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July 5, 2016

Ms. Mary Jo Kunkle
Michigan Public Service Commission
7109 W. Saginaw Highway
P.O. Box 30221
Lansing, Michigan 48909

Re: MPSC Case No. U-18014

Dear Ms. Kunkle:

Attached for electronic filing in the above-referenced matter, please find the Testimony and Exhibits of Alexander J. Zakem, as well as Proof of Service on behalf Energy Michigan, Inc.

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)
DTE ELECTRIC COMPANY)
for authority to increase its rates, amend)
its rate schedules and rules governing the)
distribution and supply of electric energy, and)
for miscellaneous accounting authority.)
_____)

Case No. U-18014

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 included
14 the overall direction and management of Quest’s power supply to its retail customers.
15 This included power supply planning, development of customized products, negotiation
16 with suppliers, planning and acquiring transmission rights, and scheduling and delivery
17 of power. It also included managing risk with respect to market price movements and
18 variation of customer loads.

19
20 Prior to joining Quest, I was employed Detroit Edison in 2001, where from 1998
21 to 2001, I was the Director of Power Sourcing and Reliability, responsible for purchases
22 and sales of power for mid-term and long-term periods, planning for generation capacity

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

3
4 Additional experience, qualifications, and publications are provided in
5 Exhibit 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 rates,
10 retail rates and regulations, recovery and allocation of costs and revenues, and the effects
11 of rate restructuring. I have also testified before the Federal Energy Regulatory
12 Commission. Case citations are provided in Exhibit EM-1 (AJZ-1).

13
14 **Q. Are you sponsoring any exhibits?**

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

16	Exhibit EM-1 (AJZ-1)	Qualifications
17	Exhibit EM-2 (AJZ-2)	2016 OMS MISO Survey Results
18	Exhibit EM-3 (AJZ-3)	Improvement in MISO Assessments
19		of Zone 7 Capacity Deficit
20		

21

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

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

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

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

15 A. I will address the following:

16 1. *Revenue Decoupling Mechanism (“RDM”)*

17 DTE Electric is proposing an RDM to compensate for lost sales under the
18 Energy Optimization (EO) program. This proposal is premature, is in part at
19 odds with aspects of DTE’s other proposals, and has several deficiencies.

20
21 2. *“Shortfall” of Capacity in MISO Zone 7* – DTE has addressed various MISO
22 capacity data in Zone 7, the Lower Peninsula of Michigan. Additional and

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

3
4 3. *Economic Development Expenses* – DTE is proposing an economic
5 development program to help bring more businesses to Michigan. The role
6 of DTE as a potential agent of state government deserves scrutiny. The cost
7 allocation effects on Electric Choice customers may not be fair.

8
9 4. *Incentive Compensation Plan* – DTE is again proposing that portions of its
10 incentive compensation program should be paid for by customers. The
11 share borne by Electric Choice customers should be commensurate with the
12 benefits they receive.

13
14 5. *Changes in Electric Choice Tariff* – DTE is proposing additional wording to
15 clarify obligations of certain Electric Choice customer groups. Energy
16 Michigan does not object to the expressed intent of the proposed changes,
17 but more precision in the proposed wording will help.

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1. Revenue Decoupling Mechanism

DTE’s proposal for an RDM should be deferred.

Q. Do you favor or oppose adjustment mechanisms such as the RDM?

A. I view the existence or non-existence of adjustment mechanisms such as the RDM as a policy issue that should be decided by the Legislature and the Commission. I am neither favoring nor opposing the concept of an RDM. At the same time, an RDM should be reasonable, fair, and reflect the type of increases or decreases that customers would see if there were a timely general rate case.

Q. What is DTE proposing?

A. DTE witness Mr. Don M Stanczak explains in his direct testimony:

The Company is proposing a provisionary RDM. Although the Company recognizes that there is currently no statutory authority that authorizes the implementation of an RDM for electric utilities in Michigan, the Company is proposing a provisional RDM in this proceeding in the event that legislation is enacted prior to an order in this proceeding that grants such statutory authority. Therefore, if there is no change in law prior to a final order, the Company would rescind its RDM proposal.

D.Stanczak, direct testimony, page 11, lines 7-13. Emphasis added.

The calculation of any revenue shortfall will be based solely on revenue lost due to the Company’s EO program. Lost sales will be determined by the residential and commercial/industrial customer groupings used in DTE Electric’s EO reconciliation proceedings. More specifically, DTE Electric proposes that any sales reductions produced by DTE Electric’s approved EO program, as determined in DTE Electric’s EO reconciliation proceedings, be recovered through the RDM. That is, any EO related sales reduction, by customer grouping, will be multiplied by average per kWh revenue for that particular grouping in order to determine the RDM surcharge revenue to be recovered from customers. Exhibit A-23, Schedule O1 provides a simple illustrative example showing how the RDM would be calculated.

1 D.Stanczak, direct testimony, page 11 line 17 to page 12 line 1. Emphasis added.
2
3

4 **Q. What is your assessment of DTE Electric’s proposed RDM based on EO?**

5 A. There are several deficiencies in the DTE proposal. First, based on DTE’s
6 testimony, the proposal is premature. DTE has stated that a court decision has ruled that
7 the Commission has no authority to order an RDM. DTE is speculating that there could
8 be new legislation. Yet, the rules or guidelines of any such new legislation are unknown
9 – how would the Commission know now that DTE’s proposal would be in accord with
10 any new legislation? Would DTE amend its proposal in this case? How can other parties
11 critique a speculative proposal, or offer changes? To have or have not an RDM is a
12 policy decision for the Legislature and the Commission, and a speculative, currently
13 unauthorized proposal is a drain on the Commission’s resources in people, time, analysis,
14 and decision-making capacity.
15

16 **Q. You have stated that the RDM proposal is in part at odds with DTE’s other**
17 **proposals. Would you explain?**

18 A. Yes. Inconsistency is a second deficiency of the RDM proposal.
19

20 First, DTE already *has* an existing incentive mechanism for EO, called the
21 “Performance Incentive Mechanism,” yet it has not addressed how that mechanism fits in
22 with the proposed RDM.
23

1 Second, in this proceeding DTE has claimed that an RDM reduces risk and affects
2 the required rate of return, yet has not proposed to reduce its requested rate of return if
3 the RDM is implemented.

