UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Seaway Crude Pipeline Company LLC) Docket No. IS12-226-000

POST-HEARING REPLY BRIEF OF APACHE CORPORATION, CHEVRON PRODUCTS COMPANY, AND NOBLE ENERGY, INC.

Submitted: June 4, 2013

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Court Cases

FERC and FPC Decisions

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES

Statutes and Regulations

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Seaway Crude Pipeline Company LLC) Docket No. IS12-226-000

POST-HEARING REPLY BRIEF
OF APACHE CORPORATION, CHEVRON PRODUCTS COMPANY,
AND NOBLE ENERGY, INC.

TO: The Honorable Karen V. Johnson
Presiding Administrative Law Judge

Pursuant to Rule 706 of the Federal Energy Regulatory Commission's ("FERC" or "Commission") Rules of Practice and Procedure, 18 C.F.R. § 385.706 (2013), and the Chief Judge's September 17, 2012 order modifying the procedural schedule in this proceeding, Apache Corporation, Chevron Products Company (a division of Chevron U.S.A. Inc.), and Noble Energy, Inc. (jointly, "ACN") respectfully submit this post-hearing reply brief. In its reply brief, ACN responds to the arguments that Seaway Crude Pipeline Company LLC ("Seaway") and the Commission Trial Staff ("Trial Staff") raised in their Initial Briefs. The Canadian Association of Petroleum Producers ("CAPP") and Suncor Energy Marketing Inc. and Canadian Natural Resources Limited (jointly, "SCN") also filed Initial Briefs in this proceeding.

I. CONTESTED FINDINGS OF FACT AND CONCLUSIONS OF LAW

This reply brief rebuts the following proposed findings of fact and conclusions of law in Seaway's and Trial Staff's Initial Briefs (internal citations ommitted):

Seaway's Contested Findings of Fact and Conclusions of Law:

2. The purpose of this case is to assess the justness and reasonableness of the initial uncommitted rates in Seaway's Tariff No. 2.0.0. The Commission's test period regulations require initial rates for new service to be based on a twelve-month projection at the time of filing of costs and revenues. It is not appropriate to establish new rates to take effect after the initial rates, or to use a second test period in this case. (Rebutted herein at Section 2).

3.B. The full purchase price related to Enbridge's acquisition of its fifty percent share of Seaway from ConocoPhillips should be included in rate base. (Rebutted herein at Section 3).

3.B.1. The Enbridge purchase price meets the Commission's requirements for inclusion in rate base, because it resulted in the pipeline being put to a new use and provided substantial benefits to shippers. (Rebutted herein at Section 3).

3.B.2. The full purchase price, including goodwill, should be included in rate base. (Rebutted herein at Section 3).

3.B.3. Of the total $1.15 billion purchase price, $1.095 billion is properly attributed to the Longhaul 30-inch System, and $55 million is properly attributed to the other assets. (Rebutted herein at Section 3).

4.A. Seaway calculated AFUDC correctly. Seaway's AFUDC should be based on all investment costs required to place the reversed pipeline in service, including the Enbridge purchase price and the depreciated original cost of the assets contributed by Enterprise. (Rebutted herein at Section 4A).

4.B. The appropriate level of operating expenses, including depreciation, for the test period is approximately $20.3 million, based on an annualized estimate of operating expenses from June 2012 through December 2012. (Rebutted herein at Section 4B).

4.D.1. The appropriate capital structure is 52.17% debt and 47.83% equity, based on the average capital structure of the oil pipeline proxy group. (Rebutted herein at Section 4D).

4.D.2. The appropriate cost of debt is 5.46%, based on the average of the oil pipeline proxy group. (Rebutted herein at Section 4D).

4.D.3. The appropriate ROE is 12.36% (nominal) and 10.69% (real). (Rebutted herein at Section 4D).

4.E. Seaway is entitled to a full income tax allowance based on a weighted average federal and state income tax rate of 33.7%. (Rebutted herein at Section 4E).

5. The throughput used for Seaway's initial rates should be the initial design capacity of 135,000 barrels per day. (Rebutted herein at Section 5).

6. Seaway's use of the revenue credit approach to calculate maximum just and reasonable uncommitted rates is appropriate and consistent with Commission precedent. (Rebutted herein at Section 6).

7. The differential between Seaway's light crude oil and heavy crude oil rates is fully justified based on the different properties of the two types of crude oil. (Rebutted herein at Section 7).

8. Seaway's initial uncommitted rates of $3.82 for light crude oil and $4.32 for heavy crude oil are just and reasonable. (Rebutted herein at Section 8).

Trial Staff's Contested Findings of Fact and Conclusions of Law:

1. Seaway's rates should be calculated using Staff's cost of service, revised as discussed in [Staff's] initial brief, Staff's proposed determinants, and the methodology contained in Exhibit No. S-27. (Rebutted herein at Sections 3, 4, and 6).

4. The rate bases for the two periods should be calculated in the same manner shown on Exhibit Nos. S-21 and S-22. However, the amount of Carrier Property in Service, Enbridge Acquisition, Column (a), shown on page 14 of these exhibits used in the calculation of rate base should be

adjusted downward to eliminate non-jurisdictional assets in the Enbridge acquisition costs to reflect only the amount of "Total PP&E Fair Value" for the 30-inch Longhaul System shown in Exhibit No. ACN-42, page 1, numbered paragraph 1. (Rebutted herein at Section 3).

20. The appropriate method of calculating the income tax allowance for the pre-expansion period is shown in Exhibit No. S-21 at 5, and in Exhibit No. S-22 at 5 for the post-expansion period. The tax amounts currently shown in these exhibits should be adjusted to incorporate the effect of the removal of non-jurisdictional assets identified in Exhibit No. ACN-42. (Rebutted herein at Section 4E).

24. The differential between the light and heavy crude oil rates of Seaway is not discriminatory and should be maintained. (Rebutted herein at Section 7).

II. ARGUMENT

As explained in ACN's Initial Brief and this reply brief, Seaway has not met its burden of showing that its filed rates are just and reasonable under the Commission's regulations, precedent, cost-based ratemaking principles, and Section 1(5) of the Interstate Commerce Act ("ICA").[1] The substantial record evidence establishes that Seaway's proposed cost of service is excessive, and its filed rates are not based on its underlying cost of providing service.[2] Additionally, if Seaway's committed rates are

[1] 49 U.S.C. § 1(5) (1977) (establishing that all rates charged for oil pipeline transportation service "shall be just and reasonable"); Farmers Union Central Exchange, Inc. v. FERC, 734 F.2d 1486, 1502 (D.C. Cir. 1984) ("Farmers Union II") (holding that a just and reasonable rate is "high enough to both maintain the [pipeline's] credit and attract capital," and "low enough so that exploitation by the [regulated business] is prevented.") (internal quotations omitted).

[2] See, e.g., Exhibit Nos. ACN-1 at 3:12-15, ACN-21, ACN-22, and SCN-57; Tr. at 415:14-18 (Wetmore Cross-examination).

not adjusted, Seaway will significantly over-recover its cost of service from its committed shippers alone.[3] Accordingly, it is important to carefully consider the cumulative effect of the high-dollar issues in this case. All just and reasonable reductions to Seaway's uncommitted shipper rates will limit Seaway's ability to recover excessive returns to the detriment of its ratepayers.

The Commission has found that Seaway has not demonstrated that it lacks market power, and denied Seaway's request for market-based rate authority on that basis.[4] Nevertheless, Seaway negotiated rates with its committed shippers, some of which are affiliates, that reflect Seaway's market position as the sole crude oil pipeline currently providing transportation service from the over-supplied Cushing hub to the higher-priced Gulf Coast markets.[5] Given Seaway's substantial market position, Seaway was able to negotiate committed rates that far exceed a just and reasonable, cost-based rate.[6] Seaway now asks Your Honor to merely deem those rates to be just and reasonable.[7]

---

[3] See Exhibit No. SCN-1 at 9:3-10:2 and Figure 3.

[4] Enterprise Products Partners L.P., 139 FERC ¶ 61,099 (2012), re'hg granted, 139 FERC ¶ 61,255 (2012).

[5] See Exhibit Nos. SCN-52 ("[T]he initial volumes of crude oil through the Seaway Pipeline were delivered to the Jones Creek facility, [which] marks the first southbound delivery of crude by pipeline from the oversupplied Cushing hub."), SCN-49 ("Seaway will transport crude oil to the Gulf Coast that is currently stranded at Cushing and is priced at a substantial discount to the oil imports being used by Gulf Coast refiners.").

[6] See Exhibit No. ACN-1 at 10:2-17.

[7] Seaway Initial Brief at 7.

If Your Honor agrees with Seaway and does not adjust Seaway's committed rates, then Seaway will earn excessive returns, regardless of the uncommitted rates that are approved in this proceeding. This is because Seaway's committed rates are so excessive, relative to a cost-based rate, that Seaway will earns revenues that substantially exceed its cost of service from its committed shippers alone.[8] This significant fact means that even if the uncommitted rate is set at $0.00, Seaway will earn excessive returns. Any uncommitted rate above $0.00 will only further increase Seaway's excessive returns. For these reasons, Seaway's filed rates are not just and reasonable under the ICA and Farmers Union II, which require an oil pipeline's rates to be set such that the pipeline is not permitted to recover excessive returns.[9]

If Your Honor determines that Seaway's committed shipper rates should not be adjusted in this case, then Seaway's uncommitted rates must be analyzed in light of the unique facts of this case. Accordingly, each issue should be decided in a manner that limits, to the greatest extent permissible under the law, Seaway's ability to earn excessive returns.

Regarding Seaway's ability to earn excessive returns, the three most significant issues in this case are as follows: 1) whether Seaway's committed rates should be adjusted downward to reflect its cost of service, and limit its ability to exercise market power; 2) whether it is just and reasonable to adjust Seaway's approximately $118

[8] See Exhibit No. SCN-1 at 9:3-10:2 and Figure 3.

[9] See 49 U.S.C. § 1(5) (1977); Farmers Union II, 734 F.2d at 1502.

million original cost rate base to include a $1.1 billion write-up for Enbridge's purchase of its interest in Seaway; and 3) how to calculate Seaway's rates to account for the fact that Seaway's capacity tripled within the first eight months of its post-reversal operations.

Adopting ACN's positions in this case will limit Seaway's ability to earn excessive returns, while fully complying with the Commission's policies, precedent, and regulations. Conversely, adopting Seaway's positions will permit Seaway to charge rates that are so excessive and reflect Seaway's market position to such a degree that they approximate unlawful market-based rates.[10]

1. Are Seaway's Committed Shipper Rates At Issue In This Docket?

ACN supports Trial Staff's positions on this issue. On December 10, 2012, Seaway filed a Petition for Declaratory Order in Docket No. OR13-10-000 ("Petition"). In its Petition, Seaway requested a Commission order declaring that Seaway's committed rates and transportation service agreements ("TSA") are not at issue in the instant case, because they are per se just and reasonable.[11] In its March 22 Order, the Commission denied Seaway's Petition, and left open the question of whether Seaway's committed rates should be adjusted in this proceeding.[12]

In its Initial Brief (at 7 and 10), Seaway argues that the Commission's March 22

---

[10] See, e.g., Exhibit No. ACN-1 at 10:2-17.

[11] Petition at 8 and 13.

[12] Seaway Crude Pipeline Company LLC, 142 FERC ¶ 61,201 at P 11 (2013) ("March 22 Order").

Order stands for the proposition that Seaway's committed rates have been deemed to be just and reasonable, and should be upheld on that basis. Seaway's argument mischaracterizes the March 22 Order, and should be disregarded. The March 22 Order denied Seaway's Petition, and simply reiterated that "the agreed-upon terms of [a TSA] will govern the determination of the committed shippers' rates over the term of the TSA."[13] As explained below, "the agreed-upon terms" of Seaway's TSAs establish that the Commission has the authority to review Seaway's committed rates under the ICA's just and reasonable standard, as proposed by ACN and Trial Staff in the instant case.

