BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

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

INITIAL POSTHEARING BRIEF

OF

MIDWEST ENERGY CONSUMERS GROUP

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COME NOW the Midwest Energy Consumers' Group (collectively referred to herein as "MECG") by and through the undersigned counsel, pursuant to the Commission's August 10, 2014 *Order Adopting Procedural Schedule, Establishing Test Year, and Delegating Authority,* and provides its initial post-hearing brief. While MECG is concerned with all of the various revenue requirement issues, it will not burden the record with further argument on most of those issues. Instead, MECG will limit this brief to the following issues: (1) Vegetation Management / Infrastructure Inspection Trackers (Issue 10B); (2) Return on Equity (Issue 16); (3) Class Cost of Service (Issue 19 and certain subissues); and (4) Noranda Rate Proposal (Issue 31).

I. INTRODUCTION

In this case, the Commission will decide several different issues. MECG urges the Commission to avoid deciding this case or these issues in a vacuum. Rather, MECG maintains that the Commission should view this case with consideration to past events. First, the Commission should consider the rapid increase in rates that Ameren customers have realized since 2007. Second, the Commission should consider that Ameren has earned a return well above that authorized by the Commission in the last case.

A. RAPID INCREASE IN AMEREN RATES

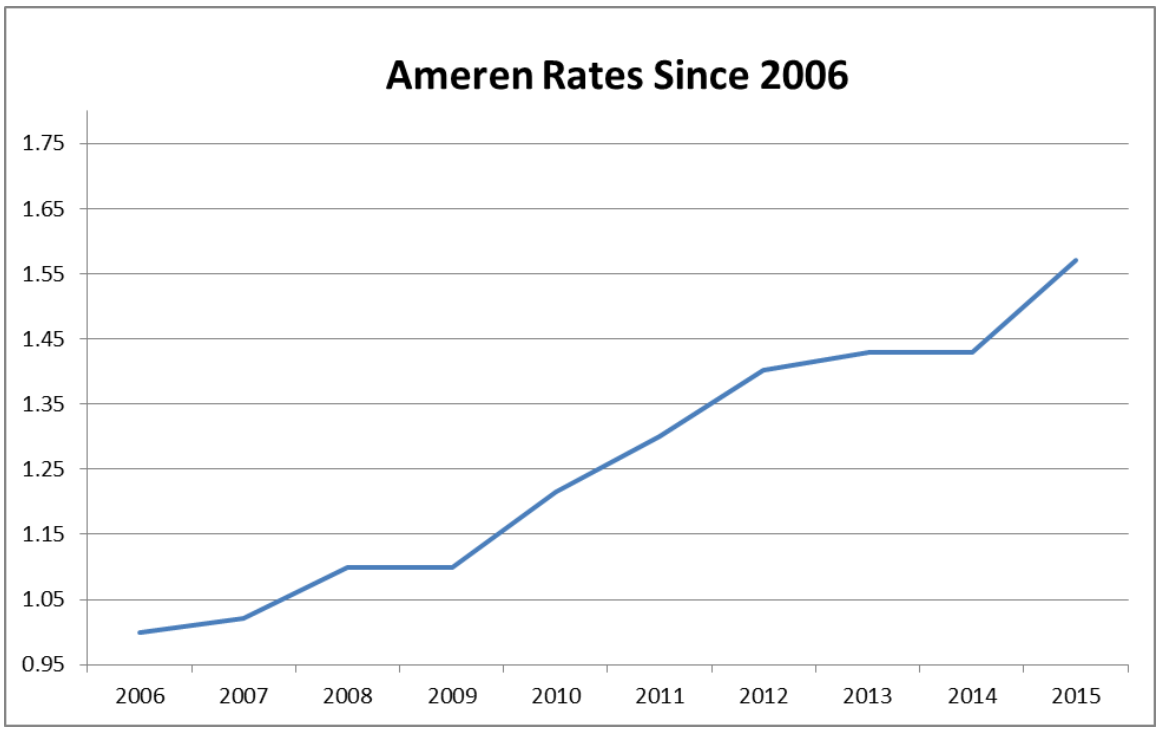
Since 2006, Ameren rates have skyrocketed. Specifically, since that date, the Commission has authorized the following rate increases.[1]

• ER-2007-0002:	$42.8 million	2.07% increase
• ER-2008-0318:	$161.7 million	7.75% increase
• ER-2010-0036:	$229.6 million	10.43% increase
• ER-2011-0028:	$173.2 million	7.11% increase
• ER-2012-0166:	$259.6 million	10.05% increase
	$866.9 million	43.16% increase

Recognizing that Ameren is still seeking a $181.2 million (6.66%) increase in this case,[2] Ameren rates will have increased by over $1.04 billion (52.7%) since 2007. Adding insult to injury, Ameren has also collected an additional $657.0 million since 2008 through 17 fuel adjustment increases.

The tremendous increase in Ameren rates is particularly noticeably when viewed graphically.

[1] Exhibit 202, Staff Cost of Service Report, page 6.
[2] See, *Reconciliation*, filed March 28, 2015.



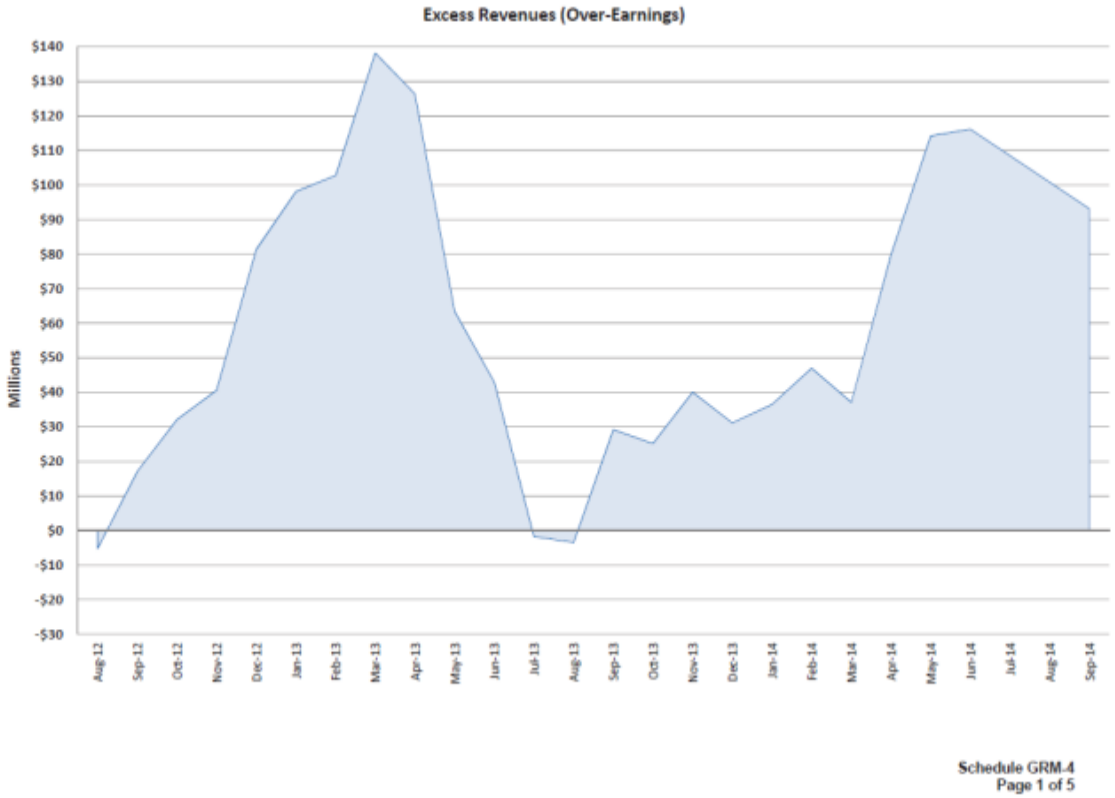
The impact of this rapid increase in Ameren rates is best understood when compared to how slow Ameren customers' household income has grown over the same period of time. Specifically, the average weekly wage of Ameren's customers has only increased by 10.51% over the same period of time.[3] Thus, by any measure, Ameren's ratepayers are spending an ever increasing portion of its limited household income on the electricity provided by Ameren. In addition, concerns must begin to arise as to the affordability of Ameren's industrial customers to compete against companies located in areas with lower, slower-rising electric rates.

B. AMEREN'S RECENT OVER-EARNINGS

While Ameren's rates have increased tremendously over the last several years, it is even more troublesome that Ameren's rates, as established in the last case, were clearly

[3] Exhibit 202, Staff Cost of Service Report, page 5.

too high. A tremendous amount of evidence was provided which showed Ameren's recent earnings. While authorized a 9.80% return on equity in December of 2012, Ameren earned tens of millions of dollars above that authorized return. The following graph demonstrates, on a rolling 12 month basis, the amount of Ameren's earnings as compared to that authorized by the Commission.



Source: Exhibit 513, Meyer Direct,

While the Commission is powerless to order Ameren to return these past over-earnings, the Supreme Court has noted that the Commission is allowed to consider these past over-earnings in the context of this proceeding. "The commission has the authority to determine the rate *to be charged, § 393.270*. 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."[4]

While the Commission is mandated to allow Ameren recovery of certain costs in this case, other portions of Ameren's proposed rate increase are discretionary in nature. Specifically, requests for an inflated return on equity and deferral of certain past costs (from a period of over-earnings) for recovery in this case should be rejected by the Commission. Through such actions, the Commission may indicate a concern for the rapid increase in and affordability of Ameren's rates.

[4] *State ex rel. Utility Consumers Council of Missouri v. Public Service Commission*, 585 S.W.2d 41, 58 (1979).

II. OVERVIEW OF POSITIONS

VEGETATION MANAGEMENT (ISSUE 10B): The Commission should discontinue the vegetation management and infrastructure inspection trackers. Through the tracker mechanism, Ameren seeks Commission authority to defer and later recover the difference between the amount of vegetation management / infrastructure inspection costs built into rates and the level of costs that Ameren actually incurs. Missouri courts have limited the recovery of deferred costs solely to situations where the cost is extraordinary. When the Commission initially promulgated the vegetation management and infrastructure inspection rule, it imposed a new cost on the utilities. As such, it was reasonable to consider such costs as "extraordinary." Recognizing that these costs are no longer "extraordinary," the trackers should be discontinued.

RETURN ON EQUITY (ISSUE 16): Consistent with the recommendation of MIEC Witness Gorman, the Commission should authorize Ameren to earn a return on equity of 9.30%. Unlike Ameren's testimony, this recommendation is consistent with previous Commission decisions and recognizes the continuing decline in utility capital costs.

GENERATION FIXED COSTS ALLOCATION (ISSUE 19A): The Commission should utilize the Average & Excess (4 NCP) methodology to allocate generation fixed costs among the customer classes.

NON-FUEL, NON-LABOR PRODUCTION O&M ALLOCATION (ISSUE 19B): The Commission should allocate the non-fuel, non-labor component of production O&M expense using the same A&E 4 NCP production allocator.

OFF-SYSTEM SALES REVENUES ALLOCATION (ISSUE 19G): The Commission should allocate off-system sales margins using the energy allocator.

INCOME TAX EXPENSE ALLOCATION (ISSUE 19H): The Commission should allocate income tax expense based upon the income tax obligation of the specific classes.

FUEL AND PURCHASED POWER COST ALLOCATION (ISSUE 19I): In the event that the Commission adopts Public Counsel's Peak & Average production allocator, it should also allocate a below average amount of fuel costs to high load factor customers in order to account for the larger amount of base load units allocated to these high load factor customers.

REVENUE ALLOCATION (ISSUE 19C): The Commission should take affirmative steps to recognize and eliminate the fact that residential rates are not currently recovering their cost of service and LGS / SP rates are well above their cost of service.

NORANDA RATE PROPOSAL (ISSUE 31): The evidence indicates that Noranda is not suffering from a liquidity crisis. In fact, given its own definition, Noranda had the same amount of liquidity when the Commission considered Ameren's last rate increase.

Despite the same amount of liquidity, Noranda agreed to an equal-percent, across-the-board rate increase in that case. Similarly, the lack of a liquidity crisis is reflected in the vastly different public statements that Noranda has made to its investors as opposed to the confidential statements that Noranda has made to the Commission.

The evidence further indicates that, under the Non-Unanimous Stipulation, customers would be better off if Noranda simply closed. Under Noranda's best case scenario, which relies upon faulty historical evidence, there is a minimal difference between the increased amount that ratepayers would pay: (1) under the Non-Unanimous Stipulation and Agreement as opposed to (2) if Noranda simply closed. As Mr. Brubaker admits, however, this minimal difference is based entirely on current rates and does not consider the additional amount that ratepayers will suffer from absorbing any rate increase in this case that would otherwise be allocated to Noranda. Furthermore, Brubaker's analysis is based upon the assumption of normal weather during the entire length of any Noranda subsidy rate commitment. As the Commission has previously found, weather anomalies, like the polar vortex, will occur in the future and will have an impact on prices.

The better evidence, which includes a forecast of future revenues that Ameren ratepayers could realize from Ameren selling the Noranda load in the wholesale market definitively shows that Ameren customers are $272 million worse off under Noranda's original proposal than if Noranda simply ceased operations. Even more egregious, under the 10-year proposal contained in the Non-Unanimous Stipulation, ratepayers are $550 million worse off than if Noranda closed its doors.

Given Noranda's current liquidity, the questionable nature of its threats to close the New Madrid smelter and the fact that Ameren ratepayers would be better off if Noranda simply discontinued operations, MECG urges the Commission to reject any special Noranda rate proposal. Instead, MECG asserts that the Commission should continue to be guided by the various class cost of service studies presented in this case. Recognizing that all of those studies, including Noranda's own study, indicate that Noranda is currently paying rates that are well below cost of service, MECG recommends that the Commission authorize a rate increase to the LTS class (Noranda) which is above the system average increase authorized to Ameren.

III. BURDEN OF PROOF

Section 393.150(2) provides that, in any rate increase proceeding, the burden of proof is on the party seeking the increased rate. In considering the appropriate hearing schedule in a recent proceeding, the Commission adopted KCPL's schedule based solely upon its acknowledged burden of proof.

> Furthermore, the Commission will adopt the order of issues proposed by KCP&L. While the Commission understands the positions argued by Staff and MEUA, the Commission concludes that KCP&L has the burden to put on its case, and should be granted considerable leeway in the order in which it would like to present its evidence.[5]

Burden of proof, however, does not only mean that the utility gets the advantages when it comes to presenting its evidence. Burden of proof also means that the utility must accept the "burden" of proving its case.

In this regard, the Supreme Court has provided a great deal of insight regarding burden of proof. Specifically, as it applies to Commission proceedings, the Supreme Court has told us: (1) that burden of proof is a "substantial right" of the customers and (2) that burden of proof should be "rigidly enforced" by the Commission.

> The rules as to burden of proof are important and indispensable in the administration of justice, and constitutes a substantial right of the party of whose adversary the burden rests; they should be jealously guarded and rigidly enforced by the courts.[6]

The Supreme Court has also provided definition for the burden of proof.

> The burden of proof meaning the obligation to establish the truth of the claim by a preponderance of the evidence, rests throughout upon the party asserting the affirmative of the issue. The burden of proof never shifts during the course of the trial.[7]

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[5] *Order Setting Blocks of Exhibit Numbers*, Case No. ER-2010-0355, page 2 (issued January 12, 2011).
[6] *Highfill v. Brown*, 320 S.W.2d 493 (Mo. 1959).
[7] *Clapper v. Lakin*, 123 S.W.2d 27 (Mo. 1938).

As such, the burden of proof means that the proponent of higher rates in a Commission proceeding has the "obligation to establish the truth" of its need for the higher rates. In this regard, customers are given the benefit of the doubt that the utility only needs the lower rate and that the utility must "prove" that the higher rate is necessary. Therefore, if there is any question regarding the legitimacy of a cost or expense; if the Commission does not adequately understand an issue; or if the Company fails to adequately explain its need for the higher rate, then the utility has failed to meet its burden of proof.

Finally, the Supreme Court has provided insight as to the implications to a party that fails to meet its burden of proof: "the failure of the plaintiff to sustain such burden ***is fatal*** to his or her relief or recovery."[8]

[8] *Id.*

IV. VEGETATION MANAGEMENT / INFRASTRUCTURE INSPECTION TRACKERS

Position: The Commission should discontinue the vegetation management and infrastructure inspection trackers. Through the tracker mechanism, Ameren seeks Commission authority to defer and later recover the difference between the amount of vegetation management / infrastructure inspection costs built into rates and the level of costs that Ameren actually incurs. Missouri courts have limited the recovery of deferred costs solely to situations where the cost is extraordinary. When the Commission initially promulgated the vegetation management and infrastructure inspection rule, it imposed a new cost on the utilities. As such, it was reasonable to consider such costs as "extraordinary." Recognizing that these costs are no longer "extraordinary," the trackers should be discontinued.

As the Commission has previously recognized, the consideration of costs from a previous period violates the traditional method of setting rates.

> ***The deferral of costs from one period to another period for the development of a revenue requirement violates the traditional method of setting rates***. Rates are usually established based upon a historical test year which focuses on four factors: (1) the rate of return the utility has an opportunity to earn; (2) the rate base upon which a return may be earned; (3) the depreciation costs of plant and equipment; and (4) allowable operating expenses. ***Allowable operating expenses are those which recur in the normal operations of a company***.[9]

Given that the ratemaking process is focused on "recurring" costs, the Commission has had to develop an alternative mechanism for the recovery of "non-recurring" costs. In such instances, and contrary to the "traditional method of setting

[9] *Application of Missouri Public Service Company*, Report and Order, Case No. EO-91-358 and EO-91-360, 1 Mo.PSC 3d 200, 205 (emphasis added). ("Sibley").

rates," the Commission has permitted the utility to defer such non-recurring costs for recovery in a future case.

> Under historical test year ratemaking, costs are rarely considered from earlier than the test year to determine what is a reasonable revenue requirement for the future. Deferral of costs from one period to a subsequent rate case causes this consideration and should be allowed only on a limited basis.

This limited basis is when events occur that cause costs that are extraordinary, unusual and unique, and not recurring. These types of events generate costs which require special consideration. The limitation on the Commission's authority to defer and allow future recovery of costs is found in the constitutional doctrine against retroactive ratemaking and the later exception for extraordinary costs.

Specifically, in the UCCM decision, the Supreme Court considered the legality of the fuel adjustment clause. Addressing an associated surcharge mechanism, the Missouri Supreme Court set forth the prohibition against retroactive ratemaking.

> The Companies take the risk that rates filed by them will be inadequate, or excessive, each time they seek rate approval. To permit them to collect additional amounts simply because they had additional past expenses not covered by either clause is ***retroactive rate making, i.e., the setting of rates which permit a utility to recover past losses or which require it to refund past excess profits collected under a rate that did not perfectly match expenses plus rate-of-return with the rate actually established***. Past expenses are used as a basis for determining what rate is reasonable to be charged in the future in order to avoid further excess profits or future losses, but under the prospective language of the statutes, *§§ 393.270(3)* and 393.140(5) they cannot be used to set future rates to recover for past losses due to imperfect matching of rates with expenses.[10]

Thus, under the prohibition against retroactive ratemaking, the Commission is prohibited from considering past costs due to "imperfect matching of rates with expenses."