4
5 Third, in this proceeding DTE has proposed additional money for economic
6 development to add load and consequently reduce costs for customers, yet has not
7 proposed a specific “decoupling mechanism” to return excess earnings to customers.

8
9 **Q. Would you explain these three inconsistencies?**

10 A. First, the intent of the current EO performance incentive mechanism was
11 explained by Company witness Ms. Vicki M Campbell in Case No. U-17049:

12 Detroit Edison has taken the information from these collaborative discussion
13 and developed a proposal to modify the performance incentive mechanism
14 that will motivate the Company to not only exceed the minimum legislated
15 energy savings standards but also encourage the Company to incorporate
16 certain specific program design elements.

17
18 U-17049, V.Campbell direct testimony, page 38, lines 11-15. Emphasis added.

19
20 In the current EO reconciliation for 2015, Case No. U-18023, DTE has calculated
21 its 2015 incentive payment at \$13 million. The EO incentive payments are *over and*
22 *above* the full cost-of-service revenues that the Commission has authorized in general
23 rate cases and separate from the proposed RDM. DTE’s exhibit shows that under present
24 rates and a 1% EO savings, DTE would collect an additional \$30.7 million. See Exhibit
25 A-23, Schedule O1, page 1. At proposed rates the RDM additional adjustments would be
26 about \$34 million.

1 The question before the Commission is how much financial motivation does the
2 Commission believe it is necessary to authorize for DTE in order for DTE to do a
3 satisfactory job with its EO program?
4

5 Second, reduction of sales volatility reduces financial risk. Financial risk is
6 considered in the rate of return that the Commission authorizes under regulation. DTE
7 witness Mr. Michael J. Vilbert states:

8 Regulatory policy plays a role in the business risk of the Company. In the
9 current environment of low electric demand growth, the fact that DTE does
10 not have a revenue decoupling mechanism or a fixed variable pricing policy
11 places it at increased risk of under-recovering its cost of service relative to
12 some companies in the sample group that benefit from such mechanisms.
13 Although the Company is applying in this proceeding for a Revenue
14 Decoupling Mechanism (RDM) that would track lost sales due to Energy
15 Optimization programs, such a mechanism would not insure against declining
16 load for other reasons, such as slow economic growth, declining industrial
17 activity, and increased weather variability—all of which are issues the
18 Company is likely to contend with in the near future.
19

20 M.Vilbert, direct testimony, page 34, lines 15-24. Emphasis added.
21
22

23 The proposed EO RDM would reduce some of the risk of sales volatility. If the
24 current rate of return authorized by the Commission does not consider the EO RDM, then
25 obviously the implementation of an EO RDM would reduce risk compared to what it
26 would be without an EO RDM. I cannot find in DTE's testimony a proposed adjustment
27 that would account for such reduction of risk in the form of a lower rate of return in the
28 event an RDM is approved.
29

1 Third, DTE is requesting additional \$3 million of O&M “to support economic
2 development activities.” Later in my testimony I will address my concerns with a
3 regulated utility undertaking the type of activities that DTE describes. For now, the
4 intent of the additional economic development activities is stated by DTE witness Ms.
5 Irene M. Dimitry:

6 Specifically for DTE Electric, the focus of economic development is to help
7 reduce costs for our customers by spreading fixed costs over a larger customer
8 base, and by reducing arrears and uncollectible expenses as Michigan’s
9 economy improves.

10
11 I.Dimitry, direct testimony, page 26, lines 3-6. Emphasis added.
12
13
14

15 Essentially, reducing costs by spreading fixed costs over a larger customer base is
16 accomplished by redesigning the rates to collect the same dollars over a *larger* sales
17 number. This is exactly the opposite of the proposed EO RDM, which is to collect the
18 same dollars over a *smaller* sales number. Thus, the Commission may want to consider
19 the combined effects of both together. If the net sum of the decrease in sales due to EO
20 plus the increase in sales due to economic development is greater than the sales level
21 used to set rates, the Commission will have to decide whether or not DTE should still
22 receive an RDM adjustment, particularly if an RDM adjustment were to increase DTE’s
23 earning above its authorized rate of return.
24

25 For sales reductions due to the EO program, DTE proposes a special, faster
26 mechanism, the RDM, to increase rates. For sales increases due to economic
27 development that would reduce rates, DTE does not propose any mechanism, thus the

1 default method for reducing rates is an ordinary general rate case. There should be some
2 parity in the speed at which rates are adjusted up and down.

3
4 **Q. What is the effect of the proposed EO RDM on Electric Choice customers?**

5 A. The effect of the EO RDM on Electric Choice customers is not known, given the
6 minimal information that DTE has offered in the description of its proposal. There are,
7 however, material questions. Electric Choice customers pay the EO surcharges,
8 including the amounts for the current performance incentive mechanism. Exhibit A-23,
9 Schedule O1, page 2 determines the “Average Non-Fuel Margin Price” using distribution
10 sales, not power supply sales; and page 1 uses this price to determine the “lost margin.”
11 The implication of this is that the EO RDM surcharge would be applied to the
12 distribution charge. Thus, the situation becomes that Electric Choice customers – who do
13 not take power supply service from DTE – would be charged for the loss of revenue
14 determined by a method that includes DTE power supply costs. Is there a reason for this?
15 It is unknown, because DTE offers no support for Exhibit A-23, Schedule O1. No
16 witness explains the rationale for the calculations – such as why only the PSCR Base
17 Revenue and surcharges are removed, why distribution sales are used, whether the
18 requested RDM is supposed to use the proposed revenues in the eventual Commission
19 order, etc.

