BEFORE THE PUBLIC SERVICE COMMISSION
<u>OF THE STATE OF MISSOURI</u>

In the Matter of the Tariff Filings of Union	)	
Electric Company, d/b/a AmerenUE, to increase	)	**<u>Case No. ER-2010-0036</u>**
Its Revenues for Retail Electric Service.	)	

INITIAL POSTHEARING BRIEF

OF

MIDWEST ENERGY USERS ASSOCIATION

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TABLE OF CONTENTS

I. INTRODUCTION

In this Brief, the MEUA will prove, through ample citation to the record, three undeniable facts. ***First***, all the evidence in this case indicates that the Large General Service / Small Primary ("LGS / SP") service class is currently paying rates that are significantly above its cost of service.[1] In fact, one witness estimates that one out of every eight dollars paid by the LGS / SP service class constitutes a subsidization of the residential class. Furthermore, examination of studies in recent cases indicates that the amount of this subsidy has been increasing rapidly over the past three years.[2] ***Second***, the Non-Unanimous Stipulation does not adequately address this rapidly growing problem with LGS / SP rates.[3] Instead, that Non-Unanimous Stipulation attempts to provide rate relief for the Large Transmission Service ("LTS") class despite the fact that four out of five cost studies indicate that Noranda[4] is currently paying rates that are below its cost of service. ***Third***, Noranda has failed to provide a reasonable showing of its need for additional rate relief. Noranda's comparison of its cost of electricity relative to its competitors is not only faulty;[5] it also fails to consider Noranda's numerous competitive advantages.[6] These competitive advantages, reflected in its low overall cost of production, has allowed Noranda to operate at full production while each of its competitors has either closed smelters or reduced production.

Once recognized, these facts will necessarily undermine the reasonableness of the Non-Unanimous Stipulation and will necessitate the rejection of that Stipulation. Instead,

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[1] *See*, pages 3-5.
[2] *See*, pages 5-6.
[3] *See*, pages 6-10.
[4] Noranda Aluminum is the only customer taking service under the LTS tariff. As such, it is the only customer that will benefit from the rate relief provided under the Non-Unanimous Stipulation. (Ex. 429, page 37).
[5] *See*, pages 18-23.
[6] *See*, pages 23-25.

the Commission should take the entirety of the benefits generated by the Non-Unanimous Stipulation and utilize that rate relief to reduce the subsidy reflected in current LGS / SP rates.

<u>II. CLASS COST OF SERVICE STUDIES SHOW THAT LGS / SP RATES ARE SIGNIFICANTLY ABOVE COST OF SERVICE. MOREOVER, THE EVIDENCE INDICATES THAT THE MAGNITUDE OF THIS PROBLEM IS RAPIDLY INCREASING.</u>

In this case, the Commission has been presented five class cost of service studies from four parties. These studies were all presented from disparate points of view. ***<u>First</u>***, the Commission was presented the class cost of service study of AmerenUE.[7] While not actually paying rates, Ameren's paramount interest is insuring that rates are indeed paid. ***<u>Second</u>***, the Commission was presented with OPC's class cost of service study.[8] As the representative of the residential class, it is not surprising that this study finds a lower residential class cost responsibility. ***<u>Third</u>***, MIEC presented a class cost of service study.[9] Composed of large industrial customers, including Noranda Aluminum, this study found a lower cost responsibility for the industrial class customers. ***<u>Fourth</u>***, Staff presented its class cost of service study.[10]

The following table reveals the revenue-neutral results of each of the five class cost of service studies:

[7] Exhibits 134-146.
[8] Exhibit 300. Actually, OPC conducted two class cost of service studies. First, OPC conducted a Time of Use study. Second, OPC conducted an Average and 4 Coincident Peak study. (Exhibit 300, pages 7-8).
[9] Exhibit 429.
[10] Exhibits 205-206.

Table One

ER-2010-0036 Class Cost of Service Results

	AmerenUE[11]	*OPC (TOU)*[12]	*OPC (4CP)*[13]	*MIEC*[14]	*Staff*[15]
Residential	$78,070	$11,804	$32,268	$129,625	$83,513
Small GS	($17,649)	($23,344)	($18,878)	($10,721)	($10,526)
Large GS / Small Primary	($64,785)	($24,388)	($30,320)	($84,603)	($73,664)
Large Primary	$2,092	$14,681	$11,970	($12,700)	($919)
Large Transmission	$2,272	$21,246	$4,960	($21,600)	$4,968

(in thousands)

While each study was prepared by parties with different motivations, the studies nonetheless share two universal conclusions. First, all of the studies, including both of the OPC studies, conclude that residential customers are paying rates that are **below** their cost of service. Even Public Counsel's study concludes that residential rates are $11.8 to $32.3 million below their cost of service. Second, all of the studies find that the LGS / SP and the SGS classes are paying rates that are significantly **above** their cost of service. This problem with the LGS / SP rates is not inconsequential. Staff's analysis indicates that 11.4% of all revenues[16] collected from the LGS / SP are actually a subsidy flowing to either the residential or the Large Transmission class. Similarly, MIEC concludes that

[11] Data Request No. MEUA 2.6 (Exhibit 551).
[12] Data Request No. MEUA 2.5 (Exhibit 552).
[13] *Id.*
[14] Exhibit 429, Schedule MEB-COS-5 (column 8).
[15] Data Request No. MEUA 2.6 (Exhibit 553).
[16] Staff's study indicates that LGS / SP rates are currently $73,664,000 over cost of service. Based upon total revenues of $646,173,550 (Exhibit 205, Schedule MSS-1), this means that current rates are 11.4% over cost.

