UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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

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

Submitted: May 7, 2013

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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, Apache Corporation, Chevron Products Company (a division of Chevron U.S.A. Inc.), and Noble Energy, Inc. (jointly, "ACN") respectfully submit this initial post-hearing brief.

I. INTRODUCTION

Prior to 2011, ConocoPhillips Company ("ConocoPhillips") and Enterprise Products Partners L.P. ("Enterprise") owned the Seaway Crude Pipeline Company LLC ("Seaway") facilities, which provided south-to-north crude oil transportation service from the U.S. Gulf Coast to Cushing, Oklahoma.[1] In November 2011, Enbridge Inc. ("Enbridge") purchased ConocoPhillips' 50 percent interest in Seaway.[2] Enterprise retained its 50 percent ownership in Seaway.

[1] Exhibit No. ACN-1 at 7:5-11.

[2] Id.

On December 2, 2011, Enterprise and Enbridge filed an application with the FERC in Docket No. OR12-4-000 stating that they planned to reverse Seaway to provide north-to-south crude oil transportation from Cushing, Oklahoma to the U.S. Gulf Coast, and seeking authorization to charge market-based rates on the reversed pipeline ("Market-Based Rate Application"). The Commission denied Enterprise and Enbridge's Market-Based Rate Application on May 7, 2012.[3] On June 28, 2012, the Commission sua sponte granted rehearing of its May 7, 2012 order.[4] The Commission's order on rehearing in Docket No. OR12-4-000 remains outstanding.

II. STATEMENT OF THE CASE

On April 13, 2012, Seaway filed FERC Tariff No. 2.0.0. reflecting initial committed shipper rates from $2.00 to $3.50, and initial uncommitted shipper rates of $3.82 for light crude oil and $4.32 for heavy crude oil ("Initial Rate Filing"). According to the Commission's regulations, oil pipelines "must establish initial rates pursuant to [Section] 342.2," of the Commission's regulations, which requires pipelines either to: 1) file cost, revenue, and throughput data supporting the rates, or 2) establish by affidavit that the rate is agreed to by at least one non-affiliated person, provided that if an initial rate is protested, the pipeline must file supporting cost, revenue, and throughput data.[5] On April 30, 2012, ACN and other parties protested the committed and uncommitted

[3] Enterprise Products Partners L.P., 139 FERC ¶ 61,099 (2012).
[4] Enterprise Products Partners L.P., 139 FERC ¶ 61,255 (2012).
[5] 18 C.F.R. §§ 342.1(a), 342.2 (2013).

rates proposed in Seaway's Initial Rates Filing.

On May 11, 2012, the Commission issued an order setting Seaway's Initial Rates Filing for hearing.[6] In its Hearing Order, the Commission made the filed rates effective May 14, 2012, subject to refund, and set for hearing "all issues raised by the [Initial Rates Filing], including but not limited to, those initially raised by the protestors."[7] The Commission also directed Seaway to "provide cost-of-service data so that the Commission may determine whether the proposed rates are just and reasonable."[8] The reversed Seaway pipeline went into southbound service from Cushing, Oklahoma to the Jones Creek Terminal near Freeport, Texas in May 2012.[9]

On May 18, 2012, the Chief Administrative Law Judge issued an order in this proceeding establishing Track Three Procedural Time Standards, and designated Your Honor as the Presiding Administrative Law Judge.

On December 10, 2012, Seaway filed a Petition For Declaratory Order in Docket No. OR13-10-000 ("Petition"), requesting the Commission to rule that it will not analyze the reasonableness of Seaway's committed rates in Docket No. IS12-226-000. On March 22, 2013, the Commission issued an order denying Seaway's Petition in Docket No. OR13-10-000, but stated, "the agreed-upon terms of [a TSA] will govern the

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[6] Seaway Crude Pipeline Company LLC, 139 FERC ¶ 61,109 at P 5 (2012) ("Hearing Order").

[7] Id. at Ordering Paragraph A, P 23.

[8] Id. at P 22.

[9] Exhibit No. ACN-1 at 7:8-11.

determination of the committed shippers' rates over the term of the TSA."[10]

From March 19, 2013 through March 25, 2013, Your Honor convened the hearing in this proceeding. During the hearing, ACN presented the prepared direct and answering and cross-answering testimony of Ms. Elizabeth H. Crowe, which establishes that Seaway failed to support its filed initial rates on a cost basis and therefore the filed rates are not just and reasonable, as is required by Commission precedent and the Interstate Commerce Act ("ICA").[11]

III. ARGUMENT

Seaway's filed rates are not just and reasonable under the Commission's regulations, precedent, cost-based ratemaking principles, and Section 1(5) of the ICA. In 1985, the Commission issued Opinion No. 154-B, the purpose of which was "to devise generic principles for the setting of just and reasonable oil pipeline rates," pursuant to Section 1(5) of the ICA, and in light of the United States Court of Appeals for the District of Columbia Circuit's order in Farmers Union II.[12] In Farmers Union II, the D.C. Circuit held that a just and reasonable rate is "high enough to both maintain the [pipeline's] credit and attract capital," but "low enough so that exploitation by the

[10] Seaway Crude Pipeline Company LLC, 142 FERC ¶ 61,201 at PP 11, 13 (2013) (internal quotations omitted).

[11] 49 U.S.C. § 1(5) (1977). Section 1(5) of the ICA establishes that all rates charged for oil pipeline transportation service "shall be just and reasonable." Id.

[12] Williams Pipe Line Company, Opinion No. 154-B, 31 FERC ¶ 61,377 (1985) ("Opinion No. 154-B") (citing 49 U.S.C. § 1(5) (1977), Farmers Union Central Exchange Inc. v. FERC, 734 F.2d 1486 (D.C. Cir. 1984) ("Farmers Union II")).

[regulated business] is prevented."[13] In other words, a just and reasonable rate compensates the pipeline for its investment, but is not excessive.[14]

Seaway admits that it did not base its filed committed and uncommitted rates on its cost of service.[15] Rather, Seaway's filed rates are the product of negotiations, in that they were agreed to by at least one of its shippers.[16] In this case, Seaway attempted to establish that those negotiated rates are supportable on a cost basis. But, for the reasons addressed in this initial brief, Seaway's cost of service presentation and rate calculations fail to establish that Seaway's filed rates are just and reasonable.

In fact, Ms. Crowe submitted testimony and evidence in this proceeding that establishes that Seaway's proposed cost of service is excessive, and its filed rates are not based on Seaway's underlying cost of providing service.[17] Significantly, Seaway's own internal documents show that Seaway expects to **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** in 2013.[18] Accordingly, Seaway's filed rates must be reduced, as described below, to ensure that Seaway is not permitted to recover excessive returns, in violation of the ICA, and to the detriment of

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[13] Farmers Union II, 734 F.2d at 1502 (internal quotations omitted).

[14] Id.

[15] Exhibit Nos. SEA-1 at 8:3-6, ACN-41 (Seaway data request response, stating "Seaway's committed and uncommitted rates were not derived or established pursuant to the Commission's cost-of-service regulations in § 346.2.").

[16] Id.

[17] See, e.g., Exhibit Nos. ACN-1 at 3:12-15, ACN-21, ACN-22.

[18] Exhibit No. SCN-57, Tr. at 415:14-18 (Wetmore Cross-examination).

its shippers.

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

ACN anticipates that it will support the Commission Trial Staff's ("Trial Staff") positions on this issue.

2. What Is The Appropriate Rate Period or Periods?

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.[19] The Commission's test period regulations provide, "[f]or a carrier which has less than 12 months' experience, the test period may consist of 12 consecutive months ending not more than one year from the filing date."[20] Further, "for a carrier which is establishing rates for new service, the test period will be based on a 12-month projection of costs and revenues."[21]

Seaway provided its first full month of southbound service in June 2012.[22] Thus, the test period in this case should be June 2012 through May 2013.[23] As Seaway witness Erik G. Wetmore admits, this test period reflects Seaway's costs and revenues for the

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[19] 18 C.F.R. § 346.2(c) (2013).
[20] 18 C.F.R. § 346.2(a)(2) (2013).
[21] 18 C.F.R. § 346.2(a)(3) (2013).
[22] Exhibit No. ACN-1 at 6:4-5.
[23] Id.

first full twelve months of its post-reversal operations.[24] However, Seaway's capacity changed significantly during the test period.[25] Therefore, as discussed in detail below, two sets of rates should be calculated in this proceeding.[26] One set of rates should reflect Seaway's test period costs and revenues for the pre-expansion period, and another set should reflect Seaway's test period costs and revenues for the post-expansion period.[27]

Seaway proposes to calculate rates in this proceeding by using projected costs and revenues for a seven-month period, from June 2012 through December 2012.[28] Seaway's proposal should be rejected for four reasons. First, Seaway's proposal to use seven months of projected costs and revenues fails to comply with the Commission's test period regulations, which require Seaway to calculate rates using cost, revenue, and throughput data for a twelve-month test period.[29]

Second, Seaway justifies its seven-month test period under a theory that the Commission's regulations require it to calculate a rate for its "initial period of

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[24] Tr. at 408:12-16 (Wetmore Cross-examination) (replying "[c]orrect" when asked, "[i]f in preparing your direct testimony you had projected costs and revenues for the first 12 months of Seaway's operations, you would have projected cost and revenues from June 2012 through May 2013; correct?")

[25] Exhibit No. ACN-1 at 6:2-14.

[26] Id.

[27] Id.

[28] Exhibit No. SEA-22 at 12:16-19; Tr. at 408:8-11 (Wetmore Cross-examination).

[29] 18 C.F.R. § 346.2(a) (2013).

operations."[30] However, the Commission's test period regulations and precedent do not distinguish between an "initial period of operations" and any subsequent period of operations. Rather, they are structured to take into account the fact that a pipeline with operating experience will have actual cost data, while a pipeline that does not have operating experience (i.e., it is providing a "new service") will have to rely on projections.[31]

Third, Seaway does not provide any support for its proposal to define its "initial period of operations" as the pre-expansion period, as opposed to its first twelve months of operations (which would take into account the expansion capacity).

Fourth, Seaway's proposal to truncate the test period in December 2012 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. As addressed in Section 5 of this initial brief, Seaway completed an expansion project in mid-January 2013 that increased Seaway's design capacity from 135,000 barrels per day to 400,000 barrels per day.[32] Seaway's revenues increased accordingly. But Seaway's costs have not proportionately increased.[33] Thus, Seaway's per-unit cost (cost of service divided by throughput) for the post-expansion period in 2013 is

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[30] See Exhibit No. SEA-26 at 51:4-52:15.

[31] See 18 C.F.R. § 346.2(a) (2013).

[32] Exhibit No. ACN-1 at 6:2-19.

