by
6 1,966 MW. Thus, a “Michigan-first” energy policy would cost customers 1,966
7 MW worth of additional capacity. At a low estimate of \$600 per kW for a simple
8 combustion turbine, the investment cost of the additional 1,966 MW would be
9 about \$1.1 billion. On a per year expense basis, using MISO’s estimated annual
10 cost of a combustion turbine, \$93,000 per MW, the annual expense would be
11 about \$180 million per year.

12
13 *Thus, an additional \$1.1 billion of investment costs to customers or an annual*
14 *expense of \$180 million per year is the price that Michigan electric customers*
15 *would pay for having what CE calls a “Michigan-first” or self-sufficient*
16 *Michigan energy policy, compared to sharing resources within MISO.*

17
18 **Q. What is your recommendation to the Commission?**

19 A. The stated purpose of CE’s proposed demand response program is to create a
20 *power supply* capacity resource to be used to satisfy CE’s capacity requirement
21 with MISO. As such, the capital expenditures of \$518,000 in Exhibit A-49 and
22 the O&M expenses of \$2,815,000 in Exhibit A-50 should be *excluded from the*
23 *distribution costs that ROA customers pay.* CE witness Ms. Anne K. Rogus

1 shows the revenue requirement for the demand response program as \$2,877,000.

2 Ms. Rogus direct testimony, page 13.

3
4 **2. Demand Response and Michigan Capacity**

5 **b. Latest MISO report shows minimal deficit and likely surplus.**

6
7
8 **Q. In its justification for the demand response program, CE cites “the capacity**
9 **shortage.” What is a capacity shortage for CE?**

10 **A.** CE witness Mr. Morales speaks about the demand response program managing
11 “the capacity shortage” and bridging “the capacity gap.” Mr. Morales direct
12 testimony, page 16, line15, and page 9, line 4.

13
14 MISO instead uses the terms “surplus” and “deficit,” and using the same
15 terminology here can clarify the discussion. MISO periodically assesses the
16 electric capacity requirements for its region and sub-regions, called “zones,” and
17 establishes specific capacity requirements for Load Serving Entities (“LSEs”) in
18 its region. MISO’s Zone 7 is the MISO area in the Lower Peninsula of Michigan.
19 The capacity requirements are set to cover each forecasted LSE’s load at the time
20 of the MISO annual system peak, plus a reserve margin that covers variation in
21 load and generation random outages. For the purpose of assessing surpluses and
22 deficits, MISO uses installed capacity (“ICAP”), which is the capability of the
23 resource without any outages, and an associated reserve margin of 15.2%.

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If the amount of capacity resources in a region or sub-region – ignoring the ability to import or export from region or sub-region via the transmission system – is more than the forecasted load plus reserve margin, MISO calls the difference a “surplus.” If the amount is less than the forecasted load plus reserve margin, MISO calls the difference a “deficit.” I will use that terminology here.

Q. What does MISO’s reserve margin represent?

A. To understand surpluses and deficits correctly, it is important to be aware that the *measurements include both the forecasted peak load and the reserve margin, and that the reserve margin is derived statistically.* MISO sets a reserve margin by *statistical modeling* such that – considering fluctuation of peak loads and random outages of generators – the modeled load will be more than the modeled running generation (called a “loss of load” hour) in no more than 24 hours in 10 years – 24 loss of load hours in 87,600 hours. The casual reference to the standard is “one day in ten years,” although the statistical modeling is by hour, not by day. MISO refers to this standard as a “resource adequacy” standard. Although MISO reserves the word “reliability” for the assessment of the transmission system, not the supply/demand system, in casual use many people apply the terms “reliability” or “reliability standard” to the assessment of the supply/demand system.

Q. How are surpluses and deficits related to reliability?

1 A *deficit* that is less than the reserve margin means that there are still enough
2 capacity resources to meet the forecasted load, but not enough to meet the full
3 reserve margin; and in this situation the so-called “reliability” of the
4 supply/demand system is less than the standard – meaning more than 24
5 statistically modeled hours in 10 years. Conversely, a *surplus* means that
6 supply/demand reliability is greater than the standard, meaning fewer than 24
7 statistically modeled hours in 10 years. The greater the deficit, the lower the
8 reliability, and the greater the surplus, the higher the reliability, determined
9 statistically.

10
11 **Q. Does “surplus” or “deficit” include the capabilities of the transmission grid?**

12 A. No. The *assessment of a surplus or deficit ignores the transmission capability*
13 *into or out of the region or sub-region.* For example, the results of the MISO
14 Planning Resource Auction in March 2016 for the Planning Year of 2016-17²
15 show that Zone 7 imported 872 MW, while the transmission Capacity Import
16 Limit was 3,521 MW – far above the import amount. Thus, while Zone 7 had a
17 technical “deficit” of 872 MW, there in fact was adequate capacity available to
18 Zone 7 from outside the zone – up to 3,521 MW total. Actual usable capacity
19 considers both the resources within Zone 7 and the amount that can be imported

² “2016/2017 Planning Resource Auction Results, Resource Adequacy Subcommittee, May 4, 2016,” page 8.
https://www.misoenergy.org/Library/Repository/Meeting%20Material/Stakeholder/RASC/2016/20160504/20160504%20RASC%20Item%2003a%202016-17_PRA_Summary.pdf

1 via the transmission system. To the contrary, the “surplus” or “deficit” for Zone 7
2 assumes there is zero transmission import capability into Zone 7.