[10] *State ex rel. Utility Consumers Council of Missouri v. Public Service Commission*, 585 S.W.2d 41, 59 (Mo. banc 1979) (emphasis added). ("UCCM").

Given the broad nature of the UCCM prohibition against retroactive ratemaking, it would appear that any deferral of costs for future consideration would be prohibited. In an appeal from the Commission's Sibley decision, however, the Court carved out a limited exception to the doctrine against retroactive ratemaking for "extraordinary" costs. In that case, the Court considered whether the Commission's deferral of extraordinary costs associated with the rebuilding of the Sibley generating station was "legal and reasonable."[11]

> The Commission's decision to grant authority to defer the costs associated with the Sibley reconstruction and coal conversion projects by recording the costs in Account No. 186 was the result of the Commission's determination that the construction projects were unusual and nonrecurring, and therefore, extraordinary. The Commission determined the projects to be unusual because of their size and substantial cost. The Commission expressed that deferral of costs just to support the current financial status distorts the balancing process utilized by the Commission to establish just and reasonable rates. Because rates are set to recover continuing operating expenses plus a reasonable return on investment, ***only an extraordinary event should be permitted to adjust the balance to permit costs to be deferred for consideration in a later period***.[12]

From the foregoing case law, several things become apparent. First, the ratemaking process is focused on the recurring costs of the utility. Second, the Commission is prohibited from engaging in retroactive ratemaking. Third, the Court has recognized a limited exception to the doctrine against retroactive ratemaking for costs that are extraordinary.

In a recent decision regarding the scope of costs that should be considered for deferral and future recovery, the Commission expressly recognized that its authority to allow recovery of deferred costs was limited solely to "extraordinary" costs.

[11] *State ex rel. Office of the Public Counsel v. Public Service Commission*, 858 S.W.2d 806, 807 (Mo.App. W.D. 1993).
[12] *Id.* at page 811 (emphasis added).

> In Missouri, rates are normally established based off of a historic test year. The courts have stated than an AAO allows the deferral of a final decision on current *extraordinary* costs until a rate case and therefore is not retroactive ratemaking. Consistent with the language in General Instruction No. 7, the Commission has evaluated the transmission costs for which Companies seek an AAO to determine if they are an unusual and infrequent occurrence. The Commission concludes they are not.[13]

Just as the Commission refused to allow KCPL to defer and later recover transmission costs, it should also disallow the deferral and future recovery of costs through the vegetation management and infrastructure inspection trackers. While these costs were once considered extraordinary (as a result of the promulgation of a new Commission rule), those costs are now ordinary and recurring. As MIEC points out:

> The Commission initially established the tracker because of a lack of historical cost experience for Ameren Missouri to comply with the Commission's vegetation management rule enacted in July 2008. The vegetation management rules required that rural circuits be trimmed every six years and that urban circuits be trimmed every four years. Ameren Missouri begin compliance with the vegetation management rule in January 2008, ahead of the rule implementation in July 2008. At the end of the true-up period in this case, Ameren Missouri will have achieved a complete cycle trim of all of its circuits. . . . Sufficient cost data now exists for this portion of Ameren Missouri's operations such that the need for a tracker no longer exists.[14]

Recognizing that these costs are no longer extraordinary and that sufficient cost data exists for the Commission to use in setting recurring rates, the Commission should discontinue the vegetation management and infrastructure inspection trackers.

[13] Case No. EU-2014-0077, *Report and Order*, issued July 30, 2014, at page 10.
[14] Exhibit 513, Meyer Direct, page 22.

V. RETURN ON EQUITY

Position: Consistent with the recommendation of MIEC Witness Gorman, the Commission should authorize Ameren to earn a return on equity of 9.30%. Unlike Ameren's testimony, this recommendation is consistent with previous Commission decisions and recognizes the continuing decline in utility capital costs.

A. INTRODUCTION AND OVERVIEW

It is well established that public utility commissions have several basic objectives. Foremost among these objectives is to ensure adequate earnings for the utility while preventing excessive (monopoly) profits.[15] Absent regulatory controls, the utility will inevitably seek to extract monopoly profits from the many (the ratepayers of Missouri) for the benefit of the few (the utility shareholders scattered across the nation).

The attempt to extract monopoly profits in this case is best seen in Ameren's request for an inflated return on equity. Rather than seeking that level of return that is "sufficient to ensure confidence in the financial soundness of the utility,"[16] Ameren seeks to bolster its corporate profits. The Supreme Court has pointed out, however, that the utility has no "right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures."[17]

In this case, Ameren requests an inflated profit (the return on equity) of 10.40%.[18] In support of this request, Ameren presents the flawed testimony of Robert Hevert. In contrast, MIEC presents the testimony of Michael Gorman who arrives at a return on

[15] Phillips, Charles F. Jr., *The Economics of Regulation*, Rev. ed. (1969) at page 124.
[16] *Bluefield Water Works and Improvement Co. v. Public Service Comm'n*, 262 U.S. 679, 692-693 (1923).
[17] *Id.*
[18] Exhibit 16, Hevert Direct, page 2.

equity range of 9.00% to 9.60% with a recommended return on equity of 9.30.[19] Staff presented the testimony of David Murray who concludes that a range of 9.00% to 9.50% with a recommended return on 9.25% is reasonable[20] Finally, OPC presented the testimony of Lance Schafer who determines that a range of 8.74% to 9.22% with a recommended return on equity of 9.01% is reasonable.[21] Clearly, Mr. Hevert's recommendation stands out as strikingly higher than that recommended by the other return on equity experts.

As this brief demonstrates, Mr. Hevert's recommendation is inflated because it is fundamentally flawed. In recent cases, the Commission has pointed our specific concerns with Hevert's methodology. Despite the clarity of the Commission's prior criticism, Mr. Hevert presents the same flawed analysis in this case. As a result of this flawed analysis, the Commission, in its last two Ameren decisions, concluded that Mr. Hevert's recommendation is "too high" and rejected his recommendation.[22] For the same reasons, the Commission should disregard Mr. Hevert's recommendation in this case.

In contrast to Hevert's inflated recommendation, Mr. Gorman presents a reasoned analysis. This analysis is identical in approach to those recently provided by Mr. Gorman and expressly adopted by the Commission. As Mr. Gorman demonstrates, Ameren's current investment grade credit rating would be fully supported at either end of his return on equity range. Furthermore, Mr. Gorman's recommendation is consistent with the continued decline in the cost of capital that has been experienced since the Commission authorized a 9.80% return on equity for Ameren in December of 2012. In this brief,

[19] Exhibit 510, Gorman Direct, page 2.
[20] Exhibit 202, Staff Cost of Service Report, page 8.
[21] Exhibit 409, Schafer Direct, page 3.
[22] Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at pages 69-70.

MECG urges the Commission to authorize Ameren a return on equity that is consistent with Mr. Gorman's recommended return of 9.30%.

B. OVERVIEW OF THE RECOMMENDATIONS

Consistent with the approach utilized in previous cases, Mr. Gorman has prepared a return on equity analysis in this case which ensures sufficient and comparable earnings while avoiding concerns of monopoly profits. Specifically, Mr. Gorman has utilized: (1) three versions of the discounted cash flow model; (2) a risk premium analysis and (3) a CAPM analysis, in his determination of a just and reasonable return on equity. The ultimate result of these models leads to a recommended range of 9.00% - 9.60%.[23]

MODEL		RESULT
DCF	Constant Growth	8.95% (Exhibit 510, Gorman Direct, page 18)
	Sustainable Long-Term Growth	8.71% (Exhibit 510, Gorman Direct, page 20)
	Multi-Stage Growth	8.57% (Exhibit 510, Gorman Direct, page 26)
Risk Premium		9.60% (Exhibit 510, Gorman Direct, page 32)
CAPM		9.24% (Exhibit 510, Gorman Direct, page 37)
Recommendation		**9.30%** (Exhibit 510, Gorman Direct, page 38)

The reasonableness of Mr. Gorman's 9.30% recommendation is best reflected by a simple comparison to the recommendations made by the other return on equity witnesses in this case.

[23] Exhibit 510, Gorman Direct, page 38.

Party Witness	ROE Recommendation
Staff Witness Murray	9.25%
MIEC Witness Gorman	9.30%
OPC Witness Schafer	9.01%
Ameren Witness Hevert	10.4%[24]

Thus, while Mr. Gorman's recommendation is supported by two other experts, Hevert's recommendation on behalf of Ameren is shown to be an outlier.[25]

The problem with Hevert's analysis is not in the models that he used. Rather, the ongoing problem with Hevert's analysis is reflected in the assumptions that he employs. Once corrected, even Hevert's analysis falls in line with the other recommendations. Specifically, after accounting for and correcting the assumptions in his methodology, even Mr. Hevert's analysis leads to a reasonable result (8.75% - 9.24%).[26]

	MODEL	HEVERT RESULT	ADJUSTED HEVERT RESULT
DCF Analysis			
	CONSTANT GROWTH DCF	9.56% - 9.73%[27]	9.00 – 9.17%[28]
	MULTI-STAGE GROWTH DCF	9.93 - 10.13%[29]	8.70 – 8.90%[30]
CAPM		10.59 – 11.92%[31]	8.80 – 9.52%[32]
Risk Premium Analysis		10.16 - 10.77%[33]	7.53% - 8.43%[34]
Recommendation		10.20 – 10.60%[35]	**9.30%**[36]

[24] Exhibit 16, Hevert Direct, page 2.
[25] The Commission has previously looked at the consistency of the return on equity recommendations in rejecting outliers like the current Hevert recommendation. See, *Report and Order*, Case No. ER-2011-0028, issued July 13, 2011, at page 70, paragraph 22.
[26] Exhibit 511, Gorman Rebuttal, page 3.
[27] Exhibit 16, Hevert Direct, page 19.
[28] Exhibit 511, Gorman Rebuttal, pages 3 and 6.
[29] Exhibit 16, Hevert Direct, page 24.
[30] Exhibit 511, Gorman Rebuttal, pages and 10.
[31] Exhibit 16, Hevert Direct, page 27.
[32] Exhibit 511, Gorman Rebuttal, pages 3 and 13.
[33] Exhibit 16, Hevert Direct, page 30.
[34] Exhibit 511, Gorman Rebuttal, pages 3 and 15.
[35] Exhibit 16, Hevert Direct, page 42.
[36] Exhibit 511, Gorman Rebuttal, page 3.

As can be seen, when based upon more reliable assumptions, Mr. Hevert's analysis provides results that are virtually identical to Mr. Gorman's recommendation as well as those of Mr. Murray and Mr. Schafer. As will be seen, this return on equity is consistent with the dictates of the Supreme Court. Specifically, this return is commensurate with the level of risk assigned to Ameren and provides financial support for Ameren's investment grade credit rating.

C. GORMAN CREDIBILITY AND OBJECTIVE ANALYSIS

In its consideration of the return on equity issue in recent rate cases, the Commission has frequently been presented with the analysis conducted by Mr. Gorman. Repeatedly in its decision in those cases, including several recent Ameren cases, the Commission has relied upon the reasoned approach presented by Mr. Gorman.

> [T]he Commission finds Michael Gorman to be the most credible and most understandable of the three ROE experts who testified in this case.[37]
>
> Michael Gorman, the witness for SIEUA, AG-P and FEA, did the best job of presenting the balanced analysis the Commission seeks.[38]
>
> In particular, the Commission accepts as credible the testimony of MIEC's witness, Michael Gorman. . . . Of the witnesses who testified in this case, Michael Gorman, the witness for MIEC, does the best job of presenting the balanced analysis that the Commission seeks.[39]

In this case, Mr. Gorman presents the same "credible" and "balanced" analysis relied upon by the Commission in those recent cases. Here, realizing the Commission's previous interest in considering the results of multiple return on equity analyses, Mr. Gorman provided the results of five different analyses: (1) a constant growth DCF

[37] Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at page 70.
[38] Case No. ER-2007-0004, *Report and Order*, issued May 17, 2007, at page 62.
[39] Case No. ER-2007-0002, *Report and Order*, issued May 22, 2007, at pages 40-41.

analysis using analysts' 3-5 year growth rates; (2) a sustainable growth DCF analysis; (3) a multi-stage growth DCF analysis which relies on a long-term growth rate equal to the consensus analysts' projection of gross domestic product; (4) a risk premium analysis and (5) a Capital Asset Pricing Model analysis.[40] The average of all of these analyses result in a recommendation of 9.00-9.60%.[41]

Unique among the recommendations provided by the return on equity experts in this case, and consistent with the directives of the *Hope* and *Bluefield* decisions, Mr. Gorman then checks to ensure that his recommended return on equity will support an investment grade credit rating. Specifically, Mr. Gorman undertook certain financial tests for Ameren based upon his recommended 9.30% return on equity.[42] Mr. Gorman then compared the results of those tests to the benchmarks for two critical S&P financial ratios: (1) debt to EBITDA (Earnings Before Income Taxes, Depreciation and Amortizations); and (2) funds from operations to total debt.[43] As Mr. Gorman's analysis reveals, his recommended return on equity will allow Ameren to meet the investment grade credit metrics for each of these financial ratios. As Mr. Gorman concludes, therefore, "[a]t my recommended return on equity of 9.30% and the Company's proposed embedded debt cost and capital structure, Ameren Missouri's financial credit metrics are supportive of its investment grade utility bond rating"[44]

[40] Exhibit 510, Gorman Direct, pages 15-19 (constant growth DCF); pages 19-20 (sustainable growth DCF); pages 20-26 (multi-stage growth DCF); pages 27-32 (risk premium analysis); and pages 32-37 (CAPM analysis).
[41] *Id.* at page 38.
[42] *Id.* at pages 39-42 and MPG-17.
[43] *Id.* page 40.
[44] *Id.* at page 43.

D. HEVERT'S FLAWED AND INFLATED ANALYSIS

In contrast to Gorman's impeccable credibility before this Commission, Mr. Hevert's credibility is questionable. Mr. Hevert has twice testified before this Commission. On both occasions, the Commission found that Mr. Hevert's assumptions and recommendations were "too high."

> However, Hevert's estimation of an appropriate ROE is ***too high***. MIEC's witness, Michael Gorman explains that Mr. Hevert relied on long-term sustainable growth rate estimates in his DCF models that are higher than the growth outlook of the economy as a whole. As he explained, it is not rational to expect that utilities can grow faster than the demand of the economies they serve.[45]

> Hevert's recommended return on equity is higher than the other recommendations in large part because he over-estimates future long-term growth in his various DCF analyses, making them ***too high*** to be reasonable estimates of long-term sustainable growth. When Hevert's long-term growth rates are adjusted to use more sustainable growth estimates based on published analyst's projections, his multi-stage DCF analysis produces a rate of return more in line with the estimates of LaConte and Gorman.[46]

Missouri is not the only commission that has recognized that Mr. Hevert's recommendations are "too high." In fact, over the past two years, state utility commissions have always awarded a return on equity that is well below Mr. Hevert's recommendation. As Exhibit 970 indicates, in 19 cases reported since January 1, 2013, Mr. Hevert has recommended an average return on equity of 10.53%. In contrast, the state utility commission decision in those 19 reported cases averaged 9.70%. Therefore, Hevert's recommended return on equity has exceeded that awarded by the various state utility commissions by 83 basis points.[47]

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[45] Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at pages 69-70. (emphasis added).
[46] Case No. ER-2011-0028, *Report and Order*, issued July 13, 2011, at page 23. (emphasis added).
[47] Exhibit 970. See also, Tr. 1121.

The reasons underlying Hevert's inflated recommendations are apparent when one digs further into Hevert's flawed methodologies. In at least four different ways Hevert has inflated the results of his various analyses.

First, Mr. Hevert employed "excessive, unsustainable growth rates" in the calculation of his constant growth DCF analysis.[48] As Mr. Gorman pointed out, "[m]ost of his [Hevert's] DCF return estimates are based on growth rates that are too high to be reasonable estimates of long-term sustainable growth."[49] Specifically, in calculating his high-end DCF return on equity, Mr. Hevert employed a proxy group growth rate of 6.96%. This is significantly above the actual proxy group average growth rate (5.34% to 5.97%)[50] that is already inflated in that it exceeds the projected GDP growth rate over that period (4.4% - 4.8%).[51]

> These proxy group mean growth estimates are substantially higher than the consensus economists' long-term growth outlooks of the U.S economy. The GDP growth of the U.S. general economy, which is a proxy for the growth rate of the economies in which these utilities operate, is between 4.4% and 4.8% indefinitely. It is simply not rational to expect that these companies can grow considerably faster than the economies in which they provide service over a long period of time.[52]

As previously indicated, this Commission has repeatedly criticized Hevert's analysis for employing growth rates which exceed "reasonable estimates of long-term sustainable growth."[53] As Mr. Gorman has shown, when more realistic growth rates are

[48] Exhibit 511, Gorman Rebuttal, pages 2 and 3-6.
[49] *Id*. at page 4.
[50] *Id*.
[51] *Id*. at page 5.
[52] *Id*.
[53] See, Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at pages 69-70 and Case No. ER-2011-0028, *Report and Order*, issued July 13, 2011, at page 23.

employed, Mr. Hevert's constant growth DCF analysis results in a DCF estimate of 8.50% to 9.60% with a midpoint of 9.10%.[54]

Second, in his multi-stage growth DCF analysis, Mr. Hevert "makes an inconsistent assumption on his long-term steady-state growth rate, in combination with his long-term steady-state dividend payout ratio."[55] Specifically, while he assumes an increasing dividend yield in his proxy group, Mr. Hevert also assumes an increasing dividend payout ratio for his proxy group. Therefore, while current proxy group dividend payout ratios are 60.33 – 61.13%, Hevert assumes that this payout ratio will increase to 67.05%.[56]

Hevert arrives at his assumption by conveniently replacing the *Value Line* three to five year payout ratio projections for his proxy companies with the *Value Line* dividend payout ratio for the electric utility industry as a whole.[57] As Mr. Gorman points out, "Mr. Hevert's changing payout ratio assumptions simply are not reasonable based on the similar projections made by *Value Line* for the industry and the individual companies included in the proxy group."[58] "Making this adjustment in his model simply inflates the growth rate for dividends relative to earnings growth. . . and increases his DCF return estimate."[59]

Third, in his multi-stage growth DCF analysis, Mr. Hevert's long-term sustainable growth rates is based on a nominal GDP growth rate that is considerably higher than consensus analysts' projections.[60] Specifically, Mr. Hevert uses a long-term

[54] Exhibit 511, Gorman Rebuttal, page 6
[55] *Id.*
[56] *Id.* at pages 8-9.
[57] *Id.* at page 9.
[58] *Id.* at page 10.
[59] *Id.*
[60] *Id.* at page 6.

historical real GDP return of 3.27%, as measured over the period of 1929 through 2013. He then adjusted for realized inflation to arrive at a long-term nominal GDP growth rate of 5.71%.[61]

It is readily apparent that Hevert's long-term GDP growth rate in his multi-stage DCF analysis is inflated. In contrast to Hevert's GDP growth of 5.71%, consensus economists' estimates of GDP growth over the next five to 10 year period range from 4.45% to 4.75%.[62] As such, Mr. Hevert's multi-stage growth DCF is inflated.