[33] Exhibit Nos. ACN-1 at 6:2-19, ACN-4. Seaway does not dispute this fact, or the accuracy of Ms. Crowe's testimony on this matter.

significantly lower than its per-unit cost before the expansion went into service.[34] Ms. Crowe calculated this impact, and determined that taking the 2013 expansion capacity and costs into account reduces Seaway's filed unit rate by 66 percent.[35]

Given that Seaway's per-unit cost of service is different for the pre- and post-expansion periods, it is not possible to calculate one just and reasonable rate based on the test period data in this rate proceeding.[36] One rate will be just and reasonable for the pre-expansion test period months, from May 2012 through December 2012, and a lower rate will be just and reasonable for January 2013 and going forward. Accordingly, it is appropriate and reasonable to calculate two sets of rates for Seaway in the instant proceeding.[37]

The first set of rates should reflect Seaway's cost of service and design capacity for the pre-expansion test period months, from June 2012 through December 2012. These rates would only be applicable to the "locked-in" period, after the reversal went into service but before expansion went into service, and would be used to calculate any

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[34] Id.

[35] Id.; Exhibit No. ACN-5 at 3, 17 (Ms. Crowe calculated this impact by first increasing Seaway's filed cost of service, which is already significantly higher than ACN's proposed cost of service, to reflect $33.9 million in capital additions associated with the expansion project, and then calculating a unit rate for that cost of service based on 400,000 barrels per day of capacity. Id.)

[36] Exhibit No. ACN-1 at 6:2-19.

[37] Id.

refunds due to shippers for May 2012 through December 2012 billings.[38] The second set of rates should reflect Seaway's cost of service and design capacity for the post-expansion period.[39] Under the Commission's test period regulations and precedent, the second set of rates should reflect the increased costs and higher design capacity that Seaway experienced during the post-expansion test period months, from January through May 2013.[40] This rate would be used to determine the just and reasonable rate for January 2013 and going forward.

If Your Honor determines that it is appropriate to calculate only one set of rates in this proceeding, then those rates should be calculated using Seaway's costs and design capacity as of May 2013, the end of the twelve-month test period in this case. Seaway's own witness, William Ordemann, admitted that Seaway's pre-expansion design capacity is not representative of the throughput that Seaway expects to experience going forward, because it is too low.[41] Similarly, Mr. Wetmore could not testify that Seaway's proposed cost of service and revenues shown on Exhibit No. SEA-24 are representative of Seaway's post-expansion costs and revenues.[42] As discussed in Section 5 of this initial brief, the purpose of a test period is to calculate rates that are

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[38] See Hearing Order at Ordering Paragraph A (accepting Seaway's filed rates, effective May 24, 2012, subject to refund).

[39] Exhibit No. ACN-1 at 3:19-4:2, 6:2-19.

[40] Id.; see also, 18 C.F.R. §§ 346.1, 346.2(a)(2), 346.2(a)(3) (2013).

[41] Tr. at 142:20-143:1 (Ordemann Cross-examination).

[42] Tr. at 313:22-25 (Wetmore Cross-examination).

representative of a pipeline's costs and revenues going forward.[43] Therefore, it is not appropriate to use Seaway's pre-expansion costs and design capacity or throughput to calculate Seaway's rates going forward.

3. What Rate Base Or Bases Should Be Used?

Rate base is the largest cost of service component at issue in this rate case. Consistent with the Commission's original cost ratemaking policies and Opinion No. 154-B, the carrier property in service ("CPIS") amount in Seaway's rate base should reflect the net book value (original cost less depreciation) of the assets devoted to jurisdictional service, and any capital additions that are related to the capacity that is in service at the end of the test period. Seaway's proposal to adjust its rate base to include a $1.1 billion write-up in excess of the net book value of the Seaway assets should be rejected, for the reasons discussed below.

Ms. Crowe calculates the CPIS in Seaway's rate base for the pre-expansion period to be $130,465,000.[44] This figure includes $118 million for the net book value of the Seaway assets devoted to jurisdictional service, and approximately $12.4 million in capital additions required to reverse the pipeline.[45] To calculate Seaway's rate base for the post-expansion period, Ms. Crowe added $33.9 million to Seaway's CPIS to take

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[43] See SFPP, L.P., Opinion No. 511, 134 FERC ¶ 61,121 at P 27 (2011) ("Opinion No. 511")("Commission policy does not support using data that is not likely to be representative of future throughput levels.")

[44] Exhibit No. ACN-21 at 17.

[45] Id. (summing line 3, column (a) and line 3, column (b) to develop the $118 million figure).

into account the capital additions required to expand Seaway's capacity from 135,000 barrels per day to 400,000 barrels per day.[46]

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 is inconsistent with the Commission's original cost ratemaking policies and precedent, and provides Seaway's owners with an unjustified windfall, in violation of Commission policy.

The Commission's original cost ratemaking methodology reflects the "longstanding principle that a jurisdictional utility can include in its rate base only that portion of an asset's purchase price that represents the net book value of the property to the original owners, regardless of the acquisition cost."[47] This is because "[e]conomic regulation looks to the value to the rate payer of services performed by the company based on its current operating costs, historical capital, and return on that capital, not on

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[46] Exhibit No. ACN-22 at 17.

[47] SFPP, L.P., Opinion No. 511-A, 137 FERC ¶ 61,220 at P 163 (2011) ("Opinion No. 511-A)(internal citations omitted); see also, Opinion No. 154-B, 31 FERC at 61,833 ("[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); Opinion No. 511, 134 FERC ¶ 61,121 at P 153 ("Commission policy generally requires removal of the effects of PAAs [purchase accounting adjustments] from the rate base component of a pipeline's cost-of-service because inclusion of PAAs would be inconsistent with original cost ratemaking.")

the value placed on the company's assets by the owners."[48] Further, the Commission has acknowledged that "[w]ithout this net book value standard, all that pipelines would have to do to raise rates and obtain greater income would be to buy utility properties from another at a price higher than original cost."[49]

No party disputes that the net book value of Enbridge's 50 percent share of the Seaway assets was approximately $59 million at the time of the acquisition.[50] Nevertheless, Seaway proposes to increase the net book value of those assets by approximately $1.1 billion, to reflect the price Enbridge paid for its interest in Seaway.[51] Seaway's proposal is thus inconsistent with the Commission's policies and precedent requiring pipelines to use the original cost, or net book value, of the assets devoted to jurisdictional service in rates.

Further, as Ms. Crowe testified, Seaway's $1.1 billion acquisition adjustment reflects a 1,755 percent increase over the net book value of Enbridge's 50 percent share of the Seaway pipeline.[52] The sheer magnitude of this write-up requires greater scrutiny in the instant case, particularly because Seaway has not shown that the Commission has approved an acquisition adjustment that nears the magnitude of the 1,755 percent rate

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

[49] Arkla Energy Resources, Inc., 61 FERC ¶ 61,004, at 61,038 (1992) (citing United Gas Pipe Line Company, 25 FPC 26, 64 (1961)).

[50] Exhibit No. ACN-6 (establishing that 50 percent of the net book value of the Seaway assets as of March 31, 2012 was approximately $59 million).

[51] See Exhibit Nos. SEA-26, at Table 1, SEA-24 at Workpaper 4.

[52] Exhibit No. ACN-1 at 9:3-9.

base write-up it proposes here.[53]

Moreover, as explained by Ms. Crowe and demonstrated at the hearing, the particular circumstances on this pipeline will "provide the owners with unwarranted potential windfall profit if the Commission were to approve rates for crude oil transportation on Seaway that include the $1.1 billion proposed write-up."[54] Simply removing the proposed $1.1 billion acquisition adjustment from Seaway's proposed rate base reduces Seaway's cost of service from approximately $188.5 million to $40 million.[55] Thus, if Seaway's proposal is accepted, Seaway would be permitted to earn $148.5 million in excess of (or 370 percent of) what would otherwise be allowed under a cost of service that is consistent with the Commission's original cost ratemaking policies.[56]

Finally, if the $1.1 billion acquisition adjustment is included in Seaway's rates, then Enterprise will be afforded a significant and unjustified windfall for the price Enbridge paid for its interest in Seaway, in violation of Commission policy. When Enbridge purchased its 50 percent interest in Seaway from ConocoPhillips, the net book

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[53] Id. Mr. Wetmore's testimony (Exhibit No. SEA-26 at 15:16-19) discussing another case where the Commission approved a $1 billion acquisition adjustment did not address the size of the write-up, relative to the net book value of the acquired assets, in that case. Here, the disparity between the largely-depreciated, net book value of the acquired assets and the price paid for those assets is massive, and must be taken into account when analyzing the justness and reasonableness of Seaway's proposal to include the write-up in its jurisdictional rates.

[54] Exhibit No. ACN-1 at 11:1-10.

[55] Id.

[56] See id.

value of Enterprise's remaining 50 percent interest in Seaway was $59 million.[57] Under the Commission's just and reasonable ratemaking standards, Enterprise is entitled to the opportunity to recover a return of, and on, its $59 million investment in Seaway.[58] But under Seaway's proposed cost of service, Enterprise (as half-owner of Seaway) would earn revenues sufficient to afford it a return of, and on, a $585 million investment in Seaway.[59] 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 on Seaway.

The Commission held that it is not appropriate to include an acquisition adjustment in a regulated entity's rates when a remaining owner stands to gain an

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[57] Exhibit No. ACN-6, Tr. at 401:6-13 (Wetmore Cross-examination).
[58] FPC v. Hope Natural Gas Company, 320 U.S. 591, 602-02 (1944).
[59] Tr. at 402:13-18, 404:5-13 (Wetmore Cross-examination).

unjustified and unreasonable windfall.[60] Seaway witness Mr. Wetmore argues that it makes "no economic sense" to deny a purchase price adjustment when a remaining owner stands to benefit from including that purchase price in rates.[61] Mr. Wetmore reasoned that Enbridge would have paid more to purchase Seaway outright, but because Enbridge only purchased a partial stake in Seaway, and Enterprise retained partial ownership of Seaway, Seaway's shippers saved money.

Mr. Wetmore's analysis is flawed because it assumes, without establishing, that Enterprise would have sold its 50 percent interest in Seaway to Enbridge in the first place. Further, it fails to take into account the fact that Enterprise could have acquired Enbridge's same stake in Seaway (in other words, Enterprise could have bought out ConocoPhillips and become Seaway's sole owner), and perhaps at a lower price, if

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[60] Longhorn Partners Pipeline, 82 FERC ¶ 61,146 at 61,543-44 (1998) ("As stated, the Commission has permitted exceptions from the general rule, when certain conditions are satisfied. In the December 20 order the Commission determined, in absence of EPC's equity interest, that this case fell within the recognized exceptions. However, the facts have changed and EPC will have an equity interest in Longhorn. To continue to allow the write-up for rate purposes in this situation would open the door to circumvention of the purpose of the original cost concept, by allowing EPC to be unduly advantaged by the sale of the asset at more than depreciated cost and to benefit from the higher valuation of the asset in the hands of Longhorn. This will not be allowed."); see, also Longhorn Partners Pipeline, 73 FERC ¶ 61,355 (1995)("Longhorn") ("If EPC or an affiliate were to acquire an equity interest in the partnership, then EPC might benefit from the higher cost of service on the line, which it cannot do as the owner of a regulated asset at this time. Therefore, we will condition our grant of the requested declaratory order so that, if Exxon or any of its affiliates should become an equity owner of the LPP system, the proper valuation of the Baytown to Crane segment, as to Exxon's ownership, shall be subject to further review.")