3
4 **Q. Has MISO published new or updated information regarding surpluses and**
5 **deficits within MISO?**

6 A. Yes. MISO, in cooperation with the OMS (Organization of MISO States, an
7 association of state regulatory agencies), has recently updated its 2015 report.
8 The new report is “2016 OMS MISO Survey Results, July 2016 Resource
9 Adequacy Committee” (“MISO 2016 Survey”).³

10
11 **Q. What does the MISO 2016 Survey show for Zone 7, compared to the previous**
12 **report in 2015?**

13 A. Page 57 of the MISO 2016 Survey shows that the “outlook” for Zone 7 for 2017
14 is now a deficit of only -0.3 GW, compared to the previous 2015 report’s deficit
15 of -1.3 GW, *an improvement of 1.0 GW* between the 2015 report and the 2016
16 report. Page 57 is shown in my Exhibit EM-2 (AJZ-2), page 3 of 4.

17
18 **Q. Is there additional generation under development in Zone 7 that MISO does**
19 **not include in its totals?**

³ “2016 OMS MISO Survey Results, July 2016 Resource Adequacy Subcommittee.”
<https://www.misoenergy.org/Library/Repository/Meeting%20Material/Stakeholder/RASC/2016/20160629/20160629%20RASC%20Item%2003%20OMS-MISO%20Survey%20Full%20Deck.pdf>

1 A. Yes. Page 58 of the MISO 2016 Survey shows about 3.0 GW of new generation
2 in various stages of development in Zone 7. *MISO has excluded all but about 0.2*
3 *GW in calculating the 2017 deficit.* Thus, only about 10% of this new generation
4 has to eventually go into service to eliminate the deficit in Zone 7. Page 58 is
5 shown in my Exhibit EM-2 (AJZ-2), page 4 of 4.

6

7 **Q. Is there additional generation under development in the entire MISO region**
8 **that MISO does not include in its totals?**

9 A. Yes. Page 14 of the 2016 MISO Survey shows that for 2017 about 8 GW of
10 potential generation additions are in various stages of development in MISO.
11 Only about 2 GW were included in MISO's totals for 2017. This page is shown
12 in my Exhibit EM-2 (AJZ-2), page 2 of 4.

13

14 Also on page 2 of 4, for 2021, the generation under development in MISO grows
15 to about 35 GW, and only about 3 GW of this was included in MISO's totals for
16 2021.

17

18 Only a small fraction of the generation under development would have to go into
19 service to eliminate the deficits that MISO shows in its report. And again,
20 "surplus" and "deficit" ignore transmission capability among the MISO zones –
21 they are tallies for a zone as if there were no transmission capability in or out.

22

23 **Q. Does MISO exclude other generation within its region?**

1 A. Yes. MISO includes only what it calls “committed” resources. This excludes
2 resources that, for example, are planning to sell their capacity outside of MISO,
3 such as to PJM. There may be other types of “uncommitted” resources and there
4 may be resources that are undecided or that can undo an external commitment in a
5 future year – MISO does not give the details, but rather keeps confidential the
6 specific responses to its survey.

7

8 **Q. What are your conclusions from the additional information you have**
9 **explained regarding the OMS MISO surveys?**

10 A. First, MISO excludes from the surplus/deficit calculations a substantial amount of
11 new capacity that it knows about and that is currently in various stages of
12 development. Consequently, MISO’s reported deficits would be eliminated even
13 if only a small fraction of what is under development goes into service.

14

15 Second, looking at the Zone 7 deficits from the 2014, 2015, and 2016 survey
16 reports, plus the actual results of the 2016 Planning Resource Auction – all of
17 which has been discussed above and displayed in my exhibits – *the Zone 7*
18 *surplus/deficit situation has improved steadily and significantly according to*
19 *MISO*, even excluding new resources under development. The change has been
20 from a deficit of -3.0 GW in the 2014 survey to -0.3 GW in the 2016 survey, an
21 improvement of 2.7 GW. The results of the three surveys and the auction are
22 summarized on Exhibit AJZ-3 (EM-3).

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3. Plug-In Electric Vehicle Program

Should Follow Cost of Service Principles

Q. How does Consumers Energy rationalize its Plug-In Electric Vehicle (“PEV”) program?

A. The testimony of CE witness Mr. Morales gives several reasons, in his direct testimony. Among them are:

- “help Michigan residents be more comfortable with their decision to purchase a PEV” Page 12.
- “Michigan should stand behind the growth of this market, and the Company can help support this new strategic direction” Page 13
- “Michigan’s Governor has advocated for Michigan to lead the country in vehicle technology” Page 14.
- “maintaining Michigan’s leadership in the PEV marketplace” Page 14.
- “help incentivize residents to purchase a PEV” Page 14.
- “adoption of PEVs can help boost our automotive state and the economy of Michigan as a whole” Page 15.
- “increase customer demand” Page 15.
- “show Michigan residents that purchasing a PEV is a good investment” Pages 18-19.
- “supporting Michigan’s goal to become a leader in renewable transportation” Page 20.
- “support the state’s auto industry” Page 20.
- “promote a green environment” Page 20.
- “help Michigan self-sufficiently manage its energy needs” Page 20.

1 **Q. In your view, which of these reasons are part of Consumers Energy’s**
2 **regulated business?**

3 A. Many of the reasons are related to CE’s assertions of state and political policies.
4 Consumers Energy is a regulated monopoly electric utility, in the business of
5 providing safe and reliable electric energy to its customers. It is not a state
6 agency; it has no obligation to carry out policies of state or local governments,
7 regardless whether it agrees with those policies or not. It is not a marketing arm
8 of an auto manufacturer. The reasons connected with the utility business are
9 “increase customer demand” and “promote a green environment.” The “Michigan
10 self-sufficiently” reason is a policy concept, rather than a fundamental service of
11 the regulated utility.

12
13 As a long-standing electric utility, CE has great expertise in analyzing and testing
14 the characteristics of new electrical equipment and the effects of such equipment
15 on CE’s grid, including appropriate pilot programs. However, PEV charging
16 stations have existed in Michigan since the late 1970s. The PEV program
17 proposed in this proceeding is essentially a marketing program to increase electric
18 demand, as recognized by CE.