When one corrects for both of the errors in his multi-stage growth DCF analysis, Mr. Hevert's multi-stage DCF analysis decreases from 10.02% to a range of 8.70% to 8.90%.[63] This is clearly in line with the results of Mr. Gorman's multi-stage DCF analysis of 8.57%.[64]

Fourth, Mr. Hevert employed inflated market risk premiums in the calculation of his CAPM return. Specifically, Mr. Hevert's market CAPM analysis employs a growth rate of 10.62% to 11.49%.[65] As Gorman notes, "these growth rates are more than two times the growth rate of the U.S. GDP long-term growth outlook of 4.6%."[66] Utilizing a more reasonable estimate of market risk premium results in a CAPM of 8.80 to 9.52% with a midpoint of 9.16%[67] Again, Hevert's corrected analysis is consistent with the result of Gorman's CAPM analysis of 9.24%.[68]

As can be seen, Mr. Hevert routinely recommends a return on equity that state utility commissions have found to be "too high." In fact, over the last two years, state

[61] *Id.* at page 7.
[62] *Id.* at page 8.
[63] *Id.* at page 11.
[64] Exhibit 510, Gorman Direct, page 26.
[65] Exhibit 511, Gorman Rebuttal, page 12.
[66] *Id.*
[67] *Id.*
[68] Exhibit 510, Gorman Direct, page 37.

utility commissions have found Hevert's return on equity to be inflated by 83 basis points. As this brief has shown, the reason underlying Hevert's inflated recommendation is found in his faulty analysis and his reliance on inflated data. If the Commission simply recognized the same 83 basis points premium that other state utility commissions have found, then Hevert's recommendation is lowered from 10.4% to 9.57% and becomes consistent with the overall decrease in capital costs.

E. CAPITAL COSTS ARE DECREASING

On December 12, 2012, the Commission issued its Report and Order in Ameren's last rate proceeding (Case No. ER-2012-0166). In that decision, the Commission authorized Ameren to earn a return on equity of 9.80%.[69] In that order the Commission found that: (1) capital costs, as reflected in both utility bond yields and national average authorized return decisions, had declined significantly from 10.27% to 9.90% in less than 2 years;[70] (2) Mr. Hevert's analysis was "too high";[71] and (3) Mr. Gorman was "the most credible and most understandable of the three ROE experts."[72]

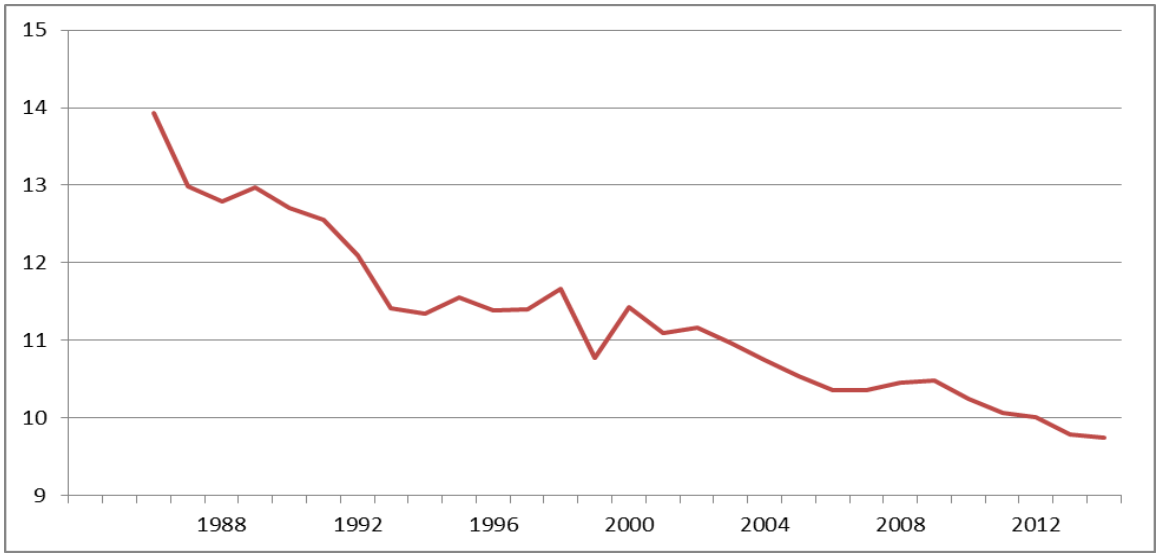
In the 25 months since the Commission issued its decision in ER-2012-0166, capital costs have continued to decrease. In the previous case, the Commission expressly noted a decrease in utility bond yields.[73] As reflected in Schedule 10 to his direct testimony, Mr. Gorman points out that utility bond yields have decreased from 2.00% at

[69] Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at page 72.
[70] *Id.* at page 67.
[71] *Id.* at page 69.
[72] *Id.* at page 70.
[73] *Id.* at page 68.

the end of 2012 to approximately 1.65% in 2014.[74] Thus, capital costs have decreased further from where they were at the time the Commission authorized a return of 9.80%.

Further evidence of the decrease in capital costs in found in the national average return on equity authorized by state utility commissions. As the following graph indicates, the authorized return on equity has been decreasing steadily since 1986.

NATIONAL AVERAGE AUTHORITY RETURN ON EQUITY



Source: Exhibit 510, Gorman Direct, Schedule MPG-10

Interestingly, Ameren's own witness admits that Ameren's cost of capital has decreased since the last case. Having now testified in three Ameren cases, Hevert has steadily reduced his return on equity recommendation from 10.70% in 2011 to 10.40% in the current case.[75]

Thus, by any measure, whether utility bond yields, the average authorized return on equity, or Ameren's own witness, cost of capital has declined since the last case. That said, Ameren's witness insists that the Commission should increase Ameren's return on

[74] Exhibit 510, Gorman Direct, Schedule MPG-10.
[75] Tr. 1119-1120.

equity by 60 basis points from 9.80% to 10.40%. Such a recommendation is not surprising. The Commission has repeatedly found that Mr. Hevert's recommendations are "too high" by an average of 83 basis points.

In contrast, Mr. Gorman's recommendation recognizes the continuing decline in utility capital costs. Specifically, Mr. Gorman recommends that the Commission reduce Ameren's authorized return on equity from 9.80% to 9.25%. Such a return decision is consistent with the declining cost of capital and the evidence in this case. As such, MECG recommends that the Commission find that a 9.25% return on equity is reasonable.

VI. CLASS COST OF SERVICE / REVENUE ALLOCATION / RATE DESIGN

In this Section, MECG will address issues 19A, B, C, G, H and I. Issues 19A, B, G, H and I all concern the proper methodology for conducting a class cost of service study. Specifically, through its decision on these issues, the Commission will provide guidance to the parties on the appropriate approach to allocating: (1) generation fixed costs (issue 19A); (2) non-fuel, non-labor components of production O&M expense (issue 19B); (3) off-system sales revenues (issue 19G); (4) income tax expense (issue 19H) and (5) fuel and purchased power costs (issue 19I) between the various customer classes. In regards to several of these issues, the Commission can take guidance from its previous decision in the 2010 Ameren case.

While the answers to these various allocation issues may have some impact on the results of the various class cost of service studies, the conclusions reached by those studies will not change. Specifically, responsive to issue 19C, each of the class cost of service studies reach the same general conclusions: (1) that residential and LTS (Noranda) rates are not recovering the cost for Ameren to serve those customer classes and (2) Large General Service / Small Primary ("LGS / SP") rates are significantly above their actual cost of service. As such, it is unquestioned that there is a significant subsidy that flows from the LGS / SP customers to both Noranda and the residential customers. The evidence demonstrates that, not only is this subsidy significant, it has existed for several years. Bottom line and most important for the Commission's consideration, no matter the decision on the various individual allocation issues, there is no question that the residential class needs to be allocated a greater share of the authorized Ameren rate increase. Similarly, while considered in the context of Issue 31, the class cost of service

studies, even that sponsored by Noranda's own witness, indicates that Noranda should be allocated a greater share of any Ameren authorized increase.

A. ISSUE 19A: WHAT METHODOLOGY SHOULD THE COMMISSION USE TO ALLOCATE GENERATION FIXED COSTS AMONG CUSTOMER CLASSES?

Position: The Commission should utilize the Average & Excess (4 NCP) methodology to allocate generation fixed costs among the customer classes.

1. Introduction

In general, utilities incur three categories of costs: (1) customer-related costs: the "minimum costs necessary to just make electric service available to the customer" (i.e., meter reading, billing, postage and customer service expenses);[76] (2) energy-related costs: the costs "related directly to the customer's consumption of electrical energy" (i.e., fuel, fuel handling, and interchange power costs);[77] and (3) demand-related costs: "rate base investment and related operating expenses associated with the facilities necessary to supply a customer's service requirements during periods of maximum, or peak, levels of power consumption each month."[78]

It is well established that the electric industry is very capital intensive. The evidence indicates that Ameren has invested almost $14.9 billion in its various production, transmission and distribution facilities.[79] "The Company's net investment in fixed production assets represents approximately 72% of net original cost rate base in this

[76] Exhibit 7, Davis Direct, page 7.
[77] *Id.* at page 8.
[78] *Id.*
[79] Exhibit 300, Accounting Schedules, Accounting Schedule 3, page 5.

case."[80] As such, the most significant issue underlying any class cost of service study concerns the method by which these generation fixed costs are allocated to the various customer classes.

While there are different methods that are utilized for allocating generation fixed costs, the difference in these methodologies generally concern the degree to the methodology considers generation plant to be an energy-related cost (focused on class energy usage) as opposed to a demand-related cost (focused on class peak demand).

The evidence indicates that production plant is both an energy and demand related cost. In fact, the evidence indicates that the need to meet both class energy needs and peak demand drives the utility decision as to the amount of capacity the utility must add as well as the type of capacity added.

> Generally, system peak demands and, to a somewhat lesser extent, excess customer demands, are the motivating factors which influence the amount of capacity the Company must add to its generation system to provide for its customers' maximum demands. However, the type of capacity (base, intermediate, or peaking) that the Company must add is not dictated by maximum customer demand alone, but also by the annual energy, or kilowatt-hours, that will be required to be generated by such capacity, i.e., the generation unit's utilization factor.[81]

2. Average & Excess Production Allocator

Recognizing that both class peak demand and energy usage are important to the utility's decision as to the amount and type of capacity to be added, both Ameren[82] and MIEC[83] rely upon the Average & Excess ("A&E") production allocator methodology.

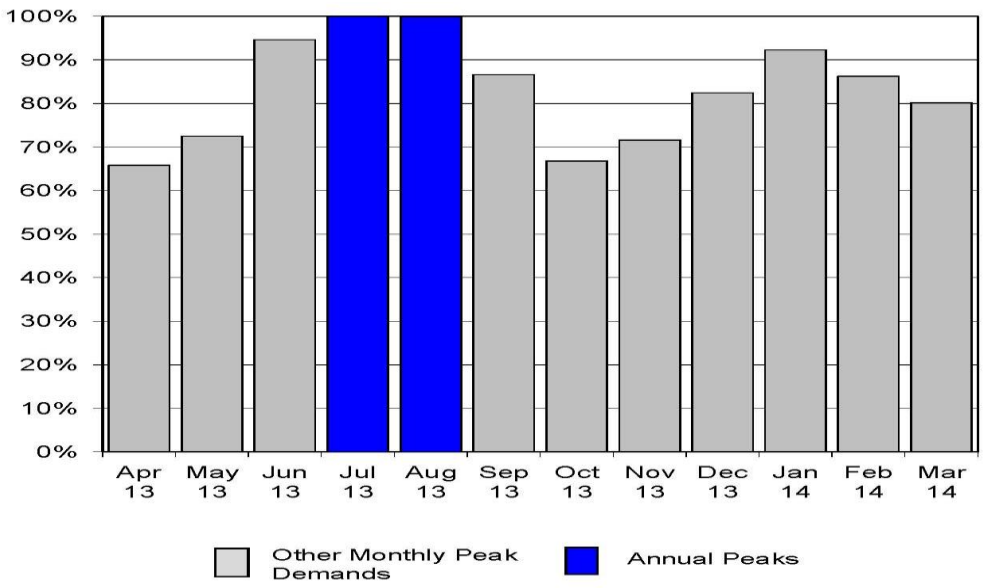
[80] Exhibit 50, Amended Warwick Rebuttal, page 7.
[81] Exhibit 7, Davis Direct, pages 10-11.
[82] *Id.* at page 11. See also, Exhibit 49, Warwick Direct, page 6.
[83] Exhibit 503, Brubaker Direct, page 27.

As Mr. Brubaker points out, the A&E methodology relies upon both class energy and peak demand in its calculation of a production allocator.

> As the name implies, A&E makes a conceptual split of the system into an "average" component and an "excess" component. The "average" demand is simply the total kWh usage divided by the total number of hours in the year. This is the amount of capacity that would be required to produce the energy if it were taken at the same demand rate each hour. The system "excess" demand is the difference between the system peak demand and the system average demand.[84]

Given that the A&E methodology considers both: (1) Average: class energy and (2) Excess: class peak demand, it recognizes both aspects of the utility's capacity addition decision: the amount of capacity to add and the type of capacity to add.

While the class peak demand is a necessary component of the A&E methodology, not all monthly peaks influence the utility's decision to add capacity. Rather, only the largest monthly peaks should be considered. The evidence indicates that, during the test year, Ameren experienced its annual peak demand in July and August.



Source: Exhibit 503, Brubaker Direct, Schedule MEB-COS-1.

[84] *Id.* at pages 25-26.

While Ameren experienced its annual peak demand in July and August, it is not advisable to simply rely on only two months as the system peak demand for calculating the excess component in the A&E methodology. Rather, more months should be considered. "The use of the 4 NCP demand option [of the A&E demand allocation methodology], rather than a lesser number of monthly NCP demands, also prevents the demand allocator for any customer class from being unduly influenced by any extreme demand in a given month."[85] Given this, both Ameren[86] and MIEC[87] relied upon the 4 NCP version of the A&E methodology.[88]

3. OPC's Peak and Average Methodology

In contrast to the logic underlying Ameren and MIEC's use of the A&E production allocator methodology, OPC relied upon a production allocator that is "inherently flawed because it double counts the average demand [energy] of customer classes." Specifically, OPC's "preferred method" is a peak and average methodology ("P&A") methodology.[89]

As the evidence indicates, the average component of both the A&E and P&A methodologies are calculated in the same fashion. In the A&E method, however, the difference between this average usage and the overall system peak is utilized for the excess component. In contrast, the P&A methodology considers all of the system peak for its second component. As Ameren witness Warwick explains:

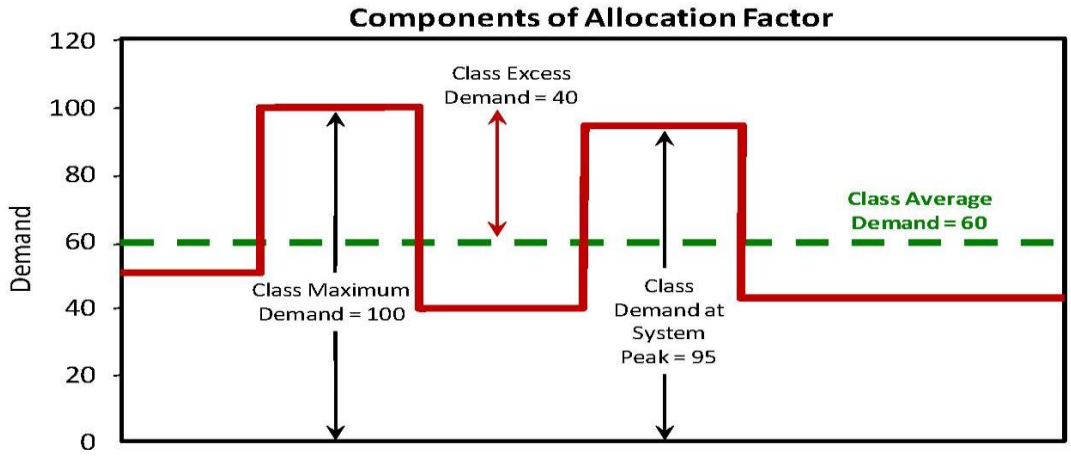
[85] Exhibit 7, Davis Direct, page 11.
[86] Exhibit 50, Warwick Amended Rebuttal, page 5.
[87] *Id.* at page 11. See also, Exhibit 49, Warwick Direct, page 6; Exhibit 503, Brubaker Direct, page 27.
[88] Office of the Public Counsel also presented a 4 NCP version of the A&E production allocator methodology. See, Exhibit 403, Marke Direct, page 26 (lines 1-6). That said, Public Counsel's "preferred method" is a Peak & Average production allocator. See, *Id.* at page 26 (line 8).
[89] Exhibit 403, Marke Direct, page 26.

> The A&E method first allocates production plant investment based on the average demand on the Company's system by the various customer classes. Any excess demand above the average demand is then allocated based on each class' contribution to these excess demands. The P&A method also initially allocates production plant investment to customer classes based on average demand, but ***instead of allocating just the excess average demand to the cost causing classes, the P&A method allocates the entire peak demand to the classes***.[90]

This recognition of the entire peak demand, instead of just the excess, introduces the fatal flaw (class energy usage is double counted) contained in the P&A methodology. As Mr. Warwick concludes, the "P&A method is inherently flawed because it double counts the average demand of customer classes."[91]

> This double counting results from the use of class average demand for a portion of production plant allocation and the use of class peak or non-coincident peak demands, which include an average demand component for the remaining allocation of production plant.[92]

In his rebuttal testimony, Mr. Brubaker agreed with Ameren's description of the flaw inherent in the P&A methodology. In addition, Mr. Brubaker graphically illustrates the differences between the A&E method and the flawed P&A method.



Source: Exhibit 504, Brubaker Rebuttal, page 5.

[90] Exhibit 50, Warwick Amended Rebuttal, page 4 (emphasis added)
[91] *Id.* at page 5.
[92] *Id.*

In this diagram, the maximum demand of this class is 100 MW, its contribution at the time of the system peak is 95, its average demand is 60, and the excess demand is 40.

As Mr. Brubaker explains, "[T]he A&E method combines the class average demand with the class excess demand in order to construct an allocation factor that reflects average use as well as the excess of each class' maximum demand over its average demand. The A&E allocation factor is developed using the average demand (60) and the excess demand (40) for this class."[93]

Unlike the A&E method which combines the average demand with the excess (40), the OPC Peak & Average method "combines the average demand (60) with the class monthly peak demand (100)."[94] Recognizing that "the average peak demand (60) is a component or sub-set of the class peak demand (100) and the class load coincident with the system peak (95)," "the average demand is double-counted."[95]

The practical result of OPC's Peak & Average methodology is to benefit low load factor customers (e.g., residential class) that utilize the Ameren system in an inefficient manner to the detriment of the efficient high load factor customers (e.g., industrial class).

