BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of Union Electric Company, d/b/a Ameren Missouri's Tariff to Increase Its Revenues for Electric Service.	))))	**Case No. ER-2014-0258** Tariff No. YE-2015-0003

STAFF'S REPLY BRIEF

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<u>STAFF'S REPLY BRIEF</u>

COMES NOW the Staff of the Missouri Public Service Commission, by and through counsel, and for its *Reply Brief,* states as follows:

<u>INTRODUCTION</u>

The purpose of a *Reply Brief* is to respond to the arguments made by parties opponent. In its *Reply Brief,* Staff will explain why the Commission should not be swayed by the arguments raised by Ameren Missouri, whose positions, after all, are intended to maximize value for the Company's shareholders.[1]

In determining each contested issue, the Commission should be ever mindful that the law places the burden of proof on the Company. Section 393.150.2, RSMo., provides:

> At any hearing involving a rate sought to be increased, the burden of proof to show that the increased rate or proposed increased rate is just and reasonable shall be upon the . . . electrical corporation . . . and the commission shall give to the hearing and decision of such questions preference over all other

[1] ***Robinson v. Lagenbach,*** 439 S.W.3d 853, 860 (Mo. App., E.D. 2014) (citations omitted): "The officers and directors of a corporation occupy a fiduciary relationship to the corporation and to the shareholders. Their position is one of trust, and in the event of a conflict, they are bound to act with fidelity and to subordinate their personal interest to the interest of the company. This fiduciary duty requires corporate directors and officers to exercise the utmost good faith in the discharge of their duties and to act for the corporation and its shareholders, giving all the benefit of their best judgment."

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questions pending before it and decide the same as speedily as possible.

What exactly does it mean that the Company has the burden of proof? In its most basic sense, the burden of proof is "that of establishing the affirmative of the ultimate issue[.]"[2] In practical terms, it means that the Company must prove that rates should be increased and any failure of proof means that the Company loses. This burden never shifts away from the Company.[3]

--Kevin A. Thompson.

ARGUMENT

1. Weather Normalization Issues:

What level of sales to Noranda should be assumed for the test year for purposes of establishing billing units?

This issue, like so many other issues in this case, has to do with risk. Given that Noranda is the only customer in the LTS Rate Class and given that certain costs are allocated to the LTS Class in the design of rates, the issue is who bears the risk if Noranda does not actually buy as much service as expected? In that case, AmMo would experience a loss (as it did in the famous ice storm of 2009). But the other side of this coin is the risk that Noranda will buy more service than expected. In that case, AmMo gets a windfall! Like everything to do with Noranda, that windfall might be several millions of dollars. That is why you are hearing this issue.

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[2] ***Been v. Jolly,*** 247 S.W.2d 840, 854 (Mo. 1952).

[3] *Id.*

Based on information from both AmMo and Noranda, Staff assumes that Noranda's reduction in energy consumption during the update period is not normal and should not be expected to continue going forward.[4]
** ____ ____ ____ ____ ____ ____ ____ ____ ____ ____ ____ ____ ____ ____

____ ____ ____ . **[5] Staff urges the Commission to keep firmly in mind that the important issue here is NOT Noranda's load factor, as AmMo would have the Commission believe, but its billing determinants.[6] After all, the load factor can vary without usage actually decreasing.[7] Staff continues to recommend the use of normalized Test Year billing determinants for the LTS Class, that is, Noranda.[8]

Staff recommends the Commission use normalized test year kWh sales for the LTS Class for the purpose of establishing billing units in this case. Staff and Ameren Missouri both found the calculation of the LTS Class energy usage during the test year to be approximately 4.3 billion kWh.[9] The LTS Class consists of a single customer, Noranda.[10] Instead, AmMo proposes a three-year average of Noranda's actual energy usage, and hypothetical demands that AmMo developed by assuming a Noranda load factor of 97%. AmMo's proposal

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[4] S. Kliethermes Surrebuttal, p. 32.
[5] Greg Meyer, Tr. 30:2099.
[6] *Id.,* pp. 277-78.
[7] *Id.,* pp. 276-77.
[8] S. Kliethermes Surrebuttal, p. 32.
[9] S. Kliethermes Surrebuttal, p. 32.
[10] Admission of Wendy Tatro, Tr. 16:246 (opening statement).

would reduce Noranda's usage for billing determinants in this case to 4,139,345 MWh annually from its test year level of 4,345,485 MWh.[11]

What is driving AmMo's proposal? Since Noranda is the only customer in the LTS Class, if Noranda does not take as much service as was assumed when rates are set, then there are no other LTS customers to pick up the slack.[12] Why does Staff oppose AmMo's proposal? Because underestimating the Noranda billing determinants will result in an over-collection for AmMo.

Staff urges the Commission to put AmMo's business risk right where it belongs, which is on AmMo. That is the one and only party that should bear the risk of any "fluctuations" in Noranda's billing determinants. Contrary to AmMo's attitude throughout this case, its customers are NOT its insurers. If the Commission makes the adjustment sought here by AmMo, however small it may appear, it will improperly shift the Company's business risk to the ratepayers. It will expose the ratepayers to a shift of millions of their dollars to AmMo.

--Kevin A. Thompson.

2. Income Tax Issues:

Staff's position is that AmMo's income taxes must, for regulatory purposes, be treated in the manner most advantageous to the ratepayers. Sometimes, that will mean accepting AmMo's tax position as filed. Other times, that will mean imputing a tax position to AmMo other than that actually filed. In all cases, the advantage of the ratepayers must control.

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[11] S. Kliethermes Surrebuttal, p. 32.

[12] Wendy Tatro, Tr. 16:246-7 (opening statement).

AmMo asserts, "as the Commission is aware, it cannot simply resolve rate case issues by choosing the position that results in the lowest possible rates."[13] The Commission must instead, AmMo contends, set "just and reasonable rates."[14] AmMo is right, so far as that goes. But what is the appropriate treatment for sophisticated corporate tax maneuvers? Must the Commission allow AmMo to take a tax position favorable to its shareholders at the expense of its ratepayers?

The answer, of course, must be "no." As the Missouri Supreme Court explained long ago, "as a part of its duty of setting reasonable rates, the commission has the power to treat some items of operating expense differently than others [but] . . . such separate treatment must be effectuated in compliance with all of the statutes governing the PSC and with the purpose behind those statutes."[15] The Court further noted that the purpose of the Public Service Commission Law is "to protect the consumer against the natural monopoly of a public utility, as provider of a public necessity, while at the same time permitting a recovery by the utility of a just and reasonable return."[16] "The spirit of this policy is the protection of the public. The protection given the utility is incidental."[17] The principle that necessarily emerges is that the Commission may treat tax

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[13] *AmMo's Brief,* pp. 31-32.

[14] *Id.*

[15] ***State ex rel. Utility Consumers' Council of Missouri, Inc. v. Public Service Commission,*** 585 S.W.2d 41, 52-53 (Mo. banc 1979) (***"UCCM"***).

[16] *Id.,* 585 S.W.2d at 47 (citations omitted).

[17] ***State ex rel. City of Sikeston v. Public Service Com'n of Missouri,*** 336 Mo. 985, 999, 82 S.W.2d 105, 110-111 (Mo.1935).

matters differently from other items and that they must be treated, for regulatory purposes, in whatever manner is most advantageous to the ratepayers. Staff's position on this matter is consistent with the structure of the asymmetric pricing provisions governing sale and receipt of affiliated goods and services by regulated entities that are contained within the Commission's affiliated transaction rules.[18]

A. Should Ameren Missouri's Net Operating Loss Carryforward related to ADIT be included in Ameren Missouri's rate base?

Staff recommends that Ameren Missouri's Net Operating Loss Carryforward ("NOLC") related to ADIT be included in its rate base, but only on a stand-alone basis in order to avoid any detrimental impact on AmMo's ratepayers. The effect would be to reduce rate base by $31 million.[19]

AmMo entered into a Tax Allocation Agreement ("TAA") with its parent and affiliates. In the past, the TAA resulted in benefits to AmMo's ratepayers, but with respect to the present rate case, it would result in significant detriments due to Ameren Corporation's divestment of its merchant generating affiliate.[20] Based on the previous discussion of the applicable regulatory policies, the Commission should resolve the question in the manner that produces the result most favorable to the ratepayers.

AmMo argues, "[w]hile this Commission may have discretion in determining the level of income tax cost which is properly associated with the

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[18] *See* 4 CSR 240-20.015(2)(A), 4 CSR 240-40.015(2)(A), and 4 CSR 240-80.015(2)(A).

[19] James Warren, Tr. 16:345.

[20] Mike Brosch, Tr. 16:387.

Company's regulated activities, it has no ability to change the tax law, nor should it."[21] But Staff isn't proposing that the Commission should in any way alter the tax laws or the relationship of AmMo to the taxing authorities or to its parent or affiliates under the TAA. Rather, Staff is urging the Commission to use its unquestioned power to determine the *regulatory* treatment to be accorded to this tax issue. And, that treatment is to include AmMo's NOLC related to ADIT on a stand-alone basis, thus protecting AmMo's ratepayers.

B. Should the Company's IRC Section 199 deduction be computed without regard to Net Operating Loss Carryovers from prior years in determining the company's income tax expense?

Staff recommends that Ameren Missouri's IRC Section 199 Domestic Production Deduction ("DPD") be computed without regard to NOLC from prior years; however, Staff asserts, if NOLC is included, then the deduction should only be computed on a stand-alone basis.

Staff's alternative position is that the NOLC used in computing the DPD taxable income limitation should be a hypothetical NOLC, not AmMo's actual, NOLC. Specifically, it should be the very same NOLC that AmMo would have had if it had always filed its income tax returns on a separate company basis instead of the NOLC it actually has as a member of the Ameren consolidated group. It is the same NOLC that Staff contends that AmMo should use with respect to Issue 2.A, above. As Staff asserted there, Staff is urging the Commission to use its unquestioned power to determine the *regulatory* treatment

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[21] *AmMo's Brief,* p. 46.

to be accorded to this tax issue. That treatment is to include AmMo's NOLC related to ADIT on a stand-alone basis, thus protecting AmMo's ratepayers.

--Kevin A. Thompson.

3. Amortizations:

A. Should the amount of solar rebates paid by Ameren Missouri and recorded to a solar rebate regulatory asset through the end of the true-up period be included in Ameren Missouri's revenue requirement using a 3-year amortization period?

Staff has determined that this issue does not require treatment in its *Reply Brief.*

B. Should the amount of pre-MEEIA energy efficiency expenditures incurred by Ameren Missouri and recorded to a regulatory asset through the end of the true-up period be included in Ameren Missouri's revenue requirement and, if so, over what period should they be amortized?

Staff has determined that this issue does not require treatment in its *Reply Brief.*

C. Should the amount of Fukushima flood study costs incurred by Ameren Missouri and recorded to a regulatory asset be included in Ameren Missouri's revenue requirement and, if so, over what period should they be amortized?

Staff has determined that this issue does not require treatment in its *Reply Brief.*

--Jeffrey A. Keevil

4. Noranda Ice Storm AAO:

Should the sums authorized for deferral in Case No. EU-2012-0027 be included in Ameren Missouri's revenue requirement and, if so, over what period should they be amortized?