19
20 **Q. How will the program be paid for?**

21 A. Public charging stations, which cost either \$12,000 or \$100,000, would be
22 installed with no installation charge to the host customer at locations such as
23 “restaurants, malls, movie theaters, hospitals, hotels, airports, and large

1 workplaces.” J.Morales direct testimony, page 13, lines 1-4. Only the energy for
2 charging at these locations “would be paid for by the station host business
3 owner.” J.Morales direct testimony, page 19, lines 1-2.

4
5 PEV owners who install at-home charging stations “will receive \$1,000 incentive
6 toward the installation of a home charging station.” J.Morales direct testimony,
7 page 19, lines 22-23.

8
9 CE might not intend to collect an installation charge from the host customer, but
10 obviously the charging stations are not free. The total cost of the charging
11 stations is \$15 million. J.Morales direct testimony, page 19, line 17. CE’s
12 proposal for cost recovery is, “The station costs will be recovered through base
13 rates as part of the Company’s revenue requirement calculation.” J.Morales direct
14 testimony, page 19, lines 20-21. Thus all customers, including all business
15 customers, will be paying a share of the cost of the charging stations that are
16 installed free for selected business customers. This scheme does not follow cost-
17 of-service principles, whereby allocation of costs is in reasonable proportion to
18 benefits received.

19
20 **Q. Do you object to the proposed PEV program?**

21 A. I am not taking a position on whether or not the proposed PEV program should be
22 approved. It is a policy decision for the Commission on whether or not to approve
23 the program, or how much should be approved. The intent of laying out the

1 above specific rationale and details of the proposed program is to show that it is
2 primarily a promotional program for the increased use of electricity. Therefore,
3 the issue of how the program is to be paid for by customers becomes relevant, and
4 it is that on which my recommendation focuses. Cost of service principles should
5 be followed.

6
7 **Q. What is your recommendation to the Commission?**

8 A. Since the program is primarily promotional, intended to increase customer
9 demand, my recommendation is that the costs of the free charging stations be
10 allocated to power supply. ROA customers see no benefit in increased demands
11 for CE, because they do not take power supply service. Some of the equipment
12 for the free charging stations might nominally be categorized as distribution
13 equipment, but nevertheless it functions as part of the power supply business –
14 increasing electricity sales – and so should be excluded from the distribution rates
15 that ROA customers pay.

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4. Economic Development Expenses

Unfair cost effects on Electric Choice customers.

Q. CE has requested additional funds for its economic development group. How does CE explain the cost-based benefits to customers?

A. In his direct testimony, CE witness Mr. Jeffrey C. Mayes lists five categories of asserted benefits with various reasons, including:

- customers “expect utilities to be leaders and participants in economic development” Page 3.
- “Political Expectations – Federal, state, and local leaders expect utility leadership on key projects” Page 4
- “failing to adequately support . . . can have a negative impact on a utility’s reputation” Page 4.

Q. Are there any reasons listed that are part of CE’s regulated monopoly utility business?

A. There is one category:

Load Growth – Growing electric load spreads a utility’s fixed costs across a larger customer base. This creates a downward pressure on rates which is beneficial for all customers. Over the past few years, our load has been relatively flat, which creates an upward pressure on electric rates making Michigan less attractive to businesses.

J.Mayes, direct testimony, page 4, lines 1-5.

Q. Do load growth and increased sales reduce rates?

1 A. There are two sides to the coin, so to speak. The conventional perspective is that,
2 as Mr. Mayes states, the present fixed costs are spread over more units delivered,
3 and therefore the average fixed cost embedded in the delivered units decreases.

4
5 However, if more resources – whether power supply, distribution, fuel, purchased
6 power, O&M, and transmission – are needed to serve the additional load and the
7 incremental cost of some of these are greater than the current average costs, then
8 it is possible for rates to go up, not down.

9

10 **Q. Are all customers affected equally?**

11 A. No, they are not. The effect of increased money for economic development on
12 both Full Service and ROA customers should be considered. Sales growth will
13 primarily affect costs in the power supply portion of CE's business. ROA
14 customers do not take power supply service. If the Commission decides to allow
15 CE to charge customers additional money for economic development, then the
16 additional amount first should be allocated to power supply and distribution
17 separately, on the basis of relative total investment.

18

19 **Q. By how much is CE proposing to increase its economic development**
20 **activities?**

21 A. CE is requesting an increase of \$3 million. J.Mayes direct testimony, page 4, line
22 17.

23

1 **Q. What is CE’s justification for significant additional money for economic**
2 **development activities?**

3 A. CE apparently believes that existing governmental agencies are not up to the task
4 of economic development:

5 Changes in state leadership and government budget challenges often create
6 confusion with siting professionals and the private sector regarding a state’s
7 commitment to business attraction and retention. This confusion and
8 appearance of volatility are a competitive disadvantage which can cost a state
9 jobs, investment, and electric load.

10
11 J.Mayes direct testimony, page 6, lines 8-11.

12
13
14 **Q. Do you agree with CE about the economic development role it proposes to**
15 **play?**

16 A. In the context of CE as a regulated utility, I do not agree. As a regulated utility,
17 CE is in the business of providing and delivering safe and reliable electric energy
18 to its customers. Regulation assures that the owners of CE – the stockholders –
19 are compensated for reasonable and prudent expenses and for a return on used and
20 useful investment.

21
22 CE as a regulated electric utility is not a state agency; it has no taxing authority;
23 it has no oversight by voters. It has no duty to provide staff services for any
24 governmental agency or other organization that it believes needs more resources.
25 It has no authority to decide what the State of Michigan’s policy should be; it has
26 no obligation to implement what it believes to be a productive economic policy
27 for any governmental unit, let alone charge its electric customers for that activity.