Article 6.06 of Seaway's committed shipper TSAs provides that the "rates payable for all Services are <u>subject to the approval of and modification by</u> the FERC or any other Governmental Authority having jurisdiction."[14] As detailed below, the courts have interpreted similar contract terms as permitting the Commission to revise the agreed-upon contract rates when those rates are unjust and unreasonable (as opposed to applying the public interest standard). For example, in <u>Kansas Cities v. FERC</u>, the United States Court of Appeals for the District of Columbia Circuit explained:

> [t]he obstacle that the public-interest standard presents to a rate change is almost insurmountable. To assume that a contractual provision pertaining to rate adjustment refers to that standard is to assume that it was intended to be virtually inoperative; whereas to interpret it as referring to just-and-reasonable changes is to give it a content that is both substantial and fair to both sides. Thus, courts and the Commission have almost universally construed contractual

---

[13] <u>Id.</u> at P 13.

[14] Exhibit No. SEA-4 at 13 (emphasis added).

references to future rate changes to authorize…a just-and-reasonable standard of proof.[15]

In that case, the court noted that the following provisions constitute "contractual references to future rate changes" that contemplate review under the just and reasonable standard:

1) a provision stating that the agreement is "subordinate to, subject to and conditioned upon the valid orders….of, and the granting of approval and authorization by" an authority having jurisdiction;
2) a provision stating that the agreement "shall at all times be subject to such changes or modifications as shall be ordered from time to time by" an authority having jurisdiction;
3) a provision stating that the agreement and rates are "subject to amendment or alteration as a result of and in accordance with a valid applicable order" of any authority having jurisdiction; and
4) a provision stating that the contract rates "may be changed during the term of the contract, but only with the approval of the appropriate regulatory agency having jurisdiction."[16]

---

[15] Kansas Cities v. FERC, 723 F.2d 82, 88 (D.C. Cir. 1982)(citing Papago Tribal Utility Authority v. FERC, 723 F.2d 950 (1982); Public Service Company of New Mexico v. FERC, 628 F.2d 1267, 1269-70 (10th Cir. 1980), cert. denied 451 U.S. 907 (1981); Louisiana Power & Light Company v. FERC, 587 F.2d 671, 675-76 (5th Cir. 1979); and Missouri Power & Light Company, 55 FPC 2693 (1976)).

[16] Id.

Here, Article 6.06 of Seaway's committed shipper TSAs similarly provides that the "rates payable for all Services are subject to the approval of and modification by the FERC or any other Governmental Authority having jurisdiction."[17] Thus, the TSAs include "contractual references to future rate changes," and are subject to just and reasonable review.[18] Furthermore, by undertaking review of Seaway's committed shipper rates under Article 6.06, Your Honor is complying with the March 22 Order's requirement that the terms of Seaway's TSAs govern the resolution of the issues in this case.[19] Only a holding that the committed shipper rates can be modified and/or approved by the FERC under the just and reasonable standard will give meaningful effect to Article 6.06.[20]

Finally, as explained above, if Your Honor does not adjust Seaway's committed shipper rates in this proceeding, Seaway is guaranteed to recover excessive returns from its shippers, in violation of the just and reasonable requirement of the ICA.[21] There is no way to modify the uncommitted rates to remedy this over-recovery—the uncommitted rates will only further increase Seaway's excessive returns. This will permit Seaway to charge what are essentially market-based rates, despite the fact that

---

[17] Exhibit No. SEA-4 at 13.

[18] See Kansas Cities v. FERC, 723 F.2d at 88.

[19] See March 22 Order, 142 FERC ¶ 61,201 at P 13.

[20] See Kansas Cities v. FERC, 723 F.2d at 88.

[21] See Exhibit No. SCN-1 at 9:3-10:2 and Figure 3; 49 U.S.C. § 1(5) (1977); Farmers Union II, 734 F.2d at 1502.

the Commission has denied Seaway's request for market-based rate authority.[22] Thus, Your Honor should hold that Seaway's filed rates—both the committed and uncommitted rates—should be adjusted to reflect ACN's positions on Seaway's cost of service, throughput, and rate design, as detailed below.

2. What Is The Appropriate Rate Period or Periods?

ACN, Trial Staff, and SCN all propose a twelve-month test period of June 2012 through May 2013.[23] Seaway proposes to calculate rates based on its cost and revenue projections for a June 2012 through December 2012 test period,[24] which is inconsistent with the Commission's test period regulations and cost-based ratemaking policies.

According to the Commission's regulations, an oil pipeline's cost of service rate filing must include supporting cost, revenue, and throughput data for the test period.[25] Seaway does not dispute that the Commission's regulations require that a twelve-month test period be used to analyze its rates in this proceeding.[26] Seaway also does not dispute that a cost of service analysis based on June 2012 through May 2013 data would reflect Seaway's costs and revenues for the first full twelve months of its post-reversal operations.[27] Thus, ACN's proposed test period of June 2012 through May 2013 is

---

[22] See Exhibit No. ACN-1 at 10:2-17; Enterprise Products Partners L.P., 139 FERC ¶ 61,099, re'hg granted, 139 FERC ¶ 61,255.

[23] ACN Initial Brief at 6; Trial Staff Initial Brief at 22-23; SCN Initial Brief at 7-12.

[24] Seaway Initial Brief at 11.

[25] 18 C.F.R. § 346.2(c) (2013).

[26] See Seaway Initial Brief at 10-11.

[27] Tr. at 408:12-16 (Wetmore Cross-examination).

consistent with the Commission's test period regulations.[28] Seaway's Initial Brief does not address or respond to ACN's proposed June 2012 through May 2013 test period.

Instead, Seaway argues that it is appropriate to analyze its filed rates based on its cost and revenues for a seven-month period, from June 2012 through December 2012.[29] Seaway proposes to truncate the test period at seven months because, according to Seaway, the purpose of this proceeding is to determine rates for what Seaway has defined as its "initial period of operations."[30] However, as explained in ACN's Initial Brief (at 7-8), the Commission's regulations do not in any way distinguish between an "initial period of operations" and any subsequent period of operations. Similarly, the Commission's regulations do not define when an "initial period of operations" ends, and another period begins. Instead, the Commission's regulations require that Seaway's filed rates be analyzed based on its costs and revenues for a full twelve-month test period.[31] Seaway's proposal to use seven months of projected costs and revenues fails to comply with the Commission's test period regulations.

As explained in ACN's Initial Brief (at 8-9), Seaway's proposal to truncate the test period to seven months also fails to take into account the increase in costs, capacity, and revenues associated with the material expansion project that went into service during the twelve-month test period in this case. If Your Honor approves Seaway's proposal to

---

[28] Exhibit No. ACN-1 at 6:4-5; 18 C.F.R. § 346.2(a) (2013).

[29] Seaway Initial Brief at 11.

[30] Id. at 11 and 15.

[31] 18 C.F.R. § 346.2(a) (2013).

calculate rates that ignore its post-expansion capacity and revenues, this will only further exacerbate the over-recoveries inherent in Seaway's proposed rates in this proceeding.

In its Initial Brief, Seaway states that it is appropriate to only calculate rates for its "initial period of operations," because the costs and volumes associated with its January 2013 expansion "were not known with precision at the time Seaway filed its direct case."[32] This argument is unavailing for four reasons. First, as SCN explained in its Initial Brief (at 10-11), "the costs that would be incurred by Seaway starting in January 2013 were no more uncertain than the June 2012 through December 2012 costs." By the time Seaway filed its direct case in this proceeding on August 2, 2012, it had already issued several press releases and circulated internal documents that detailed the costs and volumes related to the January 2013 expansion.[33] Second, elsewhere in its Initial Brief, Seaway argues that costs need not be "known with precision," if the pipeline has cost projections that were "reasonable when made."[34] Third, Seaway never stated that it <u>could not</u> develop a cost of service based on reasonable cost and revenue

---

[32] Seaway Initial Brief at 11.

[33] Exhibit Nos. SCN-46, SCN-47, SCN-48 at 11 and 17, SCN-49 (Authorization For Expenditure Request for $26 million in capital additions related to Phase II, approved April 2012), SCN-50, SCN-51 at 12, SCN-52, SCN-53, SCN-54 at 20; Tr. at 43:19-61:14 (Ordemann Cross-examination) and 321:2-323:1 (Wetmore Cross-examination).

[34] Seaway Initial Brief at 12, 32 (arguing, "[d]espite this more recent [actual] data, the original projections underlying the direct testimony remain appropriate for assessing Seaway's initial uncommitted rates because...they were reasonable when made"). Seaway's "reasonable when made" standard will be addressed in Section 4B of this reply brief.

projections for the January 2013 expansion capacity; Seaway simply chose not to do so out of its own self-interest. Fourth, the fact that Seaway did not have actual cost and revenue data for an event that occurred during the test period should not dictate the test period in this case, particularly because Seaway's actual post-expansion costs, revenues, and capacity data became available before the hearing and the close of the record in this proceeding.

Seaway relies on Exhibit No. SEA-36 to argue that a rate based on its updated data for the post-expansion period is higher than the pre-expansion rate calculated in its direct case.[35] Thus, according to Seaway, "the latest actual cost and volume data confirm the reasonableness of Seaway's original projections," and its seven-month test period is reasonable.[36] Seaway's analysis is flawed, and should be rejected. The rates on Exhibit No. SEA-36 are inflated, because they only reflect the increased costs, and not the increased capacity and revenues, associated with the 2013 expansion.

The cost of service on Exhibit No. SEA-36 exceeds Seaway's cost of service in its direct case by approximately $237,000.[37] This increase is largely due to the fact that the rate base on Exhibit No. SEA-36 includes $15 million in capital additions related to the

---

[35] Id.

[36] Seaway Initial Brief at 12.

[37] Compare Exhibit No. SEA-36 at Statement A2, line 1 with Exhibit No. SEA-24 at Statement A2, line 1.

expansion project.[38] However, Exhibit No. SEA-36 does not reflect the fact that Seaway's capacity (and thus, its revenues) tripled as a result of the January 2013 expansion.

It is true that Exhibit No. SEA-36 reflects Seaway's actual volumes shipped in January 2013. However, as explained in ACN's Initial Brief (at 50-51), Seaway experienced shutdowns and curtailments in January 2013 that render those volumes anomalous and understated.[39] Further, as discussed in Section 5 of this reply brief, Seaway's average throughput figures for June 2012 through January 2013 are not an accurate measurement of Seaway's post-expansion throughput. Exhibit No. SEA-36 is also flawed because it does not reflect the pipeline's post-expansion design capacity, which is the appropriate measurement for Seaway's throughput.[40] Thus, Seaway's argument that the updated, post-expansion data confirm the reasonableness of its direct case is misleading and based on a flawed analysis. Accordingly, this argument should

---

[38] Compare Exhibit No. SEA-36 at Statement E2, line 2 with Exhibit No. SEA-24 at Statement E2, line 2; see also Exhibit No. SCN-53 at column "Cushing Origin Pump Station" (showing approximately $15 million in capital additions associated with the new pump station that effectuated the January 2013 expansion).

[39] Tr. at 132:12-133:22 (Ordemann Cross-examination); Exhibit Nos. SCN-56 at 9, S-28 (Issued January 31, 2013, stating "[t]he curtailment order issued by Enterprise restricted flows to an average of 175,000 bpd on that final leg of the pipeline into Jones Creek," and quoting Mr. Ordemann as explaining that the Echo lateral due to be in-service before the end of 2013 "will have the ability to alleviate most of the bottlenecks we're seeing right now."), S-31 ("In the fourth quarter of 2013, Seaway expects to place into service a 65-mile lateral pipeline from Jones Creek to the Enterprise ECHO terminal in Houston, Texas.").

[40] ACN Initial Brief at 44; Seaway Initial Brief at 49.

be disregarded.

When Seaway's direct case is adjusted to take into account both the post-expansion costs and the post-expansion capacity, Seaway's calculated rate actually decreases by 66 percent.[41] Given that Seaway's per-unit cost of service is materially different for the pre- and post-expansion periods, it is appropriate to calculate two sets of rates in this proceeding, as explained in detail in ACN's Initial Brief (at 8-11).[42] SCN and Trial Staff agree with ACN's position and reasoning on this issue.[43]

In its Initial Brief (at 12-15), Seaway argues that ACN's proposal to calculate two sets of rates in this proceeding—one for the pre-expansion period, and one for the post-expansion period—is flawed because: 1) it is not appropriate to adopt two test periods; and 2) the proposal is based on the assumption that Seaway's actual volumes shipped would increase to 400,000 barrels per day in January 2013. As detailed below, Seaway's Initial Brief attacks a straw man that bears no significant resemblance to ACN's rationale for its rate proposal.