12.7% of all revenues[17] (one out of every eight dollars collected from the LGS / SP customer), are actually a subsidy.

Other conclusions, while not universal, are also easily reached from the class cost of service studies. For instance, four of five studies indicate that the LTS class (Noranda Aluminum) is currently paying rates that are **below** its cost of service. In fact, Public Counsel's time of use study concludes that Noranda Aluminum's rates are currently $21.2 million (15.3%) below cost of service.[18] Only the MIEC study, filed on behalf of Noranda Aluminum, concludes that LTS rates are above its cost of service.[19]

In addition to the above-proven conclusions (i.e., residential rates are below cost of service and LGS / SP rates are above cost), the evidence also demonstrates that this is not a temporary condition. Rather, the evidence demonstrates that the problem with the LGS / SP rates has grown rapidly over the past three years. For instance, Staff estimates that the subsidy implicit in LGS / SP rates has grown by **188%** since 2007.[20]

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[17] MIEC's study indicates that LGS / SP rates are currently $84,603,000 over cost of service. Based upon total revenues of $664,928,000 (Exhibit 429, Schedule MEB-COS-5), this means that current rates are 12.7% over cost.

[18] OPC's Time of Use study finds that Noranda Aluminum rates are currently $21,246,000 below cost. (Ex. 552). Based upon revenues of $139,156,000 (Ex. 429, Schedule MEB-COS-5; Ex. 205, Schedule MSS-1), this means that current rates are 15.3% below cost.

[19] As will be demonstrated later in this brief (pages 12 to 13), each of the cost of service studies ***understate*** UE's cost of serving Noranda Aluminum. It is unquestioned that Noranda imposes a business risk and coincident cost on AmerenUE. Instead of assigning this cost to the LTS class, each study spreads this cost among all the classes. If this cost were specifically assigned to the LTS class, the cost of service for the LTS class would be significantly higher.

[20] Exhibit 553 ($73,664,000 - $25,607,000) / 25,607,000 = 187.7%

TABLE TWO

LGS / SP Cost Differential in Last 3 Cases

	AmerenUE[21]	*Staff*[22]	*MIEC*	*OPC (TOU)*[23]	*OPC (4CP)*[24]
ER-2007-0002[25]	($51,589)	($25,607)	($71,989)[26]	($22,878)	($41,475)
ER-2008-0318	($47,863)	($31,665)	($83,041)[27]	($12,638)	($15,177)
ER-2010-0036	($64,785)	($73,664)	($84,603)[28]	($24,388)	($30,320)

While it has not taken a position as to the propriety of any of the particular studies filed in this case, MEUA maintains that, under any of the cost studies, the LGS / SP class is due a significant reduction from current rates. Even under the most conservative estimate, the LGS / SP class is due a reduction of at least $24.4 million.

III. THE NON-UNANIMOUS STIPULATION DOES NOT PROVIDE FOR JUST AND REASONABLE RATES.

A. Unreasonable Results of Stipulation

Against this backdrop of facts derived from the class cost of service studies, some parties executed a Non-Unanimous Stipulation and Agreement designed to resolve the class cost of service / rate design issues.[29] The Non-Unanimous Stipulation attempts to

[21] Exhibit 551
[22] Exhibit 553
[23] Exhibit 552
[24] *Id.*
[25] Prior to Case No. ER-2008-0318, the Large General Service and Small Primary classes were treated separately. (Tr. 3080). Beginning with Case No. ER-2008-0318, these two classes were combined in the class cost of service studies. (*Id.*). As such, the results for the Large General Service and Small Primary classes have been added together for purposes of this brief.
[26] Tr. 3079-3080
[27] Tr. 3082
[28] Exhibit 429, Schedule MEB-COS-5 (column 8).
[29] The original Non-Unanimous Stipulation and Agreement was filed on March 17, 2010. Subsequently, on March 26, 2010, the signatories executed an Addendum to the Non-Unanimous Stipulation and Agreement. In application, the Addendum addresses the same issues with largely the same resolutions. As noted in the

implement several rate changes. ***<u>First</u>***, the Non-Unanimous Stipulation imposes a roughly 1.5% revenue-neutral increase on the residential class.[30] This amounts to a revenue neutral increase for residential customers of approximately $14.5 million. ***<u>Second</u>***, the Non-Unanimous Stipulation imposes a similar 1.5% increase on the Small General Service Class. This amounts to a revenue-neutral increase for SGS customers of approximately $3.75 million. ***<u>Third</u>***, the Non-Unanimous Stipulation increases revenue-neutral rates to the Large Primary class by 1.25% or $2.1 million. ***<u>Fourth</u>***, the Non-Unanimous Stipulation provides a large rate reduction to Noranda Aluminum. At an overall UE rate increase of $225 million, Noranda Aluminum would receive a revenue-neutral rate reduction of roughly $16 million (11.74%). ***<u>Fifth</u>***, despite the universal agreement that current LGS / SP rates are between $24.4 and $84.6 million over cost, the Non-Unanimous Stipulation assigns the leftover rate reductions to the LGS / SP class. After seeing Noranda Aluminum eagerly consumer over 80% of the benefits derived from the Non-Unanimous, the crumbs remaining for the LGS / SP class amounts to a miniscule $4.6 million or approximately a 0.7% revenue neutral rate reduction. Given the results of the class cost of service studies discussed in Section II, *supra*, it is not hard to understand why MEUA rapidly objected to the Non-Unanimous Stipulation.

