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	)	Case No. ER-2014-0258
Revenues for Electric Service	)	

INITIAL POSTHEARING BRIEF

OF

MIDWEST ENERGY CONSUMERS GROUP

David L. Woodsmall
Woodsmall Law Office
308 E. High Street, Suite 204
Jefferson City, MO 65101
Phone: 573-636-6006
Fax: 573-636-6007
david.woodsmall@woodsmalllaw.com

ATTORNEY FOR MIDWEST
ENERGY CONSUMERS GROUP

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REPLY POST-HEARING BRIEF OF
MIDWEST ENERGY CONSUMERS' GROUP

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 reply post-hearing brief. In its Initial Brief, MECG addressed 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). In that Brief, and given the thorough development of issues in pre-filed testimony, MECG was able to address many of the issues that were raised by other parties in their Initial Briefs. As such, MECG will not burden the Commission by repeating those arguments. Instead, MECG will simply point out the portions of the Initial Brief which addresses those arguments for the Commission's attention.

II. VEGETATION MANAGEMENT / INFRASTRUCTURE INSPECTION TRACKERS

- MECG Initial Brief: pages 14-17
- Staff Initial Brief: pages 38-40
- OPC Initial Brief: pages 28-33
- MIEC Initial Brief: pages 11-13
- Ameren Initial Brief: pages 115-120

In its Initial Brief (pages 14-17), MECG recommended that the Commission discontinue the Vegetation Management / Infrastructure Inspection Tracker. MECG noted that the tracker was created to address an "extraordinary" cost – a cost that was incurred as a result of the recent promulgation of the Commission's vegetation management rule. Six years later, those costs are no longer extraordinary. Instead, Ameren has finished a complete cycle of both urban and rural tree trimming. As such, there is adequate historical data upon which future rates can be set. In their Initial Briefs, Staff (pages 38-40); Public Counsel (pages 28-33) and MIEC (pages 11-13) all agree that the vegetation management tracker represents poor regulatory policy and should be discontinued. In contrast, Ameren seeks to continue the vegetation management tracker (pages 115-120). In support of its position, Ameren appears to rely on 3 points.

First, Ameren maintains that the various parties' recommendation to discontinue the vegetation management tracker is rooted "in a generalized dislike for, and opposition to, deferral mechanisms."[1] Ameren fails to understand that the "generalized dislike" for deferral mechanisms is not unique to these parties. Rather, the "generalized dislike" is

[1] Ameren Initial Brief, page 117.

rooted in court decisions that disallow such mechanisms for anything other than "extraordinary" costs.

> 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.***[2]

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.

> 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.[3]

Recognizing that these vegetation management costs are no longer extraordinary (i.e., "unusual and infrequent"), Missouri case law expressly precludes the Commission from deferring such costs.

Second, Ameren argues that these costs "fluctuate from year-to-year due to factors beyond the Company's control, and will continue to do so into the future."[4] Through this statement Ameren confuses the legal standard to be applied to deferral mechanisms like trackers. As noted above, deferrals (other than fuel adjustment clauses) are considered based upon whether the underlying costs are "extraordinary." Clearly, the Ameren vegetation management costs are not "extraordinary." Given its inability to meet

[2] *State ex rel. Office of the Public Counsel v. Public Service Commission*, 858 S.W.2d 806, 81 (Mo.App. W.D. 1993) (emphasis added).
[3] Case No. EU-2014-0077, *Report and Order*, issued July 30, 2014, at page 10.
[4] Ameren Initial Brief, page 118.

this legal standard, Ameren instead seeks to apply the standard utilized by the Commission for determining whether to implement a fuel adjustment clause.

> In AmerenUE's last rate case, the Commission found that AmerenUE should be allowed to establish a fuel adjustment clause because its fuel costs were substantial, beyond the control of the company's management, and volatile in amount.[5]

Preferring the fuel adjustment clause criteria to that provided by the Missouri courts, Ameren simply ignores the "extraordinary" standard.

It is clear, however, that the criterion utilized by Ameren is limited solely to the implementation of a fuel adjustment clause. Such differing standards are allowed to exist because the fuel adjustment clause has specific statutory authority as contained in Section 386.266. In contrast, all other cost deferrals, since they lack expressed statutory authority, are judged by the "extraordinary" standard set forth by the Missouri courts.