First, ACN does not propose to use "a second test period" to calculate Seaway's rates. Rather, as explained above, ACN proposes a single test period of June 2012 through May 2013. The distinction is important, because ACN's twelve-month test

---

[41] Exhibit Nos. ACN-1 at 6:2-19, ACN-5 at 3 (Ms. Crowe calculated this impact by first increasing Seaway's filed cost of service to reflect $33.9 million in capital additions associated with the expansion project, and then unit rate based on 400,000 barrels per day of capacity.).

[42] Id.

[43] SCN Initial Brief at 7-12; Trial Staff Initial Brief at 22-26.

period is consistent with the Commission's test period regulations,[44] while Seaway's proposed test period of June 2012 through December 2012 is not. Further, explained in ACN's Initial Brief (at 10-11), if Your Honor determines that it is appropriate to calculate one set of rates, the rates should reflect Seaway's cost of service and design capacity as of May 2013, the end of the twelve-month test period. This alternative proposal similarly does not rely on a "second test period." Rather, it ensures that the rates calculated in this proceeding are just and reasonable through the end of the twelve-month test period required by the Commission's regulations, and going forward.

Second, ACN did not propose to calculate two sets of rates "based on the assumption that Seaway's throughput would increase to approximately 400,000 bpd [barrels per day] in January 2013."[45] Rather, the second set of rates is required because the substantial record evidence establishes that Seaway's design capacity increased to 400,000 barrels per day in January 2013.[46] Seaway treats its design capacity and throughput as synonymous, but they are two distinct measurements. As Seaway witness Mr. Ordemann acknowledged, "[t]hroughput is the actual volume transported

---

[44] 18 C.F.R. § 346.2(a) (2013).

[45] Seaway Initial Brief at 12-13.

[46] ACN Initial Brief at 47-48; see, e.g., Exhibit Nos. S-28 at 1, SCN-10 at 2, SCN-30 at 9, SCN-46 at 1, SCN-47 at 1, SCN-50 at 1, SCN-52 at 1, SCN-54 at 20, SCN-55 at 1, SCN-56 at 3 and 5, SCN-58, SCN-68 at 5; Tr. at 83:8-17 (Mr. Ordemann admitting that Seaway is currently capable of shipping up to 417,000 barrels per day) and 144:1-21 (Mr. Ordemann admitting that in February 2013, Seaway achieved a flow rate of 380,000 barrels per day).

on a pipeline."[47] Conversely, design capacity is "the volume that a pipeline is anticipated to be able to transport during a given time period assuming uninterrupted operation as calculated based on fixed assumptions and actual data for a number of variables."[48] It is undisputed that Seaway's design capacity is the relevant measurement for calculating Seaway's rates in this case.[49]

To the extent that Your Honor determines that Seaway's actual throughput volumes are relevant, Seaway's post-expansion throughput volumes also demonstrate the need to calculate two sets of rates in this proceeding. On Exhibit No. SEA-24, Seaway calculated a rate of $6.91, based on its proposed rate design, cost of service and design capacity of 135,000 barrels per day.[50] The unit rate (cost of service divided by annual throughput) for Exhibit No. SEA-24 is $3.83.[51] Seaway's actual throughput for February 2013—the first full month its expansion facilities were in service—was 272,000 barrels per day.[52] If the throughput on Exhibit No. SEA-24 is changed to 272,000 barrels per day, and everything else stays the same, the $3.83 unit rate decreases by more than

---

[47] See Exhibit No. SCN-62.

[48] Id.

[49] See Seaway Initial Brief at 49 (stating, "the Commission has indicated that an oil pipeline's initial rates should generally be based on initial design capacity.")

[50] Exhibit No. SEA-24 at Statement A2, line 7.

[51] Id.; Exhibit No. ACN-5 at 3, line 10 (rounded to two decimal places).

[52] Tr. at 179:6-13 (Ordemann Cross-examination).

half, to $1.90.[53] In other words, using Seaway's own cost and throughput data, Seaway's per-unit cost of providing service in February 2013 was 50 percent lower than it was during the pre-expansion period.

Finally, according to Seaway, it is reasonable to calculate one set of rates for seven months of the twelve-month test period in this case, and have shippers file a complaint to establish rates that are reasonable for the remaining five months of test period, and going forward.[54] Seaway's unprecedented and extreme proposal is not grounded in the ICA or the Commission's test period regulations. In fact, the Commission's test period regulations are meaningless if a pipeline can simply choose to calculate rates based on the test period months that best serve its interests, and then argue that the burden is on the shippers to challenge the reasonableness of the rates during the other test period months. For these reasons, Seaway's seven-month test period proposal is unlawful, and should be rejected.

3. What Rate Base Or Bases Should Be Used?

For the reasons discussed below and in ACN's Initial Brief (at 11-28), the Commission's original cost ratemaking policies and Opinion No. 154-B require that the carrier property in service amount in Seaway's rate base reflect the net book value (original cost less depreciation) of the assets devoted to jurisdictional service, and any

---

[53] This figure equals the cost of service on Exhibit No. SEA-24, divided by the result of the equation 272,000 multiplied by 365, rounded to two decimal places. Using Seaway's cost of service on Exhibit No. SEA-36 produces the same $1.90 unit rate.

[54] Seaway Initial Brief at 15.

capital additions related to the capacity that is in service at the end of the test period.[55]

A. Should the purchase price related to Enbridge's acquisition of its share of Seaway be included in rate base?

Seaway's proposal to include a $1.1 billion write-up in rate base for the purchase price Enbridge paid for its 50 percent ownership in Seaway should be rejected. As explained in ACN's Initial Brief (at 12-16), the Commission's policies and precedent require that Seaway's rate base reflect the net book value of the assets devoted to jurisdictional service,[56] and "not on the value placed on the company's assets by the owners."[57] Nevertheless, Seaway proposes to include in rate base a $1.1 billion purchase price adjustment for Enbridge's purchase of its interest in Seaway. Seaway's purchase price adjustment reflects a 1,755 percent increase above the $59 million net

---

[55] ACN understood that the issue "Should Seaway's rates be calculated using a depreciated original cost or trended original cost methodology?" was stricken from the Joint Statement of Issues. Footnote 1 of the Joint Statement of Issues provides, "the issues list may change as a result of the outcome of the...motion to strike filed in the above docket on March 8, 2013." The March 8, 2013 motion to strike addressed Seaway's testimony and exhibits related to Seaway's new depreciated original cost methodology. On March 15, Your Honor granted the March 8, 2013 motion to strike. At the hearing, counsel for ACN moved to strike the issue pertaining to depreciated original cost from the Joint Statement of Issues, and Your Honor agreed that it is "not an issue in the case." Tr. at 539:22-548:1. Accordingly, if any party addresses this issue in its reply brief, that discussion should also be stricken.

[56] See, e.g., SFPP, L.P., Opinion No. 511, 134 FERC ¶ 61,121 at P 153 (2011) ("Opinion No. 511"), aff'd, SFPP, L.P., Opinion No. 511-A, 137 FERC ¶ 61,220 at P 163 (2011) ("Opinion No. 511-A"); see also, Williams Pipe Line Company, Opinion No. 154-B, 31 FERC ¶ 61,377, at 61,833 (1985) ("Opinion No. 154-B") ("[T]he Commission concludes that...a rate base methodology derived from original cost rate making models should be adopted. As the court observed, original cost is a proven `proven alternative'.") (quoting Farmers Union II, 734 F.2d at 1530).

[57] Id.; SFPP, L.P., 114 FERC ¶ 61,136 at P 17 (2006).

book value of the acquired assets.[58]

Given the magnitude of Seaway's proposed rate base write-up, this issue must be analyzed in light of the unique factual circumstances in this case. Seaway's rate base write-up proposal will have a significant and cumulative effect on its rates, because its rate base figure affects its depreciation expense, return, and income tax expenses. If Seaway's committed rates are not adjusted, including Seaway's $1.1 billion rate base write-up in its uncommitted rates will only serve to increase Seaway's already excessive returns. For this reason, and the reasons provided in ACN's Initial Brief (at 12-28) and below, Seaway's $1.1 billion purchase price adjustment should be rejected.

1) Does the Enbridge purchase meet the Commission's standards for inclusion of an acquisition premium in rate base?

Enbridge's acquisition of its interest in Seaway does not warrant an exception to the Commission's original cost ratemaking policies and precedent, as Seaway and Trial Staff argue in their Initial Briefs.[59] To qualify for an exception to the Commission's original cost ratemaking policies, the proponent of a rate base write-up first "must show that it is either converting utility assets to a new public use, or it must show that it is placing utility assets in FERC-jurisdictional service for the first time. Second, it must prove by clear and convincing evidence that the write-up will confer substantial

---

[58] Exhibit Nos. ACN-1 at 9:3-9; ACN-5 at 17.

[59] Seaway Initial Brief at 17; Trial Staff Initial Brief at 30-32. SCN did not take a position on this issue in its Initial Brief. CAPP suggested that the Commission's substantial benefits test does not apply in the instant case. CAPP Initial Brief at 2-10.

benefits on ratepayers."[60] As Trial Staff acknowledged, the Court of Appeals for the District of Columbia Circuit has called the substantial benefits test a heavy burden.[61]

In addition to meeting the substantial benefits test, the pipeline must also show that an original owner that continues to own some portion of the assets after the sale will not be unduly advantaged if the purchase price adjustment is included in rates.[62] Seaway failed to make either of the showings necessary to support its proposed $1.1 billion rate base write-up. Accordingly, Seaway's proposed rate base write-up should be denied.

As explained in ACN's Initial Brief (at 17-18), Seaway has not satisfied the first prong of the substantial benefits test, because Seaway is not providing a new or materially changed service.[63] Additionally, its proposed rate base write-up will require shippers to pay more for the same facilities that they have always used, in violation of Commission policy.[64] In its Initial Brief (17-18), Seaway argues that the instant case is "substantially the same as Enbridge Energy," where the Commission found that a

---

[60] Longhorn Partners Pipeline, 73 FERC ¶ 61,355, at 62,112 (1995)("Longhorn").

[61] Trial Staff Initial Brief at 31-32 (citing Missouri Public Service Commission v. FERC, 601 F.3d 581, 586 (D.C. Cir. 2010)).

[62] Longhorn Partners Pipeline, 82 FERC ¶ 61,146 at 61,543-44 (1998); Longhorn, 73 FERC at 62,113; see also, Rio Grande Pipeline Company, 178 F.3d 533, 543 (D.C. Cir. 1999) ("Rio Grande") (finding, "the Commission might decide that a per se rule or even a substantially more rigid version of the benefits test is appropriate based on reasoned findings regarding affiliate transactions.").

[63] Exhibit No. ACN-1 at 13:10-18.

[64] Exhibit Nos. ACN-1 at 13:19-14:8, ACN-13; Tr. at 135:4-24 (Ordemann Cross-examination); Millennium Pipeline Company, L.L.C., 117 FERC ¶ 61,319 at P 169 (2006).

pipeline reversal project satisfied the first prong of the substantial benefits test.[65] Enbridge Energy is distinguishable from the instant case in two material ways.

First, in Enbridge Energy, the Commission applied an exception to its policy of denying acquisition adjustments when they cause the pre-acquisition shippers to pay higher rates for the same facilities after the acquisition. Specifically, the Commission found that all of the overlapping shippers assented to pay higher rates for service on the same facilities, because they were committed shippers who "expressly acknowledge[d] their support" for the project and signed transportation service agreements reflecting the higher rates.[66] That is not the case here. In fact, **[BEGIN HIGHLY CONFIDENTIAL INFORMATION]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** shippers that, to date, have shipped on both the pre- and post-reversal Seaway are uncommitted shippers that will pay the rate that results from this proceeding.[67] Thus, Seaway's proposed rate base write-up, if approved, would require them to pay a higher rate for the same facilities, in violation of Commission policy.

Second, in Enbridge Energy, a remaining owner did not stand to gain an

---

[65] See Enbridge Energy Company, Inc., 110 FERC ¶ 61,211 at PP 29-30 (2005) ("Enbridge Energy").

[66] Id. at P 30.