> [T]his double counting causes customers with higher load factors to be allocated an inequitable share of production plant investment. Also, because higher-load factor customers demonstrate a better correlation between average demands and peak demands than do lower-load factor customers, higher-load factor customers receive a disproportionate share of the non-average demand portion of production plant investment under the P&A method.[96]

In its most recent decision regarding the appropriate methodology for allocating production plant, the Commission expressly noted the double-counting of class energy as

[93] Exhibit 504, Brubaker Rebuttal, at page 6.
[94] *Id.*
[95] *Id.*
[96] Exhibit 50, Warwick Amended Rebuttal, page 5.

a flaw inherent in the Peak & Average methodology. As a result, the Commission disregarded this methodology as "unreliable."

> The Peak and Average method, in contrast, initially allocates average costs to each class, but then, instead of allocating just the excess of the peak usage period to the various classes to the cost causing classes, the method reallocates the entire peak usage to the classes that contribute to the peak. Thus, the classes that contribute a large amount to the average usage of the system but add little to the peak, have their average usage allocated to them a second time. ***Thus, the Peak and Average method double counts the average system usage, and for that reason is unreliable***.[97]

4. Staff's Base / Intermediate / Peak Methodology

Similar to OPC, Staff also disregarded the logic inherent in the A&E methodology in favor of its flawed Base / Intermediate / Peak ("BIP") method. Under this methodology, Staff attempts to categorize Ameren's production capacity as either Base, Intermediate or Peaking facilities. The investment in Base facilities is then allocated on the basis of class average demand (energy). The investment in Intermediate facilities is allocated on the basis of the class 12 CP demand, less its previously allocated average demand (energy). Finally, the investment in Peak facilities is allocated on the basis is allocated on the basis of the class 4 CP demand, less the previously allocated base and intermediate components.[98] The evidence, however, demonstrates that Staff's BIP study is inherently flawed.

First, as Mr. Brubaker points out, the BIP methodology is not widely accepted. "The BIP method first surfaced circa 1980 as an approach that some thought might be

[97] Case No. ER-2010-0036, *Report and Order*, issued May 28, 2010, at page 85.
[98] Exhibit 201, Staff's Class Cost of Service / Rate Design Report, pages 14-15. Staff also developed an Alternative Market-Based Study and a Modified-BIP study for purposes of assessing the reasonableness of the results of its detailed BIP study. Exhibit 201, Staff's Class Cost of Service / Rate Design Report, page 34. See also, Exhibit 50, Warwick Amended Rebuttal, page 3.

useful when trying to develop time-differentiated rates. However, the BIP method never caught on and is only infrequently seen in regulatory proceedings. The BIP method is certainly not among the frequently used mainstream cost allocation methodologies, and lacks precedent for its use."[99]

Second, Staff's BIP method falsely assumes that all base load plant investment is utilized simply for providing energy. Implicit in this assumption is the mistaken belief that base load investment does not provide any capacity value.

> By choosing to allocate 100% of the investment (fixed costs) associated with base load plants essentially on the basis of class energy, Staff is effectively assuming that investment in base load plants is not caused by demands and that these plants don't have a capacity cost. These are assumptions that we all know are false. All plants have a capacity cost, and provide capacity value as well as supplying energy. . . All plants contribute to meeting peak demands, and the failure to allocate the fixed costs associated with base load plants on a measure of peak demand produces a biased result that over-allocates costs to high load factor customers and under-allocates costs to low load factor customers.[100]

Third, the Staff's BIP is flawed in that it categorizes an excessive amount of Ameren's generation as base load. Specifically, Staff's calculation of the amount of Ameren's production plant investment that is associated with base load generation is contrary to the accepted definition of base load generation ("it is generally regarded that in the BIP method the base load should be considered that load which is present at all times)."[101] In its analysis, Staff has assumed that 4,500 MWs of Ameren's capacity is base load and allocated the underlying investment on the basis of average demand (energy). According to Staff's methodology then, one would expect to see at least 4,500 MWs of demand "present at all times." Reality indicates, however, that Ameren's retail

[99] Exhibit 504, Brubaker Rebuttal, page 15.
[100] *Id.* at pages 15 and 16.
[101] *Id.* at page 18 (emphasis added).

load was less than 4,500 MWs in 57% of the hours in the test year.[102] Thus, there is a disconnection between reality (Ameren's operational history) and theory (Staff's classification of base load generation). As Mr. Brubaker points out, "[o]bviously, the amount of capacity Staff has identified as base load is much higher than the capacity required to serve the load at all times. This skews the costs into the base load category and, since it is allocated on energy, the result is an over-allocation of costs to high load factor customers."[103]

Fourth, Staff's BIP methodology departs from reality again in that it assumes that intermediate plant should have a lower capacity cost than base load plant. When Staff implements its BIP method, Ameren's Sioux units are categorized in the intermediate category. As such, under the BIP theory, these units should have a lower capacity cost than base load units. As Mr. Brubaker points out, however, "[w]hen Staff calculated the costs per kW of the Sioux units, the result was that the Sioux units have a higher capacity cost per kW than the base load units."[104]

Much like the OPC's Peak and Average methodology, the Staff's BIP methodology has been demonstrated to be flawed. As such, the Commission should disregard this methodology for purposes of allocation fixed production costs. Instead, as the following section demonstrates, the Commission should continue to utilize the A&E methodology for allocating fixed production plant costs.

[102] *Id.*
[103] *Id.*
[104] *Id.* at page 19.

5. Previous Commission Decision

As previously indicated, in its 2010 Ameren decision, the Commission expressly found that the Peak & Average methodology, advocated by Public Counsel, was "unreliable." In that same decision, the Commission relied upon the A&E method for allocating production plant.[105] While this Commission is not bound by that 2010 decision, there are important policy reasons for the Commission to maintain its reliance on the A&E methodology.

> It would be desirable to continue use of the A&E 4 NCP method in this case as well because there has been no material change in the Company's load characteristics, the relative short time period between cases, and also because such consistency affords all parties the ability to rely upon a standardized method whose results can be reasonably predicted. These considerations promote CCOSS stability in that they contributed to the prevention of material case-to-case swings in class revenue responsibility for the most significant portion of the Company's investment in rate base.

For this reason, as well as recognizing the flaws inherent in the methods advanced by OPC and Staff, the Commission should again adopt the A&E methodology as recommended by both Ameren and MIEC.

B. (ISSUE 19B): HOW SHOULD THE NON-FUEL, NON-LABOR COMPONENTS OF PRODUCTION, OPERATION AND MAINTENANCE EXPENSE BE CLASSIFIED AND ALLOCATED?

Position: The Commission should allocate the non-fuel, non-labor component of production O&M expense using the same A&E 4 NCP production allocator.

[105] Exhibit 50, Amended Warwick Rebuttal, page 7.

This issue concerns the method by which non-labor production operation and maintenance costs should be allocated.[106] On this point, Ameren finds itself standing alone. As Ameren recognizes, "Staff, MIEC and OPC categorized all production non-fuel O&M expenses as fixed, and then allocated those costs based on each party's respective fixed production plant allocator."[107] In this way, if adopted by the Commission in response to issue 19A above, all production non-fuel, non-labor O&M costs will be allocated using the A&E methodology. As both MIEC and OPC witnesses point out, O&M expenses "associated with a particular type of plant should be allocated in the same way as the corresponding plant."[108] In other words, "expenses follow plant."[109]

While Ameren agrees that non-fuel labor production O&M costs should be allocated using its fixed production allocator (the A&E methodology),[110] it believes that the non-fuel, non-labor piece should be classified as either fixed (allocated via the A&E methodology) or variable (allocated using the energy allocator).[111] As Ameren then notes, the energy allocator should be applied to those costs that are variable and "relate directly to the customer's consumption of electrical energy."[112] Ameren's attempt to classify certain non-fuel, non-labor costs as variable and allocate those costs using the energy allocator, however, is illogical. As Mr. Brubaker points out, "the vast majority of these costs do not vary in an appreciable way with the number of kilowatthours

[106] Exhibit 503, Brubaker Direct, page 32.
[107] Exhibit 50, Amended Warwick Rebuttal, page 8.
[108] Exhibit 403, Marke Direct, page 29.
[109] *Id.* See also, Exhibit 503, Brubaker Direct, page 33.
[110] *Id.* at page 8.
[111] *Id.* at pages 8-9.
[112] Exhibit 7, Davis Direct, page 8.

generated, but occur primarily as a function of the existence of these plants, the hours or operation and the passage of time."[113]

Further, since these are O&M costs, they are largely maintenance costs. As Mr. Brubaker correctly points out, the maintenance on Ameren's production units is not scheduled based upon the number of kilowatt hours generated by the unit (i.e., on a variable basis). Rather, this maintenance is scheduled based simply on the passage of time.[114] Since these maintenance costs are not dependent on the amount of energy generated at the facility, it is inappropriate to allocate these costs on the basis of energy.

C. (ISSUE 19G): WHAT METHODOLOGY SHOULD THE COMMISSION USE TO ALLOCATE OFF-SYSTEM SALES REVENUES AMONG CUSTOMER CLASSES?

Position: The Commission should allocate off-system sales margins using the energy allocator.

In its 2010 Ameren decision, the Commission considered the issue regarding the allocation of off-system sales revenues. In that case, the Commission expressly stated that these revenues should be allocated among the customer classes on the basis of the energy allocator. "The Commission finds that AmerenUE's class cost of service study, modified to allocate revenues from off-system sales on the basis of class energy requirements, is the most reliable of the submitted studies."[115] The Commission's decision to use the energy allocator for purposes of allocating off-system sales among classes mirrored its previous decision to use the energy allocator for purposes of

[113] Exhibit 503, Brubaker Direct, page 33.
[114] *Id.* at page 33.
[115] Case No. ER-2010-0036, *Report and Order*, issued May 28, 2010, at page 87.

allocating off-system sales among jurisdictions. In its 2006 KCPL rate case, the Commission held:

> The only costs assigned to non-firm off-system sales is the fuel and purchased power costs – the variable costs – hence the appropriateness of using the energy allocator. This is consistent with the way KCPL itself allocates the costs relating to the energy portion of firm capacity contracts – using the energy allocator. The reason is simple – the energy allocator is used to allocate variable costs of fuel and purchased power costs relating to retail sales. ***Using the same rationale, the energy allocator is equally appropriate to use as the allocation factor for both energy of firm (as KCPL does) and non-firm off-system sales***.[116]

Despite the clarity of these previous Commission decisions, Public Counsel recommends that wholesale revenues, not simply margins, be allocated using the production demand allocator (in this case OPC's flawed Peak & Average methodology).[117]

As Mr. Brubaker points out, OPC's position is not only contrary to the previously cited Commission decisions, but is also internally inconsistent. Specifically, while OPC recommends that the wholesale revenues (not just margins) be allocated on the basis of its recommended production allocator, OPC has allocated the entirety of the costs supporting these transactions on the basis of the energy allocator.[118] Thus, revenues and costs for the same transaction are allocated differently.

The impact of OPC's disconnected recommendation is, not surprisingly, beneficial to low-load factor residential customers and detrimental to high-load factor commercial and industrial customers. "By allocating the costs on a kWh basis, and then

[116] Case No. ER-2006-0314, *Report and Order*, issued December 21, 2006, at page 39 (emphasis added).
[117] Exhibit 405, Marke Surrebuttal, page 7.
[118] Exhibit 504, Brubaker Rebuttal, page 8.

crediting the revenues which cover the fuel cost back on a demand basis, [OPC] has materially over-allocated costs to high load factor customer classes."[119]

In this case, this Commission should adopt the logic that previous Commissions have utilized. Specifically, the Commission should recognize that the entirety of the costs underlying wholesale transactions (fuel expense) are incurred on a variable basis and allocated on the basis of the energy allocator. For this reason, the off-system revenues which cover these costs should also be allocated on the basis of the energy allocator.

D. (ISSUE 19H): WHAT METHODOLOGY SHOULD THE COMMISSION USE TO ALLOCATE INCOME TAX EXPENSES AMONG CUSTOMER CLASSES?

Position: The Commission should allocate income tax expense based upon the income tax obligation of the specific class.

The primary issue concerning the allocation of income tax expense is whether that expense should be allocated on the basis of: (1) each class' portion of the overall Ameren rate base (as recommended by Ameren) or (2) income tax obligation of each customer class as a function of its taxable income (as recommended by MIEC).

As Mr. Brubaker points out, Ameren's proposal that income tax expense be allocated on the basis of class rate base "assumes that each customer class is producing the system average rate of return."[120] As each of the class cost of service studies show, however, the customer classes are not producing the same average rates of return. Given

[119] *Id.* at page 9.
[120] Exhibit 503, Brubaker Direct, page 31.

this, Ameren's allocation methodology has the "effect of over-allocating income taxes to classes whose rates of return are below average, and under-allocating income taxes to classes whose rates of return are above average." Certainly such a methodology does not allocate the income tax costs to the class that is causing the cost.

Given the flaw in Ameren's methodology for allocating income tax costs, Mr. Brubaker instead proposes to allocate these costs by "calculating income taxes separately for each customer class."[121] As such, income tax expense is allocated based upon each class' "taxable income."[122]

E. (ISSUE 19I): WHAT METHODOLOGY SHOULD THE COMMISSION USE TO ALLOCATE FUEL AND PURCHASED POWER COSTS AMONG CUSTOMER CLASSES?

Position: In the event that the Commission adopts Public Counsel's Peak & Average production allocator, it should also allocate a below average amount of fuel costs to high load factor customers in order to account for the larger amount of base load units allocated to these high load factor customers.

In this case, every class cost of service proponent chose to allocate fuel and purchased power costs based upon each class' relative energy usage. Given this, it is difficult to understand why the allocation of fuel and purchased power is an issue. The issue arises as a result of OPC's proposal to utilize the Peak & Average methodology. Under this allocation methodology, high load factor customers are allocated a

[121] *Id.*
[122] *Id.*

disproportionate amount of the production capital costs.[123] If these efficient customers are to be allocated a higher share of the base load capital costs, they should also be allocated a greater share of the cheap energy costs used by those base load units. In contrast, the less efficient rate classes (i.e., residential) should be allocated a greater share of the expensive energy costs for the intermediate and peaking units. Given this, Mr. Brubaker proposes that, if the Commission adopts Public Counsel's Peak & Average production allocator, it should allocate lesser fuel costs to these high load factor customers.

> Given these allocations of capital costs, it would not be appropriate to use the same fuel costs for all classes. Rather, the fuel cost allocation should recognize that the higher load factor classes should receive below average fuel costs to correspond to the above-average capital costs (similar to base load units) allocated to them, and the lower load factor classes should get an allocation of fuel costs that is above the average, corresponding to the lower than average capital costs (i.e., peaking units) allocated to them.[124]

Effectively, Mr. Brubaker is stating that, through the Peak & Average methodology, high load factor customers are being allocated a disproportionately large amount of Ameren's high capital cost base load generation. Similarly, the low load factor customers are being allocated a disproportionately large amount of Ameren's low capital cost peaking generation. In this situation, the Commission should also find that the high low factor customers should get the benefit of the low fuel costs that corresponds with the base load capital allocated to them. Similarly, the low load factor customers should receive the high fuel costs that are associated with the peaking units allocated to them. It is inequitable to expect high load factor customers to pay high capital costs, but then not receive the lower fuel costs that are associated with those generating units.

[123] Exhibit 504, Brubaker Rebuttal, page 10.
[124] *Id.* at pages 12-13.

F. (ISSUE 19C): HOW SHOULD ANY RATE INCREASE BE COLLECTED FROM THE SEVERAL CUSTOMER CLASSES?

Position: The Commission should take affirmative steps to recognize and eliminate the the subsidy built into LGS / SP rates for the benefit of residential customers.

In this case, the class cost of service studies reach three largely undeniable conclusions: (1) except for the faulty OPC P&A allocation study, residential rates do not cover Ameren's cost of service; (2) under each of the studies, LTS (Noranda) rates do not cover cost of service; and (3) under each of the studies, LGS / SP rates are significantly above cost of service. As such, there is a subsidy that currently flows from LGS / SP rates to the benefit of Noranda and residential customers. While the Commission's decision on the previous five allocation issues will have some effect on the magnitude of this subsidy, these conclusions are undisputed and cry for Commission attention.

	MIEC[125]	*Ameren*[126]	*Staff*[127]	*OPC 2*[128]	*OPC 1*[129]
(in thousands)	(A&E)	(A&E)	(BIP)	(A&E)	(P&A)
Residential	$68,761	$62,576	$36,029	$41,864	($3,336)
SGS	($12,585)	($13,391)	($12,494)	$1,007	($7,076)
LGS / SP	($61,912)	($59,886)	($39,129)	($48,159)	($38,338)
LP	(934)	1,030	($1,566)	$4,054	$20,793
LTS	6,674	9,830	$17,021	$10,254	$40,824
Lighting	(3)	(158)	$137	($9,019)	($12,867)

[125] Exhibit 977
[126] Exhibit 976
[127] Exhibit 978
[128] Exhibit 403 (Attachment GM-4)
[129] Exhibit 403 (Attachment GM-3)

The conclusions that can be reached in this case are not a temporary condition. Rather, the evidence clearly indicates that residential customers have been benefitting from below cost rates and enjoying the subsidy from LGS / SP customers for at least a decade. In fact, using the Commission's preferred A&E approach reflected in the Ameren and MIEC studies, it is easy to conclude that this subsidy is significant and long-standing.

	Ameren		***MIEC***	
	Residential	LGS / SP	Residential	LGS / SP
ER-2007-0002	$70,206	($51,589)	$119,916	($71,989)
ER-2008-0318	$61,693	($47,863)	$144,475	($83,041)
ER-2010-0036	$78,070	($64,785)	$129,625	($84,603)
ER-2011-0028	$75,995	($63,653)	$106,064	($74,281)
ER-2012-0166	$91,639	($59.931)	$101,034	($63,349)
ER-2014-0258	$62,576	($59,886)	$68,761	($61,912)

Source: Ameren results: Exhibits 971-976
MIEC results: Exhibit 977

Given the significant and long-standing nature of the current residential subsidy, MECG asks the Commission to take definitive steps to address the long suffering LGS / SP customers. Specifically, MECG echoes the recommendation of Walmart and asks that the Commission "apply a 25% revenue neutral movement towards cost of service."[130] After making this revenue neutral movement, any rate increase authorized in this case should be applied to all classes on an equal percentage basis.[131]

[130] Exhibit 750, Chriss Direct, page 9.
[131] *Id.* at page 10.

Such a step would be a definite step towards cost of service, while still recognizing the often-cited consideration of gradualism. In fact, by making a 25% movement, it would take at least three more cases to eliminate the current subsidy. Given that Ameren has averaged a case every 18 months, the current subsidy would continue for at least 5 more years.

A Commission decision to address the current LGS / SP rates that are significantly above cost of service is also dictated by the Commission's stated goal of advancing economic development. In this case, the Commission issued an order asking the parties to address certain economic development goals.[132] Recognizing this goal, it appears illogical for the Commission to preserve rates for business that are above cost of service. Certainly, the first step in any economic development endeavor should be to ensure that business customers are only paying rates that reflect their cost of service and nothing more.