20
21 **Q. Are there other deficiencies in the RDM proposal?**

22 A. Yes. The major deficiency is that there is no separation between loss of power
23 supply revenue and loss of distribution revenue. Because there is an Electric Choice

1 program where customers take only distribution service, in any RDM Electric Choice
2 customers should pay only for the loss of revenue due to lower distribution sales.

3
4 Another deficiency is the categorization of “non-fuel revenue” as the desired
5 metric for RDM surcharges. The true metric should be “*revenue that varies by sales level*
6 *less variable costs.*” DTE has not removed monthly customer service charge revenue
7 from the amount that is used to calculate the RDM surcharges. These service charges are
8 substantial, and DTE collects them regardless of sales level. Monthly service charges on
9 an annual basis total \$162 million for present revenue and \$246 million for proposed
10 revenue, for major rate categories D1, D3, and D11. See Exhibit A-14, Schedule F3,
11 pages 2, 15, and 24.

12
13 Failure to remove the service charges is an error, since not removing them would
14 result in overstating the RDM surcharges. A simple way to see this is to check the
15 boundary condition if the EO program were to reduce sales to zero. Then, DTE would
16 still be receiving the monthly service charges, so its revenue would not be zero. In that
17 situation, the RDM surcharges would be set to recover only the revenue that varies by
18 sales level – at zero sales – which would not include the revenue already received for the
19 service charges.

20
21 At a minimum, service charges should be removed from the calculation of the
22 RDM surcharges, along with any variable O&M costs. Some power supply O&M
23 expenses may vary depending on the amount of generation. For example, in Case No. U-

1 13808-R/U-14474, Detroit Edison proposed that the average overall generation O&M
2 expense of \$12.07/MWh be subtracted out of wholesale power sales revenues. See Case
3 No. U-13808-R/U-14474, Exhibit A-7 Revised, lines 28-32.
4

5 A third deficiency is that when sales decrease, variable energy costs decrease *at*
6 *the margin*, which is generally higher than the PSCR base which is based on average
7 costs. Variable costs can decrease from a reduction of fuel costs, purchased power,
8 capacity, and transmission, or equivalently from an increase in opportunistic spot
9 wholesale sales. The PSCR base alone does not represent the reduction of variable costs.
10 For example, if the PSCR base is 3 cents/kWh and the marginal fuel in a particular hour
11 is 5 cents, then a 1 kWh reduction in that hour reduces actual costs by 5 cents, not 3
12 cents. Likewise, if the marginal fuel is 2 cents, then the actual cost reduction is 2 cents,
13 not 3 cents. Since the PSCR base is set by an average and generation plants are
14 dispatched in economic order, the marginal cost of fuel – and therefore the savings from a
15 reduction of energy use – will be higher than the average cost of fuel over the same time
16 period. The PSCR *reconciliation* case is based on actual costs and so reflects variable
17 costs at the margin.
18

19 Full Service customers get the benefit of this reduction of actual marginal costs
20 via the PSCR reconciliation. Electric Choice customers receive no such benefit because
21 they do not take power supply from DTE and are not included in the PSCR proceedings,
22 yet – under the DTE proposal – Electric Choice customers apparently are supposed to pay
23 for loss of power supply revenue. Consequently, Electric Choice customers would pay a

1 greater share of power supply revenue reductions under the proposed RDM than would
2 Full Service customers, because Electric Choice customers would get a credit only for the
3 PSCR base, while Full Service customers would get a credit both for the PSCR base and
4 the reduction of power supply costs at the margin.

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

7 A. My recommendation is that the Commission *defer the proposed EO RDM to a*
8 *future proceeding*. The DTE proposal cannot be implemented under current law. It is
9 also not adequately articulated and supported in this proceeding. It conflicts with other
10 aspects of DTE's regulatory processes. What little is explained has several major
11 deficiencies, including affecting Electric Choice customers unequally compared to Full
12 Service customers.

13
14 DTE has stated, "In fact, for administrative efficiency, DTE Electric's EO and
15 RDM reconciliations could be consolidated." D.Stanczak, direct testimony, page 12,
16 lines 20-22. Consolidation can work well. The RDM proposal could be taken up in an
17 EO proceeding if the law is amended to make an RDM lawful. This would allow DTE to
18 flesh out, revise and correct as needed, and support its proposal, allow other parties a
19 reasonable chance to critique and offer changes, and allow the Commission to deal with
20 potential overlaps between the proposed EO RDM and the current EO Performance
21 Incentive Mechanism in a single docket.

22

1 If and RDM becomes lawful and the Commission decides to approve the
2 proposed EO RDM, then it should also order DTE to fix the following deficiencies: (a)
3 separate the reduced revenue into power supply and distribution components; (b)
4 subtract service charges from the calculation of surcharges; (c) subtract the marginal cost
5 of fuel, purchased power, and transmission instead of the average reflected in the PSCR
6 base, plus subtract increased profits from any additional wholesale sales; (d) subtract any
7 and all other variable O&M costs; and (e) subtract the amount of the EO performance
8 incentive mechanism from the amount to be recovered from customers under the EO
9 RDM. The Commission may find other deficiencies I do not address here.

10
11 **2. “Shortfall” of Capacity in MISO Zone 7**

12 **Latest MISO report shows minimal deficit and likely surplus.**
13

14 **Q. DTE testimony addresses a “shortfall” of capacity in various areas. What**
15 **does “shortfall” mean?**

16 A. The Midcontinent ISO (“MISO”) uses the terms “surplus” and “deficit,” and
17 using the same terminology here can clarify the discussion. MISO periodically assesses
18 the electric capacity requirements for its region and sub-regions, called “zones,” and
19 establishes specific capacity requirements for Load Serving Entities (“LSEs”) in its
20 region. MISO’s Zone 7 is the MISO area in the Lower Peninsula of Michigan. The
21 capacity requirements are set to cover each forecasted LSE’s load at the time of the
22 MISO annual system peak, plus a reserve margin that covers variation in load and
23 generation random outages. For the purpose of assessing surpluses and deficits, MISO

1 uses installed capacity (“ICAP”), which is the capability of the resource without any
2 outages, and an associated reserve margin of 15.2%.