[67] Tr. at 135:4-24 (Ordemann Cross-examination); Exhibit Nos. ACN-1 at 13:19-14:8, ACN-13, SEA-40 (listing **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** as uncommitted shippers).

unreasonable and unjustified windfall from including the purchase price adjustment in rates. Significantly, in that case, the Commission conditioned its approval of the write-up on the requirement that the original owner "will not hold any equity or other interest in the new pipeline at the time service commences."[68] Here, Enterprise—one of the original owners of Seaway—retained its 50 percent interest in the pipeline. As explained in ACN's Initial Brief (at 14-17), including the write-up in Seaway's rate base will afford Enterprise a return of and on a $585 million investment, while its actual investment in Seaway is only $59 million.[69] Enterprise stands to gain this excessive windfall solely due to the fact that Enbridge paid a large sum of money to become Enterprise's co-owner in Seaway. This is precisely the situation that the Commission sought to avoid in Enbridge Energy.[70]

As explained in ACN's Initial Brief (at 18-22), Seaway does not meet the second prong of the substantial benefits test, because Seaway did not meet its burden of establishing through "clear and convincing evidence that the acquisition provides substantial, quantifiable benefits to ratepayers."[71] Seaway and Trial Staff argue that Enbridge's purchase of its interest in Seaway was less costly than building a new

---

[68] Enbridge Energy, 110 FERC ¶ 61,211 at P 33 (citing Rio Grande Pipeline Company, 78 FERC ¶ 61,020 (1997) , and Longhorn, 73 FERC ¶ 61,355

[69] Tr. at 402:9-18 and 404:5-13 (Wetmore Cross-examination).

[70] Enbridge Energy, 110 FERC ¶ 61,211 at P 33.

[71] See Longhorn, 73 FERC at 62,112.

greenfield pipe.[72] Even if this statement were true (which, it is not), it is irrelevant. The Seaway pipeline was already built and providing crude oil pipeline service, so Seaway did not need to acquire idle facilities or construct a new pipeline in order to effectuate the reversal.[73] Additionally, as explained in ACN's Initial Brief (at 19-20), the fact that Seaway could construct a new pipeline with up to 450,000 barrels per day of capacity for $1.32 billion[74] does not establish that Enbridge saved Seaway's shippers money by purchasing a 50 percent interest in a smaller pipeline for $1.1 billion.

Seaway also argues that Enbridge's purchase enabled the reversed pipeline to go into service before a newly constructed pipeline would have been in service, which provided a monetary benefit to its shippers.[75] First, as explained above, Seaway already owned the pipeline facilities that now provide southbound service. Enbridge did not have to purchase or construct any pipeline facilities to effectuate the reversal; Seaway merely had to reverse the flow on its existing pipeline facilities. Thus, it is not appropriate to ascribe any benefit associated with the in-service date of the reversed pipeline to Enbridge's purchase of its interest in Seaway.

Second, Seaway relies on a fatally flawed analysis in Exhibit No. SEA-28 to argue

---

[72] Seaway Initial Brief at 20; Trial Staff Initial Brief at 31-32.

[73] See ACN Initial Brief at 18-19; Enbridge Pipelines (KPC), 100 FERC ¶ 61,260, at 61,938-39 (2002) (holding that where an entity does not choose between constructing a new pipeline and acquiring and converting a pipeline to effectuate the service in question, "the alleged savings in construction costs are not relevant."), reh'g denied, 102 FERC ¶ 61,310 (2003), aff'd, 109 FERC ¶ 61,042 (2004).

[74] See Exhibit Nos. SEA-26 at 13:8-10, SEA-42, SCN-54 at 4 and 20, SCN-68 at 11.

[75] Seaway Initial Brief at 21 (citing Exhibit No. S-28).

that its shippers will receive a substantial monetary benefit from the acquisition. As explained in ACN's Initial Brief (at 20-21), the rates used to calculate the supposed "economic benefit" on Exhibit No. SEA-28 are significantly lower than the $6.91 and $8.09 rates that Seaway calculated to include the $1.1 billion rate base write-up.[76] As the Commission recently held, to satisfy the substantial benefits test, "the pipeline must show clear and convincing evidence that its acquisition of the facilities will provide substantial, quantifiable benefits to ratepayers <u>even if the full purchase price</u>, including the portion above depreciated original cost <u>is included in rate base</u>."[77] Seaway did not calculate its supposed economic benefits using a rate that included its $1.1 billion purchase price adjustment. Thus, its analysis is fatally flawed and should be rejected.

Additionally, the netback analysis on Exhibit No. SEA-28 only shows that Seaway's average filed rates are lower than the differential between its origin and destination markets, which should be true for all economically viable crude oil pipelines.[78] Finally, the economic benefits shown on Exhibit No. SEA-28 are speculative. When applying its substantial benefits test, the Commission has held that "[t]he benefits

---

[76] Exhibit Nos. SEA-26 at 54:18-55:6, SEA-28 at column "Average Transportation Tariff."

[77] <u>Missouri Interstate Gas, LLC</u>, 142 FERC ¶ 61,195 at P 61 (2013) ("<u>Missouri Interstate</u>") (emphasis added).

[78] <u>See</u> Seaway Initial Brief at 21 (arguing that Seaway's shippers benefited from Enbridge's purchase of its interest in Seaway because "the differential is significantly greater than Seaway's tariff.").

must be tangible and non-speculative."[79] Seaway's analysis is speculative, because Seaway admits that the results are driven by the price differential between Seaway's origin and destination markets,[80] which Seaway estimates for ten of the 18 months shown on Exhibit No. SEA-28.[81] Seaway did not provide any explanation or support for its estimated price differential, and Seaway admits that the actual differential for those months may be smaller.[82] Thus, Seaway has failed to meet its heavy burden of "prov[ing] by clear and convincing evidence that the write-up will confer substantial benefits on ratepayers."[83]

Seaway and Trial Staff also point to supposed qualitative benefits to argue that Enbridge's purchase meets the Commission's substantial benefits test.[84] Trial Staff cites to Missouri Interstate to argue that it is not necessary "to produce an exact dollar amount of savings" to meet the substantial benefits test.[85] But in that case, the Commission stated that the pipeline must show "that its acquisition of the facilities will

---

[79] See, e.g., Mid-Louisiana Gas Company, 7 FERC ¶ 61,316, at 61,684 (1979).

[80] Id. (stating, "shippers as a whole received an aggregate net benefit of approximately $441 million … given the significant price differential during that period.").

[81] Exhibit No. SEA-28 at 1, lines 9-10, column "Gross Price Differential."

[82] Seaway Initial Brief at 21-22 (acknowledging that the differential could narrow, which would affect Seaway's analysis on Exhibit No. SEA-28).

[83] Longhorn, 73 FERC at 62,112.

[84] Seaway Initial Brief at 22; Trial Staff Initial Brief at 31-32.

[85] Trial Staff Initial Brief at 31-32 (citing Missouri Interstate, 142 FERC ¶ 61,195 at P 61).

provide substantial, quantifiable benefits to ratepayers."[86] In another case, the Commission held that "[t]he benefits must be tangible and non-speculative and must be quantifiable in monetary terms."[87] Thus, Trial Staff and Seaway's supposed qualitative benefits are not sufficient to meet the Commission's substantial benefits test.

Finally, all of Seaway's arguments attribute the benefits of Seaway's pipeline reversal project to Enbridge's purchase of its 50 percent interest in Seaway. But Seaway already owned the pipeline facilities that allowed the reversal project to go forward. Enbridge merely bought into that existing entity. Thus, it was Seaway's ownership of existing pipeline facilities, and not Enbridge's acquisition of its interest in Seaway, that made the reversal possible.

Seaway witness Mr. Bradley Shamla, an employee of Enbridge, provided unsupported, unsubstantiated testimony that ConocoPhillips Company ("ConocoPhillips") would not have agreed to reverse Seaway, because ConocoPhillips owned a refinery in Cushing, Oklahoma that was served by the northbound Seaway transportation service.[88] Thus, according to Seaway, it was necessary for Enbridge to buy out ConocoPhillips in order to effectuate the reversal.[89]

Seaway's logic is flawed and its assertions are not supported with credible, substantial evidence. It is nonsensical to suggest that ConocoPhillips would not agree to

[86] Missouri Interstate, 142 FERC ¶ 61,195 at P 44 (emphasis added).
[87] Mid-Louisiana Gas Company, 7 FERC ¶ 61,316, at 61,684 (emphasis added).
[88] Exhibit No. SEA-25 at 3:18-4:2.
[89] Id.; Seaway Initial Brief at 30.

reverse Seaway because it needed the pipeline to supply its refinery in Cushing, when ConocoPhillips later relinquished its control of Seaway. Further, Mr. Shamla admitted that ConocoPhillips sold its refinery in Cushing, and **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS].**[90] Additionally, as an employee of Enbridge, Mr. Shamla is not qualified to testify to ConocoPhillips' internal business decisions or intentions. In sum, Seaway has not provided substantial record evidence that establishes that the pipeline would not have been reversed absent Enbridge's purchase of its interest in Seaway for $1.1 billion. Thus, it is not appropriate to conflate the benefits of the reversal with Enbridge's purchase of its interest in Seaway.

2) Should a portion of the purchase price attributable to goodwill be included in rate base?

For the reasons explained in ACN's Initial Brief (at 11-22) and Section 3A(1) of this reply brief, Seaway's rate base should reflect the net book value of the Seaway facilities, and should not include any portion of the $1.1 billion purchase price adjustment proposed by Seaway.[91] However, if any portion of the proposed write-up is

---

[90] Id.; Exhibit Nos. ACN-13; SEA-40.

[91] Trial Staff's Initial Brief (at 26) states, "ACN and Staff reached a stipulation of fact that is an agreement as to the appropriate amount of total estimate book value for Enbridge's purchased 50 percent interest in Seaway." Additionally, the Canadian Association of Petroleum Producers' Initial Brief (at 20) states, "*ACN* proposes to recognize only a portion of the Enbridge Acquisition Cost to jurisdictional services, using a somewhat different methodology than Seaway and also excluding costs attributable to good will." These statements are not entirely accurate, and describe

allowed, then Seaway's rate base should only include the purchase price attributable to Seaway's jurisdictional assets. ACN, Trial Staff, and SCN all agree that the goodwill associated with the acquisition should not be included in Seaway's rate base.[92]

Seaway admits that goodwill "represents the excess cost of the acquired company over the sum of the amounts assigned to all identifiable assets acquired and liabilities assumed."[93] In this case, the record demonstrates that Enbridge's $1.15 billion total purchase price includes an amount for the acquired assets themselves, and also $627 million for goodwill.[94]

In its Initial Brief, Seaway erroneously argues that the goodwill portion of the purchase price should be included in rate base because, "the Commission and the courts have made clear that when the Commission's two-part test is met, the pipeline is entitled to recover the 'full purchase price of an acquired asset in its cost-of-service

---

ACN's alternative proposal, which would only apply if Your Honor finds that Seaway should be granted an exception to the Commission's original cost ratemaking policies.

[92] ACN Initial Brief at 22-24; Trial Staff Initial Brief at 32-35; SCN Initial Brief at 15-23.

[93] Seaway Initial Brief at 23 (quoting Ameren Corp., 140 FERC ¶ 61,034 at n.1 (2012)) (internal quotations ommitted).

[94] See ACN Initial Brief at 22-24; Exhibit Nos. ACN-7, ACN-42.

computations.'"[95] But the cited cases do not support Seaway's argument that goodwill should be included in rate base. In fact, the cited cases clearly state that when a purchase price write-up is allowed, the cost of the purchased asset will be allowed in rate base.[96] Because goodwill is the price paid in excess of the cost of the purchased asset,[97] goodwill, therefore, should not be included in rate base.

Seaway cites to Ameren Corp. to argue that "the Commission has held that goodwill may be recovered along with [the] rest of the purchase price where the Commission's two-part test is met."[98] Seaway's statement is misleading and incorrect. In fact, in Ameren Corp., the Commission denied the pipeline's request to write-up its rate base to reflect a purchase price adjustment.[99] Notably, Seaway could not cite to a single case where the Commission has expressly allowed a pipeline to include goodwill in rate base upon meeting the substantial benefits test. Moreover, the Commission's oil pipeline precedent acknowledges that a purchase price adjustment (the price paid for the fair market value of the acquired assets) and goodwill (all other amounts) are two

---

[95] Seaway Initial Brief at 22-23 (quoting Rio Grande, 178 F.3d at 542; citing Kinder Morgan Pony Express Pipeline LLC, 141 FERC ¶ 61,180 at P 56 (2012) (the Commission applies the substantial benefits test to determine whether to permit a "purchased asset to be included in the rate base at the full purchase price."); Enbridge Pipelines (Southern Lights) LLC, 121 FERC ¶ 61,310 at P 35, 38 (2007) (the Commission applies the substantial benefits test to determine whether to permit a "purchased asset to be included in the rate base at the full purchase price") (internal quotations ommitted)).