In its *Initial Brief,* Staff demonstrated that the Prohibition Against Retroactive Ratemaking[22] precludes Ameren Missouri's recovery of **any** of the amount deferred as lost fixed costs due to the effect on Noranda of the January 2009 ice storm. Staff based its analysis squarely upon the holding of the Missouri Supreme Court in what is still the controlling lead case, ***State ex rel. Utility Consumers' Council of Missouri, Inc. v. Public Service Commission,***[23] known fondly to Missouri utility regulatory attorneys as ***"UCCM."*** AmMo, however, does not argue ***UCCM*** -- perhaps because that case does not support its position – but relies instead upon a ruling by the Missouri Court of Appeals in ***State ex rel. AG Processing v. Public Serv. Commission***[24] that seems to say that the Commission can give AmMo what it wants.

The passage in question is as follows:

> An additional consideration supports our rejection of the [a]ppellants' retroactive ratemaking argument: [the utility's] rate adjustment applies only prospectively, to electrical service to be provided to customers after Commission approval of the rate adjustment. The rate adjustment does not modify or recalculate the rate to be charged for electricity provided to customers before the rate adjustment was approved. In prior cases, this Court has rejected claims that measures to recoup previously incurred costs constitute retroactive ratemaking, when the recoupment measures operate prospectively, and do not alter the cost of utility services previously provided to consumers. ***State ex rel. Mo. Gas Energy v. Pub. Serv. Comm'n,*** 210 S.W.3d 330, 336 (Mo.App. W.D.2006) ("This is not retroactive ratemaking, because the past rates are not being changed so that more money can be collected from services that have already been provided; instead, the past costs are being considered to set rates to be charged in the future."); ***State ex rel.***

[22] Like the Rule Against Perpetuities, this principle is so firmly established as a foundational element of ratemaking that it deserves to be stated with capital letters.

[23] ***UCCM,*** 585 S.W.2d 41 (Mo. banc 1979).

[24] ***AG Processing,*** 340 S.W.3d 146 (Mo. App., W.D. 2011).

> ***Midwest Gas Users' Ass'n v. Pub. Serv. Comm'n,*** 976 S.W.2d 470, 481 (Mo.App. W.D.1998) ("The adjustments permitted under [the adjustment clauses] are applied only to future customers on future bills. The companies are not allowed to adjust the amount charged to past customers either up or down.").[25]

Appearances can be deceiving, and so is the support that AmMo finds for its position in ***AG Processing***[26] because that case is talking about something completely different than was ***UCCM.*** ***UCCM*** was mostly about the Fuel Adjustment Clause or "FAC." In ***UCCM,*** the Missouri Supreme Court explained that the Commission was without authority to allow electric utilities to use a FAC.[27] Additionally, the FAC was objectionable as a violation of both the Prohibition Against Single-Issue Ratemaking[28] and the Filed Tariff Doctrine.[29] The Court closed its discussion of the FAC by inviting the General Assembly to authorize such a thing by statute if it thought it was a good idea.[30]

It was in the area of remedies that the Supreme Court in ***UCCM*** addressed retroactive ratemaking:

> Public counsel requested in oral argument that we remand to the commission for a determination by it of the excess amounts collected by the utilities under the FAC over that which they would have collected under a just and reasonable rate, which would include rate increases properly authorized, and to order a refund of any such excess.

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[25] AmMo's *Brief* at 26, *quoting* ***AG Processing,*** *supra,* 340 S.W.3d at 153.

[26] *Supra,* 340 S.W.2d 146.

[27] ***UCCM,*** *supra,* 585 S.W.2d at 51-56.

[28] *Id.,* at 56-57. This is another fundamental principle of ratemaking.

[29] *Id.,* at 57. Also called the "Filed Rate Doctrine." In this instance, it refers to the requirement that tariffs be "printed and open to public inspection."

[30] *Id.*

> However, to direct the commission to determine what a reasonable rate would have been and to require a credit or refund of any amount collected in excess of this amount would be retroactive ratemaking. The commission has the authority to determine the rate to be charged. In so determining it may consider past excess recovery insofar as this is relevant to its determination of what rate is necessary to provide a just and reasonable return in the future, and so avoid further excess recovery. It may not, however, redetermine rates already established and paid without depriving the utility (or the consumer if the rates were originally too low) of his property without due process.[31]

UCCM never addressed the question of whether the FAC was itself retroactive ratemaking.

AG Processing also concerned the FAC. By the time this case came around, decided 32 years after ***UCCM,*** the General Assembly had taken up the invitation extended by the Court in ***UCCM*** and authorized the Commission to grant a FAC to electric utilities.[32] In ***AG Processing,*** several parties challenged the lawfulness of the FAC of KCP&L Greater Missouri Operations Company ("GMO"), contending that it was impermissible as retroactive ratemaking.[33] The ***AG Processing*** Court first pointed out that the challenge to the FAC had to fail under the guidance of ***UCCM*** because the FAC was now authorized by statute

[31] *Id.,* at 58 (citations omitted). The Court again addressed retroactive ratemaking on page 59 in connection with an entirely illegal surcharge the Commission had granted the utility.

[32] Section 386.266, RSMo., 2005 *Missouri Session Laws,* S.B. 179.

[33] ***AG Processing,*** *supra,* 340 S.W.3d at 149. The challengers believed that the ***UCCM*** Court had based its disapproval of retroactive ratemaking on the Due Process Clause; of course, the General Assembly could not authorize a FAC if that were the case. *See* ***AG Processing,*** 340 S.W.3d at 150, *quoting* ***State ex rel. AG Processing v. Public Service Commission,*** 311 S.W.3d 361, 365 (Mo. App., W.D. 2010).

and the Supreme Court had said, in 1979, that the General Assembly could grant such authorization.[34] As the ***AG Processing*** Court explained,

> The Supreme Court clearly understood that the "automatic adjustment clauses" which the legislature could authorize would provide for the recovery of past energy costs which were not adequately reflected in prior established rates. * * * By specifically stating that the legislature could authorize fuel adjustment clauses like the one adopted by KCP & L here, the Supreme Court in ***UCCM*** presumably contemplated that such clauses would not themselves violate the retroactive ratemaking doctrine.[35]

The ***AG Processing*** Court then noted that the ***UCCM*** Court had never held that the FAC itself violated the Prohibition Against Retroactive Ratemaking because the FAC, although unauthorized in 1979, was nonetheless **part of the rates in effect at the time the service was delivered to the ratepayers**.[36] It is for that reason that the ***UCCM*** Court required the utility to refund the amounts collected under the unlawful surcharge but refused to require the refund of the amounts collected under the unlawful FAC.[37] As the ***AG Processing*** Court summed it up:

> Thus, ***UCCM*** makes clear that fuel adjustment clauses are part of the "established rate" for utility service if they are in effect at the time excess energy costs are incurred, and that it does not violate the retroactive ratemaking doctrine for a fuel adjustment clause to permit a utility to recover excess energy costs incurred at a time when the fuel adjustment clause was in effect. Applying this principle, we held in ***State ex rel. AG Processing, Inc. v. Public***

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[34] *Id.,* at 150-151.

[35] *Id.,* at 151.

[36] *Id.,* at 152.

[37] ***UCCM,*** 585 S.W.2d at 58-60. The distinction is subtle, but real. While both the FAC and the surcharge were unlawful, the surcharge was retroactive ratemaking and the FAC was not because the FAC was part of the tariff in effect when the service was delivered, while the surcharge was not.

> ***Service Commission,*** 311 S.W.3d 361 (Mo. App., W.D. 2010), that KCPL could not employ its Fuel Adjustment Clause to recover excess energy costs incurred before the Fuel Adjustment Clause itself became effective. We held that '[o]nly costs incurred after the effective date of an appropriate tariff may be recovered under a fuel adjustment clause.' In contrast, 'any adjustment to the cost of electricity based on electricity that had already been consumed by [KCPL] customers prior to the effective date [of the Fuel Adjustment Clause] clearly constitutes retroactive ratemaking.'[38]

So what does all this mean? It means that ***AG Processing*** actually provides no support at all for AmMo's quest to recover the amount deferred in the lost-fixed-costs AAO. ***AG Processing*** says that the Prohibition Against Retroactive Ratemaking is not violated if the tariff in effect at any particular time puts customers on notice that, in the event that fuel costs are higher than expected, they are going to pay a little more for power in the future in order to make up the shortfall.[39] AmMo would like it to say that it's permissible to recover unexpected shortfalls from ratepayers after the fact, but it doesn't say that.

How does this apply to the Noranda Ice-Storm AAO? It means that AmMo wins **only** if the tariff in effect between January 2009 and April 2010 provided that, in the event that Noranda unexpectedly went off-line, AmMo's other customers would pick up the difference by paying a little more for power in the future. Did the tariff in effect at that time so provide? No. That means – as Staff explained in its *Initial Brief* – that AmMo **can't recover any part of the deferral** because of the Prohibition Against Retroactive Ratemaking.[40]

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[38] ***AG Processing,*** *supra,* 340 S.W.3d at 153.

[39] ***AG Processing,*** *supra,* 340 S.W.3d at 153.

[40] The particular passage in ***AG Processing*** that AmMo quotes, at 340 S.W.3d 153, briefly discusses an additional reason why the FAC is not retroactive ratemaking, which is that the "rate

In summary, the Commission should not include any of the amount deferred in Case No. EU-2012-0027 in Ameren Missouri's revenue requirement in this case because to do so would violate the Prohibition Against Retroactive Ratemaking. Why? Because the deferred amount represents fixed costs not paid by the rate revenue collected at the time and, unlike the FAC approved in ***AG Processing,*** the future recovery of any shortfall was not contemplated by the tariff in effect at the time the service was provided.

--Kevin A. Thompson

5. Storm Restoration Expense and Two-Way Storm Costs Tracker:

A. Should the Commission continue a two-way storm restoration cost tracker whereby storm-related non-labor operations and maintenance ("O&M") expenses for major storms would be tracked against the base amount with expenditures below the base creating a regulatory liability and expenditures above the base creating a regulatory asset, in each case along with interest at the Company's AFUDC rate?

B. If the storm cost tracker is not continued, what annualized level of major storm costs should the Commission approve in this case?

C. Should an amount of major storm cost over-recovery by Ameren Missouri be included in Ameren Missouri's revenue requirement and, if so, over what period should it be amortized?

The Commission should reject AmMo's request for a storm tracker, because the Company has not shown any reason why a tracker is appropriate for its non-labor operations and maintenance (O&M) storm costs. AmMo's asserted

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adjustment applies only prospectively, to electrical service to be provided to customers after Commission approval of the rate adjustment. The rate adjustment does not modify or recalculate the rate to be charged for electricity provided to customers before the rate adjustment was approved." The very brevity of this discussion, taken out of context, permits AmMo to use it to support something that, in fact, the decision does not support.

justifications for the tracker, reiterated in its testimony and initial brief, fail in light of Staff's evidence.

Specifically, AmMo provides no explanation for the decline in distribution maintenance expense illustrated in Staff's testimony. This decline in preventative maintenance—an expense which could reduce the Company's storm expense by improving the resiliency of its distribution system[41]—is exactly the kind of spending reduction the Commission might expect to see, given its skepticism about the potential for trackers to corrupt the incentive system inherent in traditional ratemaking.[42] The fact that this spending reduction is actually taking place should be reason for pause before re-authorizing this tracker.

Without any testimony to explain this decline in maintenance spending, AmMo's reliance on previous Commission decisions is unpersuasive. AmMo's brief characterizes the Commission's reluctance to authorize trackers as a "general skepticism," but in fact the Commission's skepticism is not general. The Commission is expressly skeptical about the tracker's effect on a utility's incentive to manage its costs.[43] Presented with evidence of warped incentive in Staff's rebuttal testimony,[44] AmMo nevertheless refused to address its maintenance spending either in surrebuttal testimony or at the hearing.