[61] Exhibit No. SEA-26 at 21:17-22:6 (citing Rio Grande Pipeline Company v. FERC, 178 F.3d 533, 542 (D.C. Cir. 1999)).

Enterprise did not stand to gain from ConocoPhillips' sale to Enbridge.

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 the Commission explained in Longhorn:

> [t]he general rule on write-up of jurisdictional facilities acquired by one company from another is that such facilities must be included in the acquiring company's rate base at no more than their depreciated original cost, unless it can be shown by clear and convincing evidence that the acquisition results in substantial benefits to ratepayers.[62]

This is known as the substantial benefits test. To satisfy the substantial benefits test, the proponent of the rate base write-up "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 benefits on ratepayers."[63]

Seaway does not satisfy the first prong of the substantial benefits test, because Seaway is not providing a new or materially changed service. First, Seaway is providing the same service it always has—transportation of heavy and light crude oil, just in a different direction.[64] Ms. Crowe testified that "[i]n this respect, it is similar to

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[62] Longhorn, 73 FERC at 62,112.
[63] Id. (emphasis added).
[64] Exhibit No. ACN-1 at 13:10-18.

gas pipelines offering back-haul service, or flexible receipt and delivery points."[65] Second, one of the Commission's purposes in adopting the two-prong test was to ensure that shippers will not be forced to pay "more depreciation for the same facilities."[66] The record reflects that **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** If Seaway is permitted to include the acquisition adjustment in rate base, those shippers will pay rates that reflect a higher depreciation expense, even though the pipeline facilities have not changed. Third, only one-half of the pipeline ownership has changed as a result of Enbridge's acquisition, which does not support a finding that Seaway now is a fundamentally different, new crude oil pipeline venture.[68]

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."[69] As an initial matter, the Commission has held that where an entity does not choose between constructing a new pipeline and acquiring and converting a pipeline to effectuate the

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[65] Id.

[66] See, e.g, Millennium Pipeline Company, L.L.C., 117 FERC ¶ 61,319 at P 169 (2006).

[67] Tr. at 135:4-136:24 (Ordemann Cross-examination); Exhibit Nos. ACN-1 at 13:19-14:8, ACN-13.

[68] Exhibit No. ACN-1 at 14:9-12.

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

service in question, "the alleged savings in construction costs are not relevant."[70] Rather, the pipeline must show "specific, measurable benefits to consumers that consist of something other than [those] alleged savings to come within the exception to the original cost rule."[71] Here, Seaway already owned the pipeline assets that are the subject of its rates in this case. Seaway did not need to choose between purchasing and converting an existing pipeline and constructing new facilities; it merely reversed the flow on the pipeline that was already in service. Therefore, as a legal matter, it is not necessary to analyze any cost savings, relative to the cost to construct an identical pipeline, in the instant case.

To the extent that Your Honor deems it appropriate to consider the cost of new construction in the instant case, Seaway has not shown that its shippers saved any money by virtue of the fact that Enbridge spent $1.1 billion to purchase its 50 percent interest in Seaway. To the contrary, Ms. Crowe testified that Seaway's proposed $1.1 billion write-up is equal to, or possibly greater than, the cost of building a new pipeline.[72] This is because Enbridge paid $1.1 billion for a 50 percent stake in a pipeline with between 135,000 (according to Seaway) and 400,000 barrels per day of capacity. But the record shows that Enbridge could have constructed its own pipeline with

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[70] Enbridge Pipelines (KPC), 100 FERC ¶ 61,260, at 61,938-39 (2002), reh'g denied, 102 FERC ¶ 61,310 (2003), affirmed on remand, 109 FERC ¶ 61,042 (2004).

[71] Enbridge Pipelines, 100 FERC at 61,938-39.

[72] Exhibit No. ACN-1 at 14:16-15:10.

400,000 to 450,000 barrels per day of capacity for $1.3 billion.[73] If Enbridge could have constructed its own, larger pipeline for $1.3 billion, it does not follow that it achieved any cost savings by purchasing a 50 percent stake in a smaller pipeline for $1.1 billion.[74]

Seaway witness Mr. Wetmore avers that Exhibit SEA-28 shows that Enbridge's purchase of its interest in Seaway provides shippers with clearly demonstrable monetary benefits.[75] But Exhibit No. SEA-28 is fatally flawed in several aspects, and should be disregarded. First, Exhibit No. SEA-28, which purports to show the economic benefit of including the $1.1 billion purchase price in Seaway's rates, does not actually reflect the cost effect of the $1.1 billion write-up. Seaway witness Mr. Wetmore testified that his cost of service analysis, which included the $1.1 billion write-up, produced rates as high as $6.91 to $8.06.[76] But Exhibit No. SEA-28 considers the netback price to all shippers on its system using Seaway's average filed rates, which are significantly lower than the $6.91 and $8.06 rates that reflect the write-up.[77]

Moreoever, Commission precedent requires that Seaway demonstrate that the alleged economic benefits are "directly related to the acquisition."[78] But Seaway's netback analysis on Exhibit No. SEA-28 merely shows that Seaway's shippers can profit

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[73] Exhibit Nos. SEA-26 at 13:8-10, SEA-42, SCN-54 at 4 and 20, SCN-68 at 11.
[74] See Exhibit No. SEA-26 at 13:1-16.
[75] Id. at 14:17-15:12.
[76] Exhibit Nos. SEA-26 at 54:18-55:6, SEA-24, SEA-36.
[77] Exhibit No. SEA-28, column "Average Transportation Tariff."
[78] Millennium Pipeline Company, L.L.C., 117 FERC ¶ 61,319 at P 172.

by shipping their oil on Seaway at the average rate.[79] If all a pipeline has to do to provide "clear and convincing evidence that the acquisition provides substantial, quantifiable benefits to ratepayers" is show that its average rate is lower than the price in its destination market, presumably all economically viable pipelines would meet this standard, and Longhorn would become the rule, rather than the exception.[80]

Further, even if Seaway had met its substantial burden of showing that the purchase afforded its shippers a substantial economic benefit, Ms. Crowe testified that because Seaway's owners and affiliates own **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** capacity on the pipeline, any economic benefits associated with service on Seaway will ultimately accrue to Seaway's owners and affiliates, while the unaffiliated, third-party shippers will pay the price.[81] For these reasons, Seaway has not met the Commission's two-prong test for inclusion of a purchase price adjustment in rate base.

Finally, as Ms. Crowe observed:

> [t]he significant changes in North American oil and gas markets as a result of recent oil sand and gas shale production developments that have resulted in new flow patterns on existing pipelines should not precipitate or provide cause for new and exorbitant profits to be earned on the transportation network already in place.[82]

In sum, Your Honor should reject Seaway's proposal to include a $1.1 billion purchase

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[79] Exhibit No. SEA-26 at 14:17-15:12.
[80] See Longhorn, 73 FERC at 62,112.
[81] Exhibit No. ACN-1 at 9:13-23.
[82] Exhibit No. ACN-1 at 13:14-18.

price adjustment, and require Seaway to use the net book value of the Seaway assets in rate base in the instant case.

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

Assuming, arguendo, that Your Honor accepts Seaway's position that its rate base should reflect a write-up for Enbridge's purchase of its 50 percent interest in Seaway, the goodwill associated with the acquisition should not be included in Seaway's rate base.[83] Under the Commission's precedent and Uniform System of Accounts, a purchase price is generally comprised of two components: 1) the fair value, or market value, of the tangible assets purchased (which may exceed the net book value of those assets); and 2) goodwill.[84] Goodwill is defined by the Financial Accounting Standards Board as "an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized."[85]

The Commission has found that "goodwill is unrelated to the original cost of the assets used to provide jurisdictional service and emerges when more is paid than the

[83] Id. at 15:21-16:8.

[84] See, e.g., Great Plains Energy Inc., 121 FERC ¶ 61,069 at P 64 (2007)("For the purchase method of accounting in the Commission's Uniform System of Accounts...the cost of the acquired company allocated to plant assets, up to their fair value, in excess of depreciated original cost at the date of acquisition, is recorded as an acquisition adjustment...[T]he excess of the cost of the acquired company over the sum of the amounts assigned to all identifiable assets acquired and liabilities assumed is recorded as goodwill.") (internal citations omitted); Opinion No. 511, 134 FERC ¶ 61,121 at n.264.

[85] See Opinion No. 511, 134 FERC ¶ 61,121 at P 154.

book value (original cost minus depreciation) of an asset. These types of accounting adjustments that depart from original cost cannot be permitted to distort rates by being included in the pipeline's asset base."[86]

In this case, Enbridge determined that $627 million of the $1.15 billion purchase price it paid for its interest in Seaway is attributable to goodwill.[87] In other words, Enbridge determined that it paid $627 million for "the future economic benefits" from assets that were not separately identified in its accounting records. Notably, Seaway witness Mr. Wetmore conceded that goodwill is "not directly assigned to an identifiable asset."[88] Seaway did not show that the purchase price attributable to the other, unidentified assets (i.e., the goodwill amounts) benefits its shippers in any way, nor did it establish that these amounts are related to the provision of jurisdictional service.

In fact, Enbridge's purchase of its interest in Seaway, along with Enbridge's exclusive right to lease **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** capacity on Seaway's planned 2014 expansion facilities,[89] will permit Enbridge to increase capacity on its Flanagan pipeline, which is upstream of Seaway and currently flows into Cushing, Oklahoma.[90] At hearing, Seaway witness Bradley Shamla admitted that the Flanagan expansion will

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[86] Id. at P 179.

[87] Exhibit Nos. ACN-1 at 15:21-16:4, ACN-7; Tr. at 366:21-25 (Wetmore Cross-examination).

[88] Exhibit No. SEA-26 at 22:4-8.

[89] Tr. at 219:12-221:21 (Shamla Cross-examination).

[90] Tr. at 202:11-204:7.

increase Enbridge's revenues and profit, and the record shows that Enbridge took its Flanagan expansion into account when it purchased its interest in Seaway.[91] Accordingly, the goodwill that Enbridge paid to ConocoPhillips when it purchased Seaway is related to the future economic benefit that Enbridge will experience by expanding its Flanagan pipeline upstream of Seaway.[92] Enbridge's expansion of its Flanagan pipeline will not benefit Seaway's shippers. Rather, Enbridge's exclusive lease of capacity on Seaway may unduly discriminate against Seaway's uncommitted shippers with regard to capacity allocation and other operations. For these reasons, Seaway should not be permitted to include the goodwill that Enbridge paid when it purchased its interest in Seaway in rate base.

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. As

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[91] Id.; Tr. at 200:10-14, 209:4-10, 218:7-219:11, 234:8-23 (Shamla Cross-examination) (answering, "[y]es, it's expected to be a profitable pipeline" when asked, "[w]ill Enbridge have the potential to receive additional profits for volumes that flow on its expanded capacity into Cushing?").

[92] Exhibit No. SCN-35 at 22:1-24:18 ("It is not clear from the documents produced whether the revenue stream used in the discounted cash flow analysis represents only Seaway revenues or whether it includes other revenues that may flow to Enbridge and/or Enterprise (for example, due to incremental revenue on upstream Enbridge pipelines)…Inclusion of those goodwill amounts in Seaway's carrier property in service would allow Seaway's owners to recover those benefits twice, first in the upstream operations that give rise to them and second in Seaway's own rates.")