Third, Ameren points to the Commission's vegetation management rule as creating a presumption for allowing a deferral mechanism.[6] While that rule does reference the Commission's willingness to consider a cost tracker, Ameren fails to place this rule provision in context. Specifically, when it was promulgated, the Commission recognized that it was imposing a cost that was "extraordinary" and significantly above any vegetation management costs already included in rates. As such, the Commission indicated a willingness to consider a deferral mechanism to address this newly imposed "extraordinary" cost. Those costs are no longer extraordinary and the Commission's previous willingness to consider deferral of such costs is no longer relevant. As the Commission most recently indicated, the tracking mechanism envisioned by the rule was never thought to be "permanent". "However, as the Commission has indicated in

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[5] See, Case No. ER-2010-0036, *Report and Order*, issued May 28, 2010, at page 74.
[6] Ameren Initial Brief at page 118.

previous rate cases, it does not intend for this [vegetation management] tracker to become permanent."[7]

In the final analysis, the Commission should consider Ameren's request to continue the vegetation management tracker against the "extraordinary" standard set forth by Missouri courts. Recognizing that these costs are no longer extraordinary, the Commission should discontinue the tracker.

[7] Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at page 107.

II. RETURN ON EQUITY

- MECG Initial Brief: pages 14-17
- Staff Initial Brief: pages 43-76
- OPC Initial Brief: pages 15-28
- MIEC Initial Brief: pages 16-31
- Ameren Initial Brief: pages 50-88

In its Initial Brief, MECG recommended that the Commission authorize Ameren a return on equity of 9.30%. This recommendation is based upon the evidence provided by MIEC witness Michael Gorman. Mr. Gorman's recommendation is consistent with the recommendations provided by Staff witness Murray (9.25%) and OPC witness Schafer (9.0%). Given the similarity of these recommendations, MECG will not address the return on equity sections from the briefs of Staff, OPC, or MIEC. Noticeably, however, Ameren's recommendation is much higher (10.4%). As such, MECG will devote the entirety of this portion of its brief to addressing Ameren's flawed and inflated return on equity recommendation.

Ameren appears to provide four primary justifications for its inflated return on equity: (1) Ameren claims that the cost of capital has increased since the Commission decided the 2012 Ameren case and authorized a return on equity of 9.80%; (2) Ameren points to the Commission's recent return on equity decisions in two unrelated, and irrelevant, gas cases; (3) Ameren incorrectly lauds Mr. Hevert's evidence as "persuasive and authoritative" and (4) Ameren relies on Mr. Hevert's flawed methodologies. MECG will address each of these points in order.

First, Ameren falsely claims that the cost of capital has increased since the Commission authorized a return of 9.80% in the 2012 Ameren case.[8] Ameren reaches this conclusion by selectively latching on to various pieces of evidence that do not tell the complete story regarding the cost of capital. The complete evidence, however, indicates that the cost of capital has decreased over that time period.

As MIEC points out, since the Commission's decision in Case No. ER-2012-0166, "utility stock prices have increased and dividend yields have declined, while growth rates have been relatively stable. In the same period, utility bond yields have declined."[9] During questioning from the bench, Mr. Gorman explained how these objective financial metrics lead to the inevitable conclusion that cost of capital has declined.

> Stock prices can increase if there's a significant increase in the expected growth outlook for that stock. So the cash flow outlooks could increase. [In that case] the discount rate or the cost of capital may not change. But that's not the case here. Growth has increased a little bit, [as explained in] my testimony, relative to the last case, but not much. Dividend yields have gone down quite a bit.
>
> **Because the price of stock has gone up and other parameters of the stock have not significantly changed, that's a clear indication that investors have reduced their required cost of capital which has bid up the stock price.** So [investors are] willing to pay more for stock for the cash flows expected to be produced from that stock.[10]

In fact, contrary to Ameren's current contentions, Mr. Hevert (Ameren's witness) clearly acknowledged that capital costs have declined since 2012.[11] In fact, Mr. Hevert's own

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[8] Ameren Initial Brief, pages 51-53. ("Some parties further argue that the cost of capital is declining. A closer review indicates this position statement is without evidentiary support and indeed the evidence is contrary.").
[9] MIEC Initial Brief at pages 16-17.
[10] MIEC Initial Brief at page 19 (citing to Tr., pages 1268-1269 (emphasis added).
[11] Tr. 1119-1120.

return on equity recommendation has decreased since the last case in response to this declining cost of capital.[12]

Second, in an effort to support its inflated return on equity recommendation, Ameren directs the Commission's attention to its recent decisions regarding *Liberty Utilities* (Case No. GR-2014-0152) establishing a return on equity of 10.0% and *Summit Utilities* (Case No. GR-2014-0086) establishing a return on equity of 10.8%. Interestingly, Ameren acknowledges that "the return must be comparable to investments of similar risk."[13] Nevertheless, Ameren blindly points to these cases without any evidentiary support establishing a conclusion that either Liberty Utilities or Summit Utilities are of similar risk to Ameren.