Addendum, the only difference was to slightly increase the amount of the revenue neutral shift of costs away from the LGS / SP class. For purposes of this Brief, MEUA will be referring to the Addendum when it addresses the unreasonable nature of the Non-Unanimous Stipulation and Agreement.

[30] As reflected in the Exhibits accompanying the Addendum, the amount of the shifts varies with the final amount of the rate increase awarded to AmerenUE. For example, the amount of the shift to the residential class increases from 1.43% at an overall UE rate increase of $100 million to 1.56% at an overall UE rate increase of $325 million. For ease of reference, this brief will refer to the revenue-neutral increases occurring at the midpoint UE rate increase of $225 million.

TABLE THREE

Changes under Non-Unanimous Stipulation[31]

	Current Revenues	*Revenue Neutral Percentage Change*	*Revenue Neutral Dollar Change*
Residential	$966,332	+1.5%	$14,865,000
Small General Service	$250,178	+1.5%	$3,849,000
Large GS / Small Primary	$652,087	-0.70%	($4,579,000)
Large Primary	$166,927	+1.25%	$2,151,000
Large Transmission (Noranda)	$139,156	-11.74%	($16,294,000)

After reviewing the class cost of service studies presented to the Commission,[32] it is easy to see that the Non-Unanimous Stipulation is not based upon any reasonable estimation of the classes' cost of service. Rather, it is apparent that the Non-Unanimous Stipulation was merely a method by which to provide unjustified rate relief to Noranda. Given that the Non-Unanimous Stipulation is not based upon cost, it is inherently unreasonable. Following is a recitation of the many flaws contained within the Non-Unanimous Stipulation.

First, as reflected in Section II, *supra*, all of the class cost of service studies indicate that the Small General Service class is currently paying rates that are between $10.5 and $23.3 million above its cost of service. Nevertheless, the representatives of the

[31] The revenue neutral shifts are approximate. As the Non-Unanimous Stipulation indicates, the amount of the revenue neutral shift varies depending on the magnitude of the overall increase granted to AmerenUE. The revenue neutral dollar shifts represented in this table are those which occur at an overall UE rate increase of $225 million.

[32] *See*, page 4.

Small General Service class (the Office of the Public Counsel and the Missouri Retailers Association) have agreed that the class should receive a revenue-neutral cost increase of 1.5%. Such a provision is clearly not supported by competent and substantial evidence. As such, the Non-Unanimous Stipulation should be rejected.

Second, while the class cost of service studies indicate that LGS / SP rates are between $24.4 and $84.6 million above cost, the Non-Unanimous Stipulation assigns a paltry revenue neutral rate reduction of $4.579 million. Recognizing that Staff estimates that the subsidy inherent in LGS / SP rates has grown by 188% in the last three years, it is difficult to fathom how this $4.5 million rate shift can reasonably be expected to provide any correction to LGS / SP rates.

Third, despite the fact that four of the five class cost of service studies indicate that Noranda is currently paying rates that are between $2.3 and $21.2 million below cost, the Non-Unanimous Stipulation attempts to provide Noranda with additional rate relief. In fact, even at an overall UE rate increase of $250 million, Noranda Aluminum would still realize an overall rate reduction.[33] Thus, at the same time that residential customers are suffering a 13% rate increase, Noranda would be reveling in its rate decrease.[34] Such a result violates one of the fundamental tenets of ratemaking previously espoused by the Office of the Public Counsel – that it is "inequitable for a particular class to receive a rate reduction when other classes have received a rate increase."[35] In fact, in the last ten years, Public Counsel's witness could not recall a single time, other than the current Non-Unanimous Stipulation, in which Public Counsel has violated this

[33] *Addendum to Stipulation and Agreement*, filed March 26, 2010, at page 13.
[34] *Id.*
[35] Tr. 3106.

fundamental tenet.[36] Nevertheless, Public Counsel has eagerly tossed this tenet, as well as the results of its own class cost of service studies, in the trash in order to provide unjustified rate relief to Noranda.

Recognizing that only one cost study indicates that Noranda rates are currently above cost of service, the Signatories can only justify the Noranda rate relief provided in the Non-Unanimous Stipulation by explicitly adopting the MIEC class cost of service study. That same study, however, also finds that LGS / SP rates are currently $84.6 million above cost of service. Given that the Non-Unanimous Stipulation only provides $4.5 million of rate relief to a class that is presently paying rates that are $84.6 million above cost, it is impossible for the MIEC study to simultaneously provide the evidentiary support for the significant rate relief provided to Noranda while also supporting the paltry relief given to the LGS / SP class. For this additional reason, the Non-Unanimous Stipulation is unreasonable.

Ultimately, it is apparent that the Non-Unanimous Stipulation does not lead to just and reasonable rates. While providing significant rate relief for Noranda, the Non-Unanimous Stipulation simultaneously imposes excessive rates on the SGS as well as the LGS / SP classes. In the final analysis, it is difficult to see how the Non-Unanimous Stipulation represents anything other than a welfare handout for the benefit of Noranda Aluminum. For this reason, the Non-Unanimous Stipulation should be rejected.

B. Extent of Objection with Non-Unanimous Stipulation

Commission rule 4 CSR 240-2.115(2) discusses the procedural treatment for non-unanimous stipulations. Subsection E provides that objecting parties "may indicate that it

[36] Tr. 3122-3123.

does not oppose ***<u>all or part</u>*** of a nonunanimous stipulation and agreement." (emphasis added).