Seaway witness Mr. Ordemann testified, Seaway owns both jurisdictional and non-jurisdictional assets.[93] For the purpose of this rate filing, the jurisdictional assets are the pipeline facilities from Cushing, Oklahoma to the Jones Creek Terminal in Texas, and six crude oil storage tanks at Jones Creek.[94] Seaway's jurisdictional assets are known as the 30-Inch Longhaul System.[95] The non-jurisdictional facilities are known as the Freeport, Texas City, and Galena Park Systems.[96]

It is a basic tenet of ratemaking that a regulated entity is only permitted to include in FERC-jurisdictional rates the costs of assets that are used and useful in the provision of jurisdictional service.[97] Enbridge paid approximately $1.15 billion to purchase an ownership in Seaway's jurisdictional and non-jurisdictional assets.[98] Thus, 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 5 percent, of the full $1.15 billion purchase price to the non-jurisdictional Seaway assets.[99] Mr. Wetmore admitted that this has the effect of assigning 100 percent of the acquisition premium (the price paid in excess of the book value of the assets) to the jurisdictional facilities, and none of that premium to the non-jurisdictional

[93] Exhibit No. SEA-1 at 4:1-13.

[94] Id.

[95] Id.

[96] Id.

[97] See, e.g, Tennessee Gas Pipeline Company v. FERC, 606 F.2d 1094, 1109 (D.C. Cir. 1979).

[98] Exhibit Nos. ACN-1 at 7:12-13, ACN-7, ACN-35.

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

facilities.[100] As Ms. Crowe testified, "Seaway has grossly under-allocated its proposed PPA [purchase price adjustment] to its non-jurisdictional assets."[101]

The record does not support Seaway's proposal to assign 100 percent of the acquisition premium to Seaway's jurisdictional assets. Seaway witness Mr. Shamla testified that he relied on a study to conclude that it is reasonable to allocate $55 million of the $1.15 billion purchase price to the non-jurisdictional assets.[102] But at hearing, Mr. Shamla was unable to answer any substantive questions regarding the assumptions or calculations underlying the study, and admitted that he did not perform the study on which he relied.[103] Significantly, Seaway witness Mr. Wetmore performed a similar analysis using the same study that Mr. Shamla relied on for his analysis, but Mr. Wetmore determined that the non-jurisdictional assets have an economic value of $98 million.[104]

Moreover, Enbridge's own accounting entries demonstrate that the fair value of Enbridge's share of the non-jurisdictional assets is $ 196,058,000, which far exceeds the

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[100] Exhibit No. SEA-26 at 27:17-28:4; Tr. at 400:15-401:2.

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

[102] Exhibit No. SEA-25 at 5:7-12.

[103] 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.)

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

$55 million that Seaway proposes to allocate to those facilities in this case.[105] In Missouri Interstate, an order issued in March 2013, the Commission relied on the acquiring company's own documentation to determine the fair value of the jurisdictional assets. The Commission reasoned that it is not true "that a purchaser of an asset can allocate the purchase price in any manner it chooses."[106] "Rather, if a group of assets are purchased together there are a number of reasonable ways to allocate the purchase price, including a cost per mile allocation or a fair market value approach."[107] Consistent with Missouri Interstate, Seaway should be required to allocate the $1.15 billion purchase price to the jurisdictional and non-jurisdictional assets based on the fair market value of those assets, as reflected in Enbridge's own accounting entries. This would allocate approximately $196 million of the $1.15 billion purchase price to the non-jurisdictional facilities.[108] The remaining purchase price attributable to Seaway's jurisdictional 30-Inch Longhaul System, exclusive of goodwill, is $331,351,000.[109]

For the reasons stated in this Section 3, Seaway should not be permitted to

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[105] 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.

[106] Missouri Interstate Gas, LLC, 142 FERC ¶ 61,195 at PP 78-79, 85-86 (2013) ("Missouri Interstate").

[107] Id.

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

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

include a write-up in excess of the net book value of its jurisdictional assets in rate base. But if any write-up is permitted, it 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?

Seaway should only be permitted to accrue an allowance for funds used during construction ("AFUDC") "associated with actual investment in actual new incremental plant under construction."[110] Therefore, Seaway's proposal to accrue AFUDC on both Enterprise's share of Seaway's existing pipeline facilities and on the proposed $1.1 billion purchase price adjustment for Enbridge's share in Seaway's existing pipeline facilities should be rejected.

AFUDC is intended to compensate a pipeline (via debt costs and an equity

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

return) for its investment in new pipeline facilities during the construction phase.[111] Once the facilities are placed into service, they are transferred to rate base, and the pipeline recovers its debt costs and equity return via the rates charged for transportation service.[112]

It is undisputed that Seaway provided south-to-north crude oil transportation service until March 2012, when the pipeline was taken out of service and reversed.[113] In developing his cost of service in this case, Seaway witness Mr. Wetmore included AFUDC for Enterprise's $59 million investment in the existing pipeline facilities for the two-and-a-half month period when Seaway was out of service to effectuate the reversal.[114] Seaway's proposal to accrue AFUDC on the existing Seaway pipeline assets is inconsistent with the Commission's policies regarding AFUDC, and should be

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[111] See, e.g., ARCO Pipe Line Company, Opinion No. 351, 52 FERC ¶ 61,055 at 61,234 (1990), affirmed in pertinent part, Opinion No. 351-A, 53 FERC ¶ 61,398 (1990) ("Opinion No. 351") ("AFUDC or allowance for funds used during construction represents the cost of capital incurred by a pipeline with respect to assets prior to their inclusion in rate base. AFUDC consists of two components. The first is the cost of equity capital. The second is the cost of debt capital known as interest during construction. The ICC permitted oil pipelines to capitalize interest during construction and add the capitalized amount to rate base. The ICC did not permit the capitalization into rate base of equity used during construction. This Commission permits the capitalization of AFUDC (i.e. both interest and equity) into rate base."); 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").

[112] Tr. at 405:19-25 (Wetmore Cross-examination).

[113] Exhibit No. SEA-1 at 5, n.2.

[114] Exhibit No. SEA-24 at Statement F1, columns (a) and (b), lines 4-6 (transferring CWIP to Property In Service in May 2012), and Workpaper 6.

rejected.

As Ms. Crowe explained, "[t]he original investment in the Seaway system accrued AFUDC during its original construction period, prior to being placed into service."[115] Additionally, Seaway has already recovered AFUDC on, and been compensated for its investment in, the existing pipeline assets through its rates charged for south-to-north service since Seaway originally went into service.[116] Thus, Seaway's proposal would essentially permit it to double-recover AFUDC on $59 million related to the existing pipeline facilities, and it should be rejected.[117]

Mr. Wetmore also proposed to calculate AFUDC on Enbridge's $1.1 billion purchase price from December 2011 through April 2012,[118] despite the fact that the purchased assets were still in service, and Enbridge collected revenue associated with Seaway during that time period.[119] Ms. Crowe testified that "[i]n no case should any

[115] Exhibit No. ACN-1 at 17:10-16.

[116] Seaway has been collecting revenues, which include accrued AFUDC, through indexed and negotiated rates for service on its pipeline asset since it originally went into service. See Exhibit No. ACN-1 at 3:1-4.

[117] Ms. Crowe speculated that "[i]t might be appropriate to allow AFUDC on the NBV [net book value] of the system, to be accrued for the short time period when no oil was being transported through the system because the pipeline flow reversal was being implemented, if, in fact, the pipeline was continuing to be depreciated over that time, such that the owners would otherwise not be reimbursed for the associated return on investment for that brief period absent an AFUDC allowance." Exhibit No. ACN-1 at 17:21-18:5. However, Seaway never made such a showing. Thus, the point is moot.

[118] Exhibit No. SEA-24 at Statement F1, columns (a) and (b), lines 1-6, and Workpaper 6.

[119] Exhibit Nos. ACN-1 at 17:12-16, ACN-14, SEA-1 at 5, n.2.; Tr. at 406:17-407:13 (Wetmore Cross-examination).

AFUDC be approved for any portion of the $1.1 billion write-up."[120] This is because, as Ms. Crowe explained, AFUDC is an allowance for funds used during construction, and it accrues on CWIP, or construction work in progress.[121] It does not accrue, as Seaway proposes, on the funds a pipeline expended to purchase an ownership stake in a regulated entity from the date of the acquisition. In fact, the Commission has held that "[t]he Commission's regulations for accruing AFUDC focus on the construction activity, not on the ownership of the facilities being constructed."[122]

Indeed, Seaway's proposal to accrue AFUDC on an acquiring entity's investment in a regulated entity would extend the definition of "construction" to illogical extremes. Under Seaway's theory, an acquiring company can accrue AFUDC on the purchase price paid for an interest in a regulated entity until the merged entity files new rates. This would permit the acquiring company to accrue debt costs and an equity return for an unbounded period of time. It would also permit a company to double recover its return on investment, by earning revenues and a return on rate base from the rates charged for service on the acquired entity, while simultaneously accruing return dollars through AFUDC. In fact, that double-recovery scenario presents itself in this case.

It is undisputed that Enbridge collected revenues associated with the south-to-

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[120] Exhibit No. ACN-1 at 18:6-20.

[121] Id.

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

north service on Seaway prior to the pipeline going out of service in March 2012.[123] Nevertheless, Seaway contends, without support, that Enbridge should also be permitted to simultaneously recover an AFUDC allowance for its debt and equity costs from December 2011 through May 2012.[124] Seaway's proposal to double-recover the debt and equity costs associated with Enbridge's purchase of its interest in Seaway is wholly unsupported, and should be rejected.

Seaway's cost of service calculations also include AFUDC related to new, incremental plant costs actually incurred in connection with 1) the pipeline reversal project, and 2) the 2013 expansion. As Ms. Crowe testified, "AFUDC...associated with actual investment in actual new incremental plant under construction, is appropriate and consistent with the purpose for which an AFUDC allowance is granted to pipelines for CWIP [construction work in progress]."[125] Thus, ACN does not take issue with AFUDC calculated on new, incremental plant additions related to the reversal project and the 2013 expansion.

B. What is the appropriate level of operating expense?

Seaway's proposal to include in rates its cost projections for the period June 2012 through December 2012 is inconsistent with the Commission's test period ratemaking regulations and policies, overly subjective and arbitrary, and overstates Seaway's

[123] Exhibit Nos. ACN-1 at 17:12-16, 18:14-18, ACN-14.

[124] Tr. 407:6-13, 406:14-16 (Wetmore Cross-examination) (testifying that "a pipeline can accrue AFUDC on assets while they are in service.")

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

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's O&M expenses should reflect objective, actual cost data for a twelve-month period, and its A&G expenses should be allocated among Seaway's jurisdictional and non-jurisdictional services in a manner that is consistent with Commission precedent.