In undertaking a return on equity analysis, the analyst carefully considers the makeup of a proxy company group. Given this, Ameren's witness selected proxy companies from a "universe of companies that Value Line classifies as Electric Utilities."[14] Similarly, Messrs. Gorman,[15] Murray[16] and Schafer[17] also chose proxy companies from only electric utilities. Given that the proxy companies include only electric utilities, Ameren's current reference to return on equity decisions to gas utilities is clearly irrelevant.

Third, Ameren attempts to assign credibility to its witness and its inflated return on equity recommendation by falsely claiming that "the most persuasive and authoritative as demonstrated by the weight of the evidence is Mr. Hevert."[18] Interestingly, Ameren makes

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[12] *Id.*
[13] Ameren Initial Brief, page 54.
[14] Exhibit 16, Hevert Direct, page 9.
[15] Exhibit 510, Gorman Direct, page 13.
[16] Exhibit 202, Staff Cost of Service Report, page 27.
[17] Exhibit 409, Schafer Direct, page 7.
[18] Ameren Initial Brief at page 56.

this claim without any factual basis. In contrast, as demonstrated in MECG's initial brief, the recent decisions of this and other state utility commissions readily indicate that Mr. Hevert's recommendations are not "persuasive and authoritative."

Specifically, as reflected at page 23 of MECG's Initial Brief, this Commission has repeatedly found Mr. Hevert's "estimation of an appropriate ROE is too high."[19] Such a finding is not unique to the Missouri Commission. Rather, in the past two years, every state utility commission that has considered Mr. Hevert's recommendation has found it to be "too high." In fact, in the 19 reported cases involving Mr. Hevert's recommendation in the last two years, the state utility commission has found that Mr. Hevert's recommendation is 83 basis points too high.[20] Simply applying this inflationary factor to Mr. Hevert's current 10.40% recommendation, this Commission would authorize Ameren a return on equity of 9.57%. Clearly, Ameren has no basis for its claim that Mr. Hevert's work is "persuasive and authoritative."

Fourth, at pages 58-65, Ameren discuses Mr. Hevert's methodology and relies upon his approach as a means to justify its inflated return on equity recommendations. Ameren fails to mention, however, that this Commission has previously found that Mr. Hevert's methodology and choice of assumptions to be faulty.

> 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.[21]

Ameren further fails to mention that, despite this Commission's clear criticism of his methodology, Mr. Hevert simply repeated the same flawed approach. As detailed at

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

pages 25-27 of MECG's Initial Brief, Mr. Hevert's assumptions in his return on equity methodologies are "too high" and lead to unreasonable results. Given his continued flawed approach, the Commission should again reject Mr. Hevert's recommendation.

Bottom line, Ameren's 10.4% return on equity recommendation is clearly inflated. If adopted by the Commission, Ameren's 10.4% return on equity would be the highest authorized by any state utility commission since December of 2013.[22]

[22] Exhibit 750, Chriss Direct, Schedule SWC-7.

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

- MECG Initial Brief: pages 31-51
- Staff Initial Brief: pages 76-83
- OPC Initial Brief: pages 37-40
- MIEC Initial Brief: pages 43-48
- Ameren Initial Brief: pages 145-147

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

In its Initial Brief (pages 32-41), MECG recommended that the Commission continue to utilize the Average & Excess methodology (4 NCP version) to allocate fixed generation costs among the customer classes. As indicated at page 41 of that Brief, The Commission has previously indicated a preference for that methodology. Furthermore, the A&E method avoids the double counting of class energy usage that is problematic in the OPC Peak & Average methodology (pages 35-38) as well as the numerous downfalls of Staff's Base / Intermediate Peak methodology (pages 38-40).