The Non-Unanimous Stipulation in this case attempts to resolve several issues. Many of these resolutions are not objectionable. At pages 2 and 3, the Stipulation provides certain resolutions related to customer charges, Rider B voltage credits, reactive charges and Time of Day rates. Consistent with the directions of 4 CSR 240-2.115(2)(E), MEUA does not oppose these "parts" of the Non-Unanimous Stipulation.

In addition, relative to class cost of service, the Non-Unanimous Stipulation contains certain provisions that are not objectionable. For instance, the Non-Unanimous Stipulation imposes revenue neutral rate increases of 1.5% (approximately $14.5 million) on residential customers and 1.25% (approximately $2.1 million) on Large Primary customers. As indicated in Section 2, the evidence indicates that a larger increase for the residential class is justified. After all, one of Public Counsel's studies indicates that residential rates are $32.3 million below cost. Nevertheless, MEUA recognizes that there are practical considerations which make larger residential shifts unpalatable. As such, MEUA does not object to either the 1.5% revenue neutral increase on residential customers or the 1.25% revenue neutral increase on Large Primary customers.[37] That said, however, MEUA does object to the Non-Unanimous Stipulation to the extent that it provides significant rate relief to Noranda Aluminum while simultaneously providing little relief to the LGS / SP class. [38]

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[37] Recognizing that its members are not served under the Small General Service tariff, MEUA does not, from a financial standpoint, object to the 1.5% revenue neutral rate increase placed on the SGS class by the Non-Unanimous Stipulation. Nevertheless, as demonstrated in Section II of this Brief, there is no competent evidence to support any rate increase for this class. As such, MEUA cannot support a rate increase that is so obviously not justified.

[38] Signatories will undoubtedly direct the Commission to provision 5 of the Non-Unanimous Stipulation which provides that all the terms are "interdependent." As such, the Signatories will claim that it is

As has been shown, it is uncontroverted that the LGS / SP class is currently paying rates that are $24.4 to $84.6 million above its cost of service. Despite this fact, the Non-Unanimous Stipulation only proposes $4.5 million of rate relief to this class. At the same time, however, the Non-Unanimous Stipulation seeks to provide Noranda Aluminum, as the only customer under the LTS class, over $16.3 million of rate relief.

It has been demonstrated that four out of five cost studies indicate that Noranda is currently paying rates that are below its cost of service. Moreover, the evidence indicates that those cost studies are understated in their quantification of Noranda's cost of service. It is undisputed that AmerenUE experiences increased business risk as a result of having such a large percent of its revenues tied to serving a single customer (Noranda Aluminum).[39] Specifically, because Noranda represents over 6.3% of Ameren's revenues,[40] AmerenUE is constantly faced with the risk that it will lose 6.3% of its revenues if something happens to Noranda's load.

As a result of the uncertainty in UE's revenue stream associated with Noranda, UE experiences increased costs in the form of an inflated return on equity. Given the difficulty of segregating this risk from the other business risks experienced by the Company,[41] all of the class cost of service studies simply assigns this business risk to all

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inappropriate, despite the clear direction of 4 CSR 240-2.115(2)(E) to only object to parts of the Non-Unanimous Stipulation. As such, the Commission cannot simply rely on the Non-Unanimous Stipulation for the resolution of the non-objectionable provisions. Rather, as the Presiding Officer and Commission Davis properly recognized, the resolution of any particular issue must be based upon competent and substantial evidence and not simply the existence of a Non-Unanimous Stipulation. (Tr. 2807; 2812-2813). That said, as demonstrated in Section II, *supra*, there is competent and substantial evidence to support the revenue neutral rate shifts to the residential and Large Primary classes.

[39] Tr. 2891 and 3153.

[40] Exhibit 429, Schedule MEB-COS-5 (Noranda represents $139,156,000 of Ameren's total revenues of $2,205,595,000).

[41] Tr. 3157.

of the classes.[42] Had such costs been assigned directly to Noranda, however, the cost of service for each class would be decreased while the cost of service for Noranda would be increased. As such, each of the class cost of service studies understates the cost of serving Noranda while simultaneously overstating the cost of serving other customers.

While the individual parties have not quantified the increased risk associated with serving Noranda, recent events have quantified that risk for the Commission. Specifically, in January 2009, an ice storm demonstrated the legitimacy of this risk and quantified that risk.[43] As a result of this ice storm, AmerenUE suffered from reduced revenues for approximately one year. As reflected in its SEC filings, AmerenUE quantified these reduced revenues at $30 million over a nine month period.[44]

If the Commission were to accept this real-life quantification of the Noranda business risk ($30 million), each of the class cost of service studies would show an attendant increase in Noranda's cost of service.[45] In fact, the MIEC study, relied upon by Noranda for its stated position, would suddenly show that Noranda rates are $8.4 under cost of service.[46]

In addition to the fact that the rate relief provided by the Non-Unanimous Stipulation is not supported by class cost of service studies, rate relief for Noranda is also undermined by the fact that Noranda has twice previously been the beneficiary of rate