3
4 If the amount of capacity resources in a region or sub-region – ignoring the ability
5 to import or export from region or sub-region via the transmission system – is more than
6 the forecasted load plus reserve margin, MISO calls the difference a “surplus.” If the
7 amount is less than the forecasted load plus reserve margin, MISO calls the difference a
8 “deficit.” I will use that terminology here.

9
10 **Q. What does MISO’s reserve margin represent?**

11 A. To understand surpluses and deficits correctly, it is important to be aware that the
12 *measurements include both the forecasted peak load and the reserve margin, and that the*
13 *reserve margin is derived statistically.* MISO sets a reserve margin by *statistical*
14 *modeling* such that – considering fluctuation of peak loads and random outages of
15 generators – the modeled load will be more than the modeled running generation (called
16 a “loss of load” hour) in no more than 24 hours in 10 years – 24 loss of load hours in
17 87,600 hours. The casual reference to the standard is “one day in ten years,” although the
18 statistical modeling is by hour, not by day. MISO refers to this standard as a “resource
19 adequacy” standard. Although MISO reserves the word “reliability” for the assessment
20 of the transmission system, not the supply/demand system, in casual use many people
21 apply the terms “reliability” or “reliability standard” to the assessment of the
22 supply/demand system.

1 **Q. How are surpluses and deficits related to reliability?**

2 A. A *deficit* that is less than the reserve margin means that there are still enough
3 capacity resources to meet the forecasted load, but not enough to meet the full reserve
4 margin; and in this situation the so-called “reliability” of the supply/demand system is
5 less than the standard – meaning more than 24 statistically modeled hours in 10 years.
6 Conversely, a *surplus* means that supply/demand reliability is greater than the standard,
7 meaning fewer than 24 statistically modeled hours in 10 years. The greater the deficit,
8 the lower the 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 Planning
14 Resource Auction in March 2016 for the Planning Year of 2016-17¹ show that Zone 7
15 imported 872 MW, while the transmission Capacity Import Limit was 3,521 MW – far
16 above the import amount. Thus, while Zone 7 had a technical “deficit” of 872 MW, there
17 in fact was adequate capacity available to Zone 7 from outside the zone – up to 3,521
18 MW total. Actual usable capacity considers both the resources within Zone 7 and the

¹ “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 amount that can be imported via the transmission system. To the contrary, the “surplus”
2 or “deficit” for Zone 7 assumes there is zero transmission import capability into Zone 7.
3

4 **Q. What does DTE say about the supply/demand situation in MISO and in**
5 **Michigan?**

6 A. DTE states:

7 **Q. Are the Company’s concerns regarding the impact of environmental**
8 **regulations and a potential generation resource shortfall in Zone 7**
9 **still applicable?**

10
11 A. Yes, and perhaps even more so now than when initially presented in Case
12 No. U- 17689. Specifically, in MISO’s report titled “2015 OMS Survey
13 Results” dated June 2015, MISO projects a 1.2 to 1.3 GW Zone 7
14 Resource Requirement shortfall in the 2016-2017 plan year, with a
15 regional shortfall potentially occurring as early as 2020.
16

17 D.Stanczak, direct testimony, page 15, lines 7-14.
18

19 **Q. Has MISO published new or updated information since the report that Mr.**
20 **Stanczak mentions?**

21 A. Yes. MISO, in cooperation with the OMS (Organization of MISO States, an
22 association of state regulatory agencies), has recently updated its 2015 report. The new
23 report is “2016 OMS MISO Survey Results, July 2016 Resource Adequacy Committee”
24 (“MISO 2016 Survey”).²
25

² “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 **Q. What does the MISO 2016 Survey show for Zone 7, compared to the previous**
2 **report in 2015?**

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

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

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

15
16 **Q. Is there additional generation under development in the entire MISO region**
17 **that MISO does not include in its totals?**

18 A. Yes. Page 14 of the 2016 MISO Survey shows that for 2017 about 8 MW of
19 potential generation additions are in various stages of development in MISO. Only about
20 2 GW were included in MISO’s totals for 2017. This page is shown in my Exhibit EM-2
21 (AJZ-2), page 2 of 4.

22

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

3
4 Only a small fraction of the generation under development would have to go into
5 service to eliminate the deficits that MISO shows in its report. And again, "surplus" and
6 "deficit" ignore transmission capability among the MISO zones – they are tallies for a
7 zone as if there were no transmission capability in or out.

8
9 **Q. Does MISO exclude other generation within its region?**

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

16
17 **Q. What are your conclusions from the additional information you have**
18 **explained regarding the OMS MISO surveys?**

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

23

1 Second, looking at the Zone 7 deficits from the 2014, 2015, and 2016 survey
2 reports, plus the actual results of the 2016 Planning Resource Auction – all of which has
3 been discussed above and displayed in my exhibits – *the Zone 7 surplus/deficit situation*
4 *has improved steadily and significantly according to MISO*, even excluding new
5 resources under development. The change has been from a deficit of -3.0 GW in the
6 2014 survey to -0.3 GW in the 2016 survey, an improvement of 2.7 GW. The results of
7 the three surveys and the auction are summarized on Exhibit AJZ-3 (EM-3).
8

9 **3. Economic Development Expenses**

10 **Unfair cost effects on Electric Choice customers.**
11

12 **Q. DTE has requested additional funds for its economic development group.**

13 **How does DTE explain the cost-based benefits to customers?**

14 A. DTE apparently believes that more money for its economic development group

15 “could reduce rate pressure”:

16 The primary goal of DTE Electric’s economic development efforts is to
17 increase load growth and sales through the expansion of businesses in the
18 State of Michigan. The increase in electric sales helps spread fixed costs
19 across more customers which could reduce rate pressure on all customers.
20

21 I.Dimitry direct testimony, page 28, lines18-21.
22

23 **Q. Do load growth and increased sales reduce rates?**

24 A. There are two sides to the coin, so to speak. The conventional perspective is that,
25 as Ms. Dimitry states, the present fixed costs are spread over more units delivered, and
26 therefore the average fixed cost embedded in the delivered units decreases.