In their Initial Briefs, MIEC (pages 43-44) and Ameren (page 146) also recommend that the Commission continue to utilize the A&E methodology. While it recommended that the Commission abandon its past practice of using the A&E methodology and, instead, use the Peak & Average methodology, Public Counsel provides absolutely no discussion in its Initial Brief as to the benefits of that methodology. Similarly, while it recommends that the Commission change to its archaic

BIP methodology, Staff provides very little factual discussion. Rather, Staff simply provides conclusory statements regarding its methodology.

> Staff recommends that the Commission find in favor of the results of its Detailed Base Intermediate and Peak ("BIP") class-cost-of-service study because Staff's study methodology is the most reasonable, in that it recognizes the relationship between Ameren Missouri's generation fleet characteristics and the capacity and energy requirements of its load. Staff's results are the most reasonable because Staff's Detailed BIP study relies on a more complex and thorough allocation of the cost of owning and operating Ameren Missouri's generation fleet than is done by the other parties' studies.[23]

Noticeably, Staff fails to provide any recognition of the numerous problems underlying its faulty methodology. As detailed at pages 38-40 of MECG's Initial Brief, the Staff BIP methodology is inherently flawed. Given these flaws and the Commission's previous findings that the A&E methodology properly allocates fixed generation costs, the Commission should continue to utilize the A&E methodology (4 NCP version).

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

At pages 41-43 of its Initial Brief, MECG recommends that the Commission utilize the same A&E methodology for the allocation of non-fuel, non-labor components of production O&M expense. As MECG pointed out there, all parties, except Ameren, recommend that "expenses follow plant." Similarly, MIEC, as the only other party to brief this issue, recommends that the Commission utilize the A&E methodology to allocate these costs.[24] While it advocates a different methodology, Ameren appears to have completely abandoned this issue in its Initial Brief. As such, MECG simply refers

[23] Staff Initial Brief at page 77.
[24] MIEC Initial Brief, page 46.

the Commission to its Initial Brief and recommends that the Commission utilize the A&E methodology for allocation of these costs.

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

In its Initial Brief (pages 43-45), MECG recommended that the Commission continue to allocate off-system sales revenues on the basis of class energy usage. Ameren, MIEC and Staff all appear to agree with this recommendation. In contrast, Public Counsel recommended, in its testimony, that these revenues be allocated using the production demand allocator. Interestingly, however, while it advocates that the Commission change its policy on the allocation of these revenues, Public Counsel appears to have completely abandoned this issue in its Initial Brief. As such, MECG simply refers the Commission to its Initial Brief and recommends that the Commission continue to utilize the energy allocator for the allocation of off-system sales revenues.

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

In its Initial Brief (pages 45-46), MECG recommended that the Commission allocate income taxes on the basis of the taxable income for each customer class. As the only other party to brief this issue, MIEC provides a similar recommendation.[25] In contrast, in its testimony, Ameren recommended that income taxes be allocated on the basis of class rate base. Once again, however, Ameren appears to have abandoned this issue in its Initial Brief. As such, MECG simply refers the Commission to its Initial Brief

[25] MIEC Initial Brief, pages 46-47.

and recommends that the Commission allocate income taxes on the basis of each class' taxable income.

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

In its Initial Brief (pages 46-47), MECG recommended that, in the event that the Commission adopts Public Counsel's faulty Peak & Average allocator for production fixed costs, it should allocate a greater share of the low cost baseload fuel costs to the high load factor customer classes and a lesser share of the high cost peaking plant fuel costs to those classes. No other party addressed this issue. As such, in the event that the Commission adopts Public Counsel's fixed production allocator, MECG recommends that the Commission allocate fuel and purchased power costs as detailed in its Initial Brief and the testimony of Maurice Brubaker.

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

As MECG indicated in its Initial Brief, while the Commission's decision on the previous five allocation issues will have some effect on the magnitude of this subsidy, there are certain conclusions that can be reached from the class cost of service studies in this case. Specifically, as Ameren points out, Residential and Large Transmission Service ("Noranda") classes are paying rates below cost of service, while the Large General Service / Small Primary rate class is paying rates well above cost of service.[26]

[26] See, Ameren Initial Brief, pages 146-147.