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[42] Tr. 2890 and 3153.
[43] Tr. 2893.
[44] Tr. 2893.
[45] Noranda will inevitably argue that such there is no business risk associated with serving Noranda. In fact, given their cross-examination, Noranda will point to the inclusion of the N-Factor as reflected in the FAC stipulation and agreement. (First Non-Unanimous Stipulation and Agreement, filed March 10, 2010, at page 2 and Schedule 1, page 6). Such an argument ignores the real life demonstration of risk provided by the January 2008 ice storm. Moreover, as reflected in Ameren's testimony, the inclusion of N-Factor may help to "mitigate" this business risk. Such risk is not eliminated and Ameren continues to risk future "revenue shortfalls" associated with serving Noranda. (Tr. 2895).
[46] Ex. 429, Schedule MEB-COS-5. (-$21,600,000) + ($30,000,000) = +$8,400,000.

relief. Since being added to the AmerenUE system in 2005, Ameren has had two Missouri rate cases. In both of those cases, Noranda was the beneficiary of rate relief.[47] Because such rate relief was diverted to Noranda, the subsidy implicit in the LGS / SP rates has continued to grow. Today, Noranda seeks to crowd in at the trough again and preclude the opportunity for other customer classes to fix inequities in their rates. Such treatment is inequitable and the Non-Unanimous Stipulation should be rejected.

C. Unreasonable Results of Non-Unanimous Stipulation are Easily Corrected

As shown on page 8, the Non-Unanimous Stipulation envisions revenue neutral rate increases for the residential, small general service, and large primary classes. These rate increases serve to increase costs for these classes by a total amount of approximately \$20.9 million. The primary beneficiary of these rate increases is Noranda; who realizes a rate reduction of over \$16 million. In contrast, the LGS / SP class will receive the "leftover" benefits of approximately \$4.5 million.

While the Non-Unanimous Stipulation leads to unreasonable rates, it can be corrected with three easy steps. ***<u>First</u>***, as previously indicated, there is no competent and substantial evidence to support the rate increase provided to the Small General Service Class. As such, the SGS class should not be given a rate increase. Instead, the entirety of the revenue neutral rate increases should be limited to the residential and large primary classes. ***<u>Second</u>***, the evidence indicates that Noranda is currently paying rates that are below its cost of service. Even the study relied upon by Noranda, once corrected as shown on pages 12-13, shows that Noranda is paying rates below their cost of service. As such, Noranda should not receive any further rate relief. ***<u>Third</u>***, recognizing that all

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[47] Tr. 2894. Case No. ER-2007-0002, *Non-Unanimous Stipulation and Agreement*, filed March 22, 2007, at page 5; Case No. ER-2008-0318, *Report and Order*, issued January 27, 2009, at page 126).

class cost of service studies show that the LGS / SP customers are paying rates that are at least $24.4 million, and as much as $84.6 million over cost, the entirety of the relief should be provided to this class. The rate increases given to the residential and large primary class will allow the Commission to give the LGS / SP class a revenue neutral reduction of approximately $16.5 million. This shift, while not completely correcting the subsidies implicit in LGS / SP rates, should prevent the disparity from growing and may cause some movement back to actual cost of service.

IV. NORANDA HAS NOT PROVIDED A REASONABLE SHOWING OF ITS NEED FOR RATE RELIEF. NORANDA'S ANALYSIS OF ITS COST OF ELECTRICITY IS FAULTY AND IT FAILS TO CONSIDER NORANDA'S NUMEROUS COMPETITIVE COST ADVANTAGES.

A. Introduction

In its testimony, Noranda alleges that the viability of the New Madrid smelter is threatened because of its cost of electricity. Noranda implies that, absent immediate rate relief, the closing of the smelter is inevitable. For instance, Noranda claims "[o]n the New Madrid Smelter's long term journey, Union Electric's proposed rate increase would be a significant and unfortunate step on the ***critical path to failure***."[48] Still again, "Union Electric Company's proposed rate increase would drive the smelter's production costs so high that it ***threatens the smelter's viability***."[49] By pinning its continued existence on electric prices, Noranda attempts to place responsibility for the well being of the smelter employees and their families in the laps of the Commission. "Hundreds of Southeast

[48] Ex. 426, pages 8-9.
[49] *Id.* at page 5.

Missouri families would be ***placed in peril*** if the New Madrid Smelter was forced to shut its doors."[50]

Interestingly, Noranda's claims of peril alleged in this case, are absolutely contrary to other public statements and actions of Noranda. For instance, in recent loan and grant agreements, Noranda has made several commitments to the State of Missouri to maintain current employment for the next ten years.[51] Furthermore, SEC regulations require all publicly traded entities to file an annual report that includes a discussion of risk factors. As set forth in SEC regulations, those risk factors should include "a discussion of the most significant ***factors that make the offering speculative or risky***."[52] Since Noranda is seeking to issue its initial public offering, Noranda is required to file such a report. In that annual report, Noranda simply notes that "profitability may decline" as a result of the pending AmerenUE rate case.[53] Such a milque-toast warning stands in stark contrast to their immediate claims that the "viability" and "sustainability" of the New Madrid smelter will be "placed in peril" by this rate case. In fact, while admitting that such information would be relevant to investors,[54] Noranda's CEO recognizes that warnings about the imminent closure of the New Madrid smelter do not exist in the 10K filing.[55]

Those contradictions aside, Noranda attempts to support its viability theory by presenting the testimony of Henry Fayne. Based primarily on evidence derived from the internet, Mr. Fayne claims that Noranda's cost of electricity places it "among the highest-

[50] *Id.* at page 10.
[51] Tr. 2981.
[52] 17 C.F.R. Ch. II §229.503(c) (emphasis added).
[53] Tr. 2979-2980.
[54] Tr. 2980.
[55] *Id.*

cost smelters in the US."[56] Evidence elicited in cross-examination, however, reveals that Noranda's claims are nothing more than economic blackmail for two primary reasons.