[96] Id.

[97] See Seaway Initial Brief at 22-23.

[98] Id. (citing Ameren Corp., 140 FERC ¶ 61,034, at n.1 and P 30 (2012)).

[99] Ameren Corp., 140 FERC ¶ 61,034, at n.1 and P 30.

separate and distinct concepts, and are treated as such for accounting and ratemaking purposes.[100]

Seaway also argues that "the full purchase price, including the amount attributable to goodwill, was necessary to complete the purchase and make the benefits of the new service possible."[101] But Seaway did not provide evidence to support its position that the reversal project only happened because Enbridge paid ConocoPhillips $627 million for goodwill. In lieu of providing evidence to support its position, Seaway argues that there is "no basis to assume that the purchase would still have occurred if Enbridge had offered to pay only the approximately $527 million attributable to the…identifiable tangible assets."[102] Seaway's attempt to shift the burden to shippers to prove a negative (that the reversal would not have happened if Enbridge only paid ConocoPhillips $527 million) should be disregarded. As the proponent of the rate base write-up, Seaway has the burden of proving, with substantial record evidence, that the factual basis for its arguments is true and accurate.

Finally, as explained in ACN's Initial Brief (at 23-24), the record in this case establishes that Enbridge paid ConocoPhillips $627 million in goodwill for a future

---

[100] Opinion No. 511, 134 FERC ¶ 61,121 at PP 153-154 (stating, "the Commission finds that it is inappropriate to adjust KMEP's capital structure for either goodwill or the PAAs at issue in this proceeding."); SFPP, L.P., 111 FERC ¶ 61,334 at P 68 (2005) (explaining that goodwill and the fair market value of the acquired assets are treated differently under the Commission's Uniform System of Accounts for oil pipelines.)

[101] Seaway Initial Brief at 25.

[102] Id.

economic benefit related to an upstream pipeline expansion that will accrue to Enbridge, and not Seaway's current shippers.[103] Thus, if any portion of Seaway's proposed purchase price write-up is included in rate base, amounts associated with goodwill should be excluded.

3) What portion of the purchase price should be attributed to the Longhaul 30-inch System and what portion should be attributed to the other assets?

If any portion of Seaway's proposed write-up is allowed, only the purchase price attributable to Seaway's jurisdictional assets should be included in rate base. No party disputes that a regulated entity may only include in rates the cost of assets that are used and useful in the provision of jurisdictional service.[104] It is also undisputed that Enbridge paid approximately $1.15 billion to purchase an ownership interest in Seaway's jurisdictional and non-jurisdictional assets.[105] Thus, if the purchase price write-up is allowed, the purchase price attributable to the non-jurisdictional assets must be excluded from Seaway's rates in this proceeding.

Seaway proposes to allocate approximately $55 million, or five percent, of the

---

[103] Tr. at 200:10-14, 202:11-204:7, 209:4-10, 218:7-219:11, and 234:8-23 (Shamla Cross-examination); Exhibit No. SCN-35 at 22:1-24:18.

[104] See Seaway Initial Brief at 17; Tennessee Gas Pipeline Company v. FERC, 606 F.2d 1094, 1109 (D.C. Cir. 1979).

[105] Seaway Initial Brief at 17; Exhibit Nos. ACN-7, ACN-35. Seaway's jurisdictional assets are known as the 30-Inch Longhaul System. The non-jurisdictional facilities are known as the Freeport, Texas City, and Galena Park Systems. Exhibit No. SEA-1 at 4:1-13.

full $1.15 billion purchase price to the non-jurisdictional Seaway assets.[106] As explained in ACN's Initial Brief (at 25-28), Seaway's proposal is arbitrary and unsupported by the record, and should be rejected in favor of using Enbridge's own internal assessment of the actual cost of the jurisdictional facilities. SCN and Trial Staff agreed with ACN on this issue.[107]

Seaway relied on Mr. Shamla's discredited "analysis of the revenues projected to be derived from the other assets relative to the overall revenues to be derived from the Seaway assets as a whole" to allocate $55 million of the purchase price to the non-jurisdictional assets.[108] At hearing, Mr. Shamla was unable to answer any substantive questions regarding the assumptions or calculations underlying this study, and admitted that he did not perform the study.[109] Further, Seaway witness Mr. Wetmore performed a similar analysis using the same discredited study, but Mr. Wetmore determined that the non-jurisdictional assets have an economic value based on stand-alone revenues of $98 million.[110]

---

[106] See Exhibit No. ACN-1 at 19:1-15.

[107] See Trial Staff Initial Brief at 35 (citing Exhibit No. ACN-42, which is based on Exhibit No. ACN-7); SCN Initial Brief at 21-23.

[108] Seaway Initial Brief at 26 (citing Exhibit No. SEA-25 at 5).

[109] Tr. at 230:10-232:9 (Shamla Cross-examination) (answering that he did not perform the analysis on which he relied, he did not know for sure who performed the analysis, he did not know how the overall revenues were calculated, and he did not know how the non-jurisdictional revenues were calculated, but he did know that the study was performed after Enbridge purchased its interest in Seaway and in preparation for his testimony in this case.).

[110] Exhibit Nos. SEA-26 at 28:5-29:2, SEA-30.

Even assuming that Seaway provided some explanation or support for the study underlying Mr. Wetmore and Mr. Shamla's analyses, the analyses themselves are flawed. Mr. Wetmore and Mr. Shamla's both attempt to allocate the purchase price to Seaway's non-jurisdictional assets based on a highly subjective forecast of anticipated revenues. This is inappropriate, because the record contains evidence of Enbridge's own objective assessment of the cost of the non-jurisdictional assets.

The Commission will rely on the acquiring company's own documentation, in lieu of adopting subjective, arbitrary allocations, to determine the purchase price attributable to acquired assets.[111] Enbridge's own accounting entries demonstrate that the fair value of Enbridge's share of the non-jurisdictional assets is $196,058,000.[112] Thus, the purchase price attributable to Seaway's jurisdictional 30-Inch Longhaul System, exclusive of goodwill, is $331,351,000.[113] If Seaway is permitted to include a purchase price adjustment in it rate base, that adjustment should not exceed $331,351,000.

Finally, Seaway admitted that its proposal to assign $55 million to the non-jurisdictional assets has the effect of assigning 100 percent of the acquisition premium (the purchase price paid in excess of the net book value of the acquired assets) to the

---

[111] Missouri Interstate, 142 FERC ¶ 61,195 at PP 78-79, 85-86.

[112] Exhibit Nos. ACN-7, ACN-35, ACN-42 at Stipulation 1 (summing Enbridge's share of the Texas City System figures, the Freeport System figures, and the Galena Park and Other figures on the first page of ACN-42). At hearing, Exhibit No. ACN-42 was designated as "Highly Confidential," but counsel for Seaway contacted counsel for ACN and Trial Staff and waived the confidentiality of the information on the first two pages of this exhibit.

[113] Id. (ACN-42 shows the derivation of the $331,351,000 figure).

jurisdictional assets.[114] According to Seaway, this is appropriate because: 1) "[t]he primary value of the Seaway assets was associated with the Longhaul 30-inch System;" and 2) "the purchase and the reversal of the [jurisdictional facilities] results in the new use and benefits to shippers."[115]

Neither of Seaway's rationales support assigning the full acquisition premium to the jurisdictional assets. Regarding Seaway's first point, the record evidence shows that Enbridge valued the jurisdictional assets at approximately $331.4 million, and valued the non-jurisdictional assets at $196 million.[116] Thus, while it is true that Enbridge attributed a higher value to the jurisdictional assets, this fact does not support assigning anything other than $331.4 million to the jurisdictional assets.

Seaway's second point amounts to little more than an argument that a pipeline should be entitled to include costs that are otherwise attributable to non-jurisdictional assets in its jurisdictional rates, so long as the pipeline owns and operates jurisdictional assets for the benefit of its shippers. This argument is contrary to the basic ratemaking principle that a pipeline is only allowed the opportunity to recover a return of and on its investment in facilities that are used and useful in the provision of jurisdictional service, and should be rejected.[117]

In conclusion, for the reasons stated in this Section 3, Seaway should not be

---

[114] Seaway Initial Brief at 26-27.

[115] Id.

[116] Exhibit Nos. ACN-7, ACN-35, ACN-42 at Stipulation 1.

[117] See, e.g, Tennessee Gas Pipeline Company v. FERC, 606 F.2d 1094, 1109.

permitted to include a write-up in excess of the net book value of its jurisdictional assets in rate base. However, if any write-up is permitted, the rate base amounts attributable to Enbridge's 50 percent interest in Seaway should not exceed $331,351,000.

4) If the purchase price is included in rate base, should a portion of that amount be allocated to the expansion capacity and services of the pipeline?

ACN does not take a position on this issue.

4. What Are The Appropriate Cost Allowances To Be Included In The Cost Of Service?

A. What is the appropriate allowance for funds used during construction?

As demonstrated in ACN's Initial Brief (at 28-32), Seaway should only be permitted to accrue an allowance for funds used during construction ("AFUDC") on its "investment in actual new incremental plant under construction."[118] Seaway's proposal to accrue AFUDC on both Enterprise's share of Seaway's existing pipeline facilities, and the proposed $1.1 billion write-up for Enbridge's purchase of its interest in Seaway, should be rejected.

Seaway cites Opinion No. 351 to argue that "AFUDC is not limited solely to the cost of construction activities."[119] Seaway's argument mischaracterizes the law, and should be rejected. First, in another oil pipeline case, the Commission expressly held

---

[118] Exhibit No. ACN-1 at 16:19-17:9.

[119] Seaway Initial Brief at 30 (citing ARCO Pipe Line Company, Opinion No. 351, 52 FERC ¶ 61,055, at 61,234 (1990)("Opinion No. 351"), affirmed in pertinent part, Opinion No. 351-A, 53 FERC ¶ 61,398 (1990)).

that "[t]he Commission's regulations for accruing AFUDC focus on the construction activity."[120] Second, contrary to Seaway's mistaken belief, Opinion No. 351 requires that Seaway's AFUDC calculations be rejected.

In Opinion No. 154-B, a case that preceded Opinion No. 351, the Commission held that oil pipelines are permitted to include an allowance for funds used during construction in rate base.[121] In Opinion No. 351, the Commission found that this holding in "Opinion No. 154-B applied only to new plant."[122] Thus, Opinion No. 351 makes clear that oil pipelines may only accrue AFUDC on costs incurred to construct new plant. Seaway's proposal to accrue AFUDC on existing plant, and the purchase price Enbridge paid to acquire its interest in Seaway, is thus inconsistent with Opinion No. 351.

Notably, Seaway did not point to a single case where the Commission has held that an oil pipeline may accrue AFUDC on the net book value of existing facilities for which the construction period has ended. Seaway is also unable to cite to a single case where the Commission has held that a pipeline may accrue AFUDC on the price paid to acquire an interest in a regulated entity. This is because an oil pipeline is only allowed to accrue AFUDC on the costs it records as construction work in progress

---

[120] Kuparuk Transportation Company, 55 FERC ¶ 61,122, at 61,372 (1991).

[121] Opinion No. 154-B, 31 FERC ¶ 61,377 at n.38.

[122] Opinion No. 351, 52 FERC at 61,235; see also, Trans-Elect NTD Path 15, LLC, 117 FERC ¶ 61,214, at 62,135 (2006) ("The Commission's AFUDC method compensates the stockholders of a regulated utility for the pre-operational cost of funds invested in a new plant prior to the time the plant actually goes into service") (emphasis added).

("CWIP"),[123] and neither the net book value of existing facilities nor the purchase price paid for a partnership interest constitute CWIP.

The Commission's Uniform System of Accounts for oil pipelines defines CWIP as:

> the cost of carrier property under construction [which] includes interest and taxes during construction, material and supplies delivered to the construction site, and other expenditures that will eventually be part of the cost of the completed property....When part of a project under construction is completed and put into service, the costs applicable to that portion shall be transferred to the appropriate property account.