As Ameren notes, "[e]xcept for OPC's [Peak & Average] study, any of the CCOSS presented in this case will result in a fair and reasonable rate design."[27]

	MIEC[28]	***Ameren***[29]	***Staff***[30]	***OPC 2***[31]
(in thousands)	(A&E)	(A&E)	(BIP)	(A&E)
Residential	$68,761	$62,576	$36,029	$41,864
SGS	($12,585)	($13,391)	($12,494)	$1,007
LGS / SP	($61,912)	($59,886)	($39,129)	($48,159)
LP	(934)	1,030	($1,566)	$4,054
LTS	6,674	9,830	$17,021	$10,254
Lighting	(3)	(158)	$137	($9,019)

Given that all of the studies reach these same conclusions, the fundamental issue is focused on what, if any, steps the Commission should take to remedy this subsidy.

Not surprisingly, in its Initial Brief, Public Counsel, as the advocate for the residential class, recommended that the Commission take no action to remedy this residential subsidy. Specifically, Public Counsel recommends that the Commission "apply equal percentage system average increases to each class based on the revenue requirement increase ordered in this case."[32] Public Counsel provides no basis for this recommendation except to say that the studies are only "a general guide in determining what classes are or are not meeting fully embedded costs and meeting their allocated

[27] *Id.* at page 146.
[28] Exhibit 977
[29] Exhibit 976
[30] Exhibit 978
[31] Exhibit 403 (Attachment GM-4)
[32] OPC Initial Brief, page 39.

expense."[33] Given this, Public Counsel argues that the results of these studies, even the Public Counsel studies that show the same residential subsidy, should simply be ignored.

In their Initial Briefs, Staff and Ameren suggest that the Commission, in the interest of gradualism, take minimal steps to alleviate the residential subsidy. Specifically, Staff suggests that the residential and LTS (Noranda) classes receive a positive 0.50% rate increase in this case.[34] The problem with the Staff proposal is obvious. As Staff admits, under its study, residential rates are 3.0% below cost of service.[35] As such, if the Commission takes similar steps in subsequent cases, it will take 6 rate cases for the subsidy to be eliminated. Recognizing that Ameren files a rate case approximately every 18 months, this residential subsidy will exist for at least the next 9 years! In its Initial Brief (page 49), MECG demonstrated that the problem with the residential subsidy is long-standing, and has existed at least since 2007.

	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

[33] *Id.* at page 40.
[34] Staff Initial Brief at page 77. See also, Ameren Initial Brief, page 147 ("Ameren Missouri does not oppose Staff's proposed revenue neutral shift of +0.5 percent for the Residential and LTS classes.").
[35] Exhibit 978.

Given the chronic nature of the residential subsidy and the fact that the Staff' glacial approach will not eliminate this subsidy for at least another 9 years, MECG recommends that the Commission take a more enlightened approach. Specifically, MECG echoes the recommendation of Walmart and asks that the Commission "apply a 25% revenue neutral movement towards cost of service."[36] This would eliminate 25% of the residential subsidy in this case. After making this revenue neutral movement, any rate increase authorized in this case should be applied to all classes on an equal percentage basis.[37]

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. Finally, such a step would enhance the Commission's goal of developing economic development by ensuring that such businesses only paying for the costs actually incurred to provide them service.

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[36] Exhibit 750, Chriss Direct, page 9.
[37] *Id.* at page 10.

IV. NORANDA RATE PROPOSAL

- MECG Initial Brief: pages 52-97
- Staff Initial Brief: pages 91-103
- OPC Initial Brief: pages 40-53
- MIEC Initial Brief: pages 55-96
- Ameren Initial Brief: pages 157-187

The central focus of the issue regarding Noranda's request for a subsidized retail rate boils down to a single question: Does the Commission truly believe that the New Madrid smelter will close absent some rate relief? While Staff did not venture an opinion on this central issue, its witness did recognize the prerequisite nature of this inquiry.

> Because Staff has not said – well, has not said because we don't know whether or not Noranda would really close down. We don't know. That is a policy question for your [the Commission's] determination in this case.[38]

Absent a finding that the New Madrid smelter will close, the Commission's inquiry is largely unnecessary.

While the Staff was unwilling to venture an opinion on whether the New Madrid smelter would close, the Commission has already answered this question. In its decision from less than 8 months ago, the Commission found that "the Complainants [Noranda] have not met their burden in that they have not shown Noranda is suffering from a liquidity crisis."[39] 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

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[38] Tr. 3002.

[39] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, at page 25.

> 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***."[40]

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***.[41]

As the following analysis indicates, the evidence in this case dictates a similar finding. By finding against the threshold issue, all the remaining issues become moot.