1 Allowing CE to charge its customers for economic development activities in
2 support of state agencies and political policies amounts to creation of an economic
3 development tax that only CE customers are being asked to pay.

4

5 **Q. What is your recommendation to the Commission?**

6 A. Under regulation in Michigan, the management of a regulated utility is free to
7 make its own business decisions. However, whether or not the utility can recover
8 those costs from electric customers for those decisions is up to the Commission.

9

10 I recommend that if CE believes that the proposed additional money for increased
11 economic development activities is a wise investment, then it should be funded by
12 stockholders, not by electric customers, and certainly not by ROA customers, who
13 would see little benefit from the “spreading of fixed costs” of CE’s generation
14 investment.

15

16 If the Commission decides to allow CE to recover the additional money for
17 economic development from its electric customers, then I recommend (a) that the
18 requested amount should first be split between power supply and distribution on
19 the basis of relative dollar investment, and (b) that after the split, the power
20 supply amount should be allocated to power supply customers by power supply
21 sales in each rate class and collected in power supply rates, and the distribution
22 amount should be allocated to distribution customers by distribution sales in each
23 rate class and collected in distribution rates.

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The asserted purpose of increased economic development activities is to increase sales, and therefore allocation of the power supply and distribution portions by sales is the cost-based method to apportion the costs. An allocation by number of customers would result in the residential class paying about 90% of economic development costs but not receiving commensurate decreases in rates.

The objective of rates based on cost of service is that the rates are commensurate with the services and benefits received. The Commission makes the decision on how this is done, so as to not advantage or disadvantage a particular group of customers.

5. Revenue Adjustment Mechanism

Premature, deficient, and unfair to ROA customers.

Q. CE is proposing a Revenue Adjustment Mechanism (“RAM”). What is your assessment of this proposal?

A. The RAM proposal is certainly premature, as it is conditioned on “the enactment of legislation addressing revenue adjustment mechanisms for electric utilities during the pendency of this case.” L.Collins, direct testimony, page 24, lines 18-19.

1 CE is speculating that there could be new legislation. Yet, the rules or guidelines
2 of any such new legislation are unknown – how would the Commission know
3 now that CE’s proposal would be in accord with any new legislation? Would CE
4 amend its proposal in this case? How can other parties critique a speculative
5 proposal, or offer changes? To have or have not a RAM is a policy decision for
6 the Legislature and the Commission, and a speculative, currently unauthorized
7 proposal is a drain on the Commission’s resources in people, time, analysis, and
8 decision-making capacity.

9
10 **Q. Are there deficiencies in CE’s proposed RAM?**

11 A. Yes. An important deficiency is the categorization of “nonfuel rate revenues” as
12 the desired metric for RDM surcharges. L.Collins direct testimony, page 25, line
13 3. The true metric should be “*revenue that varies by sales level less variable*
14 *costs.*” CE does propose to separate power supply from distribution in the
15 determination of RAM charges, and this is a correct and essential separation.

16
17 First, when sales decrease, variable energy costs decrease *at the margin*, which is
18 generally higher than the PSCR base which is based on average costs. Variable
19 costs can decrease from a reduction of fuel costs, purchased power, capacity, and
20 transmission, or equivalently from an increase in opportunistic spot wholesale
21 sales. The PSCR base alone does not represent the reduction of variable costs.
22 For example, if the PSCR base is 3 cents/kWh and the marginal fuel in a
23 particular hour is 5 cents, then a 1 kWh reduction in that hour reduces actual costs

1 by 5 cents, not 3 cents. Likewise, if the marginal fuel is 2 cents, then the actual
2 cost reduction is 2 cents, not 3 cents. Since the PSCR base is set by an average
3 and generation plants are dispatched in economic order, the marginal cost of fuel
4 – and therefore the savings from a reduction of energy use – will be higher than
5 the average cost of fuel over the same time period. The PSCR *reconciliation* case
6 is based on actual costs and so reflects variable costs at the margin.

7
8 Full Service customers get the benefit of this reduction of actual marginal costs
9 via the PSCR reconciliation. ROA customers receive no such benefit because
10 they do not take power supply from CE and are not included in the PSCR
11 proceedings, yet – under the CE proposal – ROA customers apparently are
12 supposed to pay for loss of power supply revenue. Consequently, ROA customers
13 would pay a greater share of power supply revenue reductions under the proposed
14 RAM than would Full Service customers, because ROA customers would get a
15 credit only for the PSCR base, while Full Service customers would get a credit
16 both for the PSCR base and the reduction of power supply costs at the margin.

17
18 Second, some power supply O&M expenses may vary depending on the amount
19 of generation. Consequently, variable O&M costs should be subtracted.

20
21 **Q. What is your recommendation to the Commission?**

1 A. My recommendation is that the Commission *defer the proposed RAM to a future*
2 *proceeding*. The CE proposal cannot be implemented under current law. It is
3 also not adequately articulated and supported in this proceeding.

4
5 If a RAM becomes lawful and the Commission decides to approve the proposed
6 RAM, then it should also order CE to fix the following deficiencies: (a) subtract
7 the marginal cost of fuel, purchased power, and transmission instead of the
8 average reflected in the PSCR base, plus subtract increased profits from any
9 additional wholesale sales, and (b) subtract any and all other variable O&M
10 costs. The Commission may find other deficiencies I do not address here.

11

12 **Q. Does this conclude your Direct Testimony?**

13 A. Yes, it does.

Exhibits of
Alexander J. Zakem

ALEXANDER J. ZAKEM

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CONSULTANT – MERCHANT ENERGY AND UTILITY REGULATION

Provides strategies and technical expertise on competitive market issues, transmission issues, state and federal regulatory issues involving the electricity business, and associated legal filings. Scope includes the Midwest ISO Energy Market and Resource Adequacy, FERC proceedings on transmission and market tariffs, state rules for competitive supply, and negotiation of settlements.

