

THE MISSOURI PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In Re: Union Electric Company's)
2008 Utility Resource Filing pursu-) EO-2007-0409
ant to 4 CSR 240 - Chapter 22.)

**RESPONSE AND STATEMENT OF NORANDA ALUMINUM, INC.
REGARDING PARTIAL STIPULATION AND AGREEMENT**

COMES NOW NORANDA ALUMINUM, INC. ("Noranda"), through its counsel of record, and submits its response and statement regarding the Partial Stipulation and Agreement and Joint Filing that was filed in this case on August 12, 2008 ("Partial Stipulation"), as follows:

A. Introduction.

1. Although Noranda has participated in many of the IRP meetings either in person or via teleconference and commends the active parties for their contributions to the process, we have chosen not to be a signatory to the Partial Stipulation. This should not be interpreted to diminish the important work that has been done by Ameren and the many important contributions of the parties. This pleading is submitted so that the Commission, Ameren,^{1/} and the other participating parties will better understand Noranda's position on these matters. This pleading is

^{1/} For the benefit of the reader, "Ameren" is used in a generic sense to refer to Ameren, as well as Union Electric Company d/b/a AmerenUE, as the context may indicate.

also intended to provide the Commission with a timely response to the Partial Stipulation pursuant to the Commission's rules regarding non-unanimous stipulations^{2/} and are not intended to be the "comments" that are referred to in 4 CSR 240-22.080(9).

B. The Current IRP Rule: Looking at Trees But Missing the Forest.

1. To begin, Noranda understands that 4 CSR 240-22 ("IRP Rule") is designed to establish certain minimum standards surrounding the resource planning process so that "the public interest is adequately served" and the public is provided with energy services "that are safe, reliable and efficient, at just and reasonable rates"^{3/} The process is to be conducted under the assumption that "rates will be adjusted annually, in a manner that is consistent with Missouri law."^{4/}

2. The IRP Rule then sets out in considerable detail a planning process that is designed to encourage and document effective planning by the utilities and the development of a "Preferred Plan" in order to achieve the foregoing objectives.

3. While a good plan for meeting customers' future electricity needs "at just and reasonable rates" (the "Preferred Plan") is certainly its goal, the IRP Rule is not designed to

^{2/} 4 CSR 240-2.115. This response is timely in that the Commission has not yet issued its customary notification to non-signatory parties that a formal filing has been made thereby triggering the time limits specified in the non-unanimous stipulation rule.

^{3/} 4 CSR 240-22.010(2).

^{4/} 4 CSR 240-22.060(4)(B).

result in a review of the Preferred Plan, *per se*. The IRP Rule is focused on the **process**. Nevertheless, from Noranda's perspective it is the **resulting plan** that is the most important consideration. Our concerns about compliance with the IRP Rule *per se* turn on our judgment of the impact of any noncompliance on the resulting plan.

4. Noranda seeks the most cost effective approach to future electricity needs. By the very nature of its operations, Noranda is continually vigilant in its pursuit of energy efficiency. A part of the Ameren's submitted plan ("IRP") is appropriately dedicated to cost effective energy efficiency programs designed to help others also arrive at high levels of efficiency. The IRP also pursues cost effective demand side measures ("DSM"). Of course, what constitutes "cost effective" energy efficiency and DSM depends on program design, efficient administration of the programs, the cost of supply side alternatives, and the price of electricity. Collectively, Ameren and the stakeholders, in Noranda's opinion, have worked diligently to arrive at the current plan.

5. In accordance with the IRP Rule and Commission order, several parties identified deficiencies in Ameren's IRP process as compared to the process required by the IRP Rule. These are **process** deficiencies and generally there are no judgments or conclusions as to the impact these deficiencies have on the Preferred Plan that emerges from the process. Performance of the process is not an end in itself; the purpose is the rigorous

development of a Preferred Plan that meets the IRP Rule's objectives. Certainly compliance with the strictures of the IRP Rule is sought, but if analysis of the resulting Preferred Plan shows it to be irrational or inconsistent with the overall purposes of the IRP Rule itself, the process must be further examined. The process is not performed in a vacuum.

C. Noranda's Approach Is Focused On The Resulting Preferred Plan as Well as the Process Employed to Develop the Preferred Plan.

1. A continuing supply of reliable and economical electricity is extraordinarily important to Noranda. That is the lens through which Noranda reviews Ameren's IRP, the Preferred Plan in particular, and the process. In other words, Noranda's review of the process begins and continues in consideration of the Preferred Plan.

2. From this vantage point, Noranda has two serious concerns. The first is the revenue requirements calculations in the IRP. The second is the treatment of the Meramec Plant. Besides the planning issues, we also find an issue that needs to be addressed outside of the plan.