As explained in Section 2 of this initial brief, the Commission's test period ratemaking regulations require that Seaway's rates reflect twelve months of cost data.[126] Additionally, the Commission has demonstrated a strong preference for using actual cost data, when it is available, in lieu of projections.[127] Thus, Seaway's proposal to use seven months of cost projections is inconsistent with the Commission's test period regulations and precedent. Notably, Seaway witness Mr. Wetmore agreed that "actual data is more accurate than projected data."[128]

Further, Seaway's projected O&M expenses are not supported by the record, but rather are arbitrary, subjective, and excessive. Seaway proposes to recover approximately $20 million in O&M expenses, based on its projections for June 2012

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[126] See 18 C.F.R. § 346.2 (2013).

[127] 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).

[128] Tr. at 409:9-11 (Wetmore Cross-examination).

through December 2012.[129] But as Ms. Crowe testified, Seaway's proposed O&M expense is double the amount of O&M expense that Seaway recorded in 2011, and also double the amount that Seaway's own internal projections showed for the reversed pipeline for 2012.[130]

Regarding Seaway's proposed A&G costs, at hearing Seaway submitted a revised Exhibit No. SEA-41 that purports to allocate Seaway's shared A&G costs to its jurisdictional and non-jurisdictional assets using the Commission's KN Method.[131] Seaway's proposed A&G allocation is flawed. The Commission's detailed explanation of the KN Method for allocating shared A&G expenses among jurisdictional and non-jurisdictional services is as follows:

> Opinion No. 731, which originally set forth the formula for the KN Method, requires that G&A costs first be divided in labor-related, plant-related, and "other" categories. After the initial division, the "other" category is allocated between the labor- and plant-related categories in proportion to each category's total so that all costs are classified as either plant or labor related. The categories are then allocated among the jurisdictional entity's (in this case SFPP) functions by multiplying the total labor-related G&A by each function's direct labor ratio, and multiplying the total plant-related G&A by each function's direct plant ratio. Then, within each function, the costs are added together and the ratio of each total to the total amount allocated is that function's KN ratio. The final step is to multiply each G&A cost by the applicable KN ratios in order to

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[129] Exhibit No. SEA-24 at Statement B.

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

[131] Exhibit Nos. SEA-41, ACN-36, Tr. at 409:12-411:13 (Wetmore Cross-examination).

allocate it across the functions.[132]

In this case, Seaway witness Mr. Wetmore performed a simple average to develop his proposed allocation factors.[133] However, the Commission has made clear that under the KN Method, it is inappropriate to use a simple average to calculate the allocation factors.[134] Additionally, Mr. Wetmore used his carrier property in service figures to develop his gross plant allocation factor, which include Seaway's proposed $1.1 billion acquisition adjustment.[135] But the Commission has repeatedly stated that it is inappropriate to include an acquisition adjustment in the gross plant allocation factor when allocating A&G expenses using the KN Method and Massachusetts Formulas.[136] Thus, Seaway's A&G allocation shown on revised Exhibit No. SEA-41 is flawed, and should be rejected.

In order for Seaway's rates to reflect twelve months of actual cost data, and only those A&G costs attributable to the jurisdictional facilities, Ms. Crowe proposes that the "actual O&M assigned by Seaway to its long-haul pipeline in 2011 be used for purposes

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[132] SFPP, L.P., Opinion No. 522, 140 FERC ¶ 61,220 at P 188 (2012)("Opinion No. 522") (citing Kansas-Nebraska Natural Gas Co. Inc., Opinion No. 731, 53 FPC 1691 (1975), order on reh'g, 54 FPC 923, aff'd, Kansas-Nebraska Natural Gas Co. Inc. v. FPC, 534 F.2d 227 (10th Cir. 1976)).

[133] Tr. at 411:19-412:8 (Wetmore Cross-examination).

[134] Opinion No. 511, 134 FERC ¶ 61,121 at PP 148-50.

[135] Tr. at 412:10-413:1 (Wetmore Cross-examination).

[136] See, e.g., Opinion No. 511, 134 FERC ¶ 61,121 at P 142; Opinion No. 511-A, 137 FERC ¶ 61,220 at P 163; SFPP, L.P., 113 FERC ¶ 61,277 at P 89 (2005).

of setting rates in this proceeding, plus an allocated portion of G&A."[137] Specifically, Ms. Crowe proposes to allocate 38 percent of the shared A&G expenses to Seaway's jurisdictional 30-Inch Longhaul pipeline, which has the effect of allocating 62 percent of Seaway's A&G expenses to its non-jurisdictional facilities.[138] Under this methodology, Seaway's O&M expenses, including an allocation of A&G, is approximately $8.9 million.[139]

Ms. Crowe described the derivation of her 38 percent A&G allocation figure as follows:

> The 38% allocation percentage represents the average of the three measures typically used, at least for gas pipelines, to allocate overhead or other indirect costs: gross plant, revenue and direct labor ratios. Using 2011 data provided by Seaway, I calculated these ratios for the Texas City System (including Galena Park), the Freeport System and the Seaway long-haul system. These calculations are shown on Exhibit No. ACN-15. The average of Seaway's ratios for plant, revenue and labor is 38% of the total, with the Texas City System representing 45% of the total, and the Freeport System representing the remaining 17% of the total.[140]

In lieu of Ms. Crowe's O&M proposal, the Trial Staff proposes to use Seaway's actual O&M expenses for the test period.[141] However, Trial Staff annualizes only four months of actual data to develop a twelve-month O&M figure.[142] Further, Trial Staff admitted that its O&M figures mistakenly include A&G costs that should be allocated to

[137] Exhibit Nos. ACN-1 at 19:17-19, 24:13-25:2.

[138] Id. at 20:1-21-4, ACN-15.

[139] Exhibit No. ACN-20.

[140] Exhibit Nos. ACN-1 at 20:1-21:4, ACN-15.

[141] Exhibit No. S-1 at 13:18-22.

[142] Exhibit No. S-21 at 18.

Seaway's non-jurisdictional facilities.[143] Finally, Trial Staff's proposed O&M figures reflect costs associated with Seaway's oil shortage account,[144] despite the fact that Seaway is currently over-recovering for pipeline losses through the Pipeline Loss Allowance ("PLA") it collects in kind from shippers.[145] The Commission has held that where such over-recoveries occur, the amount of over-recovery must be credited to the pipeline's working capital.[146]

Accordingly, if Your Honor adopts Trial Staff's proposal to calculate Seaway's rates based on four months of actual O&M expenses, annualized, a portion of the A&G expenses should be allocated to Seaway's non-jurisdictional facilities using Ms. Crowe's A&G allocation methodology. Additionally, the oil shortage account should be set to zero, and the over-recoveries related to Seaway's PLA revenue should be subtracted from working capital.

C. What is the appropriate level of depreciation expense?

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

D. What is the appropriate cost of capital?

Seaway's overall weighted average cost of capital is 6.90%, which reflects a debt

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[143] Exhibit No. ACN-42 at Stipulation 2.

[144] Exhibit No. S-21 at 18, line 5 ("Oil Losses and Shortages").

[145] Tr. at 347:3-351:24 (Wetmore Cross-examination); Exhibit Nos. SCN-71, SCN-72, SCN-73.

[146] Opinion No. 351, 52 FERC at 61,245.

to equity ratio of 61% to 39%, a debt cost of 5.01%, and a nominal return on equity ("ROE") of 11.28%.[147]

1) What is the appropriate capital structure?

The Commission has held that if a regulated entity does not provide its own financing, it is appropriate to use the capital structure of the parent company or parent companies that do the financing to calculate rates.[148] It is undisputed that Seaway does not provide its own financing.[149] Accordingly, Ms. Crowe developed Seaway's capital structure by averaging the capital structure of Enbridge and Enterprise, Seaway's owners.[150] Using actual average capital structure as of the end of the first quarter 2012 produces a debt to equity ratio of 61% to 39%.[151] Seaway argues that Enbridge's equity ratio is anomalous, and thus, the proxy group companies' capital structures should be used in this case.[152] However, the Commission regularly approves capital structures that reflect a 60/40 debt/equity split.[153] Thus, Enbridge's equity ratio is not anomalous.

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[147] Exhibit Nos. ACN-1 at 21:3-22, ACN-21 at 5, line 14.

[148] See, e.g., BP Pipelines (Alaska) Inc. v. TAPS Carriers, 123 FERC ¶ 61,287 at P 174 (2008) (citing Entrega Gas Pipeline Inc., 113 FERC ¶ 61,327, at P 32 (2005)); Kuparuk Transportation Company, 55 FERC ¶ 61,122, at 61,376-77.

[149] Exhibit No. SEA-15 at 8:14-19.

[150] Exhibit Nos. ACN-1 at 21:3-22

[151] Id.

[152] Exhibit No. SEA-15 at 10:22-24.

[153] 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), Ingelside Energy Center, LLC, 112 FERC ¶ 61,101, at 61,653 (2005)).

2) What is the appropriate cost of debt?

Because Seaway does not provide its own financing, it is appropriate to develop Seaway's cost of debt by averaging the long-term debt cost of its two owners, Enbridge and Enterprise, with one adjustment. As Ms. Crowe testified, Seaway's debt cost data for Enbridge "included debt issued by and attributable to Enbridge Energy Partners, L.P. ("EEP") [that] is not included in Enbridge's reporting of its own long-term debt in its annual report, and should not be included in the calculation of Enbridge's own cost of long-term debt."[154] After excluding debt attributable to EEP from Enbridge's debt costs, the actual average cost of long-term debt for Seaway's two owners using 2012 data is 5.01%.[155] 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%, both of which are comparable to, and confirm the reasonableness of, Ms. Crowe's proposed 5.01% debt cost.[156]

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%.[157] 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.[158] Second, Ms. Crowe used the Commission's preferred Discounted Cash

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[154] Exhibit No. ACN-1 at 22:4-17.
[155] Exhibit Nos. ACN-1 at 21:13-22, ACN-17.
[156] Exhibit No. ACN-40.
[157] Exhibit No. ACN-18 at 1, line "Median Nominal Return on Equity".
[158] Exhibit Nos. ACN-1 at 22:20-23:2, ACN-18. In his rebuttal testimony, Dr.

Flow ("DCF") model to calculate the proxy group companies' returns.[159] In Opinion No. 511, the Commission stated,

> The objective of the Commission's DCF model is to determine the return that must be earned by the regulated entity for the entity to obtain equity capital from investors. The DCF finds that return by examining the percentage returns on equity the market requires for members of a proxy group. The members of the proxy group must fall within a reasonable range of comparable risks and have publically traded securities.[160]

Using the Commission's DCF model, the median ROE for the proxy group companies using six months of data ending September 2012 is 11.28%.[161]

As Ms. Crowe testified, Dr. Fairchild's DCF calculations for his proxy group company returns are inconsistent with Commission policy.[162] The Commission's DCF model calculates the proxy group company returns using the following formula: return=D/P (1+0.5g)+g, where "D" equals the current dividend, "P" equals the company's stock price, and "g" is a composite growth rate that reflects 1) a company-specific short-term growth rate; and 2) a long-term growth rate equal to the projected

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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. However, ACN notes that Dr. Fairchild's updated ROE calculations reduce the median ROE for his proxy group companies to 9.01%. Exhibit Nos. SEA-45 at 21:14-22:2, SEA-49. Accordingly, if Your Honor does not accept ACN's proposed ROE, she should adopt Dr. Fairchild's updated ROE on Exhibit No. SEA-49 on the condition that Seaway re-calculate its DCF results to comply to Commission policy.