PRIOR POSITIONS: Quest Energy, LLC – a subsidiary of Integrys Energy Services

Vice President, Operations

March 2002 to December 2003

Responsible for the planning, acquisition, scheduling, and delivery of annual power supply and transmission, to serve competitive retail electric customers.

- **Power Planning** -- Designed and negotiated customized long-term power contracts, to reduce power costs and exposure to spot energy prices.
- **Transmission** -- Revamped transmission strategy to reduce transmission costs.
- **Load Forecasting** -- Instituted formal short-term forecasting process, including weather normalization.
- **Risk Management** -- Developed summer supply strategy including call options to minimize physical supply risk at least cost. Instituted probabilistic assessment of forecast uncertainty to minimize transmission imbalance costs.
- **Contract Management** – Negotiated and recovered liquidated damages for power supply contracts. Included cost of transmission losses into customer contracts.
- **Operations Capability** -- Expanded the Operations staff. Oversaw daily activity in spot market purchases. Instituted back-up capability, including equipment and processes, enabling the company to schedule and deliver virtually all power during the August 2003 blackout in the Midwest.

PRIOR POSITIONS : DTE Energy / Detroit Edison — 1977 to 2001

Director, Power Sourcing and Reliability

May 1998 to April 2001

Director of group responsible for monthly, annual, and long-term purchases and sales of power for Detroit Edison, including procuring power for the summer peak season.

- **Planning** -- Planned summer power requirements for Detroit Edison, including mix of generation, option contracts, hub purchases, load management, and transmission, which balanced and optimized physical risk and financial risk.
- **Contract Management** – Established decision, review, and approval process for evaluation and execution of power transactions, including mark-to-market valuation.
- **Execution** -- Executed summer plans, contracting annually for purchased power and transmission services. Directed negotiations for customized structured contracts to provide the company with increased operating flexibility, dispatch price choices, and delivery reliability.
- **Risk Management** – Developed an optimizing algorithm using load shapes to minimize corporate exposure to volatile power prices. Developed a hedging strategy to fit power purchases to the corporation's risk tolerance level.
- **Acquisitions** -- Team leader for acquisition of new peakers.
- **Settlements** -- Negotiated and settled liquidated damages claims.

Relevant prior positions within Detroit Edison

<u>Position</u>	<u>Organization</u>	<u>Time Period</u>
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Director, Special Projects	Customer Energy Solutions	Apr 97 to May 98
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Leader of several special projects involving the transformation of the corporation's merchant energy functions into competitive business units, including merger explorations and the start up of DTE Energy Trading (DTE's power marketing affiliate).

Directed filings to the Federal Energy Regulatory Commission to establish DTE Energy Trading as a power marketer and to gain authority for sales, brokering, and code of conduct. The FERC used DTE's flexible utility/affiliate code of conduct as precedent for rulings for other power marketers.

Director, Risk Management	Huron Energy (temp affiliate)	Jan 97 to Apr 97
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Leader of team responsible for competitive pricing of wholesale structured contracts and for acquiring risk management hardware and software to support risk management policy. Prepared Board resolutions to implement risk management policy.

Director, Contract Development Customer Energy Solutions Jan 96 to Dec 96

Leader of team that formulated a business strategy for the corporation in competitive power marketing. Team leader on project evaluating an existing steam and electricity contract, recommending and gaining Board approval for revamping the corporation's Thermal Energy business and strategy.

Project Director Executive Council Staff Jan 91 to Dec 95
& Corporate Strategy Group

Project leader for competitive studies, including business risk, generation pooling, and project financing in the merchant generation industry. Team member and/or team leader for analyses of merger and acquisition opportunities

Special Assignment Executive Council Staff Mar 90 to Dec 90

Special assignment related to long-term industry strategies and mergers and acquisitions.

Pricing Analyst Marketing / Rate Aug 82 to Mar 90

Developed, negotiated, and implemented an innovative standby service tariff. Testified as an expert witness in regulatory proceedings and in state legislative hearings.

Engineer Resource Planning Aug 79 to Dec 81

Member of the company's electric load forecasting team, responsible for SE Michigan energy and peak demand forecasting, and for risk analysis. Developed the company's first residential end-use forecast model.

PRIOR POSITIONS: Prior to DTE Energy

Lear Siegler Corporation, ACTS Computing division, systems analyst and programmer from January 1973 to July 1977.

EDUCATION: M. A. in mathematics, University of Michigan, 1972
B. S. in mathematics, University of Michigan, 1968

MILITARY: U. S. Army, September 1968 to June 1970.
Viet Nam service from June 1969 to June 1970.
Honorably discharged.

PROFESSIONAL: Member, Engineering Society of Detroit (1979-present)

PUBLICATIONS & PAPERS:

- "Competition and Survival in the Electric Generation Market," published in *Public Utilities Fortnightly*, December 1, 1991.
- "Measuring and Pricing Standby Service," presented at the Electric Power Research Institute's "Innovations in Pricing and Planning" conference, May 3, 1990.
- "Assessing the Benefits of Interruptible Electric Service," presented at the 1989 Michigan Energy Conference, October 3, 1989.
- "Principles of Standby Service," published in *Public Utilities Fortnightly*, November 24, 1988.
- "Progress in Conservation," a satirical commentary published in *Public Utilities Fortnightly*, October 27, 1988.
- "Comparing Utility Rates," published in *Public Utilities Fortnightly*, November 13, 1986.
- "Uncertainty in Load Forecasting," with co-author John Sangregorio, published in *Approaches to Load Forecasting*, Electric Power Research Institute, July 1982.