Seaway's proposal to include in CWIP the depreciated original cost of its existing pipeline facilities is inconsistent with the Commission's Uniform System of Accounts in two ways. First, the construction period for the existing facilities has long since ended. Therefore, the existing facilities do not constitute "carrier property under construction." Second, the Uniform System of Accounts provides that when the new facilities are put into service, their costs must be transferred out of CWIP. Because the existing pipeline facilities went into service when Seaway originally began providing northbound service, their costs are not properly included in CWIP. Seaway also proposes to accrue AFUDC on the purchase price paid for Enbridge's partnership interest, which in no way constitutes "the cost of carrier property under construction." In sum, Seaway's proposal to accrue AFUDC on costs that are not properly included in CWIP should be

---

[123] This point is not disputed. See Seaway Initial Brief at 29.

rejected.

Seaway also argues that its AFUDC proposal is reasonable because "the pipeline needs to have an opportunity to earn a reasonable return on its investment."[124] But Enterprise has already recovered AFUDC for its existing facilities through the rates charged since it originally went into service.[125] Enbridge also collected revenues associated with service on the pre-reversal Seaway.[126] Thus, Seaway's owners have not been denied an opportunity to earn a reasonable return on their investment. Rather, Seaway's AFUDC proposal would permit its owners to double-recover their debt and equity costs, and should be rejected.

Finally, Seaway argues at length that Enbridge's acquisition costs were "necessary," and "the AFUDC associated with the Enbridge purchase is significantly less than what the AFUDC would have been if a greenfield pipeline from Cushing to the Gulf Coast had been constructed."[127] These arguments are irrelevant, and should be disregarded. The Commission does not apply a "necessary" or "economic benefits" test to determine whether a pipeline can accrue AFUDC. Rather, the Commission will determine whether the costs constitute CWIP, in that they were incurred during the

[124] Seaway Initial Brief at 30.

[125] ACN Initial Brief at 30; Exhibit No. ACN-1 at 3:1-4 and 17:10-16.

[126] ACN Initial Brief at 31-32; Exhibit Nos. ACN-1 at 17:12-16 and 18:14-18, ACN-14.

[127] Seaway Initial Brief at 30-31.

construction period[128] and were related to the construction of new plant.[129] If the answer to those questions is no, as is the case here, AFUDC is not permitted. Assuming, arguendo, that the Commission applies Seaway's rate base-type analysis to determine whether costs are properly included in CWIP, Seaway has not demonstrated with substantial record evidence that Enbridge's purchase of its interest in Seaway was "necessary" to effectuate the reversal. Seaway also failed to demonstrate that Enbridge's purchase provided any cost savings to shippers.

B. What is the appropriate level of operating expense?

As explained in ACN's Initial Brief (at 32-37), Seaway's proposal to use cost projections for the period June 2012 through December 2012 is inconsistent with the Commission's test period ratemaking regulations and policies, subjective, arbitrary, and overstates Seaway's operation and maintenance ("O&M") expenses. Moreover, Seaway's allocation of administrative and general ("A&G") costs to the 30-Inch Longhaul System is flawed.

Seaway argues that its projections should be adopted because they were "reasonable when made."[130] As an initial matter, the Commission only applies the "reasonable when made" standard to analyze electric public utilities' Period II rate

---

[128] See, e.g., Chandeleur Pipeline Company, 50 FERC ¶ 61,148, at 61,439 (1990) (stating, "CWIP treatment is available only during that period when construction is actually in progress.").

[129] Opinion No. 351, 52 FERC at 61,235; see also, Trans-Elect NTD Path 15, LLC, 117 FERC ¶ 61,214, at 62,135.

[130] Seaway Initial Brief at 32.

filings.[131] This is because the Commission has indicated its strong preference for actual data over forecasts.[132] Thus, it is not appropriate to apply the "reasonable when made" standard to Seaway's projections. Rather, Seaway's O&M expenses should reflect twelve months of actual cost data, as ACN argued in its Initial Brief (at 32-37).

Assuming, arguendo, that the "reasonable when made" standard applies, Seaway has not demonstrated that its O&M projections were reasonable when made. The Court of Appeals for the District of Columbia Circuit has made clear that the Commission must consider actual cost data in the record when analyzing whether cost projections were reasonable when made.[133] The Commission should also determine whether it is appropriate to adopt the company's projections because "unusual or unique occurrences" render the actual data unreliable.[134]

Seaway's actual cost data and internal documents demonstrate that Seaway's

---

[131] See Chatham & Riverton, Illinois v. FERC, 662 F.2d 23, 28-30 (D.C. Cir. 1981) (citing 18 C.F.R. § 35.13(d)(2)); Trunkline Gas Company, 90 FERC ¶ 61,017, at 61,047 (2000); Williston Basin Interstate Pipeline Company, 87 FERC ¶ 61,265, at 62,021 (1999) ("[T]he reasonable when made standard is not applied in natural gas pipeline rate cases.").

[132] See, e.g., Opinion No. 511, 134 FERC ¶ 61,121 at PP 28-29; Transcontinental Gas Pipe Line Corp., 11 FPC 94, 106 (1952) (rejecting estimates of costs as based on speculation, and requiring claimed costs to be based on actual costs); Williston Basin Interstate Pipeline Company, 76 FERC ¶ 61,066, at 61,384 (1996) (noting that the Commission has found that actual costs during the test period generally reflect the best evidence of what a company can expect to incur in the future).

[133] Chatham & Riverton, Illinois v. FERC, 662 F.2d at 28-30 (citing Filing of Electric Service Tariff Changes, 50 FPC 125, 127 (1973), aff'd sub nom. American Public Power Association v. FPC, 522 F.2d 142 (D.C. Cir. 1975)).

[134] Id.

projections were not "reasonable when made." Seaway projected that its O&M expense would be approximately $20.3 million.[135] As explained in ACN's Initial Brief (at 33-34), Seaway's proposed O&M expense is double the amount of O&M expense that Seaway recorded in 2011.[136] Seaway's O&M expense is also double the amount that Seaway's own internal projections showed for the reversed pipeline for 2012.[137] Seaway did not explain why its projections in this case deviated so substantially from its 2011 actual data and its own budgeted amounts.

Seaway argues that Exhibit No. SEA-34 shows that the actual June 2012 through January 2013 O&M expenses (annualized) are approximately $19.5 million. Thus, according to Seaway, the actual cost data confirm the reasonableness of its original $20.3 million projection.[138] But Seaway's actual cost data analysis on Exhibit No. SEA-34 is flawed, and should be disregarded.

First, Seaway admits that Exhibit No. SEA-34 includes at least $1.66 million in A&G costs that are attributable to Seaway's non-jurisdictional operations, and should be excluded from its cost of service.[139] Significantly, ACN demonstrated that even this $1.66 million reduction is too low, and only 38 percent of the shared A&G expenses

---

[135] Exhibit No. SEA-24 at Statement B, line 19.

[136] Exhibit Nos. ACN-1 at 24:5-7, ACN-15, ACN-19.

[137] Id.

[138] Seaway Initial Brief at 33 (citing Exhibit No. SEA-34).

[139] Exhibit Nos. ACN-36 (whereby Seaway admits that at least $1.66 million should be allocated to Seaway's non-jurisdictional operations), SEA-41 at column "Adjustment to G&A," line 19; Tr. at 409:12-411:6 (Dalhoff Cross-examination).

should be allocated to Seaway's jurisdictional services.[140]

Second, Exhibit No. SEA-34 erroneously includes $3.9 million for "Oil Losses and Shortages."[141] Seaway recovers its costs for oil losses and shortages from its shippers in-kind, through a Pipeline Loss Allowance mechanism in its tariff.[142] In fact, Seaway over-collected $2.6 million from its shippers for its oil losses and shortages during the test period, because it collected more oil from shippers than was necessary to cover its losses.[143] Once Seaway's understated A&G allocations and the Oil Losses and Shortages costs are excluded from Exhibit No. SEA-34, Seaway's actual O&M expenses are approximately $13.9 million, which is significantly lower than Seaway's projected $20.3 million O&M expenses.

Seaway's $25.5 million O&M projections through May 2013 include the same flawed actual cost data as its $19.5 million O&M figure.[144] Additionally, Seaway has provided no evidentiary support for its approximately $6.87 million in O&M adjustments for February through May 2013.[145] Finally, as Trial Staff explained in its Initial Brief (at 43), Seaway has not shown that the projected ad valorem taxes of $5.1

---

[140] ACN Initial Brief at 34-36 (citing Opinion No. 511, 134 FERC ¶ 61,121 at PP 142, 148-50); Exhibit Nos. ACN-1 at 20:1-21:4, ACN-15.

[141] See Exhibit No. SEA-34 at 1, line 5

[142] Tr. at 347:15-348:10 (Wetmore Cross-examination); Exhibit No. SCN-72.

[143] Id.; see also Exhibit No. SCN-73; Tr. at 350:12-351:15 (Wetmore Cross-examination).

[144] See Exhibit No. SEA-34 at 2, note 1 and line 5.

[145] Id. at columns "Adjustment No. 6" and "Adjustment No. 7" (referring to Exhibit No. SEA-39, where Mr. Ordemann's simply states that Seaway projected that it will incur the costs shown on Exhibit No. SEA-34).

million reflect only those taxes associated with the jurisdictional facilities that were in service at the end of the test period.

In sum, Seaway has failed to establish that O&M projections were "reasonable when made." Thus, Seaway's O&M expenses on Exhibit No. SEA-34 should be rejected in favor of using ACN's actual 2011 O&M expense of $8.9 million.[146]

C. What is the appropriate level of depreciation expense?

ACN supports the position taken by Trial Staff in their testimony, exhibits, and Initial Brief on this issue.

D. What is the appropriate cost of capital?

As demonstrated in ACN's Initial Brief (at 37-42), Seaway's overall weighted average cost of capital should be 6.90%, which reflects a debt to equity ratio of 61% to 39%, a debt cost of 5.01%, and a nominal return on equity ("ROE") of 11.28%.[147] Trial Staff, CAPP, and ACN generally agree on the proper method for calculating Seaway's return, with some differences owing to timing and proposed adjustments to the financial data.

Seaway argues that its return should be "based on financial data and reflect capital market conditions and investor expectations generally corresponding to the time Seaway's initial rates took effect."[148] Thus, Seaway argues that it is appropriate to use

---

[146] See ACN Initial Brief at 32-37.
[147] Exhibit Nos. ACN-1 at 21:7-22, ACN-21 at 5, line 14.
[148] Seaway Initial Brief at 39 (internal quotations ommitted).

the data submitted with its direct case to analyze its return, and not the updated data (which produce a lower return) in its rebuttal case.[149]

Contrary to Seaway's assertions, "the Commission prefers the most recent financial data in the record for calculating a pipeline's ROE."[150] This is because "the market is always changing and later figures more accurately reflect current investor needs."[151] Seaway did not provide any compelling reason or precedential support for its position that its return should be calculated to reflect investor expectations at the time Seaway's rates took effect.[152] Therefore, it is appropriate to calculate Seaway's return based on the most recent data in the record.

1) What is the appropriate capital structure?

It is appropriate to develop Seaway's capital structure by averaging the capital structures of Enbridge and Enterprise, Seaway's owners, because Seaway does not provide its own financing.[153] Using Enterprise and Enbridge's actual average capital

---

[149] Id.; Exhibit No. SEA-45 at 2:3-3:7 (showing that the updated cost of debt and nominal ROE decreased, relative to Seaway's direct case).

[150] Portland Natural Gas Transmission System, 134 FERC ¶ 61,129 at P 242 (2011) (citing Boston Edison Company v. FERC, 885 F.2d 962, 966 (1st Cir. 1989); Trunkline Gas Company, 90 FERC ¶ 61,017, at 61,117 (2000); Panhandle Eastern Pipe Line Company, 74 FERC ¶ 61,109, at 61,363 (1996); and Williston Basin Interstate Pipeline Company, 84 FERC ¶ 61,081 at 61,364-66 (1989)).

[151] Id.

[152] See Seaway Initial Brief at 39.