Much of AmMo's initial brief simply reiterates information about the size of storms and the magnitude of AmMo's efforts to restore service, which Staff does

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[41] Ex. 206, Boateng Surrebuttal, p. 5.

[42] ER-2010-0036, *Report and Order*, issued May 28, 2010, pg. 68; ER-2012-0166, *Report and Order*, issued Dec. 12, 2012, pg. 96.

[43] *Id.*

[44] Ex. 205, Boateng Rebuttal, pgs. 9-10.

not question. However, this testimony doesn't justify a tracker because AmMo has successfully recovered all its storm restoration expense in recent years, with or without a tracking mechanism.[45] No party disputes that storm restoration is an expensive undertaking, but Staff's unrefuted testimony shows that the utility's concern about recovering these costs through traditional ratemaking are unfounded.

AmMo repeats its claim that Staff opposes this particular tracker because of a "dislike" for deferrals generally, ignoring the fact that Staff has supported a tracker in some circumstances. Indeed, the tracker is a regulatory tool; Staff does not "like" or "dislike" tools. Staff simply believes that tools like a tracker bring both intended and unintended consequences, and therefore tools like a tracker should only be used in the appropriate situation. As explained in Staff's testimony and initial brief, AmMo has not carried its burden to show that such a situation exists for this item of expense.

AmMo also bemoans the "uncertainty" inherent in traditional ratemaking. However, no ratemaking method can *guarantee* a utility any particular return.[46]

At the hearing, AmMo attempted to illustrate this "uncertainty" by asking Staff witness Kofi Boateng to render an on-the-fly decision about whether an ice storm described in Case No. EO-2008-0218 would meet Staff's standard for an AAO—*despite the fact that the Company itself did not request an AAO for this*

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[45] Ex. 205, Boateng Rebuttal, pg. 8, lns. 1-26.

[46] ***Lightfoot v. City of Springfield*,** 361 S.W.2d 347, 352 (Mo.Ct.App. 1951). "The ultimate return to the utility as a result of the rate fixed and subsequently charged and collected will necessarily vary from time to time. 'The law, of course, did not require that the rates at any time yield any particular return.'"

storm.[47] Mr. Boateng stated that he could not render such a judgment on the fly, without a full filing by the utility that Staff could review and verify.[48] Apparently, AmMo interprets Mr. Boateng's unwillingness to render an off-the-cuff analysis without conducting a Staff review to be evidence of its "real world" concerns about unpredictability or subjectivity. In the real world, however, as Staff testified, AmMo recovered all its storm expense in recent years through traditional regulation.

AmMo argues that none of the parties claim the tracker has not worked as intended, and that Staff's opposition is simply that the tracker is not "traditional." This is not true. Staff's testimony is that the tracker is not working as intended (at least, not as the Commission intended) because it seems to be creating an incentive for the Company to reduce its distribution maintenance spending. Presumably, the Commission did not intend to authorize a tracker that would distort the utility's incentive. AmMo chose not to address Staff's evidence of this distorted incentive.

Therefore, Staff's concerns about this tracker are grounded in objective evidence, while AmMo's concerns about uncertainty are belied by actual facts. Because AmMo has not shown any objective reason or justification for the tracker, the Commission should reject this request.

--*John D. Borgmeyer.*

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[47] EO-2008-0218, *In the Matter of an Investigation of Union Electric Company d/b/a AmerenUE's Storm Preparation and Restoration Efforts.*

[48] Tr: 20:861, ll. 5-14.

6. Vegetation Management and Infrastructure Inspection Trackers:

A. Should the vegetation management and infrastructure inspection trackers be continued?

Staff recommends that the Commission discontinue the vegetation management and infrastructure inspection trackers.[49] These two-way trackers were established in 2006 in order to defray the cost when the Commission imposed new infrastructure maintenance and vegetation management obligations on electric utilities:

> In 2006, AmerenUE experienced extensive service outages due to severe thunderstorms in the summer and ice storms in the winter. In response to concerns that AmerenUE and other electric utilities had failed to properly maintain their electric distribution systems, the Commission promulgated new rules designed to compel Missouri's electric utilities to do a better job of maintaining their electric distribution facilities to enhance the reliability of electric service to customers. * * * In promulgating the stricter standards, the Commission anticipated utilities would have to spend more money to comply. Therefore, both rules include provisions that allow the utility a means to recover the extra costs it incurs to comply with the requirements of the rule.[50]

However, now the trackers should be discontinued because they have served their purpose of protecting AmMo from unknown cost overages caused by Commission mandates.[51]

> These trackers were put in place to capture the at-the-time unknown cost impact of new Commission rules 4 CSR 240-23.030 (vegetation management) and 4 CSR 240-23.020 (infrastructure inspections) designed to compel Ameren Missouri (and other utilities) to increase reliability after their failure to properly maintain their systems. Since that time, Ameren Missouri has completed the

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[49] *Staff RR Report,* p. 110.

[50] ***In the Matter of Union Electric Company d/b/a AmerenUE,*** Case No. ER-2008-0318 (***Report & Order,*** iss'd January 27, 2009) pp. 32-33.

[51] Hanneken Surrebuttal, p. 10.

> first cycles for both Vegetation Management and Infrastructure Inspections under the rules and while the costs have fluctuated somewhat from year to year, as is common with many costs, overall they have remained stable during the period the trackers have been in place.[52]

AmMo has had ample warning that these temporary trackers would be discontinued once they had served their purpose. The Commission stated in AmMo's last rate case, "[h]owever, as the Commission has indicated in previous rate cases, it does not intend for this tracker to become permanent."[53] After five years, the trackers are no longer needed.[54]

AmMo attempts to justify continuation of these trackers by pointing to annual fluctuations in these costs.

> The Commission has issued regulations that require the Company to perform vegetation management and infrastructure inspections within certain time intervals. This is not discretionary spending, as the Company has no choice but to follow these rules, continue the program, and incur the costs. The cost of trimming has varied and will continue to vary based on a number of factors outside the Company's control. These factors include, but are not limited to, the fluctuation of required distribution line miles and their classification on an annual basis; continually evolving federal requirements for transmission facilities; varying vegetation growth rates experienced annually; varying rates of tree mortality based on environmental factors; new or increasing threats from disease and insects, such as we are seeing from the Emerald Ash Borer; and changes in the cost of labor, equipment, and fuel.[55]

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[52] Hanneken Rebuttal, p. 8 (citations omitted).

[53] ***In the Matter of Union Electric Company, d/b/a Ameren Missouri,*** Case No. ER-2012-0166 (***Report & Order,*** iss'd December 12, 2012) p. 9.

[54] *AmMo's Brief,* p. 119 (trackers have been in place for five years).

[55] Wakeman Rebuttal, p. 3.

The reality is that many of AmMo's operation and maintenance costs fluctuate from year-to-year; in and of itself, such fluctuations do not support an extraordinary mechanism like a tracker.[56]

AmMo argues that these trackers should be continued for three reasons: first, Staff just doesn't like trackers and its position therefore should not be taken seriously; second, Staff is ignoring the fact that these costs fluctuate; and third, the Commission's rules themselves "include language strongly indicating the Commission intends trackers would be used to facilitate a full reflection of the costs utilities incur to comply with those rules in rates."[57] Let's take these arguments one-by-one.

Staff just doesn't like trackers. That's true; so what? A tracker is an extraordinary regulatory accounting mechanism that should only be used in extraordinary circumstances. A tracker disturbs the normal balance of risks between the shareholders and the ratepayers and tilts things in favor of the shareholders. For that reason, trackers are inherently unfair. When the Commission first imposed these new rules on the Company, these trackers were appropriate and fair, protecting the shareholders from costs that were never considered when rates were set. Now, however, when these costs are known and are built into rates at every rate case, the trackers have become inappropriate and unfair.

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[56] Hanneken Surrebuttal, pp. 10-11.

[57] *AmMo's Brief,* p. 117.

Staff is ignoring the fact that these costs fluctuate. No, Staff is not ignoring cost fluctuations; Lisa Hanneken addressed them in her testimony:

> Q. Why does Staff think that that's a better system?
>
> A. Well, because there is no longer a need for this tracker. This tracker was put in place because of the new rules that were put in place for vegetation management and infrastructure inspections. Because there was no real way of knowing what the impact of those rules –
>
> Q. Mrs. Hanneken, I'm going to interrupt you. I asked you why you think it's better to do away with the system that ensures that customers don't overpay and the company doesn't under recover.
>
> A Because now I think it is a stable cost, so there is no real volatility involved, which is one of the premises of having a tracker. In addition to that, there is some disincentive for the company to control some of the costs that are under its control and, third, I think it reduces the risk upon the company and there should be some – some accounting and some manner for that reduction of risk.[58]

The point is, **all costs fluctuate to some extent.[59]** A tracker is an extraordinary mechanism and it should be employed sparingly, as a solution for extraordinary circumstances. As Ms. Hanneken testified, there are negative aspects to trackers: they disincentivize the Company from controlling costs and they are inherently unfair because they shift business risk from the Company to the ratepayers. The underlying reality here is that AmMo wants to retain these trackers in order to shift its business risk to its ratepayers. Notice that AmMo has **never** proposed an ROE reduction in exchange for a risk-reducing tracker.

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[58] Lisa Hanneken, Tr. 20:932-933.

[59] *Id.,* p. 933.

The Commission's rules themselves include language strongly indicating the Commission intends trackers would be used to facilitate a full reflection of the costs utilities incur to comply with those rules in rates. AmMo points to this language:

> In the event an electrical corporation incurs expenses as a result of this rule in excess of the costs included in current rates, the corporation may submit a request to the commission for accounting authorization **to defer recognition and possible recovery of these excess expenses until the effective date of rates resulting from its next general rate case, filed after the effective date of this rule,** using a tracking mechanism to record the difference between the actually incurred expenses as a result of this rule and the amount included in the corporation's rates . . . Parties to any electrical corporation request for accounting authorization pursuant to this rule may ask the commission to require the electrical corporation to collect and maintain data (such as actual revenues and actual infrastructure inspection expenses) until such time as the commission addresses ratemaking for the deferrals. The commission will address the ratemaking of any costs deferred under these accounting authorizations at the time the electrical corporation seeks ratemaking in a general rate case.[60]

However, the emphasized language shows that this rule intended only **a one-time fix,** lasting only until the first rate case filed after the effective date of the rule.[61] That was June 30, 2008.[62] Nothing in the quoted rules suggests that the Commission intended these trackers to be permanent. And, we know that it did not because it has said so in plain and unmistakable language: "[h]owever, as the Commission has indicated in previous rate cases, it does not intend for this tracker to become permanent." What could be more clear?

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[60] *AmMo's Brief,* p. 118, *quoting* Rules 4 CSR 240-23.020(4) and 4 CSR 240-23.030(10).

[61] Lisa Hanneken, Tr. 20:934-935.

[62] Ted Robertson, Tr. 20:944.

The Commission has always intended to eventually discontinue these trackers. The time to do it is now.

B. What amount of money should be included in the revenue requirement for Vegetation Management and Infrastructure Inspection?