PREVIOUS TESTIMONY:

- Michigan Public Service Commission, U-18014
- Michigan Public Service Commission, U-17767
- Michigan Public Service Commission, U-17735
- Michigan Public Service Commission, U-17689
- Michigan Public Service Commission, U-17688
- Michigan Public Service Commission, U-17429
- Michigan Public Service Commission, U-17087
- Michigan Public Service Commission, U-17032
- Michigan Public Service Commission, U-16794
- Michigan Public Service Commission, U-16566
- Michigan Public Service Commission, U-16472
- Michigan Public Service Commission, U-16191
- Michigan Public Service Commission, U-15768.
- Michigan Public Service Commission, U-15744.
- Federal Energy Regulatory Commission, Docket No. EL04-135 & related dockets.
- Michigan Public Service Commission, U-12489.
- Michigan Public Service Commission, U-8871.
- Michigan Public Service Commission, U-8110 part 2.
- Michigan Public Service Commission, U-8110, part 1.
- Michigan Public Service Commission, U-7930 rehearing.
- Michigan Public Service Commission, U-7930.



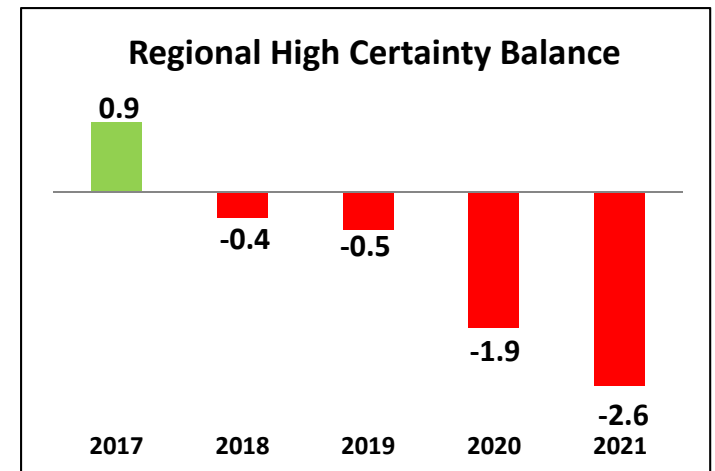
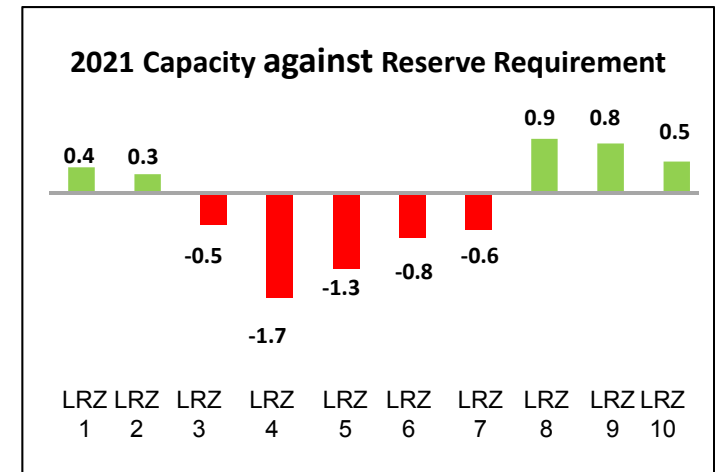
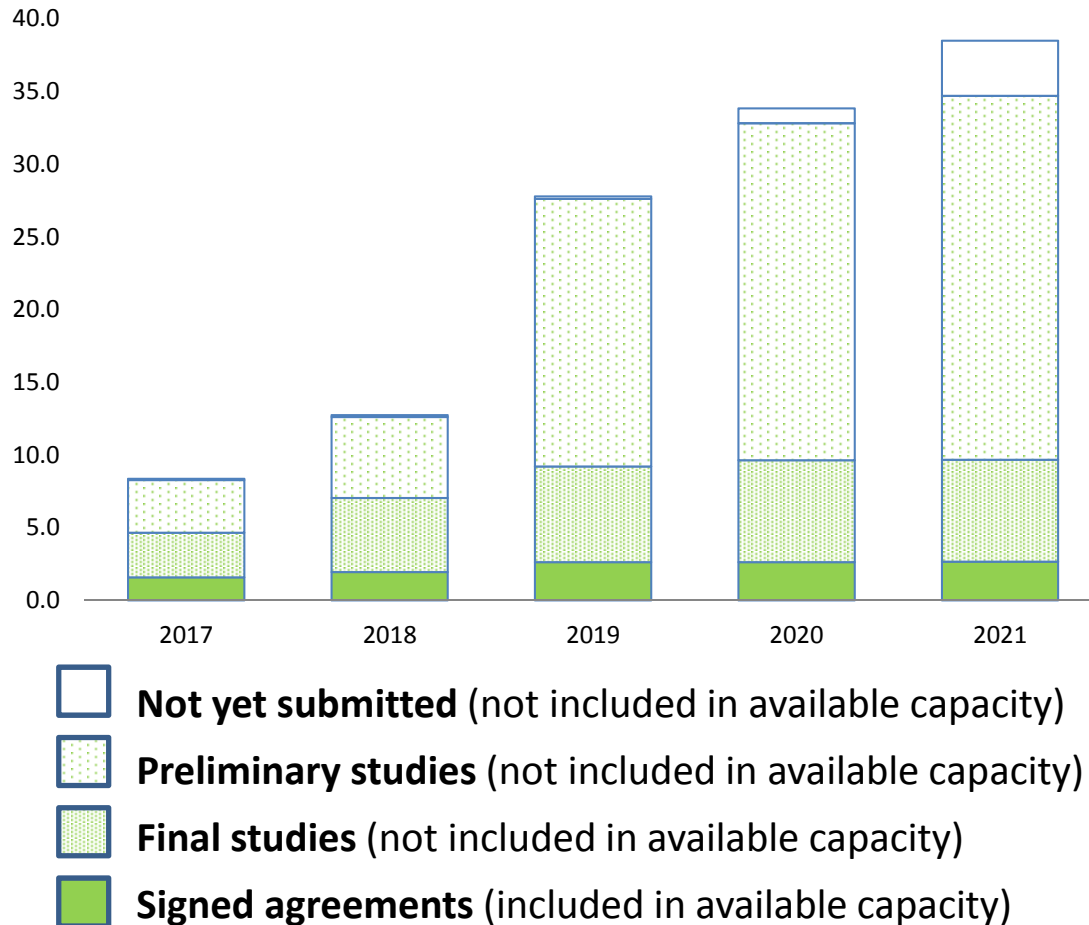
2016 OMS MISO Survey Results