1 However, if more resources – whether power supply, distribution, fuel, purchased
2 power, O&M, and transmission – are needed to serve the additional load and the
3 incremental cost of some of these are greater than the current average costs, then it is
4 possible for rates to go up, not down. Thus, the “reduce rate pressure” rationale for this
5 proposal should be viewed in the context of DTE’s asserted concerns about retirements of
6 generation plants and its need for new generation resources.

7
8 **Q. Are all customers affected equally?**

9 A. The effect of increased money for economic development on both Full Service
10 and Electric Choice customers should be considered. Sales growth will primarily affect
11 costs in the power supply portion of DTE’s business. Electric Choice customers do not
12 take power supply service. If the Commission decides to allow DTE to charge customers
13 additional money for economic development, then the additional amount first should be
14 allocated to power supply and distribution separately, on the basis of relative total
15 investment.

16
17 **Q. By how much is DTE proposing to increase its economic development**
18 **activities?**

19 A. The current level of \$0.823 million in the historic period increases to \$3.879
20 million in the proposed period. See Exhibit A-10, Schedule C5.7, page 1, line 19. This is
21 more than quadruple.

22

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

3 A. DTE apparently believes that other development organizations and governmental
4 agencies need more resources and that DTE should provide such resources:

5 Currently, DTE Energy has a staff of four economic developers, and has
6 historically relied on support from partner organizations and state agencies to
7 provide similar types of services offered by the four utilities mentioned above.
8 These partner organizations have very limited resources and capabilities,
9 especially in the areas of analytics, databases, and land information. DTE
10 Electric believes that the requested funds are critical for the Company and for
11 the State of Michigan to compete for business and load growth with the best-
12 in-class utilities across the United States.

13
14 I.Dimitry direct testimony, page 25, line 5-11. Emphasis added.

15
16
17
18 **Q. Do you agree with DTE about the role it proposes to play?**

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

24
25 DTE as a regulated electric utility is not a state agency; it has no taxing authority;
26 it has no oversight by voters. It has no duty to provide staff services in the form of
27 analytics, databases, or land information for any governmental agency or other
28 organization that it believes needs more resources. It has no authority to decide what the
29 State of Michigan’s policy should be; it has no obligation to implement what it believes

1 to be a productive economic policy for any governmental unit, let alone charge its electric
2 customers for that activity. Allowing DTE to charge its customers for economic
3 activities in support of state agencies amounts to creation of an economic development
4 tax that only DTE customers are being asked to pay.

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

7 A. Under regulation in Michigan, the management of a regulated utility is free to
8 make its own business decisions. Recovering costs from electric customers for those
9 decisions is up to the Commission.

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

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

1 distribution customers by distribution sales in each rate class and collected in distribution
2 rates.

3
4 The asserted purpose of increased economic development activities is to increase
5 sales, and therefore allocation of the power supply and distribution portions by sales is
6 the cost-based method to apportion the costs. An allocation by number of customers
7 would result in the residential class paying about 90% of economic development costs
8 but not receiving commensurate decreases in rates.

9
10 The objective of rates based on cost of service is that the rates are commensurate
11 with the services and benefits received. The Commission makes the decision on how this
12 is done, so as to not advantage or disadvantage a particular group of customers.

13
14 **4. Incentive Compensation Plan**

15 **If included in revenue requirements, the share borne by**
16 **Electric Choice customers should be commensurate**
17 **with the benefits they receive.**
18

19 **Q. What is your opinion on DTE Electric's incentive compensation proposal?**

20 A. DTE's proposal for including incentive compensation in revenue requirements
21 should be modified. DTE is proposing to include in its revenue requirement the incentive
22 compensation under several programs. The DTE incentive compensation plans are
23 shown in Exhibit A-20, Schedules L1-L4, and the expenses of the programs are shown on
24 Schedule L5, column k.

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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 over 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 affected 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. Do the proposals in Exhibit A-20 reasonably reflect the sharing of benefits of superior performance, if they were to be included in the rates of Electric Choice customers for distribution services?

A. No, in several areas they do not. The two main deficiencies are (a) failure to tie performance to benefits to customers – which affects all customers, not just Electric Choice – and (b) failure to separate distribution service benefits from power supply service benefits that Electric Choice customers do not receive – which affects Electric Choice distribution customers.

Regarding the failure to tie performance to customer benefits, Exhibit A-20, Schedule L5 shows that 62% of the incentive expense is tied to various financial goals (column k, line 14 / line 68), including return to shareholders, balance sheet “health,”

1 return on equity, DTE Electric operating earnings, cash flow, and DTE Energy corporate
2 operating earnings per share.

3
4 For any rate-paying customer to pay a bonus to a utility for increasing earning per
5 share, total return to shareholders, and the other financial goals is illogical and violates
6 the principle of paying for a shared benefit. Such a system forces ratepayers to reward
7 the utility for making them pay more, as the earnings are earned on the ratepayers' backs,
8 so to speak. Moreover, increased earnings per share benefits stockholders, not customers.
9 Therefore, if there is to be a payment to utility employees for meeting financial goals that
10 benefit stockholders, the payment should come out of stockholder earnings, not customer
11 rates.

12
13 **Q. How do the compensation metrics fit with DTE's proposal for a RDM for the**
14 **Energy Optimization program?**

15 A. When 62% of the compensation metrics are for financial performance and DTE is
16 requesting a RDM for EO and the Commission has already granted a performance
17 incentive mechanism for EO, it means that the money collected under the RDM and the
18 performance incentive goes to shareholder value, which increases several of the metrics
19 under financial performance, which in turn increases the incentive compensation payout.

20
21 In effect, some DTE employees would be receiving incentive pay – funded by
22 customers – for convincing the Commission to allow DTE to collect money from

1 customers for incentivizing activities in the EO program. Pancaked incentive pay upon
2 incentive revenue.

3
4 **Q. What is your recommendation?**

5 A. My recommendation is that if the Commission chooses to approve an incentive
6 compensation mechanism that is to be paid for by customers, then the “financial” portion
7 shown on Exhibit A-20, Schedule L5, should be excluded.