[153] ACN Initial Brief at 39; Exhibit No. ACN-1 at 21:7-22; BP Pipelines (Alaska) Inc. v. TAPS Carriers, 123 FERC ¶ 61,287 at P 174 (2008); Entrega Gas Pipeline Inc., 113 FERC ¶ 61,327 at P 32 (2005); Kuparuk Transportation Company, 55 FERC ¶ 61,122, at 61,376-77.

structure as of the end of the first quarter 2012 produces a debt to equity ratio of 61% to 39%.[154]

Seaway argues that Enbridge's equity ratio is anomalous, but Seaway's argument is irrelevant and its conclusion is flawed.[155] The relevant question is whether the parent companies' average capital structure is anomalous, because that is the equity ratio that will be used to calculate Seaway's rates. Here, Ms. Crowe testified that the average equity ratio for Seaway's parent companies is 39%.[156] As explained in ACN's Initial Brief, the Commission regularly approves capital structures for initial rates that reflect a 40 percent equity ratio.[157] Thus, ACN's proposed equity ratio is not anomalous.

Seaway also argues that Enbridge's risks are not representative of Seaway's risks, because Enbridge is a "diversified energy company involved not only in oil pipelines, but also in gas distribution, gas pipelines, processing and energy services, and investments in other entities."[158] If that is true, then the proxy group companies' risks are also not representative of Seaway's risks. The record shows that the proxy group

---

[154] Exhibit No. ACN-1 at 21:7-22.

[155] Seaway Initial Brief at 40, 42.

[156] Exhibit Nos. ACN-1 at 21:7-22, ACN-16. In its Initial Brief (at 43), Seaway stated that the average equity ratio for the parent companies was 38.69% as of March 31, 2012 and 37.81% as of September 2012. Seaway did not provide any testimony, support, calculations, or underlying data for these equity ratios.

[157] Ruby Pipeline, L.L.C., 128 FERC ¶ 61,224 at P 53 (2009) ("Ruby's ... proposed capital structure of 40 percent equity and 60 percent debt is in line with our recent orders.") (citing Mid-Atlantic Express, LLC, 126 FERC ¶ 61,019 at P 31 (2009); Markwest Pioneer, L.L.C., 125 FERC ¶ 61,165 at P 27 (2008); and Ingelside Energy Center, LLC, 112 FERC ¶ 61,101, at 61,653 (2005)).

[158] Seaway Initial Brief at 42-43 (internal quotations ommitted).

companies are also diversified companies with production, transportation, terminaling, storage, energy services, and international business segments in the natural gas, liquids, crude oil, refined products, ammonia, and asphalt markets.[159]

2) What is the appropriate cost of debt?

Seaway argues that because it is appropriate to use the proxy group companies' capital structure, its debt costs should also reflect the proxy group companies' debt costs at the time it filed its direct case.[160] For the reasons stated above, and as explained in ACN's Initial Brief (at 39), it is appropriate to use the average debt cost for Seaway's parent companies, based on the most recent data in the record. Updated data indicate that at December 31, 2012, Enterprise's cost of debt was 5.56%, and Enbridge's cost of debt was 4.68%, the average of which is comparable to, and confirms the reasonableness of, Ms. Crowe's proposed 5.01% debt cost.[161]

3) What is the appropriate rate of return on equity ("ROE")?

Seaway's nominal ROE for the six-month period ending September 2012 is 11.28%.[162] To calculate a just and reasonable ROE for Seaway, Ms. Crowe first accepted the proxy group that Seaway witness Dr. Bruce Fairchild proposed in his direct testimony.[163] Second, Ms. Crowe used the Commission's preferred Discounted Cash

---

[159] Exhibit No. S-24 at 8-15.
[160] Seaway Initial Brief at 44.
[161] Exhibit No. ACN-40.
[162] Exhibit No. ACN-18 at 1, line "Median Nominal Return on Equity."
[163] Exhibit Nos. ACN-1 at 22:20-23:8, ACN-18. In his rebuttal testimony, Dr.

Flow ("DCF") model to calculate the proxy group companies' returns.[164] Third, Ms. Crowe selected the median ROE for the proxy group companies, which is 11.28% on a nominal basis, and 9.62% in real dollars.[165]

If Your Honor does not adopt ACN's proposed ROE, Seaway should be required to use the most recent data in the record to recalculate an ROE that complies with the Commission's DCF methodology. Specifically, as explained in ACN's Initial Brief (at 39-42), Seaway should be required to use the Commission's two-stage growth rate in the dividend yield adjustment factor.[166] Seaway did not address this issue in its Initial Brief, despite the fact that it was addressed in ACN witness Ms. Crowe's testimony, Trial Staff witness Edward Alvarez's testimony, and Seaway witness Dr. Fairchild's testimony,[167] and raised at hearing.[168] Thus, Seaway has waived its opportunity to present arguments against ACN and Trial Staff's position on the Commission's DCF calculations, and any belated attempts to address this issue should be disregarded.

4) What is the appropriate cost of preferred stock?

Fairchild updated his proxy group companies and excluded Nustar Energy and Magellan Midstream Partners. Taking this update into account does not change the median ROE shown on Exhibit No. ACN-18.

[164] Id.

[165] Id.

[166] See Williston Basin Interstate Pipeline Company, 50 FERC ¶ 61,284 at n.88 (1990) (citing Generic Determination of Rate of Return on Common Equity for Public Utilities, Order No. 442, FERC Stats. and Regs. ¶ 30,677, at p. 30,058 (1985) and Generic Determination of Rate of Return on Common Equity for Public Utilities, Order No. 442-A, FERC Stats. and Regs. ¶ 30,702 (1986)).

[167] Exhibit Nos. ACN-1 at 23:2-6, S-11 at 46:5-9 and 49, SEA-48 at 23:1-24:8.

[168] Exhibit No. ACN-39; Tr. at 267:20-269:1 (Fairchild Cross-examination).

ACN does not take a position on this issue.

E. What is the appropriate income tax allowance for Seaway?

As explained in ACN's Initial Brief (at 42-44), Seaway should only be permitted to include 50 percent of the otherwise applicable income tax allowance in its cost of service, to account for the fact that one of its owners is a master limited partnership ("MLP") that does not incurs any income tax liability.[169] Seaway argues that ACN's position is "contrary to established Commission policy and precedent."[170] While the Commission has determined that MLPs are entitled to an income tax allowance,[171] ACN agrees with SCN's Initial Brief (at 30-37), which demonstrates that the Commission's findings should not apply in the instant case, given the facts and competing policy considerations.

Moreover, Seaway's income tax allowance is affected, in large part, by the rate base and return figures that Your Honor determines to be just and reasonable in this proceeding. Given the substantial rate base (and thus, return) dollars that are at issue in this case, this issue deserves special scrutiny to ensure that Seaway's ratepayers are not unduly burdened by an inflated rate base, return, and income tax allowance all at once. It is especially important to carefully consider the cumulative effect of these high-dollar issues, given that Seaway will significantly over-recover its cost of service from its

---

[169] Exhibit No. ACN-1 at 25:13-26:10.

[170] Seaway Initial Brief at 47.

[171] See SFPP, L.P., Opinion No. 522, 140 FERC ¶ 61,220 (2012).

committed shippers alone, if those rates are not adjusted in this case.[172] All just and reasonable reductions to Seaway's uncommitted shipper rates will limit Seaway's ability to recover excessive returns to the detriment of its ratepayers.[173]

F. What is the appropriate amount of accumulated deferred income taxes ("ADIT")?

ACN does not take a position on this issue.

5. What Is The Appropriate Level Of Throughput?

It is undisputed that the Commission's policies and precedent require that the throughput used to calculate Seaway's rates be based on the pipeline's design capacity.[174] As demonstrated in ACN's Initial Brief (at 44-51), Seaway's proposal to only consider its pre-expansion design capacity of 135,000 barrels per day is inconsistent with the Commission's test period regulations, does not produce cost-based rates, and will afford Seaway an unjustified and unreasonable windfall if it is adopted.

ACN, Trial Staff, and SCN all agree that Seaway's rates should reflect the pre-expansion design capacity of 135,000 barrels per day for the locked-in period (June 2012 through December 2012), and the post-expansion design capacity of 400,000 barrels per day from January 2013 and going forward.[175] This approach takes into account the fact

---

[172] See Exhibit No. SCN-1 at 9:3-10:2 and Figure 3.

[173] See 49 U.S.C. § 1(5) (1977); Farmers Union II, 734 F.2d at 1502.

[174] See Seaway Initial Brief at 49 (citing White Cliffs Pipeline, L.L.C., 126 FERC ¶ 61,070 at P 31 (2009); Enbridge Energy, 110 FERC ¶ 61,211 at P 46; and Enbridge Pipelines (Southern Lights) LLC, 122 FERC ¶ 61,170 at P 10 (2008)).

[175] ACN Initial Brief at 45-48; Trial Staff Initial Brief at 70; SCN Initial Brief at 38.

that Seaway's per-unit cost of providing service is different for the pre- and post-expansion periods,[176] will limit Seaway's ability to over-recover its cost of service, and reflects Seaway's design capacity as of the end of the twelve-month test period.

Section 5 of Seaway's Initial Brief did not address ACN's 400,000 barrels per day design capacity figure. In fact, nothing in the record, or Seaway's Initial Brief, states that Seaway's post-expansion design capacity is something other than 400,000 barrels per day. Rather, the substantial record evidence establishes that ACN's 400,000 barrels per day figure for the post-expansion capacity is accurate.[177]

In other parts of its Initial Brief, Seaway argues that it did not deliver 400,000 barrels per day on an average, monthly basis in January or February 2013, and thus ACN's "throughput" figure is inaccurate.[178] Seaway's statements are irrelevant, because ACN proposes to calculate Seaway's rates based on its design capacity, not its actual throughput. As explained in Section 2 of this reply brief, it is undisputed that a pipeline's design capacity and actual throughput are distinct concepts.[179] A pipeline's actual throughput can be lower, or—in Seaway's case—higher than, its design

---

[176] ACN Initial Brief at 8-9; Exhibit Nos. ACN-1 at 6:2-19, ACN-5 at 3.

[177] See, e.g., Exhibit Nos. S-28 at 1, SCN-10 at 2, SCN 30 at 9, SCN-46 at 1, SCN-47 at 1, SCN-50 at 1, SCN-52 at 1, SCN-53, SCN-54 at 20, SCN-55 at 1, SCN-56 at 3 and 5, SCN-58, SCN-68 at 5; Tr. at 83:8-17 (Ordemann Cross-examination) (admitting that Seaway is currently capable of flowing 417,000 barrels per day).

[178] Seaway Initial Brief at 13-14.

[179] Exhibit No. SCN-62.

capacity,[180] because throughput and design capacity are affected by different variables.

For example, Seaway's post-expansion throughput, measured in volumes delivered at its Jones Creek terminal,[181] has been affected by the current lack of takeaway capacity (i.e., refinery capacity, downstream pipeline capacity, and storage capacity) at facilities downstream of Jones Creek.[182] Seaway's June 2012 and January 2013 average monthly throughput volumes were also affected when the pipeline was taken out of service to bring new facilities online.[183] Shutdowns and service interruptions due to a lack of takeaway capacity affect a pipeline's actual delivered volumes. However, they do not affect the pipeline's design capacity, because design capacity is a calculated measurement that assumes "uninterrupted operations."[184]

In its Initial Brief (at 49), Seaway argues, "the pipeline's capacity is affected by various factors, including the specific type and mix of crude oil transported." This is because, according to Seaway, shipping heavy crude volumes "reduces the available

---

[180] See Exhibit No. ACN-40 (showing that Seaway's actual throughput exceeded its proposed 135,000 barrels per day design capacity for several months of the pre-expansion period).

[181] Although Mr. Ordemann was initially confused, he later confirmed that Seaway's throughput volumes were delivered volumes, measured at Jones Creek. Tr. at 129:5-22 and 169:2-10 (Ordemann Cross-examination).

[182] Exhibit Nos. SCN-56 at 9, S-28 (quoting Mr. Ordemann as explaining that the Echo lateral due to be in-service before the end of 2013 "will have the ability to alleviate most of the bottlenecks we're seeing right now."), S-31; Tr. 133:12-22 (Ordemann Cross-examination).

[183] See Tr. at 131:4-133:3 (Ordemann Cross-examination).

[184] Exhibit No. SCN-62.

capacity on the pipeline."[185] Notably, while Seaway attempts to paint its design capacity as a fluid concept, incapable of measurement, the Commission and other oil pipelines regularly calculate a discrete value for pipelines' design capacities.