First, Mr. Fayne's analysis is faulty.[57] The data relied upon by Mr. Fayne has been shown to be inherently unreliable. For instance, compared to audited data in this case, the data relied upon by Mr. Fayne significantly inflates Noranda's alleged cost of electricity. In addition to the unreliability of the data, Mr. Fayne also manipulates the data to support his predetermined notion that Noranda's cost of electricity is among the highest of all smelters. For example, Mr. Fayne arbitrarily includes closed smelters in an effort to reduce the national average cost of electricity for aluminum smelters. By reducing the average cost, Mr. Fayne hopes to make Noranda's cost of electricity look excessive. Even then, Mr. Fayne conveniently ignores the closed smelter with the highest cost of electricity. Worse still, Mr. Fayne includes the cost of electricity for a smelter that has built its own generation. In essence, Noranda wants to receive the benefits of self generation (i.e., lower costs) without extending the capital to build such generation. Ultimately, when corrections are applied to overcome Mr. Fayne's short-sided analysis, it will be shown that Noranda's cost of electricity is actually ***below*** the national average cost of electricity!

Second, by focusing solely on cost of electricity, Noranda attempts to avoid any analysis of its other costs of production. As cross examination demonstrated, when the analysis is broadened, Noranda benefits from numerous competitive advantages including cost of bauxite and alumina, reliability of electricity, shipping costs and other geographic

[56] Ex. 421, page 9.
[57] *See*, pages 18-23.

advantages.[58] Based upon these numerous cost advantages, Noranda has continued to operate at full production while other competitors have discontinued operations.[59] Just as it must determine the profitability of a utility based upon an analysis of "all relevant factors", the Commission should be hesitant to base any opinions of Noranda's profitability solely on one cost item. When the examination is broadened, the evidence demonstrates that Noranda's competitive position is solid and the viability of the smelter is not threatened.

B. Noranda's Analysis Electricity Costs for U.S. Smelters is Faulty

As indicated, Mr. Fayne's analysis suffers from several critical flaws. Given the apparent nature of some of these flaws, one must necessarily question whether his analysis was driven by a predetermined outcome – to show that Noranda's cost of electricity is <u>higher</u> than its competitors. Despite such a goal, evidence elicited in cross-examination appears to suggest the opposite outcome, that Noranda has a <u>lower</u> cost of electricity than other aluminum smelters.

<u>1. Problems with Underlying Data</u>

In developing his analysis, Mr. Fayne relied largely upon information provided from an online database – CRU.[60] Obviously, reliance upon information found solely on the internet raises concerns about reliability. In this case, concerns with inaccuracy in the CRU data are immediately proven to be well founded. Based upon CRU data, Mr. Fayne claims that Noranda's cost of electricity is $35.67 / Mwh.[61] While he did not independently calculate Noranda's cost of electricity, Mr. Fayne indicated that such a

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[58] *See*, pages 23-24.
[59] *See*, page 25.
[60] Tr. 3033.
[61] Ex. 421, Schedule HWF-1.

calculation is straightforward. "To calculate the [electric] cost of a smelter, the cost of electricity would require having the actual dollar cost of electricity and the kilowatt hours consumed and dividing one by the other."[62] While Mr. Fayne did not look, the information necessary to perform such a calculation is readily available in the record. In fact, information provided by Noranda's own witness indicates that Noranda's cost of electricity is ***not $35.67 / Mwh***, as alleged by CRU and Mr. Fayne. Instead, using Mr. Fayne's method for calculating the cost of electricity, Noranda's cost of electricity is ***much lower - $33.37 / Mwh***.[63]

Such a discrepancy illustrates the fundamental problem with using information found on the internet and not subject to independent verification. Potential reasons for such discrepancies may be founded in the fact that Mr. Fayne did not extract such data himself. Instead, he relied upon Noranda employees, albeit employees with a self-serving interest in manipulating the numbers, to extract the data from CRU.[64] Furthermore, such a discrepancy may be explained by the dated nature of the CRU data. When asked the period over which the data was collected, Mr. Fayne did not know.[65]

2. Failure to Uniformly Apply Criteria / Inclusion of Closed Smelters

In addition to concerns with the reliability of the data used by Mr. Fayne, there are also significant concerns with the way in which Mr. Fayne manipulated the data. For instance, in preparing his analysis, Mr. Fayne included several smelters (Alcoa Tennessee, Ravenswood, and Massena East) that are now closed. When pressed on his criteria, Mr. Fayne claimed to have included "smelters that are either operating currently

[62] Tr. 3031.
[63] $139,156,000 (Ex. 429, Schedule MEB-COS-5) / 4,170,226 Mwh (Ex. 429, page 16) = $33.37 / Mwh.
[64] Tr. 3028.
[65] Tr. 3021.

or potentially operating currently."[66] That said, Mr. Fayne readily admits that there are several other smelters, conveniently excluded from his analysis, that are potential producers including Rockdale,[67] Goldendale,[68] Frederick,[69] Columbia Falls,[70] Baden,[71] and Troutdale.[72] Despite the fact that such smelters fit his criteria as "potentially operating currently," Mr. Fayne omitted these smelters from his analysis.