8
9 **Q. The other portions of Exhibit 20 relate to customer satisfaction, employee**
10 **“engagement,” and operating excellence. How would you assess these parts of the**
11 **proposal, and what are your recommendations?**

12 A. DTE Electric has not separated distribution service benefits from power supply
13 service benefits. Specifically, five of the eight “operating excellence” measures shown
14 on Exhibit A-20, Schedule L5, lines 46-59 relate directly to power plants. Full Service
15 customers take *both* power supply service and distribution service, while Electric Choice
16 customers take *only* distribution service. Full Service customers benefit from improved
17 plant outage rates and reduction in plant expenses. Electric Choice customers do not,
18 because they are paying another supplier for power supply services, including services
19 from the MISO.

20
21 Therefore, my recommendation to the Commission is that Electric Choice
22 customers should pay only for performance of the distribution system, the three measures
23 shown on Exhibit A-20, Schedule L5, lines 37-44.

1 Also, in regard to “Employee Engagement – Gallup” shown on Exhibit A-20,
2 Schedule L5, line 26, if this is the result of some type of morale or attitude survey, then it
3 should be excluded, as it is not directly tied to the distribution or power supply services
4 for which customers pay.

5

6

5. Changes in Electric Choice Tariff

7

Metering requirement is acceptable.

8

Clarify wording to follow U-15801 order.

9

10 **Q. DTE is proposing to add a paragraph D to the Retail Access Service Rider**
11 **EC2, section E2.8. Do you agree with this change?**

12 A. DTE witness Mr. Timothy A. Block explains the reason for the change on pages
13 11-12 of his Direct Testimony. I certainly agree that the proposed change matches the
14 implementation rules set out in the September 29, 2009 order in Case No. U-15801 *et al.*
15 The order included rules under which the expansion of load by various groups of Electric
16 Choice customers would or would not count as increased participation by such customers
17 in Electric Choice.

18

19 The proposed paragraph D is shown in Exhibit A-15, Schedule G1, page 66 of 66.
20 Additional phrases can help clarify the situation of the customers affected by the
21 proposed change. Also, both the customer and DTE should have input in determining
22 whether or not a metering situation is “impractical,” and if there is no agreement, the
23 customer always has the ability to register a complaint with the Commission. Obviously,
24 if the metering situation is truly impractical, there is no reason for DTE not to waive the

1 requirement, and therefore DTE should not have “sole discretion” to refuse a waiver.
2 Finally, “expand” should have the same meaning as in the September 29, 2009 order in
3 Case No. U-15801 *et al.* that DTE references.
4

5 DTE’s proposed paragraph reads:

6 “D. Customers not eligible to expand the retail access service load at their
7 facility in accordance with the procedures adopted by the MPSC in Case No.
8 U-15801 on September 29, 2009, must install separate metering, at their
9 expense, in order to measure and bill the Full Service portion of their facility
10 load. At the Company’s sole discretion, the separate metering requirement
11 may be waived if the installation of separate metering is impractical. Under
12 this waiver, both retail access and full service loads will be estimated based on
13 the metered load of the facility.”

14 Exhibit A-35, Schedule G1, page 66 of 66, section E2.8, paragraph D.
15

16 I recommend that the paragraph be changed to read:

17 “D. Customers **who desire to expand load at their facility, where expand**
18 **means to connect new load through an existing meter, but are** not eligible
19 to expand the retail access service load at their facility **above the Cap on**
20 **Choice Participation** in accordance with the procedures adopted by the
21 MPSC in Case No. U-15801 on September 29, 2009, must install separate
22 metering, at their expense, in order to measure and bill the Full Service
23 portion of their facility load. ~~At the Company’s sole discretion, t~~ **The separate**

1 metering requirement ~~may~~ **will** be waived if the installation of separate
2 metering is impractical. Under this waiver, both retail access and full service
3 loads will be estimated based on the metered load of the facility.”
4

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

6 **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>
Director, Special Projects	Customer Energy Solutions	Apr 97 to May 98

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

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-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.