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

In its Initial Brief, MECG devoted 45 pages to the Noranda request for a subsidized retail rate. Included in this brief, MECG provided argument and evidence dispelling Noranda's claim that it is experiencing a liquidity crisis (pages 53-66). Specifically, the evidence indicates that: (1) for over the last two years, Noranda has demonstrated a stable liquidity position;[42] (2) Noranda's comments to the Commission regarding its liquidity crisis contradict the comments made to the public and investing community;[43] and (3) when faced with a similar liquidity position in the last case, Noranda accepted a full share of Ameren's 10.1% rate increase.[44] In addition, MECG provided extensive discussion regarding the flaws in Noranda's financial model and its

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[40] *Id.* at pages 7-8 (emphasis added).
[41] *Id.* at page 8 (emphasis added).
[42] MECG Initial Brief, pages 53-54.
[43] MECG Initial Brief, pages 55-59.
[44] MECG Initial Brief, pages 59-60.

assumptions that are used to support Noranda's claim of a liquidity crisis.[45] Given the extensive nature of its Initial Brief, MECG has already anticipated most of Noranda's claims on this issue. Therefore, MECG will attempt to simply refer the Commission back to MECG's Initial Brief.

1. CONTRADICTORY STATEMENTS

In its Initial Brief, Noranda makes several **absolute** statements regarding the future of the New Madrid smelter. "Without rate relief, the New Madrid smelter is not viable."[46] "But it is clear that denial of rate relief will result in the ultimate shutdown of the smelter."[47] "The New Madrid smelter cannot be sustained unless the Commission grants rate relief."[48]

In its decision in Case No. EC-2014-0224, the Commission noted that Noranda's absolute statements regarding the future of the New Madrid smelter directly contradicted the statements that it makes to the public and investing community. As detailed at pages 55-59 of MECG's Initial Brief, Noranda's most recent public statements, in the context of its quarterly investor calls, provide a much rosier view of the New Madrid smelter's financial future. Given the obvious contradiction between Noranda's statements made in these various venues, it is not surprising that the Commission has grown frustrated trying to find the truth in Noranda's financial condition.

> ***I think it is without a doubt fact that there is a difference between what you are telling investors and what you are telling us here today***. Now, I'm not telling you that it is my belief that there is not a way to find some consistency but the verbiage, the definitive nature is different between the

[45] MECG Initial Brief, pages 60-66.
[46] MIEC Brief, page 55 (emphasis added).
[47] *Id.* at page 57 (emphasis added).
[48] *Id.* at page 63 (emphasis added).

> two and what I'm asking for you, from you, is to explain to me why there might be that discrepancy. Now, you can say there's no discrepancy, I'm telling you I don't believe that. There is a difference.[49]

At times, even in its own brief, Noranda slips and reveals that the closure of the New Madrid smelter is not imminent. Rather, as Noranda notes in its Brief, the closure of the New Madrid smelter is still up for some debate and that, at times, Noranda only deems it to be "likely."[50] Similarly, at other times, Noranda simply notes that the closure of the smelter is not imminent, but simply "threatened."[51]

2. NORANDA'S EVIDENCE IS FLAWED

Given that a liquidity crisis cannot be proven from its financial statements or its statements to the public and investing community, Noranda attempts to manufacture a liquidity crisis through its use of financial modeling. At pages 63-65, Noranda discusses this modeling.

> To show how critical a sustainable power rate is to the New Madrid smelter's viability, Noranda provided a number of objective, reasonable and prudent financial scenarios (not forecasts) based on actual historical volatility patterns of aluminum prices. These scenarios showed conclusively that, at current power tariffs, the smelter faces a substantial risk of not being able to generate positive cash flows to pay its bills during the normal course of business operations or to attract and retain the capital necessary to support the continued operation of the smelter.[52]

Unfortunately for Noranda's argument, the Commission has previously found the Noranda model to be "severely flawed." Moreover, the Commission has questioned Noranda's refusal to utilize CRU price forecasts in the context of its model as well as its decision to inflate future capital expenditures.

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[49] Tr. 2546-2547 (emphasis added).
[50] MIEC Brief, pages 58-59.
[51] MIEC Brief, page 66.
[52] MIEC Brief, page 64.