Furthering our joint commitment to regional resource assessment and transparency in the MISO region, OMS and MISO are pleased to announce the results of the 2016 OMS MISO Survey

July 2016 Resource Adequacy Subcommittee

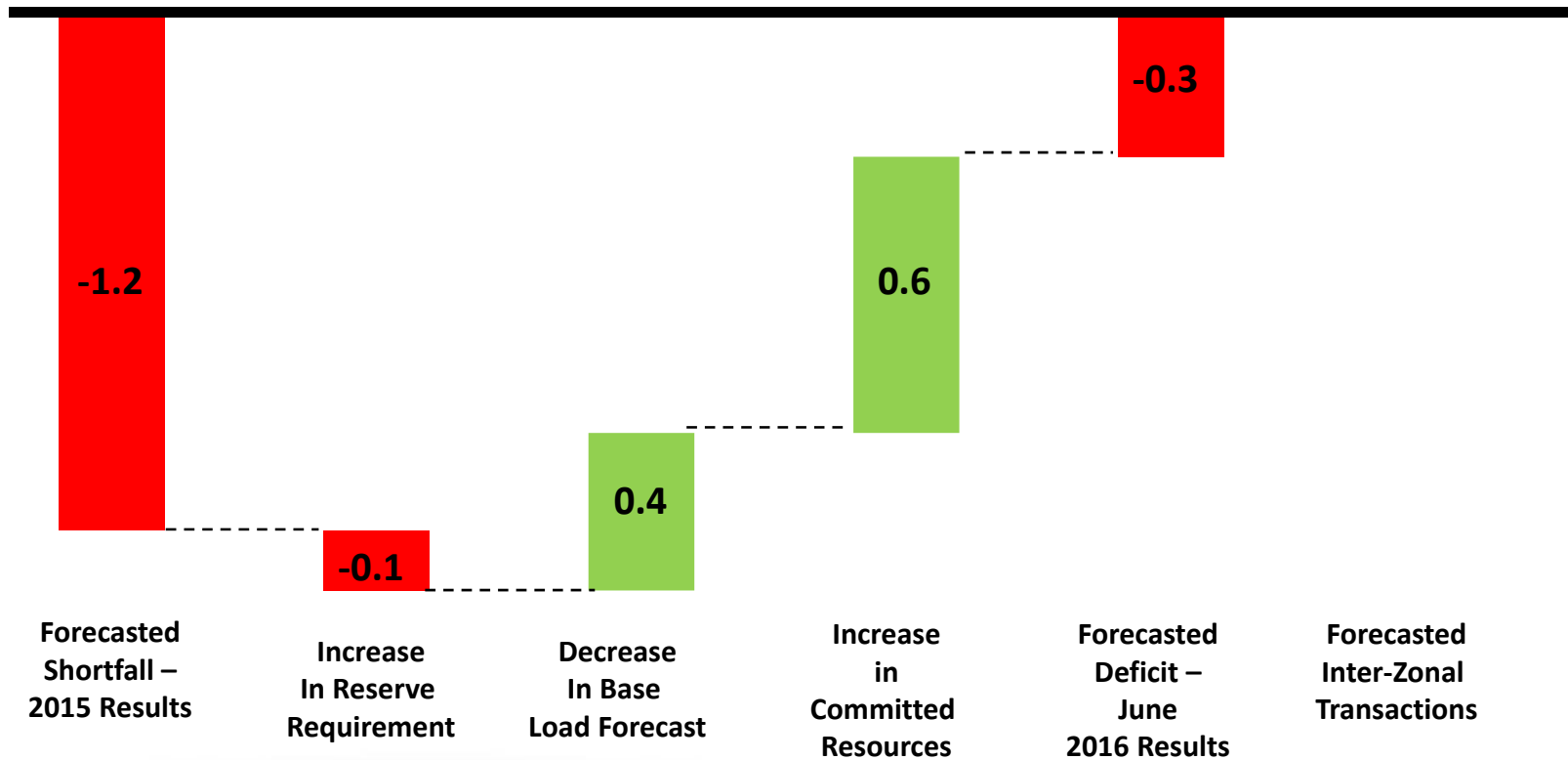
Continued commitment to firming up planned generation interconnections through the MISO process will be required