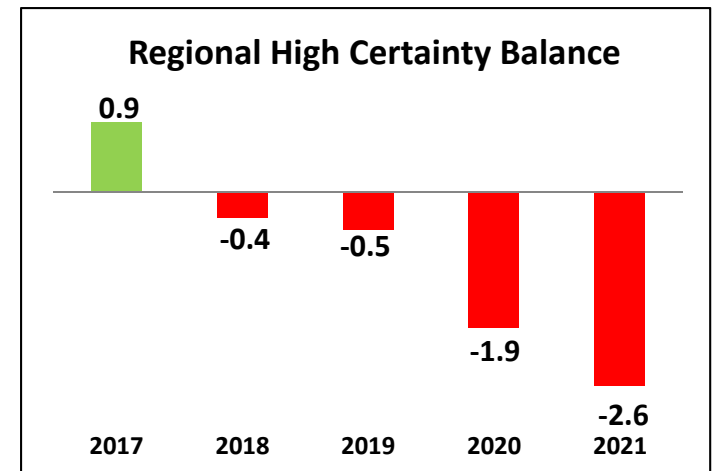
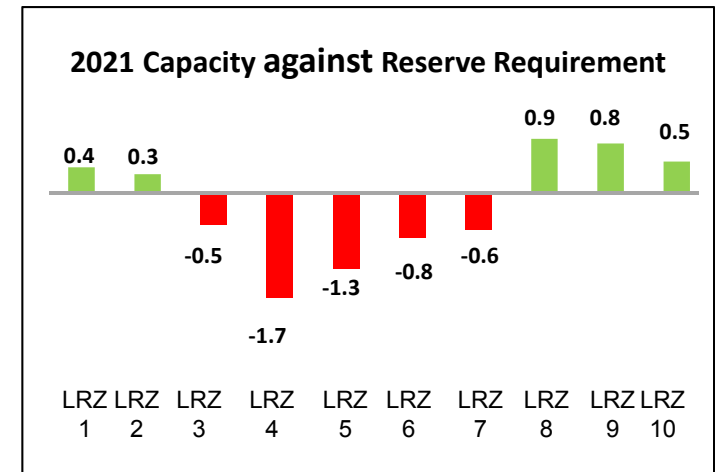
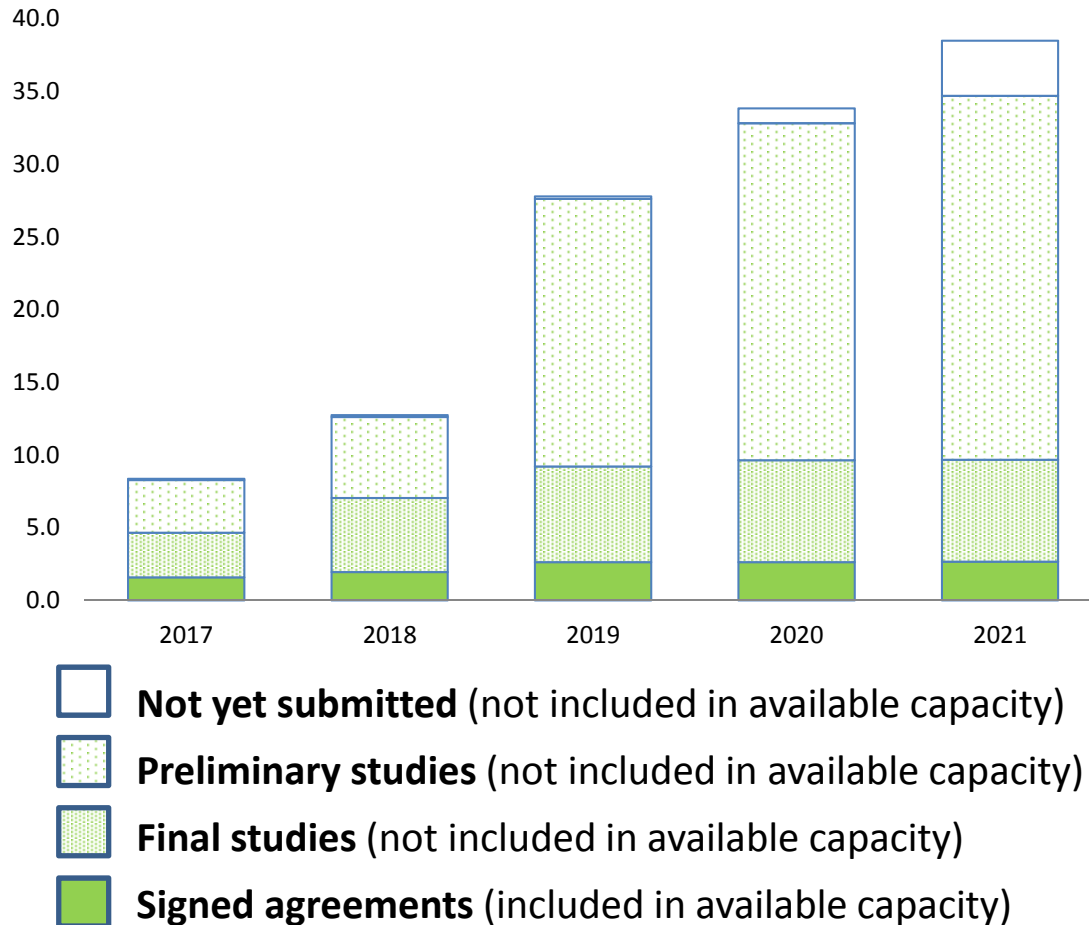
2016 OMS MISO Survey Results

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

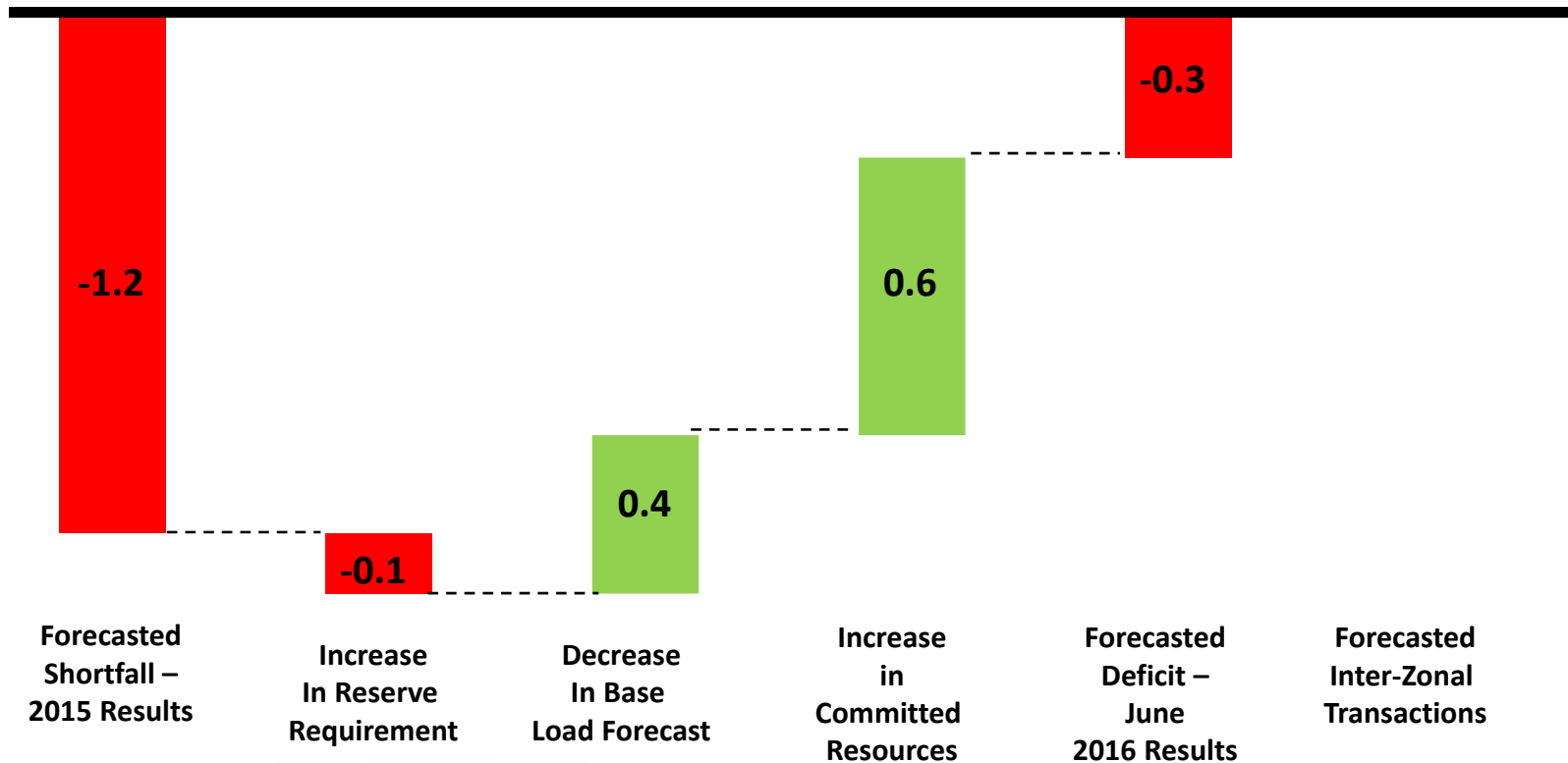
Continued commitment to firming up planned generation interconnections through the MISO process will be required