Staff recommends using a three-year average for both the vegetation management and infrastructure inspection expense to calculate the amount of expense to be included in the revenue requirement.[63] Staff proposes to include $54,504,662 for vegetation management and $5,827,267 for infrastructure inspections as ongoing levels of expense in its cost-of-service calculations.[64]

AmMo objects to using a three-year average. Laura Moore testified:

> If you look at our actual costs, the more current costs are more relevant. And even if we look at our future forecast, the costs that we spent through the true-up period are more relevant to what we think we'll spend in 2015.[65]

AmMo proposes to include in base rates about $2.1 million more than does Staff.[66] AmMo's contention is based on its position that these costs have been trending upward year-by-year.[67] The increases are primarily due, AmMo asserts, to increased labor costs.[68]

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[63] Hanneken Surrebuttal, p. 9.

[64] *Id.*

[65] Laura Moore, Tr. 20:922.

[66] *Id.,* p. 923.

[67] *Id.,* pp. 923-924.

[68] David Wakeman, Tr. 20:925.

Use of a normalized amount based on a three-year average is common for costs subject to minor fluctuations.[69] Ms. Hanneken testified that this is the appropriate accounting treatment of this cost:

> [W]hen I look at the whole body of data, I see that there are minor fluctuations from year to year. And while I see that the older periods of the tracker, when the trackers were in place and the rules were in place, it seems like that that data was, as Ms. Moore said, was less. But in the last three years, it seems like it's stabilized. But there's still those minor fluctuations that you really should take into account.[70]

Staff's goal is to find the most appropriate and reasonable amount of costs to use on a going-forward basis.[71] In this case, that amount is the three-year average proposed by Staff.

C. Should an amount for cost over-recovery be included in Ameren Missouri's revenue requirement and, if so, over what period of time should they be amortized?

Staff agrees with Ameren Missouri that an amount for cost over-recovery should be included in Ameren Missouri's revenue requirement. Therefore, this issue is not now contested.

--Kevin A. Thompson.

7. Union Proposals:

A. Can the Commission mandate or require that the Company address its workforce needs in a particular manner and, if so, should it do so?

B. Should the Commission require the additional reporting requested by Mr. Walters?

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[69] Lisa Hanneken, Tr. 20:929-930; 935-936; Ted Robertson, Tr. 20:948-949.

[70] *Id.,* pp. 930-931.

[71] *Id.,* pp. 936-937.

Staff has no position on the issues raised by the Union.

8. Return on Equity ("ROE")

In consideration of all relevant factors, what is the appropriate value for Return on Equity ("ROE") that the Commission should use in setting Ameren Missouri's Rate of Return?

The Commission is required[72] to allow AmMo an ROE sufficient to attract capital and maintain confidence in the company's financial integrity, and that ROE, moreover, must be commensurate with the returns realized on other investments of similar risk.[73] Based on the competent and substantial evidence adduced in this case, that ROE should be 9.25% as recommended by Staff's expert witness, David Murray, and supported by the corroborating recommendations of expert witnesses Michael Gorman and Lance Schafer.

Party & Expert	Recommendation
AmMo (Robert Hevert)[74]	10.20%-10.60%, **10.40%**
Wal-Mart (Steve Chriss)[75]	**9.8**
MIEC (Michael Gorman)[76]	9.00%-9.60%, **9.30%**
Staff (David Murray)[77]	9.00%-9.50%, **9.25%**
OPC (Lance Schafer)[78]	8.74%-9.22%, **9.01%**
TABLE 1 – EXPERT RECOMMENDATIONS.	

[72] ***UCCM,*** *supra,* 585 S.W.2d at 49; ***State ex rel. Missouri Water Co. v. Public Service Commission,*** 308 S.W.2d 704, 714 (Mo.1957); ***State ex rel. Missouri Public Service Co. v. Fraas,*** 627 S.W.2d 882, 886 (Mo. App., W.D. 1981).

[73] ***Federal Power Commission v. Hope Natural Gas Company***, 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333 (1943); ***Bluefield Water Works & Improvement Company v. Public Service Commission of West Virginia***, 262 U.S. 679, 43 S.Ct. 675, 67 L.Ed. 1176 (1923).

[74] Hevert Direct, p. 2; Hevert Rebuttal, pp. 124-5; Hevert Surrebuttal, p. 2.

[75] Chriss Revenue Requirement Direct, p. 13.

[76] Gorman Direct, p. 2.

[77] *Staff's RR Report,* p. 10.

[78] Schafer Direct, p. 3.

Discarding the recommendation of Wal-Mart's witness Steve Chriss, which was unsupported by any financial analysis, the recommendations of the four experts are arrayed as one cluster and one outlier, as is graphically represented in Table 2, above. The Commission is authorized to evaluate the experts' testimony and may adopt or reject any or all of the testimony of any witness.[79] When the Commission decides, in a proper exercise of its discretion, to adopt or reject an expert's testimony, a reviewing court will not second-guess that decision.[80]

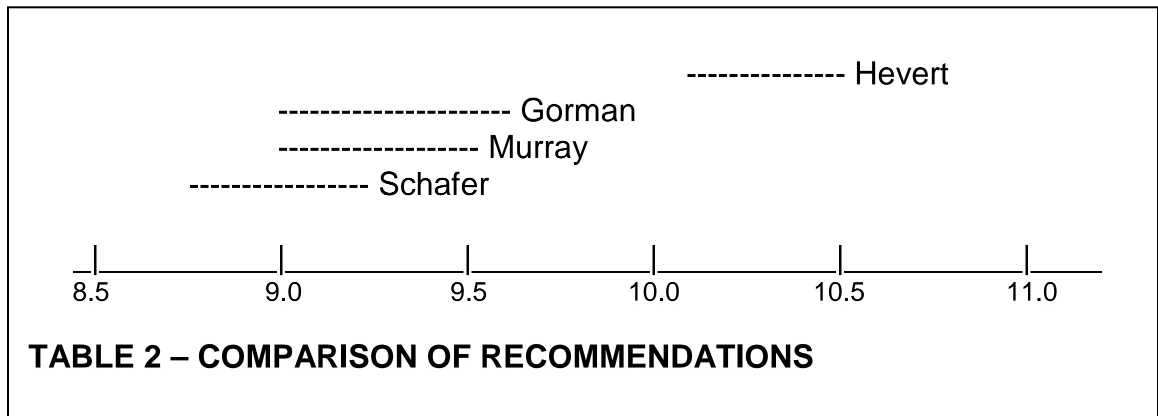

TABLE 2 – COMPARISON OF RECOMMENDATIONS

The experts used similar models but different inputs.[81] Robert Hevert, AmMo's highly-paid consultant,[82] produced a high recommendation; the other

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[79] ***State ex rel. GS Technologies Operating Co., Inc. v. Public Service Com'n of State of Mo.,*** 116 S.W.3d 680, 690 (Mo. App., W.D. 2003).

[80] *Id.*

[81] Michael Gorman, Tr. 21:1197.

[82] Robert Hevert, Tr. 21:1144.

three analysts – two of whom are salaried state employees – produced strikingly similar recommendations quite a bit lower than that of Mr. Hevert. None of this is surprising.

	Constant Growth DCF	**Terminal Stage, Multi-Stage DCF**
HEVERT	5.54%, 5.68%[83]	5.63%[84]
MURRAY	3.5%-4.5%[85]	3.0%-4.0%[86]
GORMAN	4.77%, 5.05%[87]	4.60%[88]
SCHAFER	5.02%[89]	4.86%[90]

TABLE 3 – COMPARISON OF ANALYSTS' GROWTH RATES.

A review of Mr. Hevert's methods and inputs reveals that he systematically manipulated the inputs he used to produce high results.[91] The highest values on Table 3, a comparison of the growth rates used by the experts in their DCF analyses, are Mr. Hevert's. The *lowest* growth rate used by Mr. Hevert is 83 basis points *higher* than the average of the growth rates used by the other analysts, 4.71%.[92] It is 49 basis points *higher* than the highest of the growth rates used by the other analysts, 5.05%. The contrast between the high numbers

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[83] Hevert Rebuttal, Sch. RBH-R7.

[84] *Id.,* Sch. RBH-R8.

[85] *Staff RR Report,* p. 33.

[86] Ex. 245, p. 2.

[87] Gorman Direct, pp. 18, 20.

[88] *Id.,* p. 25.

[89] Schafer Direct, Sch. LCS-2. The ten values in column 6 were averaged.

[90] Schafer Direct, p. 26.

[91] Murray Rebuttal, p. 4; Gorman Rebuttal, p. 2; Schafer Rebuttal, p. 2.

[92] (4.0 + 4.77 + 5.05 + 5.02) / 4 = 4.71.

used by Mr. Hevert and the lower numbers used by the other analysts is most striking in the third column of Table 3, the terminal growth rates used in the Multi-Stage DCF analysis. Mr. Hevert's growth rate, 5.63%, is 131 basis points *higher* than the average of the growth rates used by the other three analysts, 4.32%.[93] It is 77 basis points *higher* than the highest of their growth rates, 4.86%. Where, one inevitably wonders, is this growth going to come from? AmMo is a mature company in a mature industry; its annual load growth is negligible.

AmMo claims in its *Initial Brief* that Mr. Hevert appropriately recognizes that "considerable caution"[94] is needed in interpreting the results of the DCF model because "market data is disjointed."[95] Mr. Hevert observed and commented on current elevated p/e ratios and explained that "over time such valuation levels will revert to historic norms."[96] Staff noted that in past rate cases, Mr. Hevert did incorporate a reversion of p/e ratios to historical medians for purposes of estimating investors' expected future cash flows.[97] Although Mr. Hevert has a major concern about the higher valuation levels in this case, for some reason he did not perform a multi-stage DCF in this case to allow for a reversion to "historical norms" as he did in previous Ameren Missouri rate cases. Why not? Because doing so would cause his multi-stage DCF cost-of-equity

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[93] (3.5 + 4.6 + 4.86) / 3 = 4.32.

[94] *AmMo Brief,* p. 60.

[95] *Id.,* p. 67.

[96] *Id.*

[97] Murray Rebuttal, p. 24 and Murray Surrebuttal, pp. 11-12.

estimates to be even lower than they were without this assumption. In Staff's surrebuttal testimony, Mr. Murray quantified the impact this assumption would have on Mr. Hevert's multi-stage DCF results. If Mr. Hevert had used the same terminal p/e ratio of 15.98x (still high by historical standards) that he used in AmMo's last rate case, Case No. ER-2012-0166, his multi-stage DCF cost-of-equity estimates would have been 24 to 72 basis points lower than the results he achieved without assuming a contraction in the p/e ratio.[98] If Mr. Hevert had used the more conservative terminal p/e ratio of 13.70x that he used for AmMo's rate case in 2011, Case No. ER-2011-0028, his multi-stage DCF cost-of-equity estimates would have been 106 to 155 basis points lower than the results he achieved without assuming a contraction in the p/e ratio.[99] Consequently, Staff agrees it is important to consider recent higher valuation levels of utility stocks because, if Mr. Hevert is right in his assumption that investors are buying utility stocks expecting a contraction in the p/e ratios, then this provides even more support for Staff's position that investors are providing utility companies with equity capital at a cost significantly lower than they did when Ameren Missouri was allowed an ROE of 9.80% in 2012.

Table 4 reveals that Mr. Hevert used significantly higher risk premia than did the other analysts. Mr. Hevert used two equity market premia in his updated CAPM analysis, 9.72% and 10.45%. The *lower* of these values is 411 basis points *higher* than the average of the equity market premia used by the other

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[98] Murray Surrebuttal, p. 12, ll. 2-8.