Potential Generation Additions, in GW*

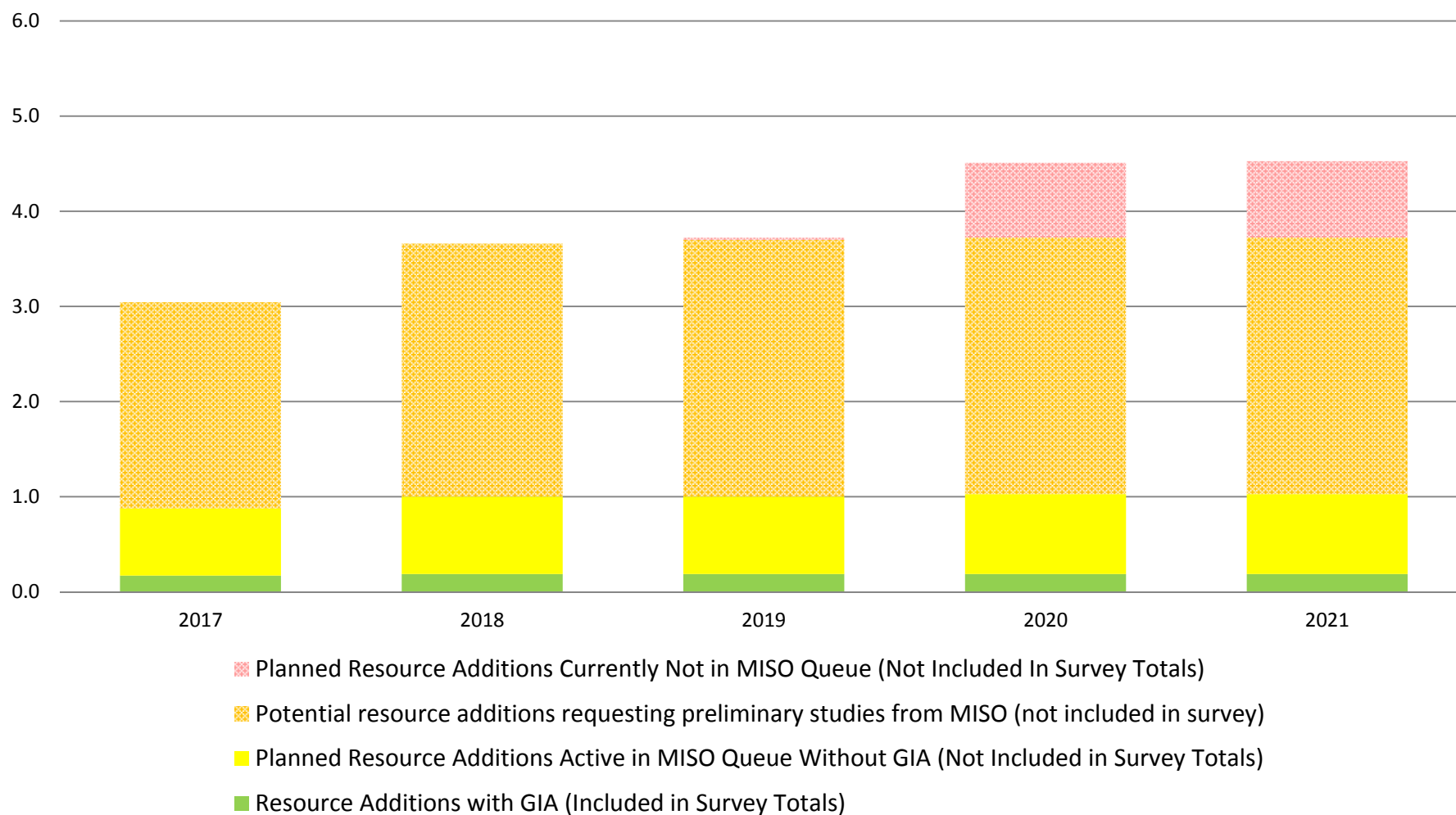


2015 vs 2016 OMS MISO Survey Results Zone 7

2017 Outlook
Comparison of committed resources
In GW



New Generation Reported in Survey Zone 7 (GW)



* Wind at capacity credit of 15.7%; solar at capacity credit of 50%

**Improvement in MISO Assessments
 of
 Zone 7 Capacity Deficit**

<u>Line No.</u>	(a) <u>GW Deficit</u>	(b) <u>Year of Deficit</u>	(c) <u>Type</u>	(d) <u>MISO Source</u>
1	- 3.0	2016	Forecast	2014 OMS-MISO Survey, Source A, page 46.
2				
3				
4	- 1.3	2016	Forecast	2015 OMS-MISO Survey, Source A, page 46.
5				
6				
7	- 0.9	2016	Actual	2016-17 MISO Auction, Source B, page 8.
8				
9				
10	- 0.3	2017	Forecast	2016 OMS-MISO Survey, Source C, page 57.
11	—			

2.7 GW improvement between 2014 and 2016

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Sources:

- A. “2015 OMS MISO Survey Results, July 2015.”
<https://www.misoenergy.org/Library/Repository/Meeting%20Material/Stakeholder/SAWG/2015/20150709/20150709%20SAWG%20Item%2002%202015%20OMS-MISO%20Survey%20Results.pdf>

- B. “2016/2017 Planning Resource Auction Results, Resource Adequacy Subcommittee, May 4, 2016.” The auction took place on March 28-31, 2016.
https://www.misoenergy.org/Library/Repository/Meeting%20Material/Stakeholder/RASC/2016/20160504/20160504%20RASC%20Item%2003a%202016-17_PRA_Summary.pdf

- C. “2016 OMS MISO Survey Results, July 2016 Resource Adequacy Subcommittee.”
<https://www.misoenergy.org/Library/Repository/Meeting%20Material/Stakeholder/RASC/2016/20160629/20160629%20RASC%20Item%2003%20OMS-MISO%20Survey%20Full%20Deck.pdf>

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

In the matter of the application of)
CONSUMERS ENERGY COMPANY)
for authority to increase its rates for)
the generation and distribution of)
electricity and for other relief.)
_____)

Case No. U-17990

PROOF OF SERVICE

STATE OF MICHIGAN)
) ss.
COUNTY OF INGHAM)

Kimberly Champagne, the undersigned, being first duly sworn, deposes and says that she is a Legal Secretary at Varnum LLP and that on the 28th day of July 2016, she served the Corrected Direct Testimony and Exhibits of Alexander J. Zakem on behalf of Energy Michigan, Inc. and this Proof of Service on the Persons identified on the attached service list via electronic mail.

Kimberly Champagne

SERVICE LIST
MPSC Case No. U-17990

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