The reason for their omission may not be hard to deduce. Noticeably, Mr. Fayne only included closed smelters which had a lower cost of electricity.[73] By including these closed smelters, Mr. Fayne was able to lower the average cost of electricity comparison. Closed smelters that had a higher cost of electricity, those whose cost would increase the average, were conveniently omitted. For instance, Mr. Fayne omitted Columbia Falls claiming that he did not have information related to the cost of electricity for this smelter.[74] Under cross examination, however, Mr. Fayne admitted that cost information for Columbia Falls was readily available in the CRU data upon which he relied.[75] Recognizing that Columbia Falls had the highest electric cost of any smelter fitting Mr. Fayne's criteria, it is apparent that, by omitting Columbia Falls, Mr. Fayne hoped to inaccurately lower the average cost of US smelters. Mr. Fayne readily admits that, had he properly included Columbia Falls, the average cost of electricity in his analysis would be higher.[76]

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[66] Tr. 3057.
[67] Tr. 3057.
[68] Tr. 3058.
[69] *Id.*
[70] *Id.*
[71] *Id.*
[72] *Id.*
[73] Ex. 421, Schedule HWF-1.
[74] Tr. 3049.
[75] Tr. 3048-3049.
[76] Tr. 3050.

3. Inclusion of Self-Generators

In addition to: (1) relying upon unreliable internet information and (2) failing to consistently apply the criteria underlying his analysis, Mr. Fayne also improperly included an aluminum smelter that self generates its own electricity.

Under cross-examination, Mr. Fayne admits that the Warrick, Indiana smelter, owned by Alcoa, produces its own electricity. Under further examination, Mr. Fayne indicated that the Warrick smelter self generates its own electricity through the neighboring Warrick generating unit, a 750 MW coal fired generating station.[77] By including such a smelter in its analysis, Noranda has sought to gain the benefits of self-generation while avoiding the enormous risks and capital costs associated with actually building and operating the power plant. To the extent that it believes that it is entitled to the lower cost of electricity associated with owning its own generation, Noranda should also be required to assume the risk of building the generating plant. Otherwise, the cost of electricity for the Warrick smelter should be removed from any competitive analysis.

4. Results Modified to Correct Oversights

As indicated, Noranda's cost of electricity analysis is misleading. As the evidence presented in this case reveals, the cost of electricity at the New Madrid smelter is not $35.67 / Mwh, as presented in the CRU data. Rather, the cost of electricity, based upon information contained in testimony provided by Noranda's witnesses is $33.37 / Mwh. Furthermore, it has been demonstrated that Mr. Fayne inappropriately applied his criteria in an attempt to reach a pre-determined conclusion. First, Mr. Fayne included smelters that are closed. His explanation for including such smelters is that they were potential competitors. That said, Mr. Fayne inexplicably excluded several smelters that

[77] Tr. 3039.

he acknowledges would fit his criteria. In fact, Mr. Fayne eliminated the smelter with the highest cost of electricity. The arbitrary picking and choosing of smelters slants his analysis to a pre-determined conclusion.

Ultimately, Mr. Fayne admits that, if his analysis were limited solely to smelters that are currently producing (i.e., eliminate all closed smelters instead of just those with high electricity costs), the average cost of electricity for U.S. smelters is $33.75 / Mwh – higher than Noranda's cost of electricity. Moreover, given that the Warrick smelter is not an appropriate comparison, (i.e., it generates its own electricity), it should also be eliminated. Mr. Fayne admits that if the Warrick smelter were also eliminated, the average cost of electricity for U.S. smelters is $34.27 – much higher than Noranda's cost of electricity.

Correction	***Cost of Electricity***
Corrected New Madrid Cost of Electricity	$33.37 / Mwh
National Average with Closed Smelters Removed	$33.75 / Mwh
National Average with Closed Smelters and Warrick Removed	$34.27 / Mwh

Ultimately, as can be seen from this table, Noranda's analysis is faulty. While Noranda claims that it cost of electricity is higher than other competitive smelters, when errors in Noranda's analysis are corrected, it appears that Noranda's cost of electricity is actually lower than other smelters currently operating in the United States. Such a conclusion is consistent with the fact, as demonstrated in the following section, that Noranda continued to operate at full production levels while other smelters closed production. Such conduct is only characteristic of a smelter that operates at a lower production cost than its competitors.

C. Noranda's Analysis Fails to Account for Other Competitive Cost Advantages

In support of its stated need for rate relief, Noranda presented an analysis that focused solely on its cost of electricity relative to other domestic aluminum smelters. In the previous section, MEUA discussed evidence which tends to indicate that Noranda's cost of electricity is not higher than its competitors, as claimed by Noranda. Rather, Noranda's cost of electricity is lower than other domestic smelters.

Noranda's competitive advantages extend past its cost of electricity. In its 10K filing with the SEC, Noranda revealed a number of other competitive advantages that it has over other domestic smelters. In this section, MEUA will discuss those numerous advantages. Furthermore, MEUA will show that these competitive advantages have been demonstrated in real life by Noranda's continued production at full capacity while other smelters have reduced or discontinued production.

Ultimately, the Commission should not be drawn to Noranda's short-sighted analysis. As the Commission is well aware, it is required to look at "all relevant factors"[78] prior to making any assessments as to a utility's profitability and its need for rate relief. Similar analysis of "all relevant factors" into Noranda's profitability should be undertaken before deciding that it needs rate relief.