D. Ameren Publicly Alleges that Revenues Under the Preferred Plan Are Inadequate - Seeks New Law.

1. The Preferred Plan is intended to provide a relatively low cost future in consideration of many important uncertainties. Callaway 2 emerges as an important part of the Preferred Plan. But all is not well with the IRP analysis of

Callaway 2. The translation of the forecast construction and financing costs into retail revenue requirements is fundamentally flawed. This conclusion proceeds from questions raised and answers proffered, in the course of the discussions surrounding the deficiencies alleged by the filings of several parties. In Noranda's view the possibility of a fundamental problem is also lifted up for the public's view by Ameren's own recent public statements outside of the IRP process.

2. Ameren suggests that it needs more rate revenue during the construction of Callaway 2 and it will be pursuing a change in the regulatory law of the State of Missouri to seek the inclusion of CWIP in rate base. That fact in itself underscores a fundamental issue inherent in the analysis. While it is Callaway 2 that draws attention, every dollar of new capital required according to the Preferred Plan contributes to a financial strain that militates for change. Change is needed, but first some discussion of the problem.

E. A Revenue Requirements Problem Arises due in Large Part to the Extraordinary Callaway 2 Capital Requirements.

1. Since Callaway 2 has emerged as a justification for change in regulatory law, we have been led to take a second look at the development of the Callaway 2 revenue requirements calculations in Ameren's analysis. At first blush it seems bullet proof. Forecast construction costs are spread through the years of construction, the financial costs are accumulated during the construction period, and then the combination of physical

construction costs and financial costs go into rate base. From that point it is a formula we know well. Operating and maintenance costs, taxes, return of and return on investment come together for one large and significant rate increase.

2. But all is not as it seems, for the revenue requirements analysis is not bullet proof. In fact, it is deficient.

3. The models used in the analysis make accurate computations as far as they go, but the financial results were left standing without due consideration and feedback to reflect the cost and rate consequences. In this important sense the planning process is incomplete. It is no surprise that, due to the extraordinary relative magnitude of new capital required under the Preferred Plan and length of construction, the financial metrics turn sour in short order. No surprise, but what, if anything, was done in response? What could have been done? What must be done now that the problem is revealed?

4. What was done? As far as we can discern, nothing was done in the context of the IRP. The analytical deficiency takes the form of interest costs that reflect an investment grade utility cost of debt while the financial metrics that emerge from the models do not. Something has to give. More revenue is needed to maintain financial health, or perhaps a higher cost of capital needs to be modeled to reflect deteriorating financial health. But these revenue needs or costs are not shown or reflected in the Preferred Plan. Either way, it appears that the

revenue requirements that proceed from the capital requirements, including Callaway 2, are likely understated during the construction period and this presents a fundamental problem with the analysis and as a result undermines the calculation of the Present Value of Revenue Requirements (PVRR) that is the foundation of the Preferred Plan. As to the IRP Rule, the requirement is that revenues reflect current Missouri law.^{5/} The IRP fails that requirement and is deficient. Regulation is more than the mindless application of formulae embodied in the models; the planning process must maintain a connection with reality.

5. What could have been done? There are many possibilities. For the purpose of this statement we will discuss two possibilities, but hasten to add that we make no representation that these are good solutions, and they are certainly not the only possible solutions. These options, and any others Ameren or others may bring to the process, need to be analyzed.

a. **Option One.** Ameren could have increased the cost of capital with higher interest rates and higher equity returns. This approach would directly address the deteriorating financial metrics. Of course, whether or not this approach is consistent with the interests of Ameren investors and customers would need to be examined.

b. **Option Two.** The revenue requirements associated with large capital expenditures are not a matter of first impression before this Commission. The Commission has approved

^{5/} 4 CSR 240-22.060(4)(B).

"Regulatory Plans" for both the Empire District Electric Company and the Kansas City Power & Light Company. These plans set forth a form of regulation geared to preserving a utility's financial health by providing revenues above and beyond what would otherwise flow under Missouri law during the periods of heavy capital outlays. Indeed, these regulatory plans could certainly have been adapted in some form for the purposes of the Ameren IRP. This approach would have put a floor under the financial metrics for the purposes of the IRP and increased the revenue requirements of the Preferred Plan during the construction period. The revenue effects would carry through the period of the plan and beyond. Of course, any approach along these lines also would need to be examined in due course to determine whether or not it would be consistent with the interests of Ameren investors and customers.

6. A superficial reader might think that Noranda is advocating higher rates inapposite to its interest and goals. Not so. The concern is rather that choices made based on understated revenue requirements undermine the ability of the Preferred Plan to achieve the intended result.

7. A recent Business Week article illustrated the current relatively positive position of Missouri in regard to electricity costs. One goal of Noranda is certainly to do what it can to ensure a robust planning process that will do all that is possible to preserve the position of relative advantage for Missouri.