[99] *Id.*, p. 12, ll. 9-12.

analysts.[100] It is 352 basis points *higher* than the highest market equity premium used by the other analysts. Mr. Gorman observed, "My major concern with Mr. Hevert's CAPM analysis is his inflated market risk premium estimates."[101]

	HEVERT[102]	**MURRAY[103]**	**GORMAN[104]**	**SCHAFER[105]**
CAPM				
Risk-Free Rate	3.04, 3.68	3.17	4.10	3.2, 4.5
Beta	0.757, 0.760 0.758, 0.750	0.74, 0.73	0.76	0.77
Equity Market Premium	9.72, 10.45	6.20, 4.64	6.2, 7.3	5.4
RISK PREMIUM METHOD[106]				
Risk-Free Rate	3.04 3.68 5.45	4.13, 4.76	4.10, 4.71	N/A
Risk Premium	7.06 6.52 5.41	3.00, 4.00	4.41, 6.28 3.03, 5.03	N/A

TABLE 4 – COMPARISON OF CAPM AND RISK PREMIUM INPUTS.

Mr. Hevert's inflated risk premia are due to his unreasonable market return expectations for the S&P 500. Mr. Hevert assumes the S&P 500 will achieve a long-term market return of 12.93% to 13.44%.[107] The forecasted returns for the S&P 500 from reputable institutional investors, such as JP Morgan Asset Management, and from the *Survey of Professional Forecasters* published by the

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[100] (6.2 + 4.64 + 6.2 +5.4) / 4 = 5.61. *See* Table 7, Staff's *Initial Brief.*

[101] Gorman Rebuttal, p. 11.

[102] Hevert Rebuttal, Sch's RBH-R11 and RBH-R12.

[103] *Staff RR Report,* pp. 42-44.

[104] Gorman Direct, pp. 27-32, 37.

[105] Schafer Direct, pp. 28-35; Sch. LCS-9. The beta value is the average of those used by Mr. Schafer.

[106] Including Mr. Murray's "Rule of Thumb."

[107] Murray Rebuttal, p. 26, ll. 1-6.

Federal Reserve Bank of Philadelphia, is about half of the returns Mr. Hevert projects.[108] This clearly should cause concern about the reasonableness of the results from Mr. Hevert's analyses.

The same observation applies to Mr. Hevert's risk premia. He used three: 5.41, 6.42 and 7.06.[109] The *lowest* of these, 5.41, is 112 basis points *higher* than the average of the risk premia used by Mr. Murray and Mr. Gorman.[110] However, it is *lower* than Mr. Gorman's highest risk premium at 6.28. However, the average of Mr. Hevert's three risk premia is 204 basis points *higher* than the average of the other analysts' risk premia.[111] Mr. Gorman criticized Mr. Hevert's Risk Premium Method as producing inflated results.[112]

It is important to understand that both Mr. Gorman's and Mr. Hevert's risk premium analyses are based on the assumption that allowed ROEs are synonymous with a market required return on common equity. This is especially problematic considering the significant increase in utility stock valuation levels through the end of 2014 and into early 2015. Utility stock valuation levels were then trading at valuation levels never before experienced for the period RRA compiles allowed ROE information.[113] The fuel for the increase in the valuation levels is that interest rates are at levels that have not been experienced

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[108] *Id.*, p. 26, l. 7 – p. 27, l. 13.

[109] Table 4.

[110] *Id.* Mr. Schafer did not perform the Risk Premium Method.

[111] (7.06 + 6.52 + 5.41) / 3 = 6.33.

[112] Gorman Rebuttal, pp. 13-15.

[113] Murray Surrebuttal, p. 30, ll. 1-11.

during the period covered by RRA.[114] The Commission should weigh the significant amount of recent capital market evidence supporting a lower cost of equity against allowed ROEs that were awarded before these capital market changes occurred.

Regardless, Mr. Hevert's recommendation is also high when compared to recent ROE awards by other utility regulatory commissions. Mr. Gorman testified that authorized returns on equity for electric utility companies in 2014, both integrated and delivery companies, range from 9.17% to 10.4%, with an average of 9.76%.[115] When these figures are adjusted to exclude cases where the commission either approved a settlement or simply used the same return on equity as was approved in a prior case, the industry average return for 2014 was 9.63%.[116]

The inevitable conclusion is that every place that Mr. Hevert had an opportunity to employ professional judgment, he employed it to skew his results to the high side. Irrationally high growth rates, irrationally high terminal p/e ratios; irrationally high risk premia – these are the inputs that Mr. Hevert used to skew his results in the direction desired by his client. Perhaps this sort of manipulation is an inevitable result of a system in which "hired gun" expert consultants make comfortable livings by abetting utility companies in their quest for bloated returns. In any event, Mr. Hevert's recommendation should be treated with great caution.

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[114] *Id.*

[115] Gorman Surrebuttal, p. 3.

[116] *Id.*

AmMo maintains Mr. Murray's "recommendation and methodologies are difficult to follow or make sense of in this case."[117] While Mr. Murray did take a different approach in this case, in which his recommendation was based on his estimate of the relative decline in AmMo's cost of equity since its 2012 rate case, his recommendation is quite easy to follow and is supported by capital market data he provided as well as commentary from electric utility stock analysts, the Edison Electric Institute and other capital market experts besides himself. Mr. Hevert's methodologies and recommendation cannot be supported by common sense tests of reasonableness, such as lower utility debt costs. In fact, Mr. Hevert is so bold as to state,

> What has changed so significantly over the past two years that equity investors now require a dramatically lower rate of return? As discussed throughout my Rebuttal testimony, neither market conditions in general, nor the Company's situation in particular supports the proposition that the required Return on Equity has fallen, as the Opposing ROE Witnesses recommend.[118]

Let's start with the market conditions in general. Mr. Hevert himself recognizes that utilities in general, and the proxy companies in particular, traded at "unusually high, and likely unsustainable, levels."[119] Consequently, Mr. Hevert does not refute the fairly straightforward understanding that utility stocks have been trading at much higher p/e ratios in recent months.

Are these p/e ratios much higher than they were in 2012, when AmMo was awarded an ROE of 9.80%? Yes, they are. Staff provided a significant

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[117] *AmMo Brief,* p. 84.

[118] Hevert Rebuttal, p. 6, ll. 5-10.

[119] Hevert Rebuttal, p. 5, ll. 11-12.

amount of capital market information in each round of testimony in this case illustrating that very fact. Staff provided a graph of the p/e ratios for Edison Electric Institute's ("EEI") *Regulated Utility Index* for the period January 3, 2012, through September 30, 2014, to show the significant increase in p/e ratios over this time.[120] In Staff's Rebuttal testimony, because of significant changes in utility stocks during the fourth quarter of 2014, Staff provided an update on the current status of the utility capital markets.[121] The total return for EEI's regulated utilities was 16.44% in just the last quarter of 2014, which made up half of the total return of 32.86% for the twelve months ended December 31, 2014.[122] Staff explained that the primary reason for the significant increase in utility stocks was an unexpected decline in interest rates through the end of 2014.[123] Staff supported its own analysis of utility capital market information with that of commentary from electric utility stock analysts that also recognized that utility stock valuations were high (expensive to investors, but cheap for companies to issue).[124] Finally, in surrebuttal testimony, Staff provided additional investment analyst commentary and analysis that explains exactly what has changed so significantly over the past two years that equity investors now require a dramatically lower rate of return.[125] If Mr. Hevert had simply performed an unbiased comparison of his DCF analyses in the 2012 rate case to his DCF analyses in this rate case, he

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[120] Staff RR Report, p. 20.

[121] Murray Rebuttal, p. 7, l. 13 – p. 11, l. 2.

[122] *Id.*, p. 8, ll. 1-12.

[123] *Id.*, p. 8, ll. 13-18.

[124] *Id.*, p. 10, ll. 3-30.

[125] Murray Surrebuttal, p. 25, l. 18 – p. 29, l. 22.

would have observed and noted the significant changes in utility investors' required returns on equity.

As far as AmMo's situation in particular goes, this one is easy if one accepts the logical conclusion that AmMo's cost of equity follows its cost of debt, at least directionally. Staff compared current required yields on AmMo's debt in this case as compared to the required yields on the same debt issuances in AmMo's last rate case. Taking a more conservative average of these debt yields for the 6 months ended December 31, 2014, Staff showed AmMo's cost of debt had decreased in the range of 35 to 50 basis points since 2012.[126] Based on the most recent yields available on AmMo's debt, its cost of debt had declined by 100 basis points or more.[127]

Consequently, the evidence is clear and is based on simple observation of straightforward capital market data. Unfortunately, Mr. Hevert attempts to complicate and confuse matters by comparing government debt costs rather than utility debt costs and also by using inflated risk premia and projected interest rates.

It is interesting that AmMo's initial brief refers to the investment analyst reports that Staff cites in its testimony as "special purpose" financial reports.[128] Although this is perhaps intended as a pejorative choice of words by AmMo's counsel, Staff will go with it because the "special purpose" of these reports is to provide expert analysis and advice from investment brokers to investors. Along

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[126] Murray Surrebuttal, p. 24, l. 10 – p. 25, l. 2.

[127] *Id*, p. l. 10 – p. 25, l. 7.

[128] *AmMo Brief,* p. 86.

those lines, the “special purpose” of rate of return witnesses is to attempt to emulate investors’ analysis and decision-making process when estimating the investors’ required return on common equity, i.e. the cost of equity. In fact, many ROR witnesses use 5-year EPS growth forecasts of these very same equity analysts when applying the DCF, even though these analysts do not do the same in their own analyses.[129] Perhaps, if other ROR witnesses had a better understanding of the inputs these investment analysts use in their analyses to determine a fair price to pay for a utility stock, their cost-of-equity estimates would be more in line with Staff’s (and the investment analysts that publish the reports). In the meantime, Staff believes it is important to discuss and analyze these “special purpose” reports at least generally because this is the type of information that provides direct evidence of investors’ required returns.

In summary, Staff urges the Commission to allow a ROE for AmMo that, based on the weight of the expert opinion adduced in this matter, is in the range 9.00% – 9.50%, midpoint 9.25%. Such an allowed ROE, based on expert testimony, will allow AmMo to attract capital, support its credit, and allow its shareholders a fair opportunity to earn a return on their investments that is commensurate to that of other investments of similar risk.

--Kevin A. Thompson.

9. Class Cost of Service, Revenue Allocation and Rate Design:

A. Which of the parties class cost of service results should the commission use to develop rates in this case?

[129] Murray Surrebuttal, p. 22, l. 12 – p. 23, l. 20.

Staff recommends the Commission make no factual findings regarding the general suitability of any class cost-of-service study method over any other. Nonetheless, for purposes of this case, Staff recommends that the Commission rely on the results of its Detailed Base Intermediate and Peak ("BIP") class-cost-of-service study because, among the studies presented, Staff's study most reasonably recognizes the relationship between the physical characteristics of AmMo's generation fleet and its load. Despite the incorrect factual allegations of MECG and MIEC in their respective initial briefs, Staff's detailed BIP recognizes the contributions to capacity and energy of base capacity, intermediate capacity, and peak capacity, and relies on the relationship between the generation of each of those plants and the capacity and energy requirements of AmMo's load.