With this in mind, certain conclusions within a recent settlement are shown to be unreasonable. Several parties (Office of the Public Counsel[133], MIEC, Noranda, Missouri Retailers Association and Consumers Council of Missouri) filed a Non-Unanimous Stipulation and Agreement which they entitled *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*.[134] While that settlement nominally claims to address economic development, it is apparent that such a notation is a fallacy. Specifically, the settlement,

[132] See, *Order Directing Consideration of a Certain Rate Design Question*, issued October 20, 2014, at page 2, paragraph 8.
[133] Interestingly, Office of the Public Counsel claims to represent all Ameren customer classes. While making this claim and despite its own evidence recognizing the existence of current residential subsidy, Public Counsel clings to this subsidy and asks that the Commission not take any action to address this subsidy. (Exhibit 403, Marke Direct, page 31).
[134] Filed March 10, 2015.

by recommending an equal percent, across-the-board increase, seeks to preserve the current residential subsidy and the inflated rates currently being paid by the LGS / SP customers.[135] As such, the non-unanimous settlement implicitly undermines the very economic development that it nominally claims to foster. In actuality, given its lack of focus on any other customer class, the settlement is simply concerned with economic development for a single customer, a customer already paying rates that are below cost of service – Noranda Aluminum. MECG asks that the Commission reject all of the terms of the Non-Unanimous Stipulation and instead take steps that foster economic development by moving the LGS / SP rates towards class cost of service.

[135] See, *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, page 2, paragraph 3.

VII. NORANDA RATE PROPOSAL

Position: The evidence indicates that Noranda is not suffering from a liquidity crisis. In fact, given its own definition, Noranda had the same amount of liquidity when the Commission considered Ameren's last rate increase. Despite the same amount of liquidity, Noranda agreed to an equal-percent, across-the-board rate increase in that case. Similarly, the lack of a liquidity crisis is reflected in the vastly different public statements that Noranda has made to its investors as opposed to the confidential statements that Noranda has made to the Commission.

The evidence further indicates that, under Noranda's original proposal or under the Non-Unanimous Stipulation, customers would be better off if Noranda simply closed. Under Noranda's best case scenario, which relies upon faulty historical evidence, there is a minimal difference between: (1) the increased amount that ratepayers would pay under either Noranda's original proposal or the Non-Unanimous Stipulation and Agreement and (2) the increased amount that ratepayers would pay if Noranda simply closed. As Mr. Brubaker admits, however, his analysis is based entirely on current rates and does not consider the additional amount that ratepayers will suffer from absorbing any rate increase that would otherwise be allocated to Noranda. Furthermore, Brubaker's analysis is based upon the assumption of normal weather during the entire length of any Noranda subsidy rate commitment. As the Commission has previously found, weather anomalies, like the polar vortex, will occur in the future and will have an impact on prices.

The better evidence, which includes a forecast of future revenues that Ameren ratepayers could realize from Ameren selling the Noranda load in the wholesale market definitively shows that customers are $272 million worse off under Noranda's original

proposal than if Noranda simply ceased operations. Even more egregious, under the 10-year proposal contained in the Non-Unanimous Stipulation, ratepayers are $550 million worse off than if Noranda closed its doors.

Given Noranda's current liquidity, the questionable nature of its threats to close the New Madrid smelter and the fact that Ameren ratepayers would be better off it Noranda simply discontinued operations, MECG urges the Commission to reject any special Noranda rate proposal. Instead, MECG asserts that the Commission should continue to be guided by the various class cost of service studies presented in this case. Recognizing that all of those studies, including Noranda's own study, indicate that Noranda is currently paying rates that are well below cost of service, MECG recommends that the Commission authorize a rate increase to the LTS class (Noranda) which is above the system average increase authorized to Ameren.

A. (ISSUE 31A): IS NORANDA EXPERIENCING A LIQUIDITY CRISIS?

1. Stable Liquidity Position:

As the basis for its request for a reduced electric rate, Noranda claims to be suffering from a liquidity crisis. Specifically, Noranda claims that "[b]ecause of seasonality across the year and the timing of cash receipts and expenditures across any particular month, we believe **_____** is the minimum liquidity necessary to have sufficient cash for uninterrupted operations."[136] Noranda then concludes that, absent an electric rate reduction, "the [New Madrid] Smelter is not viable and, therefore,

[136] Exhibit 600, Boyles Direct, page 7. Under cross-examination, however, Boyles admitted that there was nothing statistically or mathematically important about this figure. HC Tr. Page 2557.

at substantial risk of imminent closure."[137] The evidence in this case, however, is contrary to Noranda's claims of doom and gloom.

During the hearing, evidence was elicited regarding Noranda's historical liquidity position. Using Noranda's definition of liquidity ("cash we have on hand and the cash to which we have access through our revolving credit agreement"),[138] Noranda has consistently stayed above its **_____** minimum liquidity target.

	Cash	Revolving Credit	Total Liquidity
4Q2014	$25.3 million	$137.8 million	$158.3 million
3Q2014	$24.3 million	$159.2 million	$183.5 million
2Q2014	$32.9 million	$146.4 million	$179.3 million
1Q2014	$51.2 million	$139.9 million	$191.1 million
4Q2013	$79.4 million	$117.0 million	$196.4 million
3Q2013	$63.9 million	$120.0 million	$183.9 million
2Q2013	$58.8 million	$143.1 million	$200.9 million
1Q2013	$16.1 million	$142.7 million	$158.8 million
4Q2012	$36.1 million	$118.6 million	$154.7 million

Source: Transcript pages 2410-2416.

Clearly, given Noranda's definition of liquidity and its minimum liquidity target, Noranda is not presently facing a liquidity crisis.

Commission Decision in EC-2014-0224:

The conclusion that Noranda is not suffering from a liquidity crisis, is consistent with that recently made by a unanimous Commission. In its Report and Order in Case No. EC-2014-0224, the Commission also considered Noranda's claims that it faced a

[137] *Id.* at page 2.
[138] *Id.* at page 7.

liquidity crisis. In that decision, the Commission held that "the Complainants [Noranda] have not met their burden in that they have not shown Noranda is suffering from a liquidity crisis."[139]

In support of its conclusion in that case, the Commission relied upon several facts that contradicted Noranda's claim of a liquidity crisis.

> On February 19, one week after Noranda filed its direct testimony in this case, Noranda reported to its investors that as of the end of 2013, it had a total liquidity of $196 million, representing $117 million available borrowing capacity under a revolving credit facility plus $79 million in cash. At that time, Smith, speaking to investors at an earnings conference call, reported that "***today we have a healthy balance sheet and a solid liquidity position***."[140]

Still again, the Commission noted Noranda's recent public claims of healthy finances from the following quarter.

> At the end of the first quarter of 2014, Noranda reported to its investors that it had a total liquidity of $191 million, representing $140 million of available borrowing capacity plus $51 million cash. At that time, Dale Boyles, CFO of Noranda, told investors "***We believe our flexible capital structure, combined with our focus on managing controllable costs and working capital, provides us with a solid foundation as we work through the headwinds presented by this portion of the commodity cycle***.[141]

Noranda Public Statements Since EC-2014-0224:

While, Noranda's liquidity position has decreased slightly ($183.5 million to $158.3 million) since the time that the Commission issued its decision in EC-2014-0224, the evidence indicates that this decline is temporary and easily explained by capital investments in the new rod mill and its production line.

[139] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at page 25.
[140] *Id.* at pages 7-8 (emphasis added).
[141] *Id.* at page 8 (emphasis added).

> Importantly, this relative trough in liquidity at year end 2014 is due to transitory factors. As Mr. Boyles points out, a key driver is capital outlays for the rod mill project at New Madrid, with project financing deferred until 2015. Also, as Mr. Boyles notes for 2014, "our operating results have been negatively impacted by an unusually high concentration of failures in reduction cells, or pots, in which the electrolysis process occurs."[142]

Not only has Noranda's liquidity position remained stable since the Commission issued its decision in EC-2014-0224, Noranda's statements to the investing public regarding its "healthy balance sheet", "solid liquidity position" and "solid [financial] foundation" has also continued.

Specifically, since the Commission issued its decision on August 20, 2014, Noranda has released two quarters of financial results and held two earnings calls with investors. In each of those calls, Noranda portrays the financial picture of a company that is markedly different from the one it portrays for the Commission. For instance, following the third quarter of 2014, Noranda held its investor call. During that call, Noranda discussed certain slides that it had previously provided to investors. The discussion and the slides portray a healthy company.

> First, we are pleased to report third-quarter 2014 results that reflect sequential and year-over-year improvement in our operating units. This improvement was largely the result of stable aluminum product demand and better aluminum prices. . . . The average realized Midwest transaction price for primary aluminum was $1.08 per pound in the third quarter of 2014. That's $0.16 more than the third-quarter 2013, and $0.09 higher than second-quarter 2014. . . . Finally, although our total liquidity increased by $5 million during the quarter, we did consumer $9 million of cash.[143]

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[142] Exhibit 33, Mudge Rebuttal, pages 8-9. See also, Exhibit 72, page 3 (including cover page). "In August, we began to experience a concentration of failures for the pots that were replaced following the January 2009 ice storm. We are reallocating resources within the plan to increase the pace of our pot rebuilding activities, and we expect this issue to be largely behind us in the first part of 2015." (emphasis added).

[143] Exhibit 72 (pages 2 and 3 including cover page). See also, Exhibit 71, slide 3.

Noranda's statements extended beyond historical financial results, but also extended to discussion regarding improved future demand for aluminum.

> CRU forecasts 4% to 5% compound annual growth rates for primary aluminum consumption in the US through 2019, CRU's outlook also indicates solid growth for the key product segments in which we participate.[144]

Noranda's statements indicate its belief that this increased domestic demand would drive increased prices for aluminum.

> US aluminum demand supports improved LME aluminum prices and Midwest premiums, which is a good segue to the discussion on slide 6. Based on improved supply / demand fundamentals, favorable aluminum price volatility during the second half of 2014 has been encouraging.[145]

Noranda held another earnings call on February 18, 2015 to release earnings for fourth quarter of 2014. The statements made during that call and the slides continue to paint a much rosier picture than that set forth to the Commission in this case.

> For the quarter, we reported earnings excluding special items of $0.14 per share. This is an improvement from the $0.15 per share loss in fourth quarter last year and the $0.04 loss from the third quarter of 2014. . . . Total segment profit was $50 million in the fourth 2014. This is an improvement over the $21 million of total segment profit we reported in fourth-quarter 2013. It's also a sequential improvement over the $37 million of total segment profit we reported last year. . . . Slide four summarizes what we feel a favorable growth outlook for a primary aluminum consumption in United States. Besides driving our own order book, we believe strong demand is the key fundamental driver of sustainable all-in aluminum prices over the medium and long-term.[146]

Noranda's most recent statements to the public, as contained in that investor call, remain those of a "strong" industry and company.

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[144] Exhibit 72, page 3, including cover page. See also, Exhibit 71 slide 5 demonstrating demand in certain aluminum segments increasing by as much as 10%.

[145] Exhibit 272, page 4, including cover page. See also, Exhibit 71, slide 6 showing increased demand driving "higher" aluminum prices.

[146] Exhibit 69, page 3, including cover page. See also, Exhibit 70, slides 3 and 4.

> [M]acroeconomic conditions will continue to drive volatility just as they always have. However, in the medium and long-term, we believe aluminum demand fundamentals continued to be strong.[147]

Perhaps, the best evidence of the extreme disconnect between the statements that Noranda makes to the investment community ("strong" industry and company) and those made to the Commission ("substantial risk of imminent closure") is found in the fact that Noranda labeled so much of its information in this case as highly confidential and, therefore, not available to the public and investment community. Specifically, despite its claims that it has been "transparent" with the investing community,[148] Noranda has withheld from the public view, claims that it is **_____ _____**[149] Upon further examination, it became apparent that Noranda has not been "transparent" with the investing community about such a fact. Rather, investors can only **_____** information about this **_____** from its disclosures.[150] Similarly, Noranda has withheld from public view the following statements: **_____ _____**;[151] **_____ _____ _____**;[152] and **_____ _____ _____ _____**[153] Certainly the need for such broad brush use of the high confidential

[147] Exhibit 69, page 3, including cover page. See also, Exhibit 70, page 4 and Transcript pages 2529-2534.
[148] HC Tr. Page 2238.
[149] HC Tr. 2569.
[150] HC Tr. 2569-2570.
[151] HC Tr. 2570.
[152] HC Tr. 2577.
[153] HC Tr. 2578.

designation is not characteristic of a company that has been "transparent" with the public as Noranda now claims.

This difference between Noranda public statements and those made in the context of this case necessarily raises questions about the veracity of Noranda's conclusions regarding the health of the New Madrid smelter. As the Commission previously held, "the Commission believes the financial projections that Noranda has presented to its investors, and to Wall Street in general, cast considerable doubt on the financial projections presented to this Commission."[154] Similar doubts should be present in this case.

Noranda's Actions in Last Rate Case:

Despite continued liquidity above the **_____** minimum liquidity target, improved financial results and expectations for increased demand and "strong" aluminum fundamentals, Noranda still claims that the New Madrid smelter is threatened. The best evidence that Noranda does not face a financial crisis or need rate relief, however, is found in Noranda's actions in Ameren's last rate case when it was in virtually an identical liquidity position.

On February 3, 2012, Ameren filed for a $375.6 million rate increase.[155] On October 10, 2012, several parties executed a Stipulation and Agreement setting forth the manner by which any revenue increase would be allocated to the various customer classes, including Noranda.[156] Pursuant to that Stipulation, Noranda agreed that any rate

[154] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at page 26.
[155] See, Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at page 5.
[156] See, Case No. ER-2012-0166, *Revised Non-Unanimous Stipulation and Agreement Regarding Class Cost of Service and Tariff Issues*, filed October 10, 2012. See also, Exhibit 7, Davis Rebuttal, page 19.

increase would be allocated "as an equal percent of current base rate revenues."[157] Thus, when the Commission issued its Report and Order on December 12, 2012, Noranda was allocated a 10.1% rate increase.[158] Later, when it announced its 4th quarter 2012 financial results, Noranda indicated that its liquidity on December 31, 2012 was $154.7 million.[159]

Today, Noranda's reports liquidity that is slightly higher at $158.3 million.[160] Unlike the last case, however, Noranda now claims that the New Madrid smelter is likely to close absent the Commission reducing its electric rate by 20%.[161] It is certainly contradictory and casts significant doubt on Noranda's claims when one recognizes that, while facing a slightly worse liquidity position in the last case, Noranda agreed to a 10.1% rate increase. Now, when liquidity is slightly better, Noranda claims that it needs a 20% rate decrease.

Noranda's Evidence Of A Liquidity Crisis Is Flawed:

Given that its liquidity positions, public statements and previous actions do not support the notion that it is suffering from a liquidity crisis, Noranda attempts to create the image of a crisis by presenting a "severely flawed" financial model which relies upon self-serving pricing and capital expenditure assumptions. In Case No. EC-2014-0224, against a similar backdrop of strong historical liquidity positions and contradictory statements to investors, Noranda tried to create the same illusion of a liquidity crisis. Relying upon its proprietary financial model and faulty assumptions, Noranda claimed

[157] *Id.* at page 2. See also, Tr. 2646-2647.
[158] Tr. 2647.
[159] Tr. 2416.
[160] Tr. 2410.
[161] Noranda's current rate, including the fuel adjustment clause, is $42.35 / MWh. (Exhibit 503, Brubaker Direct, page 40). Under the Non-Unanimous Stipulation signed, Noranda would receive an electric rate of $34.00 with no exposure to the fuel adjustment clause. Thus, Noranda's rates would be reduced by 19.7%.

that the New Madrid smelter's viability was threatened. By utilizing deflated aluminum prices to reduce projected future revenues, and inflated capital expenditures to increase future costs, Noranda lowered expected liquidity and manufactured a liquidity crisis. The Commission, however, saw through Noranda's manipulations and claims. After criticizing Noranda's "severely flawed" financial model and unrealistic assumptions, the Commission rejected Noranda's claims.

> The financial model that Noranda presented as a basis for its claim for subsidization is severely flawed. By relying on Forward LME prices rather than more realistic forecasts from CRU that take into account a strong fundamental demand for aluminum, Noranda's model understates the likely future price for aluminum. Further, the financial model that Noranda submitted to this Commission assumes that the company will need to make $25 million in additional capital investments that it has not made in the past and that Noranda did not claim a need to make when it described its financial projects to Moody's a few weeks before it filed this complaint.[162]

Relying on the same "severely flawed" model in this case, Noranda nevertheless tries to alleviate the Commission's previously expressed concerns by changing its assumption regarding the future price of aluminum.[163] Specifically, Noranda abandoned its previous reliance on the "Forward LME" price of aluminum.[164] Noranda, however, did not rely on the CRU price forecast as suggested by the Commission. Instead, despite acknowledging the "expert" qualifications of CRU to perform such pricing forecasts;[165] despite admitting that the CRU price forecast provides the "best prediction" of future prices;[166] despite their subscription to CRU data and ready access to such data;[167] and

[162] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, pages 25-26.
[163] Exhibit 33, Mudge Rebuttal, page 13 ("Mr. Boyles appears to be attempting a new approach with regard to expected levels of aluminum pricing.").
[164] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, page 25.
[165] Tr. 2488-2489.
[166] Tr. 2515-2516.
[167] *Id.* at page 2490.

despite the Commission's suggestion in the last case to utilize CRU pricing data,[168] Mr. Boyles instead took the CRU prices and then applied an "arbitrarily derived discount".[169] The evidence in this case, however, reveals that there are a multitude of problems with the approach utilized by Mr. Boyles in calculating this "arbitrarily derived discount."

Despite lack of any training,[170] Mr. Boyles attempted to define an aluminum pricing cycle. Rather than employing any statistical methods to analyze the length of a historical aluminum pricing cycle,[171] Mr. Boyles simply "assumed" a 10 year pricing cycle.[172] While recognizing that the primary point of identifying a pricing cycle is to define a period which contains both peaks and troughs around a pricing average,[173] Mr. Boyles' arbitrarily derived 10-year cycle contains an initial 7 year period of troughs were aluminum prices are assumed to be below average.[174] Interestingly, Mr. Boyles assumption that the initial 7-years of pricing troughs is directly contradicted by CRU's stated forecast that there will be "no significant upward or downward trends" for 2015-2017.[175]

From this arbitrary 10 year period containing an initial 7 years of pricing troughs, Mr. Boyles then calculated his "arbitrarily derived discount" to apply to the CRU price forecast.[176] Clearly, since it does not provide for equal consideration of pricing peaks and

[168] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, page 25.
[169] Exhibit 33, Mudge Rebuttal, page 14.
[170] Prior to commencing employment with Noranda in November of 2013, Mr. Boyles worked for various apparel, automotive trim, gypsum and accounting companies. He readily admits that he has no experience in aluminum price forecasting. (Tr. 2482-2485).
[171] Tr. 2491-2492.
[172] Tr. 2493.
[173] Tr. 2493-2494.
[174] Tr. 2494-2497. See also, Exhibit 19, Humphreys Rebuttal, page 5 and Schedule DH-R1.
[175] Tr. 2501.
[176] Tr. 2513.

since it contradicts CRU's stated forecast of no "downward trends" for 2015-2017, Mr. Boyles' suggested 10-year pricing cycle is arbitrary and self-serving.