> 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.[53]

At pages 61-66 of its Initial Brief, MECG demonstrates that Noranda's assumption utilized in the "severely flawed" financial model are faulty. Ultimately, as shown on page 63, the result of that model, using the CRU forecasted aluminum price, is liquidity of **______** million, an increase of **______** million in liquidity.[54] 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."[55] Given the ongoing concerns with Noranda's modeling assumptions, the Commission should continue to reject Noranda's claims of financial woe.

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

Rather than focusing on its overall cost of production, Noranda focuses its entire attention of its cost of electricity.

> However, it is the cost of electricity, accounting for approximately one-third of the cost of production at most smelters, that most significantly determines whether a smelter is sustainable. The impact of power rates is most dramatically shown by the recent smelter closings. In the U.S. in 1980, there were 32 smelters, producing more than 5 million metric tons. Today, there are only 8 smelters operating in the U.S., producing about 1.8

[53] Case No. EC-2014-0224, *Report and Order*, issued August 20, 2014, pages 25-26.
[54] Exhibit 33, Mudge Rebuttal, page 19.
[55] *Id.* at page 20.

> million metric tons annually. In each case, it was the high cost of power that caused the smelters to shut down.[56]

As shown on pages 66-73 of its Initial Brief, however, Noranda's single-minded focus on the cost of electricity is misplaced. While Noranda claims that "in each case [of a domestic smelter closing], it was the high cost of power that caused the smelters to close," the evidence indicates this statement to be patently false. In fact, at the time that it closed, the Massena East smelter had the cheapest cost of electricity of any domestic smelter.[57] That cheap cost of electricity could not assure the future of the Massena East smelter. As the evidence clearly shows, the reason that Massena East closed was because of its high overall cost of production.

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Source: Exhibit 33, Mudge Rebuttal, page 43

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[56] MIEC Brief, page 66.
[57] Exhibit 979; See also, HC Tr. 2719.

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 **_______________**.

Recognizing that it is the overall cost of production, and not the cost of electricity, that dictates the viability of domestic smelters, it is interesting that the New Madrid smelter has the lowest overall cost of production.

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Source: Exhibit 33, Mudge Rebuttal, page 40.

Clearly, Noranda's continued single-minded focus on the cost of electricity is misplaced.

C. AN INCREMENTAL COST STANDARD SOLELY FOR NORANDA WOULD BE UNDULY DISCRIMINATORY

In its Initial Brief, Noranda attempts to assuage any concerns that the Commission may have over its subsidized rate request. Specifically, Noranda claims that, by allowing it to pay rates based upon Ameren's incremental cost of service, all Missouri retail customers would be benefitted.[58] The problem with Noranda's suggestion is two-fold.

First, as Noranda readily admits, the current wholesale price for electricity is below Ameren's retail electric rates. Given this current price differential, Ameren cannot fully recover the lost revenues associated with Noranda's closure by selling that power in the wholesale market. Therefore, Noranda postulates that the remaining ratepayers would be better off if Noranda were simply charged the incremental cost of electricity. Interestingly, however, this fact is not unique to Noranda. Given its inability to completely recover retail revenues by selling any displaced electricity in the wholesale market, Ameren customers would be better off if any customer that threatens to relocate or close were served at incremental cost.

Recognizing this, the concern becomes whether the Commission would allow any Ameren customer that threatens to leave the Ameren system, to reduce its electric cost to incremental cost? Would this reduced electric cost be available to residential customers or to just large industrial customers? If this is only available to large industrial customers, what criteria should be applied to the next request? Is the Commission willing and prepared to become experts on the auto, cement, beer brewing, hospital, aerospace, chemical and casino industries in order to assess the next request for incremental cost based rates?

[58] MIEC Brief, pages 60-63.

Second, the application of one pricing methodology for Noranda (incremental cost) while applying a disparate methodology for every other Ameren customer (embedded average cost) would be unjustly discriminatory. Section 393.140(5) precludes the Commission from setting rates that are "unjustly discriminatory or unduly preferential." Given this prohibition, the Commission has historically allowed for differences in rates where those differences are tied to variations in cost of service between customers.[59] That said, however, it would certainly appear to be "unjustly discriminatory" for the Commission to apply one pricing standard (incremental cost) for Noranda while applying a different methodology (embedded cost) to every other Ameren customer. Certainly, it would be unjustly discriminatory for the Commission to allow an incremental pricing standard for Noranda while denying that same pricing standard to the next Ameren customer (residential or industrial) that seeks a lower rate in order to remain on the Ameren system.