Potential Generation Additions, in GW*

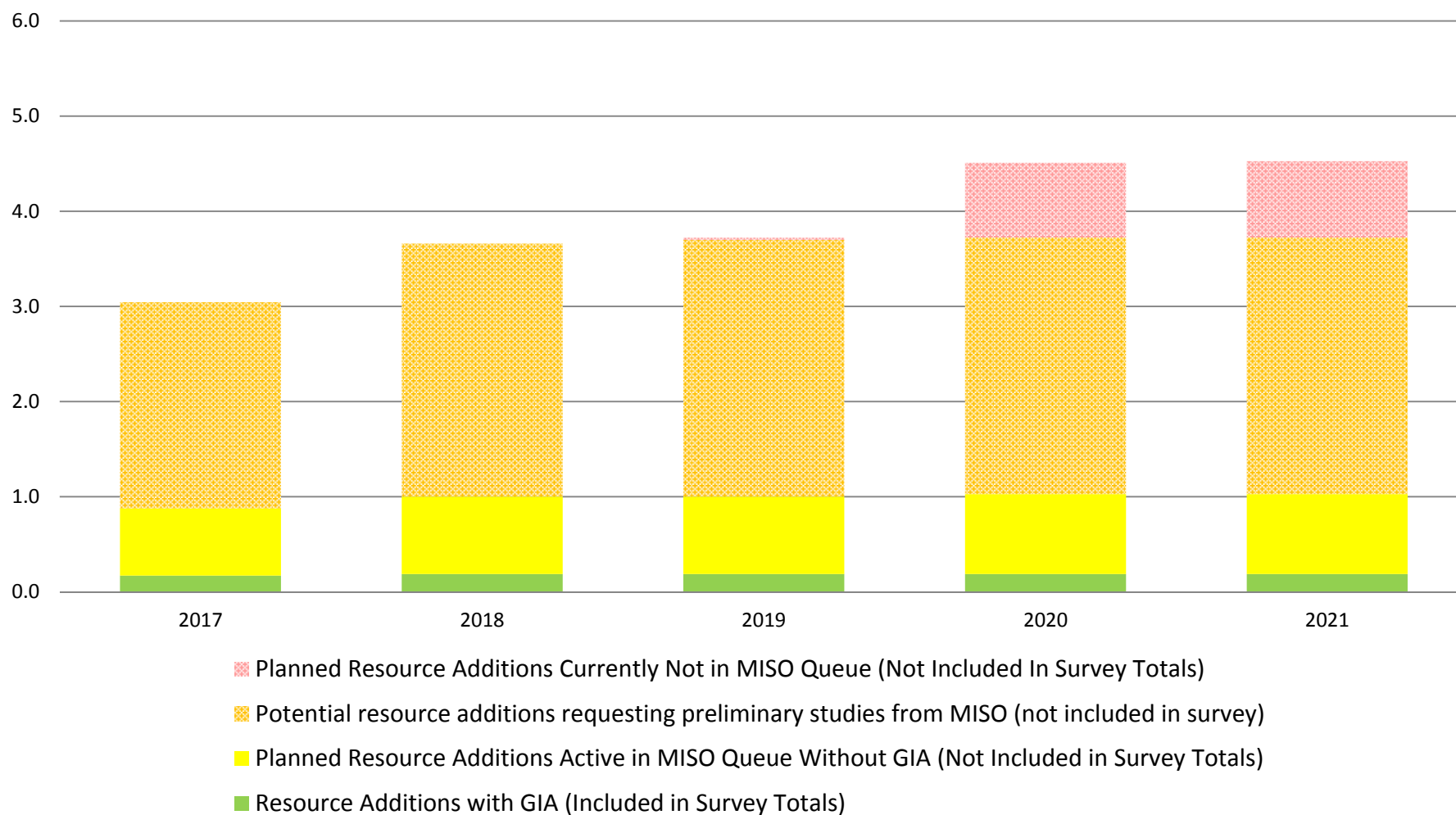


2015 vs 2016 OMS MISO Survey Results Zone 7

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	<i>GW improvement between 2014 and 2016</i>		
	====			

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)
DTE ELECTRIC COMPANY)
for authority to increase its rates, amend)
its rate schedules and rules governing)
the distribution and supply of electric)
energy, and for miscellaneous accounting)
authority.)

Case No. U-18014

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 5th day of July, 2016, she served the 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

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MPSC Case No. U-18014

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