The impact of using the deflated aluminum prices caused by Mr. Boyles' "arbitrarily derived discount" is not surprising. Specifically, Noranda anticipates liquidity of **_____** million at the end of the 10 years period using Boyles' discounted aluminum prices. In rebuttal, however, Ameren utilized the same model and simply replaced Boyles' deflated aluminum price with the CRU forecasted aluminum price for the entire 10 year period. The result of that model, using the CRU forecasted aluminum price, is liquidity of **_____** million, an increase of **_____** million in liquidity.[177] As Mr. Mudge notes, Noranda's model using CRU aluminum price forecasts, instead of deflated aluminum prices, indicate that "Noranda could operate with no reduction in electricity costs and still maintain strong liquidity."[178]

As in Case No. EC-2014-0224, Noranda's model suffers from more than a deflated, self-serving aluminum price forecasts; it also suffers from inflated estimates of future capital expenditures. As Mr. Mudge notes, "these [capital expenditure] assumptions depart from historical patterns, have not been featured in Noranda communication to external audiences, and remain in significant part unsubstantiated."[179]

As part of its financial model in this case, Noranda assumed average capital expenditures of approximately **_____**[180] These annual capital expenditures consists of two parts: (1) sustaining capital – required to support daily operations and (2) growth capital – used to implement productivity and

[177] Exhibit 33, Mudge Rebuttal, page 19.
[178] *Id.* at page 20.
[179] *Id.* at page 21.
[180] Exhibit 600, Boyles Direcct, page 9.

improvements.[181] As the evidence indicates, the unspecified nature of certain future sustaining and growth capital expenditures causes concerns that Noranda has inflated capital expenditures in order to deflate future expected liquidity positions.

> In particular, approximately **___** million in growth capital remains unspecified with no discernible impact on production (unlike the rod mill, which clearly changes the Smelter's product mix in the Enterprise model), and remote in time (years 2019-2021). When the same issue arose in Case 0224 and when asked by Ameren Missouri in that case to list and describe its planned capital projects, Noranda responded that it looks only at a detailed listing of capital projects "for the current plan year." Noranda also told Ameren Missouri that it was developing a 5-year capital expenditure plan, and expected to complete it by year end 2014. In this case, Ameren Missouri again asked Noranda for its planned capital expenditures for the next five years. Noranda responded with specific plans for 2015 only. Beyond that, Noranda has provided as a "workpaper" for the Boyles testimony a "hopper" of projects, but the hopper lacks specifics and despite numerous requests Noranda has provided no financial justification for these projects.[182]

The impact of eliminating the undefined growth capital expenditures is to increase Noranda future liquidity positions.[183]

Concerns with Noranda's future estimates of capital expenditures extend beyond the growth capital investments. In addition, concerns have arisen regarding Noranda's alleged sustaining capital investments. Specifically, without any reference in public statements, Noranda now suddenly projects increased sustaining capital investment as a result of past decisions to defer sustaining capital projects.

> It is noteworthy that Noranda has waited until this time to specify its claims about "catch-up" sustaining capital. This represents a large capital outlay in the Enterprise Model - **_____** million. Mr. Boyles argues in his testimony that deferrals of sustaining Capex justify the catch-up spending. However, notwithstanding general references to such deferrals in discovery responses, there is no analytical support for this assertion in Mr. Boyle's workpapers. Sustaining Capex achieved target levels, at

[181] *Id.*
[182] Exhibit 33, Mudge Rebuttal, pages 21-22.
[183] *Id.* at page 22.

> **_____** million, in 2013, and fell at most **___** million below target in 2014. Clearly, Noranda's claim of **_____** million of "catch-up" requires more substantiation.[184]

The important point with regard to Noranda's **____** million estimate for future capital expenditures is that, prior to 2014, **_____ _____**.[185] Despite the lack of historical support for this figure, Noranda now assumes this amount for its future modeling.

In the end, Noranda conducted 11 different modeling scenarios based upon its deflated future aluminum prices and inflated capital expenditure assumptions. Of those 11 scenarios, Noranda presented the 3 sets of results it deemed to be "representative scenarios."[186] In choosing the three "representative scenarios" to provide the Commission, Noranda did not run any type of probability analysis in order to determine whether they were realistic.[187] Instead, Noranda conveniently presented the three scenarios which provided the most negative cash flow outcomes and worst liquidity predictions.[188]

In the final analysis, the Commission should be hesitant to find that Noranda suffers from a liquidity crisis.[189] Noranda's historical and liquidity positions remain well above the minimum liquidity threshold. Additionally, while claiming to be "transparent"

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[184] *Id.* at pages 23-24.
[185] HC Tr page 2561.
[186] Tr. 2511.
[187] Tr. 2512.
[188] Tr. 2513.
[189] As detailed, the overwhelming evidence leads to the conclusion that Noranda does not suffer from a financial crisis. Nevertheless, it should be recognized that, as the Commission previous found, if Noranda does suffer from a liquidity crisis, "these problems are largely self-inflicted." "The former owner of Noranda, and still its principal shareholder, Apollo Management, L.P., took $422.8 million in cash dividends from the company after it acquired the company. Noranda had to borrow to pay the dividends, leaving it with a current debt to equity ratio of 87 percent. Under those circumstances it is not surprising that Noranda has some cash liquidity issues, especially considering the roughly $50 million per year in interest payments Noranda must pay on that debt." Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at page 26.

to the investing community, Noranda's statements to those investors are, at times, either incomplete or misleading. Furthermore, when it faced a slightly worse liquidity position in the last Ameren rate case, Noranda agreed to a 10.1% rate increase. Here, despite a better liquidity position, Noranda claims to need a 20% rate reduction. Finally, Noranda's own evidence, contained within its "severely flawed" financial model, is problematic. Ignoring the aluminum price forecasts provided by the best experts in the world (CRU), Noranda instead present aluminum prices prepared by its untrained financial officer. All of these conclusions lead to a finding that Noranda is not suffering from a financial crisis.

B. NORANDA'S SINGLE-MINDED FOCUS ON COST OF ELECTRICITY IS MISPLACED

Reflecting its own lack of confidence in its misplaced liquidity argument, Noranda trots out another well-worn argument.[190] Specifically, Noranda argues that, since the aluminum industry is a commodity seller and energy intensive, "it is the cost of electricity. . . that most significantly determines whether or not an aluminum smelter is sustainable."[191] Based upon this misplaced premise, Noranda implies that, since its price of electricity is higher than the average cost of electricity for domestic smelters, the New Madrid smelter is necessarily uncompetitive and will close.[192] As this brief demonstrates, however, Noranda's premise and conclusion is misplaced in three important ways.

[190] Noranda has relied on Mr. Fayne's misplaced comparison of smelter cost of electricity in at least four separate cases. See. Tr. 2597.
[191] Exhibit 602, Fayne Direct, page 2.
[192] See, Exhibit 33, Mudge Rebuttal, page 34. ("Mr. Fayne simply allows the impression to exist. In this way, Mr. Fayne again implicitly concedes that a comparison of electricity costs in isolation is incomplete and does not demonstrate the relevant point in determining the likely future success of the New Madrid smelter, which does not depend solely on electricity costs.").

First, it is well established that a smelter's viability is not determined solely by the smelter's cost of electricity. If this were true, every smelter would inevitably be located next to cheap hydroelectric power supplied.[193] Rather, a smelter's viability is determined by the smelter's overall cost of production.[194] In this regard, the New Madrid smelter, even with its current electric rates, is well positioned to compete and thrive.

In his rebuttal testimony, Mr. Mudge undertook an analysis that went beyond the limited analysis provided by Noranda. Specifically, Mr. Mudge provided a comparison of domestic smelters based upon overall production costs, instead of just the cost of electricity. That analysis shows that, even with current electric costs, "New Madrid already operates at the lowest total cost among U.S. smelters."[195]

[193] *Id.* at page 36, footnote 14. ("The Massena West smelter has such cheap power because, as noted in CRU publications, it receives power sourced from a hydroelectric facility owned by a public power authority. Given the very low variable cost of generating hydro power, this public power authority is in a position to offer rates power to Massena West well below the level Ameren could ever be expected to offer to New Madrid.").
[194] *Id.* at page 39.
[195] *Id.* at page 40.

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Source: Exhibit 33, Mudge Rebuttal, page 40.

The reasons underlying New Madrid's lowest total cost are readily apparent. As Mr. Mudge points out (as reflected in the blue bar in the previous graph), "the New Madrid smelter continues to benefit from the cheapest alumina supply in the nation."[196] Furthermore (as demonstrated in the purple bar in the graph), **_____

[196] *Id.* at page 41. See also, Exhibit 533, page 6 ("We believe our combination of captive alumina and bauxite, a secure electric power contract and strategically located assets give us meaningful operational flexibility in our Upstream Business. St. Ann provides a secure source of bauxite to Gramercy. Gramercy provides a strategic supply of alumina to New Madrid at costs below recent spot market prices for alumina. Because our captive alumina and bauxite production capacity exceeds our internal requirements, we also sell these raw materials to third parties. The margin from these sales effectively lowers the cost of our

_____**[197] Finally (as shown in the green bar in the graph), New Madrid "benefitted from labor costs **____** below the U.S. average. Clearly, Noranda's reliance on cost of electricity is incomplete and misleading. The New Madrid smelter already benefits from a total operating cost that is well below the current average for domestic smelters.

Second, Noranda's sole focus on a smelter's cost of electricity as the deciding factor of a smelter's viability has been shown to be patently incorrect. During his first time testifying for Noranda (Case No. ER-2010-0036), Mr. Fayne presented a similar comparison of the cost of electricity for domestic smelters. At that time (2009), Massena East benefitted from the lowest cost of electricity of any domestic smelter.[198] Nevertheless, as Mr. Fayne readily admits, Massena East shut down in 2009.[199] Eventually, Massena East re-opened. Again, despite having the lowest cost of electricity,[200] Massena East again closed.[201] Clearly then, Mr. Fayne's claim, that "[i]n every instance, the smelter shut down because of high power costs"[202], is incorrect.

In his testimony, Mr. Mudge has also provided definitive evidence that contradicts Mr. Fayne's claim that "in every case" smelters shut down because of high power costs. Rather, Mr. Mudge demonstrated that, contrary to Mr. Fayne's claims, smelters closed because its overall cost of production was well above the average for domestic smelters.

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alumina consumed internally and therefore lowers our integrated Net Cash Cost to produce primary aluminum ("Net Cash Cost")).

[197] *Id.*

[198] Exhibit 979.

[199] *Id.* See also, HC Tr. 2719.

[200] Exhibit 602, Fayne Direct, Exhibit HWF-1.

[201] *Id.* "In January 2014, Alcoa announced its plans to permanently shut down the lines at Massena East." See also, HC Tr. 2719.

[202] Exhibit 602, Fayne Direct, page 3.

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Source: Exhibit 33, Mudge Rebuttal, page 43

As this graph shows, each of the last six domestic smelters that closed were suffering from total operating costs that were well above the current average cost of **_____**. In fact, demonstrating the absolute falseness of Mr. Fayne's implications, at the time that it closed, Massena East benefitted from a cost of electricity that was almost **____** below the average cost of electricity for domestic smelters.[203] Yet, Massena East still closed. Similarly, at the time that it closed, Ravenswood benefitted from a cost of electricity that was **__** below the average cost of electricity for domestic smelters.[204] Again, despite this low cost of electricity, Ravenswood also

[203] Exhibit 602, Fayne Direct, Exhibit HWF-1.
[204] Exhibit 979.

closed. Clearly, contrary to Mr. Fayne's conclusion, smelters were closing for a reason other than high electric rates. As Mr. Mudge uncovers, the reason was total cost.

Third, Noranda's focus solely on a smelter's cost of electricity is not accurate unless it also includes some consideration of the risks underlying that cost of electricity. As Mr. Mudge explains, "[e]ach U.S. smelter has a unique power agreement and most of the smelters have agreed to, or have potentially exposed themselves to, additional costs or risk in exchange for lower rates instead of simply obtaining an unconditional supply of lower cost power as Noranda requests here."[205] For instance, while it readily claims that Hawesville and Sebree have a lower cost of electricity,[206] Noranda fails to mention that both smelters bear the risk of high prices that are associated with purchasing electricity as wholesale customers.[207] Thus, while it seeks to lower its cost of electricity below that realized by the Hawesville and Sebree smelters, Noranda is not willing to expose itself to the market risk that comes with being a wholesale customer. Similarly, while it notes that Warrick has a lower cost of electricity,[208] Noranda fails to recognize that Warrick exposed itself to tremendous capital investment[209] and environmental regulations by investing in self-generation.[210] When asked whether Noranda has "explored the option"

[205] Exhibit 33, Mudge Rebuttal, page 37.
[206] Exhibit 602, Fayne Direct, Exhibit HWF-1.
[207] Exhibit 33, Mudge Rebuttal, page 38 ("Since they have elected to source power from the wholesale market, the Hawesville and Sebree smelters are now exposed to the risk of price fluctuations in that market.").
[208] Exhibit 602, Fayne Direct, Exhibit HWF-1.
[209] Tr. 2598. (Mr. Fayne readily admits that the capital investment to self-generate could amount to "billions of dollars.").
[210] Exhibit 33, Mudge Rebuttal, page 38 ("Similarly, Warwick may be significantly threatened in the form of tightening environmental regulation affecting coal resources, as well as plant outages when market electricity must be purchased.).

of self-generation and investing the billions of dollars associated with building such a facility, Mr. Fayne frankly admitted "I would hope not."[211]

Through its comparison Noranda seeks to engage in a classic "cake and eat it too" situation. Specifically, Noranda seeks the benefits of low electric rates that come with self-generation or wholesale market participation, but does not want either the risk exposure that comes with capital investment in self generation or price volatility that comes through participation in the wholesale market.

In the final analysis, it is apparent that the cost of electricity does not define a smelter's ability to compete or its long-term viability. Despite its claims that it suffers from a high cost of electricity, it has been shown that Noranda benefits from the lowest overall cost of production of any domestic smelter. Noranda's lowest overall cost of production is wider than the domestic market and admittedly extends to the global market. In October 2014, Noranda executives met with Standard & Poor's. During that meeting, Noranda provided a presentation that clearly "puts New Madrid in the second lowest quartile on a cost basis relative to its global competitors."[212]

[211] Tr. 2599.
[212] Exhibit 33, Mudge Rebuttal, page 44.

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Source: Exhibit 33, Mudge Rebuttal, page 44.

Given its competitive advantages and its lowest overall cost of production of any domestic smelter, the Commission should disregard Noranda's claims that it suffers from a high cost of electricity.

C. (ISSUE 31B and C): AMEREN CUSTOMERS WOULD BE BETTER OFF IF NORANDA CLOSED THAN TO PROVIDE THE REQUESTED SUBSIDY

Even if the Commission were to ignore the overwhelming evidence detailed in the prior section of this brief find that Noranda suffers from a liquidity crisis, the undeniable

evidence indicates that Ameren ratepayers would be better off for Noranda to close than to pay for the subsidized rate sought in the Non-Unanimous Stipulation. In Case No. EC-2014-0224, the Commission reached a similar conclusion.

> Even Noranda's witnesses concede that the marginal cost would likely increase in future years and would need to be adjusted in future rate cases. That means the Complainants are asking the Commission to establish a rate for Noranda that would be subsidized by Ameren Missouri's other ratepayers and that would not benefit those other ratepayers. Thus, even if Complainants had succeeded in proving a liquidity crisis, they failed to establish that Ameren's other customers would benefit from the rate reduction Noranda proposed.[213]

The evidence in this proceeding conclusively demonstrates three important points. First, given all of the class cost of service studies, Noranda is currently paying rates that are already below Ameren's cost to serve Noranda. As such, given cost of service ratemaking, Noranda should receive an increase in this case. Given the initial rate and the limited escalator contained in the Non-Unanimous Stipulation, Noranda's rate would be so far below cost of service that, by the end of the term, it would be virtually impossible to return Noranda to a cost of service based rate. Second, the undisputed evidence indicates that, given the subsidized rate and term contained in the Non-Unanimous Stipulation, customers would be better off if Noranda closed and Ameren sold the available electricity on the wholesale market. Third, Noranda's evidence, which demonstrates a very slight benefit to customers associated the initial rate recommended in the Non-Unanimous Stipulation, fails to account for the revenue requirement increase to be authorized in this case and which, absent the stipulation, would be allocated to Noranda. Given that Noranda would avoid its allocated part of any rate increase, remaining customers would now have to absorb a larger increase in this case. As a result,

[213] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at pag e 26.

Noranda's claimed very slight benefit suddenly shifts to a detriment for Ameren customers.

First, the evidence indicates that, instead of a rate decrease, Noranda should be allocated a larger than average rate increase. Specifically, there were five class cost of service studies filed in this case by four different parties. Those studies indicate that Noranda should receive a revenue neutral increase of $6.7 to $40.8 million.

ER-2014-0258 CLASS COST OF SERVICE RESULTS

	MIEC[214]	*Ameren*[215]	*Staff*[216]	*OPC 2*[217]	*OPC 1*[218]
	(A&E)	(A&E)	(BIP)	(A&E)	(P&A)
Residential	$68,761	$62,576	$36,029	$41,864	($3,336)
SGS	($12,585)	($13,391)	($12,494)	$1,007	($7,076)
LGS / SP	($61,912)	($59,886)	($39,129)	($48,159)	($38,338)
LP	(934)	1,030	($1,566)	$4,054	$20,793
LTS	6,674	9,830	$17,021	$10,254	$40,824
Lighting	(3)	(158)	$137	($9,019)	($12,867)

(in thousands)

Despite the results of these studies, Noranda proposes that this subsidy be increased by providing Noranda a 20% rate decrease. Recognizing that the Non-Unanimous Stipulation envisions a 10-year term and an escalator of only 50% of any subsequent Ameren rate increases, the amount of the Noranda subsidy will continue to

[214] Exhibit 977
[215] Exhibit 976
[216] Exhibit 978
[217] Exhibit 403 (Attachment GM-4)
[218] Exhibit 403 (Attachment GM-3)

grow. The size of this subsidy becomes increasingly daunting, to the point that the Commission, in Case No. EC-2014-0224, expressed concerns over its future ability to eliminate such a large subsidy.

> Indeed, the rate relief demanded by Noranda is not designed to address a short-term crisis. Rather, in the complaint, Noranda seeks a subsidized rate that it insists must remain in place for a period of ten years if the smelter is to remain viable. The complaint does not suggest that after ten years Noranda would be able to return to a cost-based rate, and the evidence suggests that by that time Ameren Missouri's rates would have increased to a level that would make an immediate return to such rates highly unlikely. Therefore, the rate Noranda would likely be a permanently subsidized rate financed by Ameren's Missouri's other ratepayers.[219]

Given these expressed concerns, Ameren undertook a calculation to determine the amount of the Noranda subsidy at the end of its original 7-year proposal. Under Ameren's unrebutted analysis, the Noranda subsidy would increase to $81 million per year or nearly 36% below its cost of service.[220] All told, Ameren estimates that, over the course of the original seven year term, "Noranda would shift more than $400 million in costs to other Ameren Missouri customers."[221] Not surprisingly then, similar concerns regarding the Commission's ability to eliminate this subsidy have been expressed..