F. The Preferred Plan Assumes Retirement of Meramec Capacity Without a Life Extension Study.

1. The IRP **assumes** the retirement of Meramec, but with the caveat that a "retirement" study will be done before the decision is made. On the surface, this approach may appear reasonable, but on deeper analysis it is not. The two capacity charts from the Preferred Plan that are attached as an example^{6/} demonstrate the impact of the addition of Callaway 2 on the heels of the assumed Meramec retirement.

2. The need for so much of the Callaway 2 capacity ought not to be based on a retirement assumption. In fact, the IRP Rule requires a life extension study, not a retirement study. That is indeed the perspective that Noranda recommends. If it is Meramec's coal fired boilers that become the problem, options considered ought to include repowering and a potential new facility at the Meramec site here in Missouri. In any event the fundamental point is that every effort should be made to economically extend the service life of the Meramec facilities. It is fundamentally misleading to suggest that Callaway 2 is a "Preferred Plan" when there has been no study of the Meramec life extension. The point of concern is that the arbitrary assumption of a retirement date that was used for Meramec skews the need for new capacity to several years earlier.

^{6/} Although the same charts were earlier made available by Ameren marked as HIGHLY CONFIDENTIAL, they were also placed in the public domain by Ameren's posting of them on its website at http://ameren.com/ResourcePlan/ADC_IRPFullReport.asp

G. Regulatory Direction is Needed Sooner Rather Than Later.

1. What must be done now? The Preferred Plan understates the revenue requirements during the construction period for Callaway 2. It ignores this critical deficiency and leaves it without a remedy. Many of the deficiencies presented by the parties have been addressed by Ameren with promises of action in the context of the "next IRP filing." In that many of the promises represent incremental changes intended to improve the planning process, we have no quarrel with that approach in appropriate circumstance and thus have no objection to those portions of the Partial Stipulation.

2. There is however, no promise to address the revenue requirement question *in the context of this IRP*. The question arises only tangentially in the Partial Stipulation in response to a point raised about "critical uncertain factors."

3. Ironically, revenue requirements implications of the capital expansion need not be an uncertain factor at all. What is needed is a "regulatory plan" for Ameren. The plan may or may not follow the principles and metrics of previously approved regulatory plans, but it is clear that a plan is needed, and needed now, so the costs can be modeled accurately now. The question of whether they can be modeled accurately in the *next* IRP is necessarily dependent on what is done in *this* IRP proceeding. If it is not done correctly here, there is no reason to believe that it will be done correctly in the context of a *future* IRP proceeding.

4. This is not a solution that can proceed from a unilateral IRP decision by Ameren management. Rather, it can only emanate from the Commission.

H. A Conclusion But Not A Complete Solution.

1. In summary, the unavoidable conclusion must be that the Ameren IRP filing of February 5, 2008, even as subsequently modified by filings made on August 12, 2008 remains deficient. Resolution of the deficiencies in **this** IRP requires revision of the analysis to perform a life extension study for Meramec and a revenue requirements calculation that maintains an investment grade financial standing. The approach to the "next IRP filing" should be addressed as a separate matter.

2. Missouri now has two examples of regulatory plans. But Noranda is aware of no stated policy or explicit direction on which parties could rely for the purposes of the next Ameren IRP. The topics inherent in regulation in consideration of the financial strains engendered by extraordinary capital expansion must be appropriately addressed in a timely forum.

3. The only other apparent possibility is a change in the regulatory law of the State of Missouri. Although we are aware that Ameren plans to seek a change in law, we have no knowledge of specific changes that Ameren will seek. Notwithstanding, the fact is that revenue requirements are inherently important to choices among competing alternative resource plans, and the issue has not been addressed properly in **this** IRP. Moreover, we are not aware of any specific legislative language

that is or will be proposed. Noranda can have no informed opinion of the efficacy of unknown legislative changes. No doubt there will be forces at work for and against any change. But legislative possibilities are just that: Possibilities. On the other hand, it is within the expressly granted powers of this Commission to set rates.

4. A proper proceeding in which this aspect of regulation - an aspect essential to choices among alternatives for the future of economical electric energy supplies in Missouri, ought to open as soon as possible. The issues will doubtless be difficult and time is of the essence so that the "next IRP filing" will not unnecessarily suffer from the uncertainty of unknown regulatory reaction to the strains of extraordinary capital expansion.

Respectfully submitted,

FINNEGAN, CONRAD & PETERSON, L.C.

A handwritten signature in dark ink, appearing to read "Stuart W. Conrad", is written over a horizontal line.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing pleading by electronic means or by U.S. mail, postage prepaid, addressed to all parties by their attorneys of record as disclosed by the pleadings and orders herein.



Stuart W. Conrad

Dated: August 20, 2008

(7) The values of the three (3) measures of financial condition identified in subsection (4)(A);