Moreover, Seaway charges a higher rate for heavy volumes to account for the fact that they "[reduce] the available capacity on the pipeline."[186] If Seaway's rates for heavy shipments are designed to account for the capacity that Seaway loses when it ships heavy volumes, then Seaway will recover revenues equal to its design capacity, regardless of whether it ships 100 percent light barrels, 100 percent heavy barrels, or a mix of both light and heavy barrels.[187] Thus, for ratemaking purposes, Seaway's ratio of heavy-to-light barrels shipped is not dispositive of the pipeline's design capacity.

Finally, Seaway argues that its actual average throughput of 138,000 barrels per day from June 2012 through January 2013 "confirms the reasonableness" of its 135,000 barrels per day design capacity, and "would provide an appropriate level of projected throughput" should Your Honor reject Seaway's proposal.[188] But Seaway's average throughput proposal should be rejected for three reasons.

---

[185] Seaway Initial Brief at 49.

[186] See Seaway Initial Brief at 52. As explained in Section 7 of this reply brief, ACN opposes Seaway's proposed surcharge for heavy barrels because it is not cost-based.

[187] For example, if a barrel of heavy oil takes up twice as much capacity as a barrel of light oil, and Seaway charges $1 for a barrel of light oil and $2 for a barrel of heavy oil, then Seaway will make $100 if it ships 100 light barrels of oil, assuming its capacity is 100 barrels per day. It will also make $100 if it ships 50 barrels of heavy oil. Either way, its revenues always equal its design capacity.

[188] Seaway Initial Brief at 50.

First, calculating rates using the average 138,000 barrels per day figure does not reflect Seaway's post-expansion capacity. Seaway's throughput figure averages seven months of pre-expansion volumes data with only 21 days (from approximately January 11 through January 31) of post-expansion volumes data.[189] Thus, the average throughput figure can only be said to measure Seaway's pre-expansion capacity. This is significant, because "Commission policy does not support using data that is not likely to be representative of future throughput levels."[190]

Second, Seaway's proposal to use its actual volumes shipped fails to take into account the fact that Seaway's committed shippers have ship-or-pay obligations. In its Initial Brief, Seaway admitted that these ship-or-pay obligations provide Seaway with revenue for the full amount of the committed volumes, even if its committed shippers never ship a single barrel of oil.[191] Thus, Seaway's contracted-for committed volumes better reflect its revenues than its delivered committed volumes.

Third, as discussed above, Commission precedent requires that Seaway's design

---

[189] Exhibit No. SEA-40; Tr. at 132:20-133:4 (Ordemann Cross-examination).

[190] Opinion No. 511, 134 FERC ¶ 61,121 at P 27.

[191] Tr. at 416:20-420:2 and 422:9-17 (Wetmore Cross-examination); see also Seaway Initial Brief at 9 (arguing that committed shippers' ship or pay obligations provide Seaway with "assured revenues" because committed shippers are "obligated to ship (or pay for the minimum committed volume) each month during the term of the contract") (citing Enbridge Pipelines (North Dakota) LLC, 133 FERC ¶ 61,167 at P 34 (2010) (internal quotations ommitted).

capacity be used to calculate its rates in this proceeding,[192] and Seaway has not demonstrated that ACN's 400,000 barrels per day figure is erroneous in any way. In sum, Seaway's arguments should be rejected, and Seaway's rates should be calculated using the 135,000 barrels per day for the pre-expansion period, and 400,000 barrels per day for the post-expansion period. For the reasons stated in Section 2 of this reply brief, if the Presiding Judge determines that it is only appropriate to calculate one set of rates, then Seaway's rates should reflect its 400,000 barrels per day design capacity as of the end of the twelve-month test period.

6. What Is The Appropriate Rate Design Method For Calculating Rates In This Proceeding?

Trial Staff and all active Intervenors (SCN, ACN, and CAPP) agree that Seaway's rate design proposal should be rejected.[193] As explained in ACN's Initial Brief (at 51-55), Seaway's uncommitted rates should be calculated using the Commission's fully-allocated cost of service method for producing cost-based rates.[194]

In its Initial Brief (at 51), Seaway contends that the committed rates are discounted, relative to the uncommitted rates. Seaway also argues that it is appropriate to shift an alleged "shortfall" that is not recovered from committed shipper rates to the

---

[192] Seaway Initial Brief at 49 (citing White Cliffs Pipeline, L.L.C., 126 FERC ¶ 61,070 at P 31; Enbridge Energy, 110 FERC ¶ 61,211 at P 46; and Enbridge Pipelines (Southern Lights) LLC, 122 FERC ¶ 61,170 at P 10).

[193] ACN Initial Brief at 51-55; Trial Staff Initial Brief at 73; SCN Initial Brief at 42-43; CAPP Initial Brief at 25-27.

[194] Williams Pipe Line Company, 84 FERC ¶ 61,022, at 61,098 and 61,109 (1998); Exhibit No. ACN-1 at 27:12-29.

uncommitted shippers through a revenue crediting mechanism.[195] Seaway's arguments mistakenly assume that Seaway's committed rates are lower than an average rate, or unit rate.[196] In fact, Seaway's committed rates are higher than the average just and reasonable rate.[197] Moreover, Seaway will over-recover its cost of service from its committed shippers alone.[198] Therefore, there is no shortfall to shift to the uncommitted shippers. In this circumstance, Seaway's revenue crediting method produces negative uncommitted rates.[199]

Trial Staff argues that ACN's fully-allocated rate methodology produces the same rate for committed and uncommitted shippers, and thus, "is inconsistent with Commission policy and precedent."[200] As an initial matter, the Commission has held that pipelines are permitted to charge different rates for committed and uncommitted shippers,[201] but the Commission has not held that pipelines are required to do so. In any event, ACN merely set forth a cost-based unit rate in this proceeding, to enable Your Honor to assess whether Seaway's filed rates are just and reasonable. If Your

---

[195] Seaway Initial Brief at 51.

[196] See, e.g., Exhibit No. SEA-26 at 58:10-13.

[197] ACN-1 at 5:16-19 (explaining that a cost-based unit rate for Seaway is $0.5050 for the pre-expansion period, and $0.1803 for the post-expansion period), and SEA-3 at 17 (showing that the lowest committed rate is $2.00).

[198] See Exhibit No. SCN-1 at 9:3-10:2 and Figure 3.

[199] See Exhibit No. ACN-21 at 3, line 7 (subtracting the committed shipper revenues shown on Exhibit SEA-24 at Statement A2, line 2 from ACN's cost of service for the pre-expansion period).

[200] Trial Staff Initial Brief at 7.

[201] See id. at 74.

Honor determines that Seaway's filed rates should be adjusted, and that the committed should be discounted, relative to the uncommitted rates, then any such differential should be cost-based.[202]

7. Is The Differential Between Seaway's Light Crude Oil And Heavy Crude Oil Rates Justified?

Seaway did not provide any cost-based evidence to support its proposed differential between heavy and light crude oil shipments.[203] Seaway's uncommitted rate for heavy shipments is 13 percent higher than its rate for light shipments.[204] Both Seaway and Trial Staff argue that it is appropriate for Seaway's rates for heavy shipments to include a premium or surcharge, to account for the fact that heavy barrels are slower and decrease the pipeline's capacity.[205] However, neither Trial Staff nor Seaway provide any justification or support for the actual 13 percent surcharge reflected in Seaway's rates. Indeed, no participant provided evidence that Seaway's costs (in the form of lost capacity or higher O&M expenses) for shipping heavy oil are 13 percent higher than its costs for shipping light oil. In Arco Alaska, Inc. v. FERC, the Court of Appeals for the District of Columbia Circuit rejected a pipeline's proposed surcharge for heavy barrels, finding that the surcharge did "not at all reflect the difference in the

---

[202] ACN Initial Brief at 55; Exhibit No. ACN-23 at 9:18-13:7.
[203] ACN Initial Brief at 55-56; Exhibit Nos. ACN-23 at 10:10-13, ACN-41.
[204] Exhibit No. CAP-1 at 20:8-11.
[205] Trial Staff Initial Brief at 14 and 75; Seaway Initial Brief at 52-53.

cost of transporting the different streams of petroleum."[206] The same conclusion applies in the instant case.

Finally, Seaway argues that its surcharge for heavy barrels is reasonable, because the rate is below the just and reasonable rate shown on Exhibit No. SEA-24.[207] First, as demonstrated in ACN's Initial Brief and this reply brief, Seaway's cost of service and the resulting rate on Exhibit No. SEA-24 are not just and reasonable. Second, even assuming, arguendo, that Seaway's rate for heavy shipments is below a just and reasonable rate, the United States Supreme Court has repeatedly held that a rate that is found to be just and reasonable may still be unduly discriminatory under the ICA.[208] In sum, Seaway has not justified the 13 percent surcharge it proposes to assess on heavy barrels, and that surcharge should be rejected.

8. What Is The Appropriate Level Of Uncommitted Shipper Rates?

For the reasons stated in ACN's Initial Brief and this reply brief, the just and reasonable rate for the pre-expansion period (June 2012 through December 2012) is $0.5050 per barrel.[209] Taking into account the capital additions required to effectuate the reversal and Seaway's post-expansion design capacity produces a just and reasonable

---

[206] Arco Alaska, Inc. v. FERC, 89 F.3d 878 at 880-84 (D.C. Cir. 1996).

[207] Seaway Initial Brief at 52.

[208] American Express Company v. Caldwell, 244 U.S. 617, 624 (1917); ICC v. Baltimore & Ohio Railroad Company, 145 U.S. 263, 277 (1892); United States v. Illinois Central Railroad Company, 263 U.S. 515, 524 (1924); ICC v. Inland Waterways Corp., 319 U.S. 671, 686 (1943).

[209] Exhibit No. ACN-21 at 3, line 10.

rate for the post-expansion period of $0.1803.[210] Thus, despite Seaway's arguments to the contrary, Seaways' filed uncommitted rates of $3.82 and $4.32 are not just and reasonable.

ACN acknowledges that if Seaway's committed rates are not adjusted in this proceeding, Seaway will over-recover its cost of service even if ACN's rates are approved for uncommitted shippers.[211] Accordingly, it may be appropriate for Your Honor to also adopt a revenue sharing mechanism similar to those on other oil pipelines, whereby Seaway must return to shippers any revenues it collects in excess of a just and reasonable cost of service. Your Honor has discretion, under Rule 716 of the Commission's Rules of Practice and Procedure, to reopen the record if it "is warranted by any change in conditions of fact or of law or by the public interest" if necessary.[212] Given that the Commission issued its March 22 Order on Seaway's committed rates during the hearing in this case, changed conditions and/or the public interest may require supplemental proceedings to ensure that Seaway is not permitted to recover excessive returns.

9. What Is The Appropriate Level of Committed Shipper Rates?

If Your Honor determines that it is appropriate to calculate committed rates in

---

[210] Exhibit No. ACN-22 at 3, line 10.

[211] See Exhibit No. SCN-1 at 9:3-10:2 and Figure 3; Trial Staff Initial Brief at 20 ("Staff's rate design is the only one offered in Docket No. IS12-226-000 that avoids approval of rates that will result in excessive returns.").

[212] 18 C.F.R. § 385.716(c) (2013).

this proceeding that reflect a differential, relative to Seaway's uncommitted rates, any such differential must be cost-based.[213]

WHEREFORE, ACN requests Your Honor to adopt the positions taken in this reply brief, and find that Seaway's filed rates are not just and reasonable for the reasons provided herein.

Respectfully submitted,

/s/ Erica L. Rancilio
Katherine B. Edwards
John Paul Floom
Erica L. Rancilio
Edwards & Floom, LLP
1517 King Street
Alexandria, VA 22314
703-549-0888
kbe@kbelaw.com
jpf@kbelaw.com
elr@kbelaw.com

Attorneys for
Apache Corporation,
Chevron Products Company, and
Noble Energy, Inc.

DATED: June 4, 2013

[213] Exhibit No. ACN-23 at 9:18-13:7.

CERTIFICATE OF SERVICE

Pursuant to Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.2010, I hereby certify that I have this day served the public version of the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Alexandria, Virginia, this 4th day of June, 2013.

/s/ Erica L. Rancilio
Erica L. Rancilio
Edwards & Floom, LLP
1517 King Street
Alexandria, VA 22314
(703) 549-0888