[159] Exhibit No. ACN-1 at 21:16-22, 22:18-23:8.

[160] Opinion No. 511, 134 FERC ¶ 61,121 at P 242.

[161] Exhibit Nos. ACN-1 at 21:16-22, 22:18-23:8, ACN-18.

[162] Exhibit No. ACN-1 at 23:2-6.

growth of the United States Gross Domestic Product.[163] The composite growth rate is also known as the two-stage growth rate.

This case concerns the dividend yield adjustment factor, or the (1+0.5g) component of the DCF calculation. Seaway witness Dr. Fairchild proposes to use only the company-specific short-term growth rate in the dividend yield adjustment factor.[164] This approach is inconsistent with Commission policy, and Dr. Fairchild's own testimony in another proceeding, which use the two-stage growth rate in the DCF model.

In Williston Basin, the Commission noted, "[t]he issue of the proper adjustment to the dividend yield to account for the quarterly timing of dividends was the subject of extensive public comments in the Commission's generic rate of return proceedings."[165] In those proceedings, "the Commission found that the proper adjustment to the dividend yield was to multiply the dividend yield by one plus one half of the growth rate, or (1 + 0.5G)."[166] As explained above, the Commission prefers to use a two-stage,

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[163] See, e.g., Williston Basin Interstate Pipeline Company, 50 FERC ¶ 61,284 at n.84 (1990) ("Williston Basin"); Transcontinental Gas Pipeline Company, Opinion No. 414-A, 84 FERC ¶ 61,084 (1998), reh'g denied, Opinion No. 414-B, 85 FERC ¶ 61,323 (1998), aff'd, North Carolina Utilities Commission v. FERC, No. 99-1037 (D.C. Cir. 2000) (per curiam)("Opinion No. 414-A").

[164] Exhibit No. SEA-18; Tr. at 266:25-267:7 (Fairchild Cross-examination).

[165] Williston Basin, 50 FERC ¶ 61,284 at n.86 (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)).

[166] Id.

or composite growth rate as "g" in its DCF model.[167]

In recognition of these Commission's policies, as recently as 2010, Dr. Fairchild filed testimony and exhibits with the Commission that used a composite, or two-stage growth rate, in the dividend yield adjustment factor.[168] Dr. Fairchild did not provide any compelling reason for his proposal to use a different methodology in this case. Given that Dr. Fairchild's approach is inconsistent with his own methodologies in other cases, and Commission policy, it should be rejected.

Finally, if Your Honor approves any portion of Seaway's proposed $1.1 billion purchase price adjustment, Seaway's ROE should be based on the low end of the range of proxy group returns. This is because, as Ms. Crowe testified:

> Seaway's proposed PPA will afford Seaway's owners, through its affiliated shippers, substantial opportunity to exercise market power and earn significant profit margins above actual cost levels. This fact, coupled with the unprecedented size of the proposed write-up itself, warrant a substantial reduction in allowed ROE in this proceeding if any PPA is approved for ratemaking. Otherwise, the Commission will have endorsed excessive profits embedded within the write-up itself, and compounded the problem by approving a median ROE to be attributed to the write-up.[169]

4) What is the appropriate cost of preferred stock?

ACN does not take a position on this issue.

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

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[167] See Opinion No. 414-A, 84 FERC at 61,425-26 and 61,411; Tr. at 266:5-17 (Fairchild Cross-examination).

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

[169] Exhibit No. ACN-1 at 23:9-20.

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 only one of its two owners actually incurs an income tax liability. As Ms. Crowe testified, Enterprise is a master limited partnership ("MLP"), and MLPs do not pay income taxes.[170] Accordingly, Enterprise will not incur an income tax liability for its 50 percent ownership stake in Seaway.[171] Under cost of service ratemaking, the rates charged for jurisdictional service should only include costs actually incurred by, or attributable to, a regulated entity.[172] For income tax purposes, this means that "[w]here the pipeline incurs income tax liability by virtue of being owned by a corporation, income taxes are properly included in cost-based rates. Where the entity owning the pipeline does not pay income taxes, they should not be included in the pipeline's cost of service."[173] To account for the fact that one of the owners of Seaway will not incur a tax liability for its ownership stake in Seaway, Seaway should only be permitted to recover 50 percent of the otherwise applicable income tax allowance in its rates.

Further, if Your Honor approves Seaway's proposal to include the $1.1 billion acquisition adjustment in rate base, Seaway should not be permitted to calculate income taxes on the approximately $627 million goodwill portion of the write-up, because

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[170] Exhibit No. ACN-1 at 25:13-23.

[171] Id.

[172] Exhibit No. ACN-1 at 25:23-26:5.

[173] Id.

Enbridge expects that the goodwill associated with the acquisition will be tax deductible for U.S. income tax purposes.[174]

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?

The Commission's policies and precedent require that the throughput used to calculate Seaway's rates be based on the pipeline's design capacity. Seaway witness Mr. Wetmore conceded this point in his testimony, stating, "it is appropriate to use volumes equal to Seaway's initial design capacity and to match revenues to those volume levels."[175]

The primary difference between ACN's throughput figures and Seaway's throughput figure relate to when to measure the pipeline's design capacity. Seaway proposes to measure and use the pipeline's design capacity from June 2012 through December 2012, when the design capacity was 135,000 barrels per day, to calculate rates in this proceeding.[176] Conversely, ACN proposes to take into account Seaway's design capacity during both the pre-expansion period (from June 2012 to December 2012) and

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[174] Exhibit No. ACN-1 at 26:6-10.

[175] Exhibit Nos. SEA-22 at 18:5-8, SEA-26 at 51:15-19 (citing White Cliffs Pipeline, L.L.C., 126 FERC ¶ 61,070 at P 31 (2009); Enbridge Energy Company, Inc., 110 FERC ¶ 61,211 at P 46 (2005); Enbridge Pipelines (Southern Lights) LLC, 122 FERC ¶ 61,170 at P 10 (2008)).

[176] Exhibit No. SEA-26 at 51:13-19.

the post-expansion period (after January 2013).[177] Seaway's proposal to only consider its pre-expansion design capacity when calculating rates in this proceeding 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 agrees that it is appropriate, albeit conservative, to calculate rates for the pre-expansion period using the June 2012 through December 2012 design capacity of 135,000 barrels per day.[178] However, Seaway's rates going forward must reflect the pipeline capacity that was added to the system during the twelve-month test period in this case. It is undisputed that during Seaway's first twelve months of operations, its pipeline capacity significantly increased.[179] Thus, the Commission's test period regulations require that the post-expansion capacity also be considered when calculating Seaway's rates in this case.

Seaway's proposal to use its pre-expansion capacity to calculate rates will not produce just and reasonable cost-based rates. This is because, as Mr. Wetmore admitted at hearing, the costs and revenues on Exhibit No. SEA-24 do not match Seaway's post-

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[177] Exhibit No. ACN-1 at 6:2-19.

[178] Exhibit No. ACN-1 at 27:12-20, SEA-40 (showing that Seaway's actual throughput regularly exceeded 135,000 barrels per day during the pre-expansion period).

[179] See Exhibit No. SEA-39 at 4:9-18.

expansion pipeline capacity.[180] In other words, Seaway's rate calculation does not take into account the higher revenues attributable to the post-expansion capacity.

Additionally, the record shows that Seaway's capacity nearly tripled as the result of the January 2013 expansion, while its costs did not substantially increase.[181] Thus, as Ms. Crowe testified, Seaway's per-unit cost of providing service (cost of service divided by throughput) significantly decreased as a result of the expansion.[182] Seaway's proposal to continue using the 135,000 barrels per day figure to calculate rates going forward does not reflect its actual per-unit cost of providing jurisdictional service.

Further, if adopted, Seaway's proposed throughput will provide Seaway with an unjustified and unreasonable windfall. As an initial matter, Seaway's own internal documents show that Seaway's projected 2013 revenues **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]**.[183] The majority of this windfall is likely due to the fact that Seaway expects to ship significant volumes on the post-expansion facilities at its filed tariff rates.

Under Seaway's throughput proposal, Seaway will recover its cost of service if it ships 135,000 barrels of crude oil each day. It follows, then, that if Seaway ships more than 135,000 barrels per day, it will over-recover its cost of service. The record evidence

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[180] Tr. at 313:22-25, 408:17-409:8 (Wetmore Cross-examination).

[181] Exhibit No. ACN-1 at 6:2-19.

[182] Id., Exhibit No. ACN-5 at 3, 17.

[183] Exhibit No. SCN-57; Tr. at 415:14-18 (Wetmore Cross-examination).

and Seaway's own witness testimony establishes that Seaway has shipped, and will continue to ship, volumes well in excess of 135,000 barrels per day.

Seaway witness Mr. Ordemann testified that he does not believe that Seaway's proposed 135,000 barrels per day throughput figure is representative of the throughput that Seaway expects to experience in the future, because it is too low.[184] In fact, Mr. Ordemann admitted that Seaway shipped 333,000 barrels in a single day in February 2013, and Seaway shipped an average of 272,000 barrels per day for the entire month.[185] Moreover, based on Seaway's own data and projections, Seaway shipped, or is projected to ship, volumes in excess of 135,000 barrels per day (on an average, monthly basis) for six out of the twelve months in the test period in this case.[186]

In sum, Seaway's proposal to determine just and reasonable rates using the pipeline's 135,000 barrels per day design capacity in December 2012 should be rejected. The 135,000 barrels per day figure should only be used to calculate Seaway's rates for the period June 2012 through December 2012, when Seaway's capacity was limited to that figure. Seaway's rates for January 2013 and going forward should reflect the pipeline's post-expansion design capacity.

The substantial record evidence establishes that Seaway's post-expansion design

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[184] Tr. at 142:20-143:1 (Ordemann Cross-examination).

[185] Tr. at 179:6-13

[186] Exhibit No. SEA-40 at 1, line 6.

capacity is 400,000 barrels per day.[187] In fact, Seaway witness Mr. Ordemann submitted a data request response explaining that the post-expansion design capacity is 400,000 barrels per day.[188] And when asked at hearing if Seaway is currently capable of shipping up to 417,000 barrels per day, Mr. Ordemann answered in the affirmative.[189] He also testified that during February 2013, Seaway flowed at a rate of 380,000 barrels per day.[190]

Nevertheless, Mr. Ordemann testified that it is not appropriate to use 400,000 barrels per day to calculate Seaway's rates going forward, because Seaway's projected, actual throughput is expected to be between 295,000 and 335,000 barrels per day.[191] However, the distinction between actual barrels shipped and design capacity is material. The Commission has made clear, and Seaway has conceded, that the pipeline's design capacity should be used as the throughput to calculate rates in this proceeding.[192] The Commission has held that a pipeline may only calculate initial rates using actual volumes shipped when the pipeline has implemented a safeguard against over-

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[187] See, e.g., Exhibit Nos. S-28 at 1; 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,

[188] Exhibit No. SCN-10 at 2 ("the pump additions and modifications that are expected to take effect in early 2013, are anticipated to increase Seaway's capacity to (not by) approximately 400,000 barrels per day depending upon the mix of crude oil transported.")