D. THE NONUNANIMOUS STIPULATION DOES NOT FULFILL THE COMMISSION'S DIRECTION TO PURSUE A "COMPROMISE POSITION."

As previously mentioned, the Commission previously rejected Noranda's request for a subsidized in Case No. EC-2014-0224. In its Order in that case, the Commission stated that it "encourages the parties to continue to pursue negotiations on a compromise position as it could be considered in Ameren Missouri's current rate case." Still again, in its Order Denying Applications for Rehearing in that case, the Commission stated that "the parties are encouraged to continue to pursue negotiations on a compromise position that can be presented for consideration in the general rate case."

[59] See, *State ex rel. Laundry, Inc. v. Pub. Serv. Comm'n*, 327 Mo. 93, 34 S.W.2d 37 (Mo. 1931).

Recognizing the Commission's direction to "continue to pursue negotiations," Noranda claims that it "has negotiated for many months with consumer groups and other parties to find a compromise position that balances all interests."[60] While Noranda may have engaged in these negotiations, the substance of the Nonunanimous Stipulation readily reveals that it has not attained additional party support and that the stipulation does not represent a "compromise position."

1. THE NONUNANIMOUS STIPULATION CONTINUES TO BE OPPOSED

In Case No. EC-2014-0224, the Commission was also presented a nonunanimous stipulation and agreement designed to provide Noranda a subsidized electric rate. That stipulation was signed and supported by Public Counsel, Missouri Industrial Energy Consumers, the Consumer Council of Missouri, Noranda and Missouri Retailers Association.[61] As previously mentioned, the Commission rejected that stipulation and encouraged the parties to "continue to pursue negotiations." Despite the opportunity presented in the intervening months, Noranda has been unable to garner any additional support. In fact, the nonunanimous stipulation filed in this case continues to be supported by the same handful of parties. As such, despite Noranda's claims to the contrary, the current agreement does not represent "a compromise position that balances all interests."

Given its limited support, Noranda attempts to assign heightened importance to the parties that did support the nonunanimous stipulation. Specifically, Noranda claims that the settlement "has support from representatives of all customer classes."[62] Similarly, the Missouri Retailers Association claims that "[t]he Signatories represent consumers in all of the major customer classes." Further inquiry reveals, however, that

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[60] MIEC Brief, page 57.
[61] See, Case No. EC-2014-0224, *Nonunanimous Stipulation and Agreement*, filed August 1, 2014.
[62] MIEC Brief, page 56.

such claims are largely puffery. For instance, while a signatory to the settlement, MIEC is a group that includes Noranda as a member.[63] Similarly, while not a retailer, Noranda is, nevertheless, a member of the Missouri Retailers' Association.[64] Given Noranda's presence as a member in both of these groups, the Commission should necessarily be skeptical of those groups' claims to independently represent Ameren's customers of the Small General Service; Large General Service; Small Primary or Large Primary customer classes. In fact, every independent commercial and industrial party participating in this case has opposed the nonunanimous stipulation.

2. THE SIGNATORIES PROVIDE NO EVIDENTIARY SUPPORT FOR TERMS OF NONUNANIMOUS STIPULATION

As indicated in MECG's Initial Brief (pages 86-97), the key provisions of the Nonunanimous Stipulation are unreasonable and not supported by evidence. Specifically, MECG pointed out that Public Counsel's own witness disagrees with the settlement provision to exempt Noranda from the fuel adjustment clause, the 10-year term of the agreement and the limited escalator. Interestingly, neither Noranda nor the other signatories provide any support for these specific provisions of the stipulation. As such, the terms of the settlement are largely arbitrary and capricious.

[63] See, *Amended Application to Intervene*, filed July 31, 2014, at page 1.
[64] See, *Non-Unanimous Stipulation and Agreement*, filed March 10, 2015, at page 1, footnote 1.

Respectfully submitted,

WOODSMALL LAW OFFICE

David L. Woodsmall
Woodsmall Law Office
308 E. High Street, Suite 204
Jefferson City, MO 65101
Phone: 573-636-6006
Fax: 573-636-6007
david.woodsmall@woodsmalllaw.com

ATTORNEYS FOR MIDWEST ENERGY CONSUMERS GROUP

CERTIFICATE OF SERVICE

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

David L. Woodsmall

Dated: April 10, 2015