The record indicates that the Noranda smelter has several significant cost components including alumina, labor, carbon products (coke and pitch), electricity and

[78] *State ex rel. Utility Consumers Council of Missouri v. Public Service Commission*, 585 S.W.2d 41, 56 (Mo. 1979) (citing to *State ex rel. Missouri Water Company v. Public Service Commission*, 308 S.W.2d 704, 719 (Mo. 1957).

freight.[79] Despite the fact that comparative cost for each of these significant cost components was available on the CRU database, Noranda never undertook a comparative analysis of these other "significant cost components."[80] As such, Noranda's analysis is necessarily short-sighted and certainly does not meet the "all relevant factors" analysis typically relied upon by this Commission.

Noranda's failure to include any analysis of "all relevant factors" is likely based upon the fact that Noranda possesses competitive advantages related to these other cost components. In its 10K, Noranda references each of these competitive advantages. For instance, Noranda's 10K indicates that as a result of its ownership of the St. Ann bauxite mine in Jamaica and the Gramercy refinery in Louisiana, Noranda has "a strategic supply of alumina at costs below recent spot market prices for alumina."[81] Another competitive advantage relates to Noranda's "secure source of electrical power."[82] Still again, Noranda notes that it has an advantage "because the New Madrid smelter's power costs are not tied to the LME price of aluminum."[83] Furthermore, Noranda claims that its "strategic location" relative to both alumina supplies and downstream rolling mills is another competitive advantage.[84] Finally, Noranda recognizes a competitive advantage in "freight costs" as well.[85] Had Noranda conducted an "all relevant factors" analysis, each of these competitive advantages would have been considered. By limiting its analysis to electric costs, Noranda has intentionally avoided any consideration of these competitive advantages.

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[79] Tr. 2941.
[80] Alumina at Tr. 3022; Labor at Tr. 3025; Carbon products at Tr. 3025; Freight costs at Tr. 3027.
[81] Tr. 2946.
[82] Tr. 2947.
[83] Tr. 2948.
[84] Tr. 2948-2949.
[85] Tr. 2949.

Despite the fact that Noranda did not include an "all relevant factors" analysis, evidence deduced in cross-examination reveals that such an analysis would show that Noranda has lower production costs than other domestic smelters. Facing aluminum prices that are slightly lower than in January of 2008,[86] many domestic smelters have recently reduced or terminated production. Noranda's CEO testified that production at the Ferndale,[87] Alcoa Tennessee,[88] Warrick,[89] Wenatchee,[90] Massena East,[91] Rockdale[92], Ravenswood,[93] Hawesville,[94] Hannibal,[95] and Columbia Falls[96] smelters has been stopped or at least reduced. Despite facing similar commodity prices for aluminum, Noranda continues to operate at full production.[97] In fact, absent the ice storm which prevented access to electricity, Noranda would have operated at full capacity during this entire period.[98]

Certainly, relative to each of the smelters that has either closed or decreased production, Noranda has a lower overall production cost. It is this lower production cost that allowed Noranda to continue to operate at full capacity while selling at the low commodity aluminum costs. As such, it is unquestionable, that an "all relevant factors" analysis would show that Noranda continues to be profitable and its threats of imminent failure are simple rhetoric.

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[86] Tr. 2939.
[87] Tr. 2950.
[88] Tr. 2953.
[89] Tr. 2954.
[90] Tr. 2956.
[91] Tr. 2956-2957.
[92] Tr. 2957.
[93] Tr. 2964.
[94] Tr. 2966.
[95] Tr. 2968.
[96] Tr. 2969.
[97] Tr. 2963.
[98] *Id.*

D. The Beneficiaries of any Noranda Rate Relief are Primarily Located in other States

In its request, Noranda asks that it be provided rate relief. In order to effectuate such relief, Noranda asks that other customers pay costs that would otherwise be paid by Noranda. Recognizing that Noranda has already made commitments to maintain current employment levels at the smelter,[99] it is logical that the only beneficiaries of such rate relief will be the few large shareholders located in other states.[100] While Noranda has a few (eleven) minute shareholders residing in Missouri, those shareholders combined own less than five percent of Noranda's common stock.[101] Therefore, the primary beneficiaries of Noranda's rate relief request will be the hedge fund owners in New York City. Inevitably, these shareholders will see immediate returns when the share price in the Noranda initial public offering is set.

In exchange for this scheme to export Missouri dollars to New York City, Noranda asks that all of UE's ratepayers pay higher rates. Recognizing that UE has ratepayers in Excelsior Springs,[102] Noranda is asking that customers from 395 miles away. Certainly, the benefits to these customers from Noranda's existence are tenuous.

V. CONCLUSION

As the evidence indicates, LGS / SP customers continue to suffer from rates that are up to 12.7% above cost. While Noranda was benefiting from previous rate reductions, these customers saw their rates continue to move further from cost. In this case, the Signatories have executed a Non-Unanimous Stipulation. In many ways, that

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[99] Tr. 2981.
[100] Tr. 2977.
[101] Tr. 2998.
[102] UE tariffs, Mo.P.S.C. Schedule No. 5, 8th Revised Sheet No. 14. See also, *Order Setting Local Public Hearings and Directing Notice*, issued November 5, 2009 at page 4. Transcript Volume 16.

Stipulation contemplates an appropriate resolution of the class cost of service / rate design issues. To the extent that it offers rate relief to Noranda, that Stipulation is unreasonable. Instead, the Commission should take that rate relief and assign to the LGS / SP customers that everyone agrees are paying rates that are above cost.

Respectfully submitted,

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ATTORNEYS FOR MIDWEST ENERGY USERS ASSOCIATION

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing pleading by email, facsimile or First Class United States Mail to all parties by their attorneys of record as provided by the Secretary of the Commission.

David L. Woodsmall

Dated: April 23, 2010