> Because costs are rising much faster than Noranda's proposed rate, the gap between Noranda's proposed rate and its actual cost of service expands with each passing year. As this gap increases, it would likely be impossible, as a practical matter, to eliminate that subsidy after seven years because moving from a subsidized rate to a cost of service-based rate overnight would product a significant rate shock for Noranda. Consequently, ***I am concerned that eliminating the subsidy at the end of the seven-year proposed effective period and moving to a cost-based rate will not be accomplished in a single rate change but will, instead, require a very lengthy phase-in to avoid severe rate shock***. That suggests Ameren Missouri's other customers will be on the hook to subsidize rates

[219] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at page 25.
[220] Exhibit 9, Davis Rebuttal, page 22.
[221] *Id.* at page 23.

> for Noranda well beyond the proposed seven-year period and likely at an even greater level than Noranda is requesting today.[222]

Second, the evidence in this case indicates that, rather than subsidize Noranda's rate, Ameren ratepayers would be better off if Noranda closed and Ameren sold the available electricity on the wholesale market. As Ameren notes, "[l]ong-term power deals, which are analogous to the long-term rate arrangement that Noranda now seeks, must be tested against future expectations of the market."[223] As Mr. Michels points out, tools to undertake a testing of the rates under any Noranda rate proposal against "future expectations of the market" are readily available and employed.

> A detailed production cost model that includes the capacity to represent transmission system interconnections and constraints can be used to develop estimated locational marginal prices ("LMP's") for a specific location. . . . Only a production cost model that includes robust modeling of local transmission constraints and congestion, such as Ventyx's Promod model, could provide reasonably accurate results for such an analysis. Performing simulations with such a model, both with and without the specified load, would yield a reasonable estimate for the change in price at that location for a period, say a year.[224]

Based on such modeling, Ameren compared the revenues to be derived under the terms of Noranda's original proposal ($32.50 initial rate, 1.0% annual escalator, 7 year term) to the revenues that could be collected by selling that load on the wholesale market. As Mr. Michels points out, "[r]evenue under Noranda's proposal would be approximately $272 million less than the revenue that would be realized by selling the same power into

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[222] *Id.* at pages 22-23 (emphasis added). See also, Exhibit 26, Michels Amended Rebuttal, page 28 ("In fact, Noranda's proposal makes it virtually impossible for other customers to realize long-term benefits because of the issues addressed by Mr. Davis. Specifically, Mr. Davis demonstrates that the subsidy to Noranda is unlikely to be eliminated following the 7-year term proposed by Noranda. In fact, Mr. Davis believes the subsidy to Noranda from Ameren Missouri's other customers is very likely to grow larger over time.").

[223] Exhibit 26, Michels Amended Rebuttal, page 25.

[224] *Id.* at pages 27-28.

the market."[225] Thus, Noranda's original proposal is detrimental to Ameren ratepayers. In cross-examination it was shown that, because of the extended term, the magnitude of this customer detriment grows to $550 million under the terms of the Non-Unanimous Stipulation.[226]

Third, even Noranda's own evidence indicates that any customer benefit associated with the Noranda rate proposal would be very thin and, recognizing that ratepayers would be expected to absorb any rate increase in this case that would otherwise be allocated to Noranda, any customer benefit rapidly disappears. Specifically, under the Non-Unanimous Stipulation, Large Primary customers would receive a 1.50% rate increase in order to fund the Noranda subsidy.[227] That said, under some measures of historical markets prices presented by Noranda, those same customers would only realize a 1.58% rate increase if Noranda were to close.[228] Thus, under Noranda's own evidence designed to support the Non-Unanimous Stipulation, Large Primary customers would only be 0.08% better off by agreeing to the Noranda subsidy than if Noranda were to close. When asked to compare the marginal amount of benefits under the Noranda proposal versus Noranda simply closing, Mr. Brubaker responded that "it would be on the edge." [229]

Noranda's evidence of slight customer benefits, however, is misleading. As was revealed during cross-examination, Noranda's calculations are performed on a revenue neutral basis.[230] That is to say, the Noranda calculations assume current rates and do not

[225] *Id.* at page 29.
[226] Tr. 2931,
[227] Exhibit 534, MEB-COS-9, page 1 of 2.
[228] *Id.* at MEB-COS-8.
[229] Tr. 2649.
[230] Tr. 2647-2648.

take into account the additional rate increase that customers will be expected to absorb from this rate case that otherwise would have been allocated to Noranda.[231] Assuming that the Commission simply allocated any rate increase on an across the board basis, and did not address the fact that Noranda is currently paying rates that are already below cost of service, then Noranda would have been allocated roughly 5.82% of any rate increase in this case.[232] If Ameren only receives a 1.30% overall increase ($35.37 million) these Large Primary customers will be allocated an additional .081% under the Noranda proposal.[233] As indicated, the .08% benefit quantified by Mr. Brubaker quickly disappears as a result of the rate increase in this case. Given that the latest revenue requirement in this case provides for a minimum increase of $94.4 million (3.46%),[234] Ameren's customers are already worse off by agreeing to the proposed Noranda subsidy.

Clearly, by any measure, whether class cost of service studies, forward looking market prices or Noranda's own evidence, Ameren ratepayers are worse off from the requested Noranda subsidy then from Noranda simply closing.

[231] Tr. 2648.
[232] Exhibit 503, Brubaker Direct, Schedule MEB-COS-4 (Noranda's base revenues of $159,333,000 are 5.82% of Ameren's total base revenues of $2,737,799).
[233] 1.0% Ameren increase is $27.21 million. (Exhibit 28, Moehn Direct, page 5). Therefore, a 1.30% rate increase amounts to $35.37 million. Noranda's across the board share of this increase would amount be 5.86% or $2.073 million. Instead, Noranda's share of the increase would be allocated to other customers including 7.91% by Large Primary customers (Exhibit 503, Brubaker Direct, Schedule MEB-COS-9, page 1). Therefore, for every 1.0% of Ameren increase, Large Primary customers would experience an additional $163,963 of rate increase associated with Noranda be exempted from this rate increase. Given total Large Primary revenues of $202,147,000 (*Id.*), this amounts to a .081% increase for Large Primary customers.
[234] See, *Reconciliation*, filed March 28, 2015.

D. NORANDA'S CLAIM THAT THE VIABILITY OF THE NEW MADRID SMELTER IS THREATHENED IS EXAGERRATED.

Repeatedly though-out this case the Commission has been subjected to threats that, absent a rate reduction, the viability of the New Madrid smelter is precarious. The evidence suggests, however, that Noranda's threats are exaggerated. Specifically, despite the seriousness of these threats and the seemingly imminent nature of such actions, **_____**

Specifically, in his testimony, Mr. Mudge indicates the following:

> Notably, in the current case as well as Case 0224, Ameren Missouri asked Noranda several data requests relating to the claim that the smelter was "subject to closure," including requests for documents that address, discuss, analyze or otherwise relate or pertain to the possibility of closure. I would note that Noranda produced no documents that describe a possible closure of the smelter in the circumstances presented in the liquidity forecasts presented in the Boyles or Smith testimony, nor do the doucments Noranda pointed to in response to other data requests. Similarly, in this case, Ameren Missouri has also asked for documentation analyzing the impact on Noranda of closing the smelter. Noranda indicates **_____**.[235]

Given the seemingly imminent and final nature of such action, one would expect that Noranda would have explored every other possible option or would know **_____ _____**. That said, during cross-examination it was revealed that Noranda had not yet explored the possibility of **_____**; **_____** or **_____**.[236] Further despite its seemingly imminent nature, Noranda has not **_____

[235] Exhibit 33, Mudge Rebuttal, pages 10-11. See also, Schedule RSM-R1.
[236] HC Tr. pages 2563-2564.

_____**.[237] Certainly, given its lack of preparedness for such a seemingly inevitable outcome, one must necessarily find that such threats are exaggerated.

E. ANY NORANDA SUBSIDY SHOULD NOT BE BORNE BY ONLY AMEREN CUSTOMERS, BUT SHOULD BE CONSIDERED BY THE GENERAL ASSEMBLY FOR BROADER RECOVERY.

In its decision in Case No. EC-2014-0224, the Commission found that the burden associated with Noranda's request for relief should not be shouldered exclusively by Noranda's ratepayers. Instead, that request should be considered by the Legislature.

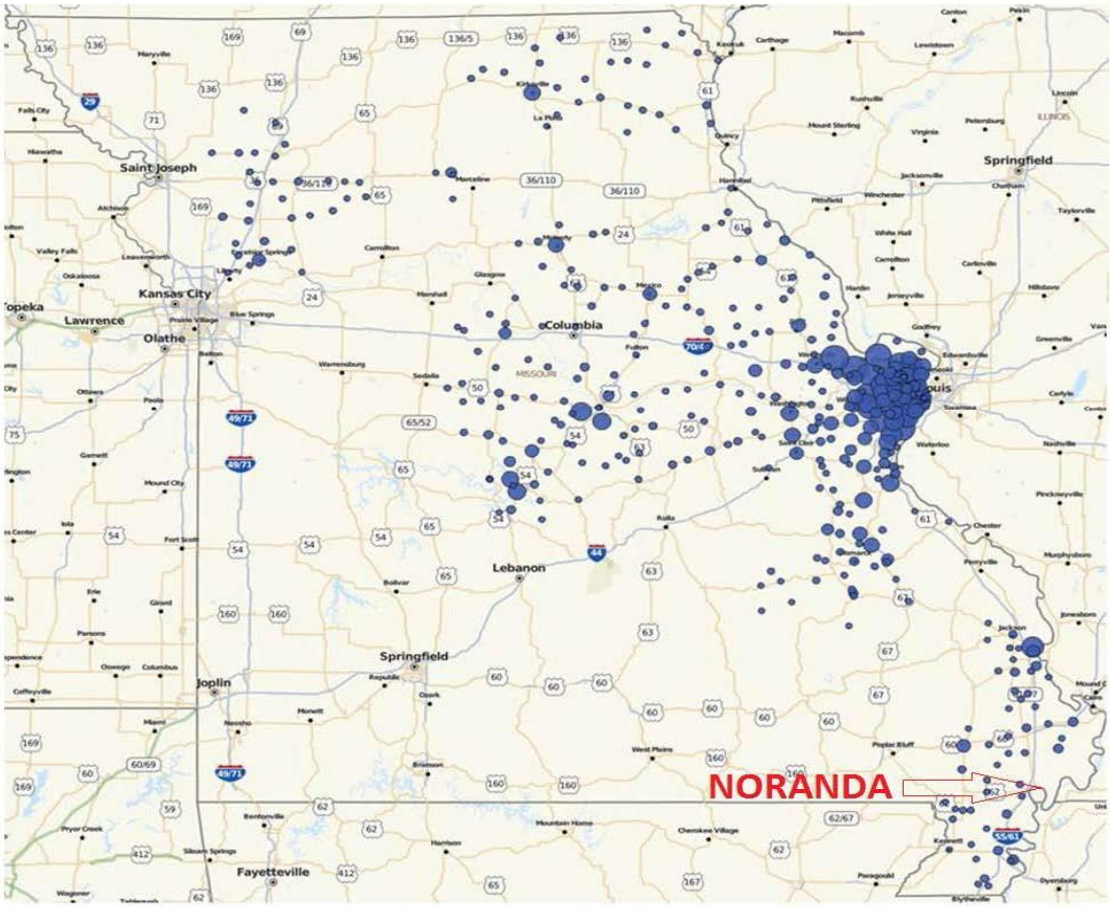
> The Complainants have not demonstrated a liquidity crisis nor adequately demonstrated that Ameren Missouri's remaining ratepayers would be better off if Noranda took service at its requested rate than they would be if Noranda exited Ameren Missouri's system. ***Finally, and importantly, a request for an economic development subsidy of this magnitude is more properly directed to the Missouri General Assembly***.[238]

Inevitably, similar concerns were raised in the context of this case.

Specifically, given that Noranda is located in the "Bootheel" region of Missouri, the vast majority of the benefits associated with the existence of the New Madrid smelter are realized by citizens in that area. That said, only half of these benefitting Bootheel households are customers of Ameren.[239] The rest are electric customers of various cooperatives or municipal utilities. Therefore, a significant number of households in the Bootheel will benefit from the continued existence of Noranda, but will not pay any of the cost associated with securing Noranda's future. Instead, Noranda proposes that the cost of keeping Noranda viable be shouldered entirely by Ameren's customers. As the

[237] HC Tr. pages 2565-2566.
[238] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, page 28.
[239] Exhbit 9, Davis Rebutal, page 27.

attached map of Ameren customer density by zip code indicates, however, very little of Ameren's customer base is found in the Bootheel region.



Source: Exhibit 9, Davis Rebuttal, Schedule WRD-R4.

The inequitable nature of Noranda's request that all Ameren customers shoulder the burden of keeping Noranda in existence is obvious when one recognizes that only 3% of Ameren's customer base is located in the Bootheel.[240] The remaining customers are located primarily in the St. Louis and Central Missouri regions. "That means that Noranda's proposal would require 97% of Ameren Missouri's customers to subsidize a company that primarily benefits, at most, the remaining 3%."[241]

[240] *Id.*
[241] *Id.*

In order to attempt to avoid the obvious inequitable nature of its request, Noranda argues that the New Madrid smelter provides economic benefits for all of Missouri.[242] As Ameren has pointed out, however, "[i]f it is true, as Dr. Haslag's testimony suggests, that closure of the smelter would impact the state's economy as a whole, then the appropriate subsidy, if one is appropriate, should burden all of Missouri's citizens and not just Ameren Missouri's other customers."[243]

> Because of the magnitude of the financial assistance Noranda is requesting, and also because a majority of economic impacts are, according to Dr. Haslag, felt at the state level, it makes much more sense for the state legislature, composed of elected representatives from across the entire state, to decide whether and how to provide economic relief to Noranda. It is simply not fair to require the Commission to make that decision or to push the costs and risks of the proposed subsidies solely on the backs of Ameren Missouri customers.[244]

MECG echoes the sentiments expressed by Ameren in this case and the Commission in the last case. Specifically, given Noranda's claims that the New Madrid smelter provides economic benefits to the entire state, then its request for economic assistance should be addressed to the General Assembly where all citizens, not just Ameren ratepayers, can be expected to help shoulder the cost of such assistance.

F. THE COMMISSION SHOULD CONTINUE TO RELY ON COST-BASED RATES

It is well established that this Commission has relied upon cost of service for the purpose of setting rates.

> The Commission usually determines whether a rate design – the means by which the responsibility to pay the utility's revenue requirement is distributed among the utility's customer classes – is just and reasonable by

[242] Exhibit 606, Haslag Direct.
[243] Exhibit 9, Davis Rebuttal, page 26.
[244] *Id.* at page 29.

> examining a class cost of service study to determine the amount of costs that should be assigned to each class on the principle that the class that causes the cost should pay that cost.[245]

This need to rely upon cost of service as the basis for establishing rates was echoed repeatedly in this case. Class cost of service studies are typically done because customers "have different service and usage characteristics and, thus, different costs of service. The Commission has long recognized that an equitable, non-discriminatory rate structure must recognize these differences. CCOSS are designed to capture and quantify those differences so that the Commission can assign the Company's overall revenue requirement to each rate class in an equitable manner."[246]

Interestingly, while now advocating that the Commission depart from such a methodology, the need for and benefits of cost of service ratemaking were espoused by Noranda's own ratemaking witness. Specifically, Mr. Brubaker states that "cost should be the primary factor" used in establishing class revenue requirements and designing rates.[247] "Factors such as simplicity, gradualism and ease of administration may also be taken into account, but the basic starting point and guideline throughout the process should be cost of service."[248] While now asking that the Commission depart from cost of service ratemaking for Noranda, Mr. Brubaker notes three critical benefits of relying on costs as the "primary factor" for setting rates.[249]

First, Mr. Brubaker notes that cost-based rates help to achieve equity. "When rates are based on cost, each customer pays what it costs the utility to provide service to that customer; no more and no less. If rates are based on anything other than cost factors,

[245] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at page 27.
[246] Exhibit 9, Davis Rebuttal, pages 18-19.
[247] Exhibit 503, Brubaker Direct, page 34.
[248] *Id.* at page 35.
[249] *Id.*

then some customers will pay the costs attributable to providing service to other customers – which in most cases is inequitable."[250] Interestingly, Mr. Brubaker now proposes that the Commission act in an inequitable fashion by setting rates based on something other than cost factors.

Second, cost-based rates help to further conservation. "Conservation occurs when wasteful, inefficient use is discouraged or minimized. Only when rates are based on costs do customers receive a balanced price signal upon which to make their electric consumption decisions. If rates are not based on costs, then customers who are not paying their full costs may be misled into using electricity inefficiently in response to the distorted rate design signals they receive." Again, by asking that the Commission depart from cost-based rates, Mr. Brubaker is asking the Commission to send "inefficient" price signals. Given its cheap electric price signal associated with paying rates that are below its full cost of service, Noranda will be encouraged to use electricity "inefficiently."[251]

Third, cost-based rates help the utility to achieve a cost-minimization objective. "When the rates are designed so that the energy costs, demand costs and customer costs are properly reflected in the energy, demand and customer components of the rate schedules, respectively, customers are provided with the proper incentives to minimize their costs, which will in turn minimize the costs to the utility."[252] Again, despite this critical objective, Mr. Brubaker asks that the Commission depart from cost of service ratemaking in order to benefit his client.

The evidence indicates that there is no "cost basis" for providing Noranda a rate that is substantially below the results of the various cost of service studies, including the

[250] *Id.*
[251] *Id.* at pages 35-36.
[252] *Id.* at page 36.

one presented by Mr. Brubaker.[253] As such, the only way for Mr. Brubaker to justify a subsidized rate for his client then is to depart from the cost of service ratemaking that he has indicated is so beneficial.

The ultimate result, however, of Mr. Brubaker's sudden request to depart from cost of service ratemaking for his client is obvious. "***A rate that is significantly less than the cost of service*** is a major – and likely unprecedented – departure from the Commission's traditional ratemaking policies and practices, is not justified by any difference in the character of the service Ameren provides to Noranda, and ***may be considered unduly discriminatory***."[254]

Given the potential unlawful consequences that come with departing from cost of service ratemaking, MECG recommends that the Commission continue to rely on class cost of service studies for purposes of establishing a rate for Noranda that is "equitable", "encourages conservation" and "leads to cost minimization" by the utility.

G. (ISSUE 31D): THE NON-UNANIMOUS STIPULATION AND AGREEMENT IS AGAINST THE PUBLIC INTEREST IN THAT IT RESULTS IN UNJUST AND UNREASONABLE RATES

Recognizing that: (1) Noranda is not suffering from a liquidity crisis; (2) Noranda has the lowest overall cost of production of any domestic smelter; and (3) customers would be better off if Noranda closed and Ameren sold that electricity in the wholesale market, MECG strongly believes that the Commission should not depart from cost of service ratemaking for purposes of establishing a rate for Noranda. Given this fundamental position, it is not surprising that MECG vehemently opposes the Non-

[253] Exhibit 9, Davis Rebuttal, page 24. Section 393.140(5) prohibits "unjustly discriminatory" rates.
[254] *Id.* at pages 21-22 (emphasis added).