[189] Tr. at 83:8-17 (Ordemann Cross-examination).

[190] Tr. at 144:1-21 (Ordemann Cross-examination); Exhibit No. S-28.

[191] Exhibit No. SEA-39 at 4:9-18;

[192] Exhibit Nos. SEA-22 at 18:5-8, SEA-26 at 51:15-19 (citing White Cliffs Pipeline, L.L.C., 126 FERC ¶ 61,070 at P 31; Enbridge Energy Company, Inc., 110 FERC ¶ 61,211 at P 46; Enbridge Pipelines (Southern Lights) LLC, 122 FERC ¶ 61,170 at P 10).

recovery, such as a revenue sharing mechanism.[193] Seaway could have implemented such a safeguard, and it chose not to. Accordingly, Seaway is bound by Commission precedent to calculate rates based on its design capacity, which is now 400,000 barrels per day.

Moreover, the record evidence establishes that Seaway can expect to run at its full capacity, given shipper demand and existing volume commitments. The shipper demand for capacity on the Seaway pipeline is so robust that Seaway has had to allocate its available capacity to shippers since the reversed pipeline went into service in May 2012.[194] Additionally, following the 2013 expansion project, Seaway's committed shipper volumes **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** barrels per day.[195] Seaway's committed shippers have a ship-or-pay obligation that requires them to ship their committed volumes, or pay a deficiency rate for the volumes that they do not ship.[196] This incentivizes Seaway's committed shippers to ship the full amount of their committed volumes in a given month. It also provides Seaway with revenue for the full

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[193] Opinion No. 522, 140 FERC ¶ 61,220 at P 50 ("[I]t is appropriate for the Commission to use conservative throughput estimates. Without any data regarding the pipeline's actual operating experience, the Commission imposes safeguards against over-recovery by requiring the pipeline to use its designed capacity to determine throughput.") (citing White Cliffs Pipeline, L.L.C., 126 FERC ¶ 61,070 at P 31; Enbridge Energy Company, Inc., 110 FERC ¶ 61,211 at P 44).

[194] Exhibit No. S-31; Tr. at 127:16-23 (Ordemann Cross-examination).

[195] Exhibit No. ACN-8, column "2013," row "Total."

[196] Exhibit No. SEA-4 at 9 (Section 3.01-"Ship or Pay Obligation") and 13-16 (Section 7-"Shortfall Payments").

amount of the committed volumes, even if its committed shippers never ship a single barrel of oil.[197]

Finally, to the extent Your Honor determines that Seaway's actual volumes shipped are relevant to this proceeding, Seaway's actual and projected volumes are not representative of the volumes Seaway can expect to ship on the post-expansion pipeline. Regarding Seaway's projected volumes, Seaway did not provide any evidentiary support for the February 2013 through May 2013 volume projections described in Mr. Ordemann's testimony, and shown on Exhibit No. SEA-40. Additionally, Mr. Ordemann's projections for April and May 2013 are inconsistent with Seaway's own internal documents, which project that Seaway will ship **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** barrels per day during those months.[198]

Regarding Seaway's actual volumes shipped, the record evidence shows that Seaway's volume data for the post-expansion period are understated and/or anomalous. First, the record only includes one full month of throughput data for the post-expansion period. As Mr. Ordemann testified at hearing, Seaway was taken out of service on January 2, 2013 to effectuate the expansion.[199] The expansion facilities did not come on

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[197] Tr. at 416:20-420:2, 422:9-17 (Wetmore Cross-examination).
[198] Exhibit No. SCN-57.
[199] Tr. at 132:12-133:3 (Ordemann Cross-examination).

line until January 11, 2013.[200] As such, the average barrels per day throughput figure shown on Exhibit No. SEA-40 for January 2013 is understated. Additionally, Seaway's January and February 2013 volumes are anomalous for two reasons. First, Enterprise issued a curtailment order in January that decreased deliveries on Seaway.[201] Second, on an Enterprise earnings call on January 31, 2013, Mr. Ordemann admitted that a bottleneck at certain takeaway facilities (i.e., refineries, storage tanks, and on the pipelines in Jones Creek, Texas) is affecting deliveries on Seaway.[202] On that same earnings call, Mr. Ordemann stated that the bottleneck will be alleviated before the end of 2013.[203]

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

Seaway's uncommitted rates should be calculated using the Commission's fully-allocated cost of service method for producing cost based rates. According to the Commission, "the traditional method for determining whether an oil pipeline's jurisdictional rates are just and reasonable is in fact a fully allocated cost

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[200] Id.

[201] Exhibit No. 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."); Tr. at 133:18-22 (Ordemann Cross-examination).

[202] 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 ("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.")

[203] Id.

methodology…i.e., the pipeline files a conventional cost-of-service with projected throughput and proposes a per barrel rate for the various markets and services involved."[204]

Consistent with this precedent, Seaway's uncommitted rates should be designed by adjusting Seaway's proposed cost of service to reflect ACN's positions discussed above, and dividing that cost of service by Seaway's design capacity.[205] "The resulting rate is thus a cost-based average unit rate for transportation on the reversed Seaway pipeline system."[206]

Seaway contends that the committed rates are discounted, relative to the uncommitted rates.[207] Seaway also argues that it is appropriate to shift the shortfall that is not recovered from committed shipper rates to the uncommitted shippers through a revenue crediting mechanism.[208] The revenue crediting mechanism subtracts the revenues collected from committed shippers from the pipeline's cost of service, and then calculates a rate based on the uncommitted shipper volumes.[209]

However, Seaway witness Mr. Wetmore admitted that "[i]f the committed rates are above the average rate, then the revenue credit approach could not be used and the

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[204] Williams Pipe Line Company, 84 FERC ¶ 61,022, at 61,098 and 61,109 (1998).
[205] Exhibit No. ACN-1 at 27:12-29.
[206] Id.
[207] Exhibit No. SEA-22 at 19:3-20:15.
[208] Id.
[209] Id.

uncommitted rates would be assessed based on the average rate."[210] This is because if the committed rates are higher than the average rate (or, unit rate), then the committed rates are not discounted rates, and there is no reason to employ a discount adjustment.

In the instant case, Seaway's committed rates are higher than the unit rate.[211] Thus, as acknowledged by Mr. Wetmore, it is not appropriate to use the revenue crediting mechanism to shift costs from Seaway's committed shippers to its uncommitted shippers,[212] because the committed rates are not discounted rates. Indeed, Seaway's revenue crediting proposal produces illogical results, when applied to a just and reasonable cost of service. Seaway calculated that it will collect $111,540,000 from its committed shippers during the 12-month test period.[213] Even assuming Seaway's committed shipper revenue calculation is accurate (which, as discussed below, it is not), subtracting Seaway's committed shipper revenues from a just and reasonable cost of service will produce a negative uncommitted shipper rate.[214] Under these facts, the revenue crediting mechanism is not just and reasonable.

Further, Seaway's revenue crediting methodology on Exhibit Nos. SEA-24 and

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[210] Exhibit No. SEA-26 at 58:10-13.

[211] 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).

[212] Exhibit No. SEA-26 at 58:10-13.

[213] Exhibit No. SEA-36 at 4, line 2 and 22, column "Annualized Test Period."

[214] 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.)

SEA-36 materially understates the committed shipper revenues that Seaway will collect during the test period, and going forward. Seaway would credit between $100,193,000 and $111,540,000 of committed shipper revenues to its cost of service.[215] These figures do not include revenues that Seaway collects from committed shippers for their ship-or-pay obligations. Seaway will collect revenues for all of the committed volumes on its system, regardless of whether those committed volumes are actually shipped.[216] Seaway's revenue crediting analysis only takes into account the revenues that Seaway collects for the volumes shipped, and thus understates Seaway's revenues.

Additionally, Seaway's revenue crediting mechanism does not take into account the fact that Seaway's **[BEGIN HIGHLY CONFIDENTIAL MATERIALS]** [redacted] **[END HIGHLY CONFIDENTIAL MATERIALS]** as a result of the expansion that took place in mid-January, 2013.[217] Suncor Energy Marketing, Inc. and Canadian Natural Resources, Limited (jointly, "SCN") witness Steven Levine took the January 2013 expansion capacity into account, and calculated Seaway's committed shipper revenues during the 12-month test period to be **[BEGIN HIGHLY**

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[215] Exhibit Nos. SEA-24 at Statement A2, line 2, SEA-36 at 4, line 2.

[216] Tr. at 416:20-420:2, 422:9-17 (Wetmore Cross-examination).

[217] Exhibit Nos. ACN-1 at 6:5-8, ACN-8, SEA-1 at 12:14-13:9 (explaining that Seaway's rate calculation on Exhibit No. SEA-24 only reflected projected volumes and revenues for the pre-expansion period, from June through December 2012), SEA-26 at 54:23-55:6 (explaining that Seaway's rate calculation on SEA-36 reflected "annualized actual...volumes for the period June 2012 through January 2013.") For the reasons stated in Section 5 of this initial brief, Seaway's January 2013 volumes do not reflect the expansion capacity.

CONFIDENTIAL MATERIALS] [redacted] [END HIGHLY CONFIDENTIAL MATERIALS].[218] In sum, Seaway's committed shipper revenues are materially understated, and its revenue crediting methodology should be rejected.

Trial Staff proposes to calculate Seaway's uncommitted rates by adjusting a cost-based, unit rate to reflect a differential, relative to a cost-based committed rate.[219] If Your Honor determines that it is appropriate to calculate uncommitted rates that are higher than a cost-based committed rate, as Trial Staff proposes, the basis for the differential must be cost-based.[220] Ms. Crowe suggests that one way to do this would be to calculate Seaway's cost-based committed rate using a cost of service that reflects an ROE at the low end of proxy group returns, while calculating the uncommitted rate using the median ROE.[221]

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

As Ms. Crowe testified, Seaway did not provide any cost-based evidence to support its proposed differential between heavy and light crude oil shipments.[222] When asked to provide support for the differential between the rates for light and heavy crude oil shipments, Seaway simply referred to the fact that its filed rates are negotiated

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[218] Exhibit No. SCN-1 at 9:3-10:2.
[219] Exhibit No. S-14 at 17:16-24.
[220] Exhibit No. ACN-23 at 9:18-13:7.
[221] Id.
[222] Exhibit No. ACN-23 at 10:10-13.

rates.[223] Thus, the differential is not justified on a cost-basis.