AmMo contends that the Commission should rely on the results of its four non-coincident peak version of the Average and Excess Demand Allocation method.[130] Staff further advised the Commission that the class-cost-of-service results of all of the parties indicate that the Residential and LTS classes should receive a positive revenue-neutral adjustment and the SGS, LGS, and SPS classes should receive a negative revenue-neutral adjustment. AmMo does not disagree, stating:

> However, if the Commission believes it appropriate to adjust current class cost allocations to bring them more in line with the point CCOSS results, Ameren Missouri does not oppose Staff's proposed revenue neutral shift of +0.5 percent for the Residential and LTS classes and -0.63 percent for the SGS, LGS, and SPS

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[130] *AmMo Brief,* p. 146.

classes before any rate increase approved in this case is spread across all classes on a uniform percentage basis.[131]

B. How should any rate increase be collected from the several customer classes?

AmMo "proposes to spread a rate increase in this case across-the-board to all rate classes on an equal percentage basis."[132] Staff's rate design recommendations in this case are more complex and entail based on a six-step process: (1) the Residential and LTS classes should receive a positive 0.50% revenue-neutral adjustment and the SGS, LGS, and SPS classes should receive a negative 0.63% revenue-neutral adjustment;[133] (2) assign directly to the applicable customer classes the portion of the revenue increase or decrease that is attributable to the amortization of energy efficiency programs from the Pre-MEEIA program costs;[134] (3) determine the amount of revenue increase awarded to Ameren Missouri that is not associated with Step 2;[135] (4) order Ameren Missouri's rate schedules to be uniform for certain interrelationships among the non-residential rate schedules that are integral to Ameren Missouri's rate design;[136] (5) based on Staff's class-cost-of-service results and Commission policy on energy efficiency, the residential customer charge should stay at the current charge of $8.00 per month (see below);[137]

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[131] *Id.,* p. 147.

[132] *Id.*

[133] Scheperle Direct, pp. 3-4, ll. 19-21 & 1-2.

[134] *Id,.* at p. 4, ll. 4-8.

[135] *Id.,* at ll. 10-14.

[136] *Id.,* at ll. 16-25.

[137] *Id.,.* at 27-28.

(6) each rate component of each class should be increased across-the-board for each class on an equal percentage basis after taking in to consideration Steps 1 through 5.[138] Ameren Missouri's expert witness William R. Davis agreed that Staff's recommendation is reasonable and confirmed that there is basic agreement between the parties on which classes are below cost of service and which are above cost of service.[139]

C. What should the residential customer charge be?

Staff recommends the Commission maintain the current residential customer charge at $8.00. AmMo, on the other hand, proposes to increase the monthly customer charge by the same across-the-board uniform percentage as all other rates, resulting in a residential customer charge of $8.50.[140]

Staff's recommendation is based on its study of cost causation, which determined that Ameren Missouri's cost of making service available to a residential customer allocates to $8.11 on a per-customer basis,[141] and on considerations of "rate simplicity, stability, and customer understandability."[142] Staff's recommendation is also consistent with the Commission's guidance in Ameren Missouri's last rate case proceeding where the Commission stated, "[s]hifting customer costs from variable volumetric rates, which a customer can reduce through energy efficiency efforts, to fixed customer charges, that cannot

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[138] *Id.,* at 30-32.

[139] William R. Davis, Tr. 23:1494.

[140] *AmMo Brief,* p. 150. Note that the $8.50 is an estimate.

[141] *Staff's Rate Design and Class-Cost-of-Service Report,* p. 43 n. 27 (*"Staff's RD Report"*).

[142] *Id.*

be reduced through energy efficiency efforts, will tend to reduce a customer's incentive to save electricity."[143] The Commission also noted that increasing the customer charge would send the wrong message to customers.[144] All of these concerns remain equally valid in the present rate case.

AmMo devotes some effort in its brief to arguing that the Commission was wrong in its calculus of public policy in AmMo's last rate case decision. Its arguments are:

- "[W]hatever the record in Ameren Missouri's last rate case may have shown, there is no evidence in this case that increasing the Residential customer charge will reduce customers' incentive to save electricity by implementing energy efficiency measures."[145]

- "[T]he Commission's finding ignores the fact the final order in this case will increase Ameren Missouri's volumetric rates. In light of that increase, a minimal increase to the monthly customer charge should not be enough to dissuade customers who are considering adopting energy efficiency measures from doing so, because adopting such measures will enable them to mitigate the impacts of increased volumetric charges. Moreover, it is unreasonable to assume the meager increase in the customer charge Ameren Missouri seeks – which likely will total less than $6.00 over the course of an entire year – will have any impact on customers' energy efficiency decisions."[146]

- "[A] artificially inflating volumetric charges sends inaccurate price signals to customers regarding the savings potential of energy efficiency measures. Higher volumetric charges will certainly make energy efficiency measures appear to be more attractive and cost-effective, and also will shorten the payback period on any measures customers decide to adopt."[147]

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[143] *Report and Order,* Case No. ER-2012-0166, p. 110, ¶12.

[144] *Id.,* at p. 111, ¶ 13.

[145] *AmMo Brief,* p. 152.

[146] *Id.*

[147] *Id.*

The fact is, it is simply **common sense** that moving costs from the variable portion of the rate to the fixed customer charge would be inimical to the public policy of encouraging energy efficiency. The less financial reward that energy efficiency efforts yield to customers, the less they will engage in such conduct. AmMo's attempt to impugn the Commission's prior decision on this basis is ill-advised.

The customer charge is a fixed element of the bill that does not vary with usage; even customers who use no electricity at all must still pay the customer charge.[148] AmMo's drive to raise the residential customer charge is motivated by its desire to get more of its fixed costs into the fixed customer charge:

> [A] large portion of the fixed costs Ameren Missouri incurs to provide electric service are still reflected in its volumetric rates. This discrepancy is particularly pronounced for the Residential rate class, where about eighty percent of costs are fixed, but only about ten percent of those costs are reflected in the customer charge. That is one reason the current customer charge is only $8.00 while the Company's CCOSS supports a customer charge in excess of $20.00.[149]

AmMo goes on to complain that its residential customer charge is not only the lowest of all Missouri's investor-owned electric utilities, but lower than that of any of Missouri's electric cooperatives.[150] AmMo notes that it has sought to raise the customer charge in each of its last five rate cases, to no avail.[151] Clearly, the Commission knows bad regulatory policy when it sees it.

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[148] *Staff RD Report,* p. 43.

[149] *AmMo Brief,* pp. 150-151.

[150] *Id.,* p. 151.

[151] *Id.*

Because Ameren Missouri has failed to show that the residential customer charge should be increased, and because an increase to the residential customer charge would impede the public policy of encouraging energy efficiency, Staff recommends the residential customer charge remain at $8.00.

D. *Should the Commission approve Wal-Mart's proposed shift to increase the demand component of the hours-use rate design for Large General Service and Small Primary Service?*

Staff opposes Wal-Mart's proposal because it is unsupported by specific customer impact analysis.[152] Staff proposes, instead, to increase all rate components across all the classes on an equal percentage basis.[153]

AmMo also opposes Wal-Mart's proposal, which would apply half of any rate increase approved for the LGS and SPS rate classes to the initial usage block and the other half to the demand charge, leaving rates for the second and third energy blocks unchanged.[154] AmMo conducted a study that shows that Wal-Mart's proposal, if adopted, would unfairly throw a greater proportion of the costs of each class upon lower load customers.[155] Wal-Mart is not a lower load customer. AmMo points out, "lower load factor customers could see double-digit percentage bill increases in addition to whatever rate increase the Commission authorizes in this case."[156] The Commission should reject Wal-Mart's proposal.

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[152] Fortson Rebuttal, p. 7.

[153] *Id.,* at p. 8.

[154] *AmMo Brief,* pp. 147-148.

[155] *Id.,* pp. 148-149.

[156] *Id.,* p. 149.

E. Should the Commission approve Wal-Mart's recommendation to require the Company to present analysis of alternatives to the hours-use rate design in its next rate case?

As it stated in its brief, Staff believes that the hours-use rate design is an appropriate demand rate design that functions on the basis of the customer's monthly load factor.[157] However, Staff does not oppose specific customer information and analysis of alternatives to the hours-use rate design in future rate cases.

F. What methodology should the Commission use to allocate income tax expense among customer classes?

AmMo evidently did not address this issue in its initial brief.

Staff recommends that the most reasonable way to allocate income tax expense to the various customer classes is to allocate based on class earnings. AmMo's method, which is based on net plant, would reduce Staff's residential customer charge by approximately $0.50.[158] Additionally, AmMo's method for calculating income tax allocation as applied to the plant balances in this case would result in an unreasonable allocation because the depreciation reserve associated with FERC account 369 is currently in excess of its plant balance, which results in a negative value to be applied to the distribution services function.[159]

--Kevin A. Thompson.

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[157] *Id.,* at ll. 5-6.

[158] R. Kliethermes Surrebuttal, p. 5.

[159] *Id.* at p. 5 and n. 8.

10. Economic Development Rate Design Mechanisms:

A. Should the Commission expand the application of Ameren Missouri's existing Economic Development Riders?

Both Staff and AmMo support the establishment of a collaborative to explore all questions relating to economic development riders across all regulated industries. For that reason, the expansion of AmMo's economic development riders at this time is premature.

B. Should the Commission modify Ameren Missouri's existing Economic Development Riders to require recipients to participate in the Company's energy efficiency programs?

Staff and AmMo agree that this step should not be taken at this time.

C. Should the Commission open a docket to explore the role economic development riders have across regulated industries (i.e. water, electric, natural gas) and/or to further explore issues raised by parties in this case and issues the Commission inquired about at the beginning of the case?

Both Staff and AmMo support the establishment of a collaborative to explore all questions relating to economic development riders across all regulated industries.

--*Kevin A. Thompson.*

11. Lighting Issues:

A. Cities' Street Lights Issue:

1. Can the Commission mandate or require that the Company sell its street lights to the Cities?

2. Should the Commission approve a revenue-neutral adjustment between customer-owned and Company-owned lighting rates?

3. Should the Commission eliminate the termination fees from the Ameren Missouri-owned lighting rate?

Staff repeats that it generally does not believe that it would be appropriate for the Commission to require Ameren Missouri to sell street lighting facilities to the cities who wish to purchase them, but does support a two-step process wherein Ameren Missouri and a city agree to transfer ownership to the city and then the transaction is presented to the Commission for approval.

B. LED Street Lighting:

Should the Commission order Ameren Missouri to continue to study the cost-effectiveness of replacement of all or parts of existing company-owned street lights with LED lights, and, no later than twelve (12) months following the Commission's Report and Order in this case, to file either proposed LED lighting tariffs or an update to the Commission on when it will file a proposed LED lighting tariff to replace existing company-owned street lights?

This issue has been addressed by a *Stipulation and Agreement* between the parties.

C. Other Lighting Tariff issues:

Should the Commission order the Company to eliminate the 7(M) lighting class (Municipal Incandescent Street Lighting)?

Staff supports the Company's proposal to eliminate service classification 7(M) as it has become unnecessary.

--Kevin A. Thompson.

12. Labadie Electrostatic Precipitators:

Should the Company's investment in electrostatic precipitators installed at the Labadie Energy Center be included in the Company's rate base?

The only issue between the Company and Staff respecting the electrostatic precipitators at the Labadie Energy Center related to the costs associated with some 94 damaged plates. That issue has been resolved by a

Stipulation and Agreement entered into by the parties. Therefore, Staff supports the inclusion of $183,282,825 in rate base for this project.