Unanimous Stipulation by which certain parties[255] seek to provide Noranda a rate that is not based on cost of service and results in a huge subsidy for Noranda. In this section of the Brief, MECG will address several of the critical aspects of that settlement and will show that the Non-Unanimous Stipulation is inherently unjust and unreasonable.

1. Initial Rate Under the Non-Unanimous Stipulation is Unreasonable

Under the terms of the Non-Unanimous Stipulation, Noranda would receive an initial rate of $34.00 / MWh with no increase due to the authorized increase granted to Ameren in this case.[256] The unreasonable nature of this initial rate is demonstrated in three ways. ***First***, while Noranda's current base rate is $37.95 / MWh,[257] each of the class cost of service studies filed in this case indicate that Noranda's current rate is below its actual cost of service. For instance, Noranda's own witness indicates that Noranda's rate is already 4.2% below cost.[258] Thus, if Ameren receives a 4% rate increase in this case, Noranda's cost based rate should be $41.13. Interestingly, Public Counsel, a signatory to the current Non-Unanimous Stipulation filed a class cost of service study which indicates that the current Noranda rate is already 25.62% below its actual cost of

[255] One must necessarily question the independence of at least two of the entities that signed the Non-Unanimous Stipulation. For instance, while a signatory to the settlement, MIEC is a group that includes Noranda as a member. (See, *Amended Application to Intervene*, filed July 31, 2014, at page 1). Similarly, while not a retailer, Noranda is, nevertheless, a member of the Missouri Retailers' Association. (See, *Non-Unanimous Stipulation and Agreement*, filed March 10, 2015, at page 1, footnote 1). Given Noranda's presence as a member in both of these groups, the Commission should necessarily be skeptical of those groups' claims to represent Ameren's customers or the Small General Service; Large General Service ; Small Primary or Large Primary customer classes.

[256] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at page 3 (paragraph 7) ("Set. . . an effective base rate of $34.00 / MWh for the aforementioned new IAS class, to become effective on the operation of law date in this case.").

[257] Exhibit 9, Davis Rebuttal, page 4.

[258] Exhibit 977.

service.[259] Thus, while now advocating a rate of $34.00 / MWh, Public Counsel evidently believes that Noranda's actual cost of service is greater than $47.67 / MWh.[260] Assuming a 4.0% rate increase in this case, OPC's witness believes that Noranda's cost of service is approximately $49.58 – approximately 46% above the rate it supports in the Non-Unanimous Stipulation. Clearly, the rate envisioned by the Non-Unanimous Stipulation bears no relationship to the cost for Ameren to serve Noranda.

Second, while Noranda benefits from the lowest overall production cost of any domestic smelter, the $34.00 / MWh rate envisioned under the Non-Unanimous Stipulation would decrease Noranda's overall cost of production and give Noranda the second lowest cost of electricity. "If Noranda's request is granted **_____** will be the only currently operating smelter in the U.S. with cheaper power.[261]

Third, while the Non-Unanimous Stipulation provides for a $34.00 / MWh rate, Noranda has already agreed, within the context of this case, that a $34.44 / MWh rate is reasonable. Specifically, the various Signatory Parties to the Non-Unanimous Stipulation have previously filed a different Stipulation in this case. As provided under that previous settlement, Noranda would receive a rate of $34.44 / MWh.[262] On October 16, 2014, Noranda filed its Statement of Support indicating that it "supports" the "terms and conditions" of that settlement.[263] Strangely, while Noranda deemed the $34.44 / MWh rate to be reasonable, the "consumer representatives" deemed it appropriate to give Noranda an even lower rate this time around. Clearly, in addition to have no bearing to

[259] See, Exhibit 403, Marke Rebuttal, Attachment GM-3.
[260] $37.95 / MWh (current rate) increased by 25.62% = $47.67
[261] Exhibit 33, Mudge Rebuttal, page 36.
[262] See, *Non-Unanimous Stipulation and Agreement*, filed October 10, 2014, at page 2, paragraph (c). ("Set an effective base rate of $34.44 / MWh for the aforementioned new IAS class.").
[263] *Statement of Support for and Agreement with Non-Unanimous Stipulation and Agreement and Jointly Proposed Procedural Schedule*, filed October 16, 2014

Ameren's cost of service, the rate contained in the current Non-Unanimous Stipulation also has no rational relationship to other domestic smelter electric rates or even that rate which Noranda itself deems to be reasonable.

2. The Limited Escalator in the Non-Unanimous Stipulation is Unreasonable

The fact that the Non-Unanimous Stipulation provides a rate for Noranda that is, by Public Counsel's estimates, approximately 46% below cost of service is egregious enough.[264] The unreasonableness of the Non-Unanimous Stipulation is exacerbated by the fact that, while that settlement lasts for 10 years, Noranda would only be subjected to 50% of the rate increases authorized to Ameren during that period.

Specifically, that settlement provides that "during the Term, the new IAS class shall be subject to a base rate adjustment of fifty percent (50%) of the system average increase."[265] Thus, while providing a rate that, by Public Counsel's own estimates is 46% below cost of service, the settlement envisions that, through the limited escalator, the Noranda rate would be permitted to deviate further from cost of service.

As indicated in the Introduction to this brief, with its current request, Ameren's rates will have increased 52.7% since 2007.[266] Thus, if Ameren's rates continue to increase at the rate experienced over the last 8 years, Noranda will only be exposed to 26.35% of that increase. The remainder will be absorbed by the remaining Ameren customers. So, in addition to being already being 46% below Public Counsel's estimate

[264] As indicated in the Class Cost of Service section of this brief, MECG does not agree with Public Counsel's class cost of service methodology. MECG simply cites to the Public Counsel's evidence, as the self-described representative of all customer classes, to demonstrate the unreasonable nature of the Non-Unanimous Stipulation.
[265] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at page 3 (paragraph 10).
[266] See page 4 of this brief.

of Ameren's cost of service, the Non-Unanimous Stipulation envisions that growing by 26.35% over the next several years. It is little wonder then that Ameren wonders whether the Commission, after the 10 year term, would ever be able to return Noranda to a true cost based rate.

> Another concern that I have is about how, or even if, Noranda would ever return to a cost of service-based rate. The Commission uses cost of service as the primary basis for the rate design aspect of utility ratemaking. As a result, when Noranda's rates are no longer liked to the cost of service, I am concerned there will be nothing to guide the Commission regarding how the rate subsidy Noranda proposes can be unwound in future periods.[267]

3. The Exemption from the Fuel Adjustment Clause is Unreasonable

In addition to setting an unreasonably low rate, the Non-Unanimous Stipulation also seeks to exempt Noranda from the effects of Ameren's fuel adjustment clause.[268] Amazingly, unlike the base rate and escalator provisions which can be modified as a result of Noranda's liquidity position, the Noranda's exemption from the FAC appears to be absolute for 10 years regardless of Noranda's financial position.[269]

The unreasonable nature of the FAC exemption is obvious. The fuel adjustment clause represents adjustments for the cost of fuel that the customer used in prior periods.

> All Ameren Missouri retail customers are subject to FAC charges. These charges represent adjustments to customer rates for fuel and purchased power related expenses that represent a large portion of Ameren

[267] Exhibit 9, Davis Rebuttal, page 22.

[268] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at page 3 (paragraph 8) ("Effective with the Implementation Data in this case, exempt the new IAS class from Rider FAC through the end of the ten-year term of the Stipulation.").

[269] *Id.* ("through the end of the ten-year term of the Stipulation."). Also, please note, paragraph 19(a) allows for Signatories to seek an increased escalator in rate cases when Noranda liquidity reaches $250 million. Paragraph 19(b) allows Signatories to seek a higher rate when Noranda liquidity reaches $300 million. No liquidity provision allows for Noranda to be subjected to the fuel adjustment clause.

> Missouri's cost of service. Exempting one retail customer from such charges while including them for all other customers raises issues as to whether the rate proposed by Noranda is unduly preferential and is a significant reason why Noranda's proposal cannot be adopted by the Commission in this case.[270]

Therefore, through its payment of the fuel adjustment clause, Noranda is simply paying the increased cost of fuel that is directly attributable to the electric service that it received in a prior period. By exempting Noranda from the application of the FAC, there is no assurance that Noranda would even be paying the incremental cost for Ameren to serve it. Rather, other customers would be expected to absorb these variable costs that were otherwise attributable solely to Ameren's service to Noranda.

As previously indicated, Public Counsel's own evidence contradicts the rate envisioned by the Non-Unanimous Stipulation. Similarly, Public Counsel's evidence also contradicts the proposed exemption from the fuel adjustment clause.

Q. SHOULD THE COMMISSION GRANT NORANDA'S REQUEST NOT TO PAY THE FUEL ADJUSTMENT CLAUSE?

A. No, it should not. Noranda like every other Ameren Missouri customer, is served by an integrated production system with varied resources ideally designed and built to meet that load. Resource variety is the key to providing low cost, reliable supply of energy to all customers; even customers as large as Noranda. The energy used by Noranda contributes to the cost of fuel to meet Ameren Missouri's system requirements just as the usage of Ameren's Missouri's other customers contributes to the cost of fuel. And just as the existence of the other customers reduces the amount of energy and capacity Ameren Missouri can sell on the market, the existence of Noranda as a customer of Ameren Missouri reduces the amount of energy and capacity that Ameren Missouri can sell as purchased power. Therefore, neither Noranda nor any other Ameren Missouri customer should be excluded from the FAC.[271]

[270] Exhibit 26, Michels Amended Rebuttal, page 21.
[271] Exhibit 401, Mantle Rebuttal, pages 34-35.

Clearly then, in addition to disregarding its own evidence regarding the cost to serve Noranda, Public Counsel also disregards its own evidence regarding the ubiquitous application of the Ameren fuel adjustment clause.

4. The 10-Year Term of the Non-Unanimous Stipulation is Unreasonable

In addition to providing a significantly reduced rate, less exposure to future rate increases and an exemption from the fuel adjustment clause that ensures that Noranda pays at least its incremental costs, the Non-Unanimous Stipulation also envisions that this significant subsidy will last for ten years.[272] Again, in agreeing to this provision, Public Counsel ignores the positions of its own experts.

Specifically, when asked its opinion regarding the length of term for any discounted Noranda rate, Staff responded that such a rate should only last until the next rate case.[273] Interestingly, OPC's witness previously was employed by the Staff. When asked on cross-examination to put aside her current status as a consultant for Public Counsel, Ms. Mantle indicated that she probably would agree with Staff's opinion that any discounted rate should only last until the next rate case.[274]

5. The Liquidity Thresholds in the Non-Unanimous Stipulation are Laughable

While providing Noranda a rate that is significantly below cost of service, limiting Noranda's exposure to future rate increases, exempting Noranda from the

[272] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at page 3 (paragraph 9) ("fix the effective base rate applicable to the new IAS class for a period of ten (10) years from the Implementation Date (the "Term")").
[273] Tr. 3009.
[274] Tr. 3047-3048.

application of the fuel adjustment clause and providing this advantage for a period of 10 years, the Non-Unanimous Stipulation also provides a liquidity provision seemingly as a customer protection. As this brief demonstrates, however, that liquidity provision, to the extent it is designed to protect Ameren's other ratepayers, is laughable.

Specifically, the Non-Unanimous Stipulation provides that, after year five of the Term, Noranda's liquidity will be calculated. In the event that Noranda's liquidity exceeds $250 million, ratepayers can seek to increase the amount of the rate case escalator.[275] Similarly, to the extent that Noranda's liquidity exceeds $300 million, ratepayers can seek to increase Noranda's base rate.[276] While undoubtedly well intentioned, the liquidity provisions are laughable for purposes of protecting Ameren ratepayers.

First, as expressly provided in paragraphs 19(a) and (b), the various liquidity targets are only applicable "after year 5 of the term." In this regard, the liquidity targets do nothing to protect Ameren ratepayers during the initial five years of the agreement. Recognizing the tremendous subsidy that is envisioned by the settlement, Noranda's liquidity will rapidly rise during the first five years of that agreement. Yet, as envisioned by the Signatories, the Commission and ratepayers would be powerless to take any steps in the first five years no matter how high Noranda's liquidity increases.

Second, the liquidity thresholds are exceedingly high. In previous cases, Noranda has offered its opinion on the amount of liquidity necessary for it to compete in the

[275] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at pages 6-7 (paragraph 19a).
[276] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at page 7 (paragraph 19b).

domestic aluminum industry. Specifically, in Case No. EC-2014-0224, Noranda provided certain liquidity targets.

Q WHAT LEVEL OF LIQUIDITY IS NECESSARY FOR NORANDA TO REMAIN A COMPETITIVE SMELTER IN THE U.S.?

A **_____ _____ _____ _____**[277]

Despite Noranda's own opinion that target liquidity is **_____**, the Non-Unanimous Stipulation envisions that Noranda will be permitted to attain a liquidity level that is much higher prior to any action being allowed under the settlement. Specifically, Noranda would be allowed to reach a liquidity threshold of $250 million before the rate case escalator can be addressed and $300 million before the subsidized rate can be addressed.

Third, the laughable nature of the settlement liquidity thresholds is best demonstrated through simple mathematics. As previous pointed out, Noranda's last reported liquidity position was $158.3 million as of December 31, 2014.[278] Between the reduced base rate and the exemption from the fuel adjustment clause, the Non-Unanimous Stipulation envisions a decrease in Noranda's rates, and thus the creation of an annual subsidy, in the amount of $33,210,000.[279] Given its limited escalator in future cases, the amount of this subsidy will undoubtedly increase.[280] Therefore, Noranda's liquidity should increase by at least $33.21 million per year. Therefore, after only 3 years, Noranda's liquidity should increase by $99.63 million. When added to Noranda's

[277] HC Tr. 2409.
[278] Tr. 2410.
[279] Exhibit 534, Schedule MEB-COS-9, page 1 of 2, column 6, line 8.
[280] Exhibit 9, Davis Rebuttal, page 22 ("the deviation between Noranda's rate and its cost of service will expand in each subsequent rate case.").

current liquidity, Noranda's liquidity at the end of three years will be approximately $257.9 million, already well above the $250 million liquidity threshold. Worse still, this is well in excess of the **_____** which Noranda claims to need to be a competitive smelter.

Yet, despite the rapid increase in Noranda's liquidity envisioned under the settlement, the Commission and the Ameren ratepayers will be powerless to take any steps to address the ongoing subsidy. By the time that year five arrives and the subsidized Noranda rates can be addressed, Noranda's liquidity will have likely reached at least almost $325 million.[281] Clearly, as a customer protection, the liquidity thresholds are laughable.

Fourth, while the liquidity thresholds would allow the Commission and ratepayers to eventually address the rate case escalator and the amount of subsidy in the Noranda rate, there is no similar provision to address the possibility that Noranda will subsequently be exposed again to the fuel adjustment clause. Specifically, paragraph 19(a) applies a $250 million liquidity threshold prior to any change in the rate case escalator. Similarly, paragraph 19(b) applies a $300 million liquidity threshold after any potential change in the amount of the Noranda subsidy. That said, the exemption from the fuel adjustment clause is absolute for 10 years. "Effective with the Implementation Date in this case, exempt the new IAS class from Rider FAC ***through the end of the ten-year term of the Stipulation***."[282]

[281] $33.21 million per year for 5 years = $166.05 million plus current liquidity of $158.3 million = $324.35 million.

[282] *Non-Unanimous Stipulation and Agreement Regarding Economic Development, Class Cost of Service, Revenue Allocation and Rate Design*, filed March 10, 2015, at page 3 (paragraph 8).

Fifth, despite the existence of the liquidity thresholds, there are no assurances that the liquidity provided under the Non-Unanimous Stipulation will be utilized for the best interests of Noranda and the Bootheel or Missouri economies. As Noranda indicates in its 10K, Apollo "substantially influences" the company even to the point of causing actions which normal shareholders would "otherwise view favorably."

> *Apollo has the ability to substantially influence our company and the outcome of matters voted upon by our shareholders, and to prevent actions which a shareholder may otherwise view favorably.*
>
> As of December 31, 2014, Apollo owned approximately 33.1% of our common stock. As long as Apollo owns more than 10% of our common stock, it will have the right to cause the Board of Directors to nominate to our Board of Directors at least four Apollo designees. Thus, Apollo has the ability to significantly influence our decisions.
>
> The interests of Apollo could conflict with or differ from stockholder interests as a holder of our common stock. For example, the concentration of ownership held by Apollo could delay, defer or prevent a change of control of Noranda or impede a merger, takeover or other business combination that stockholders or debtholders may otherwise view favorably. Additionally, Apollo is in the business of making or advising on investments in companies and holds, and may from time to time in the future acquire interests in, or provide advice to, businesses that directly or indirectly compete with certain portions of our business or are suppliers or customers of ours. Apollo may also pursue acquisitions that may be complementary to our business, and, as a result, those acquisition opportunities may not be available to us. A sale of a substantial number of shares of stock in the future by funds affiliated with Apollo could cause our stock price to decline.[283]

During cross-examination Noranda attempted to minimize concerns with Apollo's significant ownership and ability to appoint board members. Specifically, it was revealed that, in addition to the four Apollo board members, there are five independent board members plus the Mr. Smith.[284] While Noranda seeks to portray Mr. Smith as a non-Apollo board member and therefore independent, the evidence raises questions about Mr.

[283] Exhibit 533, page 22.
[284] Tr. 2437.

Smith's independence from Apollo. While Mr. Smith has never taken a paycheck directly from Apollo, he readily admits that "I have run or -- all or parts of five different companies for them [Apollo], including Noranda."[285] Recognizing Mr. Smith's long-standing relationship with Apollo, one must necessarily his independence and his willingness to prevent Apollo from taking "actions which a shareholder may otherwise view favorably."

H. CONCLUSION

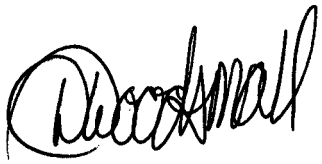
As the evidence and this brief readily demonstrate, Noranda is not suffering from a liquidity crisis. Instead, Noranda has demonstrated a history of stable liquidity positions. In fact, when faced with a similar liquidity position in the last Ameren rate case, Noranda agreed to an equal percent, across-the-board increase which resulted in a 10.1% increase to Noranda. Now, with the same liquidity position, Noranda claims to need a 20% rate reduction. Certainly, Noranda's recommendations in the last case cast serious doubt on its alleged liquidity crisis and positions in this case.

The Commission should continue to base rates in this case on cost of service. Recognizing that all class cost of service studies indicate that Noranda is currently paying a rate that is below cost of service, the Commission should take steps to eliminate the subsidy in Noranda's rate.

[285] *Id.*

Respectfully submitted,

WOODSMALL LAW OFFICE



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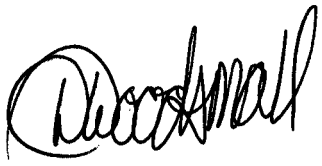
CERTIFICATE OF SERVICE

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: March 31, 2015