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

Based on the positions taken in this initial brief, Seaway's just and reasonable uncommitted rate for the pre-expansion period (June 2012 through December 2012) is \$0.5050 per barrel.[224] Notably, this rate is comparable to Seaway's rates on the pre-reversal pipeline.[225] Taking into account the capital additions required to effectuate the reversal, and Seaway's post-expansion design capacity, produces a just and reasonable rate for January 2013 and going forward of \$0.1803.[226] Ms. Crowe determined:

> [t]his rate is 64% lower than the \$0.5050/bbl rate for initial service discussed above. As this comparison shows, it is very important that the Commission establish two separate sets of rates in this proceeding in order to preclude Seaway from earning even greater levels of excessive profit at the expense of its ratepayers.[227]

However, ACN acknowledges that if Seaway's committed rates are not adjusted in this proceeding, Seaway will over-recover its cost of service even if Your Honor approves ACN's proposed uncommitted rates. This is because the record evidence shows that Seaway will collect revenues that substantially exceed its cost of service from its committed shippers alone.[228] Accordingly, it may be appropriate for Your Honor to also adopt a revenue sharing mechanism similar to those on other oil

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[223] Exhibit No. ACN-41.
[224] Exhibit No. ACN-21 at 3, line 10.
[225] Exhibit No. ACN-1 at 28:5-7.
[226] Exhibit No. ACN-22 at 3, line 10.
[227] Exhibit No. ACN-1 at 28:18-29:3.
[228] Exhibit No. SCN-1 at 9:3-10:2.

pipelines, whereby Seaway must return to shippers any revenues it collects in excess of a just and reasonable cost of service.

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

For the reasons explained in Section 6 of this initial brief, if Your Honor determines that it is appropriate to calculate Seaway's committed rates in this proceeding that reflect a differential, relative to Seaway's uncommitted rates, any such differential must be cost-based.[229]

IV. FINDINGS OF FACT AND CONCLUSIONS OF LAW

ACN Proposed Findings of Fact:

1. Seaway's proposed cost of service is excessive.
2. Seaway's filed rates are not based on, or supported by, Seaway's underlying cost of providing service.
3. Seaway's proposed test period fails to take into account the increase in costs, capacity, committed volumes, and revenues associated with the material expansion project that went into service in January 2013.
4. Seaway's per-unit cost (cost of service divided by throughput) for the post-expansion period in 2013 is significantly lower than its per-unit cost before the expansion went into service.
5. Seaway has not shown that the Commission has approved an acquisition adjustment that nears the magnitude of the 1,755 percent rate base write-up it proposes here.
6. Seaway's proposal to include a $1.1 billion write-up in excess of the net book value of the Seaway assets will afford Enterprise and Enbridge a windfall, relative to the cost of service using the net book value of the same assets.

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

7. Under Seaway's proposed cost of service, Enterprise (as half-owner of Seaway) would earn revenues sufficient to afford it a return of, and on, a $585 million investment in Seaway.

8. If Seaway is permitted to include the acquisition adjustment in rate base, those shippers that have shipped on both the pre- and post-reversal pipeline will pay rates that reflect a higher depreciation expense, even though the pipeline facilities have not changed.

9. Seaway did not need to choose between purchasing and converting an existing pipeline and constructing new facilities; it merely reversed the flow on the pipeline that was already in service.

10. Seaway has not shown that its shippers saved any money by virtue of the fact that Enbridge spent $1.1 billion to purchase its 50 percent interest in Seaway.

11. Enbridge could have constructed its own pipeline with 400,000 to 450,000 barrels per day of capacity for $1.3 billion.

12. Exhibit No. SEA-28, which purports to show the economic benefit of including the $1.1 billion purchase price in Seaway's rates, does not actually reflect the cost effect of the $1.1 billion write-up.

13. Exhibit No. SEA-28 merely shows that Seaway's shippers can profit by shipping their oil on Seaway at the average rate.

14. Any economic benefits associated with service on Seaway will ultimately accrue to Seaway's owners and affiliates, while the unaffiliated, third-party shippers will pay the price.

15. Goodwill is the value paid for the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized.

16. The goodwill associated with Enbridge's purchase of its interest in Seaway is $627 million.

17. Seaway did not show that the purchase price attributable to the other, unidentified assets (for which it paid the $627 million of goodwill) benefit its shippers in any way, nor did it establish that these amounts are related to the provision of jurisdictional service.

18. The goodwill that Enbridge paid when it purchased Seaway is related to the future economic benefit that Enbridge will experience by expanding its Flanagan pipeline upstream of Seaway.

19. The record does not support Seaway's proposal to assign 100 percent of the acquisition premium to Seaway's jurisdictional assets.

20. The fair value of Enbridge's share of Seaway's non-jurisdictional assets is $ 196,058,000.

21. The purchase price attributable to Seaway's jurisdictional 30-Inch Longhaul System, exclusive of goodwill, is $331,351,000.

22. Seaway provided south-to-north crude oil transportation service until March 2012, when the pipeline was taken out of service and reversed.

23. Seaway has already recovered AFUDC on, and been compensated for its investment in, the existing pipeline assets through its rates charged for south-to-north service.

24. Enbridge collected revenues associated with the south-to-north service on Seaway prior to the pipeline going out of service in March 2012.

25. Seaway's proposal to accrue AFUDC on Enterprise's share of the existing pipeline facilities and the purchase price Enbridge paid for its share of Seaway will permit Seaway to double-recover its debt and equity costs.

26. Seaway's O&M projections are overly subjective, arbitrary, and excessive.

27. It is appropriate to allocate 38 percent of the shared A&G expenses to Seaway's jurisdictional facilities, and 62 percent to the non-jurisdictional facilities.

28. The actual O&M costs assigned by Seaway to its 30-Inch Longhaul System in 2011 reasonably reflect twelve months of actual cost data.

29. Seaway's overall weighted average cost of capital is 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%.

30. Ms. Crowe's 39% equity ratio is not anomalous.

31. Enterprise will not incur an income tax liability for its 50 percent ownership stake in Seaway.

32. Seaway's design capacity for the pre-expansion period (from May 2012 through December 2012) was 135,000 barrels per day.

33. Seaway's design capacity for the post-expansion period (after January 2013) is 400,000 barrels per day.

34. Seaway has shipped, and will continue to ship, volumes well in excess of 135,000 barrels per day.

35. Seaway can expect to run at its full capacity, given shipper demand and existing volume commitments.

36. Seaway's committed shippers have a ship-or-pay obligation that requires them to ship their committed volumes, or pay a deficiency rate for the volumes that they do not ship.

37. Seaway's actual and projected volumes for January 2013 through May 2013 are not representative of the volumes Seaway can expect to ship on the post-expansion pipeline.

38. Seaway's revenue crediting methodology on Exhibit Nos. SEA-24 and SEA-36 materially understates the committed shipper revenues that Seaway will collect during the test period, and going forward.

39. Seaway's proposed differential between its uncommitted light and uncommitted heavy rate is not cost based.

ACN Proposed Conclusions of Law:

1. Seaway's filed rates are not just and reasonable under the Commission's regulations, precedent, cost-based ratemaking principles, and Section 1(5) of the ICA.

2. The proper test period in this case is June 2012 through May 2013.

3. Seaway's proposal to calculate rates in this proceeding by using projected costs and revenues for a seven-month period, from June 2012 through December 2012, is inconsistent with the Commission's test period regulations and ratemaking policies and precedent.

4. The Commission's test period regulations and precedent do not distinguish between an "initial period of operations" and any subsequent period of operations.

5. Given that Seaway's per-unit cost of service is different for the pre- and post-expansion periods, it is not possible to calculate one just and reasonable rate based on the test period data in this rate proceeding.

6. It is not appropriate to use Seaway's pre-expansion costs and design capacity or throughput to calculate Seaway's rates applicable to the post-expansion period.

7. It is appropriate and reasonable to calculate two sets of rates for Seaway in the instant proceeding. The first set of rates should reflect Seaway's cost of service and design capacity for the pre-expansion test period months, from June 2012 through December 2012. The second set of rates should reflect the increased costs and higher design capacity that Seaway experienced during the post-expansion test period months, from January through May 2013.

8. The carrier property in service amount in Seaway's rate base should reflect the net book value (original cost less depreciation) of the assets devoted to jurisdictional service, and any capital additions that are related to the capacity that is in service at the end of the test period.

9. 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 is inconsistent with the Commission's original cost ratemaking policies and precedent.

10. If the $1.1 billion acquisition adjustment is included in Seaway's rates, then Enterprise will be afforded a significant and unjustified windfall for the price Enbridge paid for its interest in Seaway, in violation of Commission policy.

11. Enbridge's acquisition of its interest in Seaway does not warrant an exception to the Commission's original cost ratemaking policies and precedent.

12. Seaway does not satisfy the first prong of the substantial benefits test, because Seaway is not providing a new or materially changed service.

13. Seaway does not satisfy 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.

14. It is not necessary to analyze any cost savings, relative to the cost to construct an identical pipeline, in the instant case.

15. Seaway has not demonstrated that the alleged economic benefits are directly related to the acquisition.

16. The goodwill associated with Enbridge's acquisition of its interest in Seaway should not be included in Seaway's rate base.

17. Under the Commission's precedent and Uniform System of Accounts, a purchase price is generally comprised of two components: 1) the fair value, or market value, of the tangible assets purchased (which may exceed the net book value of those assets); and 2) goodwill.

18. 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.

19. Seaway should be required to allocate the $1.15 billion purchase price to the jurisdictional and non-jurisdictional assets based on the fair market value of those assets, as reflected in Enbridge's own accounting entries.

20. Seaway should only be permitted to accrue AFUDC on its actual investment in new, incremental plant under construction.

21. Seaway's proposal to accrue AFUDC on both Enterprise's share of Seaway's existing pipeline facilities and on the proposed $1.1 billion purchase price adjustment for Enbridge's share of Seaway is inconsistent with the Commission's policies and precedent regarding AFUDC, and does not constitute just and reasonable ratemaking.

22. AFUDC does not accrue on the funds a pipeline expended to purchase an ownership stake in a regulated entity from the date of the acquisition.

23. Seaway's O&M expenses should reflect objective, actual cost data for a twelve-month period, and its A&G expenses should be allocated among Seaway's jurisdictional and non-jurisdictional services and facilities in a manner that is consistent with Commission precedent.

24. Seaway's O&M cost projections for the period June 2012 through December 2012 are inconsistent with the Commission's test period ratemaking policies and regulations.

25. Seaway's A&G allocation is not consistent with Commission precedent.

26. It is appropriate to use the capital structure of the parent companies that do the financing (Enbridge and Enterprise) to calculate Seaway's rates.

27. Because Seaway does not provide its own financing, it is appropriate to develop Seaway's cost of debt by averaging the long-term debt cost of its two owners, Enbridge and Enterprise.

28. Dr. Fairchild's DCF calculations use the wrong growth rate in the dividend yield adjustment factor, and therefore do not comply with Commission policy.

29. 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 only one of its two owners actually incurs an income tax liability.

30. The Commission's policies and precedent require that the throughput used to calculate Seaway's rates be based on the pipeline's design capacity.

31. 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.

32. Seaway's uncommitted rates should be calculated using the Commission's fully-allocated cost of service method for producing cost-based rates.

33. Seaway's proposed revenue crediting mechanism is not just and reasonable.

34. Any proposed differential between committed and uncommitted shipper rates, and between the uncommitted rates for light and heavy crude oil shipments, must be cost-based.

35. Seaway's just and reasonable uncommitted rate for the pre-expansion period (June 2012 through December 2012) is $0.5050 per barrel.

36. Seaway's just and reasonable uncommitted rate for the post-expansion period (January 2013 and going forward) is $0.1803 per barrel.

WHEREFORE, ACN requests Your Honor to adopt the Findings of Fact and Conclusions of Law of ACN as set forth above.

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: May 7, 2013

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 7th day of May, 2013.

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