--*Kevin A. Thompson.*

13. Fuel Adjustment Clause ("FAC"):

A. *Did the Company fail to comply with the "complete explanation" provisions of 4 CSR 240-3.161(3)(H) and (I) and, if so, would this justify the elimination of the Company's fuel adjustment clause?*

B. *Did the Company fail to provide information on the magnitude, volatility and the Company's ability to manage the costs and revenues that it proposes to include in its FAC and, if so, would this justify the elimination of the Company's fuel adjustment clause?*

C. *If the FAC continues should the sharing percentage be changed to 90%/10%?*

D. *Should transmission charges associated with power that is generated by Ameren Missouri for its load or transmission charges associated with off-system sales be included in the FAC as transportation of "purchased power"?*

E. *If the FAC continues, what costs and revenues should be included in the Company's FAC:*

1. *Should only fuel and purchased power costs, transportation of the fuel commodity, transmission associated with purchased power costs and off-system sales revenues be included?*

2. *If costs and revenues other than those listed in item 1 above are included in the FAC, should cost or revenue types in which the Company has incurred less than $390,000 in the test year be included, and what charges and revenues from MISO should be included?*

3. *Should transmission revenues continue to be included in the FAC?*

All Fuel Adjustment Clause ("FAC") issues between Staff and the Company have been resolved. Staff does not support the efforts by other parties to significantly modify or even discontinue the FAC.

--*Kevin A. Thompson.*

14. Noranda Rate Design Issues:

A. Is Noranda experiencing a liquidity crisis such that it is likely to cease operations at its New Madrid smelter if it cannot obtain relief of the sort sought here?

1. If so, would the closure of the New Madrid smelter represent a significant detriment to the economy of Southeast Missouri, to local tax revenues, and to state tax revenues?

2. If so, can the Commission lawfully grant the requested relief?

3. If so, should the Commission grant the requested relief?

Noranda's Liquidity Crisis:

Noranda's position is generally corroborated by the unrefuted evidence adduced showing a very significant decline in the number of operating aluminum smelters in the United States since 1980.[160] Staff notes that the competent and substantial evidence of record would support a finding either in the affirmative or the negative on the question of the imminence of Noranda's closing.

[160] Fayne Direct, p. 3: "In the U.S. in 1980, there were 32 smelters, producing more than 5 million metric tons. Today, there are only 8 smelters operating in the U.S., producing about 1.8 million metric tons annually. In every instance, the smelter shut down because of high power costs (HWF Exhibit-1 shows the U.S. smelters currently in operation)."

Would Closure of Noranda Constitute an Economic Detriment?

Yes, it would. Staff agrees that the closure of the New Madrid smelter would represent a significant detriment to the economy of Southeast Missouri, to local tax revenues, and to state tax revenues.[161]

Can the Commission Grant the Requested Relief to Noranda?

Staff repeats that, if the Commission finds that Noranda is experiencing a liquidity crisis such that it is likely to cease operations at its New Madrid smelter in the absence of significant rate relief, the Commission could lawfully grant a load retention rate to Noranda so long as the additional costs imposed thereby on Ameren Missouri's other customers are *less* than the additional costs they would experience if Noranda ceased operations. This is not a matter of just picking a number that reflects some amount of margin above incremental cost at a given moment in time. Some sort of adjustment mechanism would also be required to maintain the benefit as conditions change over time.

AmMo argues that the Commission cannot grant relief to Noranda because to do so would constitute unlawful "undue" discrimination.[162] AmMo relies on Section 393.130.3, RSMo., which provides:

> No gas corporation, electrical corporation, water corporation or sewer corporation shall make or grant any undue or unreasonable preference or advantage to any person, corporation or locality, or to any particular description of service in any respect whatsoever, or subject any particular person, corporation or locality or any particular description of service to any undue or unreasonable prejudice or disadvantage in any respect whatsoever.

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[161] Haslag Direct, including Report, and Haslag Surrebuttal.

[162] *AmMo Brief,* pp. 158-159.

AmMo also cites an 85-year-old Missouri Supreme Court decision, ***Laundry, Inc.,*** for the proposition that difference in charges must be based upon difference in service.[163] In addition to mischaracterizing the style of the case,[164] AmMo has misstated the Court's ruling, which actually was as follows:

> Since the regulation and fixing of rates or charges for public utilities, and the classification of the users or consumers to whom such rates or charges shall be applicable, is primarily a legislative function, it follows that the Public Service Commission, which is purely and simply an administrative agency or arm of the Legislature, is exercising a legislative or quasi legislative function in the performance of those powers which have been conferred upon it by the Public Service Commission Law, among which are the powers to regulate and fix rates or charges for public utilities, and to classify those users or consumers to whom such rates or charges shall be applicable. Such classification, in order to be valid, must comport with the rule or principle of sound legislative classification. The rule is thus clearly stated by this court en banc in ***State ex inf. v. Hedrick,*** 294 Mo. 21, 74, 241 S. W. 402, 420: "The basis of sound legislative classification is similarity of situation or condition with respect to the feature which renders the law appropriate and applicable. A law may not include less than all who are similarly situated. If it does, it is special and therefore invalid, because it omits a part of those which in the nature of things the reason of the law includes. The question is not whether, considering all the circumstances which exist, the Legislature might not constitutionally make a law which would include a larger class. On the contrary, it is whether it appears beyond a reasonable doubt that there are no distinctive circumstances appertaining to the class with respect to which it has legislated which reasonably justify its action in restricting the operation of the law to the persons, objects, or places to which the law is made applicable."[165]

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[163] ***State ex rel. Laundry, Inc. v. Public Service Commission,*** 327 Mo. 93, 108-112, 34 S.W.2d 37, 44-45 (Mo. 1931).

[164] Which is "***Laundry, Inc.,***" not "***The Laundry, Inc.***"

[165] *Id.,* 34 S.W.2d at 43.

The Court next noted what are now §§ 393.130.3, RSMo. (set out above) and 393.130.2, RSMo.,[166] as significant for indicating that the General Assembly, in enacting the Public Service Commission Law, "apparently [had] in mind the aforestated rule or principle of sound legislative classification[.]"[167]

Perhaps the first and most obvious observation is that §§ 393.130, 2 and 3, RSMo., do not apply to actions of the Commission but rather impose limitations upon the actions of public utilities. Perhaps that is why the ***Laundry, Inc.*** Court did not base its holding upon them. The holding in question is nothing more that the well-established principle that government must treat similarly-situated persons similarly. The United States Supreme Court, in *dicta* quoted by the ***Laundry, Inc.*** Court, expounded upon this principle:

> No one can doubt the inherent justice of the rules thus laid down. Common carriers, whether engaged in interstate commerce or in that wholly within the state, are performing a public service. They are endowed by the state with some of its sovereign powers, such as the right of eminent domain, and so endowed by reason of the public service they render. As a consequence of this, all individuals have equal rights both in respect to service and charges. Of course, such equality of right does not prevent differences in the modes and kinds of service and different charges based thereon. There is no cast iron line of uniformity which prevents a charge from being above or below a particular sum, or requires that the service shall be exactly along the same lines. But that principle of equality does forbid any difference in charge which is not based upon difference in service, and, even when based upon difference of service, must have some reasonable relation to

[166] Which provides, "No gas corporation, electrical corporation, water corporation or sewer corporation shall directly or indirectly by any special rate, rebate, drawback or other device or method, charge, demand, collect or receive from any person or corporation a greater or less compensation for gas, electricity, water, sewer or for any service rendered or to be rendered or in connection therewith, except as authorized in this chapter, than it charges, demands, collects or receives from any other person or corporation for doing a like and contemporaneous service with respect thereto under the same or substantially similar circumstances or conditions."

[167] *Supra,* 34 S.W.2d at 44.

> the amount of difference, and cannot be so great as to produce an unjust discrimination.[168]

To restate the rule, discrimination is undue when it is not based upon factual differences substantial enough to support the difference in treatment. The question of whether discriminatory rates are unlawful and unjust is usually a question of fact.[169]

Once the controlling rule is understood, it is immediately apparent that the Commission can, in fact, grant the requested relief to Noranda because the well-established facts show that **Noranda is different from every other customer that AmMo has.** Consider:

- Noranda is AmMo's largest single customer;
- Noranda consumes some 10% or 11% of AmMo's generation everyday, as much as the City of Springfield, Missouri;[170]
- Noranda's load factor is close to 98%, 24 hours a day, 365 days each year;
- Noranda is the only customer in the LTS rate class.

Because Noranda *is* different, *Noranda can lawfully be treated differently,* as long as the difference in treatment has a rational relation to how Noranda is

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[168] ***Western Union Telegraph Co. v. Call Pub. Co.,*** 181 U.S. 92, 99-100, 21 S.Ct. 561, 564, 45 L.Ed. 765, ___ (U.S.1901).

[169] ***State ex rel. Mo. Office of Pub. Counsel v. Mo. Pub. Serv. Comm'n,*** 782 S.W.2d 822, 825 (Mo. App., W.D. 1990).

[170] Noranda is so large, in fact, that AmMo is still here whining about losing two-thirds of the revenue it expected from Noranda for a few months in 2009 – 2010.

different.[171] When consideration of Noranda's differences is extended to the fact that its closure would be devastating to the impoverished region known as the Missouri Bootheel, it is beyond cavil that the Commission can authorize a load-retention rate for Noranda. AmMo's argument is disingenuous at best.

Nor is the relief sought by Noranda at all like the economic development rate disallowed by the Commission in the ***Civic League of St. Louis*** case.[172] In that case, the City tariffed preferential rates for manufacturers for economic development reasons. The Commission, which ultimately disallowed the rate, stated:

> Fixing a smaller rate where a large amount of water is used is not unreasonable. So rates may be made less to one class where there exist differences in conditions affecting the expense or difficulty of performing the service which fairly justify a difference in rates.[173]

The load-retention rate sought by Noranda can be viewed as a subsidy, as AmMo insists.[174] It can also, however, be viewed as a sensible precaution intended to protect the ratepayers from the even higher rates that will result from Noranda's closing. It's not at all unusual to ask the ratepayers to shoulder an increased rate now to avoid yet higher costs in the future; but it is usually the utility that is asking for public largesse rather than a customer. In fact, that is **exactly** the argument AmMo has made in this case in support of its bloated

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[171] *See* ***UCCM,*** *supra,* 585 S.W.2d at 52-53: "as a part of its duty of setting reasonable rates, the commission has the power to treat some items of operating expense differently than others[.]"

[172] ***Civic League of St. Louis et al. v. City of St Louis, Water Department,*** 4 Mo.P.S.C. 412 (1916).

[173] *Id.,* at p. 447 (citations omitted).

[174] *AmMo Brief,* p. 158.

ROE request in this case -- if returns to investors aren't good enough, AmMo (and ultimately its ratepayers) will have to pay more to access the capital markets:

> The electric utility infrastructure supported by on-going capital investment is critical to our communities and to the Missouri economy. Maintaining a financially viable utility worthy of investment is in the long-term best interest of not only the Company's investors but customers and the state generally. Capital markets are competitive, there is no dispute. It follows that the return opportunity afforded to equity investors must be competitive as well.[175]

Why does AmMo think this argument works for it but not for Noranda?

An additional point is that since 1916, it has become standard regulatory practice to reflect public policies in rates that have nothing at all to do with the actual cost of service.[176] Rates are manipulated to encourage consumption or to discourage consumption; to be simple or understandable or to avoid rate shock or to promote conservation; there is often talk of whether rates are sending the right message to consumers or not.[177] All of these are departures from the notion current in 1916 that a reasonable rate is the cost of service plus a mark-up to provide a rate of return.[178]

In summary, Staff contends that a load-retention rate based upon competent and substantial evidence of record as to the ways that Noranda is

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[175] *AmMo Brief,* p. 51.

[176] Lowell E. Alt, Jr., ***Energy Utility Rate Setting*** (Lulu, 2006), pp. 82-84; Charles F. Phillips, Jr., ***The Regulation of Public Utilities: Theory and Practice*** (PUR, 1993), Chapters 10 and 11.

[177] *Id.*

[178] In 1916, the Commission noted: "Aside from variations due to abnormal conditions, the reasonableness of the rate is to be tested by the relation between the cost of furnishing the service and the charge for the service." ***Civic League of St. Louis,*** *supra,* 4 Mo.P.S.C. at 446-447.

different from all other AmMo customers, although below cost of service, is nonetheless reasonable and non-discriminatory if it confers a commensurate benefit on other ratepayers and marginal costs are recovered. Any such rate design would necessarily need to include an adjustment mechanism so that the benefit to AmMo's non-Noranda customers would be maintained as conditions change over time.

Should the Commission Grant the Requested Relief to Noranda?

Staff's expert witness Sarah Kliethermes testified, "If you believe that without rate relief Noranda will close down, the Staff says, yes, something's better than nothing. Mitigate it as best you can. If you do not believe Noranda would close down, then we recognize they're currently paying below cost of service and should move closer to it."[179] This continues to be Staff's position.

B. Would rates for Ameren Missouri's ratepayers other than Noranda be lower if Noranda remains on Ameren Missouri's system at the reduced rate?

Yes. Staff repeats, under test year conditions, at a rate of $32.50 with no participation in the FAC, the rates for Ameren Missouri's other ratepayers would be *lower* if Noranda remains on Ameren Missouri's system than if Noranda ceased service with Ameren Missouri.[180] This analysis is premised on no change to: (1) the wholesale power prices used in Staff's modeling, (2) the level of transmission costs such as MISO 26a, average ancillary service costs, and

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[179] Sarah Kliethermes, Tr. 35:3002-3003.

[180] Sarah Kliethermes, Tr. 35:3003-4, testified that the incremental cost to serve Noranda was $31.50 at Noranda's meter. $32.50 is the incremental cost plus $1.00 of margin. The average wholesale power price used in Staff's production modeling is $28.29.

MISO charges assessed on load or load ratio share, and (3) Ameren Missouri's cost of fuel and purchased power. If these or other conditions change, other ratepayers' rates would vary.

C. Would it be more beneficial to Ameren Missouri's ratepayers other than Noranda for Noranda to remain on Ameren Missouri's system at the requested reduced rate than for Noranda to leave Ameren Missouri's system entirely?

Yes. Staff repeats, under test year conditions, assuming no change to the (1) wholesale power prices used in Staff's modeling, (2) the level of transmission costs such as MISO 26a, average ancillary service costs, and MISO charges assessed on load or load ratio share, and (3) Ameren Missouri's cost of fuel and purchased power, rates for Ameren Missouri's other ratepayers would be lower if Noranda remains on Ameren Missouri's system at a rate of $32.50 and without participation in the FAC, than if Noranda ceased receipt of service from Ameren Missouri.[181] If these or other conditions change, other ratepayers' rates would vary.

D. Is it appropriate to redesign Ameren Missouri's tariffs and rates on the basis of Noranda's proposal, as described in its Direct Testimony and updated in its Surrebuttal Testimony?

1. If so, should Noranda be exempted from the FAC?

2. If so, should Noranda's rate increases be capped in any manner?

3. If so, can the Commission change the terms of Noranda's service obligation to Ameren Missouri and of Ameren Missouri's service obligation to Noranda?

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[181] *Id.*

4. If so, should the resulting revenue deficiency be made up by other rate payers in whole or in part?

Staff contends that a load-retention rate based upon competent and substantial evidence of record as to the ways that Noranda is different from all other AmMo customers, although below cost of service, is nonetheless reasonable and non-discriminatory if it confers a commensurate benefit on other ratepayers and marginal costs are recovered. Any such rate design would necessarily need to include an adjustment mechanism so that the benefit to AmMo's non-Noranda customers would be maintained as conditions change over time. AmMo is entitled to a reasonable opportunity to earn a fair rate of return, so known revenue deficiencies would need to be made up by other ratepayers; however, other ratepayers should not bear responsibility for AmMo's price risk in obtaining wholesale power to serve Noranda.

5. If so, how should the amount of the resulting revenue deficiency be calculated?

6. If so, can the resulting revenue deficiency lawfully be allocated between ratepayers and Ameren Missouri's shareholders?

i. How should the revenue deficiency allocated to other ratepayers be allocated on an interclass basis?

ii. How should the revenue deficiency allocated to other ratepayers be allocated on an intra-class basis?

7. If so, what, if any, conditions or commitments should the Commission require of Noranda?

E. What is Ameren Missouri's variable cost of service to Noranda?

Staff repeats that, under test year conditions, assuming no change to the (1) wholesale power prices used in Staff's modeling, (2) the level of transmission

costs such as MISO 26a, average ancillary service costs, and MISO charges assessed on load or load ratio share, and (3) Ameren Missouri's cost of fuel and purchased power, using the wholesale cost of power assumed in Staff's fuel run, Ameren Missouri's variable cost of service to Noranda is approximately $118,777,387.[182] This equates to a per MWh cost at Noranda's meter of $28.29.[183] The four-year average wholesale cost as relied upon by the Commission in Case No. EC-2014-0224 was $31.50. For purposes of determining marginal cost, $31.50 is the most reasonable amount contained in the record.[184]

1. *Should this quantification of variable cost be offset by an allowance for Off-System Sales Margin Revenue?*

2. *What revenue benefit or detriment does the Ameren Missouri system receive from provision of service to Noranda at a rate of $32.50/MWh?*

Under test year conditions, assuming no change to the (1) wholesale power prices used in Staff's modeling, (2) the level of transmission costs such as MISO 26a, average ancillary service costs, and MISO charges assessed on load or load ratio share, and (3) Ameren Missouri's cost of fuel and purchased power, using the wholesale cost of power assumed in Staff's fuel run, Noranda would contribute approximately $40,595,593[185] in excess of what Ameren Missouri would spend to procure that energy, at a rate of $32.50/MWh if Noranda remains

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[182] S. Kliethermes Surrebuttal, App. 1-6.

[183] Ex. 246, p. 2.

[184] Sarah Kliethermes, Tr. 35:3003-4.

[185] $1.00 x Noranda's Test Year total MWh.

on Ameren Missouri's system at a rate of $32.50.[186] If these or other conditions change, the estimated benefit or detriment will vary.

F. Should Noranda be served at rate materially different than Ameren Missouri's fully distributed cost to serve them? If so, at what rate?

Staff's expert witness Sarah Kliethermes testified, "If you believe that without rate relief Noranda will close down, the Staff says, yes, something's better than nothing. Mitigate it as best you can."[187] This continues to be Staff's position.

G. Is it appropriate to remove Noranda as a retail customer as proposed by Ameren Missouri in its Rebuttal Testimony?

1. Can the Commission cancel the Certificate of Convenience and Necessity that was granted for Ameren Missouri to provide service to Noranda and, if so, would the cancellation of the CCN be in the public interests?

Staff repeats that it does not object to AmMo and Noranda reaching a reasonable agreement at a reasonable price on reasonable terms. However, under AmMo's proposal, all risk of the contract price not covering AmMo's actual cost to provide wholesale service to Noranda would fall on AmMo's captive retail customers.[188] This is objectionable to Staff.

2. Can the Commission grant Ameren Missouri's proposal since notification regarding the impact of this proposal on its other customers' bills was not provided to Ameren Missouri's customers?

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[186] Four-year average wholesale cost plus $1.00.

[187] Sarah Kliethermes, Tr. 35:3002.

[188] S. Kliethermes Surrebuttal, App. 1.

The existence of § 91.026, RSMo., has, since its enactment, served as notice to all the world that Noranda may elect to leave Ameren Missouri's system.

3. If the Commission grants Ameren Missouri's proposal, should the costs and revenues flow through the FAC?

Staff repeats that it cannot provide specific recommendations until Noranda and Ameren Missouri have permitted Staff to review the actual terms of their proposed wholesale contract. However, Staff recommends that should Noranda become a wholesale customer of Ameren Missouri, due to the size of Noranda's load, it will likely be necessary to allocate the cost of service of Noranda to the wholesale jurisdiction. If this is necessary, Staff recommends that the Ameren Missouri Missouri-jurisdictional revenue requirement otherwise found in this case be reduced by this wholesale jurisdictional amount. Staff does not recommend that any such contract be flowed through the FAC, thus slight modifications to the Ameren Missouri FAC tariffs will be necessary if Ameren Missouri and Noranda do enter into a wholesale contract.

4. Can Ameren Missouri and Noranda end their current contract without approval of all of the parties to the Unanimous Stipulation and Agreement in the case in which Ameren Missouri was granted the CCN to serve Noranda?

Staff repeats that nothing in the *Unanimous Stipulation and Agreement* approved by the Commission in Case No. EA-2005-0108, or in the Commission's order of March 10, 2005, approving that *Unanimous Stipulation and Agreement,* purports to require the approval of the signatory parties for Noranda and Ameren Missouri to end their contract. It is, therefore, Staff's

opinion that Noranda and Ameren Missouri may mutually agree to end their contract at any time.

15. Questions Raised by Commissioner Hall:[189]

A. What is the risk concern that Ameren and Noranda have concerning the wholesale agreement proposal that Ameren's put forth?

1. To what extent can the Commission in an Order or a tariff mitigate or eliminate that risk?

2. To what extent can the General Assembly mitigate or eliminate that risk?

Staff does not believe that any reply with respect to this question is necessary.

B. How and to what extent would ratepayers be harmed by moving Noranda to wholesale service?

1. Can the Commission or General Assembly mitigate or eliminate that harm?

Staff does not believe that any reply with respect to this question is necessary.

C. What would be the effect on Ameren and its customers of eliminating the 12(M) adjustment of off-system sales in the current FAC tariff? Is it appropriate to do so?

Staff does not believe that any reply with respect to this question is necessary.

D. Assuming that the AAO granted to Ameren for the ice storm that shut down Noranda was appropriate and was for lost fixed costs,

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[189] At the hearing, Commissioner Hall announced four questions that he specifically wanted to be addressed in the parties' briefs. Tr. 35:3080.

what legal basis is there for denying recovery of those amounts deferred?

See discussion at Section 4 of this Reply Brief, above.

--Kevin A. Thompson.

CONCLUSION

In conclusion, Staff continues to recommend that the Commission grant Ameren Missouri a general rate increase amounting to approximately $94,407,550 and set its ROE at 9.25%, resolving each contested issue as Staff has recommended. In this way, just and reasonable rates will be set and all relevant factors considered, with due regard to the interests of the various parties and to the public interest.

WHEREFORE, on account of all the foregoing, Staff prays that the Commission will issue its findings of fact and conclusions of law, determining just and reasonable rates and charges for Ameren Missouri as recommended by the Staff herein; and granting such other and further relief as is just in the circumstances.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served, either electronically or by hand delivery or by First Class United States Mail, postage prepaid, on this **10th day of April, 2015,** to the parties of record as set out on the official Service List maintained by the Data Center of the Missouri Public Service Commission for this case.

/s/ Kevin A. Thompson